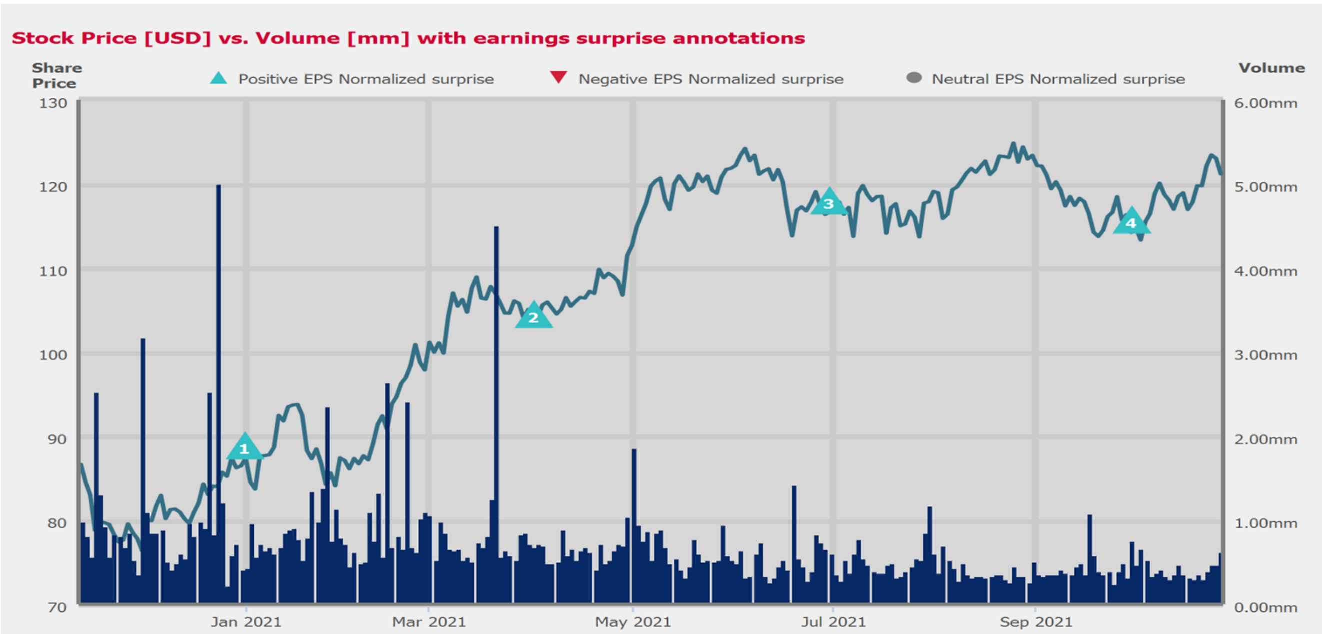
# Cincinnati Financial Corporation NasdaqGS:CINF
# FQ3 2021 Earnings Call Transcripts

## Thursday, October 28, 2021 3:00 PM GMT

## S&P Global Market Intelligence Estimates

| | -FQ3 2021- | | | -FQ4 2021- | -FY 2021- | -FY 2022- |
|---|---|---|---|---|---|---|
| | CONSENSUS | ACTUAL | SURPRISE | CONSENSUS | CONSENSUS | CONSENSUS |
| **EPS Normalized** | 0.91 | 1.28 | ▲40.66 | 1.41 | 5.49 | NA |
| **Revenue (mm)** | 1743.30 | 1785.00 | ▲2.39 | 1787.23 | 8012.95 | NA |

Currency: USD
Consensus as of Oct-28-2021 11:39 AM GMT




**- EPS NORMALIZED -**

| | CONSENSUS | ACTUAL | SURPRISE |
|---|---|---|---|
| **FQ4 2020** | 1.20 | 1.61 | ▲1 34.17 % |
| **FQ1 2021** | 1.10 | 1.37 | ▲2 24.55 % |
| **FQ2 2021** | 0.98 | 1.79 | ▲3 82.65 % |
| **FQ3 2021** | 0.91 | 1.28 | ▲4 40.66 % |

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# Call Participants

## EXECUTIVES

**Dennis E. McDaniel**
*VP & Investor Relations Officer*

**Michael James Sewell**
*CFO, Principal Accounting Officer, Senior VP & Treasurer*

**Stephen Michael Spray**
*Senior VP, Chief Insurance Officer & Director*

**Steven Justus Johnston**
*Chairman, President & CEO*

## ANALYSTS

**Charles William Lederer**
*Wolfe Research, LLC*

**James Paul Bach**
*Keefe, Bruyette, & Woods, Inc., Research Division*

**Mark Alan Dwelle**
*RBC Capital Markets, Research Division*

**Paul Newsome**
*Piper Sandler & Co., Research Division*

# Presentation

**Operator**

Good day, and thank you for standing by. Welcome to third quarter 2021 earnings conference call. [Operator Instructions]

I would now like to hand the call over to your speaker today, Mr. Dennis McDaniel, Investor Relations Officer. Sir, you may proceed.

**Dennis E. McDaniel**
*VP & Investor Relations Officer*

Hello. This is Dennis McDaniel, Investor Relations Officer at Cincinnati Financial. Thank you for joining us for our third quarter 2021 earnings conference call.

Late yesterday, we issued a news release on our results, along with our supplemental financial package, including our quarter end investment portfolio. To find copies of any of these documents, please visit our investor website, cinfin.com/investors. The shortest route to the information is the Quarterly Results link and a navigation menu on the far left.

On this call, you'll first hear from Chairman, President and Chief Executive Officer, Steve Johnston; and then from Chief Financial Officer, Mike Sewell. After their prepared remarks, investors participating on the call may ask questions. At that time, some responses may be made by others in the room with us, including Chief Investment Officer, Marty Hollenbeck; and Cincinnati Insurance's Chief Insurance Officer, Steve Spray; Chief Claims Officer, Marc Schambow; and Senior Vice President of Corporate Finance, Theresa Hoffer.

First, please note that some of the matters to be discussed today are forward-looking. These forward-looking statements involve certain risks and uncertainties. With respect to these risks and uncertainties, we direct your attention to our news release and to our various filings with the SEC.

Also, a reconciliation of non-GAAP measures was provided with the news release. Statutory accounting data is prepared in accordance with statutory accounting rules and therefore is not reconciled to GAAP.

Now I'll turn over the call to Steve.

**Steven Justus Johnston**
*Chairman, President & CEO*

Thank you, Dennis. Good morning, and thank you for joining us today to hear more about our third quarter results. Overall, it was another good quarter. While weather-related catastrophes were lower than a year ago, communities across our country were impacted by hail, wind, flooding and fire. As we send our field claims associates into these communities, they shine, providing excellent service in reassuring affected families and businesses.

Net income for the third quarter of 2021 fell $331 million compared with the third quarter of last year due to $457 million less benefit on an after-tax basis in the fair value of securities held in our equity portfolio. Equity portfolio fair value changes have caused significant earnings volatility for several quarters recently, and net income increased $1.3 billion for the first 9 months of 2021 compared with a year ago despite the third quarter decrease.

Non-GAAP operating income for the third quarter of 2021 more than tripled, up $146 million or 232% versus a year ago, with lower catastrophe losses on an after-tax basis, contributing $31 million of the increase.

Our 92.6% third quarter 2021 property casualty combined ratio was 11 percentage points better than last year with decreased catastrophe losses this year, representing 4.1 points of the improvement.

Our current accident year combined ratio before catastrophe loss effects also continued to improve and was 2.5 percentage points better than the first 9 months of 2020.

Premium growth continued at a nice pace during the quarter as a strengthening economy and great relationships we enjoy with our agents helped us grow ahead of industry estimates.

Consolidated property casualty net written premiums rose 10% in the third quarter of 2021. We continue to focus on risk segmentation, giving our underwriters the tools they need to retain and write more profitable accounts while walking away from opportunities when we determine pricing is inadequate.

Renewal pricing during the third quarter continued to be ahead of our estimate for prospective loss cost trends for each property casualty segment.

Our commercial lines insurance segment again experienced mid-single-digit percentage range estimated average renewal price increases, down slightly from the second quarter. Our third quarter personal lines segment average renewal price increases slowed a little compared with the second quarter, including personal auto in the low single-digit range, while the excess and surplus lines insurance segment continued in the high single-digit range.

Our commercial lines segment had an outstanding quarter with this 80.6% combined ratio improving by 21.8 percentage points compared with the third quarter a year ago and growing net written premiums by 10%. For our personal lines segment, third quarter net written premiums grew 7% as it continued to benefit from planned expansion of high net worth business produced by our agencies. Its third quarter 2021 combined ratio was higher than a year ago, largely due to driving patterns moving towards pre-pandemic levels, increasing our personal auto loss ratio. Personal auto still produced a small underwriting profit for the third quarter. And for the first 9 months of 2021, our personal lines segment, in total, had an underwriting profit. Our excess and surplus line segment produced a sub-95% combined ratio for the third quarter and the first 9 months of the year and grew third quarter net written premiums by 30%.

Cincinnati Re and Cincinnati Global each grew net written premiums in the third quarter of 2021. While both experienced significant losses from Hurricane Ida leading to underwriting losses for the quarter, we weren't surprised by the level of loss we saw for an event of this magnitude based on our models.

Our life insurance subsidiary produced third quarter 2021 net income of $11 million and grew term life insurance earned premiums by 8%.

I'll conclude with the value creation ratio, our primary measure of long-term financial performance. Strong operating results, measured as net income before investment gains, were the largest component of our VCR for both the third quarter and the first 9 months of the year. VCR through September 30, 2021, was 12.4%, already reaching our annual average target range of 10% to 13%.

Now our Chief Financial Officer, Mike Sewell, will add perspective on some other areas of our financial performance.

**Michael James Sewell**
*CFO, Principal Accounting Officer, Senior VP & Treasurer*

Thank you, Steve, and thanks to all of you for joining us today. Investment income grew nicely during the third quarter of 2021, up 7% compared with the same period a year ago. Third quarter dividend income was up 11%, and net purchases for the equity portfolio totaled $153 million for the first 9 months of the year.

Interest income from our bond portfolio grew 7%, and the pretax average yield was 4.06%, up 3 basis points from the third quarter a year ago. The average pretax yield for the total of purchased taxable and tax-exempt bonds during the third quarter of 2021 was 3.43%.

Investing in the fixed maturity portfolio continues to be a priority with net purchases during the first 9 months of the year totaling $694 million. Valuation changes for our investment portfolio during the third quarter of 2021 were modestly unfavorable for both our stock and bond portfolios. The overall third quarter net loss was $158 million before tax effects, including $105 million for our equity holdings and $80 million for our bond holdings. At the end of the third quarter, total investment portfolio net appreciated value was approximately $6.7 billion, including $5.8 billion for our equity securities.

Cash flow was very strong in the third quarter, as it has been all year. It contributes to investment income and was a major factor in the 7% increase in interest income we reported for the third quarter. Cash flow from operating activities for the first 9 months of 2021 generated $1.5 billion, a 36% increase compared with the year ago period.

Expense management is another area we focus, always trying to optimize the balance of strategic business investments and expense controls. The third quarter 2021 property casualty underwriting expense ratio was 0.9 percentage points higher than last year's third quarter, including 1.2 points due to higher accruals for profit sharing commissions for agencies.

Moving on to loss reserves. Our approach to reserving remains consistent and aims for net amounts in the upper half of the actuarially estimated range of net loss and loss expense reserves. As we do each quarter, we consider new information, such as paid losses and case reserves and then updated estimated ultimate losses and loss expenses by accident year and line of business.

During the third quarter of 2021, we experienced $102 million of property casualty net favorable development on prior accident years. It favorably contributed to the combined ratio by 6.4% for the quarter. On an all-lines basis by accident year, net reserve development for the first 9 months of the year was favorable by $225 million for 2020, $46 million for 2019, $39 million for 2018 and $21 million, in aggregate, for all accident years prior to 2018.

Regarding capital management, we also follow a consistent approach, including share repurchases as part of a maintenance intended to offset issuance of shares through equity compensation plans. We believe that our quarter end financial strength was in good shape and provides plenty of financial flexibility. During the third quarter, we repurchased approximately 100,000 shares at an average price per share of $119.03.

I'll conclude my prepared remarks, as I typically do, with a summary of third quarter contributions to the book value per share. They represent the main drivers of our value creation ratio. Property casualty underwriting increased book value by $0.59. Life insurance operations increased book value by $0.05. Investment income, other than life insurance and net of noninsurance items, added $0.81. Net investment gains and losses for the fixed income portfolio decreased book value per share by $0.39. Net investment gains and losses for the equity portfolio decreased book value by $0.51, and we declared $0.63 per share in dividends to shareholders. The net effect was a book value decrease of $0.08 per share during the third quarter to $73.49 per share.

And now I'll turn the call back over to Steve.

**Steven Justus Johnston**
*Chairman, President & CEO*

Thank you, Mike. The COVID-19 pandemic has continued to demand flexibility in how we accomplish our day-to-day tasks. However, by staying focused on the steady execution of our long-term initiatives, we are able to keep producing these strong results. We have the people, the technology and the drive to continue delivering strong value for shareholders for years to come. As a reminder, with Mike and me today are Steve Spray, Marc Schambow, Marty Hollenbeck and Theresa Hoffer.
Grace, please open the call for questions.

# Question and Answer

**Operator**

[Operator Instructions] The first question comes from the line of Paul Newsome from Piper Sandler.

**Paul Newsome**
*Piper Sandler & Co., Research Division*

I'm curious as to whether or not you are seeing any of the same issues that some others have reported in personal lines with trying to get rate getting pushed back from the regulators. Because obviously, there was kind of effectively a windfall last year, but that's, I think, obviously temporary, but it doesn't really go into the math of how you file rates. Any thoughts on that? And if you -- are you seeing any some of the same issues that some others are seeing?

**Steven Justus Johnston**
*Chairman, President & CEO*

Well, I would say our relationships with our regulators are good that -- as a general statement, we are doing fine and getting rate increases or just changes to our rate structure approved. There are obviously some states that are tougher than others. But I think, overall, again, with good relationships with the regulators, we're in a good position vis-a-vis getting adjustments to our rating plans approved.

**Paul Newsome**
*Piper Sandler & Co., Research Division*

Great. And a broad question, I think, on inflation trends. Some of your peers have talked about the potential for a little bit higher inflation, particularly in the commercial lines side as we see maybe a resumption of cases coming through the courts and maybe perhaps a lag effect with some of the inflation that we've seen early on in home and auto showing up in the commercial lines side of the house. Any thoughts on that? Do you think that's a reasonable assumption? And does it show up in any way in your own numbers?

**Steven Justus Johnston**
*Chairman, President & CEO*

We certainly see the prospects. There's social inflation. There's the inflation of the cost and goods that we used to settle claims for cars, for houses, supply chain issues. There could be lags in the court system and so forth. We build this all into our models. And as we look at what we see to be loss cost trends, we try to be very prospective and look forward into what we think loss cost will be in the prospective policy period that we will be ensuring and feel comfortable that we're getting rate that is ahead of those loss cost trends in each of our segments.

**Paul Newsome**
*Piper Sandler & Co., Research Division*

Great. Congrats on the quarter. Always appreciate your insights.

**Steven Justus Johnston**
*Chairman, President & CEO*

Thank you, Paul.

**Operator**

Next up, we have Mike Zaremski from Wolfe Research.

**Charles William Lederer**
*Wolfe Research, LLC*

This is actually Charlie Lederer on for Mike. So for my first question, can you talk about the sustainability of the strong underlying margins? Were there any like notable like current year reserve development that benefited it?

**Steven Justus Johnston**

*Chairman, President & CEO*

We feel good, Charlie, about the sustainability of our results as we look forward with estimates of loss cost trends and pricing and feel comfortable in making our best estimates of our reserves, and we're very optimistic for the future performance of the underwriting of the company.

**Charles William Lederer**
*Wolfe Research, LLC*

Okay. And I know you mentioned the reserve releases by accident year. Could you give any color around the releases, particularly from the recent accident years?

**Michael James Sewell**
*CFO, Principal Accounting Officer, Senior VP & Treasurer*

Yes. Charlie, this is Mike Sewell. So related to -- as I mentioned, for the quarterly, it was 6.4 points. There was certain areas that were more on the current more recent accident years, which is probably no surprise when you think about the short tail lines, which would be commercial property, commercial auto, all of the personal lines. So mainly those developments were favorable in accident year 2020. But even with that, I'd be cautious with -- there's a lot of uncertainty with the pandemic and other things going on around there.

If I look at the workers' compensation, that's one of our longest tails that we have. That one has favorable development that I would say goes over several accident years, back a few years. So you're seeing favorable development there. The claims frequency seems to have declined a little bit, but we put a lot of cost control measures in over the years that has really been benefiting the workers' comp line of business.

And then lastly, commercial casualty, really, there, looking at the paid loss, case reserve data over time are important factors for how that -- how those develop. Those have been favorable and some of the more recent accident years, the last couple, not just the last one.

But as we look at, in total, for the property casualty business, you look at paid losses as a percent to incurred, it was up slightly for year-to-date 2021 versus last year, but it is below the 2017 through 2019 averages. So you'll see that in our supplement.

**Operator**

Your next question comes from the line of Mark Dwelle from RBC Capital Markets.

**Mark Alan Dwelle**
*RBC Capital Markets, Research Division*

Yes. Just a couple of questions. First, on the E&S unit, there was -- it wasn't very much in dollar terms, but there was a reserve addition there. I was wondering if you could talk about that in a little more detail as those are sort of rare.

**Steven Justus Johnston**
*Chairman, President & CEO*

I just think as we look at the environment, Mark, we see a little bit maybe of a -- I don't know if you call it, but a slowdown in the settlement rate there as we have claims that are taking a little bit longer to settle. And so in terms of coming up with our best estimate there, we want to recognize that, and that's what you're seeing.

**Mark Alan Dwelle**
*RBC Capital Markets, Research Division*

Okay. The second question I wanted to ask, I mean, you had a pretty strong growth in new business, certainly over the last year, but it was a pretty good quarter for new business. Anything that you're seeing in terms of the type of customers that you're winning or geographic spread of where you're winning? Just a little bit of color on where the new stuff is coming from.

**Stephen Michael Spray**
*Senior VP, Chief Insurance Officer & Director*

Yes. Mark, this is Steve Spray. We're seeing it across our entire footprint. And I think it -- as you mentioned, there's a little bit of an easier comp from the pandemic year last year. But I just think it -- again, it is execution of our agency-focused strategy, doing business locally, face-to-face with our agents, building deep relationships, underwriting and pricing every single account policy by policy. We're out there. We're aggressively trying to help our agents write business, solve problems. Our field reps, our field underwriters, we use that interchangeably, have the same pricing tools that our renewal underwriters have here. So we feel good about the pricing of the new business that we're writing. It's just -- I think it's just continued solid execution, quite frankly, across all of our segments on the new business front, and it goes to those deep relationships we have with our agents.

**Mark Alan Dwelle**
*RBC Capital Markets, Research Division*

And then one other question, also kind of relating mainly to renewals and the extent that you're getting premium audits that are flattering results a little bit. Can you just talk about kind of exposure unit growth? And to what degree that impacted the overall premium growth in the quarter?

**Stephen Michael Spray**
*Senior VP, Chief Insurance Officer & Director*

Sure. So on -- for commercial lines, all in, I would say that for the premium increase, about -- it's about half rate and about half exposure.

**Operator**

[Operator Instructions] Your next question comes from the line of James Bach from KBW.

**James Paul Bach**
*Keefe, Bruyette, & Woods, Inc., Research Division*

So you mentioned that the percent of paid losses to incurred was up, and I just wanted to see if you could give a little more detail on the negative 35% in IBNR that was reported for commercial lines on the quarter, just kind of some more detail on that.

**Steven Justus Johnston**
*Chairman, President & CEO*

Well, I think our actuaries, they look at a variety of methodologies. They use several methods. They look at a lot of different data points. In addition to paid losses, they'll look at case reserves, incurred losses, try to get an estimate for what we're seeing in terms of inflationary factors and set the best estimate that we can every quarter.

And I think it's been a good track record now with 31 or 32 years in a row now where we've had favorable development, so we're very confident it's an experienced team that hasn't changed over the years and feel comfortable with the estimates that they're making.

**Operator**

There are no further questions at this time. I will turn the call over back to our CEO, Mr. Steven Johnston, for any closing remarks. Sir?

**Steven Justus Johnston**
*Chairman, President & CEO*

Thank you, Grace. Excellent job with the call. And thanks to all of you for joining us today. We look forward to speaking to you -- with you again on our fourth quarter call. Have a great day.

**Operator**
Thank you, presenters. This concludes today's conference call. Thank you all for joining. You may now all disconnect.