Heritage Insurance Holdings, Inc. [HRTG]
Q4 2023 Earnings Conference Call
Tuesday, March 12, 2024, 9:00 AM ET

Company Participants
Kirk Lusk, Chief Financial Officer
Ernie Garateix, Chief Executive Officer

Analysts
Maxwell Fritscher, Truist Securities
Paul Newsome, Piper Sandler

Presentation

Operator: Good morning and welcome to the Heritage Insurance Holdings Conference Call. [Operator Instructions] Please note, this event is being recorded. I would now like to turn the conference over to Kirk Lusk, Heritage Chief Financial Officer. Please go ahead.

Kirk Lusk: Good morning, and thank you for joining us today.

We invite you to visit the Investors section of our website, investors.heritagepci.com, where the earnings release and our earnings call will be archived. These materials are available for replay or review at your convenience.

Today's call may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based upon management's current expectations and subject to uncertainty and changes in circumstances. In our earnings press release and our SEC filings, we detail material risks that may cause our future results to differ from our expectations.

Our statements are as of today, and we have no obligation to update any forward-looking statements we may make. For a description of the forward-looking statements and the risks that could cause our results to differ materially from those described in the forward-looking statements, please refer to our annual report on Form 10-K, earnings release and other SEC filings.

Our comments today will also include non-GAAP financial measures. The reconciliation of, and other information regarding these measures, can be found in our press release.

With me on the call today is Ernie Garateix, our Chief Executive Officer. I will now turn the call over to Ernie.

Ernie Garateix: Thank you, Kirk, and good morning to everyone.

As we review our fourth quarter and full year 2023 results, I'm pleased to reflect on a period of achievement and strategic advancement for our company.

Our efforts over the past 2 years include deliberate actions and focused execution, culminating in improved financial outcomes and a strengthened market position.

Our financial results for the fourth quarter demonstrate the positive impact of our efforts towards tightening underwriting, working towards rate adequacy, diversifying our portfolio and managing our reinsurance costs. Our net income for Q4 2023 was $30.9 million, marking a substantial improvement from $12.5 million in the same quarter last year.

Over the last 2 years, the actions we have implemented are now being realized and reflected in our financial statements as premium from rate increases earned over the policy period. A cornerstone of our strategy has been our disciplined approach to exposure management. Our strategy to reduce the Florida personal lines book of business and obtain adequate rates significantly improve the book of business.

We have extended this strategy to all states within our 16-state platform. We intentionally reduced our multistate personal lines policies in in-force by 15% and total insured value by 6.9% to not only manage our reinsurance costs, but more effectively, but also improve the overall quality of our book of business. This strategic reduction led to only a slight decline in in-force premium from our overall personal lines business of 2.3%, a move we deem necessary to align with our long-term vision of rate adequacy and selected geographic expansion.

The commercial residential segment has seen a remarkable increase in premiums in force by 63.9% year-over-year. This growth set against a backdrop of market opportunity underscores our ability to allocate capital to products and regions with the potential for improved margins.

Our exposure management strategy has been particularly effective, resulting in a deliberate decrease in our policies in force, while in-force premiums once again hit an all-time high at $1.4 billion and up 5.6% year-over-year. These moves were made to manage our reinsurance costs efficiently and ensure that we maintain our portfolio where the premium is adequately reflective of the risk. We continue to foster our relationships with our reinsurance partners that provide critical support to our core strategy.

Looking ahead, our strategy remains clear and focused. With the successful equity raise recently completed, we are well positioned to pursue selective growth opportunities, especially in geographies where our rate adequacy meets our stringent criteria. Our commitment to operational excellence, coupled with strategic clarity, provides a solid foundation for sustained growth and value creation for our shareholders.

In conclusion, the achievements of 2023 reflect our team's dedication, strategic insight and operational discipline. As we move forward, I am confident in our ability to maintain this momentum, driven by our solid foundation and the unyielding dedication of our team across our 16-state platform.

Let me turn things over to Kirk for a review of the results in the quarter and key financial performance metrics.

Kirk Lusk: Thank you, Ernie. Good morning, everyone.

In the fourth quarter of 2023, Heritage Insurance Holdings demonstrated that the execution of our strategic decisions over the past 2 years are starting to produce the results we were anticipating. We had advised that improving the rate adequacy and overall quality of our book of business was a multiyear process, and we are pleased with the progress we have made, and we will continue to focus on these strategic initiatives going forward.

We remain committed to generating an underwriting profit in all our geographies through rate adequacy, selective underwriting, providing products appropriate for the market and diligent claims handling. The progress we have made with those objectives is demonstrated by the favorable fourth quarter results and reflects our ability to adapt in a dynamic insurance landscape.

With net income of $30.9 million or $1.15 per diluted share, we achieved a solid improvement from $12.5 million or $0.48 per diluted share in the same quarter of the previous year. The 147.5% increase in net income is primarily attributable to our premium increases nearly keeping pace with the increase in new reinsurance costs, improved investment income and an improved loss ratio.

Our gross premiums earned increased 7% to $339.6 million, while net premiums earned rose by 6.9% to $177.7 million, underscoring the effectiveness of our pricing strategy and underwriting standards. In addition, these actions led to an increase in the average premium per policy of 24.2% over the prior year quarter.

The net loss ratio for the quarter was 51%, which is an 11.4 point improvement from the prior year losses from weather were $11 million this year compared to $27.5 million in the prior year quarter, an improvement of $16.5 million. The improvement is attributable to favorable weather and also what we believe is an improved portfolio which is able to mitigate some of the weather events. The net expense ratio remained relatively stable at 33.9% and our combined ratio improved to 84.9%. These metrics are a statement to our focused underwriting discipline and effective cost management.

Our net investment income for the quarter increased by 36.1% to $6.7 million, reflecting our proactive management and investment decisions. The diversification of our investment portfolio and alignment with the yield curve had positioned us well to capitalize on market opportunities while managing risk.

Capital management remains the priority. We have continued the suspension of the quarterly dividend as we focus on reinvesting in our core operations and exploring strategic growth opportunities such as the strategic actions taken regarding the commercial portfolio in 2023.

Our approach to capital allocation is geared towards maximizing long-term returns and shareholder value. We will continue to actively manage underperforming areas of our business and seek opportunities to position the company for long-term profitability and shareholder returns.

As we move into 2024, our strategy remains centered on selective growth in geographies where rate adequacy aligns with our underwriting standards and product design. Our disciplined approach to exposure management, combined with our strategic investments in technology and process improvements, position us to navigate the evolving market dynamics and capitalizing on growth opportunities.

In closing, the fourth quarter results reflect the strategic discipline we have executed over the past few years. We have a highly dedicated and talented team throughout the organization that provides the analysis, insights and execution in their respective roles that has driven the results and position us well to continue our trajectory of profitable growth.

Thank you for your continued support. We look forward to updating you on our progress in coming quarters. We are now ready to take questions.

Questions and Answers

Operator: (Operator Instructions) And our first question will come from Paul Newsome of Piper Sandler.

Paul Newsome: Congratulations on the quarter.

Ernie Garateix: Thank you, Paul.

Kirk Lusk: Thank you, Paul

Paul Newsome: I want to ask a little bit more on the capital management question. The recent offerings suggest maybe you're a little bit light on capital coming into the year, but you also kept the dividend off. So I'm guessing you're still in a capital accumulation phase, if that's right. So that's the question.

And then in terms of select growth, I mean, does that include the potential for M&A or maybe even takeouts as well? So I'll start with there.

Kirk Lusk: Yes. Well, I mean, first, yes, the capital raise, we just looked at that as being opportunistic. And the other thing is we think that there's a lot of opportunities within our market space for other opportunities to take advantage of. So really, the capital raise was to do that as opposed to a shortage of capital position. And so that's kind of the way we're looking at that. I mean we do think that there are a number of opportunities.

Takeouts, we continually look at takeouts. And just sometimes, because, of the pricing of our product versus citizens, we don't think it would be incrementally beneficial to us, but it's one of the things we continue to look at.

Paul Newsome: Great. My other question is I wanted to ask about sort of your sense of the cat load as we go forward. Obviously, there've been a number of moving parts. And maybe you could look at this maybe not so much on a quarterly basis, but on an annual basis. What do you think is the right cat load? And how has it changed over time as we look forward?

Kirk Lusk: Yes. I mean I think the cat load has definitely changed as has the cost of reinsurance reflecting that. And from that perspective, I mean, that's why we've been diligent in our exposure management process and then also with taking the rates that we think we need to keep up with that pace.

Paul Newsome: Has the cat load gone down or up? I guess we'll start with that annual basis.

Kirk Lusk: And by cat load, let me just make sure I understand what you're referring to as cat load.

Paul Newsome: Cat load is the amount of catastrophe losses that would be normal for a year relative to premium.

Kirk: Yes. And what we do, we've expected that to increase, however, our premium has been keeping pace with that. So therefore, net-net, we've been positive from that perspective.

The other aspect of that, though, is the underwriting that we've undertaken over the last several years to improve our underlying portfolio, which we think has the ability to withstand some of the weather events and so therefore, has the tendency to mitigate some of those weather losses.

So I think cat loads in general have gone up, but with the premiums that we've taken and the underwriting actions we've taken, we think that we're outpacing that.

Paul Newsome: Okay. And I guess my last question, and I'll let somebody else ask, any thoughts on tort reform in Florida so far?

Ernie Garateix: Yes. So we continue to monitor that. We do see some positive trends in the data that we're receiving regarding litigated losses. As we've always said, we do believe that's going to take 18 to 24 months to grow with the system, but we're very optimistic that the Florida market is improving when it comes to litigated losses.

Operator: The next question comes from Maxwell Fritscher of Truist.

Maxwell Fritscher: I'm calling in for Mark Hughes. I guess going off of the Florida tort reform question, the loss ratio this quarter was very good. I was just wondering how durable is that? I guess a better way to put it is, how much of that was due to better portfolio set up versus – and better regulatory environment versus more mild weather in the quarter?

Yes. Well, and that is actually something that we've been trying to analyze and understand just because it's very difficult to compare what is the exact driver of that. I mean weather losses for us have been lower, but they've also been lower throughout the season. And I would say, particularly when we look at some of the severe convective storms that occurred throughout the year, I think a number of people had fairly large losses associated with those severe convective storms, and we did not have the same type of loss.

So I think from that standpoint, that gives us an indication that our portfolio is performing better but some of it does have to do definitely with a little bit lower weather. And I think that the -- as Ernie mentioned, the tort reform, I think, is probably having some positive impacts, but it's just so hard to quantify.

Maxwell Fritscher: Yes, that's helpful. And then on the expense ratio, pretty much the same for the full year, a little down. Can we expect this to be steady in 2024? How do you see that looking for this year?

Kirk Lusk: Yes. I think the -- looking forward, expense ratio overall, probably be fairly flat. We are doing some continuing investments in IT and productivity, which I think is going to allow us to grow in the future. But I think we do have some continuing investments in '24.

Maxwell Fritscher: Congrats on a good quarter.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to Ernie Garateix for any closing remarks.

Ernie Garateix: We want to thank everybody for joining the call today and hope everyone has a great day.

Operator: The conference has now concluded. Thank you for attending today's presentation and you may now disconnect.