Hippo Third Quarter 2021 Earnings Transcript

Corporate Participants

Assaf Wand, Chief Executive Officer

Stewart Ellis, Chief Financial Officer

Richard McCathron, President

Cliff Gallant, Investor Relations

Analyst Participants

Matt Carletti, JMP Securities

Alex Scott, Goldman Sachs

Christopher Martin, KBW

Cliff Gallant, Investor Relations

Thank you, operator. Good afternoon, everybody, and thank you for joining Hippo's third quarter 2021 earnings conference call. Earlier today, Hippo issued a shareholder letter announcing its third quarter results, which is also available at investors.hippo.com. Leading today's discussion will be Hippo's Chief Executive Officer, Assaf Wand, President Rick McCathron, and Chief Financial Officer, Stewart Ellis.

Following management's prepared remarks, we will open the call to questions. Before we began, I'd like to remind you that our discussion will contain predictions, expectations, forward looking statements, and other information about our business that is based on management's current expectations as of the date of the presentation. Forward looking statements include but are not limited to, Hippo's expectations or predictions of financial and business performance, and conditions and competitive industry outlook.

Forward looking statements are subject to risks, uncertainties and other factors that could cause our actual results to differ materially from historical results and or from our forecasts, including those set forth in Hippo's Form 8-K filed today. For more information, please refer the risks, uncertainties, and other factors discussed in Hippo's SEC filings.

Cautionary statements that we make during this call are applicable to any forward-looking statements we make wherever they appear. You should carefully consider the risks, uncertainties, and other factors discussed in Hippo's SEC filings. Do not place undue reliance on forward looking statements as Hippo is under no obligation, and expressly disclaims any responsibility for updating, altering or otherwise revising forward looking statements, whether as a result of new information, future events or otherwise, except as required by law.

Additionally, during this conference call, we will also refer to non-GAAP financial measures, such as Total Generated Premium and adjusted EBITDA. Our GAAP results and description of our non-GAAP financial measures with a full reconciliation to GAAP can be found in the third quarter 2021 shareholder letter, which has been furnished to the SEC and available on our website.

With that, I'll turn the call over to Assaf Wand, co-founder and CEO of Hippo.

Assaf Wand, Chief Executive Officer

Thank you, Cliff.

Q3 was an incredibly strong quarter for Hippo. Our results demonstrate exciting progress in the areas of our business that matter most. We delivered robust growth, improved our loss ratio, and made a number of investments which will strengthen our foundation for the future.

Total Generated Premium grew 94 % year over year. Premium retention increased to 89%. And customer satisfaction remained among the best in the industry.

We are now more convinced than ever that partnering with our customers to proactively protect their homes and prevent losses is setting a new standard for the industry and is positioning Hippo for long-term success.

Our omni-channel distribution strategy continues to deliver. In addition to strong results in our direct, independent agent, and builder channels, I'm excited to report that we launched a major new partnership with national home lender PennyMac, giving us the opportunity to offer quotes to millions of additional homeowners.

Reflecting our strong performance in Q3 and our expectations of continued momentum in Q4, we are raising our full year guidance for Total Generated Premium from the $560 to $570 million we shared last quarter, to $600 to $605 million now

We also delivered an improved loss ratio during the quarter, coming in at 128% vs. 155% a year ago. While we are pleased by the progress, we still have work to do to reach our long-term targets. In a moment, Rick will talk about how we are using our proprietary technology to learn and implement change at an accelerated pace to continue our momentum in this area.

Another advantage that we now have is a world-class insurance leadership team. In recent months, we have welcomed new leaders of our actuarial, underwriting, and risk functions, and announced the future addition of a new leader for our claims organization. This team brings many decades of experience at leading insurance companies and sees the power in the technology platform that we've built to deliver better insurance results for Hippo.

I am personally excited by the rapid operational progress we are making under these new leaders. It will take time for the changes we are making to work their way into our reported results, but early signs are positive and I am more confident than ever that we will deliver.

In an unpredictable environment impacted by pandemics, climate change, and inflation, we believe that our tech-driven operating agility allows us to act more quickly and decisively than our competitors and puts us in a better position to win in the long-term.

Thank you and I will pass it over to Stewart, our CFO, to discuss our Q3 results in more detail.

Stewart Ellis, Chief Financial Officer

Thank you Assaf.

As Assaf said, our third quarter results highlight the ongoing strong demand from customers for our products and services, our improving loss ratio, and early indications that we are seeing the benefits of operating leverage as we grow.

Total Generated Premium, or TGP, was up 94% year over year to $162m in Q3. Pro-forma for the acquisition of Spinnaker, TGP was up 51% year over year. Additions to our book of business, or "new" total generated premium were up 66% year over year to $75 million, which is an acceleration from 53% last quarter.

We continue to geographically diversify. Led by growth in Colorado and New Jersey, 63% of new Hippo homeowners premium in the quarter came from states outside of Texas and California, up from 55% last quarter. As our business grows nationally, we are continuing to develop a much more balanced portfolio of geographic exposure, which should help reduce the volatility of our loss ratio over time.

Premium retention remained strong and continued to edge upward, reaching 89% in the quarter. Our high retention rates are a driver of top line growth, and because loss frequency declines with customer age, a benefit to improving loss ratio over time.

Revenue was up 64% year over year to $21 million, driven by growth in Total Generated Premium.

As we highlighted last quarter, geographic concentration in homeowners insurance can result in higher loss ratio volatility. While our concentration in north Texas worked against us in the first half of 2021 due to historically bad weather, it benefited us in Q3.

The industry was hit hard by the devastation of Hurricane Ida this quarter, but we managed to improve our gross loss ratio to 128%, down from 155% last year.

Prior period reserves remained stable with minor favorable development.

Digging deeper into the components of loss ratio, catastrophic weather losses contributed 50 percentage points of loss ratio in Q3, versus 75 percentage points a year ago.

Our underlying attritional loss ratio was 63%, a - 5% point improvement from a year ago. Rick will talk more in a moment about the specific actions we have taken and will continue to take to bring the loss ratio down to our long-term targets.

As I mentioned earlier, we are starting to see the benefits of operating leverage as we scale, with the major components of our operating expenses growing more slowly than our Total Generated Premium.

Sales and Marketing increased 27% year over year to $22.4 million and we continue to generate more dollars of new TGP for each dollar of sales and marketing we spend. This trend is giving us increased confidence that our message is resonating with potential customers and

as a result, we expect to invest more aggressively in 2022 to build a differentiated and nationally recognized brand in home protection.

Technology and Development increased 46% year over year to $8.3 million as we continue to invest in our platform by integrating new data sources, improving our underwriting model, onboarding new partnerships, expanding into new states, and launching new products.

General & Administrative Expenses decreased 17% to $13.4 million, with the increased costs of operating as a public company being more than offset by reductions year over year in stock-based compensation.

Our net loss attributable to Hippo for the quarter was $30.9 million or $0.08 per share compared to a Net Loss of $38.6 million or $0.44 per share in the prior year quarter.

We've ended the quarter well-capitalized, with cash, cash equivalents and investments of $850 million.

Looking forward, we remain confident in our ability to execute our growth strategy and believe we will exceed the forecast we shared with you previously. As Assaf mentioned earlier, we are increasing our full year guidance for Total Generated Premium from a range of $560 to $570 million to $600-$605 million.

I'd now like to turn it over to Rick McCathron, our President, to talk more about the rapid operational progress we are making on the insurance side of our business.

Richard McCathron, President

Thank you, Stewart.

We continue to leverage our technology to improve and rapidly iterate in all aspects of our operations, from generating new business, to underwriting, to servicing customers and to handling claims. Specific to the loss ratio, we've made several enhancements to promote better results.

We are beginning to leverage our new carrier relationships as we implement our multi-carrier strategy. Ally filings have been made in 14 states and Incline have been made in Massachusetts and North Carolina. These will allow us more flexibility in matching the right price to the right customer's risk.

We incorporated 5 new data sources during the quarter and added 50 new variables to our data sets which we expect to introduce in Q4.

We have adjusted rates, up and down, including a recently approved 24% increase in California. We have also enhanced our home inspection processes.

In addition, Hippo continues to diversify its portfolio geographically. This will address some of the volatility seen in results over the past two years. Actions to restrict new business in portions of CA and TX, our two largest states, have been combined with growth in other strategic states. The states generating this diversifying growth were chosen based on the health of the marketplace and our perception of our ability to adequately price and select business in the

state. We expect this change in geographic footprint will also help to improve our attritional loss results.

There's a lot of actions being taken here, and I want to be clear that our operating model was designed for this kind of continuous improvement and quick execution. As Assaf said, we're living in an unpredictable world, and we have an operating model built to adapt.

And now, let me turn it back over to Assaf for some final words.

Assaf Wand, Chief Executive Officer

Thanks Rick. And thanks to everyone for joining Hippo's earnings call today. Our Q3 results are just beginning to prove that we have the right strategy, the right team, and resources to execute our growth strategy. We are on the path to transform this massive market. We believe Hippo is the future of home insurance. With that, we'd be happy to take your questions.

Q & A

Matt Carletti, JMP Securities

Good afternoon. I thought I'd start with a premium question. Assaf commented, in the opening commentary, as well as I found the letter, that that new premium growth has really accelerated from prior quarters. And I'm hoping you could peel back the onion there a little bit, and maybe give us some color on what you view as the real drivers of that new business growth.

Richard McCathron, President

Yeah, thanks for the question. Stuart, I'll take it and then others can join in. I'll start by saying we're excited about what we're seeing in each of our distribution channels. Net growth in the quarter was balanced across the range of ways we go to market. In Q3, we saw a particular strength in the builder and partner channels, which represented over 20% of our new Hippo homeowners premium for the first time. And given the launch of our partnership with PennyMac, we expect to see continued strength in this area of our business going forward. Geographically, we also did make progress diversifying our geographic exposure in the quarter. 63% of new Hippo homeowners premium came from outside of California and Texas. So we have states that we've been live in for a while that are starting to accelerate in growth. And that 63% was the highest ever level for us up from 55% last quarter. I also think that this doesn't relate directly to new premium, but the overall growth, we benefit from increased premium retention that remained strong and went up in the quarter to 89%. Which of course is a benefit for us because the higher our premium retention, the smaller the headwind we have to overcome from departing customers.

Assaf Wand, Chief Executive Officer

I would just add a couple of more things. There's also some, some aspects that I will put under the title ‘maturation’. The longer we are in the market, as the market matures, usually conversion improves, or the market improves. We are starting to see the value of being in a market for longer, and it's very effective for us longer partnerships. Partnerships we've been with a while, also perform better. New products that we have started tend to mature as well. I think last quarter, we announced our homeowner association and Community Association will now be live in eight states. So we're starting to see the benefit of that. Additionally, we are a technology company. And because of that, what we do is to basically constant iterations and fine tuning or funnel of data components and all kinds of components. And we are seeing all the longer we are in the market, the more we are improving, and that also improves our growth. So I think it's a combination of all of these things, and customers are better leaning into our strategy and for that.

Matt Carletti, JMP Securities

Great, thank you. And then one more if I could. The theme I think, across, not just in short tech, but more broadly, last quarter, and definitely this quarter has been elevated marketing costs, and particularly in certain performance channels and kind of lower marketing efficiency. Can you comment a little on what you've seen? And specifically, I'm wondering if you know, given that you produce a good amount of your business through some of the partnerships you just talked about Well, as you know, more traditional agent means, if that is, you know, shielding you from, you know, some of what some others might be seeing that are relying more on direct mechanisms.

Stewart Ellis, Chief Financial Officer

Yeah, Matt, this is Stewart. I think we talked a bit about this phenomenon last quarter. And I'm happy to report that we're still not seeing this effect in our business. In fact, we're seeing improved marketing efficiency over time, as we are generating more dollars of PGP for every dollar we spend on sales and marketing. I think some of the reasons that we've been less affected maybe than others have to do with our business. Home Insurance is often an event driven purchase that's centered around the actual purchase of the home. So that's one potential reason why. And then also, I think the way we have historically gone to market hasn't been as reliant on social media as a channel, as it really has not been a significant part of our go to market strategy. I also think it is it's actually quite difficult to find a homeowner's policy online in a direct way. There are not very many people out there who do that. And so I think that that also may influence the amount of money that's being spent in this channel. And so we have an advantage there, I think that that, at least for now, has been persistent. I think finally, I'll also say that now that we're reaching true nationwide scale, we are planning to launch a national brand campaign next year that we think will further reinforce our differentiated consumer experience. And our approach to partnering with our customers who want to better protect their homes, which, as you mentioned, along with our omni channel strategy, which we think has been the

right choice for us and for our customers in the beginning, should help insulate us from things like this in the future.

Matt Carletti, JMP Securities

Great, that makes a lot of sense. Thank you very much for taking my questions and best of luck.

Stewart Ellis, Chief Financial Officer

Absolutely. Thanks, Matt.

Alex Scott, Goldman Sachs

Good afternoon, thanks for taking the question. I just wanted to maybe dig into the operational changes that were referenced in the letter. Could you provide some more detail on some of those actions you're taking and maybe how the Ally and Incline partnerships are intertwined to some of those actions. And, you know, any way for us to think about, you know, how quickly that will push your loss ratio towards some of your targeted levels.

Richard McCathron, President

This is Rick. I'll happily answer that question. From an operational perspective, we've taken quite a bit of action. As Stuart mentioned earlier, our diversification outside of Texas and California have certainly taken hold. And we're doing a better job of managing our non-cat via underwriting, leveraging data and technology. As I mentioned, we've got five new data sources that we've integrated this quarter, we have 50 new data variables that we're using. Also, the multi carrier strategy that you mentioned is certainly allowing us to accelerate by having multiple underwriting companies, multiple price points, multiple underwriting guidelines, that will allow us to accelerate our rate improvement and loss ratio improvement. Certainly our tech stack also helps SAC. The fact that we have a, you know, a open architecture tech stack that enables us to integrate with multiple carriers in a quick way, will help us accelerate the rate of which we're doing that, as well. As you know, we have a capital like structure, and using Ally and Incline not only makes us more capital efficient, but also allows us to accelerate those actions. So we anticipate writing our first business on Ally and Incline in Q1. We've already filed a combination of 16 states on Ally and Incline. And we're excited to launch those and then write our first policy, as I mentioned in Q1.

Stewart Ellis, Chief Financial Officer

Alex, this is Stuart, I'd also say just more generally, you know, we talked a little bit about this last quarter, but you know, the supply chain issues with COVID and other kind of inflationary aspects of remediation and costs in the industry. I think our proprietary platform that we own

and control gives us an ability to react more quickly, generally, to changing market conditions. So whether it's rate filings, whether it's underwriting guidelines, I think we feel confident that we are in a strong position to react to whatever the market conditions are in the future. And we view that as really one of the differentiators of the technology platform.

Alex Scott, Goldman Sachs

Got it, thank you. Maybe just a quick follow up to that. I mean, when you think through some of the actions you're taking, and you mentioned that the California rate increase in the initial comments, we expect to have any impact on retention. Is there any way for me to think about the way that that would trend? Or any sort of early insights you have on that?

Richard McCathron, President

Yeah, no, Alex, good question. I think I think we're in an inflationary cycle. I think the entire industry is taking rate. It's a combination of increased frequency and severity, I think, weather changes. So I don't think this is something that's isolated to Hippo. And I think, if you look at the data, you're going to find that most incoming carriers are taking rate, and we're no different.

Alex Scott, Goldman Sachs

Got it. Just in terms of the catastrophe losses, you know, I appreciate that this year has been very active that, you know, every quarter, there's been different things that have impacted. How should we think about that level of going forward and just thinking through, you are concentrated in some areas that are more cat exposed right now. And maybe that that's sort of a more elevated normalized level, kind of eventually giving way to a more normal cat budget that you'd see in other companies with a nationwide distribution. Any way for us to think through how that'll progress and where it'll be over the near term?

Richard McCathron, President

Yeah, I think, you know, clearly, this has not been a great year for the industry generally, because of the cat that you had mentioned, and a PCS events. I think, from our perspective, sort of a normalized cat load is a very state specific situation. As we continue to diversify. Outside of places like California and Texas, you'll see a very different shift in a cat load versus and attritional load over time. I think what's important for us is that we really price each customer based on each state where we believe we will have an underwriting profit. So to us, it's staying ahead of that curve. Obviously, we have some catch up work to do, we've been doing it with all the rate filings. But we are we're certainly improving that. And I do think you're noticing that, you know, the diversification that Stuart mentioned earlier, you know, 63% are out of those high concentrated areas. And that's up from 55% last quarter. So you're certainly seeing that and over time, we want to get to loss ratios in the 60s.

Stewart Ellis, Chief Financial Officer

And, this is Stewart, even within, say for example, the state of Texas, we would also consider what we've been doing over the past couple quarters to be diversification within the state. So our concentration within Texas has historically been in the north Texas area near the Dallas Fort Worth area, which is more hail exposed. Texas is a very, very large state. And so even though we're continuing to write business in Texas, that new business that we're bringing into the portfolio is diversifying our cat exposure away from things like hail.

Alex Scott, Goldman Sachs

Thanks for the responses.

Christopher Martin, KBW

Hey, guys, congrats on the quarter. A very positive look at the total premium generated. A quick question on some of the constraints we see on the supply chain in the home builder space in those partnerships you have. Have you seen any kind of slowdown in those channels in the recent quarters? And how should we think about kind of, as you're splitting up your diversification of distribution, that pieces with Lennar, etc, could be a little bit constrained versus what you may have thought about six months ago.

Assaf Wand, Chief Executive Officer

So as mentioned before, that builder is one of our fastest growing categories. What we've seen is yes, that overall, there are several constraints for this industry, but for our partners, what they've seen is the growth. And our attach rate is growing as our partnership with them is deepening. We launched in more states, I think we're live now in 15 states and selling unique products, which is a Ratio 5 product that many people don't know is actually a dedicated insurance product that was developed very closely with our partners. They have all kinds of features and nuances that caters to their needs. And we're starting to see more and more adoption. We're currently working with three out of the top 15 builders, and keep on deepening these partnerships with the vendor that we have. And we're very open to add more and more builders. We're very excited about this product. And there's no stopping at that. We just see tailwinds.

Christopher Martin, KBW

Great. That makes a lot of sense. And now we have the deepening of the relationships versus what the constraints may be. That's all I had for now, though. You guys answered everything else previously. Thank you.

Assaf Wand, Chief Executive Officer

Thanks, everybody. Just wanted to say thank you for coming today, and we're looking forward to talking to you in the next quarter.