

Selective Insurance Group, Inc.

NasdaqGS:SIGI

FQ4 2012 Earnings Call Transcripts

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S&P Global Market Intelligence Estimates

	-FQ4 2012-			-FQ1 2013-	-FY 2012-		
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	
EPS Normalized	(0.17)	(0.04)	NM	0.36	0.45	0.58	
Revenue (mm)	455.37	448.98	▲ (1.40 %)	461.41	1739.35	1734.10	

Currency: USD

Consensus as of Feb-01-2013 2:11 AM GMT

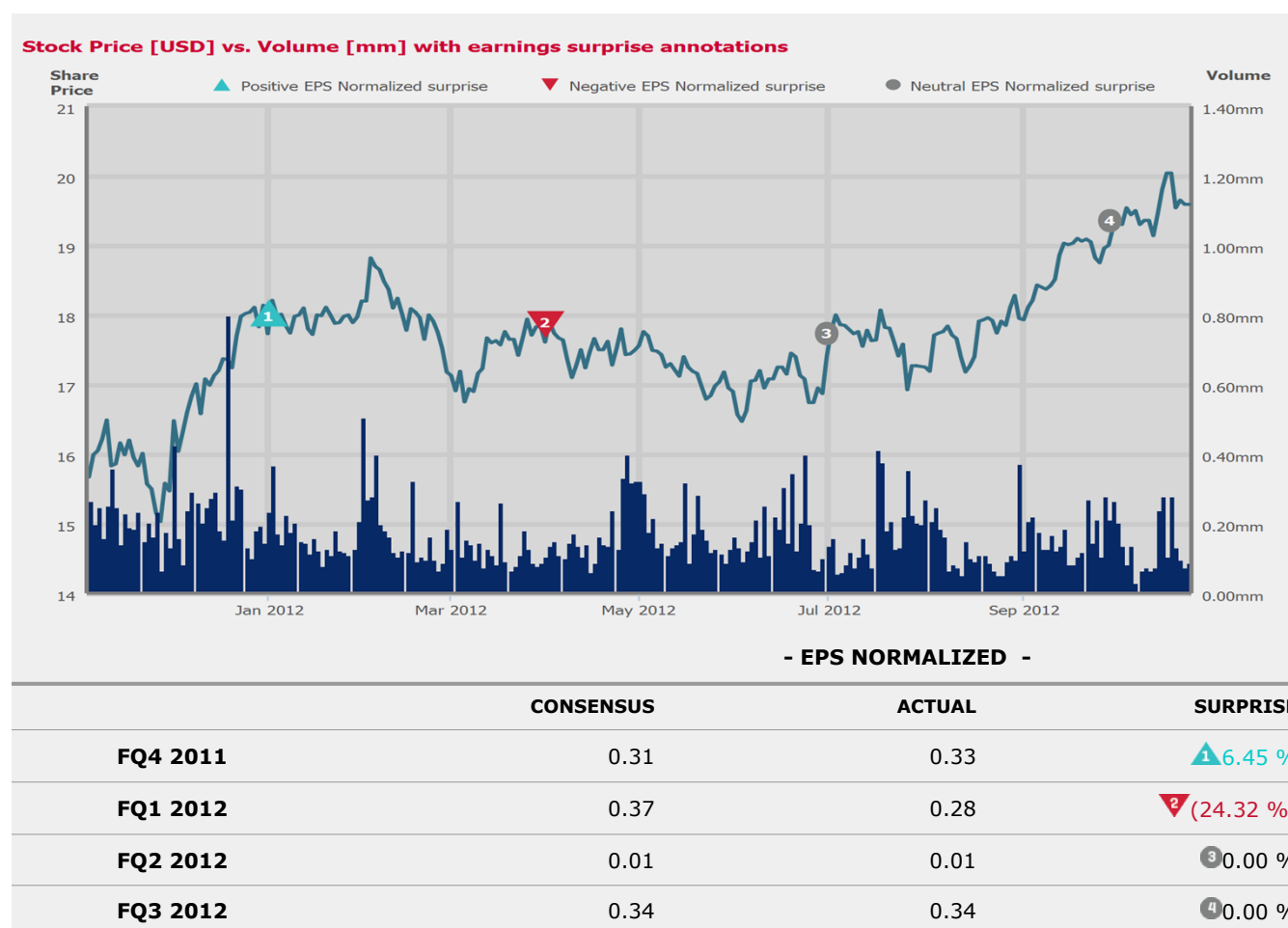


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Call Participants

EXECUTIVES

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

Gregory Edward Murphy

Chairman & CEO

Jennifer Wilson DiBerardino

Former Sr. Vice President, Investor Relations & Treasurer

John Joseph Marchioni

President & COO

Ronald J. Zaleski

Former Chief Actuary and Executive VP

ANALYSTS

Alison Marnie Jacobowitz

BofA Merrill Lynch, Research Division

Christopher J. Maimone

Macquarie Research

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Ronald David Bobman

Capital Returns Management, LLC

Presentation

Operator

Good day, everyone and welcome to the Selective Insurance Group's Fourth Quarter 2012 Earnings Release Conference Call. At this time, for opening remarks and introductions, I would like to turn the call over to Senior Vice President, Investor Relations and Treasurer, Ms. Jennifer DiBerardino. Ma'am, you may begin.

Jennifer Wilson DiBerardino

Former Sr. Vice President, Investor Relations & Treasurer

Thank you. Good morning, and welcome to Selective Insurance Group's fourth quarter 2012 conference call. This call is being simulcast on our website and replay will be available through March 1, 2013. A supplemental investor package which includes GAAP reconciliations of non-GAAP financial measures referred to on this call is available on the Investor's page of our website at www.selective.com.

Selective uses operating income, a non-GAAP measure, to analyze trends and operations. Operating income is net income excluding the after-tax impact of net realized investment gains or losses, as well as the after-tax results of discontinued operations. We believe that providing this non-GAAP measure makes it easier for investors to evaluate our insurance business.

As a reminder, some of the statements and projections that will be made during this call are forward-looking statements, as defined by the Private Securities Litigation Reform Act of 1995. Forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties. We refer you to Selective's Annual Report on Form 10-K and any subsequent Form 10-Qs filed with the U.S. Securities and Exchange Commission for a detailed discussion of these risks and uncertainties. Please note that Selective undertakes no obligation to update or revise any forward-looking statements.

Joining me today on the call are the following members of Selective's Executive Management Team; Greg Murphy, CEO; Dale Thatcher, CFO; John Marchioni, EVP of Insurance Operations and Ron Zaleski, Chief Actuary.

Now I'll turn the call over to Dale to review the fourth quarter results.

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

Thanks, Jen, and good morning. 2012 was shaping up to be a decent year and we are on-track to meet our original guidance of 101.5% combined ratio until we had a visitor named Sandy on October 29th. As you are well aware, we have consistently frowned on the industry practice of playing takeout, if not for these large losses, if not for this Hurricane or that earthquake, etcetera.

Unfortunately, as we put together our prepared remarks this quarter, we came to the realization that to adhere to our historic standard would leave you with only one takeaway; Sandy was a big event. It would cloud your ability to analyze underlying trends, both positive and negative. So we decided to give you all the Sandy numbers upfront and then have the remainder of the prepared remarks address our business as if Sandy never happened. We will gladly answer any questions you have at the end either with or without Sandy and we provided extensive disclosures in our online investor packet both with and without Sandy. Trust me, we know it happened. Hurricane Sandy impacted many of our customers and represents the largest single loss in our history. Ultimately, the storm's impact on Selective's results on a net basis was in line with our November 28th preannouncement.

Pretax gross losses for Sandy are currently estimated to be \$136 million, up slightly from our preannounced expectation of \$100 million to \$120 million. We are still receiving claims and we are working through various coverage issues on individual claims so the number could still move up or down, but we feel the current estimate is reasonable. The components of our pretax net loss of \$55 million are as follows:

Under our reinsurance program, we retained the first \$40 million of losses. To that, we add \$6.6 million for our 5% co-participation in the first layer of reinsurance and 10% co-participation in the second layer. We then add another \$8.6 million for our ceded reinsurance reinstatement premium. From that, we subtract \$16 million, which is the positive Sandy collect related claims revenue we received as a result of being the national flood insurance programs' sixth largest writer and carrier. All of these items combined, net of the \$39.6 million pre-tax, \$25.7 million after-tax or \$0.46 per diluted share.

Overall, for the quarter, we reported an operating loss per diluted share of \$0.04 compared to operating income of \$0.37 a year ago. The fourth quarter statutory combined ratio was 110.4%. Excluding the impact of hurricane Sandy, the combined ratio for the quarter was 100.6%. Sandy's impact on the components of the combined ratio, including the \$8.6 million in reinstatement premium is as follows:

Loss in LAE from the storm was \$47 million and the corresponding ratio increased by 11.3 points. The loss in LAE ratio also increased 1.4 points due to the reinstatement premium impact on earned premiums. Flood claim revenue of \$16 million partially offset these losses and reduced the reported combined ratio by 3.7 points. The expense ratio increased by 0.8 points due to the \$8.6 million reinstatement premium and its impact on the denominator of net premiums written.

By line of business, Sandy increased the combined ratios for homeowners by 75.1 points, commercial property by 32.7 points and BOP by 53.8 points. Non-Sandy related capacity losses added another 1.3 points to the combined ratio, partially offset by favorable prior year casualty development of \$2 million in the quarter or 0.5 points.

Reinstatement premium on the property capacity program also detracted from net premiums written growth in the quarter. Total statutory premiums were up 5% in the quarter, but without reinstatement premium would have increased by nearly 8%.

Now that we have dealt with Sandy, the reminder of our prepared comments completely exclude the effects of Sandy on our numbers. Remember, the effects from the storm are seen in premiums, losses, LAE and all ratios. Excluding all effects of catastrophes and prior year casualty development, our fourth quarter loss in LAE ratio was 65.8%, an improvement of 0.8 points over 2011. This underlying improvement reflects our continued granular pricing strategy in which earned rate exceeds loss trend, because of our underwriting and claims initiatives.

The fourth quarter's expense ratio increased by 1.2 points compared to 2011, partly driven by the lower discount rate that increased pension expenses and added 0.6 points to the ratio. Premium growth was driven by standard commercial lines and personal lines renewal price increases, strong retention in both personal and commercial lines and \$29 million in E&S contract binding authority premium.

Standard commercial lines pure price was up 6.7% in the quarter with modest monthly acceleration culminating in a 7.1% increase in December. Retention for standard commercial lines also improved to 83% in the quarter, one point higher than the fourth quarter of 2011. The standard commercial lines statutory combined ratio for the quarter was 101.1% including 0.8 points of other catastrophe losses.

Underlying property lines results in the quarter were solid. Commercial property reported an 83.7% combined ratio, while commercial auto reported 95.6% and BOP 91.4%. These underlying results reflect the pricing success we have been able to achieve along with underwriting initiatives taking hold.

Workers compensation results deteriorated in the quarter to 119.2% combined ratio compared to 111.9% in the fourth quarter of 2011. This increase reflects unfavorable development of \$3 million or 4.7 points driven by higher than expected emergence in prior years.

General liability results saw some deterioration this quarter to a combined ratio of 108.3% compared to 104.1% a year ago as a result of 3.1 points of unfavorable development compared with 2.2 points of favorable development in the fourth quarter of 2011. The unfavorable development in the fourth quarter of 2012 was largely driven by a review of older accident years.

As you will notice in our line of business exhibit in this quarter's investor packet, we are showing E&S as its own segment and we'll be reporting the results separately going forward. 2012 was a transitional year

for E&S as we focused on integrating the operations. The combined ratio of 112.8% for the quarter and 118.1% for the year reflected combination of acquisition and integration costs and a higher than expected loss ratio. Given the relatively small size of the operation throughout the year, it didn't take a lot of losses to push around the loss ratio.

Personal lines statutory net premiums written were up 7% to \$72 million in the quarter including renewal pure price of 8.3%. The personal lines statutory combined ratio for the quarter was 93.9% including 3.6 points of other catastrophe losses and 2.7 points of favorable development. The homeowners combined ratio was 84.7% including 3.2 points of favorable development and 7.6 points of other catastrophe losses. It compares favorably to a year ago when the combined ratio was 95.4% including 3.8 points of cap losses.

We continue to push significant rate increases through our homeowners' book targeting a high 80s combined ratio in a normal catastrophe year. As a result, renewal peer price for homeowners increased 10.8% in the quarter.

We successfully renewed our 2013 property catastrophe treaty adding a new \$150 million top layer and increasing reinsurer participations in each of the expiring 3 layers. This expands the program to \$585 million in excess of \$40 million retention. As we increased our cap reinsurance program, we look for ways to minimize the credit risk inherent in a reinsurance transaction by dealing with highly rated reinsurance partners and by purchasing collateralized reinsurance products particularly for extreme tail events.

The current program provides \$116 million in collateralized limits; the 43% increase in the total limits placed for 2013 as well as market pricing fluctuations and exposure changes resulted in \$11 million increase from the 2012 seeded premium. We calculate the peer price change for our expiring cat layers to be approximately 7% which is below the 10% price increases reported broadly in the marketplace for loss impact of January 1, treaty renewals.

Fourth quarter after tax net investment income increased 16% from a year ago to \$26.3 million. The increase was driven by alternative investments which generated income of \$4 million pretax compared to a loss of \$3 million in the 2011 fourth quarter.

For the year overall, our alternative portfolio generated an 8% return or \$10 million compared to a 17% return or \$21 million in 2011 when the portfolio generated more distributions. In 2012, the alternative portfolio lagged expectations largely due to under performance in the energy strategy, continued lack of traction in real estate and inconsistency in venture capital returns.

Pretax income from fixed maturity securities was down 4% for the quarter and for the year reflecting the effect of the continued low interest rate environment. After tax yield declined 22 basis points to 2.5% for the year and fixed maturity new money rates are running at approximately 1.64% after tax, placing ongoing pressure on overall portfolio yields.

Partially offsetting the impact of lower yields, our investment assets increased 5% from a year ago to \$4.3 billion. Our fixed income portfolio has an overall credit rating of AA minus and duration of 3.4 years including short-term investments. We continue to invest in corporate, high quality municipals and mortgage-backed securities.

We have an unrealized gain position of \$188 million pretax at December 31, 2012, up from \$150 million a year ago. The unrecognized gain position in the fixed income held to maturity portfolio was \$40.6 million pretax or \$0.48 per share after tax.

Surplus and stockholders equity remained at \$1.1 billion despite the impact of catastrophes. Book value per share increased 1.6% to \$19.77 from \$19.45 a year ago. All book values have been restated to reflect the adoption of the deferred policy acquisition cost accounting change on January 1, 2012.

Now I'll turn the call over to John Marchioni to review the insurance operations.

John Joseph Marchioni
President & COO

Thanks, Dale. Good morning. While Hurricane Sandy significantly impacted our performance in the quarter, events like this allow Selective to respond and demonstrate our excellent claim service capabilities. Selective employees in claims, flood and other areas of the company have worked tirelessly to assist customers and mitigate the impact of the financial losses to homes and businesses in expeditious manner, given the infrastructure damage caused by Hurricane Sandy.

Overall in 2012, we performed well with a 101% combined ratio excluding the impact of Hurricane Sandy. It was led by a strong 97.3% combined ratio of personal lines, driven by pricing success and our homeowner strategies to drive better cost sharing. In addition, the standard commercial lines combined ratio was 100.6%. Our granular pricing success along with underwriting initiatives drove the improvement in commercial lines.

E&S attracted one point from the overall combined ratio due to an elevated loss ratio and the acquisition related cost borne in 2012, but we fully expect these operations to improve substantially in 2013 and beyond. We completed our 15th consecutive quarter of positive commercial lines pricing with 6.7% in the fourth quarter. Momentum throughout the quarter was positive with December up 7.1%.

For the year, commercial lines pricing was up 6.2%. 2012 was our fifth consecutive year of personal lines price increases which were up 6.7%. Retention remains very strong with standard commercial lines at 82% and personal lines at 86% for the year.

Achieving price increases while maintaining strong retention levels demonstrates the success of our granular pricing strategy and the true partnerships we have with our agents. We provide our underwriters with specific policy level guidance allowing them to target the highest rate increases on the worst performing accounts while protecting retention on our best accounts.

In 2012, we obtained 13% pure rate on our lowest quality accounts and held point of renewal retention at 72%. We obtained a 5% pure rate increase on our highest quality accounts while they retained at 90%. We measure retention at point of renewal because by removing mid-term cancellations we think it best illustrates the impact of our pricing strategies.

The granularity of our pricing decisions will continue to drive mixed improvement as we earn overall rate increases in excess of loss trend. Commercial lines new business in the quarter was essentially flat with a year ago and for the full year was up 11% from 2011 levels.

After a very strong first quarter, we experienced the mixed new business market for the rest of the year. We have seen some competitors be fairly aggressive in one quarter and pull back in the next. Despite the inconsistent market for new business, we continue to use our sophisticated underwriting and pricing tools to identify and write the highest quality new business accounts at adequate pricing levels.

As a result, standard commercial lines new business in the fourth quarter totaled \$52 million, flat with a year ago. By market size, new business for the full year compared to a year ago was as follows. Small business was up 8% to \$74 million and middle market and large account business was up 13% to \$162 million. In terms of ongoing challenges, workers comp results remained under pressure turning into 114.5% combined ratio over 2012.

We are account underwriter and generally lead with the non-workers comp lines. However, we expect to get this line to an acceptable level of profitability as we continue to aggressively manage rates. In fact, the workers comp line saw the largest commercial lines rate increase for the year of 8%.

We are focused on changing the mix of business by writing more small, low hazard classes. We have also implemented a number of claims initiatives, including a more specialized adjuster model and proactive medical management to further address profitability.

Workers comp remains an industry wide challenge and in 2013, we expect renewal price increases in the 9% range and we will continue to execute on our underwriting and claims initiatives to address profitability. The personal lines underline a combined ratio for the year, was a profitable 97.3%. While catastrophes are clearly a part of our business, an increased activity needs to be priced into the rates

moving forward. We want to highlight the progress that we have made to overall rate increases in excess of trend, underwriting guideline changes and mix improvements.

We continue to drive profitability in the homeowners' line by offsetting weather related losses. We've driven rate across the book and made underwriting changes including raising deductibles to increase cost sharing. Additionally 2013, we have significantly tightened our underwriting appetite for model line homeowners.

As Dale noted, we expanded our property catastrophe treaty and our bi-payroll rating platform allows us to allocate this additional cost into our pricing structure at a very targeted fashion. We are pleased with the improvement we have experienced in 2012 and continue to refine our underwriting initiatives to generate further profitability improvement in this line. We are targeting a combined ratio in the high 80s in a normalized catastrophe year. For 2012, our homeowners' line produced a combined ratio of 91.2%. For personal auto, we have been consistently getting price above loss cost trend achieving 5.7% in 2012. We continue to increase the geographic diversification of our auto book and have made progress on increasing the age of the book from 3 to 3.2 years outside of New Jersey.

We believe that the continued rate action and ongoing improvement in the underwriting mix of business and maturity of the auto book will continue to drive improvement in this line for long term success. Results in 2012 for our E&S contract finding authority business are below our expectations, but we remain very confident in our ability to run this operation with a consistent underwriting profit. We expect the statutory combined ratio for E&S to be in the 100% to 102% range for 2013 and to be at a similar profitability level as our standard lines of business in 2014.

As Dale mentioned, results were negatively impacted in 2012 by a higher than usual expense ratio due to acquisition costs and a higher than expected loss ratio. Our focus to this point was getting the operations integrated, reviewing the portfolio and applying our best practices for underwriting in claims. Upon completion of a detailed review we've taken aggressive steps to address the underperforming segments. Pricing in the E&S binding authority market is firming and we expect that trend to continue through 2013.

Now I will turn the call over to Greg.

Gregory Edward Murphy
Chairman & CEO

Thank you, John and good morning. Although market conditions for new business remain challenged, we are pleased with the execution of our profit improvement initiatives and the positive impact that they have had on our 2012 results. That's catastrophe losses and reserve development, which modestly beat our expectations. We established a 3-year targeted statutory combined ratio of 95% by year end 2014. Looking at our results on a non-cat basis, we are on track to meet this goal because cat losses are inherently unpredictable and lately even more so, we believe it's best to examine our progress excluding these losses so each analyst can make their own weather predictions. Our 2014 95 combined ratio target becomes 92 after excluding 3 points of expected cat losses.

For 2012, our combined ratio, excluding cats and reserve development, improved 1.6 points to 98.8, driven by a lower loss and loss adjustment expense ratio of 66.2. The most powerful element in reducing the loss and loss adjustment expense ratio is generating price above the predicted loss trend. Our 3-year price target is 5% to 8%. For 2012 we achieved a 6.3% overall renewal price increase, 6.2% in commercial and 6.7% in personal, higher than our budget of 5.8%. Our overall earned renewal price for 2012 was 4.7% compared with a stable 3% loss trend. The quick math for combined ratio improvement is to multiply the spread between the earned rate and the loss trend times the 66% loss ratio, which in this case yield about 1.1 point improvement.

As John said earlier, we achieved renewal price increases due to our sophisticated underwriting tools and strong agency relationships. We're starting 2013 in a much better position than last year and we are confident that we should meet or exceed our multiple year pricing strategy. We anticipate overall pricing for 2013 between 7.5% and 8%, and our early January estimated renewals support commercial lines pricing in the mid-7% range. We deployed multiple claims initiatives to lower our loss and loss adjustment

expense ratio by 3 points over time. These expectations are part of our plan to reach a 92% ex-cat combined ratio by 2014.

The most significant initiatives include medical cost containment through extensive network renegotiations, enhanced nurse case management, sophisticated fraud and recovery predictive models, legal fee management and a complex claim unit. The complex claim unit handles large difficult liability and property claims with line of business specialists. Our overall objective for claims is to achieve the best outcome, while providing a positive customer experience. These initiatives will have the greatest impact on our workers compensation and general liability lines of business.

The continued extremely low interest rate environment imposed under an intense monetary policy by the Federal Reserve Bank had several significant impacts on our business. Some are beneficial, while others pose a challenge. The benefits are lower inflation that keeps loss trends down as well as reduce our cost of capital, which currently stands at about 8%, down from 10% 2 years ago. However, it presents a significant challenge in generating after tax returns in our investment portfolio.

For 2013 we believe our total portfolio after tax return will be about 2.2 points. At year-end, we had \$3.95 of invested assets per dollar of stockholder's equity that in 2013 should contribute almost 9 points to our return on equity. As fixed income investments mature and new money is invested at lower interest rates, additional pressure mounts to improve industry wide combined ratios in order to achieve targeted return on equity levels. For 2013 we expect a statutory combined ratio of 96 excluding catastrophes and any prior year development favorable or non-favorable; a 3 point estimate for catastrophe losses, after tax investment income of approximately \$90 million to \$95 million, and weighted shares of approximately \$56 million.

Now I will turn the call over to the operator for your questions.

Question and Answer

Operator

[Operator Instructions] Mark Dwelle, RBC Capital Markets.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Couple of quick questions, first on the guidance on investment income, the \$90 million to \$95 million that's simply the fixed income component, correct? That's not inclusive of any distributions from alternative funds?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

No, actually it's the all-in number. So basically you got ongoing pressure in terms of yield and you will see that kind of the yield rolling down. The alternatives obviously could come in higher or lower than what's included in our expectation, but that's the all-in number.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

So \$100 million this year and obviously we expect ongoing pressure on the thing. So if you look at 2011 we were at \$109 million, 2012 we were at \$100 million, so we are projecting that onward pressure.

Gregory Edward Murphy

Chairman & CEO

The only other thing I would add to that is that reflects the current interest rate environment. That's the line that we've snapped, so obviously if rates were to move higher, it would modify that projection. But as you know, it's only the roll over effect and the new money effect as that might elevate that number.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Okay, so that is after tax, however. So I would be comparing it to \$100 million after tax, 132ish almost \$132 million pretax, as the 2012 number to which I would compare that 90 to 95 range?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

Right; this is an after tax number that we are providing.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Okay, just making sure. The same question I wanted to hit. Greg, you were talking through a series of numbers and it seemed like a pretty important point, I just want to make sure I had it exactly right. You were talking about 4.7% earned rate increases and 3% loss trend and that triangulated to 1.1 point improvement in accident year combined ratio. Could you step through that math again real briefly? I just want to make sure I got it right, because it's pretty critical to your model.

Gregory Edward Murphy

Chairman & CEO

Sure. There is an actual way that you calculate it, but the quick math is, you generally take the -- so let's say our earned price is 4.7 -- you do that, subtract the 3% loss trend and that gives you 1.7 and then you multiply that by the loss ratio to give you a combined ratio impact. The actual way that you would calculate that is, you take your prior year loss ratio and you divide that by 1 over your earned price trend

increase times the inflationary trend that you have on our losses. It's the technical way you correct it, you calculate it, but I think it's a lot easier to do the quick math method.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

I like your way, that's fine.

Gregory Edward Murphy

Chairman & CEO

The easy way to do it, I have my actuary here, calculating it the way I...

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

He's got a slide ruler out.

Gregory Edward Murphy

Chairman & CEO

Yes. That's exactly right.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

Two other quick questions, one's just a number question if I may. I just wanted to make sure, on the overall prior period development for the quarter was \$2 million, 0.5 points and that was comprised of 2.7 favorable in personal lines and minus, I think it was, 3.1 in commercial lines?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

You are right. The total favorable was \$2 million for the quarter, and let me get to the breakdown here. So if you look at the -- hold on, I am getting there. So you've got workers' comp and general liability are both unfavorable by \$3 million. You have favorable in C&P of \$2 million, favorable in commercial auto of \$3 million, favorable in personal auto of \$1 million, favorable in homeowners of \$1 million and favorable in bonds of \$1 million. So all that nets down to your \$2 million. You've got roughly 0 on the commercial lines and about \$2 million favorable in personal lines when you net all those pieces out.

Mark Alan Dwelle

RBC Capital Markets, LLC, Research Division

One last question and I guess it's probably an observation and partly a question. It seems like when you are thinking about the overall Selective, exiting your margin improvement or margin improvement in general, you know it seems like there is a pretty important split between the standard or traditional business and then the impact that your reported results are going to have from the E&S as that gets up to whatever we call the right run rate speed. Is that how you are looking at it or are you really looking at it that the standard lines business has to kind of run a little faster to make up for the ramp on the E&S?

Gregory Edward Murphy

Chairman & CEO

I would say that our improvement in standard is pretty well articulated and we view it that we are going to ramp the E&S operation quickly to the same level or better and our profit improvement initiatives. You know they just have a lot more flexibility, they can change deductibles, they've got pricing, they've got a lot more bandwidth to make changes in E&S side than we do. So we would expect their improvement to get to our level in the next 2-year period.

Ronald J. Zaleski

Former Chief Actuary and Executive VP

I guess the way we look at it, Mark, is that they are both on a path for a 95, or call it a 92 ex-CATs in 2014. It's just that they have 2 different starting points, but they are both on that path to the same kind of an ultimate destination there. Although, obviously, we expect continued improvement beyond that.

John Joseph Marchioni

President & COO

And as you will see in the reported numbers, this is John, you will see in the reported numbers for the quarter versus what we put out there for next year of the 100 to 102 range, our ability to achieve loss ratio improvement in a lot more quick fashion because of the size of that book number. One on the E&S side but also because of the fact that it's got a much lower retention, E&S business does. So when you put a new pricing structure in place, it applies to your new business and your renewal business consistently and allows you to drive that improvement through a lot more quickly, realize the underwriting improvements are a lot more quickly in \$130 million book than \$1.2 billion. That's got an 82% retention level on it.

Operator

Your next question comes from Ray Iardella from Macquarie.

Christopher J. Maimone

Macquarie Research

This is Chris on for Ray. Just hoping to clarify, the commercial lines or at least or maybe the overall pricing increases that you mentioned earlier, that's baked into your guidance for 2013. Did you say 7% to 8% overall? Is that implied in the statutory 2013 combined ratio guidance?

John Joseph Marchioni

President & COO

Yes.

Christopher J. Maimone

Macquarie Research

Okay, and can you break that down between personal and commercial or is that as much detail as you can give?

John Joseph Marchioni

President & COO

Well, commercial lines, I will tell you, generally is in the 70 to 75 range. Personal line hangs in there about the same level.

Christopher J. Maimone

Macquarie Research

And then, I know you ran through the modifications, the property and casualty insurance program, would you mind briefly just repeating those points again if you don't mind?

Gregory Edward Murphy

Chairman & CEO

Sure, basically, we added an extra \$150 million layer at the top and then beyond that what we did was we increased the amount of placement on each of the underlying layers. So if you look at the co-participation percentage for 2012, we were at a 5% co-participation in the first layer and then 10 and 10 and the next 2 layers. So for 2013, we are now at a 3%, 4% and a 5% co-participation for those first 3 layers and then we are at a 2% co-participation on the brand new top layer. So the total for that is that we did end up, we will increase the dollar amount that we are seeding because obviously we are buying more reinsurance and we are participating less in the layers means there is going to be an \$11 million increase in seeded

premium for 2013 versus 2012. And that means that we have basically the combination of all that is we have increased the total limits placed by 43%.

John Joseph Marchioni

President & COO

This is John, the other thing just to add a little bit more context to Greg's comment to the commercial lines number of AB1 [ph] prices are [indiscernible]. So when you think about that loss ratio improvement, you are going to want to temper that a little bit, [indiscernible] in 2012 so it will drop it a little bit in terms of the earned rate for 2013.

Christopher J. Maimone

Macquarie Research

Got you and maybe going back to the implied pricing expectations for the combined ratio guidance. Are you guys basically baking in just the current run rate of pricing increases to get to that number? You are not expecting any acceleration later in the year?

Gregory Edward Murphy

Chairman & CEO

We are baking in our expectations for 2013.

Christopher J. Maimone

Macquarie Research

I will also comment when you saw how we outperformed relative to our budget. So that's our expectation and we will move with the market if things change during the course of the year. So our prepared comments that our budget was about 5.8% and we came in at 6.20 for commercial lines overall. So you saw how we did move higher than the market -- so higher than our budget. So we will modify that as we move forward if we can.

Operator

Your next question comes from Alison Jacobowitz with Bank of America Merrill Lynch.

Alison Marnie Jacobowitz

BofA Merrill Lynch, Research Division

I have just -- but most of my questions has been talked through with the last couple of questions, but I just want to just clarify maybe how you are looking at timing. So the 96 ex-cat combined ratio going to the 92 for 2014, I assume you mean that the 92 will happen maybe more gradually throughout the year and it might be something by the end of year that we saw in 2014. Is that the right way to look at it?

Gregory Edward Murphy

Chairman & CEO

No, it's a full year combined ratio for 2014.

Alison Marnie Jacobowitz

BofA Merrill Lynch, Research Division

So you are thinking then for 2014, ex-CATs we could see a 92 for the full year if you are on budget?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

That is correct, yes.

Operator

Your next question comes from Ron Bobman of Capital Returns.

Ronald David Bobman

Capital Returns Management, LLC

I had a couple of questions. For starters, the \$136 million gross Sandy loss, and how does that split between personal and commercial?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

It's 55% personal lines and 45% commercial lines in terms of loss dollars.

Ronald David Bobman

Capital Returns Management, LLC

Gross loss dollars.

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

Yes, excuse me, the other way.

Ronald David Bobman

Capital Returns Management, LLC

I'm sorry, 55 in commercial lines?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

55% commercial and 45% personal.

Ronald David Bobman

Capital Returns Management, LLC

So commercial is more?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

Yes, slightly more.

Ronald David Bobman

Capital Returns Management, LLC

Okay. And you made a point of sort of reminding us, unfortunately, obviously, the Sandy number. I guess it grows to 136 as an increase in the 100 to the 120 which was your original estimate, which is -- not to take this question critically, but what I'm trying to ask is, what deviated in the underlying areas, was it a greater number of claim counts that continued to come in, was it the greater severity? Would you add a little bit description as to sort of what you learned since the initial estimate date that prompted the increase?

John Joseph Marchioni

President & COO

Yes, this is John, I'll respond to that. I'll start. So we've got a pretty disciplined process around projecting catastrophes as they happen, and obviously in an event of this magnitude and when you think about the infrastructure damage and the amount of time that some properties were not even able to be gotten to by the owners of the property, that certainly adds to the reporting timeframe. So with the experience we've had over the last couple of years, unfortunately, it has allowed us to refine that process and project it. So we will project overall claim counts that we expect to get over time. We'll project the percentage of those claims we expect to be closed with payment and close without payment and we continue to fine tune that as actual claims get reported over time and sit down and go through that on a weekly

basis. I will say on this one, though, in addition to the ability to physically get to properties, the business interruption component of this particular loss and off-site power failure and how that impacts or doesn't impact business interruption has added to the complexity and I think taken a little bit longer in terms of the claim settlement process. So I would say all of those factors as we look at them, as the catastrophe event matures, we continue to fine tune it as the actual data starts to come through.

Ronald David Bobman

Capital Returns Management, LLC

So should I assume that the increase was A, particularly concentrated on commercial lines and that it's somewhat severity related to BI or and again I -- don't take this critically, I'm just trying to understand where was it centered as far as the increase.

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

I think what you saw was certainly there was a little bit of what you just articulated, the severity came up a little bit, there was a little bit more on the BI. But also quite frankly just the claim reporting period lasted a little bit longer than we expected it. I mean we are basing our projections off of what we saw with Irene and how that developed and what percentage of ultimate losses had come in by a certain date. This reporting period just drug on a little bit longer than we expected, so we had to update our estimates.

Ronald David Bobman

Capital Returns Management, LLC

Okay. And would you the [indiscernible] sales in personal lines claims, could you split that between auto and home for us, please.

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

We don't. Although we have that internally, we haven't released all that information.

Ronald David Bobman

Capital Returns Management, LLC

Because what I heard in the prepared remarks will answer any Sandy questions, but I will say that a little bit in jest. Actually, one more question about the reinsurance, how come you opted to co-participate less, I can totally understand the buying of a higher tower but what's prompting the reduction in your co-participation? Obviously you could have stayed the same, you could have said we are going to keep more now because rates are picking up at maybe a little greater rate. What's prompting the reduction in co-participation?

Dale Allen Thatcher

Former Executive VP, Treasurer & CFO

We just felt that the overall reinsurance coverage that we had was an appropriate amount to buy. We had the availability in the marketplace to be able to achieve that kind of higher co-participation and it just benefited our overall risk management as we looked out and ran the various numbers.

Operator

[Operator Instructions] At this time, there are no further questions.

Gregory Edward Murphy

Chairman & CEO

All right, if you have any follow-up matters, please contact Jennifer or Dale and thank you for participating in the call.

Operator

This does conclude today's conference. Thank you for attending. You may disconnect at this time.

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