S&P Global
Market Intelligence

American Financial Group, Inc. NYSE:AFG

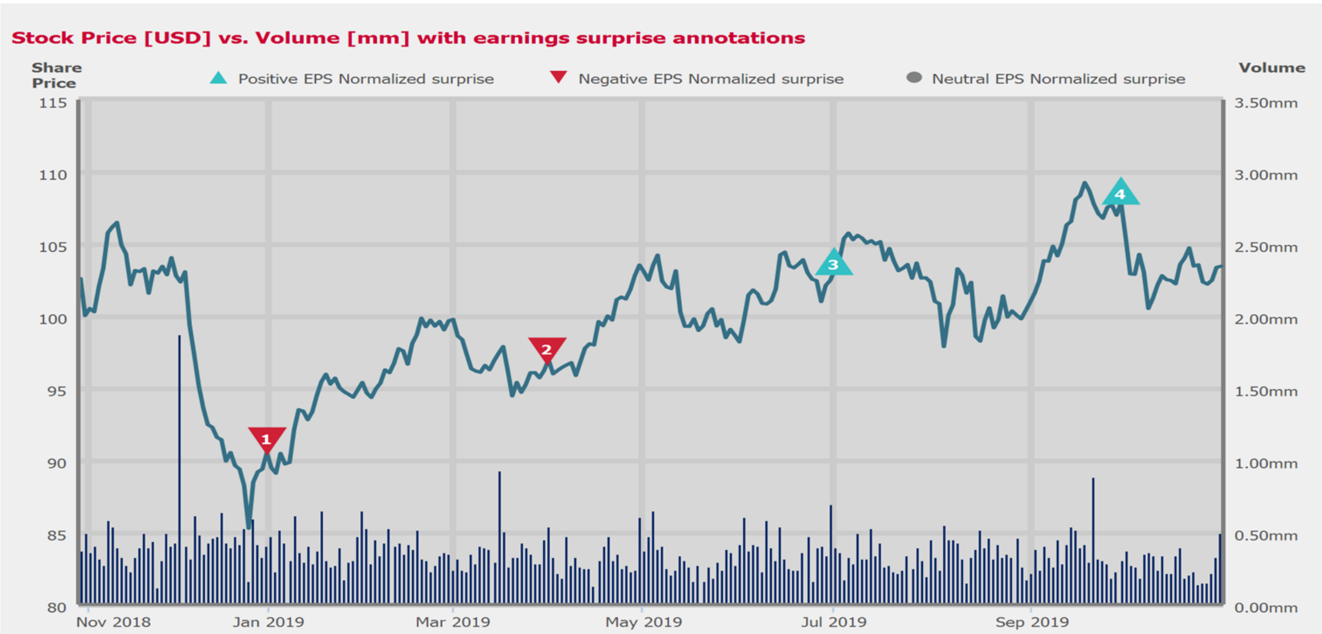
FQ3 2019 Earnings Call Transcripts

Wednesday, October 30, 2019 3:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2019-			-FQ4 2019-	-FY 2019-	-FY 2020-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	2.00	2.25	▲12.50	2.45	8.61	8.95
Revenue (mm)	1312.60	1442.00	▲9.86	1300.93	5543.92	5732.44

Currency: USD
Consensus as of Oct-30-2019 12:57 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2018	1.95	1.75	▼1 (10.26 %)
FQ1 2019	2.20	2.02	▼2 (8.18 %)
FQ2 2019	2.04	2.12	▲3 3.92 %
FQ3 2019	2.00	2.25	▲4 12.50 %

Table of Contents

Call Participants

EXECUTIVES

Carl Henry Lindner
Co-President, Co-CEO & Director

Diane P. Weidner
Assistant Vice President of Investor Relations

Joseph E. Consolino
Executive VP, CFO & Director

Stephen Craig Lindner
Co-President, Co-CEO & Director

ANALYSTS

Amit Kumar
The Buckingham Research Group Incorporated

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Jay Adam Cohen
BofA Merrill Lynch, Research Division

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

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

Presentation

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the American Financial Group 2019 Third Quarter Results Conference Call. [Operator Instructions] Please be advised that today's conference is being recorded. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Diane Weidner. Thank you, and please go ahead, ma'am.

Diane P. Weidner
Assistant Vice President of Investor Relations

Good morning, and welcome to American Financial Group's Third Quarter 2019 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 CFO.

Our press release, investor supplement and webcast presentation are posted on AFG's website. These materials will be referenced during portions of today's call.

Before I turn the discussion over to Carl, I would like to draw your attention to the notes on Slide 2 of our webcast. Certain statements made during this call may be considered forward-looking statements as defined under the Private Securities Litigation Reform Act of 1995. These statements are not guarantees of future performance. Investors should consider the risks and uncertainties that could cause actual results and/or financial condition to differ materially from these statements. A detailed description of these risks and uncertainties can be found in AFG's filings with the Securities and Exchange Commission, which are also available on our website.

We may include references to core net operating earnings, a non-GAAP financial measure, in our remarks or in responses to questions. 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 am pleased to turn the call over to Carl Lindner III to discuss our results.

Carl Henry Lindner
Co-President, Co-CEO & Director

Good morning. We released our 2019 third quarter results yesterday afternoon. If you would please turn to Slide 3 of the webcast slides for an overview.

AFG reported core operating earnings of $2.25 per share reflecting strong operating profitability and investment results in both our Specialty Property & Casualty and Annuity operations. Third quarter 2019 annualized core operating return on equity was 15.3%. Net earnings per share were $1.62 and included $0.15 per share in after-tax net realized losses on securities, a negative impact of $0.23 per share for annuity noncore items, including the impact of fair value accounting for fixed-indexed annuities, other items related to changes in the stock market and interest rates and unlocking.

Net earnings also included $0.25 per share to strengthen our A&E reserves. Craig and I thank God, our talented management team, and our great employees for helping to achieve these results.

We have narrowed the range for our expected 2019 core net operating earnings per share to $8.50 to $8.70 from the range of $8.40 to $8.80 announced previously, while keeping the midpoint at the same $8.60 per share. Craig and I will discuss our guidance for each segment of our business in more detail later in the call.

Now let's turn our focus to our Property & Casualty operations. Please turn to Slides 4 and 5 of the webcast, which include an overview of third quarter results. As you'll see on Slide 4, gross and net written premiums in our Specialty Property and Casualty insurance operations grew by 12% and 11%, respectively, year-over-year. As we previously reported, delayed planting of spring crops resulted in late acreage reporting in our crop operations, which increased our overall third quarter premiums. But when you exclude crop premiums, gross and net written premiums each increased a healthy 9% when compared to the 2018 third quarter.

Core operating earnings and AFG's Property & Casualty insurance operations were $194 million in the third quarter of '19 compared to $158 million in the prior year period, an increase of $36 million or 23%. Specialty Property and Casualty insurance operations generated an underwriting profit of $88 million in the third quarter compared to $55 million in the third quarter of 2018. Higher year-over-year underwriting profits in our Property and Transportation and Specialty Financial Groups were partially offset by lower underwriting profit in our Specialty Casualty Group.

The third quarter 2019 combined ratio of 94% was 1.7 points lower than the 95.7% reported in the comparable prior year period and included 1.6 points in catastrophe losses and 3.1 points of favorable prior year reserve development.

Average pricing across our entire Property & Casualty group was up in excess of 3% for the quarter. When you exclude our workers comp business, renewal pricing was up about 6% in the third quarter, reflecting a continued improvement from the renewal rate increases achieved during the first half of 2019. In fact, renewal pricing in our Specialty Property and Casualty Group overall is the highest we have achieved in over 5 years, meeting or exceeding our expectations in each of our Specialty Property & Casualty subsegments. I'll discuss in more detail as we review the results of each. Although loss cost trends across our Specialty Property & Casualty businesses remain stable overall, we do continue to closely monitor loss activity and the impact to social inflation along with general loss cost inflation and interest rates.

Now I'd like to turn to Slide 5 to review a few highlights from each of our Specialty Property & Casualty business groups. The Property and Transportation Group reported an underwriting profit of $38 million in the third quarter of 2019 compared to breakeven underwriting results in the comparable prior year period. Although nearly all businesses in this group reported higher year-over-year underwriting profits, the increase was driven primarily by higher underwriting profit in our Transportation and Property and Inland Marine businesses. And these increases were partially offset by the absence of underwriting profit in our crop business in the third quarter of 2019. Catastrophe losses in this group were $8 million in the third quarter of this year and $13 million in the comparable 2018 period.

Third quarter 2019 gross and net written premiums were 17% and 18% higher, respectively, than the comparable 2018 period. The increase was largely the result of year -- higher year-over-year premiums in our Transportation businesses and the timing of the recording of crop premiums. Now if you exclude crop, gross and net written premiums were very strong, increasing 13% and 14%, respectively, year-over-year. Overall, renewal rates in this group increased 4% on average in the 2019 third quarter. And I continue to be pleased with the broad-based rate strengthening in this group, with nearly all businesses reporting increases in the quarter and corrective rate actions in our Singapore and Aviation businesses.

Excessive rainfall early in the planting season in the Midwest and the upper plain states have made for a challenging 2019 crop year. As I discussed last quarter, we incurred a record number of prevented planting claims due to spring flooding and excess moisture and termed our expectations for the crop year as below average. As a result of delayed plantings, corn and soybean yields are expected to finish below their long-term averages, and a recent freeze event throughout much of the Midwest will have a meaningful negative effect on yields.

Commodity pricing held up well and appears that the harvest discovery pricing is within 2% to 3% percentage points of the spring pricing. But based on the impact of prevented planting claims and our updated expectations from the quality crops of harvest, we do not expect to record any crop profits in the fourth quarter of 2019. We're now prepared to call 2019 a poor crop year.

I continue to be very pleased with the results in our Transportation businesses, which achieved double-digit year-over-year growth in the third quarter. In addition to rate increases and exposure growth, we're seeing new business opportunities in several of our specialty transportation lines. Rate increases in our commercial auto liability book were about 9% in the third quarter. This is our eighth year of rate increase in this line of business. We've been talking about this for a long time dating back to when we first saw an uptick in commercial auto loss severity in 2012. We were able to address issues through underwriting and rate actions and got this business back on track after years of concerted effort, and we continue to obtain appropriate rate increases. But we do believe our starting point is different than the industry overall.

Specialty Casualty Group reported an underwriting profit of $23 million in the 2019 third quarter compared to $49 million in the comparable '18 period. Higher profitability in our Worker's Compensation and social services business was more than offset by higher underwriting losses in Neon and adverse prior year reserve development in our excess and surplus businesses. Underwriting profitability in our workers comp business continues to be excellent.

Catastrophe losses for this group were $10 million in the third quarter of 2019 compared to $12 million in the comparable prior year period. I am pleased with the healthy growth achieved in this group for the third quarter. Gross and net written premiums increased 8% and 7% respectively when compared to the same prior year period. There are 2 primary factors driving the growth: first, the addition of premiums from ABA Insurance Services, which was acquired in the fourth quarter of 2018; and second, strong growth in our Excess and Surplus Lines and excess liability businesses.

The growth in our E&S and excess liability businesses is primarily the result of new business opportunities, rate increases and higher retentions on our renewal business. Lower premiums in Neon, primarily due to foreign currency translation as well as lower premiums in our workers comp businesses resulting from rate decreases, partially offset the growth in the other businesses in this group. But excluding workers comp, year-over-year growth in third quarter gross and net written premiums was healthy in the segment at 12% and 13%, respectively. I'm very pleased with these results.

Renewal pricing for the Specialty Casualty Group was up 4% during the third quarter. Excluding rate decreases in our workers comp businesses, renewal rates in this group were up a very strong 9%. Both measures are an improvement from renewal rate increases achieved in the second quarter of 2019 and are the highest we've seen in 5 years. I'm really pleased with the broad-based pricing momentum across the businesses in this group during the quarter, including double-digit increases in our excess liability and umbrella businesses.

Specialty Financial Group reported an underwriting profit of $26 million in the third quarter of 2019 compared to $9 million in the third quarter of '18. Higher underwriting profit in our Financial institutions business was the primary driver of the increase. Catastrophe losses for this group were $3 million and $13 million in the third quarters of '19 and '18, respectively. The businesses in this group continue to produce excellent underwriting margins.

Third quarter 2019 gross and net written premiums increased by 6% and 9%, respectively, when compared to the same 2018 period, primarily as a result of higher premiums in our Fidelity/Crime and equipment leasing businesses. Renewal pricing for this group was flat during the third quarter.

Now please turn to Slide 6 for some review of our 2019 outlook for the Specialty Property & Casualty operations. Based on results for the first 9 months of the year, we now expect the 2019 combined ratio for the Specialty Property and Casualty Group overall between 93% and 94%. But we narrowed the range from our prior estimate of a 92% to 94%. We have also adjusted our estimate for overall growth in net written premiums to be in the range of 4% to 7%, an increase from the range of 2% to 5% estimated previously.

Looking at each segment, we now estimate a combined ratio in the range of 93% to 96% in our Property and Transportation Group narrowed a bit from our previous range of 93% to 97%. As noted earlier, our revised earnings guidance includes the expectation that based on a poor 2019 crop year, we won't record any crop profits in the fourth quarter.

The first half of 2019 included 2018 crop year earnings that were recorded as claims were settled following a strong 2018 crop year. Given our expectations for poor crop results this year, we don't expect to record any 2019 crop year earnings in the early part of 2020. Growth in net written premiums is now expected to be between 5% and 8%, an increase from the previous range of 4% and 8%. Our Specialty Casualty Group is now expected to produce a combined ratio in the range of 92% to 95%, up from the range of 90% to 94% estimated previously. And we now expect growth in this -- in net written premiums for this group to be between 4% and 7%, an improvement from the previous range of 2% and 6%, reflecting growth opportunities and strong pricing momentum in the majority of businesses in this group. And we now expect the Specialty Financial Group combined ratio to be in the range of 86% to 89%, an improvement from our initial estimate of 87% to 91%. Additionally, we raised our projection for growth in net written premiums to be in the range of flat to up 3%, a change from the previous estimate of down 4% to flat year-over-year.

Our guidance with regard to Property & Casualty net investment income has changed, with results in 2019 expected to be up 4% to 7%, an improvement from the previous estimate of 2% to 6%. And we expect overall Property & Casualty renewal pricing in 2019 to be up approximately 3%. Excluding workers comp, we expect renewal rate increases to be in the range of 5% to 6%.

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

Stephen Craig Lindner
Co-President, Co-CEO & Director

Thanks, Carl. I'll start with a review of our annuity results for the third quarter beginning on Slide 7.

Statutory annuity premiums were $1.1 billion in the third quarter of 2019 compared to $1.4 billion in the third quarter of 2018, a decrease of 22%. Higher traditional fixed annuity premiums were more than offset by lower fixed-indexed annuity premiums. In response to the continued drop in interest rates in 2019, we have implemented numerous crediting rate decreases in order to maintain appropriate returns on Annuity sales, which has tempered new sales.

In the second quarter of 2019, we changed the way we define Annuity core operating earnings. Beginning with the 2019 second quarter, Annuity core operating earnings exclude the impact of items that are not necessarily indicative of operating trends, such as the impact of fair value accounting for fixed-indexed annuities, unlockings and other items related to changes in the stock market and interest rates.

Core operating earnings now include an expense for the amortization of fixed-indexed annuity option cost, which is a better measure of the cost of funds for fixed-indexed annuities. We believe these changes provide investors with a better view of the fundamental performance of the business and a more comparable measure of the Annuity segment's business compared to its peers.

Turning to Slide 8. You'll see the components of pretax Annuity core operating earnings under this new definition. Results for the prior -- for the periods prior to the second quarter of 2019 are shown at a comparable format to the new definition of Annuity core operating earnings and are reconciled to previously reported Annuity core operating earnings. Growth in average invested assets contributed to higher year-over-year Annuity earnings, which were offset by lower earnings from investments mark-to-market through operating earnings and higher option costs. Earnings from investments mark-to-market vary from quarter-to-quarter based on the reported results of the underlying partnerships and investments. Higher amortization of option costs reflects growth in AFG's annuity business as well as higher renewal option cost related to the inforce business.

Turning to Slide 9. You'll see that our quarterly average annuity investments and reserves both grew by approximately 11% year-over-year. AFG's spreads in the third quarter of 2019 were lower than in the third quarter of 2018 as spreads in 2018 reflect higher returns on certain investments that are mark-to-market through operating earnings as well as the impact of higher option costs in 2019. I'm pleased with our results in this challenging interest rate environment. Our third quarter Annuity segment reflects -- results reflect a core operating return on equity in excess of 12%. Due to the significant decrease in both long-term and short-term interest rates throughout 2019, AFG performed a detailed review or unlocking of the actuarial assumptions underlying its annuity operations in the third quarter 2019. This review resulted in a net after-tax unlocking charge of $1 million or $0.01 per share. This unlocking charge is excluded from annuity core operating earnings and takes into account the negative impact of lower interest rates, which resulted in negative impacts related to lower expected future investment income and higher assumed persistency on certain blocks of business as well as the positive impact related to lower expected cost for fixed-indexed annuity renewal options, including anticipated renewal rate action.

AFG monitors the major actuarial assumptions underlying its Annuity operations throughout the year. Historically, the company has conducted detailed reviews or unlocking of its assumptions in the fourth quarter of each year. Beginning this year, AFG will conduct this review in the third quarter of each year. We believe that this timing is consistent with the norm for our publicly traded life and Annuity peers.

Please turn to Slide 10 for a summary of the 2019 outlook for the Annuity segment. Taking into account the new definition of Annuity core operating earnings beginning in the second quarter of 2019 and based on the $294 million of operating earnings reported by the Annuity segment in the first 9 months of 2019, AFG now expects its full year 2019 pretax Annuity core operating earnings to be in the range of $380 million to $400 million. This compares to the most recent guidance of $375 million to $405 million . Incorporated in our guidance is an assumed annualized return of 8% in the fourth quarter on investments required to be mark-to-market through operating earnings, in contrast to the 10.5% earned on an annualized basis in the first 9 months of 2019.

Our guidance also reflects the impact of lower interest rates, and particularly, the impact of lower short-term rates, which will have a negative impact on the Annuity segment's approximately $3 billion net investment in floating rate securities. In response to the continued drop in market interest rates in 2019, we've implemented numerous crediting rate decreases on our products in order to maintain appropriate returns on Annuity sales. Based on the results to date, we now expect 2019 Annuity sales will be down 9% to 10% from our record $5.4 billion of premiums in 2018. In addition to rate decreases on new Annuity sales, we've also begun implementing renewal rate decreases on certain inforce Annuity blocks of business.

Please turn to Slide 11 for a few highlights regarding our $54 billion investment portfolio. AFG reported third quarter 2019 net realized losses on securities of $14 million after-tax and after deferred acquisition cost. This compares to net realized gains on securities of $27 million in the third quarter of 2018. Approximately $20 million of the realized losses recorded in the third quarter of 2019 pertain to securities that AFG continued to hold at September 30, 2019. As of September 30, 2019, net unrealized gains on fixed maturities were $920 million after-tax and after DAC.

As you'll see on Slide 12, our portfolio continues to be high-quality, with 91% of our fixed maturity portfolio rated investment grade and 98% with a NAIC designation of 1 or 2, its highest 2 categories. We have provided additional detailed information on the various segments of our investment portfolio in the Quarterly Investor Supplement on our website.

I'll now turn the discussion over to Jeff, who will wrap up our comments with an overview of our consolidated third quarter 2019 results and share a few comments about capital and liquidity.

Joseph E. Consolino
Executive VP, CFO & Director

Thank you, Craig. Slide 13 summarizes AFG's third quarter consolidated core operating earnings results. AFG reported core EPS of $2.25 in Q3 2019. Core net operating earnings in the quarter were $205 million. The year-over-year increase in core earnings in the 2019 third quarter was primarily the result of strong operating earnings and investment results in our insurance businesses. Interest and other corporate expenses were $2 million higher year-over-year. Parent company interest expense increased by $2 million from Q3 2018. This is the result of the March 2019 issuance of $125 million principal amount of hybrid 40-year 5 7/8% subordinated debentures. Other expenses were flat year-over-year.

Slide 14 provides a reconciliation of core net operating earnings to net earnings. In the third quarter of 2019, AFG recognized $14 million, or $0.15 per share, in net after-tax realized losses on securities. Annuity noncore items reduced net earnings attributable to shareholders by $21 million, or $0.23 per share. Annuity segment noncore items include the negative impact of the decrease in market interest rates during the third quarter of 2019 as well as the $1 million unlocking charge that Craig referred to earlier. Finally, AFG's net earnings were reduced by an A&E reserve strengthening of $23 million, or $0.25 per share.

According to data provided by A.M. Best, industry 3-year survival ratios for asbestos and environmental reserves were 7.3x paid losses as of year-end 2018. The 3-year survival ratio for AFG's P&C insurance businesses now stands at 15.6x paid losses.

As indicated on Slide 15, AFG's adjusted book value per share was $59.65 as of September 30, 2019. Annualized growth and adjusted book value per share plus dividends was a very strong 18.2% for the first 9 months of 2019. We returned $36 million to our shareholders in the third quarter, with the payment of our regular quarterly dividend. In August 2019, we announced an increase in our regular annual dividend by 12.5% from $1.60 per share to $1.80 per share. AFG has increased its dividend in each of the last 14 years. The increased quarterly dividend was paid on October 25. Parent cash was approximately $270 million at the end of the third quarter. We maintained solid levels of capital in our insurance businesses to meet our commitments to the rating agencies. Our excess capital stood at approximately $865 million at September 30, 2019. We'll plan to hold approximately $200 million to $300 million of dry powder to maintain flexibility for opportunities as they arise. We'll evaluate our excess capital position before the end of the year. We note that the $1.50 per share special cash dividend paid in May does not preclude our consideration of additional special dividends or opportunistic share repurchases for the balance of 2019.

To conclude, Page 16 shows a single page presentation of our updated 2019 core earnings guidance. At the top of the page, you can see we're keeping the midpoint of our 2019 core EPS guidance the same at $8.60 per share and have narrowed the range from $8.50 to $8.70, to $8.50 to $8.70. Our guidance assumes an effective tax rate of approximately 20% on core pretax operating earnings. AFG's expected 2019 core operating results exclude noncore items such as realized gains and losses, annuity noncore earnings and losses and 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] And our first question comes from the line of Paul Newsome with Sandler O'Neill.

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

I wanted to ask about -- on the life side, that there's some investigations in the Teacher's Annuity business, and obviously, you have a relatively small part of that business. But any thoughts around indications on your relationships with how you do business with the Teachers on the annuity side that could be similar or different from [indiscernible] or some of the other companies?

Stephen Craig Lindner
Co-President, Co-CEO & Director

Yes. Paul, this is Craig. We have not received any kind of a notice related to that. And as a matter of fact, we're not licensed in New York, is my understanding at the -- at least the recent announcement was related to business being done in New York. To our knowledge, we're not -- it's not an issue at all with us.

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

Great. And then switching over to the property casualty side. I mean, obviously, the topic du jour of this quarterly earnings has been what happened to Travelers with their commercial auto business. And I think they're arguing at least that besides the relevant point of where you start from, like, a profitability point, your starting point, that there seems to be an acceleration of attorney involvement in claims that have been released over 2018. And as you probably saw, they put some slides out there that suggests that. Is that something you're seeing as well in your business, that acceleration in the tort environment? Or is it just not in your -- or you're -- maybe there's something else going on in your business that is different from a trend line on the claims side?

Carl Henry Lindner
Co-President, Co-CEO & Director

This is Carl. I think we've seen an uptick in severity going back to 2012. So hard to say whether there's an acceleration over the past year. We identified the first uptick, like I said, back in 2012, and we're in our 8-year of rate increase so -- and in underwriting actions. And I think that's why we we're blessed to be where we are profitability-wise at National Interstate and in our Great American Trucking. That said, we continued in the commercial auto liability part of the business. We continue to see the severity trend up, and that's the reason why we took 9% in price in the quarter. And because of those trends, we'll continue to be aggressive on price. We -- that's one part of our commercial auto business there at National Interstate that we feel we want to improve our underwriting profitability on even though we're making a -- probably a small underwriting profit.

Operator

And our next question comes from the line of Greg Peters with Raymond James.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

I'll focus on 2 questions in the property casualty business and then give Craig a chance to have another glass of -- another sip of water and ask an annuity question. First, in your comments, Carl, you mentioned how the 2019 year included some benefits -- earnings benefit from crop business from 2018. And then you went forward and said, it's reasonable to assume that because of the poor results in the 2019 crop year, you won't see that same sort of benefit in 2020. Now assuming I heard you correctly, I was wondering if you could give us some numbers around that?

Carl Henry Lindner
Co-President, Co-CEO & Director

We don't give specific crop numbers in that. We don't break those out. But you heard correctly. A lot of times, the -- we have not settled all the claims for a given year until the next year. So there's always the potential for favorable development or unfavorable development either way. And generally, we're fairly conservative. So there have been years where we've had favorable development when previous years turn out to be very good, and that was the case this past year. So yes, since we're saying this year, we feel like we're not going to make any money there. It's a 0 crop profit year. There's nothing at this point we feel that would get carried over into next year in the first half.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Yes. So I guess, since you're not giving us the numbers, it's probably not material to your overall consolidated financial position. At least that's what I'm going to infer. If I can pivot to the casualty business. I noticed a bunch of comments around pricing, about growth, and it usually came along with the caveat excluding workers comp. And I was wondering if you could update us on your views on your workers comp business. Is this a growth business for you? Is the rate environment still attractive for you to grow the business or -- give us a perspective on how you're viewing that business, please?

Carl Henry Lindner
Co-President, Co-CEO & Director

Sure. I'm happy to. Just to put things in perspective, workers comp is a little under 19% of our overall direct written premium that we're projecting for 2019. Our overall 9-month results for this year are very good, a healthy accident year combined ratio and a very healthy calendar year combined ratio through 9 months. And the outlook is the same for the whole year. Gross and net written premiums overall are down low single-digits for 9 months, and it would be about the same through year-end, and mainly reflecting the price decreases that there have been in some of our larger states in that. When you look at the pieces of our business, the large entities that make up are the acquisition of Summit, we're making a small accident year underwriting profit, a healthy calendar year underwriting profit. Price premiums down 3% to 4%. Price is down about 11%. The loss cost trends continue to be very favorable. In California, small -- which is a smaller part of our business these days, premiums are down about 9%, with pricing down 11% this year. We're projecting a modest accident year underwriting loss for our California business and about a breakeven calendar year number. So we feel California is a stable claims environment. We feel our reserves are strong in both our Summit and Republic parts of our business. Loss cost trends seem to -- in California, seem to be in control.

The other part of our business, National Interstate's comp business, is doing well. Our Strategic Comp, the large deductible part of our business, very healthy, accident year, calendar year and some little bit of growth there. So I think what's really driving the premium change are really because of the experience from the prior years has been continuing to improve over the past couple of years, that's brought about rate declines in a large number of states. So that's -- I think because of the rate declines, we don't foresee really there being a lot of growth. And in fact, as I mentioned before, through 9 months, our premiums are down low single-digit. Does that help?

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Yes. It does. Would you characterize your rate decreases in workers comp as being in line or better than what is coming out of NAIC?

Carl Henry Lindner
Co-President, Co-CEO & Director

I think it's generally in line.

Charles Gregory Peters

Raymond James & Associates, Inc., Research Division

Okay. So I thought I'd just pivot to Craig, and it sounded like you were -- you had a frog in your throat during your prepared remarks. Anyways, on Slide 15 of your supplement, you provide a very detailed breakout of premium by -- segment by financial institutions, by retail, by broker, et cetera. And it's noted because of what you said about the interest rate environment that your total premium volume is down pretty meaningful as it compared to certainly the fourth -- the third quarter of last year and then, of course, the fourth quarter -- or the fourth quarter and the first quarter of this year. And I'm just trying to gauge, looking forward, because it seems like there's further rate increases -- rate decreases that are possible. Is there going to be another step down in premium production? Or maybe I suppose it's contingent upon how the rest of the competitors are on the market. Maybe you could give us some perspective on that, Craig?

Stephen Craig Lindner
Co-President, Co-CEO & Director

Sure. First of all, thanks for letting me rest my voice for a couple of minutes. I Appreciate that. The environment has been pretty competitive this year, Greg. We historically have been faster to change rates from the downside and the upside when we see significant changes in interest rates. Some of our competitors, frankly, wait much, much longer than we do. Some of them don't make changes for, in some cases, 3, 4 or 5 months no matter what rates you're doing. We are much quicker to make changes and therefore, when interest rates are declining, we're reducing credit rates faster. It has an impact on our premiums. It has a negative impact on our premiums. When rates are going the other direction, we historically have been quicker to increase rates, again, to hit our targeted rates of return. And consequently, in those periods, our premiums typically grow faster than the industries. I mean my experience in the business is that over time, most competitors become rational. So -- and if you look at our history, typically, after a couple of very strong premium years, there can be declines for some period of time. But I think we have a great relationship with our distribution partners. I think on the investment side, we're among the best in terms of the performance. And I think our costs are competitive with about anybody in the industry. So long-term, I believe our premiums are going to be just fine and our market position is going to be just fine. I can't predict it quarter-to-quarter, but I feel very confident that certainly, over the next couple of years, premiums will regain a growth trend.

Operator

And our next question comes from the line of Amit Kumar with Buckingham Research Group.

Amit Kumar
The Buckingham Research Group Incorporated

Just a few questions. Maybe starting with P&C. I want to go back to, I guess, Paul's question on travelers comments. Is your book different versus what a travelers commercial auto book might be? Can we just, like, maybe talk a bit more about the quality or the nature of the book versus some other players?

Carl Henry Lindner
Co-President, Co-CEO & Director

Well, our book, obviously, is heavier passenger transportation and probably -- I don't -- I'm not a student of travelers business, but travelers probably is -- their book would be probably smaller to medium-sized in a risk for the biggest part would be my guess. That would be my understanding of the differences in that. We're -- again, we're focused on passenger transportation and different niches within the transportation side.

Amit Kumar
The Buckingham Research Group Incorporated

Yes. Okay. That's helpful. The second question I had was on Neon. And again, we've had a bunch of conference calls, so I might have missed if you made any recent remarks. Any thoughts on that going forward? I know there was a lot of comments in the trade press previously on that, and I'm curious if you had an update or how should we think about that going forward?

Joseph E. Consolino
Executive VP, CFO & Director

Amit, this is Jeff. Clearly, we don't endorse or comment on speculation in the trade press or things of that nature. So I really don't have anything to say about that. We were disappointed with Neon's results this quarter. It's disappointing because the third quarter of 2018 was one of Neon's better quarters. You'll see in the press release it contributed to a little bit of negative variance in our Specialty Casualty segment. We did hold our full cat load in the quarter to evaluate Dorian and other events that happened. So we didn't have cat earnings in the quarter, which is the heaviest cat quarter of the year. And then we were impacted by margin losses in our [blood] stock and some other areas that were above our expectations as well as some expenses related to the management changes that we announced earlier in the year. So we're working hard on the business. We believe that Lloyd's can be a good place to be a specialty insurance and reinsurance company. AFG is an excellent specialty insurance company, and we're working towards making Neon be the kind of business that's consistent with the results we can generate in our businesses here. And if we can get the appropriate return on capital there, Neon can be a part of our business for a very long time.

Amit Kumar
The Buckingham Research Group Incorporated

Got it. That update is actually helpful. The other question then. This might be for you, Jeff. On the excess capital, in the opening remarks you talked about nothing would preclude you from a special dividend in Q4. Can you talk about your appetite for what's out there? I'm curious just based on how the market has been, how the valuations are in the P&C space. Probably, should we lean more towards an excess -- I'm sorry, a special dividend at this stage? Or how should we think about that?

Joseph E. Consolino
Executive VP, CFO & Director

Amit, this is Jeff. As the CFO, I provide analysis and our CEOs determine what to do with excess capital, so I'm some going to invite Carl or Craig to comment on that.

Carl Henry Lindner
Co-President, Co-CEO & Director

I think the only thing we'd say at this point, Amit, is that we're going to take a look at what our capital demands are over the next month or so, and we'll determine whether we want to do another special dividend at that time. So that's probably the best I can do.

Amit Kumar
The Buckingham Research Group Incorporated

Okay. No. That's helpful. The other question I had was on your investment portfolio. You have, in the CLO's in that, there's obviously been a lot of discussion on CLO's going forward. I was curious if you had any COGS on that asset class? And how should we be thinking about your exposure to CLO's going forward?

Stephen Craig Lindner
Co-President, Co-CEO & Director

Yes. Amit, this is Craig. We do have investments in CLO's. The vast majority of the investments are in the very highly rated tranches, and we're very comfortable with the credit quality. We do invest a small amount of money in the equity portions where in most cases, we're actually the manager of the CLO's. It's been a great business for us if you include the fees that we get for managing that activity. The returns have been extraordinarily strong. So I don't think you're going to see a big change in our position there. We -- it's something that we obviously monitor very closely, but we're pretty comfortable with our position there.

Amit Kumar
The Buckingham Research Group Incorporated

Got it. And I guess staying on the topic of Annuity segment. Can you remind us with every 25 basis point shift, what is the impact on your sales? And how should we think about that impact on the book for 2020?

Stephen Craig Lindner
Co-President, Co-CEO & Director

So when you say -- you mean 25 basis points change in interest rates?

Amit Kumar
The Buckingham Research Group Incorporated

Yes, sir.

Stephen Craig Lindner
Co-President, Co-CEO & Director

So as it relates to premiums, it really depends upon what our competitors do with their credited rates. We are going to do our best to adjust credit rates to earn our targeted rates of return and, hopefully, our competitors are going to do the same thing. Historically, over time, they get disciplined, and our expectation would be that will be the case again this time around. But certainly, from the standpoint of industry sales of traditional fixed and indexed annuities, the environment is better in a higher interest rate environment than lower interest rate environment. In terms of our competitive position with the decrease in rates, we're trying to predict what impact on premiums might be. That's tough for me to do unless I know what the competitors are going to do with their credited rates.

Amit Kumar
The Buckingham Research Group Incorporated

Got it. That's helpful. And last question on P&C. Again, going back to, I guess, Paul's question. Broadly, when you look at the poor climate, the social inflation, the jury awards, there's obviously differentiated commentary coming from different players regarding how to think about margin expansion from here. I'm curious if you had any thoughts or are you thinking about your loss fixed differently versus maybe 1 or 2 quarters ago when you look at the climate out there?

Carl Henry Lindner
Co-President, Co-CEO & Director

Yes, Amit. We do actuary reviews on all of our businesses and had discussions with management every quarter. So as we see changes and trends or severity or frequency up or down, severity up or down, we're -- numerous times during the year, we're making whatever adjustments we feel are necessary to conservatively project what we think our current accident year profitability is business-by-business. So we're always thinking about those things, and we have a pretty specific process to address those changes in that. So in our case, sure, we have some concerns on more aggressive and effective attorney activity and the jury awards seems like the desensitization of jury awards and as it impacts various businesses. I think, in our case, we really see that in just a few -- more so in a few places. There's only -- overall, our loss cost trends were very stable. It would be a commercial auto liability, which I've kind of already talked about, and we've seen that for a long time. And actually, we continue to take a pretty big rate increase in the commercial auto liability part of our business to keep up with things. But that business is meeting our profit targets today, and in fact, we look at that as an opportunistic area as we have our house in order and, whether it's the Atlas transaction or being able to grow double-digit organically even outside of that. So we think we've been at that a long time. The D&O area is probably the second area that we kind of see the impact of those trends. And of course, we're adjusting our perspective on things in that.

In the D&O side, I think the good news, bad news for us, the good news is public D&O is really kind of where we're seeing those trends the most. In our case, public D&O only represents about 15% of our D&O premium in our executive liability business. And our limits are low. Our average net limits are under $5 million. So -- but we are adjusting rates, retentions, limits along with the market there. And our --

as our -- as with our commercial auto liability or commercial auto business, our overall D&O business is performing fine. It's the public D&O part that we'd like to see performing better. I think it's probably going to take a couple of years even with the size of the rate increases for the industry to achieve rate adequacy with some of the trends that everybody is seeing in D&O. So we'll be increasing our -- that part of our business with rate and very -- or increase our appetite cautiously as we feel rates are getting more adequate. But I think it's going to be a couple of years.

And then the other part of our business, a bit -- part of our business that's very profitable today and that we're pleased with but we're watching the loss cost trends, which are a little above normal for some of these same reasons is the excess liability, an umbrella area of our business. And particularly in -- when we look at our book, it's accounts with underlying commercial auto liability exposures that seem to be contributing to the severity in the excess layers, and we're taking a significant rate and taking underwriting actions also in our habitational part of our business there that we see some of those trends affecting. So overall, very pleased with our excess liability and umbrella business, and it's probably those 2 pieces of the business that we're seeing those trends impact the most.

I think, as we're opportunistic and entrepreneurial, and I think it's giving us some opportunities in that area. Frankly, we're growing double-digit and we're -- our renewal rate increases are double-digit in our overall excess liability and umbrella business. So I see that as an area of opportunity for us. Again, another example kind of like commercial auto where I think we have our house in order. And it's just a few pieces of the business that we're paying more attention to. So does that help?

Operator

And our next question comes from the line of Christopher Campbell with KBW.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Yes. My first question is on Property and Transportation. Were there any benefits from Atlas this quarter?

Carl Henry Lindner
Co-President, Co-CEO & Director

We're early on into the Atlas real transaction. There were some small amount of premiums in the quarter from Atlas, but I think it will be more significant as we move into the fourth quarter and next year.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. And then how much is that premium estimated? Is that about $100 million annually?

Joseph E. Consolino
Executive VP, CFO & Director

Chris, this is Jeff. What was disclosed as part of the transaction and by Atlas is the paratransit book is approximately $120 million. And so we've got the right to go through and work with them to write the business on our pricing terms. We hope to write it at the rates that we're comfortable with and will renew whatever business sticks at what we consider to be the right rate. That will be a 12-month cycle from start all the way through.

Carl Henry Lindner
Co-President, Co-CEO & Director

Yes. Chris, if I were to put a dollar amount on it, I think, probably in the fourth quarter we might see $10 million to $15 million of business. And then as we're working through some systems transition in that, which I think will improve our ability to renew the business going into 2020, so.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Great. That's helpful. And then also within Property and Transportation, you guys have some core loss ratio improvement this year, which has been the first time we've seen that get better year-over-year in a while. I guess, what are the big drivers there?

Carl Henry Lindner
Co-President, Co-CEO & Director

Well, I think the transportation results continue to be very strong. Property and the Marine, I think, there's been some improvement.

Joseph E. Consolino
Executive VP, CFO & Director

Chris, we improved in the quarter on the accident year ex-cat loss ratio by about 2 points. Property and Marine, our unit there, was responsible for the majority of that. In Aviation, it's not the results that we're hoping for. But compared to a year ago's quarter, we've see an improvement there as well.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Great. And then switching over to Specialty Casualty, I think the press release noted part of the growth was driven by E&S, but then you also had an adverse charge in that. So I guess, just how do feel comfortable growing that business and feeling that you're rate adequate right now?

Carl Henry Lindner
Co-President, Co-CEO & Director

Chris, could you repeat the question about the adverse charge, please?

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Yes. So I was just wondering is a big part of the growth this quarter in Specialty Casualty was called out to be E&S, excess and surplus, within the press release, but then you also had a reserve charge within that. Some I'm just trying to get a sense of where you guys feel you are in terms of rate adequacy.

Joseph E. Consolino
Executive VP, CFO & Director

Well, I'd default to what Carl had just said. Overall, we're very pleased with the excess and umbrella businesses that operate within that. They're performing at a high-level. There are places we're taking a look at and making sure that we're applying our underwriting criteria appropriately and writing the business we want at the rate we want. That's ongoing. But overall, I think Carl's comment was we feel like our house is in order there and we've got the opportunity to grow that business.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. And then just what loss cost assumptions do you have on the overall book? Like, I know some competitors used to have 3% to 4% and then they've increased those to maybe 4.5%. Where do you guys sit in general like on that boat? What's the long-term loss cost assumption that you guys bake into pricing?

Carl Henry Lindner
Co-President, Co-CEO & Director

I think probably in the range of 3.5% to 4%, something like that on a loss ratio trend for just that segment.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Got it. And then is that -- would that be similar overall? Or would that be slightly higher with commercial auto or, I guess, just...

Joseph E. Consolino
Executive VP, CFO & Director

Chris, probably commercial auto is seeing the highest loss ratio trend. But when Carl was talking in response to Amit's earlier question and recognizing social inflation, D&O is one place where we're seeing it, but that excess and umbrella business is certainly a place we're seeing it as well. It's a double-edged sword. You need to make sure that you've properly reflected it to maintain reserve adequacy and pricing integrity. But since new trends are well-known, that creates the rate opportunity that we're seeing. And since we believe that we are prudently reserved and well aware of the loss cost trends, we feel like, in a lot of ways, we're in a position to grow effectively in that kind of environment because we're not, for the most part, dealing with big problems.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. And then just -- I mean -- so if you're thinking about commercial auto are like, the rates like -- are loss cost trend like high single digits? Because you said -- I think Carl said, you guys were at target profitability and then looking to grow. So I mean, is it -- are you guys taking rates like in line with that and you guys think you can grow because everybody else in the industry needs to take more? I guess just what's the opportunity to take market share in commercial?

Carl Henry Lindner
Co-President, Co-CEO & Director

Well, we think -- again, we're in our 8th year of rate increase. And National Interstate, we took -- I think we've got about 5% in the quarter, and we had 9% commercial auto in commercial auto liability. Overall, National Interstate, loss ratio trends are 4%-ish, a little higher than average. And again, it was one of the areas that I had mentioned that severity is higher and that we're appropriately continuing to take rate. We'd like to improve our commercial auto liability combined ratio even more, even though we're profitable today. So we feel our house is in order, and we're able to continue to take advantage of opportunities. We're pleased to have the opportunity on the Atlas transaction at our prices. We're pleased to have an opportunity as the market is in disruption with lots of people taking care of business. We see that as -- we're opportunistic. With our house in order, we feel that we can carefully grow our business, and we're growing at double-digit today and also take it -- pick up some opportunities on the M&A side. So does that answer your question?

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Yes. It does. That's very helpful. And then one on annuity. So is $95 million a good quarterly run rate going forward, like, as we think about modeling into 2020? And what factors could put that at risk or either way, right? Which -- where -- what could help drive the outperformance? And then what could lower that run rate?

Stephen Craig Lindner
Co-President, Co-CEO & Director

Sure. Well, first of all, growth in the assets and reserves, obviously, is an additive. I mean, that's a plus factor. Swings in mark-to-market on the investments that are in that category that are mark-to-market quarter-to-quarter, their -- those investments continue to grow, but the returns have been very, very strong historically over the last couple of years. And our hope is that, that will continue, but that can obviously impact the quarterly numbers. And then the negative impact of lower short-term rates on our $3 billion -- or a little over $3 billion of floating rate securities, and we do hold some cash in addition to that. But I think as a starting point, the number that you threw out is probably a reasonable number. And then you have to make adjustments for growth on the positive side, impact of lower short-term rates on the negative side. So there are a lot of -- obviously, a lot of moving pieces that impact the profitability, but -- and just reinvestment rates right off of the existing portfolio and reinvestment at lower rates.

But I guess I would say the flip side to the negative impact of lower short-term rates is -- that are certainly are some investments that we've made over the last 3, 4 years that are big beneficiaries of the lower rates. We've been a fairly meaningful investor in real estate, specifically apartments over the last several years, and cap rates on the apartments just continue to come down. Most of those are held in partnerships that are mark-to-market. So if I were taking a guess on the marks, assuming interest rates remain low, I think the marks on those investments should be pretty positive going forward. So it's not all negative in terms of impact on investment income. There are some investments that we've made that will benefit from the lower rates.

Operator

And our next question comes from the line of Jay Cohen with Bank of America.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Just -- I think I know the answer to this but just for my modeling purposes, on the crop business, the benefit you had in the first quarter from the 2018 year, that all showed up in favorable prior year development. Is that correct?

Joseph E. Consolino
Executive VP, CFO & Director

Not entirely, Jay. Some of that would show up in commission adjustments, which would show up in acquisition costs.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Okay. I think I got that though. All right. Good. And then the other question, Specialty Casualty. As we look into 2020, it seems as if the E&S business given the rate increases has the potential to improve margins, one with respect, Neon, given the actions you're taking should see better margins and price increases -- better margins next year. Arguably, the workers comp business could feel some pressure on margins. All-in, just directionally, do you think the margins in that business should improve in 2020 versus '19? Forgetting any big catastrophes.

Carl Henry Lindner
Co-President, Co-CEO & Director

Jay, we're -- we haven't issued guidance for 2020. And we generally try to do a pretty accurate thoughtful job when we discuss that. So we haven't issued that. As far as your assumptions with rate should come margin improvement where we're getting rate ahead of loss cost trends. That would be accurate. And workers comp, as rates move down, I think it's a good assumption that even though our workers comp underwriting profitability is excellent, that we probably won't earn the same margins going forward. So I think all those things will get -- as we consider -- thoughtfully consider what our guidance should be segment-by-segment, sure, we'll pack all of those things into the guidance that we'll issue, so.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Got it. I will await that guidance when we hear it.

Operator

And our last question comes from the line of Larry Greenberg with Janney Montgomery Scott.

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

I really just have one question, and it also relates to crop and maybe picks up a little bit where Greg and Jay left off. If I look at the Property and Transportation unit over the last 4 years, so 2016 and then inclusive of this year, the first quarter almost always had the biggest reserve for leases. And so I guess, 2 questions. One, was there favorable crop in each of these 2016 to 2019 years? And then, two, is it reasonable to assume that the difference between the first quarter reserve development versus the other quarters of the year is mainly attributable to the crop contribution?

Joseph E. Consolino
Executive VP, CFO & Director

Larry, this is Jeff. I have to say that I'm not walking around with quarterly development going back all the way to '16. So I'm not really comfortable giving you a specific answer on that. I think directionally, you would have seen favorable crop development making a big contribution to last year's quarter. Maybe just taking a step back. Why do we feel like it was appropriate to make a comment about crop given that we're not issuing guidance for 2020 yet. If we're saying we have 0 crop earnings in the fourth quarter and we're not likely to -- if we don't say that we're not likely to see favorable claims development early in 2020, we just didn't want you all to say, well, crop is 0 this year, but were going to throw some amount in 2020, and that's going to be a significant growth because you need to be aware of the fact there was favorable development in the first half of '19. We'll give you a thoughtful answer on guidance, which I know Jay is eagerly awaiting, and we'll put that out when we put out our earnings in February.

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

But just -- you could pass on this one, too. I mean Just conceptually, would the difference between the first quarter and other quarters of the year be largely attributable to crop?

Joseph E. Consolino
Executive VP, CFO & Director

Larry, it depends on the year. And -- so we've had favorable reserve development from the other units within Property and Transportation over time. So I wouldn't want to isolate that just to crop.

Operator

Thank you. And that does conclude today's question-and-answer session. I would now like to turn the call back to Diane Weidner for any further remarks.

Diane P. Weidner
Assistant Vice President of Investor Relations

Thank you all for joining us this morning. We look forward to talking with you again as we share our results for the fourth quarter. Thank you.

Operator
Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.