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EDITED TRANSCRIPT

FAF.N - Q3 2026 First American Financial Corp Earnings Call

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OVERVIEW:

Company Summary

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Terry Ma *Barclays Services Corp - Analyst*

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PRESENTATION

Operator

Greetings, and welcome to the First American Financial Corporation third quarter earnings conference call. (Operator Instructions)

A copy of today's press release is available on First American's website at www.firstam.com/investor. Please note that the call is being recorded and will be available for replay from the company's investor website and for a short time by dialing (877) 660-6853 or (201) 612-7415 and enter the conference ID 1376-3251.

We will now turn the call over to Craig Barberio, Vice President, Investor Relations, to make an introductory statement.

Craig Barberio - *First American Financial Corp - Vice-President - Investor Relations*

Good morning, everyone, and welcome to First American's earnings conference call for the third quarter of 2026. Joining us today on the call will be our Chief Executive Officer, Mark Seaton; and Matt Wajner, Chief Financial Officer.

Some of the statements made today may contain forward-looking statements that do not relate strictly to historical or current fact. These forward-looking statements speak only as of the date they are made, and the company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made.

Risks and uncertainties exist that may cause results to differ materially from those set forth in these forward-looking statements. For more information on these risks and uncertainties, please refer to yesterday's earnings release and the risk factors discussed in our Form 10-K and subsequent SEC filings.

Our presentation today contains certain non-GAAP financial measures that we believe provide additional insight into the operational efficiency and performance of the company relative to earlier periods and relative to the company's competitors. For more details on these non-GAAP financial measures, including presentation with and reconciliation to the most directly comparable GAAP financials, please refer to yesterday's earnings release, which is available on our website at www.firstam.com.

I'll now turn the call over to Mark Seaton.

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Mark Seaton - *First American Financial Corp - CEO*

Thank you, Craig. Our adjusted earnings per share this quarter was $1.78, an increase of 5% from the prior year. Our commercial business had another outstanding quarter with national commercial services generating its highest third quarter revenue on record.

The strength was broad-based with 8 of our 11 asset classes growing year-over-year and our average revenue per order reaching a record for the fifth consecutive quarter. We closed 22 transactions generating more than $1 million of premium during the quarter, up from 12 last year.

Only six of these transactions were data centers, indicating a broader strength to the market that includes energy, industrial and multifamily. Commercial refinance was another significant contributor with premium revenue increasing 49% from the prior year.

The residential side of the business remains more challenged. Purchase revenue decreased 3% as affordability constraints continue to weigh on existing home sales, refinance revenue decreased 1%. Over the last six months, the 30-year fixed mortgage rate has increased approximately 100 basis points to 7.5%, the highest since the second quarter of 2024.

Higher mortgage rates reinforce our expectation for a lower for longer residential origination environment. Our business is cyclical. And while higher rates extend the challenging environment we are operating in, they also provide us an opportunity to make transformational changes to our business. We are using this period to deepen our customer relationships and accelerate the rollout of our new AI native title and settlement platforms.

I'll start with Endpoint. During the third quarter, we launched wave two of our Washington pilot, expanding the platform to additional users in the Seattle metro area. Everyday provides valuable learnings about both the product and how we train our team to work effectively on the new platform.

We continue to make meaningful progress on automating the tasks required to close a transaction. Our automation rate increased from 30% in the first quarter to 34% in the second quarter and reached 42% in the third quarter. This represents a fundamental shift in how title and settlement work gets done. As workflows become more standardized and automated, the role of our people increasingly shifts from executing routine tasks to managing exceptions and focusing on higher value customer interactions.

The results should be less time processing a file and more time spent with customers while also creating a more consistent and efficient experience. We are applying the lessons learned from our Washington pilot to prepare for an accelerated national rollout next year, where we intend to have the majority of our direct division revenue running through endpoint by the end of 2027.

We are also making significant progress with Sequoia, our instant title decisioning platform. During the third quarter, we launched Sequoia for purchase transactions in three additional counties in Southern California. We are now successfully completing 17% of California purchase transactions processed through [Sequoia](corrected by company after the call) up from 11% last quarter.

We also expanded Sequoia for refinance transactions into 33 additional counties across Northern California and are now completing 34% of California refinance transactions processed through the platform.

Another important metric we track is human review time. As we scale Sequoia, we continue to review every order it generates. While the time required for each review continues to decline. The average review time for a purchase transaction fell from 83 minutes in the first quarter to 74 minutes in the second quarter and 56 minutes in the third quarter. We expect further improvement, particularly as we introduce new tools in the fourth quarter to streamline the review process.

Sequoia already reduces processing time by two-thirds compared with our traditional process and we expect it to become even more efficient over time.

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One of First American's most important competitive advantages is our title plant data. We acquire source documents directly from counties, extract and structure the relevant data and apply our underwriting expertise and advanced technology to produce fully insurable title commitments.

As Sequoia matures, we believe we can produce these commitments faster and at a lower cost than anyone else in the industry by leveraging this unique end-to-end capability. Importantly, these commitments are backed by First America's balance sheet, combining speed and efficiency with the financial strength and underwriting certainty our customers expect.

Looking ahead in the fourth quarter, we plan to launch Sequoia for purchase transactions throughout Northern California and expand into Florida across both our direct and agency operations. Similar to Endpoint, we expect to be processing a majority of our orders on the Sequoia platform by the end of 2027.

Once fully mature, we believe Sequoia will give us the most modern title production platform in the industry with a goal of automating approximately 80% of refinance transactions and 70% of purchase transactions in markets where we maintain title plants.

Another important driver of our earnings is our bank, First American Trust, which provides a growing and increasingly diversified source of investment income.

In Q3, title segment investment income grew 11%, driven by a 39% increase at First American Trust, which is benefiting from growth outside our capital title business, including ServiceMac and our 1031 exchange business.

Turning to our outlook, we expect the recent trend of a strong commercial market and a sluggish residential market to continue. For the first three weeks of October, our open purchase orders are down 8%, refinance is down 35% and commercial is down 7%. Based on our order pipeline, we still believe commercial will have a strong finish to the year. However, given the elevated mortgage rates, we'll be in a lower for longer residential origination environment.

We expect these trends to continue into 2027, and in that backdrop, we will keep a laser focus on modernizing our capabilities in our core title business and growing our adjacent businesses that are more cyclically resistant, including First American Trust, ServiceMac, Home Warranty and our data business. Now, I'll turn the call over to Matt, who will discuss our financial results in greater detail.

Matthew Wajner - *First American Financial Corp - CFO*

Thank you, Mark. This quarter, we generated GAAP earnings of $1.72 per diluted share. Our adjusted earnings, which exclude the impact of net investment losses and purchase-related intangible amortization, were $1.78 per diluted share. In the title segment, total revenue was $2 billion, up 7% compared with the same quarter of 2025.

Commercial revenue was $297 million, a 21% increase over last year, driven by a 13% increase in average revenue per order and a 7% increase in closed orders. Purchase revenue was down 3% during the quarter due to a 5% decline in closed orders, partially offset by a 2% increase in average revenue per order.

Refinance revenue was down 1% compared with last year due to a 4% decline in average revenue per order, partially offset by a 3% increase in closed orders. Refinance accounted for just 5% of our direct revenue this quarter, illustrating how depressed refinance activity remains relative to historical levels.

In the agency business, revenue was $868 million, up 9% from last year. Given the reporting lag in agent revenues of approximately one quarter, these results primarily reflect remittances related to second quarter economic activity.

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Information and other revenues were $292 million during the quarter, up 6% compared with last year, primarily driven by a 31% increase in fee revenue at ServiceMac related to growth in its loan portfolio. Investment income was $169 million in the third quarter, up 11% from last year, primarily driven by growth in our investment portfolio associated with higher deposit balances at First American Trust.

Personnel costs were $574 million in the third quarter, up 6% compared with the same quarter at 2025. The increase was mainly due to higher salary and incentive compensation expense. Other operating expenses were $306 million in the quarter, up 11% compared with last year, primarily attributable to increased software expense and higher production expense. Our success ratio for the quarter was 87%, above our 60% target.

We recorded $8 million of one-time expenses during the quarter related to an operational restructuring and an indirect tax matter. We also continue to invest in certain businesses outside of our domestic title operations such as ServiceMac. The investments at ServiceMac are supporting the meaningful growth in its loan portfolio. The provision for policy losses and other claims was $45 million in the third quarter or 3.0% of title premiums and escrow fees, unchanged from the prior year.

The third quarter rate reflects an ultimate loss ratio of 3.75% for the current policy year and a net decrease of $11 million in the loss reserve estimate for prior policy years. Interest expense was $31 million in the current quarter, up 27% compared with last year due to higher interest expense related to the growth in deposit balances at First American Trust. Pre-tax margin in the title segment was 12.4% or 12.7% on an adjusted basis.

Moving to the Home Warranty segment. Total revenue was $115 million this quarter, flat compared with last year. Pre-tax income was $11 million for the quarter, down 30% compared with last year, primarily attributable to higher marketing expense to drive continued growth. In our direct-to-consumer sales channel. The loss provision was 47%, essentially unchanged compared with the third quarter of 2025. Pre-tax margin in the Home Warranty segment was 9.9% or 9.7% on an adjusted basis.

The effective tax rate in the quarter was 22.4%, which is slightly below the company's normalized tax rate of 24%. Our debt-to-capital ratio was 30.3%. Excluding secured financings payable, our debt-to-capital ratio was 22.2%.

Regarding dividends, we targeted payout ratio of 40% over the cycle. Given our current year results and our future outlook, we raised our common stock dividend during the quarter by 11% to an annual rate of $2.44 per share to bring the dividend payout ratio more in line with our target.

During the quarter, we repurchased 23,000 shares for a total of $1 million at an average price of $64.24. So far, in October, we repurchased 143,000 shares for a total of $9 million at an average price of $62.40.

Now, I would like to turn the call over to the operator to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Bose George, KBW.

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Bose George - *Keefe Bruyette & Woods Inc - Analyst*

Actually, just first on expenses, so you guys noted that I guess it was the one-time $8 million, but can you just talk a little more broadly about margin expectations in 2027 if volumes -- if resi volumes remain around this $2 trillion or even I guess [NDA] is looking for even less than that. And then commercial potentially flat just given the comps are going to get pretty challenging.

Matthew Wajner - *First American Financial Corp - CFO*

Hi, Bose. Thanks for the question. Yeah, so I'll kind of take it by each of the major markets that we have. So where we sit today based on the factors that you just said there and what Mark talked about in his script, our outlook today is essentially flat for revenue year-over-year when we look at '27 compared to full year '26. We expect commercial, like you noted, to be strong next year.

As we said, we expect to have a record year this year. We do think we can have modest growth next year because we do think it's going to continue to be strong and could strengthen. So we expect to have some modest growth in commercial next year, which would make '27 a record year for us.

Obviously, the residential market, we're more pessimistic about both for purchase and refi. So. We would expect revenue to be down next year compared to this year.

One tailwind that we expect to see next year is investment income. It's been growing, especially investment income net of interest expense year-to-date has grown about 8% when compared to last year. We expect that to continue to be strong next year, given the expectation that rates will be higher, both short-term rates and US Treasury rates. [Think] should benefit our investment portfolio, both the investment portfolio and the returns we get on our deposits. So we think we'll see some growth in investment income.

And then when we turn to expenses, we expect to have the normal inflationary pressures around personnel and other operating expenses primarily in salaries and technology costs.

And the other thing. It's too early to say, but when we think about the loss ratio, right, we've been at 3% for this year and we were at 3% last year and that's comprised of 3.75% for the current policy year with a release of prior years of 75 basis points.

And when we think about our business, it's typically a 4% to 5% loss rate over the cycle and we've been below that for several years now and that's largely due to the fact that during the pandemic when things were uncertain, we had a little bit of a higher loss rate and it turned out that those claims didn't manifest, so we've been releasing some of that excess. I think it's likely that at some point here in the near future will either slow the release or cease the release, but any changes will obviously be related to how claims come in.

Bose George - *Keefe Bruyette & Woods Inc - Analyst*

Great, that's very helpful. And just sort of to sum that all up, do you feel like the margin ends up being kind of flattish or could there be room for upside?

Matthew Wajner - *First American Financial Corp - CFO*

I mean, I would say the margin right now, I don't see a lot of room for expansion. I think it's all going to depend on how the commercial market does next year. If commercial exceeds our expectations, we may be able to expand, but right now I don't see margin expansion next year.

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Bose George - *Keefe Bruyette & Woods Inc - Analyst*

Okay, great, thanks for that color. Then just actually one on Sequoia and endpoint from the expense side. As that rollout continues, does the benefit in terms of the initial benefits on expenses really happen when you shut down fully the other platforms and is that something that happens potentially in 2028 or is that a little while just as kind of some stuff remains on the older platforms?

Mark Seaton - *First American Financial Corp - CEO*

It really depends on the platform we're talking about, whether it's Endpoint or Sequoia. I mean in the case of Sequoia, we'll get benefit as we roll out Sequoia. I mean next year is going to be a big year for us strategically as we roll out both these platforms. And we'll start to get incremental benefit.

For example, Sequoia, as we roll out, as our fulfillment rates improve, as we run more orders through Sequoia, we save on every order that goes through Sequoia. And so we don't necessarily need to wait for the old platform to be decommissioned before we start saving.

And I would say it's kind of a similar, different but similar with Endpoints. So next year is a big year strategically. And we'll start to really kind of start to see the benefits in 2028 if we can successfully execute next year.

Operator

Mark Hughes, Truist Securities.

Mark Hughes - *Truist Securities - Analyst*

On the [title] pre-tax margin, I think you suggested you don't see margin expansion next year. If you take a little more investment income, a little higher expense, does that mean stable pre-tax?

Matthew Wajner - *First American Financial Corp - CFO*

Yeah, I would say I think we could be stable to -- I think about stable is what I would expect right now. There may be a little bit of pressure, so it could contract a little bit, but right now where we sit today, I don't see considerable deviation.

Mark Hughes - *Truist Securities - Analyst*

How about investment income for the third quarter? How is that -- I'm sorry, not third quarter, but for the fourth quarter, how is that shaping up?

Matthew Wajner - *First American Financial Corp - CFO*

I would expect investment income to follow the same. Growth rate that we saw the first three quarters. So when you think about investment income, I think I spoke about it last quarter, but we really look at investment income net of interest expense since a lot of the growth in investment income has been due to the growth in deposits at the bank, right?

So there's an offsetting interest expense. So when we look year-to-date, investment income is up 11% year-over-year, interest expense is up 31% and the net increased by 8%. I think that net increase of 8% is a good number for Q4.

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Mark Hughes - *Truist Securities - Analyst*

Then on the commercial side, it sounds like you've got good confidence next year. In your experience, how sensitive is that to interest rates if it's higher for longer on rates? What does that mean for refi and then purchase and just maybe as part of that, sounds like refi was quite strong in commercial this quarter. People trying to get under the wire or is that just good underlying activity?

Mark Seaton - *First American Financial Corp - CEO*

Fortunately for us, Mark, it's just not as sensitive to interest rates. And I'm sure there's a little sensitivity, but I think especially for these big deals like data centers and big energy deals that we're doing just aren't sensitive to rates. I mean, we're seeing those deals close. And the other thing too on the commercial side is that you don't have 30-year mortgages, right, like you do on the residential side. I mean, a lot of these commercial loans are they're shorter in duration now too.

I mean, they're typically five years. And I've talked to several clients that are coming in even less than that just because they think that, hey, rates are high and why should we take out a 10-year loan. We can do a three-year loan. And so that just creates more transaction activity, more refinance activity in our pipeline over the next couple of years. And so it's just commercial is just more of a stable business when it comes to refinance volume in the residential side, which is obviously good for us.

Mark Hughes - *Truist Securities - Analyst*

Very good. Thank you.

Operator

(Operator Instructions)

Terry Ma, Barclays.

Terry Ma - *Barclays Services Corp - Analyst*

Hey, thank you. Good morning. Maybe just to follow-up on the margin outlook for 2027. How should we think about the ability to sustain title margins around this level if residential gets worse and some of the momentum in commercial kind of softens? Like what additional levers do you have on the expense side if that happens?

Mark Seaton - *First American Financial Corp - CEO*

Well, I'll just talk about -- I'll start with that, Terry. I just think when we look at it next year, we're already at just a tough market. I mean, the refinance market. Has been like a 1 out of 10 here for the last couple of years.

And now, as I mentioned, our open refinance orders are down 30%-plus in October, but I mean, it's from a very low level here. And I could say something very similar about the purchase side. I mean, the purchase side has been kind of at rock bottom for four years now. Our orders, our open orders in October down 8%.

And so we have levers to pull. But I'll just say that our focus really is on next year in this tough market, and it's going to get a little bit tougher. We just want to get really close to our customers. We want to gain market share in a down market. We want to invest in our business and roll out these new platforms next year. That's going to be the focus to really prepare us for the next cycle.

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And it's really that process is working. I mean, in the last 12 months, we've gained 60 basis points of market share. And we've done zero acquisitions. And so we want to just keep that momentum going. So we always have leverage. There's always things we can do, but we're thinking like three to five years out and not next quarter. So that's our process right now.

Terry Ma - *Barclays Services Corp - Analyst*

Got it. That makes sense. And then just on commercial, any color on what the pipeline kind of looks like as you look out in the fourth quarter? And then for the ARPU growth this quarter did decelerate notably.

Anything to kind of call out, was it kind of mixed driven or did you have some deals kind of slip into the next quarter? Any color around that would be helpful. Thank you.

Mark Seaton - *First American Financial Corp - CEO*

Well, the first part of that, we're very bullish on commercial here in Q4, very bullish. We've already closed three deals over $1 million in premium. We've got a really good pipeline getting into Q4. You never really know, right? I mean, the last two weeks of December is when you kind of find out like how your quarter went for Q4. But the pipeline is just really strong. We've been saying that all year and we just have a lot of momentum.

And it's really broad-based, it's broad geographies. And we think, like Matt said, we think it's going to carry into next year too. So we're very bullish on commercial for Q4.

And in terms of the ARPU, maybe Matt can touch on that.

Matthew Wajner - *First American Financial Corp - CFO*

Yes, thanks. So the ARPU decelerated from Q2. So just to be clear, ARPU expanded year-over-year. It did decelerate from Q2. That's largely when we've talked about this before, but when we think about commercial, around 70% of our commercial revenue comes from our national commercial business, which Mark talked about in his prepared remarks.

And 30% of it kind of comes from our local business. And actually in our NCS, which is our national commercial business, ARPU was actually up. Year-over-year and up sequentially. So what that means is there were some large deals that happened last year or sorry, last quarter in Q2 outside of centralized commercial, which really strengthened that ARPU. That ARPU was a record ARPU. So it's still a really healthy ARPU. It just didn't have the support of maybe some of large deals coming through the non-centralized channel.

Operator

Oscar Nieves, Stephens Incorporated.

Oscar Nieves - *Stephens Inc - Equity Analyst*

Good morning. You made some comments earlier about the rollout of Endpoint in Sequoia. My question is, following up on that, as Endpoint goes national next year, what are the biggest execution risks, and do you expect the transition to weigh on cost before benefits show up potentially in 2028?

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Mark Seaton - *First American Financial Corp - CEO*

Thanks so much for the question, Oscar. I think the biggest risk with Endpoint, when we initially started Endpoint, the biggest risk was just, I'd say, technology execution. There was we're trying to do something that had never been done before and there were real technological hurdles for us to execute.

Now, that risk is kind of gone now. We feel really good about our ability to build products, and we've got a great product design engineering team at Endpoint. The flywheel is really turning with technology, so we feel really good about where our product is, which was the risk. I think the risk now is more on the change management side.

Our team has been using FAST, which is our system, for 25 years. And it's an inefficient system today by today's standards. But they're used to it, right? They're used to going on and they're efficient on an inefficient system.

And now we're rolling out a new system. And there's a lot of change management that has to go into that. And so you're teaching someone who's been on a system again for 25 years to use an AI native platform. And that is a big risk right now is just change management. And so it's one of the things that we're testing in these Washington pilots is not just improving the product, but also, okay, how do we train our people? Are we giving them enough training? Are we doing the right things? And so that I think is going to be the biggest risk going into next year.

In terms of just the costs, I don't think there's going to be materially more costs. It's kind of already baked into our run rate. Maybe there will be some, but it's worth investing to get it right next year. But I don't think it will be a material increase in cost next year relative to that initiative.

Oscar Nieves - *Stephens Inc - Equity Analyst*

That's very helpful. My next one is on the bank, on the growth of the bank. You've mentioned for a few quarters now how First American Trust continues to grow. Can you comment on how big you think that part of the business can become relative to the company and how you think about its sensitivity to rates and the deposit mix?

Mark Seaton - *First American Financial Corp - CEO*

Well, I'll start with that and then Matt can talk about the sensitivity to rates and the deposit mix. But I'll just say that our bank is. Is a big strategic advantage for us for two reasons. One is it makes our operations a lot more efficient. And so one of the things as a settlement company is we deal with escrow funds all day long. And the fact that we have a bank that's tightly integrated to our operations, we can open accounts, close accounts, move money faster than anybody.

So there's an operational benefit. But then, of course, the second piece is there's a big financial benefit too in the sense that we can push certain deposits to our own bank and earn a spread on those and it has been growing pretty much every single year. I think we've pretty much maxed out, not quite, but I would say 95% of our own internal deposits that we can push to First American Trust, we do and so the really the growth prospects from here on out are what I'll call these non-title deposits.

And so we are going to there's 20,000 different title agents out there that use their own banks. And we're going to them and saying, hey, why don't you bank with First American Trust? And we're having some success with that.

We also -- when we acquired ServiceMac, they have deposits too that we can push to First American Trust. And we talked about this last quarter, but we never had our 1031 exchange balances at First American Trust, but we built a product and now we've got about $1 billion deposits at First America Trust.

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So we are growing these non-title deposits, I think, very successfully. How big can it get? I don't really have an answer to that, but what I do know is every single month we're signing up new agents and we're growing our deposit base. So I'll hand it over to Matt to talk about the sensitivity.

Matthew Wajner - *First American Financial Corp - CFO*

Yeah. And then regarding the sensitivity of the bank, so most of the bank's assets are -- in its bond report invested in the bond portfolio. So the portfolio, you can think about it as having a five-year duration and roughly $50 million to $60 million is thrown off in cash every month that we reinvest. So that's a way to think about it if you look at the forward curve and then think about that amount getting reinvested at those rates.

And then just one thing on the growth. Year-over-year, when we look at average deposits in Q3 '26 versus Q3 '25, deposits grew almost 38% and almost all of that came, like Mark said, from our subservicing business ServiceMAC and our 1031 exchange business. So I wouldn't expect that pace of growth to continue, but there's opportunities to continue to expand. I just don't think it would continue to expand at that rate.

Oscar Nieves - *Stephens Inc - Equity Analyst*

That helps. And my last one is turning now to the reserves. You mentioned that title losses typically run in the 4% to 5% range over the cycle and that you've been below that for several years following COVID. If those releases as you have because you have released some of the reserves, if those releases slow or stop, after we think about the provision going forward and how much of today's rate is the release and where does the current year rates settle?

Matthew Wajner - *First American Financial Corp - CFO*

So when we're so currently, we're reserving at 3%. So the way we think about that is 3.75% is for the current what we call the current policy year. So for new policies that we're issuing, we reserve at 3.75% and then as we release reserves that are unneeded from prior years, that's the 75 basis points reduction that gets us to 3%. So we would think of it in the current environment as for new policies as 3.75% is kind of the right loss reserve right now.

Operator

That is all the time we have for questions today. That concludes this morning's call. We'd like to remind listeners that today's call will be available for replay on the company's website or by dialing (877) 660-6853 or (201) 612-7415 and enter the conference ID 1376-3251. The company would like to thank you for your participation. This concludes today's teleconference. You may now disconnect.

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