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SIGI.OQ - Q1 2022 Selective Insurance Group Inc Earnings Call

EVENT DATE/TIME: MAY 05, 2022 / 2:00PM GMT

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CORPORATE PARTICIPANTS

John Joseph Marchioni *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Mark Alexander Wilcox *Selective Insurance Group, Inc. - Executive VP & CFO*

Rohan Pai *Selective Insurance Group, Inc. - Senior VP of IR & Treasurer*

CONFERENCE CALL PARTICIPANTS

Grace Helen Carter *BofA Securities, Research Division - Research Analyst*

Meyer Shields *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Scott Gregory Heleniak *RBC Capital Markets, Research Division - Assistant VP*

PRESENTATION

Operator

Good day, everyone. Welcome to Selective Insurance Group's First Quarter 2022 Earnings Call.

At this time, for opening remarks and introductions, I would like to turn the call over to Senior Vice President, Investor Relations and Treasurer, Rohan Pai. Sir, you may proceed.

Rohan Pai - *Selective Insurance Group, Inc. - Senior VP of IR & Treasurer*

Thank you, Jill, and good morning, everyone.

We're simulcasting this call on our website, selective.com. The replay is available until June 4.

We used 3 measures to discuss our results and business operations. First, we use GAAP financial measures reported in our annual, quarterly and current reports filed with the SEC. Second, we use non-GAAP operating income and non-GAAP operating return on common equity to analyze strength in operations. We believe these measures make it easier for investors to evaluate our insurance business.

Non-GAAP operating income is net income available to common stockholders, excluding the after-tax impact of net realized gains or losses on investments and unrealized gains or losses on equity securities. Non-GAAP operating return on common equity is non-GAAP operating income divided by average common stockholder's equity.

Adjusted book value per common share differs from book value per common share by the exclusion of total after-tax unrealized gains and losses on investments included in accumulated other comprehensive loss or income. And GAAP reconciliations to any referenced non-GAAP financial measures are in our supplemental investor package found on the Investors page of our website.

Third, we make statements and projections about our future performance. These are forward-looking statements under the Private Securities Litigation Reform Act of 1995. They are not guarantees of future performance and are subject to risks and uncertainties. We discuss these risks and uncertainties in detail in our annual, quarterly and current reports filed with the SEC, and we undertake no obligation to update or revise any forward-looking statements.

Now I'll turn the call over to John Marchioni, our Chairperson of the Board, President and Chief Executive Officer, who will be followed by Mark Wilcox, our EVP and Chief Financial Officer. John?

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John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Thank you, Rohan, and good morning. At the start, I want to focus on our continued strong operating results and financial position, as well as key industry trends. Mark will provide further details on the quarter's financial results, and I'll return with brief closing comments before we take questions.

In the first quarter, we generated solid financial results, notably a 12.8% annualized non-GAAP operating ROE, above our 11% target. Underwriting profitability and investment performance were both meaningful contributors to our financial results.

Net premiums written growth remained strong at 11%, driven by overall renewal pure price increases averaging 4.6%, exposure growth of approximately 3.5% on our renewal book for Commercial Lines, excellent retentions across all 3 segments and overall new business growth of 14%.

Our 93.1% combined ratio for the quarter included 2.5 points of net catastrophe losses, offset by 2.5 points of net favorable prior year casualty reserve development. The underlying combined ratio was also 93.1%.

And looking at the quarter, I want to discuss some important themes. First, I'm extremely pleased with how our team has effectively leveraged their strong market position with our best-in-class distribution partners to accelerate growth and execute our granular pricing strategy as market conditions have improved over the past 3 years.

Our growth is truly a testament to our strategic competitive advantages, which include: the unique field model, placing empowered underwriting staff in proximity to our distribution partners and customers; a franchise value distribution model defined by meaningful and close business relationships with a group of best-in-class independent agents; our ability to develop and integrate sophisticated tools for risk selection, pricing and claims management; and delivering a superior omnichannel customer experience, enhanced by digital platforms and value-added services.

We've maintained a consistent approach to managing renewal pure pricing and retention across Commercial Lines' pricing cycles, both firm and soft. Over the last decade, we have been disciplined and consistent in obtaining renewal pure price increases, along with underwriting and claims improvements, in line with or above expected loss trends.

Our approach incorporates prudent processes that integrate projected loss trend and delivers pricing guidance to our underwriters at the individual account level. As we look forward, these tools and capabilities give us confidence in our ability to effectively manage profitability in a more uncertain loss trend environment.

The industry continues to face uncertainty related to forward loss trends, a theme we have been highlighting for the past several quarters. There are 3 primary drivers of this increased uncertainty: economic inflation, social inflation and the atypical frequency and severity patterns resulting from the COVID-19 pandemic, as evidenced in the 2 most recent accident years. These factors influenced our decision to embed a higher loss trend assumption in our 2022 loss picks, as discussed last quarter.

When assessing our underlying combined ratio, it is important to note that our first quarter results generally have seasonally higher non-cat property losses. Furthermore, note that the year-over-year change is impacted by a particularly favorable first quarter of 2021, which benefited from lower pandemic-related loss frequencies. However, the current quarter also includes the impact of elevated severities in the property and commercial auto physical damage lines, which we attribute to elevated economic inflation.

We use multiple levers to help mitigate the impact of rising loss trend over time. The first is obtaining the appropriate renewal pure price increases, which we continue to do, especially in the lines of business where the impact of inflationary pressures is the greatest.

While renewal pure price in Commercial Lines was 4.8% for the quarter, we saw a favorable movement as the quarter progressed. In fact, pricing was 5.1% in both February and March, and we saw this trend continuing into April with renewal pure price of 5.2%. The lines most impacted by economic inflation, commercial auto and property, generated renewal pure price increases of 7.4% and 7.6%, respectively, during the quarter. Commercial Lines retention was very strong at 87%, a reflection of the successful execution of our granular pricing strategy.

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In addition to rate, we continue to ensure exposure bases are accurate. Through sound upfront data collection and post-policy auditing, our general liability and workers' compensation policies capture additional premium in line with actual payroll and sales growth.

On the property lines, we routinely evaluate our overall portfolio to ensure building values are reflective of current replacement cost estimates and our insurance to value, or ITV, has always been strong. We also have a formal process to update property values as policies renew.

In the quarter, we saw exposure growth of approximately 3.5% on our overall Commercial Lines portfolio. While there may be some portion of exposure that favorably impacts loss ratios, we made no explicit assumption in our loss pick for that potential benefit.

The third lever is business mix improvements, which we look to implement continuously by managing granular pricing and retention based on profitability cohorts. Over time, these efforts should yield loss ratio improvements in the book.

For the first quarter, the cohort of accounts with the lowest expected future profitability, representing about 8% of our portfolio, had renewal pure rate increases 6.6 points higher than our top-performing cohort. Retention rates for our lowest-performing cohort were 7.6 points lower than the average for our top-performing cohort, representing 22.5% of our book.

In addition, we are always seeking to enhance our claims processes and drive efficiency gains, which over time reduce losses and loss adjustment expenses.

Final thing I wanted to highlight is the impact of rapidly rising rates on the investment returns, as well as GAAP equity. During the quarter, higher interest rates drove a negative total return on our fixed income portfolio that produced $275 million after-tax in mark-to-market loss on our fixed income securities portfolio. This drove the $3.51, or 8%, reduction in book value per share for the quarter.

Simultaneously, we actively traded a portion of our portfolio to optimize higher new money investment yields, which should increase income on our fixed income security portfolio going forward. We remain pleased with our investment portfolio's positioning, principally allocated to highly rated and highly liquid securities.

Overall, I am proud of our strong execution, which positions us to meet our operating and financial targets for the year. Our consistent track record of managing rate and retention relative to expected loss trend is one of the key drivers of why 2021 marked our eighth consecutive year of delivering double-digit operating ROEs. Despite increased uncertainty in forward loss trend, we remain confident in our ability to continue delivering strong underwriting margins.

Now I'll turn the call over to Mark.

Mark Alexander Wilcox - *Selective Insurance Group, Inc. - Executive VP & CFO*

Thank you, John, and good morning. I'll review our consolidated results, discuss our segment operating performance, our capital position and our updated 2022 guidance.

We reported net income available to common stockholders per diluted share of $0.89 and non-GAAP operating EPS of $1.41. Underwriting results and investment performance were both meaningful contributors to our strong growth. The results translated to an annualized non-GAAP operating ROE of 12.8%, which is above our 11% target.

Turning to our consolidated underwriting results. We reported 11% growth in net premiums written, driven by strong growth in our Commercial Lines and E&S segments. We reported a consolidated combined ratio of 93.1%. Included in the combined ratio were $21 million of net catastrophe losses, or 2.5 points, and $20 million of net favorable prior year casualty reserve development, also 2.5 points.

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On an underlying basis, or excluding catastrophes and prior year casualty reserve development, the combined ratio was 93.1%. This underlying combined ratio was up 3.1 points from the year ago period and above our 91% guidance for the full year, with the variance to both relating primarily to high non-cat property losses.

As John mentioned, there are a couple of drivers here. First, in comparison to the year ago period, non-cat property losses were 2.6 percentage points higher. As a reminder, the year-ago period benefited from lower frequency, principally driven by the pandemic. In addition, first quarter non-cat property losses have historically been about 1.1 points seasonally higher than the full year, and this is built into our quarterly combined ratio expectations.

After factoring in the seasonality, our first quarter non-cat property losses came in about 1.1 points higher than we would have expected. This was principally driven by higher severities in our commercial auto physical damage line, which were impacted by inflationary pressures from new and used commercial auto prices, parts shortages and high labor costs.

We are closely monitoring the impact of inflationary trends on our book, and we expect these trends will have some negative pressure on underlying margins this year, principally for short-tail lines, which is reflected in our updated full year guidance.

As John mentioned, we've been increasing renewal pure prices to reflect this trend and also expect business mix shifts and claims process improvements to help mitigate the impact of inflationary pressures.

Moving to expenses. Our expense ratio was 32.1% for the first quarter, which was in line with the prior year period. The expense ratio is below our full year run rate expectations of 32.5% due to the timing of some travel, entertainment, advertising, bad debt, foundation and other overhead expenses, which we expect to come through in the coming quarters.

We remain focused on lowering expense ratio through a range of initiatives while ensuring we are investing appropriately to support our long-term strategic objectives. Corporate expenses, which are principally comprised of holding company costs and long-term stock compensation totaled $11 million in the quarter, with the year-over-year increase related to relatively strong share price performance.

Turning to our segments. Standard Commercial Lines net premiums written increased 11%, driven by renewal pure price increases averaging 4.8%, excellent retention of 87%, exposure growth of approximately 3.5% and new business growth of 12%. The Commercial Lines combined ratio was a profitable 93.6% and included 2.3 points of net catastrophe losses and 3 points of net favorable prior year casualty reserve development.

The favorable prior year casualty reserve development was driven by $10 million for workers' compensation, $5 million for general liability and $5 million for bonds for accident years 2019 and prior.

The Commercial Lines underlying combined ratio was 94.3%. This was 3.7 percentage points higher than the 90.6% for the prior year period, with the increase principally coming from 3.3 points of high non-cat property losses and driven by commercial auto physical damage severities, as I mentioned earlier.

In our Personal line segment, net premiums written were flat relative to the prior year period. Renewal pure price increases averaged 0.6%, retention was slightly up relative to a year ago at 84% and new business was down 2%. The combined ratio was 91% and included 6 points of net catastrophe losses. The underlying combined ratio of 85% was 3 points higher than the prior year period, driven by 3.9 points of higher non-cat property losses, principally driven by higher frequencies and severities in the personal auto physical damage line.

In our E&S segment, net premiums written grew 29% relative to a year ago. Renewal pure price increases averaged 7.7%. Retention remained strong and new business was up 25%. The Argo renewal rights transaction that we entered into late last year was not a meaningful factor in premium growth.

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The combined ratio for this segment was an extremely profitable 91.1% in the quarter and included 1.7 points of net catastrophe losses. The underlying combined ratio of 89.4% was 4.6 points accrued from 94% in the prior year period, driven mainly by 2.7 points of improved non-cat property losses and to a lesser extent, improved casualty margins and a lower expense ratio.

Moving to investments. Our investment portfolio remains well positioned. As of quarter end, 90% of our portfolio was invested in fixed income and short-term investments, with an average credit rating of A+ and an effective duration of 4.1 years, offering a high degree of liquidity.

Risk assets, which include a high-yield allocation contained within fixed income, public equities and alternative investments represented 11.8% of our investment portfolio.

For the quarter, after-tax net investment income of $58.5 million was up 4% from the year ago period. Alternative investments, which are reported on a 1 quarter lag, contributed $15.1 million of after-tax gains.

The after-tax yield on the total portfolio was 3% for the quarter, which translated to 8.7 points of annualized non-GAAP operating ROE contribution. The after-tax yield on the fixed income securities portfolio was 2% -- 2.6% in the first quarter, which is up relative to the prior 2 quarters.

We were active during the quarter trading a portion of our fixed income portfolio to optimize risk-adjusted investment yields in a rapidly rising interest rate environment. We put approximately $920 million to work in new fixed income securities during the quarter, with $436 million coming from active sales and the remaining cash flow coming from maturities, operating cash flow and deploying available cash and short-term investments.

These purchases had an average credit rating of AA- and a duration of 5.3 years. The average after-tax new money yield on these purchases was up meaningfully to 2.6% from 2.1% last quarter and 1.7% in the comparative quarter. This purchase activity, combined with higher resets on our floating rate securities and the sale of lower-yielding securities, increased the pretax book yield of our fixed income portfolio by approximately 19 basis points in the quarter.

Looking ahead, we expect to generate about $1 billion of investable cash flow during the remainder of 2022 from maturities, coupons and operating cash flow that will be invested most likely at higher reinvestment rates.

We will continue to be judicious in terms of trading the portfolio as we manage the impact of crystallizing losses versus building book yield. In addition, securities with floating rate characteristics accounted for 14% of our fixed income portfolio at March 31. And as these securities are currently resetting at high benchmark rates, they will also help improve our book yield. As a reminder, with our 3x investment leverage, a 100 basis point increase in pretax investment yield translates to approximately 2.4 points of ROE.

While the higher interest rate environment was a tailwind from reinvestment rates, it did negatively impact total return on book value per share. The total return on the portfolio was negative 3.5%. And significantly higher benchmark interest rates and slightly wider credit spreads resulted in a meaningful reversal of our net unrealized gain position.

We reported $245 million of after-tax net unrealized investment losses in stockholders' equity during the quarter. In addition, we reported $32 million of after-tax net realized and unrealized losses and net income driven by $9 million of after-tax realized losses as well as $21 million in after-tax credit and intent-to-sell impairments. The impairments were largely driven by higher benchmark interest rates. Despite recording impairment charges, we have not experienced a deterioration of the overall credit quality of our portfolio, which remains very, very strong. We have no direct exposure to Russia or Ukraine within our investment portfolio.

Turning to capital. Our capital position remains extremely strong, with $2.8 billion of GAAP equity as of March 31. Book value per share declined 7.6% during the quarter, with our strong earnings more than offset by an increase in net unrealized losses. Adjusted book value per share increased 1.3% in the quarter and is up 13.1% over the last 1-year period.

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Our financial position remains extremely strong. Our holding company has $518 million of cash and investments, which is above our longer-term target. Our net premiums written to surplus ratio of 1.36x is at the low end of our target range of 1.35 to 1.55x. Our debt-to-capital ratio of 15.4% is also very conservative.

During the first quarter, we repurchased 1,000 shares of our common stock at an average price of $75.49 per share for a total of $75,500. We did not repurchase any shares subsequent to the quarter end. We have $96.5 million of remaining capacity under our share repurchase program, which we plan to use opportunistically.

I'll conclude with an update on our guidance for 2022. A GAAP combined ratio, excluding catastrophe losses, of 91%, inclusive of net favorable casualty reserve development from the first quarter. Our guidance assumes no additional prior accident year casualty reserve development. Our catastrophe loss assumption remains 4 points on the combined ratio.

We are now projecting after-tax net investment income of $205 million, up $5 million from our prior guidance of $200 million, inclusive of $15 million in after-tax gains from our alternative investments, which is down from our prior guidance of $20 million. The net impact is on nonalternative after-tax net investment income expectations of $10 million.

Also recall, we report alternative investment income on a 1 quarter lag, and we expect the poor first quarter capital market returns to result in net losses from our alternatives allocation in our second quarter results.

An overall effective tax rate of approximately 20.5%, which includes an effective tax rate of 19.5% for net investment income and 21% for all other items, and weighted average shares of $61 million on a diluted basis, which does not reflect any share repurchases we may make under our share repurchase authorization.

Overall, a strong start to the year in terms of growth and profitability. With that, I'll turn the call back over to John.

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Thanks, Mark. We continue to execute our plans to generate growth and profitability that significantly outperform the Commercial Lines industry results over time. Our strong capital position allows us to evaluate the most efficient forms of capital deployment to support our initiatives to enhance our market position and generate attractive shareholder returns.

Our Commercial Lines geographic expansion plans continue to progress. We are on track to open the states of Alabama, Idaho and Vermont this year, with others planned for subsequent years.

Geographic expansion is an attractive long-term growth opportunity. We opened the Southwestern states of Arizona, Colorado, Utah and New Mexico in late 2017 and early 2018. These 3 states, in addition to our expansion into New Hampshire, generated $145 million of direct premiums written in 2021, up 42% year-over-year. The business mix is similar to our existing portfolio, and profitability remains in line with our expectations.

We continue to migrate our personal lines business towards the mass affluent market, where our strong coverage and service capabilities provide us a competitive advantage. In the quarter, new business in our target market was up 7%, and total premium in that market was up 11%. As the year progresses, we expect to achieve increased rate levels on a written basis to address rising loss severities.

Our E&S business has been a particularly strong contributor to our financial results over the past 2 years. We target smaller account and lower hazard risks with a casualty focus, reflecting the characteristics of our Commercial Lines book. We invested in and have implemented a new automation platform for general liability, property and package business. This technology investment should increase our capacity to grow and improve our underwriting controls, agency integration options and process efficiency.

As we look at the balance of 2022, we are confident we can successfully navigate an uncertain economic environment with a consistent underwriting discipline that has marked our last decade, generating strong profitability and growth.

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With that, we will open the call up for questions. Thank you. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Grace Carter with Bank of America.

Grace Helen Carter - *BofA Securities, Research Division - Research Analyst*

Thinking about, I guess, the underlying loss ratio in Commercial Lines through the quarter. I know that you talked about some seasonality in non-cat property losses. I guess I was wondering if that was -- if the losses, in excess of your usual expectations, were solely driven by severity or if there was any sort of outsized kind of more volatile large property losses in there? Just kind of trying to figure out any read-through from the quarter's results to how the rest of the year might play out.

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Yes, Grace. Thank you for the question. So first point I would make is the non-cat property losses that we saw were probably more of an auto physical damage-driven item than they were a property-driven item, either commercial or personal property. So the volatility that others have pointed to with regards to property losses, in particular, we certainly see. But in this quarter, I don't really see anything outstanding relative to the property of the pure property lines, be it commercial property, home or BOP.

With regard to auto physical damage, that really is all severity. And I think that's an important point for us to really focus on. That drove the result in the quarter. We do expect and we would expect, as I made the comment in my prepared remarks that, that's probably driven by economic inflation. And everybody is in a similar position. I think some companies might have larger or smaller commercial auto books, but that's a purely severity-driven increase that we saw in the quarter.

And it's actually -- we assume those trends will continue through the balance of the year, and that is embedded in our full year combined ratio guidance. So if you were to look at our combined ratio guidance, we don't anticipate any additional -- we never anticipate any additional prior year development.

There's about a 70 basis point impact from the full year earn-through of the higher severities that we saw in auto physical damage. So our assumption is they're economic inflation-driven and our assumption is that they'll continue through the balance of the year. But you always have to put that in context of what it means in terms of the size of the portfolio.

So auto physical damage for us, when you -- if you combine commercial and personal, there's less than -- just under 10% of our total premium. So that's where we've seen some of the higher-than-expected inflationary impacts. It's a relatively small premium base. And that premium base is pretty similar to your distribution of losS dollars as well, and that's why the impact on the full year guidance is about 70 basis points higher than it would have otherwise been.

Grace Helen Carter - *BofA Securities, Research Division - Research Analyst*

Okay. And I guess switching to kind of more the casualty side of things. How -- I mean, as we've seen courts reopen and starting to process some of the backlog of cases in the past few years, have loss trends on the long tail side of things kind of trended in line with where you thought they would be relative to historical social inflation just as all of these claims are being processed?

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John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Yes. So what I would say is, yes, they have, but I do want to recall the point that we made at the end of 2021. We did embed a higher loss trend assumption in our casualty loss picks for 2022. And then we increased our overall loss trend from 4% to 5%. There's a little bit of variation from line to line. And at the time, we pointed to social inflation being one of those factors.

So -- but I would say so far, we are -- the trends are in line with expectations. I will say, we continue to see a little bit of better-than-expected frequencies on a few of the casualty lines, not all, but a few of the casualty lines relative to pre-pandemic levels.

And from an economic inflation perspective, you actually saw medical inflation tick down in the most recent print this year compared to where it was last year. So we haven't updated our trend assumptions, but there are certainly some favorable items in there, along with the unfavorable item we just talked about relative to auto physical damage.

Operator

Our next question is from Scott Heleniak with RBC Capital Markets.

Scott Gregory Heleniak - *RBC Capital Markets, Research Division - Assistant VP*

Just wanted to ask first on the rate trends that you're seeing in Commercial Lines and Excess and Surplus. You mentioned the Commercial Lines to get a little bit better as the quarter progressed. In E&S, they were up a little bit, too, sequentially. That's not what we're seeing from others. The others, peers, the trends are weakening. And I'm just curious if you can talk about the -- would you attribute that to any specific areas? And do you expect that to continue over the next few quarters?

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Yes. Thanks for the question. I'm going to hit E&S first, and I'll come back and hit Commercial Lines.

E&S was strong in the quarter at 7.7%, and that was consistent across property and casualty. And I think that trends pretty well with what we saw at least in the latter half of last year. Although it did tick up from about -- I guess, from about 6% in Q4 in E&S. So the premium growth remains strong, and we think there's an opportunity to continue to generate some favorable rate there. So I think we feel good about the outlook for that line.

On Commercial Lines, I'm glad you picked up on the point because we continue to see a little bit of sequential improvement in the quarter. And then we also gave you the April number at 5.2%. We didn't put the January number in there. You could solve for it. January is a bigger premium month, but January was 4.5%. So from January to April, it's about a 70 basis point pickup in renewal pure pricing.

And I think it really ties into our earlier commentary relative to where the loss trend move is happening, and it is on the shorter tail lines. And that's where we're focusing. So as we go forward, we think there's an opportunity and a need to raise rates on those shorter tail lines to address some of the economic inflation that everybody is fighting here. But again, this is all in the context of really strong margins and very consistent margins and continued strong operating ROEs for Selective.

Scott Gregory Heleniak - *RBC Capital Markets, Research Division - Assistant VP*

Yes. That makes sense. It sounds like it's more commercial auto and property-driven than compared to the other kind of liability lines and based on what you're saying.

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And wanted to ask, too, on commercial auto. You mentioned the severity, which certainly, that's pretty evident out there. Average claims sizes and inflation is definitely hitting how much the average claims are. But I was wondering if you could talk, too, on the commercial auto side, what you're seeing in terms of frequency, whether you feel like that is sort of back to pre-pandemic levels? Or are you still getting a benefit there, but that benefit is offset by the increased severity? Just kind of what you're seeing on that line and what you're expecting for '22 and '23?

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Yes. I think, from a commercial auto perspective, they continue to be a little bit better than pre-pandemic levels and actually probably a little bit better than expected. Personal auto is a lot closer to pre-pandemic levels at this point. So it's really just more of a move in severity from our perspective.

But frequencies are still a slight benefit on the auto physical damage side. And we continue to actually see favorable frequencies, as I mentioned, on a couple of the casualty lines, specifically in workers' comp and, to a lesser extent, auto liability and E&S liability.

Scott Gregory Heleniak - *RBC Capital Markets, Research Division - Assistant VP*

Okay. That's helpful. And then the last one I just had was on the Argo renewal rights deal. I think you mentioned early on that you expected $20 million to $40 million in premium from that. And then you mentioned this quarter, it wasn't a major contributor. Last quarter, it wasn't. Are you still expecting that to be within that range? Or you're just not picking up as much business as you thought from that?

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Yes. I think, and I know Mark made reference to this in his prepared remarks, we are not seeing the success rate that we had anticipated. Now again, that deal was structured where it's a pretty low-risk deal for us. We did pick up a fair amount of talent and some agency partnerships.

But the point that we made when that transaction was announced is that the opportunity to renew that business was going to be dependent on our comfort level from an underwriting and a pricing perspective. And what we're seeing now is our hit ratios are significantly lower than expected because we're maintaining that discipline. And again, all of this is in the context of really strong E&S growth for us.

So there's opportunities out there. It's just that, that portfolio, I think, has been more of a struggle to meet our pricing and underwriting criteria as we look to renew those accounts. So overall, I would anticipate less than expected over the first year term of that renewal rights transaction.

Scott Gregory Heleniak - *RBC Capital Markets, Research Division - Assistant VP*

Okay. Yes, figured. Just wanted to clarify on that. I appreciate that.

Operator

(Operator Instructions) We have a question from Meyer Shields with KBW.

Meyer Shields - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Assuming that my math is correct, it looks like the underlying accident year loss ratio for GL actually went up on a year-over-year basis. I guess, I wasn't expecting that because you talked about higher loss trends in shorter tail lines. So I was hoping you could talk us through what's going on there.

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John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Yes. So -- and I'll start and Mark can provide the details. But Meyer, are you talking full year compared to the first quarter? Or are you talking first quarter to first quarter? Because first quarter to first quarter, the accident year, GL is pretty much spot on. It was 88.9% last year, 89% this year, if we just back out the prior year development.

Meyer Shields - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Yes. So I was looking year-over-year, but I guess it seems to be the same trend. It's not huge, just I guess, I would expect it to...

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

We're talking 1/10 of a point on the quarter and less than 1 point on the other, 60 basis points on the full year. So I would call that flat on an accident year basis. And it's flat and really strong on an accident year basis at 89%.

Meyer Shields - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Okay. That's definitely a fair description. I guess, if I can shift gears, I know the workers comp book hasn't been huge, and I think we've talked about this in the past. But are you seeing higher wages make their way into indemnity claims yet?

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Well, I don't -- I can't give you a specific answer on that, but I think it's a fairly safe assumption that the wage growth that we're seeing coming through is assumed in our indemnity loss cost assumptions. So we view that as one of the areas where exposure is a loss ratio-neutral item. It doesn't hurt you, it doesn't benefit you on the indemnity side.

So our assumption would be if it hasn't actually happened yet, if those wages are coming through as exposure, your losses will move in tandem with it. And there's potentially a benefit on the medical side because wages, economy-wide, not talking specific to our book, but wage inflation is above medical inflation.

So there is an inherent medical loss ratio benefit and -- in our portfolio, and I think this is fairly reflective of the industry, the loss dollars, ultimate loss dollars are about 50-50, indemnity and medical.

Operator

Gentlemen, at this time, I have no further questions.

John Joseph Marchioni - *Selective Insurance Group, Inc. - CEO, President & Employee Director*

Okay. Well, thank you all for your participation, and look forward to speaking to you again soon.

Mark Alexander Wilcox - *Selective Insurance Group, Inc. - Executive VP & CFO*

Thank you.

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Operator

This does conclude today's conference call. We thank you all for participating. You may now disconnect, and have a great rest of your day.

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