

2023 FINANCIAL SUMMARY

RESULTS OF OPERATIONS

State Fund's results of operations for years ended December 31, 2023 and 2022 and its corresponding financial ratios are shown below:

(In millions)	<u>2023</u>	<u>2022</u>
Net premiums earned	\$ 1,140	\$ 1,175
Losses incurred	430	842
Loss adjustment expenses (LAE) incurred	72	296
Underwriting and administrative expenses	<u>453</u>	<u>438</u>
Net underwriting gain (loss)	185	(401)
Net investment income and net realized gain	570	568
Other (loss) income	<u>(132)</u>	<u>14</u>
Income before dividends	623	181
Dividends to policyholders	<u>(95)</u>	<u>(101)</u>
Net income	<u>\$ 528</u>	<u>\$ 80</u>
Loss ratio	37.7%	71.7%
LAE ratio	6.3%	25.2%
Underwriting expense ratio	<u>39.7%</u>	<u>37.5%</u>
Combined ratio	<u>83.7%</u>	<u>134.4%</u>

State Fund's premium decreased by \$35 in 2023 mainly due to less new business written. Losses incurred decreased by \$412 mainly due to prior accident years' reserve releases of \$448 and \$133 for current year and last year, respectively, and \$97 favorable outcome in the current accident year. LAE incurred decreased by \$224 mainly due to \$200 LAE reserve release this year and none in prior year. The significant releases in reserves were attributed to lower claims trend in California workers' comp market and Claims programs' continued improvement to quality, maintaining, and increasing closure rates.

Underwriting and administrative expenses increased by \$15 due to unfavorable increase of \$12 in salaries, \$5 in release of premium deficiency reserve in prior year and none this year, and \$5 in rental expense. This increase was offset by decrease of \$7 in commission & brokerage fees. State Fund had \$586 increase in underwriting results mainly due to decreases in losses and LAE incurred.

Net investment income of \$556 was \$50 higher than prior year due to an increase in reinvestment rates and income from additional bonds acquired. Realized capital gains of \$14 were \$48 lower than prior year due to less call redemptions, corporate actions, and less sell orders in equity. Other loss is primarily due to recognizing a \$140 of premiums receivable charge off related to executive shelter-in-place order period.

Net income before dividends to policyholders of \$623 was \$442 higher than prior year mainly from the significant increase in underwriting results of \$586 given the aforementioned releases in reserves, increase in net investment income of \$50, offset by \$146 increase in other loss, and \$48 decrease in realized capital gains.

In 2023, State Fund declared regular dividends of \$102 and large account safety dividends of \$6 for policies that incepted from January 1, 2023, through December 31, 2023. In addition, State Fund released \$13 of dividend reserve for policy years 2019, 2020, and 2021 which netted dividends to \$95, and resulted in net income after dividends of \$528 in comparison to \$80 in 2022.

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FINANCIAL POSITIONS

State Fund's financial positions at December 31 are as follows:

(In millions)	<u>2023</u>	<u>2022</u>
Admitted Assets		
Bonds, at amortized cost	\$ 19,265	\$ 18,714
Preferred stocks	38	-
Common stocks	667	809
Real estate	282	289
Cash and short-term investments	13	241
Other invested assets	81	4
Total cash and invested assets	<u>20,346</u>	<u>20,057</u>
Other assets	419	399
Total admitted assets	<u><u>\$ 20,765</u></u>	<u><u>\$ 20,456</u></u>
Liabilities and Policyholders' Surplus		
Loss and LAE reserves net of reinsurance	\$ 10,625	\$ 11,270
Other liabilities	<u>2,959</u>	<u>2,546</u>
Total liabilities	13,584	13,816
Policyholders' surplus	<u>7,181</u>	<u>6,640</u>
Total liabilities and policyholders' surplus	<u><u>\$ 20,765</u></u>	<u><u>\$ 20,456</u></u>

State Fund maintained a balanced investment portfolio that was focused on both credit quality and investment yield (89% of the \$19,265 bond portfolio was rated NAIC 1, the NAIC's highest quality credit class). The weighted average credit quality of the overall bond portfolio was Aa3/AA- by Moody's and Standard & Poor's respectively. Book yield at December 31, 2023 was 3.3%, increased from 3.1% at December 31, 2022. In November 2023, State Fund started investing in perpetual preferred stocks.

Management believes that its Loss and LAE reserves are adequate, and State Fund's appointed Actuary, Michael L. DeMattei of Milliman Inc., consulting actuaries, opined to the adequacy of State Fund's carried reserves as of December 31, 2023, and 2022, respectively.

State Fund operates in conformity with the California law imposed for risk-based capital (RBC). As of December 31, 2023, and 2022, policyholders' surplus exceeded the minimum RBC requirements. In addition, it passed all the Insurance Regulatory Information System (IRIS) tests for year ended December 31, 2023.

Policyholders' surplus increased by \$541 compared to prior year. This increase is a result of the net income of \$528, favorable decrease of \$104 in non-admitted assets, and net increase of \$25 in unrealized capital gains in equities and alternative investments. The increase was offset by a \$116 reclassification of special surplus to recognize State Fund's share of Pension and OPEB as liabilities in compliance with Statements of Statutory Accounting Principles (SSAP) No. 5R – "Liabilities, Contingencies, and Impairment of Assets".

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CASH FLOW

State Fund's statements of cash flow are summarized below:

(In millions)

	<u>2023</u>	<u>2022</u>
Premiums collected net of reinsurance	\$ 1,096	\$ 1,125
Net investment income	571	550
Miscellaneous income	7	15
Benefits and loss related payments	(868)	(942)
Other underwriting expenses	(796)	(733)
Dividend paid to policyholders	(46)	(70)
Net cash used in operations	<u>(36)</u>	<u>(55)</u>
Proceeds from investments sold, matured, or repaid	2,156	3,015
Cost of investments acquired	<u>(2,778)</u>	<u>(2,836)</u>
Net cash (used in) provided by investments	<u>(622)</u>	<u>179</u>
Net cash provided by (used in) financing and miscellaneous sources	<u>430</u>	<u>(24)</u>
Net change in cash, cash equivalents and short-term investments	(228)	100
Cash, cash equivalents and short-term investments, beginning of year	<u>241</u>	<u>141</u>
Cash, cash equivalents and short-term investments, end of year	<u><u>\$ 13</u></u>	<u><u>\$ 241</u></u>

Primary sources of cash included cash flow from premiums, investment income, and sales or maturities of invested assets. Primary uses of cash included purchases of long-term investments and payments of benefits, loss related expenses, and other underwriting expenses.

Cash from operations increased by \$19 from prior year due to \$98 decrease in payment for loss and dividend, and a \$21 increase in investment income, offset by a \$63 increase in payment for LAE and underwriting expenses, and a \$37 decrease in premium collection and miscellaneous income.

After 11 rate hikes, increasing interest rates caused cash flow from investments to decrease primarily driven by the slowdown in principal related proceeds. There were \$400 fewer principal pay downs and \$250 fewer call redemptions. Additionally, State Fund sold \$250 fewer stocks in 2023 compared to 2022 where multiple sell orders were executed.

Cash from financing and miscellaneous activities increased by \$454 from prior year due to increased borrowings from FHLB (Federal Home Loan Bank) line of credit to take advantage of wider spreads and investment arbitrage opportunities.