

Travelers
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Jay Gelb: Okay. Good morning, and welcome, everyone. Thanks, everyone, for joining us over the next several days at the Barclays Global Financial Services Conference. I'm Jay Gelb, senior analyst covering the U.S. insurance industry. It's our great pleasure to have Travelers' Chairman and CEO, Alan Schnitzer, with us today. Travelers has been a fixture at the Barclays Financials Conference. The company is among the largest commercial and personal lines property casualty insurance companies in the U.S., with a superior track record of creating shareholder value. Alan, thanks for joining us today.

To start off Alan, can you describe the current operating environment for Travelers?

Alan Schnitzer: Sure. But before I do that, Jay, I'm duty bound to share that to the extent we get around to forward-looking information today, and I suspect we will, that there are risks and uncertainties involved, and I would encourage everyone to look at our SEC filings for the factors that can cause those statements to be untrue.

But back to your question, operating environment. We approach the operating environment from the perspective of long-term stewards of other people's capital, and we're confident that we've got the competitive advantages we need to outperform over time in this business which is the way we think about it.

Now, in the short-term, things are always going to change in this business. So, whether it's social inflation, whether it's interest rates, whether it's regulation, things are going to change. And what's important from that perspective is to have the experience and expertise to manage through that. We feel very good from talent, tenure, experience perspective that we got all that. Then you think longer-term about the operating environment it would be an understatement to say that the world is changing and we've identified the forces of change before that we see impacting our industry.

So, customer expectations are changing, right. Every engagement we have with any stakeholder is measured against their last experience on Amazon, right. So, we've got to be up to that challenge. Technology is changing overnight. What we can do today with data and analytics is very exciting. And the distribution model is evolving.

And so, we're highly conscious of those forces of change and we think about the operating environment and we've established three priorities to respond to those things. So, we've built a business over decades in being we think the best at understanding risk and the products and services our customers need to manage their risk. And we need to, in this environment, continue to invest to extend that lead. We've got to provide great experiences for customers, for our distribution partners, and for our employees too.

And we've got to do more with less. We've got to improve and optimize productivity and efficiency and we've been very successful in that in recent years. But we think long-term from an operating, to get back to your question, the operating environment, we think the winners in this industry are going to be those with a foundation of excellence that can innovate successfully on top of that and that's what we're focused on.

Jay Gelb: Excellent. I think that's a great jumping off point. Travelers' objective is to deliver a mid-teens core return on equity over time. The company's ROE was 11% in the first half of 2019 including the impact of catastrophe losses. And since 2005, Travelers' ROE has averaged 13%. How achievable do you feel this low-teens return on equity goal is over the next few years?

Alan Schnitzer: We get that question a lot because we express our -- make no mistake about it, return on equity is the primary measure we use to manage the company. We get that question a lot because we do express our objective as mid-teens over time. I've said many times and I'll just remind everybody again that we developed that mid-teens objective in 2005 when the ten-year treasury was about 5%.

I looked this morning at the ten-year. I think it was around 1.6%. So, in an environment of a 1.6% ten-year it's very hard to get to mid-teens. And there was nothing magic about a mid-teens return on equity. All that really was, was a qualitative description of what in 2005 would've been industry-leading in the context of a 5% ten-year. Clearly, we're not in that environment and something less than mid-teens is industry leading today.

So, I've said before and I'll say again, we really need the interest rates to get to a more normal level by historical standards in order to get back to that mid-teens. And I'll remind you that a year ago, about this time, the ten-year treasury was about 3% and we all thought heading up and that was encouraging. But we're not there today, but in any event, our objective is to deliver industry leading returns.

Jay Gelb: At the same time, the company is generating industry leading returns on the underwriting side in terms of its contribution to return on equity, right?

Alan Schnitzer: Yes, we feel good about the underwriting return.

Jay Gelb: Okay. Let's discuss the commercial P&C cycle and also catastrophe exposure. The commercial P&C pricing cycle has been on an upward trend, including several factors, such as large industry catastrophe losses, which have impacted industry results over the past two years. The peak of hurricane season is already approaching, and seasonal California wildfire risk typically peaks later in the year. How has Travelers addressed its catastrophe exposure from events such as hurricanes and wildfires, including its reinsurance protection?

Alan Schnitzer: So, if you take a step back and look at weather, weather losses have been trending up over time if you look back over some number of years and we certainly worked that into our perspective when we think about our pricing and risk management. But you've got to take a step back from that and you've got to look at catastrophe losses. And you've got to say, OK, to what extent are these increasing catastrophe losses coming from higher frequency and severity of perils, and to what extent is it coming from other factors, for example demographics.

So, the population is growing. So, you'd expect just by virtue of that for there to be a higher degree of catastrophe losses. And on top of that, the population is growing and in fact, home values are growing in harm's way. So, think in areas that have a higher propensity for tornadoes and the coast where you've got hurricanes and wildfires.

So, you've got to separate out the weather from the non-weather. Now, we do see a changing weather pattern. So, you've got some areas of the country where you've got

higher levels of drought. You've got other levels of the country where you've got higher levels of precipitation. We can see that in the data.

It also seems reasonably likely -- it's a little less clear in the data -- but it seems reasonably likely that we're also seeing increased frequency and severity of thunderstorms and hurricanes and Dorian is a great example. Dorian is -- this will make the fourth consecutive year when we've had a Category 5 hurricane in the Atlantic and I believe that is the longest streak on record. And Dorian tied for the strongest hurricane to make landfall. I think it tied with a 1925 hurricane.

So hard to look at the anecdotal evidence and ignore that. But even what we see in the data would suggest it is reasonably likely that those storms are getting more frequent and more severe. But these are perils that you manage over a long time, that you manage over decades or longer. And when we look back over our experience over the last decade, there haven't been many things that have surprised us other than the wildfires. The wildfires were a surprise and we've adjusted to that. It's one of the areas where we've got -- the industry has the least developed models for managing that peril. But that's really been the only surprise.

Whether there's an event that surprises you or not, after every event you take a step back and you say, did I expect that event? Was that event in my playbook? And then whether or not it was in your playbook, you say were the losses that came out of that event consistent with what I would've expected for that event. There's always lessons to learn. When you take the data, you take literally just the loss data. You take the experience. You take lessons learned from postmortem and you factor that into your underwriting and your claims handling, and you try to do better next time.

I'll must make a quick pitch for our claims group. In 2018, for the most significant catastrophic events we had in the U.S., we closed 95% of our property claims within 30 days of the event, which we think -- I don't have the data to support it but I'd be surprised if anybody did any better than that. And what that means is if you're a Travelers' customer and you're impacted by a hurricane this time of year, it's probable that -- there's some possibility I guess that you've got a better chance of getting back in your home to enjoy Thanksgiving than if you don't have a Travelers' policy. And we think that's important.

Jay Gelb: Fair enough. And since you brought it up, Hurricane Dorian, any initial thoughts on that in terms of what the impact could be on Travelers and perhaps the broader industry?

Alan Schnitzer: I don't have a number to share. It's certainly not as severe a storm in terms of losses anyway as if it had followed some of the early projected tracks. I don't have a number to share. I will say that our thoughts and prayers are with those people in the Bahamas that really did take the brunt of that storm.

Jay Gelb: Okay. Let's turn to pricing. Travelers' domestic business insurance renewal rate trends have been favorable with a 3.6% increase in the most recent quarter, which was the highest level in five years. Can you talk a little bit about what's driving those trends in terms of increased pricing? And is this accelerating trend continuing into the third quarter?

Alan Schnitzer: Yes, so the second quarter, that statistic you just mentioned, that was the 10th straight quarter where rate change had been up year over year. So that's pretty good news. As we look at initial data coming in for the current quarter, we would expect rate change in

the third quarter to be somewhat higher than rate change in the second quarter of this year.

Obviously, it's what, September 9. So, I don't have a full quarter yet. I can't tell you exactly what I think it's going to be. But we do think pricing in the third quarter will be up over the second quarter. And by the way, that's after the headwind that we're seeing from workers comp, which is a big line for us. So that's a number of years of compounding rate, which is a good thing.

The factors that are driving that rate change, I would categorize broadly speaking as just rate adequacy isn't there. So, we're coming off some number of years where pricing didn't keep up with loss trends so there was a diminishing margin during that period of time. You've got loss trend I think that's a factor for many in the industry, including us. And so that's coming both from the property and casualty side of this business. I do think there continues to be a question mark in terms of weather losses.

And we've got interest rates continuing to look like for some period of time into the future they're going to be pretty low. So, all of those factors that have been out there driving this rate environment I think are still out there. And on top of that, you've got some capacity. It's not that the capital is not there but you've got some markets that have withdrawn from lines or businesses completely because they weren't getting adequate returns.

So, you take all those factors together and we'd say they still persist. And so, we're encouraged that there's room for this to run.

Jay Gelb: That's great and certainly a positive trend on rate momentum. Social inflation seems perhaps to be a factor that could be affecting casualty insurance lines. What are your thoughts around that? What are the emerging trends and what are you keeping most watch on?

Alan Schnitzer: So, in the fourth quarter of 2018 and the second quarter of this year, we identified a more aggressive tort environment generally as a factor for us. And it's important to note, it's not that we weren't expecting that. We were expecting that. We've been following that trend for a long period of time.

But what we saw in the fourth quarter and what we saw in the second quarter were implications of a tort environment that came in even above our expectations. And this is a very complicated topic and I'm trying to sum it up in a couple of sentences. So, I'm speaking in generalities here. But broadly speaking, that comes up in a couple of ways in our data and one is the rate of attorney involvement on claims.

And so that's been trending up for some period of time. We've been watching that. We've got an expectation for an upward trend, but we saw that come in even above what our expectations were. And one consequence of that is you get a lengthening of the claim development patterns, which is the way the actuaries compile the data to come up with their loss estimates. And so that's one of the reasons why you get a result that you didn't expect.

Now, unfortunately, and not unlike what we saw in the fourth quarter and the second quarter, as we look at the more recent data coming in subsequent to the second quarter, we continue to see loss activity that is coming in hotter than we would've expected and that's after the higher level of expectation we had after the fourth quarter and the second

quarter. So, this is an issue that continues to persist and we're going to see the impact of that in the third quarter.

Everything we see gives us a very high degree of confidence this is environmental and so we'll respond through both price and a litigation claims handling strategy.

Jay Gelb: Right. So, with regard to -- my sense is your comment on having claims inflation impact results in the third quarter, any kind of order of magnitude investors should be thinking about on the underlying loss ratio?

Alan Schnitzer: We haven't closed the books yet and so it would be premature for me to share. So, it would be premature for me to give an order of magnitude.

Jay Gelb: Okay. Something we'd be able to see though probably.

Alan Schnitzer: Oh, yes.

Jay Gelb: All right. I hate to keep going on this but to what extent do you feel that might be fully addressed in 3Q?

Alan Schnitzer: I'm always hesitant to tell anybody that boy, we've got it. We swung a big stick at it and it's done. And if I'd said that after the fourth quarter or the second quarter, I would have been wrong. And the fact of the matter is what we're really trying to do is look at the data that we have and react to the data that we have. And missing it too high is no better than missing it too low. Our objective is to get it right.

So, we're confident that we've got the right data, that we've got the right analytics, we've got the right people looking at it. And this is a business where you don't know your cost of goods sold when you sell the product. So, there's a lot of assumptions that go into it. You take all that and you make your best estimate. And we price in reserve on the basis of those estimates. So, we can't really -- it's a mistake to run this business in any way other than by the numbers. And we're very, very disciplined about that and things are going to change from period to period but very confident in our ability to manage this over time.

Jay Gelb: Is it particular lines that you're seeing it like commercial auto or areas have been a little hot until now?

Alan Schnitzer: Again, too early for me to get -- we haven't closed the books. Too early for me to get into specifics.

Jay Gelb: All right. Workers compensation. Overall industry rates continue to decline, and my understanding is that's a pretty sizable part of Travelers' business. To what extent is Travelers addressing workers comp to prevent underwriting margin compression?

Alan Schnitzer: Definitely a large line for us. It's our largest line of business in business insurance. We're the number one writer of workers comp in the country and we're really good at that business and we feel really good about that business. So, I'm happy with that. The good news is that the pricing pressure that we're feeling in workers comp is a function of the fact that returns have been very healthy for some time. And so it's not a health of the line issue.

It's a highly regulated line of business and so there are going to be cycles in the pricing and we can see over long a period of time those cycles have actually lagged the results.

And so, what's important for us is that we've got the competitive advantages to manage through that. We've got the competitive advantages to -- in terms of risk selection, in terms of segmentation, in terms of claims handling.

Think about 500 nurses. We've got 500 nurses that are managing this line for us. We've got a model that predicts chronic pain and therefore opioid addiction. So, we've applied this model now to a cohort of about 65,000 people over some number of years and among that cohort, we've significantly reduced opioid usage. We've significantly reduced surgeries and we've significantly improved return to work. So those things make a difference.

We've got -- and so that's where our models look at a situation and say, boy, high-risk of severity, watch out. And that requires a high degree of intervention. On the other side, we've got models that will look at a particular worker's injury and say low risk of severity. And for those cohort of people, we've developed a mobile solution that lets them manage their own return to work through a mobile app.

And I hesitate to describe it as a mobile app. It's way more than that. We've completely redesigned the work effort behind that. So, I share those as examples of the type of things that we've done that we think gives us an advantage in this business. And again, we're active managers of our business. You give us a level playing field and we think we'll outperform.

Jay Gelb: Of course. Okay. Let's talk about an interesting growth area, cyber insurance. There seems to be substantial increases in demand for that coverage, although there's also been some large industry losses. How is Travelers approaching this business line?

Alan Schnitzer: So, the cyber product is an important product for our customers and we think it's an important business opportunity for us. And so, it's an important part of our business. Having said that, it is a coverage and a line of business that is evolving. And so, we take a very measured approach to taking on that risk. We manage it through very strong operationally. So, we've got very strong underwriting. We've got very strong risk management. We've got a very strong and very specialized claim response for it.

And then you manage the product itself. You manage the terms. You manage the limits. The vast majority of our limits for cyber are under \$1 million and you think about reinsurance. It's one of the very few lines that we have a quota reinsurance policy for. And that's just a reflection of the fact that we want to be in it. We think it's an important opportunity. It's important for our customers but we are very, very respectful of the risk. And so we're going to be very thoughtful about the nets that we keep on our balance sheet.

I'll also say an issue for the entire industry and for us is the modeling for cyber catastrophes needs to evolve. It's very early days for that. That's a significant priority for us and we work with some third-party partners to make sure that we're advancing the science for cyber catastrophe modeling.

Jay Gelb: So, it sounds like a great growth area for Travelers and at the same time, meaningfully addressing aggregate type of exposures from an overall basis and then obviously, on a per client basis gives reinsurance protection.

Alan Schnitzer: Exactly.

Jay Gelb: Okay. Good. Let's turn to the U.S. economy. Travelers is among the largest insurers of businesses in the U.S., which gives it unique insight into economic activity. Travelers generated over 5% growth in gross written premiums year to date, which includes the benefits of pricing, new business growth, and also business retention. What trends are you seeing in Travelers' business insurance customer base and are there any differences in those trends, say, among small, mid-sized and large businesses?

Alan Schnitzer: Let me start on the growth piece because we're very pleased with that. From 2008 to 2016, we grew at about 1.8% per year. From 2016 to 2018, we grew at about three times that rate, close to 5.5% per year. Part of that is the economy, as you mentioned, but part of that is initiatives that we've taken on.

We've said for a long time -- I said earlier this morning that our key measure for managing our company is return on equity, that is the key measure that is front and center for all of us. But we're also highly aware of the fact that you can't have a strategy to deliver leading returns unless you've got a strategy to grow over time. And at our last investor day we said as much, and we laid out a bunch of initiatives and we said these innovation initiatives are designed in large part to put us in a position to grow.

And it's really important to reflect it that way. Because you talk about growth in this industry. People reflexively think, gee, you're going to reduce price to grow or you're going to change your risk profile to grow. We don't want to do either of those things and we haven't done either of those things.

But we've put in place a number of initiatives across all of our businesses and functions to put us in a better position to grow when we think the opportunities are right for that. And the consequence of that and just do a lot a hustle and successful execution is that we've grown again 2016 to 2018 at three times the rate of the prior bunch of years. So, we feel good about that.

But back to your question. The economy helps. That obviously shows up in our exposure and we don't -- as we look through business sizes, we don't see a lot of trends that -- a lot of distinction between the trends in small, medium or large businesses.

Jay Gelb: Okay. A lot of investors broadly sort of worry about where we are at this point in the economic expansion. Any signs of looming recession that you're seeing in your businesses, whether on the hiring front or anything around increases in property plant and equipment, insurable elements of that?

Alan Schnitzer: We've got a sub-4% unemployment rate. We've got wages growing. We've got the number of people looking for jobs growing. And so, I think we've got to be careful not to talk ourselves into a recession. Because there's a lot of signs out there that says the economy is in okay shape and continue to expand for a while. So I want to be careful that we don't talk ourselves into a recession here.

Jay Gelb: That makes a lot of sense. I'd expect declining interest rates to be at least somewhat of a drag on the company's recurring investment income. How much of a headwind might investors expect from that impact?

Alan Schnitzer: So net investment income has been a very reliable contributor to our results, as you know. And no change in our investment strategy. We're very consistent about it. And so, we don't change our stripes as a result of changing interest rate environment.

Our fixed income portfolio turns over reasonably slowly, and as you know, every quarter we give an outlook for our net investment income, at least from our fixed income and short-term investments. The outlook that we gave last quarter for the third quarter, there's no change in that outlook. What we said a quarter ago was that for the third quarter we would expect net investment income from our fixed investment portfolio and short-term investments to be about \$10 million to \$15 million higher than in the third quarter of 2018. We continue to believe that's going to be the case.

As you point out, the interest rates are lower today than they were when we gave that outlook. And so we'll recalibrate the fourth quarter and next year when we report earnings next quarter -- I mean next month, but it will have an impact.

Jay Gelb: Okay. I think that would be expected. On the key topic of mergers and acquisitions, how is Travelers approaching the potential for further industry consolidation both in terms of bolt-on as well as the potential for transformational deals?

Alan Schnitzer: M&A is always a tool that we've got available to create shareholder value and that's the way we think about it. What are the opportunities for us to create shareholder value through mergers and acquisitions? And we've been very consistent about the lens we apply to thinking about mergers and acquisitions.

We will do deals when we think it will improve our return profile, when it will lower volatility, or provide us with some other strategic capability. Having said that, we say all the time some of the best deals we've done are the deals we didn't do. And so we are very disciplined in the analysis and any deal of any significance that we did would have to make sense, first and foremost strategically, but also financially.

Now, more recently, and I don't think this is what you're asking about because I'm talking very small dollars, but we've made some very small investments in capabilities as we think about a very aggressive innovation agenda. So, we made an investment in a company called Carpe Data. It's just one great example. It's the next generation of predictive modeling and it's -- there are tools that we can use both in our underwriting and our claims handling, and things like that are exciting.

And so again, very small dollars but we've done some of that over the last year or so and we hope to do more of that.

Jay Gelb: That's great. Okay. Travelers' expense ratio was 29.9% in the first half. That improved 70 basis points year over year. Could the company's expense ratio continue to improve, taking into account ongoing investments in the business?

Alan Schnitzer: So, thanks for mentioning the 70 basis points and that's a great result but it's actually a slightly better story than that. When you look at 2008 to 2015, our expense ratio averaged 32% over that period. And that wasn't bad when you look across the industry in our mix of businesses. There was nothing wrong with a 32%.

But again, when we look at the forces of change, the way we need to respond, having identified productivity and efficiency as a strategic objective, we said in 2016 we've got to do better. And fast forward to the first half of 2019, our expense ratio as you mentioned was-sub 30%. So that's a two-point decrease, but as a percentage matter that's about a 7% improvement.

And so, we feel really good about that and we accomplish that by leveraging investments in technology and workflow to grow the business, while keeping our G&A expenses about flat. And that's what produced that result. And so that's a great result for us.

Your question, could it get better? Sure. It could get better. It continues to be a strategic priority for us. But I'll just remind you that it's not necessarily a lower expense ratio we're looking for. It's operational flexibility we're looking for. So, to the extent we can continue to optimize productivity and efficiency, that gives us the flexibility to take those dollars. We could either let it fall to the bottom line, we could continue to invest it in important strategic initiatives or to the extent we think we need to or want to, we could put it into pricing without compromising our return objectives.

Jay Gelb: Perfect. Okay. Let's switch gears to personal lines property casualty insurance, which is obviously coverage for vehicles and homes. And that has some different dynamics than commercial P&C. Travelers has substantially raised auto insurance rates, resulting in improved underwriting margins. At what point could the company refocus its efforts on increasing policies in force?

Alan Schnitzer: So, in the auto business, it's always a balance of profitability and growing. And if you look back just a couple of years, 2016, in the personal lines auto business, we had a \$4 billion book of business that was not meeting our return objectives. Fast forward to today. We've got a \$5 billion book of personal lines auto business that is meeting our expectation. So really great effort by the team to improve the profitability of that book and we feel good about it. And from here, we'll continue to make sure that we're balancing growth and profitability. And I would hope for some modest growth in policies in-force in the coming quarters.

Jay Gelb: It appears that insurers selling coverage directly to insureds, especially in auto insurance, are generating nearly all the industry's growth. Travelers' distribution is nearly all through independent agents. Can Travelers create profitable growth in personal lines P&C focused on that channel?

Alan Schnitzer: Yes, we think so. So, if you look back over the last four years or so, the independent agency channel has really held its own in terms of market share. And over that same period of time, we've increased our market share through that channel. So, we feel pretty good about that. In addition, Michael Klein and the group have a number of initiatives inside. We call it meet the customer where they are.

And this might surprise you but 25% of our personal insurance premium actually comes through alternative distribution. And we're investing in that and we're growing there. So, we feel good about that. And on top of that, we've got an aggressive product strategy. So, you think about the new home product we rolled out, Quantum Home 2.0. That's had a successful rollout and a number of other products we're investing in that we think have the opportunity to generate profitable growth. So we feel good about the trajectory of the personal lines business.

Jay Gelb: That's great. Can you talk a little bit more about alternative distribution and what that means?

Alan Schnitzer: Yes. So, we are investing and growing in our direct to consumer business. We've got an affinity business. We've got other partnerships and distribution initiatives that are -- that make up that called national accounts business.

Jay Gelb: Appreciate that. Travelers' robust capital management strategy has set a high bar for the rest of the insurance industry. Can you describe how Travelers approaches share buybacks and dividends?

Alan Schnitzer: Sure. Pretty straightforward. So, our objective is to maintain a level of capital to continue to be a strong double A credit and so that's where we start. Beyond there, every single dollar of capital that we generate we aspire to invest back in the business if we can do that and create shareholder value.

And so that could be through investing in things like Carpe Data that I mentioned. That could be investing in people, products, systems, technology. Or it could be maintaining more capital on the balance sheet for growth. So, the level of growth that we've had requires that we keep additional capital on the balance sheet. So that gets overlooked sometimes in modeling. So people should keep that in mind that the level of growth we had requires us to keep more capital on the balance sheet.

But when we can't deploy that capital in a way that we think is going to create shareholder value, we're going to give it back to shareholders. We feel as stewards of other people's money, that's the right way to treat it. And as we have, we're going to give it back through a combination of dividends and share buybacks.

We started our share buyback program in 2006 and since 2006, I'm always happy to point this out, we've returned something like \$44 billion of capital through dividends and share repurchases. And share repurchases that we've done, we've done at an average price per share of about \$66. So we think that our capital management strategy has created a lot of shareholder value.

Jay Gelb: Clearly that's a great result. With regard to supporting growth that you just mentioned, does that mean perhaps that perhaps Travelers would not return 100% of operating earnings a year going forward if you add up shareholder dividends and buybacks?

Alan Schnitzer: Yes, if you look carefully at our disclosures, we've never said that we're going to return 100% of our earnings. I know that the people reflectively go there as sort of a shorthand for the way we think about capital. And I think actually that distorts the modeling. And what we've said is it won't be more than income because there are other uses of capital, whether it's pension contributions, or investments or in this case keeping capital on the balance sheet to grow. So, the level of growth will impact the capital we have to return.

And we think that's the right trade. We think if we can grow at returns that meet our objectives we think that's what we ought to be doing with the capital. But again, we're very disciplined stewards of that money. If we don't think we can deploy it in a business in a way that creates shareholder value, we're going to give it back.

Jay Gelb: Absolutely. Let's turn to the audience response system. So, the way this works is you each have a controller in front of you and we're going to ask a question and you can key in your response and then we'll immediately get the readouts from people. So, we can start the clock now. And this question is if you don't currently own shares of Travelers or happen to be underweight, what would cause you to change your mind?

And the outcome here, somewhat evenly split. We've got around a third saying a lower valuation. I know you don't want that.

Alan Schnitzer: I'm not going to help.

Jay Gelb: Second would be a return -- improved return on equity and then perhaps tighter property casualty market. Any thoughts around that, Alan?

Alan Schnitzer: Just that when it comes to lower valuation, we don't intend to help.

Jay Gelb: I think we talked about a lot of those factors as well. Clearly, the property casualty market is tightening so that could be a benefit. Next question please. This question is on -- we can start the clock -- the question is on operating return on equity. As I mentioned, 11% in the first half of 2019, including the impact of cat losses and 13% since 2005. And here, we'll get investors' expectations of what they expect over the next several years.

So around three-quarter saying between 10% to 12%. Decent baseline, right.

Alan Schnitzer: We give an outlook for margins in our 10-Q every quarter. I'm not going to go further than that and comment on this. But given where, again, we talked about the ten-year treasury being at, you know, 1.6% this morning. That's not so surprising.

Jay Gelb: Next question please. So, this is a question that often comes up with regard to investors with regard to the underlying combined ratio, which was 93% in the first half and we're looking for investors' directional expectations over the next few years, whether they expect it to improve, not change or perhaps deteriorate.

Around half are expecting modest improvement in the underlying combined ratio over the next several years. A quarter saying no change and also a quarter saying modest deterioration. Given some of the factors we talked about today and I believe this is also something the company provides some outlook on in its quarterlies and annuals. Any perspectives around that?

Alan Schnitzer: I'm going to let our 10-Q speak for itself. We give some qualitative outlook on underlying margins by business segment in our 10-Q. We update that every quarter. Sometimes we get it right. Sometimes a little better, sometimes a little worse. But we give you the best look that we have.

Jay Gelb: With probably some pressure in 3Q as you mentioned.

Alan Schnitzer: Yes.

Jay Gelb: Okay. Next question please. Alright, so, this one is on acquisitions. And we can start the clock. This question is should Travelers target a major acquisition in the property casualty industry, if it would not be substantially dilutive to tangible book value and also expected to quickly be accretive to earnings per share and return on equity. The feedback from the audience is decidedly --

Alan Schnitzer: Everybody is decisive.

Jay Gelb: That's right. Half saying yes and half saying no. You talked a little bit about --

Alan Schnitzer: I agree by the way.

Jay Gelb: And so, you've talked about what the factors you take into account in terms of looking at major acquisitions. Travelers probably going back to the St. Paul deal in I believe 2003 probably --

Alan Schnitzer: 2004.

Jay Gelb: 2004 -- hasn't done a major acquisition since then. Is it something that's on your list of possibilities?

Alan Schnitzer: I think it has to be. I think our shareholders should demand that we've got a perspective on transactions that we'd like to do and on what terms we'd like to get them done, and that we try to do that. So, we think we're pretty good at it. We think we're pretty good at finding them, assessing them, doing the diligence. We think we could do it. But there aren't really significant gaps in our platform or our strategy.

And so, I don't feel a sense of urgency to do anything other than to continue just day by day managing this business successfully.

Jay Gelb: Right, of course. That makes a lot of sense. We've got a couple minutes for questions from the audience if there are any.

Unidentified Audience Member: Hi, thanks. You said if I recall that you operate your business in the context of double A ratings at the OpCo. That's the framework you set up for capital management. That's correct?

Alan Schnitzer: That's correct.

Unidentified Audience Member: Okay. And so far, your capital structure has been fairly uncomplicated. It's been fairly straightforward. Senior debt, you run debt to cap ratio of X and that's how it works. There's been no use of capital securities or securities that get equity rating or bucket treatment by agencies to manage that rating. Do you expect that to -- should we expect that to continue to be the case or is -- given where rates are, and where structure is, and differences in benchmark rates, should we expect any change in that strategy or not?

Alan Schnitzer: What I can tell you is that you could and should expect that we're very thoughtful about how we put our balance sheet together. We've got a steady stream of people that are coming through our office trying to sell us on one thing or another, and you should assume that we're very good listeners. We evaluate those and try to figure out whether there's a way to lower our cost of capital.

If we could lower our cost of capital in a way we thought made sense, we would absolutely do it. Having said all of that, we really like having a very simple balance sheet. Having a simple fortress balance sheet in this business is a very good place to be and we've all been through periods of time when we've appreciated the simplicity and strength of the balance sheet. And so that's a priority too.

And so, I can't say that we won't take advantage of any of those opportunities if we saw a good one and we would. So nobody should write down they're not going to do it. But we think about priorities simple as a priority.

Unidentified Audience Member: Okay. And so far, the structure you've seen -- so far, the structures you've seen don't lower your cost of capital in your view. There's nothing that's attractive to you that's been propped in terms of helping your cost of capital. Is that a fair thing to say based on what you just told us?

Alan Schnitzer: I'm hesitant to go too far down that road and lead you to a definitive conclusion one way or another. So, I'm going to resist doing it. All I'll say is we haven't seen anything relative to the complexity so far that in the circumstances made sense for us. Whether things will change, I don't know for sure, but you should know that we look at it. We take our cost of capital very seriously and we like simplicity.

I'm sorry the answer is not completely satisfying yet, but I'm hesitant to give a definitive answer.

Jay Gelb: Excellent. I'm afraid we're out of time. But please join me in thanking Alan Schnitzer from Travelers. Great job again today.

Alan Schnitzer: Nice to be here. Thank you, Jay. Excellent.

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Explanatory Note

Forward-Looking Statements and Non-GAAP Financial Measures:

This transcript contains certain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, may be forward-looking statements. Words such as "may," "will," "should," "likely," "anticipates," "expects," "intends," "plans," "projects," "believes," "estimates" and similar expressions are used to identify these forward-looking statements. These statements are likely to relate to, among other things, our outlook, our future results of operations and financial condition (including, among other things, anticipated premium volume, premium rates, renewal premium changes, underwriting margins and underlying underwriting margins, net and core income, investment income and performance, loss costs, return on equity, core return on equity and expected current returns, and combined ratios and underlying combined ratios), our share repurchase plans, the sufficiency of our reserves, the impact of emerging claims issues as well as other insurance and non-insurance litigation, the cost and availability of reinsurance coverage, catastrophe losses, the impact of investment (including changes in interest rates), economic (including inflation, changes in tax law, changes in commodity prices and fluctuations in foreign currency exchange rates) and underwriting market conditions, strategic and operational initiatives to improve growth, profitability and competitiveness, the Company's competitive advantages, new product offerings, the impact of new or potential regulations imposed or to be imposed by the United States or other nations, including tariffs or other barriers to international trade, and the impact of legislation enacted or to be enacted by states.

The Company cautions investors that such statements are subject to risks and uncertainties, many of which are difficult to predict and generally beyond the Company's control, that could cause actual results to differ materially from those expressed in, or implied or projected by, the forward-looking information and statements. Some of the factors that could cause actual results to differ include, but are not limited to, the following:

- catastrophe losses could materially and adversely affect the Company's results of operations, its financial position and/or liquidity, and could adversely impact the Company's ratings, the Company's ability to raise capital and the availability and cost of reinsurance;

- if actual claims exceed the Company's claims and claim adjustment expense reserves, or if changes in the estimated level of claims and claim adjustment expense reserves are necessary, including as a result of, among other things, changes in the legal, regulatory and economic environments in which the Company operates, the Company's financial results could be materially and adversely affected;
- during or following a period of financial market disruption or an economic downturn, the Company's business could be materially and adversely affected;
- the Company's investment portfolio is subject to credit and interest rate risk, and may suffer reduced or low returns or material realized or unrealized losses;
- the Company's business could be harmed because of its potential exposure to asbestos and environmental claims and related litigation;
- the intense competition that the Company faces, and the impact of innovation, technological change and changing customer preferences on the insurance industry and the markets in which it operates, could harm its ability to maintain or increase its business volumes and its profitability;
- disruptions to the Company's relationships with its independent agents and brokers or the Company's inability to manage effectively a changing distribution landscape could adversely affect the Company;
- the Company is exposed to, and may face adverse developments involving, mass tort claims such as those relating to exposure to potentially harmful products or substances;
- the effects of emerging claim and coverage issues on the Company's business are uncertain;
- the Company may not be able to collect all amounts due to it from reinsurers, reinsurance coverage may not be available to the Company in the future at commercially reasonable rates or at all and we are exposed to credit risk related to our structured settlements;
- the Company is also exposed to credit risk in certain of its insurance operations and with respect to certain guarantee or indemnification arrangements that we have with third parties;
- within the United States, the Company's businesses are heavily regulated by the states in which it conducts business, including licensing, market conduct and financial supervision, and changes in regulation may reduce the Company's profitability and limit its growth;
- a downgrade in the Company's claims-paying and financial strength ratings could adversely impact the Company's business volumes, adversely impact the Company's ability to access the capital markets and increase the Company's borrowing costs;
- the inability of the Company's insurance subsidiaries to pay dividends to the Company's holding company in sufficient amounts would harm the Company's ability to meet its obligations, pay future shareholder dividends and/or make future share repurchases;
- the Company's efforts to develop new products, expand in targeted markets or improve business processes and workflows may not be successful and may create enhanced risks;
- the Company may be adversely affected if its pricing and capital models provide materially different indications than actual results;
- the Company's business success and profitability depend, in part, on effective information technology systems and on continuing to develop and implement improvements in technology, particularly as its business processes become more digital;
- if the Company experiences difficulties with technology, data and network security (including as a result of cyber attacks), outsourcing relationships or cloud-based technology, the Company's ability to conduct its business could be negatively impacted;
- the Company is also subject to a number of additional risks associated with its business outside the United States, such as foreign currency exchange fluctuations (including with respect to the valuation of the Company's foreign investments and interests in joint ventures) and restrictive regulations as well as the risks and uncertainties associated with the United Kingdom's withdrawal from the European Union;

- regulatory changes outside of the United States, including in Canada, the United Kingdom, the Republic of Ireland and the European Union, could adversely impact the Company's results of operations and limit its growth;
- loss of or significant restrictions on the use of particular types of underwriting criteria, such as credit scoring, or other data or methodologies, in the pricing and underwriting of the Company's products could reduce the Company's future profitability;
- acquisitions and integration of acquired businesses may result in operating difficulties and other unintended consequences;
- the Company could be adversely affected if its controls designed to ensure compliance with guidelines, policies and legal and regulatory standards are not effective;
- the Company's businesses may be adversely affected if it is unable to hire and retain qualified employees;
- intellectual property is important to the Company's business, and the Company may be unable to protect and enforce its own intellectual property or the Company may be subject to claims for infringing the intellectual property of others;
- changes in federal regulation could impose significant burdens on the Company and otherwise adversely impact the Company's results;
- changes in U.S. tax laws or in the tax laws of other jurisdictions in which the Company operates could adversely impact the Company; and
- the Company's share repurchase plans depend on a variety of factors, including the Company's financial position, earnings, share price, catastrophe losses, maintaining capital levels commensurate with the Company's desired ratings from independent rating agencies, changes in levels of written premiums, funding of the Company's qualified pension plan, capital requirements of the Company's operating subsidiaries, legal requirements, regulatory constraints, other investment opportunities (including mergers and acquisitions and related financings), market conditions and other factors.

For a more detailed discussion of these factors, see the information under "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our most recent Form 10-K, filed on February 14, 2019, as updated by our subsequent periodic filings with the Securities and Exchange Commission ("SEC"), which are accessible on the SEC's website (www.sec.gov). Our forward-looking statements speak only as of the date of this presentation or as of the date they are made, and we undertake no obligation to update those statements.

Also, this transcript includes some non-GAAP financial measures. Reconciliations to the most comparable GAAP measures are included in our recent earnings press releases, financial supplements, and other materials available in the Investors section on our website (www.travelers.com). A glossary of financial measures is included in our 10-K.