The Hartford Financial Services Group, Inc. NYSE:HIG

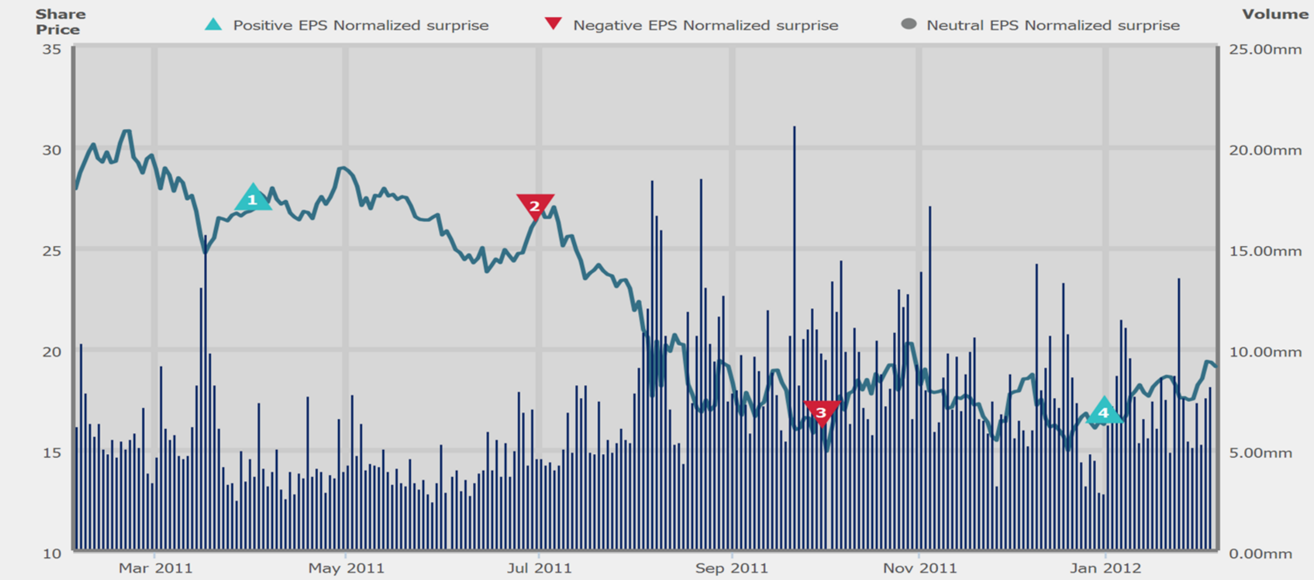
FQ1 2012 Earnings Call Transcripts

Thursday, May 03, 2012 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2012-			-FQ2 2012-	-FY 2012-	-FY 2013-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.06	1.25	▲17.92	0.78	3.64	3.95
Revenue (mm)	5385.92	7661.00	▲42.24	5529.21	22635.14	22137.81

Currency: USD
Consensus as of May-03-2012 11:41 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2011	0.95	1.16	▲1 22.11 %
FQ2 2011	0.01	0.00	▼2 (100.00 %)
FQ3 2011	0.25	0.05	▼3 (80.00 %)

FQ4 2011	0.62	0.69	▲11.29 %

Call Participants

EXECUTIVES

Christopher John Swift
Chairman & CEO

David N. Levenson
Former Executive Vice President and President of Wealth Management

Douglas G. Elliot
President

Liam E. McGee
Former Chairman

Sabra R. Purtill
Senior Vice President of Investor Relations

ANALYSTS

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John Matthew Nadel
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Presentation

Operator

Good morning. My name is Nicole, and I will be your conference operator today. At this time, I would like to welcome everyone to the Hartford First Quarter 2012 Earnings Conference Call. [Operator Instructions] I would now like to turn the conference over to Sabra Purtill, Head of Investor Relations. You may begin your conference.

Sabra R. Purtill
Senior Vice President of Investor Relations

Thank you. Good morning, and welcome to The Hartford's First Quarter 2012 Conference Call. Our speakers today are Liam McGee, The Hartford's Chairman, President and CEO; and Chris Swift, our CFO. Other members of our senior management team here today include Doug Elliot, Alan Kreczko, Dave Levenson, Andy Napoli, Bob Rupp and Hugh Whelan. After Liam and Chris' presentation, we will have time for questions.

Please note that as discussed on Page 2 of the presentation, any statements made today concerning The Hartford's future results or actions should be considered forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements are not guarantees of future performance, and actual results may differ materially from these statements. We assume no obligation to update the forward-looking statements.

You should also consider the important risks and uncertainties that may cause results to differ, including those discussed in our press release, our first quarter 10-Q, our 2011 10-K and other filings we make with the SEC. These documents are available in the Investor Information section of The Hartford's website.

I also need to mention that our presentation today includes some financial measures that are not derived from generally accepted accounting principles. Definitions and reconciliations to these measures -- of these measures to the most directly comparable GAAP measures are provided in our financial supplement, press release and 10-Q. I'll now turn the call over to Liam.

Liam E. McGee
Former Chairman

Thank you, Sabra. Good morning, everyone, and thank you for joining us today. Yesterday, we announced strong first quarter results, with core earnings up 11% to $1.25 per diluted share. Our P&C combined ratio was 95.7%, a very good result. Strong pricing momentum continued in the P&C Commercial segment, and we had significantly improved new business growth in Consumer Markets.

We also achieved several significant accomplishments. We concluded the strategic evaluation of the businesses and announced our plan to focus on the Property & Casualty, Group Benefits and Mutual Funds businesses. This is The Hartford's best path forward to deliver greater value for shareholders. So in order to increase transparency on our go-forward businesses, we expanded P&C disclosures this quarter, providing more details on Small Commercial, Middle Market and Consumer Markets. Going forward, our presentations will focus on greater detail on the performance about our go-forward businesses and the progress in reducing the size and amount of risk in the Runoff division. We are moving quickly to execute the plan we outlined in March, including selling businesses, placing the annuity block into Runoff and exploring options for the Runoff division. Let me update you briefly on each of these.

The sales processes for Individual Life, Retirement Plans and Woodbury Financial are going well. The offering memoranda for each are in the marketplace. There is great interest in each property. We expect to have a competitive auction process, and we expect definitive agreements later this year. I am proud of the hard work and dedication of the employees in these businesses. They are focused on delivering successful and valuable businesses to the ultimate buyers. The proceeds from these sales will give us additional financial flexibility that, over time, we expect to use for capital management actions and some debt reduction. We will also consider options for reducing risk in the Runoff businesses or reinvesting in our go-forward businesses.

In addition, last week, we announced an agreement to sell the Individual Annuity new business capabilities. This sale does not change our decision to put the in-force block into Runoff, nor does it have a material financial impact on The Hartford. However, it does provide an opportunity for us to place our innovative products, strong distribution capabilities and talented employees with an organization committed to the annuity space. We are also working hard on initiatives to further reduce the size and risk of the Life runoff segment, which will shrink over time through policyholder lapses. While our ultimate goal is to isolate or separate the annuity block from our go-forward businesses, the management team is currently concentrating on transactional and operational opportunities for individual books of business.

With respect to transactions, we are exploring a wide range of potential opportunities, including sales, reinsurance and other structural concepts. A variety of parties have expressed initial interest in parts of the block. Of course, any transactions will need to balance short-term economics with the long-term objective of reducing liabilities, which would allow us to redeploy some of the capital currently allocated to the Runoff block. It's still early, but we do expect some of these potential opportunities to materialize over time, particularly as the capital markets continue to stabilize.

On the operational side, we are pursuing options such as outsourcing or different fund options that will reduce risk or expenses. And of course, we anticipate achieving expense reductions of $100 million before tax in 2013 by placing Individual Annuity segment into Runoff.

In April, we also refinanced the Allianz debt and repurchased their warrants. The refinancing strengthens our balance sheet by reducing long-term interest costs and improving financial flexibility by extending the debt maturity schedule. The warrant repurchase eliminates a material source of future dilution. Allianz remains a major shareholder of The Hartford, and we appreciate their support.

We are already beginning to execute on our strategy. By focusing on the Property & Casualty, Group Benefits and Mutual Fund businesses, we will, over time, deliver sustained superior returns and greater shareholder value. In order to achieve these objectives, we are focused on 3 key goals: first, improving margins and ROEs in our go-forward businesses; second, strengthening overall capital generation; and third, reducing the volatility of our earnings and capital. So let me go through each of these in a little more detail.

Our go-forward businesses have strong ROEs, although there is room for improvement. Combined, we expect them to achieve a 12% to 13% ROE for 2012, and we are hard at work to improve this in 2013 and beyond. To achieve this, we're concentrating on improving margins in Middle Market and Group Benefits and growing the top line in Small Commercial and Mutual Funds.

In the P&C Commercial segment, our Small Commercial business is a long-standing market leader, with good opportunities for continued profitable growth, particularly as the U.S. economy and small business formation recover. Written premiums were up 8% this quarter with a 91.8% combined ratio. We continue to be a preferred company for small business customers, driven by our long-term record of innovation, ranging from product to technology to service capabilities.

In Middle Market, Doug Elliot and his team are improving product diversification and pricing, particularly in workers' compensation. I'm especially pleased with the pricing and margin improvements we've achieved over the past 6 months, although that has meant giving up some top line growth. Middle Market's combined ratio, x cats, in prior year was 99.2%, down from last year but still above what we need to achieve acceptable returns. In the first quarter, retention remained strong despite price increases of approximately 10% for the total Middle Market book.

In Group Benefits, we achieved good rate increases on the first quarter renewals, but earnings are well below the segment's potential. The incidence in termination trends we are seeing are consistent with our competitors and largely due to the high unemployment rate, but we need to do better. With the new Group Benefits management in place, we have initiatives underway in sales, pricing, underwriting and claims. It will take time before the financial benefit of this work falls to the bottom line, particularly on pricing, given the 3-year contract terms in this business. Nevertheless, we like the mortality and morbidity underwriting margins of this business, as well as its long-term growth and return prospects. We have a strong franchise with a top-tier market position and excellent sales and distribution capabilities. With the success of our initiatives and some lift from an improving economy and unemployment trends, we believe that Group Benefits will once again achieve sustained superior returns.

The principal goal for Consumer Markets has been to improve margins, and Andy Napoli and his team have made great progress. The current year combined ratio, x cats, is improving year-over-year for 4 of the last 5 quarters, and we are increasing rates in homeowners to reflect high-cat and non-cat weather experience. With better margins, Consumer Markets is now striving for top line growth through both increasing retention and new business growth. We're doing well in both of these metrics. Retention has improved as a result of customer outreach and pricing initiatives, while new business levels have improved strongly. New business growth was favorable for the third quarter in a row and has now returned to acceptable levels. This success was due to improved response and conversion rates, as well as to our award-winning customer service. This week, J.D. Power and Associates announced that The Hartford was ranked highest in customer satisfaction with the auto insurance shopping experience, an important accomplishment for our Consumer Markets team and for our customers.

In Mutual Funds, we are confident that going forward, we are well positioned to generate good growth in this high-return business. We are moving quickly to leverage our expanded relationship with Wellington. We want to transition all of the fixed income investment management to Wellington by the end of June, and we expect that the second half of the year will produce significant improvement in net flows.

Improving margins and ROEs also requires us to remain focused on continued expense efficiency across the entire organization. After reducing expenses by $150 million in 2011, we took out another $30 million in the first quarter. We are continuing to execute on the efficiency objectives we established last year. In addition, we recently established a dedicated business transformation process to ensure that we remove all costs associated with the 3 businesses being sold and that corporate overhead and other shared service expenses are rightsized for the go-forward Hartford businesses.

Our second goal for creating sustained superior performance is improving capital generation. Our go-forward businesses have historically been strong capital generators, but the Runoff businesses and Individual Life and Retirement Plans have not. As a result, our Life statutory capital generation has been constrained over the past several years. Statutory capital requirements in the Life company should decline over time, with the sale of the 3 Life businesses and the reduction of the Runoff book through lapses or management actions. The statutory earnings power of the P&C, Group Benefits and Mutual Funds businesses will grow in the future. Combined, we expect our total capital generation going forward to be stronger than what it has been in the last few years.

Finally, a third goal is to significantly reduce the sensitivity of our capital and earnings to financial markets risks. Our go-forward businesses are less sensitive to changes in the capital markets. Of course, we're focused on reducing the size of the variable annuity block, which is the primary source of our current market volatility. Some of this will occur naturally over time through policyholder lapses and withdrawals. But in addition, we will be prepared to take advantage of potential opportunities to isolate or separate the Runoff block that are both feasible from a regulatory perspective and create shareholder value. Through these efforts, we will ultimately free up capital from our divestitures and Runoff businesses, and we will be able to redeploy in our go-forward businesses and return to shareholders. And over time, The Hartford's financial profile will evolve into more of a property and casualty company, with strong returns and capital generation and limited sensitivity to capital market volatility.

This was a strong quarter for The Hartford. We had good financial results, favorable momentum in many of our go-forward businesses and have successful debt refinancing and warrant repurchase. The sales processes are going well, and with our sharper strategic focus, I am confident that we are on the right path to generate sustained superior returns and create greater shareholder value going forward. I and the rest of the team are very optimistic and excited about our future.

I'll now turn the call over to Chris.

Christopher John Swift
Chairman & CEO

Thank you, Liam. Good morning, everyone. I'll begin on Slide 5. First quarter core earnings were $612 million or $1.25 per diluted share, representing an 11% improvement over prior year. Excluding the $192 million DAC unlock, core earnings were $420 million or $0.86 per diluted share, so it's a 7% increase compared to prior year. These results were largely in line with the estimate we provided on March 21, except for catastrophes. Cats were running about $20 million favorable to budget through mid-March. But with the late March storm activity, total cats ended the quarter at $46 million after tax, in line with our budget. Prior-year development was slightly favorable at $19 million after tax, with releases in personal lines offset by some modest development in P&C Commercial.

The investment portfolio yield was stable this quarter at 4.2%, excluding partnerships. We are modestly increasing allocations to higher-yield assets and purchasing longer-duration bonds. Returns on alternatives and limited partnerships were 8%, and we continue to expect an annualized return of 9% for 2012. Impairments and changes to the mortgage loan loss reserve remained low at $28 million pretax in the quarter.

Slide 6 shows book value per diluted common share on a restated basis for the new DAC accounting standard. At the end of the first quarter, book value per diluted share was $43.25, an increase of 12% over last year. Excluding AOCI, book value per diluted share rose by 1% to $40.55.

Let's turn to our business results by segment. Slide 7 shows the summary results for P&C Commercial. Core earnings were $162 million, a decline of 8% from prior year. Results included $13 million, after tax, of prior-year net reserve strengthening across multiple lines. Importantly, there were no meaningful reserve adjustments related to our workers' compensation loss experience. The combined ratio, x cat, x prior year, was 96.4%. We expect this to improve as written price increases earn in over the remainder of 2012.

We continue to see strong price momentum in P&C Commercial. In the first quarter, we achieved renewal price increases of 7%, the highest level since the fourth quarter of 2003. We're especially pleased with renewal price trends in Middle Market workers' compensation, where first quarter price increases were up 14%. Policy count retention remained strong at 83% for standard commercial. This metric is clearly influenced by the large number of Small Commercial policies. If you look at retention on a premium weighted basis, over the past year, Small Commercial retention has been flat, while Middle Market retention has declined. This retention decline has been more than offset by improved pricing. We are very pleased with this trade-off as this will lead to continued margin expansion and ROE improvement.

Shifting to Group Benefits, core earnings of $5 million remain well below our expectations. The loss ratio of 83% reflected elevated disability incidence and the lack of improvement in termination trends. We're addressing these disappointing results in 2 ways. First, we continue to take rate actions on accounts that are not meeting profitability targets. As Liam mentioned, it will take some time to get the profitability of the book to targeted levels, given the multiyear nature of the rate guarantees. Given our rate actions and the very competitive marketplace, persistency declined in the first quarter -- on first quarter renewals to 66% from 72% in the prior year. Ongoing sales are down 7%, primarily driven by a 21% decline in group disability sales. Group life sales increased 5% from the prior year.

Second, we are reviewing all operational processes to identify ways to improve profitability. We recently appointed a new leader for this segment, Mike Concannon. Mike's property and casualty background brings a fresh perspective for potential improvement opportunities in many operational areas, like underwriting, pricing and claims management.

Turning to Slide 9, Consumer Markets reported first quarter core earnings of $102 million, down $9 million from prior year. Andy Napoli and his team are successfully executing on the strategy for this business. The combined ratio and retention improved, and new business production was strong. First quarter combined ratio, excluding cats and prior-year development, was 88.8%, a slight improvement from last year's 89.0%. We continue to manage our rate increases appropriately, with a 6% renewal written price increase in homeowners and 4% in auto. Like the rest of the personal lines industry, our homeowners book requires additional rate and underwriting actions to respond to recent weather trends. Overall retention was up 2 points to 84% in auto and 85% in homeowners. While we are pleased with the improvement, we still need another point or 2 in order to reach our targeted levels. New business written premium was up 30% in auto and 32% in home. After declining in the first half of 2011, new business premiums are now back to historic levels. Most of the new business growth is coming from our more profitable channels. For example, written premiums in AARP Agency almost doubled to $27 million from the prior year. We provided additional granularity in our financial supplement on written and earned and premiums by channel, so you can track our progress.

We're encouraged by these positive results. With improving margins, Consumer Markets is now poised to profitably grow while also improving their ROEs.

Wealth Management results are summarized in Slide 10. First quarter core earnings, x DAC unlock, were $154 million, 15% lower than prior year. This decrease was largely due to a 7% decline in assets under management primarily from net outflows in Individual Annuities. Individual Annuity core earnings, x DAC unlock, were $96 million, down 11% from prior year. This segment will be reported in the Runoff division next quarter.

The first quarter annualized lapse rate for the U.S. in-force VA block was about 14%, in line with our expectations. Since our announcement to exit the Individual Annuity businesses, lapses have increased approximately 20% in the U.S. and 4% in Japan. It's too soon to judge whether lapses will remain at these levels, but if they do, it will accelerate the runoff of the VA book.

Core earnings in Individual Life, x DAC unlock, were $34 million, a decline of $4 million from prior year due to lower alternative investment returns, as well as slightly higher expenses. Individual Life sales were up 13% over prior year and increased across all key distribution channels.

In the individual Retirement Plans, core earnings were $4 million, down $5 million from the prior year. Spread compression on the general account products continues to weigh on results. Assets under management had a record $57.2 billion, aided by rising equity markets and positive net flows.

As a result of our planned sales, we have evaluated the goodwill balances for Individual Life and Retirement Plans in the first quarter. No impairment is necessary at this time. However, we will continue to monitor its recoverability.

Moving to Mutual Funds, core earnings were $20 million, down $7 million from prior year due to lower assets under management. First quarter fund performance improved, particularly in our largest fund, Capital Appreciation Fund. Overall, more than 80% of the funds outperformed their benchmarks. This strong quarterly performance contributed to an increase in non-proprietary fund deposits of 18% on a sequential basis.

The results of our Runoff division are on Slide 11. Core earnings, x DAC unlock, were $105 million, basically in line with prior year. As Liam discussed, we have a number of initiatives underway to shrink the size and risk of this book. This will allow us to redeploy the capital allocated to this business over time. As you know, rising equity markets, higher interest rates and a weakening yen are all positives for our in-force VA book. The economic value of the VA book is greatly improved as a result of these market conditions. During the quarter, the net amount at risk related to our VA book declined substantially. For example, the NAR related to the U.S. and Japan GMDB business improved $5.3 billion during the quarter. This improvement isn't always evident in our GAAP and statutory accounting results, given the mismatch between the carrying value of the hedge assets and the VA reserves.

As you can see on Slide 12, that on a GAAP basis, the net change in VA reserves and hedge assets generated a loss of approximately $1.1 billion, which reflects the asymmetrical accounting for our U.S. GMDB and Japan guarantees. On a statutory basis, the decline in the value of the hedge assets exceeded the change in the value of the U.S. VACARVM reserves by $183 million.

It's important to note that our hedge program continues to work as designed. Its primary focus is economic risk, not GAAP accounting results. As the markets change, we will adjust our targets in order to maintain appropriate hedging levels.

On Slide 13 is our statutory surplus roll-forward. U.S. statutory surplus increased approximately $600 million in the first quarter before dividends. Consistent with our practice, a $200 million dividend was declared from the P&C to the holding company in order to cover interest, dividends and other expenses. The P&C operations generated more than $300 million of statutory operating income and almost $200 million of other positive surplus impacts, including investment-related gains. Life statutory operating income, excluding VA, turned positive this quarter and was approximately $100 million. This was largely offset by the VA hedge-related impacts I mentioned earlier. In total, the Life operations ended the quarter with a modest increase in statutory surplus.

As you can see on Slide 14, we ended the quarter with $17.9 billion of capital resources. Holding company resources declined almost $100 million in the quarter, reflecting dividends, interests and share repurchase activity. We expect holding company resources to decline modestly in the second quarter due to this element of the warrant repurchase.

Turning to Slide 15, we were very pleased to complete the Allianz transactions, which were a major step in restructuring the balance sheet and enhancing our financial flexibility. On April 17, we repaid $1.75 billion par value of Allianz junior subordinated debt with the proceeds from the issuance of $1.55 billion of senior notes and $600 million of new junior subordinated debt. This new debt has a blended interest rate of approximately 6% versus the 10% coupon on the Allianz debt. This reduces annual interest paid by $45 million on a pretax basis. As a result, our statutory dividend coverage ratio is improved by almost 0.5 point to 4x.

In the second quarter, we will take an after-tax charge to net income of approximately $600 million to reflect the premium paid to retire the debt and to write off the related unamortized discount and debt costs. We also purchased all the outstanding Allianz warrants for $300 million. This transaction reduced first quarter book value by $0.61 per diluted share.

In addition, early in the first quarter, we purchased 2.6 million shares of common stock. To date, we have completed $394 million of the $500 million equity repurchase authorization. We intend to complete the remaining $106 million on a timely basis, taking into consideration market conditions and trading restrictions.

Turning to Slide 16, I wanted to conclude with our outlook for the second quarter. We expect second quarter run rate core earnings to be in a similar range to the first quarter, absent higher loss cost seasonality. In the second quarter, we expect higher cats with a budget of $84 million after tax, which is $0.08 per diluted share, higher than the first quarter, which brings our total estimate to $0.70 to $0.75 per diluted share. This estimate does not include DAC unlocks, prior-year reserve development, restructuring charges related to the Wealth Management division. These restructuring charges, which include retention awards and other expenses, may be up to $20 million or about $0.04 per share.

Our businesses this quarter performed largely in line with our expectations, with the exception of Group Benefits. We currently expect full year earnings for Group Benefits to be essentially flat with 2011. We expect pricing momentum in the P&C businesses will expand margins in the second half of 2012. Our earnings outlook for Individual Life and Retirement Plans businesses hasn't changed, although we expect sales to be down as a result of our recent announcements.

Looking forward, the ongoing businesses are executing under 2012 initiatives to grow and increase margins. We look forward to sharing progress with you, and we will provide more information about the P&C, Group Benefits and Mutual Fund operations in the quarters to come. In addition, we'll keep you updated on the other operational and strategic actions we may take within our Runoff division. The strength and momentum in our ongoing businesses, combined with the actions we are taking to be a more focused company, will improve the earnings and the ROE profile of The Hartford over time.

At this point, I'd like to turn the call over to Sabra to begin the Q&A session.

Sabra R. Purtill
Senior Vice President of Investor Relations

Thank you, Chris. We'll now open the call for questions. [Operator Instructions]

In addition, I just wanted to make one slight clarification of Chris' comments referring to the Individual Annuity business. Since our announcement to exit the Individual Annuity business, lapses have increased to approximately 20% in the U.S. and 4% in Japan on an annualized basis. Nicole, can you please give the instructions for asking a question?

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Mark Finkelstein with Evercore Partners.

A. Mark Finkelstein
Evercore ISI, Research Division

Liam, in your opening remarks, you talked constructively about some alternatives on the VA side, whether it's reinsurance or what have you. Can you expand on those comments? And I guess what I'm interested in is, how would you weigh the probability of success and how meaningful could one of these structures be in terms of capital release?

Liam E. McGee
Former Chairman

Well, Mark, it's early, and what I expressed was we have received interest from a variety of parties on different parts of the book and different parts of the block. Our team is working hard evaluating those options, and we do think some of them will materialize over time. But I think it's also important, as I said in my comments as well, Mark, that we'll balance the short-term economics with the ultimate goal of getting them off our books. So it's early in the process. I think we're constructively optimistic with the level of interest that's being presented, the kind of thinking that our teammates are doing on it, with the assistance of advisors in some cases, that some of these transactions will materialize over time.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay. I guess my follow-up will just be on the Annuity business as well. I guess we've seen markets go higher, a little bit of interest rate volatility, but I guess what is the opportunity to kind of restrike some of the options and reduce that cost at this stage? Is that a -- do we need markets to go higher from here, or is there opportunity to kind of reduce that long-term cost at this stage?

Liam E. McGee
Former Chairman

That's a great question. And I'll make a comment, and I know Chris would like to add something as well. As Chris said in his remarks, we are looking at the hedges. We refer to them as a dynamic hedging program, particularly in Japan. So with the markets having appreciated as they have, particularly equity markets, and although it's backed up a little bit, the yen weakening, offset by lower interest rates, I would tell you we evaluate our hedging levels on a daily basis, led by our HIMCO teammates and our Chief Risk Officer, Bob Rupp, now in conjunction with our Runoff group. So we look at it every single day. And there may be opportunities because of strengthening market levels to reduce it. And Chris, other things you might say?

Christopher John Swift
Chairman & CEO

I think it's exactly right. Mark, we're very sensitive on the economic cost side. So particularly, as markets reach 1,400, 1,450 on the S&P and beyond, there are definitely opportunities to be much more cost-effective. So I think you should take away that we're working hard to appropriately balance risk and economics, like we have always said.

Operator

Your next question comes from the line of John Nadel with Sterne Agee.

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

I have a question on the VA business as well. In the U.S., in particular, but in Japan as well, your net amount at risk and the in-the-moneyness, if I focus on the living benefit guarantees, came down very nicely quarter-over-quarter. My question is for the U.S., can you give us a guesstimate on about how much higher do you think markets need to move for that level of in-the-moneyness to essentially be wiped out or moved to 0?

Christopher John Swift
Chairman & CEO

John, thanks for the question. In the U.S., if you look at sort of the cohorts of when we put a lot of business on the books '05, '06, '07, '08, we were approaching that level just by the nature of the disclosure that we made. So to me, when you get into the 1,400, 1,500 levels, 1,500, I think you'd be virtually at breakeven from the moneyness perspective.

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

Okay. And then on the Japan side, I assume -- is that going to be -- should we be looking more at that being influenced more by the yen than necessarily market levels?

Christopher John Swift
Chairman & CEO

Yes, I've always said about 50% of sort of just the risk comes from yen-dollar, yen-euro.

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

Got it. Okay. And then just a separate question is -- I'm interested in the move up that you mentioned in the annualized surrender rate on the U.S. VA book. Obviously, one month doesn't necessarily make a trend. But I was wondering if you have any granularity on the composition of that higher surrender rate. Specifically, what proportion of those lapses reflected contracts where the living benefit guarantee was in the money? Has that changed? I think historically, you've mentioned around 40% of lapses were in the money.

David N. Levenson
Former Executive Vice President and President of Wealth Management

So John, it's Dave Levenson. So for April, as you know, we've been -- we were running at 20% annualized lapse rate. As we look at the weekly numbers, that has been pretty consistent. So we've seen it maybe moderate slightly. I think over time, we'll have a much better read on that. As far as lapses in the money versus out of the money, your 40% to 50% number is right on.

Operator

Your next question comes from the line of Andrew Kligerman with UBS.

Andrew Kligerman
UBS Investment Bank, Research Division

First question, just around the group guidance had been for a benefits ratio of around 77%, 80%. Of course, you came in at about 83%, and I know the pricing takes time. So what should we be thinking about in terms of the guidance going forward? And then the second question would be around the -- with all the restructuring and changes going on, some people have suggested that maybe it might not be a bad idea to IPO part of the P&C business, maybe a minority interest, 15%, 20%. Is that something you've thought about? Would that make some sense?

Douglas G. Elliot
President

Andrew, let me -- this is Doug. Let me take the second part of the question on the Group Benefit. Number one, there are macroeconomic headwinds across that business. But we are encouraged, and I think there are some reasons for optimism across our Group Benefit business as we work our way through Q1 into Q2. Clearly, our incidence level look like they're flattening. We look like we, on the long-term side, have some flattening signals over the past 5 quarters. In the short-term area, it looks like we've got some improvement on our incident trends, so that's a positive. Clearly, as we've talked in the past, our terminations are down and running lower than our historical run rate. We are working all the levers available to us. We have additional disclosure for the quarter in there. We achieved 4 points of rate increase, which is why we were slightly down in retention, but I think that's a good trade. And our overall price improvement in the book for the first quarter was about 10%. So I feel like we're making significant strides toward improving our margin, and overall, I'm also encouraged by what I would say is an improving pricing climate in disability.

Christopher John Swift
Chairman & CEO

Hey, Andrew, it's Chris. I think you...

Andrew Kligerman
UBS Investment Bank, Research Division

One quick second, Doug, though. So therefore, you think you could achieve guidance for the year or the original guidance?

Douglas G. Elliot
President

I think Chris gave you the adjusted guidance.

Andrew Kligerman
UBS Investment Bank, Research Division

I'm sorry, I missed that.

Christopher John Swift
Chairman & CEO

Yes, Andrew, what I was trying to be clear in my prepared remarks is that we really see group now just basically flat to prior year. When we were with you in December, we saw group hopefully improving earnings 15%, 16%, 17%, high teens. I would consider that business now just sort of flat with prior year.

Andrew Kligerman
UBS Investment Bank, Research Division

Got it.

Liam E. McGee
Former Chairman

Andrew, this is Liam. And as far as your question about possible other structures for the company, I'll just remind you what I've said consistently that management and the board, since the middle of last year, looked comprehensively at virtually every alternative. We've chosen a path, and that's the path we're going to execute against.

Operator

Your next question comes from the line of Tom Gallagher with Crédit Suisse.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Liam, you had talked about the sales process going well. Can you just give a little bit of color on that? Because in my mind, the greatest risk here is while there may be buyers lined up, if the bid is 50% of book value or some very low amount, then it may be a decision of deciding not to sell some of the properties that you've put up for sale. But your comments certainly seem to indicate that you're comfortable with the way things are progressing. So maybe you can talk a little bit about just the process and whether you've gotten any price indications yet and whether you're comfortable with those.

Liam E. McGee
Former Chairman

Well, Tom, we are confident that we will sell the businesses at an appropriate value. You can appreciate where we are in the process with just the process itself that -- I'm not going to get into too much detail. But I think based on the volume of parties that are interested in each of the 3 properties, both objective and subjective feedback that we're getting from the market, we feel pretty confident we're going to sell these businesses and have definitive agreements certainly in the latter part of this year.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Okay, that's helpful. And then just one follow-up. I guess it would be for Chris. When you guys talk about potentially freeing up capital from the closed block, should we think about it being a normal process, where you first need to sell these businesses and then the proceeds would give you more flexibility to consider solutions? So in other words, should we think about the freeing up of capital being a 2013 or 2014 event? Can you help a little bit about tying those 2 things together?

Liam E. McGee
Former Chairman

Well, Tom, let me just make a high level comment first, and I know Chris is anxious to give his own perspective as well. When you look at the actions that we're taking, first of all, we will not be selling new life products, which, in general, have been capital-consumptive; secondly, selling the businesses, which will create proceeds and subsequently, some capital release as well from those businesses. The natural lapsing -- and if the elevated lapse rates continues, so the better. And then any actions that were effective in our runoff business -- this is a company that, over the next couple of years, should liberate capital. We're more confident in the strength of our balance sheet, and to be more specific than that, now would be premature obviously. There's timing, market levels, et cetera, but I think we position the company as we execute effectively, and we're focused on -- laser-focused on execution, on the things that we've described. And over time, we will liberate capital, and we'll have a variety of choices as what to do with it. And of course, our primary guiding principle will be to the benefit of the shareholder. Chris?

Christopher John Swift
Chairman & CEO

I think that you're right on. There's nothing other to add, Tom, other than, again, if you look at sort of the sequence of events and timing in different constituencies that we want to bring along with our plans, whether it be regulators, agencies, and how we would use, I'll call it, the incremental value that we monetize and the capital that's backing those blocks, we know how to work with those constituencies to bring them along, to make sure everyone understands what they're trying to accomplish and what we're going to do with that deployable capital at the time. But as Liam said, we'd rather not just speculate right now on size, timing and amounts just given that there's a lot of variables outside of our control right now. But I think my view is we're going to have a good competitive option on these properties.

Liam E. McGee
Former Chairman

Certainly, Tom, we have certainty and clarity about our direction. And along with creating superior financial performance, a big part of generating superior shareholder performance will be over the next periods of time, and we have very specific actions. We've articulated them, I think, very clearly. We need to execute on them. We understand very clearly that, over time, those activities will result in capital that we'll be able to deploy in, as Chris says, appropriately, in consultation with our normal constituents, which I think we've demonstrated our ability to effectively do in the steps we've taken in the past couple of years. I think this is a company that will definitely do that, and I think we've made the decisions to position us to do that.

Operator

Your next question comes from the line of John Hall with Wells Fargo Securities.

John Arthur Hall
Wells Fargo Securities, LLC, Research Division

I have 2 questions around capital. And not to be repetitive here, on the VA book of business, I think initially, when you talked about it potentially being put into Runoff, you didn't see capital being freed up. Lapse rates are substantially higher now. Does that change the view there about the speed of capital return from that book?

Liam E. McGee
Former Chairman

Chris will give you an answer on that, John.

Christopher John Swift
Chairman & CEO

John, directionally, yes. I think we view net lapses as positive from a capital side. As long as they're balanced and steady, net-net, it's positive because we just have to hold less capital against the liabilities, particularly in stress scenarios.

John Arthur Hall
Wells Fargo Securities, LLC, Research Division

Great. And then my second question has to do with the Mutual Fund operation and I guess where it's held within the enterprise. Being owned by a life insurance company, I guess, constrains your ability to use the cash that it generates. In everything that you're doing about moving things around and the like, are you considering trying to transfer the ownership out from the life company to a holding company that wouldn't be insurance regulatory-constrained?

Christopher John Swift
Chairman & CEO

John, I think that one of our work streams that we have is just the, we called it, legal entity simplification process, and that's part of it. But I wouldn't view it necessarily as a constraint. It's more potentially simplifying sort of a holding company structure. But just because Mutual Funds is owned by a life group right now, I wouldn't have you necessarily think of any extraordinary restraints or conditions on that entity, its use of proceeds and cash flows that we would generate from it. But we are looking at just the overall simplification of the legal entity structure.

Liam E. McGee
Former Chairman

Yes, I agree with, John, with everything Chris said, particularly as it relates to Mutual Fund business. But I'd reiterate we will simplify the legal structure of the company, and that body of work is underway. If it has such a benefit, so be it. But we're really trying to simplify the company and its legal structure.

Operator

Our next question comes from the line of Vincent DeAugustino with Stifel, Nicolaus.

Vincent M. DeAugustino
Stifel, Nicolaus & Company, Incorporated, Research Division

Just 2 quick questions. On commercial auto, it looked like there was some adverse development that ran a little bit higher than recent quarter's trends. I was just curious of your thoughts on, I guess, what you're seeing is driving that and then specifically, if there's any particular accident years that, that's flowing from?

Douglas G. Elliot
President

Vincent, this is Doug. I would characterize the $12 million as rather insignificant against the entire period. A little bit of pressure with the last couple accident years, '09, '10, '11, primarily '11, and primarily in Small Commercial. So there's nothing there that I think is systemic. I think we're all over the issues.

Vincent M. DeAugustino
Stifel, Nicolaus & Company, Incorporated, Research Division

Okay, great. And then just a real quick follow-up. Since reporting your strategic restructuring plans, were there any segments that are maybe facing incremental headwinds as a result of the changes you're putting in place? Or is everything outside of the units potentially up for sale going as planned and no kind of cross headwinds there?

Liam E. McGee
Former Chairman

No, not at all. I think as our results indicated, Vincent, our Property & Casualty businesses are really performing very well, top line growth in Small Commercial and in Consumer and after margin improvement in Consumer. I think Doug and his team,, as you saw in the pricing actions, are making the right trade-off between getting price and the persistency rate there. Obviously, like everyone else in the industry, there are some challenges in Group Benefits, but that has nothing to do with our announcements. And finally, I think Mutual Funds, we could not be more excited about the prospects of that. And the feedback we get from the distributors is they're pretty excited about it, too. The unique combination of The Hartford and the Wellington's sub-advisory, cross-equity and fixed income is really, really creating, I think, a very positive reception. So I'd say if anything, other than just the systemic and macroeconomic issues around Group Benefits, the go-forward businesses are firing at all cylinders.

Operator

Your next question comes from the line of Jeff Schuman with KBW.

Jeffrey R. Schuman
Keefe, Bruyette, & Woods, Inc., Research Division

A kind of a mundane question but a necessary one, I guess. With all of the unusual levels of corporate activity, it seemed like corporate expenses were a little higher this quarter. Can you give us a sense of kind of where those expenses might go directionally from here?

Liam E. McGee
Former Chairman

Down.

Christopher John Swift
Chairman & CEO

Jeff, it's Chris. I would tend to think in terms of the corporate level of expenses, this quarter is maybe $15 million to $20 million higher than sort of the normalized run rate. We had some just accrual adjustments coming out of year end and a little bit of restructuring charges. I think going forward, we plan to break that out as clear as possible as far as restructuring expenses, whether it be severance benefits, whether it be stay bonuses, things along those lines. But I think from a model perspective, you ought to think this quarter is $15 million to $20 million higher than a normal run rate.

Liam E. McGee

Former Chairman

Yes, and Jeff, my one-word answer was meant to convey this management team's determination to run this company in, I think, a financial services environment that requires it as efficiently as possible. As I said in my remarks, and I want our investors to understand it, about The Hartford management team, there was $150 million of efficiencies realized last year, $30 million in the first quarter. We're going to stay focused on the efficiency and process improvement actions through the balance of 2012. Obviously, we will get the expenses as we sell the businesses. All expenses, whether they're solid or dotted line, are going to come out. And then we think we have a very unique opportunity, truly a once-in-a-lifetime opportunity, for the go-forward business to really reinvent how we do things at The Hartford and better and more efficient. So you'll hear more consistently more from us on our process improvement and efficiency. And I think we've demonstrated our ability to do that on the old construct of The Hartford. We'll continue that and even with greater urgency because we do believe we have a unique opportunity here.

Sabra R. Purtill
Senior Vice President of Investor Relations

Thank you. Thank you all for joining us this morning. We know it's a busy morning with a lot of conference calls being held. So as always, we appreciate your interest and support of The Hartford. And for any follow-up questions, we're available today and tomorrow to take them. Thanks.

Operator
Thank you for participating in today's conference call. You may now disconnect.