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Earnings Call

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Call Participants

EXECUTIVES

Brian Scott Hertzman
Senior VP & CFO

Carl Henry Lindner
Co-CEO & Director

Diane P. Weidner
Vice President of Investor & Media Relations

Stephen Craig Lindner
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ANALYSTS

Andrew E. Andersen
Jefferies LLC, Research Division

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

Michael David Zaremski
BMO Capital Markets Equity Research

Presentation

Operator

Good day, and thank you for standing by. Welcome to the American Financial Group Third Quarter 2024 Conference Call. [Operator Instructions] Please be advised that today's conference call is being recorded.

I would now like to hand the conference over to your first speaker, Diane Weidner, Vice President of Investor Relations. Please go ahead.

Diane P. Weidner
Vice President of Investor & Media Relations

Thank you. Good morning, and welcome to American Financial Group's Third Quarter 2024 Earnings Results Conference Call. We released our 2024 third quarter results yesterday afternoon. Our press release, investor supplement and webcast presentation are posted on AFG's website under the Investor Relations section. These materials will be referenced during portions of today's call.

I'm joined this morning by Carl Lindner III and Craig Lindner, Co-CEOs of American Financial Group; and Brian Hertzman, AFG's CFO.

Before I turn the discussion over to Carl, I would like to draw your attention to the notes on Slide 2 of our webcast. Some of the matters to be discussed today are forward-looking. These forward-looking statements involve certain risks and uncertainties that could cause our actual results and/or financial condition to differ materially from these statements.

A detailed description of these risks and uncertainties can be found in AFG's filings with the Securities and Exchange Commission, which are also available on our website.

We may include references to core net operating earnings, a non-GAAP financial measure, in our remarks or in responses to questions. A reconciliation of net earnings to core net operating earnings is included in our earnings release.

And finally, if you're reading a transcript of this call, please note that it may not be authorized or reviewed for accuracy. And as a result, it may contain factual or transcription errors that could materially alter the intent or meaning of our statements.

Now I'm pleased to turn over to Carl Lindner III to discuss our results.

Carl Henry Lindner
Co-CEO & Director

Good morning. I'll begin my remarks by sharing a few highlights of AFG's 2024 third quarter, after which Craig and I will walk through more details. I will then open it up for Q&A, where Craig, Brian and I will be happy to respond to your questions.

I'm pleased to report an annualized third quarter core operating return on equity of 16%. Underwriting margins in our Specialty Property and Casualty Insurance businesses held up nicely despite elevated catastrophe losses particularly from Hurricane Helene during the quarter. And higher interest rates increased Property and Casualty net investment income by 15% year-over-year. Craig and I thank God, our talented management team and our great employees for helping us to achieve results.

I'll now turn the discussion over to Craig to walk us through some of the details.

Stephen Craig Lindner
Co-CEO & Director

Thank you, Carl. Please turn to Slides 3 and 4 for a summary of earnings information for the quarter. AFG reported core net operating earnings of $2.31 per share in the 2024 third quarter. Higher year-over-year catastrophe losses related primarily to Hurricane Helene and lower favorable prior year reserve development in the P&C insurance operations were partially offset by higher investment income.

Now I'd like to turn to an overview of AFG's investment performance and financial position and share a few comments about AFG's capital and liquidity. The details surrounding our $15.7 billion investment portfolio are presented on Slides 5 and 6.

Looking at results for the third quarter, Property and Casualty net investment income was approximately 15% higher than the comparable 2023 period, reflecting impact -- the impact of rising interest rates, higher balances of invested assets and higher returns on alternative investments.

As you'll see on Slide 6, approximately 67% of our portfolio is invested in fixed maturities. In the current interest rate environment, we're able to invest in fixed maturity securities at yields of approximately 5.5%. Current reinvestment rates compare favorably to the 5% yield earned on fixed maturities and our P&C portfolio during the third quarter of 2024. The duration of our P&C fixed maturity portfolio, including cash and cash equivalents was 2.9 years at September 30, 2024.

The annualized return on alternative investments at our P&C portfolio was approximately 5.4% for the 2024 third quarter compared to 4.2% for the prior year quarter. Longer term, we continue to remain optimistic regarding the prospects of attractive returns from our alternative investments with an expectation of annual returns averaging 10% or better.

Please turn to Slide 7, where you'll find a summary of AFG's financial position at September 30, 2024. During the quarter, we returned $59 million to our shareholders through the payment of our regular quarterly dividends. In conjunction with our earnings release, we declared a special dividend of $4 per share payable on November 26, 2024, to shareholders of record on November 15, 2024. The aggregate amount of the special dividend will be approximately $335 million. This special dividend is in addition to the company's regular quarterly cash dividend of $0.80 per share which was recently increased to 12.7% over the previously declared rate and paid on October 25, 2024.

With this special dividend, the company has declared $50 per share or $4.2 billion in special dividends since the beginning of 2021, including $6.50 per share in 2024. Carl and I consider these special dividends to be an important component of our total shareholder return. We expect our operations to continue to generate significant excess capital throughout the remainder of 2024 and into 2025, which provides ample opportunity for acquisitions, special dividends or share repurchases over the next year.

For the 3 and 9 months ended September 30, 2024, AFG's growth in book value per share, excluding AOCI plus dividends, was 4% and 13.9%, respectively. Our strong operating results, coupled with effective capital management and our entrepreneurial opportunistic culture and disciplined operating philosophy enable us to continue to create value for our shareholders.

I'll now turn the call back over to Carl to discuss the results of our P&C operations.

Carl Henry Lindner
Co-CEO & Director

Thanks, Craig. Please turn to Slides 8 and 9 of the webcast, which include an overview of our third quarter results. As you'll see on Slide 8, our Specialty Property and Casualty Insurance business generated a 94.3% combined ratio in the third quarter of 2024, 2.1 points higher than what we reported in the third quarter of 2023. Results for the 2024 third quarter included 4.4 points of catastrophe losses compared to 3 points in the third quarter last year.

Losses from Hurricane Helene represented about 2/3 of our catastrophe losses in the third quarter. No named storm exceeded our corporate property cat retention of $70 million during the quarter, and we believe our careful management of coastal exposures has served us well over many years. The losses we incurred from Hurricane Helene were not driven by coastal exposure with the vast majority of these losses coming from noncoastal areas in Georgia and the Carolinas.

Although our remarks are focused on third quarter results today, I'd like to comment on estimated losses from Hurricane Milton, which made landfall in Florida on October 9. We currently estimate that pretax losses from Hurricane Milton will be about $30 million and will be reflected in our fourth quarter results.

Results in the third quarter benefited from 0.8 points of favorable prior year reserve development compared to 2.3 points in the third quarter of 2023. Prior year reserve development continued to be favorable within each of our Specialty Property and Casualty groups during the third quarter. Favorable prior year reserve development in our workers' compensation businesses, along with several other businesses more than offset some adverse development and selected social inflation exposed casualty businesses.

Third quarter 2024 gross and net written premiums were up 19% and 14%, respectively, when compared to the third quarter of 2023, driven primarily by additional premiums from the Crop Risk Services acquisition. Gross and net written premiums, excluding crop insurance, each grew 7% year-over-year. We continue to achieve year-over-year premium growth as a result of a combination of new business opportunities, increased exposures and a good renewal rate environment.

Average renewal pricing across our Property and Casualty Group, excluding our workers' comp businesses, was up approximately 8% in the third quarter and up approximately 7% overall. Third quarter average overall renewal pricing was about 1% higher than pricing increases achieved in the second quarter. We've reported overall renewal rate increases for 33 consecutive quarters and we believe we are achieving overall renewal rate increases in excess of prospective loss ratio trends to meet or exceed targeted returns.

Now I'd like to turn to Slide 9 to review a few highlights from each of our Specialty Property and Casualty business groups. Details are included in our earnings release, so I'll focus on summary results here. The businesses in the Property and Transportation Group achieved a 96.5% calendar year combined ratio overall in the third quarter of 2024, 1.7 points higher than the 94.8% reported in the comparable '23 period. Higher year-over-year underwriting profit in our agricultural businesses was more than offset by higher catastrophe losses, primarily from Hurricane Helene.

Third quarter 2024 gross and net written premiums in this group were 32% and 26% higher, respectively, than the comparable prior year. The primary drivers of the growth include additional premiums from the Crop Risk Services acquisition and to a lesser extent, later reporting of crop acreage, which shifted the timing of reporting of some crop premium from the second quarter to the third quarter of 2024. Excluding crop premiums, third quarter gross and net written premiums each grew 11% year-over-year in this group, which is attributable primarily to new business opportunities, a favorable rate environment and increased exposures in our commercial auto, property & inland marine and ocean marine businesses.

Crop insurance premiums represented about half of the net earned premiums in this group for the third quarter of 2024, reflecting the seasonality of the crop business and growth from the CRS acquisition. Consistent with historical practice, we record results in the current year to a combined ratio in the high 90s, which, particularly in the third quarter, elevates our overall combined ratio to some extent until we had better visibility into our full year crop results. The majority of the calendar year crop profitability is generally reflected in our fourth quarter financial statements.

As we think about crop profitability for the current crop year, it's important to remember that most of our crop insurance is revenue protection where both the harvest price of the crops and yields impact claims. Harvest pricing for corn and soybeans, which was determined in October, settled 11% and 13% lower than the spring discovery prices, respectively. The harvest of corn and soybean crops is running ahead of 5-year averages. Yield variability will be important to our final results. Noting that the average farmer deductible is a little over 20% and considering harvest pricing, we're optimistic about an above-average crop year.

Some Property and Transportation. Overall, renewal rates in this group increased 7% on average in the third quarter of 2024, about 1 point lower than the pricing achieved in the group for the second quarter of 2024. I'm particularly pleased with the renewal rates achieved in our commercial auto liability line of business where rates were up 12% in the third quarter. This is our 13th year of rate increases in this line.

So the businesses in our Specialty Casualty Group achieved a strong 90% calendar year combined ratio overall in the third quarter. Higher underwriting profit in our target markets businesses was more than offset by lower year-over-year underwriting profit in our excess and surplus businesses and to a lesser extent, our workers' comp and executive liability businesses. Underwriting profitability in our workers' compensation and executive liability businesses continues to be excellent.

Third quarter 2024 gross and net written premiums increased 6% and 4%, respectively, when compared to the same prior year period. Primary drivers of growth were new business opportunities and favorable renewal pricing in several of our targeted market businesses and our excess liability business. Our mergers and acquisitions business also benefited from an increase in M&A activity. This growth was tempered by slightly lower workers' compensation premiums.

Excluding workers' compensation, third quarter gross and net written premiums in this group both grew 8% year-over-year. Excluding our Workers' Compensation businesses, renewal rates for this group were up approximately 10% in the third quarter and up 8% including Workers' Comp. Both measures improved about 3 points from the renewal pricing in the previous quarter. And I continue to be pleased that we continue to achieve renewal rate increases of 10% or better during the quarter in several of our social inflation exposed businesses, including our social services, excess liability and public entity businesses.

Specialty Financial Group continued to achieve excellent underwriting margins and reported a 91.9% combined ratio for the third quarter of 2024, 4.3 points higher than the prior year period. Cat losses contributed 14.4 points to the third quarter '24 combined ratio compared to 9.3 points in the prior year third quarter.

Improved results in our lender services business were more than offset by lower profitability in our Surety and Fidelity businesses. Third quarter 2024 gross and net written premiums were up 7% and 9%, respectively, when compared to the prior year period, due primarily to the growth in our financial institutions business. Renewal pricing in this group was up 6% for the quarter, consistent with the previous quarter.

To conclude, we're pleased with the results in the third quarter and year-to-date. Through the first 9 months of 2024, our annualized core operating return on equity is excellent at 18%. The calendar year combined ratio in our Specialty Property and Casualty business is 91.9%, 0.6 points above where we were last year at this time. In addition, we're selectively growing our Specialty businesses at a healthy rate, pricing is exceeding expectations and investment performance continues to be strong. We're well positioned to continue to build long-term value for our shareholders for the remainder of 2024 and beyond.
We'll now open the lines for the Q&A portion of today's call, and Craig and Brian and I will be happy to respond to your questions. Thank you.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Michael Zaremski of BMO.

Michael David Zaremski
BMO Capital Markets Equity Research

First question is kind of a high-level question on the loss ratio. A number of companies or a handful of companies, sorry, have kind of been proactively disclosing that they've been adding to their IBNR, so incurred but not reported, bucket of reserves over the past year or 2 in light of just a rising trend line, especially in social inflationary lines. Just curious if you'd be able or willing to kind of give us a flavor of whether AFG has -- great American and American Financial Group has also been adding to that kind of that bucket as a percentage of historical levels?

Brian Scott Hertzman
Senior VP & CFO

So when you look at our businesses, it's really a business unit by business unit as in addition to looking for rate increases in the social inflation exposure business and getting them there. We also have changed some terms and conditions. So it could be a little tricky to analyze the IBNR when, for example, in an excess business, maybe the attachment point is different than it was before. So it's not exactly the same product as what you might have seen in previous years. But we look at each business unit, the reserve position of each business unit every quarter and react to new information very quickly, particularly negative news. That process can result in favorable or adverse development for any business unit in any quarter. We've just been fortunate to have more favorable [indiscernible] adverse development in those periods. This particular a quarter, we did see some elevated large losses in our umbrella and excess liability businesses and reacted to that and to the best that we can, we would reflect new information into all of our action year pick, so that can cause us to elevate our picks and then book some IBNR. But I think in looking at the IBNR versus case reserves, there's lots of factors going into it that you can't just really give a number.

Michael David Zaremski
BMO Capital Markets Equity Research

Okay. Got it. Yes. I appreciate there's a lot of moving parts. Okay, maybe switching gears a bit, Craig, I believe you made remarks -- prepared remarks saying you think the alternative investment portfolio can eventually get back to 10% plus returns, but you can correct me if I'm wrong. Just curious, is that -- is the market normalizing in terms of fundamentals for real estate? And is that kind of a -- you're becoming just incrementally more confident that in the quarters to come, you'll get kind of back to the target returns?

Stephen Craig Lindner
Co-CEO & Director

Sure. Let me start out by giving you my view of the more traditional private equity investments. Hard to predict the returns, but certainly a strong market -- stock market should favor marks on the traditional private equity investments.

Now let me switch to multifamily, I give you my view. So multifamily represents a little less than half of our alternative investments. And the operations have held up just fine. We're projecting that for the year, even with the new supply coming into the market, our NOI will be flattish with last year. We did incur some negative marks. Our general partners do March every quarter on the properties that we've invested in. And we -- because of increased cap rates that are driven by higher interest rates, we did incur some negative marks that we booked in the first 9 months of the year. We do benefit from having very attractively priced fixed rate debt on 54 of our 58 properties. I think the average rate on those 54 properties, the loans out of 54 properties is around 4% or just over 4%. So we're in like -- we're different than some others in that we have -- do have good protection because of the financing that we have in place.

Let me give you my view of the multifamily business. Multifamily starts now are at a 10- or 11-year low. So we've had a lot of new building in the last couple of years, a lot of new supply coming on stream. I think the peak of that is probably right now, probably the third quarter and fourth quarter is the peak of multifamily completions. Given that new starts are at a 10- or 11-year low, there's been a couple of point in time probably toward the end of next year where the new supply is going to be absorbed, and we're going to, once again, have very strong pricing power. So think it probably takes another 9 months, 12 months or so to absorb the new supply that's coming on the market. I do think that toward the end of next year, when there is going to be very little new supply hitting the market, that the pricing power will again be very strong.

One other thing that has changed here recently is clearly, there are -- there is significant buying interest in multifamily properties again. That has changed here in the last couple of months. We just signed an agreement to sell one of our properties. It's a property in Colorado, that we agreed to sell at a 4.60% cap rate based upon trailing 12 months NOI, which we found pretty attractive. And we are seeing some transactions now for the first time in a while. So that's kind of my view of multifamily and kind of what we expect in the next year or so.

Michael David Zaremski
BMO Capital Markets Equity Research

That's comprehensive. And just lastly, I'm pivoting back to the Property and Casualty Insurance operations and specifically kind of the competitive environment on pricing. So in the Specialty Casualty, it feels like we see that your pricing sequentially kind of accelerated fairly meaningfully. I'm going to assume that that's kind of coming from the social inflationary exposed lines. I feel like we've been seeing data points from that from your peers. I don't know if you have any comments on that. Property and Transportation, I don't know if you might have given us an update. I know your commercial auto rate increases were -- have been running well in excess of, I think, the market in recent quarters. If you can kind of remind us how that's trending. I see that pricing was down a little bit sequentially there, too. But just curious on kind of the pricing environment for the social inflationary exposed lines like commercial auto and some of the Specialty Casualty stuff.

Carl Henry Lindner
Co-CEO & Director

Yes. I think I mentioned earlier that I feel good about the continued favorable pricing environment, particularly with the social inflation exposed to lines. Commercial auto liability, we got another 12% price increase in the third quarter. I believe that number is 16% year-to-date. So a good favorable number. Things can vary quarter-by-quarter. And then in the businesses like excess liability lines, public sector, our nonprofit businesses that are some of the more social exposed businesses in that 10% plus strong double-digit increases in those lines is what we continue to have, both in the third quarter. And when you look at year-to-date, it's pretty much the same. So I feel good about that, and the continued favorable pricing environment that we're in.

Operator

Our next question comes from the line of Andrew Andersen at Jefferies.

Andrew E. Andersen
Jefferies LLC, Research Division

You had mentioned some adverse development on social inflation lines. Could you please talk about what action years that was from and maybe size the magnitude?

Brian Scott Hertzman
Senior VP & CFO

This is Brian. I think when you look at our Casualty businesses, I think the first thing to kind of anchor in on is the results overall, where our Casualty Group has a combined ratio of 90% for the third quarter and 88.4% for the first 9 months. With those kinds of combined ratios, that's ROEs in the high 20s or better, so they're really good results overall for our Casualty businesses. But if you just want to focus in on the favorable development there and still on that favorable development, as we noted, we did have continued good favorable development out of Workers' Comp, but we have that offset by some of the social inflation exposed businesses. And it is large loss activity over a number of years.

So it's not just the older years, it is a little bit in some of the more recent years. We're talking about it because it is reducing our favorable development overall, but the results in general are very good. And we feel confident with what we know on now with our reserves, not that things can't happen, but we're really good with ROEs that come from business that's in the 90s in the long run.

Andrew E. Andersen
Jefferies LLC, Research Division

And maybe sticking on just the Casualty segment. The underlying loss ratio had some pretty notable improvement year-over-year. Could you just maybe talk about some of the drivers there?

Brian Scott Hertzman
Senior VP & CFO

Sure. So particularly in like our targeted markets business where we would have things like Public Sector business or Specialty Human Services business, there's ones where we have been getting significant rate and ones where in some of the prior periods, we had some adverse development, we're seeing improvements in the action year results there as we have taken action in those books both pricing wise and terms and conditions wise and appetite-wise, that we're seeing much improved results out of those targeted markets and consistent results in the Workers' Comp.

Operator

Our next question comes from Meyer Shields of Keefe, Bruyette, & Woods.

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

So one quick reserve question, if I can. Because Carl, you sounded very optimistic about commercial auto, I'm wondering whether that was a line that faced any social inflation requiring a reserve adjustment?

Brian Scott Hertzman
Senior VP & CFO

Are you asking us the -- if the -- if any of the adverse development was related to commercial auto liability?

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

Yes.

Brian Scott Hertzman
Senior VP & CFO

So we didn't really have that in our Transportation segment. What I would say in some of our program businesses in Casualty, there was a little bit of adverse development [indiscernible] commercial liability, but it wasn't a big driver of the numbers.

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

Okay. That's helpful. Second question, and I don't want to suggest an overreaction. But when you talk about -- again, Carl talked about the non-coastal exposure to Hurricane Helene, how do you think about sort of reassessing noncoastal exposure to catastrophes after an issue like this?

Carl Henry Lindner
Co-CEO & Director

Meyer, it's always interesting during my career, each catastrophe then always has things that you learn from it. Even going back to Hugo and things where again, there is more loss inland than what you think. And even in some of the California earthquakes where they weren't supposed to be fault lines like in Northridge, I believe when I think they had, so I think you always try to learn from every event and tighten up where you can. And the kinds of things that we can do is change our -- the price that we're charging, like in our lender-placed property or property in the marine. You can always limit flood exposure more if you want to. So there's lots of levers that you can pull to kind of customize your approach within the property side. So believe me. Every time we have an event, we learn and we look at the numbers, and we try to make sense changes in our approach.

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

Okay. Perfect. And if I can throw 1 quick question in for Craig. It looks like the market today is anticipating higher for longer interest rates. And I was wondering how should we think about the response in terms of asset allocation or portfolio duration throughout the investment portfolio?

Stephen Craig Lindner
Co-CEO & Director

Meyer, as you know, we have intentionally kept the duration of the portfolio fairly short. We just didn't see lots of value or we didn't think it was the right time to be buying a lot of long-duration securities. I think we're going to be certainly a beneficiary of a higher interest rate environment. On the conference call, I talked about a 5.5% reinvestment rate with rates moving up the way they have today. I'd say it could be something over 5.5%, which compares to the 5% yield that we reported in the last quarter. So I think we're positioned very well for a higher interest rate environment. I think today, we would think that yields are not, certainly short-term rates are coming down, but longer-term rates are not. We're very pleased with our position to a short-duration portfolio. And if rates do move much from here, we're in a position to benefit from that.

Operator

Our next question comes again from Andrew Andersen of Jefferies.

Andrew E. Andersen
Jefferies LLC, Research Division

Just thinking about higher cats this year and then the comment about above-average crop profitability. If we go back to the beginning of the year, you kind of had some underlying business plan assumptions, including $11 of EPS and a similar combined ratio relative to 90.3% in 2023. Do you still expect to achieve both of those metrics?

Carl Henry Lindner
Co-CEO & Director

Well, we're not changing our perspective on our business plan right now. I think we -- you still can have more catastrophes in the fourth quarter. Our Milton projected losses seem to be reasonable and kind of within our model at this point. And then it kind of gets down to really through year-end, just how good of a crop year we end up having in that. And now it's a matter of seeing what actual claims, the numbers of claims, kind of the average claims, and that kind of thing through in that business through year-end and into January. I think we'll have a much better feel of our overall crop profitability and just how good it is the next time we report for sure.

Operator

At this time, I'm showing no further questions. I would now like to turn the call back to Diane Weidner, Vice President, Investor Relations for closing remarks.

Diane P. Weidner
Vice President of Investor & Media Relations

Thank you, and I appreciate all the good questions today, and thanks for your time joining us this morning as we recap our third quarter results. We look forward to talking with all of you again next quarter, and hope you have a great rest of your day.

Operator
Thank you for your participation in today's conference. This does conclude the program, and you may now disconnect.