S&P Capital IQ

CONTENTS

The Allstate Corporation NYSE:ALL

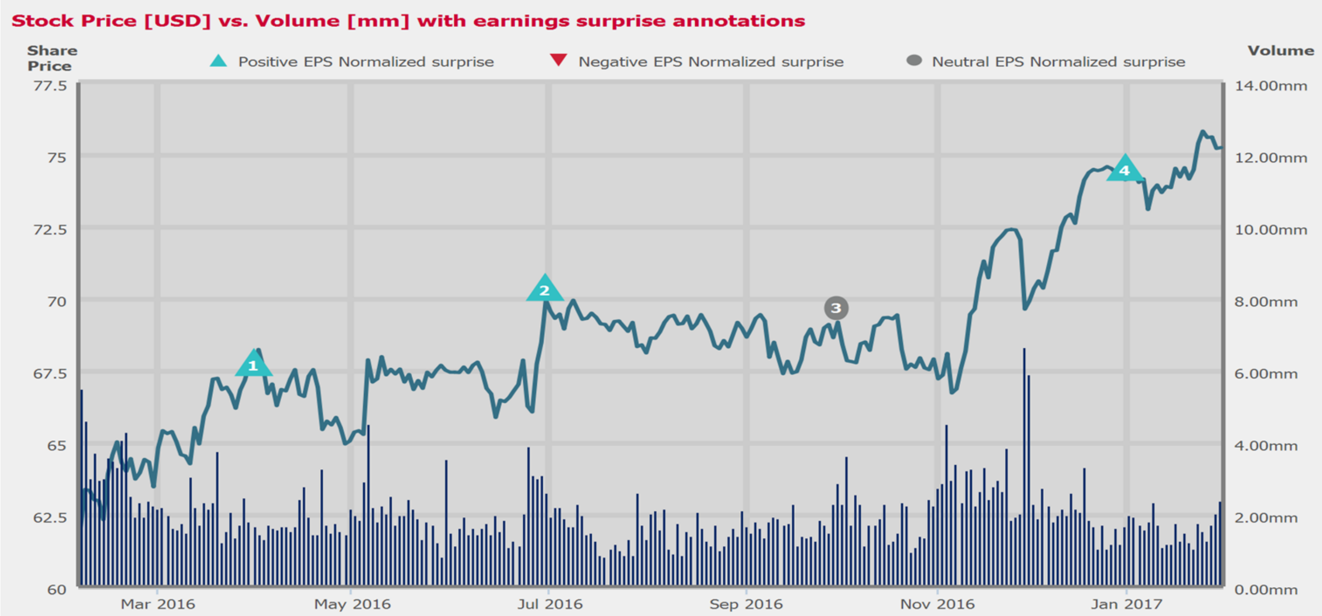
FQ1 2017 Earnings Call Transcripts

Wednesday, May 03, 2017 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2017-			-FQ2 2017-	-FY 2017-	-FY 2018-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.10	1.64	▲49.09	1.33	6.26	6.87
Revenue (mm)	7927.60	7959.00	▲0.40	8007.00	32191.60	33209.67

Currency: USD
Consensus as of May-03-2017 11:12 AM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ1 2016	0.67	0.84	▲1 25.37 %
FQ2 2016	0.58	0.62	▲2 6.90 %
FQ3 2016	1.26	1.26	3 0.00 %
FQ4 2016	1.61	2.17	▲4 34.78 %

Call Participants

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Head of Investor Relations

Matthew E. Winter
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Deutsche Bank AG, Research Division

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Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Allstate First Quarter 2017 Earnings Conference Call. [Operator Instructions] As a reminder, today's program is being recorded.

I would now like to introduce your host for today's program, John Griek, head of Investor Relations. Please go ahead, sir.

John Griek
Head of Investor Relations

Well, thank you, Jonathan. And good morning and welcome, everyone, to Allstate's First Quarter 2017 Earnings Conference Call. After prepared remarks by our Chairman and CEO, Tom Wilson; Chief Financial Officer, Steve Shebik; and me, we will have a question-and-answer session. Also here are Matt Winter, our President; Don Civgin, the President of Emerging Businesses; Mary Jane Fortin, President of Allstate Financial; Sam Pilch, our Corporate Controller; and John Dugenske, our new Chief Investment Officer, who joined the team on March 1.

Yesterday following the close of the market, we issued our news release and investor supplement, filed our 10-Q for the first quarter and posted the results presentation we will use this morning in conjunction with our prepared remarks. These documents are available on our website at allstateinvestors.com.

As noted on the first slide, our discussion today will contain forward-looking statements about Allstate's operations. Allstate's results may differ materially from these statements, so please refer to our 10-K for 2016, the slides and our most recent news release for information on potential risks. Also, this discussion will contain some non-GAAP measures for which there are reconciliations in our news release or our investor supplement. We are recording this call and a replay will be available following its conclusion and, as always, I will be available to answer any follow-up questions you may have after the call.

Now I'll turn it over to Tom.

Thomas J. Wilson
Chairman & CEO

Well, good morning. Thank you for joining us to stay current on Allstate's operating results. Turn to Slide 2, and we'll get started.

We're off to a strong start in 2017 on both our operating priorities and strategic initiatives. You can see the value of having a broad based business model that provides a broad set of protection to customers across North America was evident this quarter as we had excellent profitability despite several large hailstorms. Net income of $666 million, while operating income per share was $1.64. Auto insurance profitability improved due to the profit improvement actions that were started in 2015 and mild weather in January and February. Homeowners insurance generated an underwriting profit despite significant catastrophe losses. The Property-Liability combined ratio was 93.6 and the underlying combined ratio was 84.8 in the first quarter, below the full-year outlook we provided of 87 to 89.

Investment results were solid with higher investment income, which also increased Allstate Financial's operating income. We also closed the acquisition of SquareTrade, which expanded the protection products we offer, gives us distribution to major retailers and added 30 million policies in force. We returned $371 million to shareholders and as you can see at the bottom of the slide, return on equity on an operating income basis was 11.9% for the last 12 months.

If you turn to Slide 3. Given the continued expansion of our business model, we added 2 You Are Here charts. So when you're at the mall or in a park and you're trying to get a picture of the entire place, you're looking for those You Are Here maps. Well, Slide 3 graphically shows the breadth of our businesses.

Allstate's purpose is to protect people from life's uncertainties, and we do this through a wide variety of products and distribution channels. Starting in the center. Our customer focused strategy has resulted in 73 million proprietary policies issued. We also broker over $2 billion of premiums through Allstate agency financial, and we had third-party service relationships with Allstate Roadside, Allstate Dealer Services and Arity. The second ring shows the breadth of our distribution. The outer ring shows the products we provide, with the largest group on the left being the Property-Liability products sold through the Allstate Encompass and Esurance brand. The right hand of the oval shows the wide variety of products and services sold through an extensive distribution network.

If you turn to Slide 4, and we carry this concept further to show the relative impact on the overall company. The upper left pie chart identifies the products that comprise the proprietary policies, including the policies we added with SquareTrade. The middle pie chart shows that most of our revenue is still from the traditional Property-Liability products. The table on the right breaks out this quarter's operating income by 2 major segments, Property-Liability and Allstate Financial. We'll now walk through the components of operating income in greater detail, starting with the Property-Liability business.

Let's go to Slide 5, it shows the Property-Liability results. And starting at the table at the top. Net written premium for the first 3 months of 2017 was $7.7 billion, which was a 2.8% increase from the prior year. The recorded combined ratio was 93.6, 4.8 points better than the prior year quarter. When we exclude catastrophes and prior reserve reestimates and, of course, is our underlying combined ratio for the first quarter, that was 84.8, 2.4 points below the prior year. The 4 Personal Property-Liability customer segments are shown on the diagram at the bottom of the page. The Allstate Brand, which is in the lower left hand, comprises 90% of our premiums written. And that serves customers who prefer our branded products and value personal advice and local relationships. The underlying combined ratio was 83.5, with the decrease from the prior year being driven primarily by auto insurance, which had a 90.9 underlying combined ratio, 5 points below the prior year.

Given the continued progress made in improving Allstate brand auto margins, we're beginning to invest in expanding distribution and marketing to move back into policy growth mode. Esurance, in the lower right, serves customers who prefer a branded product but are comfortable handling their own insurance needs. Our focus is on improving financial results and customer satisfaction. The underlying combined ratio for Auto Insurance improved and was below 100 in the first quarter. The Homeowners business continues to grow rapidly with underlying profitability that reflects startup cost. Encompass in the upper left competes for customers who want local advice and are less concerned about a brand experience and hence are served by independent agencies.

We're focused on improving returns and executing our profit improvement plan in this brand. The underlying auto combined ratio of 97.9 improved 5 points compared to the prior year quarter. Homeowners underlying profitability still needs to be lower than 69.9, given the impact of catastrophies on our reported results. We'll cover the results of the 3 underwritten brands in more detail in the subsequent slides. Now let me turn it over to John.

John Griek
Head of Investor Relations

Thanks, Tom. Let's go to Slide 6 to cover the results for Allstate brand auto. Starting in the upper left graph, the recorded combined ratio for the first quarter was 90.6, which was 8.4 points below the prior year quarter and benefited from increased average earned premium, lower frequency, 1.8 points of favorable prior year reserve reestimates and lower catastrophe losses. The underlying combined ratio of 90.9 in the first quarter 2017 improved by 5 points compared to the first quarter 2016, driven by a 5.4 point improvement in the underlying loss ratio.

The chart on the top right shows the drivers of this improvement. Annualized average premium increased 6.7% to $989 compared to the prior year, while underlying loss and expense increased by 1.1%. This resulted in a favorable GAAP of $90 per policy. We'll provide additional insight into our loss trends by coverage. The bottom half of the page shows the paid severity and frequency trends for both property damage and bodily injury. Property damage paid frequency, shown by the blue bar, decreased 3.2% in the first quarter 2017 compared to the prior year quarter. Better-than-expected improvement was observed mainly in January and February as the country broadly experienced milder than normal winter weather. Absolute frequency levels in March were more consistent with the fourth quarter of 2016. Paid frequency trends over the last 4 quarters have now been flat or declined year-over-year.

Property damage paid severity increased by 4.8% in the quarter due to the impact of increased third-party subrogation payments, higher cost to repair new model vehicles and increased volume of total losses. On the bottom right, bodily injury paid frequency decreased 20.5% in the first quarter, while paid severity increased by 25.1%. These results are consistent with the trends experienced over the last 2 quarters. Frequency and severity should be looked at in combination to get a sense of the true underlying loss trends. And as we discussed the past 2 quarters, the decline in BI paid frequency and corresponding increase in paid severity was driven by process enhancements related to our claim handling discipline around the establishment of liability for BI. These changes involve requiring enhanced documentation of injuries and related medical treatment and resulted in a reduction in the mix of smaller dollar claims paid.

When we adjust for the impact of this BI process change, the increase in BI severity is more consistent with medical inflationary trends, partially offset by improvements in loss cost management. We continue to be comfortable with our bodily injury incurred severity trends. You can see by the inset box in the bottom right graph that the combined impact of frequency and severity since the process change last year has essentially been flat.

Slide 7 provides detail on premium and policy growth for Allstate brand auto. Net written premium growth, shown in blue on the top chart, reflects continued average premium increases, stabilizing retention and improved new business trends, partially offset by a 2.9% decline in policies in force. We are taking a balanced approach to profitable growth and margin improvement by continuing to execute our auto profit improvement plan in markets with returns below target levels, while implementing growth plans in markets that have achieved rate adequacy. Growth investments include expanding distribution capacity and marketing.

In the first quarter, approved rate increases totaled 1.7% for the Allstate brand, of which 0.6 points was driven by an improved rate in California. We anticipate the overall magnitude of rate increases to moderate going forward as profitability trends improve. The charts on the bottom of the page show new issued applications and retention for the last 3 years, along with historical ranges represented by the dashed gray line. As we implement growth plans, we are beginning to see positive signs of growth with new business applications shown in the bottom left of 4.5% in the first quarter.

Auto retention, shown on the bottom right, also has a significant impact on growth and has stabilized over the last few quarters.

Slide 8 highlights Allstate brand homeowners. The top part of the page provides detail on our profitability results. The homeowners recorded combined ratio was 93.7 in the first quarter, which generated $107 million in underwriting income despite elevated catastrophes late in the quarter. Over the last 12 months, $1.1 billion of underwriting income has been generated by this product line. The underlying combined ratio of 61.3 continues to reflect strong profitability and is within our long-term target range of the low 60s for this line.

The bottom half of the page provides detail on our growth trends. New business and retention levels declined, leading to a 1.4% reduction in policies in force. New business and retention levels in the first quarter are performing near the middle of the historical range shown by the gray lines. Our work to improve auto margins beginning in 2015 has impacted the homeowners line, since many of the customers in this segment prefer to bundle their purchases. The impact of the auto profit improvement actions on homeowners tends to lag auto by a quarter or 2 because of the 12-month policy and generally has a different renewal effective date compared to auto. As auto has experienced an improved trajectory in new business trends, we have begun to see moderation in the rate of decline in homeowners new business.

Slide 9 highlights Esurance results. Esurance is focused on improving financial results and customer satisfaction. So the recorded combined ratio of 102.4 in the first quarter, shown towards the bottom of the upper left-hand table, was 3.8 points below the prior year quarter driven by lower expenses. The expense ratio decreased 5.9 points for the quarter and reflects reduced advertising, improved customer service efficiency and a smaller impact from the amortization of intangible assets. Shown in the upper right is the decline in the combined ratio over the last 2 years. The auto underlying combined ratio, highlighted on the bottom right of the page, was 99.8 in the first quarter, 3.8 points better than the first quarter 2016. Lower expenses and better frequency and severity trends contributed to the improvement in underlying margins. Esurance growth trends are highlighted on the bottom left of the page. Net written premium continues to grow on increased average premium, while policies in force were flat to the first quarter of 2016. Policy growth in homeowners is offsetting the decline in auto policies. New issued applications declined as a result of lower advertising, while auto retention improved by 0.8 points.

Going to Slide 10, it highlights results for Encompass. Encompass results for the first quarter were impacted by elevated catastrophes in March and profit improvement actions that continue to be implemented in states with inadequate returns. The recorded combined ratio was 111.7 and included 23.7 points or $67 million of catastrophe losses in the first quarter. Encompass results were significantly impacted by the March 26 hail event in Texas. The auto recorded combined ratio of 100.7 was 5 points better than the prior year quarter. The underlying combined ratio of 86.6 in the first quarter was better than the first quarter of 2016 as profit improvement actions continue to take hold. The decline in premium and policies in force in states with inadequate returns has impacted overall top line trends. And at the same time, we've begun to selectively implement targeted growth plans in states with adequate rate levels.

Now I'll turn it over to Steve.

Steven E. Shebik
CFO & Executive VP

Thanks, John. Slide 11 covers SquareTrade's results. We acquired SquareTrade for $1.4 billion in January. Through purchase accounting we revalued the balance sheet, assigning $486 million to amortizable intangible assets such as customer relationships and technology and $1,080,000,000 to goodwill. On the income side, as a service business, premiums written of $81 million for the quarter reflect the magnitude of product sales, while earned premium of $59 million reflects the recognition of that premium over the approximately 2.5-year average duration of coverage. The underwriting loss of $35 million for the quarter is significantly impacted by expenses related to growing the business as well as $23 million of amortization of purchased intangibles. We anticipate amortizing approximately $90 million in 2017. The intangible assets are being amortized on an accelerated basis with approximately 75% expected to be amortized by 2021. As highlighted in the exhibit on the upper right, SquareTrade had a small $16 million dilutive impact to our consolidated operating income in the quarter, including the underwriting loss and their financing cost. This excludes the amortization of purchase intangibles I've mentioned above and $13 million of after-tax onetime transaction cost reported in net income, but not operating income. We are developing operating statistics and performance metrics for SquareTrade to help you understand quarterly results, which will be included in the second quarter earnings.

Turning to Slide 12. Allstate Financial premiums and contract charges totaled $593 million in the first quarter, an increase of 4.8% compared to the prior year quarter. Operating income of $110 million, an increase of 5.8% over the prior year quarter, was driven by improved investment returns, partially offset by higher mortality in the Life business. Net income of $108 million was $40 million or 59% higher than the prior year quarter due to lower net realized capital losses. Net operating income trends by business are shown in the chart at the bottom of the page. Allstate Life net income of $57 million was flat to the prior year, while operating income of $59 million was $7 million below the first quarter of 2016 as higher mortality was partially offset by higher premiums. Allstate benefits net and operating income were both $22 million in the first quarter of 2017, with operating income consistent with the prior-year quarter.

Premiums and contract charges increased 7.2% compared to the prior year quarter, primarily related to growth in critical illness, accident and hospital indemnity products. Higher expenses were driven by continued growth and onetime expenses, including guaranty fund assessments. Allstate annuities recorded operating income of $29 million in the quarter, an increase of $14 million over the first quarter of 2016 due to higher investment spread.

Slide 13 provides details of our investment results. We manage the portfolio's risk profile proactively and holistically, considering relevant market conditions and our corporate risk appetite. The chart at the top left shows how we have migrated the portfolio to more balanced risk and return profile. We reduced interest rate risk to a lower allocation to investment grade interest-bearing assets as well as targeting a shorter fixed income duration with the belief that markets weren't providing a sufficient compensation for taking interest rate risk. Through our performance-based investing, we're replacing market risk with idiosyncratic risk, emphasizing ownership over lending. These investments now comprise $6.2 billion or 8% of the portfolio, and while they require higher economic and regulatory capital, we expect them to deliver attractive economic returns for our shareholders.

Pretax yield by business segment are shown at the upper right. The interest-bearing yield reflects the stability of fixed income portfolio earnings, while the total yield includes the variability of performance-based investments across the quarters. The Property-Liability interest-bearing yield is close to market yields and respond quickly to increases in interest rates. Allstate Financial has a higher-yielding longer duration profile aligned with its liability structure. Net investment income by strategy is shown in the lower left graph. The portfolio total return is provided in the lower right. Total return for the first quarter was a solid 1.6%, reflecting fixed income price appreciation and credit spread tightening and strong equity market performance. Investment income has delivered a consistent contribution to return of approximately 1% per quarter.

Slide 14 highlights the continued strength of our capital position and our financial flexibility. Shareholders' equity of $21.2 billion at quarter end reflects the increase of $818 million for our first quarter 2016. The debt-to-capital ratio of 23.1% is 3 points higher than prior year, due to the issuance of $1.25 billion in senior unsecured debt in December 2016 to fund the acquisition of SquareTrade. We also held $2.7 billion in deployable holding company assets at quarter end. Book value per share of $52.41 increased by 7.2% from the first quarter 2016, primarily due to retained income. We returned $371 million in cash to common shareholders in the quarter, with a repurchase of 3.2 million shares for $249 million and $122 million in shareholders' dividends. At the end of the first quarter, there was $442 million remaining on the $1.5 billion repurchase authorization.
Now I'll ask Jonathan to open the line up for your questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Josh Shanker from Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

Two hopefully quick questions, one Allstate and one SquareTrade. Let's just say that you guys have the pricing right and everything's good to go. I know you do have Esurance, you have Encompass, but really Allstate Brand is the main driver here. What's going to make sure you get the maximized shots on goal? How do you get people into the stores compared to a Progressive that's online or independent agencies? Are you going to have a chance to reach all the possible customers you want to?

Thomas J. Wilson
Chairman & CEO

Josh, thank you for the questions. This is Tom. I'll start and then Matt can talk about the things we're doing to make sure we grow all of our businesses. But first, if you go back to Slide 3, it's really about creating shareholder value and improving our long-term strategic position at the same time. So both today and tomorrow, right? And so if you remember, the left-hand side of that, those are the low unit growth markets like auto and home insurance, and our strategy there is to really match value and price. So we have, of course, our trusted advisor initiatives. We're doing the Allstate agencies, Esurance is raising customer satisfaction and doing more stuff online, more electronically. In those businesses, once you get done matching value and price, you just have to make sure you're looking at both share of market and share of profits. We manage both of those. We're not interested in taking share and losing money, nor are we interested in not having many customers and making a higher return. So it's a share of both market and profits. When you look around, there are the higher growth markets like Allstate Benefits, we've had a 9% comp on annual growth rate in the business for 17 years running. And we get mid-teens returns in that business. So we obviously try to grow quite rapidly there. In the newer emerging markets, things like Arity, our new Roadside model, our SquareTrade, it's really about building a stronger strategic position, which includes both growth and building out our skills and capabilities. Matt, maybe you want to talk specifically about Josh. And Josh, I think you were talking about auto insurance, primarily.

Joshua David Shanker
Deutsche Bank AG, Research Division

Allstate brand, understanding how it grows.

Matthew E. Winter
President and President of Allstate Insurance Company

Josh, it's Matt. I think one of the core fundamental assumptions you have to have is that despite the fact that we have a foursquare, I would not describe the foursquare quite the way you implied in your question. It's not really pure trade-offs. It's not as if in the lower left, the Allstate brand is not providing technology support for online lead generation or self-service capabilities. It's really our goal in the Allstate brand is to provide many, if not all, of the same tools, capabilities and points of convenience that are available for the lower right quadrant or the upper left quadrant, plus the local advice and service of an Allstate agency owner. So I don't think of it as us naturally limiting ourselves to a subsegment. We're certainly focused there, because that's where we believe we're focused in the Allstate brand on those people with the bias towards a branded product and local advice and service. But we don't ask them to give up things. We don't ask them to give up the capability for using technology or self-service capabilities. So we believe our growth prospects are quite strong because we believe we're offering something few, if any, are able to do. We're offering quality products at a fair price, good value features and the special expertise of local trusted advisors in the community.

Joshua David Shanker

Deutsche Bank AG, Research Division

Okay. I realize you have all the fingers in the pie and we'll see what happens. Let's talk about SquareTrade a little bit. I'm surprised, from my reading, if I read it right, you're actually taking more underwriting risk at SquareTrade. I thought that was in the distance as you get the capability? Maybe I misunderstood a little bit. To what extent are you going to be making underwriting gains and losses at SquareTrade versus how much you're ceding to partner channels and whatnot? What's the time line we should think about an understanding the learning curve for Allstate?

Don Civgin
President of Emerging Businesses - Allstate Insurance Company

Josh, it's Don Civgin. SquareTrade, since we just closed the transaction at the moment, they're retaining their existing agreements as far as underwriting the paper and so forth. So we don't have any risk at this point. We do intend to transition to the Allstate taking the risk in the future. I don't want to give you a time line as to exactly when we're going to do that, but we need to get ourselves lined up to do it. We're working on it and there's no reason that we shouldn't take that risk to Allstate.

Joshua David Shanker
Deutsche Bank AG, Research Division

So what does it mean when you cite a combined ratio? What numbers -- my ratio -- is SquareTrade the entity based on its partners or just the Allstate portion of what's going on?

Don Civgin
President of Emerging Businesses - Allstate Insurance Company

It's just the Allstate portion of what's going on.

Joshua David Shanker
Deutsche Bank AG, Research Division

Okay. And then there's premiums coming in, I guess, to Allstate. I guess, I don't understand why -- if you guys aren't taking the risk, I thought you'd just be getting commissions, not necessarily premium volume.

Thomas J. Wilson
Chairman & CEO

It's a little confusing. I understand what you're saying. It doesn't sound like a normal combined ratio. Over time, it will start to look more like a normal combined ratio, but as Don pointed out, we, of course, cede most of the underwriting risk in a quarter, actually, to a third-party. We're working on bringing that back in-house. So we will actually, in watching underwriting risk, it will add to our return on capital and add to our profitability.

Operator

Our next question comes from the line of Greg Peters from Raymond James.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

I wanted to come back at you with another question around your competitive positioning. With an 84.8% underlying combined ratio at Allstate and the 90.9 in the Allstate Brand Auto, do you think you might be getting to a point where you're at a competitive disadvantage from a pricing perspective? Or maybe a better way to ask the question would be is, what's the right long-term target for the underlying combined ratio as we think about it?

Matthew E. Winter
President and President of Allstate Insurance Company

Greg, it's Matt. So this is what we spend the vast majority of our time doing, which is trying to ensure that we're walking that fine balance between profitability and long-term growth potential to maximize shareholder value in the long term. And I don't believe that we are placing ourselves at a competitive disadvantage. I think we got out in front of the frequency spike. We reacted quickly. We reacted strongly. And we, in my opinion, have put it, for the most part, behind us. There's, of course, a few geographical exceptions to that. But as a general matter, we believe we have essentially caught up and we are now able to react to and price to emerging trends in frequency and severity as they appear. And we feel very good about that position. We do not believe we overshot the target. We benefited in this quarter from significantly better weather and frequency results in January and February that I think is either sustainable or that was expected. We saw March return to something much more like fourth quarter of 2016. And so we believe that we are positioned very well. It's all a question now, when you have a complex decentralized entrepreneurial system as we do. It's now a question of building momentum again for growth within that system. And because it's a complex system, there's a time lag. There's a time lag both ways, but once that momentum gets built it's a very powerful flywheel. And that's really built through agent confidence in their investment, since it's an entrepreneurial system. And in large part, it's not just the result of how much we invest in marketing and lead generation, it's whether or not the agencies and the agency owners are investing and whether they're adding staff, whether they're putting money in local marketing funds and lead generation. And as they see our competitive position improving, as they see shopping behavior triggered by competitor rate actions, and as they see our rate taking stabilize and moderate, they're in a much stronger position to invest and for us to begin the momentum on the growth side.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Excellent color. Maybe, I guess, slightly technical, but you have reported favorable reserve development in the last couple of quarters. And I'm just curious what the underlying trends are there that are driving that favorable reserve development. Is that a trend that we should expect to continue?

Steven E. Shebik
CFO & Executive VP

Greg, this is Steve. When we look at the trends of our business, we talked multiple times about how we set our reserves. We look at a lot of information. And at each quarter end period, reporting period, we feel that our reserves are properly stated. So things change. And as Matt talked about last year on a number of occasions, something we would call claims excellence, we're making changes in our claims practices. And over time, that develops and if you look at the reserves that we've been reestimating in prior periods, a lot of it's just based on what we're seeing in terms of what we've been doing in our underlying practices. So if you look at the reporting, it's a cross of primarily Allstate brand, property -- probably the physical damage coverage has had some of the favorable impact as do the injury coverages, which are over a period of time.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

So just safety stuff.

Thomas J. Wilson
Chairman & CEO

Remember, Matt I think mentioned it last time. When we do our claim reserves, we count frequency. We look at how many claims we have, we look at what types. And some people do their reserves based on a targeted loss ratio. They say this book of business, we're going to get 70% and they book the 70% until such time as they see something differently. We do it from the ground up, that gives us a slightly different pattern the way we do it.

Operator

Our next question comes from the line of Sarah DeWitt of JPMorgan.

Sarah Elizabeth DeWitt

JP Morgan Chase & Co, Research Division

Just first on the guidance. Curious on your thought process, why we you didn't lower the underlying combined ratio outlook given the 85% this quarter. And how much was that result helped by mild weather?

Thomas J. Wilson
Chairman & CEO

On the guidance, 1 quarter does not a year make. We've made this -- that number every year since I started doing it, I don't know, 10 or 11 years ago. We do it, so we're going to be in the range. We still think 87 to 89 is good. Matt mentioned that we have pretty good frequency in January and February. We don't expect January and February frequency results to be reflected throughout the entire year. So we're still comfortable at 87 to 89.

Sarah Elizabeth DeWitt
JP Morgan Chase & Co, Research Division

Okay. And the mild weather is about 1 point, 2 points?

Thomas J. Wilson
Chairman & CEO

That kind of variance analysis is almost impossible to do because it, of course, varies by geography, by time of day and trying to get the weather analysis down to be that specific. That said, if you look at our results and you compare them to the only other real public competitor where you can see monthly results. If you look at Progressive's monthly results, they were down in the 3% and 4% of frequency in January and February and then about 1/3 of that down in March. Our overall results underlying combined ratio was 2 or 3 points better than theirs in total, but our trend looks similar to theirs.

Sarah Elizabeth DeWitt
JP Morgan Chase & Co, Research Division

Okay, great. And then one of your largest competitors, State Farm, had a big auto underwriting loss in 2016. Are you seeing any opportunity to take some profitable market share now that you've fixed your auto business?

Thomas J. Wilson
Chairman & CEO

Well, I think that it sort of links -- that links to Josh's and Greg's question. Maybe take Matt's comments where we do a little competitive comparison to it to help. I think the answer is yes, we think we're positioned to start to grow again, but it takes a while. So Matt mentioned, this is -- our proprietary channel is, as Josh pointed out, is most of the business and it's a really powerful channel, man. When you want to get something done, whether that's change your risk profile, get margin initiatives going, you can move that channel because you are, in effect, completely aligned with them in terms of your business objectives. And that also includes growth. That said, there's somewhat of a lag in growth because as Matt talked about, that business it works as a combined system as opposed to -- this is where I can maybe help you see the comparison. If you're an independent agency company, the flow coming through those independent agencies as new business is pretty much the same. Who gets it? It's different. So if an agency is writing 100 units a month and you've got 20% of them and you decide you're getting 20% a month and then you decide you want less, you get 10%. If 6 months later you decide you want to go back to getting 20%, you can get 20% again. That said, it's a jump ball, and you've got to fight for that business on largely a price basis. In our system, it takes a little longer to get going and drive that growth up than an independent agency channel. But it's much more sustainable. And you can build a stronger economic value proposition with longer lifetime values.

Operator

Our next question comes from the line of Paul Newsome from Sandler O'Neill.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

The growth comments you made, are they uniform across the distribution systems? Obviously, you've already spoken about the Allstate brand business, but what about the growth of the other pieces?

Matthew E. Winter
President and President of Allstate Insurance Company

It's Matt. I'll start with Encompass and then I'll pass it over to Don for some comments on Esurance. I'd tell you it's similar, although it's delayed. So first of all, within the Encompass system, we are a smaller system than the Allstate branded system. As a result, it doesn't have the benefits, the same benefits of scale as the Allstate system. It's more volatile, it's more subject to odd-outsized results, both negative and positive, depending upon on weather fluctuations and cats. But it also has a 12-month policy, which delays the earning rate and the effectiveness of some of the rate actions. So while I think we started the response to the frequency spike at a similar time within the Encompass channel, it will take longer before they emerge the way that the Allstate brand has emerged. That's not to say we don't see improvement already in certain geographies. It's going through quite nicely. We do have the advantage there, as Tom just talked about, that's an independent agency system. So when we decide to retract or retrench in a state, we can do it pretty quickly. And when we are in a profit challenged state, we can decide to pull back and impact the results fairly significantly and fairly quickly, which we're not able to do quite the same way in an Allstate proprietary channel. So the takeaway is you will see the same dynamics, but there will be a little more volatility in the Encompass side and it will take about 12 to 18 months longer than it has on the Allstate side. And now I'll pass it over to Don to talk a little about Esurance.

Don Civgin
President of Emerging Businesses - Allstate Insurance Company

Esurance is a little different as well for a variety of different reasons. Obviously, it's a different customer mix, it's a slightly different product. We do our own pricing and we have our own loss trends we watch and so forth. But it's also a direct business, which means in some ways it can react more quickly. We acquired Esurance a little over 5 years ago. It basically doubled in the first 4 years. So we know it can grow. And we know the brand, particularly with Allstate behind it, can work. And but having said that, the combined ratio was getting higher. And maybe it wasn't as big a deal when it was only $850 million in premium, but when it doubles, it begins to impact the corporation's results as well. So we decided to focus on achieving more profit -- more GAAP profitability. I think we've said consistently over the years, we run Esurance on an economic basis, so we simply want to make sure that we're writing business that's good over its lifetime. And the accounting convention related to direct businesses where you expense the marketing in the quarter you take it, it creates kind of a discontinuity between GAAP and the economic numbers. So I'm really pleased that they've been able to do that. I know Steve mentioned that they've been focused on achieving profitability and improving the customer experience. They've made great progress on both those fronts. When you look at the combined ratio this last quarter, it's down substantially. And if you look at the trend, not just year-over-year but sequentially it's down. I like where the underlying loss ratio is, I like what they've done with expenses, but the reality is they only grew 1% in written premium. So we would like to see them return to growth, but with the underpinnings of having the profitability where they want to be. Once they begin to pivot off that, I think it will occur probably faster because it's direct as opposed to going through the agency force, and their policies are 6-month policies as well.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

And my second question relates to the distribution expansion that you talked about as well. If you could just give us some more details about exactly how that's progressing and number of agents and where the distribution is expanding. I assume that you're usually talking about the Allstate brand product when you're talking about this expansion of distribution.

Thomas J. Wilson
Chairman & CEO

So if your question is about the Allstate brand, we can do that. But we also obviously have distribution to benefit brokers with Allstate Benefits. We do most major retailers now with SquareTrade. We have lots, mid-thousands of other distribution points whether it be auto dealers, and third-party arrangements we have with telcos and auto companies on roadside. But so are you assuming then on Allstate, Matt can talk about that if that's it.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

I'm most interested in -- obviously, I recognize that distribution is broadening out other places, but I'm most interested in that resumption of the actual distribution growth in the Allstate branded business.

Matthew E. Winter
President and President of Allstate Insurance Company

Sure. Paul, it's Matt. Well as you know, we disclosed in the investor supplement some of the agency data, Allstate agencies and licensed sales professionals and Allstate independent agencies. So I'll refer you to Page 14 of the investor supp for that data, but let me just give you some color on it. One of the most difficult things to do during a time that you're taking a lot of rate to catch up to a frequency or severity spike is to add new agency owners, because they depend exclusively on their ability to put on new business. They don't have an in-force to rely on. And as a result, during that period of time from late '14 through '15 and the beginning of '16, it was exceptionally difficult for us to maintain what has been our historical pattern of adding agency owners each and every year, each of them adding licensed sales professionals and also growing exclusive financial specialists to partner with them. And so during that period of time that we were focused on rate, the ability to add the newer agencies was diminished. And so what we focused on there was encouraging our existing agencies to add licensed sales professionals and to open up satellite agencies and branches. But it was difficult to start scratch agencies. What we've been able to do now is to reinvigorate that effort. And that is an effort that I would say is geographically focused in that it is strategic deployment where we go through a fairly thorough and sophisticated analysis of market potential by geography in order to decide where to place them. But it's so dispersed, I can't tell you it's concentrated in one particular area, other than to say that we tried to go where we haven't been before. And so there are vast areas of the United States and even within our existing states, areas where we have historically not had Allstate agencies that we are intentionally putting on those Allstate agencies. We've also changed our deployment plans, some new agency owners coming into the system are coming in with 3 licensed sales professionals as opposed to our historical pattern of 1 or 2. And so as they come on, they're able to get up to speed faster, they're able to have an impact faster and we believe they'll be more sustainable. So it's a fairly significant effort. It is focused on all 3 prongs: exclusive agents, licensed sales professionals and exclusive financial specialists. We have a couple of efforts within that to focus on veterans. We have a veterans licensed sales professional hiring initiative, where we're partnering with several agencies within the Department of Defense in order to provide job opportunities to returning veterans from Iraq and Afghanistan. And we're quite pleased with that, not only because we think it's the right thing to do, but we're adding quality already licensed sales professionals to our agency force. So the distribution focus and points of presence focus is an ongoing effort. And as we've mentioned, it's a system. It takes a while to get that going. The classes take a while before they're up and running and before they'll have an impact. But we had a great first class in the first quarter, a fairly significant sized group. And we -- the pipeline looks exceptional. We're putting in greater effort on recruiting. We have more assistance from the corporation in recruiting. The human resource area is helping provide it. We're using data analysis and decision sciences to help us recruit and select better. So it's a full-fledged, full force effort on the part of the corporation to improve points of presence.

Operator

Our next question comes from the line of Elyse Greenspan from Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

I had another question, just to get a little bit more color on how you guys think through the growth that we're going to see, both the new business and your retention stabilized and how that can pick up from here. I know we think back over the past couple of years, a lot of players in the auto space have kind of grown into some margin problems just given the elevated frequency and some companies seeing elevated severity trends. So how do you guys balance this renewed push to growth with the mindset of still looking to reach your margin goals?

Thomas J. Wilson
Chairman & CEO

Elyse, there's a lot in there. I mean, maybe a little -- overall, we think the competitors who we follow publicly and then we, of course, follow all the mutuals in terms of their filings and reciprocals are increasing their prices, some of them quite rapidly, we think that will lead to increased shopping behavior. And Matt can talk about how we're capturing that with both new business and what that also does and then where we are in the pricing cycle, what that does for us on retention.

Matthew E. Winter
President and President of Allstate Insurance Company

It's an important issue. I also, though, I want to point out at the outset that for the most part, a lot of our conversation so far this morning on growth has been related to new business. But in fact, the biggest lever we have in total item growth is retention improvement. And when you look back to the time frame that we were really growing a couple of years ago, retention was about 1 to 1.5 points higher than current levels. And that's a very powerful thing at our retention levels. And with our size of the in-force. So while you talk a lot about points of presence and lead generation and increased investments in growth on the new business side, I don't want to discount the fact that really one of the most crucial leverage we have is on the retention side where we have a lot of energy and effort to improve the retention, especially first retention in our book. We have the whole new on-boarding process. We have a whole lot of work being done, again, with data analytics and emerging technologies to change the on-boarding and the initial experience with our new customers to ensure that their initial experience is as strong as possible. And we think that now that we're moderating our rate, we're going to trigger less shopping behavior on our customers and improve retention. At the same time, many of our competitors are still taking fairly outsized levels of rate and triggering shopping behavior on theirs. So to the extent they're taking higher rate levels than we are, we're moderating ours. We believe that we'll be able to benefit from that and capture some of those customers. The balance with our profitability, we feel, as I've said, really good about it. We believe that our approach to the business and you can look back over the years, we have a tremendously strong profitability muscle. It's a natural muscle of this organization. If you know the movie The Blind Side, our natural reaction is protect profitability. And we do that innately and intensely. That being said, we're excited about our growth possibilities with those newly restored margins. And the final comment I'd make is, remember that this is geography by geography, and we approach it on a micro basis. So some of the things I'm talking about are general comments, when you go state by state and subgeography by subgeography, there will be different dynamics. In some areas, we're way ahead of the game and our profitability is fully restored. And we have the foot on the gas completely. There are other geographies where we still have a little more work to do and we will maintain our margin discipline before putting the foot on the gas on growth.

Thomas J. Wilson
Chairman & CEO

Elyse, one other factor is, Matt was talking about our second objective, make sure we achieve target return on economic capital. Our first corporate objective is better serve our customer. We measure that by Net Promoter Score. And the Net Promoter Score was up in the first quarter. So just as we overachieved our combined ratio of goal for the first quarter, we feel like we overachieved on our Net Promoter Score. Elyse, that's exactly what Matt is talking about. It's point of retention to point of growth.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay, that's great. And then just tying together some of this commentary. As I look at the Allstate brand auto book and the underlying loss ratio within that. Obviously, there was some favorable frequency trends that you pointed to in the Q1. As you think about improving your retention, some new business growth combined with still taking rate on areas of the country that aren't at profitable levels. I mean, do you see the kind of X favorable frequency underlying loss ratio within that book still continuing to improve from here?

Thomas J. Wilson
Chairman & CEO

It's really hard to project what frequencies are going to do from here. What we do is just when we see it we react. I think the point Matt made, which is we're not behind the curve now, we're at where we need to be. So if things happen, we can adjust from there. You have to do it a little more aggressively if it moves quickly. So if it was to move like it did in 2015, we might have to go right back to what we did again. If it is more normal and less out of pattern, then the impact on our business would be substantially less than it has been in the last 2 years.

Operator

Our next question comes from the line of [Alan Pisano] from Columbia Management.

Unknown Analyst

I certainly appreciate that you guys have improved the claims management process as far as BI goes, I'm looking at Slide 6, and Allstate has always been very good at making sure they don't pay claims they're not supposed to pay. One question of you though, is it possible to get a sense, and if you can't do it numerically maybe more subjectively, is it possible to get a sense as to what these frequency and severity numbers for BI severity on Slide 6 would have looked like under the old system? I'm just trying to get a sense if we're at any sort of inflection point or not.

Matthew E. Winter
President and President of Allstate Insurance Company

It's Matt. I think if you look at PD, paid frequency and severity trends, you get a little bit of an insight into overall trends in the business. I remind you that one of the problems we were looking at, the BI chart on the lower right, is that's paid frequency and paid severity, which is a little more volatile. So you can't -- it's influenced a little bit more by the mix. You could have 1 large loss in there that throws it off. So it's not a mathematical, you can't just a 25.1 and minus the 20.5 and come up with the answer. It's -- you have to do it on a longer-term basis. I'll go back to something that Steve said and that Tom referenced. We feel comfortable that our BI trends, our incurred severity trends, are where they should be based upon medical inflation and all the work we're doing to manage claims cost. We are laser focused on it, as we should be, to pay the right amount, the fair amount and the amount that the customer or the injured party deserves, but not more and not less. And so the process enhancements are working. We feel good about them. We, as Tom mentioned, reserving is not impacted because we take into account in a reserving exercise, all of these process changes and operational changes and incurred trends and pay trends. And so I don't want you to think that the distortion caused by some of our operational excellence things influence our reserving trends. They don't. We're well aware of those and at the time we do the reserving, that's all factored in.

Matthew E. Winter
President and President of Allstate Insurance Company

If you're thinking long term, right, so there's always this question about with machine-to-machine communication, smart cars, antilock breaks, all the safety stuff, there will probably be fewer accidents in the future. We, of course, didn't see that in the last couple of years. And you can make the same argument about fewer bodily injury accidents, or bodily injuries, because of the air bags and safety equipment. But we haven't seen any big break there. So there's nothing changing from a long-term standpoint. What Matt is referring to is just the way we count.

Unknown Analyst

Well that's helpful, and I appreciate that. I have one other question if I could, which is I guess a bigger question. The Allstate captive agency is a tremendous asset. And as you guys said, you've been very focused on profitability there. You've always taken profitability over growth. At the same time though, we have other businesses which have been, I think, have been dilutive to your margins, dilutive to returns, whether it's Encompass or Esurance or now with SquareTrade. And I'm trying to square these two things. Because you have been so disciplined on the Allstate side, but yet we've expanded into other distribution areas to increase the volume that Allstate has available to it, but at the harm of returns and margins. I just wonder if you could talk about that, Tom.

Thomas J. Wilson
Chairman & CEO

Yes, I will. So if you go back to Page 3, what you referred to is really the left-hand side of the page where we know how to both moderate our market share and our profit share quite effectively. When you start to walk around the top, the life and retirement piece off the top, we get good low teens return on life business. It works well with our agencies broadly. So as I said, that's a value add. Our Allstate Benefits, I mentioned, gets mid-teens and is growing quite rapidly. Allstate Annuities is a detractor, as you point out. We stopped writing that business. In addition, we took an action which hurts ROE but helps long-term shareholder value, but we did it on purpose. And that is so we have some long dated payout annuities, about $12 million of them. And really, that's like a pension fund. And so you should be more invested in equity life securities. The capital charges associated with that are substantially higher than it would be by having fixed income. Even though economically, it is absolutely the right thing to do. So we decided to take the ROE hit and increased shareholder value. When you look at our actuarial stuff, assuming it all pans out, that was a good move. So that one, the Allstate Annuities, is a drag on it. When you look at Roadside, we have a new fulfillment model. We get about 5 million claims a year. We've improved the average time of arrival by about 30% with our new fulfillment model. And it's about $400 million business in revenues. If you were to put that business outside the company, it would have higher value. I believe people would look at it and think it's a fabulous business. You might say, well why don't you get rid of it? Because it's really linked to Arity, which is down below, which is our connected car business. And that's a place where we have -- we're building a strategic platform so that we can leverage our position on the left-hand side with our customers to really both improve that business with Arity, do better pricing, give more effective roadside service, but also maybe offer that to other people. Dealer Services is a business whose profit has gone down. It's a relatively small piece. And then SquareTrade, of course, we bought and we said it is dilutive, but we think broadening our product portfolio to include computers and TVs and cell phones makes a lot of sense to us and the broader distribution through all the major retailers offers a lot to growth potential. So it's about balancing overall growth and we try to do that both with individual things. We hold each of them to their own individual standards, so Don said we backed off on Encompass -- on Esurance. We could have kept growing Esurance, but we decided it has to be economically viable. We apply that same logic to all the businesses, but with the goal of making sure we build a broad-based strategic platform that can weather all kinds of changes.

Operator

Our next question comes from the line of Jay Gelb from Barclays.

Jay H. Gelb
Barclays PLC, Research Division

Going back to catastrophe losses in the quarter. It was the worst catastrophe quarter for the U.S. insurance industry at least 20 years. And I think it's worth noting that a 10-point impact on Allstate's combined ratios is obviously manageable within the scope of that damage. Can you talk a little bit about what the company's done, either from a policy term standpoint or broader risk management, that kept the impact of those catastrophes on Allstate's results in check?

Matthew E. Winter
President and President of Allstate Insurance Company

Jay, it's Matt. Well, we don't like a 9.8% combined ratio impact, but it could've been a lot worse. We spent a tremendous amount of time working on PML optimization, PML, Probable Maximum Loss work and risk concentration work, to try to spread out and diversify our risk. We use our economic capital model in a fairly sophisticated manner to ensure we are earning appropriate returns based upon the risks in those specific geographies. So that when something like this happens, we feel okay about it and we can focus where we should be focused, which is on serving our customers and helping restore them back to normal. I would point out, unfortunately, in an organization like Encompass, which doesn't have the scale benefits and as a result, the diversification benefits, the hailstorm and the catastrophe in March had a greater impact on -- proportional impact on Encompass than it did on Allstate brand, despite the fact that we've done great work there over the last several years to reduce the risk concentration. But nevertheless, when you have a smaller business like that, it's just not as diversified, which is why we have a two-part program going on right now in Encompass, which is to retrench from those states in which we're not earning an appropriate return and grow in other states where we believe that we can earn it in appropriate return, and therefore, diversify our risk. Within the Allstate brand, we do, as I say, lots of offsetting work and offsetting trades. It's interesting that you can add some homes on Long Island and therefore be able to grow a little bit in Harris County. You've seeing announcements that we're doing limited selective homeowners writing again in California and Florida, and that's because our diversification work and PML work has been successful. And we feel that those additional added items will actually be helpful to our diversification, and not pose undue risk.

Thomas J. Wilson
Chairman & CEO

Okay. We're looking forward -- we're going to stay focused on those 5 operating points for 2017, make sure we're balancing the short term and the long term in a way that enables us to create value for our customers, our shareholders and all of our stakeholders. So thank you. We'll talk to you next quarter.

Operator
Thank you, ladies and gentlemen, for your participation in today's conference. This does conclude the program. You may now disconnect. Good day.