S&P Capital IQ

CONTENTS

The Allstate Corporation NYSE:ALL

FQ2 2014 Earnings Call Transcripts

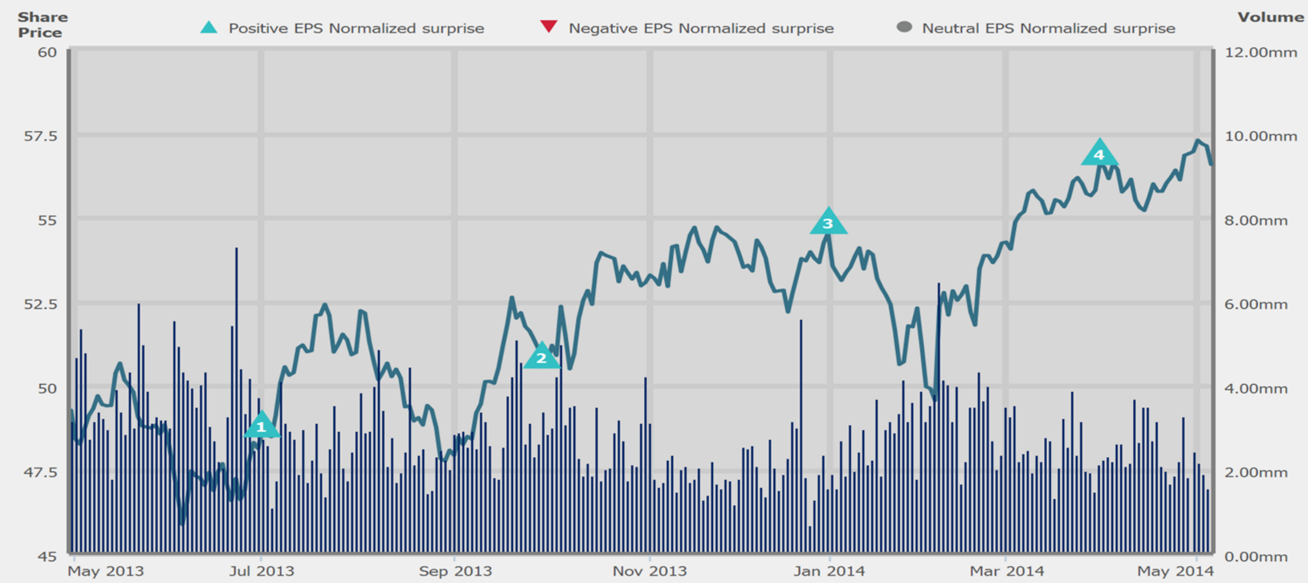
Thursday, July 31, 2014 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ2 2014-			-FQ3 2014-	-FY 2014-	-FY 2015-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.68	1.01	▲48.53	1.20	4.91	5.72
Revenue (mm)	7195.30	7204.00	▲0.12	7369.79	28949.73	30118.63

Currency: USD
Consensus as of Jul-31-2014 12:04 PM GMT

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



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2013	0.98	1.12	▲1 14.29 %
FQ3 2013	1.38	1.53	▲2 10.87 %
FQ4 2013	1.37	1.70	▲3 24.09 %
FQ1 2014	1.18	1.30	▲4 10.17 %

Call Participants

EXECUTIVES

Donald J. Bailey
Former President of Emerging Businesses

Matthew E. Winter
President and President of Allstate Insurance Company

Patrick Macellaro

Steven E. Shebik
CFO & Executive VP

Thomas J. Wilson
Chairman & CEO

Unknown Executive

ANALYSTS

Jay H. Gelb
Barclays PLC, Research Division

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Kai Pan
Morgan Stanley, Research Division

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

Presentation

Operator

Good day ladies and gentlemen, and welcome to the Allstate Second Quarter 2014 Earnings Conference Call. [Operator Instructions] As a reminder, today's program is being recorded. I would now like to introduce your host for today's program, Pat Macellaro, Director of Investor Relations.

Please go ahead.

Patrick Macellaro

Thanks, Jonathan. Good morning, everyone, and thank you for joining us today for Allstate's second quarter 2014 earnings conference call. After prepared remarks by Tom Wilson and Steve Shebik, we'll have a question-and-answer session.

Yesterday, following the close of the market, we issued our news release and investor supplement, filed our 10-Q for the second quarter, posted a slide presentation to be viewed in conjunction with our prepared remarks. We also posted an update to the description of our reinsurance program. These are all available on our website at allstateinvestors.com.

As noted on the first slide, our discussion today may contain forward-looking statements regarding Allstate's operations. Allstate's results may differ materially from these statements, so please refer to our 10-K for 2013, our 10-Q for the second quarter, slides and our most recent news release for information on potential risks.

Also this discussion will contain some non-GAAP measures which there are reconciliations in our news release and on our website. We're recording the call today and a replay will be available following its conclusion.

I, along with Steve Shebik, will be available to answer any follow-up questions you may have after the call.

And now, let's begin with Tom Wilson.

Thomas J. Wilson
Chairman & CEO

Well, good morning and thank you for investing your time to keep updated on Allstate's progress.

In addition to Pat and Steve with us today in the room is the team that delivered these results. Matt Winter, who leads Allstate personal lines; Don Civgin, who's responsible for Allstate Financial and Insurance; Kathy Mabe, who leads Business to Business; Judy Greffin, our Chief Investment Officer; and Sam Pilch, our Corporate Controller.

Let's begin on Slide 2. Allstate's second quarter results demonstrated our ability to concurrently grow the business and generate attractive returns. Our strategy to create unique customer value propositions for each consumer segment is working and has helped us compete in new and different ways. So in the last 12 months, we've added almost 750,000 Property-Liability policies in force.

In addition, we added another 900,000 relationships through our Good Hands Roadside in Allstate Benefits offerings. Positive growth momentum is building, particularly in the Allstate brand.

Secondly, we made good progress on all of our 2014 operating priorities.

Third, we recorded very good financial results. Net income was $614 million for the quarter, which you can see in that bottom table, which was higher than last year since there was a loss on the extinguishment of high-cost debt in the 2013 results.

Operating income was $1.01 per share, excellent results in light of incurring $936 million of catastrophe losses. Strong underlying profitability, lower expenses and good investment results all contributed to the positive operating result. The decline in operating earnings versus the prior year was due to higher catastrophe losses.

Lastly, we improved our financial strength while returning capital to shareholders. The 18-month $2.5 billion share repurchase program approved in February is now 40% complete after 4 months. Open-market purchases were made throughout the quarter to accelerate the stock repurchase program and the company share repurchases, which were alongside that program. I think, when you look at the supplemental number of people that didn't understand the fact that the company's repurchases are in addition to the open-market purchases made under the ASR.

Overall, we're executing well and we're poised to grow with attractive returns and further leverage our capabilities to create shareholder value.

We go to Slide 3, this visually combines our strategy and our current operating results for each customer segment. So overall, the 750,000 increase in Property-Liability policies represents a unit growth rate of 2.2%. Increased average premiums for our Allstate Protection net written premium growth to 5.5% over the prior year.

The reported combined ratio of 97.4% reflects 13 points of catastrophe losses. Therefore, the underlying combined ratio for the quarter was 84.7%.

Let's walk through each of the customer segments, starting with the Allstate brand, which represents 91% of written premiums. As you can see in the lower left quadrant, Auto policy growth increased again this quarter and was 2.3%. Working across the growth line, the decline in homeowners continues to shrink and was now down to 0.5% this quarter. Other personal lines are growing, bringing total policy in the fourth -- force growth in this segment to 1.5% and net written premium growth to 5%.

We're also pleased with the profitability in this segment with a recorded combined ratio of 95.4%, which you can see in the third line on the far right there. If you go back to the left, the Auto reported combined ratio was also 95.4%, which results from a disciplined and precise set of operating processes focused on matching price to risk and costs. We continue to have modest increases in Auto prices, which were up 0.5% this quarter, excluding Canada.

A few analyst called about the investor supplement, which shows no increase in total because it impacts a large mandatory reduction in Ontario auto pricing.

Another measure of Auto pricing discipline is average gross written premium, which is 2.6% higher than a year ago.

Moving to the next column. The reported homeowners combined ratio was 98.6%, despite almost 39 points of catastrophe losses. An underlying combined ratio of 60.2 for this product gives us confidence that we can create shareholder value and improve our competitive position by growing this line.

Esurance in the lower right had another quarter of strong growth with policies in force of 17.5%, although this is lower than last year, as expected. The combined ratio of this brand reflects the immediate expensing of acquisition costs has improved from last year due to profit-improvement actions taken to ensure we get acceptable economic returns.

Encompass in the upper left also continued to grow policies, but at a slower rate than last year, also as expected. With an underlying combined ratio of 94.8%, there's still more work to be done to raise returns.

Answer Financial sells nonproprietary policies, that's in the upper right, through the Web and call centers. Nonproprietary premium increased 12.6% over the prior year.

Our 5 operating priorities are shown on Slide 4. So we just covered the second quarter results on growth and profitability, so I'll give you a chance to just read the bullet points, then I'll move on to the next 3 priorities.

Investment returns were favorable in the quarter as higher limited partnership income more than offset the expected decline in interest income. You will remember the risk and return trade out we made in shortening the duration of the Property-Liability portfolio, which resulted in capital gains but lowered investment income by over $100 million annually.

Our efforts to modernize the operating model showed up in lower operating expenses at Allstate Financial, reflecting actions taken because of the sale of Lincoln Benefit. The benefit plan changes made in 2013 also led to lower expenses.

Long-term growth efforts include expanding our Allstate agency capacity in underserved markets. Allstate agencies are also investing in growth alongside the company, and collectively, we're working to improve the effectiveness and efficiency of this powerful local model.

Esurance continue to expand its business and it offers auto insurance in 43 states; renters insurance in 18 states; motorcycle insurance in 9 states; and homeowners insurance in 7 states as of the end of the quarter, and we continue to expand that product portfolio throughout the year.

The breadth of this set of underwritten products is designed to give us a competitive advantage by better serving customers and lowering acquisition costs in comparison to other direct writers.

We're also investing aggressively in telematics and are achieving rapid growth in utilization of the Allstate-branded Drivewise and Esurance DriveSense offerings. We're testing additional features, which extend the benefits of being connected beyond more accurate pricing.

In summary, halfway through the year, we've made very good progress on our 2014 priorities.

Steve will now cover the operating results in greater detail.

Steven E. Shebik
CFO & Executive VP

Thanks, Tom. I'll begin by reviewing the second quarter financial highlights on Slide 5.

Beginning with the upper left, Property-Liability earned premium of $7.2 billion in the second quarter was 5% higher than the second quarter of 2013. Recorded combined ratio of 97.4% increased 1.3 points versus the comparable 2013 quarter, driven by $936 million in catastrophe losses, which were 45% higher than the prior year.

The underlying combined ratio was an 84.7% for the second quarter and 86.6% year-to-date, which is below our full year outlook range of 87% to 89%.

Net investment income for the Property-Liability segment increased 2.3% from the prior year quarter, driven primarily by limited partnership income. Property-Liability operating income in the second quarter was $364 million, 15.9% lower than the second quarter of 2013.

The Property-Liability combined ratio on a recorded underlying basis is shown in the chart on the upper right-hand side of this slide. You can see that while the recorded combined ratio rose in the second quarter due to catastrophe losses, the underlying combined ratio was very favorable, as we did not experience a repeat of the adverse weather encountered in the first quarter.

A tail below this chart provides a view of the underlying combined ratio of trends by brand for the past 6 quarters. We have also broken out Esurance underlying loss ratio to remove the impact of investments in advertising and expansion, which are immediately expensed and provide greater transparency to our ongoing profit-improvement actions.

As Tom mentioned earlier, you can see the Esurance loss ratio starting to benefit from the actions that we've taken to date.

Allstate Financial, on the bottom half of the slide, had a 10.5% decrease in premiums and contract charges in the second quarter, resulting from the sale of Lincoln Benefit Life. Operating income of $165 million was a 5.1% improvement over the second quarter of 2013, driven by higher investment and benefit spreads and lower operating expenses.

Net income of $145 million for the second quarter includes an additional $13 million after-tax loss on the sale of Lincoln Benefit Life.

Excluding LBL's second quarter 2013 results, operating income increased by 31%, and net income declined by 10.5% in the second quarter of 2014. Our second quarter 2014 10-Q and investor supplement both contained estimated historical results for Lincoln Benefit Life, provided with further contexts.

Allstate Financial is now a smaller but more focused company, but still capable of producing meaningful operating income.

On Slide 6, we showed net written premium and policies in force growth rates for Allstate Protection and by brand. For Allstate Protection, in the upper left chart, the red line shows the continued trend of policy growth that began in the second quarter of 2013. Policies have grown by 735,000 or 2.2% from last year's second quarter and 407,000 or 1.2% from yearend 2013.

Each brand where we accept underwriting risk achieved growth in the second quarter in both written premium and policies compared with the prior year quarter.

Moving over to the upper right chart. Allstate Brand policies ended the quarter 1.5% higher than the second quarter of 2013, growing 463,000 policies. The Allstate Brand grew net written premium 5% in the second quarter versus the prior year quarter, driven by continued variable trends in new business, retention and higher average premium. Allstate Brand Auto net written premium increased 4.9% from the prior year, while policies rose 450,000 or 2.3% from the second quarter of 2013.

Allstate Brand homeowners net written premium grew 4.3%, while the rate of decline in policies in force slowed to 0.5% or 28,000 policies compared with the prior year quarter.

On the bottom 2 charts, you can see the growth trends for Encompass and Esurance. Encompass policy in force growth continues to slow, reflecting actions taken to ensure acceptable, long-term returns. Net written premium growth of 8.3% in the second quarter compared to the second quarter 2013 reflects higher average premiums due to rate increases that are earning in over time.

Esurance's rate of premium and policy growth continues to slow due to its increasing size, as well as the ongoing pricing and underwriting actions underway to ensure long-term profitability.

Total Esurance premium has grown over 65% and policies in force over 80% since its acquisition in October of 2011.

Slide 7 highlights Allstate Brand auto and homeowners underlying margin trends. The charts on the left side show Allstate Brand auto and home combined ratio trends, while the charts on the right show quarterly change in earned premium and underwriting loss trends.

As you can see, while there's volatility in the trends in the charts on the right, longer-term, underlying combined ratio results on the left have been fairly stable and demonstrate the success we experience with maintaining auto margins while improving homeowners.

For Allstate Brand Auto, in the upper right-hand chart, we expect frequency results that performed within historical ranges in the second quarter, as the adverse impact of severe winter weather in the first quarter was not repeated.

Severity results showed only modest increase over the prior year, resulting in a decline in the average underlying loss in the second quarter of 1% compared with the second quarter of 2013. We continue to earn previously approved Auto rate increases as average earned premium increased 1.6% in the second quarter compared to the prior year quarter.

For Allstate Brand homeowners, in the lower right-hand chart, we also experienced more favorable underlying losses in the second quarter compared with the first quarter. Average earned premium continues to increase, although at a slowing rate as we approach rate adequacy in total.

We continue to take rate increases as needed in both lines to keep pace with loss trends and maintain our underlying combined ratio.

On Slide 8, in the top left graph, you see the composition of the investment portfolio and the impact of the sale of Lincoln Benefit Life, which reduced the size of the portfolio by $12 million. Over time, we are shifting the portfolio composition to an asset mix we believe will have higher returns, relying less on interest-bearing assets and more on equity and other assets where return is derived from idiosyncratic operating performance.

Our total portfolio return presented in the top right was a strong 2.2% in the second quarter, reflecting increased fixed income valuations and positive equity market performance. You can see, however, the devaluation impact is highly variable, while the income yield has been relatively constant over the last 5 quarters.

Our second quarter investment income before expenses was $932 million, with a total portfolio yield of 4.7%. The lower half of the slide provides the investment income in yield for the Property-Liability and Allstate Financial portfolios, each of which now comprise approximately 50% of the portfolio.

For the Property-Liability portfolio, in the lower left graph, the interest-bearing yield has stabilized after the 2013 rate risk reduction actions Tom mentioned, while the total yield illustrates the variability in income, then a result of equity investments, including our limited partnership investments.

The Allstate Financial Portfolio in the lower right graph trends more consistently. However, you can see the decline in our second quarter income driven by the sale of Lincoln Benefit Life.

Our capital position is strong.

Turning to Slide 9. On the left side, you can see the change in the composition of our capital structure over time from senior debt to hybrid debt and preferred stock. A pro forma view of our capital mix adjusted for the expected repayment of $650 million of senior debt in August is also shown on the far left bar.

We took advantage of favorable market conditions in the second quarter, issued additional $250 million of noncumulative actual preferred stock, providing further financial and strategic flexibility.

During the quarter, we repurchased 142 million of common shares through open-market purchases and paid $125 million in common stock dividends for a total cash return to common shareholders of $267 million, bringing total common shareholder cash returns to $1,370,000,000 year-to-date.

We completed the accelerated share repurchase program announced in March on June 29, with receipt of 1.77 million in additional shares.

Book value per common share was a record $47.97, increasing 5.9% since yearend, and 15.2% since June 30th of last year. Our estimated statutory surplus at June 30 is $18 billion. Allstate Life distributed $700 million in a return of capital to its parent, the Allstate Esurance company during the quarter.

Our operating income return on equity was a strong 13.7% in the second quarter on a trailing 12-month basis, but lowered in the full year 2013 return of 14.5%, reflecting the impact of higher catastrophe losses in the first half of this year, along with higher equity. The increased equity is a result of our 2013 benefit and planned assumption changes.

As you can see in the table in the upper right, average trailering equity is essentially flat from yearend 2013 to June 30. The impact of the benefit changes were entered into the calculation in the third quarter.

Overall, we continue to make good progress on the execution of our customer-focused strategy and our operating priorities in the second quarter.
Now let's open the call up for your questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Jay Gelb from Barclays.

Jay H. Gelb
Barclays PLC, Research Division

The underlying P&C combined ratio of 84.7%, if my data is right, that's the best of any quarter in the past 6 years. So first, it's a great result. Second, just wanted to see if there was any lack of knockout weather or other factors that would cause that to be lower than you might think on a go-forward basis?

Thomas J. Wilson
Chairman & CEO

Jay, make sure I get the second part of that question, so the question was whether weather had an impact on growth?

Jay H. Gelb
Barclays PLC, Research Division

No. I'm sorry. The underlying combined ratio of knockout weather or any other factors.

Thomas J. Wilson
Chairman & CEO

Yes. First, thank you. We feel like we've made a lot of progress. Matt can talk about the underlying combined ratio.

Matthew E. Winter
President and President of Allstate Insurance Company

Jay, there was nothing out of the ordinary this quarter from an underlying standpoint. As you know, we just had -- we had a lot of rate earning in, we had a fairly careful management of claims continuing and we had an underwriting expense ratio that was down. And as a result, all of the discipline that's been put into the business over the past many years is just starting to show through. Frequency improved, trends were broad-based, paid severity was pretty much in line on the BI side. On the PD, actually, we had some claims that shifted over from first quarter to second quarter because of such a high claim volume in the first quarter. So some third-party subro demands came in, in the second quarter. And so that just changed quarter-over-quarter a little bit on the PD side. But overall, there was nothing extraordinary there, nothing out of the ordinary. And we think it's just a continuation of the hard work that's been put into the business.

Jay H. Gelb
Barclays PLC, Research Division

All right. And then, the pace of share buybacks slowed pretty meaningfully in 2Q relative to 1Q. And as you mentioned in the prepared remarks, the accelerated share repurchase program probably had a fair amount to do with that. But I'm just trying to get a better sense of what a normalized buyback pace might be on a go-forward perspective.

Steven E. Shebik
CFO & Executive VP

So as I said, we completed our accelerated share buyback program we started in March. I think, Tom noted, instead of June 29, it was actually July 29 that we completed it. When we got into a program like that, effectively we give the buyback program for that piece to another party, in this case, it was Barclays. So they buy over a period of time, in this case, 4 months. So we buy alongside them, but we effectively get a fair amount of the shares, from the money we provide to Barclays, upfront. So we recorded all that in the first quarter. So we had such a strong buyback number in the first quarter. In the second quarter is really open-market purchases alongside the program and that program has now ended this week and we are back in the market ourselves buying. So if you think we are -- it was announced within the $2.5 billion buyback over 18 months essentially, you do some division, it's about $150 million a month is kind of the ongoing rate we go and there are times when we accelerate that generally earlier in the program. Over the summer, we generally go a little bit slower than $150 million. Now we do have a strong capital position, clearly. So we have probably more flexibility than we've had in prior years when during the hurricane season, probably July to September, we'd slow down our program.

Thomas J. Wilson
Chairman & CEO

Jay, let me build on Steve's answer there. So we're 40% of the way done in 20% at the time. So there should be no confusion as to our commitment to do this aggressively. I think, what you do see is the way the numbers get accounted that makes it look like we're not active in the market. We're active in the market and we're aggressively buying back as much as we think is prudent, given the flow.

Operator

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

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

I want to pyramid into your bullet point on modernizing operating structure in Allstate Financial, just to get a sense of where the cost structure is on a go-forward basis. You have a program that reduce expenses, you're absorbing a little bit more of corporate overhead without Lincoln in the mix. When are you sort of at your right run rate of expenses and how much lower can it go from the current rate?

Thomas J. Wilson
Chairman & CEO

Bob, let me make a comment about general corporate expenses. And then, Don can address Allstate Financial. So we've always been about reducing expenses, whether that be the benefit plan changes we talked about last year, which reduced expenses and you see ran through the P&L, or just our normal continuous improvement simplification. The benefit we now have is by growing revenues, you'll see more of that flow through the bottom line. So in the past, when revenues and PIF counts were going down, it's hard to get ahead of that in terms of your expense ratio. So what you should begin to see is our growth rate a little more incremental margin for us. And Don can talk specifically about Allstate Financial because he's doing a great job of getting ahead of the downsides in there.

Donald J. Bailey
Former President of Emerging Businesses

All right. Thanks, Tom. So the strategy for Allstate Financial has been the same for a number of years, that's been to simplify our focus so that we're all about the Allstate customer and the Allstate Agency. The Lincoln benefit transaction, obviously, was an important step in that because it not only reduced the size of the balance sheet, allowed us to free up some capital for the parent company, but also then allowed us to focus all of our efforts on 1 distribution channel, which is the Allstate channel. There has been a lot of hard work, and thanks for noticing it, that has taken place to try and get our cost structure down because we're a smaller company. I think, we've made good progress, you see it in the numbers. At the same time, we're taking cost down, we're simplifying what we do so that we can be more effective, it's serving the Allstate customers and the Allstate agencies. We're not through the transition yet with Lincoln Benefit Life. We still have a good year or so of work to do to get that behind us. But I expect to see us continue to work hard to manage our expenses so that we can continue to deliver really strong operating results.

Thomas J. Wilson
Chairman & CEO

And Bob, I'd just add 1 other point, as part of corporate overhead, I prefer to call it corporate value add.

Robert Ray Glasspiegel
Janney Montgomery Scott LLC, Research Division

Tom, you sort of anticipated my follow-up and gave a partial answer to the question I was going to ask which is on the PC side, you see it in the solid expense ratio improvements. Going forward, are we likely to see any underwriting improvement more likely to come from the expense ratio than a loss ratio given that you're saying you're trying to move rates up in line with loss cost growth?

Thomas J. Wilson
Chairman & CEO

I'll let Matt answer it for ff course, our biggest business, which is the Allstate agency piece. I would just point out, as it relates to Esurance, the expense ratio is dependent on how aggressively we want to grow the business and how much advertising we're doing.

Matthew E. Winter
President and President of Allstate Insurance Company

Bob, it's Matt. Thanks for your question. We're looking -- we try to manage both components. I wouldn't say that we're trying to use 1 lever over the other lever. I think, we have to be conscious of and monitor and manage both the loss cause and the expense side of the house. As Tom mentioned, now that we're in growth mode, it gives us the flexibility of making some investments for the long term. It gives us the ability to leverage our scale and efficiency. It gives us the ability to do some things, some of the work we're doing now in continuous improvement to really go through some of our processes, really make sure they're as efficient, effective and customer-focused as possible. That will help us leverage our scale and size that will help us be more efficient. And so my expectation and the team's expectation is that we will be diligent on both components of the combined ratio and not look to just use 1 lever versus the other.

Operator

Our next question comes from the line of Josh Stirling from Bernstein.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

So listen, I wanted to switch gears a bit and talk a bit about growth. You guys have come out of a number of years of sort of stabilizing the business and shrinking volumes in some of your lines, you've been growing for the past year. Longer term, really interested in what you guys can do to get more leverage out of your -- the other core Allstate Agency platform. It sounds, from, what, your presentation this morning, that it sounds like you're starting to add agents again. Kind of curious if that's new headcount in agencies, is it new principals? And also, you've done a lot, I think, to sort of reposition the organization to focus more on cross-selling and trying to leverage benefits package and things like that. I'm wondering if you can give us a sense of sort of broadly what you're doing? And then, for big picture, whether these are the sorts of things that can kind of help you maintain share, whether there's -- whether any of them are sort of material to allow them -- you to actually begin to grow unit volumes, say, in excess of household formations or something like that?

Thomas J. Wilson
Chairman & CEO

Let me start with the last part, and Matt can give you the specifics on the Allstate Agency piece. So our overall plan to increase share of the business is really focused on having unique customer value propositions for each segment. And so Matt has a unique customer value proposition that for those people who want local advice and a branded product, he can talk about the things he's doing to make that resonate, which includes many of the things you mentioned. At the same time, we look at both share of revenue and policies, as well as share of profits. So as you know, the overall industry return in the property casualty business, broadly defined, including commercial and personal lines, is about 7%. We'd like to continue to maintain our attractive returns and have a greater share of that than we do the top line, we believe we can grow both with our differentiated proposition and Matt will talk about specifically what he's doing. And he is -- that business is building momentum, I feel good -- the flywheel is turning on that one.

Matthew E. Winter
President and President of Allstate Insurance Company

Josh, thanks for your question. As you noted, there's been a fairly strong emphasis on getting the Allstate agency force growing again and getting the entire Allstate brand business growing again. So we look at it in a couple of different categories and we refer to capacity building, capability building and activity creation. And so on the capacity building, we are, in fact, increasing points of presence, points of distribution presence, both EAs and license sales professionals. So we do have a fairly significant and aggressive campaign to grow the Allstate agency force, but it is not just putting on numbers, it's putting on quality agencies in strategically deployed areas where we're under-penetrated and we believe that there's extra market potential. And we will continue to do that fairly aggressively because it's working for us, we're doing that in areas where we have not historically been able to penetrate. And we're using new and fairly creative methods of doing that, including the Allstate Auto dealer program, where we place Allstate agencies in car dealerships, which, in the heartland especially, is enabling us to service a very wide geographic area in a very efficient way. We're also using what was formerly the Allstate direct group in a support mode for the Allstate agencies, we call it the extra hands. And so we are deploying that large call center force to create additional capacity for the agencies, both after hours, weekends, and in additionally, for overflow, when they're capacity-constrained during the day. So in the capacity creation, lots of things going on that we think create long-term sustainable growth capacity. On the capabilities side, Tom has mentioned, I think, on several calls, our push to create an advisory capability within the Allstate agency and grow that. So we refer to it as trusted advisor. It's our initiative to focus the Allstate agency force on more advisory and service functions and less transactional functions where we believe their differentiation stands through to the customer base where we think that they provide extra value, where we de-commoditize Esurance and do not accept the fact that auto or homeowner insurance is merely a pricing play. That's truly just a commodity. We don't believe that and so we're expending a lot of energy and effort building the advisory capability within our Allstate agency force from a technology perspective, from a service perspective, information perspective, process and marketing perspective, you'll see a lot of our recent marketing and our agent recruiting materials are very focused on the trusted advisor piece. And on the activity side, we spent a lot of energy and effort improving our close rates, improving quote activity, improving retention through customer-focused experience work and other things to improve our relationships with our customers and retain them for a longer period of time. So on the activity side, we think we've been quite successful with our broadening the target, with our quote generation. And you'll see -- you have seen how that's flowed through in the Auto results. On the home side, as Tom mentioned, the deceleration in the decline in homeowners is just accelerating. So we are flattening out and positioning to grow there as well. And as Tom mentioned many times, our goal there has been to grow in a very disciplined manner so that the volatility of that line is still acceptable for our shareholders, our customers and for the corporation. And we think we've been pretty successful on that. If you just look at the last 8 quarters, we've had 8 consecutive quarters with a recorded combined ratio under 100. And during that time, we had $2.1 billion of underwriting income at a combined ratio of 83.1%, despite $2.5 billion in tax. That's a pretty significant event, that's a fairly significant accomplishment. And that has given us the confidence to begin growing the homeowners line again in a thoughtful and disciplined manner. And when we look at that and we look at the underlying combined ratio during that same 8 quarter periods was 63.2%. And as we've said multiple times, our goal is to deliver low 60s combined ratio in the homeowners business and we did that in a period that included Superstorm Sandy and some of the worst winter weather we've seen in quite a while. So the last part of your question, which was the ability to cross-sell, we -- you've seen an uptick in our other personal lines business. You saw that in 2013 that, that line was declining. In 2014, we began growing again in that. Most of that growth is driven by renters and condo, which we think are very important to creating long-term relationships with our customers and enabling cross-sell of other products, including auto. It probably would have been faster had it not been for the decline in the involuntary auto piece of that line. And as you know, the involuntary auto is what we get depending upon whether other auto carriers, specifically in New York and New Jersey, accept higher-risk customers. And lately, they've accepted more customers. We've had less involuntary auto, and so that has slowed down the growth in other personal lines. But overall, we feel quite good about our ability to serve all the needs of our customers. We have stopped really referring to it as cross-sell and refer to it as providing household solutions to meet the needs of our customers. So we're not so interested in trying to acquire a customer and then push another product on them, but to acquire a customer and meet all of their needs and the needs of their households with our full product portfolio. So we feel quite good about our positioning for growth and our ability to sustain that growth over the long term.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

Matt, that's really pretty comprehensive. I guess, maybe sort of a high-level question for Tom. You've increasingly given more visibility in your communications to all of us talking about telematics and you mentioned the strategic investments here today. I'm wondering if you can give us some color on how you guys thinking about sort of your go-to-market strategy is evolving in Esurance and Allstate? And big picture, is this something that's going to be a growth engine for you guys? Or is it more an opportunity to increase your connectivity with customers and something we should basically look for as a benefit to, say, retention, for example?

Thomas J. Wilson
Chairman & CEO

It's a good question. I would say that the connected car space is developing rapidly. We're right in the middle of it and it's hard to determine exactly where it will come out. But I can give you the 3 components that we're working on. So first and most importantly, being able to be connected with our customers helps us get more accurate pricing on their behalf. And as we've talked about in the past, we're making estimates as to what an individual customer should have. We've been very good at that, and that's given us a competitive advantage. You can see that in the homeowner results that Matt was talking about. Knowing how a specific person drives gives us the ability to do an even better job, and we can provide them a 10% to 30% discount if in fact they connect with us. And it's every bit as powerful as credit, so we're actively and aggressively working to expand that portion of our business. Secondly, we're working to improve the driving experience. So we have a number of features that we're developing, which improves somebody's driving experience which takes their relationship with us essentially beyond auto insurance. We don't know where that will exactly come out yet, we're investing aggressively. And to Bob Glasspiegel's point, and what Matt said, was look, we invest where we want to invest, and we cut cost where we think it's not really adding customer value. In that component of our telematics offering, we're investing aggressively in trying to decide what are the number of alternatives. We've launched some new features last quarter on teen driving and we'll continue to roll out new features to better the driving experience. The last component of our offering is how do we best utilize and monetize some of the data that will be created from that connection on behalf of our customers. And we're collecting billions of miles of traffic data and all kinds of other data, how cars work, what they work, what they're like in different weather condition. And that is the most nascent of our efforts. It's not an area where we have a traditional source of expertise in monetizing data. I was very good in using data. And we make a lot of money by monetizing on behalf of our shareholders, how we help other people use that data and how we capture that revenue source on behalf of the company is yet to be determined. So it is both more accurate pricing, better experience which lead in part to retention. But we also think mainly to other revenue streams and then just solely new revenue streams. So it's really all 3 of those components.

Operator

Our next question comes from the line of Michael Nannizzi from Goldman Sachs.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

I guess, 1 question I had, sort of bigger picture, I mean, the homeowners trending well, underlyings are good, PIF trends moving in the right direction, auto underlying was nice, and it doesn't like -- or from your comments, it doesn't sounds like it was a one-off. Other personal lines growing, looks like low 80s underlying there. And then, Esurance is improving. So I'm just trying -- I guess, I'm trying to understand, your 87 to 89 combined as a target, it would seem that we're on a glide path to come in below that, unless I'm missing something. Can you comment on how we should think about that?

Thomas J. Wilson
Chairman & CEO

Sure, Michael. First, we, of course, as you point out, we give an operating range of a couple of points for the year, at the beginning of the year, because we want you all to have some confidence that this is where we think the business will come out. And this year, we picked 87 to 89 which was a point lower than the range we had last year, which was reflective of our team -- here is confidence in the -- in all the metrics you just talked about. So for the first 6 months, I would point out, you're right, we're slightly below that in terms of the underlying combined ratio over towards the lower end. But as you also know, frequency can bounce around a good point in any period of time. So we don't feel any need to change that range. We don't do it to try to help people get -- do operating EPS calculation. We do it to give you a sense to how good we feel about the business. We still feel good about the business. We think 87 to 89 generates really attractive returns and we can grow in that range. So we don't have any plans to change it at this point. What I would take the opportunity to do is sales message, we saw all the things you talked about, that means evaluation should be a much higher multiple of both.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

All right. That's fair. I guess, the other question I have was just, so would you guys calculate an industry loss estimate for 2Q just across the country? Because it looks like you guys are at about 900, just over that. I mean, I look at some industry loss estimates, it did show that 2Q was a relatively light quarter. Can you try to help -- I was trying to square that, is it where you're located or maybe just a conservative view of where losses may end up? I'm just trying to...

Thomas J. Wilson
Chairman & CEO

Are you talking about auto and home?

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Yes. So I mean, you're not -- looking at some cat losses for the second quarter, 930. It looks like industry loss estimates are somewhere in the $6 billion to $7 billion range and that's commercial, personal, across-the-board and domestically. So I mean, just trying to square that versus your sort of market share.

Thomas J. Wilson
Chairman & CEO

Yes, I think, I would make 2 comments. One, it's a little early to figure out where exactly the industry is because people are just reporting now and it takes us a while to get the information. Secondly, we do obviously look externally at how our results compare to everybody else. But we break it down. We look in total, but we're really more concerned about what happens locally. So this is a local business. We underwrite price, do our agencies, everything is local. And so we would really look and say, well, how are we doing it in Colorado relative to other people in Colorado on all fronts. That would be not just in catastrophes, it would be BI, it would be physical damage. And we have a number of tools we use to do that. Obviously, starting with pricing, but going all the way through to claims or some industry databases we use on claims. And I think, the summary, I would say, of all that is the machine that we have in place, which is a set of business processes, disciplines, rewards, recognition, analytics, they help us maintain our profitability. And the zones we talked about is working, we think it's working well. We see Matt's team is adjusting where they need to adjust and that has obviously been through for a long time on auto insurance. You're now seeing that same discipline and set of practices being applied to the homeowner's business. And so we feel good about where we're at relative to the industry.

Michael Steven Nannizzi

Goldman Sachs Group Inc., Research Division

Great. And then, just really quickly, Esurance, as your actions continue, I mean, it looks like you took mid single-digit rate, PIF is still in that high teens. What do you expect or what are you hoping to kind of get that to or when were you hoping to get that to sort of underlying profitability or at least getting that loss back down as close to 0 as possible?

Thomas J. Wilson
Chairman & CEO

I'll let Don talk about the specifics that they're doing at Esurance. I would tell you though, from a capital allocation standpoint, the conversations that Steve and I, and Don and I have about that business are it should grow as fast as they can, assuming we are earning above our cost of capital on the business that we write. If we're not getting the right return on it, then we're not interested in growing. The returns on the business we write are well above our cost of capital, slightly below what we would make in a large existing business like Allstate, which has a huge legacy book associated with generating a lot of profitability. But it's got to be profitable what we do.

Donald J. Bailey
Former President of Emerging Businesses

I mean, there's a -- little I can add to that. I mean, the reality, our goal is to run Esurance in a way where we're economically profitable. What you're looking at is the GAAP profitability, which of course, is impacted by the fact that we're expensing the advertising upfront and there's also a couple of points of investment in other products and expansion that doesn't necessarily pay off in the quarter as well. I'm really pleased that the work that Gary and his team have done over the last year or so, the loss ratio is beginning to pay off. We're beginning to see it in the numbers with the loss ratio coming down again. So I feel good about where they are. We'd just like to see them continue to grow. And I don't think we want to put an artificial target of a GAAP combined ratio because I think that will stifle the growth that we're seeing at economic terms right now.

Operator

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

Kai Pan
Morgan Stanley, Research Division

Just first question is on the loss cost trend. If you would look at your Slide 7, it looks like both from auto and homeowner, the underlying loss trend have been ticking down from recent adequate levels. So could you give a little bit more color on that? And how do you think about sort of, in general, the economy, the inflation and as the economy recovering?

Matthew E. Winter
President and President of Allstate Insurance Company

Yes, Kai, it's Matt. Well, I'm looking at that, I looked at those same 2 charts on 7, and I look at it as kind of reverting more towards the norm. I don't see it as that much of a directional change. I think, we had an aberration on the auto side for a couple of quarters. It looks like it's stabilized where it should be and where it has been historically and the same on homeowners. So we feel very good about the underlying margin trends in both of those businesses. As we've been saying historically, we manage this very disciplined. We keep on top of loss cost and we keep on top of expense cost and we manage it on a micro basis for the benefit of the overall system. So we manage those in each geography and each micro-geography and the result of that is a systemic result that looks the way you see on these charts with positive long-term trends. From the overall economy, if you look at our current severity, we haven't seen that much of an impact from the inflationary trends. Obviously, there's some. But really, it's been relatively mild and relatively benign. Most of the severity fluctuations that we've seen have been the result of age of closures, geographic mix, policy limit shifts and things like I discussed earlier about just backlog of third-party subro demands and things like that. So, so far, the trends have been relatively benign. That being said, it's 1 of the reasons that we have to stay on top of taking rate, it's 1 of the reasons we thought it's so important to point out that we have continued to take rate on the Auto side even though it was masked a little bit by the Ontario rate decrease. We believe it's essential that we take rate as needed on a moderate basis consistently across the business. It's less disruptive to customers, it's less disruptive to the agency force, it improves retention and it allows us to stay ahead of any inflationary trends that might occur.

Thomas J. Wilson
Chairman & CEO

Let me provide a point of clarification on these 2 charts on Page 7 as well. Obviously, 2 drivers of profitability are price and loss cost, and we've shown them to you because we think they're relevant. Unfortunately, I think, sometimes, it shifts the focus to just price as a tool to manage profitability. And let me expound on what Matt just said and give you the example of homeowners. So risk selection, product design, claims, performances, are all equally important to profitability. So if you look at homeowners over the last 5 years and you look at our cumulative price increases relative to our competitors, you're not really that much different at the end of this 5-year period. That said, we took a whole bunch of other actions, which give us the confidence that what we've done has made it sustainable. So for example, we used to have it as peak 7.8 million policies, we now have a little over 6 million. That's 1.8 million down. We're down 1.2 million just since 2009. What we do is went through re-underwrote the book, decided that those risker underpriced pieces of business we were no longer going to insure. We moved those to somebody else. We Improved. Matt's got a whole new set of inspection processes going on in terms of the way we look at new business. We obviously use sophisticated technology in claims. And then, they've redesigned the product in House & Home. I think, you're in what percentage of the country it is?

Matthew E. Winter
President and President of Allstate Insurance Company

We're in about...

Steven E. Shebik
CFO & Executive VP

31 states and it's a growing percentage of the book of business.

Matthew E. Winter
President and President of Allstate Insurance Company

It's about 12% of our overall book, 85% of our new business writings.

Thomas J. Wilson
Chairman & CEO

So all of that stuff is underneath that story. So when we're -- I would encourage you to think about it, we have to look at these charts and show you price, but price is not the only tool we have to manage profitability. Matt was talking about that system. It has all of those tools available to it. And the strength of our execution is in being able to have a leadership that knows how to manage that well.

Kai Pan
Morgan Stanley, Research Division

That's very comprehensive. Second question is on Encompass. It looks like that's the only segment you have year-over-year deterioration in terms of underlying combined ratio. I see that you're taking pricing action, as evidenced in the PIF growth slowing down. Could you talk a little bit more about the competition in the independent agency channel?

Unknown Executive

In Encompass, we're focused, as you know, on the mass affluent, and so we compete day-to-day with Met, Hanover, Chubb, AIG and Crestbrook. Right now, we see that it's competitive, certainly, but it's not irrational from a pricing perspective. We're still seeing really solid growth on our package policy, we had 10% quarter-over-quarter on our package policy growth, which now makes up the majority of our book. And we see more room, more elasticity in Auto. So if you look at Auto, quarter-over-quarter, we're up almost 2 points in retention. So that tells me we have more room to increase margin in the back half of the year and we plan to do that to get our underlying in line. With regard to deterioration you're seeing on the overall underlying of 2 points, you have some non-cat quoted weather in there, we had a really tough quarter in terms of weather and you have non-cat quoted weather, and you see the impact of a onetime rather sizable premium refund that's driving some of that, too. So all those things combined are driving that underlying. But overall, we still see room for margin expansion in the back half of the year. And if you look at the investor supplement, you'll see that we take most of our rates in the back half of the year on Encompass. And so, you'll see us earn an even more rate on Auto and Home as the year progresses. And we think we have room to do that.

Thomas J. Wilson
Chairman & CEO

Why don't we do 1 more question?

Operator

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

Joshua David Shanker
Deutsche Bank AG, Research Division

Back to Allstate Financial, the results were just excellent and it's not just on expenses. I know it's the spread of net investment income to interest credit after I take out the impact of Lincoln Benefit, it's also growing and the benefits to premium ratio has been declining. There's a lot of good stuff going on there. Can you sort of talk about not just the efficiencies, but actually the underlying profitability of the business, I guess, being generated, what's happening?

Steven E. Shebik
CFO & Executive VP

Yes, I'm happy to do that. I do feel good about the overall results at Allstate Financial. And the operating income, obviously, at $165 million, given the size of our business today, is a terrific result. We're hitting on a lot of cylinders, as you pointed out. It isn't just expenses. I think, benefit spread continues to be nice and stable and we're seeing good results on that year-over-year. Where we're seeing a really great result year-over-year is investment spread. So it looks, if you look at the reported numbers, we're up $12 million in investment spread. If you take out LBL, it was actually $68 million. And so we've talked about that in the past with the investment strategy we've taken, we are hoping for higher returns, we're expecting higher returns, it will come with some volatility and we're prepared for that. But at the moment, the investment income, benefit spread, expenses, everything has worked well for us and that's why you see the results you're seeing.

Thomas J. Wilson
Chairman & CEO

Okay. Thank you all. I know there's number of calls today. So I'll close it off where we began. This quarter's results show the benefits of both having a focused strategy and solid execution. The net is growth at attractive returns.

Thank you very much, we'll talk to you next 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.