S&P Global
Market Intelligence

CNA Financial Corporation NYSE:CNA

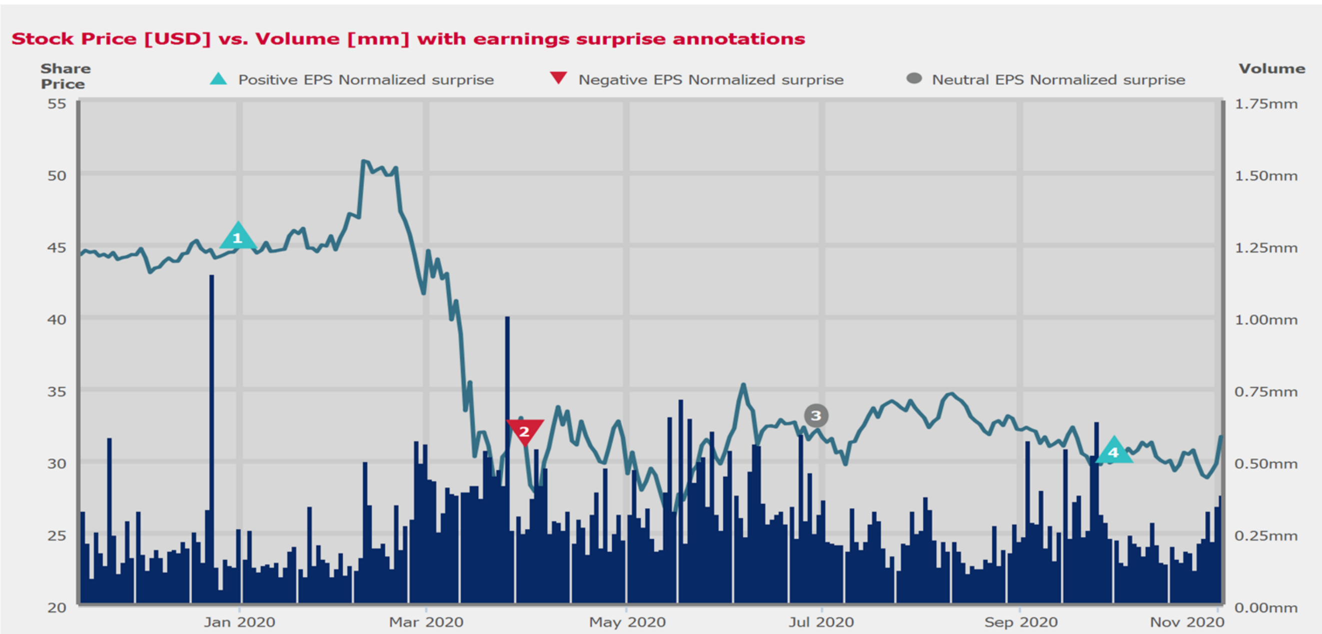
FQ3 2020 Earnings Call Transcripts

Monday, November 02, 2020 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2020-			-FQ4 2020-	-FY 2020-	-FY 2021-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.60	0.71	▲18.33	1.06	2.52	NA
Revenue (mm)	NA	1821.00	NA	NA	NA	NA

Currency: USD
Consensus as of Nov-02-2020 8:16 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2019	0.93	0.97	▲1 4.30 %
FQ1 2020	0.56	0.40	▼2 (28.57 %)
FQ2 2020	0.36	0.36	●3 0.00 %
FQ3 2020	0.60	0.71	▲4 18.33 %

Table of Contents

Call Participants

EXECUTIVES

Albert Joseph Miralles
Executive VP & CFO

Dino Ennio Robusto
Chairman & CEO

ANALYSTS

Gary Kent Ransom
Dowling & Partners Securities, LLC

Joshua David Shanker
BofA Merrill Lynch, Research Division

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

Ronald David Bobman
Capital Returns Management, LLC

Presentation

Operator

Good morning, and welcome to CNA's discussion of its 2020 third quarter financial results. CNA's third quarter earnings release, presentation and financial supplement were released this morning and are available via its website, www.cna.com. Speaking today will be Dino Robusto, CNA's Chairman and Chief Executive Officer; and Al Miralles, CNA's Chief Financial Officer. Following their prepared remarks, we will open the line for questions.

Today's call may include forward-looking statements and references to non-GAAP financial measures. Any forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from the statements made during the call. Information concerning those risks is contained in the earnings release and in CNA's most recent SEC filing. In addition, the forward-looking statements speak only as of today, Monday, November 2, 2020. CNA expressly disclaims any obligation to update or revise any forward-looking statements made during this call.

Regarding non-GAAP measures, reconciliations to the most comparable GAAP measures and other information have been provided in the financial supplement. This call is being recorded and webcast. During the next week, the call may be accessed on CNA's website. If you are reading a transcript of this call, please note that the transcript may not be reviewed for accuracy, thus it may contain transcription errors that could materially alter the intent or meaning of the statements.

With that, I will turn the call over to CNA's Chairman and CEO, Dino Robusto.

Dino Ennio Robusto
Chairman & CEO

Thank you, Rolando. Good morning. It's very good to be with you today, and I hope you and your families are coping well. Despite these unprecedented times, CNA continued to operate effectively as our underlying business performance improved once again this quarter as evidenced by the ongoing acceleration in rate achievement as well as higher overall growth and growth in new business. We also had an improved underlying loss ratio and a lower expense ratio for the quarter.

As we have done in previous years, we completed our annual Life & Group review in the quarter, which importantly includes the long-term care gross premium valuation, or GPV, analysis of our active life reserves. As part of our analysis, we took strong action to address the lower interest rate environment we now face compared to a year ago by conservatively modifying our discount rate assumptions.

First, we have lowered our expectation for the normative 10-year treasury yield to 2.75%, a reduction of 100 basis points from last year. Second, we extended the time period to grade up to that normative rate from 6 years to 10 years. Since long-term care reserves are discounted, these changes reflect our ongoing prudent approach to reserving and our steadfast resolve to protect our capital and earnings in an ongoing low interest rate environment. Al will provide you with much more detail associated with this year's GPV review.

Turning to P&C. Our underlying combined ratio of 92.6% for the quarter improved by 2 points from a year ago and is the lowest underlying combined ratio for CNA in the last 10 years. The underlying loss ratio improvement consisted of only a 0.5 point benefit due to lower frequency from the ongoing economic downturn, with most of the improvement driven by our International business, which has steadily returned to profitability as a result of our reunderwriting efforts in our London operation over the last 18 months.

As I mentioned last quarter, we expected only a relatively modest impact from loss frequency benefit because a substantial portion of our portfolio consists of insureds in essentials industries, such as construction, health care and manufacturing that were not subject to shelter-in-place restrictions. And we continue to assume a potential for higher severity in casualty lines like auto and general liability as the economy is restored over time. So we believe that it's still early to react too favorably to the short-term trends.

The lower P&C expense ratio of 31.8% largely reflected our growing premium base, which contributed approximately 0.7 points of the improvement in our underlying combined ratio. As I have said on prior calls, our strategy has been to simultaneously make substantial investments in talent, technology and analytics to position us for sustained success while streamlining our operation in order to keep our overall underwriting expenses flat. Then by growing the company in a disciplined and prudent fashion, we would steadily decrease the expense ratio, which you can clearly see in this quarter as more of the growth earned in.

Turning to the dynamics of this hard market and starting with pricing. Rate increases continued to accelerate as we achieved plus 12% in P&C overall, up 1 point from the second quarter. Importantly, excluding workers' comp, which had slightly negative rate, and our very profitable Affinity programs, which had a small positive rate increase. The rate change was plus 17%, up 2 points from Q2 and 5 points from Q1. Importantly, the increases, apart from these 2 areas, were broad-based as each business unit and essentially all product lines achieved higher rate.

The acceleration in our written rate increases over the last 6 quarters has led to 4 quarters of earned rate increases now at plus 9%. This compares to our long-run loss cost trend assumptions of slightly more than 4%, excluding our Affinity book. As mentioned on our last call, we had previously increased our view of long-run loss cost trends in 2020 as we continue to feel the impact of social inflation on our portfolio, in particular, in our aging services and auto portfolios.

In the quarter, we remained comfortable with our latest view and did not further need to increase them. However, as I also mentioned last quarter, the impact of the pandemic could be obfuscating the social inflation dynamic. So there still is some uncertainty around future impacts, along long-run loss cost trends, which is why we remain cautious to acknowledge margin expansion from the earned rate trend being amply above current levels. The great news, however, is that all the dynamics fueling the hard market, which we and others have articulated repeatedly, should allow us to achieve strong rate increases well into 2021, so that the margin gap, all else equal, should continue to grow, net of any added pressure from long-run loss cost trend in 2021. And as we see this play out over the next couple of quarters, we will then be in a better position to incorporate the benefit into our loss ratio picks.

In terms of growth, gross written premium ex captives grew 9%, while net written premium growth was 7%, both higher than the second quarter. Exposure continued to be a headwind to our growth as it was down 3 points compared to the third quarter last year. As was the case in the second quarter, new business growth in the third quarter was again higher than the same period last year, which evidences our ability to provide strong service to our agents and brokers in this remote working environment. The investments we made at the end of the first quarter to respond quickly, to shorter time frames on submissions, that I mentioned on the last call, continued to pay dividends this quarter.

Retention declined 1 point from the second quarter to 82% due to our reunderwriting efforts in our London operations, which will essentially be completed in the fourth quarter and to our targeted actions in the U.S. to improve the profitability of certain lines within health care and manufacturing that I have spoken about previously. Completing the picture for the quarter, our overall combined ratio was 100.9%, which included 0.4 points of favorable development and 8.7 points of loss activity from a series of natural catastrophe events. Also, as indicated in our press release, we made no change to our COVID-19 catastrophe loss estimate.

In the quarter, there were no significant changes in the regulatory environment. The claim notices we received in the third quarter have been modest and very little has been paid out. Of course, that was our expectation all along as we knew the claim outcomes from this event would play out slowly over time. As a result, our previously established COVID-19 ultimate loss estimate of $195 million remains appropriate for all events that occurred through the third quarter from which we believe claims will eventually emerge, and our loss estimate is still virtually all in IBNR.

Moving to investments. The overall portfolio fared well in the third quarter with the unrealized gain position increasing once again, and net investment income was strong driven by LP positions. Despite this strong quarter, we continue to see a reduction in our net investment income from our fixed income portfolio supporting P&C due to the lower interest rate environment that we believe is unlikely to change meaningfully anytime soon. This is a key dynamic fueling my perspective for a protracted hard market as it will take time for us and the industry to achieve an offsetting increase in underwriting income. Finally, our core income for the third quarter was $193 million or $0.71 per share. Net income was $213 million or $0.79 per share.

And with that, I'll turn it over to Al.

Albert Joseph Miralles
Executive VP & CFO

Thanks, Dino, and good morning, everyone. As Dino indicated, I will now provide details of our results by business segment.

Starting with Specialty. The combined ratio was 89.5% this quarter. The combined ratio includes favorable prior period development of 2 points and 1 point from catastrophe losses. The favorable prior period development was largely driven by continued strong profitability on the Surety business partially offset by unfavorable development in health care.

The underlying combined ratio for Specialty was 90.5% this quarter, 1.6 points of improvement compared to third quarter 2019. The underlying loss ratio was 60%, and the expense ratio was 30.5%. The expense ratio has improved by 1.3 points compared to third quarter 2019 due to both growth in net earned premium and lower expenses.

The gross written premium growth ex captives was plus 11% in Specialty for the quarter and was 9% on net written premium. Rates continued to increase at plus 13%, up from 11% last quarter. Retention was 86% this quarter, which was flat to last quarter. New business volume was strong with growth of 14% over the prior year's quarter.

The combined ratio for Commercial was 111.5% this quarter. This is 9.9 points higher than third quarter 2019 and includes 17 points of catastrophe losses and 0.6 points of unfavorable prior period development. The cat losses are attributable to severe weather-related events in the quarter primarily Hurricanes Laura, Isaias, Sally and the Midwest derecho. The underlying combined ratio for Commercial was 93.9% this quarter, 0.1 points higher than third quarter 2019, but 0.9 points improvement on a year-to-date basis versus prior. The underlying loss ratio was 61% compared to 61.5% in the prior year, reflecting a modest benefit from lower frequency in the quarter, as Dino mentioned.

The expense ratio was 32.3% compared to 31.7% in the third quarter of 2019. The prior year expense ratio included a release associated with the state loss assessment fund, which is muting the favorable impact of current year net earned premium growth and lower expenses.

Gross written premium growth ex captives was plus 7% in Commercial for the quarter, and net was plus 4%. The rate change of 11% was up 1 point from last quarter. Retention was 81%. New business growth was down 3% versus prior quarter and up 8% on a year-to-date basis.

The combined ratio for International was 98.1% this quarter compared to 107.4% in the third quarter of 2019. The combined ratio includes 3 points of catastrophe losses for the quarter. The underlying combined ratio for International was 95% this quarter, an improvement of 10.3 points compared to prior year quarter.

The underlying loss ratio was 60.1%, and the expense ratio was 34.9%. The underlying loss ratio improved 7.2 points fueled by our reunderwriting execution, while expense ratio declined 3.1 points driven by lower acquisition and underwriting expenses.

The gross written premium in International increased by 5%, and net increased by 10%, both in comparison with the prior year. The net written premium growth comparison to the prior period was impacted by a change in timing of the reinsurance treaty. Rate change of 16% was up 2 points from prior quarter. Retention was 70% this quarter, which is in line with 2019 levels and reflects the progression of the reunderwriting strategy.

Before I review the results of our Life & Group segment, including the impacts from our annual reserve reviews, I would ask you to refer to Slides 11 through 13 of our earnings presentation, as I take a moment to walk through our approach to the long-term care business and the actions we've taken over time. More than 5 years ago, we commenced efforts focused on the active management of long-term care with the goal of reducing the risk to CNA while also effectively serving our policyholders. This encompass significant investment in the business and a commitment to proactively and effectively address risks.

We've made considerable progress on these objectives, including reducing risk across many dimensions of the block, achieving meaningful rate increases and taking preemptive actions on the reserving assumptions. The actions we have taken with our 2020 annual review of our Life & Group reserves are reflective of this continued approach and commitment. As a reminder, our annual Life & Group reserve reviews include the long-term care; gross premium valuation, or GPV, of our active life reserves; as well as the long-term care claim reserve analysis. In addition, we completed a claim reserve review for our structured settlements block, which I will also address.

Starting with the long-term care GPV review. The most significant change resulting from this review was an update of our discount rate assumptions. These changes associated with the discount rate are detailed on Slides 14 and 15. It is important to note that the discount rate is a function of the current investment portfolio yield as well as the reinvestment yields assumed for future investments. The benchmark we use in reference to the risk-free reinvestment yield is the 10-year U.S. Treasury. While we project these risk-free rates over the short and intermediate term, assume long-term rate or normative rate is of critical importance given the duration of the liabilities. In the previous 2 years' reserve reviews, we have reduced our expectation for the normative 10-year treasury yield by 105 basis points of our 2019 review assuming that this benchmark rate would get to 3.75% by 2025.

In light of the current interesting rate -- interest rate environment and expectation of these conditions persisting, we've taken several critical actions on our discount rate assumptions. First, we have lowered our expectation for the normative rate to 2.75%, a reduction of 100 basis points from last year and 205 basis points cumulatively over the last 3 years. Second, we've extended the time period to grade up to that normative rate from 6 years to now 10 years. This means that it's not until 2030 that we will assume the new 2.75% normative rate. And finally, we are using the forward curve for the first 3 years of the projection, and then we'll grade up to the normative rate over the remaining 7 years.

You will see on Slide 15, we are not assuming the 10-year will get back to the 2% level until 2027, a significant change compared to our prior year expectations. I should also note, we did not make any meaningful changes to investment spread assumptions or portfolio credit quality as part of this review. The sum of all the assumption changes on the discount rate resulted in an unfavorable pretax impact of $609 million. These discount rate changes, including the significant decrease in the normative rate, extended time frame to get to the new normative rate and the use of the forward curve over the next several years reflects our prudent approach to reserving and meaningfully reduces the reinvestment risk assumed in these liabilities.

With that, I will move on to other key assumption changes, including morbidity, persistency and rate increases, all highlighted on Slide 16. With respect to morbidity, along with our change in the level of interest rates, we also lowered our expectation of inflation. This change impacts our assumption for cost of care for future claims and together with other morbidity assumptions had a favorable pretax impact of $51 million. With respect to persistency, the key assumption change was an increase to mortality rates for older age policyholders not on claim and reflective of our experience for this cohort. Persistency changes had a favorable pretax impact of $152 million.

Finally, regarding future premium rate increases. As a reminder, our approach is to include rate increases that have been approved, filed but not approved or that we plan to file as part of the current rate increase program. Over the past year, our actual rate achievement has exceeded our prior year expectations, contributing $200 million of favorable impact. In addition, we are continuing to file for additional rate increases under existing programs. Updating our assumptions to reflect our actual rate achievement, in addition to the updates to existing programs, had a total favorable pretax impact of $318 million. And I should note that the weighted average duration of future rate increase approvals assumed in the reserves is only 1.5 years.

Overall, and as highlighted on Slide 17, our annual GPV analysis for long-term care resulted in reserve deficiency and charge to earning of $74 million on a pretax basis. While these changes, and notably the change on the discount rate are significant, they reflect our continued approach to prudently and proactively address risk associated with this business. In addition to the GPV analysis, we have also concluded our annual long-term care claim reserve review, which is a review of the sufficiency of our reserves covering our claim population. The impact from this review is favorable with a $37 million release of reserves driven by lower expected claim severity. Specifically, we observed higher claim closure rates, most notably driven by claim recoveries.

I should note that it's the fifth year in a row the result of the claim review is favorable, which is a validation of our responsible approach to actuarial assumption setting. Finally, and as indicated on the bottom of Slide 17, we had an unfavorable impact associated with the claim reserve review for our structured settlements block. These structured settlements are agreements to provide fixed periodic payments to claimants associated with historic P&C claims. Total reserves for our structured settlement block were approximately $550 million at the end of the third quarter.

Similar to our long-term care block, these reserves are held on our balance sheet on a present value basis and thus are subject to changes in assumed discount rates. As well, many of these policies have life contingencies and thus are impacted by changes in mortality assumptions. As part of the reserve review this year, we made adjustments to both the discount rate and mortality assumptions resulting in a reserve strengthening of $46 million on a pretax basis.

Turning to Slide 18. Overall, our Life & Group segment produced a core loss of $35 million in the quarter. The sum of the reserve changes covering both the long-term care and structured settlement blocks was a pretax charge of $83 million or $65 million after tax. Separate from the impacts of these reserve reviews, the segment produced core income from current operations of $30 million for the third quarter. These results were favorable to expectations and primarily driven by morbidity experience. Specifically, we continue to experience lower-than-usual new claim frequency, higher claim terminations and more favorable claim severity amid the effects of COVID-19.

As referenced in the previous quarter, given the uncertainty of these trends, we are taking a cautious approach from an income recognition perspective and then holding a higher level of IBNR reserves. In addition, as we continue to deem these trends as temporary and short term in nature, we did not incorporate this more recent experience into our GPV assumption setting efforts. Our corporate segment produced a core loss of $19 million in the third quarter.

Now let me turn to investments. Pretax net investment income was $517 million in the third quarter compared with $487 million in the prior quarter (sic) [prior year quarter]. The results reflected favorable returns from our limited partnership and common equity portfolios, which produced pretax income of $71 million compared to $18 million during the same period last year. Pretax net investment income from our fixed income portfolio was $443 million this quarter compared to $462 million in the prior year quarter. The pretax effective yield on our fixed income holdings was 4.5% for the period. The decrease is primarily in our P&C portfolio, which, as Dino mentioned, has been impacted by lower reinvestment rates.

Pretax net investment gains for the quarter were $27 million compared to a gain of $7 million in the prior year quarter. The gain was primarily driven by the continued recovery of the mark-to-market on our nonredeemable preferred stock investments and higher net realized investment gains on fixed maturity securities partially offset by a loss on the redemption of our $400 million of senior notes due August 2021.

Our unrealized gain position on our fixed income portfolio stood at $5 billion, up from $4.4 billion in second quarter. The change in unrealized during the quarter was driven by the tightening of credit spreads across the market, while risk-free rates remain low. Fixed income assets that support our P&C liabilities had an effective duration of 4.5 years at quarter end in line with portfolio targets. The effective duration of the fixed income assets that support our Life & Group liabilities was 9 years at quarter end. Slides 21 and 22 of the earnings presentation will provide you with additional details of the investment results and the composition of the investment portfolio.

Our balance sheet continues to be extremely strong. At quarter end, shareholders' equity was $12 billion or $44.30 per share driven by the increase in our unrealized gain position during the quarter. Shareholders' equity, excluding accumulated other comprehensive income, was $11.6 billion or $42.78 percent -- per share. We continue to maintain a conservative capital structure with a low leverage ratio and a well-balanced debt maturity schedule.

As I noted, in August, we issued 50 -- $500 million of senior notes at a record low coupon of 2.05% with tremendous demand for the paper, and we subsequently redeemed our 2021 debt, the net of which will reduce our annual interest expense by nearly $13 million. And at quarter end, all of our capital adequacy and credit metrics remain above target levels, supporting our credit ratings.

In the third quarter, our operating cash flow was strong at $758 million driven by higher premiums and, to a lesser extent, lower paid losses. In addition to our positive operating cash flow, we continue to maintain liquidity in the form of cash and short-term investment and have sufficient liquidity holdings to meet obligations and withstand significant business variability. And we are pleased to announce our regular quarterly dividend of $0.37 per share.

With that, I will turn it back over to Dino.

Dino Ennio Robusto
Chairman & CEO

Thanks, Al. One last point of emphasis before we move on to the question-and-answer portion of the call. Each quarter this year, I have developed greater confidence in the strength and duration of the hard market because of the widespread industry awareness and, therefore, increasing customer awareness of the adverse impact of a protracted low interest rate environment, social inflation dynamics as well as years of depressed pricing and elevated catastrophe activity.

Increasingly, it is understood this will take more than a few additional quarters of correction to allow the industry to achieve required levels of return to responsibly protect the customer risks we assume. I am optimistic that we will be able to take full advantage of this correction period to achieve stronger pricing, better terms and conditions, growing our top line premium as well as our share of high-quality new business and improving both our underlying loss and expense ratios. And with that, we'd be happy to take your questions.

Question and Answer

Operator

[Operator Instructions] We'll take our first question from Josh Shanker with Bank of America.

Joshua David Shanker
BofA Merrill Lynch, Research Division

I hope you'll indulge me with maybe more than 2, but you can cut me off if you want. So first question on the expense ratio in the P&C business, absolutely a great number. Anything we need to think about in terms of T&E or COVID-related expenses making this atypically low? Or is that a good number to think about going forward?

Dino Ennio Robusto
Chairman & CEO

Al, do you want to take that? Or...

Albert Joseph Miralles
Executive VP & CFO

Yes. Sure. Josh, it's a good question. So I would say modest impacts from travel, right? We're not a huge T&E spend company. So I would say the expense ratio are modestly benefited from less or very little travel, but not a lot really the pickup -- largely driven by our pickup in earned growth.

Joshua David Shanker
BofA Merrill Lynch, Research Division

And so that might be -- obviously, it's just one quarter, but it might be a useful number. If we're thinking about going forward, it's not unreasonable?

Albert Joseph Miralles
Executive VP & CFO

I don't think it's unreasonable. Remember, our strategy has been to try to hold underwriting expenses flat while we invest in the business. And I think what you saw in the quarter was just that good efforts in holding flat. We continue on our path of investing in talent, technology, analytics, but the discipline shown through on the -- our expense, spend. And then again, you see the path of our written growth, and we're starting to see that really show up in our earned.

Joshua David Shanker
BofA Merrill Lynch, Research Division

And then in terms of long-term care, just a few quickies. One is, I just need to understand exactly. I thought that the future rate increases are not included in the assumptions. And I guess when I was reading the press release, it said that the 2019 rate increases came through better than expected. I'm trying to understand exactly, how does that work? The expectations, should they -- were they built into the numbers? Or what is that $318 million exactly?

Albert Joseph Miralles
Executive VP & CFO

Sure. So Josh, remember this gross premium valuation, effectively what it is, is it takes all of your future cash flows, premiums, claims, expenses and then it discounts it all back onto your balance sheet in the form of a reserve. Okay. So that includes your premiums, and that's just how it works from a life company perspective.

Now what we include, from a rate increase perspective, we would deem to be prudent. Like I said, we take rate increases that we've gotten approved already, but haven't yet kicked in or come through as actual premium that we've filed but have not yet been approved. Or that we have a current approved program but has not gone through the filing process yet.

The sum of what is in our reserves, pursuant to rate increases, is $265 million. So that's the balance that is outstanding. Last year, that balance was $230 million baked into our reserves, okay? So what basically I'm saying with that $318 million is what was the change and some of the rate increases actually earned in and then you have your updated assumptions. The bulk of that change, that $318 million, was purely based on last year's estimates what we thought we could achieve versus what we actually achieved that has been outperformed. We got greater rate than we would have anticipated.

But our approach and our philosophy is to be prudent about what we think we can earn and do not go far out in the future. And you will see, you could hear other long-term carriers speak, they all have a little bit different perspective. But some will go further out into the future and will have a bit more aggressive expectations in terms of what they achieve. Because we don't know and there's uncertainty of what the rate environment will be, we've always taken a very prudent approach on that. And then -- so what you're seeing is basically our ability to outperform on those assumptions.

Joshua David Shanker
BofA Merrill Lynch, Research Division

And I was looking over, not just yours but some other companies' rate increase approvals and whatnot, and some of them are quite staggering. Are we at the point where you are ambivalent about whether a policyholder takes the offer of the new rate or cancels the policy and gets a compensation in return? You'll still see some rate increase. Are we getting to the point where you're happy to have those policyholders on because you're getting the rate that you need? How should we think about that?

Albert Joseph Miralles
Executive VP & CFO

The way you should think about that is where we set the rates is basically -- the rate that we put out is actuarial equivalent to what options we'd give them on benefit reductions, right? So that if someone says, I want to reduce my inflation, I don’t want to reduce my daily benefit, then doing so versus accepting the rate is essentially equivalent. Now what we've seen...

Joshua David Shanker
BofA Merrill Lynch, Research Division

And is canceling equivalent as well?

Albert Joseph Miralles
Executive VP & CFO

Well, canceling, they're basically giving up all of their benefits. So canceling, they're basically forgoing what they would have paid in premiums over the years, so I wouldn't look at that the same.

Joshua David Shanker
BofA Merrill Lynch, Research Division

That's not an option -- the cash benefit return in exchange for forgoing your benefits?

Albert Joseph Miralles
Executive VP & CFO

These policies do not have cash value. So there's not a surrender value.

Joshua David Shanker
BofA Merrill Lynch, Research Division

There's not. Okay. Some of them did have that. Okay. And one last question. Can you parse for me how much COVID mortality there is in the persistency benefit you had in the quarter?

Albert Joseph Miralles
Executive VP & CFO

And you mean current operations as opposed to in our reserve reviews?

Joshua David Shanker
BofA Merrill Lynch, Research Division

There was, I think, $150 million in persistency benefit. It was mortality related. I assume some of that is COVID mortality.

Albert Joseph Miralles
Executive VP & CFO

In our current operations, that is the operating result we had of $30 million, there is some mortality benefit, which you should think of as what came through the results would be kind of more permanent impacts of the business, that is that we had a lower level of paid claims and really more severity. And then as well, you would have some mortality coming through there, both in our, what we call, healthy lives as well as our claim population. And what we are holding and being more cautious about is more of the claim frequency component.

Operator

And up next, we will hear from Gary Ransom with Dowling & Partners.

Gary Kent Ransom
Dowling & Partners Securities, LLC

I wanted to ask a little bit about expenses as well. I'd like to hear your thoughts on how the COVID experience might cause permanent changes in expense levels. And I'm thinking maybe there's some rejiggering of real estate or in travel and entertainment, maybe some processes work just as well with people at home. And I wanted to ask a question, how do you make the best of what you might have learned over the past 7 months? Is there some changes you can make?

Dino Ennio Robusto
Chairman & CEO

I'll start now, and then you can jump in. I think maybe starting a little bit with the second part. Gary, it's Dino. There are things that we are clearly learning in the process. And the ability for us to work in this remote environment does generate an ability for us to say, well, going forward, I think there's probably going to be less overall travel and expenses. You will continue to do that. We have branch operations. We'll go with them to those locations. We will, obviously, meet with our agents and brokers across all of those locations, but our agents and brokers are also valuing the calls that we make in a virtual environment. Our clients are also -- everyone is generating some efficiency gains from that process. So I think there will be some potential benefit.

Now I want to be a little bit careful just on the point that, as Al had mentioned, travel and expense is not a large component of our numerator, can easily get assumed by our decisions that we continue to make on talent and, in particular, analytics and technology. But there are some definitive positives that has been generated from a process standpoint, a work standpoint that we anticipate -- from a talent standpoint, as you can secure talent, from a remote environment in trying to work effectively. Of course, we're all looking forward to getting -- to a large extent, getting back in offices, but there are clearly some benefits.

I don't want to suggest that, that has a big impact on the numerator at this particular juncture for travel and expenses, but less of an issue for all of the other component. But nevertheless, as Al pointed out, because of the earned premium growth that's going to continue -- going into 2021, it'll continue to have a benefit.

Gary Kent Ransom
Dowling & Partners Securities, LLC

So I guess I was trying to fair it out if there was a way to reduce expenses, but it sounds like this is really more part and parcel of your keeping expense dollars flat and just letting the premium grow. Is that fair?

Dino Ennio Robusto
Chairman & CEO

Yes. So I think that's a fair way where we spend today. We're always -- to keep it flat as you make investments in all the other areas, you are having to gain operational efficiencies in other areas. And I'm sure the COVID-related circumstance will also provide some operational efficiencies. I just wanted to put it in context that it's not being a big driver of our numerator within underwriting expenses, Gary.

Gary Kent Ransom
Dowling & Partners Securities, LLC

All right. And my other question was on terms and conditions, so shifting gears a little bit, and how you've been tightening those, either in International or in segments that need it here. You've had experience with past cycles, so you might have a view of how that terms and conditions change contributes to the overall improvement and how the timing might flow through. I'm just trying to get a sense of how big of an increment on top of the rate might be coming from the terms and conditions changes.

Dino Ennio Robusto
Chairman & CEO

Yes. So it's clear that as this market continues to harden, you get a lot of benefits within the construct of terms and condition beyond the pricing. You get policy terms, we get a lot more restrictive. You get better deductible, the exclusions that you can add in certain components of exposures that have gotten expanded in a softer market. Clearly, this is an opportunity to take advantage of these changes in terms and conditions, and we're clearly doing that.

And I do think -- the way that I think about it, having seen the '85 -- the '86 hard market, '87 and then right after 2001 is that the terms and conditions tend to persist, Gary, beyond when the rates -- the rate increases start to subside. So the rates moderate first, the terms and conditions persist a little bit longer. And then as you get deeper into a softer cycle, you get the pressure on terms and conditions.

So we are clearly taking advantage of the ability to do that in all areas, in particular in areas we've been reunderwriting, like our health care portfolio in the United States; some of our large property; clearly, some of the property from an International standpoint. And this is going to serve us well beyond even when rates start to moderate again, which in and of itself is going to be a little bit of a ways out there.

Gary Kent Ransom
Dowling & Partners Securities, LLC

So do you think we're already seeing a meaningful benefit from terms and conditions changes?

Dino Ennio Robusto
Chairman & CEO

I mean I would say to you that our reunderwriting efforts in the aggregate are clearly providing a benefit. A good example, Gary, that I would use is the International calendar year combined ratio, which was under 100 in the third quarter, notwithstanding the catastrophes in the United States. And I point that out only because in the past, prior to our International reunderwriting, we would have it in considerable catastrophe activity emanating out of our London operation on U.S. catastrophes. And we clearly saw a benefit in this quarter, in the last 18 month, has done a really -- has made a big impact.

So I'd put it within the broader umbrella of the reunderwriting initiatives where you can already start to see it. I think you’d see it also in areas like health care where we've been able to get considerable deductibles on our professional liability, something that you have not seen before. So those are the part of the broader reunderwriting that we've been focused on for a while. Yes, I do think it's having a meaningful impact.

Operator

And up next, we'll hear from Meyer Shields with KBW.

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

I guess it's a question for Al. The fixed income portfolio within P&C seems to have risen, I don't know, somewhat abruptly from the second quarter to the third quarter. I was hoping you could talk to what's driving that.

Albert Joseph Miralles
Executive VP & CFO

Sure, Meyer. And you mean the value of the portfolio?

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

No. The portfolio duration.

Albert Joseph Miralles
Executive VP & CFO

Duration. Yes, correct. Yes, the duration is up. That is not a function of any changes in the portfolio. What you're seeing there, Meyer, is with our current low-rate environment rate staying low, a lot of the modeling companies basically recalibrated their scenario modeling to reflect that rates could go lower prior to, more recently, the head floors in that would say rates aren't going to go any lower than this level. They've basically reduced those floors and now have the potential that you could drop to 0.

And so basically, with that sensitivity now into the duration modeling, with lower rates, lower -- the potential of lower rates and lower coupons, the durations are higher, but that has nothing to do with us changing anything in the portfolio.

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

Okay. So there's no incremental risk or anything like that?

Albert Joseph Miralles
Executive VP & CFO

Correct. Correct. We would essentially would have been flat quarter-over-quarter in duration, but for that modeling change.

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

Okay. Within Specialty, I guess, I was hoping you could quantify the offsetting reserve development patterns from Surety and health care?

Dino Ennio Robusto
Chairman & CEO

Okay. I'm not sure I understood that all. Can you just repeat that, Meyer, do you remind?

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

Yes. No, I don't mind at all. So Al talked about offsetting -- if I understood correctly, offsetting reserve development for the Specialty segment where I think, boiled down, you had releases within Surety and some charges within medical or with -- or health care. I was hoping you could quantify that.

Dino Ennio Robusto
Chairman & CEO

Al, can you -- do you want to jump in there?

Albert Joseph Miralles
Executive VP & CFO

Sure. Meyer, you're going to see that, obviously, as the Q comes out. So you have about $40 million of benefit from the Surety business, and that's really a continuation of the exceptional profitability we've seen in that business.

And then health care, some adverse development really driven by some large loss activity. And again, kind of -- a bit of the kind of trend that we've been seeing. And obviously, we would expect that will dissipate as we conclude the reunderwriting of that book.

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

Okay. That's helpful. And then just finally on reserves. But within Commercial, the last few quarter have had -- maybe more than a few, have had favorable workers' compensation reserve development. I was hoping you could talk through how that played out in the third quarter.

Dino Ennio Robusto
Chairman & CEO

Al, the favorable -- on work comp, do you have those numbers?

Albert Joseph Miralles
Executive VP & CFO

Yes. So on worker -- and work comp, again, you've got a couple of puts and takes on Commercial on workers' comp. You're going to see a favorable development there, really reflective of continuation of favorable medical trends that we've been experiencing.

Operator

And up next, we'll hear from Ron Bobman with Capital Returns.

Ronald David Bobman
Capital Returns Management, LLC

Dino, you have a specialty in the health care area, and I'm wondering if you might give us a little bit more sort of color as to what's going on in the various sort of subsegments, sort of loss activity or claims activity, underwriting -- sort of the underwriting environment, just sort of some more info would be interesting, please.

Dino Ennio Robusto
Chairman & CEO

Okay. And just to make sure I got all of that, related to health care, subsegments related to the COVID or just in general?

Ronald David Bobman
Capital Returns Management, LLC

Yes. Really -- I guess really the COVID impact on the various segments, whether it's doctors, nursing facilities, hospitals, other specialties. Obviously, it's got to be -- create a lot of upheaval and challenges, and it’d be interesting to hear about what you're seeing, what you're learning.

Dino Ennio Robusto
Chairman & CEO

Yes. So the health care, as we had indicated, when we put out our ultimate loss reserve, we had indicated that a good portion of -- or the larger portion of the ultimate loss, Ron, was indeed medical malpractice and, in particular, aging services.

And now what we did at the time to try to set an ultimate since we didn't have actual much claim activity, we took a look at what came in from a claim notice standpoint. And although that was relatively limited, we then also addressed -- took some of the public information and looked at the number of depths within aging services facilities that we insure. And what we did is took an estimate of what percentage over time might turn into claims.

And then what we did was, in the third quarter, as I indicated in my prepared remarks, not much changed. We've got even fewer additional claims on the health care aging services side than we did in the second quarter. So as I had indicated, it was possible that when we put up that ultimate, it might end up subsuming activity that we see in the third quarter, which is essentially what it has.

But again, I just want to caution, right, we indicated this is going to be slow moving. These things will take some time. So notwithstanding a relatively limited claim notice activity at this juncture, I think, we feel that the ultimate we did put up, of which -- again, the larger portion was medical malpractices is still appropriate.

Does that answer your question?

Ronald David Bobman

Capital Returns Management, LLC

Yes. And [it'd be interested to know], how do you handle renewals? You, obviously, have a lot of accounts, I presume, with like light claim count, maybe no claim count, but you do face -- renewals come due. And what's the underwriting approach to writing those? It'd be very interesting.

Dino Ennio Robusto
Chairman & CEO

Yes, sure. That’s -- yes. And as you know, we had embarked early on, and I think I can comfortably say we led the market in the churn on health care. Because we are a major player and we are respected, we started to get rate increases and have had double-digit rate increases for multiple years now.

And what we have said is we're going to get or achieve the terms and conditions and the rate increases we need or we're going to let it go. And what you saw over the course of the last several quarters was the willingness to drop the retention ratio, and we have, in particular on aging services, it had dropped considerably below the overall retention ratios we drive at CNA. But that was fine. We decided we were going to do that.

Now we're getting substantial rate increases going into the third quarter. We had aging services alone was up 56% in rate increases. It's about 13 points higher than it was in the second quarter. If you take all of health care combined, about 32% versus 28% in the second quarter. And so we continue to drive this in the right direction.

What is particularly comforting to us is over the course of the last couple of quarters maybe, as I say, that proverbial straw that broke the camel's back with COVID, you're seeing other players really take -- follow our lead. And so we actually have been able to generate some substantial rate increases while actually increasing our retention, the implication simply being that others are following suite.

So yes, it's been substantial. And what we -- and our position remains the same. If we can't get the terms and conditions we deem appropriate, and after 20-plus years of experience we think we know what it is, what they should be, then we are prepared to walk away in the subsegments that have been problematic and that have had higher long-run loss cost trends.

Does that give you the color you needed?

Ronald David Bobman
Capital Returns Management, LLC

Yes, it's very helpful. And I assume those rates that you mentioned, which is they’re significant, that's separate and apart from the benefits of terms and condition changes, I presume.

Dino Ennio Robusto
Chairman & CEO

Correct. Correct. Because you get deductibles, you get tighter policy language, migration, although the vast majority of claims made, but continuing to move that. And so that's over and above, and quite frankly, in our opinion, needed.

Operator

And there are no further questions in queue. I'll turn the call back over to CEO, Dino Robusto, for additional or closing remarks.

Dino Ennio Robusto
Chairman & CEO

Okay. Thank you very much, and we look forward to chatting with you next quarter. Thank you.

Operator
And ladies and gentlemen, this concludes today's call. We thank you for your participation, and you may now disconnect.