S&P Global
Market Intelligence

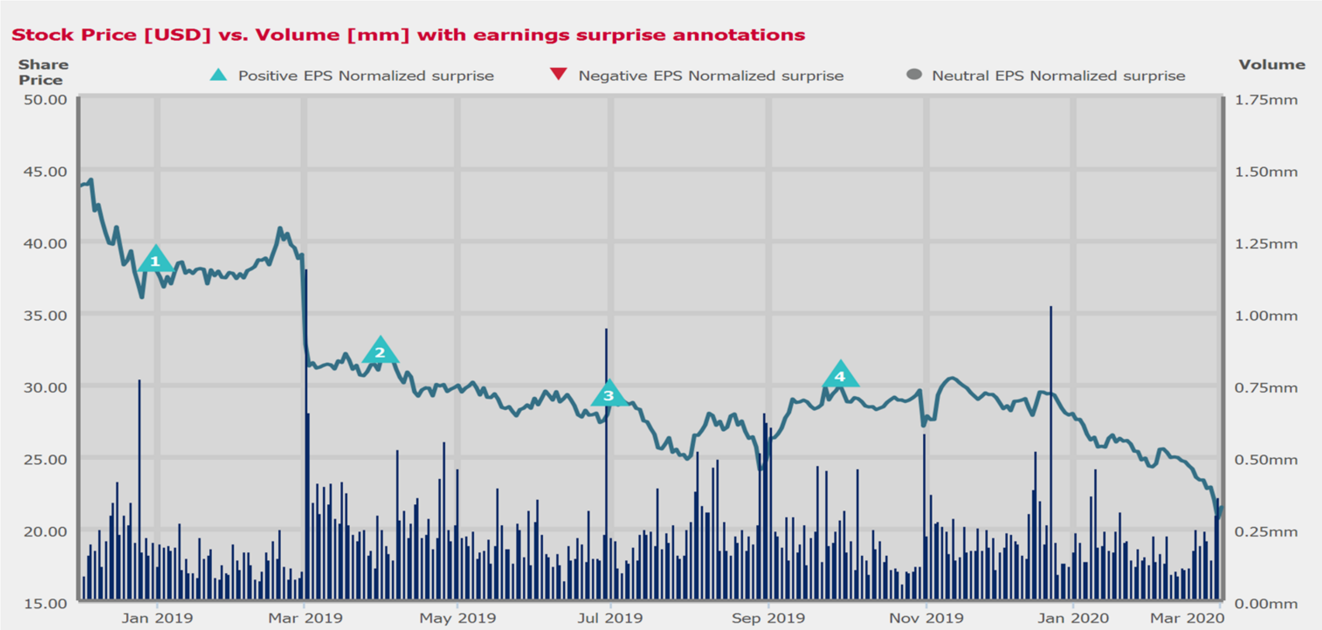
Universal Insurance Holdings, Inc.
NYSE:UVE
FQ4 2019 Earnings Call Transcripts

Tuesday, March 03, 2020 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2019-		
	CONSENSUS	ACTUAL	SURPRISE
EPS Normalized	0.50	0.61	▲22.00
Revenue (mm)	227.76	229.64	▲0.83

Currency: USD
Consensus as of Oct-07-2019 9:10 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2018	0.06	0.13	▲1 116.67 %
FQ1 2019	0.98	1.00	▲2 2.04 %
FQ2 2019	1.00	1.05	▲3 5.00 %
FQ3 2019	0.50	0.61	▲4 22.00 %

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Call Participants

EXECUTIVES

Frank Crawford Wilcox
CFO & Principal Accounting Officer

Jon William Springer
President, Chief Risk Officer & Director

Rob Luther
Vice President of Corporate Development, Strategy & Investor Relations

Stephen Joseph Donaghy
CEO & Director

ANALYSTS

William Harry Broomall
Dowling & Partners Securities, LLC

Presentation

Operator

Good morning, ladies and gentlemen, and welcome to the UVE Fourth Quarter 2019 Earnings Conference Call. [Operator Instructions] As a reminder, this conference call is being recorded.

I would now like to turn this over to Rob Luther, Vice President of Corporate Strategy and Investor Relations.

Rob Luther
Vice President of Corporate Development, Strategy & Investor Relations

Thank you, and good morning, everyone. Welcome to our discussion on our fourth quarter 2019 earnings results, which we reported yesterday. On the call with me today is Steve Donaghy, Chief Executive Officer; Jon Springer, President and Chief Risk Officer; and Frank Wilcox, Chief Financial Officer. Before we begin, please note today's discussion may contain forward-looking statements and non-GAAP financial measures. Forward-looking statements involve assumptions, risks and uncertainties that could cause actual results to differ materially from those statements. For more information, please see the press release, our earnings presentation and UVE's SEC filings, all of which are available on the Investors section of our website at universalinsuranceholdings.com and on the SEC's website. A reconciliation of non-GAAP financial measures to comparable GAAP measures is included in the quarterly press release.

With that, Steve, I'll turn it over to you.

Stephen Joseph Donaghy
CEO & Director

Thank you, Rob, and good morning, everyone. Thank you all for joining us today. We ended 2019 with total revenue up 14% to $939.4 million, driven primarily by higher organic premium volume and retention due to our effective marketing strategy, agent relations and customer service efforts and premium pricing flowing through the book and our investment portfolio performance, partially offset by increased reinsurance costs. During 2019, we also returned a record $92.3 million to shareholders through share repurchases and dividends. Since taking over as CEO in July of 2019, we have continued to respond to the well-documented current Florida dynamics that have affected all industry participants. In spite of these challenges, we produced an annualized return on average equity of 9.2%. This annual result includes enhanced conservatism across many different fronts, including the run-up of claims prior to the effective date of new AOB legislation, the impact of a hardening reinsurance market and the overall influence of social inflation. As disclosed, we bolstered our prior and current year reserve position in addition to building conservatism into our subrogation expectation, despite 2019 being our highest subrogation receivables collected in the company's history. Our financial strength including a debt-to-equity ratio of only 2%, along with filing for a 12.4% primary rate increase in Florida and our direct-to-consumer platform Clovered have positioned us for long-term, sustainable bottom line growth going forward into 2020 and beyond. As we noted in our press release, we believe the diligent work we have put forth the last several months, in addition to having already secured over 75% of our reinsurance capacity for June 1, 2020, puts us in a position to provide 2020 guidance of GAAP and non-GAAP adjusted earnings per share range between $2.8 and $3.10. And a return on average equity between 17% and 20%, both of which assume no extraordinary weather events in 2020. So with that, let me turn it over to Frank to walk through our financial results. Frank?

Frank Crawford Wilcox
CFO & Principal Accounting Officer

Thank you, Steve, and good morning, everyone. As a reminder, discussions today on adjusted operating income and adjusted EPS are on a non-GAAP basis, and exclude effects from unrealized and realized gains and losses on investments and extraordinary reinstatement premiums and related commissions. Adjusted operating income also excludes interest expense. EPS for the quarter was a loss of $1.55 on a GAAP basis and a loss of $1.57 on a non-GAAP adjusted basis. For the year, we were profitable, generating EPS of $1.36 on a GAAP basis and $1.18 on a non-GAAP adjusted basis. Turning to underwriting. Direct premiums written grew by 12.5% in Q4 compared to the prior year, led by the impact of rate increases in Florida and other states taking effect as well as strong direct premium growth in the fourth quarter of 23.3% in states outside Florida. For the full year, direct premiums written were up 8.6%, led by the rate increases taking effect and policy mix as well as strong direct written premium growth of 27.6% in other states and a slightly improved policy retention. On the expense side, the combined ratio increased 31.7 points for the quarter to 142.9% and 16.6 points for the full year to 103.9%.

The full year increases were driven primarily by 9 loss ratio points from reduced claims settlement fees as prior year's catastrophe claims conclude an 8.5% increase for current year core loss ratio strengthening. An increase of 2.7 points for the increase in weather in 2019, partially offset by a 2.5 point decrease in prior year reserve development, which includes the impact of reducing anticipated subrogation recoveries.

Turning to services. Total services revenue increased 20.5% and to $14.7 million for the quarter and 11.5% to $55.6 million for the full year, driven by commission revenue earned on reinsurance contracts placed by our intermediary, Blue Atlantic, and an increase in MGA, policy fees and other revenue related to new and renewal policy volume.

Moving on to investments. Net investment income decreased 0.3% for the quarter, but increased 23.9% for the year, primarily due to increased assets under management and asset mix shifting towards higher-yielding investment-grade bonds during 2018 and 2019. These results were partially offset by a lower trend in yields on cash and short-term investments during the second half of 2019. In regards to capital deployment, as Steve mentioned, in 2019, we returned a record $92.3 million to shareholders through share repurchases and dividends. As far as guidance is concerned for 2020, we expect a GAAP and non-GAAP adjusted EPS range between $2.80 and $3.10 assuming no extraordinary weather events in 2020 and a return on average equity between 17% and 20%. The guidance assumes no extraordinary weather in 2020. And also assumes a flat equity market for GAAP EPS. Whether that exceed plan, we expect to see both the benefit from our claims adjusting business and increased loss costs. Let me now turn it over to Jon to walk through some additional specifics.

Jon William Springer
President, Chief Risk Officer & Director

Thank you, Frank, and good morning. I would like to start with some additional color on past cat events, and talk briefly about our enhanced conservatism across many fronts, including the run-up of claims prior to the effective date of new AOB legislation and the reinsurance market. On past cat events, we continue to make more progress on closing past catastrophe claims. I really can't say enough good things about the effort of our in-house claims staff, our claims staff have handled over 110,000 total catastrophe claims since the day Irma made landfall approximately 2.5 years ago. As of year-end, Hurricanes, Matthew and Florence, each had less than 15 open claims and are nearing the end. Hurricane Michael had approximately 250 open claims, and we did increase the ultimate at year-end by $10 million from $350 million to $360 million. This is our first change in ultimate for Michael and represents just a 2.9% increase. On Hurricane Irma, we started the quarter with just under 2,000 claims remaining open. And by year-end, that number was down to 800. We increased the ultimate to $1.4 billion at year-end. As a reminder, from a net exposure standpoint, at this point in the life cycle of Hurricane Irma, the vast majority of this increase in ultimate is covered by the Florida hurricane catastrophe fund.

Turning now to our year-end loss bookings. In the fourth quarter, we set aside an additional $84.4 million for prior accident years by booking $43.7 million of prior year's adverse development and reducing our prior year's anticipated subrogation recoveries by $40.7 million. In addition, we strengthened the current accident year by a total of $41.4 million, which included $16.7 million allocated to current year weather events beyond plan and $24.7 million to further bolster our 2019 reserves, primarily related to the run-up of lawsuits filed on claims with an AOB prior to the effective date of the new legislation. As an unfortunate consequence to the new legislation, May, June and July were 3 of our largest months ever for lawsuits filed on claims with an AOB. Thankfully, we have seen a reduction in these type of lawsuits in the months following. As an update on reinsurance, for the most part, the 2019 hurricane season was a much needed year off for Florida primary insurance companies, policyholders and their reinsurance partners. We have begun the process of securing capacity for our June 1, 2020, renewal and with the Florida Hurricane catastrophe fund and multiyear capacity, we currently stand with over 75% of our desired catastrophe capacity already secured. It is still too early to speculate on the ultimate impact of the upcoming June 1 reinsurance renewals, but we are encouraged that our multiyear buying strategy and the recent rate filing will afford us stability in keeping our primary rates in sync with changes in reinsurance pricing.

With that, I'll turn it back to Rob.

Rob Luther
Vice President of Corporate Development, Strategy & Investor Relations
Thanks, John. I'd like to ask the operator to now open the line for questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Bill Broomall with Dowling.

William Harry Broomall
Dowling & Partners Securities, LLC

Great. If I could just jump in to a couple of items, starting with the cats, I think it was a total of $16.7 million for 2019. Can you just maybe break that apart for us what was Q4 related and what might have been from earlier in the year?

Jon William Springer
President, Chief Risk Officer & Director

Yes. The $16.7 million is all IBNR bill and it's related really to all of the events, starting with those that happened earlier in the year and progressing on to the fourth quarter.

William Harry Broomall
Dowling & Partners Securities, LLC

Okay. Got it. And when we -- on the adverse development is that really almost all related to, I guess, is it all in Florida and all related to the litigation trends, 100%. Is that the best way to think about it?

Jon William Springer
President, Chief Risk Officer & Director

Well, I don't know that I would say 100%. But as we said in our opening remarks, that is a driver of it, definitely.

William Harry Broomall
Dowling & Partners Securities, LLC

Okay. Got it. And then switching over to the Subro change. So if I remember correctly, that started in 2016 is when you might have made a larger effort to address the Subro issue. And the -- I think in your prepared remarks, you mentioned that this quarter was the largest kind of recoveries that you've gotten under that program. Can you just help us think about with that background, how you thought about the change this quarter, maybe the process you went through to come to that number? And any background you might be able to give on the whole Subro process and your assumptions would be great.

Stephen Joseph Donaghy
CEO & Director

Yes. Thanks, Bill. This is Steve. As we look at the subrogation, and we look at a go-forward platform for Universal, we assessed and discussed the conservative approach to our business on a go-forward basis. Since 2016, we've built the underpinnings of a very dedicated group of people that pursue subrogation on behalf of Universal and have successfully recovered tremendous amounts of funds on behalf of the company and our individual insureds who received their deductible back when we recover funds. In light of that, and also in light of the fact that a lot of shareholders would ask a lot of questions about the subrogation, how we retain -- how we achieve the results, we felt that it was best at this time and the fact that our financial position is so strong that we could put the type of reserve adjustment into our subrogation business to make it as sound as possible on a go-forward basis. So as we sit here across the entire company. We've never been in a position where all of our reserve development was IBNR for a go-forward basis. So we feel very comfortable as we look out at the business in the future to achieve the results that we've put in, in our estimate of return on equity, et cetera. And then if for a specific number, in 2019, we took in over $20 million in subrogation for the for all years.

William Harry Broomall

Dowling & Partners Securities, LLC

Got it. Perfect. And do you -- I know you probably look at it internally, but do you use an outside firm to also help you think through the assumptions?

Jon William Springer
President, Chief Risk Officer & Director

I'm sorry, you cut out there to think through the assumptions, did you say?

William Harry Broomall
Dowling & Partners Securities, LLC

Yes. I guess, when you think about the subro, I know you probably have an internal view, but do you -- does Universal also use an outside firm to help look at to kind of analyze the process?

Jon William Springer
President, Chief Risk Officer & Director

Yes, most definitely, the opportunity for subrogation is also reviewed by our third-party actuary every year.

William Harry Broomall
Dowling & Partners Securities, LLC

Okay, perfect. And in the change, the $40 million dollars, is that spread across? How does that work? Is it attached to different accident years? Or...

Jon William Springer
President, Chief Risk Officer & Director

Yes.

William Harry Broomall
Dowling & Partners Securities, LLC

Okay. And was there 1 maybe -- or 2 years out might have been more -- a bigger change than others?

Jon William Springer
President, Chief Risk Officer & Director

Yes, I think -- yes, I think at a high level, I can say that 2017 is actually the -- probably the driver followed closely by 2016 in terms of the years that we're driving the number that we put up.

William Harry Broomall
Dowling & Partners Securities, LLC

Great. Perfect. And then maybe switching gears a little bit. I think it's on the -- your 10-K that the direct core loss ratio was 38.9% in 2019. And I was just wondering, within your guidance, are you still -- I think it was last year, if I remember correctly, you've changed your direct loss pick to 37%. Is that still kind of what we should be thinking about going forward? Or have -- has there been any adjustment to that estimate?

Stephen Joseph Donaghy
CEO & Director

Yes, Bill, you're very observant. We have increased that loss pick to 40%, again, based on our view of the business and our intent on running the business as conservatively and well as we can. We thought 40% was the right number and gives us an ability to review that on a quarterly basis as we kind of go through our internal controls on a go-forward basis for reserves, subrogation, et cetera. So 40% of the number.

William Harry Broomall
Dowling & Partners Securities, LLC

Got it. Okay. And that's what's in the guidance. Okay. Perfect. Got it. And switching over to claims. Thank you very much for the Irma update on the claim count where we were. I was just wondering from a macro level, do you have a view on what you think claims could look like for Irma in going forward as we run up to the 3-year statute on filing new claims?

Jon William Springer
President, Chief Risk Officer & Director

Well, we forgot to bring our crystal ball in this morning, Bill, but how do we send somebody out for it? No, I think that other people have talked about this, and we've reviewed our historical events and do anticipate that there could be an increase as we approach that statute of limitations. It remains to be seen how much of a run-up that will be, but that is definitely a possibility.

William Harry Broomall
Dowling & Partners Securities, LLC

Okay. Understood. And then the -- I think earlier in my comments, you talked about the strength of your capital position and being able to absorb some of these trends, I think it was related to the subrogation. But it was there? Did you have to put any capital downstream any capital into the subs?

Frank Crawford Wilcox
CFO & Principal Accounting Officer

Yes, Bill, this is Frank Wilcox. We did fund an additional $30 million in the month of February, which under the rules of the state of Florida can be counted as of [12/31], if 2 things happen. If -- first of all, you fund that amount, and it settles and you seek approval from the OIR before you file your financial statements. So we achieved both of those, and we're able to count that as of [12/31] for UPCIC. That would not be a capital contribution for GAAP purposes until 2020. We are very strong at the holding company level. If you look at the register on only financial statements that are contained in the 10-K, you'll see that we've got plenty of capital there. Should the need arise going forward. However, we feel pretty confident that the measures that we have taken put UPCIC in a better position going forward.

William Harry Broomall
Dowling & Partners Securities, LLC

Got it. Perfect. And then...

Stephen Joseph Donaghy
CEO & Director

The only other thing that I think is important for people to also understand is relative to us compared to other people in the space who may have financed M&A deals or other transactions. We had 2% debt-to-equity on our balance sheet, and we're pretty proud of that. And that's attributable to our organic business growth model where we generate all of our business through -- naturally through our agents network, and we don't have to grow through other means such as take-outs from the state and/or M&A.

William Harry Broomall
Dowling & Partners Securities, LLC

Good point. That's a very good point. So thank you for outlining that. And then my last one, then I will get off is so you -- you had a modest amount of reinstatement premiums in the quarter. And I know in Q2 and Q3, you talked about the fact that you took some necessary action earlier in the year to help position yourself for -- if we did see additional development on Irma claims, you kind of took some preventative actions ahead of a trend we're kind of seeing now. Is -- can you just kind of update us on your thoughts on how those actions have worked in your favor? And kind of update us on -- there was a little bit of reinstatement premiums. So like how should we think about that? Is that kind of these new claims that are reopening that might not have been covered under your previous action that you did to kind of help control the cost? If you could give us any kind of thoughts around that would be helpful.

Stephen Joseph Donaghy

CEO & Director

Yes, sure. Bill, I think you're referring to the comments we've made that we did front-load the loss adjustment expenses on several claims including some flat fee deals where we did need outside counsel. So what we're seeing now is, as we're nearing the end on Hurricane Irma, we are closing claims and really, the only change is the indemnity portion, the loss adjustment portion change is minimal, if at all, so that relates to the comment that we made in our opening remarks that the vast majority of this increase will go to our Florida hurricane cat fund coverage. We were a 90% buyer in 2017. In fact, we've been at 90% buyer every year. So we will be covered at the 90% level plus the reimbursement that we get from the floor hurricane cat fund for loss adjustment expenses. So what you're seeing in terms of exposure to our open market is really just a minimal amount that's trickling through, and that's what's driving the small amount of reinstatement premium booked.

William Harry Broomall
Dowling & Partners Securities, LLC

And do you still feel comfortable with where you stand for the event going forward that the private market is in a good place that if we do, like you said, on see kind of some run up to the 3-year statute that there shouldn't -- it should be kind of captured in that private market layer? And then I'm done.

Stephen Joseph Donaghy
CEO & Director

Yes. Well, thanks for the questions, Bill. It, of course, depends on what kind of a run-up we're talking about. And we've spoken about this in previous quarters. If the situation does present itself, where we will need to retain some of the losses beyond our open market coverage, it will be a relatively small percentage of the loss as the loss grows beyond the $1.4 billion that we've booked to date.

William Harry Broomall
Dowling & Partners Securities, LLC

And just so, I keep coming back, and apologies, but just so I understand, it's -- because it's a 10%, it's really the 10%. Just so I have an understanding what would you retain? It would be the kind of the 10% debt of the indemnity, not covered by the FHCF, right? And then any LAE above kind of that 5% multiple that FHCF provides? Is that the way to think about it?

Stephen Joseph Donaghy
CEO & Director

Yes, except that in a lot of these claims that we're closing now, we've already incurred the LAE. So we would be reimbursed for [90-plus 1.05] factor on that. So we'd be reimbursed from the Florida hurricane cat fund for 94.5%. We will be responsible for that remaining 5.5% plus any small amount of LAE that may trickle through.

Operator

[Operator Instructions] I'm showing no further questions in queue at this time. I'd like to turn the call back to Mr. Donaghy for closing remarks.

Stephen Joseph Donaghy
CEO & Director

In closing, I would like to thank our associates, consumers, agents and our stakeholders for their continued support of Universal. This concludes our call.

Operator
Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.