S&P Global
Market Intelligence

The Hanover Insurance Group, Inc. NYSE:THG

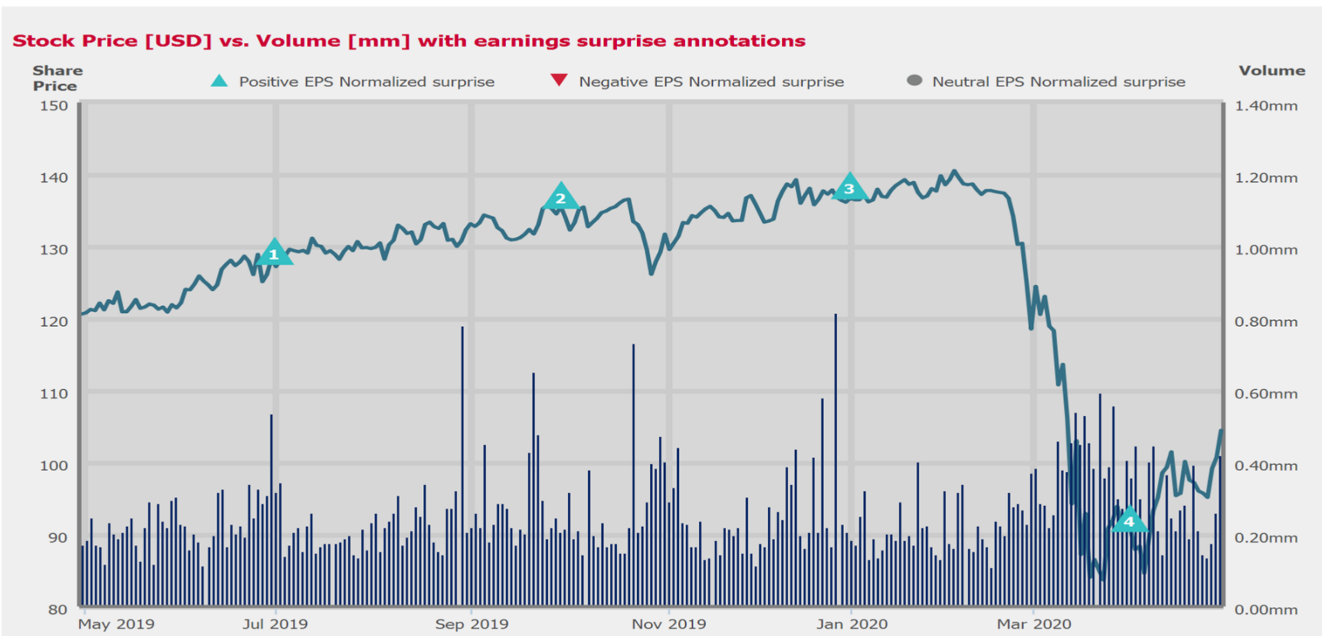
FQ1 2020 Earnings Call Transcripts

Wednesday, April 29, 2020 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2020-			-FQ2 2020-	-FY 2020-	-FY 2021-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	2.03	2.23	▲9.85	2.14	8.44	8.75
Revenue (mm)	1153.15	1136.90	▼(1.41 %)	1177.85	4760.90	5011.10

Currency: USD
Consensus as of Apr-29-2020 2:45 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2019	1.76	1.88	▲1 6.82 %
FQ3 2019	2.11	2.31	▲2 9.48 %
FQ4 2019	1.98	2.01	▲3 1.52 %
FQ1 2020	2.03	2.23	▲4 9.85 %

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Call Participants

EXECUTIVES

Jeffrey Mark Farber
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John Conner Roche
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Richard William Lavey
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Presentation

Operator

Good day and welcome to The Hanover Insurance Group's First Quarter 2020 Earnings Conference Call.

My name is Cole, and I will be your operator for today's call. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Oksana Lukasheva. Please go ahead.

Oksana Lukasheva
Vice President of Investor Relations & Financial Planning

Thank you, operator. Good morning, and thank you for joining us for our quarterly conference call.

We will begin today's call with prepared remarks from Jack Roche, our President and Chief Executive Officer; and our Chief Financial Officer, Jeff Farber. Available to answer your questions after our prepared remarks are Dick Lavey, President of Agency Markets; and Bryan Salvatore, President of Specialty Lines.

Before I turn the call over to Jack, let me note that our earnings press release, financial supplement and a complete slide presentation for today's call are available on the Investors section of our website at www.hanover.com. After the presentation, we will answer questions in the Q&A session.

Our prepared remarks and responses to your questions today other than statements of historical facts include forward-looking statements regarding, among other things, our outlook for 2020 and the ongoing impact of the COVID-19 pandemic on company performance. There are certain factors that could cause actual results to differ materially from those anticipated. We caution you with respect to reliance on forward-looking statements and in this respect refer you to the Forward-Looking Statements section of our press release, the presentation deck and our filings with the SEC, which includes supplemental risk factors related to the COVID-19 pandemic and general economic conditions. Today's discussion will also reference certain non-GAAP financial measures such as operating income and accident year loss and combined ratios excluding catastrophes, among others. A reconciliation of these non-GAAP financial measures to the closest GAAP measure on a historical basis can be found in the press release, the slide presentation or the financial supplement, which are posted on our website, as I mentioned earlier.

With those comments, I will turn the call over to Jack.

John Conner Roche
President, CEO & Director

Thank you, Oksana. Good morning, everyone, and thank you for joining our call.

Before we begin, I'd just like to say on behalf of the Hanover team that we hope each of you, your families and friends are safe and healthy and managing through this public health crisis as well as possible.

Our company delivered very strong results in the quarter while continuing to navigate the unprecedented, challenging and very dynamic environment defined by the COVID-19 pandemic. We are well positioned to navigate this crisis and have the resiliency and resolve to continue to deliver on our commitments to all of our stakeholders. I will begin with some comments about our business in the context of COVID-19 and the current environment, and then I will provide a high-level overview of our first quarter 2020 performance. Jeff will take you through our operating results by segment, an in-depth review of our investment portfolio; and provide thoughts on our 2020 financial outlook. We will then open the line for your questions.

Over the past 2 months, COVID-19 has created unprecedented changes in the way we live and work. Today, most people in the U.S. and more than 2 billion worldwide are under some form of stay-in-place order, but the families of over 200,000 whose lives have been taken by this disease, this is an especially tragic time. Thanks to the selfless dedication of our health professionals and first responders, with the unique collaboration of scientists and the overwhelming response from the private sector, I'm confident our country will meet this challenge head on just as we have so many other times throughout our history. For the Hanover's part, if anything has emerged from the coronavirus crisis, it's that our company is resilient, nimble and compassionate in the face of this pandemic; and that we are committed to working together to deliver for our shareholders. Our business is running at full speed. Our service levels remain strong, and we continue to deliver on our proud tradition of being there for our customers and agents when they need us most.

With the health and safety of our employees being our earliest priority, we had to adjust to a virtual work environment in short order, and we were ready. Over 95% of our workforce has seamlessly transitioned to a remote work environment while continuing to deliver high-quality service to our customers. The substantial investments we have made in technology and workflow over the last several years, our business continuity planning and a cultural shift to agile and flexible work practices have prepared us well. I am incredibly proud of our outstanding team of 4,300 employees across the country, who have shown commitment, creativity and resolve. Thank you for stepping up.

I am also proud of our robust response to support our policyholders, agents and local communities. Our extensive customer financial relief program includes a 15% personal auto premium return for April and May as well as flexibility on bill payment options to those in need. It also contemplates expanded personal auto and homeowners terms to cover delivery of essential goods, living and rental car expenses resulting from repair delays and other adverse circumstance. We have also implemented steps to provide our operational and technological support to our partner agents. Finally, we have committed $500,000 to local community funds and nonprofit organizations to provide pandemic-related assistance and donated critical medical supplies to local health professionals.

From a financial perspective, our company remains very strong. We have a solid balance sheet, ample liquidity and a high-quality investment portfolio. Our insurance portfolio is built on thoughtful and conservative underwriting practices and mix management, and it continues to generate broad-based profitability. We believe these elements will allow us to successfully manage through the impacts of COVID-19. We have executed a comprehensive financial scenario modeling process with multiple economic scenarios incorporating detailed underwriting risk exposure reviews. Our modeling indicates that even in the most stressed scenarios our overall operating performance should remain relatively stable in 2020, with some potential puts and takes by business and by quarter as the year progresses.

In Personal Auto, we expect that various stay-in-place orders to result in a short-term frequency benefit. This reduction in auto frequency will be offset to some degree by premium return, higher cost of materials and other exposure impacts, depending on the length of the economic downturn. We do not expect a material impact on our homeowners business. While spending a lot of time at home will likely enable policyholders to mitigate potential losses before they become significant, this benefit could be offset by an increase in costs of materials due to supply chain disruptions and moral hazard claims. In our Core Commercial Lines, the economic pause might mean lower claims activity in the short term, but if the slowdown continues, we are mindful of the potential for an increase in vacancy-related risks such as fires and possibly elevated social inflation down the road. By and large, the effect on our Specialty business should be similar to our Core Commercial business given the retail agency small account focus of our Specialty portfolio. We consider direct D&O and management liability claim potential to be limited based on the small private company focus in this book. We have no exposure to first responders and limited exposure to medical professionals workers' compensation.

Now I would like to share some thoughts regarding business interruption. The overwhelming majority of our commercial multi-peril policies are ISO-based and have an explicit virus exclusion. We have 538 policies split between our CMP line in Core Commercial and health care businesses within Specialty, where we believe coverage could be triggered under specific circumstances. Consistent with our underwriting intent, these policies provide coverage with only $25,000 sublimits. Many of these insureds have not closed their facilities. We have reviewed these exposures in any others and, based on our current actuarial and underwriting assessment, have earmarked approximately $13 million of reserves to address direct COVID-19 related exposures, with the BI exposures making up the vast majority of the expected liability.

Overall, based on our mix of business, we expect the net impact of the coronavirus to our 2020 underwriting results to be very manageable. 40% of our business is Personal Lines. In Commercial Lines, we predominantly use ISO-based forms. We have a low percentage of our premium in workers' compensation at roughly 7%; and 0 exposure to event cancellation, travel insurance, trade credit or similar coverages. The impact of COVID-19 on net written premiums is much harder to predict both for our company and the industry overall, considering the many uncertainties related to the longer-term scope and impact of the pandemic and how the macroeconomic environment unfolds. Short term, growth will likely slow or even show some temporary premium declines due to premium return in Personal Lines, cancellations, mid-term endorsements; and other effects of a reduction in overall economic activity. In terms of insurance [spicing] environment, we expect that the industry rate trajectory will likely continue as the need for rate in certain lines exists.

As previous downturns have demonstrated, rate is typically more dependent on the insurance cycle than the economic cycle. We were on a steady trajectory of consistent rate increases in Core Commercial through March; and we believe it will continue, fueled by continued increases in loss inflation. We also believe that lower new money yields will serve as an additional catalyst for enhanced pricing.

A number of investors have asked us about the potential for regulatory or legislative changes that may adversely affect the industry and how we see that playing out. Unfortunately, we don't have a crystal ball, so I can only speak from the perspective of history and the fundamental role of contract law in the economy. It's not unusual during a crisis to see a flurry of regulatory and legislative proposals aimed at the insurance industry and its operations. We expect and will comply fully with temporary regulatory actions such as moratoriums on cancellations, which are routine in crisis situations. That said, we expect the courts to continue to uphold the sanctity of contracts as guaranteed by the constitution, in particular where virus is explicitly excluded as a peril. We are encouraged by the statements by the NAIC and many state insurance commissioners as well as the efforts of the American Property Casualty Insurance Association to protect the strength and stability of the insurance sector. And we're in close contact with regulators and legislators nationwide to ensure the industry continues to work efficiently for our customers and agency partners.

Now turning to our first quarter performance.

We generated net written premium growth of 3.5%, in line with our expectations. Growth was driven by Core Commercial with a meaningful pickup in small commercial new business and Specialty excluding our program business. Core Commercial rate excluding exposure continued on its upward trajectory at 4.6% in the first quarter. Additionally, we saw continued sequential rate increases in our Specialty business as well. Personal Lines growth was tempered by the impact of consistent 5% rate increases on our retention, which was largely anticipated. We didn't experience a contraction in growth in the first quarter due to COVID-19, as most of our business renews 45 to 60 days in advance.

Our current accident year loss experience in the quarter was defined by several factors, which on balance resulted in a minor increase in losses relative to our expectations. First, we had one large fire loss in our middle market business, which triggered an annual aggregate deductible under our property per risk reinsurance program. Second, we experienced favorable winter weather this quarter, as well as a decline in personal auto frequency starting in mid-March due to lower miles driven. Commercial auto frequency hardly changed in the quarter, which we believe is due to some businesses switching to enhanced delivery services. Third, we increased reserves to reflect potential COVID-related claims, which Jeff will touch on.

In terms of prior year reserve development, we are very comfortable with where we stand from a balance sheet perspective, with slight favorability overall driven by workers' compensation. Current and prior year reserve movements in the quarter are consistent with our philosophy of reacting to issues promptly to avoid bigger issues down the road.

Looking at our capital allocation strategy. In February, we completed the $150 million accelerated share repurchase program we announced last year. In addition, we subsequently repurchased approximately 350,000 shares of our common stock in the open market. We stopped repurchasing Hanover stock in mid-March. We will continue to follow prudent and disciplined capital allocation strategies as we move forward.

In summary, our first quarter results were in line with our overall expectations. Based on our strong financial position; sound underwriting practices; product expertise; and our broad, well-diversified portfolio, we are confident we can continue to successfully navigate the current environment. We remain committed to maintaining the health and safety of our employees, being responsive to the needs of our customers and agents and acting in the best long-term interest of our shareholders.

With that, I will turn the call over to Jeff.

Jeffrey Mark Farber
Executive VP & CFO

Thank you, Jack. Good morning, everyone.

For the first quarter, we reported a net loss of $40 million or $1.04 per basic share compared with net income of $122.4 million or $2.97 per fully diluted share in the prior year first quarter. After-tax operating income was $86.8 million or $2.23 per diluted share compared with $80.7 million or $1.96 per diluted share in the prior year quarter. The difference between net loss and operating income in the first quarter of 2020 primarily reflects the decrease in the fair value of equity securities and to a lesser extent fixed-income impairments. These impairments are a subset of the adjustments made to reduce the unrealized appreciation of investment recorded in stockholders' equity.

Our combined ratio was 95.2% compared with 95.8% in the prior year quarter. Lower expenses and catastrophes contributed to the combined ratio improvement, while the current accident year loss ratio was slightly higher by 0.4 points. Catastrophe losses totaled $37.9 million in the first quarter of 2020 or 3.3% of earned premium, below our expectations for the quarter. Relatively quiet weather in January and February gave way to a more active March, with a notable impact from tornadoes that struck Tennessee which accounted for a large part of the cat losses we incurred in the quarter.

With respect to prior year reserve development, we were slightly favorable for the quarter. Small adjustments in some older legacy voluntary pools business were more than offset by net favorable development in our ongoing P&C business. We experienced favorability in workers' compensation and certain specialty lines, which continued to develop better than expectations. At the same time, we saw unfavorable development in commercial and Personal Auto due to additional activity in prior accident years on the bodily injury side. However, we remain comfortable with our current accident year '18 and '19 auto picks. Reflecting our disciplined approach to financial management, expenses came in favorable to our expectations in the quarter due to lower discretionary spend and the timing of certain accruals.

Looking at our underwriting results by line. Personal Lines combined ratio excluding catastrophes was 87% for the first quarter, down from 91.6% in the same period last year, driven primarily by the improvement in current accident year losses. Personal Auto loss ratio of 67% improved 3.6 points from the first quarter of 2019, primarily reflecting a more favorable winter weather experience in our footprint throughout the quarter as well as the observed decline in physical damage and comprehensive auto property frequency starting in the second half of March due to various stay-in-place orders. Although we are expecting a meaningful decline in frequency in the second quarter, we expect the favorable result to be somewhat muted as a result of potentially higher severity associated with an increase in the cost of repairs and by the $30 million premium refund we announced earlier this month. These unusual and temporary impacts aside, underlying trends in Personal Auto are performing in line with our expectations.

Homeowners loss ratio of 48.4% was stable compared with last year. We have experienced favorability from mild ex cat winter weather similar to auto, which was partially offset by an increase in fire losses.

Personal Lines net written premiums increased 2.1% in the quarter, underscoring our focus on profitability in a competitive market. We seek to strike a successful balance between rate and retention as well as the expansion of our whole account offering with many of the industry's best agents. Our continued discipline and enhanced account proposition will position us well in the coming months as the competitive landscape responds to more normal loss trends and continued severity pressures.

Turning now to Commercial Lines. Our combined ratio excluding catastrophes was 94.7%, up from 92.6% in the first quarter last year. The increase primarily reflected a higher current accident year loss ratio, partially offset by favorable development and reduced expenses. Excluding catastrophes, the Commercial Lines current accident year loss ratio increased 2.4 points to 61.2%, reflecting 2 major drivers: one unusually large fire loss and COVID-related reserve actions. The fire loss occurred in the CMP line and hit our property per risk annual aggregate deductible in the "$10 million excess of $10 million" layer for the full amount of $10 million, driving a substantial portion of the increase in the CMP loss ratio in the quarter. We had determined that an economic benefit existed in maintaining this annual aggregate deductible, but it is always more painful in a quarter that a large loss presents itself.

Our Commercial Lines loss picks also include an increase in a reserve provision specifically to cover potential COVID-19 related losses, primarily in those sublimited policies that we specifically offered limit coverage for virus-related exposures. As Jack mentioned, we conducted a very thorough review of policies and contract language in our Commercial Lines business. We identified a total of 538 commercial multiple-peril policies in Core Commercial and monoline property policies in our health care business within Specialty with BI endorsements that, by our intention, do not have an explicit virus exclusion. Many of these policies could see potential losses due to being shut down for cleaning rather than business closure since many of them are essential businesses. Each of these policies has a $25,000 total sublimit for this coverage. To put this number of policies in context: We have nearly 400,000 commercial policies in total. Based on these facts, we set aside $13 million of our reserves, including reserve additions in the first quarter. The majority of our COVID exposures and accordingly of these reserves relate to these 538 policies. Given the population and low sublimits, we believe that the losses will be quite manageable.

Commercial Auto current accident year loss ratio excluding catastrophes improved 3.3 points to 66.5%. We are seeing the benefit of prior rate increases and targeted underwriting actions that we've talked about in prior calls. Compared with Personal Lines auto, we didn't see quite the same level of frequency declines in March, which most likely reflects the stepped-up delivery activity in certain industry sectors and geographies.

Turning to workers' comp. The ex cat accident year loss ratio increased 3.7 points from the prior year quarter to 63.4%. The increase reflects our prudent loss selections in the face of an industry-wide decrease in rate as well as the timing of a loss selection adjustment in the first quarter of last year. We are very comfortable with our overall book of business. However, we are remaining prudent in the current pricing environment.

In other commercial lines, the current accident year loss ratio excluding catastrophes improved 2.3 points to 55.3%, reflecting a favorable comparison to heavy property losses a year earlier. The loss ratio in this line is elevated relative to our plan and includes a portion of the increased reserve provision to cover potential COVID-19 losses that I mentioned earlier.

Commercial Lines net written premiums grew 4.5% in the first quarter. Our team is laser-focused on growing in businesses, industries and geographies that meet our profitability targets while continuing to execute on granular underwriting and pricing actions in areas such as nonspecialized programs. We saw strong growth in our Core Commercial businesses, led by CMP and workers' comp, as we continued to push rate in auto lines. The strong underlying growth momentum through March was partially offset by the planned reduction in our programs portfolio of about 6%.

Moving to investment performance. Our net investment income was $69.6 million for the quarter. The vast majority of our net investment income is very resilient to the current market environment. Our portfolio duration is 4.2 years, so just less than 1/8 of our portfolio is expected to turn over every year. Short-term interest rates have a manageable effect, and we continue to prudently navigate the decline in interest rates and recent widening of corporate credit spreads.

It is worth noting that included in our investment income in the first quarter was approximately $7 million of partnership income, which included the impact of income and market appreciation through the end of 2019. We report partnerships on a 1-quarter lag, as the results come in after we have released our earnings. Our partnership mix has a higher weighting toward credit and mezzanine funds, which have historically been less volatile than the broader equity markets but are still somewhat correlated to the S&P. Based on valuations at March 31, it is certainly a possibility for us to report a loss on these partnerships in the second quarter.

We are confident in the fund managers, and we know that this is a long-horizon asset class with strong long-term returns for the investor who can tolerate the volatility. We remain confident and comfortable with the composition of our investment portfolio. It is high quality, well laddered and well diversified by industry and asset class. Fixed income and cash represent 85% of our overall $8 billion portfolio with a weighted average quality of A+, and it is 96% investment grade. At the end of the first quarter, equity securities represented approximately 6% of our total investment portfolio. Additionally, over the past 3 years, we have reduced our exposure to BBB issuers from 6% of fixed income to 4% and our exposure to below-investment-grade issuers from 6% to 4%. As a result, we are comfortable that our portfolio can absorb potential downward ratings migration associated with the economic fallout of the coronavirus outbreak. We have also meaningfully reduced our exposure to certain fixed-income industry classes that are inherently more volatile. Energy, for example, now makes up only 2.9% of our overall fixed income portfolio compared with 5.3% 3 years ago and is 92% investment grade. More than half of our energy exposure is in the midstream subsector, where most of the operations are backed by fixed fee contracts, making them more resilient in times of economic uncertainty. We have limited exposure to some of the industries that are more sensitive to the economic impact of COVID-19, including airlines, hospitality and retail which together make less than 3% of our portfolio.

Our commercial mortgage-backed securities are 95% AAA rated; and well diversified by property type, metro area and vintage year. Our CMBS holdings also benefit from greater than 30% credit enhancement. And we have substantially lower exposure in our CMBS holdings to retail industries than the public conduit universe, with very strong loan-to-value metrics.

Despite the strength of our investment portfolio, it was not immune to the unprecedented volatility in the first quarter, leading to an overall decline in book value per share of 5.1% even after accounting for the solid operating income. We are long-term capital allocators and are confident that we will effectively manage current financial market risk and volatility. In fact, based on the market values as of last Friday, we have recovered a substantial portion of the decline in book value, underscoring the strength and quality of the portfolio.

Before opening the line for questions, let me provide some thoughts on our 2020 outlook. As Jack mentioned, we undertook a very comprehensive financial modeling exercise, with strong cross-functional participation across the company. We further stressed several assumptions across our entire business portfolio, including prolonged stay-in-place orders; potential related premium cancellations and endorsements; as well as pressure from increased risks of vacant properties, lawyer activity and recession-related losses such as surety-related risks. We feel really good about the output of this exercise, which provides helpful parameters for our updated 2020 outlook. Accordingly, we are reaffirming our original ex cat combined ratio guidance of 91% to 92%.

Because of the great uncertainty around the length of the slowdown and the level of premium decline, it is not possible for us to give guidance on premium growth today. Beyond the premium return measures that we announced earlier this month, we are closely monitoring endorsement, new business and cancellation activity, which will depend on the level and speed of the economic recession and ultimate recovery that is now very hard to predict. Regardless of where premium levels land and the related reduction in loss frequency, we feel confident about our financial discipline and ability to flex our expenses over the course of the year while balancing short-term needs with longer-term strategic focus.

Closing out underwriting performance, we still expect catastrophe losses at 4.6% on a full year basis. Please note, given our geographic footprint and seasonality, our second quarter catastrophe assumption is set at 5.6%.

In terms of net investment income, putting the partnership component aside, we still feel good about the bulk of our income assumptions for various asset classes. Incorporating the likely loss from partnerships in the second quarter and assuming a gradual improvement of current market conditions over time, our overall NII outlook now stands at around $255 million for 2020, give or take a little variability on either side. We believe second quarter will be lower than the quarterly run rate for net investment income in 2020 given the potential for marks on investment partnerships. As a reminder, our investment partnerships represent less than $300 million of the overall $8 billion investment portfolio.

To summarize. We are optimistic about our overall expected 2020 results and have confidence in our ability to navigate the economic impact on premiums in future years. We have demonstrated our ability to perform in very challenging times, and we will continue to do so. Our company remains very strong. Over the years, we have diversified the portfolio by state and mix while strengthening our earnings stream in each business. We have a solid balance sheet, strong liquidity and a high-quality investment portfolio. We believe these elements will allow us to successfully manage through any market challenges and emerge as an even stronger performer in the industry.
With that, we will now open the line for questions. Operator?

Question and Answer

Operator

[Operator Instructions] And our first question today comes from Matt Carletti with JMP.

Matthew John Carletti
JMP Securities LLC, Research Division

Just a few questions. Maybe I'll start with Jack and Jeff. Is there any insights you can give us into what you've seen in April, so far? I mean I appreciate your comments that we have no idea of kind of how long this goes or kind of the shape of the downside and the upside, but in terms of even just qualitatively new business production, retentions, endorsements, cancellations, just any color you could give on what you've seen so far in April as we've gotten further into this stay-at-home stuff would be helpful.

John Conner Roche
President, CEO & Director

Yes, Matt. This is Jack. Thanks for the question. I would tell you that it is still very early. We are pleasantly surprised that many of our agents have transitioned very well to the remote environment. I think, as an industry, I'm impressed, frankly, that the business of property and casualty insurance is, I think, going well and being responsive to customers' needs. The early indications are that there is some new business submission activity that will come down. It's early to say that we see anything specific, but we also expect that, that ranges substantially by industry class and, to some degree, geography. What we're encouraged about is that our work to use our analytical approach with agents and doing more active pipelining will help us through that period where we have accounts that we've identified that we want to work on with agents and that we're not just responding to the flow that comes out that may in fact get reduced. We do expect that retentions will escalate. I think that early indications are that, that will in fact happen. And then the wild card will be, over time, how much do we see in terms of cancellations and midterm adjustments and exposures that will come into the factor and at least affect the top line trajectory, but I would tell you in the early innings we're encouraged that there is a level of stability at the onset.

Jeffrey Mark Farber
Executive VP & CFO

And Matt, on the claims side, clearly we're seeing reductions in claims across a lot of areas, and they're quite meaningful.

Matthew John Carletti
JMP Securities LLC, Research Division

Okay. Maybe tying that into your -- some of the guidance pieces, really my question centers around you suspended the top line guidance, which makes complete sense to me. I think that's pretty common and I don't think anybody can predict the future there, but you affirmed the expense ratio guidance, which I think some peers have indicated they expect upward pressure on expense ratio, not downward. Can you talk a little bit about that dichotomy there where, with the fuzzier outlook on net written premiums, the ability to kind of reaffirm your expected expense ratio improvement, is that -- Jeff, does that relate to kind of what you referenced in your comments about you can make decisions about where to pull back and not pull back, be able to more flex in the optional spend than maybe some other people?

Jeffrey Mark Farber
Executive VP & CFO

Yes. So if you break the combined ratio into its 2 components: The expense ratio, we reaffirmed a 10 basis point improvement. So we have the ability to balance the long term and the short term and focus on expenses to be able to deliver on that in the expense scenarios in 2020 that we can see. From a loss ratio perspective, we're pretty confident that the claims activity will offset the decline that we're likely to see or seeing in premiums.

Matthew John Carletti
JMP Securities LLC, Research Division

Okay, all right. And last one, if I can, just, Jeff, on capital management. Maybe just give us an update on your views there. I mean we saw the ASR closed out in Q1. There were some additional open-market purchases. And either -- I forget who commented, but you said you had kind of halted activity in mid-March. How do you think about capital management looking forward? I mean you've referenced kind of, at least near term, likely some downward pressure or at least reduced growth on top line and obviously your stock trading at a lower valuation than it did recently. How should we think about that?

Jeffrey Mark Farber
Executive VP & CFO

So Matt, yes, as you said, we finished the ASR. We did another $40 million or so additional buybacks, and then we paused in mid-March. And I think our view on buybacks at the moment is really take a wait-and-see approach. So we haven't determined that we're going to jump back in. We also haven't determined that we're done for the year. It will really depend on how things go and how we feel about it. At the moment, we have ample capital and we feel good about operations, but I think we're being prudent to wait and see. It may go without saying, but just to be clear: We don't anticipate any changes. And ordinary dividend would be impacted. My guess is any view of special dividends would certainly follow the same view as buybacks.

Operator

And our next question comes from Paul Newsome with Piper Sandler.

Jon Paul Newsome
Piper Sandler & Co., Research Division

I've got just 2 questions, normal 2 questions. One is big picture. One is very small. So maybe the big picture one: Every time we've seen a major, really big, big event like this, we've seen changes in how people underwrite things. I'm wondering. From your perspective, are there areas where you think the underwriting will fundamentally change and how either you or others look at risk?

John Conner Roche
President, CEO & Director

Yes, Paul. This is Jack Roche. Thanks for that question. Jeff had talked about some of the financial scenario work that we've done to look at our existing portfolio and start to -- contemplating what could happen and how would -- do we think the financials will respond based on the various factors that might be coming at us. At the same time, Dick and Bryan have been actively working and absorbing kind of thoughts around, if this goes and prolongs; and if our hunch is right that the way we do business and, frankly, the way a lot of our customers do business are going to change in an accelerated pace, what would be the implications to the sectors of the business that we would be interested in or that might see some aversion. So the long and short of it is that, when we've done that analysis, we're pretty proud of some of the shifts we've already made that -- and Dick, maybe you can comment on this, that we have really reduced our penetration in some of the restaurants and hospitality and some of the areas. And we did that because of some of the liability trends that we observed a couple years back, but I think those will serve us well. We actually scaled back a little bit in the major metropolitan areas as part of that effort. I think that will serve us well. So as we project into the future, I think we see the service economy continuing to prosper but in a much different way. And we're doing a fair amount of scenario work to try to anticipate that and position ourselves for success in the future. Dick?

Richard William Lavey
Executive VP & President of Hanover Agency Markets

Yes. So just briefly adding some color to that. We do agree that our -- we think our core book sort of provides us a bit of resiliency in the downturn to some of what Jack said, specifically restaurants, hospitality. You think about those sectors as those being most affected here. That's less than 7% of our book, which is a small percentage. The work we did to move out of major metropolitan areas, that's down about 20% over the last 4 years. And certainly we know that those metro areas are those that are more substantially impacted by COVID. Maybe just one other color commentary I'd make is, as we look at classes and industries and how this may affect them, certainly our underwriting today looks at their operations but also their financial strengths, and that will become an important component. You think about schools and things that are happening in that arena, making sure their financial stability is rock solid. So we think our current [drill] will serve as well.

Jon Paul Newsome
Piper Sandler & Co., Research Division

Now sort of a [newer] question. I'm getting a couple of questions on the Commercial Auto environment. And you've had some -- maybe you can talk a little bit about what triggered the reserve development there. And I guess we all hope that maybe this year would be the year it would turn around in general, but can you just give us a little sense of what's going on there?

Jeffrey Mark Farber
Executive VP & CFO

So Matt (sic) [Paul], I would think, if you look at our prior year development overall, let's remember it was favorable overall. It was favorable in Personal Lines. It was favorable in Commercial Lines overall. It was favorable in other commercial lines. And you're right. It was unfavorable in auto, offset by workers' comp favorability. I think we feel very comfortable with our overall reserves. In this particular quarter, we saw some unique situations with auto, particularly Commercial Auto on bodily injury, and we felt that we needed to react to those. We still feel very good about our '18, '19 and '20 picks there and all of the rate that we've been getting really over the last 6 quarters and the reunderwriting. So I think we're in reasonable shape overall.

Jon Paul Newsome
Piper Sandler & Co., Research Division

So those are changes for what, specific case issues? Or that's trend changes.

Jeffrey Mark Farber
Executive VP & CFO

Mostly it's specific case issues, so some unique issues. Obviously we're not immune to litigation trends, as people have seen really over the last few years, but mostly it's specific case issues there.

Operator

[Operator Instructions] And our next question comes from Meyer Shields with KBW.

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

Great. I think it was a question for Jeff. Can you talk about new money rates and whether there's any shift in your investment allocation strategy for new money now?

Jeffrey Mark Farber
Executive VP & CFO

No, we really haven't changed our portfolio mix in any material way. The new money rates are down. Obviously rates have come down and spreads have widened a little bit, so the spreads have covered some of that gap. And with a 4.2-year duration, it takes sort of about 8 years for the portfolio to roll off. And because of the timing of cash flows, we generally don't do a lot of new investing in the first 4 months of the year. It tends to be later, so now we're about to go at that. So the new money yields are down a little bit. And we've baked those levels into our guidance that we've given for the year, but no, we're not seeking or chasing higher yields or reshaping the portfolio, Meyer.

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

Okay. Second question: Can you give us a little insight into the expenses that you pulled back on in the first quarter and maybe how that would impact operations over the rest of 2020?

Jeffrey Mark Farber
Executive VP & CFO

So we really didn't make any specific decisions in the first quarter. I mean expenses were down year-over-year, but they were not down as much in terms of our guidance. Expense ratio was down a little bit relative to guidance. So it was largely just the timing of new hires or things of that nature or some accrual adjustments. I think more importantly, as we think about the year, there will be some expenses that just naturally go down like travel and entertainment, conferences, things like that. And then there'll be other expenses that we have some flexibility around in order to be able to manage the decline in premium to deal with the -- an expense ratio.

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

Okay. And then final question. It looks, if my very rough math on the fourth quarter is right, like the Commercial Lines absolute -- like the rate change slowed a little bit. And I was hoping you can talk about that.

John Conner Roche
President, CEO & Director

This is Jack. You're -- let me make sure I understand the question. You're asking about the trajectory of our Commercial Lines pricing...

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

Yes.

John Conner Roche
President, CEO & Director

And specifically rate.

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

Yes.

John Conner Roche
President, CEO & Director

Yes. What we articulated in the script is that the rate trajectory within Commercial Lines continues to tick up. So we're having sequential improvement. What you saw in fourth quarter was that we had a pretty large pricing result that showed a particularly high swing in the exposure side. And I think we tried to speak to that in the fourth quarter call so people would know that 7.9% or whatever it was in terms of total pricing was a little bit inflated, if you will, based on the exposure base that ran through that particular quarter. And I would say that there's a similar phenomenon in the first quarter where the exposure element is actually a little bit lower than what we normally would see, not affected by the economy but by the normal ebbs and flows of exposure-based. So when you look at that core 4.6% rate that's running through the book, we -- that is actually an improvement over what we've been getting. And if you look even further into our specialty portfolio, we're seeing some additional incremental improvement in that portfolio.

Operator

And this will conclude our question-and-answer session. I'd like to turn the conference back over to Oksana Lukasheva for any closing remarks.

Oksana Lukasheva
Vice President of Investor Relations & Financial Planning

Thank you, everybody, for your participation today. We are looking forward to talking to you next quarter, and stay healthy.

John Conner Roche
President, CEO & Director

Be well.

Operator
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your lines, and have a great day.