Hippo Holdings Inc. NYSE:HIPO

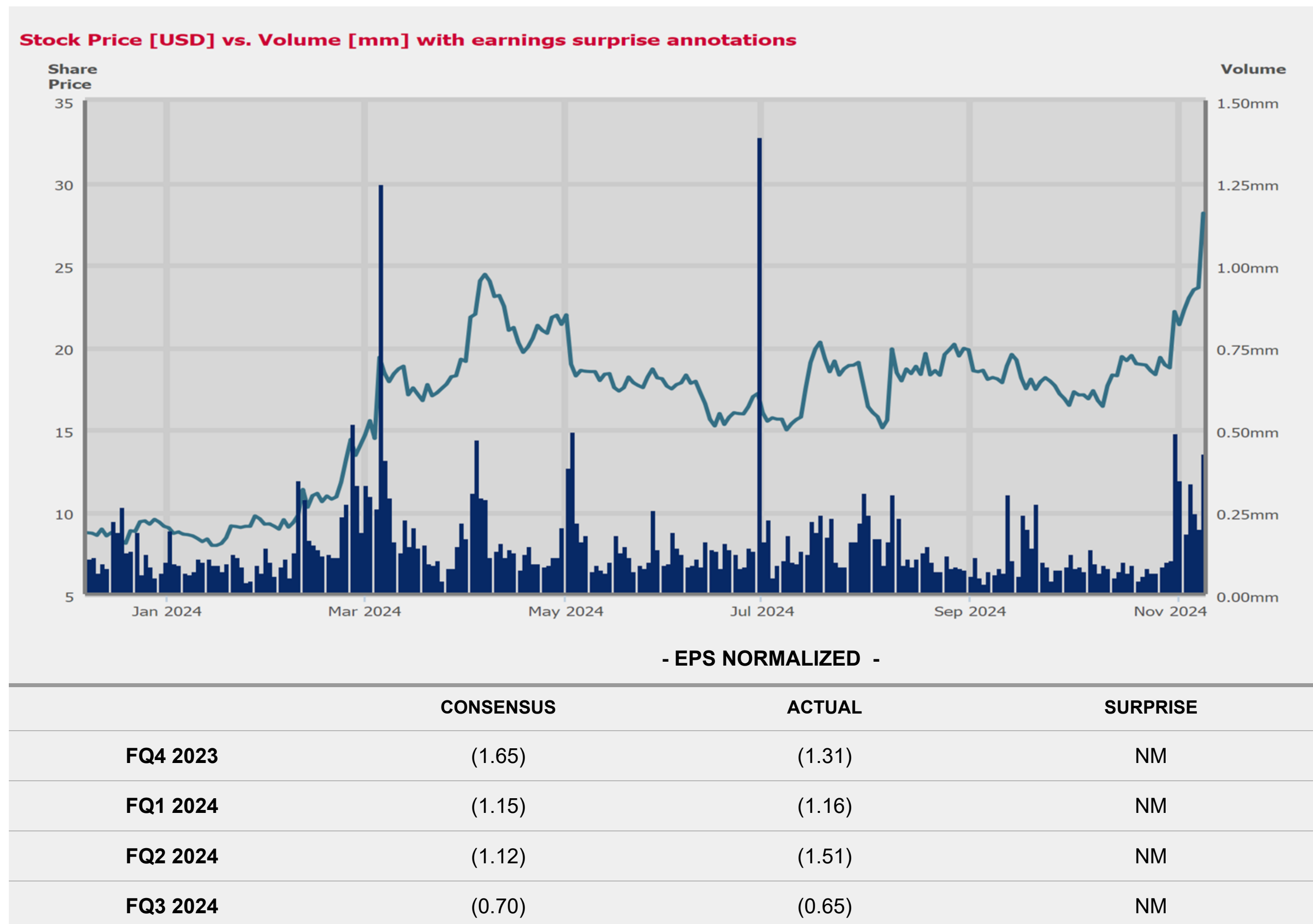
FQ3 2024 Earnings Call Transcripts

Friday, November 8, 2024 1:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2024-			-FQ4 2024-	-FY 2024-	-FY 2025-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	(0.70)	(0.65)	NM	(0.10)	(3.38)	NA
Revenue (mm)	94.08	95.50	▲1.51	100.48	369.22	NA

Currency: USD
Consensus as of Oct-15-2024 6:18 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2023	(1.65)	(1.31)	NM
FQ1 2024	(1.15)	(1.16)	NM
FQ2 2024	(1.12)	(1.51)	NM
FQ3 2024	(0.70)	(0.65)	NM

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Call Participants

EXECUTIVES

Mark Olson

Richard Lyn McCathron
President, CEO & Director

Stewart Andrew Ellis
Chief Financial & Strategy Officer and Treasurer

ANALYSTS

Thomas Patrick McJoynt-Griffith
Keefe, Bruyette, & Woods, Inc., Research Division

Yaron Joseph Kinar
Jefferies LLC, Research Division

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Presentation

Operator

Hello, and welcome to the Hippo Holdings' Third Quarter 2024 Earnings Call. My name is Maxine, and I'll be coordinating the call today. [Operator Instructions] I will now hand over to Mark Olson, Director of Communications, to begin. Mark, please go ahead when you are ready.

Mark Olson

Thank you, operator. Good morning, and thank you for joining Hippo's 2024 Third Quarter Earnings Call. Earlier today, Hippo issued a shareholder letter announcing its Q3 results, which is available at investors.hippo.com. Leading today's discussion will be Hippo President and Chief Executive Officer, Rick McCathron; and Chief Financial Officer, Stewart Ellis. Following management's prepared remarks, we will open up the call to questions.

Before we begin, we would like to remind you that our discussion will contain predictions, expectations, forward-looking statements and other information about our business that are based on management's current expectations as of the date of this presentation.

Forward-looking statements include, but are not limited to, Hippo's expectations or predictions of financial and business performance and conditions and competitive and 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 forecast, including those set forth in Hippo's Form 10-Q filed today and our Form 10-K filed earlier this year. For more information, please refer to the risks, uncertainties and other factors discussed in Hippo's SEC filings, in particular, in the section entitled Risk Factors in our Form 10-Qs and Form 10-K.

All cautionary statements are applicable to any forward-looking statements we make whenever they appear. You should carefully consider the risks and 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, offering or otherwise revising any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

During this conference call, we will refer to non-GAAP financial measures such as total generated premium and adjusted EBITDA. Our GAAP results and the description of our non-GAAP financial measures with a full reconciliation to GAAP can be found in the third quarter 2024 shareholder letter, which has been furnished to the SEC and is available on our website.

And with that, I will turn the call over to Rick McCathron, our President and CEO.

Richard Lyn McCathron
President, CEO & Director

Thank you, Mark, and good morning, everyone. For the third quarter of 2024, we continued the positive momentum we've been building over the course of the year and made a significant step forward on our path to profitability. We also strengthened the foundation for growth in our New Homes channel.

During the quarter, top-line premium and revenue continued to grow quickly, while we posted a Hippo best ever year-over-year improvement in our HHIP non-weather loss ratio. Our PCS loss results came in at expected levels despite an active hurricane season. And we delivered another quarter of improved operating leverage as the investments we've made to streamline our operations continued to pay off.

As we've discussed previously, we believe we have the best platform to help buyers of newly built homes secure cost-effective insurance quickly and easily. Beyond the benefits to consumers, Hippo's New Homes program provides homebuilders access to a scalable, embedded insurance solution that streamlines the closing process for sales teams, lenders and homebuyers by automating the evidence of insurance process.

In Q3, we expanded homebuilder access to the program in California, Florida and Texas, welcoming new builders Perry Homes and Van Daele to our roster of builder partners, with more additions to come in Q4.

By year's end, we expect to be in a position to provide access to insurance for almost 50,000 new homes annually in these states through both our Hippo program and our panel of carrier partners. After the close of the quarter, Hippo sold a majority stake in its

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independent agent platform, First Connect Insurance Services, to Centana Growth Partners for approximately $48 million, with the opportunity to earn additional proceeds of up to $12 million if First Connect achieves certain performance targets.

This transaction allows us to further increase focus on our core business while simultaneously freeing up First Connect to increase its level of investment to fulfill its potential as the premier independent agent distribution channel for carriers and MGAs. Hippo will continue to be an enthusiastic customer, carrier partner and minority shareholder in First Connect.

The proceeds from the transaction further strengthen our cash position, and we have taken this as an opportunity to repurchase and retire some of our own shares.

Over the past couple of years, we've been striking a balance between improving our efficiency and investing in our business to support future growth. The work our team has been doing is increasingly visible in our financial results, and I'm optimistic about what is to come.

Now, I'd like to turn the call over to our Chief Financial Officer, Stewart Ellis, to walk through the highlights of our Q3 2024 financial results as well as our expectations for the future.

Stewart Andrew Ellis
Chief Financial & Strategy Officer and Treasurer

Thanks, Rick, and good morning, everyone. Our Q3 results illustrate the benefits of investments we've been making over the past several years. We've delivered strong top line growth and substantial improvement in our loss ratio and operating leverage. As I walk through the key lines of our P&L, I'll explain the drivers behind our results and how the benefits of the investments we've been making are now visible in the P&L.

In Q3, TGP grew 21% year-over-year to $368 million. TGP in our Hippo Home Insurance Program segment declined 18% as a result of managing our exposure to high-CAT geographies, but this was more than offset by TGP growth in our Insurance-as-a-Service segment of 12% and 46% TGP growth in our Services segment.

Our TGP mix continued to shift towards the areas of the business that are less exposed to underwriting risk and weather volatility. The collective premium from the Services and Insurance-as-a-Service segments was 81% of our total TGP this quarter, up from 74% a year ago.

Revenue growth in Q3 again outpaced TGP growth, increasing 65% year-over-year to $95 million, up from $58 million in Q3 2023. Much like last quarter, the higher premium retention at HHIP and the volume increases in the Insurance-as-a-Service and Services segments were the primary drivers of the growth.

As we have discussed previously, our increasing confidence in both the magnitude and the predictability of our loss ratio has enabled us to retain a greater share of the premium we write on our own balance sheet. As a result of this higher premium retention, net earned premium as a percentage of gross earned premium in our HHIP business rose to 75% in Q3, up from 23% a year ago.

Like in previous quarters, Insurance-as-a-Service revenue growth was mostly driven by the premium growth from existing programs, augmented by slightly higher risk-retention with some of the programs.

In our Services segment, revenue grew more slowly than TGP due to the continued mix shift from our agency, where we earn commissions on a gross basis, to our First Connect platform, where we take a percentage of the gross commissions paid by carriers to our agency customers and recognize revenue on a net basis. We will not see this effect in future quarters because following the sale of First Connect on October 29th, our agency will be the only driver of the Services segment's financials.

Loss results in Q3 improved substantially year-over-year despite an active hurricane season. HHIP PCS accident period loss ratio came in at 18%, an improvement of 20 percentage points quarter-over-quarter and an improvement of 7 percentage points versus Q3 of last year.

Despite the significant improvement in our PCS results, the real star of the show this quarter was the improvement in our HHIP non-PCS accident period loss ratio, which improved an unprecedented 15 percentage point year-over-year to 52%. This improvement was driven by aggressive rate and underwriting actions across the portfolio as well as a favorable mix shift toward new homes, which generally experience lower non-weather losses than older homes. We achieved this improvement despite the shift at a portfolio level away from higher-CAT geographies, which, all things equal, would tend to raise the non-PCS loss ratio.

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The combination of year-over-year improvements in both weather and non-weather loss ratios drove a substantial improvement in our total HHIP accident period loss ratio, which improved by 22 percentage points to 70% from 92% in Q3 of last year. This portfolio-level improvement, combined with the improvements to our reinsurance structure, drove an even larger improvement in our HHIP net loss ratio, which came in at 84% during the quarter, an improvement of 67 percentage points versus Q3 of last year. Excluding the benefits of reserve releases in Q3 of '23, this improvement would have been 126 percentage points.

In Q3, we again delivered significant top line growth while simultaneously reducing our operating expenses both as a percentage of revenue and on an absolute dollar basis.

Relative to Q3 of last year, our GAAP sales and marketing, technology and development and general and administrative expenses collectively declined by $17 million, a year-over-year decrease of 33%. When combined with the increases in our revenue over the same period, these costs fell from 89% of revenue in Q3 of last year to 36% of revenue this quarter.

Q3 net loss came in at $8.5 million, a $45 million or 84% improvement versus Q3 of 2023. Compared to last quarter, our net loss improved by 79% or $32 million. The primary drivers of the year-over-year improvement were a 67 percentage point improvement in our HHIP net loss ratio, better operating leverage, continued growth in our businesses that are less susceptible to weather and underwriting volatility, an $8 million gain on the sale of a shell insurance carrier, and a $5 million reduction in stock-based compensation.

Our Q3 adjusted EBITDA loss came in at $7.5 million, a $31 million or 81% improvement versus Q3 of 2023. And compared to last quarter, our adjusted EBITDA loss improved by 70% or $17 million.

Q3 ending cash and investments increased quarter-over-quarter by $54 million to $545 million. This increase was driven primarily by higher collections from reinsurers, reducing the amounts outstanding that are owed to Hippo and the $8 million of proceeds from the sale of a shell insurance carrier, partially offset by the losses from operations.

And now, 2 additional updates beyond our Q3 financials. After the end of the third quarter, on October 29th, we entered into an agreement with Centana Growth Partners to sell a majority of our shares in our independent agent platform, First Connect Insurance Services. As part of the agreement, Centana invested additional capital in First Connect to support its future growth, and Hippo realized cash proceeds of approximately $48 million, with an opportunity to earn up to an additional $12 million over the next few years if First Connect achieves certain performance targets. Hippo also retains a 19.2% stake in First Connect.

This transaction allows us to further increase focus on our core business while simultaneously freeing up First Connect to use the incremental investment from Centana to increase its level of investment in its future growth.

The proceeds from this transaction have further strengthened our cash position. After the First Connect transaction closed, Hippo used $15.6 million of the proceeds to repurchase and retire 957,242 or 3.8% of our total shares outstanding. This reduction in shares outstanding is reflected in the shares outstanding we reported today on the cover of our Form 10-Q.

Turning now to our Q4 guidance. The removal of First Connect from Hippo's financials from the beginning of November will lower our expected Q4 TGP by approximately $50 million to $60 million and expected revenue by approximately $1.5 million to $1.8 million, but will have only a negligible impact on our expected net loss and adjusted EBITDA. Even with these effects and the expected impact of Hurricane Milton, we'd like to reiterate our previous Q4 guidance for revenue of $95 million to $99 million and adjusted EBITDA of positive $5 million to $6 million.
And with that, operator, I'd now like to open the floor to questions.

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Question and Answer

Operator

Our first question today comes from Yaron Kinar from Jefferies.

Yaron Joseph Kinar
Jefferies LLC, Research Division

So I want to start with the entry into California, Florida and Texas, homebuilders that will offer access to 50,000 new homes annually. Can you maybe offer us an equivalent kind of nationwide number?

Richard Lyn McCathron
President, CEO & Director

This is Rick. I would reclassify it not as an entry into California, Florida and Texas. We are already in California, Florida and Texas with our existing homebuilder partners. These are the additional homebuilder partners in those particular states.

As of now, the homebuilders that we've publicly announced in this quarter, those are states that they are heavier in and concentrated more in, but we feel very good with both the quality of expected loss ratio from these builders and the diversification we have from other builders already on our platform and those that will be joining our platform in Q4. So we feel good that we're doubling down on our homebuilder channels in markets that we feel positive in.

Yaron Joseph Kinar
Jefferies LLC, Research Division

So if there are about, what, just over 1 million homes built annually currently in the United States, how many of those can you service today?

Richard Lyn McCathron
President, CEO & Director

Yes. We have access to approximately 200,000 of the new homes with our existing partners. Again, I'll reiterate that we have an active business development cycle with various partners at various stages in that cycle. I think the number is a little bit more than 1 million. I think on average, it's somewhere between 1 million and 2 million. And we anticipate closer to 1.5 million as the addressable market in 2025.

Yaron Joseph Kinar
Jefferies LLC, Research Division

Great. And maybe too early to say given a somewhat limited history here, but do you have any data points that would offer any color on the retention rates in the homebuilders' channel as the insured homes roll off of the builders' warranties? And maybe also similarly, how the loss ratio looks as the roll off occurs?

Richard Lyn McCathron
President, CEO & Director

Yes. Certainly, it's a very high, very favorable retention rate. And there's a couple of different ways of looking at it. The way we look at it is these customers come to us more as an agency than as a particular Hippo home insurance product. So at times, we place those policies on HHIP, and at other times, we place those policies with our carrier partners. And both HHIP and our carrier partners typically offer policies that shift or transition as those homes become older into more of a traditional homeowner's policy. So we not only have a very high retention, but we have the opportunity to transition those homes from a new construction policy to a more traditional policy as those homes age.

Stewart Andrew Ellis
Chief Financial & Strategy Officer and Treasurer

Yaron, this is Stewart. On the loss ratio side, I agree it's a little bit early for us within our own portfolio to really have a longer-term view on ours specifically. But the early data that we do have suggests that the new homes perform better than older homes, both in

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PCS events and also on the non-weather losses. And that this is -- at a portfolio level for us, it is a highlight and one of the drivers of improvement to our loss ratio.

I think, as Rick said, the policies shift to more traditional homeowners' policies as the homes age. And so you'd expect that after 10, 20 years, et cetera, these things would start to look more like sort of a traditional homeowner's loss ratio. But we're excited about the results that we're seeing on the loss ratio for the earlier period of the homes' lives.

Yaron Joseph Kinar
Jefferies LLC, Research Division

Got it. And then one quick one, if I could. I understand that the First Connect stake sale would have a negligible impact on EBITDA. But I assume it's a negligible positive impact because it was loss running, right, and as it was building up?

Stewart Andrew Ellis
Chief Financial & Strategy Officer and Treasurer

That's correct. Yes. It's a small positive impact on adjusted EBITDA because it is on an operating income basis still not yet profitable. And one of the things that, that business it makes sense for them to do is to increase their investment over time. So we felt like this was a nice time to allow that business to chart its own path. Creating a marketplace to connect agents and third-party carriers is a great business, but it's not our core business, and it's at a scale where allowing it to make the choices that are right for it and its future growth and value makes all the sense in the world.

Operator

Our next question comes from Tommy McJoynt from KBW.

Thomas Patrick McJoynt-Griffith
Keefe, Bruyette, & Woods, Inc., Research Division

Did you talk about sort of the rationale for why Spinnaker sold that, that sale part of the business? Was it just a noncore unutilized piece? Or was there any other rationale there?

Richard Lyn McCathron
President, CEO & Director

Tommy, this is Rick. It is something that was dormant sort of on our shelf. So if you think about Spinnaker as a fronting carrier, Spinnaker actually has 4 different companies within its banner. So it has Spinnaker, which is the admitted A- rated carrier. It has Spinnaker Specialty, which is also rated surplus lines carrier. We had Mainsail, which is the one that we sold that was an unused asset, widely licensed. And we also have Wingsail, which is an unused asset. We had a partner that wanted access to their own carrier, and we thought it was a great way to monetize that transaction on an asset that was redundant given the fact that we also have Wingsail. So it just made sense to move it out, but there was really no other rationale behind it.

Thomas Patrick McJoynt-Griffith
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. It makes sense. And then switching over to the HHIP program. Obviously, it's been a great turnaround in that segment, in that program. With a lot of the underwriting actions that you've taken, are you looking to kind of re-grow -- sort of growing that business into 2025? What are some early thoughts when you think about the potential growth rate in that segment?

Richard Lyn McCathron
President, CEO & Director

Yes. I think, Tommy, that as we've said since really Q2 of 2023, our first priority is to remediate the historical or legacy portfolio that was in HHIP. We've made a ton of progress on that. And I think not all the progress that we have made is actually even showing in the financials. As you know, these things take effect at renewal, and then it takes an entire year after renewal to work it into the financials. So there'll still be a positive impact on that.

We still have a little bit of work to do to clarify that portfolio, but we are also writing new business in areas that we believe strongly in that don't contradict the hard work our team has done to turn it around. A lot of that is around the new builder channel. But we are accelerating our growth in that. There will still be a bit of a headwind for another quarter or 2 on the stuff that we're still getting rid of, but we are writing new business in areas we have a high likelihood of a positive expected loss ratio.

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Thomas Patrick McJoynt-Griffith
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. So we should still think of the services and IaaS growth rates into '25 as larger than the HHIP?

Richard Lyn McCathron
President, CEO & Director

That's right. We're going to give our guidance for 2025 next quarter, but IaaS, the Spinnaker platform, is doing exceptionally well, as is our agency, both in top line growth and operational efficiency and -- in the Spinnaker realm and quality of programs that it partners with. And that will be -- that will continue to be our primary driver in the short run, but we're looking forward to rebuilding the top line momentum in HHIP as well.

Thomas Patrick McJoynt-Griffith
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. And then just last one. The decision to repurchase some shares, did you feel that was a onetime sort of bullet with the proceeds from the sale of First Connect? Or should we think about buybacks being a recurring part of the story going forward?

Stewart Andrew Ellis
Chief Financial & Strategy Officer and Treasurer

Tommy, this is Stewart. As you know, the Board has previously approved a programmatic share buyback program. And after the second quarter of 2023 with the wind and hail events, we paused the purchases under that program just to get a little bit better sense of kind of the trajectory of the business and how things were going to be developing.

As we get closer to profitability, I think we'll continue to explore ways to be opportunistic when we feel like repurchasing shares would be in the best interest of our shareholders. In this case, we had an opportunity to acquire shares at a discount to market with the incremental cash from the First Connect transaction. And I think with our increasing -- our increasingly close proximity to profitability, we will continue to look for opportunities to be optimistic.

Operator

[Operator Instructions] We have no further questions. So I'll hand back over to Rick McCathron for closing remarks.

Richard Lyn McCathron
President, CEO & Director

Well, I would just like to thank everybody for joining the call. We're very excited about the progress in Q3, and look forward to sharing our continued improvements in Q4. Thank you, everyone. Have a great day.

Operator
Thank you. This does conclude today's call. Thank you for joining. You may now disconnect your lines.

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