# Third Quarter 2024
# Earnings Call Transcript

November 5, 2024

## CORPORATE PARTICIPANTS

**Christopher Uchida,** *Chief Financial Officer*

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**Jon Christianson,** *President*

## CONFERENCE CALL PARTICIPANTS

**Mark Hughes,** *Truist Securities*

**Paul Newsome,** *Piper Sandler*

**David Motemaden,** *Evercore ISI*

**Andrew Andersen,** *Jefferies*

**Meyer Shields,** *KBW*

**Pablo Singzon,** *JPMorgan*

## PRESENTATION

**Operator**

Good morning, and welcome to the Palomar Holdings Inc. Third Quarter 2024 Earnings Conference Call.

During today's presentation, all parties will be in a listen-only mode. Following the presentation, the conference line will be open for questions with instructions to follow. As a reminder, this conference call is being recorded.

I would now like to turn the call over to Mr. Chris Uchida, Chief Financial Officer. Please go ahead, sir.

**Christopher Uchida**

Thank you, Operator, and good morning, everyone. We appreciate your participation in our earnings call.

With me here today is Mac Armstrong, our Chairman and Chief Executive Officer. Additionally, Jon Christianson, our President is here to answer questions during the Q&A portion of the call.

As a reminder, a telephonic replay of call will be available on the Investor Relations section of our website through 11:59 P.M. Eastern Time on November 12, 2024.



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Before we begin, let me remind everyone that this call may contain certain statements that constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These include remarks about Management's future expectations, beliefs, estimates, plans and prospects. Such statements are subject to a variety of risks, uncertainties and other factors that could cause actual results to differ materially from those indicated or implied by such statements. Such risks and other factors are set forth in our quarterly report on Form 10-Q filed with the Securities and Exchange Commission. We do not undertake any duty to update such forward-looking statements.

Additionally, during today's call, we will discuss certain non-GAAP measures, which we believe are useful in evaluating our performance. The presentation of this additional information should not be considered in isolation or as a substitute for results prepared in accordance with U.S. GAAP. A reconciliation of these non-GAAP measures to the most comparable GAAP measure can be found in our earnings release.

At this point, I'll turn the call over to Mac.

**Mac Armstrong**

Thank you, Chris, and good morning.

I'm very pleased with our third quarter results as they clearly demonstrate our successful efforts to deliver consistent earnings and returns. In a quarter that experienced a heightened level of cat activity, we delivered 39% adjusted net income growth, a 77% adjusted combined ratio and a 21% adjusted ROE. Our results further validate the concerted efforts that we have undertaken to diversify the business, reduce the volatilities in our earnings base and profitably growth.

This quarter's strong financial results also reflect the sustained execution of our 2024 strategic imperatives, grow where we want, manage dislocation and diversification, provide consistent earnings and scale the Organization. Our first imperative is centered on achieving strong premium growth across the portfolio with an emphasis on those segments that generate the strongest risk adjusted returns. For the third quarter, we delivered topline growth of 32% driven by solid execution across our book of business, highlighted by continued strong growth from our earthquake and casualty books of business, as well as significant growth in our young crop book. It's worth noting that the same store sales growth was 38%.

Our second strategic mandate requires navigating and capitalizing on dislocation in the market while further diversifying our business. During the quarter, we raised $160 million through a primary equity issuance to help further diversify our specialty insurance franchise and strengthen our position in existing classes of business where we see both opportunity and dislocation. We earmarked a portion of the proceeds to finance our acquisition of surety insurer, First Indemnity of American Insurance Company, or FIA. Proceeds also strengthened the balance sheet to support our rapidly growing crop business. Lastly, we are using the remaining portion of the capital for organic growth and targeted increase in risk participation in lines like earthquake.

Our third imperative is a steadfast commitment to delivering consistent earnings. As I mentioned, we achieved adjusted net income growth of 39% with an adjusted return on equity of 21% despite elevated catastrophe losses in the quarter. Steps taken to reduce the volatility in our portfolio is best exemplified by Palomar being a consensus for the eighth straight quarter, even in a period of atypical hurricane activity and the associated catastrophe losses incurred. Separately, our crop business and the pending entry into the surety business will lead to earnings from products uncorrelated with the traditional P&C cycle.

The fourth imperative is scaling the Organization and making the requisite investments to accomplish our Palomar 2X objectives. This effort starts with an investment in people and I'm proud to say that we've continued to recruit industry leading talent to join Palomar this quarter. Notable additions to our team include



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David Sapia, Head of E&S Casualty, Benson Latham, Head of Crop, and Althea Garvey, Chief Claims Officer.

In addition to our entrepreneurial and innovative culture, a key factor in attracting experienced industry veterans is the growth scale and reputational heft that Palomar is achieving, highlighted by AM Best upgrading our financial strength rating to an A from an A minus. I'm humbled and thrilled by the talent that we've been able to recruit in 2024.

I would now like to review the performance and market conditions of our five product categories. Firstly, our core earthquake franchise grew gross written premium 19%. Our residential earthquake business continued to generate strong new business growth and high policy retention. Additionally, our residential earthquake E&S book saw 74% growth year-over-year as personal lines business continues to flow into the non-emitted market in California. It's worth noting that our E&S rates are considerably higher on a like-for-like basis. In peak zones like West Los Angeles they are more than 50% higher.

We feel that growth in residential earthquake business will sustain given the continued dislocation in the California homeowner's market, combined with the CEA continuing to reduce their exposure and coverages. This can be seen by the CEA's decision not to renew $750 million of expiring excess of loss reinsurance on October 1. As the CEA continues to reduce coverage and claims paying capacity, Palomar will remain the primary option in the California residential earthquake market.

Our commercial earthquake business saw solid growth in the quarter. In the third quarter, commercial rates did plateau as the average account renewed flat on a risk-adjusted basis. Terms and conditions continue to improve, and the underlying profitability metrics such as average annual loss to premium and 250-year probable max loss to premium are at the best levels in our company history.

Current market conditions in earthquake confirms our strategy of writing both commercial and residential earthquake business to navigate any market cycle. The 10% inflation guard in our residential policies provides a meaningful cushion above inflationary levels and therefore enhances our margins in a flat-to-down reinsurance market. Our commercial book allows us to generate meaningful risk increases when market conditions permit or demand. Ultimately, the performance of our earthquake franchise remains strong, and we are confident that earthquake premiums will grow in the high teens to 20% range for the full year 2024.

Our Inland Marine and Other Property category, which consists of seven property products: Builder's Risk, Excess National Property, All Risk, Motor Truck Cargo Contractors Equipment, Hawaii Hurricane, and Residential Flood grew 22% year-over-year. As a reminder, this is a product category where we are investing in growth and reducing exposure as we continuously measure risk-adjusted returns line by line.

During the quarter, we saw strong performance from our Excess National Property and Hawaii Hurricane lines of business, whereas our All Risk book continued to contract, a trend that we expect in 2025 as well. The All Risk book was the primary driver of catastrophe losses in the quarter and is expected to be the same for Hurricane Milton. On the heels of this robust and active hurricane season, we continue to assess our options to reduce the potential losses from continental U.S. windstorms.

Builder's Risk, our largest Inland Marine product and our Excess National Property line, which typically writes business in non-catastrophe-exposed regions, continued to experience robust premium and submission growth as well as higher regionally focused underwriters. During the quarter, we implemented a new facultative reinsurance treaty for the Excess National Property team that allows them to write large limits while keeping a small net line size and do so in an automated fashion. This new reinsurance agreement will enhance our servicing and quoting capabilities and ultimately production.



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Hawaii Hurricane premiums grew 74% in the third quarter as the 23% rate increase approved last quarter is now flowing through our renewals. We have rolled over 90% of our enforce Palomar Specialty Insurance Company policies onto our Laulima Reciprocal. This effort meaningfully reduces Palomar's exposure to a large loss from a hurricane in Hawaii and enhances our fee income base.

From a pricing standpoint, rate activity varies widely by region and product. For instance, our Builder's Risk rate increases nationwide were flat, but in Texas we're seeing increases of 5% to 10%. Hawaii Hurricane, as previously mentioned, is up 23%. In the circumstance of flood, pricing was flat in California, although we are waiting on a rate increase approval. But in states impacted by Hurricane Helene, we are renewing policies up 10%.

All Risk policies were down 6.4% in the quarter, but that level of decline is likely to accelerate, at least in Florida and Texas, on the heels of losses from Hurricanes Milton, Helene, and Beryl. It really does vary product by product and territory by territory.

Shifting to Casualty, the product group had another strong quarter of growth with premiums increasing 91% over the previous year. Standout performers this quarter included niche casualty classes, such as real estate errors and omissions, which grew 40%, commercial contractors general and excess liability, and environmental liability, both of which grew greater than 100%. We're growing these lines of business, and all casualty segments for that matter, by adding underwriting talent, broadening our distribution footprint, and increasing our submission intake and quoting activity.

Our approach to the casualty market, which now comprises 14% of our total book, remains anchored in underwriting targeted niche segments of the market. We employ prudent risk management tactics, such as modest gross and net line size, avoidance of heavily bodily injury, another high severity exposure, and conservative reinsurance to call our loss potential in the classes we write.

During the quarter, our average gross line for miscellaneous professional liability, contractors general liability, real estate E&O, and environmental liability was $2.1 million, that netted down to $890,000 after the application of reinsurance. As it pertains to pricing and rate accuracy, we continue to see decent rate increases and excess of loss costs across the casualty book.

Our miscellaneous professional liability products saw a blended increase of 7.6%, while real estate errors and omission rates increased 9%. The excess liability book was up 11%, and the contractor's general liability book saw an increase of 6%, with those accounts that have auto coverage up 17%. Beyond the rate increases, we limit auto liability and include many exclusions in the policy language in both general and excess liability policies.

For the quarter, the casualty book's loss ratio remained in line with our conservative loss picks, with reserves continuing to build. It's worth noting that nearly 80% of our reserves are IBNR, which is higher than industry averages for casualty. At the same time, we are quick to recognize outsized large loss activity, and we have experience in conservative reserve force to do shock losses. We are optimistic that as the book seasons, reserves will develop favorably.

Lastly, and most importantly on Casualty, in September, David Sapia joined Palomar as Head of E&S Casualty. David brings 30 years of casualty underwriting field management experience, most recently having run E&S Casualty for Hannover Re's HDI subsidiary. His strategic vision will not only bolster our current operations, but also fuel our growth initiatives.

Turning to our Fronting business, we experienced an 11% decline in premiums given the separation from Omaha National. The termination of the contract will impede the Fronting group's growth over the next several quarters as we work to replace the lost business with new partnerships. Our prospects are healthy



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with quality Fronting partners in the pipeline. This quarter we forged a new partnership with an affiliate MGA of an international reinsurer. We will remain selective as we closely manage the risk of this segment, though.

On an exciting note, we turned to Crop. We wrote $60 million in premium in the seasonally strong third quarter. Year-to-date, we've written over $100 million in premiums compared to just $12.1 million last year. Overall, it has been a good planting season and a market acceptance has been strong.

During the third quarter, we experienced product mix shift, which will move a portion of our production to crops that are planted in the fourth quarter. This will result in a portion of our gross written premium shifting to the fourth quarter as well. We also plan to write livestock premium in the fourth quarter, given our strong expertise in the sector and the availability of new capital to support this diversifying initiative.

Additionally, I'm pleased to report that Benson Latham has joined Palomar as Executive Vice President and Head of Crop. With an impressive 30 years in the crop industry, Benson brings a wealth of experience and expertise to our team. He is responsible for founding the Validus Insurance Group's agricultural practice and has held executive roles at ProAg, Crop Risk Services AIG, and Great American Insurance Company. With Benson's addition to the team, there is even more conviction that Palomar will become a market leader in the $19 billion crop insurance market.

Turning to reinsurance, the third quarter is light from a placement standpoint, but we are pleased with the quarter's accomplishments and feedback received from our broad panel of reinsurers after several marketing trips. As previously mentioned, we successfully placed an automatic facultative reinsurance program for our Excess National Property line this quarter. Additionally, our real estate E&O quota share treaty successfully renewed and improved economics.

Lastly, we also put in place a quota share for a new E&S general liability program targeting security guards. Importantly, we were able to leverage the relationships with key trading partners to get support for our de novo casualty program at Competitive Economics. Palomar's stature in the global reinsurance market proved a competitive advantage in this instance.

While it is only November, and as such, we are more than six months away from the renewal of our XOL program, we do think it is worthwhile to offer our current views on the prospects for our renewal following the cat losses year to date. To our expectation, the catastrophe excess of loss pricing for Palomar should be flat to down next year. The reasons are several. One, we currently are not putting any losses into our XOL program. Two, we continue to reduce the hurricane exposure in the treaty, and our expectation at 6/1 is that 97% of the treaty will be earthquake only. Three, the CEA non-renewing over $750 million of earthquake excess of loss limit will create excess capacity that can conceivably support our growth. Fourthly, earthquake catastrophe bonds raised after Hurricane Milton were issued at prices down year-over-year. Again, these items are germane to Palomar's placement only and inform our view on Palomar's unique position at the 6/1 renewal.

I also want to briefly discuss our pending acquisition of FIA, the contract surety insurer. We expect to receive regulatory approval by year end and close the acquisition in early 2025. As a result, we do not expect to receive any financial contribution in the fourth quarter. Overall, FIA is performing very well, and the integration should be straightforward.

Chris will go into detail on our guidance for the remainder of the year, but it's important to point out that despite the catastrophe losses from this hurricane season, we not only beat consensus in the third quarter, but also with our tightened guidance range of $124 million to $128 million of adjusted net income, we are affirming the low end of our guidance range. The consistency in our financial performance affirms our Palomar 2X strategy and the quality of our team and operation.



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With that, I'll turn the call over to Chris to discuss our financial results in more detail.

**Christopher Uchida**

Thank you, Mac.

Please note that during my portion referring to any per share figure, I'm referring to per diluted common share as calculated using the treasury stock method. This methodology requires us to include common share equivalents, such as outstanding stock options, during profitable periods and exclude them in periods when we incur a net loss.

For the third quarter of 2024, our adjusted net income was $32.4 million, or $1.23 per share, compared to adjusted net income of $23.3 million, or $0.92 per share for the same quarter of 2023, representing adjusted net income growth of 39%.

Our third quarter adjusted underwriting income was $31 million, compared to $25 million last year. Our adjusted combined ratio was 77.1% for the third quarter compared to 70.9% in the third quarter of 2023. Excluding catastrophes, our adjusted combined ratio was 67.6% for the quarter compared to 71.5% last year.

For the third quarter of 2024, our annualized adjusted return on equity was 21%, compared to 22.3% for the same period last year. The third quarter adjusted return on equity continues to validate our ability to maintain topline growth with a predictable rate of return above our Palomar 2X target of 20%. Even in the face of elevated cat activity, like what we experienced in the third quarter and with the additional capital raised during the quarter.

Gross written premiums for the third quarter were $415 million, an increase of 32% compared to the prior year's third quarter, 38% growth, excluding run-off business.

In the quarter, we have continued to regroup our written premium to align with our five key specialty insurance products, Earthquake, Inland Marine and Other property, Casualty, Fronting, and Crop. It is important to remember the seasonality of our crop premium. The majority of our crop premium is written and earned in the third quarter of each year, with only modest premium in the second and fourth quarters. That said, as Mac indicated, as the market changes, and as we write more livestock premium, we would expect to see a bit more premium written in the fourth quarter relative to our original expectations.

Additionally, the Crop premium written and earned in the third quarter has a seasonal effect on our ratios calculated as a percentage of gross earned premium in the third quarter, specifically the ratios for net earned premium, acquisition expense, and other underwriting expenses. Since the majority of our Crop premium is ceded, the net impact to our financials has been small and will look similar to previously shared expectations.

Net earned premiums for the third quarter were $135.6 million, an increase of 58% compared to the prior year's third quarter. For the third quarter of 2024, our ratio of net earned premiums as a percentage of gross earned premiums was 34.3% compared to 31.6% in the third quarter of 2023, and compared sequentially to 37.4% in the second quarter of 2024.

The year-over-year increase in this ratio is reflective of improved excess of loss reinsurance and of the higher growth rate of our non-fronting lines of business, including earthquake, that cede less premium. These results include the first full quarter of new excess of loss reinsurance placement that started June 1. While the dollars associated with this placement are higher to facilitate continued earthquake growth, the risk-adjusted rate online is lower than the previous year.



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With our excess of loss reinsurance in place and the majority of our Crop premiums written and earned during the third quarter, for which we currently cede about 95%, we expect the third quarter to be the low point of our net earned premium ratio. From there, we expect the net earned premium ratio to increase to the remainder of the reinsurance treaty in a similar pattern to last year. While there is some expected seasonality in our net earned premium ratio, we expect the net earned premium to continue to grow.

Losses and loss adjustment expenses for the third quarter were $40.3 million, comprised of $27.4 million of non-catastrophe attritional losses and $12.9 million of catastrophe losses from Hurricanes Beryl, Debby, and Helene. Our loss ratio for the quarter was 29.7%, made up of an attritional loss ratio of 20.2% and a catastrophe loss ratio of 9.5%. As Mac indicated, we believe this quarter's results were a testament to our continued effort to derisk our portfolio over the past few years.

Our acquisition expense as a percentage of gross earned premium for the third quarter was 10.5%, compared to 9.9% in last year's third quarter and sequentially to 11% in the second quarter of 2024. This percentage decreased sequentially, primarily from strong growth from Crop that has primarily written and earned in the third quarter. Most of the Crop premium is ceded, resulting in higher ceding commission and a lower acquisition expense ratio for the quarter. We expect this ratio to move up from the low point in the third quarter.

The ratio of other underwriting expenses, including adjustments to gross earned premiums for the third quarter was 5.9%, compared to 6.7% in the third quarter last year and compared sequentially to 7.3% in the second quarter of 2024. As expected, the lower result for the quarter was influenced by the Crop premium written in the quarter.

As demonstrated by our new hires over the last six months, we are extremely committed to investing in all aspects of our organization as we continue to grow profitably. We continue to expect long-term scale in this ratio, while we may see periods of sequential flatness or increases as we continue to invest in scaling the Organization within our Palomar 2X framework.

Our net investment income for the third quarter was $9.4 million, an increase of 56% compared to the prior year's third quarter. The year-over-year increase was primarily due to higher yields on invested assets and a higher average balance of investments held during the three months ended September 30, 2024, due to cash generated from operations.

Our yield in the third quarter was 4.6% compared to 3.9% in the third quarter last year. The average yield on investments made in the third quarter was 5.7%. We continue to conservatively allocate our positions to asset classes that generate attractive risk-adjusted returns.

Our stockholder's equity has reached $703.3 million, a testament to consistent profitable growth and the capital raise. At the end of the quarter, our net run premium-to-equity ratio was 0.84% to 1%.

Turning to our full year adjusted net income guidance, we initiated 2024 with a range of $110 million to $115 million at the beginning of the year. Given our strong performance and execution through the second quarter, we increased that guidance range to $124 million to $130 million. Now we are tightening our full year 2024 adjusted net income guidance to $124 million to $128 million, including approximately $8 million of catastrophe losses from Hurricane Milton in the fourth quarter, significantly ahead of our original full year guidance outlined in February that did not include any estimate for catastrophe losses.

The midpoint of our updated guidance range represents adjusted net income growth of 35% compared to 2023 and an adjusted ROE greater than 20%, including a capital raise in August, which puts us well on the path to achieving our Palomar 2X goal of doubling adjusted underwriting income in three years.



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With that, I'd like to ask the Operator to open the line for any questions. Operator?

**Operator**

Thank you. We will now be conducting a question-and-answer session. Our first question comes from the line of Mark Hughes with Truist Securities. Please proceed with your question.

**Mark Hughes**

Yes. Thank you. Good afternoon. When we think about the quake business for next year, you talked about the Earthquake Authority not renewing a proportion of its reinsurance. What are the growth prospects next year maybe thinking about commercial versus residential as well?

**Mac Armstrong**

Hey, Mark, this is Mac. Good question. I think overall we feel very good about the growth prospects for earthquake broadly. As I said in my remarks, we really like the fact that we have a balanced book of residential and commercial quakes. Right now, it's probably about 55% residential, 45% commercial. As I mentioned, rates are plateauing in commercial, but the metrics still remain very attractive. We want to continue to grow in commercial earthquake, even if there is some degradation in rate because, again, the metrics are compelling.

We do think that we can maintain high teen's growth—well, we said 18% to 20% for '24 but we think we can sustain growth in the teens next year. We'll probably see a little more growth from residential on a relative basis versus commercial. But, again, it will be a balanced approach. But I think the one thing that I want to emphasize is with residential quake, we have flat rates that renew with a 10% inflation guard, which, again, is covering inflation at this current day. It's providing scale as reinsurance pricing is flat and certainly nice scale and quite elegant scale if reinsurance pricing declines.

We feel good about the prospects for quake, like our balance book of residential and commercial. You'll continue to see us invest, especially, as you pointed out, reinsurance capacity becomes even more available on the heels of the changes that the CEA just made.

**Mark Hughes**

Chris, some nice improvement in the earned premium ratio. You may have touched on this, but how much of that is mix of business versus pricing for your reinsurance? How do we think about that on a go-forward basis? If you've taken this step up year-over-year, and then it's going to continue to step up sequentially, is that going to trend positively as we think through 2025? I won't go beyond that, but in the 2025.

**Christopher Uchida**

Yes, thanks, Mark. Good question. Obviously, we talk about net earned premium, and there's just the growth in the dollars that we're seeing there from the overall performance of the business. When you get down to the overall fundamentals of what's underlying, it's all of the above of what you talked about. It's going to be driven by rate. It's going to be driven by mix and then also driven by the strong performance that we saw in the excess of loss placement at 6/1 of 2024.

When I look at it, we've talked about it before that we do believe when we look at the net earned premium ratio that the low point will be Q3 of this year. When we went into this quarter, I would probably expect it to be a little bit lower than the 34% that we saw; strong performance by the overall book did help that. I do



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expect Q3 still to be the low point. Incrementally, I expect it to continue to move up from this point in Q3 to Q4 and Q1 of next year and then reset a little bit at the next excess of loss renewal just with the normal placement where we buy to fund, let's call it the growth in our cat exposed lines, primarily earthquake. But overall, we expect to see that same trend. But the tea leaves are showing strongly that we should see favorability and strong growth in our net earned premium dollars as we go through the end of 2024 and through 2025.

**Mac Armstrong**

Mark, this is Mac. One thing I would add, and Chris talked about it, the fact that our Fronting business now is growing slower than our other lines, that's going to also drive net earned premium growth. That's one silver lining, so to speak, of the slowdown in Fronting and the expiration of our one Fronting partnership with Omaha National. That's also a catalyst that is encouraging.

**Mark Hughes**

I appreciate it. Thank you.

**Mac Armstrong**

Thanks, Mark.

**Operator**

Thank you. Our next question comes from the line of Paul Newsome with Piper Sandler. Please proceed with your question. Paul, are you on mute?

**Paul Newsome**

I was hoping to ask a little bit of a big picture question about your property businesses. Not just like this quarter, but obviously they've been the main source of volatility. It's fairly natural. But if you look back over the period of time, have they been profitable over time as you've reduced your exposures it's more a matter of reducing volatility? Or has there actually been something where it really hasn't been profitable and that's what you needed to deal with over time, not this last quarter?

**Mac Armstrong**

Yes, Paul. We look at across the board our property portfolio and casualty portfolio alike to look at risk-adjusted returns and the volatility that they can bring. Also, in the case of property, what we call our cat payback. How long would it take if there are losses, severe or average from a catastrophe to recoup them through rate or underwriting changes? When we look at our portfolio, hold aside earthquake, which has performed well of what we call our Inland Marine and Other Property products, that's seven different products: Builder's Risk, Motor Truck Cargo, non-cat exposed Excess National Property, Hawaiian Hurricane, Flood, Commercial Equipment and 17 All Risk.

I think what you could say within any portfolio, you're going to have some strong performers and some that are underperforming. Builder's Risk has been exceptional, Excess National Property exceptional. Hawaiian Hurricane is now becoming more of a fee generator. We're long that product, so to speak. Then Motor Truck Cargo is a consistent small limit performer as well.

I think the ones that we are watching have been Flood and the All Risk book. Flood has been profitable. Losses have been a bit amplified this year by the atmospheric rivers in California and then some of the



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storms. Then All Risk is one that's been probably disproportionately volatile. We have done a very good job of reducing our limits in that line of business. For instance, if you look at Helene, the average exposed net limit there was about $400,000, same for Hurricane Milton.

We're not taking big pops. But if you get 40 claims and the average exposed limit is $400,000, it's a 50% damage ratio. That's where you get $8 million of losses from Milton. That puts a little bit of pressure on something that's only 3% of our premium or something along those lines. Long winded way of saying, generally speaking, the property book has been profitable and performed well. There are a couple of underperformers that we're continuing to look at and likely will pull back exposure to.

**Paul Newsome**

Somewhat related, the Crop business, is that a net diversifier for your P&Ls, or is it additive to the property exposures?

**Jon Christianson**

Yes, Paul, this is Jon Christianson. I can take that one. No, it's a great diversifier for us. As you think about the types of impacts that can affect a negative crop year, it's really drought. That's an uncorrelated risk with as you think about the rest of the property book. It's a really nice diversifier and a complement to everything that we've built over the past decade. We have a lot of conviction in that line and believe that it'll be a great source of diversification on a go-forward basis.

**Mac Armstrong**

I think the other thing that I would add to Jon's point is that it is uncorrelated to P&C market cycles too. It can be a nice steady contributor to earnings on a go-forward basis. On the heels of us raising capital in August, it is our intention starting 1/1 of ’25, to take some more risk in that line, the balance sheet affords it. The team that we brought on has the competence and then some to do it. We are, again, really enthused about what we can do in Crop.

**Paul Newsome**

Fantastic. Thank you very much. Appreciate the help as always.

**Mac Armstrong**

Thanks, Paul.

**Operator**

Thank you. Our next question comes from the line of David Motemaden with Evercore ISI. Please proceed with your question.

**David Motemaden**

Hey, thanks. Good afternoon. I had a question just on the catastrophe losses. Looks like this year it'll settle out in the five point to six point of an impact on the combined ratio. Is that the expected level that you guys would expect in a given year, given the mix of business? Or any commentary you could provide on the AAL or your expected cat load would be helpful? Because a lot of things have changed over the last several years in terms of your mix.



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**Mac Armstrong**

Yes, Dave, that's a good question. What I would say, it's slightly elevated this year to what the AALs had, whether that was because of severe convective storm activity in Texas and really, tore hail loss that was a one in 100 type of event, and then a little bit of elevated flood losses. I think with the wind, what I would say is all of these events have been well within our retention. That's something that we feel good about from an ongoing capital or reinsurance support standpoint. But what it also means is that does it, again, generate the cat payback that we're looking for, the risk adjusted return.

I would expect us to pull back some of our continental hurricane PML over the course of 2025, and therefore bring down that cat load some. I think we've talked about it being three to four points. I think that's a good steady state number, especially with some of the underwriting changes or yes, underwriting changes we expect to make.

**David Motemaden**

Got it. Thanks. That's helpful. Then, Chris, on the other underwriting expense ratio at 5.9%, obviously a bunch of moving pieces this quarter. Could you just help us give us a sense of what's the run rate underwriting expense ratio as we think about as the business scales and adjusting for some of the mix impacts that may have flattered this quarter's result?

**Christopher Uchida**

Yes, no, good question, and we've talked about it. The Crop premium that comes in in the third quarter, and when you look at the ratios, the expense ratios on a gross basis, there was, call it max $60 million of written premium. Almost all of that is earned during the quarter, that does artificially push the underwriting expense ratio down a little bit, that 5.9%. I would expect it to be a little, call it steadier in the mid-6% to 7%. That's probably the right way to think about it on a, call it, run rate basis.

I'd say the one thing I would continue to emphasize is that we are adding talent. We are adding scale to the Organization; we are still building. I am not beholden to try and hold the other underwriting expenses at a certain level, to call it hit profitability. We are very profitable. We can afford to invest in all of our teams and our people, and we will continue to do that. Overall, I still expect strong scale in the other underwriting expenses as we continue to grow over the long-term, but we are not going to slow down in trying to build this organization to continue to grow in scale.

Overall, it's performing well. It's performing within our expectations, but I will point out we will continue to invest, but I don't expect this ratio to jump to, call it 10%, but it will, call it, vary and move around from quarter-to-quarter, but I'd say mid-6% to 7% is probably a good way to think about it as we continue to grow this organization.

**Mac Armstrong**

Yes, and just to add some color to Chris's comments. You bring someone on like a David Sapia. The great thing is that they are a player coach. They're producing business, but also going to be adding underwriters who can extend our footprint and our growth long-term. That's an investment that you're making up front that you get great returns on long-term. Same thing for Benson Latham. Like Chris is saying, we're not going to sacrifice the investment in long-term growth and earnings to maintain that ratio in the short-term, but it's not going to vacillate wildly. I think Chris has given very good direction on where it will go to.

**David Motemaden**



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Great. That's helpful. Thanks. Good to see some of that scale come through considering the investments that you guys are making. Maybe just lastly, Mac, you spoke about just the market conditions and commercial earthquake, and I'm wondering if maybe you could provide a little bit more detail on where that incremental competition is coming from. We've heard the London market being a little bit more competitive. I know you guys don't directly write in the London market, but I know that that is another avenue for some of the commercial quake business. I'm just wondering, is that really driving that plateauing in the commercial earthquake rates?

**Mac Armstrong**

Yes. I think the plateauing in earthquake rates is driven by a few things. One is you've had four years of consecutive rate increases on loss-free business. When you look at, let's call it a homeowner's association in California, a small midsize account risk, they're getting what we call fatigue in terms of rate increases. What we'll do in many instances is sacrifice rate, but hold terms and conditions, move up deductibles, or make it name peril of earthquake only as opposed to a DIC policy. That's contributing to it somewhat.

But yes, there has been new capacity that's come in. It's been a few MGAs that have brought in capacity. Lloyd syndicates are indeed guilty in that instance of some of that new capacity. Then there's been some business in the D&F market that's been aggressive. But on the whole, the metrics and profitability of the line remain compelling. As such, we're going to look to grow in commercial earthquake. I think we can grow in commercial earthquake next year. But it is a little bit more competitive than it's been the last 1.5 years.

**David Motemaden**

Got it. Understood. Thank you.

**Mac Armstrong**

Thanks, Dave.

**Operator**

Thank you. Our next question comes from the line of Andrew Andersen with Jefferies. Please proceed with your question.

**Andrew Andersen**

Hey, good afternoon. I think you had previously pointed to $125 million to $150 million of Crop premium for the year. I know you mentioned some shift to 4Q and some new products online. But do you still expect that to be the case for the full year?

**Mac Armstrong**

Hey, Andrew, yes. I don't think we said $150 million. I think we said $100 million to $125 million. If I said $150 million, that may have been my bold ambition. But nonetheless, I think we feel good about getting to that close to that $120 million number. I think importantly, with the addition of Benson Latham and James Long, two terrific hires in the last quarter and a half, we feel very good about building it into a $0.5 billion plus franchise in the next several years. We think we're going to be a market leader here.

**Jon Christianson**



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Yes. Andrew, Jon Christianson here. One thing I'd add is, we are really proud of our achievements in Crop year-to-date. Mac and Chris both talked about it, surpassing that milestone of $100 million in the first nine months of the calendar year, despite commodity prices being down year-over-year. I mentioned that we had some favorable, what I call favorable product mix shift throughout the year. As a result, we'll see a bit more in Q4 being written. But as it was mentioned before, just to reiterate, Q3 will remain the seasonally high quarter for Crop, followed by Q1, and Q4 and Q2 will make up the difference.

**Andrew Andersen**

Thanks. Then on excess liability, I think I heard 11% rate increase. It seems like a deceleration to the 20% in the prior quarter. Was that just a mix shift? Or is there anything else going on there we should be thinking of?

**Mac Armstrong**

Well, it's a bit of a mix shift, but it's also, we've tightened terms and conditions and put in more policy exclusions. I think when you look at the actual risk adjusted increase, we feel great about that. I think the other thing too is we remain very tight on the excess liability keeping the auto either out of it altogether or tightly constrained from a fleet size and range of activity standpoint. It's a combination of rate and then constriction of coverage, which is something that we and our reinsurance panel are strongly endorsing.

**Andrew Andersen**

Thank you.

**Christopher Uchida**

Thank you.

**Operator**

Thank you. As a reminder, if anyone has any questions, you may press star, one on your telephone keypad. Doing so will ensure that you are joined in the queue to ask a question.

Our next question comes from the line of Meyer Shields with KBW. Please proceed with your question.

**Meyer Shields**

Okay. Thanks so much. Really a couple of follow-ups on earlier questions. One of the things we've heard over the course of this earnings season is that rate trends are smaller, commercial property risks are rising. Are you seeing that in the earthquake space too, or is that just a different market?

**Mac Armstrong**

I would say that's a different market, Meyer. I think smaller risks, and particularly our book are the ones that you're starting to run into budgetary constraints, especially in California, where you also have fire premiums rising. We are not seeing that in commercial earthquake.

**Meyer Shields**

Okay. That's helpful. Thank you. The attritional loss ratio in the third quarter, obviously, is fantastic, and I think better than guidance. Does that have any impact on your expectations for 2025?



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**Christopher Uchida**

Meyer, I think that's a great question. First thing I'd point out is that, yes, the attritional loss ratio performed very well this quarter. I'm very happy with the results. One thing, and one key thing I'd point out there, is that we are not touching any of our casualty reserves. There is no, call it, takedown of any casualty reserves in there. This is really driven by strong performance in our property lines of business that had a very strong quarter, some minor prior period development in there, but overall, casualty loss ratios are being held steady as we continue to build on that book. That's the first thing I'd point out.

The other thing I'd point out is that, we've talked about a little bit before, our attritional loss ratio does have some mini-cats in it. This quarter was obviously elevated from a frequency and activity standpoint. I would say that some of those cats were elevated—or some of those mini-cats were elevated into the cat category, so let's call it, took out maybe one to two points of our, what would be attritional losses, and moved it into the cat loss category. That brings that loss ratio up a little bit.

Overall, it is doing what we expect it to do as the mix shifts, changes for the business, the loss ratio, the attritional loss ratio has continued to move up. I expect that trend to continue in 2025 as the mix in those lines of business continues to improve, or continues to diversify, and so that we move away from some of our lines that have no losses, earthquake, and fronting—or not move away from, but diversify around those lines. I expect it to still continue to move up. But, again, still very highly profitable lines of business, still very strong overall combined ratio lines of business.

**Mac Armstrong**

But, Meyer, I would just add, and I want to make sure I give credit where credit is due to our underwriting team. If you look at just the attritional loss ratio year-over-year ticked up from 19.4% to 20.2% while the casualty book grew 90% year-over-year. I think that shows the quality of the underwriting, the property side, and with not touching reserves on the casualty side. I agree with everything Chris said, it's going to tick up, it's not going to tick up like a step function. It's going to tick up very gradually and steadily, and I think this third quarter was a prime example of the great job our team did underwriting.

**Meyer Shields**

Yes, no, that makes perfect sense. A final question for you, Mac, do you have any thoughts on the availability or ceding commissions on casualty reinsurance as we head into 2025?

**Mac Armstrong**

Well, I was just in Bermuda two weeks ago and saw about 20 reinsurers there, and I think on the whole, they continue to have capital. When I look at our casualty book, we're in the market now on one treaty. We got two done in the third quarter at expiring or improved economics. We got a de novo, one done, market consistent and frankly, attractive economics to us. We feel like there is capacity for niche casualty lines. The other thing that we feel good about that's unique to Palomar is, by being the stature of a buyer that we are now on the XOL, Chris talks about it, we spent $265 million just on our excess of loss costs, and we have over now 100 reinsurers that we're working with.

Our balance in the market certainly helps us feel good about strong support on the casualty side, ‘24, rest of ‘24, and into ‘25. We have not seen any pressure on our ceding commissions at this point, and we feel good about our prospects individually, and I think the market, on the whole, there is still ample capacity in capital, especially with Milton looking more like an earnings event and not a capital event by any stretch.



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**Meyer Shields**

Okay, fantastic. Thank you so much.

**Mac Armstrong**

Thanks, Meyer.

**Operator**

Thank you. Our next question comes from the line of Pablo Singzon with JPMorgan. Please proceed with your question.

**Pablo Singzon**

Hi, good afternoon, guys. First question, could you offer your latest views and you talked about this already, but something more specific, your latest views on how fast the attritional loss duration will pick up over the next couple of years as you shift the business mix?

**Christopher Uchida**

Yes, no, I think, I've talked about it. It would be, call it, one point to two points, potentially a quarter. I think two is very aggressive. I'd say one is probably a little more consistent. If we finish this year in the, call it, low 20s, the guideposts have been 21% to 25%, based on this quarter's strong results, I'd probably say, expect to see that on the lower end, let's call it, the 22% to 23% range. Well, within the guideposts. I would expect if it moved up a point, so three points to four points by the end of next year would be my expectation overall as we look at the growth.

One caveat I always give to that is that that's with similar risk participation. We do have some new capital burning a little bit of hole in our pocket. We may try and use that strategically on lines of business that we're really bullish on and have been performing really well. But overall, it doesn't change my overall expectations really on where that's going to move up to. I would expect it to be, call it, in that 26% to 28% type range by the end of next year as we think about the growth and diversification of our own lines of business. Overall, still feel fairly good about that. That type of loss ratio still gets you into a sub-80% combined ratio overall.

**Pablo Singzon**

Yes. That makes sense. Thanks for that, Chris. Then second question, I think, Mac, you had mentioned how fast E&S residential earthquake is growing. It was a big number, I think it's above 70%. I don't remember the exact number. Can you talk about the admitted side of the resi earthquake book? You did mention there's an inflation guard. But apart from that—outside of that, how fast is that piece of the business growing? Then if you take a step back, to what extent in your opinion is growth in resi earthquake being influenced by this, I'll just call it, migration of risks from admitted to E&S on the personal line side. I think that's pretty well known at this point. You're benefiting from it. But in other words in a more normal market, and who knows when that happens, do you think your growth profile will change? There's a bunch in there, but hopefully…

**Mac Armstrong**

Yes, Pablo, let me just give you my views on growth in residential quake, and I think we'll probably be able to touch on it. I think first and foremost, we feel very good about the growth prospects for residential earthquake, both admitted and E&S. When we talk about E&S, outer bounds that can probably be about



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20% of our book. It's going to be concentrated in higher value risks. It's going to be concentrated in selected geographic areas like West Los Angeles and certain pockets of the Bay Area where the housing stock is expensive and the exposure is more pronounced.

If you look at our new business right now, it is very consistent across both admitted and E&S. Now E&S, we're getting more risk-adjusted rate, and we'd like to continue to grow that like we did in the third quarter. But I don't want you to think that we are going to—even as the market grows increasingly E&S in California, you're going to see us not write as much on just the standard residential earthquake side of the book.

Additionally, we have benefited certainly from the dislocation in the California homeowners' market, and as well the changes to the CEA. Those changes to CEA continue to grow through the market, but also the changes in the homeowners' market where companies like State Farm are non-renewing large swaths of their book, that means they have to leave the CEA, and that means we get the chance to compete for them. That's going to be standard policies, and again, a driver of the standard residential value-select products growth.

I think the other thing that we are cautiously optimistic about, which might be a '25 growth driver, might be a '26-growth driver, as interest rates come down, we do expect to see housing sales and transaction activity pick up, and when that happens, that means you're going to see new buyers of residential quake come into the market, and those will more than likely be on the standard side. On the whole, we feel very good about the growth in residential quake. It was pretty close to the same level as commercial in this quarter. It's a high teens grower on a bigger base, and I think we feel that that is sustainable, especially when you do have a 10% inflation guard and policy retention in the high 80s, low 90s, depending on the month.

**Pablo Singzon**

Yes, that makes sense, Mac. Then, just last from me, as you're growing outside of earthquake, I'd be curious to hear the investments you're making outside of underwriting, and basically what I have in mind is something like claims as you say more Casualty business, those types of policies or claims that get more litigated. What's happening outside of the new business underwriting functions, and speak to the investments you're making? Thank you.

**Mac Armstrong**

Yes, great question, and thanks for asking. It gives me a chance to do a little bit of a commercial for someone we just brought on. We just hired Althea Garvey as our new Chief Claims Officer. She will work alongside Angela Grant, our Chief Legal Officer, on the claims side. Althea has over 30 years of experience as both an insurance defense counsel and litigator, as well as running property claims for large E&S companies like Lexington and AIG, and then also having run TPAs. She's got a very holistic view of the claims process, and part of her charge will be not only management of TPAs that we work with, but also continuing to build our in-house capabilities. That organization is growing, and there are certain areas that we will probably be leaning into and taking more active control of, especially on the casualty side.

Good question. You'll probably be hearing more over the course of '25 about the investments we're making on the claims side, and certain actions that we're taking to further invest in loss management, prevention and control.

**Pablo Singzon**

Thank you.

**Operator**



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Thank you. There are no further questions at this time. I would like to turn the floor back to Mac Armstrong for a closing remark.

**Mac Armstrong**

Great. Thanks, Operator.

**Operator**

Ladies and gentlemen, this does conclude today's teleconference, and we do thank you for your participation. You may disconnect your lines at this time.



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