S&P Capital IQ

CONTENTS

The Hartford Financial Services Group, Inc. NYSE:HIG

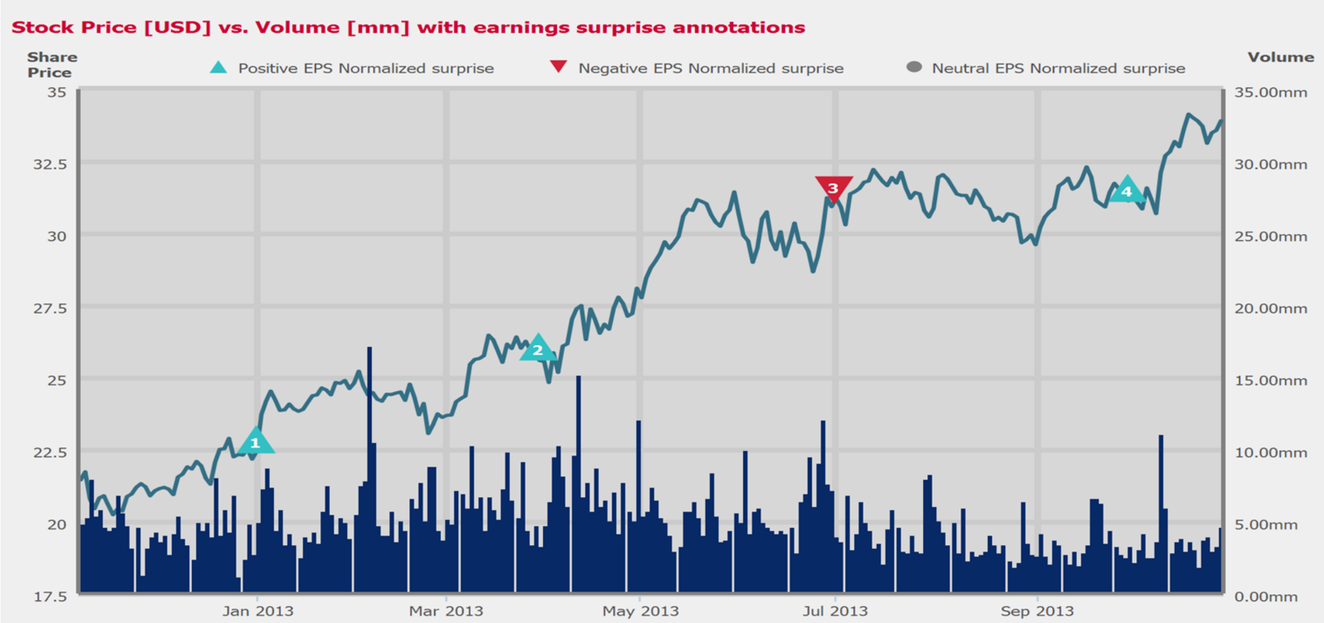
FQ4 2013 Earnings Call Transcripts

Tuesday, February 04, 2014 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ4 2013-			-FQ1 2014-	-FY 2013-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	0.90	0.94	▲4.44	0.92	3.52	3.55
Revenue (mm)	4881.00	6087.00	▲24.71	4880.00	24406.97	26236.00

Currency: USD
Consensus as of Feb-04-2014 1:15 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2012	0.35	0.54	▲54.29 %
FQ1 2013	0.83	0.92	▲10.84 %
FQ2 2013	0.71	0.66	▼(7.04 %)

FQ3 2013	0.83	1.03	24.10 %

Call Participants

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Former Executive Vice President and President of Consumer Markets & Enterprise Business Services

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Chief Financial Officer and Executive Vice President

Christopher John Swift
Chairman & CEO

Douglas G. Elliot
President

Liam E. McGee
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Presentation

Operator

Good morning. My name is Ginger, and I will be your conference operator today. At this time, I would like to welcome everyone to The Hartford Fourth Quarter and Full Year 2013 Financial Results and Outlook Conference Call. [Operator Instructions] Thank you. Ms. Sabra Purtill, Head of Investor Relations, you may begin your conference.

Sabra R. Purtill
Senior Vice President of Investor Relations

Thank you, Ginger, and good morning to everyone. Thank you for joining us for The Hartford's 2013 financial results and 2014 outlook conference call. I would just note that our prepared comments this morning run a little bit longer than normal, so we have allowed for some extra time on the back of the call beyond 10:00 for the Q&A session.

Our speakers today include Liam McGee, Chairman, President and CEO; Doug Elliot, President of Commercial Markets; Andy Napoli, President of Consumer Markets; and Chris Swift, Chief Financial Officer. Other members of our executive management team are also available for the Q&A section of this call, including Beth Bombara, President of Talcott Resolution.

As described on Page 2 of the slides, today's presentation 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 any forward-looking statements. A detailed description of those risks and uncertainties can be found in our SEC filings, available in the Investor Relations section of our website.

Also note that our presentation 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 and also in the earnings release and financial supplement.

I'll now turn the call over to Liam.

Liam E. McGee
Former Chairman

Thank you, Sabra. Good morning, everyone. And thanks for joining our earnings call. 2013 was an outstanding year for The Hartford. We executed our strategy and delivered superior results for shareholders. Heading into 2014, we have positive momentum with expanding margins in P&C and Group Benefits and improving performance in Mutual Funds. With the company's strong financial position and improved capital generation outlook, we are pleased to announce a new 2-year capital management plan, which includes $2 billion of equity repurchases and $656 million of debt repayments.

As you know already, last night, we reported excellent fourth quarter and full year 2013 results. Full year core earnings increased 26% to $1.7 billion or $3.55 per diluted share. Core earnings in the P&C, Group Benefits and Mutual Fund businesses increased 41% year-over-year. The increases in P&C and Group Benefits were driven by disciplined underwriting, expanding margins and lower CATs, which was a welcome reprieve after several years of elevated CAT losses.

As Doug will discuss, this was the sixth consecutive quarter of 8% renewal written price increases in P&C Standard Commercial. Our pricing philosophy is unchanged, and written pricing continues to outpace loss cost trends.

In Talcott Resolution, the size and risk of the annuity blocks have been significantly reduced. The number of VA contracts in Japan declined 26% in 2013, as surrenders increased due to market performance in the moneyness and aging of the block.

In the U.S., the number of VA contracts declined 14%, driven by improving markets, as well as the successful ESV program. We've achieved over 90% of our $850 million expense reduction target, including cost related to the divested businesses. Plans are in place to take out the rest this year. We are instilling a culture of continuous improvement that will ensure we operate more effectively and efficiently going forward.

We also prudently managed The Hartford's capital resources in 2013, reducing holding company debt by $820 million and returning a total of $856 million to shareholders, including common and preferred dividends and $633 million in equity repurchases.

For 2014, The Hartford's strategy is unchanged. We are focused on driving profitable growth, further reducing risk in Talcott and increasing operational effectiveness, with the goal of continuing to deliver shareholder value.

Our core earnings outlook is $1.65 billion to $1.75 billion. Adjusting for light CATs, favorable limited partnership returns and prior year development in 2013, we expect growth in earnings from P&C, Group Benefits and Mutual Funds will offset the anticipated decline in Talcott earnings as the legacy business runs off.

The Hartford is well positioned to achieve additional margin improvement in 2014. Markets are competitive, but our emphasis is on small and mid-sized businesses and individual consumers, markets where we have competitive advantages and positive momentum. We are a leader in the Small Commercial space, where our core strengths and customer value, ease of doing business and a contemporary distribution platform place us at the top of the industry. We have also added new talent to the existing Middle Market team, enabling us to diversify product offerings to complement our historic workers' compensation strength, all of which makes us a more attractive partner for agents and brokers.

In Consumer Markets, our AARP Agency channel initiative further leverages our exclusive relationship with AARP and gives us a unique value proposition in the marketplace. And to build on these competitive advantages, we are investing over $1 billion through 2016 to improve our execution capabilities, including P&C underwriting and claims management.

In Group Benefits, we expect the rebound in profitability to continue, driven by disciplined pricing and book management, as well as improving disability loss ratios. In addition, we are continuing to develop new products to increase The Hartford's penetration in the voluntary market.

In Mutual Funds, our strong partnership with Wellington is delivering solid, long-term fund performance. Sales and assets grew in 2013, and we expect this momentum to continue.

In Talcott, we will continue to focus on reducing the size and risk of the annuity blocks. Surrenders in Japan and the U.S. are expected to remain elevated, given the moneyness of the annuity contracts.

Also, while global markets in 2014 have been volatile, we are well protected with the combination of our hedge program and strong balance sheet.

Capital generation from the businesses will continue to supplement our financial flexibility. Our P&C businesses have consistently been dividend sources for the holding company. In addition, we expect both the Group Benefits and Mutual Fund companies to pay dividends directly to the holding company in 2014. With the significant reduction in VA risk, particularly in Japan, we also expect Talcott to begin paying dividends in 2014.

Having narrowed the focus of the company, we see many opportunities to run the organization more effectively and efficiently. As Chris will detail, we will reduce the run rate of the controllable expense base by eliminating $200 million over the next 3 years from the year-end level of about $3.6 billion.

So The Hartford is executing on its strategic plan and is on a clear path forward. I am very proud of how much the team has accomplished to get the company to this point, but we still have a lot of work to do. I am very optimistic and excited about The Hartford's further potential. Our goal is to achieve top-quartile financial performance, driven by growth in book value per share and ROE. And we have the strategy and execution capabilities in place to achieve this goal.

Thanks again for your interest in The Hartford, and thanks for joining our call. We look forward to sharing our progress with you in 2014 and beyond.

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

Douglas G. Elliot
President

Thank you, Liam, and good morning, everyone. Today, I'll cover the 2013 highlights for P&C commercial and Group Benefits, and then share some thoughts for 2014.

We finished 2013 in very strong fashion, and our overall theme remains unchanged. Significant core margin improvement across the business. For P&C commercial, 2013 was a very solid year, with $827 million of core earnings and a combined ratio of 96.1. This was an increase of $316 million from 2012, largely driven by 6.8 points of improvement in the combined ratio.

The underlying combined ratio, which excludes catastrophes and prior development, was 93 for the year, representing 3.6 points of fundamental margin improvement. As always, there are many moving pieces inside our business that contribute to our aggregate result, but the final analysis demonstrates a simple fact: We made substantial progress this year in expanding underlying margins across our P&C commercial business units. While catastrophes were much lighter in 2013, we achieved real success on the front lines, where pricing and underwriting decisions are executed.

Turning to the top line, our written premium of $6.2 billion was consistent with 2012. Two significant factors contributed to this outcome. First was our relentless focus on achieving pricing gains. We made difficult choices to walk away from certain accounts where we could not meaningfully improve pricing adequacy, causing our retention to suffer a bit. Second, we continued to reduce our Programs and Captives book of business, generating over $80 million of written premium year-over-year. We believe these decisions were appropriate for the loss trends and interest rate environment that have characterized the last 2 years, and our margin improvement in 2013 supports that conclusion.

These actions offset top line growth in other areas. We've been encouraged by our overall new business momentum over the back half of 2013 and specifically, with 3 consecutive quarters of Middle Market written premium growth, continued success in our National Accounts business and exciting traction developing with the rollout of our new automation platform in Small Commercial. On balance, we're extremely pleased with our overall progress in the market.

Let me share a few additional details with specific comments across our 4 business units, starting with Small Commercial. Small Commercial continues to be a centerpiece for our franchise. 2013 was another year of organic growth, while achieving a combined ratio of 90.6. Renewal written pricing gains of 7% for the full year more than addressed loss trends, and new business for the year was almost $0.5 billion. Many competitors in this market sector don't have an in-force block that size.

Moving to Middle Market. I'm excited with our progress. We delivered dramatic improvement in margins and made deliberate incremental steps in the last 3 quarters to increase the pace of our top line. The all-in combined ratio was 98.3 for the year, and our underlying combined ratio of 95.4 has improved 7.5 points since 2011. Our renewal written pricing for the full year remains strong at 8%, achieving more on lesser performing accounts and focusing on higher retention for better performing accounts.

No question, we experienced a more competitive pricing environment at the end of the year, but we continue to execute account-by-account with our deep segmentation approach. The top line in Middle Market showed positive progress during the year, benefiting from solid retention and new business production of $422 million, up 26% from 2012.

Our push toward property and general liability continues, and the new business growth rate in these 2 lines outpaced workers' compensation. Of our total new business writings, workers' compensation represented 31%, a much more balanced outcome and reflection of our growing multi-line capabilities.

Within Specialty Casualty, our business units experienced very divergent results. National Accounts posted a terrific year, with strong performance in both the top and bottom line. Premium retention was in excess of 90%, and strong new business success drove written premium growth of 8%. In fact, for every account loss during the year, we wrote nearly 4 new accounts; just an excellent year. Our Financial Products group also had a strong year with an all-in combined ratio in the mid-80s. The underlying combined ratio was 96, down more than 6 points from 2012.

As we have discussed on previous calls, our Programs and Captives business has been under stress during 2013. Much of this pressure has centered on commercial auto and in particular, 5 programs that we have now discontinued. We will continue to refine our Programs and Captives area, but I believe we have completed the actions necessary to deal directly with the key profitability issues in the book.

Now let me pivot to Group Benefits, where we had an outstanding year. Core earnings for 2013 were up over 50%. Even after adjusting for some favorable items, our earnings were well ahead of 2012 and our targets for 2013. Sales for the year hit $393 million, nearly the same as 2012. However, the fourth quarter was the third quarter in a row of increasing year-over-year sales, supporting our growing optimism as we look ahead. It's also a testament to our outstanding sales force, who have remained focus and committed to our success throughout our journey. All in, this has been a very gratifying outcome for a business that is not only a market leader, but one historically, has been a top performer here at The Hartford.

So as we close the chapter on 2013, we're very encouraged, not only by our strong financial progress, but also by the strength of our underlying execution across the entire Commercial Markets franchise. Importantly, the key brokers and agents who distribute our products are sharing with me that they can sense our expanded product breadth and our disciplined yet proactive attitude in the marketplace.

Let me conclude my comments with a few thoughts on 2014. First, as Liam mentioned, we're investing heavily in our capabilities as an enterprise, much of that geared to the business units of Commercial Markets. We're addressing important product development opportunities, building more efficient business platforms and creating easy-to-use technology applications for distributors, customers and employees. As an example, this year, we will begin rolling out a new claims management platform that crosses most of our P&C businesses. This investment in our future gives us greater tools to improve customer experience, manage indemnity costs and lower internal operating expenses.

Second, I'm excited about our go-to-market strategy in each business unit. Our Small Commercial business is uniquely positioned with market-leading products, services and technology that enable us to deliver superior results. This year, we will roll out a new product for our commercial auto, along with the completion of our new business quoting and issuance platform, ICON. We will advance our online service capabilities, expand our distribution and deliver new value to agency partners.

Our Middle Market business is well positioned to compete effectively on a multiproduct basis, announcing our historical strengths in workers' compensation with growing skills in property and general liability. During 2013, we were able to attract a number of product and underwriting professionals across all lines of business to our ranks. Now partnered with our outstanding field team, we are making our presence felt in the marketplace, feeding more effectively on accounts that might have passed us by in previous years.

Specialty Commercial will build off the successful position in National Accounts. In our niche of a $1 million to $5 million accounts size, we have demonstrated a unique package of products, service and claim expertise that resonates with our customers. Few companies bring our suite of tools and the financial strength to this sector of the marketplace.

Within Program and Captives, we expect to further reduce our active accounts as we move away from those that do not meet our financial or strategic goals and focus on the profitable relationships that align well with our core underwriting and claims management capabilities.

And in Group Benefits, we're excited about the accelerated pace of our profit improvement, while we are investing aggressively in the products and services that are important for our future.

Based on our early analysis, persistency on National and Middle Market accounts renewing in January 2014 is expected to be between 75% and 80%, a significant improvement from January 2013. This bodes well for overall book persistency throughout the year.

From a marketplace perspective, we will continue our drive into voluntary capabilities and position this business to adapt to the rapidly changing benefits marketplace.

Third, we're prepared for a more competitive market in 2014, particularly in the large guaranteed cost sector. Our rate adequacy has improved substantially over the past 2 years, and clearly, we have fewer accounts that need significant pricing actions. Given the level of written price increases we achieved in 2013 and our focus on maintaining pricing ahead of loss cost in '14, we believe that margins will continue to improve but to a lesser degree than the prior 2 years. We will aggressively monitor our loss trends, particularly as they may be affected by changes in the medical industry for both workers' compensation and disability. The Affordable Care Act is in its infancy, and it's nearly impossible to fully anticipate its ultimate impact on our business. Nonetheless, we're studying multiple scenarios very closely for how this legislation may change consumer, broker and medical provider behavior. We believe that both risks and opportunities will emerge, and we will be prepared to adapt accordingly.

And finally, across all of Commercial Markets, we will continue to enhance our execution skills and leverage our much strengthened talent base. Over the past year, we've attracted a number of top-notch executives across all of our business units, deep experts in distribution, product management and operation. These colleagues are blending well with our strong team to build market momentum with our customer and distributor-focused go-to-market strategies.

In summary, we're very pleased with our progress in 2013 and more excited than ever about our future.

Let me now turn the call over to Andy Napoli.

Andre A. Napoli
Former Executive Vice President and President of Consumer Markets & Enterprise Business Services

Thanks, Doug, and good morning. Today, I'd like to cover Consumer Markets results for 2013 and then discuss our plans for 2014. The bottom line is we're very pleased with our 2013 results that reflect our focus on profitable growth. During the year, we expanded margins and generated higher-than-expected written premium growth. Growth was fueled by strong new business production, coupled with improved retention. Margin expansion of 2.2 points for the year was primarily driven by 5 points of favorable catastrophe results and a slight increase in underlying margins, offset by a decline in favorable prior year development.

In homeowners, coming off of very favorable 2012, strong earned pricing, coupled with continued favorable frequency for both weather and non-weather claims, were more than offset by increases in severity.

In auto, we're pleased with our margin expansion as our combined ratio, excluding CATs and prior year development, declined nearly 1 point, driven by expense reductions.

Full year auto liability frequency for 2013 came in as expected. However, frequency for the second half of the year, impacted by higher miles-driven as the economy continued to improve, developed a bit higher than the favorable results we saw in the first half of the year. In the fourth quarter, we increased our current accident year reserves to reflect this development.

Written premium growth was driven primarily by strong new business in our AARP Direct and AARP Agency channels. In other agency, new business premiums decreased 2% for the year. However, both the third and fourth quarter recorded positive growth over the comparable 2012 period. The combination of new business growth and a 1-point improvement in policy retention led to a year-over-year increase in auto policies in-force for the first time since March 2009.

As we look ahead to 2014, we are pleased that AARP Direct auto ended 2013 near its combined ratio target. Going forward, our focus in this channel is to balance profit achievement and growth by pricing ahead of expected loss trends while not compromising retention. Our new auto class plan is designed to more accurately match price to risk, while simultaneously increasing our competitiveness among the 50- to 59-year-old AARP age segments. The continued implementation of our telematics program, called TrueLane, will also help attract and retain better auto risk.

Going into 2014, we expect slightly negative frequency, combined with low single-digit severity to produce a mildly positive overall auto loss trends for the year and for this loss trend to be exceeded by pricing, yielding auto margin expansion.

Shifting to homeowners, the primary focus here is margin expansion. While we've made good progress over the past several years, work remains to achieve profit targets in this line. In addition to high single-digit rate increases, we'll continue to evolve terms and conditions by increasing withheld deductibles in targeted states, promoting account-rounded business and tempering roof claims severity through reduced coverage product offerings. Understanding that there will be significant year-to-year variation in homeowners loss cost due to weather patterns, we expect rate increases to exceed loss trends and yield underlying margin expansion.

2014 will also include strategic investments in digital capabilities across all channels and tactical steps to enhance our other agency channel offering. Our investment in digital will greatly enhance our customer and agent self-service capabilities, with a growing focus on mobile technology. In the other agency channel, our strategy is to carefully expand our auto class plan to more accurately and competitively price an incrementally broader market, with the intent of generating additional profitable growth for consumer going forward.

In closing, we're proud of the progress we made in 2013 to improve margins, expand top line growth and grow policies in-force. Our strategic objective remains unchanged: To achieve above average industry growth, while also recording an all-in combined ratio of 92.

I'll now turn the call over to Chris.

Christopher John Swift
Chairman & CEO

Thank you, Andy. This morning, I'll cover several topics. First, I'll quickly review 2013 results and discuss our '14 outlook, including our capital management plan for 2014 and '15. Second, I'll provide a year-end update on several important metrics for Talcott and the company, including capital margins, and finally, I'll cover our first quarter 2014 outlook.

Let's begin on Slide 19. Doug and Andy have covered the results for our Commercial and Consumer Markets. Let me now briefly touch upon the other segments. Mutual Funds core earnings rose 5% in 2013, in line with our original outlook as we continue to strengthen and position this business for future growth opportunities. Retail mutual funds net flow performance improved in 2013, driven by higher sales and better distribution effectiveness, supported by solid fund performance throughout the year. Assuming normal market conditions, we expect 2014 core earnings growth of roughly 10%, driven by improved earnings in retail mutual funds, partially offset by the runoff of VA mutual funds.

Turning to Talcott on Slide 20. Core earnings declined 9% in 2013, which was less than expected, attributable to higher partnership returns, lower DAC amortization and higher market levels. As Liam mentioned, we have made significant strides to reducing the size and risk of Talcott, which will enable us to begin returning capital from Talcott in the second half of 2014, initially from HLIKK, our Japan subsidiary. Talcott 2014 core earnings is expected to decline approximately $165 million or 20% from 2013 core earnings, reflecting lower fees due to higher surrenders. This outlook projects an additional 31% decline in policy counts in Japan and 12% in the U.S., which will permanently reduce risk, but will also continue to reduce earnings in 2014 and 2015.

Slide 21 summarizes the Corporate segment, which includes interest, expense and other items not allocated to the businesses. In 2013, Corporate had core loses of $250 million compared with core losses of $313 million in 2012. The difference was principally due to the reduction in interest expense, as well as a net $41 million benefit from insurance recoveries, settlements and tax-related items, offset by higher incentive compensation cost in 2013. We expect corporate core losses in '14 to be approximately $270 million.

Looking at full year 2013 on Slide 22. Core earnings were $1.74 billion, up 26%, reflecting improved margins, lower catastrophes and higher limited partnership returns from the prior year. For the full year, core earnings ROE was 9%, up 7% from 2012. Full year 2013 core earnings included catastrophe and other items that totaled the favorable $19 million or $0.04 per diluted share as highlighted on the slide. Excluding these items, as well as limited partnership returns in excess of 6% target, core earnings were approximately $1.65 billion, with an adjusted ROE of 8.6%.

At year end, The Hartford's book value per diluted share, excluding AOCI, was down slightly to $39.30 per diluted share, principally due to Japan DAC and debt tender charges we incurred in the first quarter of 2013. Book value per diluted share includes the impact of $633 million of share and warrant repurchases throughout the year. Our average common share repurchase price in 2013 was $31.20 per diluted share, about 21% below book value at the end of 2013. As Liam mentioned, 2013 was an outstanding year, with many accomplishments and strong financial performance. We are now focused on 2014 and beyond.

Slide 23 summarizes our outlook announced yesterday afternoon. Our 2014 core earnings outlook is $1.65 billion to $1.75 billion. At the midpoint of this outlook, core earnings would be up approximately 4% over 2013 after reflecting the adjustments to 2013 results. Now CATs core earnings are expected to decline by approximately $165 million, which we expect will be offset by core earnings growth from the rest of the businesses. Our 2014 outlook translates into a core ROE in the range of 8.7% to 9.2%.

During 2013, we achieved significant progress on our expense reduction targets, including expenses associated with the businesses sold, eliminating about 90% of the $850 million goal with the rest to be taken out this year. We are now focused on the next phase of our expense initiatives aimed towards reducing controllable insurance and other operating expenses.

Adjusted for the Catalyst 360 sale, we ended 2013 with an annual run rate expenses of $3.62 billion. We plan to reduce this base by approximately $200 million by the end of 2016, which is about a 5% reduction. To achieve this increased efficiency, we are simplifying and improving processes, enabled by the approximate $1 billion investment in new systems and capabilities over the next 3 years.

Our 2014 outlook includes a catastrophe load of about 4.7 points on the P&C combined ratio compared to 3.2 points actual in 2013. Our outlook does not include prior year P&C loss reserve development, with the exception of the accretion of discount on workers' compensation reserves.

With respect to investments, the pretax portfolio yield is expected to decline from 4.3% to 4.1% in 2014. This is largely due to lower assumed returns on limited partnerships and alternative investments, which are 6% compared to the 10% realized in 2013.

Finally, our forecast assumes equity repurchases totaling approximately $1 billion. The actual impact of these share repurchases on weighted average diluted shares will depend on the purchase price over the course of the year. For modeling purposes, we are estimating a weighted average diluted share count of approximately 468 million shares.

The company's capital resources and financial flexibility have remained strong over the last year even after our significant capital management actions in 2013. Last night, we announced a new $2.656 billion capital management plan for 2014 and '15, which is summarized on Slide 24.

We intend to repurchase $2 billion of equity over this 2-year period and plan to repay $656 million of maturing debt in 2014 and '15. This plan allows us to continue our balanced capital management programs, targeted at equity repurchases and paying down debt.

Funding for this share repurchase and debt repayment program will come from increased dividends from our operating subsidiaries, including P&C, Group Benefits, Mutual Funds and Talcott.

Our current outlook is for total dividends to the holding company of approximately $1.2 billion in 2014. Included in this outlook is about $150 million from HLIKK, Talcott's Japan subsidiary, which is expected to occur in the second half of 2014. Looking ahead, we expect additional dividends from both Talcott's U.S. and Japan operations in 2015.

We'd now like to update some key data on Talcott end capital similar to the metrics from our April Investor Day. Slide 25 provides an update of the market consistent value or economic value of our 2 VA blocks. We use this metric to measure the risk and the economic value of the VA blocks. It does not represent the market value of the blocks a willing buyer and seller would agree upon. Details on the methodology for MCV can be found in the appendix.

Let me summarize a few key points about the change in MCV over the period. First, as of December 31, 2013, the MCV for the 2 blocks is an asset of $1.7 billion compared to a liability of $500 million at the end of March 2013. Second, the MCV improvement was largely driven by market factors, adding $2.9 billion to the MCV, offset by approximately $800 million in fees that we collected and recorded as revenue during the year. Third, the MCV calculation does not include hedge results.

During the last 3 quarters of 2013, hedge losses offset approximately 80% of the MCV improvement, consistent with our hedging approach and targets.

This slide also shows the comparison of MCV results to statutory reserves. The reserves and surplus backing these blocks provide substantial resources as these risks run-off. Of note, the Japan VA retained business in HLIKK is lapsing more quickly than expected, which lowers risk levels, resulting in the HLIKK balance sheet being much stronger today. This has allowed us to adjust downward our hedging targets for the exposure retained in the Japan legal entity.

Although MCV is the principal methodology we use to value and hedge the VA blocks, we understand that many investors like to see cash flows specific to each of our deterministic scenarios. Slide 26 summarizes the base case scenario. In this scenario, the net present value of cash flows is $3.0 billion.

Beginning on Slide 34 in the appendix, we show cash flows for updated favorable and stress scenarios that reflect 2013 experience in market levels. The net cash flows improved in each scenario from those we presented in April, although not to the same extent in each case. As a reminder, a high level of 2013 surrenders reduced future fees in each scenario and have a similar impact on future claims and hedging costs. The key point for both the MCV and cash flow scenarios is the positive embedded value in the VA blocks, which can be harvested over time, along with the associated capital and return to the holding company as the blocks run off.

Turning to Slide 27. As of December 31, our capital resources totaled $17.7 billion, an increase of $1.1 billion from the prior period. Life surplus, including HLIKK surplus, was about $7.8 billion and the capital margins remained strong with an estimated RBC ratio of 450% in the Hartford Life and Accident group.

We have received formal approval from the Connecticut Department of Insurance to complete the Group Benefits' legal entity separation project, including the movement of cash and subsidiaries, which will be completed in March of this year. No holding company resources are needed for this separation.

Slide 28 provides an update on our capital margins using the same scenarios from the cash flow projections. Capital margins in the base, favorable and stress scenarios all remained strong, with the base case margin estimated at $7.6 billion at the end of 2015. These margins assume the full execution of the 2014 and '15 capital management plans in all the scenarios. Capital margin represents the excess of AA capital for the P&C company, and 400% RBC for the Group Benefits company. The target for U.S. Talcott entities is 325% RBC. The holding company liquidity is targeted at approximately 1.5x annual interest in dividends. As you can see, our capital margins remained strong in all these scenarios. In the stress scenario, we have $2 billion of capital margin even after full execution of the capital plan, with Talcott remaining capital self-sufficient.

Before turning to your questions, let me provide a brief summary of our first quarter outlook, which is on Slide 29. Our core earnings outlook for the first quarter of 2014 is $450 million to $475 million, or $0.94 to $0.99 per diluted share. This outlook assumes catastrophe losses of $57 million, after tax, and prior-year development only for the accretion of discount on workers' compensation reserves. I would note that our CAT experience through the end of January was still within our outlook, and we feel good about our CAT budget for the first quarter, but there are 2 months to go.

Finally, core earnings outlook for Talcott is in the range of $160 million to $170 million.

To wrap up, let me summarize some of the key comments Liam, Doug and Andy made in their remarks. 2013 was an outstanding year for The Hartford, with strong financial results and significant progress made in the company's strategy to grow profitably, P&C, Group Benefits and Mutual Funds. Talcott made exceptional progress during 2013, with a significant reduction in VA risk exposure. And finally, based on our progress in 2013 and momentum headed into 2014, our capital resources and financial flexibility continue to strengthen, enabling us to return a significant amount of capital to shareholders in 2014 and 2015.

Now, I'll turn the call over to Sabra to begin the Q&A session. Sabra?

Sabra R. Purtill
Senior Vice President of Investor Relations
Thank you, Chris. We have about 30 minutes for Q&A. [Operator Instructions] Ginger, could you please give the Q&A instructions again?

Question and Answer

Operator

[Operator Instructions] Your first question is from Brian Meredith from UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of questions for you. First, with your first quarter outlook, I noticed there really was no mention of higher CAT losses, and given all the weather and some of the warnings by some other companies,. I wonder if you could comment on that. and what the potential impact on the Hartford could be.

Christopher John Swift
Chairman & CEO

Brian, it's Chris. As I said in my comments, we've looked at January results, we still feel good about our CAT assumptions for the full first quarter. January's CATs were maybe a little elevated from normal, but still, we feel good about the overall budget for the first quarter. As it relates to the non-CAT weather, Doug might be able to comment a little bit. But there was really nothing unusual in our book of business, whether it be commercial or personal lines that we're seeing in the first month of January. But, Doug, any additional color?

Douglas G. Elliot
President

Well, Chris, I think you hit it. As I look at the balance in January, we know it's a colder month, but I think we're within our general norms, and we'll continue to work our way through the rest of the quarters. So I don't see anything really that is so significant we should comment on.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. And then second question for Doug. I'm just curious, you talked about preparing for some increased competition here going into 2014. However, if I look at your renewal rate activity, you seem to be holding in there better than most of the other competitors. I wonder if you could kind of comment on that and why you think that is.

Douglas G. Elliot
President

I guess, a few thoughts for you, Brian. One is, I would remind you, we have a big Small Commercial book of business, and that has performed well. It's been a steady component of our business that's here for a long time, and that rate performance is very solid for an extended period. Secondly, in prior calls, we worked hard at our auto line of business and the auto line is still achieving and taking rate, and given some of our profit dynamics, we think that is exactly the direction we need to head. And through it all, we were pleased with the fourth quarter. I did point to the fact that my view is at the end of the fourth quarter, things got a bit more competitive. But I look at 2013 across-the-board, I looked at overall performance in the fourth quarter, I'm very pleased with the progress we made.

Operator

Okay, your next question is from Vincent DeAugustino from KBW.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Switch gears a little bit on Personal Auto. So just noticed the prior quarter or current accident year frequency adjustments stemming from the higher second quarter '13 estimates. And I'm just wondering if that's all 3Q '13-related, or perhaps if there's sort of late reported claim that are popping up that might be causing the adjustment?

Andre A. Napoli
Former Executive Vice President and President of Consumer Markets & Enterprise Business Services

Vince, this is Andy. So first, I'll say that is a normal part of our process to make current accident year reserve adjustments throughout the course of the year, as we see emerging trends in frequency or severity for auto liability. So occasionally, liability frequency can exhibit some volatility from quarter-to-quarter. And so ultimately for 2013, auto liability frequency ended right about where we expected at the beginning of the year. Just sort of the way it played out was that the first of the year, we saw some favorability and then in the second half, we saw some unfavorability and we booked that in the fourth quarter. So you're seeing a full year impact all getting booked in the fourth quarter.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, great. And then just switching over to the Mutual Funds business. So it seems like you have really strong fund performance and we had good market performance for the ICI fund flows were positive. But you guys' retail fund flows were still a little troublesome. So I'm just curious of your thoughts on improving that and whether if you feel this is a distribution hurdle or if there's anything else that's holding back the business because all is equal it seems, like the performance there is pretty solid.

Christopher John Swift
Chairman & CEO

Vincent, it's Chris. Jim Davey, if he were here today, he had a prior commitment with his Mutual Fund Board. He would answer it along the lines of -- He really is positive about 2014. We do think we could have net positive flows for all of '14. We would look back in '13. We had good, decent performance from our partner, Wellington. We also did have maybe 2 major accounts, 401(k)-type money that rolled off. We did shut down now since our money market fund and roll those assets to another new provider. So was it a couple of a one-time items, but overall, we do think we could begin to grow net fund flows in 2014.

Operator

The next question is from our Erik Bass from Citigroup.

Erik James Bass
Citigroup Inc, Research Division

Just hoping if you could talk a little bit more within your capital plan, what you're assuming for dividends from Talcott in 2014 and 2015? I know you mentioned specifically the Japan target, but given the ability to request a special dividend from the U.S. block in 2014? And I guess, if not, what's preventing you from taking capital out, given the significant lapsation you're seeing.

Liam E. McGee
Former Chairman

Erik, in a high level, and I'm sure Chris may want to give you more perspective. As Chris noted, we'll take out from HLIKK this year and next year, and we do intend to have an extraordinary dividend out of the U.S. in 2015. Obviously, that will require regulatory approvals. I think it's premature for us to comment in more than it is our intent to do so. And as we work through that process, we'll give you more details. Chris?

Christopher John Swift
Chairman & CEO

I would say, Erik, in addition to Liam's points, just the context of Talcott's capital return, as I said in my prepared remarks, we are taking out, I'll call it, to the holding company $1.2 billion of cash flow. And really, some of those cash flow resources are from old Talcott operations, whether it be Mutual Fund or

Group Benefits. So we plan to take out roughly $70 million of dividends from Mutual Funds next year, $100 million from Group Benefits. So in a way, we think Talcott's already contributing. As we said, Japan is coming online with dividend distributions. We expect, I would say $150 million to $200 million over the next 4 or 5 years on average to come out of Japan. As Liam said, we have some things that to still do in the U.S. And really what I mean is, I want to get completed that legal entity separation. We are beginning work on collapsing White River REIT, our Vermont captive into the ILA, and then we'll approach the regulators in the second half of the year and have that discussion, that multi-year discussion, on what we think is an appropriate funding source coming out of the remaining 2 U.S. life legal entities for Talcott. So I think we have a plan, and I think we've been executing it pretty well and we're very confident that, particularly in '15, increased cash flows will come out of Talcott.

Erik James Bass
Citigroup Inc, Research Division

That's helpful color. And just -- could you provide an update on the stack capital levels to the different blocks within Talcott similar to what you gave in April?

Christopher John Swift
Chairman & CEO

I think what our plan is, we'll do that at the first quarter once we complete the legal entity separation and just have, I'll call it, the new structure lock down and just present it to you there. So I would say that there is nothing dramatically changed from the April presentation, but we'll update you first quarter.

Operator

The next question is from Jay Cohen from Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

A question on the current year reserve adjustment in the auto side. Can you quantify that just so we can get a good sense of what the underlying numbers look like there?

Andre A. Napoli
Former Executive Vice President and President of Consumer Markets & Enterprise Business Services

Sure. It was 2.6 points on the quarter. And then for the year for auto, it was about just over a half point.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

With ownership on the auto...

Andre A. Napoli
Former Executive Vice President and President of Consumer Markets & Enterprise Business Services

On the auto, right.

Operator

The next question is from John Nadel from Sterne Agee.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

I'm curious on the outlook for the runoff of the Japanese variable annuity block. It looks like you're expecting the surrender rate will remain somewhere around that 30% level in 2014. Obviously, we've had some very early 2014 market weakness and yen movement. I'm just wondering if that 30% outlook takes into account the more recent market activity or is there some risk that, that surrender rate comes lower.

Liam E. McGee

Former Chairman

John, I'll have Beth comment in more detail. But I'll remind you that even at a yen of 101 and the topics where it is now, we're really back where we were just a few months ago when the redemption rate, what it is, right -- the lapse rate, I should say, is similar to what it is right now. So with that context, Beth, do you want to give more details?

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Yes. I would agree. So where we are right now, what we saw in January, our surrender rates were pretty much in line with what we would have expected. January is typically a little bit slower just because of a lot of holidays and so forth. And the other thing, 2 other points just to keep in mind is, one, the funds backing the account value in Japan, about 40% of that is allocated to equities and of that, half of it is to Japan equities. So it's not all linked to what we're seeing in the Japan equity movements. And then secondly, we do have a very significant amount of account value that starts to come up to the annuitization, the annuity commencement date in 2014, about $2 billion worth of account value. And most of that account value at the end of the year was above 110% of the guarantee amount. So very significant amount out of the money, and our experience has been that, for contracts that come to the annuity commencement date, if they're out of the money, we see a very high number of those choosing to take the lump sum. So if you put all of those factors together, we still feel good about our surrender rates assumption for the year.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

That's excellent color. And then, Chris, maybe just a clarification on your Slide #28 that talks about the capital margins. So, at the end of 2015, if the base scenario comes to 4, that $7.6 billion is effectivity your excess capital at The Hartford above those requirements for P&C Group and Talcott?

Christopher John Swift
Chairman & CEO

I think, John, it's our definition of capital margin, we've never, call it, quantified it per se as excess, because excess then would take into account which is really deployable. And, as you know, I mean, particularly for the Life group, we're still in the U.S. Life group in an extraordinary dividend land. It can't be readily turned into cash. So that's the only nuance. But, yes, I think you should think about capital margins as a buffer above our AA targets, our 400% RBC, particularly in Group Benefits as a healthy margin. And we would manage that over time.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

I assume this really goes to supporting the dialogue that you guys expect to have with some of the insurance regulators around this sort of multi-year dividend planning?

Christopher John Swift
Chairman & CEO

Yes, I mean, obviously, we share all our data with all our constituencies, whether it be regulators, agencies, as the like. I think the only other thought, John, just on that base number, I mean, that's the margin at the ATCOS, plus the holding company liquidity. And we do have targets that are roughly 2x annual the interest in dividend, so that would be, in essence, the subtraction from a deployable capital number also.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

Okay. And then just to -- just one last point on this. Given how much that capital margin moves, especially under the stress scenario, I guess it's fair to assume that most of that capital margin is -- resides in Talcott, given Talcott would probably be the piece that requires more capital under that stress scenario?

Liam E. McGee
Former Chairman

Remember, we've always said, that we're managing Talcott to remain capital self-sufficient, and Talcott is in this scenario. The actual breakdown of that $2 billion is, there's $1 billion at the holding company, because we're always solving for a minimum liquidity at the holding company, and P&C's got $600 million and Life group has $400 million. So those are the components of the $2 billion capital margin in the stress.

Operator

Your next question comes from Mark Finkelstein from Evercore.

A. Mark Finkelstein
Evercore ISI, Research Division

Maybe start with Chris. Chris, for 2014, what is the economic cost of hedging that you are assuming? And what I mean is that, kind of a number that falls below the line, if markets operate the way you expect them to.

Christopher John Swift
Chairman & CEO

I would say on the hedging, in general, we have a context right. Markets moved dramatically in 2013 and maybe we could talk about the cost of the hedging program in general over the life of the block as it runs off. But the answer to your specific question, I mean, Talcott, you would assume roughly $225 million of after-tax hedge losses recorded in realized losses. I translate that into -- from our core ROE to a net income ROE, that's about a 1 point cost of that hedge program. I think on the overall cost, we may able to provide some updates, and I'll compare and contrast. So I always start with Japan. In prior years, we talked about 200 basis points of cost. You see sort of a run rate cost going forward, primarily because the market moves so dramatically where they are today with about 70 basis points. U.S., that 40 basis points on average now is around 30 basis points. And then from a macro program, I would have you think of our spend going forward of roughly $75 million.

A. Mark Finkelstein
Evercore ISI, Research Division

And that's all after -- or pretax, right?

Christopher John Swift
Chairman & CEO

The basis points was after-tax and then the spend $75 million was a pretax number.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay. So after-tax on the 70 and 30. Okay. Just on the dividend out of P&C group in Mutual Funds, did you back off the $1.50 billion at Talcott, it's $1.50 billion. Is there any reason to think that, that number shouldn't kind of trend with earnings? Is there anything that would drive it up above the earnings or perhaps below in terms of that kind of capital release?

Christopher John Swift
Chairman & CEO

I think that's a pretty decent trend. The way we think about it more importantly is what is -- what is distributable earnings, sort of the statutory income or GAAP income on our Mutual Fund operation. What do we need from a holding company side, considering the growth in the investments, that Doug and Andy in the go-forward businesses need it to make. But that's how we think about sort of the growth sources of flows and then what we would take up to the holding company, and what I described for 2014 is what we're taking up the holding company in '14.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay. And then one final quick one if I may. Doug, what is your expectation around lost trend in Standard Commercial for '14 if maybe a directly comparable number to the 8% rate increase that you showed in the fourth quarter?

Douglas G. Elliot
President

Mark, I would say that in our planning for '14, we're expecting loss trend to be about where it was in '13. So, from a loss trend perspective, single digits generally across all lines, we've had some good news on the frequency side and workers' compensation, and auto, the auto line has been a little warmer than the overall rest of the book. But generally, '14 in line with '13.

A. Mark Finkelstein
Evercore ISI, Research Division

And just remind me, what, like, 4% range, 3%?

Douglas G. Elliot
President

Yes. Yes. 3.5% to 4% is a good point to be at.

Operator

Your next question is from Jay Gelb from Barclays.

Jay H. Gelb
Barclays PLC, Research Division

I wanted to touch base on the Talcott outlook initially. In the slide, it says continued VA surrenders will lead to further core earnings reduction in 2015 for Talcott. I was trying to get a sense of magnitude on that.

Christopher John Swift
Chairman & CEO

Jay, it's Chris. I mean, I think the way to think about it is in relation to AUM. Contracts will decline, but then, your market factors in forces can increase that, but on your earnings fees kind of called higher asset base, per policy basis. So that's sort of the calculus. I think in terms of just roughly numbers, I would expect in '15, Talcott decline another $125 million to $150 million after-tax.

Jay H. Gelb
Barclays PLC, Research Division

$125 million to $150 million?

Christopher John Swift
Chairman & CEO

Correct.

Jay H. Gelb
Barclays PLC, Research Division

Second point is on the overall or, let's say, core return on equity. Around 9% in 2014. Tell us how you plan to get that into double digits.

Christopher John Swift
Chairman & CEO

A lot of hard work. To me, it starts with, and I'm looking at Doug and Andy and the business leaders. I mean, we're going to, as Liam said, the strategy is to profitably grow the go-forward businesses as Talcott shrinks. And you can see what we think is a prudent capital management plan, focused on equity and debt. That philosophy will continue. You add in sort of the expense efficiency targets. And we think 10% is on the horizon. It will take a lot of work, but we still feel comfortable in growing ROE in the 40 basis points plus or minus annually going forward, through earnings growth, through accretive capital management plans and driving more efficiency into the organization.

Jay H. Gelb
Barclays PLC, Research Division

Great. And the debt retirement, Chris, by our estimates, you should get to that 23% range, debt to capital ex-AOCI by the end of 2015. Does that mean that debt retirement should pretty much be complete by the end of '15?

Christopher John Swift
Chairman & CEO

Jay, I'd like to execute our '14 and '15 plans and we'll talk a lot about '16 and beyond. But I've always said we would like to get into low 20s. I always defined low 20s as 22%. And obviously, improving our coverage ratios and when we get our targets, we could then start to think about a different approach, or will it be '15 or '16, I mean, know that we're trying to get to our targets.

Operator

Your next question is from Tom Gallagher from Credit Suisse.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Chris, I wanted to come back to question on Talcott. And if I heard you correctly in response to Mark's question, your hedging costs are going to be going down. So can you talk about whether you expect Talcott to generate meaningful capital, assuming your base plan for market expectations? And if so, how much? And also, I know you're focused on core earnings, but I know net income has been very weak on that block. Is that getting better or worse, factoring in the cost of hedging?

Christopher John Swift
Chairman & CEO

I think, 2 points. On your first one on the surplus, I do expect both Life and P&C to generate a couple of $100 million of surplus after dividends next year. So, we think Talcott specifically can begin to generate surplus based from the net income side. That's why we try to frame it at that $225 million after-tax, that's assuming markets grow 4% and rates follow our trend. And basically, FX remains stable. So I would say, if that's the market condition, we're printing less hedging losses so that there is less of a difference between core and net income. And I tried to frame it as that 1 point ROE difference right now based on our hedging cost going forward.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Got it. And then also, I just want to get a better handle on the way you guys are thinking about valuing this business, because I was just a little confused thinking about the $2.2 billion increase in market consistent value and then the $3 billion of NPV of cash flow positives. And then contrasting that with the 80% offset from hedge losses. So I understand there's capital, that we can put a value on capital depending on how quickly it gets returned. But then there's the valuing the cash flows and the business itself. How do you think about it, taking those 3 other data points that I just mentioned if you can help reconcile those?

Christopher John Swift
Chairman & CEO

No. I mean, you're describing a classic actuarial valuation, right? Value of the block of business, assets and liabilities and the value of the surplus, but we think about it is the same way. I think my comments in my script was trying to lead you to conclude that MCV would not be a transaction value because a willing buyer and seller would have to negotiate, but it is sort of a risk-neutral value that helps build the foundation for your thinking in any potential transaction.

Thomas George Gallagher
Crédit Suisse AG, Research Division

So Chris, sorry, just to follow-up on that. So I would start with 100% of surplus size, I assume, and add, on top of that, market consistent value of 2.2 and then adjust that based, to your point, based on the bid-ask spread from a buyer and seller, if you want to think about it along those terms. But then would I then adjust that downward by 80% considering hedge losses or am I hitting that too hard considering the impact to the hedge losses?

Christopher John Swift
Chairman & CEO

I think you're going to think in terms of the hedge losses, those printed hedge losses are reading results, right? I mean, we booked them as realized losses, so it's in surplus already. So I would say you're already have accounted for it in your reconciliations. And Tom, I'd love doing this with you, but why don't you and Sabra visit, and if you want a little help on any thoughts on the model, we could talk to you off line.

Operator

The next question is from Chris Giovanni from Goldman Sachs.

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

I guess, question on the U.S. VA book. Obviously, lapse has slowed. I know you touched there. I think recently you talked about the possibility of exploring another ESV program. So can you talk maybe where we stand with that? And maybe why or is that still a focus given where NAR stands today?

Liam E. McGee
Former Chairman

Well, Beth will give you her views on that, Chris. I think the ESV performance played out as we said it would. And so now, Beth can give her perspectives on what if anything else things that she's thinking about.

Beth A. Bombara
Chief Financial Officer and Executive Vice President

Yes, thanks, Liam. So currently, in the plan we have right now, we have built in an expectation of doing an offer related to our fixed annuity book. And our plan includes about $30 million of cost associated with that, so it's sort of the next evolution of offerings that we're looking at. Beyond that, the team continues to look if there are other, again as we talked about in the past, sort of nearly focused parts of the business that we would look to. So you should expect that we'll continue to look for that. And as our plans in that area firm up, we will share them with you.

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

Okay. And then, you obviously give us a look in terms of buybacks through January. But wondering how we should think about kind of the cadence of buybacks here over the next couple of years. Will you be optimistic around price or would it be fairly balanced on a quarterly basis?

Christopher John Swift
Chairman & CEO

Chris, I think the way we think about it is $1 billion $1 billion first order, and then we do want to be stable and consistent and prudent, but we'll look at buying opportunities. And in fact, I can just give you an update through yesterday, we had purchased $151 million of shares back in through January, and then first business day of February. So we're been opportunistic when we see it, but we also want to be stable and steady, too.

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

Okay. And then one last quick one. Liam, you talked about in terms of one of the approaches for long term value, top quartile growth in book value, and how should we think about that just in terms of if you were to be executing on transactions within Talcott that could potentially reduce GAAP book value? I mean, is that a focus or is that just studying economics in terms of thinking about what that would do versus your translation of GAAP book value?

Liam E. McGee
Former Chairman

I want to clarify my statement, was that we want to be a top quartile company as measured by total shareholder return over trend. We think that will be driven, we have conviction that, that will be driven by growing book value. And as Chris discussed earlier, increasing our ROE. Obviously, if we were to seriously consider a transaction, we would do what was economic. And as I've always said, we take a look at the purchase price, the amount of capital that could be released versus what our view is of the underlying economics. And that will really inform our decision as opposed to, if you will, solving to a book value answer per se. I will certainly be part of the equation, we're well aware of that. But I think the longer-term view that I'm trying to impart is we are focused on being a top quartile CSR company. We know that will be driven by prudent growth to book value, as well as an increase in ROE, and I think I've given you a consistent frame of reference for how we might view a potential transaction.

Operator

And, Ginger, I think we have time for one more question. I think Chris, had a quick follow-up to Tom Gallagher's question on hedge cost first.

Christopher Giovanni
Goldman Sachs Group Inc., Research Division

Tom, it's Chris. Actually, I think it was Mark that I probably misspoke just a little bit. The 70 and 30 basis points we're hedging for Japan and the U.S. are pretax numbers, consistent with the $75 million spend, which is also a pretax number. So sorry if I confused.

Sabra R. Purtill
Senior Vice President of Investor Relations

Ginger, can we have just the next question or the last question, please?

Operator

Yes, ma'am. Your final question comes from Bob Glasspiegel from Janney.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

Question on whether I'm thinking about Talcott correctly. It seems like 2013 was a nirvana environment with the U.S. stock market up, Japan up, weakening yen, higher interest rates, good for sort of operating results, good for our balance sheet, bad for hedging. We certain reverse those dynamics in the first quarter, yet you have Talcott's sort of earning more than a quarter of the full year earnings. So I just want to make sure that the guidance sort of fully reflects the 255 10-year and the other impacts of the yen, and the Nikkei, et cetera.

Liam E. McGee

Former Chairman

Thanks, Bob. For the question again, Beth and Chris may have their own context. I remind you that yen/dollar on TOPIX/Nikkei are really back where they were just a few months ago. So, well above what we started last year wasn't even at the end of the first quarter. So let's be sure we have that context. So I'd turn over to Chris and Beth for any additional comments you might want to make to Bob's question.

Beth A. Bombara
Chief Financial Officer and Executive Vice President

No. Again, I think that we've taken all those into consideration, and the guidance that we've provided and reflecting the surrender activity that we saw during 2013, kind of our starting point for 2014, and the expectation that we have goes for surrender activity, as well as the impact of the annuitizations that begin in Japan.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

Okay. So it's just when I saw the year end 10-year at 220 -- 320, which has a pretty big grade up from where we are today. I didn't know if that reflected a feeling that this is just a blip in the 10-year, something that you're managing.

Christopher John Swift
Chairman & CEO

Bob, it's Chris. I think the way we thought about our overall plan is that those were our point estimates. I think the ranges that we have around a lot of -- our data provides enough sensitivity for different market conditions. Interest rates, U.S. interest rates and sort of the returns on the assets that back those Japan liabilities aren't directly correlated. So, as we said, at the point estimate, I think at $570 million of core earnings for Talcott, where we sit here today, we still think that's our best estimate, knowing some of the market noise that even happened during the last few weeks.

Sabra R. Purtill
Senior Vice President of Investor Relations

Thank you, and thank you all for joining us for the call today. We appreciate your taking the extra time that we took today for the call. And if you have any follow-up questions, Sean and I are available after the call. Thank you, and have a good day.

Operator
Ladies and gentlemen, this does conclude today's conference call. Thank you for participating. At this time, you may now disconnect.