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The Hanover Insurance Group, Inc. NYSE:THG

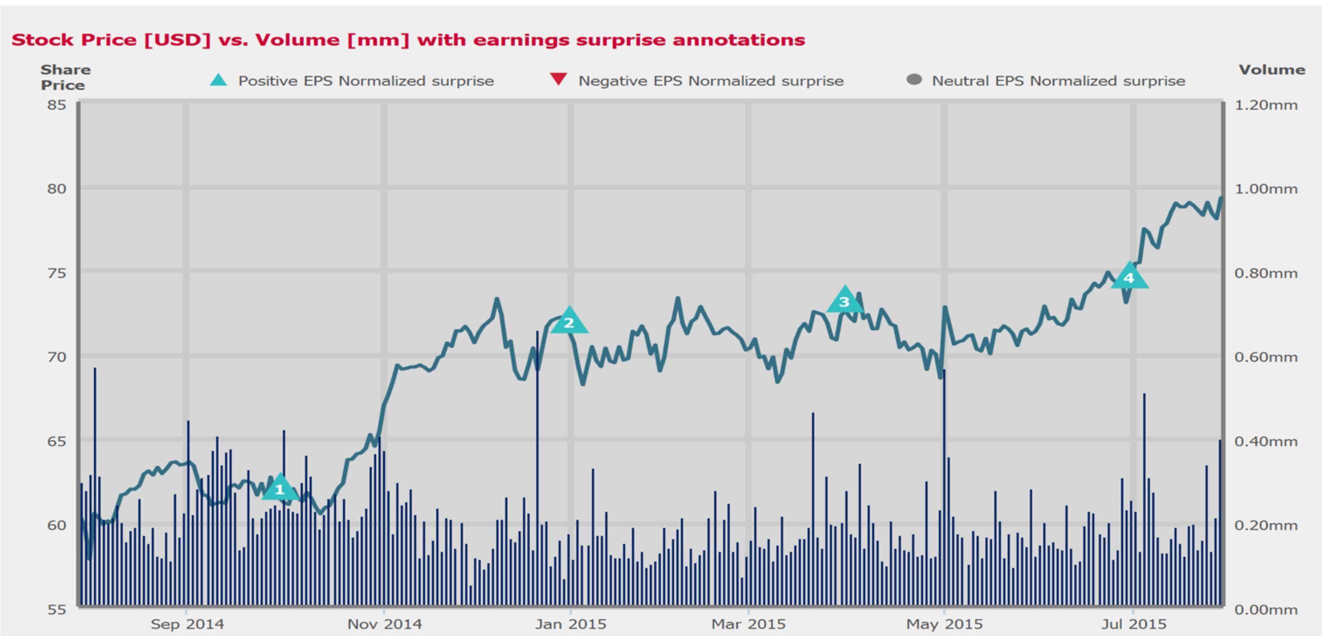
FQ3 2015 Earnings Call Transcripts

Thursday, October 29, 2015 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ3 2015-			-FQ4 2015-	-FY 2015-	-FY 2016-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.45	1.61	▲11.03	1.60	5.93	6.29
Revenue (mm)	1214.70	1199.60	▼(1.24 %)	1076.40	4784.00	4814.20

Currency: USD
Consensus as of Oct-29-2015 1:46 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2014	0.91	1.06	▲16.48 %
FQ4 2014	1.50	1.77	▲18.00 %
FQ1 2015	1.08	1.27	▲17.59 %
FQ2 2015	1.40	1.56	▲10.64 %

Call Participants

EXECUTIVES

Andrew S. Robinson
Former Executive Vice President of Corporate Development and President of Specialty Insurance

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

John C. Roche
President of Hanover Agency Markets

Oksana Lukasheva
Vice President of Investor Relations

Richard W. Lavey
Chief Growth Innovation Officer

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Charles Joseph Sebaski
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Piper Jaffray Companies, Research Division

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Janney Montgomery Scott LLC, Research Division

Matthew John Carletti
JMP Securities LLC, Research Division

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

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Quarter 3 2015 The Hanover Insurance Group, Inc. Earnings Conference Call. My name is Mark, and I will be your operator for today. [Operator Instructions] As a reminder, this call is being recorded for replay purposes.

I would like to turn the call over to Ms. Oksana Lukasheva, Vice President of Investor Relations. Please proceed, ma'am.

Oksana Lukasheva
Vice President of Investor Relations

Thank you, Mark. Good morning and thank you for joining us for our third quarter conference call. We will begin today's call with prepared remarks from Fred Eppinger, our President and Chief Executive Officer.

Available to answer your questions after our prepared remarks are Andrew Robinson, President of Specialty Lines; Dick Lavey, President of Personal Lines; Jack Roche, President of Business Insurance; Bob Stuchbery, President of International Operations; and finally also with us in the room today is our Interim Chief Financial Officer, Gene Bullis.

Before I turn the call over to Fred, let me note that our earnings press release, financial supplement and a complete slide presentation for today's call are available in the Investor Section of our website at www.hanover.com.

After the presentation, we will answer questions in the Q&A session.

Our prepared remarks in responses to your questions today, other than statements of historical fact, include forward-looking statements, including our earnings guidance for 2015.

There are certain factors that could cause actual results to differ materially from those anticipated by this press release, slide presentation and conference call. We caution you with respect to reliance on forward-looking statements, and in this respect, refer you to the Forward-Looking Statements Section in our press release, Slide 2 of the presentation deck and our filings with the SEC.

Today's discussion will also reference certain non-GAAP financial measures such as operating income, operating results excluding the impact of catastrophes and accident share 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 or the financial supplement which are posted on our website, as I mentioned earlier.

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

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Thank you, Oksana, and good morning, and thank you for joining our third quarter earnings call.

Before I discuss our quarterly results, I'd like to take a moment to express our deep sadness at the sudden passing of David Greenfield, the Hanover CFO, a little over a week ago. I'm sure that those of you that had the opportunity to work with David will remember as a consummate professional and a wonderful person. We will remember him as a strong leader, a thoughtful friend and a tireless mentor to many people in the organization. He had a lasting impact on our company and our people. We are thankful to all of you who have shared your wishes and prayers with us over the last several days, and our heartfelt condolences go out to his family.

I would like -- I would now like to provide you with some thoughts on the third quarter strategic progress and review our results by segment. I will then discuss our outlook and conclude with an update on the executive search and succession planning.

Starting with the third quarter results. We had a strong quarter and performed in line with expectations, with solid earnings in both our Chaucer and domestic businesses. We delivered an operating income per share of $1.61, up 52% from $1.06 in the prior year quarter.

Our overall combined ratio was 94.9%, and excluding catastrophes, the combined ratio was 91%.

Most importantly, we delivered an operating ROE of 10.8% for the quarter and 10.2% year-to-date. We are pleased with our results, and we remain on track to achieve our financial goals for the year and have visibility to continued improvement into 2016.

Along with our financial results, our key metrics and business indicators are tracking in line with our expectations.

Specifically, domestic business grew by 5%, led by Commercial Lines with improved retention and consistent pricing increases, which should lead to future increased profitability. Underlying results in these businesses improved in line with our expectations, while lower overall catastrophe losses in the quarter were offset by some non-catastrophe property and prior-year large loss activity.

Operating results at Chaucer remain strong, as we benefit from our strong market position and underwriting expertise. At the same time, growth at Chaucer was subdued as the result of market conditions.

We actively and effectively managed our capital during the quarter. We repurchased $22 million of high coupon debt and $87 million of shares between the end of June and October 27, which almost exhausted our old share repurchase authorization. The board also increased the authorization by $300 million.

I will now review our financial results in more detail as well as the progress we have made in each of our business segments, starting with Commercial Lines.

Each of our Commercial Lines businesses grew in the quarter, resulting in overall growth of 7%. We continue to capitalize on the opportunities within this business segment, successfully navigating what remains a relatively healthy market.

In Small Commercial, which is key to our long-term business strategy, we have seen increased traction throughout the year, particularly in the third quarter. The business as a whole is maturing nicely as we substantially improve our business mix with more territories now contributing meaningful to growth, while we continue to gain attractive shelf space with the top agents of the country through market consolidations.

With our Small Commercial offering, we've carved out a unique position in the market between large nationals and small regional companies. We are able to offer the best of both worlds to a select group of agency partners. This includes a broad product offering, ease of use, local underwriting expertise, proprietary coverages, and a world-class service center.

Our distinct operating model allows us to cost effectively target and underwrite the point of sale and non-point of sale Small Commercial market. Our strategy of limited distribution, distinctive product offering, local presence and business insights enables us to build and strengthen the segment as a driver for sustainable growth. Overall, we are very satisfied with the momentum in Small Commercial business with mid-80s retention and high single-digit new business growth.

Middle market also performed well in the quarter. We grew nicely as our profit improvement initiatives wind down, our retention numbers strengthen, and the agents turn to us more actively for new business. The market overall remains competitive, as evident in recent industry pricing surveys. And while we are not immune to this environment, we believe our small account size and agency-centric strategy enables us to better hold rates.

Our Commercial Lines pricing held at 5.4% in the third quarter, while retention improved approximately 1 point to 84% compared to the prior year quarter.

In Specialty Lines we grew by 7% in the quarter. We continue to build scale and presence in areas where we have strong differentiation and unique capabilities that allows us to gain access to agents' most profitable businesses.

Turning to Commercial Lines profitability. Through our efforts in both rate and business mix management, we were able to drive additional underlying improvement in the loss ratio for most lines in the quarter. An increase in loss ratio in other commercial lines reflects some expected volatility in property lines, which consistently have delivered very strong levels of profitability.

We sustained less catastrophic losses than expected, while we experienced unfavorable prior year loss development in the quarter. We are still reporting some unfavorable development in commercial auto and within our Commercial Lines driven by the auto losses. This is an area where we've made significant progress on, and we are seeing meaningful improvement. We will continue to take a very conservative position given the market environment. But overall, results remain in line with our expectations.

Additionally, we reported unfavorable prior year development in CMP, where last year and recent trends have been flat to slightly favorable. We experienced an occurrence of some large loss activity from existing liability claims in the last couple of accident years. As you know, we take a conservative approach when we see this type of activity. Therefore, we took steps to recognize this in the quarter.

We will continue to keep a close eye on this line of business going forward, but we remain comfortable with the overall profitability of this business.

Expense ratio improved by over 1 point compared to the prior quarter to less than 36%, due in part to a favorable timing in recognizing certain expenses. We remain on track to deliver approximately 1 point of expense improvement in Commercial Lines for the year.

Moving on to Personal Lines. We generated modest growth in the quarter of approximately 1% as rate increases held at 5% for both auto and home. We made further improvement in retention, which at 82% was up almost 1 point compared to the same period last year. We expect to see some continued increase into 2016 as we work through some of our monoline and agency management actions.

The Hanover Platinum offering continues to set us apart in the eyes of our best partner agents, helping to build upon our position in the bundled account sector. We remain keenly focused on future growth by utilizing multiple levers to further enhance our position with our best partners. We continue to work on agency engagement programs and operating enhancements, as discussed last quarter, as well as build upon our strong capabilities in the higher end of our current appetite. We expect that these initiatives will allow us to improve our growth rate in 2016.

We continue to see benefit of ongoing pricing and underwriting actions in the underlying loss trends. With the third quarter combined ratio of 94% and 89% excluding catastrophes, we remain substantially on track to deliver bottom line improvements we targeted in Personal Lines for the quarter and for year-to-date.

Catastrophe losses were lower than our third quarter long-term average for Personal Lines. And this was offset by some higher-than-unusual severity of large losses, primarily fire in the homeowners line, particularly in the month of July, which can be uneven month-to-month and quarter-to-quarter.

Personal auto performed well, generating an accident year loss ratio fundamentally in line with the lower-than-usual third quarter 2014.

Along with the rest of the industry, we too are seeing an increase in auto severity, primarily in the property coverages associated with the high cost of repairs, due to more complex and expensive accident avoidance technology equipment in the newer car models.

Others in the industry have also noted a significant uptick in physical damage and collision frequency. Though our mix of business insulates us somewhat from this trend, we do not exclude a possible impact in the future given the macro economic factors, including the improving economy. We remain very confident that we can continue to hold pricing at levels above loss cost and deliver improved results.

Finally, the Personal Lines expense ratio was in line with our expectations of 28% for the quarter.

Turning to Chaucer. Our Lloyd's segment delivered a strong performance in the third quarter with a combined ratio of 87%, despite continued competition in many lines of business. This result reflects the breadth and balance of our underwriting portfolio and the strength of our underwriting expertise. Catastrophe losses in the quarter were $12 million, which included the Chinese port loss estimated at $19 million as well as favorable development on prior period events.

Non-cat losses also developed favorably in the quarter, resulting in a release of $32 million from prior year reserves.

Net written premiums were down 4%, excluding the impact of the foreign exchange translations in the transfer of the U.K. motor business, which was completed last quarter.

The Lloyd's market remains challenging and we continue to be thoughtful in our approach, leveraging our strong market position and strong underwriting capabilities to manage our portfolio mix to maximize our financial returns. We continue to find attractive opportunities in areas like the U.S. casualty business as well as marine, including political risk and political wile.

Additionally, we continued to invest in business capabilities and talent. For instance, we recently acquired a specialist U.K. cargo and freight liability underwriting team that specializes in smaller-sized risks, which will enhance our existing marine practice capabilities. We will continue to look for additional business development opportunities that support our specialty focus in the future.

Overall, we are very satisfied with the underwriting results in all of our businesses in the quarter and remain confident in the strategic direction of each going forward. And we believe we are on track for continued earnings growth for the remainder of 2015 and into 2016.

Moving on to our investment results. Cash and invested assets were $8.4 billion at the end of the quarter, with fixed income securities in cash represent 89% of the total. The portfolio remains high quality and well laddered for a changing rate environment.

We increased net investment income by 1% in the quarter to $68 million, despite transferring $385 million of the portfolio as part of the U.K. motor exit in the second quarter of 2015. Higher operating cash flows and slightly increasing total portfolio yield helped us offset the reduction in these investment assets.

Book value per share grew roughly 0.5% to 66.55% in the third quarter. Book value per share, excluding net unrealized gains on investments and derivatives, increased approximately 2% for the quarter, reflecting our strong earnings. Our total capitalization is $3.7 billion.

During the quarter, we continued to actively manage our capital. We opportunistically purchased almost 800,000 common shares, benefiting from the recent market volatility. Year-to-date, we've spent over $110 million on these repurchases, paying an average cost of $77 per share. In addition, we also purchased about $22 million of debt in the quarter.

Additionally, our Board of Directors increased our share repurchase program by $300 million. This reflects our board's confidence in the company's financial condition, ability to further improve returns and our commitment to deliver shareholder value.

Overall, we are proud of our third quarter results, and we have achieved -- and what we have achieved in the year so far and remain on track for continued earnings growth in 2015 and 2016. Our strong market momentum built on our unique agency distribution strategy, broad and innovative product offerings and well-rounded talent positions us well to continue our momentum.

Based on our third quarter results and trends, we remain on track to achieve our EPS targets for the year. And given we are entering the fourth quarter, we are narrowing our guidance to the top end of our range to $5.85 to $6 a share for the year, including an assumption of approximately 4.5% for catastrophes in the fourth quarter.

Before I open the line for your questions, I would like to comment on our transition planning. As announced in September, I will be retiring from The Hanover in mid-2016. Although my decision comes with mixed emotions, the Hanover franchise is stronger than ever and is well positioned for future success. As I mentioned earlier, I'm fully committed to stay on board as long as needed to ensure continued progress and a smooth transition. And our team remains very focused on maintaining our strong momentum and earnings growth.

As you may know, our Board of Directors has initiated the search and is looking to name a new CEO as soon as practically possible, and I'm excited about assisting in this effort. However, it's an important decision for the company's future, and the board is going to be thoughtful and deliberate in choosing a successor. We will update everyone as appropriate, but at this time, we do not have any further information to report.

Turning to the CFO position. As you know from our press release last night, Gene Bullis, who is the CFO of The Hanover prior to David, will join us to lead our finance team until a permanent successor is named. I am very pleased to have Gene back with the team, and I look forward to working with him over the coming months.
I would now like to open the lines for questions. Operator?

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Matt Carletti, JMP Securities.

Matthew John Carletti
JMP Securities LLC, Research Division

I had a couple of questions. First one, kind of 30,000-foot relating to the pricing that you're continuing to be able to get, the kind of 5-plus percent both in Commercial and Personal. I'm just curious, your views as to why you guys have been so successful and continuing to get kind of mid-single digit pricing ahead of loss costs, when a lot of your larger peers have struggled to do so and have -- kind of a lot of their rate increases have -- they're still positive but certainly shrinking and questionable whether they're still ahead of loss cost?

John C. Roche
President of Hanover Agency Markets

Yes, Matt, this is Jack Roche, I'll speak from a Commercial Lines perspective and kind of be redundant with what we've said in the past. And we really believe that we're starting to fully appreciate the benefits of our strategy and the 3 dimensions that we think contribute to that pricing result. First is our agency strategy, right? We are very close with our distribution. We work hard to deliver value to them. And I think the inclination is to not move business unless they absolutely have to. And we've created a lot of value with that distribution. We've also focused primarily on the small- to mid-sized accounts. And as everybody knows at this stage of the cycle, the upper middle-market is being a little over-appreciated from a pricing standpoint, and we believe that our account size, and even within that, the sectors within the market that we focus in on are just a little less price sensitive. And then, last but not least, we have built a lot of product differentiation, a lot of segmentation, a lot of fringe coverages, a lot of expertise that I think makes it advantageous to retaining our renewal book.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Dick, do you want to add?

Richard W. Lavey
Chief Growth Innovation Officer

Yes, so this is Dick Lavey. For Personal Lines, it's a similar story, right? The strength of our agency relationships helps tremendously. We have really deep insight and transparency into their books of business, and we work together. The strength of our product offering and our service offerings, the platinum experience, also helps, right, to sustain that level. I think it's a coveted the offering in the market. So you couple our capabilities along with our distribution intimacy, and I think that helps explain it. The fact that we're targeting the middle market account customer, not the bottom end of the monoline auto business, obviously sort of helps to sustain that pricing level.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

You had another question, correct?

Matthew John Carletti
JMP Securities LLC, Research Division

I do, yes. And the another one, just on the buybacks. I mean, it's been ramping up nicely through the year. I think it was 100,000-ish shares Q1, 200,000 in Q2. It was almost 800,000 in Q3. I obviously recognize the $300 million repurchase authorization that was just announced. Can we look at Q3 as kind of a more normal run rate? Is there something in the quarter that made it higher or lower than we could expect? Any guidance there would be appreciated.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, Matt. So this is Fred. If you think about it, we think about capital mostly, first and foremost, dedicated to profitable growth and generating shareholder value that way. But what happened -- a couple of things this year, right? We obviously sold the U.K. motor book, and we've had very good earnings. And we've been able to have excess capital. And we always are thoughtful about how we deploy it. We have done, as you know, through the year, about -- I think it's $90 million of debt repurchase as well. But we felt, with the excess capital, it was appropriate for us to take advantage of the volatility that we saw in our stock to move forward on the share buyback. So I think our last trend will continue -- our trends where we are now will continue for a while, but you'll see as kind of assess it the way I just described going forward with those kind of priorities, first, about profitable growth, but if we have excess, we'll always be thoughtful about buying opportunities when we see them.

Operator

Your next question comes from the line of Charles Sebaski, BMO Capital Markets.

Charles Joseph Sebaski
BMO Capital Markets Equity Research

I guess the first question I have is, I just would like some additional color on kind of penetration. Obviously, the growth from the Commercial and Personal Lines is looking good. And I'm just curious if this is kind of coming through the penetration effort that you guys have made? Or is this coming more through exposure growth of current policies? I'm just trying to get a handle on how that's coming along on of a more strategy basis.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, so let me -- and I'll hand it to both Jack and to Dick. Obviously, we've shared in public forums that there are 2,300 agents -- 2,200 agents in the 2,600 locations. And we, obviously, are pretty detailed how we both work with those and plan with those folks. We also talked about how we now roughly $4 billion with the top thousand, and we've had really good penetration. And so what we're looking at is share by agent in categories, and we believe we're seeing really good -- some share shift to us in both Personal and Commercial and Specialty with our partners. And I would ask Dick and Jack and Andrew to elaborate on that.

Richard W. Lavey
Chief Growth Innovation Officer

Yes, absolutely, I mean. We look at our performance, and we do see our relationships deepening. And based on our strategy, that's essential, right? Now market share doesn't move month-to-month, quarter-to-quarter, so it is sort of a sustained little bit of a longer runway. But as Fred point out, we have such great knowledge and we understand perfectly what our share and our penetration is agency by agent, and we obviously, spend energy and effort in places where we see that potential upside. So for the Personal Lines of business it is about a share and a penetration story. We have some new appointments as part of our strategy, but it is more about penetration of existing distribution.

John C. Roche
President of Hanover Agency Markets

Yes. And this is Jack. I think I would build on it. If you look at, for example, in our Small Commercial business that Fred was referencing earlier, clearly, what we're seeing is broader penetration, more success with more agents. Let's face it. The strong retention in pricing we get doesn't hurt, right? You're building off of a very solid base and historically high base, and we're getting more new business from more partners at deeper levels. So that -- we believe that is building, and that even as we look into some of the middle-market areas, which is a little bit more selective -- and Andrew can speak to the Specialty -- we're getting more support and more help from more people as we -- as these relationships mature.

Andrew S. Robinson
Former Executive Vice President of Corporate Development and President of Specialty Insurance

Yes, this is Andrew. Just one additional point. We have gained such intelligence and knowledge through our partnership with our agents. Much of what we do in terms of new product launches is geared in a way that we know exactly who we're going to bring it to and the speed in which we're able to build positions in the specialty world, one recent example is what we've done in Allied Healthcare. The momentum that we've gained and the speed that we gained around that product launch is directly attributable to the knowledge and the partnership and the intimacy we have with our distribution. I think that, that's one of the unique qualities that obviously translates into a more substantive share of their book. And so I think that, that's another attribute that's true in all of our businesses in different ways.

Charles Joseph Sebaski
BMO Capital Markets Equity Research

All right. On the Personal Lines then, when I look at the 1% growth relative to the pricing and the retention, I mean, obviously, it's positive, but I guess, I would've thought 5% rate plus increase in retention might have had growth a bit higher. And I'm just wondering, if it's an exposure issue or if it's discount or just what's -- how the growth you think of it relative to that rating story and retention increase?

Richard W. Lavey
Chief Growth Innovation Officer

Yes, so this is Dick. Yes, so we are not undertaking an increase in exposure management, but as Fred mentioned, we still are working off some of the monoline issue and some standard agency management work that is, frankly, just good hygiene. So you do have some of that working through the book, the mechanics of it all. We do feel good. We feel good about our position, our retention, the rate that we're pushing through. Our account business, when you look underneath it, is growing. That PIF is growing year-over-year. And as you know, that's a core focus of our strategy. And we're staying disciplined, right? So we do have in some of our bigger states some competition that I would argue is not as disciplined on pricing, and we continue to be disciplined. So you do see some PIF challenges on the new business side of things. So it's a core focus of ours as we continue to invest, strengthen our offering for that middle market account customer, building out some of the product availability. So it's not a very specific movement off of the books.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, Chuck. I think it's a good observation you're making, Chuck, because -- and if you look, there's probably a couple of points of retention here continuing to run off some of the monoline from our legacy book that we think is less attractive. And so that drain, we believe, as that reduces, what you're going to see is, to your point, that's going to gravitate up. The growth is going to gravitate up.

Richard W. Lavey
Chief Growth Innovation Officer

That's right. We're sitting at, call it, an 82 retention, and we would see an 84, 85 is ultimately what our retention PIF would be.

Matthew John Carletti
JMP Securities LLC, Research Division

Excellent. And then I guess just finally, Fred, from a timing standpoint -- obviously, this is new and unfortunate with David's unfortunate passing. But do you guys need to name a successor for you, Fred, before a permanent CFO? Does that conceptually make more sense for?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, I think, if you think about it, I think there is some attractiveness to that sequence. But I would also say, Chuck, that there's a lot you can do in parallel. And so as I've talked to people about my position and the excitement about -- there are a lot of terrific people that I think are going to be excited about the position. There were some things on the CFO side as well that we can do in parallel. And as you know, because of some of the things going on in the industry with changes and consolidation, there's a lot of good candidates. So my view is that there is merit to that kind of sequence you're talking about. But there will be a lot of parallel work to be done, so we'll be able to move pretty quickly. And Gene has been kind to join and will be here until we need to make the change.

Operator

Your next question comes from the line of Meyer Shields, KBW.

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

Fred, you mentioned something that I thought was -- when you're talking about personal auto, you said that you're not immune from external trends, which is fair, and you still can anticipate an uptick in frequency. Why would you see it in the future if you haven't seen it yet, given that all of these macro issues are there?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

That's a great question. What we're saying is we're trying to be thoughtful about the difference between our rate and our trend and continuing to take the rate. Obviously, one of the interesting things is our mix is different. And we would also say, if you look at the data in the industry, a lot of that is coming from California, Texas and Florida, where we're not in. So we feel pretty good about where we are, right, Dick?

Richard W. Lavey
Chief Growth Innovation Officer

That's right. So I think what Fred is saying is our geographic mix sort of insulates us from this a bit, and our account mix, right, the fact that we have strong account. And you're seeing some of this frequency pop in the lower and the monoline auto business, which is not core to our strategy. So I think we're watching it closely. For us, it is definitely more of a severity trend, but in all cases, our pricing is comfortably above our lost cost trend.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, yes. And in some ways, it helps us, right, because everybody's talking about price increases. And we've seen a lot of action from a lot of people, which is insulating us to be able to kind of sustain what our growth strategy is, which is more of a steady state increase.

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

Yes, that makes perfect. I was -- this is insignificant from a financial standpoint. But we've had quarter after quarter of adverse commercial auto development. Is that new information or just a reflection of when you do the reviews or something else? In other words, why isn't there just sort of like a one big charge to reflect that?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, we -- I'll hand it to Jack in a second here and talk about it. But this is a place where we've been at pretty aggressively. We think we're on the other side of it. We like what we're seeing as far as it's unfolding. In our recent accident years, we've done a lot on mix. We've done a lot on pricing. But what we're doing is we're basically reacting to any prior year activity and just taking it to the bottom line, and we have done that. And we think it's a conservative thing to do because of all the noise in the marketplace, but we feel pretty darn good about where we are on the progression of going after this issue. And as I said, the net for us as we look forward is -- all of this stuff is kind of within our expectations as when we talk about increasing earnings as a company. So everything is kind of in expectation so far. So Jack, is there anything else you...

John C. Roche
President of Hanover Agency Markets

Yes, I think the question is a valid one in that -- and I think what we've talked about in the past is that this is a new phenomenon, and so the industry has been chasing this is a bit. I think you saw, even in this quarter, some folks that may be a little bit late to the party in understanding this dynamic. Predominantly you have 2012, 2013 elevated BI severity, accentuated by litigation in the major Metro areas. So the issue is, I think, relatively well understood now. Different people are at different points in understanding it or identifying it or addressing it. But the reason why we haven't put up a big charge is because we're chasing a trend here, and you don't know until you get to the top of it whether you're at top of it. And so we haven't tried to over react to it, but we're certainly -- got a great alignment, the best alignment we've ever had between underwriting claims, actuarial and our finance group, so that we're constantly assessing where we think we are. The good news that we do want to share is that we think that accident years 2014 and 2015 are looking a lot more stable in terms of our original picks versus what we're seeing in our development there. We're feeling better than ever about the hangover from '11 to '13. The claims inventory of soft tissue cases is clearly coming down. And so we have less claims to worry about in that development cycle. But also, I think the good news in this is that because this issue continues to persist, the pricing environment is staying relatively disciplined. And given the prop of challenges that we continue to see in some of our competitors, we expect that the auto pricing is going to hang in there for a while and that should allow us to work through this thing quite nicely because the returns still need to improve.

Operator

Your next question comes from the line of Larry Greenberg, Janney.

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

Fred, I'm just wondering if you could give us more color on why this was the right time for you to step down. Obviously, there's been a lot of speculation in the media as to what drove the announcement. So I'm just looking to hear from you a bit more on this so you could maybe set the record straight.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Sure. Sure. It's not very exciting, though. It'll be 13 years when I step down. That's roughly 2.5x the average CEO. And I just felt it was time in a lot of ways. We've worked hard as a group to get the place in a place as strong as it is. I've got, I believe, the best leadership team in the industry, and we have great business leaders in place and functional leaders in place. Our strategy is kind of really moving forward in a very strong way with a lot of momentum and a lot of insight into how we'll continue to do so into '16. So for me, I just felt it was a good time to step back and let somebody else kind of take the next up. And I think I'm excited about the opportunity to do that. But there is no real -- there is no magic to it. It's been, obviously, something I've loved to do, and I have a lot embedded in this institution and a lot of energy and a lot of hours. But Patty and I felt this was a good time to really kind of step away and let it go to the next step without us. So again, I've committed to -- I gave the board a lot of time, and I'm working hard with them to make sure that we take the right next step with the right people. But there really is no intrigue to it, to tell you the truth. And I would tell you that, when I said to my kids that I was going to get to spend more time with them, I didn't get as positive a reaction as I thought, but I'm not reconsidering it.

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

I appreciate that. And then, your Chairman, in an interview talked about potential international expansion. And I'm just wondering if you could give us your thoughts on where Hanover stands in the M&A landscape. Obviously, there's certain geographies in the U.S. where I know you'd maybe like to be. But maybe just a big picture view on that.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Sure, Larry. It's a good point because I think there was kind of a misquoting in that article. What we are saying is that we're constantly looking for opportunities. We just brought in a team at Lloyd's in a category that I mentioned in my script. We're constantly looking for the ability to expand our Specialty capabilities at London, and I think he was probably referring to that. But there is no big plan to go kind of beyond kind of the way we've been doing it to date into some kind of different focus internationally. What I would tell you is, as I've said before, we did a lot of transactions in a kind of 3 to 4 year period as we really built our portfolio. Where I'd say we are now -- and we're looking at a couple of small things right now. Where can we enhance our capabilities? Where can we fill in, to your point, that kind of enhances our position? But the need for a transaction to change or transform the company is really -- we really don't need that. But we are constantly looking for an ability to enhance our capabilities in various areas, and we'll continue to do that. I don't personally see anything -- big, significant thing on the horizon or anything like that. It's not something in our need. What's really nice right now is that our organic growth potential is pretty significant across our footprint. And so I think that's going to be where most of our effort is. But that's kind of the story of where we are right now.

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

Great. And then just finally, in both Commercial and Personal Lines through 9 months, if you look at your underlying loss ratios, they both improved about 0.5 point versus 9 months a year ago. Is that a good barometer in your view? Or might there be any non-cat weather noise or other noise in there? Or is that fairly well representative of where the underlying improvement is at right now?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, I think -- again, I think there's a little bit of noise with large losses, particularly in the property side of Personal Lines that we talked about and a little bit of the same, actually, property losses that we saw in some of our really attractive businesses -- HSI, marine -- that were a little noisy. And so I think you're going to see a tad more improvement than that as we go to the end of the year. And as I said, I think our outlook for the year is kind of we're on track to what we said at the beginning of the year. And I think we'll end up at kind of in the range I talked about in the script. So I feel we have -- a little bit more improvement than that would show, and I think we have more to go, more to come, too.

Operator

Your next question comes from the line of Dan Farrell, Piper Jaffray.

Daniel D. Farrell
Piper Jaffray Companies, Research Division

Just a question on commercial auto and just sort of recent years' loss picks and also the current the loss pick. That's coming down, but you've also had some reserve additions. And then if I look at sort of pure loss ratios, you versus the industry over the last few years, you're a few points lower. So I think part of it is the fact that you've been early in taking rate and that's why you're able to see some improvement here in the current, even though there's some additions in the prior years. But I was wondering if there's anything else in mix of business that might have you a few points lower than the industry.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Great observation. Jack, do you want to?

John C. Roche
President of Hanover Agency Markets

Yes. I think clearly -- again, if we go back to our whole account size view, right, pound for pound, we have less larger fleets. We have less pronounced exposures in some of the major metro areas because of the kind of business we write. But I think your observation is a good one in that 3 years ago, we were part of a small group of unpopular folks that were talking about this emerging issue. And early on, there was some angst about that. I think now, what we can say is that we were clearly in the top quartile of companies that identified the issue and have been addressing it kind of as you go. So my hope and expectation is, is that we're substantially on top of this issue, but also that the industry is not going to let commercial auto settle at its current profitability level. So that gives me confidence to the earlier question that we're going to improve because as long as people keep putting out commercial auto results like they are, pricing should stay firm, underwriting actions should continue, and we should be able to improve our portfolio further from here.

Daniel D. Farrell
Piper Jaffray Companies, Research Division

Great. That's helpful. And then just a question on personal auto. In just thinking about state mix, how do you think about the footprint you have now and potential expansion? And I'm wondering if we're in an environment where the industry seems like it's going to have to be putting through some rate. Does that give opportunity to maybe think about footprint a little differently?

Richard W. Lavey
Chief Growth Innovation Officer

This is Dick. Yes, I think it does. We obviously are thinking about that pretty aggressively. We have a 17-state footprint currently, and we have some holes within that current footprint. So we think of that as our first priority to sort of fill out that footprint, Pennsylvania being that first state that we see. So I think we've expressed that we're working hard on a platform. And then, from there we'll think about what our next set of states would be. So what we do, we look at it opportunistically. We're going to do it carefully, right? We're going to pursue the same strategy. As we think about expanding Personal Lines, we're going to think about the same distribution strategy. This is not a proliferation of agents and putting our point-of-sale black box on as many desktops as possible. This is leveraging our franchise, leveraging our Commercial Lines relationships and building a broader franchise relationship with agents in those expansion states.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

And because of our insight, we have pretty good data with our Commercial partners in the states we're targeting, the segment we're going after, how much they have, who's it with. And so we're pretty set up.

Richard W. Lavey
Chief Growth Innovation Officer

Yes, In fact, there is a real pull, right? We have such strong relationships and performance that they are eager for us to be as equally strong of a partner on the Personal Lines side. So we're being patient and cautious. We're taking our time. We're going to do it right. But your insight is a good one. I think it does create some opportunity for us.

Daniel D. Farrell
Piper Jaffray Companies, Research Division

And Fred, I just wanted to say, I've had the opportunity to cover you guys since the very beginning. And I really think -- I don't know if there's many examples of companies that have had the transformation that you guys have had over that time period. So I think you deserve a lot of credit for the vision, but also the quality of people that you put in place to help execute that over the whole time. And I think David Greenfield was the perfect example sort of in the last few years of helping to execute that. And it's also, I think, really a credit that you're able to bring back Gene, who played an important part before and can help you out in this time. So I just felt like that needed to be said.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Thank you, Dan. That was very kind.

Operator

Your next question comes from the line of Richard Rosen, Columbia.

Oksana Lukasheva
Vice President of Investor Relations

Do we have any other questions?

Operator

There are no further questions.

Oksana Lukasheva
Vice President of Investor Relations

All right. Thank you very much, everybody, for your participation today. And we're looking forward to speaking with you next quarter.

Operator
Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect. Please have a good day. Thank you.