S&P Capital IQ

CONTENTS

Mercury General Corporation NYSE:MCY

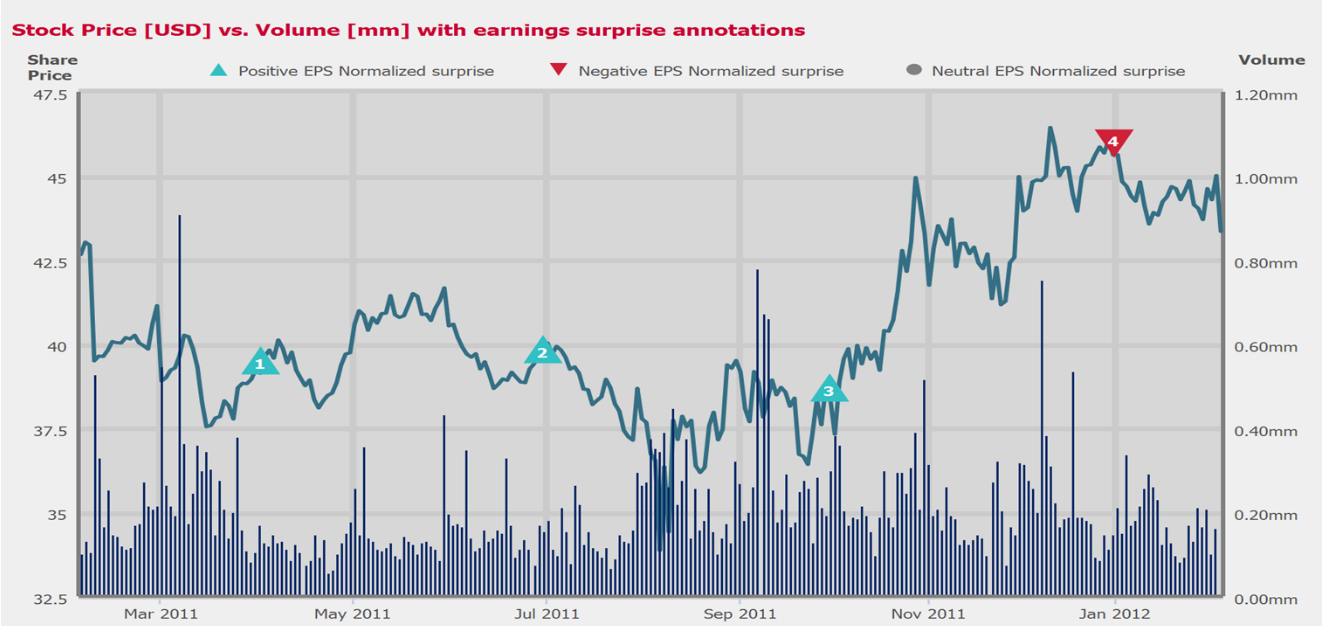
FQ1 2012 Earnings Call Transcripts

Monday, April 30, 2012 5:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2012-			-FQ2 2012-	-FY 2012-	-FY 2013-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.69	0.71	▲2.90	0.68	2.68	2.70
Revenue (mm)	661.50	658.29	▼(0.49 %)	640.44	2592.90	2626.00

Currency: USD
Consensus as of Apr-30-2012 2:14 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2011	0.53	0.72	▲1 35.85 %
FQ2 2011	0.62	0.76	▲2 22.58 %
FQ3 2011	0.69	0.72	▲3 4.35 %
FQ4 2011	0.69	0.59	▼4 (14.49 %)

Call Participants

EXECUTIVES

Gabriel Tirador
Chief Executive Officer, President and Director

Theodore R. Stalick
Chief Financial Officer and Senior Vice President

ANALYSTS

Alison Marnie Jacobowitz
BofA Merrill Lynch, Research Division

Tak-Sun T Lee
Keefe, Bruyette, & Woods, Inc., Research Division

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

Presentation

Operator

Good afternoon. My name is Kimberly, and I will be your conference operator today. At this time, I would like to welcome everyone to the Mercury General Quarterly Conference Call. [Operator Instructions] This conference call may contain comments and forward-looking statements based on current plans, expectations, events and financial and industry trends which may affect Mercury General's future operating results and financial position. Such statements involve risks and uncertainties which cannot be predicted or quantified and which may cause future activities and results of operations to differ materially from those discussed here today.

Thank you. I would now like to turn the conference over to Gabriel Tirador. Please go ahead.

Gabriel Tirador
Chief Executive Officer, President and Director

Thank you very much. I would like to welcome everyone to Mercury's First Quarter Conference Call. I'm Gabe Tirador, President and CEO. In the room with me is Mr. George Joseph, Chairman; Ted Stalick, Vice President and CFO; Chris Graves, Vice President and Chief Investment Officer; and Robert Houlihan, Vice President and Chief Product Officer.

Before we take questions, we will make a few comments regarding the quarter. Our first quarter 2012 underwriting results improved as compared to the first quarter of 2011. Our combined ratio was 97.6% in the first quarter of 2012 compared to 98.2% in the first quarter of 2011. In the first quarter of 2012, we recorded $6 million of unfavorable reserve development compared to $1 million in the first quarter of 2011. Excluding the impact of reserve development in both years, the combined ratio was 96.7% in the first quarter of 2012 compared to 98% in the first quarter of 2011.

The combined ratio was aided during the quarter by our continued focus in reducing expenses. Consequently, our expense ratio declined to 26.8% from 28.3% in the first quarter of 2011.

Premiums written were essentially flat this quarter. However, there were some moving parts to the written premiums, primarily resulting from the California personal auto revenue-neutral class plan that we implemented in December of 2011. The plan improved our risk segmentation but also caused dislocation to some of our existing customers. The refined pricing improved our competitive position for new business, and our California new business private passenger auto sales increased year-over-year in the quarter by 16%. The rate dislocation caused our renewal rates to decrease but at a rate lower than we had expected. We are pleased to report that our operations outside of California posted a combined ratio under 100% in the quarter. We have made great strides in our operations outside of California, but we are not where we want to be, and the environment in some states, such as Florida, are challenging. We continue to aggressively make changes to our rating plans to improve our segmentation and overall pricing adequacy. After-tax investment income declined by 10% to $28 million in the quarter. As we mentioned in our annual report, going forward, it will become increasingly difficult to maintain the current after-tax yields as bonds with higher coupons mature or are called, and the reinvestment of those proceeds will most likely be made at lower after-tax yields. The after-tax yield in the quarter was 3.8% compared to 4.1% in the first quarter of 2011. With that brief background, we will now take questions.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Alison Jacobowitz of Bank of America.

Alison Marnie Jacobowitz
BofA Merrill Lynch, Research Division

So I guess a couple of questions. It looks like the tax rate on net investment income has been drifting up. Should we expect this to continue? And then also on the expense ratio, I think last quarter, you suggested that a normalized expense ratio might be a little bit higher than 27%. I think it was a 27% to 28% range. This quarter came in a little lower. Would you make an adjustment to that statement, or do you still think the expense ratio might tick up a little bit?

Theodore R. Stalick
Chief Financial Officer and Senior Vice President

The tax rate is slightly higher on investments, but I don't expect that to continue to trend up. It may come back down even. As far as the expense ratio going forward, we're still looking at around 27% is where we're expecting it to run.

Operator

[Operator Instructions] We do have a follow-up question from the line of Alison Jacobowitz with Bank of America.

Alison Marnie Jacobowitz
BofA Merrill Lynch, Research Division

So on the combined ratio, if you're now making money outside of California overall, but overall combined ratio, I don't think it has really changed much over the past several years, does it mean that the California combined ratio is deteriorating? Or am I missing something in the math there?

Gabriel Tirador
Chief Executive Officer, President and Director

Well, we have had some pressure in our California combined ratio. It's still below 100%, and we do have some rate increases that are pending. We have both the homeowner rate fine that we made a few years ago that just -- we finished up with a hearing there and expect the result from the judges over the next several months. And we have a California private passenger auto rate that we filed that we are in discussions with the Department about, and we have a meeting scheduled with them sometime in May. And that's for about a plus 6%, so we do have some rates that we plan on implementing sometime in the future in California to help with the combined ratio in California, although I will say that the combined ratio in California still combined well below 100%.

Alison Marnie Jacobowitz
BofA Merrill Lynch, Research Division

And then just if there were any cat losses in the quarter, could you tell us -- can you talk about frequency into varied trends maybe in general, if any states are more problems than others? Some have brought up Florida again as being an issue. Just talk about what you're seeing there.

Theodore R. Stalick
Chief Financial Officer and Senior Vice President

Florida continues to be an issue. We're seeing pressure on our loss cost. We have been taking quite a bit of rate increase there. Generally, though, we're seeing slight increases in frequency, low single digits, as well as in severity. As far as cats go, it was pretty a quiet quarter for Mercury, at least, as far as cat plan.

Operator

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

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

I was curious if you might be able to comment on the accident years that the adverse development in the first quarter of '12 happen to come from?

Theodore R. Stalick
Chief Financial Officer and Senior Vice President

Primarily 2011 and 2010, and that was mostly in California auto. We did have a little bit of positive development from some states outside of California offsetting that.

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

Okay. And then I guess just looking at your pending rate increase in California auto and then just taking a look at some of the other insurers, it seems like the pending time that it takes to get a request through is somewhere in the neighborhood of maybe 5 to 6 and maybe even more months than that. I'm just curious if, in your opinion, if there's been any change in the current administration in the California Department of Insurance compared to previous ones or if, say, half a year is what it's always taken to get a rate request through it. It just seems like -- I guess maybe I'm wrong here, but it seems like that's a long time to be able to get an approval when we're looking at that being a one-plus policy period.

Gabriel Tirador
Chief Executive Officer, President and Director

Well, it's longer than we would like. I'll put it that way, and we're going to continue to work with the department in trying to get them implemented as quickly as possible. It is running longer than we would like at this point.

Operator

[Operator Instructions] Your next question comes from the line of Frank Lee of KBW.

Tak-Sun T Lee
Keefe, Bruyette, & Woods, Inc., Research Division

Just experienced any current year favorable development in the quarter or any adverse?

Gabriel Tirador
Chief Executive Officer, President and Director

Well, it's only the first quarter, so there wouldn't be any.

Tak-Sun T Lee
Keefe, Bruyette, & Woods, Inc., Research Division

In the current year, nothing?

Gabriel Tirador
Chief Executive Officer, President and Director

Correct.

Tak-Sun T Lee
Keefe, Bruyette, & Woods, Inc., Research Division

And then I noticed also that debt came down a little bit the past 2 quarters for the interest rate. Going forward, is this a good run rate we should be looking at?

Theodore R. Stalick
Chief Financial Officer and Senior Vice President

Right. We refinanced all of our debt last fall, and our $120 million credit facility was -- one of the financial institutions is now at a LIBOR plus 40 basis point floating rate, and that will vary based on what LIBOR does, but it's significantly lower than it was last year.

Tak-Sun T Lee
Keefe, Bruyette, & Woods, Inc., Research Division

So we can save pretty much if you just follow LIBOR, and this would be a pretty good run rate then?

Gabriel Tirador
Chief Executive Officer, President and Director

Correct.

Operator

And at this time, there are no further questions.

Gabriel Tirador
Chief Executive Officer, President and Director

Okay. Well, I'd like to thank everyone for joining us this quarter, and we look forward to talking to you again in the second quarter. Thank you very much.

Operator
Ladies and gentlemen, this concludes today's conference. You may now disconnect.