Q4 EARNINGS: KEY THEMES TO FOLLOW

This week kicks off Q4 earnings which will stretch over the next 1-2 months. Travelers, a bellwether for the P&C group will release its figures tomorrow, and it will be followed by a frenzy of releases over following two weeks.

Q4 P&C earnings calendar (announced firms only)

Source: Company reports, SNL

MO/YR	MON	TUES	WED	THURS	FRI	SAT
JAN 2021	18	19	20	21 Travelers Truist	22	23
JAN 2021	25 Brown & Brown	26 RenRe WR Berkley	27 Axis Progressive RLI	28 AJ Gallagher Marsh & McLen. Old Republic Selective	29	30
JAN 2021	1	2 Chubb	3 Allstate Hanover Horace Mann	4 Hartford	5 Aon	6
FEB 2021	8 Everest	9 Arch Willis Towers Wat.	10 Cincinnati	11	12	13
FEB 2021	15	16 Mercury	17 Argo United Fire	18 State Auto	19	20 Berkshire
FEB 2021	22	23	24 Amerisafe	25	26	27

Despite a lack of Street Q3 EPS revisions which points to a relatively uneventful quarter for the industry, we highlight six themes that will be watched closely during this earnings season:

- Rates and underlying margins in commercial lines following Q3 reports suggested accelerating rate (in excess of trend) and pandemic-related frequency benefits. Will this gap continue to widen?
- Covid losses that remain a cliffhanger following the new wave of nationwide and local lockdowns in Q4. RenRe and Axis already pre-announced 142% and 53% reserve increases on their existing Covid charges. We also expect additional update on Covid BI litigation as it progresses through the legal system.
- Reinsurers' perspective on what appeared to be a softer-than-expected 1/1 renewal.
- Catastrophe losses, with reinsurer pre-announcements and personal carriers' monthly disclosures skewing to an above-average cat quarter.
- The InsurTechs' delivery on growth will be a major focus, along with the work they are doing to refine their mousetraps.
- Auto continues to benefit from low accident frequency, however margins are contracting as accident frequency normalizes and competition rises.

Lastly, we'd point out that the quarter was the last chance to kitchen sink bad news in a year that will likely remain notorious by most standards. Hence, we wouldn't be surprised to see some firms taking this opportunity for one-time reserve true ups. Details below.

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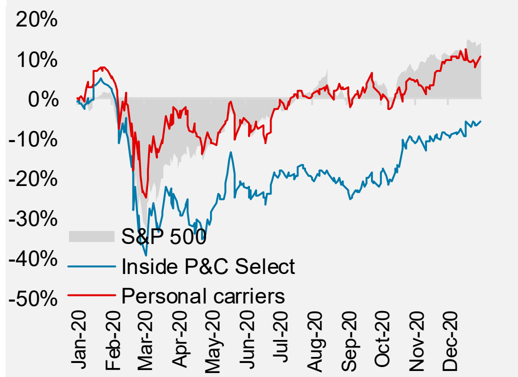
Composite	YTD px chg.	P/B
Large comm.	4.3%	1.0x
Regional	6.0%	1.5x
Specialty	(1.8)%	1.5x
Personal	(1.3)%	1.9x
Bermuda	(2.9)%	1.1x
Florida	2.1%	0.9x
Brokers	(2.7)%	-
IPC Select	1.5%	1.2x
S&P 500 Fin.	4.7%	-
S&P 500	1.1%	-

1YR Price Peformance



EPS expectations mostly unchanged since Q3

Despite the impact of the recession, 16 of the 29 Inside P&C Select firms with 3+ available analyst estimates are expected to grow earnings in Q4. Some firms are expected to report substantial earnings increases due to favorable year-on-year comparisons driven by company-specific factors.

For example, one year ago Argo took sizeable reserve true-ups. Similarly, United Fire had issues with its commercial auto book and took substantial reserve charges for prior period cats. Alleghany and Axis earnings are expected to significantly improve due to favorable cat comp. State Auto's comp was impacted by the issues within the carrier's auto line and elevated weather losses.

This reflects rate increases and the overall resiliency of P&C firms' ability to generate revenues in a down economy, as well as their ability to save on travel costs. Additionally, pandemic-related reductions in frequency (particularly in personal lines) benefited margins. All these drivers persisted during the fourth quarter.

Exhibit: Q4 consensus EPS change (YoY)

Source: FactSet

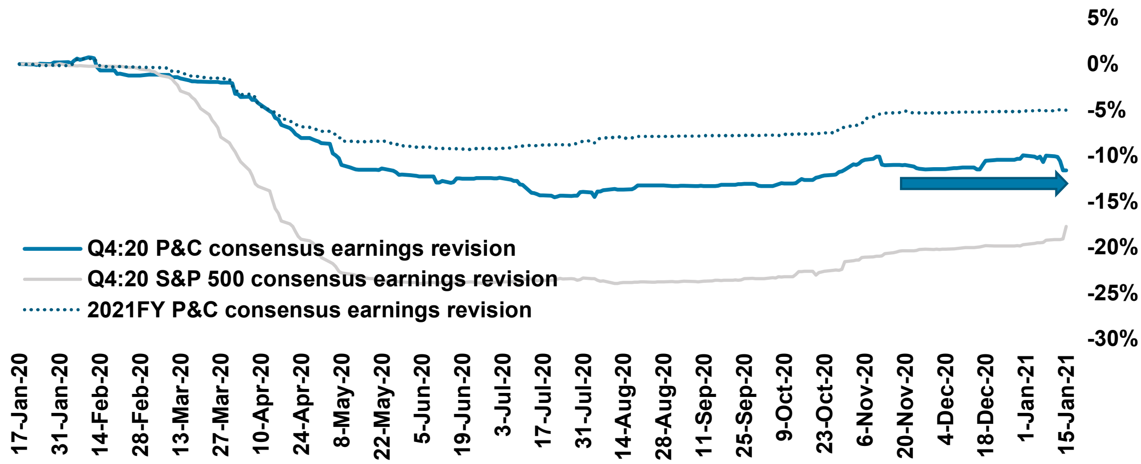
Company	Peer group	Q4-19 EPS	Q4-20E consensus	% chg	Est. #
Alleghany	Other	-$6.09	$6.50	NM	3
Argo	Bermuda	-$2.15	$0.39	NM	6
United Fire	Regionals	-$1.04	$0.13	NM	3
Axis	Bermuda	$0.05	$0.65	1202%	9
State Auto	Regionals	$0.29	$0.60	107%	3
Berkshire	Other	$2713.99	$3422.33	26%	4
Progressive	Personal	$1.31	$1.64	25%	18
Chubb	Large Comm.	$2.28	$2.83	24%	20
Horace Mann	Personal	$0.75	$0.90	19%	4
Allstate	Personal	$3.13	$3.69	18%	17
Hanover	Regionals	$2.01	$2.31	15%	5
Everest Re	Bermuda	$3.20	$3.62	13%	10
WR Berkley	Specialty	$0.74	$0.79	7%	10
Kemper	Personal	$1.45	$1.55	7%	6
RLI	Specialty	$0.63	$0.66	5%	7
CNA	Large Comm.	$0.97	$0.99	2%	4
Cincinnati	Regionals	$1.23	$1.18	-4%	7
AFG	Specialty	$2.22	$2.13	-4%	5
Travelers	Large Comm.	$3.32	$3.16	-5%	20
Hartford	Large Comm.	$1.43	$1.33	-7%	17
AIG	Large Comm.	$1.03	$0.91	-12%	17
Selective	Regionals	$1.37	$1.20	-13%	7
Donegal	Regionals	$0.42	$0.33	-22%	3
Arch	Bermuda	$0.74	$0.52	-29%	12
Heritage	Florida	$0.44	$0.25	-44%	5
Markel	Specialty	$35.66	$9.03	-75%	6
FedNat	Florida	-$0.59	-$1.48	-151%	3
United Ins	Florida	-$0.36	-$1.29	-259%	4
RenRe	Bermuda	$0.52	-$1.00	-NM	11

Reflecting a fairly uneventful quarter for the industry, street estimates for Q4 earnings remained relatively flat since Q3. Recall, in Q3 following the positive rhetoric from commercial carriers around rates outpacing loss costs (most notably Chubb and Travelers), the industry had a wave of positive EPS revisions.

Over a one-year period, consensus estimates for the Inside P&C Select aggregate earnings (Q4:20) were down over 10%, reflecting the recession and lower interest rates. This compares with a ~20% drop for the S&P 500's earnings.

Exhibit: Inside P&C Select earnings revisions (aggregate earnings)

Source: FactSet



For the industry, continued cat activity was perhaps the most notable earnings event for the quarter. Last quarter, United Insurance (UPC) disclosed an expectation to take up to $55mn in losses in Q4 from October cat events, a figure that it doubled to $100mn on December 16.

Last week, RenRe pre-announced $175mn of Q4 weather-related losses and $170mn of additional Covid losses which led to EPS downgrades for Bermuda firms.

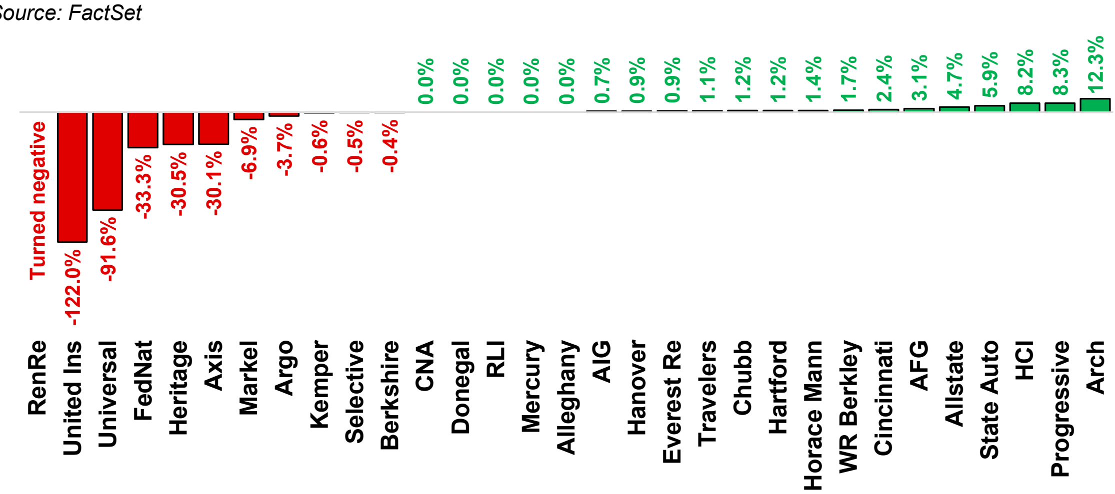
Since November 15 – which we use as the end date for the Q3 earnings season – the firms with high cat exposures saw the biggest downside revisions.

RenRe is estimated to report ~$50mn net operating losses on the back of its recent pre-announcement, versus ~$100mn in profit it was expected to report per estimates recorded on November 15. Over the same period, analysts' net operating loss estimates for UPC more than doubled, reflecting the firm's updated claims guidance.

Other firms with substantial downside EPS revisions include Universal, FedNat, Heritage, and Axis. Most other firms had their earnings revised up during the period (see chart below).

Exhibit: EPS consensus change on Q4:20 earnings since November 15, 2020

Source: FactSet



Possibility of elevated cat losses

The 2020 hurricane season had a record-breaking number of hurricanes. By mid-September, the World Meteorological Organization's naming protocol started pulling names from the Greek alphabet as its 21 human names list ran out.

This is only the second time where the Greek alphabet has been used to name storms. In 2005, the last named storm was Zeta. Last year, an additional three storms used Greek letters beyond Zeta.

Q4's biggest tropical storms – hurricanes Zeta and Delta – occurred in October, with US insured losses from each exceeding $3bn and $2bn respectively. Later, after moving erratically in Mexican Gulf and Caribbean regions, hurricane Eta mad landfall in the Florida Keys, costing ~$550mn in US insured losses.

Exhibit: Q4 most destructive US hurricanes

Source: RMS, Aon, other public sources

Storm name	Dates	US loss est.	Major impact area in the US
Hurricane Zeta	Oct 24 - Oct 29	$3bn-$5bn (RMS)	Louisiana, Alabama
Hurricane Delta	Oct 5 - Oct 10	$2bn-$3.5bn (RMS)	Louisiana
Hurricane Eta	Oct 31 - Nov 13	$550mn (Aon)	Southwest of Florida

Exhibit: Q4 major hurricanes map

Source: Mapped with Weather Information Network

To date, few carriers have pre-announced catastrophe estimates. The low number of data points send a mixed message but are skewed towards an above-average cat quarter for the industry.

RenRe released guidance for $170mn in weather losses (2% of equity). The number is lower than $237mn in Q4:19 largely from Typhoon Hagibis, but higher than $121mn in Q4:18 (Hurricane Michael and California wildfires) and $151mn in Q4:17 (California wildfires).

Axis pre-announced $70mn-80mn of weather losses (2% of equity), significantly lower than the trailing three-year Q4 average of $181mn.

UPC pre-announced $85mn-$100mn of cat losses for October and November, the second highest quarterly loss toll for the carrier, next to the $140mn it charged just last quarter.

Allstate's October weather losses amounted $345mn, substantially higher than in October 2019 and October 2018 (see table below). The personal carrier said that 85% of the losses came from hurricanes Zeta and Delta.

Exhibit: Q4 cat pre-announcements (in $mn)

Source: Company reports

Company	Est. Q4:20 cat losses	vs Q4:19	vs Q4:18	vs Q4:17	as % of NEP (assuming flat NEP YoY)	as % of equity (assuming flat equity QoQ)	Notes
RenRe	$170	-28%	40%	13%	18%	2%	Also disclosed $175mn of Covid losses
Axis	$70-80	-46%	-72%	-44%	13%	2%	Also disclosed $125mn of Covid losses
United Insurance	$85-$100 (Oct-Nov only)	+381%	+122%	+6,512%	49%	20%	Mostly from Delta, Zeta and Eta

*For all Axis and UPC relative values mid-point estimates are used

Exhibit: October cat disclosures (in $mn)

Source: Company reports

Company	Oct 2020 cat losses	vs Oct 2019	vs Oct 2018	vs Oct 2017	Notes
Allstate	$345	46%	71%	-33%	85% of losses from hurricanes Zeta and Delta
Progressive	$105	NA	-24%	557%	Derived using net cat points of 2.7%

Covid losses remain a cliffhanger

After massive Covid-related charges in both Q1 and Q2, pandemic-related losses moderated in Q3 as most countries eased lockdowns through the summer period as the virus became better understood (see table below for YTD Covid loss disclosures).

Exhibit: YTD reported Covid losses

Source: Company reports

Company	Q1 Covid losses	Q2 Covid losses	Q3 Covid losses	9M Covid losses as % of NEP	9M combined ratio
Chubb	$13mn	$1,365mn	$0mn	6.0%	98.9%
AIG GI	$272mn	$458mn	$185mn	5.2%	104.9%
Berkshire P&C Reinsurance	$225mn	$350mn	$113mn	7.8%	108.0%
Markel	$325mn	$0mn	$47mn	9.1%	101.0%
Everest	$150mn	$160mn	$125mn	6.9%	100.6%
Arch	$87mn	$173mn	$12mn	5.7%	95.1%
Axis	$235mn	$0mn	$0mn	7.2%	109.6%
Hartford (P&C)	$0mn	$213mn	$37mn	2.8%	96.2%
Alleghany	$153mn	$135mn	$51mn	7.7%	103.2%
Travelers	$86mn	$114mn	$133mn	1.6%	97.9%
CNA	$13mn	$182mn	$0mn	3.7%	103.5%
WR Berkley	$65mn	$85mn	$0mn	2.9%	96.4%
American Financial	$10mn	$105mn	$0mn	3.2%	93.2%
RenaissanceRe	$104mn	$0mn	$19mn	4.2%	97.4%
Cincinnati	$0mn	$65mn	$0mn	1.5%	101.8%
Argo	$26mn	$17mn	$17mn	4.6%	104.8%
Hanover	$13mn	$6mn	$0mn	0.6%	95.2%
RLI	$5mn	$6mn	$4mn	2.4%	93.4%

However, with Covid-related restrictions tightened again internationally and several nationwide lockdown measures implemented during Q4, there appears to be potential for further large Covid losses to incur. Since lockdown measures were significantly more severe outside the US, the large asymmetric losses are likely to come from internationally focused writers with contingency and events cancellation exposures.

During Q4, Australia and most key European economies implemented nationwide or local lockdowns. In the US, only California implemented a second lockdown ordering individuals to stay home except for essential work.

Exhibit: Countries and regions implemented second and third lockdowns

Source: Various public sources

Country	Region	Second lockdown			Third lockdown		
		Start date	End date	Length (days)	Start date	End date	Length (days)
Australia	Melbourne	8-Jul-20	27-Oct-20	111			
	Regional Victoria	6-Aug-20	16-Sep-20	41			
	South Australia	19-Nov-20	22-Nov-20	3			
	Brisbane	8-Jan-21	11-Jan-21	3			
Austria	Nationwide	3-Nov-20	30-Nov-20	27	26-Dec-20	7-Feb-21	43
Belgium	Nationwide	2-Nov-20	14-Dec-20	42			
Canada	British Columbia	7-Nov-20	8-Jan-21	62			
	Quebec	25-Dec-20	11-Jan-21	18			
	Ontario - South	26-Dec-20	23-Jan-21	28			
	Ontario - North	26-Dec-20	9-Jan-21	14			
Denmark	Nationwide	25-Dec-20	17-Jan-21	23			
France	Nationwide	30-Oct-20	14-Dec-20	45			
Germany	Nationwide	2-Nov-20	31-Jan-21	90			
Ireland	Nationwide	21-Oct-20	1-Dec-20	41	24-Dec-20	31-Jan-21	38
Italy	Nationwide	24-Dec-20	6-Jan-21	13			
Netherlands	Nationwide	15-Dec-20	9-Feb-21	56			
Portugal	Nationwide	15-Jan-21	15-Feb-21	31			
United Kingdom	England	5-Nov-20	2-Dec-20	27	5-Jan-21	16-Feb-21	42
	Scotland	26-Dec-20	1-Feb-21	37			
	Northern Ireland	27-Nov-20	11-Dec-20	14	26-Dec-20	6-Feb-21	42
	Wales	23-Oct-20	9-Nov-20	17	20-Dec-20	29-Jan-21	40
United States	California	7-Dec-20	28-Dec-20	21			

For the time being, only RenRe and Axis pre-announced additional Covid losses to be incurred in Q4 financial statements with Axis citing new information from clients, the quarter's global shelter-in-place orders and the recent court verdicts as the reasons for the reserve charge.

RenRe's pre-announcement included $175mn additional Covid charge (on top of the existing $123mn) and Axis estimates its Q4 pandemic losses at $125mn (on top of the existing $235mn).

Commercial margins in focus

Pricing discussions during the third quarter and in-between earnings suggest that the sustained market hardening remains a consensus view. However, in an environment where rate in excess of trend and frequency benefits are manifesting more broadly, and where interest rates are seemingly mean-reverting, how much further carriers can push the current market firming cycle is becoming a key question for commercial carriers' bull cases.

We expect rates and margins to become one of the most hotly discussed topics on Travelers' and Chubb's earnings calls. Recall, during Q3 calls, Chubb and Travelers management suggested accelerating rate in excess of trend, pointing to a larger underlying margin tailwind going forward. Whether this will translate into a real ROE expansion remains to be seen.

Furthermore, frequency trends will be a close focus this quarter after signs that the lower claims activity is manifesting more broadly within commercial space. While the benefits are being treated conservatively by the underwriters, particularly for long tail lines, any additional color will be worthy of attention.

TRV	*"As we look towards the second half of the year, I would expect that where we [would see claims] are going to be more on those, what I would call, lines that are impacted by the continuing economic crisis as opposed to exposure to the disease itself. So trade credit would be an example"* - ***CFO Dan Frey***

WRB	*"Clearly, there is an impact stemming from COVID-19 and the shutdown and what that has meant for frequency. It is unclear to what extent that impact is just temporary, and we will see a surge in claims and a catch-up or whether that is a permanent shift, though we expect things will ultimately return to a more normal level. For purposes of our income statement, we have not assumed anything other than we continue to carry things, by and large, at the loss ratio we used at the beginning of the year"* - ***CEO Rob Berkley***

RLI	*"We've seen fewer claims and, I guess, in some sense, frequency. It varies by product. When it comes to the way we look at booking things and stuff, we take a much more longer-term view. But certainly, in the short term, we've seen a reduction in claim counts and frequency of loss in both auto exposures, but across a lot of liability products"* - ***CEO Craig Kliethermes***

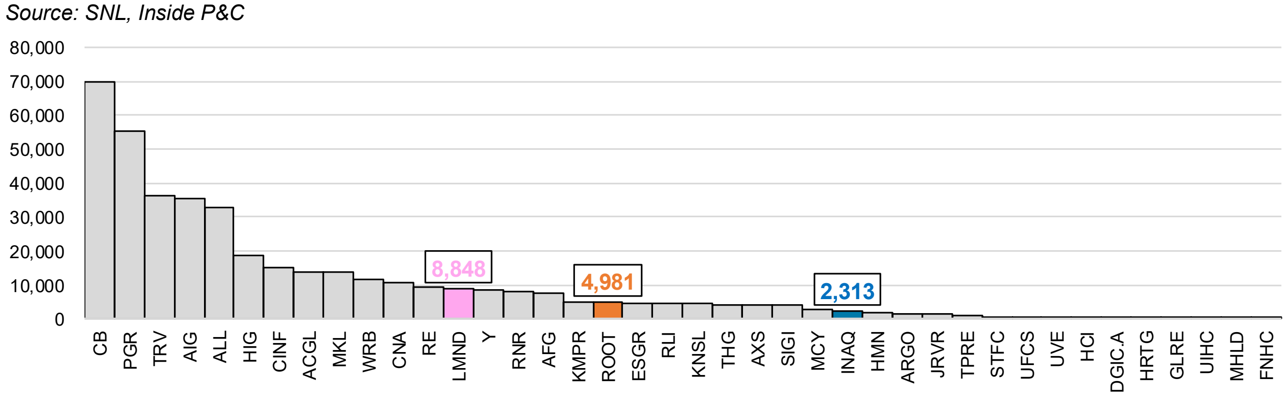
With the pandemic nearing its first anniversary, the belief that the world is passing through a secular shift in the behavior of all economic agents is becoming increasingly prevalent, which may imply some long-term shifts in claims activity within the commercial space.

InsurTech hype likely to persist as long as there's growth

Hype continues to circle the InsurTechs, especially Lemonade and Root which have recently IPO'd. More specifically, strong growth prospects have kept investors optimistic and valuations high. As a result, we expect managers at the public InsurTechs to highlight what's being done to refine their mousetraps and create "delightful" experiences. Additionally, we expect Root to highlight its data/ML/analysis/tech capabilities and how future versions of their UBI model will fix their high loss ratios.

Exhibit: IPC Select market capitalization ranked ($mn)

Source: SNL, Inside P&C



That said, while valuations remain high (both price/book & price/DWP), the InsurTech field is showing mixed results on PIF growth. On the high end, Lemonade has been able to maintain a high sequential growth rate at ~15%. On the other end one finds Root which saw 0% sequential growth in Q2:20 and -3.6% in Q3:20.

It's important to distinguish that Lemonade focuses on renters and has been both taking share and attracting new customers into its market while Root is more directly competing against major direct-to-consumer (DTC) carriers including Geico and Progressive. This competitive dynamic has led to growth reversals in states where Root has taken strong rate action as loss ratios remain unsustainable.

Exhibit: PIF - Nominal & percent growth

Source: Company reports, Inside P&C

Firm, PIF growth	Q1:19	Q2:19	Q3:19	Q4:19	Q1:20	Q2:20	Q3:20
PIF nom growth (QoQ)							
Lemonade	62,736	71,181	119,499	80,867	86,207	84,835	127,153
Root (Auto)	64,443	44,357	22,095	38,679	52,899	118	**(11,904)**
Progressive (Direct)	316,800	193,100	187,600	150,500	259,800	381,300	266,700
Geico	342,000	228,000	276,000	222,000	380,000	550,000	69,225
PIF % growth (QoQ)							
Lemonade	20.3%	19.2%	27.0%	14.4%	13.4%	11.6%	15.6%
Root (Auto)	57.7%	25.2%	10.0%	15.9%	18.8%	0.0%	**-3.6%**
Progressive (Direct)	4.5%	2.6%	2.5%	2.0%	3.3%	4.7%	3.1%
Geico	2.0%	1.3%	1.5%	1.2%	2.1%	2.9%	0.4%

Further highlighting the competitive dynamics in Auto, Metromile (which was founded nearly a decade ago), has roughly 92k policies and saw ~4% and 8% annual PIF growth in 2020 and 2019.

Auto: frequency benefits and direct channel growth to carry into Q4

Covid's impact on mobility significantly impacted the insurance business in 2020. While some insurers were adversely affected such as writers with contingency and events cancellation exposures, auto exposed names such as Progressive, Allstate, and Geico benefitted from favorable frequency trends. The favorable frequency ultimately led to wider underwriting margins that offset lower investment yields.

That said, as states continue to re-open and business regulation loosens, the frequency benefits continue to moderate. This is especially true when compared to the initially hit months that resulted in premium rebates across the peer group. Our view remains that carriers will compete away any lasting excess margins, and that the secular winners will be those with exposure to competitive direct-to-consumer (DTC) policy distribution channels like Progressive and Geico.

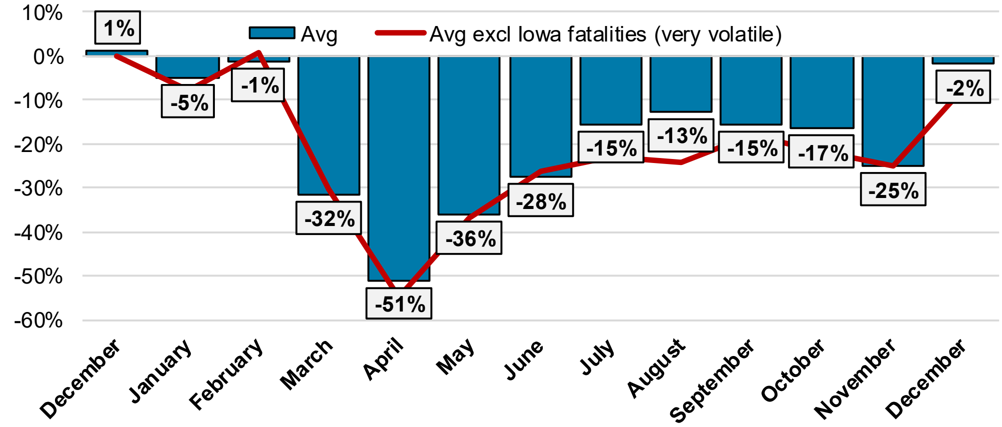
Frequency benefits … what frequency benefits?

As discussed in our recent auto frequency note, auto accident frequency appears to be trending back to pre-Covid levels as restrictions ease and businesses re-open. Combined with a historically low rate/inflation environment, carrier margins have also been trending back to pre-Covid levels. Coming in to Q4 earnings, we'd expect loss ratios to rise on a sequential basis but remain subdued on a YoY basis as a completed vaccine rollout is needed for the economy to fully re-open.

For context, shutdowns that began earlier this year in mid-March resulted in drastic declines in miles driven and thus accident frequency, benefitting carriers via lower losses. Frequency lows were seen in April at -51% when the US experienced a near-full month of lockdowns. Since then, accident frequency has trended upwards (estimated on a YoY basis) to the low single digits with December down just 2%. That said, it's possible that data-entry is a bit more lagged during the holiday seasons - but that would imply auto frequency to be even higher than reported.

Average sample state auto accident frequency

Source: State level DOT, Inside P&C

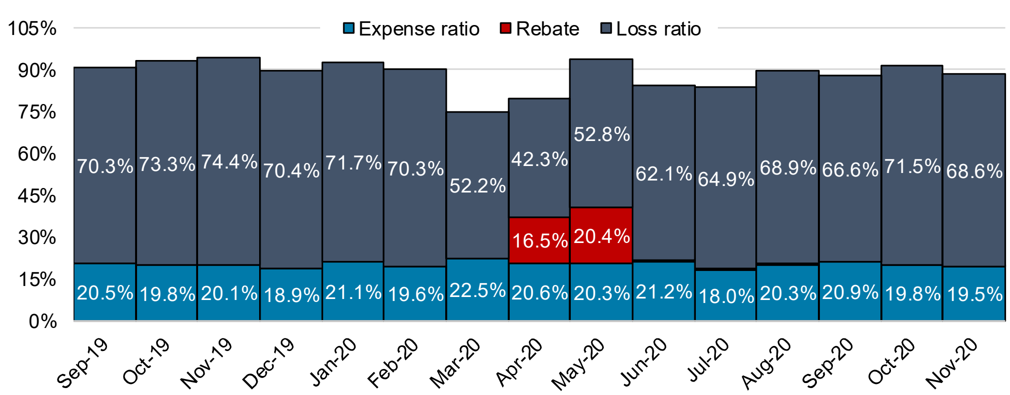


While frequency figures are useful as a leading indicator, Progressive's monthly figures also provide great insight on the PPA market. The results typically release a couple weeks into the following month, and as an industry leader in telematics, it is quick to recognize – and price for - cyclical aspects of the market.

As visible below, combined ratios have substantially risen from lows in March/April following a mix of premium rebates (which hit the expense ratio) and a rise in loss ratios following the initial shutdowns.

Exhibit: Progressive PPA combined ratio breakdown

Source: Company reports, Inside P&C



We expect Q4 calls to provide additional clarity on the frequency environment, and also guidance on when to expect a return to "normal" on the margin front.

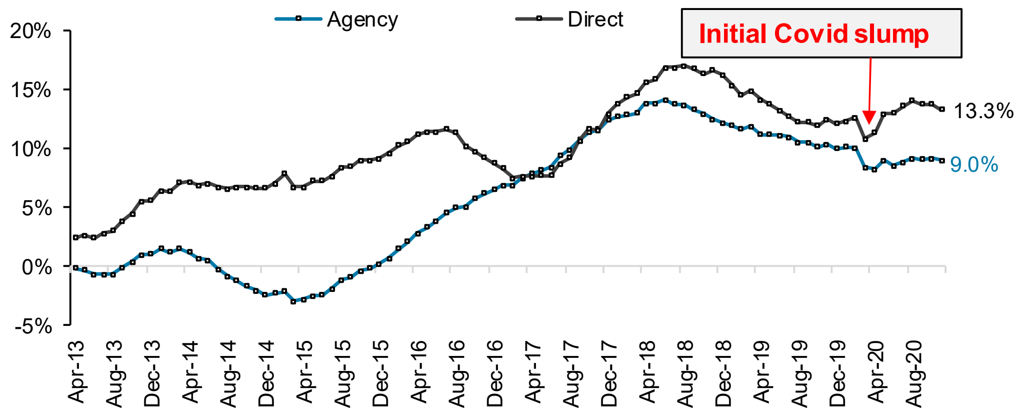
Growth trends in focus with shift to digital storefronts

In addition to commentary on the current frequency environment, we expect Q4 calls to provide insight on specific channel growth trends. As seen in most sectors, the pandemic has accelerated the adoption of digital distribution. This stands to benefit carriers with significant exposure to direct-to-consumer (DTC) policy distribution channels like Progressive, Geico, Root, Metromile, Lemonade, etc.

As an example, Progressive's direct business has shown itself to be resilient when compared to its independent agency business and more specifically peers heavily reliant on the captive agency channel.

Exhibit: Progressive monthly PPA PIF growth (YoY) by channel

Source: Company reports, Inside P&Cs



Notably, and as mentioned above, InsurTechs including Root and Metromile have seen slowdowns in PIF growth (negative for Root on a sequential basis). We expect continued commentary from their leadership on how they plan to reignite growth, especially with slowdowns occurring during a period in which they should have experience growth tailwinds, as Progressive and Geico have demonstrated.

This research report was written by Insider Publishing's Research team which includes Amit Kumar, Gianluca Casapietra, and Dan Lukpanov.

The content of this report includes opinions based on publicly disclosed financials and management commentary.