United Fire Group, Inc.

Fourth Quarter Earnings Conference Call

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CORPORATE PARTICIPANTS

Randy Patten – *Director of SEC Reporting and Investor Relations*

Randy Ramlo – *Chief Executive Officer*

Michael Wilkins – *Chief Operating Officer*

Dawn Jaffray – *Chief Financial Officer*

PRESENTATION

Operator
Good day and welcome to the United Fire Group 2015 Fourth Quarter and Year End Financial Results Conference Call and Webcast. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star then one on a touchtone phone. To withdraw your question, please press star then two. Please note this event is being recorded.

I would now like to turn the conference call over to Mr. Randy Patten, Director of SEC Reporting and Investor Relations. Mr. Patten, the floor is yours, sir.

Randy Patten
Thank you. Good morning, everyone, and thank you for joining this call. Earlier today, we issued a news release on our results. To find a copy of this document, please visit our website at www.unitedfiregroup.com. Press releases and slides are located under the "Investor Relations" tab.

Our speakers today are Chief Executive Officer, Randy Ramlo; Michael Wilkins, our Chief Operating Officer; and Dawn Jaffray, Chief Financial Officer.

Please note that our presentation today may include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. The company cautions investors that any forward-looking statements include risks and uncertainties and are not a guarantee of future performance. These forward-looking statements are based on management's current expectations and we assume no obligation to update them. The actual results may differ materially due to a variety of factors, which are described in our press release and SEC filings.

Please also note that in our discussion today, we may use some non-GAAP financial measures. Reconciliations of these measures to the most comparable GAAP measures are also available in our press release and SEC filings.

At this time, I'm pleased to present Mr. Randy Ramlo, Chief Executive Officer of United Fire Group.

Randy Ramlo
Thanks, Randy. Good morning, everyone, and welcome to UFG Insurance 2015 fourth quarter and year end conference call. It is my pleasure to report 2015 was a strong year for UFG. Our current and long-term 2020 vision goals we first communicated in 2014, including increasing ROE and written premium, providing best-in-class service, and being a best place to work, continue to take hold as shown both by our progress and profitable performance.

For the 2015 year, operating income was $3.46 per share, net income was $3.53 per share and our GAAP combined ratio was 92%. This compares with operating income of $2.13 per share, net income of $2.32 per share and a GAAP combined ratio of 97.8% for 2014.

We are reporting year-over-year improvement in operating earnings and net income of $1.33 per share and $1.21 per share respectively and 5.8 points of improvement on the combined ratio.

For the full year of 2015, we reported a solid return on equity of 10.5% compared with 7.4% in 2014, in spite of reduced investment returns and lower level of earnings from our Life segment. We closed 2015 with a book value of $34.94 per share, up from $32.67 per share at the end of 2014.

In the Property and Casualty segment, we benefited throughout the year from modest rate increases, a lower base of catastrophic events, favorable claims activity and favorable reserve development on our prior accident years. I'll let Mike address more specifics with respect to P&C market conditions and performance in a few moments.

For the first time in UFG history, we reached a $1 billion in total revenue, thanks to the hard work and dedication of our employees and agents, the continued execution of our strategic plan, and the loyalty of our customers. This milestone included an 11.7% year-over-year increase in written premium, driven by organic growth and rate increases.

It might be suggested that our strong premium growth within the current competitive marketplace might be leading to adverse selection. We believe it is our focus on the actions in support of our 2020 vision that our key to our organic growth. Our approach to continuing into 2016 remains steadfast focused on executing our strategic initiatives, including expanding our geographic footprints and agency plans and penetration, and leveraging expansion of our product portfolio, while maintaining true to our core underwriting discipline in the diminishing rate environment.

For specifics in terms of growing our book of business profitably, we continue to pursue more association business and to expand our product offerings, including organically building the specialty business. As we discussed in the third quarter, we exceeded our original target of between $15 million and $17 million in specialty lines and ended 2015 with $21.2 million in written premium. We are targeting additional opportunities in growing small business products, including expanding our service center. These are generally accounts with less than $10,000 in premium and include a complete package.

We have expanded our West Coast business utilizing United Fire and Casualty products. We added $1 million in new business premium associated with our geographic expansion into the state of Ohio, despite not writing new business there until August 1st. We anticipate more premium growth from geographic expansion on the horizon.

In this business, the value of sustaining long-term profitability, agency and customer relationship can't be understated. We value our partnerships with our agency force in growing our business in geographic regions and target product lines that we seek. We meet with a council of agents throughout the country for regular feedback so we can understand how we can continue to improve or evolve our product offerings and service. We listen and we follow through.

Along with geographic expansion, our strategy includes pursing new agency appointments to achieve our goals where appropriate. We still, however, will sever our ties when we don't believe our profitability goals are achievable within a reasonable timeframe.

Our 2015 property and casualty loss and loss adjustment expense ratio was 61% compared to 66.5% in 2014. Along with disciplined underwriting, our investment in loss control has yielded positive results in strengthening our customer relationships and claims experience, another factor indicative of our loss ratio improvement. We believe these investments of time and resources are key factors in minimizing frequency and severity of losses, as well as offering our customers the opportunity to hold the line on escalating insurance costs and minimizing disruption.

Moving on to our Life segment, for the fourth quarter we reported a small net loss as compared to a $2 million of net income of $0.08 per share in the fourth quarter of 2014. For the full year, the Life segment reported net income of $4 million or $0.15 per share, compared to $7 million or $0.27 per share in 2014.

As we have reported all year, the low interest rate environment and a lower asset base due to declining deferred annuity deposits has impacted our investment returns in this segment. We are not chasing production and continue to appropriately price our annuity products, while not creating a long-term disadvantage when interest rates improve. During 2015, with the actions we have taken, we have increased our annuity spreads by 32 basis points. We will continue to deploy excess capital from the Life business to support the expansion of the Property and Casualty business as appropriate.

Strategically, we have implemented various initiatives targeting growth in traditional Life business, including expanding product offerings such as our graded benefit whole life and qualified care rider, as mentioned in prior quarters. During the fourth quarter, we had strong sales of our single premium whole life policies, contributing 54.1% of the increase in premiums earned and 29% for the full year of 2015 compared to the same period in 2014.

We are not satisfied with our performance and continue to look for areas where we might expand our products, territories and agencies along with managing expenses and improving productivity to strengthen profitability in this segment.

With that, I'll turn it over to our Chief Operating Officer, Mike Wilkins.

Mike Wilkins
Thanks, Randy, and good morning, everyone. During the fourth quarter, competitive market conditions continued for both renewals and new business and are accelerating. We've seen some early stage aggressive rate quotes by competitors on larger new business accounts where the differential to what UFG would deem reasonable is significant.

Commercial lines renewal pricing has varied by region with average percentage increases in the low-single digits on most small and mid-market accounts. Larger accounts remain more competitive, with flat to small percentage decreases prevailing for best-in-class risks.

Improved industry results in the property line has made it more challenging to obtain increases. We pushed and obtained higherlevel rate increases on the commercial auto line of business, as a result of deteriorating loss experienced industry-wide.

We continue to increase pricing and/or non-renew accounts with loss issues, including the lowest performing accounts. Albeit diminishing, this is the 17th consecutive quarter of commercial lines pricing increases on our overall book of business.

We continue to believe lost cost trends will remain at low levels and the margin between loss cost and rate increases will narrow. We currently believe loss cost trends are approximately 3%, earned premium growth should continue to outpace loss cost trends during 2016, as rate increases achieved over the past several quarters earn out.

Personal lines renewal pricing has averaged percentage increases in the low to mid-single digits. Premiums written from new business declined from the third quarter; however they increased compared to the fourth quarter of 2014.

Our success ratio on quoted accounts remains unchanged and is at an acceptable level with the most success in accounts with premiums less than $25,000. Premium and policy retention have remained strong and holding at 85% and 83% respectively consistent with third quarter experience.

The US economy continues to experience slow growth. Premiums from endorsements and premium audit continue its positive trends, up from the third quarter and when compared to the fourth quarter of 2014.

During the fourth quarter, property and casualty premiums written increased 10.3%; 2.7% is attributed to new business, 4% is attributed to endorsements, and 3.6% is attributed to rate change and exposure increases.

Randy mentioned though we had terrific success building our specialty business during 2015, as competition heats up, standard markets may become more willing to write this business at standard line pricing. We will carefully monitor pricing in this segment and remain true to our underwriting fundamentals, including our focus on competing on service more than price, should competition erode margins. We believe opportunities remain at this time in this segment, but we will remain vigilant.

We are proactively targeting growth in the small business owner product segment. These accounts generally have less than $10,000 in premium and include a complete insurance package. We are further expanding our service center to capitalize on this area of business growth, with expanding automation to allow us the opportunity to more efficiently underwrite these products.

We are looking to continue to grow our personal lines business, which remains profitable. In 2015, the personal lines net loss ratio improved 21.3 percentage points compared to 2014. The change was primarily due to a decrease in net losses incurred in the fire and allied lines of business and to less catastrophe losses in 2015.

In addition to our earthquake, hurricane and storm mapping tools, we have implemented predictive analytics and data prefill for our personal automobile line. Data prefill is a data accessing methodology that allows for a more complete profile of our customers at the agent's point of sale during a quotation process.

Catastrophe losses for the fourth quarter and for the full year were less than we would normally expect. Pretax catastrophe losses for the quarter totaled $5 million or $0.13 per share after-tax compared to the $2.5 million or $0.06 per share after-tax for 2014.

For the full year 2015, our pretax catastrophe losses were $32.3 million, compared with $49.7 million. For the fourth quarter and full year of 2015, catastrophe losses added 2.2 percentage points and 3.8 percentage points respectively to the combined ratio. Our expectations for catastrophe losses in any given year are approximately 6 percentage points on the combined ratio.

During 2015 our catastrophe losses included 37 catastrophes or our largest single pretax catastrophe loss totaled $4 million, in contrast to 2014, which had 26 catastrophe losses with the largest single pretax catastrophe loss totaling $7.7 million. We believe the combination of disciplined underwriting and the use of sophisticated mapping software to effectively manage our concentration of risk has helped us manage our exposure.

Although our aggregate commercial lines loss ratio for the full year of 2015 has improved by almost 5 points across all lines, we have experienced deterioration in commercial auto much like the industry for the full year 2015. Our 2015 commercial auto loss ratio has increased approximately seven points year-over-year. We continue to successfully push rates in this line of business as well as modify underwriting guidelines to address these trends.

Large losses, which we define as losses greater than $500,000, totaled $25.4 million in the fourth quarter. This compares to $16.1 million in the fourth quarter of 2014. Although disappointing, during the fourth quarter we had six more large loss claims than the fourth quarter of 2014, which added $8 million of losses year-over-year.

Full year 2015 large losses of $87.3 million remain within our expectations and are essentially flat when compared to 2014 at $83.2 million. I'll remind you that 2014 experience included several unusually large fire losses. As its very nature, we expect large losses to vary from quarter-to-quarter and year-to-year.

Frequency was up for the quarter, impacted by southern storm claims; however, year-to-date frequency was down significantly compared to the same period in 2014, due in part to reduced catastrophic storm losses. Severity for the year was essentially flat compared to 2014; however, the severity arose with liability lines versus property lines of business. With our underwriting initiative emphasizing reducing our hazard class exposure mix, we continue to see improvement in our workers' compensation line of business.

We provide many different metrics in our earnings release and in this conference call. If there is one thing we feel good about and want to emphasize, it is the core margin expansion that UFG achieved during 2015. Our core loss ratio excluding catastrophes and prior period reserve development improved 5.5 points. We are very proud of this and feel it is a reflection of the planning, execution and hard work of all our regions and all of our supporting departments.

Our accident year loss ratio has improved in every line except commercial automobile in 2015 and our overall accident year loss ratio improved over 8 points on a gross direct basis.

We track first year profitability on new business written in each year, and we saw improvement in the first year profitability of new business for the third consecutive year in 2015.

With that, I'll turn the financial discussion over to Dawn Jaffray.

Dawn Jaffray
Thanks, Mike, and good morning. Reinforcing what Randy and Mike have already stated, 2015 was a good year for UFG with respect to financial performance. Our stockholders' equity increased 7.5% to $879 million at December 31, 2015, from $817 million at December 31, 2014. Return on equity year-over-year, as we reported this morning in our press release, improved 3.1 percentage points.

Further adjusting ROE to exclude the impact of unrealized gains, our adjusted ROE was 12.6% as compared to 8.9% in 2014. For the fourth quarter, we reported consolidated net income, including net realized investment gains and losses of $30.9 million or $1.21 per share, compared to $34.8 million or $1.38 per share for fourth quarter 2014. For the full year, consolidated net income, including net realized investment gains and losses, was $89.1 million or $3.53 per share compared to $59.1 million or $2.32 per share in 2014.

As Randy and Mike covered the discussion on premium and elements of our losses, I'll provide more detail on the impact of loss development. Losses and loss settlement expenses increased by $13.8 million or 12.2% during the fourth quarter, compared to the fourth quarter of 2014 and $12.8 million or 2.4% for the full year.

As has been historicallyconsistent reserving practice for UFG, we are conservative in setting initial reserves. As a result, we often have favorable reserve adjustments that vary from year-to-year across our book of business. Favorable reserve development for the fourth quarter was $16.3 million compared to $24.2 million in the fourth quarter of 2014.

The impact on net income for the quarter in 2015 was $0.41 per share compared to $0.62 per share in 2014. For 2015, our quarterly favorable development impacts across our Property and Casualty segment mirrors the annual story, which I'll detail momentarily.

For the full year of 2015, the Property and Casualty segment experienced $40.4 million of favorable reserve development for prior accident years. Three lines accounted for the majority of the favorable development. The largest single contributors for favorable development were long-tail liability, with $23 million, followed by workers' compensation with $22.1 million, and auto physical damage, with $4.4 million.

The favorable development is attributable to reductions in reserves for reported claims, as well as reductions in IBNR combined with continued successful management of litigation expenses. The favorable development was partially offset by adverse developments, with the majority coming from three lines, which include property at $5.6 million, assumed reinsurance with $8.1 million and commercial auto liability with $2.8 million for the year ended December 31, 2015.

There were other miscellaneous amounts, favorable and adverse. However, no other single line of business contributed a significant portion of the total development. The improvement in our underlying book can be seen when we look at calculating an adjusted accident year loss ratio.

For the fourth quarter, by removing the impact of catastrophes at 2.2 percentage points for 2015 and 1.2 percentage points for 2014, the longest removing impact of favorable developments of 7.3 percentage points for 2015 and 11.9 percentage points for 2014, the quarterly loss and loss settlement expense ratio would be 58.8% versus 63%, resulting in a quarter-over-quarter improvement of 4.2 percentage points. On an earnings per share basis, this would translate to an adjusted earnings per share for the fourth quarter 2015 of $0.93 versus $0.78 for 2014.

Looking to the full year of 2015, likewise removing the impact of catastrophes at 3.8 percentage points and 6.5 percentage points for 2014, along with removing the impact of favorable development of 4.7 percentage points for 2015 and 7.4 percentage points for 2014, the annual loss and loss settlement expense ratio would be 61.9% versus 67.4% resulting in a year-over-year improvement of 5.5 percentage points. On an adjusted earnings per share basis for the full year 2015, this would translate to $3.25 versus a $1.95 for 2014.

Following Mike's comments with respect to catastrophes, our book of business remains primarily in regions of the country that are susceptible to seasonal weather, including winter and spring convective storms. As a result, I caution our listeners that we may experience volatility in our results from quarter-to-quarter and year-to-year. At December 31, 2015, our total reserves remained relatively flat and within our actual estimates.

Moving on to the expense ratio, the fourth quarter 2015 expense ratio was higher by 2 percentage points compared to the fourth quarter of 2014. Increases in various employee benefit costs, including pension amortization and profit sharing impacted the year-over-year comparison. For the full year, the expense ratio at 31 percentage points was flat as 31.3 percentage points in 2014. Due to the slight improvement in interest rates at year end 2015, our pension and post retirement benefit amortization in 2016 will be less than the amortization in 2015.

Consolidated net investment income was $26.6 million for the fourth quarter, which was a 3% decrease as compared to $27.4 million in the fourth quarter of 2014. For the year, consolidated net investment income was $100.1 million, a decrease of 4% as compared to net investment income of $104.6 million for 2014. The decreases are primarily due to lower reinvestment rates along with a lower invested asset base.

During the fourth quarter of 2015, in conjunction with our regular portfolio review of investment assets, we determined it was appropriate to record an other-than-temporary impairment of one energy and resource sector fixed maturity security. The impairment was $1.3 million pretax and impacted our Life segment results.

There were no material realized gains and losses for the quarter or year-to-date in 2015 or 2014 on our $3.2 billion base of investment assets. We continue to feel the impact of lower investment yields on the majority of our investment portfolio and we expect the continuation of low interest rates into 2016. The weighted average effective duration of our fixed maturity securities portfolio at December 31, 2015 was 5.2 years and our overall portfolio yield was 3.2%.

With respect to capital management, during the fourth quarter we declared and paid a $0.22 per share cash dividend to stockholders of record on December 1, 2015. For the full year, we declared and paid dividends of $22 million. We have paid a quarterly dividend every quarter since March of 1968.

Under our share repurchase program, we may purchase United Fire common stock from time to time on the open market or through privately negotiated transactions. The amount and timing of any purchases will be at management's discretion and will depend on a number of factors, including the share price, general economic and market conditions, and corporate and regulatory requirements.

During the fourth quarter, we did not repurchase any shares of our common stock. In the year ended December 31, 2015, we purchased 79,396 shares of our stock, common stock, for $2.4 million, at an average cost of $30.51 per share. We are authorized by our board of directors to purchase an additional 1,528,886 shares of common stock under our share repurchase program, which expires in August of 2016.

Subsequent to year end in February 2016, we entered into a new credit agreement with KeyBanc, which provides for a $50 million four year unsecured revolving credit facility. The new credit agreement also allows us to increase the aggregate amount of the commitment by up to $100 million.

Although UFG does not have any debt on our books currently, we felt having access to a line of credit for various corporate purposes is a prudent capital management decision. The terms of a new agreement provides for lower fees on the unused commitment amount, as well as access to an overall larger credit line.

And with that, I'll open the line for questions.

QUESTIONS AND ANSWERS

Operator
Thank you, ma'am. We will now go ahead and begin the question and answer session. To ask a question, you may press star then one on a touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you would like to withdraw your question, please press star then two. Again, that is star then one to ask a question. At this time, we will just pause momentarily to assemble our roster.

The first question we have comes from Paul Newsome of Sandler O'Neill. Please go ahead.

Paul Newsome
Good morning. Congratulations on the quarter and the year, folks.

Randy Ramlo
Thank you, Paul.

Paul Newsome
Is it possible for you, given what you have done with rate to date, that the combined ratio could actually improve in 2016?

Randy Ramlo
This is Randy, Paul. It's possible, I guess everything is possible. If you'll recall, we first got rate increases, I think, in the fourth quarter of 2011. And so by virtue of us getting rate increases, though very minimal, in the fourth quarter of 2015, those policyholders have had rate increases for quite a number of years. And it goes to say that possibly going forward we might still be able to continue with a little bit of rate increase.

Mike mentioned that commercial auto, we're still able to get some rate increases, some areas of the country with storm-susceptible property, we were able to get some rate increases. Some smaller accounts we're able to get some and personal lines we were still able to get some rate increases.

Rate increases on larger accounts have become very difficult. And so we had a pretty small overall rate increase in the fourth quarter even though it was positive. If our trends continue, we're probably going to move closer to flat. But even if we were to remain at this rate level for the rest of the year, we'd be very comfortable; our combined ratio would still be very good at the end of 2016.

Do you have anything to add, Mike?

Mike Wilkins
Yes. Paul, this is Mike. I think our expectation with the increases we received over the last four quarters would be that the earn premium as those increases earned through would roughly equal a low cost inflation, so from that perspective, maybe looking at a flat year, the wildcard, of course, is always the CAT losses, what's going to happen with CAT losses in the year. This past year, we had a pretty good CAT year. So if we have another CAT year like that, I think we could equal or improve our combined—CATs are higher obviously that could impact it the other way.

I do think we've done a lot of things to try to improve our CAT exposure, spread of risk, better reinsurance. With reinsurance being cheap, we've added a little cover and changed some things there that we think will be helpful. So we're optimistic again for 2016.

Paul Newsome
Fantastic. Congratulations, again.

Randy Ramlo
Alright. Thanks a lot, Paul.

Operator
As a reminder, if you'd like to participate in today's Q&A, please press star then one on a touchtone

phone. Again, that is star then one. Again, we will just pause momentarily to assemble our roster.

Again, that's star then one to ask a question.

CONCLUSION

Operator
At this time, we have no further questions. We'll go ahead and conclude the question and answer session. I would now like to turn the conference back over to Mr. Randy Patten for any closing remarks. Sir?

Randy Patten
That concludes our conference call. As a reminder, a transcript of the call will be available on the company website at www.unitedfiregroup.com. On behalf of the management of United Fire Group, I wish all of you a pleasant day.

Operator
And we thank you, sir, also for your time and to the rest of your management team. The conference call is now concluded. At this time, you may disconnect your lines.

Thank you, again, and have a great day, everyone.