S&P Capital IQ

CONTENTS

The Allstate Corporation NYSE:ALL

FQ1 2018 Earnings Call Transcripts

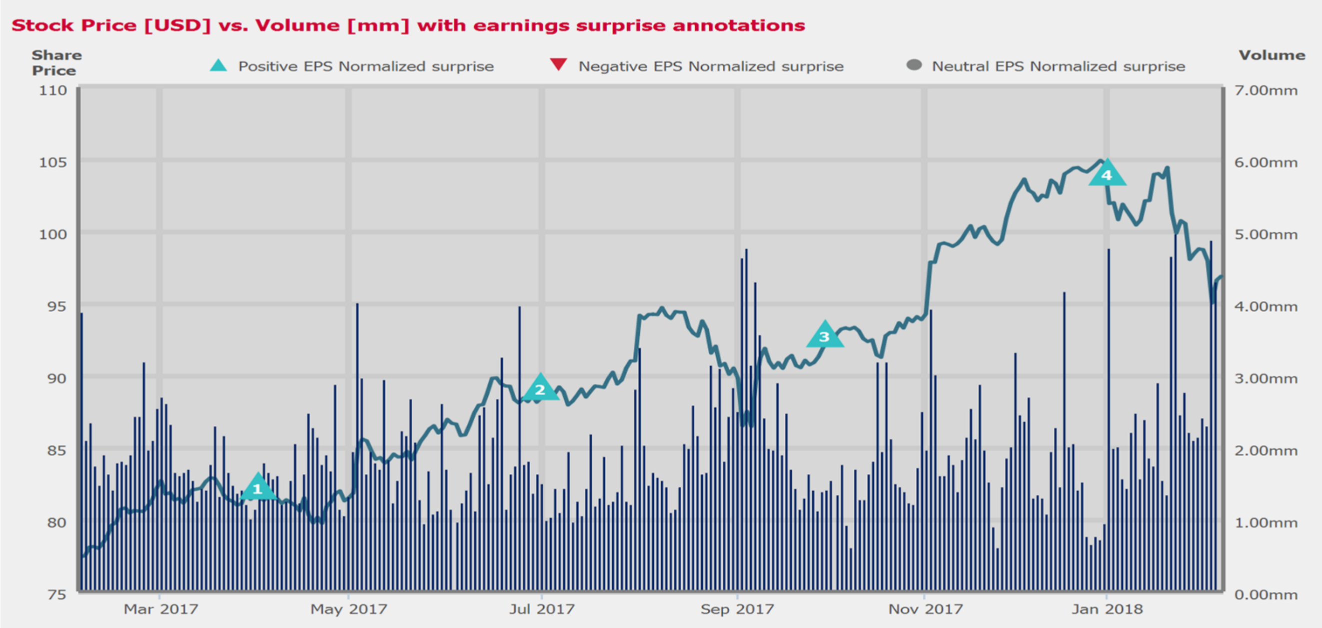
Wednesday, May 02, 2018 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2018-			-FQ2 2018-	-FY 2018-	-FY 2019-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	2.64	2.96	▲12.12	1.69	9.08	8.67
Revenue	-	-	▲3.25	-	-	-
Revenue (mm)	8025.14	8286.00	-	8111.00	32916.57	34083.29

Currency: USD

Consensus as of May-02-2018 12:58 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2017	1.10	1.64	▲49.09 %
FQ2 2017	0.90	1.38	▲53.33 %
FQ3 2017	0.83	1.60	▲92.77 %
FQ4 2017	1.53	2.09	▲36.60 %

Call Participants

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President of Allstate personal lines

John Edward Dugenske
President

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Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Allstate First Quarter 2018 Earnings Conference Call. [Operator Instructions] As a reminder, today's program is being recorded.

And now I'd like to introduce your host for today's program, Mr. John Griek, Head of Investor Relations. Please go ahead.

John Griek
Head of Investor Relations

Well, thank you, Jonathan. Good morning, and welcome, everyone, to Allstate's First Quarter 2018 Earnings Conference Call.

After our prepared remarks by our Chairman, President and CEO, Tom Wilson; Chief Financial Officer, Mario Rizzo; and me, we will have a question-and-answer session.

Also here are Steve Shebick, our Vice Chair; Glenn Shapiro, the President of Allstate Personal Lines; Don Civgin, the President of Service Businesses; John Dugenske, our Chief Investment and Corporate Strategy Officer; Mary Jane Fortin, President of our Life Retirement and Benefit Businesses; and Eric Ferren, our Controller and Chief Accounting Officer.

Yesterday, following the close of the market, we issued our news release and investor supplement, along with an update to our 2018 reinsurance program, filed our 10-Q for the first quarter and posted the results presentation we will use this morning in conjunction with our prepared remarks. These documents are available on our website at allstateinvestors.com.

As noted on the first slide, our discussion today will contain forward-looking statements about Allstate's operations. Allstate's results may differ materially from these statements, so please refer to our 10-K for 2017, the slides and our most recent new release for information on potential risks.

This discussion will contain some non-GAAP measures, for which there are reconciliations in our news release or our investor supplement.

We are recording this call, and the replay will be available following its conclusion. And as always, I will be available to answer any follow-up questions you may have after the call.

And now I'll turn it over to Tom.

Thomas Joseph Wilson
Chairman, President & CEO

Well, good morning. Thank you for joining us in staying current in Allstate's operating results.

Let's begin on Slide 2. So we had excellent execution in the operating plan, which increased growth and profitability in the first quarter. And we also benefited from an unexpected decline in auto accident frequency, lower catastrophe losses and a reduction in federal taxes.

Net income was $946 million or $2.63 per share, with adjusted net income of $1.07 billion or $2.96 per share. Adjusted net income return on equity was 15%.

In the table, you can see revenues grew 3.4% on the Property-Liability insurance premiums. Net investment income also increased on good performance-based result.

If you move to Slide 3, we're making good progress on all of our 5 2018 operating priorities. The first 3 priorities of better serve our customers, achieve target economic returns on capital and grow the customer base are intertwined to ensure that profitable long-term growth creates shareholder value.

We made progress on better serving customers as the Net Promoter Score increased. Customer retention improved in both the Allstate and Esurance brands, which is a key driver of growth.

Returns on shareholder capital were also strong. The property-liability recorded combined ratio of 88.0, generated $959 million in underwriting income for the quarter, which was an increase of $411 million from the prior year quarter. Auto insurance underwriting income increased to all 3 underwritten brands, and Allstate brand homeowners insurance continue to generate substantial income and benefited from lower catastrophe losses. Allstate Life and Allstate Benefits also generated attractive returns, in part due to lower taxes.

Going to the third one, grow customer base. Allstate brand policies in force increased as the auto and other personalized line grew over the prior year quarter. Esurance policies increased on growth in the homeowners line. Allstate Benefits continued its long track record of growth, with policies in force increasing 6.7%. And SquareTrade policies grew $11.9 million or nearly 40% compared to the prior year quarter.

Investment income increased due to continued strong results from the performance-based portfolio. Total return on the $83 billion portfolio was a negative 50 basis points, which included a stable contribution of about 1% in net investment income, but that was more than offset by lower fixed income valuations and a decline in equity markets.

Lastly, we're also committed to building long-term growth platforms. SquareTrade is making good progress on the objectives supporting the acquisition, and Arity is helping to drive the expansion of Allstate and Esurance's telematics utilization.

If you go to Slide 4, it shows the Property-Liability segment results by customer segment and brand. Starting with the table at the top. Net written premium was $7.8 billion, a 5% increase from the prior year quarter. The reported combined ratio of 88.0 was 4.9 points better than the first quarter of 2017 due to lower catastrophe losses, increased premiums earned and lower auto accident frequency. It was partially offset by higher operating costs and lower favorable prior year reserve reestimates. When catastrophes and prior year reserve reestimates are excluded, the underlying combined ratio was 84.2 for the first quarter of 2018.

As you know, our strategy is to provide differentiated customer value propositions for the 4 consumer segments in the personal lines insurance market. The Allstate brand in the lower left competes in the local advice and branded segment. Net written premium was 5.2% higher in the first quarter of 2018 compared to the prior year quarter. The underlying combined ratio was 83.2, slightly above the prior year quarter as continued improvement in auto insurance was offset by an increase in homeowners insurance.

Esurance in the lower right serves customers who prefer branded product but are comfortable handling their own insurance needs. Esurance net written premium grew 7.9% compared to the prior year quarter. The underlying combined ratio of 98.4 was 1.8 points better than the prior year quarter, with improvements in both auto and homeowners insurance.

Encompass in the upper left competes with customers who want local advice and are less concerned about the brand of insurance they purchase, so they mostly go through independent agencies. Premium declined due to the net impact of improving underlying margins. The underlying combined ratio was 87.9, up 1.3 points as we invest in building capabilities to support profitable growth.

John will now go through these Property-Liability results in more detail.

John Griek
Head of Investor Relations

Thanks, Tom.

Slide 5 shows the underlying drivers of policies in force for Allstate brand auto insurance.

Starting with the graph at the top. Overall policies in force grew by $52,000 or 0.3% in the first quarter of 2018.

The bottom 2 charts highlight our balanced approach to growing the business. The renewal ratio of 88.3 was an improvement of 0.9 points from the prior year quarter, benefiting from our continued focus on the customer experience and a stable rate environment. New issued applications grew year-over-year for the fifth consecutive quarter, increasing 17% compared to the first quarter of 2017. Growth in new business is due to improved competitive position, increased agency productivity and the expansion of the agency footprint.

Let's go to Slide 6 to cover the underwriting results for Allstate brand auto insurance.

Starting with the top left graph. The recorded combined ratio for the first quarter was 88.5, 2.2 points lower than the prior year quarter and generated $579 million in underwriting income. The primary drivers of profitability improvement were increased average earned premium, lower frequency and lower catastrophe losses. The underlying combined ratio of 90.0 in the first quarter of 2018 improved 0.9 points compared to the first quarter of 2017, driven by a 1.8 point improvement in the underlying loss ratio. The expense ratio of 25.0 was 0.9 points above the prior year quarter due to higher agent- and employee-related compensation costs.

The chart on the top right highlights the drivers of the Allstate brand auto underlying combined ratio. Annualized average premium, shown by the blue line, increased 4% to $1,029. While underlying loss and expense, shown by the red line, increased 3% to $926. This resulted in a favorable gap of $103 per policy. The positive gap between these 2 trends widened in the first quarter based on lower accident frequency, partially offset by higher severity and expenses.

The bottom left chart on this page provides Allstate brand auto property damage gross frequency and paid severity results indexed to 2013. In the first quarter, property damage gross frequency declined 2.5% compared to the prior year quarter, and favorable trends remained geographically widespread. After experiencing a sharp increase in accident frequency in 2015 and 2016, trends have improved. And as of the first quarter of 2018, property damage gross frequency is performing in line with levels experienced in 2014. While frequency has declined, property damage paid severity has experienced average annual increases of 4.3% since 2013.

The chart on the bottom right shows the quarterly trends for bodily injury paid frequency and severity. As you can see, these statistics can be volatile, given the timing between opening and settling claims as well as the impact of internal process changes. Given this volatility, we will no longer provide bodily injury paid statistics beginning next quarter. We will be reviewing other measures that could explain economic results on this longer tail coverage.

Slide 7 shows the operating results for Allstate brand homeowners. The top part of the page provides detail on profitability. Homeowners returns were good, with a recorded combined ratio of 80.8 in the first quarter, 12.9 points better than the prior year quarter due to lower catastrophe losses. Performance for this line is better evaluated over a 12-month period, given weather seasonality and variability. Allstate brand homeowners insurance generated $949 million of underwriting income over the last 12 months.

The bottom half of the page provides detail on policies in force. On the lower left, the renewal ratio of 87.5 was 0.4 points higher than the first quarter of 2017, and new issued applications growth accelerated to 14.7%. On the lower right, you can see the size of this line of business, which generates $6.9 billion of premium from 6.1 million policies.

Slide 8 provides financial highlights for Esurance. Esurance generated a combined ratio of below 100 in the first quarter, and policies in force grew. The recorded combined ratio of 99.3 in the first quarter, shown on the left chart, was 3.1 points below the prior year quarter, primarily driven by increased premiums earned and lower catastrophe losses, partially offset by increased loss costs. Esurance growth trends are highlighted on the right chart. Net written premiums continued to grow on increased average premium and policy growth. Policies in force increased 1.1% compared to the first quarter of 2017, after being relatively flat since 2015, which followed a period of rapid growth. This quarter's growth was driven by homeowners policies as auto policies in force were essentially flat to the prior year.

Slide 9 provides additional highlights for Encompass. Encompass continues to execute its profit improvement plan. Encompass' recorded combined ratio was 98.4 in the first quarter of 2018, 13.3 points lower than the prior year, primarily due to lower catastrophe losses. The underlying combined ratio of 87.9 for the first quarter was 1.3 points higher than the prior year period as a higher expense ratio more than offset improvement in the underlying loss ratio. Shown on the right chart, Encompass trailing 12-month net written premium declined 8.2%, and policies in force were 12.8% lower in 2018.

Planned reductions in states and local markets with inadequate returns has impacted overall top line trends.

Now I'll turn it over to Mario.

Mario Rizzo
Executive VP & CFO

Thanks, John. Let's go to Slide 10, which provides detail on the Service Businesses.

In the first quarter, revenue growth accelerated to $313 million, and policies in force reached $46.5 million. The adjusted net loss was $5 million in the quarter, a $5 million improvement over the prior year quarter as favorable loss experienced at SquareTrade was partially offset by investments in research and business expansion at Arity.

As you can see on the right, SquareTrade revenues were $122 million or $63 million above the prior year, with $30 million of that was due to the adoption of a new accounting standard.

Revenues from the other businesses were flat to prior year. SquareTrade also made progress on the 3 objectives supporting its acquisition in January 2017, as you can see from the box at the bottom of the slide. Policies in force grew to $41.8 million in the first quarter of 2018, an increase of $11.9 million over the prior year quarter, largely from domestic customers. Improved loss experience led to adjusted net income of $2 million in the quarter compared to an $8 million loss in the first quarter of 2017. The transition of underwriting risk to Allstate paper is essentially complete, and continued progress is being made, expanding European cellphone protection policies.

Turning to Slide 11. Let's review our Allstate Life Benefits and Annuities results. Allstate Life generated attractive returns on capital. Adjusted net income, shown in the top left chart, of $69 million in the first quarter increased $10 million compared to the prior year quarter. This is primarily due to a lower effective tax rate and higher premiums and contract charges, partially offset by adverse mortality.

Allstate Benefits adjusted net income, shown in the top middle chart on the page, was $28 million. The $6 million increase from the prior year quarter was due to higher premiums and contract charges and a lower effective tax rate, partially offset by higher contract benefits. Allstate Benefits continued its strong track record of growth, with premiums and contract charges, shown on the bottom middle chart, increasing 6.3% compared to the first quarter of 2017 and policies in force growth of 6.7%.

Allstate Annuities, on the far right, had adjusted net income of $35 million in the quarter and continued to benefit from good performance-based investment results. Economic returns remained low due to the relatively high regulatory capital requirements.

Slide 12 highlights our investment results. The chart at the top of the slide provides our asset allocation over time. We proactively manage our investment portfolio based on our long-term strategic risk profile, relevant market conditions and corporate risk appetite. We have increased the portfolio's equity allocation in response to historically low market yields and to utilize available risk capacity. Our performance-based investments, which now total $7.7 billion or 9% of the portfolio, are expected to deliver attractive risk-adjusted returns.

In the lower left, net investment income for the first quarter was $786 million, 5.1% or $38 million higher than the first quarter of 2017. Market-based investment income, shown in blue, was stable. Performance-based investment income, shown in gray, was the primary driver of the increase over 2017, generating

$181 million of income in the first quarter. Performance-based income was lower than the prior 3 quarters, which benefited from outperformance by certain investments.

The components of total return on our diversified $83 billion portfolio are shown in the table on the lower right. The return was slightly negative in the quarter, reflecting lower fixed income valuations due to increased market yields and a decline in equity markets. The 12-month trailing return was 3.8%.

With the adoption of the fair value accounting standard during the quarter, changes in the valuation of public equity securities are now a component of realized capital gains and losses as opposed to unrealized gains and losses.

Slide 13 provides an overview of our capital strength and financial flexibility. Our capital position is excellent. We delivered strong returns, increased book value and maintained a conservative financial position while increasing shareholder's ownership in the company by reducing the number of outstanding shares. Adjusted net income return on equity was 15% for the 12 months ended March 31, 2018, an increase of 3.1 points compared to the prior year period, and book value per common share increased 11.9% to $58.64.

We returned $465 million to common shareholders in the first quarter. This included repurchasing 3.5 million shares of our common stock for $333 million, leaving $935 million remaining on our current repurchase program.

We paid $132 million in common shareholder dividends. As a reminder, the Board of Directors approved a 24% increase in the quarterly dividend per common share to $0.46, which was paid on April 2 and is not included in the amount returned in the first quarter.

We continually look to optimize our capital structure. And in the first quarter, we issued $575 million of perpetual preferred stock and $500 million of senior notes. The proceeds of these issuances are for general corporate purposes, including the redemption, repayment or repurchase of certain outstanding securities.
Now I'll ask Jonathan to open the line for questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Greg Peters from Raymond James.

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

I suppose the most obvious place to start would be just around the underlying combined ratio guidance for the year. Considering that the first quarter result was substantially better than what your annual target is, I'm curious if your thinking has changed or what your perspective about that is. And also in the context of generating that really attractive result, I'm curious about what your view is on product positioning and competitive positioning in the marketplace.

Thomas Joseph Wilson
Chairman, President & CEO

Greg, this is Tom. I'll start, and then maybe Glenn can add color to that as well. So first, thanks for the question. Good morning. Based on the 3 -- 3-month result is too soon to change the underlying combined ratio guidance. The returns we earned on auto insurance are really good, even at the outlook range, and the best way to increase shareholder value at that point is to grow policies in force. We're obviously, as you point out, at the low -- below the low end of the range in the first quarter, and that was really due to an unexpected decline in auto accidents frequency versus the prior year. It looks like other companies experience similar declines in the first quarter, but that's based on only a really small sample of the overall industry. Our projections did assume that there would be an increase in auto accident frequency. And as you well know, auto accident frequency had been very volatile over the last 3 years. It increased significantly in 2015 and '16 and then decreased in 2017. Actually, you can see that on John's slide. And of course, the underlying drivers of frequency are miles driven, economic activity, how many people are working -- weather -- all of which are difficult to predict individually, in combination, and doing it geographically is nearly impossible. And so at this point, we're not changing our frequency outlook for the whole year or our underlying combined ratio look -- guidance. But let me give you a couple of math points as well. Auto frequency is usually highest in the fourth quarter. And the second half of the year has 3 more days than the first half of the year, and 1 calendar day has over 0.5 point of impact on the quarterly loss ratio, all other things being equal. So the returns we get are really good at any level, and so we're focused on maintaining that and growing. Our competitive position, Glenn could talk about it. But I would say from my standpoint, the best way to analyze the competitive position is your retention levels in your new business, and both are good.

Glenn T. Shapiro
President of Allstate personal lines

Yes. Thanks, Tom. And Greg, good question. On competitive position, we feel good about where we are from all the metrics we look at. We monitor our competitive position in every state and every market across the country. And if you look at how we're growing right now, we're growing in a pretty balanced way. As Tom said, we're retaining more of our customers. Always best to retain the ones we fought hard to attract in the first place. And our new business is up. With the new business up, if we were getting the same number of quotes but significantly increasing our closed rate, you look at it and think that we've broadened appetite or something in the way that we got it. But from a competitive standpoint, we're getting a lot of looks at people. We're getting a lot of quotes. Our quotes are well up. We're closing an appropriate amount of those, so our competitive position feels like we're in good shape.

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

Just as a follow-up, I know you mentioned in your comments about your emphasis on your agency and distribution force. And I was looking at some of the statistics on, I guess, Page 11 of your supplement.

And you talked about Allstate agencies, and it looked like it was down sequentially a little bit, licensed sales agencies, sales professionals and Allstate independent agencies. Maybe you could just provide some color around which of those buckets you expect to grow over the course of the next year or 2? And which might be deemphasized?

Glenn T. Shapiro
President of Allstate personal lines

Yes, Greg, I'm glad you pointed that out because I really think the way to look at this is on a year-over-year basis. We're -- we've been committed for several quarters. We've been talking about growing our distribution footprint, and I think we are effectively growing the distribution footprint. If you look year-over-year, we're up about 1,200 points of presence, 100 agents, 1,200 licensed sales professionals. When you look at this, much like a lot of our other results, there's a little bit of a seasonality to it. It's the end of the year. A lot of folks are running to get some people in place. The pipeline dries up a little bit. We tend to have higher turnover in the first quarter. But the first quarter this year, our turnover was less than what we anticipated, so that was favorable. So as you look at the starting point at the end of first quarter last year to now, we've got 1,200 more points of presence. A little bit down sequentially, but we're really always down sequentially at that we're less down than we would have anticipated at this point. So as we build throughout the year and we continue to look to increase our distribution footprint, we're starting from good foundation.

Operator

Our next question comes from the line of Sarah DeWitt from JPMorgan.

Sarah Elizabeth DeWitt
JP Morgan Chase & Co, Research Division

I guess, first, I was hoping, could you just elaborate a bit on what drove the unexpected decline in auto frequency? And do you have any view on what that could look like going forward?

Thomas Joseph Wilson
Chairman, President & CEO

Sarah, this is Tom. So it's really too early to tell what the drivers of it would be. When we look at a variety of items, there is no one thing that popped out in your mind, obviously, weather would have some impact in the first quarter, and there was different kinds of weather in different parts of the country. Secondly, when we look at miles driven, it's actually up a little bit when you look at our DriveWise data, so that wouldn't automatically lead you to conclude that it should be down. In fact, it would be opposite of that. So we don't have a good read now. And in often times, even in reverse looking at 2015 and '16, it's hard to determine attribution between specific elements. What we do know is that it was down, and obviously, we've reserved well so we're feeling good about where the profitability in the business is. But we also know that if it goes up, we're still positioned to be at very attractive returns in the business.

Sarah Elizabeth DeWitt
JP Morgan Chase & Co, Research Division

Okay. Great. And then just on the performance-based investment income, that declined quarter-over-quarter. How should we be thinking about modeling a good run rate for that?

John Edward Dugenske
President

Sarah, it's John Dugenske. Thank you for asking the question. First, I wouldn't view the quarterly decline is meaningful. If you think about how we own these assets generally, we own these assets versus longer-tail liabilities. The performance has been consistent with what we've hoped to achieve with the allocation over time. Looking at a little more detail, in any given quarter, you may get a specific event, a transaction where something is liquidated, a particular performance of an individual investment that may make those returns a little bit volatile. I would encourage you to smooth the data and look at multiple quarters and look at the overall trend. We -- notably, in the fourth quarter of last year, we had a number of very positive events, 3 liquidations of deals that just as well could have taken place this quarter but took place in the fourth quarter. It gave us a very good fourth quarter number, along with some other things. So overall, the trend is in place, and we feel good about it.

Sarah Elizabeth DeWitt
JP Morgan Chase & Co, Research Division

Okay. So just in terms of modeling that, if you -- $200 million or so is a good run rate?

Thomas Joseph Wilson
Chairman, President & CEO

Sarah, you might look at it as on a yield basis and on a rolling basis, so I know that's hard to stick into a quarterly number. But John is being a little humble. We had great results in quarters 2, 3 and 4 last year. The yield on that portfolio, if you just took income over the balance, was in the mid-teens. We did not expect to be in the mid-teens on that kind of level. We expect it to be above where you would get from equities, public equities. But so I think you really have to look at it on that basis, and we tend to think about it relative to the overall company in terms of volatility. I know you're looking at individual line. But catastrophe bounced around. Performance-based income bounces around. What we agree to -- or what we seek to do is to increase total long-term return despite the fact that it bounces around, and the fact that it does bounce around gives us the opportunity. And as we have the ability to enable and handle that volatility, gives us the ability to earn better returns.

Operator

Our next question comes from the line of Kai Pan from Morgan Stanley.

Kai Pan
Morgan Stanley, Research Division

Just first question, just a follow-up in the frequency questions. Just wondering if you could quantify the delta between the results versus your expectations.

Thomas Joseph Wilson
Chairman, President & CEO

Kai, we don't give out the subcomponents of our expectations because we'll only end up spending a whole bunch of time talking about it, assumptions, which on things like frequency, it's all an estimate. It's even hard to look backwards and determine why it happened. So we don't give out the subcomponents. Glenn, maybe you can talk a little bit about the absolute decline in frequency and where we saw it, and that will give Kai some additional color.

Glenn T. Shapiro
President of Allstate personal lines

Yes. So we saw -- obviously, we saw a decline in frequency. One way to look at this is as you compare to sort of the broader trends, like so we clearly have wind at our backs. When it comes to frequency, it's down. Our frequency appears to be down, as you look over the last few quarters, a little more than the industry. And some of that is, as our book shrunk a little bit, we got to a little bit higher quality on average of the book of business. In terms of -- just longer-term trends, there's a lot of -- as Tom said, it's hard to predict. There's a lot of different theories on there between miles driven, miles driven per operator, safety features in cars. So we'll continue to monitor that going forward.

Thomas Joseph Wilson
Chairman, President & CEO

So -- and I think Glenn is right, broad-based, geographically, decline in frequency this quarter, by accident type, it was down most of the accident types. Now the tenure of the customer was down across all tenures of customers. So it wasn't just one state, one group of customers, it was broad-based, which, as Glenn said, leads us to conclude that other people had the same thing, but we don't know that for sure.

Kai Pan
Morgan Stanley, Research Division

So just to clarify, you still expect positive frequency through the remaining of the year?

Thomas Joseph Wilson
Chairman, President & CEO

Kai, we haven't changed our underlying combined ratio outlook for the year would be the way I would say that.

Kai Pan
Morgan Stanley, Research Division

Okay. That's great. And then my second question is a -- more sort of like a high level. If you -- there's a recent IPO on the personal line brokerage, and they're looking into sort of -- they're growing very rapidly in the multi-carrier platform independent agency model. You -- Allstate have the platform, the Encompass, all this different distribution model. But the captive agency distribution is still the majority of the revenue as well as income. How do you feel about the captive model over the long run?

Thomas Joseph Wilson
Chairman, President & CEO

We like the Allstate agency model for a number of reasons. First, it gives us the ability to have the right price value comparison. When you're an independent agency channel, you often get spreadsheet [comparative rater], and it's harder to maintain consistency in your pricing. Secondly, the captive channel gives us the ability to really control the customer experience, which is really important when you're delivering value. And as we head into telematics, it gives us an ability to build even greater relationships because people will be more connected with us. That said, we think there is a place in our portfolio for all the businesses. So we like to do it direct with Esurance. We'd like to grow Encompass. We want to get its profitability right and get its capabilities positioned, which is, I mentioned, we're working on. So we'd like to grow on that channel as well. And of course, we have a platform which we believe is the biggest in the industry right now called Answer Financial, which does -- it's an electronic version of an independent agency, and it's got a very strong position. And we're continuing to build up that model, leaning into telematics on that piece as well.

Operator

Our next question comes from the line of Jay Gelb from Barclays.

Jay H. Gelb
Barclays Bank PLC, Research Division

As the Allstate brands auto policies in force are now growing, how can the company make sure it doesn't become impacted by the new business penalty, where the margins for the new business tend to be somewhat lower than legacy business?

Thomas Joseph Wilson
Chairman, President & CEO

Well, Jay, you're correct in that it's particularly in the preferred customer segment. There tends to be a new business penalty where you earn less money on a new customer than you would on somebody who has been around for 7 or 8 years, and so that is basically endemic to the industry and to growth. What I would say is I would maybe take your question, it's really not possible not to be impacted by that. But what I would say is we feel comfortable that we know how to manage growth and overall profitability, should be able to increase shareholder value by both growing and maintaining margins. And Glenn mentioned this. We run the business at a local level so we're looking at it by state, by product line, by risk class. We slice and dice it every which way. So to the extent that the growth would not be properly priced in certain places, we would obviously be able to -- we'd see that, and we'd react accordingly. And then I would also say the increasing use of telematics also helps us get even more accurate in our pricing.

Jay H. Gelb
Barclays Bank PLC, Research Division

That's helpful. The -- on the investment side, I guess, I was a little surprised that the market base, essentially the fixed income investment portfolio, investment income that, that generates was down year-over-year and then also versus the prior quarter. I thought with higher interest rates, that could be rising. What am I missing there?

John Edward Dugenske
President

Yes. Jay, it's John again. Thanks for the question. I would encourage you to take a look at the portfolio as a whole and think about how income has been generated that way. There are a number of dynamics going on in market base. First, as our performance-based assets increase, our market base assets decrease. So it's just a lower base by which it can generate income. Second, the asset mix within our market base assets changes. So generally, we've used high yields and other higher-yielding assets within market base to fund our performance-based assets. So lower balance and lower high-yielding assets will decrease that. We -- another thing to think about is just how does the book react to higher interest rates. Think about Allstate, real simply, it's 2 different books, our life and annuities business, which generally tends to be liability-matched, and where there's not a lot of new purchases, the turnover is very low. That doesn't react very quickly. Even within our protection businesses, only a small part of the portfolio will roll over in any period of time. Therefore, it only captures an interest rate rise gradually throughout the year. I can give you further statistics on that. But again, a real rough gauge would be if interest rates moved up 100 basis points across the course of the year, given turnover and everything else, expecting no other changes in the portfolio, we'd expect our yield to move up by 6 basis points or roughly $45 million to $50 million in net income.

Jay H. Gelb
Barclays Bank PLC, Research Division

That's really helpful. And then just finally, just wanted to recognize. I think this is the first quarter since 2007 the company has generated over $1 billion in operating income, and at the same time, the share count has been reduced by 40%. So keep up the good work.

Thomas Joseph Wilson
Chairman, President & CEO

Thank you, Jay. I was here then and I'm here now.

Operator

Our next question comes from the line of Paul Newsome from Sandler O'Neill.

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

I have 2 unrelated questions. The first one is there -- and that's not going to be on any [indiscernible] actually. The -- there's a lot of private equity and other folks looking to buy blocks of annuities. Do you have any additional thoughts on your own annuity and life books? And what you -- would you interested -- or have you thought about some of those increased demand for people to buy some of these blocks?

Thomas Joseph Wilson
Chairman, President & CEO

That's a really good question, Paul. The returns on capital are low for the payout annuity block versus the deferred annuity block. So we split it into 2 chunks. And the payout annuity block is backed a lot of structured settlements, really long dated liability, and it is underperforming. Our approach in -- with all of our underperforming business, as you know, has been to go at it multiple ways, to be proactive, to -- but take action. And that block is about $12 billion. So we're doing the same thing that we've done on all of our businesses. So just if you go back and go up a little bit, we transferred the VA block versus reinsurance in 2006. At first, we got lucky, and that was before the financial markets crash. We shut down sales in new annuities over a period of years. We saw that they can benefit for cash. So we've taken a variety of actions. What we've been doing on this one is, first and foremost, getting the investments correct. So that rather than funding that block with fixed income, we've been funding portions after 7 years with payout annuity or with performance-based, which generates a much bigger return. That generates more capital for us and makes it less underperforming on a long-term basis. What it does on a short-term basis is it makes it even more underperforming because you have to put up a whole bunch of capital for those equities even though you really shouldn't have to because the risk of being in equity. It's actually lower than the risk of being in fixed income for a long dated liability. So what we've been doing is working with NAIC to reduce the capital requirements, and we made some progress to the extent we can do that, that will enable us to free up some capital. At the same time, we're also looking at how we structure those investments so we may be able to structure them in different ways so you don't have to carry as much capital. Obviously, as interest rates go up, that should help that portfolio. And the lower tax rate has obviously also increased value. So we have improved value in that block. We have things to do to further improve it, but we're not done. And of course, our goal is to maximize our economic value for shareholders, so we'll continue to look at all different ways to do that.

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

My second question is, has there been any change on the regulatory front for the insurance business in your opinion?

Thomas Joseph Wilson
Chairman, President & CEO

Insurance, I missed that last part of the call.

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

Just any change in the regulatory environment in the insurance business?

Thomas Joseph Wilson
Chairman, President & CEO

Well, that's a broad question. I would say there are a couple of things from a regulatory environment that we're all looking at, one at cybersecurity. The New York Department of Financial Services brought out the new cybersecurity rules. We're all working hard -- we work hard anyway to make sure we're protected, but we're working to make sure we have those -- the specific element in those specific regulations covered. Secondly, there's always the issue of privacy in data. And you're starting to see it is not yet in insurance, but we're thinking about how would we deal with increased requirements on it. So as it relates to pricing, claims and a variety of things, I would say it's business as usual. Glenn, do you agree with that?

Glenn T. Shapiro
President of Allstate personal lines

Yes, I agree. There was a lot of discussion last quarter about with the tax change and everything, but we continue to work with regulators on a state-by-state basis. And our filing process is business as usual.

Operator

Our next question comes from the line of Bob Glasspiegel from Janney Montgomery.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

Question on where we are in the competitive landscape, which you have sort of spoke about. As we look to the rest of the year, it looks like the industry came in maybe 3 points better in 2017, and your key competitors were around 103. But if you take Allstate and Progressive, they were 106. So we're trying to sort of handicap or I'm trying to handicap how the -- your mutual competitors and Travelers and Progressive are going to take the rate actions over the balance of the year. Looks like you're competing and winning on the margin. But are we looking at rate increases to be more moderate by your competitors? And where do you think the world is going, rate-wise?

Thomas Joseph Wilson
Chairman, President & CEO

Well, we don't know, Bob. I can't tell you what everybody else's plans are. We see the same numbers you see, and perhaps, at a greater level of granularity. So we look at Progressive, GEICO, State Farm not only in total but by state, by risk class. We think some of that group still has some -- if we were them, we would be increasing prices. I don't know what they will do, given that we are not them. But Glenn can talk about our rate outlook for the future, which is modest.

Glenn T. Shapiro
President of Allstate personal lines

Yes. If you look at our -- where we are now, it's always dangerous to talk about this in a global level. Because as Tom said, it really is state-by-state. We have rate need in some places, and we don't in others. Broadly speaking, we're clearly in a better pricing and rate situation than we were a couple of years ago. I would also caution you as you think about that, Bob, to look at what happened from the last year because a lot of what -- is in the result this year as what rates they took last year. So when you look at whether it's the CPI and compare to how rates are coming in, in auto insurance in the first quarter, it really is the rate that we're taking over the last 12 months, and so a lot of this year is already baked from whatever folks did last year in the rates, and what they do this year is really more on a forward-looking basis.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

It looks like you and Progressive's margin -- underwriting margin versus the industry just continues to widen year after year. I think I had it at 12 points for the 2 of you versus the industry last year. Is it technology pricing? You got the rates up right? What do you think sort of explains how your margin versus the industry continues to widen on an auto basis?

Thomas Joseph Wilson
Chairman, President & CEO

Yes. I think, Bob, when you look over a long period of time, Progressive, Allstate and GEICO are, combined ratios, looked to be about the same and much better than the industry. The 12 points seems like a bigger gap to me than I've seen versus the industry, but we have traditionally been about the same zone. I think, yes, in part, pricing accuracy, I think it's a different view as to what return on capital we want to get out of the business. Mutual companies have a different view as to what their capital objective function is. But -- and I think we're effective and efficient in the way we do it. That would be auto insurance. What I would say in homeowners insurance is we appear to be substantially better than the other people in industry, and I don't think there is many companies with our size and scale that generate the kind of income we have. And if you look at the slide John showed, it's over $900 million of income from underwriting income from homeowners business in the last 12 months, and it's been pretty consistent like that for 5 or 6 years. So I would not ignore the benefits that we generate from being in the homeowners business.

Operator

Our next question comes from the line of Josh Shanker from Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

So looking at the growth rates of Allstate brand and Esurance. Obviously, Esurance is a much smaller base, but there's a lot of natural growth in direct. I would have thought you'd be adding policies in direct at this point in time right now, given that I assume the pricing metrics you have around both distribution channels are similar. Why is the Allstate brand channel growth here than direct? Is there a theory behind that? Or is it just times changed and different products sell better at different times?

Thomas Joseph Wilson
Chairman, President & CEO

First, I don't think there -- you're appealing to different customers, different geography bases, and therefore, different competitive environments. We feel good about the Allstate brand business, and that's really been coming -- as Glenn said, we expanded distribution all through last year. You didn't see it any in last year's numbers, but you see it this quarter. And we would expect that growth to continue in terms of distribution, and hopefully, that will turn into growth in items in force. So Esurance, slightly different position. Its growth is really driven by expansion in homeowners. But we think there's plenty of opportunity to grow Esurance as well. You just didn't see it this quarter. So I think both businesses, we would expect to grow items in force as we go forward from here.

Joshua David Shanker
Deutsche Bank AG, Research Division

Okay. Sometimes I tell people it's hard to tell why stocks are going to go up in the future as it is to explain what they did in the past. And I think you've talked around this, but I hope you can answer the question better than me. We have enough time past the 2015 frequency spike, and now we are in a frequency -- I don't know what even to call it right now. Levels proved they were lower than they were before the spike back then. I think you touched upon it, but I'm hoping maybe of a little better color. Is there a grand theory about why frequency went up 3 years ago and maybe another grand theory about why it seems to be coming down right now?

Thomas Joseph Wilson
Chairman, President & CEO

A grand theory makes it sound like there's like one reason. So no. I would say -- so look, frequency came down for a long, long period of time because we had third tail light, anti-drunk driving laws, 3 cars per household versus 2 drivers, antilock brakes. There's a whole variety of things that happened. And then it kind of leveled out for a period of time, maybe 5, 6 years. And then in 2015 and '16, it spiked up. Some of that was obviously related to economic activity, more people back at work. Because about 1/3 -- if you look at where people drive their cars, about 1/3 is to work, about 1/3 is on errands, and 1/3 is for leisure. So they were driving more to work. And if you have more money, you do more leisure. And so miles driven went up, so people got more accidents. Some people would say it was somewhat related to distracted driving. I think that's impossible to predict because you're talking about knowing whether somebody was looking at their phone or just put their phone down right before they got in an accident. That information just is not available, so people are looking at results and trying to come up with concluding as to why it might be that way. What we do know is that it went up, and we had to react. It went up for 2 years in a row. We increased our prices to account for it. It came down last year. And I think the clarity on that is as clear as the increase, which is we just know it went down, and that puts us in a better profit position and gives us the opportunity we need to grow. It was down this quarter. But I don't think you should take that to a trend. I think frequency bounces around a lot. And when we give our underlying combined ratio guidance, it's because it does bounce around. It had nothing to do with our view on the economics of the business. We earn really high economic rents from our customers because we do a really good job for them. And we do that when our competitors don't. So it's not like we're taking advantage of anybody. We're just good at what we do. And we think that auto business is a good profit generator and a growth vehicle. It will be in the future, irrespective of what happens to frequency.

Operator

Our next question comes from the line of Yaron Kinar from Goldman Sachs.

Yaron Joseph Kinar
Goldman Sachs Group Inc., Research Division

Just a couple of quick ones, I think. So looking at the 17% year-over-year growth in new issued applications in Allstate brand auto, did you see momentum accelerate there over the quarter? Or did it decelerate? Was it roughly constant?

Thomas Joseph Wilson
Chairman, President & CEO

The 17% year-over-year growth in new business, I think, Glenn, the question was...

Glenn T. Shapiro
President of Allstate personal lines

Yes.

Thomas Joseph Wilson
Chairman, President & CEO

Accelerate. Well, you're getting into monthly numbers, which we don't disclose.

Glenn T. Shapiro
President of Allstate personal lines

Well, so thanks, Yaron. First of all, the growth came in pretty balanced way. We got growth across a lot of different states. We got growth in areas that we targeted that we want growth. We invested in local marketing. What I would say is that it's been pretty balanced and pretty healthy in that the whole system is responding right now. As Tom mentioned, we've talked about for a few quarters the fact that we're trying to grow our distribution system but also make it more effective. So I'd say, one, it's growing, I mentioned that before, 1,200 more points of sale out there and less turnover. Two, the system is more efficient. We've got quotes per agent up, new business per agent across the country up. We have -- we're serving our customers’ needs more broadly because we're selling across the system more so even -- and I know you're talking about the 17% in auto, but we're up 15% new business in home, too. So we're selling across the system more effectively. And then, and I think maybe most importantly, is the system is investing in itself right now. Agents feel good. Everywhere I go across the country, agents are positive. They're feeling good about their opportunity, their economic opportunity in the system. They're marketing in their local environments. They're hiring staff and leaning in. So all of those elements are really driving pretty broad growth.

Yaron Joseph Kinar
Goldman Sachs Group Inc., Research Division

That's helpful. And then my second question is around prior year development. So the adjustment for the company's bodily injury claim handling has clearly been a positive for favorable prior-year development. How much longer do you think this favorable tailwind continues? And then are there other initiatives in place or on the way that could lead to lower losses or more efficient reserving?

Mario Rizzo
Executive VP & CFO

Yes. This is Mario. So I'd say, look, we are continually looking at our reserve balances across all coverages, and we feel really good about where our reserve position is. Because of some of the things we've done on the claim side to manage, particularly the injury coverages, we've seen some favorable development over the last several quarters, I would tell you it's -- I'm not going to sit here and predict whether that'll continue or not. I will tell you we'll continue to look at reserves. And claims, I think, is a process. That's a moving target. You always want to get better in your claim handling. And when we talk about continuous improvement, that's really an area where continually reinventing ourselves in how we handle claims is really a critical part of our business model. And we've been pretty successful at that, historically, and I think that what's generated some of the equity you've seen in our reserve position. But we feel good about our reserves. We'll keep looking at then. And it's hard to predict whether they'll continue to favorably develop at the same pace.

Operator

Our next question comes from the line of Elyse Greenspan from Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

I -- my first question is just on the capital side of things. You guys issued debt and some preferreds in the quarter. Can you just update us, is this part of just normal adding to your leverage? Do you see yourselves as using it to your buyback? Or is there may be a component of having some capital flexibility for future acquisitions built in there? And then if there is a component of flexibility for acquisitions, if you could just update us on some things that you might be thinking about in terms of that could be additive to the Allstate profile.

Mario Rizzo
Executive VP & CFO

Thanks, Elyse. This is Mario. So I guess, where I'd start it, we feel really good about our capital position. We had a really strong capital position overall. And having said that, we're always looking for ways to optimize our capital structure. And what you really saw in the first quarter was an opportunity to issue security at attractive levels both from a senior debt perspective as well as perpetual preferred stock, which we view as really a permanent part of our capital structure. So we did the issuances. We're going to use the proceeds to pay down some debt. That's maturing in May. And also call some junior subordinated debt that had lost equity credit, and then on a floating rate basis, had a relatively higher coupon. So we're going to do that. We're going to swap out some debt for some of the debt that just we issued at more attractive rate. And then we have the opportunity -- and we haven't decided on this yet. We have the opportunity to call some of our preferred stock later in the year. And we took the opportunity to issue, again, what we view as permanent capital at really attractive levels, and we'll make that decision in terms of what to do with the proceeds going forward. But we feel very good about where we're at from a capital perspective, and we really like the flexibility that gives us both to invest in growth in the business and look for other opportunities that might come along.

Thomas Joseph Wilson
Chairman, President & CEO

And with our capital position, earnings power, we don't need to pre-fund anything to do an acquisitions. We don't need to go out and raise money in advance to try to do some. If we wanted to do something, we would just fund at that point in time.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And are there -- is there something, Tom, on your radar screen? Or it's just dependent upon maybe some things that become available on the market?

Thomas Joseph Wilson
Chairman, President & CEO

If you look at our track record, we're not averse to buy things, but we're kind of picky. And it's got to be related to our strategy, and that has to be a good company. So SquareTrade, which we bought a little over a year ago, was related to our strategy to insure more things for people, and particularly the electronic items that they have. And Don, you might want to just comment on how we've done relative to that. But we said we're thoughtful about it. Other places we might look would be to extent we could expand other lines of business that were -- could be sold by our agencies, Allstate agencies, would be interesting to us. And then as -- there is always new stuff in the market. So we're not averse to it, but I don't have like a list of here's 5 companies we have to buy so that we can be strategically sound. We're in a really good position. Don, maybe you just want to mention the -- about SquareTrade.

Dogan Civgin
President of Service Businesses - Allstate Insurance Company

Yes. Look, the first full year is behind us now. And as I'm sure you were all thinking about a year ago, a lot can go wrong when you do an acquisition, we laid out 3 objectives for the acquisition. I'm happy to say we're hitting all of them. The first was growth. And you can see, again, this quarter continued growth both in policies and in premiums. Second was to be able to improve the returns in the business. And as Mario mentioned, we've taken more of the underwriting in-house. But on top of that, the loss ratios are running well, and the company is performing well from a profitability point of view. The third was to improve their growth opportunities outside U.S. retail, which is where the main business is, and they've done a really nice job in that. The European business, albeit a little under 10% of their total book, has nearly doubled in the last quarter. So the 3 objectives we set, I feel like we're hitting all of them. If you remember, we did the acquisition, we said we chose SquareTrade because they were service-obsessed, and that fit well with the way we want to treat our customers. Having met with a number of their existing and prospective customers, I can tell you they are really good at onboarding and serving their end customers and creating value for the retailers. So I feel like we made the right choice. Glad we did it. And if we had that choice again, I'd do it in a heartbeat.

Thomas Joseph Wilson
Chairman, President & CEO

And maybe just add one other piece there. So when we talk retailers, that's both electronic and big box.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Okay. Great. And then just really quickly on SquareTrade. There was a $30 million boost to the top line from the accounting change in the quarter. Was there any impact from that accounting change on the bottom line earnings in the quarter?

Mario Rizzo
Executive VP & CFO

No, it was net neutral to income. It was just a revenue impact from the accounting change.

Operator

Our final question comes from the line of Amit Kumar from Buckingham Research.

Amit Kumar
The Buckingham Research Group Incorporated

I guess, very quickly, just going back to the questions on the unexpected decline in frequency. Should investors brace for a time when we would have an unexpected reversal in frequency, too? Is that a subtle takeaway in constantly reminding us that this frequency is an outlier? How should we think about that?

Thomas Joseph Wilson
Chairman, President & CEO

Amit, I think you brace for things when something bad is going to happen to you. What I would say is our auto business is very profitable. It would be very profitable, and we should be growing it even if we were at a combined ratio that was 86 to 88, which is our annual outlook. And so what I think investors should be excited about is the fact that we have a business that is very profitable. It's -- we're starting -- that business is starting to grow, and that should add -- increase shareholder value when it was getting smaller over the last couple of years as we improved its profitability. So we no longer need to do that, so we're on the offense of now beginning to grow that business. And I think that's what investors should be focused on versus it's -- this is not just a profit machine. It's a shareholder value machine. We got auto insurance. We got home insurance. We got our performance-based stuff. We got our life business, its benefits. We got SquareTrade. And all of those things create incremental value for our shareholders, and they're consistent with our strategy. So I think the -- to get too focused on one specific measure, and that in -- it's just the wrong way to think about it investing in our company. That's not the way we run the company. We run the company for long-term shareholder value. And so I wouldn't get -- I wouldn't brace for anything. I would be looking forward and being optimistic about the amount of money we're making in this business and how we can grow it.

Amit Kumar
The Buckingham Research Group Incorporated

Got it. But the only other quick question I have is on the pricing discussion, and we didn't spend time on discussing the rate trends, which you have shown on Page 18 of the supplement. How should we think about, I guess, the trajectory of rate filings from here?

Thomas Joseph Wilson
Chairman, President & CEO

Well, we've talked about this before. Given the kind of combined ratios we have, you shouldn't expect to see big increases in the top line on a average premium standpoint, but we'll make up for that in part by growing the business. So it's -- I will just say don't get too focused on the one measure of performance on one line for the entire company. This is a large corporation. We got lots of ways in which we make money and add value to our customers. All of those did really well in the first quarter, better than we expected. And even if they had been at the level we expected, it still would've been a great quarter. So I feel like there's -- don't get too focused on one item, really think about the whole value creation, and we got lots of value to create by growing the business at really attractive returns.

So thank you all. We're off to a good start. We look forward to seeing -- talking to you in the second quarter.

Operator
Thank you, ladies and gentlemen, for your participation in today's conference. This does conclude the program, you may now disconnect. Good day.