S&P Capital IQ

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The Hartford Financial Services Group, Inc. NYSE:HIG

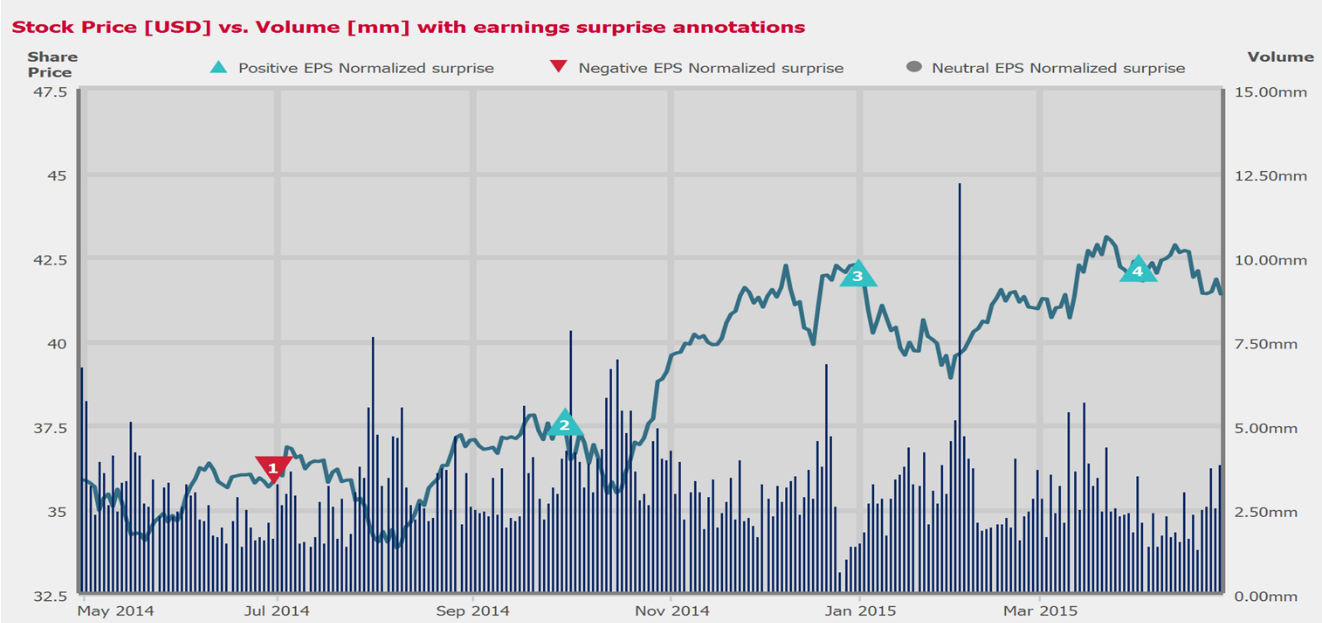
FQ2 2015 Earnings Call Transcripts

Tuesday, July 28, 2015 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ2 2015-			-FQ3 2015-	-FY 2015-	-FY 2016-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.77	0.91	▲18.18	0.96	3.94	4.18
Revenue (mm)	4742.00	4685.00	▼(1.20 %)	4795.36	18934.68	19178.58

Currency: USD
Consensus as of Jul-28-2015 12:26 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ2 2014	0.67	0.31	▼1 (53.73 %)
FQ3 2014	0.84	1.06	▲2 26.19 %
FQ4 2014	0.93	0.96	▲3 3.23 %

FQ1 2015	0.97	1.04	▲7.22 %

Call Participants

EXECUTIVES

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Chief Financial Officer and Executive Vice President

Christopher John Swift
Chairman & CEO

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President

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Presentation

Operator

Good morning. My name is Chris, and I'll be your conference operator today. At this time, I would like to welcome everyone to The Hartford's Second Quarter 2015 Financial Results Conference Call. [Operator Instructions]

Sabra Purtill, Head of Investor Relations, you may begin your conference.

Sabra R. Purtill
Senior Vice President of Investor Relations

Good morning, and welcome, everyone, to the Hartford's second quarter webcast. Our news release, investor financial supplement, second quarter financial results presentation and 10-Q were all released yesterday afternoon, and are posted on our website. Our speakers today include Chris Swift, Chairman and CEO of The Hartford; Doug Elliott, President; and Beth Bombara, CFO. Following their prepared remarks, we will have about 30 minutes for Q&A.

Just a few notes before Chris begins. Today's call includes forward-looking statements as defined under the Private Securities Litigation Reform Act of 1995. These statements are not guarantees of future performance, and actual results could be materially different. We do not assume any obligation to update forward-looking statements, and investors should consider the risks and uncertainties that could cause actual results to differ from these statements. A detailed description of those risks and uncertainties can be found in our SEC filings, which are available on our website.

Our presentation today also includes several non-GAAP financial measures. Explanations and reconciliations of these measures to the comparable GAAP measure are included in our SEC filings, as well as in the news release and financial supplement.

I'll now turn the call over to Chris.

Christopher John Swift
Chairman & CEO

Thank you, Sabra, and good morning, everyone. Welcome to the call. Last night, we reported strong financial and operational performance for the second quarter of 2015, completing a successful first half of the year. We continue to navigate in a dynamic market environment and reported improved results across all of our businesses.

Core earnings per diluted share for the second quarter was $0.91, a significant increase compared with the prior year. P&C, Group Benefits and Mutual Funds each delivered better operating margins and top line growth this quarter. This quarter's strong performance contributed to a 12-month core earnings ROE of 9.6%. The quarter also included net favorable items compared with last year, including higher limited partnership income, lower CATs, a federal tax benefit, lower A&E reserve strengthening and a favorable litigation outcome. Even when adjusting for these items, underlying results were strong. Doug will provide more details on P&C and Group Benefits in a few minutes, but I'd like to share with you a few highlights from the quarter.

In P&C, our combined ratio, when adjusted for CATs in prior year development, was 88.9, a 3.8-point improvement over the second quarter of 2014. We are especially pleased to see improved underwriting results in both Commercial and Personal Lines.

In Group Benefits, the results reflect our focus on new business generation and disciplined underwriting. Sales increased 29%, and after-tax core earnings margin increased to 6.3%. We continue to successfully manage the runoff of Talcott with year-over-year declines in variable and fixed annuity contract counts of 12% and 11%, respectively, since June 2014.

In addition to strong earnings, we are also pleased to announce that our Board of Directors approved an increase in the company's capital management plan and extended it through December 2016. Beth will review the details in a few moments. The plan reflects the successful strategic and financial transformation of the company, including a sharpened focus on P&C, Group Benefits and Mutual Funds businesses. Since the beginning of 2014, we have returned to shareholders more than $2.8 billion of capital. With the increase in this plan, we intend to return nearly $5.3 billion in share repurchases and common dividends over the 3-year period ending 2016.

Our primary refocus going forward continues to be on the profitable expansion of P&C, Group Benefits and mutual funds businesses where we hold competitive market positions. As you know, we have been investing aggressively in these businesses with a goal of improving operating capabilities. This effort includes a significant upgrade in technology, such as our market-leading Small Commercial icon system and the recent introduction of a new claims platform, and we have additional upgrades planned. As we consider management of excess capital in the future, we will prioritize opportunities that accelerate our premium growth and operating capabilities. In the event that we do not find opportunities that meet our strategic and financial objectives, we will continue to return excess capital to shareholders.

Looking forward, I am confident that we have the right strategy, capabilities and people required to successfully compete in a dynamic market environment. The Hartford strategy is focused on 4 areas: First, is product expansion. We continue to expand our products to meet a broader range of policyholder risk needs. We are also participating more deeply in targeted industries and extending our risk selection capabilities.

The second is distribution effectiveness. We are actively expanding The Hartford's Commercial Lines sales and underwriting presence in key geographies, particularly in the West and Midwest. This expansion, supported by enhanced marketing efforts and rigorous sales execution, is driving better outcomes.

Third, we continue to improve the customer experience and the operating capabilities of our company through things like process efficiency improvements, technology upgrades and digital access.

And fourth, we continue to invest in talent. We are proud of our employees, and we are working diligently to attract, retain and develop the best talent in the industry. For example, we recently hired Mo Tooker as our new Chief Underwriting Officer for the P&C businesses, and we added 2 new executives to complement the Personal Lines team, Mary Boyd and Casey Campbell.

Like the rest of you, we are closely watching developments across the industry, including recent M&A activities. These activities will certainly have repercussions on our markets. While change brings risk, it also brings opportunity. We are prepared to address and benefit from opportunities that arise, particularly those that fit our primary focus of expanding products, increasing distribution effectiveness, improving the customer experience and our operating capabilities and becoming a destination for great talent.

As I reflect on my first full year as CEO, I am truly appreciative of the many contributions that our Hartford's employees make everyday. What makes the Hartford special is our strong character. Throughout the past year, we have received numerous accolades for ethical conduct, risk management, governance and diversity and inclusion practices, and those attributes are incredibly important to us.

In conclusion, we are well positioned to achieve continued success, and we remain focused on our goal of increasing ROE and book value per share to drive shareholder value creation.

Thank you. And now I'll turn the call over to Doug.

Douglas G. Elliot
President

Thanks, Chris, and good morning, everyone. Our Property & Casualty and Group Benefits businesses posted strong bottom line results for the second quarter. Favorable property experience, for both catastrophe and non-catastrophe losses, was a significant contributor to earnings. In other lines, our businesses produced solid margins, consistent with recent quarters as loss trends remain benign. And with the benefit of strong retention, we also delivered solid top line growth.

Favorable weather patterns were clearly the primary force behind our outstanding property results. While we've been increasing our property capabilities in recent years, and I'm confident that our improved acumen and risk selection and analytics is an important driver for our long-term success, we know that quarter-to-quarter results will be subject to the presence or absence of severe weather. A well-balanced product mix that includes property is a competitive advantage with customers and agents, and we remain steady on our long-term strategic goals in this line of business.

Competitive dynamics across all our businesses are largely unchanged from last quarter. As I commented then, adequately priced new business opportunities are more limited, and we remain disciplined in our risk-selection approach. We continue to find success in our local relationships with agents and brokers, and we've been investing in sales and underwriting professionals along with our product and technology capabilities to improve our market position. I'll provide some additional insights on this, as I share the second quarter performance of our individual business units.

In Commercial Lines, core earnings was $264 million with a combined ratio of 92.2. This was an earnings increase of $51 million from second quarter 2014, largely driven by favorable property experience, margin improvement and workers' compensation and higher net investment income. Renewal written pricing in standard Commercial Lines was 3% for the quarter, essentially flat with first quarter 2015 and down 2 points from the second quarter last year. Pricing continues to be strongest in commercial auto, where our profit improvement remains a focus. Trends in workers' compensation pricing are generally in line with first quarter as we execute a very disciplined strategy to retain our best performance business at margins that meet or exceed our return targets.

Catastrophe losses for second quarter 2015 were slightly higher than a year ago, but below our expectations.

In Small Commercial, written premium grew 4% in the quarter, driven mainly by strong policy retention as our new business growth rate has slowed somewhat in recent quarters due to competitive forces. The underlying combined ratio, excluding catastrophes and prior year development, was an outstanding 85.1. The decrease of 2.5 points versus a year ago is the results of lower non-CAT property losses and improved workers' compensation margins. We're very pleased with our sustained performance in this business. Our strong written premium growth rate and profit margins have been very resilient, as our underwriting and pricing analytics have helped to guide our book of business management actions.

In Middle Market, we posted a strong quarter with an underlying combined ratio of 89.3, improving 8.3 points versus second quarter 2014. Much like in Small Commercial, the improvement is coming primarily from excellent non-CAT property experience with contribution from margin improvement in workers' compensation. A large portion of the favorable property result came from our Marine business, where we had an excellent second quarter.

Written premium growth was 8%, driven by strong retention and workers' compensation and increased new business in both construction and Marine. We're pleased with recent success in these industry-targeted businesses as they are a strategic focus for us. This is a positive indication of the traction we're gaining in the market as a result of talent and product investments made over the last several years. Since earlier this year, we've been adding underwriters in regions where we believe we can cultivate agency partnerships and compete effectively for new business. This is a longer-term strategy for growth, and it will take time to build momentum in these local markets. However, we believe it is the right time to be investing in talent to put our improved product and technology platform to even greater use in the market and develop new books of profitable business.

In Specialty Commercial, the underlying combined ratio was 98.8 versus 101.5 in the prior year. The 3 main businesses comprising Specialty Commercial are all operating within our target return range. We posted solid top line growth of 4%, while margin improvement was driven by improved loss experience in financial products and a mix shift in our results toward bonds with a smaller CAT to this business.

In Personal lines, core earnings was $42 million for the quarter versus last year's $27 million loss. Much of this improvement is due to favorable catastrophes, which are down this year by $64 million pretax. In addition, we had significant improvement in our non-catastrophe homeowner losses versus last year when we experienced elevated homeowner fire losses. Comparatively, fire losses this year were at their lowest level in the last 5 years. And $11 million is the improvement in core earnings was due to a favorable resolution of outstanding litigation. The underlying combined ratio of 89.1 improved 2 points from last year, largely driven by the homeowner results I just described, partially offset by a slight uptick in auto liability severity. In addition, we've been closely monitoring increased auto physical damage severity, having begun to see adverse trends several quarters ago. Industry trends in early 2015 also appeared to be somewhat elevated. We have identified several opportunities for improvement to our physical damage claim practices and have taken action. Our early observations from these initiatives indicate that we're driving improved outcomes, particularly in areas such as subrogation and total loss management.

Total written premium for the quarter grew 1%, including 1% growth in AARP direct and 14% growth in AARP Agency. We continue to be encouraged by the growth in solid margins of our AARP business.

On the Direct side, new business increased by 4%. In other agency, written premium was down 9% versus second quarter 2014. We're aligning ourselves with highly partnered agents who seek to deliver competitive, yet value-based products and services to their customers. As we move in this direction, there will be some agents and customers that do not match our profile and may seek other options.

Shifting over to Group Benefits. Core earnings in the second quarter was $56 million, up 8% over the prior year, achieving a core earnings margin of 6.3%. The increase is primarily attributable to top line growth and a lower expense ratio compared to prior year. Earned premiums, excluding Association-Financial Institutions, was up 5% in the quarter, driven by growth in our employer group life and disability lines.

For the quarter, fully insured ongoing sales was $58 million, up $13 million from prior year as we continue to have success marketing our differentiated service offering. In addition, our employer group business continues to maintain strong book persistency around 90% on an annualized basis.

The overall loss ratio was essentially flat to prior year. Improvement in the group disability loss ratio was largely offset by less favorable mortality in group life, which looks to be a function of normal volatility in the line. This is another excellent quarter for Group Benefits. Markets remained competitive, and we're performing well in all assets of our business. We are well positioned with strong book persistency and improved capabilities allowing us to compete for new accounts. And we're executing on planned initiatives for our voluntary platform, further enhancing our value proposition.

With that, let me conclude my comments by reiterating that we had a strong second quarter. We enjoyed favorable results from catastrophe and non-catastrophe property losses and the performance of other lines of business remained strong. Across our Property & Casualty and Group Benefit businesses, we have strengthened our products, technology and talent. Over the last 6 months, we've attracted a number of experienced industry leaders to our team who will help drive our near-term execution and our long-term strategic objectives. We're confident that the business platform we've been building in recent years will serve us well as we balance growth and profitability for the long term.

Let me now turn the call over to Beth.

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Thank you, Doug. I'm going to briefly cover results for the other segments and investments, and we'll then review our updated capital management plan. In addition to Commercial and Personal Lines, P&C includes the P&C Other Operations segment, which has a block of runoff liabilities, including asbestos and environmental. Core losses in this segment were $113 million in the quarter, down from losses of $146 million in the second quarter of 2014 due to lower reserve strengthening on our A&E reserves. As many of you know, we complete the annual ground-up A&E reserve study in the second quarter. As a result of this year's study, on a pretax basis, we strengthened our net reserves by $146 million for asbestos and by $52 million for environmental or a total of $198 million. This is down from 2014 when we had net reserve strengthening of $239 million comprised of $212 million for asbestos and $27 million for environmental.

The asbestos reserve strengthening reflects lower-than-projected improvement in new mesothelioma claims for a handful of our peripheral accounts, less than 20 out of more than 1,100. The remainder of the accounts are trending in line with the assumptions used to set our reserves. The environmental reserve strengthening was driven by higher new claim severity, including at a handful of Superfund sites but frequency has declined. We are often asked why we haven't done A&E reinsurance deal. We evaluate options for A&E periodically but today, these deals have not been cost-effective taking into account many factors, including the value we add by continuing to manage these claims ourselves, the price charged by potential reinsurers, the lack of a full assumption reinsurance or sale option and the potential loss of investment income. Last year, investment income in the P&C Other segment totaled $129 million before tax. Notwithstanding another year of adverse development on the A&E book, we believe that we can create a better outcome for shareholders if we continue to manage this book ourselves. We will, of course, continue to consider alternatives for these exposures as options and costs could change.

Turning to the financial results of our other segments. Mutual Funds core earnings rose 5% in the second quarter, primarily due to higher fee income on increased average assets under management, excluding Talcott variable annuity funds. As expected, Talcott-related AUM continued to run off, which reduced the segment's total AUM over the past year.

Fund performance remained solid this quarter with 69% of funds outperforming peers over the last 5 years, helping to improve net flows to a positive $250 million in the quarter. For the first half of 2015, net positive flow totaled $779 million, the strongest net flow performance since 2010.

Talcott posted very strong core earnings of $171 million this quarter, well above our expectation because of a $48 million federal tax benefit and a higher investment income, largely from very good returns on limited partnerships. Driven by private equity and real estate funds, limited partnership returns have been very strong this year, running at more than double the rate we used in our February outlook. Talcott's annuity contract counts continued to decline. Our ISV program added slightly to the fixed annuity runoff, while variable annuity runoff was a more normal level since we did not have a Surrender-focused contract-holder initiative this quarter. We continue to evaluate contract-holder initiatives and other programs that can help accelerate the decline in these books of business.

In July, Talcott paid the second $500 million dividend of the year bringing the total to $1 billion. We expect another $500 million in early 2016.

Corporate segment's second quarter 2015 core losses declined compared with the prior year and with the first quarter, largely due to lower interest expense as a result of debt repayments. We expect interest expense to decrease in the second half due to the second quarter bond call and the fourth quarter $167 million debt maturity. For the full year, interest expense, excluding the impact of any debt tenders or repurchases, is expected to be about $357 million, down 5% from 2014.

Turning to investments. The credit performance of our portfolio remained strong, with a modest $11 million of impairments during the quarter. Our annualized portfolio yield, excluding limited partnerships, was 4.1% and continues to hold up reasonably well despite the headwinds from low interest rates.

New money yields remain low, although within the range we expected for the year, which will continue to put downward pressure on investment income and yields as higher-yielding investment mature and are reinvested at lower returns. Helping offset this somewhat, similar to the first quarter, we had higher levels of income from fixed income make-whole premiums and other nonroutine items, and also from limited partnerships whose annualized yield was about 13% in the quarter.

To wrap up on our results, we had a strong quarter with consolidated core earnings per diluted share up significantly and a 12-month rolling core earnings ROE of 9.6%, both reflecting lower CATs, strong limited partnership income, a few favorable tax and other items, partially offset by unfavorable prior year development. Excluding net unfavorable items from both periods, core earnings per diluted share was up 66% over second quarter 2014.

In addition, book value per diluted share, excluding AOCI, also rose up 4% from year-end 2014 and 8% from June 30, 2014, reflecting net growth and shareholders' equity excluding AOCI and the accretive impact of the equity repurchase program. Outstanding and diluted shares have decreased by 9% since June 30, 2014, as a result of the equity repurchase program.

Before turning to Q&A, I'd like to wrap up by reviewing our capital management plan. As announced last night, the equity repurchase authorization was increased by $1.6 billion and extended through year-end 2016. This provides us a slightly more than $2 billion of equity repurchase authorization for the balance of 2015 and 2016. We currently expect to use this amount ratably over the period subject to market conditions and other factors. Yesterday's increase brings the total equity repurchase authorization to nearly $4.4 billion for 2014 through 2016. Debt reduction remains part of our capital management plan, as we strive to reduce our rating agency adjusted debt-to-total-capital ratio to the low-20s over time. Yesterday, we announced that we intend to repay the 2016 debt maturity of $275 million. As previously stated, we intend to repay the $167 million issue that matures in November of this year. In addition, we have a $180 million remaining under the current debt management plan, which was extended through December 31, 2016. When and how we will utilize that the portion -- that portion will depend on various factors, including market conditions.

The increase in the capital management plan will be funded by current holding company funds as well as future dividends from the operating subsidiaries and other sources. During July, we received about $900 million in dividends to the holding company, including $500 million funded by Talcott. For the remainder of the year, we expect approximately $300 million in dividends from subsidiaries for a total of about $1.9 billion for the year, unchanged from our February projections. In 2016, our current outlook is for about $1.9 billion of subsidiary dividends and other cash flows to this holding company, including $800 million in dividends from the P&C company.

Finally, recognizing the strong improvement in our P&C, Group Benefits and mutual funds earnings, the board authorized a 17% increase in the quarterly common dividend to $0.21 a share, effective with the October dividend payment. Including the impact of share repurchases, we expect to pay dividends of about $330 million over the next 12 months or about 30% of trailing 12 months consolidated net income, excluding Talcott. Combined with our equity repurchase plan, we are clearly delivering a substantial amount of excess capital back to shareholders.

As Chris discussed, with our strategic and financial transformation largely complete, our priority for excess capital utilization going forward is to find opportunities to invest in our businesses, helping to drive premium and earnings growth and expand our capabilities. We will continue to evaluate capital management options as it remains a good tool that we can use to return excess capital to shareholders in the event that we do not find opportunities that meet our overall objectives.

I will now turn the call over to Sabra, so we can begin the Q&A session.

Sabra R. Purtill
Senior Vice President of Investor Relations
Thank you, Beth. Before beginning the Q&A session, I would like to remind you all that consistent with past practice and company policy, we do not comment on market rumors or speculation. We appreciate your keeping that in mind, so the Q&A session can be productive for everyone on the call. Chris, could you please repeat the Q&A instructions?

Question and Answer

Operator

[Operator Instructions] Our first question is from Michael Nannizzi with Goldman Sachs.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Beth, I just wanted to circle back to the comment you made there. So for '16, you said the current outlook is $1.9 billion of dividends, including $800 million from the sub. So am I missing some -- where is the other $1.1 billion coming from?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Sure, Mike. So as you recall, I mentioned that we do anticipate getting $500 million of dividends from Talcott in early 2016, so that would be included. And we also expect dividend from Group Benefits and Mutual Funds. And similar to this past year, we would expect to have favorable tax receipts at the holding company as well. And all of that comprises the $1.9 billion that I mentioned.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Got it, great. And then maybe for Doug. Can you break out -- is it possible to break out the margin improvement that we saw in both Small Commercial and Middle Market that came from either the favorable non-CAT weather or underlying margin improvement related to comp?

Douglas G. Elliot
President

Mike, let me try to give you a little bit of color. You're right, it was a very good property quarter and workers' comp improvement, too. It was about 4 points in Middle Market and a little bit less than that in Small Commercial and just in terms of the margin improvement in that line of business.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay. So that -- those points you mentioned are related to the property and the remainder would then be related to workers' comp.?

Douglas G. Elliot
President

Those are the 2 line drivers, yes.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay, okay. And then in the homeowners, would it be possible to quantify the -- or just give us some marker around the impact of the favorable fire losses on the underlying?

Douglas G. Elliot
President

I could do that. You obviously get the CAT numbers, and you can see the CATs are down q-to-q, 7 points from last year. The fire losses, as I mentioned, were down at the lowest level in the last 5 years. I think we're about 5 to 7 points less than the higher years during that 5-year period, so I would use as a gauge inside our non-CAT property element.

Michael Steven Nannizzi

Goldman Sachs Group Inc., Research Division

Okay, got it. Great. And then last question, I guess. On the other agency business, obviously premiums there have declined. I'm guessing that's because of -- or maybe not acceptable levels of profitability. Can you talk a little bit about kind of what's happening there in terms of your profitability and what actions you're taking and -- it seems like the prudent thing to do, but just to get an idea of kind of where that is relative to your AARP business, for example?

Douglas G. Elliot
President

Sure. Mike, a few things. One is, and we're working all angles to this, right? We're working on tuning our open-road product, which is our new auto class plan. So those tuning requirement continue throughout the country. We are investing and working hard on our homeowners product, probably a little bit more going forward than over the last 3 to 4 years. We think homeowners is an important line relative to our personal line strategy. So a lot of work going on in homeowners. Clearly, challenge in the agency stays thinking about how we compete and looking for partners that are willing to work with us, work on a value prop play. We've been turning that segment, and we'll continue to tune. We do feel good about progress and very pleased with our overall return efforts. But also, I want to see if we can get the top line moving a little bit more positive direction.

Operator

The next question is from John Nadel with Piper Jaffray.

John Matthew Nadel
Piper Jaffray Companies, Research Division

Doug, maybe just a quick follow-up. Maybe -- I understand the -- following up on Mike's question about the favorable weather and the impact that, that had. Can you just sort of characterize that for the Commercial segment overall as well as for the Personal Line segment overall? Significant accident year loss ratio improvement, but I'm just wondering what you think the actual underlying sustainable level of improvement really is, recognizing each quarter can be somewhat volatile.

Douglas G. Elliot
President

Yes. John, the underlying and small, again -- really across all our commercial businesses on property was probably several points less than sustainable, and that doesn't mean that we haven't seen improvement, but I would say 2 to 3 points. When I look at our spectrum product in Small Commercial, a couple of points under where we've been last second quarters of prior years. And really the key property business has performed pretty consistently last couple of years. So at consistent levels, but at solid levels. So I like our last performance, I think, both annuity and CAT really were very good shape, but probably a couple of points better than a run rate perspective.

John Matthew Nadel
Piper Jaffray Companies, Research Division

Got it. Okay, that's really helpful. And then maybe a question for you, Chris. I appreciate certainly the improvement that we've seen in the underlying fundamentals, the improvement in the balance sheet, et cetera, and the commentary about seeking opportunities to accelerate growth. I'm curious because it still appears that there's a reasonable amount of financial flexibility and conservatism in your updated capital outlook. And so the question for you is this, do you think really buybacks versus potential acquisitions to accelerate growth has to be a mutually exclusive concept? Or do you believe you have the capacity to pursue both?

Christopher John Swift
Chairman & CEO

John, thanks for the question. I wouldn't exclude one or the other at this point. I think you've seen our history and track record, particularly working to improve our financial position and delever the firm and obviously reward shareholders with accretive capital management. So the way we think about it is we announced the -- a plan through 2016, that's our intention. It's our highest and best use of excess capital. But I think what we were trying to signal is a little bit of an inflection point because we feel in a different place. We're in a different company today. And we can be a little bit more offensive-minded about opportunities in the marketplace.

John Matthew Nadel
Piper Jaffray Companies, Research Division

Totally appreciate that. And I guess, just a quick follow-up along those lines, Chris. Any specific areas within P&C or even on the group insurance side that you feel like are areas where you want to expand, where you want to be able to find that faster paced of growth, where you maybe lack some scale today?

Christopher John Swift
Chairman & CEO

John, I think we think about opportunities across all our businesses. I mean, you mentioned a couple. But in Commercial, we really think about 2 main themes. If you've heard Doug and I and Beth -- we're continually talking about adding product in underwriting capabilities to the platform in a deeper and broader risk player, that's really what we mean in growing our future capabilities in industry verticals. So we think of a specialty in that area. We think in terms of larger parts of the U.S. economy, maybe we haven't participated as deeply as I think we can or should. And you referenced, and you heard Doug talked about marine, construction, real estate, infrastructure-related. Those are the types of things we talk about as far as the real economy and expanding and along with our geographic penetration and focus. So anything along those lines in Commercial would be very intriguing to us. And you mentioned Group Benefits. If you fairly look at our platform, I'd say we gear it more towards a national or large account platform, a very balanced LTD, STD and life in business, about 50% of premiums in each of those categories. So if there are opportunities in the small and medium case segments and folks that potentially could accelerate the pace of our voluntary sales growth, those are the things we would think about there. And then lastly, in Personal Lines, we don't aspire to be a broad market player, but we think we have unique skills and capabilities in direct marketing and sort of those niche areas. And we think in those terms, John, if there are opportunities to use our brand and direct marketing skills and our wonderful claims skills. So that's just to give you a little bit more of a flavor.

John Matthew Nadel
Piper Jaffray Companies, Research Division

No, I really appreciate the color.

Christopher John Swift
Chairman & CEO

John, last point there. I think in all this and hopefully, you of all people know and others is that we continued to be very thoughtful. I would say disciplined and deliberate in this area, just knowing where we're coming from and how we want to use shareholders' capital in the most prudent fashion going forward. But we did signal a change this quarter.

John Matthew Nadel
Piper Jaffray Companies, Research Division

Yes, no question, Chris. I have a lot of confidence.

Operator

The next question is from Meyer Shields with KBW.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Two quick questions, I think for Doug. One, within the overall 3% standard commercial rate increases, is there a difference between the property and liability lines?

Douglas G. Elliot
President

Meyer, all the lines do have their own nuances to them. As I mentioned, auto is right now achieving more rate across commercial than the other lines, that's the lead line. Our workers' compensation has been a bit more under pressure over the last couple of quarters. And even between Small and Middle, there are nuances. So yes, very different dynamic across the lines. But in general, pleased we still see rational competition. Maybe a bit more pressure, but I'm very pleased about what we've put up this second quarter and feel good about our efforts first half of the year.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And can you talk a little bit about the adverse development of the commercial, the size, the asbestos and environmental in terms of what's going on there?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

I'll take that, this is Beth. So in -- we have very, very modest adverse development, excluding A&E. We had some favorable development in our workers' comp lines, which is offset a little bit by unfavorable development as it relates to the discount on workers' comp reserves with just -- which reflects the fact that as we've been settling claims at a faster paced, the month of actual discount that you have in the reserve changes. And then the other aspects were really just small puts and takes across the various lines, really nothing that is worthy of calling out.

Operator

The next question is from Brian Meredith with UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

I'm just wondering could you talk a little more about when you're evaluating acquisitions kind of the financial benchmarks that you're going to be looking at, be it IRR is such a need, return invested capital, how it relates to share buyback, those types of things, tangible book value dilution?

Christopher John Swift
Chairman & CEO

Brian, happy to. I think a couple of points. One, first, any acquisition opportunity first needs to be strategic and financially compelling to make sense. I think second, we also think about it, and we talk internally of the comparison to building organically because largely what we have been doing is a organic focus. So an acquisition needs to be weighed generally in terms within organic build. And those organic builds required investment, requires time lines, obviously patience because it won't happen overnight. So you sort of weigh all that to sort of see what acquisition opportunity really accelerate our growth and makes sense. I think also, two, really since our transformation, we've really driven down our cost of equity capital, reduced our leverage, improved our valuation. So I think today, we have greater flexibility, think about acquisitions. And ultimately, we view it as ROI or IRR types of analysis where it needs to add value over a longer period of time and exceed our cost of equity capital today, or else we won't do it. I think from their then, the historical metrics of EPS and book value per share will emerge in the accounting records that I think then will create value over a longer period of time for shareholders. So as I said to John, we continue to be very thoughtful, disciplined and deliberate in this area. So that's how we're thinking.

Brian Robert Meredith
UBS Investment Bank, Research Division

And do you relate it all to kind of share buyback? Your thoughts on return share buyback versus M&A, organic growth?

Christopher John Swift
Chairman & CEO

Yes, it's part of the overall equation. But again, from a strategic side, we're trying to grow our capabilities and grow our earnings. It also needs to be weighed in because -- I mean, by itself, share buybacks don't increase the nominal dollars of earnings going forward. So -- but we do weigh that all very carefully, Brian.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. And then just one quick follow-up here. For Doug, the investment spend that you've been doing the last couple of years seems to just build out, those types of things. Where do we stand in that kind of process as far as expenses? And how much longer do you think it's going to be a drag on the expense ratio?

Douglas G. Elliot
President

Brian, when I think about our invest, I think about it over a longer period of time. So I don't think about it over spurts of quarters. It's a long-term process. I know we shared quite a bit of that progress in Charlotte with the Investor Day in June. We've got some of those investor going on in the middle. So yes, a little bit of pressure in expense ratio. But I look back at where we are in kind of our quarterly expense in our annual expense targets and I think about what's happening through the bottom line in our margins, I'm comfortable with those invest and actually see them over a longer period of time than I do over just '15 or '16.

Christopher John Swift
Chairman & CEO

Brian, it's Chris. I think just another thing you need to think in terms of -- is -- I'm not sure where the industry stands in totality. I like to speak from as our company, but we really do need to modernize our tools, capabilities, infrastructure, digital content. And as Doug said, I mean this isn't a simple one and done over the next 12 to 18 months here, but -- and this is a commitment to fundamentally improve our customer-facing exchanges, interfaces, for the long term. So we're going to be disciplined about expense management. But on the invest side, I mean we're over clubbing to really improve our capabilities in this area. So we'll try to -- I think we are balancing the best way we can in this dynamics. But make no mistake about it, we're committed to fundamentally improving our infrastructure and capabilities to improve our customer experiences.

Operator

The next question is from Erik Bass with Citigroup.

Erik James Bass
Citigroup Inc, Research Division

In Group Benefits, you continue to have nice growth momentum. So just hoping you could talk a little bit more about the competitive dynamics in the market and how much of your growth is coming from new products and your expanded voluntary products set.

Douglas G. Elliot
President

Eric, this is Doug. A couple of thoughts about it. Really, we had a terrific start to 2015. So we're encouraged about that progress, and really feel like we have priced our way through the challenges of 2 and 3 years ago. So that is in rearview mirror. As I look ahead, there are strong competitors around us, but I feel good about our ability to earn our way into the finals and we've -- we won our share. Inside our new sales, there's a positive story both on new customer, but there's also a positive story on growing inside our current customers with -- at issue sales in addition to where we were last year with that current customer. So that's point number two. And then lastly, voluntary has been an important part of our strategic growth these last couple of years, particularly just getting the product ready to meet the Street. I think we feel good that we were able to work those 11 15 [ph] and now into 15 accounts with our abilities in the voluntary area. It is slow. It's probably a little slower that Chris and I thought it might be. As we finish the year, our sales probably in the voluntary area will be just in the gap product area, probably under $10 million for the year. But what's important is that we're able to be at the table with customers that demand that is part of their suite, and I think we're there today. And a couple of years ago, I was not able to say that.

Erik James Bass
Citigroup Inc, Research Division

And then just quick one for Beth. You mentioned that still expect to pay a $500 million dividend from Talcott in early 2016, which I believe in the past, you've said it doesn't include 2015 statutory earnings. So given the pretty strong results you've seen Talcott so far in '15, is there a potential to take either an upsize dividend or an additional dividend from Talcott in 2016?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Yes. So that is correct. I have only included the $500 million that we've previously talked about. As it relates to '15, I think we've always said that they want to see how '15 year actually ends. Through 6 months in June, Talcott statutory surplus is actually relatively flat once you take -- once you adjust for the dividends. And so what we really need to see is where we end the year. Right now we would anticipate that we would generate statutory surplus still in that $200 million to $300 million range. But as I said previously, kind of at the lower end of that range, but it really is going to be a function of just where interest rates land at the end of the year and how that potentially impacts reserves that we have to set. So until the end of the year, we'll evaluate where the statutory surplus is and there could then be potential, but we're not putting that into our projections at this point.

Operator

The question is from Tom Gallagher with Crédit Suisse.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Chris, just to start out. I just want to get a sense for the way you're thinking about potential M&A. Would you contemplate transformative M&A? Or are we talking about more modest opportunities as ways of deploying excess capital?

Christopher John Swift
Chairman & CEO

Tom, thanks. I would say, I think our current thinking right now is more modest adding to capabilities in product lines. And I made -- point to be clear, I mean we're a U.S.-focused company and organization right now. So I assume if we're talking about transformative, you're thinking maybe beyond our borders. But our intent is that I think we have opportunities to capture more market share with expanded products and capabilities in our U.S. territory. But also be sensitive to maybe following U.S. customers abroad with some other skills, but we don't think about building international local market expansion currently.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Okay, that's helpful. And then I just want to be clear here. The current buyback authorization, is that going to be competing with M&A when you contemplate what you've announced so far? So in other words, if you found attractive deals that could consume some of the buyback? Or do you have additional resources or excess capital that's actually slotted for M&A?

Christopher John Swift
Chairman & CEO

Tom, it's a balancing act. I wouldn't say it's competing, that's our plan, that's our intention, that's what we think is the highest and best use. And if there's alternatives that come along, we'll put that as far as the overall equation. But I think, myself and Beth, we are appropriately prudent in managing the balance sheet and always have flexibility in mind.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Okay. And then, I guess, either Chris or Beth. Just to be clear, though. Your current capital plan doesn't necessarily allocate some additional capital buffer for M&A, or am I -- can you comment on that at all whether there's something in the plans for 2016 that is allocating something that you're not holding on to for M&A? Or -- anyway, can you comment on that?

Christopher John Swift
Chairman & CEO

Tom, Beth can add her point of view. Again, how we think about it, and maybe others have talked about it too, is we said that the deal needs to be strategic and make financial sense. And if we find something from an acquisition side, hits those hurdles and makes our ROIs and ROIs work, we'll figure out how to finance it. And that's why I said earlier, we've reduced our leverage and we'll continue to reduce it. But we do have flexibility to figure out how we would, I'll call it fund or finance a deal if we found the right one. So that's all I would say at this point.

Operator

The next question is from Randy Binner with FBR Capital Markets.

Randolph Binner
FBR Capital Markets & Co., Research Division

You all discussed the A&E resolution market a little bit in your comments. Do you have any update on annuity risk transfer market from our perspective? It seems active. And so would be interested in any update you have on that market. Or should we think of Talcott as continued to be internally-managed resolution?

Christopher John Swift
Chairman & CEO

Randy, is Chris. Beth can add her point of view also. But I think right now, we're very pleased sort of what is the runoff in total of Talcott, particularly in the capital that we've been taking out. Remind you, we've taken $1 billion out this year. We plan, as Beth said, to take $500 million out in early 2016. So we understand the risk. It's well-managed. It's well-contained from our perspective. And as Beth might comment upon, we do really believe in this low interest rate environment, and that does depress valuation. So these are all the things that we consider in sort of a transact versus a continued runoff mode. Beth, what would you add?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

I think, Chris, as always, I think you've captured it very well. I think it's very consistent with what we've talked about in the past, and we are always open to the consideration of transactions. But at the end of the day, needs to make economic sense for us and where we sit today with the capital that we're able to extract, and as Chris said, to manage the risk in that book. We feel very comfortable but, of course, we'll always be open to other considerations as market change.

Randolph Binner
FBR Capital Markets & Co., Research Division

Great. And then the follow-up there is just on the withdrawals, which the kind of the 12%, 11% year-over-year basis is good. And I think that's kind of -- as some of your programs that increase surrenders are winding down, do you have any plans to kind of continue to push new programs there to continue to accelerate the wind-down on those liabilities?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Yes. As we've said in the past, we'll always consider other policyholder-type initiatives that could further reduce the exposure in that book of business. We've been very pleased with those that we've had in the past. As I've said, pretty consistently, is -- our thought process is to really be very targeted as we look at those initiatives. So we don't have one right now in place. There is a team that consistently evaluates those to see if there's something that could be done. But overall, when we look at the continued reduction in the contract counts, we feel very good with the activity that we're seeing.

Randolph Binner
FBR Capital Markets & Co., Research Division

And those have been well-received, those plans, by agents, clients. There's been no real pushbacks, is that right?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Yes. I mean, I think the results speak for themselves in what we've be able to achieve with those programs. Again, we've always said they're not right for everyone and that's why policyholders have a choice. But as we said, we've been pleased with the results that we've been able to achieve on both the programs we've had in the variable annuity and the fixed annuity space.

Operator

The next question is from Scott Frost with Bank of America Merrill Lynch.

Scott Frost

From the debt side, appreciate the clarity in communicating your debt management goals. But wanted to talk briefly about your junior subissues as you may have expected. It's topical in our world. First, with respect to the 8 and 8s [ph] and then to the Glen Meadows. How would you characterize the efficiency of each of these instruments in your capital stack? And I have a brief follow-up.

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Thanks for the questions. So again, as we've been talking about in the past, we are focused on reducing our overall rating agency adjusted debt-to-capitalization ratios, also focused on things like coverage rates and so forth. And we really look at our capital, our debt structure sort of across the spectrum. And today, as we sit here, I think that the 18s [ph] do provide us benefit, and that we do get equity credit as we look at managing that ratio. And over time, we'll continue to evaluate the debt stack keeping all those factors in mind. But no change in our views as to how we think about those.

Scott Frost

Okay. And just specifically for the Glen Meadows, is it your understanding that this issue will continue to receive favorable capital treatment from NRSROs at the float date in 2017?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Yes. We've -- we do not expect any change in how we view -- how those would be considered.

Operator

The next question is from Jimmy Bhullar with JPMorgan.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

Most of my questions were answered, but I had one for Doug. Overall, I thought P&C results are pretty strong, but you did have weak premium growth and the non-AARP Agency channels. So just wondering what's driving that and what are you doing to turn that around, what your expectations are for that business -- for that channel.

Douglas G. Elliot
President

So that part of the challenge in our Personal Lines area is not new to the quarter. So we have had pressure in there. We see lots of competition. There are lots of names that continue to compete in that space. I'm very encouraged. I like where our team is headed. As you know, we've made a couple of very important additions in the last 90 days, so I feel good about that. And I think Jimmy, we'll be talking more about strategy as we move to the next couple of quarters, particularly in that Personal Lines area.

Operator

That next question is from Bob Glasspiegel with Janney.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

It seems like there's a lot of deals going on right now in the marketplace, and I've never seen the property casualty world undergo more changes than we're seeing today. And the glass half-full is just going to create opportunities as there's disruption in competitors. The glass half-empty perspective would be maybe you need rethink where you are as far as scale, tax structure, technology efficiency, et cetera. Where do you see Hartford in this world? And I'm sure you're going to take the glass half-full preference, but maybe respond to the negative issues that some might suggest are popping up.

Christopher John Swift
Chairman & CEO

Bob, it's Chris. I think you outlined some good points. We think about it generally as we are entering a very dynamic cycle. And that every really company, including our own, needs to think about sort of competitive advantages. There's really a couple of drivers that we see. One, not all the industry participants have really joined -- enjoyed the price increases that we and others have had, over the last 3 years, and pushed so hard to maintain. Generally, lower economic growth and continued low interest rates really has a compounding effect on company's balance sheets and ability to invest in new technology and capabilities while producing good financial results. Alternative capital is, obviously, disrupting some of the reinsurance base. It's got the potential to creep into other aspects of the market. And then very important, I think for all of us, is that distribution in our agents and broker partners are really going through their own form of industry consolidations, which ultimately means, in my judgment, that fewer carriers are going to be on panels, and brokers and agents will continue to look for those companies that have the most to offer for their clients. So I think the table stakes are higher to sort of meet the requirements of today. Ultimately, as a national company, Bob, with -- a lot of great strengths, brand, reputation, capabilities, a new energy and vigor around it. I'm very optimistic of our ability to continue to compete and have competitive advantage to drive shareholder value going forward. So it's probably not anyone of those things, it's probably all of it that we're trying to, I'll call it, manage for outcomes that we think are best for our shareholders and ultimately, our employees and customers.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

It's a very fair answer. Is the pivot to M&A recognition that scale is going to be increasingly important and you need more volume to do that technology spend that you are signaling is necessary?

Christopher John Swift
Chairman & CEO

Yes. I would say, in and by itself, scale is not a driver. If you really look at our words, and really what we've talked about here is adding new capabilities. What we don't have today are areas in the market -- the risk-taking market. We'd like to participate more in. I think that is more of immediate focus, but you make a good point. Scale helps out to, obviously, from an expense and efficiency side. And if you look at least one big deal that happened in New Jersey not too long ago, I mean, we really think in terms of, it will over a longer period of time to be a very compelling transaction that drives down unit cost, has greater tax efficiency, has greater capital-based to potentially to take on risk. So those are all of the things that you are very aware of, but we also know what we're focused on and particularly our segments on the market that we think we have great competitive advantage in.

Operator

There are no further questions at this time.

Sabra R. Purtill
Senior Vice President of Investor Relations

Thank you, Chris. I'd like to thank you all for joining us today and for your interest in The Hartford. Also, I want to note that Beth Bombara will be attending the KBW insurance conference on September 9, and we hope to see you all there. If you have any follow-up questions, please don't hesitate to contact either Sean or myself today by phone or email. Thank you and so long.

Operator
Ladies and gentlemen, this concludes today's conference call. You may now disconnect.