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Liberty Mutual Holding Company Inc.

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S&P Global Market Intelligence Estimates**

Estimates data is not available for this transcript hence the table is not generated.

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David Henry Long
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Edward Jose Pena
Senior VP & Treasurer

Neeti Bhalla Johnson
Executive VP, President & Chief Investment Officer of Investments

Timothy Michael Sweeney
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Presentation

Operator

Good morning, ladies and gentlemen, and welcome to the Liberty Mutual Insurance Conference Call on its Fourth Quarter and Full Year 2020 Financial Results.

While this call is available online at the URL included in the Liberty Mutual Insurance press release, analysts should participate by phone in order to ask a question.

To begin Liberty Mutual's presentation is Ed Peña, Executive Vice President and Treasurer. Mr. Peña?

Edward Jose Pena
Senior VP & Treasurer

Good morning. And welcome to Liberty Mutual's Fourth Quarter and Full Year 2020 Earnings Call. Hopefully, you have seen the earnings release and the financial statements posted on our website.

David Long, Chairman and Chief Executive Officer of Liberty Mutual Insurance, will begin his opening remarks by speaking to the results in the quarter. Following David, you will hear from Tim Sweeney, President, Global Retail Markets; Dennis Langwell, President, Global Risk Solutions; Neeti Bhalla Johnson, Chief Investment Officer, on the results of their operations in the quarter.

Chris Peirce, Liberty's Chief Financial Officer, will conclude our prepared remarks with a review of our full year financial results. Also participating on today's call is Jim Kelleher, Chief Legal Officer.

Also, as a reminder, today's discussions may contain forward-looking statements that represent the company's beliefs concerning future operations, strategies, financial results and other developments. Actual results may differ materially from those expressed or implied. Please refer to our website for a complete discussion of the risk factors related to this presentation and the company. The company does not intend and does not undertake any obligation to update these forward-looking statements which speak only as of today's date.

I will now turn the call over to David for his opening remarks.

David Henry Long
Chairman, President & CEO

Thanks, Ed, and good morning, everybody. I'd first like to take a moment to reflect on what was an extraordinary year. COVID-19 had a profound effect on all of our lives, including the tragic loss of loved ones. And sadly, we were reminded that racial inequality remains embedded in our society. We must face both challenges head on as we move into 2021 and beyond. I'm proud to say, though, that the spirit of our employees has not wavered as they continued to work tirelessly to fulfill the promises we make to our customers.

We exist to help people embrace today and confidently pursue tomorrow. And I'd like to thank all our employees for their continued effort and for living our values at a time when our customers, partners and families needed us most.

For the fourth quarter, we reported net income attributable to LMHC of $162 million compared to a net loss of $301 million in 2019. The change versus the prior year quarter was driven by favorability in core underwriting results across both businesses and strong investment results reflected in realized gains of $415 million and income from our LP, LLC and other equity method investment portfolio of $494 million.

These drivers were partially offset by prior year strengthening and restructuring charges, both of which I'll discuss in more detail in a moment. Within GRS, we added an additional $115 million in losses related to COVID-19, and Dennis will discuss these shortly.

The industry continues to grapple with adverse loss trends in U.S. casualty lines. And as you may recall, we have economic protection under several adverse development covers with National Indemnity company which reduced reserve volatility in long tail lines. During the quarter, we strengthened reserves by $653 million, a portion of which is ceded to NICO under the ADCs.

The development in the quarter includes at $211 million for asbestos and environmental, following our annual review of these exposures, with the remaining balance primarily in casualty and general liability lines. While the market firming has been encouraging, more rate is still needed in these lines. That said, we do believe that written rate is exceeding trend, and we expect this will have a more meaningful positive impact as it earns its way through the book in 2021.

Last fall, the company announced a voluntary early retirement program. This opportunity enables eligible U.S. employees who are approaching retirement the chance to do so with added benefits while providing material run rate savings for the company. Pretax restructuring charges of $577 million related to this option were recognized in our fourth quarter results. This offering will allow us to manage costs across the organization, invest back in our business and create value for our policyholders.

Net written premium in the quarter was $10.1 billion, an increase of 3.5%. The growth in the quarter reflects meaningful rate increases in GRS as well as strong new business production and higher retention in U.S. personal lines, which is an area we're targeting for growth.

Additionally, the nonrenewal of a ceded reinsurance quota share at the beginning of 2020 within GRS contributed to the top line favorability. The combined ratio in the quarter was 101.9%, down from 106.7% in the fourth quarter of 2019. This reflects an improved core loss ratio, which decreased 5.8 points to 62.6%. Rate increases and lower loss activity within GRS, coupled with lower frequency and personal auto contributed to the favorability in the quarter.

We also booked 1.9 points of favorable reestimation in the quarter driven by U.S. auto liability in GRM as we recognized the lower frequency trends we've seen throughout the year. This compared with 1 point of unfavorable reestimation in the prior year quarter.

This favorability was offset by several factors: prior year strengthening contributed 6.4 points to the all-in combined ratio compared to 5.6 points in the prior year quarter; catastrophe losses contributed 3.5 points, up from 2.8 points; and COVID-19 losses contributed an additional 1.1 points.

Finally, the expense ratio in the quarter increased 1.3 points to 30.2%, driven by increased employee-related costs from a onetime benefit in Q4 2019 and increased variable expenses and advertising spend in GRM as we accelerate growth in this business. And Chris will provide color on the full year expense ratio and how we're thinking about expenses going forward.

Before I turn it over to Tim, I'd like to highlight the progress we've made towards the priorities we discussed at the beginning of the year. The investments we're making in growth within GRM resulted in over 6.5% TIF growth for the year in U.S. personal lines. Rate increases and re-underwriting efforts resulted in a 5.7 point improvement in the GRS full year core combined ratio.

And lastly, we're taking a handful of strategic actions, such as the early retirement program to drive operating efficiencies in the business. Building on this momentum, we feel we're well equipped to continue executing on these priorities in 2021.

I'll now turn it over to Tim for the discussion of GRM.

Timothy Michael Sweeney
Executive VP & President of Global Retail Markets

Thank you, David. Moving on to business results. Global Retail Markets' net written premium in the quarter was $6.7 billion, a decrease of $9 million or 0.1% from the prior year. The decline was driven by results in commercial auto, workers' compensation and commercial multi apparel within U.S. business lines as well as a risk appetite change in the West region. This was partially offset by strong homeowners and private passenger auto results in the U.S. Excluding the impact of foreign exchange, our net written premium increased by $30 million or 0.5%.

In the U.S., homeowners premium increased by 7.2%, driven by strong new business production and retention, which were up 23.6% and 0.2 points, respectively, versus the fourth quarter of 2019 resulting in an increase in policies in force of 6.7%.

We also ended the quarter with strong growth in private passenger auto premium in U.S. personal lines, which was up 3.9% from the same period in 2019. Auto policies in force increased by 6.5% as new business production increased by 25.9%.

Our growth in U.S. personal lines offset new business and retention shortfalls in our business lines portfolio, which were down 17% and 6.4 points, respectively. The business lines decline was driven by continued COVID-19 recessionary impacts in addition to pricing actions we continue to take in order to improve our long-term profitability.

In our international operations, our organic net written premium decreased by 7.5% in the West region and 11.4% in the East region, as we continue to experience the negative economic impacts from COVID-19.

Within the East region, 6.5 points of the decline was due to the sale of our Russian operations earlier in the year. Growth was also negatively impacted by the U.S. dollar strengthening relative to global currencies, most notably the Brazilian real.

GRM pretax operating income for the quarter was $815 million, an increase of $402 million versus the fourth quarter of 2019. This increase was primarily driven by lower frequency in noncatastrophe auto losses in the U.S. and West region as a result of fewer vehicle miles driven. Adding to the improvement was the reserve release on prior year catastrophes, partially offset by higher current accident year catastrophe losses due to an increase in severity and frequency compared to the prior year.

Turning to U.S. loss trends. In U.S. personal lines, collision frequency was down 15% to 20% in the fourth quarter. Miles driven have consistently stayed below pre-COVID levels, while roads continue to be less congested during commuting hours, leading to fewer accidents.

The low frequency was partially offset by an elevated severity trend, driven by a continued shift toward total loss claims and higher used car prices. While the value of used cars and trucks remained elevated, values have started to moderate.

Auto bodily injury frequency trends were also down in the fourth quarter, partially offset by elevated severity. Fatality rates were elevated and increased uninsured and underinsured motorist activity is putting upward pressure on loss trends. Delayed medical treatments and more pressure on medical costs are also expected to contribute to higher severity trends.

For GRM U.S. business lines, auto frequency remained low in the fourth quarter, partially offset by elevated severity trends, driven by the same pressures that we saw in personal lines.

General liability frequency remained low and slightly below pre-COVID levels driven by lower-than-typical foot traffic in continued social distancing, offset by higher severity trends.

Workers' compensation trends are expected to be higher in the near term due to elevated severity from increasing medical costs, the impact of delayed medical treatments, fewer jobs for workers to return to and a shift to a higher wage labor force.

The combined ratio in the quarter was 91.4%, a decline of 5.4 points from the prior year quarter, driven primarily by a reduction in noncatastrophe losses driven by lower auto frequency in the U.S. and West regions. The decrease was also driven by reserve releases in prior year catastrophe and noncatastrophe losses, offset by higher current year catastrophe losses.

Adding to the increase was our expense ratio which was 1.2 points higher, primarily driven by higher advertising spend and variable expenses in U.S. personal lines in support of our growth.

I'll now pass it off to Dennis to discuss GRS.

Dennis James Langwell
Executive VP & President of Global Risk Solutions

Thank you, Tim. Global Risk Solutions net written premium was $3.4 billion in the quarter, an increase of $353 million or 11.5% over the prior year primarily driven by our Liberty Specialty Markets segment as well as the nonrenewal of a quota share reinsurance agreement at the beginning of 2020. The aggregate renewal rate increased in the quarter, including terms and conditions changes, was 25% excluding workers' compensation, and 21% for all lines.

Liberty Specialty Markets net written premium was 14% higher than the prior year as renewal rates increased 24% in the quarter, well in excess of loss trends and reestimation of ultimate premium in certain classes of business contributed as well.

Retention was 10 points below the prior year due to re-underwriting and repositioning of the portfolio. GRS North America's net written premium declined 1.4% versus the prior year. Fourth quarter renewal rates, including changes in terms and conditions, increased approximately 20% overall and 26%, excluding workers' compensation, which had a 5% renewal rate increase. The exposure reduction in the quarter reflects re-underwriting of the portfolio, coupled with the economic impact from the pandemic.

While loss trends in liability lines remain elevated, the rate increases in the quarter exceeded loss trends, although only marginally in workers' compensation. We anticipate that this rate activity will continue for the foreseeable future and expect that the impact of COVID-19, coupled with the low interest rate environment, will serve as a catalyst for more meaningful rate increases in workers' compensation going forward.

Liberty Mutual Surety's net written premium declined $5 million or 2% from the prior year reflecting a slowdown in infrastructure spending and increased reinsurance costs. As respect to profitability, excluding the impact of catastrophes, COVID-19 and prior period loss development, pretax operating income was $397 million in the quarter, a $392 million improvement over the prior year. After the impact of catastrophes, COVID and prior year development, we had a pretax operating loss of $3 million versus a pretax operating loss of $357 million in the prior year.

The combined ratio before the impact of catastrophes, COVID and prior period incurred losses was 93.9%, a reduction of 12.2 points from the prior year. This reflects a 10.5-point reduction in the loss ratio and a 1.7-point reduction in the expense ratio. The loss ratio improvement reflects reduced large loss activity as a result of re-underwriting within the first-party portfolios, limit reductions and repositioning in liability lines, exiting certain classes of business and rate increases in excess of loss trends in nearly all lines.

The expense ratio improvement reflects lower travel and entertainment expenses due to the pandemic, operating model efficiencies and general expense control, coupled with growth. The combined ratio, including catastrophes, COVID-19 and prior year incurred losses, decreased 11.6 points to 106.3%.

In addition to improved core results 2020 had lower catastrophe losses than in 2019. Partially offsetting this improvement were COVID-19 losses of $115 million, which added 3.6 points to the loss ratio, primarily from the workers' compensation and contingency lines.

The combined ratio was also impacted by 6.5 points of adverse prior year reserve development in 2020 related to U.S. casualty lines.

Overall, we're pleased with the progress made on our core operating performance through loss ratio improvement as a result of improved risk selection, pricing and business mix, in combination with the expense ratio improvement.

And now I will turn the call over to Neeti to discuss investment results.

Neeti Bhalla Johnson
Executive VP, President & Chief Investment Officer of Investments

Thank you, Dennis. Overall, the investment portfolio performed well in Q4, generating $953 million in net investment income, split evenly between the fixed income and equity portions of the portfolio. We also generated $415 million of realized gains in the quarter, reflecting $205 million of unrealized gains on equity securities, $169 million of net gains on fixed maturity sales and a $50 million net gain on derivatives.

COVID-19 continues to be an ongoing threat, with virus variants quickly spreading around the world, risking a stunted economic recovery and increased economic scarring. Vaccine distribution to date has been below expectations, but going in the right direction. Vaccinations, rapid testing, stricter health care policy measures and the warmer weather should enable us to start to "live" with the virus going into the second half of the year.

If sustained economic recovery remains key to an optimistic market trajectory, we expect a continuation of robust fiscal and monetary policies to support growth and asset markets. While we are positive on risk assets, we are cognizant of the high valuations and potential risk from a rise in interest rates, which could lead to episodic volatility. We continue to favor credit risk over equity risk and are finding better value in private markets relative to public markets. That said, we are very mindful of the divergence between markets and the challenges the virus poses to the underlying economy.

Portfolio positioning was largely unchanged over the quarter. In terms of the current interest rate environment, we continue to believe that rates will remain low across developed economies. While the persistent low rate environment heralds a downward trajectory in net investment income, we have been able to mitigate some of the deterioration in the near term.

Our total return fixed income approach proved highly accretive in the volatile markets of 2020, and we have also been expanding our exposure to more bespoken and liquid portions of the fixed income market like private ABS.

In the equity, or as we refer to it, growth portion of the portfolio, we saw strong results. The main driver in the quarter was our PE book, where our long-standing overweight to venture boosted results. Buoyed by the resumption of a strong IPO market and GP realizations, partnerships contributed roughly $500 million with the lion's share coming from our private equity exposure.

Please recall that these results are on a 1-quarter lag. Given that PE results are reported on a 1-quarter lag, marks do not yet reflect the Q4 rally in public equities. The Q4 private equity results underscore the benefit Liberty enjoys as our 30-plus years in the space affords us access to top-tier GPs.

And now Chris will conclude our prepared remarks with a discussion of full year financial results.

Christopher Locke Peirce
Executive VP & CFO

Thanks, Neeti, and good morning, everyone. Net income attributable to LMHC was $758 million, down $279 million from 2019. This includes the early retirement charge that David mentioned earlier. Excluding the after-tax impact of the early retirement charge, net income in the year was $1.2 billion.

Net written premium for the year was $40.6 billion, an increase of $810 million or 2%. Excluding the impact of foreign exchange, net written premium grew 2.7%. Premium growth was predominantly driven by global Risk Solutions posting an aggregate renewal rate increase of 15%, with the increase coming from nearly all lines of business.

In GRM, strong premium growth in U.S. personal lines was offset by roughly $300 million in auto and small business premium refunds and U.S. business lines where the combination of the COVID-19 related economic impact and underwriting actions taken on historically unprofitable segments were meaningful.

Full year 2020 pretax operating income before partnerships, LLC and other equity method investment income was $187 million, down $385 million from 2019. The decrease primarily reflects higher catastrophe losses and the impact of COVID-19 related losses.

This was partially offset by core loss ratio improvement, which benefited from lower auto frequency in GRM and lower large loss activity in GRS. The core combined ratio for the year was 91.6%, down 3.8 points from 2019, primarily reflecting the loss ratio improvement previously mentioned.

This was partially offset by a 0.9-point increase in the expense ratio driven by higher technology investments, higher commission expenses, increased advertising spend in GRM and increased employee-related costs driven by a onetime benefit in 2019 that did not recur.

As we've discussed at length, expense efficiency is critical to our long-term growth strategy. Our long-term target expense ratio was 27%, roughly 3 points below our current position. We anticipate that the decisions we've made to invest in technology as well as the early retirement offer that Dave referenced will generate significant progress towards our expense goals. That said, along the way, we will strike a balance between allowing savings to flow through to the bottom line and reinvesting back into our business.

The all-in combined ratio of 101.8% was relatively flat versus the prior year. This includes 1.7 points of losses related to COVID-19 and an increase in the catastrophe ratio of 2.6 points, largely offset by the improvement in the core combined ratio and a 0.4-point decrease in prior year development.

Partnership, LLC and other equity method investment income increased $10 million to $711 million, reflecting favorable valuations in private equity investments due to improving market conditions.

Net realized gains for the year were $790 million, an increase of $347 million from 2019, driven by $1 billion of net gains on fixed maturity sales and a net change of $123 million in equity unrealized gains. This was partially offset by a $205 million net loss on the Liberty Energy LLC transaction, which we discussed in the second quarter.

Turning to our capital and capital structure. We issued $800 million of 40 Non-Call 5 fixed-for-life Junior subordinated notes with a coupon of 4.3% representing the first broadly syndicated $1,000 par fixed-for-life capital offering. The historically low rate environment and compressed spreads presented an opportune time for us to look further down the capital structure and explore this unique financing vehicle. We are pleased with the outcome of this transaction as it offers us improved financial flexibility.

Our financial leverage stands at 25.9% and is comfortably in line with the expectations for our ratings. On the reinsurance side, we entered the year after a successful renewal cycle where, among other changes, we issued our first Mystic Re catastrophe bonds since 2012. This transaction demonstrates Liberty's continued participation in both the traditional and ILS markets, the commitment that has allowed us to use a variety of reinsurance and sources of reinsurance capital to optimize protection across our broad portfolio of insurance risks.

Cash flow provided by continuing operations was $6.4 billion, an increase of $3 billion from the prior year, reflecting favorable pay loss activity and premium collections from both businesses, collection of subrogation recoveries and the nonrecurrence of the payment for the NICO casualty reinsurance transaction, partially offset by lower investment income collected.

GAAP equity at the end of the year was $26 billion, an increase of roughly $2.4 billion over the prior year-end, driven primarily by unrealized investment gains due to a decline in interest rates and net income of $758 million.

Statutory surplus at the end of the year was $22.8 billion, up from $20.5 billion in 2019, primarily reflecting affiliated unrealized gains, capital contributions received and statutory net income of $782 million.
This concludes our prepared remarks, and we'll now open it up for questions.

Question and Answer

Operator

[Operator Instructions] And we'll take our first question from Chad Stogel with Spectrum Asset Management.

Chad Stogel
Spectrum Asset Management, Inc.

A couple of questions here. The first one, is there any color you can provide on the Texas situation? I don't expect you to give a number yet, but just what you're seeing, where you're seeing maybe claims coming in. And if there's any discussion in terms of reinsurance, and do you expect those treaties to apply to this event?

David Henry Long
Chairman, President & CEO

Chad, this is Dave. Thanks. And yes, it's going to be ugly, but not ugly enough to have reinsurance kick in. I'm going to hand it over to Tim, but I think we've had something like 20,000 claims reported already. And it's a little early to frame what the total loss could be, but it will be easily in the sort of mid-range, hundreds of millions of dollars, but this will unfold over time.

Tim -- and by the way, it's not just Texas. There's a whole host of states that were impacted. But Tim, do you want to chime in?

Timothy Michael Sweeney
Executive VP & President of Global Retail Markets

Sure. Thanks, Dave. Primarily Texas and Oklahoma, but several other states with kind of 500 claims or so here and there, but we do expect it to be a 20,000 to 25,000 claim event, primarily homeowners. And as David said, a substantial event, but not one that pierces our reinsurance, but primarily Texas, although it bleeds into other states and primarily homeowners and you can be thinking about 20,000 to 25,000 of ultimate claims is our best guess. And I would just highlight that this is very fluid and very early. So that's our best estimate right now.

Chad Stogel
Spectrum Asset Management, Inc.

That's very, very helpful. And a tactical question on the Liberty Mutual Insurance company RBC ratio. I see it declined quite a bit. If you just operate in the 400%, it's been floating around this 350% to a high 300% level for a while. Do you plan to build that back up? Or are you comfortable with that at that level?

Christopher Locke Peirce
Executive VP & CFO

Chad, this is Chris. I can jump in on that one. And so the short answer is we are still targeting an RBC for LMIC of 400% or hopefully a little bit over that.

And you're right, we have sort of drifted down below that over the last few years. One of the challenges we face is LMIC tends to be the main vehicle we use to fund our foreign operations. And so we've had a lot of growth in GRS over in Europe, so a lot of the capital has come from LMIC for that. So we are also looking -- if you noticed, we disclosed, the fire company is north of 500%. And Wausau is close to 500%.

So we'll continue to look at sort of optimizing the balance of the risks amongst the mutual companies. And I'd also say that the capital transactions that we've completed in Q1 will bring us meaningfully closer back to the 400%. So we are still targeting to get that back to 400% and keep it there.

Chad Stogel
Spectrum Asset Management, Inc.

Okay. Great. And if I could just squeeze in on the PYD. Did you note the accident years that the adverse came from outside of A&E, the balance that you mentioned?

Christopher Locke Peirce
Executive VP & CFO

We have not disclosed the accident year on that, and it is a bit of a mix. I mean some of the construction liability stuff is older accident years and legacy Ironshore stuff. And obviously, that sort of is covered by that ADC, but there's a sublimit on construction. So that's older stuff that's sort of run off legacy.

Some of the D&O and casualty would be more recent years. But beyond that, we're not going to disclose accident years.

Operator

And we'll take our next question from Jeff Bernstein with Insight Investment.

Jeffrey Bernstein
Insight Investment Management Limited

Two quick questions. Chad asked most of the questions I had on mind. The first one, have you guys said what you think your run rate savings are going to be up on the restructuring charges?

And the other question is on leverage. Any sort of guidance on where do you think leverage will get to pro forma with the deal that you did in January? And I think you have some maturities this year. Any update on how you're thinking about leverage?

David Henry Long
Chairman, President & CEO

Yes. Thanks. Thanks, Jeff. I don't think we did state the run rate savings, but I'm happy to give you a swag at it. So just to give you an idea on the early retirement program, folks will be leaving the organization at different points during 2021. So January, April, summertime, September, end of the year. And so it will be a phased-in approach.

We think the payback period, and Chris can chime in here. We think the payback period on NRO is a little over 2 years. The run rate savings once done, which we'll see mostly in 2022, not 2021, it's somewhere around $260 million.

Chris, do you want to just make sure that I'm on the money there and then talk a little bit about leverage?

Christopher Locke Peirce
Executive VP & CFO

Yes, you've got both goes right on the money. So right about $260 million will be an annual run rate savings that will be fully there in 2022 and beyond. So --

And on leverage, we don't comment on future plans. We obviously went through our transaction already at the beginning of this year. I think we feel generally good about where we are. We'll continue to look at 2022 maturities and make decisions there, but I wouldn't expect any major changes.

Operator

[Operator Instructions] We'll take our next question from Matthew Healey with Fidelity Investments.

Matthew Healey

My question -- first question is in GRM, the re-underwriting actions that you're taking there in commercial auto and commercial multi-peril. Can you just give me some additional color on when those started, when you expect them to be finished? What sort of business is going by the wayside? What kind of margin are you targeting? Like how much margin improvement can you get? And when do you expect to achieve that?

Timothy Michael Sweeney
Executive VP & President of Global Retail Markets

Sure. Sure, this is Tim. So our underwriting improvement efforts began in the latter part of 2019, continued into last year. We feel pretty good about our loss ratio improvement. We actually -- our combined ratio suffered last year because of the top line shortfall related to COVID. So we actually pivoted a little bit from the loss ratio challenge or an expense ratio challenge during the year last year.

We continue -- we're comfortable with the progress. We're nonrenewing accounts that don't meet our appetite. We're taking rate where we need it. A lot of monoline commercial auto is the subject of scrutiny as we go forward and just other things that are out of appetite and poor quality risks. I think we were the victim of adverse selection for a little bit of time. So we're kind of cleaning that up. And we expect to be kind of in the 95% to 97% combined ratio by end of 2022. So probably another 18 months or so in that cleanup. We're not looking for growth unless we can do it profitably, and we'll be at our target returns late in 2022.

Matthew Healey

And so we should probably see retention move back up from this roughly 74% area that we have now for overall U.S. business lines?

Timothy Michael Sweeney
Executive VP & President of Global Retail Markets

For sure. A lot of that retention hit last year, I think it was around 6 points. A fair amount of that is going to be business failures. It's going to be premium retention impacted by premium audits that we did because payrolls were down. So yes, you can see -- you can expect retention to bounce back by several points this year.

Matthew Healey

Great. And then I don't know if you can just help me a little bit. I'm having a little difficulty on the financials. Just for the PYD, a lot of it -- I'm just trying to add it all up and a bunch of it showed up in corporate and other. Why is it there? Maybe just is there something I'm missing there?

Christopher Locke Peirce
Executive VP & CFO

Sure. This is Chris. Do you want to jump in, Dave? Or you want me to go?

David Henry Long
Chairman, President & CEO

Well, so the reason there's a piece in corporate, Matthew, is that Chris mentioned this, the residential construction defect, which is left over from Ironshore is essentially something that we no longer do. So it's a run-off operation. It doesn't really -- it wasn't part of the Liberty system. It's not something that we're doing on an ongoing basis. So we put that in corporate.

Chris can talk to the rest of it. But I would just add that I think on some D&O and some of the casualty lines, I think we remain pretty negative on the trends, probably more negative than most out there.

We've seen slowdown in payments over the course of the past 12 months for obvious reasons. And that's reflected in the cash numbers that you see. But we think it's all going to bounce back. We don't view that as any kind of positive news. We think the trends that we saw before COVID are going to come back post COVID and we're just making sure that our opinions on how far they come back are reflected in some of those prior year reserves? Chris, do you want add there?

Christopher Locke Peirce
Executive VP & CFO

Yes. The only thing I would add to that on included in corporate is $200 million of reserves that were ceded to the casualty ADC that we entered into in 2019. So those are fully ceded and economically recoverable. Because of the retroactive reinsurance accounting, we have to take the P&L charge for it in 2020, but will recover through the P&L in future years as the underlying claims are actually paid and settled. So that's a block of reserves that we have sort of moved into corporate as well.

Operator

[Operator Instructions] Our next question comes from Brett Gibson with JPMorgan.

Brett G. Gibson
JPMorgan Chase & Co, Research Division

Can you help me understand how we should think about the right mix between GRS and GRM over the long-term versus the current 1/3, 2/3 mix.

So I get in the near term, you're going to be focused on growing retail, but I'd love to hear where this can settle long term, including what organic components may drive it and if M&A may play a role at all.

David Henry Long
Chairman, President & CEO

That's -- it's a great question. And if I had an exact answer for you, I'd give it to you. I would say, Brett, that the whole idea is we're going to -- we're taking a look at making sure that we're growing in places organically that are generating the right returns for us. And so to the extent that we look across the business, we're going to invest in those lines that are generating the best returns, and that will drive how we look on a go-forward basis.

And so I would say that we haven't really been in a position to do that because we've been doing a little fix-it work over the past few years, but it's a timely question that I can't give you the answer for other than to say that the sort of go forward, the go-forward mix of the business will be driven by where we think we can get the best returns. And so if that means that we move from 70-30 to 80-20 or to 60-40, we will do that and we'll deploy capital in the places where we think we're going to get the best long-term returns.

But I think what you see today is a reasonable estimation of what it will look like in the future, at least in the short-term future, but longer term, that could switch, depend upon what we get the best returns.

Acquisition-wise, we don't tend to talk about it. But I would say that when we're looking to do acquisitions, at this point, it would be for a particular reason and whether that be to strengthen our position in a country, to get access to better technology, to get access to better talent, to get access to products that we might not have. As I look across the company, there's not an awful lot of places where we would make an acquisition to get into a particular distribution channel or to get products that we don't have because we kind of have them all. So I think a lot of what you might see is to strengthen our position in a place where we think we would need something. So yes, we're focused as much on how we grow organically as we are on what we might need to acquire out there at the moment.

Brett G. Gibson
JPMorgan Chase & Co, Research Division

Great. That's really helpful. And then just one last follow-up for me. I just wanted to follow-on to Jeff's leverage question. And I just wonder if you can help us understand what exactly your target range is for leverage. In the MD&A, you talked about current leverage being within the target range. Maybe just if you can quantify that.

And then I think again, to Jeff's question, I'd just love to understand directionally where you think that may trend over time, not exactly trying to get specific about where it would go. But just directionally?

David Henry Long
Chairman, President & CEO

Chris, why don't you walk that one?

Christopher Locke Peirce
Executive VP & CFO

Yes. So we don't have a hard range and not one that we would give you. We certainly are cognizant of the expectations of the rating agencies around leverage and what we generally say is that statement that our current levels are consistent with our ratings. And we think we're comfortable with them and the rating agencies are comfortable with them.

So obviously, as we grow our equity through earnings, that creates a little more capacity without raising the leverage ratios. And I think, honestly, that's where our biggest focus is, just to make sure we're generating sufficient organic capital through earnings and not looking to really in any meaningful way to increase those leverage ratios.

Operator

[Operator Instructions] We'll take our next question from Marc Cohen with Guggenheim Partners.

Marc Cohen

A few questions, if I may for -- ask. I wanted to go back on the COVID-19 losses that were recorded in the fourth quarter. They represent about 17% of the total year's COVID-19, best estimates on COVID losses. Can you give some color as to what changed in the fourth quarter that resulted in that $150 million increase to COVID-related exposures.

David Henry Long
Chairman, President & CEO

Dennis, do you want to talk a little bit about COVID?

Dennis James Langwell
Executive VP & President of Global Risk Solutions

Yes. So Marc, as you know, there was another wave in the fourth quarter, and a lot more exposures. So the majority of what we booked in the fourth quarter was workers' compensation reserves for both new reportings and expected reportings and just also a potential increase in losses from just deferred medical, as Tim had mentioned in his comments.

The balance of it was primarily a small amount of event cancellation for the remainder of 2021 events. So they hadn't been canceled yet, but with the new wave of COVID, our expectation is that they'll be canceled. So we basically accrued all of the 2021 exposure. And then there were some other miscellaneous lines for a small amount.

Marc Cohen

Was any of the workers' compensation related to medical-related exposures of coverages for health care individuals. And from your comments, it doesn't seem that the recent legal actions or decisions that were made in the U.K. were the impetus for that increase in the fourth quarter. Is that a correct assumption?

Dennis James Langwell
Executive VP & President of Global Risk Solutions

I really couldn't understand much of what you were saying. If you could repeat it just so that I catch you.

Marc Cohen

My apologies. I just wanted to understand the workers' compensation losses that you've highlighted that -- due to the recent wave. Was that related to health care-related costs and that's the first, I guess, subpart. And then the second subpart was just for clarification purposes, the additional expense had nothing to do with the U.K.-related legal decision that was made in respect to COVID-related coverages on business interruption.

Dennis James Langwell
Executive VP & President of Global Risk Solutions

Okay. Yes. So the COVID on workers' compensation is really a combination of medical and indemnity for folks who obviously were out of work because they were sick.

As far as the U.K. decision, it had very little impact on us. We had very little activity with the policy forms that were involved.

Marc Cohen

Understood. My second question is in respect to the reestimation that was recognized in the fourth quarter. Could you clarify, were these predominantly these short-tail lines that had that reestimation that was -- that benefited the company in the fourth quarter? I believe you highlighted lower frequency events that would be incidences. I just want to confirm if they were predominantly in the short-tail line businesses.

Christopher Locke Peirce
Executive VP & CFO

Yes. This is Chris. So yes, the answer is yes. We were a little bit cautious through the earlier part of the year to fully recognize the benefit on primarily on personal auto. Just trying to be a little bit cautious. So we really have not adjusted any of our long-term loss ratio picks for the COVID slowdown. I think, as Dave mentioned, there obviously has been a dramatic decrease in paid losses and claims activity in general, but we are not recognizing that in our loss pick. So it is from the short-tail lines.

Marc Cohen

Okay. And if I could squeeze one more in and then I'll go back into queue. The company recognized some asbestos environmental decreases in reserves in the fourth quarter. Overall, I mean, on the full year, it seems pretty well managed. But I'd like to understand and I know that A&E tends to be reviewed in the fourth quarter.

Is this recent developments that have occurred, and it's consistently occurring every year versus taking a larger charge from your full A&E analysis on active lives and the exposures that you have? I'd like to try to understand, you highlighted a 2.8 A&E charge in 2019. Now, in 2020, it was a 2.1 percentage point on the loss ratio. I wanted to get some color in terms of what the company is thinking in terms of their best estimates on A&E.

Christopher Locke Peirce
Executive VP & CFO

Sure. So we do a full review, and it typically will hit in Q4 of each year. The one thing that's probably a little bit interesting or different about our 2020 charge was it's actually a little more than half of that was due to pollution. Typically, asbestos has been the bigger driver.

So we did have just a couple of large individual pollution cases that hit that we would not expect to be indicative of future trends. So the asbestos part of that charge in Q4 was less than 50% of it. The asbestos trends just remain sort of the same. We've been talking about the defense costs continue to be meaningful and even where we have no indemnity, we still have duty to defend and defense costs and the frequency of meso claims continues to be elevated.

But we would -- if you look at that charge, and we can't give -- we don't know what the future will hold, but we probably wouldn't expect the same level of pollution on an ongoing basis. And we think our held reserves, if we benchmark against other industry players, look pretty good, I would say, better than average, and we still do have about $615 million of limit left on -- from the sublimit on the ADC that we did back in 2014.

Operator

[Operator Instructions] We'll take our next question from Reed Eckhout with Legal and General

Reed Eckhout
Legal & General Investment Management America Inc.

Just as it pertains to Global Risk Solutions and the margin improvement and the rate that you're achieving. Could you just talk about rate in excess of loss trend and just your expectations around how sustainable these rate increases are for the balance of this year and into next year? And how you expect to see GRN as a contributor to continuing to get your overall underlying combined ratio lower -- GRS, sorry.

Dennis James Langwell
Executive VP & President of Global Risk Solutions

Yes. This is Dennis again. So the rate we achieved for all lines for the year in GRM was about 15%, as Chris mentioned. Net of loss trend, that's about 10 points of margin change. So you can see that our margin change was about 5 points. And the reason for that is that there was a fair amount of current year reestimation to reset the baseline based upon prior year development. So that largely offset that loss ratio improvement we would have expected of 7 points.

So rate net of trend, 10 points. That would impact the loss ratio by about 7, and then we had the current year reestimation of a couple of points. So that gets us to a 5-point margin improvement.

Going forward, we'd expect continued margin improvement. We expect for the next year or 2, our expectation is that we'll be in this elevated rate environment for the foreseeable future. And at the same time, that's helping our expense ratio. So the combination of both controlling expenses and the rate increases will bring the expense ratio down as it did this year, 2020.

Reed Eckhout
Legal & General Investment Management America Inc.

Okay. And then just within the investment portfolio, how are you guys approaching your various allocations to energy investment, just with where energy prices are currently and especially the heightened ESG focus from rating agencies and other stakeholders?

Neeti Bhalla Johnson
Executive VP, President & Chief Investment Officer of Investments

Reed, this is Neeti. What I would say is, as we discussed in the Q2 call, we are not looking to increase our private energy exposure any further. You'll probably have noticed that the oil and gas direct investments now show up in the LP and LLP line as we had discussed, and that's really what shows up as the increase on that line.

But other than that, we are committed to energy transition. We continue to increase our exposure to energy transition-related investments, and we recently became the first large P&C insurer to sign on to the UN principles of responsible investing.

And so we continue to march down the path we've discussed in the past, which is we're not looking to increase our direct private energy exposure in any way at this point and are focused on identifying and capturing opportunities on the energy transition side.

Operator

[Operator Instructions] We'll take our next question from Matthew Healey with Fidelity Investment.

Matthew Healey

I have another one for Neeti. With regard to sort of bespoke ABS, you talked about your ability to look at and look for sort of higher alpha, less liquid assets, private ABS. Maybe just flesh that out a little bit more. What do you think -- talk about Liberty Mutual strengths and the strengths of your origination partners that you work with? And what are you looking for? What do you think is most attractive right now? And kind of what are your overall targets for growing your exposure to these types of assets?

Neeti Bhalla Johnson
Executive VP, President & Chief Investment Officer of Investments

Sure. Thank you. Thank you for that question. So what I would say is first of all, just the fact that we have been playing in the private space and had exposure to it for an exceptionally long period of time, in the remarks, I mentioned 30-plus years, I think that really gives us an edge with respect to our experience into how to think about portfolio construction, impact of private capital, in terms of access to top-notch GPs and then, of course, the fact that liquidity is plentiful. It's something we look at and track very closely. But that's not an issue as the allocations are small relative to the large liquidity -- the liquid fixed income portfolio that we have.

So I would say the other advantages to your question is really, our size allows us to be a valued partner, but we don't always have to be in the market, right? We're not as large as a very large Canadian pension plan or a sovereign wealth fund where we have to do things in large size.

And for debt instruments, we get great influence in terms of structuring. So combine that with the partners, the influence on terms and structuring, the experience with portfolio construction, what I would say is on the private ABS side, really what we're doing is providing solutions to partners where we can leverage those strengths as well as the deep kind of research and underwriting capabilities that we have on that.

So overall, what I would say with respect to the portfolio at this point. We added about just about $1.3 billion in private ABS over the course of 2020. The new purchase rating was greater than single A across the private markets.

We continue to see spreads, in fact, where we acquired was spreads of over 250 over public markets. And we con -- while spreads have compressed, we continue to see higher spreads relative to public markets. And so -- and it's a very diverse collateral profile with respect to the balanced portfolio allocation across commercial resi, structured credit consumers.

So really looking at it from access, to the ability to influence structure, having underwriting capabilities, thinking about it from a portfolio construction diversity standpoint and really, the portfolio carries a single A rating, as I said. And we do -- we don't have to do this.

So the way we set this up is it's really a relative value that we look at. And so if we don't believe we're being paid for the liquidity or we're not getting the terms and the structures that we like, we are not obligated to do anything.

Does that answer?

Matthew Healey

Great.

Operator

And Mr. Peña, it appears there are no further questions at this time. I'd like to turn the conference back over to you for any additional or closing comments.

Edward Jose Pena
Senior VP & Treasurer

Thank you. And thanks, everybody, for joining us and also for your questions, which we really appreciate. If you have any other follow-up questions, please feel free to reach out to the Investor Relations team here at Liberty. Thank you.

Operator
Thank you. And this concludes the Liberty Mutual Fourth Quarter and Full Year 2020 Financial Results Presentation. Thank you for participating.