S&P Capital IQ

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American Financial Group, Inc. NYSE:AFG

FQ4 2014 Earnings Call Transcripts

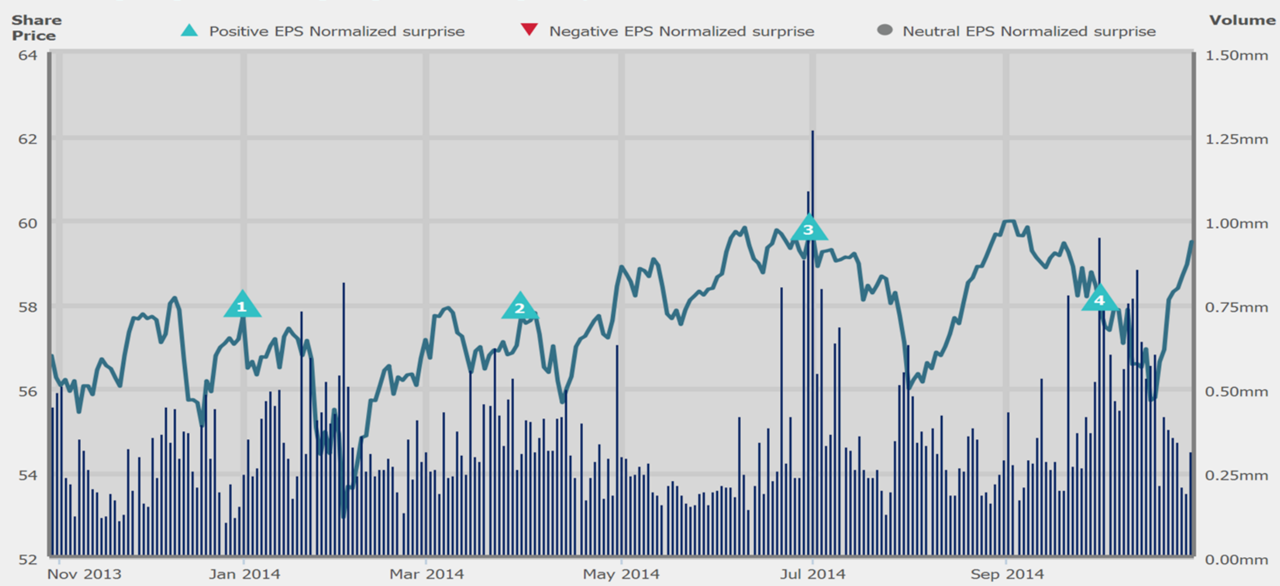
Tuesday, February 03, 2015 4:30 PM GMT

S&P Capital IQ Estimates

	-FQ4 2014-			-FQ1 2015-	-FY 2014-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	1.29	1.35	▲4.65	1.14	4.76	4.82
Revenue (mm)	1079.21	1061.00	▼(1.69 %)	1078.67	4127.21	3878.00

Currency: USD
Consensus as of Feb-03-2015 12:03 PM GMT

Stock Price [USD] vs. Volume [mm] with earnings surprise annotations



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2013	1.21	1.28	▲1 5.79 %
FQ1 2014	0.97	1.00	▲2 3.09 %
FQ2 2014	0.95	1.07	▲3 12.63 %
FQ3 2014	1.16	1.40	▲4 20.69 %

Call Participants

EXECUTIVES

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Craig Lindner
Former Co-President and Director

Diane P. Weidner
Assistant Vice President of Investors Relations

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

ANALYSTS

Amit Kumar
Macquarie Research

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

Ryan J. Byrnes
Janney Montgomery Scott LLC, Research Division

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the American Financial Group 2014 Fourth Quarter and Full Year Results Conference Call. [Operator Instructions] As a reminder, today's conference is being recorded.

I would now like to turn the call over to Diane Weidner.

Diane P. Weidner
Assistant Vice President of Investors Relations

Thank you. Good morning, and welcome to American Financial Group's Fourth Quarter 2014 Earnings Results Conference Call. I'm joined this morning by Carl Lindner III and Craig Lindner, co-CEOs of American Financial Group; and Jeff Consolino, AFG's Chief Financial Officer. If you are viewing the webcast from our website, you can follow along with the slide presentation if you'd like.

Certain statements made during this call are not historical facts and may be considered forward-looking statements and are based on estimates, assumptions and projections, which management believes are reasonable but, by their nature, subject to risks and uncertainties.

The factors which could cause actual results and/or financial condition to differ materially from those suggested by such forward-looking statements include, but are not limited to, those discussed or identified from time to time in AFG's filings with the Securities and Exchange Commission, including the annual report on Form 10-K and the quarterly reports on Form 10-Q.

We do not promise to update such forward-looking statements to reflect actual results or changes in assumptions or other factors that could affect these statements.

Core net operating earnings is a non-GAAP financial measure, which sets aside significant items that are generally not considered to be part of ongoing operations, such as net realized gains and losses, discontinued operations and certain nonrecurring items. AFG believes this non-GAAP measure is a useful tool for analysts and investors in analyzing ongoing operating trends and will be discussed for various periods during this call. A reconciliation of net earnings attributable to shareholders to core net operating earnings is included in our earnings release.

If you are reading a transcript of this call, please note that it may not be authorized or reviewed for accuracy. Thus, it may contain factual or transcription errors that could materially alter the intent or meaning of our statements.

Now I'm pleased to turn the call over to Carl Lindner III to discuss our results.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Good morning. We released our 2014 fourth quarter results yesterday afternoon, and I'm assuming that our participants have reviewed our earnings release and the investor supplement posted on our website.

We're pleased to report core net operating earnings per share of $1.35, a 5% increase from the comparable prior year period. These results reflect higher underwriting profit and higher net investment income in our Specialty Property and Casualty operations, which was partially offset by lower core operating earnings in our Annuity and Run-off Long-term Care and Life segments. These results set new AFG records for the fourth quarter and full year core operating earnings per share. Craig and I thank God and our management team and all of our employees for helping to achieve these results.

Annualized core operating return on equity was 11.7% for the 2014 fourth quarter compared to 11.8% for the fourth quarter of 2013. Net earnings per diluted share were $1.41 and includes $0.06 per share of realized gains, generating a fourth quarter annualized return on equity of 12.1%. We also focused on returning capital to shareholders over the course of the year.

Turning to Slide 4, you'll see a few highlights. We paid $169 million in dividends during the year, representing $81 million in regular common stock dividends and an $88 million special dividend paid in December of 2014. Our quarterly dividend was increased by 14% to an annual rate of $1 per share beginning in October of 2014. And we repurchased $191 million of AFG's common shares at an average price per share of $57.73.

We also intelligently deployed capital through the acquisition of Summit, launch of our Aviation division and a purchase of renewal rights to grow our Public Sector business. We also acted upon opportunities to grow our Specialty Casualty insurance businesses, and we achieved 17% annual growth in average annuity investments during the year. Craig and I are very pleased with the results.

Five-year compounded growth in AFG's adjusted book value per share plus dividends was 12% through year-end 2014. AFG's annualized total 5-year shareholder return, representing growth in share price plus dividends, was 23%. This substantially exceeds the total return performance of the S&P 500 and the S&P Property and Casualty Index over the same period.

We've established our 2015 core operating earnings guidance for AFG in the range of $5.10 to $5.50 per share. And Craig and I will discuss our guidance for each segment of our business later in the call.

Slides 5 and 6 of the webcast include an overview of the results in our Specialty Property and Casualty operations. On Slide 5, you'll see that gross and net written premiums were up 22% and 25%, respectively, in the 2014 fourth quarter compared to the same quarter a year earlier due primarily to higher premiums in our Specialty Casualty Group, which does include results from Summit, our specialty workers' comp subsidiary acquired on April 1, 2014. Excluding Summit, our Specialty Property and Casualty gross and net written premiums grew by 8% and 7%, respectively, during the fourth quarter of 2014.

Specialty Property and Casualty insurance operations generated underwriting profit of $79 million for the 2014 fourth quarter compared to $75 million in the fourth quarter of 2013. The fourth quarter 2014 combined ratio of 92.6% was 1.3 points higher than the comparable prior year quarter and included 1 point of adverse prior year reserve development.

Fourth quarter 2014 Property and Casualty net investment income was about 12% higher than the comparable 2013 period, reflecting the investment of cash received in connection with the Summit acquisition. Nearly 2/3 of our Property and Casualty businesses reported pricing increases during the fourth quarter, resulting in an overall renewal rate increase of approximately 2%. This is the 13th consecutive quarter that we have reported overall price strengthening.

Pricing continues to keep pace with loss cost trends in many of our businesses, and loss cost trends appear to be relatively benign across almost all of our Property and Casualty businesses.

On Slide 6, you'll see a few highlights from each of our Specialty Property and Casualty business groups. Property and Transportation Group reported an underwriting profit of $22 million in the 2014 fourth quarter compared to underwriting profit of $17 million in the comparable prior year period. I am pleased that focused efforts to improve results produced higher underwriting profitability in our property and inland marine operations. These results were partially offset by lower underwriting profits in our transportation business where we continue to focus on improving pricing and risk selection within our commercial auto liability lines.

Although we had anticipated break-even results in our crop insurance business, actual results were better than expected but still below historical levels of profitability. We achieved growth in gross and net written premiums in most business units within this group during the fourth quarter, with overall net written premiums up 7% over the prior year period.

Overall renewal rates increased 4% on average for the quarter, with our National Interstate sub achieving a 5% rate increase. For the full year, this group achieved a 5% rate increase overall.

Specialty Casualty Group reported underwriting profit of $36 million in the fourth quarter of '14 compared to $32 million in the fourth quarter of '13. Our workers' compensation businesses continued to generate strong underwriting profitability, and we're pleased with the results from Summit, which continues to meet our expectations. Nearly all the remaining businesses in this group produced strong accident year underwriting profit margins during the fourth quarter and full year 2014.

I am disappointed, however, with results in our international operations. Growth has been strong in this group, the result of acquisitions and underlying organic growth. While nearly all the businesses in this group reported growth year-over-year, the acquisition of Summit, along with growth in our workers' compensation and excess and surplus lines businesses, were the primary drivers of the higher premiums. Excluding premiums from Summit, 2014 fourth quarter net written premiums grew by 11% when compared to the fourth quarter of 2013. And 2014 full year net written premiums, excluding Summit, grew by 19%.

Pricing in this group was up about 1% on average for the quarter and in line with our experience in the previous quarter. After about 4 years of rate increases in our workers' compensation and excess and surplus lines businesses, we're experiencing some rate deceleration as a result of excellent underwriting profit margins.

Specialty Financial Group reported an underwriting profit of $18 million in the fourth quarter, slightly higher than a year ago, and a combined ratio of 85.6%. Nearly all the businesses in this group continued to achieve excellent underwriting margins. Full year results in our financial institutions business, the largest business in this group, continued to be excellent. Gross and net written premiums were down slightly in the 2014 fourth quarter when compared to the same 2013 period, and pricing was flat during the quarter.

Now if you please turn to Slide 7 for an overview of the 2015 outlook for Specialty Property and Casualty operations. Despite the competitive environment, we're optimistic about this year, 2015, and our guidance contemplates a further improvement in underwriting profitability. We're targeting an overall combined ratio between 92% and 94% for Specialty Property and Casualty Group. We estimate growth in net written premiums to be in the range of 4% to 8%. 2014 results include 9 months of Summit's premiums. Excluding the impact of Summit premiums, growth during 2015 is expected to be between 2% and 6%.

Looking at each of our Specialty Property and Casualty Groups, we expect net written premiums in our Property and Transportation Group to be flat to up 4% when compared to 2014 levels. Excluding our crop insurance business, we expect growth in net written premiums to be in the range of 3% to 7%. We also expect to see improvement in the combined ratio in this group and estimate it to be in the range of 94% to 98%.

Net written premiums in our Specialty Casualty Group are expected to grow in the range of 8% to 12% during 2015. And excluding Summit, we expect growth in this group to be between 4% and 8%. Our estimate for the combined ratio in this group is in the range of 90% to 94%. We expect net written premiums in our Specialty Financial Group to be up 1% to 5% compared to 2014. Our estimate for the combined ratio in this group is in the range of 86% to 90%.

We're targeting overall average renewal rates in 2015 for the Specialty Property and Casualty Group to be flat to up 2%. Our assumptions include continued rate increases in our Property and Transportation Group and pricing that's flat year-over-year in our Specialty Casualty and Specialty Financial Groups. And we expect Property and Casualty net investment income to grow by 5% in 2015.

Now I'll turn the discussion over to Craig to review the results in our Annuity segment and AFG's investment performance.

Craig Lindner
Former Co-President and Director

Thank you, Carl. The Annuity segment reported core pretax operating earnings of $85 million in the 2014 fourth quarter compared to $92 million in the comparable 2013 period, an 8% decrease as shown on Slide 8. This decrease was largely the result of the impact of fair value accounting on our fixed-indexed annuities. Annuity earnings before the impact of fair value accounting were $93 million during the fourth quarter, which compares to $86 million in the fourth quarter of 2013, an 8% increase.

AFG's 2014 earnings continue to benefit from growth in annuity sales and a favorable impact of lower-than-expected surrenders. Our quarterly average annuity investments and reserves grew approximately 14% and 15%, respectively, year-over-year. However, the impact of this growth was partially offset by the runoff of higher-yielding investments. In addition, fourth quarter earnings in both years benefited from unanticipated investment and other income.

In 2014 and 2013, AFG conducted a detailed unlocking review of the major actuarial assumptions underlying its annuity operations. The results of the unlocking review were immaterial in both the fourth quarters of 2014 and 2013. Interest rate and stock market fluctuations have an impact on the accounting for fixed-indexed annuities, and these accounting adjustments are recognized through AFG's reported core earnings, as shown on Slides 8 and 9.

In the fourth quarter of 2014, the combination of an increase in the stock market but a decrease in longer-term interest rates as measured by the Corporate A2 rate resulted in an unfavorable impact on earnings. Conversely, in the fourth quarter of 2013, the combination of a much larger increase in the stock market and a moderate increase in long-term interest rates resulted in a favorable impact on earnings. Additional information about the components of spreads for AFG's fixed annuity operations can be found in AFG's quarterly investor supplement posted on our website.

Turning to premiums. Annuity premiums were $971 million in the fourth quarter of 2014. Although this represents a decrease of 30% from the comparable prior year period, it represents an increase of 20% from the third quarter of 2014. Despite the low interest rate environment, AFG's $3.6 billion of annuity premiums in 2014 represent the second highest level of annuity premiums in the company's history. We're very proud of this achievement.

Please turn to Slide 10 for an overview of the 2015 outlook for the Annuity segment. We expect average fixed annuity investments and average fixed annuity reserves to grow in the range of 8% to 12% in 2015. The decrease in interest rates in January is likely to put pressure on core annuity earnings in the first quarter due to fair value accounting for fixed-indexed annuities.

For the full year of 2015, we expect reported core pretax annuity operating earnings to be in the range of $310 million to $340 million compared to the $328 million reported for the full year of 2014. For the full year of 2015, we estimate that our net spread earned, which is the basis for GAAP reported earnings, will be 100 to 135 basis points compared to 141 basis points achieved for the full year of 2014. This estimate reflects the January 2015 decrease in interest rates.

Excluding the impact of fair value accounting, we estimate that our net spread earned in 2015 will be 20 to 25 basis points lower than in 2014, reflecting the impact that low interest rates are expected to have on our investment portfolio. Furthermore, 2014 annuity results include a significant amount of favorable items related primarily to net investment income, including unusually strong partnership income, additional income from early redemptions and prepayments of fixed income investments, as well as several other items. While we tend to have similar items every year, our annuity plan does not reflect the sizable reoccurrence of such items in 2015. In addition, 2014 included a significant benefit from the impact of lower surrenders than expected.

Based on information currently available, we expect premiums for the full year of 2015 will be flat to slightly down from the $3.7 billion reported in 2014. Significant changes in interest rates and/or the stock market from today's level could lead to additional positive or negative impacts on the Annuity segment's results.

AFG's Run-off Long-term Care and Life segment reported a core pretax operating loss of $7 million in the fourth quarter of 2014 compared to a core pretax operating loss of $3 million in the comparable prior year period. Included in the results for the fourth quarter of 2014 is a $5 million loss on the commutation of a long-term care reinsurance agreement.

In the fourth quarter of 2014, with the assistance of an external actuarial consulting firm, we completed our review of the major actuarial assumptions for AFG's Run-off Long-term Care business, which resulted in no charge to earnings and an updated net loss recognition margin of $11 million.

On Slide 11, you'll see a progression of the net loss recognition margin from the $64 million reported at 12/31/2013 and the primary factors contributing to the $23 million -- to the $53 million decrease.

Changes in rate increase assumptions increased the margin and partially offset the decreases caused by changes in assumptions related to claim costs, reinvestment rates and expenses.

The table on Slide 12 illustrates the impact of the net loss recognition margin of changes in key loss recognition assumptions. The result of each assumption change represents a change in the net loss recognition margin that would result from using the changed assumption. Favorable changes in the assumptions would increase the net loss recognition margin. Unfavorable changes would decrease the margin and potentially result in a net loss recognition charge to earnings. Each item reflects a change to a single assumption without changes to other assumptions. These amounts are valid for a point in time and will change in future periods as the in-force block ages and its actual performance deviates from the assumptions used at 12/31/2014.

We have added a 2-page appendix to our investor supplement this quarter that includes information about our long-term care net loss recognition margin and interest rate assumptions used in long-term care recognition testing and annuity unlocking.

Please turn to Slide 13 for a few highlights regarding our $36 billion investment portfolio. AFG recorded fourth quarter 2014 net realized gains on securities of $5 million after tax and after deferred acquisition costs, compared to $41 million in the comparable prior year period. Unrealized gains on fixed maturities were $604 million after tax, after DAC at 12/31/2014, an increase of $163 million from year-end 2013. Unrealized gains on equities were $139 million after tax at 12/31/2014, an increase of $18 million from year-end 2013.

As you'll see on Slide 14, our portfolio continues to be high-quality, with 87% of our fixed maturity portfolio rated investment grade and 97% with an NAIC designation of 1 or 2, its 2 highest categories. We've provided additional detailed information on the various segments of our investment portfolio in the quarterly investor supplement on our website.

I will now turn the discussion over to Jeff who will wrap up our comments with an overview of our consolidated fourth quarter 2014 results.

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

Thank you, Craig. We've been through a lot of detail on a very pleasing quarter and on our 2015 earnings guidance. I'm going to tie it all together in a few slides before we open up the lines for questions.

Slide 15 shows our fourth quarter consolidated results by segment. Core net operating earnings per share in the quarter were a record $1.35. $1.35 is based on core net operating earnings in the quarter of $122 million.

Looking at core pretax operating earnings by segment. You'll see our P&C segment improved by $10 million against last year's quarter. On Slide 5, Carl showed you that the Specialty P&C Group's underwriting profits increased by $4 million. You can see on Page 4 of the investor supplement that Q4 2014 investment income for the P&C segment was $8 million higher than the prior year, thanks to the increase in average P&C invested assets resulting from the Summit acquisition.

Other expenses within the P&C segment increased by about $2 million in the quarter. This is primarily the amortization of Summit's acquisition intangibles, which run about $7 million per year. The sum of these 3 items produces the $10 million improvement in the P&C segment core pretax operating earnings.

We closed on the Summit acquisition at the beginning of the 2014 second quarter. Q1 2015 will be the final quarter where our Specialty P&C segments' quarterly comparatives are affected by the Summit transaction.

Craig previously covered our Annuity segment earnings, which were $7 million lower quarter-over-quarter, thanks to the vagaries of fair value accounting. Interest expense of parent holding companies increased $2 million due to the hybrid debt offering in September of 2014. Other expense was lower by $12 million than the year-ago fourth quarter, largely as a result of third-party fee income paid to our American money management subsidiary, lower accruals associated with certain employee benefit plans, as well as other miscellaneous items. You may recall that the third quarter other expense comparison was also favorable for 2014 against 2013. Our guidance range, however, does not anticipate similar beneficial impacts in 2015.

Turning to Slide 16. You'll see the realized gains contributed $0.06 per share to diluted earnings per common share.

On Slide 17, you'll see that AFG's adjusted book value per share was $48.76 at December 31, 2014, its highest level ever. Our excess capital showed at [ph] approximately $810 million at December 31, 2014, and included $290 million of parent company cash. We earned net income of $127 million in the fourth quarter and returned $174 million to our shareholders through dividends and through share repurchases.

Approximately 4.5 million shares remain under our repurchase authorization as of February 2, 2015. We plan to continue returning excess capital to our shareholders through the course of 2015.

On Slide 18, you'll find a single-page summary of our 2015 guidance. It shows AFG's core net operating earnings guidance of $5.10 to $5.50 per diluted share as well as guidance reviewed earlier in the call for key financial measures in the Specialty Property and Casualty Group, and for the Annuity segment. AFG's expected 2015 results exclude noncore items, such as realized investment gains and losses as well as other significant items that may not be indicative of ongoing operations.
Now we'd like to open the lines for any questions.

Question and Answer

Operator

[Operator Instructions] The first question comes from Amit Kumar from Macquarie.

Amit Kumar
Macquarie Research

Just a few quick questions. Number one, just going back to the discussion on adverse development in international, did you expand on the cause for that reserve development or not?

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

This is Jeff Consolino. We did not expand on it, but I'm prepared to expand on it a little bit here if you like. First of all, I think it's important to note that we believe our reserves are as adequate at the year-end December 2014 date as they were at the beginning of the year. That's to say that our balance sheet is as strong at year-end as it was when we began the year, and I make this comment after considering the growth in our reserves during the year, including the growth attributable to Summit. Overall, Specialty P&C Group prior year development in the quarter was unfavorable by just under $10 million, $9.9 million. And again, I know we're talking about a specific quarter, but in the context of this, please consider that we had favorable development in the Specialty P&C Group for the whole year. Among our subsegments, Specialty Financial is still showing favorable development. We had modest unfavorable development in Property and Transportation mainly attributable to reserve change in our non-National Interstate transportation business. And so out of the $14 million of unfavorable reserve development in the Specialty Casualty subsegment, $11 million of that was associated with our international operations. In those international operations, management made a year-end adjustment to reserves. Some people have asked the question, so I'll answer it. The adjustment was not related to Italian public hospital business. The adjustment spans a number of lines of business in the international business, and I really can't single out any one line as something that contributed more than others. So that's the lion's share of what happened in that Specialty Casualty subsegment. Again, within that segment, we had favorable development in the aggregate for our workers' comp units, favorable development in the aggregate for our E&S in specialty liability units. Outside international, we did strengthen reserves somewhat for some other items, such as extra-contractual obligations or discontinued profit centers, and that would be the balance outside of international in what you saw in that move.

Amit Kumar
Macquarie Research

Got it. So net-net, it was more a change in, I guess, methodology versus any specific meaningful adverse trend, is that correct?

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

I don't want to say a change in methodology. The methodology remains broadly the same. There was a year-end adjustment, and the year-end adjustment covered a lot of the lines of business in international, and that's where we chose to book it.

Amit Kumar
Macquarie Research

Okay, that's helpful. The other question I had is on the commercial auto, and this was sort of a go-forward sort of broader question. Some reports are out there which predict that U.S., I guess, commercial auto will grow for 2015. And can you sort of talk about how you're thinking about loss cost trends for commercial auto and maybe the correlation they might have with gas prices?

Carl H. Lindner

Co-Chief Executive Officer, Co-President and Director

Jeff, since you're the Chairman of National Interstate, and that's the biggest part of our -- you want to talk about loss cost trends or -- within National Interstate?

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

Sure. First, I would encourage you to dial into the National Interstate earnings call at the end of February if you'd like to hear from management on the business directly from them. National Interstate did put out a preannouncement last night that talked about their expectations for the fourth quarter and full year 2014. And embedded in that is the commentary that they had adverse severity coming through in the quarter. Amit, that has been an issue with National Interstate in many but not all quarters going back a couple of years. And it really is severity that we're having in that unit a harder time getting our arms around rather than frequency. In terms of loss cost trends, what you will see when the company reports its full year results is a continued migration upwards in the accident year combined ratios for 2014 and some of the recent years. National Interstate has been assertive in obtaining appropriate rate increases. It's been a focus for management. They've been diligent in non-renewing the business that they didn't think would be profitable for them. But when faced with an escalation in severity and skinning of margins, I think you'll hear from management that they're going to redouble their efforts there and they're going to need to continue to get rate. It's clear that rate is available, and it's clear that these trends are affecting more companies than just National Interstate. But they really do need to keep working to restore the business to a level of profitability that management will be proud of and we as shareholders will be proud of.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

On the Great American side, a lot of the business is physical damage, so the loss cost trend on that business is probably more around 2% or so in that. As far as -- I don't think we consider ourselves experts as to the impact on lower gas prices -- on our business. I -- my gut would say that it has a potentially larger impact on private passenger auto, which may be -- may tie directly more towards increased miles driven in that. I think we're still trying to figure out how much or how little impact that has on our overall commercial auto business and that clearly, lower gas prices have to help the profitability of our customers in that. So I think that's probably a positive.

Amit Kumar
Macquarie Research

Okay. And just finally, and then I'll stop, in terms of the outlook, I know it's too early right now, but I guess the commodity prices for your -- some of the crops, off -- down double digits versus prior year. Maybe it's too early, but can you sort of give the early view on your crop insurance book? And are you thinking about the reinsurance differently based on the pricing outlook in the reinsurance market, maybe use more reinsurance for crop? That's the final question I have.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Sure. If you look at our Property and Transportation guidance for 2015, you'll see our overall guidance for that is 0 to 4%. If you exclude crop, that range turns into 3% to 7%. So I mean, if you kind of look between the lines there, roughly, the crop -- right now, when you look at spring discovery prices from last year and when you take a look at futures prices as they are right now, that and -- considering the commodity price decrease being offset by business we pick up, rough and dirty, I think right now, we're thinking that the -- our crop premium might be down 7%, 8%, something like that. And as far as how much we reinsure in that, that's something that we're really kind of setting the strategy on right now as we move forward.

Operator

The next question comes from Vincent DeAugustino from KBW.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Just to, I guess, start with the trade credit kind of notation in the press release, I guess I'm assuming that, that relates, I guess, in some way to dollar strengthening here up until year-end, if that's correct?

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

I wouldn't assume that, Vincent.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, easy enough. And then just on National Interstate, just a clarification. Was the rate increase there 5% for fourth quarter '14? Or did I get that wrong?

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

Sorry. Say that again, Vincent?

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

On the National Interstate rate increase for the quarter, did you mention that the pace was 5% for fourth quarter '14?

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

Correct.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Yes, that's correct.

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

I would also refer you to National Interstate's preannouncement, which talks about average rate increases throughout the year of approximately 7%.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, look forward to that call. And then I guess, Craig, on the annuity side, is there any opportunity, just from a top line standpoint, for just any new intermediary expansion as far as growth as an opportunity?

Craig Lindner
Former Co-President and Director

Yes. We certainly are focusing on the bank market, Vincent, and establishing new relationships there. That is the segment that we're pretty optimistic about. There is somewhat of a barrier to entry. You need a certain minimum level of ratings to get in most of the big banks. And so that's the area that we're really focusing on in this environment for growth.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And then sticking with you, Craig, and then, I guess, Jeff, if it makes sense. So on the long-term care disclosure, I mean, first, thank you very much for the additional disclosures and the teach-in on the mechanics. I recall last quarter, there was some discussion around assumptions on interest rates and then kind of coaching us to not think about just doing a complete level set change and really assuming some normalization on the out-year. So on the $34 million, can we kind of dive into what the 2 parts were on the initial and the out-year assumptions and then kind of where the current assumptions on reinvestment are today?

Craig Lindner
Former Co-President and Director

Yes. If you flip, so we did make a disclosure in the supplement. I don't know whether you saw that or not. Turn...

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Page 28, 29? Okay, there we go.

Craig Lindner
Former Co-President and Director

And Page 29. So our assumption is this year, we're going to earn a net -- we're going to have a net reinvestment rate of a 4.52%, and that will climb to a 6.25% over a 7-year period of time. I would make the point to you that the duration of the liabilities in long-term care is very, very long, so it does give us the opportunity to buy some things in the long-term care operation that wouldn't be appropriate for the Annuity business.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, makes sense. And then just lastly for me. Carl, on the P&C guidance as far as top line, so the x Summit numbers we have, I'm assuming, though, that there is no assumed benefit from any M&A activity into the current top line forecast?

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

That's correct. There's no additional acquisitions that are figured in that.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And then just from an M&A standpoint, clearly, we're seeing a lot more press releases. I mean, those are some pretty big transactions. On the smaller side, are you guys seeing the pipeline still looking pretty good?

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

We always get a shot at a lot of different opportunities, so I think it's about the same as it has been.

Operator

Next question comes from Ryan Byrnes from Janney Capital.

Ryan J. Byrnes
Janney Montgomery Scott LLC, Research Division

Just had a question with the long-term care. There was, again, a $40 million positive coming from rate changes. Have those rate changes been passed? Or are those proposed rate changes? Just want to see when those changes come into effect.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Yes, it's both. The last couple of years, we have been quite a bit more successful at achieving rate increases than what we had assumed when we did our last major review back at the end of 2012. So it does incorporate what we've experienced over the last several years and our kind of updated judgment of what we're going to experience going forward.

Ryan J. Byrnes
Janney Montgomery Scott LLC, Research Division

That's great. And then also I noticed that -- in the quarter that the results from the runoff in the long-term care, again, they were worse than usual. Was that a result of any of the actuarial changes? Or is that just a kind of a onetime blip? Just trying to, from a modeling perspective, think about that segment.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

The biggest part of it was the commutation of a reinsurance agreement, $5 million GAAP loss related to that.

Ryan J. Byrnes
Janney Montgomery Scott LLC, Research Division

Got you. And then again, as interest rates have dropped another 50 basis points in January, what kind of year-end outlook is baked into your assumption for the annuity block? Just trying to figure out what you guys -- I realize it's your best guess, but just trying to figure out what you guys are using for your estimate.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Yes. I meant -- as it relates to reinvestment rates, I mean, we're assuming we're going to -- we're assuming that we're going to earn something in the neighborhood of 3.5% on money [ph], if you turn to Page 29, you'll see the assumption that we're using related to reinvestment rates for this year and progressing out over the next 7 years.

Operator

The next question comes from Paul Newsome from Sandler O'Neill.

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

I think we have got some more pieces here. Could you -- it was in your disclosure. Could you talk about the ROE of your businesses with and without the excess capital in runoff businesses and how those compare?

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Sure. Yes, this is Carl. If you look at the rough and dirty, the specialty casualty part of our business earns about a 17% return on equity based on kind of a calendar year basis. Specialty Financial, around 18%; Property and Transportation, around 5%, which the total is roughly 13% in the P&C side.

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

That's terrific. Is it similar on the life side or...

Craig Lindner
Former Co-President and Director

In the Annuity business, if you look at the core operating earnings, it's -- was a little over 11%. I think it was around 11.5% last year. That doesn't include realized gains, and the numbers Carl just gave you don't include realized gains. Typically, that's additive to the returns.

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

Yes, I think it's an upper belly [ph] credit for that with the insurance investors. The -- could you also just review kind of how you think about the excess capital piece? And I think there's a little bit of a buffer there that you'd like to keep, but the most recent views on how much excess capital you like to keep at the holding company as well as in other places within the corporate structure.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Yes, Paul. This is Carl. I mean, it's not too much different than what we've kind of talked about in the past. And we like to keep hundred -- couple hundred million dollars of dry powder, both for defensive reasons and offensive reasons opportunistically. The rest, basically every year is a little bit different. If you take a look at last year versus the year before, every year is -- we're very opportunistic. So we're opportunistic repurchasers of our shares. We try to do that opportunistically. We've paid special dividends when we thought that, that made sense. We've increased our dividend at a double-digit rate pretty much. We're out there looking at starting businesses and acquiring businesses. And so we're always looking for the highest and best use of our capital in that, and we don't -- I don't see this year as any different.

Operator

[Operator Instructions] The next question comes from Jay Cohen from Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

A couple of questions. The first is, I guess, the one part of the guidance that was a little surprising to me on the positive side was the property casualty investment income moving higher. Are you making any changes in the portfolio that will protect the yield to some extent?

Joseph E. Consolino
CFO, Executive VP, Director and Chairman of the Board of Neon Capital Ltd

Jay, this is Jeff. We're certainly very proud of our American money management subsidiary who's done an excellent job for AFG over time. But the major factor there is we closed on Summit April 1, 2014. That involved a $400 million investment into the P&C Group plus all of the reserve balances being invested for Summit. So we'll have higher average P&C invested assets in 2015 than we would have in 2014 because we only had 9 months' worth of that for '14 versus the full year. Absent that, there's no special thing, and in fact, we've taken a very close look, as Craig would say, about reinvestment rates and tried to make sure they reflect current market when we went ahead and prepared our guidance.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it. And the other question. Carl, you had just given us these ROE figures for the different pieces of the business. I assume you were referring to specifically 2014 results?

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

That's correct, Jay.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Okay. I didn't know if these were normalized or not, then the Property, Transportation seemed a little low, but certainly, I understand what happened in '14.

Carl H. Lindner
Co-Chief Executive Officer, Co-President and Director

Yes. National Interstate is a pretty large chunk there, and that kind of pulled the average down.

Operator

I am showing no further question.

Diane P. Weidner
Assistant Vice President of Investors Relations

Thank you for joining us this morning. We look forward to talking with you again as we share our first quarter results in 2015. This concludes our call for today.

Operator
Ladies and gentlemen, that does conclude the conference for today. Again, thank you for your participation. You may all disconnect. Have a good day.