S&P Global
Market Intelligence

The Hartford Financial Services Group, Inc. NYSE:HIG

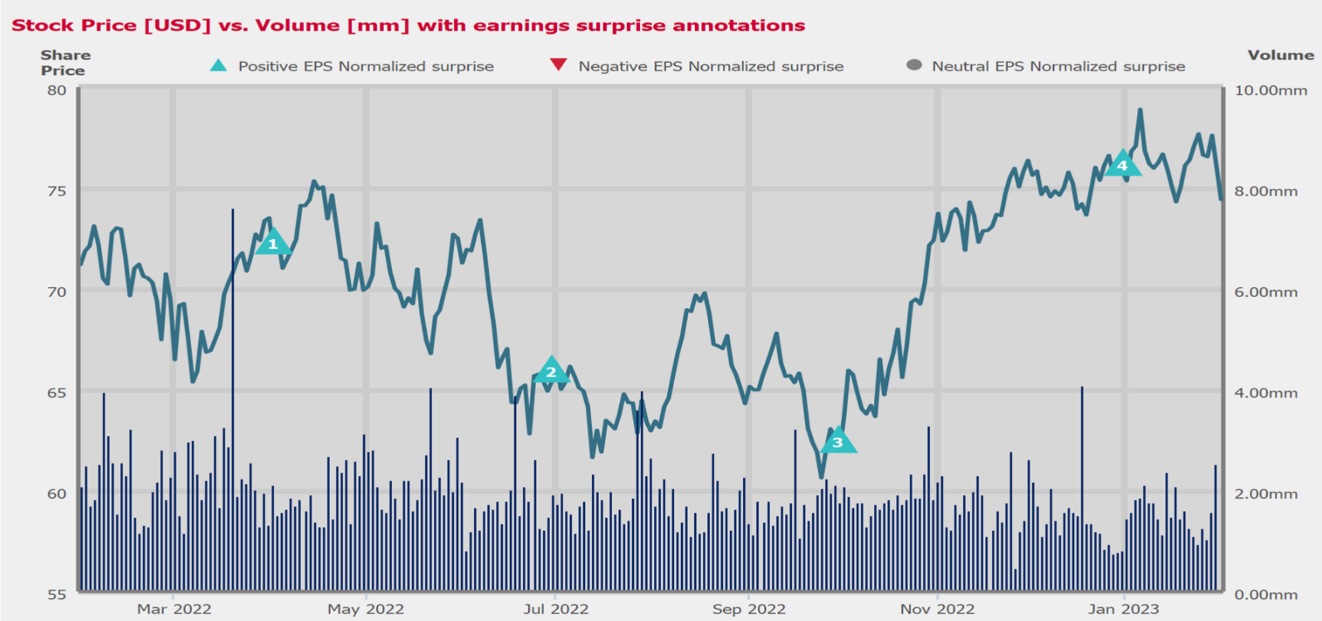
FQ4 2022 Earnings Call Transcripts

Friday, February 3, 2023 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2022-			-FQ1 2023-	-FY 2022-			-FY 2023-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	1.87	2.31	▲23.53	2.09	7.15	7.56	▲5.73	8.46
Revenue (mm)	5737.93	6016.00	▲4.85	5953.36	22648.93	22362.00	▼(1.27 %)	24092.51

Currency: USD
Consensus as of Feb-03-2023 8:50 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2022	1.55	1.66	▲7.10 %
FQ2 2022	1.52	2.15	▲41.45 %
FQ3 2022	1.22	1.44	▲18.03 %
FQ4 2022	1.87	2.31	▲23.53 %

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Presentation

Operator

Good morning, ladies and gentlemen, and thank you for attending today's Fourth Quarter 2022 The Hartford Financial Results Webcast. My name is Alex, and I'll be the moderator for today's call. [Operator Instructions]

I would now like to pass the conference over to your host, Susan Spivak with The Hartford Group. Susan, please go ahead.

Susan Spivak Bernstein
Senior Investor Relations Officer

Good morning and thank you for joining us today for our call and webcast on fourth quarter 2022 earnings. Yesterday, we reported results and posted all of the earnings-related materials on our website.

For the call, our participants today are Chris Swift, Chairman and CEO of The Hartford; Beth Costello, Chief Financial Officer; Jonathan Bennett, Group Benefits; Stephanie Bush, Small Commercial and Personal Lines; and Mo Tooker, Middle & Large Commercial and Global Specialty.

Just a few comments to cover before Chris begins. Today's call includes forward-looking statements as defined under the Private Securities Litigation Reform Act of 1995. These statements are not guarantees of future performance, and actual results could be materially different. We do not assume any obligation to update information or forward-looking statements provided on this call. Investors should also consider the risks and uncertainties that could cause actual results to differ from these statements. A detailed description of those risks and uncertainties can be found in our SEC filings.

Our commentary today includes non-GAAP financial measures. Explanations and reconciliations of these measures to the comparable GAAP measure are included in our SEC filings as well as in the news release and financial supplement.

Finally, please note that no portion of this conference call may be reproduced or rebroadcast in any form without The Hartford's prior written consent. Replays of this forecast and an official transcript will be available on The Hartford's website for 1 year.

I'll now turn the call over to Chris.

Christopher Jerome Swift
Chairman & CEO

Good morning and thank you for joining us today. Today, I will start with a summary of our fourth quarter and full year 2022 results and accomplishments. Then I will turn the call over to Beth to dive deeper into our financial performance and key metrics. After which, I will close our prepared remarks with a review of expectations for 2023. We will then be joined by our business leaders as we move into Q&A.

So let's get started. The Hartford is pleased to report an excellent fourth quarter, capping an outstanding year of financial performance and progress against our strategic objectives. Quarter after quarter, we are delivering strong financial results, demonstrating the power of the franchise and the depth of our distribution relationships. Our commitment to superior customer experience, the benefits of significant investments made over the last few years and superb execution by our 19,000 employees drive our success.

These competitive advantages helped us deliver exceptional results in 2022, including: Core earnings growth of 14% with core EPS growth of 23%; top line growth in Commercial Lines of 11%, with an underlying combined ratio of 88.3%; Group Benefits fully insured premium growth of 6%, with a core earnings margin of 6.5%; strong investment results with excellent limited partnership returns and increasing fixed income portfolio yields; and core earnings ROE of 14.4% while returning $2.1 billion of excess capital to shareholders. Looking forward, with strong momentum across all lines, I am confident we can continue to deliver superior results.

Now let me share a few highlights from each of our businesses. In Commercial Lines, written premium growth for the year was driven by strong exposure growth, pricing increases, higher policy retention and continued strong new business. Underlying margins improved by nearly 1 point driven by earned pricing, exceeding loss cost trends across most lines and growing expense leverage driven in large part by our Hartford Next program.

Across Commercial Lines, our brand, depth of distribution and enhanced underwriting capabilities, combined with excellent customer experience, have positioned us well to capture market share while maintaining or improving already strong margins. Small

Commercial results continue to be exceptional, consistently producing sub-90 underlying combined ratios with industry-leading products and digital capability, all of which drove record-breaking written premium and new business levels in 2022.

Going forward, Small Commercial will remain a growth engine for The Hartford. For example, beyond our traditional product lines, we will continue to expand our addressable market with capabilities in the excess and surplus binding lines. This portion of the E&S business is about an $8 billion market serving small business owners' property and liability exposures. With current written premiums exceeding $100 million and the evolving innovative capabilities within our broker quoting platform, we expect to become a leading destination for E&S binding opportunities and a strong complement to our existing admitted retail offering.

In Middle & Large Commercial, our team has done a tremendous job improving underlying margins by approximately 7 points since 2019 with a written premium compounded growth rate of 6% over the same period. In 2022, written premiums grew 10% for the year with improved policy retention and solid new business. Advancements in data science capabilities, industry-leading pricing and segmentation analytics and exceptional talent have delivered healthy margins, which I believe positions us well to continue driving profitable growth in this business.

In Global Specialty, I'm extremely pleased with the team's accomplishments since the strategic acquisition in 2019. Their tireless efforts have enabled us to meaningfully increase the size and scale of our specialty business to $3.6 billion of gross written premium, including over $800 million of E&S premium. We are leveraging the Global Specialty franchise to further grow and expand our capabilities across Commercial Lines in this $82 billion E&S market.

Global Specialty results in 2022 were outstanding, with an underlying margin of 84.6%, improving over 4 points from prior year and over 11 points from 2019, demonstrating our execution tenacity, enhanced underwriting tools and the expertise of the team. Our competitive position, breadth of products and solid renewal written pricing drove a 9% increase in gross written premium for the year, including 41% in our global reinsurance business, 19% in ocean marine and 27% in international casualty.

Turning to pricing. Commercial Lines renewal written price increases for the quarter were 4.9%, flat compared to the third quarter. Underneath, U.S. standard Commercial Lines renewal written pricing, excluding workers' compensation, accelerated from the third quarter to 7.9%, up 1 point, primarily driven by auto and property lines. Workers' compensation pricing remained positive, benefiting from average wage growth.

Within Global Specialty, excluding public company D&O, renewal written pricing remained stable in the mid-single digits, and in aggregate, in line with loss cost trends. Wholesale property, auto, primary casualty, all saw higher pricing increases over the third quarter, as did U.S. and international marine. Additionally, the public D&O market continues to be competitive with rate pressures, which requires new business discipline and a focus on retaining profitable current accounts.

Moving to Personal Lines. Pricing has accelerated across auto and home, resulting in written premium growth of 4% for the fourth quarter and 2% for the full year. Like others in the industry, auto underlying combined ratios remained elevated as we continue to experience inflationary pressure. We have been actively responding with rate filings throughout the year. In the fourth quarter, filed auto rates averaged 8.3% increase, up 3.4 points from the third quarter. In homeowners, we have kept pace with loss cost trends through net rate in insured value increases reflected in renewal written pricing of 10.7% for the year and 13.3% through the fourth quarter.

Turning to Group Benefits. Core earnings margin of 8.3% for the quarter and 6.5% for the full year represent significant increases from last year as excess mortality has materially declined. Meanwhile, long-term disability trends are stable and within our expectations for incident rates and recoveries. Fully insured sales for 2022 were $801 million, up 5%. And employer group persistency was approximately 92%, a strong result for the year. First quarter is off to an excellent start with persistency modestly higher and outstanding new sales results.

We expect the Group Benefits marketplace to remain dynamic as digital transformation, product innovation and customer demands accelerate. As a result, we are making significant investments today and have a clear road map for the future that I am confident will only strengthen our market leadership position going forward.

Now I will turn the call over to Beth to provide more detailed commentary on the quarter.

Beth A. Costello
Executive VP & CFO

Thank you, Chris. Core earnings for the quarter were $746 million or $2.31 per diluted share with a 12-month core earnings ROE of 14.4%.

In Commercial Lines, core earnings were $562 million. Written premium was up 9%, reflecting written pricing increases and exposure growth, along with an 18% increase in new business in Small Commercial and 6% in Middle Market. Policy count retention also increased in Small and Middle Market.

The underlying combined ratio of 87.4 improved from the prior year fourth quarter with both a lower loss ratio and expense ratio. Small Commercial continues to deliver superior operating results with an underlying combined ratio of 87.5. And Middle & Large Commercial delivered a solid 90.2. Global Specialty's underlying margin improved 5.8 points from a year ago to an outstanding 83 as it benefited from strong earned pricing increases.

In Personal Lines, core earnings for the quarter were $42 million. The underlying combined ratio was 96.2, reflecting continued auto liability and physical damage severity pressure driven by elevated repair costs as well as increased bodily injury trends and includes 2 points of losses related to prior quarters in 2022.

Written premium grew 4% for the quarter, largely reflecting pricing increases in both auto and home. In home, overall loss results were in line with our expectations. Non-CAT weather frequency continues to run favorable to long-term averages, and together with the effect of earned pricing increases, mitigates material and labor costs which remain at historically high levels. The expense ratio decrease of 3.5 points was primarily driven by lower marketing spend.

Current accident year CAT losses in the quarter were $135 million, which includes the benefit of a $68 million reduction in estimates from catastrophes that occurred during the first 3 quarters of 2022, including $31 million related to Hurricane Ian. Winter Storm Elliott losses were $167 million net of reinsurance, of which, $150 million was in Commercial Lines.

Total net favorable prior accident year development within core earnings was $46 million, primarily related to reserve reductions in workers' compensation, catastrophes and bonds, partially offset by reserve increases in general liability and commercial auto.

We completed our annual asbestos and environmental reserve study in the fourth quarter, resulting in a $229 million increase in reserves comprised of $162 million for asbestos and $67 million for environmental. All of the $229 million was ceded to the adverse development cover, leaving $256 million of limit remaining. The increase in asbestos reserves was primarily due to an increase in the cost of resolving asbestos filings and a modest increase in the company's share of loss on a few specific individual accounts. The increase in environmental reserves was mainly due to an increase in the estimate for PFAS exposures, one large account settlement and higher estimated site remediation costs.

Before turning to Group Benefits, I would like to review the January 1 reinsurance renewals. Overall, we are very pleased with placements and terms and conditions for our programs against the backdrop of a challenging renewal season. Our per occurrence and aggregate property catastrophe protection were renewed at an approximate 20% increase in cost and 28% on a risk-adjusted basis, which based on publicly available information compared favorably with overall market increases and speaks to the quality of our book of business and favorable experience.

Overall, the structure of our property CAT program did not change significantly. We increased the attachment point on the $200 million aggregate cover to $750 million, up from $700 million. There were also some changes in the treaty that provides coverage for certain loss events under $350 million. We have summarized these changes in the slide deck.

In addition to our property catastrophe program, we also successfully renewed several other reinsurance treaties, which also experienced rate increases with limited changes in terms and conditions. The rates we charge insureds already have been incorporating these higher costs, and therefore, we do not expect any significant adverse combined ratio impact from these renewals.

Turning to Group Benefits. Core earnings in the fourth quarter of $141 million and the 8.3% core earnings margin reflect a lower level of excess mortality losses and growth in fully insured premium. The disability loss ratio improved 6.1 points from the prior year quarter, which had elevated estimated long-term disability incidence trends.

In addition, COVID-19-related short-term disability losses were lower this quarter. All-cause excess mortality was $43 million before tax compared to $161 million in the prior year fourth quarter. The group life loss ratio, excluding excess mortality, increased 4.7 points primarily due to higher accidental death losses as compared to very favorable experience in the fourth quarter of 2021.

Turning to Hartford Funds. Core earnings were $39 million, reflecting lower daily average AUM primarily due to equity market declines and higher interest rates over the past 12 months.

And lastly, investment results were strong in the quarter with net investment income of $640 million. Our fixed income portfolio is continuing to benefit from the higher interest rate environment. The total annualized portfolio yield, excluding limited partnerships, was 3.7% before tax, a 40 basis point increase in the third quarter. We anticipate our portfolio yield, excluding limited partnership returns, will increase by approximately 50 to 60 basis points in 2023 compared to the full year 2022 before tax yield of 3.2%.

Our partnership returns of 16.8% in the fourth quarter and 14.4% for full year 2022 were exceptional. Performance was primarily driven by income from opportunistic sales within our commercial real estate JV equity portfolio which generated annualized returns of 31% in the fourth quarter. Our private equity holdings were also resilient, delivering a 7% annualized return in the quarter. For the full year, real estate generated a 22% return and private equity generated a 14% return.

As we enter 2023, we expect continued volatility in markets. Given outlooks for a slowdown in consumer consumption, corporate investment and M&A activity, we expect our private equity returns to be below our long-term target. At the same time, the increase in financing costs and the reduced availability of real estate financing is expected to impact sales activity in our real estate JV equity. With this backdrop, we expect a 4% to 6% return for partnership and other alternative investments in 2023.

Turning to capital. As of December 31, holding company resources totaled $1 billion. For 2023, we expect dividends from the operating companies, of $1.5 billion from P&C, $400 million from Group Benefits and $125 million from Hartford Funds.

During the quarter, we repurchased 4.9 million shares for $350 million. As of the end of the year, we have $2.75 billion remaining on our share repurchase authorization through December 31, 2024.

To wrap up, our businesses performed strongly in 2022, and we are well positioned to continue to deliver on our targeted returns and enhance value for all our stakeholders.

I will now turn it back to Chris.

Christopher Jerome Swift
Chairman & CEO

Thank you, Beth. Let's take it forward, where I'd like to share a few thoughts about 2023. Underpinning the outlook is our commitment to disciplined underwriting and expanding or maintaining margins while prudently growing our book of business.

In 2023, we are expecting a Commercial Line's underlying combined ratio in the range of 87 to 89. Total renewal written price increases in Commercial Lines, excluding workers' compensation, are expected to be fairly stable compared with 2022. Meaningful increases in standard commercial property, auto and general liability pricing are somewhat offset with competitive pricing headwinds in parts of our financial lines business. In our Global Reinsurance book, we expect meaningful written price increases, including over 30% for U.S. and European product coverage. Commercial loss cost trends are expected to remain fairly stable with some moderation in property severity as inflation is expected to ease during the second half of the year.

Before I get into specific trends for our market-leading workers' compensation business, let me remind you of its current margin strength and stellar contribution to our overall Commercial Line results.

Looking back over the last 25 years, our loss ratio results have outperformed the industry on average by approximately 5 points, reflecting our significant competitive advantages in pricing sophistication, underwriting analytics and claim management. In addition, our scale and wealth of data allow us to anticipate, identify and quickly react to emerging trends as we manage retention and growth in this line.

Over the past 10 years, our standard Commercial Lines workers' compensation book has produced combined ratios averaging near 90, while our premier Small Commercial book has performed even better with an average combined ratios in the mid-80s. Also impressive is the 6-point underlying loss ratio improvement since 2019 in Middle Market, accomplished by equipping our underwriters with advanced risk segmentation tools. We expect workers' compensation to remain a highly profitable business and an important earnings contributor to The Hartford.

Turning to a few specifics in our forecast. Workers' compensation renewal written pricing, which is comprised of net rate and average wage growth, is projected to be flat to slightly negative. Loss costs are expected to be up slightly as long-term frequency and severity selections remain unchanged from 2022. We will continue to use our market-leading tools and underwriting expertise in risk selection and book management to minimize any margin compression. In 2023, we expect workers' compensation returns to remain attractive, with deterioration equating to roughly 0.5 point on the Commercial Lines underlying combined ratio.

In summary, for Commercial Lines, we are extremely confident in our ability to manage our book through a variety of economic and market environments. An underlying combined ratio within a range of 87 to 89 will be an outstanding result and reflects our ability to execute consistently and deliver superior margins.

Turning to Personal Lines. We expect a 2023 underlying combined ratio in the range of 93 to 95. In auto, renewal written price is expected to accelerate into the mid-teens by the second quarter and remain there for the balance of the year. By midyear, we expect new business to be price-adequate. Loss cost trends, primarily driven by severity, are expected to remain elevated during the first half of the year before returning to more normal levels in the second half. In homeowners, we expect earned pricing to generally keep pace with loss cost trends throughout 2023.

As we navigate this inflationary period across Personal Lines, we are focused on balancing rate adequacy, quality of new business and marketing productivity. Overall, I am confident we have the right execution plans to return this business to targeted profitability in 2024.

In Group Benefits, we expect the 2023 core earnings margin to be between 6% and 7%, consistent with our long-term margin outlook of the business. With COVID shifting from pandemic to endemic state, excess mortality losses are expected to improve versus 2022. However, we expect mortality trends will settle above prepandemic levels, and we are pricing business accordingly. All in, group life loss ratios are expected to improve versus 2022. And in group disability, we expect some moderation of recent favorable incidence and recovery trends.

Before closing, I'd like to share a few recent ESG achievements. This year, The Hartford will be honored as 1 of 2 global Catalyst Award winners for advances we have made in diversity, equity and inclusion. The Catalyst Award is the premier recognition of organizational DE&I efforts driving representation and inclusion for women. The Hartford was also named to the Bloomberg Gender Equality Index and to America's Most Just Companies list for 2023, having earned both honors every year since their inception. The recognition we continue to receive is a testament to our long-standing commitment to sustainability and the dedication and hard work of our teams.

In closing, let me summarize why I'm so bullish about the future for our shareholders.

One, our 2022 financial results demonstrate the effectiveness of our strategy and the benefits of continued investments in our business, resulting in strong growth and margins in Commercial Lines, Group Benefits operating at targeted returns and a Personal Lines business tracking back to target margins.

Two, we have the capability to sustain superior returns as a result of our performance-driven culture, outstanding underwriting and pricing execution, exceptional talent and innovative customer-centric technology.

Three, investment income is increasing, supported by a diversified portfolio of assets. And credit quality remains healthy.

And finally, we are proactively managing our excess capital to be accretive for shareholders.

All these factors contribute to my excitement and confidence about the future of The Hartford. Our franchise has never been better positioned to deliver industry-leading financial performance with a core earnings ROE range of 14% to 15% while creating value for all our stakeholders.

Let me now turn the call over to Susan for Q&A.

Susan Spivak Bernstein
Senior Investor Relations Officer
Thank you. Operator, we have about 30 minutes for questions. Could you please repeat the instructions for asking a question?

Question and Answer

Operator

[Operator Instructions] Our first question for today comes from Brian Meredith from UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of questions here. First one, just curious, if I look at Hartford Next, it looks like you got another $65 million to recognize on expense saves coming through in 2023, get to about 0.5 points on the expense ratio. Are there some offsets we should think about in '23 that will maybe make it so we don't see that 0.5 points?

Christopher Jerome Swift
Chairman & CEO

Brian, thanks for the question. Thanks for joining. You are right. I mean The Hartford Next program is contributing to our overall efficiency and effectiveness. And it does have about a 0.5 points benefit in -- as we head into 2023.

The second part of your question is, do you see any challenges to executing on that? As we sit here today, no. I mean I think that's a good assumption, if I understood your question correctly.

Brian Robert Meredith
UBS Investment Bank, Research Division

Yes, yes. Exactly, that's it. So I mean, the 0.5 points should be beneficial. Okay. Good.

And then, Chris, I'm just curious. Obviously, a really strong property market right now from a pricing perspective. It sounds like you took advantage of some of the property pricing in the reinsurance marketplace. I'm just curious, could you maybe talk a little bit about your capabilities, capacity, willingness to kind of lean into the property markets right now and see some good growth in that business, and perhaps margin-accretive for your '23 results?

Christopher Jerome Swift
Chairman & CEO

I think, Brian, you've picked up on one of our key strategic initiatives over, really, the last 5 years: To be a bigger property writer. Maybe it's not known by you sort of firsthand, but we have about $3 billion of property premium, including homeowners premium of about $1 billion. So it is an area of focus. It's an area of growth for us. We do operate on the small end with a BOP product in middle and large. And we also have developed an E&S property capability. And as I mentioned in my prepared remarks, we have some assumed reinsurance property exposures around the world.

So it is, on a primary basis, an area we're leaning into that will ultimately help continue to diversify our book of business so that we're a more balanced organization going forward. So yes, it is a focus of ours going forward.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. If I could just squeeze one more in. Group Benefits, are you seeing any impact yet from some of the layoffs that we're seeing at large corporations?

Christopher Jerome Swift
Chairman & CEO

I would share with you and ask Jonathan Bennett to comment. Generally, no. I mean we have a book of business that range from, obviously, large global organizations to small and middle-sized organizations. But the trends in our book are fairly stable.

Jonathan, what would you add?

Jonathan Ross Bennett
Executive VP & Head of Group Benefits

I definitely agree with what you said, Chris. I'd point out, in the fourth quarter, we had growth of earned premium and fees of about a little over 8%, so a strong fourth quarter. And as you pointed out in your comments, we're off to a great start in January with good new sales and strong persistency. So we're on the watch. We are aware of all the announcements that's happening as well. But where we sit today, we're in pretty good shape, and looking forward to 2023.

Operator

Our next question comes from Mike Ward of Citi.

Michael Augustus Ward
Citigroup Inc., Research Division

I had a question on workers' comp. I'm just curious what you're assuming around underlying losses. And how big might you say the headwind is to the year-over-year underlying combined ratio?

Christopher Jerome Swift
Chairman & CEO

Yes. Thank you for the question, Michael. I alluded to some of this in my prepared remarks, so I will try to connect the dots maybe a little bit better.

But as we defined sort of renewal pricing, a combination of pure net rate and then exposure growth with additional workers, I mean, that's likely to be flat at best to slightly negative. And then if you overlay sort of our consistent long-term medical cost inflation of 5 points and a frequency assumption that is generally consistent with our long-term trends, I mean, that will have a negative impact on our combined ratio. And I sized it about 0.5 point in relation to our overall Commercial Lines combined ratio.

I think the other hand, though, you got to connect the dots, as -- again, as I said in my prepared remarks, we are getting good net rate in auto, property particularly, and the expense efficiencies, that more than offsets that 0.5 point of decline. And really, at the point, if I really measure it more precisely, we see 0.5 point of Commercial Lines improvement year-over-year.

Michael Augustus Ward
Citigroup Inc., Research Division

Okay. Great. Maybe on the CAT loss guidance. Curious, how are you able to keep it relatively similar to last year? Just thinking about inflation and modestly higher retentions under the reinsurance treaties.

Christopher Jerome Swift
Chairman & CEO

Yes. I would -- again, good question. I think the gist of it, as Beth said in her prepared remarks, our reinsurance treaties have not changed dramatically from a risk side. We're very pleased with the overall renewal. And that's consistent sort of with our modeling and expectation, particularly given the exposures that we enjoy today.

So would you add any other color, Beth?

Beth A. Costello
Executive VP & CFO

Yes. The only other thing I would add. I mean it is up just 0.1 points if you look at what our guidance was last year. And as a reminder, we've been talking about we've been taking rate in the property book. So that obviously is there to mitigate some of the cost pressures that you referred to. And then again, as Chris commented on, our structure of our CAT program, not changed significantly.

Operator

Our next question comes from Greg Peters of Raymond James.

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

I'm going to -- for the first question, I would like to focus on the retention steps that you put in your supplement, both for Commercial and Personal Lines. In listening to the comments of others, it seems like the trends of retention might be moving up in Commercial and down in Personal. Yet when I look at your numbers, it looks pretty stable. Can you talk to us, both in Commercial and Personal, about what you're seeing on policy retention and how that factors into your outlook for next year? Or this year, I should say.

Christopher Jerome Swift
Chairman & CEO

Sure, Greg. And then I might ask Stephanie and Mo to add their color in their respective businesses. I would say at the outset, it's sort of been our priority to really take care of our book of business, principally because we've worked so hard to improve it, so hard to acquire the right new customers. And I mean, you see the margins and the returns that we're generating.

So the #1 priority we have going into the year is taking care of customers, trying to do everything you can to prevent a piece of business going out to bid and creating a shopping opportunity. And that's good to retain. It's obviously not so good when you're looking to see if there's new business opportunities. But generally, it's the most profitable strategy, to just take care of your existing customers with the necessary rate increases that keeps pace with loss cost trends.

So Stephanie, how -- what would you say in Small and Personal Lines?

Stephanie Bush
Head of Small Commercial & Personal Lines

Sure. So in Small Commercial, I would share is that it is very strong and stable, which I really believe is a testament to our entire business model. And I've shared these comments before in other forums. Everything that we do across the entire business model really lives into 3 key principles: Being easy to do business with; being accurate when we provide that pricing and that overall experience; and then being consistent, particularly when you come from a renewal perspective.

We have been consistently, particularly in the BOP and the auto lines, been taking rate, measured rate over an extended period of time. And so we continue to build confidence with our agents and our small business owners. So I would expect that you would still continue to see healthy and strong retention in Small Commercial.

When I go over to the Personal Lines space, and I'll start with auto. As we all know, the market is -- there's a bit of disruption going on. And as you can see in our results, we've been very stable. We have been taking rate for 12 quarters straight, and we'll continue to take rate. And so it gives us confidence in terms of our overall offering.

We're continuing to step up the rate changes that Chris and Beth referenced in their prepared comments. But overall, I would expect Personal Lines to be somewhat stable. Potentially a very modest decline in auto this year in 2023, but overall stable.

Christopher Jerome Swift
Chairman & CEO

Mo, what would you add?

Adin Morris Tooker
Head of Enterprise Sales & Distribution, Global Specialty, Middle and Large Commercial

Yes, I'd echo many of Stephanie's Small Commercial themes. I think we feel really good about both the Middle & Large Commercial and the Global Specialty books in terms of the quality of what we have. And as such, will -- the retention will play an important role in our strategies.

We are watching closely -- as Chris has talked about, we were watching closely the workers' comp and the public D&O. We feel really good about the quality of those books, but there's a little bit more pressure there. So I think retention and rate is a little bit more tactical there. But again, we feel great about the quality of both books, and we'll protect them.

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

Just as a follow-up, and I know you addressed it in your opening comments, and Stephanie just mentioned it again. But -- and I'm looking at your guidance for Personal Lines for '23 of 100.5 to 102.5. And then I'm looking at what happened in auto, particularly in the combined ratio, really spiking up in the fourth quarter. I know there's rate coming.

Is it your sense that we're sort of beginning to approach sort of like the peak or trough profitability for auto in the next couple of quarters? Or do you expect it to remain at these elevated levels as we see in the fourth quarter?

Christopher Jerome Swift
Chairman & CEO

Yes. What I would say, Greg, is that, at least the first half of the year, I think you're going to see an elevation, maybe a modest decline from where we are today. And remember, we have about, Stephanie, 5 points of seasonality in sort of the auto results this quarter.

So -- but if you even look at the full year auto results of 101, 102, yes, it's got some improvement to do. We're focused on it. But I think that improvement will accelerate in the second half of the year, to the point where we could actually see margin improvement during the fourth quarter.

But we're going to have to execute hard on rate plans, work with all our government relations and regulator friends to get those approved, which we know how to do. But it's -- there's a magnitude of volume of activity that does need to happen.

Operator

Our next question comes from Elyse Greenspan from Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Appreciate all the color on the call. My first question, Chris. You -- it sounds like you upped the ROE guidance, right, 14% to 15% as it previously been 13% to 14%. When going through the pieces of everything, it sounds like it's more a reflection, right, of just improved investment income in -- on the fixed income portfolio. But am I missing something in making those observations?

Christopher Jerome Swift
Chairman & CEO

Yes. Thanks for joining us, Elyse. I would say you're right. The NII is a big component, particularly coming off just the interest rate moves in our fixed income portfolio. But as Beth also said, we do expect lower alternative returns this year. But I do think that there is underlying margin improvement in our commercial book of business that maybe is underappreciated, and I would explain that.

The guidance that we set, I think, is prudent. It's thoughtful, it's reactive of the conditions that we have. But we have a high degree of confidence of achieving particularly at the midpoint. So from there then, we play to outperform. And I think we've got a good track record of outperforming over time, and that's the mission next year.

So the guidance says what it is. It does imply really when -- really measure it on a refined basis, about 50 basis points of improvement. But I don't think we're going to be done from there. And all that goes into our views of what our overall ROEs will be next year, including our buyback programs.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And then my second question -- you guys are -- the dividend to the holdco are going to be higher this coming year. Group did go up. And I know you guys have kind of targeted a balanced level of capital return. But given the extra dividends to the holdco, could we expect capital return to pick up in '23 via share repurchase?

Beth A. Costello
Executive VP & CFO

Yes. So Elyse, yes, you're right. The dividend from Group Benefits are increasing. I would characterize that as sort of kind of getting back to normal. The last couple of years, they've been lower because obviously the statutory results have been impacted by the higher mortality losses. So we're kind of getting to more of our normal run rate, which we had contemplated when we evaluated the size of the update that we did to our share repurchase authorization. So I would call the increases just totally in line, and we're going to continue to execute on the plan that we have.

Operator

Our next question comes from Jimmy Bhullar of JPMorgan.

Jamminder Singh Bhullar
JPMorgan Chase & Co, Research Division

I had a question on workers' comp, following up on some of Chris' comments earlier. Obviously, margins have been pretty good, and it seems like you're expecting that to continue through 2023. Is it reasonable to assume that there's going to be a lot of pushback from regulators in allowing price hikes over -- even if you look beyond this year, until margins get a lot worse from where they are? Or do you think that at some point over the next 1 to 2 years, that the market could begin to show signs of an uptick in pricing?

Christopher Jerome Swift
Chairman & CEO

Yes. Again, as I said in my opening remarks, I mean, the trends there are some modest level of deterioration in our combined ratios, principally due to the pricing environment set by various regulators, and the experience that the industry has had.

I think you're really asking is, when do you see a turn? And it's a hard question to ask. But I think the components of a turn in pricing are starting to emerge, particularly as we get through the pandemic period, where frequencies were just down due to less economic activity, less work in general.

And those -- usually, the look-back period is 3 years on rate filings. So if you think of experience in '20 -- '19, '20, '21, that starts to leave your rate filings in '24. So I'm optimistic that there can be some at least reversal of negative price trends coming out of NCCI or other rating bureaus to allow maybe modest price increases some time in '24 heading into '25.

Jamminder Singh Bhullar
JPMorgan Chase & Co, Research Division

Okay. And then on Personal Lines, obviously, the loss ratio picked up, but the expense ratio declined considerably this quarter. Should we assume a similar expense ratio, given lower marketing, until the loss ratio begins to improve? Or what are your thoughts on that over the next year?

Christopher Jerome Swift
Chairman & CEO

Well, let me just start, and then I'll ask Stephanie to add her planning. Again, this year, we really cut back on marketing, particularly in the fourth quarter, to make sure that we had opportunities to add new customers that were really -- could be profitable with us as we earn that in. And we just really sort of slowed down marketing at this point in time. And as we head into '23, though, as I said, I think we become rate-adequate by the middle of the year and gives us an opportunity to think about marketing slightly differently.

But Stephanie, what would you say from a strategy side and then really an expense perspective?

Stephanie Bush
Head of Small Commercial & Personal Lines

I think you captured it well, Chris. A couple of other points I'd either underscore or add is that, yes, our marketing and media change was intentional in the late third quarter into the fourth quarter. We moved really more to more targeted and very productive marketing sources, so I want to confirm that we were still marketing. It's a very dynamic process, marketing source by marketing source.

But as Chris mentioned, we believe that we will be new business rate-adequate by midyear in the majority of the states. And you should expect to see our media spend continue to build throughout the year.

And then finally, with that new business rate adequacy, I would expect that we begin to start to see new business PIF count growth in the back half of the year. So think about how all of those components work together.

Christopher Jerome Swift
Chairman & CEO

But Jimmy, just to tie it all together. I would expect, on a year over year basis, expenses to be relatively flat.

Operator

Our next question comes from Andrew Kligerman of Credit Suisse.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Looking at Slide 16 of your presentation, I see that the annualized investment yield ex the LPs has really picked up nicely just Q-over-Q, from 3.2% to 3.7%. And we're seeing a little bit of pressure now on rates, but can you talk about where you see that annualized investment yield ex the LPs going over the next few quarters? And any insight you could provide there?

Beth A. Costello
Executive VP & CFO

Yes, I'll start with that. So as I said in my prepared remarks, when you look at that number and you think about for the full year, we're on an annualized basis of 3.2%, expecting that 50 to 60 basis point increase.

When you look at fourth quarter, just a couple of things, I think, to highlight on that is that, included in the yield ex partnerships, it's not just fixed maturities, it's also some other items as well. Think about dividends on equity securities and things like that. That can sometimes be a little bit lumpy.

So when I think about where we're ending the quarter at 3.7% as sort of going into Q1, probably not expecting to see a big increase quarter-over-quarter kind of on a run rate basis, and that kind of continues as we go through 2023. If you really look just at the fixed maturity yield, we're definitely seeing some increases there, and we'd expect to see that as we go through 2023 on that line. And you can see the details in our investor financial supplement of fixed maturities versus some of these other asset classes like equity securities and mortgage loans.

So we see it as a nice trajectory. We obviously had a nice lift this quarter. Our average purchases that we did, the yield was around 6%, which was a bit elevated. I wouldn't expect that to be the norm as we kind of go into Q1. It was a little bit elevated just because we ended the quarter -- ended the third quarter with some excess cash because we had divested of some treasury securities and pretty -- opportunistically invested at pretty high points from a yield perspective, which drove that up.

And I'd expect, like looking at January, that 6% is probably more like 5%, 5.10%. Does that help?

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Yes, very helpful. And Chris, I'm just -- I'm trying to get my arms around this workers' comp issue and when it's going to temper. I know you've already gotten 2 questions on it. Maybe you could give us a sense of how much -- you mentioned renewal written premium, slight negative. What was the rate component for that? Was that a pretty heavy negative? Was that 4 points down, [3] points down?

And with the stellar ratios that Hartford -- and I get that Hartford is probably best-in-class, period, in workers' comp. The second part of that question is, with ratios that have been around 90%, small and mid even better than that, will the regulators allow you to raise rates? Or will they penalize you for being best-in-class?

So I'm just trying to get my arms around that. Two questions, the rate and then again maybe a little more color on that outlook for getting rate in the future.

Christopher Jerome Swift
Chairman & CEO

Well, again, thanks for the question. Andrew, I would say it's always better to be best-in-class at anything, so you know that.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Agreed.

Christopher Jerome Swift
Chairman & CEO

So I'm going to disappoint you and say that, look, there's a lot of detail we provided. There's a lot of metrics that you could triangulate on, just focus on a sub-line with really nuanced details from an operating side. All I said is I really do think the rate -- the net rate and the rate then that we would get from increasing exposure. So the exposure of that acts like rate is going to be negative next year, slightly negative. And that's all I'm saying.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Okay. Maybe I'll just throw a quick one. And I was hoping -- I wasn't expecting a detailed answer. But fully insured group benefits sales up 52%. Maybe a little color on the products that were quite strong in the quarter.

Christopher Jerome Swift
Chairman & CEO

Yes. I'll let Jonathan add his color.

Jonathan Ross Bennett
Executive VP & Head of Group Benefits

Sure. In terms of our sales, good numbers in there, yes. Sometimes late in the year, you get opportunistically a sale or 2. A lot of our business trades in the first quarter, and then some other big numbers will happen oftentimes at the beginning of the third or maybe the fourth quarter.

But -- so some nice numbers for us in the quarter. Strong disability results for us, I would say, primarily. And we continue to see really good response to our voluntary, our supplemental, health product set. So those would include critical illness, hospital indemnity and accident. And that book has been building for us steadily now for a number of years and had our highest sales numbers in 2022 since inception of those programs.

So I think those are the ones that are really driving it, disability and sup health. We continue to compete effectively on the life side, but definitely a stronger mix on the disability and sup health side.

Operator

Our next question comes from Meyer Shields of KBW.

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

Broadly speaking, can you talk about your appetite for allocating more investments to LPs and alternatives over the next few years, given the higher interest rate environment?

Christopher Jerome Swift
Chairman & CEO

Meyer, I had a hard time hearing your question. I don't know, Beth, if you heard the question. You -- were you asking about the investment philosophy of alternatives, or dollar amounts?

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

So really just the plans. I was thinking about it in a percent -- on a percentage basis, whether there's more or less appetite for current cash flows to go to alternatives and LPs.

Christopher Jerome Swift
Chairman & CEO

Yes. I would say, generally, we have our targeted portfolio that we update every year. And I would say, generally, we had a slight increase to our targeted alternatives. Think of 1%. So not a meaningful change, but it's something we have really deep skills in.

And I think if you look at our performance over a longer period of time, Meyer, you'll see that I think we've outperformed consistently with just lower volatility. So from a pure sharp ratio side, it's -- I think it's a great trade.

And we've got great partners in that area, particularly in the real estate area. But Beth, what would you add?

Beth A. Costello
Executive VP & CFO

I think you captured it well. I mean it is an asset class that we've been slowly increasing allocation to. And as Chris said, continue to look to do that, but really not in a meaningful change in the overall construct of our portfolio. But as you said, it's an asset class that we've been very pleased with.

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

Okay. That's helpful. And obviously, this is overwhelmed by positive news. But we've had a few quarters of adverse development for commercial auto liability. I was hoping you could talk us through that.

Beth A. Costello
Executive VP & CFO

Yes. So we have experienced some large losses that have come through in that book that, as we've closed the last several quarters, we've decided to increase our reserves there. It is a line also that we're looking very closely at from a rate perspective and continuing to re-underwrite and look at the risks that we're putting on. So nothing specific that I'd point to, but we have had just a few large losses that we've reacted to as we made our quarter end judgments on reserves.

Operator

Our next question comes from David Motemaden from Evercore.

David Kenneth Motemaden
Evercore ISI Institutional Equities, Research Division

Just had a question on the workers' comp loss costs. Chris, I think you said that you expect loss cost to be slightly up, but that includes 5% medical cost severity. Could you just talk about what you're assuming on frequency? Are you assuming negative frequency there? And maybe how we should think about that in the current environment. And then maybe just talk about on the indemnity side as well.

Christopher Jerome Swift
Chairman & CEO

Yes. Thank you for joining us, David. I will just be clarifying. The trends that I talked about on the loss cost side were relatively flat and stable year-over-year. Medical severity at 5. I didn't give you a frequency, and I'm not. But those trends are fairly consistent. What changed, though, is sort of net rate and exposure. That excess rate, that is going to be down slightly year-over-year into a slight negative territory.

On the wage indemnity side, it's sort of a self-balancing equation from my perspective. We charge more, we collect more as salaries go up, and it's sort of a natural hedge for increasing the indemnity payments that we get to collect upfront. And then there's a little bit of a medical severity benefit because only 50% of loss content in workers' comp is wage. So that's what I would share with you.

Beth A. Costello
Executive VP & CFO

Yes. The only thing maybe I'll -- just to clarify one item. As Chris said, when we talk trend, right, when we think about the trend relative to loss, we're not making a change year-over-year. But again, as you said, medical severity with 5 points, some of the other items that he referenced, wouldn't result in negative trend. So from a pure loss cost perspective, you'd expect some increase. But all the other components that Chris talked about then also affects overall results.

David Kenneth Motemaden
Evercore ISI Institutional Equities, Research Division

Got it. Okay. That's helpful. And then just on -- I guess, Chris, you had said you expect 50 basis points underlying combined ratio improvement in Commercial Lines, and you gave a lot of detail. Just -- it sounds to me like you expect most of that to come from the expense ratio as opposed to the loss ratio, just given the headwind from workers' comp, obviously offset by expansion on other lines. Is that the right interpretation?

Christopher Jerome Swift
Chairman & CEO

[No, you misinterpreted it, I would say, half and half. So the point of combined ratio improvement in Commercial Lines year-over-year, 0.5 points for expense, 0.5 points for margin. That again, as I said, I am confident we're going to achieve. We're going to play for upside from there as we execute during the year.]

David Kenneth Motemaden
Evercore ISI Institutional Equities, Research Division

Hello?

Christopher Jerome Swift
Chairman & CEO

David, sorry, I was on mute. I was going to say no. I think you've misinterpreted. 0.5 points of expense ratio improvement and 0.5 points of loss ratio improvement. And feel highly confident on that 0.5 points of, I'll call it, loss ratio improvement. And we're going to play for upside from there. Again, highly confident of achieving sort of those midpoints, and we're going to aim to overachieve during the year.

David Kenneth Motemaden
Evercore ISI Institutional Equities, Research Division

Got it. So 0.5 points on the underlying loss ratio. So I guess that would imply -- I guess you're assuming 1.5, 2 points of expansion on everything, excluding comp, I guess. If I just take -- if I just do a weighting, 33% your book is comp. And then the balance, I would expect you to get 1.5 points of improvement. Is that the right way to think about it?

Christopher Jerome Swift
Chairman & CEO

Yes. I don't -- we have had a tough time to communicating. I think that the overall expense ratio improvement is going to be driven by, again, expense and then pure loss ratio improvement over the years. So -- but in total, David, I'm expecting a 0.5 points of combined ratio improvement in Commercial Lines year-over-year.

But we start with a negative 0.5 points because of comp. So that means you've got to get 1 point elsewhere. And that 1 point elsewhere, as I said to you, half of it comes from expense and half of it comes from pure loss. And we feel highly confident on achieving that, and we're going to play for upside, meaning my language of communicating to you is, I think we're going to outperform that point estimate I just gave you. Is that clear?

David Kenneth Motemaden
Evercore ISI Institutional Equities, Research Division

That is clear. I appreciate your comments.

Operator

We will take no further questions for speed, so I'll hand back to Susan Spivak for any further remarks.

Susan Spivak Bernstein
Senior Investor Relations Officer

Thank you, Alex. I apologize to those we didn't get to your questions, but we are here all day, and we'll reach out and follow up with you. And thank you all for joining us.

Operator
Thank you for joining today's call. You may now disconnect your line.