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Old Republic International Corporation NYSE:ORI

Earnings Call

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Call Participants

EXECUTIVES

Carolyn Jean Monroe
Senior Vice President of Title Insurance

Craig Richard Smiddy
President, CEO & Director

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

ANALYSTS

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Gregory Lee Powell
Miller Howard Investments, Inc.

ATTENDEES

Joe Calabrese

Presentation

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Old Republic International's Fourth Quarter 2023 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded, Thursday, January 25, 2024.

I would now like to turn the conference over to Joe Calabrese with the Financial Relations Board.

Joe Calabrese

Thank you. Good afternoon, everyone. Thank you for joining us for the Old Republic conference call to discuss fourth quarter 2023 results.

This morning, we distributed a copy of the press release and posted a separate financial supplement which we assume you have seen and/or otherwise have access to during the call. Both of the documents are available at Old Republic's website, which is www.oldrepublic.com.

Be advised that this call may involve forward-looking statements as discussed in the press release and financial supplement dated January 25, 2024. Risks associated with these statements can be found in the company's latest SEC filings.

This afternoon's conference call will be led by Craig Smiddy, President and CEO of Old Republic International Corporation and several other senior executive members as planned for this meeting.

At this time, I'd like to turn the call over to Craig Smiddy. Please go ahead, sir.

Craig Richard Smiddy
President, CEO & Director

Okay, Joe, thank you. Good afternoon, everyone, and welcome again to Old Republic's Fourth Quarter and Year-end 2023 Earnings Call. With me today is Frank Sodaro, our CFO of ORI; and Carolyn Monroe, our President and CEO of our Title Insurance business.

So our focus on specialization and diversification across title and P&C insurance enabled us to produce a consolidated combined ratio of 93.3%, and $237 million of consolidated pretax operating income in the quarter. For the full year, the consolidated combined ratio was 92.6% compared to 91% in 2022, and consolidated pretax operating income was $938 million compared to $1.059 billion in 2022.

In General Insurance, we continued to produce strong underwriting results with a 92% combined ratio and $195 million of pretax operating income in the quarter. For the full year, the General Insurance combined ratio was 90.2%, just slightly higher than our 89.5% in 2022, and pretax operating income was $788 million, up 14% from the $690 million we produced in 2022.

And despite the headwinds from mortgage insurance rates and the soft real estate market, Title Insurance produced profitable underwriting results with a 95.5% combined ratio and $44 million of pretax operating income in the quarter. For the full year, Title's combined ratio was 97.1% compared to 93.2% in 2022 and pretax operating income for Title was $134 million, down from the $309 million in 2022.

So our conservative reserving practices continue to produce favorable prior year loss development in all 3 segments, which, by the way, marked our ninth consecutive year of favorable prior year development.

Our balance sheet, it remains solid even as we continue to return capital to shareholders through both dividends and share repurchases, while we continue to invest in new underwriting subsidiaries, people and technology, all with a focus on the long term.

So with those introductory comments, I will now turn the discussion over to Frank, and then Frank will turn things back to me to cover General Insurance, followed by Carolyn, who will discuss Title Insurance. And then we'll open up the conversation, as we always do, to Q&A.

So with that, Frank, I hand it to you.

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

Thank you, Craig, and good afternoon, everyone.

This morning, we reported net operating income of $190 million for the quarter and $750 million for the year. On a per share basis, comparable year-over-year results were $0.69 versus $0.80 for the quarters and $2.63 versus $2.79 for the full years. Net investment income increased 19% and 26% for the quarter and year, respectively, driven primarily by higher yields.

Our average reinvestment rate on corporate bonds during the year was 5.35%, while the comparable book yield on bonds disposed of was just over 2.8%. Bond portfolio book yield is now nearly 4% compared to 3.3% at year-end last year.

Our investment portfolio mix remained consistent with last quarter and the quality of our bond portfolio remains very high with 99% in investment-grade securities with an average maturity of 4.3 years.

During the quarter, the valuation of our fixed income securities increased by approximately $445 million driven by interest rates. The value of the stock portfolio increased by about $110 million and ended the year in an unrealized gain position of just over $1.1 billion.

From a loss reserve perspective, all 3 operating segments recognized favorable development for all periods presented. In total, the consolidated loss ratio benefited by 4.7 and 4.6 percentage points for the quarter and year, respectively, compared to 7.4 and 3.7 percentage points for the same period a year ago.

Turning to our run-off mortgage insurance operations. We expect the previously announced sale to close in the first half of 2024. In the meantime, results were consistent with recent periods and this group paid a $25 million dividend in the quarter, bringing the total return to $210 million for the year. We ended the year with book value per share increasing to $23.31, which contributed to total book value return of 15.3% for the full year. This return was driven by our strong operating earnings and higher investment valuation.

In the quarter, we paid $67 million of dividends and repurchased $55 million worth of our shares for a total of just over $120 million return to shareholders. For the full year, we paid over $275 million in dividends and repurchased $530 million worth of our shares for a total of just over $805 million returned to shareholders.

I'll now turn the call back to Craig for a discussion of General Insurance.

Craig Richard Smiddy
President, CEO & Director

Okay. Thanks, Frank. So General Insurance net written premiums were up over 12% in the quarter and up nearly 10% for the year. What contributed to this was strong renewal retention ratios and new business growth, including new business produced through our new underwriting subsidiaries. And we continue to achieve rate increases across most of our portfolio, which helps with the exception of D&O and workers' compensation.

As discussed a minute ago, the General Insurance group combined ratio was 92% for the quarter and 90.2% for the year, and pretax operating income was $195 million for the quarter and $788 million for the year. So we continue to produce very profitable results in our General Insurance business as is reflected in these numbers.

The loss ratio for the quarter was 65.1%, which included 5.1 points of favorable development, and it was 62% for the year, which included 5.7 points of favorable development. The expense ratio for the quarter was 26.9%, and it was 28.2% for the year. All of this is very much in line with our coverage mix.

So turning specifically to our 2 largest lines of coverage. Commercial auto net premiums written grew almost 20% in the quarter while the loss ratio came in at 78.3% for the quarter and 71.5% for the year. As we mentioned in the release, that loss ratio of 78.3% in the quarter includes an increase for all 4 quarters of 2023. This is because severity pushed our loss trend into the low double digits. And as we have reported in the past, we react very quickly when we see things come through in the way of higher severity and loss trends.

However, for both the quarter and the year, we continued to experience favorable prior year loss development on this line, and we feel very comfortable with where we're at in those prior years sitting at the higher end of our reserve actuaries' ranges. Rate increases were in the 10% range. So we continue to push for rate to cover loss trends. And we're also pulling other portfolio management levers such as increasing deductibles and leveraging data analytics for risk selection.

Moving to workers' compensation. Net premiums written there declined for the quarter, while the loss ratio came in at 42.6% for the quarter and 41.1% for the year. Here, too, for both the quarter and for the year, we continued to experience favorable prior year loss development. Frequency for workers' comp continues to trend down as we've seen over many years, while severity trend remains relatively stable. So we think our rate levels remain adequate even with some rate decreases in the low single-digit range.

So in General Insurance, we expect solid growth and profitability to continue in 2024, reflecting the success of our specialty strategy, our excellence initiatives in our new underwriting subsidiaries.

So I'll leave it at that for now with General Insurance, and we'll turn the discussion over to Carolyn to report on Title Insurance. Carolyn?

Carolyn Jean Monroe
Senior Vice President of Title Insurance

Thank you, Craig. In the Title group, we reported premium and fee revenue for the quarter of $645 million, a 23% decrease from the fourth quarter of 2022.

Our agency premiums were down 25% and direct premiums and fees were down 11% from the fourth quarter of prior year.

Our pretax operating income of $44 million did compare to $45 million in the fourth quarter of 2022, and our combined ratio of 95.5% compared to 96.2% in the fourth quarter of prior year.

As we have discussed on previous earnings calls, 2023 was a challenging real estate market. Our full year premiums and fees reflect those market conditions and were down around 33% compared to 2022. Agency premiums made up 79% of our total premium and fees in 2023. While our full year pretax operating income of $134 million was lower than 2022, we are really pleased with the progress we did make during the year. We were able to reduce our operating expenses 19% compared to 2022 and we ended 2023 with a full year combined ratio of 97.1%.

In addition to managing our costs, our leadership team has continued with a focus on strategic planning. From an IT perspective, modernizing the company has been a real priority. We have had a multiyear approach with several initiatives to optimize our processes, procedures and operating structure. This includes improvements in automation and technology. These initiatives improve the efficiency of our teams which will allow us to take advantage of improving market conditions when they occur with less of a need to scale up. During 2024, we will continue looking to identify all economy of scale advantages.

Commercial transactions were really not exempt from the market contraction. We saw a small decrease of around 1% in commercial premiums during the fourth quarter compared to the third quarter. Our 2023 commercial premiums decreased in line with overall premiums compared to 2022. Commercial premiums were 22% of our total premiums for both years. We believe our transformed nationwide footprint positions us well for when the commercial market rebounds.

Although housing affordability, low inventory and relatively elevated interest rates persist as we begin 2024, we are optimistic that market conditions will improve with just a little bit of uncertainty when this will take place.

And with that, I'll turn it back to Craig.

Craig Richard Smiddy
President, CEO & Director

Thank you, Carolyn. So we remain pleased with our continued profitable growth in General Insurance, which is helping to mitigate the lower revenues and profit levels in Title Insurance. And we also remain pleased with our capital management efforts, including the $806 million returned to shareholders through dividends and share repurchases in 2023.

For 2024, as I say, we remain optimistic for continued profitable growth within General Insurance, while we remain, as Carolyn indicated, of the view that Title Insurance will continue to face mortgage interest rate and real estate marketplace headwinds.
So that concludes our prepared remarks. And we'll now open up the discussion to Q&A, and either I'll answer your question or I'll ask Frank or Carolyn to respond.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Gregory Peters from Raymond James.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Well, good afternoon, everyone. So I guess the stock markets kind of was surprised today by your numbers, even though they were pretty good. But, Craig, maybe you could give some more detail around what's going on in severity and commercial auto. And talk about some of the rate actions you've accomplished or achieved over the last year or 2 to sort of mitigate what's going on in severity there?

Craig Richard Smiddy
President, CEO & Director

Sure, Greg. I'd be happy to add more color with regard to commercial auto. So I'll reiterate first by saying what I said a few moments ago, and that is, when we see something unfavorable, we react quickly. When we see something favorable, we react slowly. And what we saw in the current accident year was severity that pushed up. I reported on the last quarterly call that we were seeing severity of around 10%. That moved up into the lower double-digits, more toward the 12% range. And we took a look at where we were at in the current accident year and decided to raise our accident year loss ratio, commensurate with what we were seeing in that severity uptick.

I think the issue that gets masked, just looking at that fourth quarter result is, as we said in the release, we're putting 4 quarters of increased loss ratio pick into the fourth quarter. But certainly -- that loss ratio is certainly not what we expect going forward. And just to put things in context here, if you look at where we ended the year, we ended the year at a current accident year loss ratio of 76.2%. Last year in 2022, our accident year loss ratio pick was 76.4%. So this is very stable. And by no stretch are things developing in a way that we think we're overreacting to. And again, just looking at those current accident year picks, very stable.

So just to round out the picture to our reported numbers, in 2023, we reported a 71.5% loss ratio. That included 4.7 points of favorable development and then the 76.2% accident year loss ratio that I spoke to. So juxtaposing that against 2022, we reported a 66.6% loss ratio for that year, but that included 9.8 points of favorable development.

And as we indicated on our calls when we saw very robust favorable development numbers in certain quarters, we made it very clear that those were not sustainable kind of favorable development numbers. But the 4.7% in '23 is still a very robust prior year development result. So back to '22, you have the 66.6% reported loss ratio, development -- favorable development of 9.8% for that year and the initial loss pick of 76.4%. Rounding it back out where I started, that loss pick in '22 of 76.4% compares to where we ended '23 at 76.2%. So as I say, put it in context, things are very stable.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

And just to go back to part of your answer, where this is, I think, something consistent inside Old Republic, where you recognize the bad news quickly, but recognize the good news more slowly, is there -- when I think about the commercial auto, our views to think on previous calls, the concept of a lockbox, are you still on the case in commercial auto, not really recognizing any favorable trends from the most recent accident years? Is that a fair assessment of what's going on inside that line of business?

Craig Richard Smiddy
President, CEO & Director

Yes. Consistent with our past practice, as you say, Greg, our approach is to lock down the accident years, raise those lock picks if we see anything coming through that looks unfavorable. And the only time, as you and I have discussed on prior calls, that where we feel forced to release some reserves is when we exceed the higher end of the range and because our reserves are still redundant, in those prior years that we would be deemed excessive. That's the only case where we would consider looking at those lockdown years.

But relatively speaking, it -- the practice is absolutely the same as it has always been; very conservative approach, and we hold as much as we possibly can on prior years in the way of those loss ratio picks.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Fair enough. And then I wanted -- in the press release and in previous conversations, you've highlighted this concept of what the targeted combined ratio of the combined General Insurance business should look like over the course of the cycle. In your press release, I think you cited this 90% to 95% sort of range. And if I look at the results for the last 3 years, all at the low end of what -- or the low end of that range, coming in around 90%. I think that's kind of consistent with what's going on with pricing because there's -- we've been in pretty much of a hard market.

Is there anything that's happened in the last year that would cause at least the near-term outlook to go from this low 90s to the upper end or the middle of the range, other than some of maybe the severity issues causing it? Or just give us some perspective on how you feel about where '24 will settle out inside that range. If you can provide some guidance, that would be helpful.

Craig Richard Smiddy
President, CEO & Director

Thanks, Greg, for the question. Right. So the current year result is, of course, inclusive of prior year favorable development. And as I mentioned just a few moments ago, as I mentioned in prior quarters, we've had very robust favorable prior year development.

So coming in at that level as we go forward, we ended '23 at 5.7 points of favorable development, that's more than we should expect going forward, consistent with comments previously made. We want to err on the side of at least a couple of points of favorable development each year. We'd better err on the side of favorable development, of course, as opposed to unfavorable.

So consistent with your question and those comments, you could expect that favorable development has been coming in the last few years again, in a very robust way that is not sustainable. However, on the current accident year loss ratio, we're not where we want to be yet. We still have areas in our business where that current accident year loss ratio is higher than we want it to be.

So as we continue to make improvements and here, too, we take a very conservative approach where even though we see the improvements being made, they're coming through in the short term, we are very reluctant to lower accident year loss picks until we have a high degree of confidence that they'll hold. And so we've gone very slowly.

Maybe we think -- I'll give an example, maybe we think that we've improved the loss ratio by 5 points. But our pick, maybe we will only take 1 point of improvement in the pick, and gradually get to where we think we are. So the point being that we would expect over time, the accident year loss ratio to trend lower, but we would also expect, going back to where I started, that this high level of favorable prior year loss development, it won't be sustained.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

I'm kind of smelling as I hear Chicago's finest, driving back to the station from lunch hour. It seems to be a quarterly tradition with your conference calls.

Craig Richard Smiddy

President, CEO & Director

What would be an Old Republic International conference call without Chicago Fire Department?

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Returning from lunch exactly. Can we pivot -- my last question, I'd like to give Carolyn some -- an opportunity to talk. And I think in your prepared remarks, Carolyn, you talked about technology investments, and with revenue having declined so substantially in Title, curious how the technology budget has changed with the lower revenues and how you think about these investments going forward.

Carolyn Jean Monroe
Senior Vice President of Title Insurance

So we're very mindful of the way the slower revenues, but there's just some things that when you're a company that manages for the long run that you have to continue doing. And we are fortunate that we've been allowed to continue investing in our technology, and a lot of it has to do with being prepared for -- with the cyber issues, that type of thing. It just isn't the right time to really cut back. We have put some things that maybe we could say were a lower priority that we've set aside.

But the things that really help us manage our business, that help it make it easier to do business with us, that enable us to be more efficient, we really didn't have to cut back doing. We're allowed to continue with those investments.

Operator

[Operator Instructions] Our next question comes from Greg Powell from Miller Howard Investments.

Gregory Lee Powell
Miller Howard Investments, Inc.

My question is about the runoff business. I was a little surprised that you had a loss on that sale given that you've been dividend and cash out of it. So I have 2 questions. Could you just explain the loss? And second, is the $25 million the last dividend from that unit?

Craig Richard Smiddy
President, CEO & Director

Sure. I'd be happy to start with the easy part, which is yes, the $25 million is the last dividend. The other part of the question is there are several factors here. You've looked at what mortgage insurance companies are valued at right now and they're valued at approximately book value. And then you compare that to a runoff mortgage company without any new business coming in and the valuation, which we did a very robust market evaluation of with our investment banker and a very robust bidding process. I believe there were about actually 30 different parties that we reached out to, the valuation was actually very good, in our opinion, and in many other outsiders' opinion as to where we ultimately sold the business.

The thing you have to look at is the diminishing level of premium that is occurring in that book of business, as it is run off, and the diminishing level of reserves commensurate with that premium, and then ultimately, how much, going forward, we would be able to generate additional revenue that would allow us to produce a profit and release much more capital.

At some point, things like fixed expenses hit a point where you just can't cut any more and premiums are coming down. So you hit a point where you actually will create an earnings drag and that makes it very difficult to produce revenue and the ability to release capital diminishes over time.

So we really hit an inflection point, where it made perfect sense to enter into the sale even though if it was at a loss to book value. We think over time, again, we would have seen an earnings drag and not been able to release the levels of capital that we had extracted. We had extracted a large amount of capital since the business went into runoff, and again, we were hitting an inflection point.

Gregory Lee Powell
Miller Howard Investments, Inc.

Okay. Can you tell us what's the book value?

Craig Richard Smiddy
President, CEO & Director

With the book value you're saying -- that at year-end...

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

It's about $170 million at year-end.

Craig Richard Smiddy
President, CEO & Director

So 80% of that was -- that component was 80% price for the sale, and then we have transaction costs. The net of tax loss should be about $30 million.

Gregory Lee Powell
Miller Howard Investments, Inc.

Okay. Gotcha. And just on the commercial auto, could you just maybe give us a little more confidence that the 10% price increases are enough?

Craig Richard Smiddy
President, CEO & Director

Well, as best we can. We keep a very close eye on it, and I would refer to our track record, vis-à-vis our competitors to the industry. I think we're one of the very few that has prior year favorable development on commercial auto because we got in early, recognized, and I'm going back 4 or 5 years, recognize the severity trends, achieved rate increases above or at those severity trends, which is why we were able to produce such levels of favorable development in those prior years.

So I think our track record speaks for itself, that you just look at the level of favorable reserve development from those prior years as a result of us keeping up with trend. And the action we took on accident year '23 in the fourth quarter, was because it's doing exactly what we say we do, when we see something we [Technical Difficulty]

Operator

Ladies and gentlemen, this is the operator. We are experiencing technical difficulties. Please stand by.

Craig Richard Smiddy
President, CEO & Director

Can you hear us?

Francis Joseph Sodaro
Senior VP, CFO & Chief Accounting Officer

Now we can.

Craig Richard Smiddy
President, CEO & Director

I don't want to [Technical Difficulty]

Gregory Lee Powell
Miller Howard Investments, Inc.

Hello?

Operator

Hello, Mr. Powell.

Gregory Lee Powell
Miller Howard Investments, Inc.

Yes.

Operator

This is the operator. I'm just reconnecting.

Gregory Lee Powell
Miller Howard Investments, Inc.

Okay. Great.

Craig Richard Smiddy
President, CEO & Director

Okay. Thank you very much. We here in Chicago are back on. There was a technical difficulty, and we lost our connection, and we apologize to everyone for that.

So I'll just pick up with that last question about severity on the commercial auto. Again, we think our track record speaks for itself. We, unlike most of our competitors, have had favorable prior year reserve development on commercial auto. And why that is the case is because 4 or 5 years ago, when severity started to come through, we reacted with rates and risk selection and produced those strong accident year results that led to favorable development.

So we're very quick to react when we see severity coming through and the rate increases that we've had over the last many years has demonstrated in the numbers that we do a very good job of noticing severity and reacting to severity, particularly with making sure that our rate changes are commensurate with that severity or even in excess of that severity that we're observing.

So I'll leave it at that. Are there any other questions?

Gregory Lee Powell
Miller Howard Investments, Inc.

I'm all set.

Operator

We have no further questions in queue. I would like to turn the call back over to management for closing remarks.

Craig Richard Smiddy
President, CEO & Director

Okay. Well, thank you, everyone, very much. Again, we apologize for that technical glitch, but we appreciate your patience. We appreciate your support, and we had a strong 2023, and we are very optimistic as we head into '24, that 2024 will be a very strong year as well.

Thank you all very much.

Operator
This concludes today's conference call. Thank you for your participation. You may now disconnect.