

Equity Research

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Earnings Revised — July 20, 2023

Commercial Lines Insurance

The Travelers Companies, Inc. (TRV)

TRV: It's Raining Rate; Conference Call Round-Up

Our Call

TRV shares traded up modestly as the stronger-than-expected BI margin benefited from 1.5 points of favorable property results plus the company saw adverse development in BI.

The stock from here: TRV traded up on the day given the better-than-expected BI margins and re-acceleration of BI RPC including both RRC and exposure. While the improvement in rate was good there were a few other issues weighing on the stock, in our view: **(1)** the BI RPC benefited from property accounting for 21% of domestic premiums in the quarter (vs 13% in Q1), **(2)** there was ~\$350M of unfavorable development in BI ex. WC releases and **(3)** personal auto is still not at written price adequacy.

Estimate and price target changes: Our 2023 EPS estimate goes to \$12.30 (from \$13.50), 2024 EPS goes to \$18.15 (from \$18.35) and our 2025 EPS goes to \$20.50 (from \$21.00) to reflect weaker personal auto results, higher interest expense, a higher cat load and lower repurchases in 2H 2023. Our price target is unchanged at \$185 based off 10.2x 2024E EPS and 1.66x 2024E book value.

Read thrus: **(1)** Continued firming in commercial pricing aided by seasonally higher property renewals, **(2)** exposure re-accelerated, which should bode well for the brokers, **(3)** personal auto severity remains stickier than expected with loss costs in the low double digits, and **(4)** TRV added to its reinsurance program and pointed to repurchases being lower in the second half given the outsized cat losses to start the year, which we could potentially see from others.

BI margin benefited from favorable non-cat losses. BI saw an underlying combined ratio of 89.4%, a 3 point improvement Y/Y, with a 2.5 point benefit from favorable property losses, implying 50bps of core improvement. The 50 bps was driven by earned rate exceeding los trend. BI saw \$101M of PYD, including \$350M of strengthening ex comp driven by other liability lines led by umbrella. Even with the reserve strengthening, TRV said they did not change their 5.5-6.0% loss trend assumption.

Personal auto still struggling: TRV did not reach its target of written price adequacy by mid-year given loss costs is stickier than expected, with severity remaining in the low double digits. They expect the auto RPC to continue to rise from here, but they did not provide a timeline on when they expect to reach price adequacy. The higher severity is being a higher mix of accidents that involve BI coverages, which is offsetting some PD easing, particularly from wholesale prices.

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Rating	Equal Weight
Ticker	TRV
Price Target/Prior:	\$185.00/NC
Upside/(Downside) to Target	8.5%
Price (07/19/2023)	\$170.56
52 Week Range	\$149.65 - 194.51
Shares Outstanding	230,976,565
Market Cap (MM)	\$39,395
Enterprise Value (MM)	\$45,912
Average Daily Volume	1,599,973
Average Daily Value (MM)	\$273
Dividend (NTM)	\$3.93
Dividend Yield	2.3%
Net Debt (MM) - last reported	\$6,517
ROIC - Current year est.	13%
3 Yr EPS CAGR from current year (unless otherwise noted)	18%

\$	2022A	2023E	2023E	2024E	2024E
EPS	Curr.	Prior	Curr.	Prior	
Q1 (Mar)	4.22 A	4.11 A	NC	4.54 E	4.79E
Q2 (Jun)	2.56 A	0.05 A	1.31E	3.47 E	3.37E
Q3 (Sep)	2.20 A	3.13 E	3.02E	4.14 E	4.13E
Q4 (Dec)	3.40 A	4.99 E	5.08E	6.02 E	6.09E
FY	12.43 A	12.30 E	13.50E	18.15 E	18.35E
P/E	13.7x	13.9x			9.4x

ROIC - Current year est.: Represents return on equity (ROE) 3 Yr EPS CAGR from current year (unless otherwise noted); Using 2019-2022 for CAGR calculationEPS: Operating EPS Source: Company Data, Wells Fargo Securities estimates, and Refinitiv. NA = Not Available, Volatility = Historical trading volatility

Takeaways for the Non-Life Insurance Group

The main takes that stand out from TRV to us, and the laterals for the rest of the group are below.

Net-net, the biggest takes are that TRV continues to see pretty poor personal auto results (although the margin did improve sequentially), commercial lines continue to see strong rate including sequential accelerations in both rate and exposure, and investment income continues to be a strong tailwind for earnings as they raised their NII guide. TRV also saw a sizable reserve increase for other liability lines within BI, and we expect there to be a focus on reserve movement we see from other insurers this quarter. Highlights of the laterals that we see for the group follow below:

- **Commercial lines pricing momentum continues.** TRV said that its renewal rates in BI were +7.2% in Q2, accelerating sequentially from +4.7% in Q1 showed a continued firm market. We suspect the higher property renewal (21% of total domestic BI premiums in the quarter vs 14.6% in Q1) in the Q2 had some impact on the higher rate but TRV said every line in BI saw a sequential increase vs the Q1 showing broad-based strength. **The strong pricing and strong new business growth in commercial in addition to TRV saying loss costs have not significantly changed is a positive for the commercial peers, and the seasonally higher property renewal in the Q2 should boost rates and exposures for the group.**
- **Exposure growth accelerates sequentially.** Exposure growth saw a sequential uptick in BI in Q2 as TRV saw exposure growth of 5.6% vs the 4.7% in Q1. When looking at the RPC, the higher RRC and exposure growth led to an RPC of 12.8%, which was a record-high for TRV. **The re-acceleration of exposure growth should be a good sign for all insurance brokers. Further, TRV is more of a small-middle market insurer (RPC was up a point in Select and more than two points in Middle Market), it is the best take for AJG and BRO, but does point to a potentially good quarter for the brokerage group in general.**
- **Personal auto continues to see elevated margins.** TRV printed a 103.5% personal auto underlying combined ratio, remaining above the company target of mid-90s to perhaps a range above the upper-end of the mid-90s. RPC was 16.1% in the quarter, accelerating from 14.0% in the prior quarter but TRV noted they are still not at written price adequacy, which they previously guided to, given severity has remained stickier than their expectations with loss trends in the low double digits. **These results highlight personal auto carriers are still higher severity than they originally expected, pushing out the timeline on when carriers can return to target margins.**
- **Adds to its reinsurance coverage.** TRV increased their coverage under the NE property treaty by fully placing the \$850M layer above the attachment point of \$2.5B (vs last year they placed a \$750M layer above a \$2.25B attachment point). They also added a new hurricane cat excess of loss reinsurance program in their personal insurance property book that provided 50% coverage for the \$1.0B layer above the attachment point of \$1.75B. They said the margin impact of this new program was de-minimis and the overall impact from higher reinsurance program across all programs should little or no impact on expected margins given the rate they are taking (which is offsetting the higher costs). **We expect other insurers to potentially add to their programs for the back half of this year given cats are on a record-pace to begin the year.**
- **Point to repurchases being lower in the second half.** With the higher cat losses to start the year and going into wind season, TRV pointed to repurchases being lower in the second half vs the first half. **We could see other companies pullback on repurchases in the back half to preserve capital, especially depending on the updated reinsurance programs at mid-year renewals where retentions are higher.**
- **After-tax fixed Income NII revised up.** The company raised its fixed income net investment guide to \$570M for Q3 (from \$555M) and \$595M in Q4 (from \$570M). We believe this could perhaps point to modestly higher investment income at other players, although we do not expect much to provide specific NII guidance as most carriers don't provide specific guidance (**CB guides one quarter ahead**).

What the Companies Are Saying—TRV

Outlook. When asked about their loss cost assumptions of 5.5% to 6.0%, TRV pointed to loss costs not being significantly different even after adding to their umbrella reserves within Business Insurance. They did not give a specific margin guide but did agree with the statement that if their loss costs are fairly unchanged and RPC is accelerating, they should be able to improve their margins. TRV pointed to reinsurance costs being higher at mid-year renewals and highlighted a new program they added that will provide protection for hurricane losses for their personal insurance property book. The new program provides 50% coverage above a \$1.75B attachment point up to \$1.0B coverage and covers all US coastal states from Texas to Maine, excluding Florida. The overall higher reinsurance costs and the new reinsurance treaty should have little to no impact on margins as they are passing on the higher costs through rate.

Pricing. Within personal lines, TRV guided to RPC in auto accelerating from here for the remainder of the year (16.1% in Q2) and home RPC remaining at the high-teens for the remainder of the year (19.2% in Q2). They did not provide a timeline for when auto would reach written price adequacy within personal auto given it depends on how quickly rates get approved, how fast inflation comes down, and how loss experience trends from here.

Guidance. The [exhibit](#) below highlights TRV's commentary and expectations for 2023.

- **Fixed income investment guide raised.** The only precise guidance that Travelers provides is around its quarterly view for fixed income plus short-term investment income, on an after-tax basis. TRV is now looking for fixed income and short-term investment income to be \$570 million after-tax in Q3 and \$595 million in Q4. This is up from the previously guided \$555M for Q3 and \$575M for Q4.
- **Personal lines RPC guide.** Within personal auto, TRV said they are not at written price adequacy as of mid-year as previously guided to given severity has remained stickier in the low double digits. They expect RPC to climb from the 16.0% in Q2 for the remainder of the year while they expect home to remain in the high-teens (was 19.2% in Q2).
- **Lower repurchases in the back half.** Given the outsized cuts they have seen to start the year, TRV pointed to repurchases being lower in the back half of this year when compared to the first half of the year when they bought back \$862 million. TRV has \$6.2B left under its repurchase authorization as of 6/30.

Investments. TRV raised their fixed income and expects after-tax investment income of \$570M in Q3 (up from \$555M prior) and \$595 million in Q4 (up from the prior \$575 million). The non-fixed income portfolio delivered positive returns (4.0% in the quarter), which was higher than the 2.8% in Q1 but below the 10.2% return in the prior year quarter. As of 6/30, real estate and real estate partnerships accounted for 31% of their non-fixed portfolio (vs 33% in the prior quarter) but remains a minuscule portion of the entire portfolio at 2.2% of their total invested portfolio.

Liquidity and Capital. TRV has \$2.0 billion of capital at the holding company (up from just under \$1.5 billion at the end of 2022 and the \$1.6B at end of Q1) with all of their capital ratios at or better than target levels. They issued \$750M of 30-year senior notes (5.45% annualized coupon) in May (priced 5/22) to fund business growth bringing their debt to capital ratio to 23.3%, which is still within their target range of 15-25%.

Exhibit 1 - 2023 Guidance Tracker

	2023 Guidance Tracker	Provided With Q3 2022 Earnings	Provided With Q4 2022 Earnings	2023 Outlook	Provided With Q1 2023 Earnings	Provided With Q2 2023 Earnings
Underlying Margin Outlook		Business Insurance: Pointed to loss trends being unchanged from 5.5% to 6.0% with pricing remaining less than one point ahead Bond & Specialty: No outlook commentary	Business Insurance: Did not give specific guide but said earned pricing exceeded loss trend in all three segments Bond & Specialty: No outlook commentary	Business Insurance: No outlook commentary Personal Lines: Expect to reach or at least be close to rate adequacy in the majority of states by mid-year. TRV noted the loss environment is incrementally more challenging adequacy by mid-2023.	Business Insurance: No outlook commentary Personal Lines: Did not reach written price adequacy by mid-year; did not provide an updated timeline on reaching rate adequacy	Business Insurance: No outlook commentary Personal Lines: Did not reach written price adequacy by mid-year; did not provide an updated timeline on reaching rate adequacy
Expense Ratio Outlook		No outlook commentary for 2023	Expect FY2023 Expense Ratio to be 28.5% - 29.0% (versus FY22 ratio of 28.5%)	Business Insurance: TRV saw continued acceleration of pricing in property given hardening reinsurance market and capacity constraint. Bond & Specialty: Written premium contracted modestly in their international business due to tougher YY compars and a significant decline in M&A activity	Business Insurance: TRV said that RPC was not just property and saw broad-based rate across all lines as all lines were up sequentially vs the Q1	Business Insurance: TRV said that RPC was not just property and saw broad-based rate across all lines as all lines were up sequentially vs the Q1
Renewal Premium Growth		Business Insurance: No outlook commentary Bond & Specialty: No outlook commentary	Personal Lines: Expect RPC to rise from these levels	Personal Lines: Expect auto RPC to moderately rise from these levels (13.9% in Q1) and remain there for the remainder of the year. Expect home RPC to remain at these elevated levels for the remainder of the year (20.2% in Q1).	Personal Lines: Expect auto RPC to rise from these levels (16.0% in Q2) in the remainder of the year. Expect home RPC to remain in the high-teens for the remainder of the year (19.2% in Q2).	Personal Lines: Expect auto RPC to rise from these levels (16.0% in Q2) in the remainder of the year. Expect home RPC to remain in the high-teens for the remainder of the year (19.2% in Q2).
Investment Income		Fixed Book: Expect after-tax fixed NII to be from a range of \$515 million in Q1 2023 to \$560 million in Q4 (with an average of \$535 million per quarter) Alternatives: No outlook commentary	Fixed Book: Expect after-tax fixed NII to be from a range of \$515 million in Q1 2023 to \$560 million in Q4 (with an average of \$535 million per quarter) Alternatives: No outlook commentary	Fixed Book: Expect after-tax fixed NII to be from a range of \$530 million in Q2 2023 to \$570 million in Q4. Alternatives: No outlook commentary	Fixed Book: Expect after-tax fixed NII to be from a range of \$530 million in Q2 2023 to \$570 million in Q4. Alternatives: No outlook commentary	Fixed Book: Expect after-tax fixed NII to be from a range of \$530 million in Q2 2023 to \$570 million in Q4. Alternatives: No outlook commentary
Capital Management		No outlook commentary for 2023		They do not expect to continue to be able to return nearly 100% in terms of operating earnings between buybacks and dividends and the higher reinsurance retention does not impact their view of capital adequacy.	They expect repurchases to lower in the second half vs the first half (first half saw \$62M of repurchases)	They expect repurchases to lower in the second half vs the first half (first half saw \$62M of repurchases)

Source: Company reports and Wells Fargo Securities, LLC

Highlights of Our Estimate Changes

Overview of our estimate changes. The exhibit below highlights the changes we made to our earnings model following Q2 2023 earnings.

- **2023 EPS** goes down to \$12.30 (from \$13.50) to the higher cats/PYD in the Q1 results, a higher interest expense, and a higher share count given lower repurchases in the second half of this year, partially offset by a lower tax rate in the Q1 results and better underlying margins in Business Insurance.
- **2024 EPS** goes down to \$18.15 (from \$18.35) to reflect a higher cat load, a higher share count (as a result of lower repurchases in 2023), and higher interest expense partially offset by modestly higher NII and better underlying margins in Business Insurance.
- **2025 EPS** is revised down to \$20.50 (from \$21.00) to mainly reflect a higher cat load, a higher share count (as a result of lower repurchases in 2023), higher interest expense, and a modestly higher assumed expense ratio.

Exhibit 2 - TRV Summary of Estimate Changes

(\$ in millions, except as noted)	2023E	2024E	2025E	Prior Estimates			Delta (Absolute)			2023 Outlook Guidance
	2023E	2024E	2025E	2023E	2024E	2025E	2023E	2024E	2025E	
Gross premiums written	42,781	45,161	47,680	42,030	44,372	46,852	751	789	828	
% growth (YoY)	13.0%	5.6%	5.6%	11.0%	5.6%	5.6%	2.0%	(0.0%)	(0.0%)	
Net premiums written	40,097	42,133	44,279	39,550	41,558	43,672	547	576	607	
% growth (YoY)	13.2%	5.1%	5.1%	11.7%	5.1%	5.1%	1.5%	0.0%	0.0%	
Increase in unearned premiums	(2,503)	(1,407)	(1,480)	(2,111)	(1,395)	(1,467)	(392)	(12)	(13)	
Net premiums earned	37,594	40,726	42,799	37,439	40,162	42,205	155	564	594	
% growth (YoY)	11.3%	8.3%	5.1%	10.9%	7.3%	5.1%	0.5%	1.1%	0.0%	
Net investment income (pre-tax)	2,953	3,412	3,750	2,943	3,390	3,725	9	21	25	Expecting \$570-\$595MM from Q3 to Q4 2023 for Fixed NII
Fee income	450	489	513	468	500	525	(17)	(11)	(12)	
Other income	348	348	348	332	345	345	16	3	3	
Total revenue	41,345	44,975	47,410	41,182	44,398	46,800	163	577	610	
Losses and loss adjustment expenses	26,274	27,194	28,590	25,883	26,824	28,156	392	370	434	
Amortization of deferred acquisition costs	6,204	6,745	7,094	6,179	6,652	7,005	25	93	88	
General and administrative expenses	5,328	5,718	5,979	5,277	5,629	5,842	50	89	138	
Interest expense	376	393	393	352	352	352	24	41	41	
Total expenses	38,182	40,050	42,055	37,691	39,457	41,355	492	593	700	
Pretax operating income	3,163	4,925	5,355	3,492	4,941	5,445	(329)	(16)	(90)	
% growth (YoY)	(11.1%)	55.7%	8.7%	(1.9%)	41.5%	10.2%	(9.2%)	14.2%	(1.5%)	
Income tax expense/(benefit)	308	843	914	357	849	936	(50)	(6)	(22)	
After-tax core income	2,855	4,082	4,441	3,134	4,092	4,509	(279)	(10)	(68)	
% growth (YoY)	(4.8%)	43.0%	8.8%	4.5%	30.6%	10.2%	(9.3%)	12.4%	(1.4%)	
Company income tax rate (%)	9.7%	17.1%	17.1%	10.2%	17.2%	17.2%	(0.5%)	(0.1%)	(0.1%)	
Weighted average number of diluted shares	230.8	223.8	215.7	230.8	221.9	213.8	(0.0)	1.9	1.9	
Participating share-based awards	16.0	19.0	19.0	19.0	19.0	19.0	(3.0)	0.0	0.0	
Adjusted Operating EPS	\$12.30	\$18.15	\$20.50	\$13.50	\$18.35	\$21.00	(\$1.19)	(\$0.20)	(\$0.50)	
Profitability Metrics										
Loss and loss adjustment expense ratio	69.4%	66.3%	66.3%	68.7%	66.3%	66.3%	0.8%	(0.0%)	0.1%	
Underwriting expense ratio	<u>28.6%</u>	<u>28.6%</u>	<u>28.5%</u>	<u>28.5%</u>	<u>28.5%</u>	<u>28.4%</u>	<u>0.1%</u>	<u>0.1%</u>	<u>0.1%</u>	Expecting expense ratio of 28.5-29% for 2023
Combined ratio	98.1%	94.9%	94.9%	97.2%	94.8%	94.6%	0.9%	0.1%	0.2%	
Cat points on the combined ratio	7.5%	5.3%	5.3%	6.6%	5.0%	5.1%	0.9%	0.2%	0.1%	
PYD points on the combined ratio	(0.7%)	(0.3%)	(0.2%)	(0.7%)	(0.3%)	(0.2%)	0.0%	0.0%	(0.0%)	
Current accident year combined ratio	91.3%	89.9%	89.8%	91.3%	90.1%	89.7%	0.0%	(0.2%)	0.1%	
Underlying loss ratio	62.7%	61.3%	61.3%	62.8%	61.6%	61.3%	(0.1%)	(0.3%)	(0.0%)	
Segment Underwriting Income:										
Business Insurance	\$736	\$1,022	\$1,085	\$802	\$950	\$1,173	(\$66)	\$72	(\$87)	
Bond & Specialty Insurance	\$733	\$647	\$676	\$673	\$643	\$680	\$60	\$4	(\$4)	
Personal Insurance	(\$1,195)	(\$75)	(\$76)	(\$872)	\$1	(\$90)	(\$323)	(\$76)	\$14	
Book value per share	\$100.52	\$111.39	\$124.64	\$100.01	\$111.07	\$124.83	\$0.51	\$0.32	(\$0.18)	
ROE	12.7%	17.1%	17.4%	14.0%	17.4%	17.8%	(1.3%)	(0.3%)	(0.4%)	

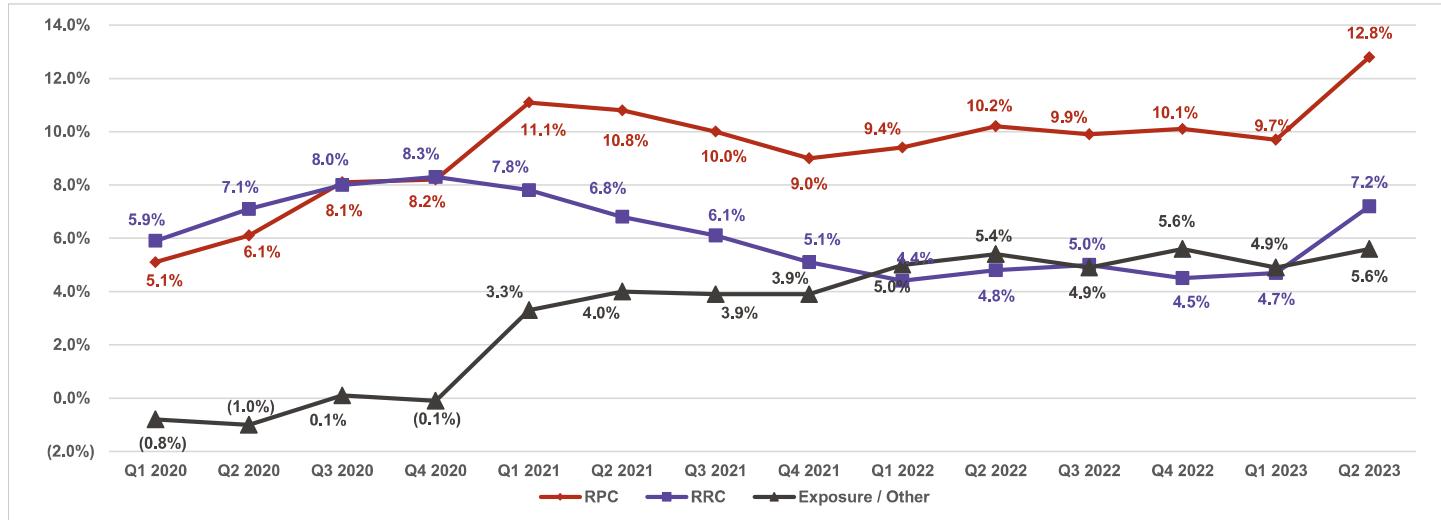
Source: Company reports and Wells Fargo Securities, LLC estimates

Pricing Highlights—Commercial Lines

Business Insurance Rating Environment—TRV Rates Up to Record-Level, Exposure and RRC Both Up

- In Q2, the **Business Insurance** renewal rate change was +7.2%, a strong acceleration from the +4.7% in the prior quarter. Exposure growth was up 5.6%, up from the 4.9% in Q1 and remaining at strong levels. The 12.8% of RPC in Q2 was a record-high for TRV and was well above the 9.7% in Q1 and the 10.2% in the prior year quarter. The exhibits below show the trends in TRV's quarterly domestic Business Insurance (BI) renewal rate change since 2020.

Exhibit 3 - Pricing and Exposure Growth Seen By Travelers



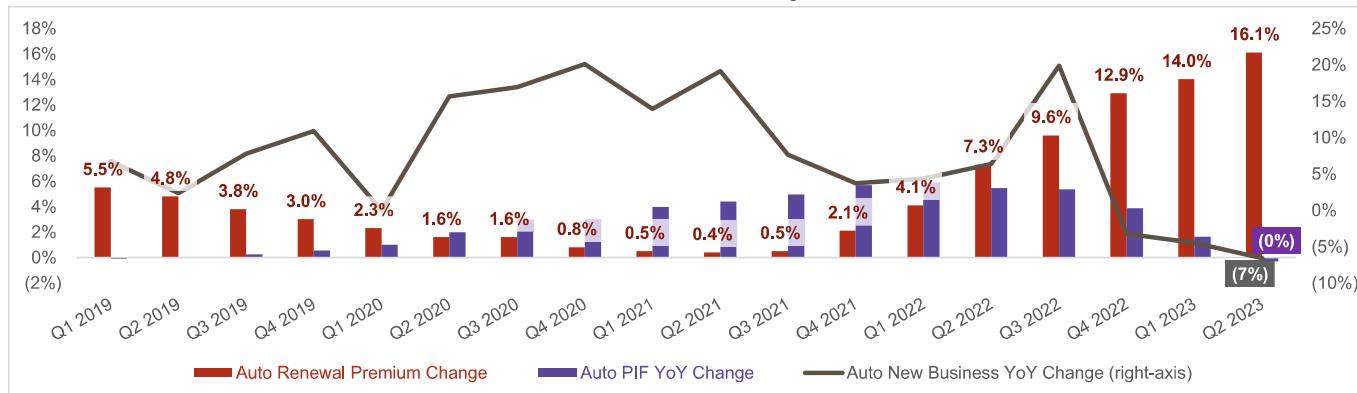
Source: Company data and Wells Fargo Securities, LLC

Pricing Highlights—Personal Lines

Personal Lines—TRV Continues to See Rate Acceleration, Margins Remain Elevated

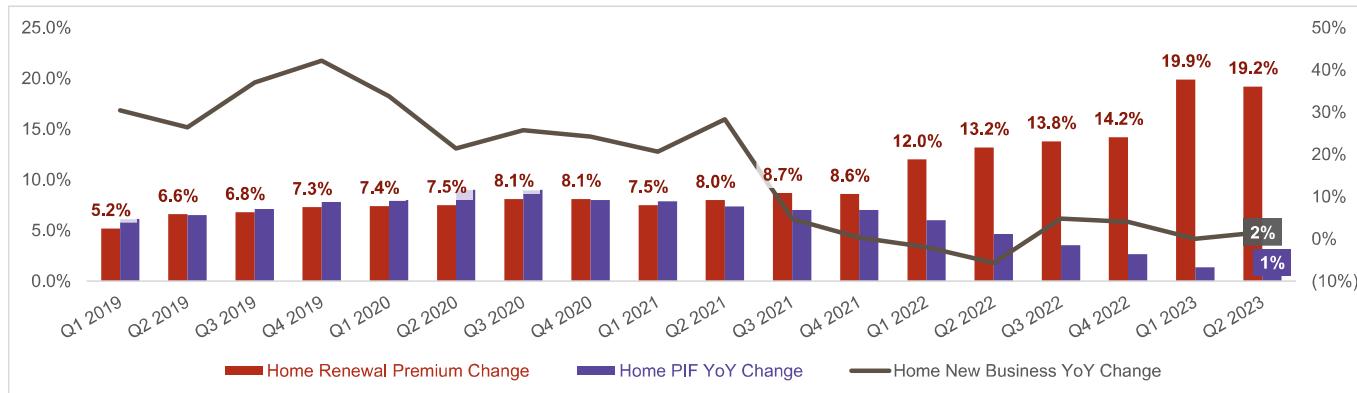
- Within **Personal Auto**, TRV saw renewal premium change continue to accelerate sequentially at 16.1%, which was up from the 14.0% last quarter; however, their auto underlying margin remained above 100% for the fifth straight quarter (103.5% in Q2) and was up 1.7 points Y/Y highlighting the need for additional rate (and the lag in these rates earning through) and was modestly higher vs the 103.4% in the Q1, which is a seasonally favorable quarter. TRV said they are not at written price adequacy, missing their previous guide of being close to or at written price adequacy, which is not surprising given the monthly results we have seen from PGR in the Q2. They expect RPC to continue to rise from these levels for the remainder of the year but did not give a timeline on reaching price adequacy. They said severity has proven stickier than previously expected, currently in the low double digits.
- Homeowners'** RPC decelerated modestly sequentially to 19.2% from the record-high 19.9% in Q1 but remains at strong levels. They expect the RPC in home to remain in the high-teens for the remainder of the year.
- Auto PIFs decline sequentially, while home modestly up.** Travelers' new business in auto decreased 7% Y/Y to \$297 million, after decreasing 4% Y/Y last quarter and marked the third straight quarter with Y/Y declines as TRV continues to pull new business away from states where they are not getting enough rate and abiding by stricter underwriting standards. This is also reflected in the PIF numbers, as auto PIFs declined 0.7% sequentially, which was the second straight sequential decline after Q1 saw the biggest sequential drop since Q1 2014. Home new business was up 2% Y/Y at \$321 million and up from the flat Y/Y growth in the prior quarter. From a PIF standpoint, home saw a 0.5% sequential increase, which was a slowdown from the 1.4% sequential increase last quarter.

Exhibit 4 - Personal Auto Statistics - RPC, PIF, and New Business Y/Y Change



Source: Company Reports and Wells Fargo Securities, LLC

Exhibit 5 - Homeowners' Statistics - RPC, PIF, and New Business Y/Y Change



Source: Company Reports and Wells Fargo Securities, LLC

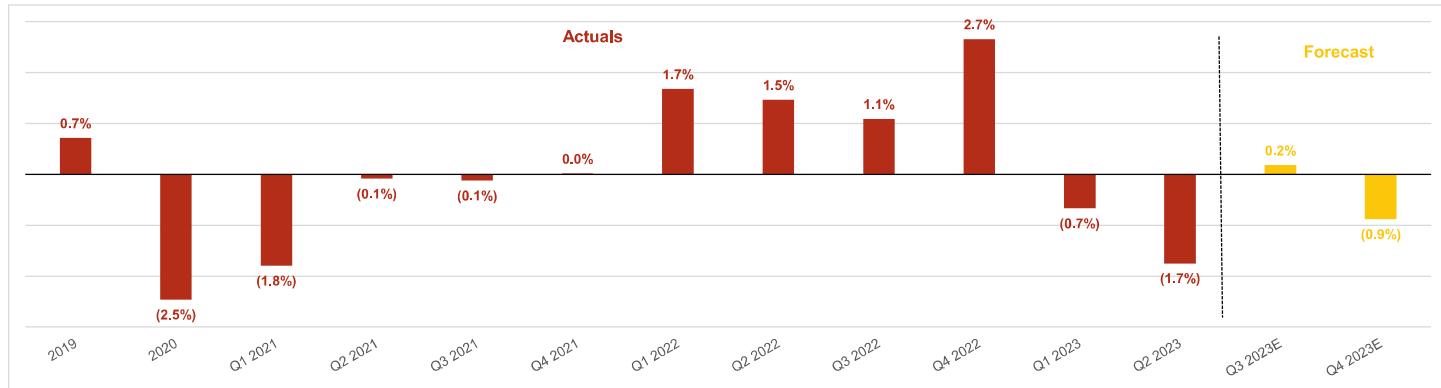
Underlying Margin Tables

Exhibit 6 - Consolidated Underlying Margin Trends

Underlying Margin Trends	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023
Reported Combined Ratio	93.7%	98.4%	101.5%	92.4%	95.5%	103.7%	94.9%	86.7%	96.6%	95.3%	98.6%	88.0%	91.3%	98.3%	98.2%	94.5%	95.4%	106.5%
Catastrophe Losses, net of reinsurance	2.8%	5.3%	3.4%	1.2%	4.6%	12.3%	5.3%	0.4%	11.3%	6.3%	6.4%	0.4%	2.0%	9.0%	5.9%	5.2%	6.0%	16.1%
Prior Year Reserve Development (Unfavorable)/Favorable	(0.7%)	(1.8%)	4.1%	(0.8%)	(0.4%)	(0.0%)	(1.9%)	(2.4%)	(4.3%)	(2.4%)	0.8%	(1.2%)	(1.9%)	(3.5%)	(0.2%)	(2.1%)	(1.2%)	(0.7%)
Underlying Combined Ratio	91.6%	94.9%	94.1%	92.1%	91.3%	91.4%	91.5%	88.7%	89.5%	91.4%	91.4%	88.7%	91.2%	92.8%	92.5%	91.4%	90.5%	91.1%
Underlying (Improvement)/deterioration	(0.8%)	1.3%	1.1%	0.9%	(0.3%)	(3.5%)	(2.5%)	(3.3%)	(1.8%)	(0.1%)	(0.1%)	0.0%	1.7%	1.5%	1.1%	2.7%	(0.7%)	(1.7%)
Underlying Loss Ratio	61.9%	64.7%	64.5%	63.0%	61.3%	60.4%	62.2%	59.3%	59.7%	61.7%	62.0%	60.2%	62.2%	63.8%	64.4%	63.5%	61.8%	62.5%
YoY Change	0.1%	1.8%	1.3%	1.3%	(0.7%)	(4.3%)	(2.3%)	(3.6%)	(1.6%)	1.2%	(0.2%)	0.9%	2.5%	2.1%	2.4%	3.3%	(0.4%)	(1.3%)
Underlying Expense Ratio	29.7%	30.2%	29.5%	29.1%	30.0%	31.0%	29.3%	29.4%	29.9%	29.7%	29.4%	28.5%	29.0%	29.0%	28.1%	27.9%	28.7%	28.6%
YoY Change	(0.9%)	(0.5%)	(0.2%)	(0.4%)	0.3%	0.8%	(0.2%)	0.3%	(0.0%)	(1.3%)	0.1%	(0.9%)	(0.9%)	(0.7%)	(1.3%)	(0.6%)	(0.3%)	(0.4%)

Source: Company reports and Wells Fargo Securities, LLC

Exhibit 7 - Consolidated Underlying Combined Ratio Y/Y (Improvement)/Deterioration



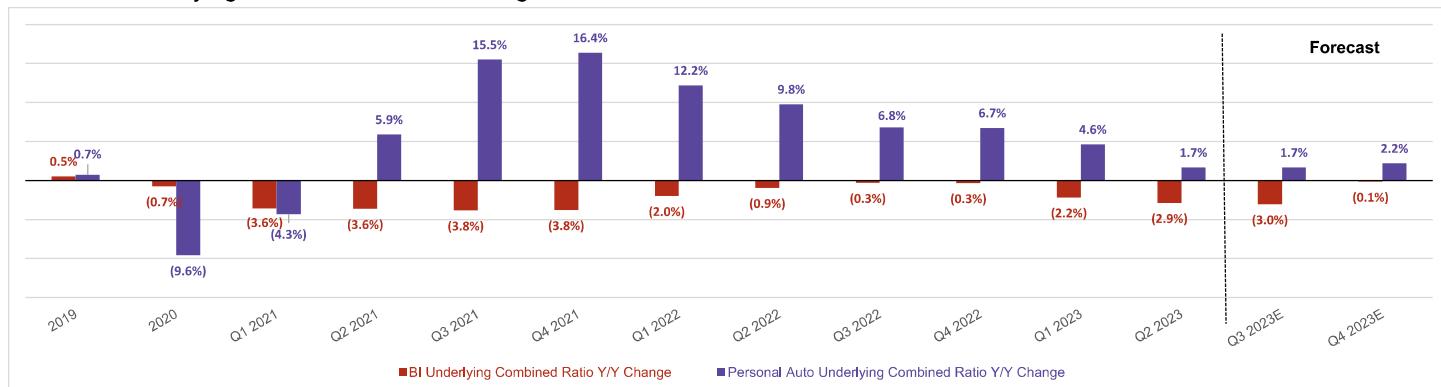
Source: Company Reports and Wells Fargo Securities, LLC Estimates

Exhibit 8 - Underlying Combined Ratio Trends by Segment

Underlying Combined Ratio Trends	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023
Business Insurance	95.0%	97.4%	95.9%	96.4%	97.3%	97.0%	94.0%	93.6%	93.7%	93.4%	90.2%	89.9%	91.7%	92.4%	89.9%	89.5%	89.6%	89.6%
Underlying (Improvement) deterioration	(0.5%)	0.9%	0.5%	1.0%	2.3%	(0.4%)	(1.8%)	(2.8%)	(3.6%)	(3.6%)	(3.8%)	(3.8%)	(2.0%)	(0.9%)	(0.3%)	(0.3%)	(2.2%)	(2.2%)
Bond & Specialty	81.1%	81.0%	83.6%	81.3%	85.7%	88.1%	89.0%	85.0%	84.2%	83.4%	83.4%	83.3%	82.2%	82.2%	82.2%	82.2%	82.2%	82.1%
Underlying (Improvement) deterioration	0.4%	0.5%	5.3%	3.2%	4.6%	7.1%	5.5%	3.7%	(1.5%)	(4.7%)	(5.6%)	(1.7%)	(2.0%)	(1.2%)	(1.2%)	(1.1%)	0.0%	(0.1%)
Personal Insurance	89.1%	94.6%	94.0%	88.4%	84.0%	84.0%	88.7%	83.1%	85.4%	91.0%	95.2%	88.7%	92.8%	96.0%	99.3%	96.2%	92.9%	94.1%
Underlying (Improvement) deterioration	(1.4%)	2.0%	1.1%	0.5%	(5.1%)	(10.7%)	(5.3%)	(5.3%)	1.4%	7.0%	6.5%	5.6%	7.4%	5.0%	4.2%	7.5%	0.1%	(1.9%)
Personal Insurance Breakdown:	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Automobile	92.1%	93.8%	92.7%	99.6%	90.9%	86.1%	81.5%	87.4%	86.6%	92.0%	97.0%	103.8%	98.8%	101.8%	103.8%	110.5%	103.4%	103.4%
Underlying (Improvement) deterioration	(4.2%)	(1.7%)	0.1%	2.7%	(1.2%)	(7.7%)	(11.2%)	(12.2%)	(4.3%)	5.9%	15.5%	16.4%	12.2%	9.8%	6.8%	6.7%	4.6%	4.6%
Homeowners & Other	82.6%	92.9%	93.5%	73.6%	75.7%	82.0%	96.8%	78.5%	84.1%	89.9%	93.3%	73.4%	86.9%	90.3%	94.9%	82.2%	82.7%	85.2%
Underlying (Improvement) deterioration	2.4%	7.7%	5.0%	1.1%	(6.9%)	(10.9%)	3.3%	5.0%	8.4%	7.9%	(3.5%)	(5.1%)	2.8%	0.3%	1.6%	8.8%	(4.2%)	(5.0%)

Source: Company data and Wells Fargo Securities, LLC

Exhibit 9 - Underlying Combined Ratio Y/Y Change - BI and Personal Auto



Source: Company Reports and Wells Fargo Securities, LLC

Valuation

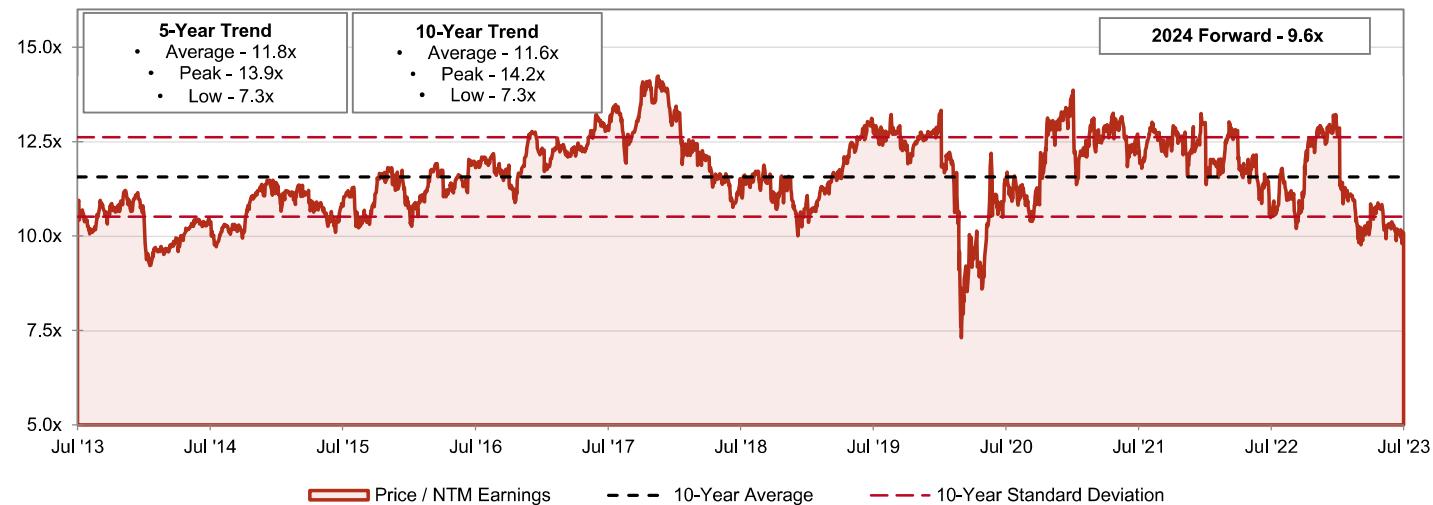
Current valuation. The TRV shares are now trading at 1.81x Q2 2023 book value, which is above its 5-year (1.47x) average, and its 10-year (1.41x) average multiple but below the peak level of 2.05x. The P/B multiple continues to be elevated as reported book value has higher unrealized losses on TRV's investment portfolio vs historical averages; when excluding unrealized losses (net), shares are currently trading at 1.42x Q2 adjusted book of \$121.71, which is modestly above the 1.37x 5-year average ex AOCI. On a price-to-earnings basis, the shares are trading at 9.6x our 2024 EPS estimate versus the 5-year average of 11.7x, 10-year average of 11.6x and the 5-year and 10-year peak of 14.2x.

Exhibit 10 - TRV Historical P/BV



Source: Company reports, Factset, and Wells Fargo Securities, LLC estimates

Exhibit 11 - TRV Historical Price-To-Earnings Multiples



Source: FactSet and Wells Fargo Securities, LLC

Exhibit 12 - TRV Consolidated Earnings Model

	2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023E	2023E	Q1 2024E	Q2 2024E	Q3 2024E	Q4 2024E	2024E	Q1 2025E	Q2 2025E	Q3 2025E	Q4 2025E	2025E
(\$ in millions, except as noted)																					
Summary																					
Business Insurance																					
Bond & Specialty Insurance	2,889	811	813	560	884	3,068	713	485	847	3,115	950	825	918	1,085	915	1,024	915	1,143	1,092	1,104	
Personal Insurance	833	239	285	275	1,103	248	289	284	1,070	253	243	279	264	297	266	262	279	279	279	279	
Other	939	252	260	147	65	1,065	58	165	173	1,078	160	160	19	387	537	1,039	244	1,021	279	1,042	
WFS Estimate Versus Consensus	<u>(\$639)</u>	<u>(\$51)</u>	<u>(\$51)</u>	<u>(147)</u>	<u>(65)</u>	<u>(1,065)</u>	<u>191</u>	<u>102</u>	<u>102</u>	<u>1,071</u>	<u>102</u>										
Adjusted Pre-Tax Operating Income	<u>1,207</u>	<u>751</u>	<u>621</u>	<u>980</u>	<u>3,559</u>	<u>922</u>	<u>1,13</u>	<u>15,6%</u>	<u>15,6%</u>	<u>1,13</u>	<u>1,256</u>	<u>931</u>	<u>1,110</u>	<u>1,120</u>							
Tax Rate	17.8%	13.3%	16.9%	15.3%	17.3%	15.7%	15.4%	15.4%	15.4%	15.7%	15.9%	17.4%	15.6%	16.5%	16.5%	16.5%	16.5%	16.5%	16.5%	16.5%	
Taxes	(127)	(127)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	(128)	
Adjusted After-Tax Operating Income	<u>1,039</u>	<u>624</u>	<u>526</u>	<u>810</u>	<u>2,989</u>	<u>970</u>	<u>15</u>	<u>725</u>	<u>1,145</u>	<u>2,055</u>	<u>1,037</u>	<u>785</u>	<u>1,333</u>	<u>927</u>	<u>1,333</u>	<u>927</u>	<u>1,333</u>	<u>1,333</u>	<u>1,333</u>	<u>1,333</u>	
Adjusted Operating EPS	<u>\$13.04</u>	<u>\$4.22</u>	<u>\$2.56</u>	<u>\$2.20</u>	<u>\$3.40</u>	<u>\$12.43</u>	<u>\$4.41</u>	<u>\$0.05</u>	<u>\$2.43</u>	<u>\$4.09</u>	<u>\$12.30</u>	<u>\$4.54</u>	<u>\$3.47</u>	<u>\$4.14</u>	<u>\$0.02</u>	<u>\$18.15</u>	<u>\$5.35</u>	<u>\$2.98</u>	<u>\$4.66</u>	<u>\$5.53</u>	<u>\$0.50</u>
YoY Change in Adjusted Operating Income	<u>32.7%</u>	<u>42.2%</u>	<u>(29.8%)</u>	<u>(20.2%)</u>	<u>(36.6%)</u>	<u>(10.9%)</u>	<u>(28.8%)</u>	<u>(10.9%)</u>													
Consensus EPS	<u>33.0%</u>	<u>54.7%</u>	<u>(25.7%)</u>	<u>(15.4%)</u>	<u>(34.6%)</u>	<u>(10.9%)</u>	<u>(28.0%)</u>	<u>(10.9%)</u>													
WFS Estimate Versus Consensus	<u>(\$639)</u>	<u>(\$51)</u>	<u>(147)</u>	<u>(65)</u>	<u>(1,065)</u>	<u>191</u>	<u>102</u>														
Premiums																					
YoY Change in Gross Premiums Written																					
Investment Income (Pre-Tax)																					
Fixed Maturities Pre-Tax Annualized Yield	1,989	505	512	534	562	2,113	575	591	615	638	2,418	660	681	701	721	2,762	739	758	775	792	3,064
Alternatives	2.6%	2.7%	2.9%	3.1%	3.2%	3.0%	3.2%	3.2%	3.3%	3.4%	3.3%	3.6%	3.6%	3.7%	3.8%	3.7%	3.8%	4.0%	4.1%	4.1%	
Alternatives Pre-Tax Annualized Yield	1,077	142	197	46	419	53	78	117	120	130	368	125	130	135	138	503	132	135	138	140	545
Short-Term Securities	18.8%	8.8%	13.8%	3.2%	2.3%	7.3%	3.6%	5.3%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.2%	8.2%	8.3%	8.3%	8.2%	
Investment Expenses	5	2	9	23	39	73	47	55	56	57	215	50	50	50	50	200	50	50	50	50	159
Total Pre-Tax Net Investment Income	3,031	637	707	593	625	2,662	663	712	776	802	2,053	819	842	865	886	3,412	907	928	948	967	3,750
Margins	3.7%	3.0%	3.3%	2.7%	2.8%	3.0%	3.0%	3.2%	3.5%	3.6%	3.6%	3.6%	3.6%	3.6%	3.6%	3.6%	3.6%	3.6%	3.6%	3.6%	
Loss Ratio	65.1%	62.3%	69.3%	70.1%	66.8%	67.2%	66.7%	77.0%	68.2%	64.1%	69.4%	63.6%	63.6%	63.6%	63.6%	65.0%	69.2%	67.8%	65.5%	65.5%	68.3%
Expense Ratio	94.5%	91.3%	98.3%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.5%	94.9%
Combined Ratio	1,847	160	746	512	459	1,877	535	1,481	500	300	2,816	450	800	550	350	2,150	475	825	375	375	2,250
Catastrophe Losses	6.0%	2.0%	9.0%	5.9%	5.2%	5.0%	5.6%	6.0%	5.2%	5.2%	3.0%	7.5%	4.6%	5.3%	3.0%	15	21	31	53	53	53
Points on Combined Ratio	(538)	(153)	(291)	(20)	(115)	(649)	(105)	(60)	(12)	(93)	(327)	(36)	(41)	(3)	(4)	(15)	(2)	(2)	(2)	(2)	
Reserve Development	(1.7%)	(1.9%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	(1.2%)	
Adjusted Margins																					
Underlying Loss Ratio	60.9%	62.2%	63.8%	64.4%	63.5%	61.8%	62.5%	61.6%	62.0%	62.7%	61.4%	62.0%	62.0%	61.6%	61.6%	60.6%	61.3%	61.3%	61.3%	61.3%	
Underlying Combined Ratio	90.3%	91.2%	92.8%	91.4%	92.5%	91.7%	91.7%	90.1%	92.7%	90.1%	90.5%	90.5%	90.5%	90.5%	90.5%	90.5%	90.5%	90.5%	90.5%	90.5%	
YoY Change in Loss Ratio (Favorable)	0.0%	2.5%	2.1%	1.1%	1.4%	2.7%	2.7%	1.9%	2.7%	1.9%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%	0.4%
YoY Change in Combined Ratio (Favorable)	(0.5%)	(1.7%)	(1.4%)	(1.1%)	(1.4%)	(1.1%)	(1.1%)	(1.1%)	(1.1%)	(1.1%)	(0.2%)	(0.2%)	(0.2%)	(0.2%)	(0.2%)	(0.2%)	(0.2%)	(0.2%)	(0.2%)	(0.2%)	
Book Value and Return on Equity																					
GAAP Book Value per Share	\$106.40	98.39	98.39	84.94	92.90	99.80	99.46	97.05	100.52	100.52	100.52	100.52	100.52	100.52	100.52	100.52	100.52	100.52	100.52		
Operating Return on Equity	11.8%	14.9%	10.1%	9.7%	15.3%	11.7%	17.1%	12.7%	13.0%	13.0%	20.2%	12.7%	17.8%	13.4%	15.6%	22.0%	17.1%	18.9%	13.7%	15.7%	21.4%
Share Count	241.2	240.0	237.3	234.4	232.1	231.0	228.9	227.2	225.5	225.5	220.6	218.2	215.8	213.5	211.3	209.1	206.9	204.7	202.8	201.7	
Funding Common Shares	256.9	245.7	241.1	237.9	235.3	239.7	234.4	229.7	230.2	230.2	228.8	227.0	224.8	222.7	220.6	223.8	218.6	216.6	214.7	212.8	
Weighted Average Diluted Shares																					
Capital Return to Shareholders																					
Common Dividends	876	225	221	221	221	881	218	233	229	227	220	907	226	225	224	222	222	222	222	222	
Share Repurchases	2,156	559	501	501	501	462	680	633	527	2,369	676	680	677	675	676	674	672	672	672	672	
Total Capital Returned	3,032	773	722	722	722	1,492	1,059	1,059	46.1%	83.0%	86.6%	73.1%	66.3%	57.1%	78.0%	67.1%	68.2%	68.2%	68.2%	68.2%	
Total Payout Ratio (% of Operating Income)																					
Beginning GAAP Equity	29,201	28,887	25,531	22,874	19,906	28,887	21,560	23,052	21,685	22,051	21,560	22,051	21,560	22,051	22,051	22,669	23,385	23,136	24,043	24,548	
Net Income	3,667	1,020	225	(214)	(232)	(881)	(218)	(223)	(229)	(227)	(227)	(227)	(227)	(227)	(227)	(227)	(227)	(227)	(227)	21,043	
Common Dividends	(876)	(1,020)	(225)	(214)	(232)	(501)	(462)	(400)	(300)	(450)	(450)	(450)	(450)	(450)	(450)	(450)	(450)	(450)	(450)	4,441	
Share Repurchases	(2,156)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	(1,059)	894	
Change in AOCI	(1,309)	(3,795)	(2,553)	(2,753)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	(1,463)	1,800	
Other	(360)	(192)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	(71)	0	
Ending GAAP Equity	28,887	28,331	22,874	19,906	21,560	23,052	21,565	22,051	22,669	23,031	24,043	24,548	24,548	24,548	24,548	24,548	24,548	24,548	24,548	24,548	
Debt Capital	20.2%	22.2%	24.2%	26.8%	25.3%	25.3%	24.0%	25.0%	24.8%	24.3%	24.3%	24.0%	24.0%	24.0%	24.0%	24.0%	22.9%	22.8%	22.7%	22.0%	

Source: Company Reports, Factset and Wells Fargo Securities, LLC estimates

Investment Thesis, Valuation and Risks

The Travelers Companies, Inc. (TRV)

Investment Thesis

We believe that TRV will continue to benefit from the hard commercial market as pricing should continue to have legs given inflation and higher weather volatility. Although we are positive on the commercial lines space as a whole, we are more cautious on TRV relative to peers due to its smaller account exposure, higher workers' comp focus as both are getting less rate than other lines/account sizes, and personal lines exposure, particularly auto, which is well above target margins of mid-90s. We still believe that risk remains around social inflation, lower reserve releases, but we believe that these risks are adequately reflected in shares with the risk/reward now more neutral and rate the shares Equal Weight as a result.

Target Price Valuation for TRV: \$185.00 from NC

Our price target of \$185 is based on around a ~1.7x multiple of our projected 2024 book value estimate of around \$111 and just over 10x our 2024 EPS estimate of \$18.15.

Risks to Our Price Target and Rating for TRV

Risks to the downside include large catastrophe losses, adverse reserve development, increased competition, a deterioration in loss costs, and a rise in D&O claims, while risks to the upside include stronger premium growth and reported / underlying margins coming in better than expected.

Required Disclosures

I, Elyse Greenspan, certify that:

- 1) All views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers discussed; and
- 2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

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Additional Information Available Upon Request

The Travelers Companies, Inc. Rating History as of 07-19-2023

powered by: BlueMatrix



Initiation (I); Drop Coverage (D); Overweight (BUY); Equal Weight (HOLD); Underweight (SELL); Suspended (SR); Not Rated (NR); No Estimate (NE)

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STOCK RATING

OW=Overweight: Total return on stock expected to be 10%+ over the next 12 months. **BUY**

EW=Equal Weight: Total return on stock expected to be -10% to +10% over the next 12 months. **HOLD**

UW=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

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