September 4, 2023

THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

Volume CCVIII Number 5

Published biweekly

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Latest Comments

"I still see a softer landing from an economic perspective, even though we're contracting. But inflation is trending down. So the need for the Fed to raise interest rates is no longer there."

Joseph Rinaldi, Quantum Financial Advisors

"If you think about it, it takes more work to become a confident investor in a small- or micro-cap name than it does in a big one."

P. Ross Taylor III, ARS Investment Partners

"We are long-term bulls on sustainability. It makes all the sense in the world for investors to incorporate sustainability insights into company analysis."

Nathan Moser, Impax Asset Management

Investing Strategies

In this issue of *The Wall Street Transcript*, seasoned money managers discuss navigating today's uncertain market and playing the trends for the longer term.

Joseph Rinaldi is President and CEO at Quantum Financial Advisors.

"Utility stocks offer a high dividend at this juncture. And anytime you can earn 5% qualified dividends, which are more tax-friendly than regular CDs or bonds, it's a great place to be. And if you look at the utility sector, stocks have come down quite a bit; some of them are close to their 52-week low.

"We are enamored with Duke Energy. That's a five-star utility that has performed very well. And we've been adding in the high-$80s, offering a dividend close to 5%. We also like FirstEnergy for the same reason. And Dominion Energy, which is a great add at this juncture; their dividend yield is over 5%."

P. Ross Taylor III is a Partner with ARS Investment Partners.

"In our small-cap area, we own shares in a company called Perma-Fix. It's basically a nuclear cleanup company. They actually have a business with the Hanford nuclear reservation, probably the most polluted place in the western world. The government's been looking at cleaning up for decades, but Perma-Fix has a unique capability to pull low level nuclear waste out of water.

"We look at that as a company that's trading now around $12. We think from that one project the company will earn a run rate of $3 a share a year, and it will grow from just that one project.

"We have a micro-cap name in the defense space, TechPrecision. They make key components for attack and ballistic submarines, as well as for certain aircraft programs.

"It's a $7, $7.50 stock. In our math, we go, 'OK, it's a micro-cap.' But we see where they can earn $1.50 to $1.80 a share run rate in free cash flow, when the DoD gets these submarine programs up."

Nathan Moser, CFA, is a Senior Portfolio Manager at Impax Asset Management.

"I think health care companies are well-positioned to act defensively.

"And what's nice about this space is depending on the investor appetite, there are defensive-type names in the space that are on the pharmaceutical or health care service side, and then if you want to play offense, you can do that through biotech, specialty pharmaceutical or medical devices.

"One of those companies helping reduce the potential for opioid addiction is a small-cap medical device company called SI-BONE. They've developed a solution to lower back pain that originates in the sacroiliac joint ... they're starting to catch fire with converting doctors to use their devices."

that they've already placed with us, and then finally, improve the premium audit process for their customers.

"Good news now is, the tides have turned, and over the past 18 months, the sharp increase that we've seen in interest rates has really improved our investment income to the point that our first quarter of 2023 investment income was $28 million, and that was the highest of any other quarter in our history as a publicly traded company."

The payroll providers I mentioned earlier, like ADP and Paychex, for example, are a significant segment of our business. We partner with the largest payroll providers in the U.S., and those companies sell our insurance products along with their payroll and accounting services through their own insurance agencies and field sales staff. We're always looking to grow those partnerships, find new partnerships and invest in that segment.

We also have a specialty segment of our business where select insurance agencies who possess deep expertise in specialized industries will market and sell our insurance products to businesses, and those are businesses that generally fall outside of our traditional appetite such as senior care and parcel delivery. Like payroll, we're always looking at new opportunities to expand our specialty segment.

And then, we also have a rapidly growing segment of customers that connect to us via our proprietary API to submit and quote and bind policies, so these are strategic partnerships with digital marketplace platforms as well as digital retail and wholesale agencies. And we refer to that segment as our alternative distribution channel.

An industry shift is currently occurring with more agents moving to digital marketplace platforms and so forth.

And then finally to address the changing buying behavior of small and micro businesses, I mentioned that we launched our Cerity brand to offer digital insurance solutions including direct-to-consumer coverage. We want to continue to make that process more and more efficient, and so integrating the Cerity brand more with the back-end services Employers offers will be important over the next couple of years.

While investing in our distribution is important, I also mentioned claims handling, which we feel is another big differentiator for us and where we want to invest. Workers' compensation exists to protect businesses and their injured employees, and we really take pride in the fact that we provide a superior claims handling experience when an employee is injured on the job.

We collaborate closely with the injured employee, their treating physician, and the employer to reduce the amount of time that an employee is out of work when they've been injured.

Through our extensive managed care network, by partnering thoughtfully with selected health care providers and expert physicians, nurses, claims professionals and so forth, to provide quality and cost appropriate and timely care, we minimize the downtime for the injured worker. That not only boosts the morale of the employee, it also reduces claim costs, which can negatively impact small businesses.

So by investing in the claims area we can continue to provide superior care and make it more efficient for everyone involved in the claims process to get those employees back to work, as quickly as possible.

I mentioned we are also investing in premium audit. We've identified that as a huge pain point especially for small businesses. And so we're trying to automate and streamline the process, so small businesses can get through it very quickly and in a less painful way than how insurance companies have historically managed that process.

And then finally on the customer service side, we feel like there's still a lot we can do to optimize our call center efforts and internally improve our workforce experience, which will then in turn improve our customer experience. So our automation efforts will seamlessly connect all the departments at Employers so that we can process policies, endorsements, audits, you name it, quickly and efficiently and take any pain points out of the process for our agents and injured workers.

TWST: Are your customers as a clientele, as a whole, still concerned about the economy — specifically about a recession?

Ms. Antonello: I think fears of a recession have subsided somewhat. Small businesses were significantly impacted during the pandemic and I've always felt like recessions can be very different in the sectors that they impact, right? And so, I think if we were to have a recession, it depends on what type of a recession it is and what sectors of the economy are most impacted.

Because we focus on small businesses — like I've said before, restaurants, hospitality — they can have an oversized impact or they can be not impacted quite so much. So, if a recession presents itself, I'm hopeful that it would not impact small businesses because they were hit so hard during the pandemic.

TWST: Have you been impacted by interest rates?

Ms. Antonello: Yes, we have been impacted by interest rates. In fact, it has been both a challenge and an opportunity in recent years. I'm going back 10 years, a dozen years, the prolonged low interest rate environment had a large effect on us.

The two primary sources of income for insurance companies are underwriting profits and investment income, and the low interest rate environment and the yields that endured for many, many years really did limit the investment income opportunities, not just for us, but for all insurance companies.

But we and other well-run insurance companies recognized the need to focus our energies during that period on underwriting profits. And we did not, and will never, attempt to grow our market share by reducing prices well below those of our competitors. So, like I said, during the prolonged low interest rate environment, we focused on underwriting.

Good news now is, the tides have turned, and over the past 18 months, the sharp increase that we've seen in interest rates has really improved our investment income to the point that our first quarter of 2023 investment income was $28 million, and that was the highest of any other quarter in our history as a publicly traded company. So it is nice to see investment returns coming back.

We're still very much focused on underwriting profitability. But investment income is a tailwind for us now. There's the flip side to the rising interest rates and yields which has also had an impact on us. The bolstered investment income has come at the expense of some unrealized fixed income losses on our balance sheet, even though those losses are temporary in nature and unwind over time if they're ultimately held to maturity which is often the case.

TWST: Is there anything that you wanted to mention that we haven't discussed?

Ms. Antonello: Yes. I would in closing reiterate that in 2022, we wrote over $700 million of workers' compensation premiums, and that was the third-highest amount in our history as a publicly traded company. We currently expect to write more premiums in 2023 than any other year.

I talked a bit about our key operating metrics in recent years and the improvement that we're seeing there. We're confident that improvement will continue. I'm also confident that the expense improvement that investors have seen over the last few years will continue because, as I said, now our efforts are shifting so that we can achieve scale through automation.

Most of our departments continue to work from home very effectively, which has allowed us to reduce our real estate footprint. Those savings are going to be realized in our financials over the next year or so, and our willingness to allow employees to work from home is one reason we're able to attract and retain exceptional talent from across the country, so that's been a real positive for us.

I mentioned we pride ourselves in our prudent claims handling and our disciplined loss reserving philosophy is another thing I want to mention. We've experienced net favorable loss reserve development in every calendar year since 2015.

And then, I'd also want investors to know that we're building technology and analytics capabilities to support our future growth initiatives and provide us with greater pricing precision and flexibility and promote long-term value creation for our shareholders.

I'll just end with saying we believe that we're an undervalued gem. Our company is strong, it's successful and opportunistic, and our current market value does not reflect our recent successes or our near-term outlook or our long-term potential.

And as a result we're a big proponent of share repurchases, and have reduced our shares outstanding from 33 million shares at the end of 2008 to just 26 million today. So that's a reduction of more than 20%.

So again, we truly believe we're an undervalued gem and we're very, very bullish about the future of the company.

TWST: Thank you. (CJ)

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THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

Founded 1963

Founder Richard A. Holman

Volume CCVIII Number 5

(ISSN0043-0102)

Publisher

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Editorial

Managing Editor

Judy Lessin

Sales & Marketing

(212) 952-7400

Published by

Wall Street Transcript Corporation

622 3rd Ave, 34th Floor

New York, NY 10017

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The Wall Street Transcript (ISSN 0043-0102) is published bi-weekly for $1890 per year by Wall Street Transcript Corporation, 622 3rd Ave, 34th Floor, New York, NY 10017. Periodicals postage paid at New York, NY, and additional mailing offices. POSTMASTER: Send address changes to The Wall Street Transcript, 622 3rd Ave, 34th Floor, New York, NY 10017.

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