Q3 2014 Earnings Call

Company Participants

- Dino Robusto, EVP & President, Commercial and Specialty Lines
- John Finnegan, Chairman, President, & CEO
- Paul Krump, EVP & President, Personal Lines and Claims
- Ricky Spiro, â ªEVP & CFO

Other Participants

- Clifford Gallant, Analyst
- Ian Gutterman, Analyst
- Jay Cohen, Analyst
- Jay Gelb, Analyst
- Josh Shanker, Analyst
- Josh Stirling, Analyst
- Kai Pan, Analyst
- Meyer Shields, Analyst
- Mike Nannizzi, Analyst
- Vinay Misquith, Analyst

Presentation

Operator

Good day, everyone. Welcome to The Chubb Corporation's Third Quarter 2014 earnings conference call. Today's call is being recorded.

Before we begin, Chubb has asked me to make the following statements. In order to help you understand Chubb, its industry. And its results, members of Chubb's management team will include in today's presentation forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995.

It is possible that actual results might differ from estimates and forecasts that Chubb's management team makes today. Additional information regarding factors that could cause such differences appears in Chubb's filings with the Securities and Exchange Commission. In the prepared remarks and responses to questions during today's presentation, Chubb's Management may refer to financial measures that are not derived from generally accepted accounting principles or GAAP.

Reconciliations of these non-GAAP financial measures to the most directly comparable GAAP measures and related information are provided in the press release in the financial supplement for the Third Quarter 2014 which are available on the investor section of Chubb's website at www.chubb.com. Please also note that no portion of this conference call may be reproduced or rebroadcast in any form without Chubb's prior written consent.

Replays of this webcast will be available through Friday, November 21, 2014. Those listening after October 23, 2014, should please note that the information and forecasts provided in this recording will not necessarily be updated. And it is possible that the information will no longer be current.

Now I will turn the call over to Mr. Finnegan. Please go ahead, sir.

John Finnegan {BIO 1735942 <GO>}

Thank you for joining us. We are especially pleased with our results for the Third Quarter.

We posted record operating income per share of $2.17 and outstanding net income per share of $2.47. For the first nine months, operating income per share was $5.35 and net income per share was $6.28, both which were the second-highest in the Company's history.

Our results in the Third Quarter reflected strong premium growth of 5% and continued high levels of retention in all of our business units. I'm also happy to say that we continued to achieve mid-single-digit increases in our US rate change metrics. Our combined ratio for the Third Quarter was an excellent 85.8% reflecting strong underwriting performance in all the business units as well as relatively low catastrophe losses. Dino and Paul will provide more detail later.

Annualized operating ROE for the Third Quarter was 14.1% while annualized GAAP ROE was 14.4%. GAAP book value per share at September 30, 2014, was $70. That's an 8% increase in share in 2013 and a 13% increase in September 30 a year ago. Our capital position is excellent. And we continued to make good progress on our share repurchase program.

In light of our excellent performance in the Third Quarter and our outlook for Fourth Quarter, we've increased our guidance for full-year 2014 operating income per share to a range of $7.35 to $7.45 from the $6.75 to $6.95 range we provided in our July 2014 guidance. Ricky will discuss our increased guidance in greater detail.

Before turning it over to Dino, I want to take a moment to let you know about a Form 8-K filing we expect to make in December related to my previously announced retirement from Chubb at the end of 2016. Under my employment agreement, Chubb is required to deliver me a notice of non-renewal two years ahead of my retirement, in other words by December 31, 2014.

This notice will be delivered sometime in December with an effective date as of December 31. And a copy of the notice will be included in a Form 8-K that we will file shortly thereafter. As a result of the delivery of the notice, my employment will terminate on December 31, 2016, consistent with my previously announced scheduled retirement on that date.

I just wanted to make you aware that this filing will not be new news. But merely fulfills a technical requirement under my agreement related to my previously announced retirement date. Chubb's Board of Directors CEO succession planning is ongoing. There is nothing new to report at this time as my retirement is still more than two years off.

And now for more details on our operating performance, we will start with Dino who will discuss Chubb's Commercial and Specialty operation.

Dino Robusto {BIO 15021398 <GO>}

Thanks, John. Chubb Commercial Insurance and Chubb's Specialty Insurance both had strong performance in the Third Quarter characterized by excellent underwriting results and good growth reflecting high levels of premium retention and increased new business. We continued to successfully execute our stated plan of emphasizing the retention of our very profitable portfolio while continuing to push for a rate on those accounts that still require it.

Starting with CCI, Third Quarter written premiums grew at 4% to $1.3 billion. CCI's Third Quarter combined ratio was 89.5% compared to 93.3% in the Second Quarter of 2014 and 85.2% in the Third Quarter of 2013. The Third Quarter impact of catastrophe losses accounted for 2.6 points of the combined ratio in 2014. And 1.4 points in 2013.

Excluding the impact of catastrophes, CCI's Third Quarter combined ratio was 86.9% this year compared to 83.8% last year. The latter being a particularly strong results from an historical perspective. But this year's Third Quarter improved from this year's Second Quarter and the ex-cat combined ratio was 88.4%.

The casualty combined ratio for the Third Quarter was 95.3%. This compares favorably to the 98.5% posted in the same quarter last year.

Our Workers Compensation combined ratio of 83.9% was outstanding. A little more than a 7 point improvement over our very good 91.2% that we posted in the Third Quarter of 2013. And we had another strong performance in the Third Quarter for multiple peril with a combined ratio of 81.9% was essentially the same as in the prior-year period.

For the property and marine lines, you will recall that on our last quarter's earnings call, we indicated that we had experienced abnormally high levels of non-cat large losses in the Second Quarter, which adversely impacted the combined ratio. Also, we suggested that we expected a reversion to a more normal level which we are happy to report was indeed the case as the property and marine ex-cat combined ratio improved to 86.7% in the Third Quarter. While this is somewhat higher than our five-year average, it represents a 10.7 point improvement over the Second Quarter's 97.4%.

Notwithstanding this meaningful improvement, this year's Third Quarter result is higher than the extremely low 67% in the same period last year. On the conference call last quarter, we also stated that in light of the rate increases over the past several years, we were focusing on retaining profitable business and taking advantage of better priced new business. This focus is contributing to our positive growth rate.

While we will never shy away from calling accounts where we cannot secure appropriate rates in terms and conditions, our underwriting and pricing actions over the past few years have resulted in there being fewer accounts that needed to be culled. Indeed, CCI's Third Quarter retention of 87% in the US was the same as the high level we achieved the Second Quarter. Even with this high retention, we achieved an overall rate increase of 3% for the book.

This is the 14th consecutive quarter we obtained rate increases. And the earned premium impact continues to exceed our long run loss cost trends. Outside the US, CCI's average renewal rate increases in the Third Quarter remained in the low single digits.

With respect to new business, our new to lost ratio was 1.0 to 1. We continue to take advantage of our unique expertise, products and services, the target the market segments we specialize in. And within those segments, we only choose those accounts that we believe meet our required return targets.

Turning now to Chubb's Specialty Insurance, net written premiums were up 5% in the Third Quarter to $701 million. CSI's Third Quarter combined ratio was an outstanding 78.3% in 2014, versus 82.3% in 2013. For the professional liability portion of CSI, which represents the majority of the portfolio, net written premiums were up 6% to $629 million, continuing the positive growth trends that we have seen in recent quarters. Third-quarter growth was driven by higher pricing, increased renewal retention. And increased new business.

As we have noted in the past, premium growth in professional liability can vary from quarter-to-quarter because of the absence or presence of large premium accounts. And the level of growth in any one quarter is not always an indicator of what growth may be in subsequent quarters. However, we believe that our professional liability business is positioned to continue to grow profitably over time.

The combined ratio for professional liability improved again this quarter to a terrific 81.3% from 87.6% in the Third Quarter of 2013 and from 83.2% in the Second Quarter of 2014. The continued improvement in the combined ratio over time reflects our disciplined underwriting and culling actions, aided by our advanced analytics and predictive modeling, skillful portfolio management. And the compound affect that the price increases we have achieved over the last few years.

The quarter also benefited from a lower expense ratio. The improvement in the combined ratio was broad-based with most lines of business showing improvement over the Third Quarter of 2013. Renewal retention for professional liability in the US in the Third Quarter improved to 89% from 88% of the Second Quarter of this year. Our rate taking and underwriting actions in prior periods have continued to earn into our renewal portfolio.

Moreover, in the Third Quarter, we secured a strong 5% average renewal rate increase in the US which continues to exceed long run loss cost trends. In markets outside the US, renewal rate increases in the Third Quarter remain consistent with prior quarters rising by low single digits. As I stated previously, we have been increasingly focused on retaining our profitable renewal business.

Given the health of our overall portfolio, we are comfortable with the rate retention balance our skilled underwriters are achieving. Our new to lost business ratio for professional liability in the Third Quarter was 1.3 to 1, which was driven by less lost business as we focus on retaining our profitable accounts. It also reflected our success in writing better priced new business available in the market after several years of industry rate increases and underwriting action.

Turning now to the surety portion of the CSI book, net written premiums were down 5% to $72 million. This compares to an increase of 8% in the Second Quarter of 2014 and was driven by a decrease in US construction activity among a few of our larger customers. As we have said in the past, surety is a lumpy business from both a premium growth and a combined ratio standpoint.

The combined ratio was 54.8% compared to 41.3% in the Third Quarter of 2013. Despite the occasional large loss, our expertise in customer selection, underwriting. And portfolio diversification have enabled us to achieve outstanding long-term results in our surety line making this business very attractive to us.

Before turning it over to Paul, I would conclude by saying, while the commercial market is competitive and quite frankly, it always is, our value-added underwriting driven approach continues to work very well. Our strong loss ratio, improved retention levels. And increased new business volumes demonstrate our ability to succeed in this market place. With that, I'll turn it over to Paul who will review our results for CPI and corporate-wide claims.

Paul Krump {BIO 5211397 <GO>}

Thanks, Dino. Chubb Personal Insurance performed very well in the Third Quarter. CPI net written premiums increased 6% to $1.2 billion. And CPI produced a combined ratio of 85.9% compared to 88.3% in the corresponding quarter last year.

The impact of catastrophes on CPI's Third Quarter combined ratio was 3.5percentage points in 2014. In the Third Quarter a year ago, the cat impact on CPI's combined ratio was 7 points. On an ex-cat basis, CPI's combined ratio in the Third Quarter of this year was

82.4% versus 81.3% in the corresponding quarter last year. Homeowners premiums grew 4% in the quarter and the combined ratio was 80.3% compared to 84.3% in the corresponding quarter last year.

Cat losses accounted for 5.6 points of the Homeowners combined ratio in the Third Quarter of 2014 compared to 11.1 points in the Third Quarter of 2013. Excluding the impact of catastrophes, the 2014 Third Quarter homeowners combined ratio was 74.7% compared to 73.2% in the same period a year ago.

You may recall that during last quarter's conference call, we talked about the elevated level of US homeowners fire and ex-cat weather losses we experienced in the first half of this year. We discussed the randomness of these types of losses. And that in the short term, good or bad fortune can play a meaningful part in the loss ratio performance. We went on to say that we believed our book was well underwritten. And that the losses should average out over time.

The Third Quarter bore this out and in fact, the impact from fire and ex-cat weather losses was consistent with our five-year average for such losses. As a result. And including a small benefit from typical Third Quarter seasonality, the fire and ex-cat weather impact in the Third Quarter was 9 points lower than the average impact in the first and Second Quarters of this year.

Homeowners rate and exposure renewal premium increases totaled 7% in the US in the Third Quarter. The same as in the Second Quarter. As we have noted in the past, our panorama analytics give us the ability to very accurately pinpoint the right price for each risk in our portfolio. This enhances the retention of our best-performing accounts, while enabling us to secure equitable rate increases for the others, thus making the entire portfolio stronger.

In personal auto, written premium growth was 3% for the quarter. The Personal Auto combined ratio was 95.2% compared to 95.8% in the corresponding quarter a year ago. CPI policy retention in the US in the Third Quarter was 90% for Homeowners and 89% for Personal Auto. Both were unchanged from the Second Quarter of this year.

In Other Personal, which includes our accident, personal excess liability and yacht lines, premiums increased 13% and the combined ratio was 95.4% compared to 94.9% in the Third Quarter a year ago. Growth in Other Personal was driven by accident and personal excess.

Turning now to corporate-wide claims, catastrophe activity for the Third Quarter was relatively quiet with losses totaling $74 million before tax. There were six cat events in the US, two in Canada. And one in Mexico. The events included wind, hail, flood. And earthquake. And no single event was individually significant. The cat claim dollars were about evenly split between personal and commercial.

And now, I will turn it over to Ricky who will review our financial results in more detail.

Ricky Spiro {BIO 15061279 <GO>}

Thanks, Paul. Looking first at our operating results, we had strong underwriting income of $439 million in the quarter. Property and casualty investment income after tax was down 4% to $270 million due once again to lower reinvestment rates in our fixed maturity portfolio.

Net income was higher than operating income in the quarter due to net realized investment gains before tax of $110 million or $0.30 per share after tax of which $0.12 per share came from alternative investments. For comparison, in the Third Quarter of 2013, we had net realized investment gains before tax of $18 million or $0.04 per share after tax including $0.06 per share of net realized gains from alternative investments. As a reminder, unlike some of our competitors, we do not include our share of the change in the net equity of our alternative investments in property and casualty investment income. We include it in net realized investment gains and losses.

Unrealized depreciation before tax at September 30 was $2.5 billion compared to $2.6 billion at the end of the Second Quarter. The total carrying value of our consolidated investment portfolio was $44.1 billion as of September 30, 2014. The composition of our portfolio remains largely unchanged from the prior quarter. The average duration of our fixed maturity portfolio is four years and the average credit rating is AA3.

We continue to have excellent liquidity at the holding company. At September 30, our holding company portfolio had $1.8 billion of investments, including approximately $425 million of short-term investments. Book value per share under GAAP at September 30, 2014, was $70 compared to $64.83 at year end 2013. And $62 and $0.04 a year ago.

Adjusted book value per share, which we calculate was available for sale fixed maturities at amortized cost, was $65.17 compared to $61.86 at 2013 year end and $58.52 a year ago. As for loss reserves, we estimate that we had favorable development in the Third Quarter of 2014, our prior-year reserves by SBU as follows. In CPI, we had about $10 million; CCI had about $55 million; CSI had about $90 million; and the runoff reinsurance assumed business had none bringing our total favorable development to about $155 million for the quarter.

This represents a favorable impact on the Third Quarter combined ratio of about 5 points overall, including an adverse impact from prior year catastrophes of less than $10 million. For comparison, in the Third Quarter of 2013, we had about $190 million in favorable development for the Company overall including $20 million in CPI, $100 million in CCI, $70 million in CSI. And an insignificant amount in reinsurance assumed. The favorable impact on the combined ratio in the Third Quarter of 2013 was about 6 points overall including slightly less than half a point from catastrophes.

For the Third Quarter of 2014, our ex-cat accident year combined ratio was 88.6%, the same as in last year's Third Quarter. During the Third Quarter, our loss reserves decreased by $9 million, including an increase of $1 million for the insurance business and a decrease of $10 million for the runoff reinsurance assumed business. The overall decrease in reserves reflects a decrease of $58 million related to catastrophes. The impact of currency translation on loss reserves during the quarter resulted in a decrease in reserves of about $75 million.

Turning to capital management, during the Third Quarter, we repurchased approximately 4.7 million shares at an aggregate cost of $425 million. The average cost of our repurchases in the quarter was $90.38 per share. At the end of the Third Quarter, we had $399 million available for share repurchases under our current authorization. And as we have said previously, we expect to complete this program by the end of January 2015.

Let me conclude with a few comments on the revised guidance we announced in today's press release. As John mentioned, based on our nine-month results and our outlook for the Fourth Quarter, we are revising our 2014 full-year operating income per share guidance to a range of $7.35 to $7.45 from the previous guidance range of $6.75 to $6.95. This revised guidance is based on operating income per share of $5.35 in the first nine months and an estimated range of $2 to $2.10 for the Fourth Quarter.

The revised guidance assumes 2percentage points of cats for the Fourth Quarter which would result in 3.9 points of cats for the calendar year. This compares to the full-year cat assumption of 5.3 points included in our previous guidance. The decrease being due to the lower than expected cats in the Third Quarter.

The impact on 2014 operating income per share of each point of cats for the full-year is approximately $0.33 and the impact on Fourth Quarter operating income per share of each point of Fourth Quarter cats is approximately $0.09. The revised guidance is also based on an assumption of 243 million average diluted shares outstanding for the full year.

And now, I'll turn it back to John.

John Finnegan {BIO 1735942 <GO>}

Thanks, Ricky. We had an excellent Third Quarter and the numbers speak for themselves. Let me summarize a few of the key highlights. We had record operating income per share of $2.17 and net income per share of $2.47, our second best quarterly result.

With respect the US market, we continued to enjoy mid-single-digit rate increases while maintaining our overall high retention levels. The upshot was ex-currency premium growth of 5% in the quarter consistent with the Second Quarter and up from 3% in the first half of this year. All three SBUs contributed to our profitability for the quarter.

We were particularly pleased by the results of our professional liability business which reflected rate increases and our ongoing underwriting initiatives. Our Third Quarter combined ratio in professional liability of 81.3% represented almost a 6.5 point improvement from the Third Quarter of 2013 and about a 15 point improvement from the Third Quarter of 2012. In fact, the 81.3% posted in the Third Quarter is better than our professional liability performance in any quarter over the past seven years.

We had an excellent overall combined ratio of 85.8%, with an ex-cat combined ratio of 83.4%. Our annualized GAAP ROE was 14.4% and our annualized operating ROE was 14.1%. GAAP book value per share at September 30 was $70, up 13% from a year earlier and 8% from a year end 2013. For the first nine months of 2014, on a per share basis, both the operating income of $5.35 and net income of $6.28 were our second best nine months results ever.

We returned a total of $1.6 billion to shareholders through share repurchases and dividends through nine months, including $544 million in the Third Quarter. Our strong performance in the Third Quarter and outlook for the Fourth Quarter have enabled us to increase our 2014 operating income per share guidance to a ranges of $7.35 to $7.45.

The midpoint of our revised guidance is $0.55 per share higher than the midpoint of our July guidance of $6.75 to $6.95. And $0.15 per share higher than the midpoint of our initial January guidance. Achievement of this updated guidance would result in the second highest full-year operating income per share in the Company's history.

In summary, we had a great Third Quarter and we continue to be pleased with our underwriting performance with respect to both risk selection and pricing. With that, I'll open the line to your questions.

Questions And Answers

Operator

(Operator Instructions)

Mike Nannizzi with Goldman Sachs.

Q - Mike Nannizzi {BIO 15198493 <GO>}

Thank you. To start off here, growth was clearly better than we had in all of the segments. That was fantastic. But just trying to understand the combined ratios, excluding development and cats, look like they were a bit light, again, in all of the segments. Just trying to understand was there some underlying or unusual weather or anything else that was going on there? Maybe something in specialty as well or is there any relationship between accelerated growth and the deterioration in underlying? Thanks.

A - John Finnegan {BIO 1735942 <GO>}

Mike, you need to elaborate. What are you looking at in terms -- I guess you are looking at our -- you are trying to focus on ex-cat accident combined ratio? Is that what you're referring to?

Q - Mike Nannizzi {BIO 15198493 <GO>}

If I peel out development and cats, we were assuming with pricing that was coming through, that there would be some margin improvement year over year. And you grew a lot more. But it didn't seem like there was a lot of margin improvement year over year. So I was just trying to square why that might be. And is it maybe that you are pursuing growth more actively? Your profitability hurdles? Just trying to get some understanding there. Thanks.

A - John Finnegan {BIO 1735942 <GO>}

I think that what you are really talking about is first of all, our accident year, this Third Quarter this year versus Third Quarter last year was about flat. And this year, while we've been talking. And Dino and Paul have both talked about the fact that our Third Quarter losses in the area of homeowners, non-cat related weather and fire losses, as well as property, marine. And commercial, represented a good deal of improvement from the Second Quarter. It was still somewhat higher than our average in those areas over time and certainly higher than the Third Quarter of last year which was a pretty low quarter.

The headwind was again, sort of unusual losses which were better. Better than the first half and not so bad that we couldn't generate record results. But the comparison is difficult because of the unusual low level last year of these type of losses. And specialty was a record and our loss ratio was about three points higher than an accident year than it was last year at this time.

Q - Mike Nannizzi {BIO 15198493 <GO>}

Right. Great. Okay. That makes sense. Thanks. Then just on comp, it looks like one of the few lines in the Commercial segment where premiums didn't grow and it's been a big grower here recently. It seems like that's an area that is still getting a lot of rate. Can you talk about kind of the dynamic there? Is it just other areas are more attractive maybe or from a concentrations standpoint maybe?

A - Dino Robusto {BIO 15021398 <GO>}

It's Dino. In general, the work comp growth has been decelerating from prior years when we were achieving large double-digit rate increases. Also in the Third Quarter, the growth was impacted by a little bit of less new business, which frankly can fluctuate quarter by quarter. We don't target mono-line work comp. So it depends more on the number of multi-line opportunities we see in the quarter.

Additionally, there was some policies that renewed this quarter with policy revisions that changed the structure from guaranteed cost to large deductible. This has the impact of lowering premiums as insurance assumes more of the losses. But clearly we are very pleased with our work comp results. We have great results and we continue to be very optimistic about it.

Q - Mike Nannizzi {BIO 15198493 <GO>}

Great. Thank you. So much.

Operator

Jay Gelb with Barclays.

Q - Jay Gelb {BIO 21247396 <GO>}

Thanks. Good afternoon. I also had a question about top line growth. How much of this is being driven by exposure growth versus new business?

A - Dino Robusto {BIO 15021398 <GO>}

Actually, in commercial, the exposure growth was minus 1% in the Third Quarter of 2014, which is an improvement about a point from the Second Quarter and it's roughly comparable to what was in the Third Quarter. So it's slightly down.

A - Paul Krump {BIO 5211397 <GO>}

On the homeowners side, Jay, we had rate and exposure increases that totalled 7% and that was pretty evenly split between rate and exposure.

Q - Jay Gelb {BIO 21247396 <GO>}

That's helpful. Thank you. Also, I've been trying to get a perspective on what benefit to Chubb there could be from the big decline in reinsurance rates. Can you give us some perspective on that? How you are thinking about it this year and also for 2015?

A - Dino Robusto {BIO 15021398 <GO>}

Sure. The benefit I guess would be several fold. The obvious one being that we have been able to enjoy lower reinsurance costs based on the renewal of our major cat treaties back in April. So that obviously will be helpful. And that we use other reinsurance as well. Although we are not a big buyer, we do have some other reinsurance programs in place. So that's always helpful.

We obviously are paying close attention to the developments in the marketplace. And looking at all the different things that are going on and all the different structures. And we have an open mind about it. We're monitoring whether some of these alternatives would help improve our overall performance of a portfolio either by promoting growth or by managing some of our volatility. And we'll continue to look at some of these.

We haven't found any of these big new structures that make sense for us at the time being. But we are looking at them. Our individual businesses are looking at the lower reinsurance cost to see if there is ways that it can benefit their business. So we're keeping an open mind. And it's kind of hard to pinpoint exactly how the lower reinsurance costs will impact us but clearly, in the near term we are going to enjoy the benefit of lower costs.

Q - Jay Gelb {BIO 21247396 <GO>}

That's great. Thank you.

Operator

Josh Stirling with Bernstein.

Q - Josh Stirling {BIO 17463087 <GO>}

Hi. Good evening. Thank you for taking the call. First a question on commercial and professional lines for Dino. Year to date, you guys have had really strong improvement in casualty results. Broadly defined, your casualty I think has improved 5 points year over year, workers comp similar, professional liability something like 7. And so all of these long-tail lines are now running between 83% and maybe a 90% on a combined. That's really impressive results but I am wondering if -- how sustainable will you guys think this is going to be?

Can we be thinking about you as running in the 80s in cat and casualty lines which seems a good result for long term? And I'm wondering if maybe you can give us some color around sort of what target combined ratios you actually price to and how you think about the underlying run rate profitability in these businesses that's realistic to the future.

A - Dino Robusto {BIO 15021398 <GO>}

Josh, it's Dino. We're not going to be able to speculate about what it's going to be in the future. Clearly, if you look at our historical results, we have generated strong performance. We're obviously very disciplined underwriters. We continue to do that. We're also -- continue to get some good rate increases. So we are going to continue to do what we do, be very cautious, look for the opportunities. And we think there are good opportunities out there for the long-tail lines, casualty, professional liability.

We have very diversified portfolios, diversified also around the globe by geography so that gives us some opportunity. As you know, we are niche underwriters. We focus on a couple of dozen very specialized segments. And we have generated an enormous amount of expertise, specialized products and services, specialized claims handling. And those are the areas we focus on. Those are the things we're going to continue to focus on. We continue to be very optimistic about the opportunities. But hard to say how it's going to play out and in particular long-tail lines over time.

A - John Finnegan {BIO 1735942 <GO>}

Joshua, we'll We will accept the kudos and directionally we understand the question. But casualty didn't have a particularly great quarter. It was 95. So we weren't running the low 80s. And for the first nine months, 90 is a great number for casualty. But we aren't running in the low 80s or anything in that line of business.

Q - Josh Stirling {BIO 17463087 <GO>}

Okay. Well we will stay tuned. Paul, I wonder if I could ask you just a question. We don't spend as much time with you guys because this is our one chance each quarter. Big picture when you think about the high net worth business. Your homeowners business might be the best property business in the country. But it's attracted a lot of competition in recent years.

I was wondering, to sort of build on Jay's question, thinking about all the new capital flowing into the industry and just given how hard it is to get a coastal home insured these days. And how much potential premiums there are in the market for that. Whether you're thinking about this as something that you guys have to respond to, because ultimately there may be some pressure from others trying to take smaller firms using more alternative capital and be much more competitive and what really has historically been the sweet spot of your business.

A - Paul Krump {BIO 5211397 <GO>}

Sure, Josh. Let me kind of back, just give you our perspective on this. There has been an awful lot of chatter, I guess, about a couple of new entrants into the marketplace over the last four or five years. And that is true. But we have also seen recently one of the longer-term players that has specialized in this area who looked to be exiting the business. New entrants come, new entrants go. I'd say all of the competition in my mind is really not that much greater than it has been for decades.

The bulk of the ultra high net worth and high net worth business really resides with the direct writers. When you look at the handful of players that specialize in the high net worth space with us, we probably make up about 20%, 23% of what we define as the high net worth and ultra high net worth market place. We occasionally are trading accounts. We have certainly stepped up and used some reinsurance maybe more aggressively in the last 12 months where pricing is at.

We've been trying to get that on longer-term basis so that we can offer our clients some stability. We are not immune to slugging it out with a couple of these players on some business but ultimately, we are trying to take market share from the direct writers and a lot of the regional players because that's where the bulk of the businesses. There's plenty of room for everybody to grow in this business.

Q - Josh Stirling {BIO 17463087 <GO>}

Okay. Thank you. Good luck.

Operator

Josh Shanker with Deutsche Bank.

Q - Josh Shanker {BIO 5292022 <GO>}

Good evening, everyone. I wanted to get a sense of your house view of weather. I know that you said that compared to 3Q 2013, 3Q 2014 had a lot more non-cat weather. Was this a bad quarter? Was 3Q 2013 a good quarter?

When I hear non-cat weather, my gut tells me you are talking just about the weather. It's difficult for me to contemplate that things didn't seem aggressively difficult for insurers over the past three months. But maybe I'm wrong about that. Maybe you have a decade worth of thought about where we are.

Is this worse than we've seen over the past decade? Is this a normal quarter? What's the house view?

A - John Finnegan {BIO 1735942 <GO>}

I'd say this. If you just compared to a five-year average, the Third Quarter was a little --. You know, we're talking -- we're looking at a couple of things and the homeowners line we're looking at non-cat weather and fire losses, which may be more significant this time of year than non-cat weather. In commercial, property. And marine, we are looking at large losses but as a proxy for it, we look at the movement in the combined ratio, especially since any negative movement in property and marine, probably due to large losses because we have been getting rate in that line of business. So it's not due to deteriorating margins. It's a rough proxy.

I'd say that what you have to start with is last year, let's take commercial property, we were in something like a 63 in the Third Quarter, unprecedented sort of third best. And second best in ten years. This Third Quarter was worse than last year. It was a little bit worse as you combine all of these areas, a little bit worse than the five-year average, not much. And the five-year average may be distorted a little bit but in extremely low years, we had great experience. We used to talk about it back two or three years, we had some great experience.

So we're not unhappy where we came out in terms of these unusual loss areas. But they weren't unusually low. They were a little bit higher than the norm. Much, much better than the Second Quarter. Worse than what was an unusually good Third Quarter last year.

Q - Josh Shanker {BIO 5292022 <GO>}

That sounds perfect. I don't mean to make any difficulties. I'm curious when you talk about the announcement of your retirement coming soon, is there any thoughts about when we will learn about succession planning and what not?

A - John Finnegan {BIO 1735942 <GO>}

That's an ongoing process and it is ongoing. The Board is working hard at it. But I have no idea when we would be making any announcements or any disclosure. We are a long ways away. I've still got almost two and a half years to go.

Q - Josh Shanker {BIO 5292022 <GO>}

Okay. Thank you very much. And congratulations on a good quarter.

Operator

(Operator Instructions)

Vinay Misquith from Evercore.

Q - Vinay Misquith {BIO 6989856 <GO>}

Hi. Good evening. I was wondering if you could touch on lost cost trends and also looking at pricing is about 3% right now in the commercial. Are you comfortable with seeing margins decline in the future especially considering that the yield on the investment portfolio is still declining for maybe the next couple of years? Thanks.

A - John Finnegan {BIO 1735942 <GO>}

You know I think CCI earned premium rate increases are about 5%, a little bit higher than the written. I think the basis of the question is that if earned rates went down to 2% or 3% like written rates, is margin contraction inevitable? In answer to your question why I like higher rates, yes but I think the answer to the question about margin contraction being inevitable or combined ratios increasing, is that it's not but like most things, it's complicated and can go a number of ways.

I think some of it is definitional. Let's take -- when we talk about long-term long run loss cost trends, we generally mean -- well let me just think what we call longer-term loss cost trends and expected lost cost increases. When we talk about long-term loss cost trends at Chubb, we generally mean the economic forces. Our portfolio face before consideration of any underwriting strategy.

Let's take workers compensation. The trends we're talking about simply mean the expected long-term upward trend in average severity over time due to the increasing cost of medical care, as well as higher wage replacement cost. And higher statutory indemnification of various types of injuries. Given the nature of these type of longer-term costs generally effect industry participants with similar business mix in a similar way. They can't do anything else.

What we call longer-term loss trends are based on macroeconomic factors and implicitly assume a passive underwriting approach. But in reality, we are constantly seeking to improve our business through focused underwriting initiatives. So let's go back to workers compensation. These initiatives include the ongoing reprofiling of the book and the success we've had in reducing the cost of fraud through our predictive analytics and case management practices. We don't adjust downward. Importantly, we don't adjust downward what we call longer-term loss cost trends for the positive impact of these underwriting initiatives. But they're obviously factored into our expected loss cost increases. The basis on which we. And you, should assess the future profitability of our products.

Bottom line, if we are successful in our underwriting initiatives, our costs should be 1 to 2 points less than the short term and the long-term lost cost trend itself. But let's put the numbers together. That while we might have a 4% longer-term trend from a macroeconomic factor, our expected short-term loss increase is closer to 2 to 3 points. That's a range which is often cited by other carriers as their loss trend rate. Again though, since we believe the longer-term macroeconomic trends similarly effect carriers in similar lines of business, I think this probably just represents sort of a definitional difference. As we develop our forecast for the coming year, we will be comparing forecast rate changes to our expected short-term loss increases. These vary by line and by the success of various underwriting initiatives. But are in the aggregate closer to the 2 to 3 point range than the 4 point longer-term loss trend.

Also, another caveat but even then combined ratio projections based solely on this margin analysis will rarely be accurate, because actual losses in any given period are often a good deal above or below longer-term loss trends. That's what we been talking about in this quarter. Since predicting variances a year out is virtually impossible, the focus has got to be determined on whether or not the base period from which you are extrapolating, which is today, is representative of longer-term trends so you need to adjust the (inaudible) unusually high or low.

I worked up an example to see how distorted this analysis could be at Chubb. If you go to last year, we ran a CPI at an unusually low combined ratio ex-cat of about 80% in the first nine months of 2013. Since earned rates have exceeded long-term loss trends by about 3 points over the ensuing 12 months in the time in between, you would have projected a simple margin analysis that we would've run a 77% in the first nine months of 2014. In actuality, our ex-cat combined ratio for CPI for the first nine months of 2014 was 86%. So 6 points worse than last year and about 9 points worse than would have been implied by margin expansion analysis.

What's the reason? It simple. Actual year-over-year loss experience deviated significantly from longer-term loss trends. And I obviously picked a period in which the deviation was large. For example, our homeowners non-cat weather and fire losses, which fluctuate significantly from quarter to quarter, were extremely low in the first nine months of 2013. That's the base period that would be used for the projection. And unusually high in the first nine months of 2014, the endpoint of the projection. This confluence of unusually deviant loss experience greatly subsumed the impact of rates being higher than theoretical long-term loss trends.

You'd find a similar example if you looked at CCI over this period although to about half the extent. You would have greatly overestimated our 2014 CCI profitability because it would've been based on a historically low base period for property losses. Going forward, I just warn that to project CCI combined ratio next year simply based on margin expansion or contraction analysis is probably flawed. I don't know what the real answer is going to be but the fact is that our property losses in the first nine months of this year were far higher than not only last year but our average experience was somewhat higher than our experience over the last five years.

When we look at it, we don't know and we could be wrong but as a starting point, we expect some reversion to loss levels closer to historical norms when we develop a forecast. And we saw some of that in the Third Quarter although, in this area, these things aren't linear and Third Quarter improvement will have nothing to do with what will happen next year. But basic projection analysis, we assume a little bit of reversion to more normal levels. This is the type of thing you should remember.

We were talking about last year from the other end when we said don't extrapolate based on 3 points of margin expansion to our current combined ratio because this thing is darn low. It isn't representative of -- it isn't a representative base period from which to extrapolate. I think nine months this year is similar but not to such a great magnitude on the other side. It's somewhat high.

Like most things complicated and it probably more than you ever wanted to know about it. But I think the answer is I wouldn't -- if earned rates are 2% to 3%, for a variety of reasons I wouldn't necessarily assume we're going to have margin contraction next year. We'll offset some of that with underwriting initiatives. And then it could go either way based upon actual loss experience. But I think the base period has to be adjusted for something that's a little bit more normal if not totally the norm. That's it.

Q - Vinay Misquith {BIO 6989856 <GO>}

That's very helpful. Thank you. Just as a follow-up, the expense ratios in personal insurance and professional liability declined about a point each. Just curious what's happening there.

A - John Finnegan {BIO 1735942 <GO>}

I think the expense ratio was down about a half a point, wasn't it, overall. And a lot depends on relative growth between the SBUs in the period. That drives it. There's nothing significant there. Overall, our expense ratio is down somewhat because of growth and also because of the fact that our comp expense is a little bit down from last year, especially in the pension area where we benefited from terrific performance in 2013. And also a very low year end 2013 interest rate from which we reevaluated our liabilities and we got a reasonably significant positive impact. That will reverse partially going into 2013 if interest rates continue at the current levels.

Q - Vinay Misquith {BIO 6989856 <GO>}

Thank you.

Operator

Kai Pan with Morgan Stanley.

Q - Kai Pan {BIO 18669701 <GO>}

Good evening. Thanks for taking my call. The first question is on the growth really from the acquisition perspective. So if you look at the platform, is there any lines of business or geography you would like to grow faster and potentially through acquisitions?

A - John Finnegan {BIO 1735942 <GO>}

There's probably a lot of areas we'd like to grow. We'd certainly like to grow overseas, although the economics and currency haven't helped us. And we're recently diversified. But haven't helped us recently. We have 25% of that business. There are niche areas like, for example, a big growing area is accident and health. It's been an outstanding success. But I can't say that we are looking to growth through acquisitions. That hasn't been in our

DNA. And we have no reason to -- you should have no reason to believe that we are looking at it any differently now.

Q - Kai Pan {BIO 18669701 <GO>}

Okay. That's good. Then secondly on reserve side. It looks like the CCI have a big drop from year ago period. I understand that each quarter probably has some big variations like quarter from quarter. Anything behind that? And also some of your peers have been reporting higher reserves additions for the asbestos and environmental charges. And just wondering if you have seen similar trends in your reserve book.

A - Ricky Spiro {BIO 15061279 <GO>}

Sure, Kai. It's Ricky. I'll address this. The question I think you are asking is did the change in prior period development from the year ago Third Quarter. So in CCI it was 100, this quarter it was 55?

Q - Kai Pan {BIO 18669701 <GO>}

Yes.

A - Ricky Spiro {BIO 15061279 <GO>}

Okay. Terrific. A couple of thoughts. The one thing it was driven -- the drop was driven in large part by property and marine. In the Third Quarter 2013 given some of the comments you heard John talk about where we had very favorable property experience last year. Property marine was significantly favorable in the Third Quarter of 2013 but it was flat in this quarter. In addition on the A&E side, we did have some adverse development in A&E. But it wasn't a huge amount of money. But there was some adverse development. Paul can give some color on that if you'd like.

A - Paul Krump {BIO 5211397 <GO>}

Sure. We incurred $11 million of asbestos losses in the Third Quarter. We had $15 million incurred on environmental losses in the quarter. They're really was no -- there's nothing really behind it. There's no new asbestos loss theories or trends going on. These changes were really just from developments on a handful of accounts. In particular, they were from a couple of excess liability layers that we wrote in the past that we didn't think that would hit our layer. But they did.

Q - Kai Pan {BIO 18669701 <GO>}

Great. Thanks for the details.

Operator

Cliff Gallant with Nomura Securities.

Q - Clifford Gallant {BIO 1854853 <GO>}

Thank you. Wanted to ask about cyber insurance, whether or not it's a product line that you expect could be meaningful. And two as a follow-up to that, is there any risk to your, D&O, professional lines from cyber risk exposures?

A - Dino Robusto {BIO 15021398 <GO>}

Hi. It's Dino. We have been thoughtfully underwriting cyber for several years. We have a small book that has performed well so far. And it's really based on our disciplined underwriting that is often informed incidentally by consultation one of the leading cyber breach consulting firms.

We also offer extensive risk mitigation support to our customers. We have a good team of cyber specialists that know how to that understand the cyber threats and know how to underwrite it. Of course, this is always -- it's very dynamic so they're always actively monitoring the cyber threat, the landscape. And a balance the portfolio across industry segments. And they avoid exposure to high risk industries such as large retailers and payment card processing firms.

We have a balanced portfolio. It's balanced by size of accounts, limits of insurance, we focus on companies that understand the threat and are prepared to respond appropriately. And so it's a conservative approach. And we are comfortable for now with our methodical approach to it. We also have a quarter share reinsurance that protects us on cyber. So small book, conservative underwriting. And that's how we'll continue to move it forward. Cliff, does that answer your question?

Q - Clifford Gallant {BIO 1854853 <GO>}

Yes. Thank you. And is there potential exposure in the professional lines?

A - Ricky Spiro {BIO 15061279 <GO>}

There could technically be n exposure to the extent there are situations where you could have large breaches. And the directors and officers are viewed as having managed it effectively. Now again, as I was just indicating, we tend to avoid the larger exposure types relative to our book. But in general if you're asking, you could end up having some D&O exposure if you've got a large cyber breach.

Q - Clifford Gallant {BIO 1854853 <GO>}

Okay. Thank you.

Operator

Meyer Shields with KBW.

Q - Meyer Shields {BIO 4281064 <GO>}

Thanks. Good afternoon, all. You mentioned when you're talking about surety that there was a slowdown in construction activity. Does that look like something systemic to you or just sort of randomness?

A - Ricky Spiro {BIO 15061279 <GO>}

No, more just randomness. We have a very, very high quality portfolio of surety contracting firms and engineering firms and really in any one quarter, as I said, it is lumpy. And the prior period we compared it to had growth. It's just a question of they didn't have -- they didn't get the sort of contracts that we saw in the same period last year. But we believe our customer and the prospects they have, because they are clearly the highest-quality companies. We continue to think that they are going to win in the markets. So we remain very optimistic and the growth potential for our surety business. There's just some lumpiness.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. Thanks. When we look at the various -- I guess I'm thinking workers compensation and professional liability, has there been any change in the claim frequency regardless of whether those claims are ultimately successful? Have you seen that over the past few years?

A - Ricky Spiro {BIO 15061279 <GO>}

I will turn it over to Paul to let him talk about some of the claim trends.

A - Paul Krump {BIO 5211397 <GO>}

The claim trends overall are fine. It's actually been very, very benign. The claim counts on the book are up about 1% Q3 over Q3 2013. If you think about the premium growth over that period of time, that is next to nothing. Even more impressive, I think, is if you look at the first nine months of 2013 and compare it to the first nine months of this year, you have a 1% increase in the overall claim count. It's been a very steady stable number.

Q - Meyer Shields {BIO 4281064 <GO>}

Does that flow through to workers comp also?

A - Paul Krump {BIO 5211397 <GO>}

Yes. Obviously, it varies a little bit by line. They think the -- they are really -- I don't have that exact number tight in front of me but they are all clumped in there. There's not a lot going on there on any one of many big changes. Probably one of the numbers that sticks out the most is what we've been watching like the EPL claim activity. And from a frequency standpoint there, there's been a real nice decrease in the notification -- new rise of claim activity over the past couple of years. We've been excited to see that because obviously we've been working on that book of business pretty hard.

The other area that we've seen some decent movement in the merger and acquisition of objection claims. We brought a couple of underwriting tools to bear there. One was just a propensity to see those kind of suits and another was just an all-out effort to raise the deductible specifically for merger and acquisition objection claims. In the past, let's say we had 18% to 20% of the market, we'd have a catch rate on those M&A claims that say 18% to 20% so it pretty much matched up with our market share today. That catch rate is cut in half. Then you add on the impact of deductibles and you really see what Dino was talking about before about the importance of applying underwriting tools and techniques to the book.

A - Dino Robusto {BIO 15021398 <GO>}

Just to pick up on a point that John made clearly and back to your point on work comp. One thing that's a little bit structural is the predictive modeling and the analytics that we have now applied on the claim side. And in particular related to its ability to mitigate fraud clearly a lot more effectively. We are seeing some benefit from clearly our investments in predictive analytics on the claim front for workers comp claims specifically to your point.

Q - Meyer Shields {BIO 4281064 <GO>}

Okay. Fantastic. Thank you very much.

Operator

Ian Gutterman with Balyasny.

Q - Ian Gutterman {BIO 18249218 <GO>}

Thank you. So I guess couple of things. First on CCI, you talked about pricing is down just 3% and where that is versus last year. And so forth. I was sort of curious about the bigger picture question. Do you view 3% here as approaching the floor or are you concerned that given what you're seeing competitively from others that next quarter might be 2% and the quarter after that is 1% and so forth.

A - John Finnegan {BIO 1735942 <GO>}

Ian, the simple answer is I don't know. We do know a few things. The industry had three years of pretty reasonable rate increases and we also know that this year rates have continued to increase but at incrementally lower levels. It's hard to deny that the environment for rate increases is less favorable that it has been in the last few years. I guess there are some obvious factors. We are going after fourth year rate increases. The carriers all have growing price adequacy in their books. It overall increases in the competition.

The good news today is that the (climate) rate increases has been incremental. In our case, about a point a quarter in commercial professional liability lines. Going forward, barring some extraordinary event I guess it's likely that the recent pressure on rates will continue. It will be hard to argue with a thesis that rate increases will be less next year than they were in the past year. Having said all of that, I'll refer to my initial response which was that I don't know where rates will eventually go. I talked about the fact that it's driving the market down and why couldn't persist on the other (technical difficulty).

And finally, interest rates remain incredibly low so that places a great pressure on combined ratio that could only be sustained by adequately priced business. So I guess like the two-handed economist. On one hand I expect recent downward pressure on rates to continue. But I also expect any market softening to be less precipitous than it was in past cycles. I don't know whether that means that the level of rate increases stabilized at inflation or even at zero. And in each line it could be different.

All I can say if Chubb will react to these circumstances by doing what we do best, selecting the best risk, underwriting carefully, leveraging a superior expertise in claims. And cultivating strong relationships with the producers. And we'll see where it goes. The pressure is there but it's not clear how much more it will grow.

Q - Ian Gutterman {BIO 18249218 <GO>}

Got it. And are there any places where you are seeing, whether it be large accounts or excess layers or any type of business where there is more below the three than above the 3?

A - Dino Robusto {BIO 15021398 <GO>}

I can give you a little bit of color. I think in general, clearly the market is competitive. But I think the pricing dynamics are rational. What you see is usually the most profitable accounts is where you are going to see rising pressure. And that make sense. But to your point, in terms of lines of business property, a little bit more competitive and especially in the larger premium accounts.

Professional liability, you actually see a similar dynamic in the industry with better business be more aggressively priced larger premium tends to attract much more interest. Then across our lines of business, a few of them are a little bit above that average. And then a couple of lines of business below that average. And it's usually also pretty rational if you look at, for example, in professional liability certain lines like EPL that have been less profitable for -- in the industry. And also for us. Still getting rate increases that are higher than the overall 5 points that we are getting in professional liability.

So there is clearly variation. Then just in general, this is a business, our aggregate number is really a function of all of the individual account decisions that we make and there is still a considerable amount of variation on an account basis, if you look at it in our book of business.

Q - Ian Gutterman {BIO 18249218 <GO>}

That helps. That's great. If I could ask one more on professional lines. I was just looking the year-to-date development reserve releases, is the best in about four or five years. I was just curious if you can give any color by accident year or by line of business and especially in the beginning of the year there was some concerns that might tail off. Just doing the crude analysis, the triangles and they obviously haven't proven out. I'm just sort of curious to where the upsides come from.

A - John Finnegan {BIO 1735942 <GO>}

Yes, I thought going into the year that being conservative, we thought that we've been running pretty high levels of overall favorable development. And that we'd -- it certainly might be prudent to suggest that favorable development could decline this year. I guess it has really. In the Third Quarter, it was down a significant amount. Happens professional liability went the other way. Our loss experience continues to prove very good in that area. I couldn't be happier with that. In terms of where it comes from, I think it comes from like in 2010 and prior. And 2011 to 2013 we're each close to flat in the Third Quarter.

Q - Ian Gutterman {BIO 18249218 <GO>}

Got it. Thanks so much.

Operator

Jay Cohen with Bank of America Merrill Lynch.

Q - Jay Cohen {BIO 1498813 <GO>}

Thank you. Rick, you may have given this number and I apologize if you did. The new money yields where you are investing new assets, can you give us a sense of where that is?

A - Ricky Spiro {BIO 15061279 <GO>}

Sure. Not where we'd like it to be. But I will tell you where it is. Obviously, it does vary as we talked about in the past by asset class. But broadly speaking today, in our muni portfolio, in the US tax exempt portfolio, we're reinvesting it roughly 140 basis points lower than the mature and book yields on the weighted average of the portfolio. 35 basis points lower in our domestic taxable securities and roughly 70 points lower outside the US in our non-US fixed income investments.

Q - Jay Cohen {BIO 1498813 <GO>}

Surprising. That's helpful. Thanks, Ricky.

A - Ricky Spiro {BIO 15061279 <GO>}

Sure.

Operator

At this time, I show no further questions in the queue.

A - John Finnegan {BIO 1735942 <GO>}

Thank you very much for joining us and have a good evening.

Operator

That does conclude our conference for today. Thank you for your participation.