S&P Capital IQ

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The Travelers Companies, Inc. NYSE:TRV

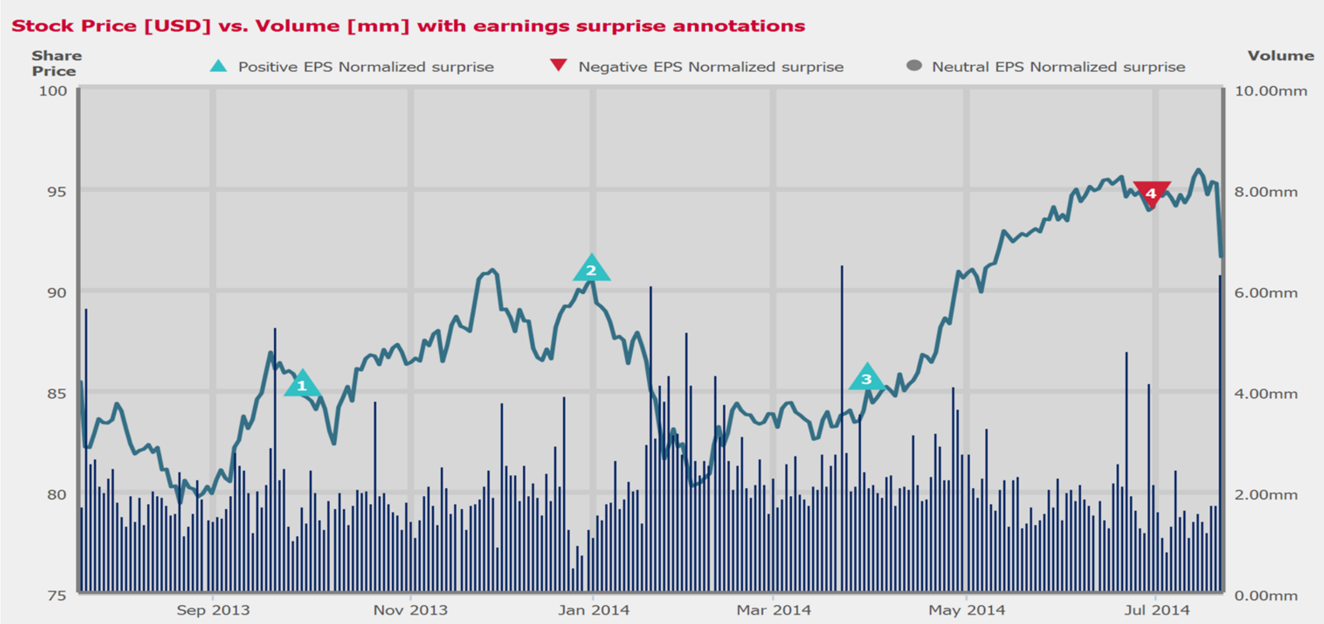
FQ3 2014 Earnings Call Transcripts

Tuesday, October 21, 2014 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ3 2014-			-FQ4 2014-	-FY 2014-	-FY 2015-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	2.29	2.61	▲13.97	2.52	9.72	9.26
Revenue (mm)	5930.46	5983.00	▲0.89	5992.77	23684.61	24190.66

Currency: USD
Consensus as of Oct-21-2014 1:51 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ3 2013	2.06	2.35	▲1 14.08 %
FQ4 2013	2.16	2.68	▲2 24.07 %
FQ1 2014	2.16	2.95	▲3 36.57 %
FQ2 2014	2.07	1.93	▼4 (6.76 %)

Call Participants

EXECUTIVES

Alan David Schnitzer
Chairman of the Board & CEO

Brian W. MacLean
President and Chief Operating Officer

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

Gabriella Nawi
Senior Vice President of Investor Relations

Jay S. Fishman
Former Executive Chairman

Jay Steven Benet
Vice Chairman and Chief Financial Officer

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Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Vinay Gerard Misquith
Evercore ISI, Research Division

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to the third quarter results teleconference for Travelers. [Operator Instructions] As a reminder, this conference is being recorded on October 21, 2014.

At this time, I would like to turn the conference over to Ms. Gabriella Nawi, Senior Vice President of Investor Relations. Ms. Nawi, you may begin.

Gabriella Nawi
Senior Vice President of Investor Relations

Thank you, Julian. Good morning, and welcome to Travelers' discussion of our third quarter 2014 results. Hopefully, all of you have seen our press release, financial supplement and our webcast presentation released earlier this morning. All of these materials can be found on our website at www.travelers.com under the Investors section.

Speaking today will be Jay Fishman, Chairman and CEO; Jay Benet, Vice Chairman and Chief Financial Officer; Brian MacLean, President and Chief Operating Officer; as well as Alan Schnitzer, Vice Chairman, Chief Executive Officer of Business and International Insurance; and Doreen Spadorcia, Vice Chairman, Chief Executive Officer of Claim, Personal Insurance and Bond and Specialty Insurance.

They will discuss the financial results of our business and the current market environment. They will refer to the webcast presentation as they go through prepared remarks, and then we will take questions.

Before I turn it over to Jay, I would like to draw your attention to the explanatory note included at the end of the webcast. Our presentation today includes forward-looking statements. The company cautions investors that any forward-looking statement involves risks and uncertainties, and is not a guarantee of future performance. Actual results may differ materially from those projected in the forward-looking statements due to a variety of factors. These factors are described in our earnings press release and in our most recent 10-Q and 10-K filed with the SEC. We do not undertake any obligation to update forward-looking statements.

Also, in our remarks or responses to questions, we may mention some non-GAAP financial measures. Reconciliations are included in our recent earnings press release, financial supplement and other materials that are available in the Investors section on our website.

And now, Jay Fishman.

Jay S. Fishman
Former Executive Chairman

Thank you, Gabby. Good morning, everyone, and thank you for joining us today. As I'm sure you've read, the results this quarter were just terrific, as demonstrated by our operating return on equity of 15.2%. In addition to posting very strong financial results, the underlying dynamics in our businesses are showing very solid performance, and give us continued optimism about our future financial results.

Starting with Personal Insurance. Quantum 2.0 is proving to be a real success. New Auto business is a clean double from last year's third quarter, and loss experience, while still early, is very much consistent with our original plans. Retention in our entire Auto book remains high. On a sequential quarter basis, total Auto policies enforced increased for the first time since the second quarter of 2011, and we expect to see sequential policy growth again in the fourth quarter.

Lastly, and positively, we believe our Homeowners business is actually showing some lift from Quantum Auto.

In our Business Insurance segment, it's business as usual. We continue to achieve rate gains where needed, and we see no fundamental change in the competitive environment, that is, trends remain generally the same. Retention is actually up in almost all of the business units, and we remain optimistic about our ability to continue to successfully execute our granular pricing strategy and achieve improving returns.

In our Bond & Specialty Insurance business, we couldn't be more pleased that we've navigated through the financial crisis and the great recession as successfully as we have, as evidenced by consistently strong results. This performance demonstrates the underwriting thoughtfulness and skill that is such a part of the fabric of our organization. And we're particularly proud of our investment department performance. In a challenging environment, they've maintained their investment criteria and done the right things, another example of our discipline.

While it's always nice to post a strong quarter, I think it's important to remember that we're committed to running this organization successfully over the long term. The results that we posted this morning were driven by decisions made years ago, that have been translated to successful marketplace strategies. Our long-term performance is really the result of thoughtful analysis, a commitment to analytics, insightful discipline applied to a risk-taking business and, to be candid, a little bit of good fortune.

Our energy is going to be committed to two things: First, more of the same. First-rate execution of thoughtful data-driven strategies. Second, notwithstanding the more of the same approach, we are also committed to challenging our own conventional wisdoms to identify opportunities and making the decisions today that are necessary, perhaps even critical, to making sure that our financial performance remains top tier.

In addition to hearing from Jay and Brian this morning, Alan and Doreen will provide a commentary on the performance of their business segments.

And with that, let me turn it over to Jay.

Jay Steven Benet
Vice Chairman and Chief Financial Officer

Thanks, Jay. We were very pleased with our results this quarter with operating income per diluted share of $2.61 and an operating ROE of 15.2%, driven by very strong underwriting and investment results. Underwriting results benefited from a slightly lower level of catastrophe loss this quarter, $83 million pretaxes compared to $99 million pretax in the prior year quarter. In contrast to the lower level of cats, we incurred higher non-cat weather-related losses this quarter as compared to the prior year quarter, which more than offset the benefit of earned pricing increases that exceeded loss cost trends in each of our business segments and drove a slight 0.5 point uptick in our underlying combined ratio.

Underwriting results also benefited from net favorable prior year reserve development of $113 million pretax, down from $158 million pretax in the prior year quarter. Current quarter net favorable prior year reserve development included a $250 million pretax increase to our asbestos reserves, driven mostly by increases in the company's estimate of projected settlement and defense costs related to a broad number of policyholders due to a higher level of litigation activities surrounding mesothelioma claims than we've previously anticipated as well as a $77 million pretax increase in our ULAE reserves by the accrual of interest resulting from a recent court decisions relating to the asbestos direct action litigation.

On the positive side, current quarter reserve development included a $64 million pretax benefit, resulting from better-than-expected loss experience related to an old Workers' Compensation reinsurance pool that we participated in, along with another pretax benefit of $98 million that resulted from the final commutation of assumed and ceded reinsurance treaties associated with that pool.

Current quarter reserve development also benefited from better-than-expected loss experience in GL, property and fidelity and Surety in recent accident years. And year-to-date, on a combined stat basis for all of our subs and excluding A&E, all accident years developed favorably.

Over time, we've generated much more capital than what is needed to support our business. This has allowed us to return over $900 million of excess capital to our shareholders this quarter. We paid dividends of $186 million and repurchased $751 million of our common shares, consistent with our ongoing capital management strategy. And year-to-date, we returned almost $2.9 billion of excess capital to our shareholders through dividends of $553 million and common share repurchases of $2.3 billion.

Shifting from the current year, let me provide a historical view of how our capital management strategy has performed over time. Our Board of Directors initiated the current share repurchase program on May 2, 2006, a little over 8 years ago. On May 1, 2006, the day before the board authorization, Travelers' market capital is $30.2 billion, and we had approximately 696 million shares outstanding.

Since that time, we've repurchased over $416 million -- 416 million shares at an average price of $56.50 per share, issued a net amount of approximately 51 million shares, mostly in connection with share-based incentive comp awards and now have 331 million shares outstanding at the end of the current quarter, a 52% reduction in our common shares. And if you add in the dividends that we paid during this time period, we've returned approximately 98% of our May 1, 2006, market cap to our shareholders. We accomplished this all throughout this period while maintaining capital, in support of strategic business opportunities, such as those in Brazil and Canada, with very strong holding company liquidity and modest debt levels.

Notably, our ratings increased during this time period from already very high levels to industry-leading levels. And even after returning all this capital to our shareholders, our market cap stands at $31.6 billion today. Operating cash flows of over $1.8 billion were extremely strong this quarter, bringing total operating cash flows to almost $3.2 billion year-to-date. We ended the quarter with holding company liquidity of almost $1.9 billion, and all of our capital ratios were at or better than their target levels.

Our debt-to-total capital ratio of 21.3% was lower than its target range. And during the quarter, book value per share increased 1%, and adjusted book value per share, which excludes net unrealized investment gains and losses increased 2%, while year-to-date book value per share increased 9%, and adjusted book value per share increased 6%.

Finally, net unrealized investment gains were approximately $2.9 billion at the end of the third quarter, as compared to $2 billion at the beginning of the year.

With that, let me turn things over to Brian.

Brian W. MacLean
President and Chief Operating Officer

Thanks, Jay. Before Alan and Doreen go over the segment results, I'd like to give some perspective on how we view the overall market. And to do that, I'll start with returns.

We're a return-focused company, and as such, we're pleased with our reported ROE for the quarter and year-to-date. We're especially pleased that we were able to deliver these results in what continues to be a very challenging investment environment, where one where 10-year treasury yields continue to hover between 2% and 2.5%. When we look at our returns below this aggregate level, we are also encouraged.

To understand our product profitability, we look at accident year returns at the line level. And at this more detailed level, we are very pleased, both with the improvement that we have seen over the last several years and with the absolute level with those returns are at today. There are obviously differences line-by-line, but overall, we continue to see signs of a rational marketplace.

Doreen and Alan will go through the segment production statistics, but as we analyze our results at a very granular level, we see that we continue to be successful in executing our pricing strategy, which is to retain a high percentage of our best business, improve profitability, where needed, and write new business that meets our target returns. I don't have a crystal ball and I'm not predicting the future, but based on what we see today, there is nothing in the market that would cause our ability to continue to execute on this pricing strategy to be meaningfully changed.

We are also encouraged that as overall returns have become more consistent with our long-term objective, we've begun to see improving top line trends. We have said many times that volume is never our goal, but that we always seek opportunities to add business that meets our target returns. We have seen improved retention across most of the businesses and higher new business volume in many of them, and we believe that these trends are the results of our strategic focus on delivering meaningful and sustainable competitive advantages in the markets we serve.

So overall, through the first 9 months of 2014, fairly stable market conditions and very strong underwriting results.

And with that, I'll turn it over to Alan.

Alan David Schnitzer
Chairman of the Board & CEO

Think you, Brian, and good morning. In Business and International Insurance, third quarter operating income was $552 million. The underlying combined ratio, which excludes the impact of cats and prior year reserve development, was 94.9% for the quarter, up 1.7 points over the prior year. The 1.7 point change resulted from an increase of 2 points, largely from non-cat weather in both our domestic and international businesses, as well as the impact of the inclusion of the Dominion, partially offset by the favorable impact of about 1 point from earned price exceeding loss trend. We also saw a modest uptick in our expense ratio, mostly attributable to a favorable item in 2013.

Turning to production trends for Domestic BI. Compared to the second quarter, overall retention was up about 1 point, and total renewable premium change was up slightly, as the increase in exposure more than offset a lower level of positive rate change. Year-over-year, new business was about flat.

In Select, we're pleased to see an improvement in retention to just over 80%, with total renewal premium change of nearly 9%. We wrote $92 million of new business, representing a 5% increase over the same period last year.

In Middle Market, as a greater percentage of the business has achieved attractive returns, we've increased our focus on keeping the better-performing accounts. Accordingly, we were pleased to have achieved a 2-point increase in retention to a very strong 85%, with positive rate change declining less than 0.5 point, and each case is compared to the most recent quarter.

Lastly, new business of $236 million for the quarter grew by nearly 10% as compared to the same period last year. Overall, we feel very good about the production results, but as you have heard from us many times in the recent quarters, the aggregate numbers don't tell the entire story. The detail of where we are getting rate and which accounts we are retaining is key to evaluating the success of our production strategy.

In our Middle Market businesses, the data beneath these exhibits shows that on our best-performing business, our retention has improved to around 90%, and we continue to achieve slightly positive rate increases. On our poor-performing accounts, we are achieving low double-digit rate increases with meaningfully lower retention. These results are consistent with our marketplace strategy.

Looking at production results for our international business, retention remains strong, renewal premium change was down somewhat from recent quarters due primarily to lower rate and exposures in Lloyd's, a new business was up in the prior year due to the acquisition of the Dominion.

Before I turn it over to Doreen, I'd like to make an observation about margins. Many industry observers seem to focus -- overly so, in our view, on the relationship between written rate change and loss trend. Particularly with rate change for the quarter of 3.3 points, dipping just below our current estimate of loss trend, which is about 4 points in the aggregate, I'd like to point out that underwriting margins are impacted by a number of other factors, including changes in exposure, underwriting actions, business mix, the impact of new business, weather, and so on. So particularly with written rate and loss trend in such a narrow band, we'd caution you against drawing conclusions about the outlook for underwriting margins based solely on those measures.

To wrap it up, I'm pleased with our strong results for the quarter, and in terms of execution going forward, we intend to pursue more of the same.

And with that, let me turn it over to Doreen.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

Thank you, Alan. I'd like to begin by saying how excited I am to again work with Tom Kunkel and his leadership team in managing our market-leading Bond & Specialty Insurance business. Also, I'm really proud of the progress we've made in Personal Insurance, and look forward to continuing to work with Greg Toczydlowski and his team. Now for the results.

In the Bond & Specialty Insurance segment, operating income of $165 million was 38% higher than the prior year quarter. The increase was driven by higher levels of favorable prior year reserve development, along with improved underlying underwriting margin. The underlying combined ratio for the quarter was a very strong 81.7%, a 4-point improvement from the prior year, primarily due to exiting our Management Liability excess-of-loss reinsurance treaty as well earned pricing in excess of loss cost trend across the segment.

Net written premium for the quarter was $556 million, an increase of 1% compared to the prior year. Across our Management Liability businesses, retention of 84% was consistent with recent periods in the prior year, while new business of $34 million was down slightly from recent period. Renewal price -- renewal premium change, which can be somewhat lumpy due to variations and things like limits written, liability attachment points and policy duration, was 4.6% for the quarter, up somewhat from the second quarter. In sum, strong profitability through Bond & Specialties continued underwriting discipline and market leadership.

Turning to Personal Insurance. Operating income of $239 million for the quarter was down 9% compared to the third quarter of 2013, driven by lower favorable prior year reserve development in Homeowners. The underlying combined ratio is 84% in the quarter, an improvement from 2013 of more than 1 point, primarily due to the benefits of earned pricing that exceeded loss cost trend, our previously announced expense reduction initiative and lower Homeowners' commissions, partially offset by a higher mix of new business.

As it relates to our expense reduction, to date, we have executed on initiatives responsible for about 90% of the $140 million run rate savings target. As we've mentioned in the past, about half of these reductions relate to claim management expenses, the impact of which shows up in the loss ratio. We remain on track to achieve the full run rate savings by the end of this year, in line with our original expectations.

Looking at Agency Auto, retention remains strong at 82%, while renewal premium change was about 6%. We also are extremely pleased with the progress we've made on new business production, driven by the impact that Quantum Auto 2.0 is having. New business premium of $166 million is more than double the third quarter of 2013, with 90% of the $166 million coming from Quantum 2.0. This increase in new business drove a year-over-year increase in net written premium of 3%, and as Jay noted, policies in force increased from the most recent quarter for the first time since the second quarter of 2011.

As for the rollout, Quantum 2.0 is now live and all, but a handful of prior Quantum states, and the expectation is that these remaining states will go live over the next quarter or 2.

Turning to Agency Auto profitability. The underlying combined ratio of 96.1% for the quarter was an improvement of 1.5 points over the prior year, driven primarily by the expense initiatives and earned pricing that exceeded loss cost trend, partially offset by the impact from higher new business volume. Our current view of overall Auto loss cost trend is about 3%, a slight improvement from what we communicated in recent quarters, driven by some moderation in bodily injury severity.

In looking at the improvements in revenue and profitability, we believe our fundamental changes have made our Auto product more competitive.

Looking at Agency Homeowners and Other. Production was strong in the quarter with renewal premium change of about 6%, while retention remained at 84%. New business volume of $95 million was up about 30% from the prior year quarter, due to some lift from higher volumes in Quantum 2.0.

Overall, home production is in line with our expectation. From a profitability perspective, the underlying combined ratio of 70.1% was an improvement of 1.5 points over the third quarter of 2013, driven by earned pricing that exceeded loss cost trend as well as lower expenses. So overall, in Personal Insurance, a great quarter with both strong financial results and production metrics, and we remain pleased with the results of the Quantum 2.0 rollout, so far.

And with that, I'll turn the call back to Gabby.

Gabriella Nawi
Senior Vice President of Investor Relations
Thank you. Julian, we're now ready for the Q&A portion. [Operator Instructions] Thank you.

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

I want to touch base on exposure growth in Business Insurance. It appears to be accelerating in the Middle Market. Commercial business and Select is showing more stable growth. Can you talk about the differences that are driving that?

Alan David Schnitzer
Chairman of the Board & CEO

Yes. The difference in Middle Market versus Select?

Jay H. Gelb
Barclays PLC, Research Division

Yes. In terms of -- the rate of change and exposure growth, I think stronger in Middle Market than Select.

Alan David Schnitzer
Chairman of the Board & CEO

Yes. The exposure impact really isn't from sales in payroll, it's -- and if you look at the starting and ending points -- you're probably looking at the webcast. If you look at the starting and ending point, it's actually a pretty straight line from those 2 end points. The way we calculate the number, the impact of audit premium creates a dip per quarter to -- after we report exposures and particularly in the Middle Market. And so we would that to develop over time into more of a straight line.

Brian W. MacLean
President and Chief Operating Officer

I think that -- this is Brian. The other point on Select. A lot of that exposure growth is values on the property component of CMP.

Alan David Schnitzer
Chairman of the Board & CEO

And that's been an affirmative effort on our part to try to improve the values.

Jay H. Gelb
Barclays PLC, Research Division

Okay. So any other underlying difference in terms of exposure growth on the small business versus Middle Market?

Alan David Schnitzer
Chairman of the Board & CEO

No. There isn't really. Other than on the small side, we've really been working on the insurance to values in the Middle Market, it really is a function of how we account for the audit premium in the exposures.

Jay H. Gelb
Barclays PLC, Research Division

Okay. And then I had a separate question on capital return. So year-to-date, if my math is right, share buybacks plus dividends are $2.9 billion, operating income $2.6 billion. So clearly, capital return running well ahead of operating income on the order of around 110%. Can you give -- and you had a prior comment also saying that there's a continued level of excess capital being generated. I don't know if you'd care to update us on the capital management strategy in terms of, could that gap between capital return on operating income continue to grow over time similar to what we've seen this year?

Jay Steven Benet
Vice Chairman and Chief Financial Officer

Hi Jay. This is Jay Benet. Thanks for asking the question. I think what you're really seeing is a timing difference in the generation of the excess capital versus the time frame in which it's purchased -- it's repurchased. So when we look at a particular year like 2014, one of the things you have to take into account is, how did the end of the 2013 come up -- come out. And it was a very strong fourth quarter. And when we did our year-end capital calculations, we found that we had some excess capital that we carried into this year. So we're playing a little bit of catch-up now. But there's no change in strategy, there's no change in execution. It really goes back to the words that we used to describe the program, which is, we're generating at, over time, primarily through new income and maintaining the capital we need to support our businesses, so that the ratings are maintained and the posture of the balance sheet doesn't change and then to the extent we have the excess capital that's getting generated, we're buying it back over time, but it's really driven by earnings and you have to look at it more broadly than just a 9-month period.

Jay H. Gelb
Barclays PLC, Research Division

Okay. So based on that, we should still generally think about buybacks and dividends being roughly equal to annual operating earnings?

Jay Steven Benet
Vice Chairman and Chief Financial Officer

I'm not saying it's roughly equal. In our 10-Q and 10-K, we talk about having enough capital to support the growth in the business, and occasionally we make pension contributions to our qualified pension plans. So there are other things that we'll utilize capital into place, but the creation of capital is from the earnings.

Operator

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

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Just a couple of questions. In terms of the Auto business, what we're trying to figure out, you talked about 6% rate increases and we're trying to square that with the rate declines that you've taken and talked about taking on the Quantum business that you've repriced. Can you help sort of square those 2 things?

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

Michael, this is Doreen. Are you looking at the webcast with renewal premium?

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Yes.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

That would be also our existing book on the renewal book of business.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Okay. So for a business that you're -- Quantum is for new business only. Is that -- so that's your -- okay.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

Yes. Quantum 2.0 is for new business only.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Got it. Okay. That makes sense. And then one question on just -- on Business Insurance. I'm kind of looking at the margins that there and what have happened. How much of an impact on the year-over-year comparison does Dominion having, if at all? And how should we think about that trend? I know you mentioned some non-cat weather, but just trying to parse out sort of rate versus loss trend and underlying margin.

Alan David Schnitzer
Chairman of the Board & CEO

It's Alan Schnitzer. On the Dominion, as we get through the year end post close, we're going to try to resist the temptation to break out the impact of that in particular. I will tell you that, at least in the current period, it's sort of leaving out the unusual whether that we've had in Canada. There's that hailstorm in Alberta and floods in Toronto, but leaving that out, the Dominion was probably about 0.5 point on the loss ratio, a couple of tenths on the expense ratio, but we'd really like to move away from quantifying the impacts of that transaction. It just gets harder and harder to do as we integrate.

Gabriella Nawi
Senior Vice President of Investor Relations

And sorry, and it's Gabby. Just to be clear, that's because it wasn't in the prior quarter, he's not setting a level for Dominion.

Alan David Schnitzer
Chairman of the Board & CEO

That's right.

Operator

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

Kai Pan
Morgan Stanley, Research Division

Just on the margin, just to follow on that, is that you mentioned some non-cat, largely like a weather-related losses. How much -- if you can quantify that in terms of how much that to drag on the 50-basis point deterioration year-over-year. And also, is that a pattern we have seen in the past few quarters, because, I guess, your peers reported some sort of non-cat large losses in the past few quarters as well.

Alan David Schnitzer
Chairman of the Board & CEO

We've been observing for a couple of years that, that the weather seems to be getting more extreme, and so this is consistent with what we've been seeing over a couple of years. In the quarter, weather was worth something like a 1.5 points on the delta.

Jay Steven Benet
Vice Chairman and Chief Financial Officer

This is Jay Benet. I'd add to that, that when you're asking are there trends involved, we are always going to have quarter-over-quarter different -- differences associated with things like non-cat weather or large losses, and what we try to do is point that out to give you some insight into what's taking place. But I wouldn't say that in all cases, when we say the weather is higher, it means the weather was terrible. I mean it's just higher than it was last year. So I wouldn't have called this a really bad, bad weather quarter, but last year's third quarter was actually a little on the favorable side.

Kai Pan
Morgan Stanley, Research Division

Great. And my second question is on the reinsurance side. Just given what's happening in the marketplace in reinsurance, basically pricing coming down, there are alternative solutions. And I'm just wondering what's your overall reinsurance strategy, are you thinking about setting up some structure, like -- alternative structure, including internal or captive reinsurers?

Jay S. Fishman
Former Executive Chairman

This is Jay Fishman. So we're certainly looking at everything. There's obviously a lot of activity in that space. We're not a big utilizer of reinsurance, broadly speaking. When you look at the amount of ceded premium that we'd put out to the marketplace, it really isn't enough to jump through a lot of hoops and incur a lot of costs to create something that looks snappy but doesn't really accomplish much financially. So we're -- that doesn't mean we're giving up. I'm mindful of the fact that it's getting a tremendous amount of attention. So I've actually been spending some of my own time in making sure I can actually understand it and make sense of it. So far, without a lot of effect to be completely blunt with you, but we will obviously keep looking. I don't anticipate, for us, not to say that somebody else, I don't anticipate that the change in reinsurance pricing in any broad measure will have a meaningful impact on us again, not because -- for example, our property cat treaty wasn't less expensive, it was. But it's just not enough on a premium base of our size to make up a substantial difference. I've also been asked whether we would be interested in building a book of business, and in effect, arbitraging it against the reinsurance opportunity. And I'm always mindful that when you take on a risk on the right side of your balance sheet, there's some permanence to it, and the reinsurance profile on the left may or may not be permanent, and you've got to be very cautious and careful about not finding yourself in an unreinsured position or in a mismatch, which can happen and has happened, I think, back to September 11, and what a bunch of reinsurers did shortly in the days thereafter and lots of us found ourselves with primary exposure without underlying reinsurance to cover. So there's a lot of moving parts here and we're sure looking at it pretty hard. But so far, I'd say nothing that really excites me, at least, a great deal.

Alan David Schnitzer
Chairman of the Board & CEO

Michael, let me just clarify. Just so we pull these 2 questions and don't leave any confusion here. So what we said was, there was about a 2-point increase in the combined ratio due to both weather and the Dominion. That was 2 points, all in, about 1.5 points of that is weather and about 0.5 point of it is Dominion.

Jay S. Fishman
Former Executive Chairman

And again, just speak to direction please.

Alan David Schnitzer
Chairman of the Board & CEO

It's increase.

Jay S. Fishman
Former Executive Chairman

An increase of 1.5 points due to weather and an increase of 0.5 points due to Dominion.

Operator

Our next question comes from the line of Vinay Misquith from Evercore.

Vinay Gerard Misquith
Evercore ISI, Research Division

The first question is in pricing and loss cost trends. I believe you said not to focus too much on pricing, being up and about 3.3% and loss cost trend at about 4%. But just thinking about it, at a 50,000 foot level, should we expect a small amount of margin compression next year? And also, looking at the loss cost trends, if you could help us understand -- I mean, peers are looking at loss cost trend in the 2% to 3% range. Your 4% number seems a little bit high, just wanted to know if there's some amount of conservatism in that?

Jay S. Fishman
Former Executive Chairman

Well, I think perhaps, we'll split the question between myself and Alan. First, the reason that we're just cautioning against evaluating 3.3% versus 4% is that, that arithmetic is pretty easy to do but doesn't take into account all of the factors that affect the profitability of our business. We've reminded people frequently that, a not insignificant amount of exposure base, particularly for example in our Small Commercial business, will act as an increase in rate, absent the change in loss profile. As an example, to the extent we collect more premium due to inflation adjustments on property, unless the loss exceeds what would have been the previous total insured value level, that increase in exposure functions exactly the same as rate. And so it's easy to talk about a widening margin, and I'm going to make up numbers here, it's easy to talk about it when you've got -- to make up a number, 7% rate and 4% loss trend. And I suspect it would be easy if we were talking about 1% rate and 3% loss trend. But in and around the number, it's just not that precise to conclude that within 0.7% point, that margins will necessarily contract or not contract. I -- candidly, I'm not -- our 10-Q is going to say in Business Insurance or it does -- I don't know if we filed it this morning, or we did file it. It says that we anticipate margins to be flat -- equivalent in Business Insurance into 2015. And that is our best judgment at the moment. It's funny -- it's -- people seem to think that there's a stunning amount of difference between talking about plus 0.2% versus minus 0.2%, but they understand that there's no big difference between plus 2.2% and plus 1.8%. It's the same 0.4%. It just happens to be around a different baseline number. So our caution is simply to let you know that notwithstanding all of our analytical skill and insight into the numbers, this is getting pretty precise to make arithmetic calculations based on these numbers. So we just caution against it.

Alan David Schnitzer
Chairman of the Board & CEO

On the second question on loss trend, it's hard for us to comment on anybody else's loss trend, but I would suggest you might want to look at mix.

Vinay Gerard Misquith
Evercore ISI, Research Division

Okay, that's helpful. Just as a follow-up, on the Homeowners commission expense ratio was low. I was just curious of how that was.

Jay S. Fishman
Former Executive Chairman

Can you repeat the question, please?

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

Homeowners commission. I couldn't hear it, I'm sorry.

Vinay Gerard Misquith
Evercore ISI, Research Division

Yes. Sorry. On the Homeowners, I believe the commission expense ratio was lower this year versus last year, I'm just curious why.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

We did reduce the Homeowners commission rate. Yes, we implemented those in 2000 -- probably the middle of '13, maybe a little bit earlier than that.

Brian W. MacLean
President and Chief Operating Officer

And some of the expense initiatives that we had from -- relative to Quantum was also impacted.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

Yes, exactly. So about 25% of our expense reductions fell to the Homeowners line.

Jay S. Fishman
Former Executive Chairman

But the Homeowners commission expense number fell because of a change in the rate that we pay on Homeowners business, we implemented that again in the middle of '13. That's the driving factor there.

Operator

Our next question comes from the line of Jay Cohen from Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Just a couple of questions. I think maybe the first quick one for Doreen. You had mentioned, I think it was the Specialty or Professional liability business that you would change your reinsurance session there that helped earnings. Can you talk a little bit more about that? And then separately, asbestos, I'm surprised no one's asked you yet about it, but another very sizable charge. Can you talk about really what you're seeing there now. It just feels as if this is an annual sizable charge and you're almost going on the pay-as-you-go basis and we should almost expect this kind of charge going forward. I'm wondering if you could give more insight into the asbestos.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

This is Doreen. I'll talk first about the Bond & Specialty Insurance reinsurance treaty and then I'll turn it over to Jay Benet for asbestos. But as I think we reported in the past, the decision was made to exit from our Management Liability excess-of-loss reinsurance treaty, and that decision was made at the end of 2013. And essentially what you're seeing is that as we looked at our book of business, both from a limit standpoint, the quality of the underwriting, we just felt like the ceded premium didn't make sense given the performance of the book. And so if you were to look at the underlying combined ratio being up about 4 points, it's about 3 of that underlying improvement. And it's really just looking at what premium you wanted to pay for your loss content. So a great decision was made and we see it in the results.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

That's helpful.

Jay Steven Benet
Vice Chairman and Chief Financial Officer

So hi Jay, it's Jay. As it relates to asbestos, as you know, we follow this very closely every quarter and we supplement the quarterly procedures with what we refer to as the very in-depth claims study that gets done annually, and we've been completing it in the third quarter. So what's going on with the data? First of all, every time we put up an asbestos reserve, it's our best estimate of what the totality of the losses will be, and as you know, there are pages and pages in our 10-K and 10-Q describing all the uncertainties associated with asbestos and what's taking place or not taking place in the environment. So in terms of the overall environment, I'd remind everybody that we've had the asbestos exclusion in our policies for decades. At this point, the product isn't used the way it's formally used decades ago. And the assumptions that we build into the reserves are that there'll be a tailing off of claims over time based on the aging population and all the other dynamics that go along with that. So we are making these estimates and then periodically, looking to see are the estimates holding up in terms of the data that's emerging. And what's been happening in the last couple of years, and we can come up with anecdotes as to perhaps why it's happening, but what's -- keeps happening over time is that our estimates, which are the best estimates at the point in time, are proving to be a little short as new information emerges. And in talking to our claim people who deal with this and asking the age-old question, why doesn't this stuff drop off at the rate that we had expected? Some of the anecdotal answers tend to be, and I underscore anecdotal, that well, perhaps, we have a situation where years ago, given where general medicine was at that point, people were dying of, of different things like heart attacks or forms of cancer, and with medical advances they're perhaps living longer, and by living longer and not dying of those particular diseases, mesothelioma might develop and suddenly, now you have an asbestos claim. So part of this is the estimation process, part of this is just trying to understand the trends that are going on, but I welcome the day when we can all watch a sporting event and not see a plaintiff's attorney ad saying, if you ever heard the word mesothelioma, call this number. But that's the environment. But I will say that there isn't a fundamental change in the environment, and it's not new theories or anything like that. It's more a matter of trying to estimate what's actually out there. I hope that was helpful.

Operator

Our next question comes from the line of Larry Greenburg from Janney Capital.

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

I respect that you don't want to get into too much detail on Dominion, but given the fourth quarter will be the first where we're on an apples-to-apples basis, it would be helpful to just know what Dominion is growing at organically. And I think when you did the deal, you expected it to be modestly accretive to 2014, and I'm wondering if that's coming to fruition.

Alan David Schnitzer
Chairman of the Board & CEO

Larry, it's Alan. I'm just trying to process the questions here. In terms of -- on Dominion, I should just take a step back and say that we're very pleased with the transaction. The integration is going very well. They're very pleased with the local team in Canada and the way the 2 teams are integrating and very pleased with the way that the -- both teams in Canada and our U.S. businesses are integrating. So I should really start off -- and I think this is the important message about the Dominion, it's going very well, there's no surprises and we're enthusiastic about the deal today as we were when we signed it.

Jay S. Fishman
Former Executive Chairman

And I -- let me just add in because it's a great time to do it. A non-insignificant portion of the rational here was to export and make available in the Canadian marketplace product and expertise that we had here in the U.S. that had not been developed up in Canada. That is still very much the plan. So we are at the early days here. We are very much at the early days.

Lawrence David Greenberg
Janney Montgomery Scott LLC, Research Division

I'm sorry, but I think that was helpful.

Alan David Schnitzer
Chairman of the Board & CEO

Larry, in terms of your specific questions, I think we'd really prefer on a business this size, probably not to go down to that level of detail other than to say it's on track. There's -- whenever you do a deal this size, there's always some surprises that are a little bit good and a little bit bad, but all of those are within the range of expectations and we're very, very pleased with the transaction.

Operator

Our next question comes from the line of Al Copersino from Columbia Management.

Al Copersino

I was wondering if you all had available or were willing to share for the Bond & Specialty segment or for the Personal segment, we have the renewal premium change in the slide deck. But I was curious if you were able to give us the rate changes specifically.

Jay S. Fishman
Former Executive Chairman

It operates -- so Brian and I will chat here, but those businesses in particular, it's really quite difficult to parse rate change and renewal premium change because they operate so much together. For example, the policy limits, right, so if you got an inflation element in the underlying property, for example, that's going to affect premium. But that happens in many cases, in effect, automatically. So we don't track rate and renewal premium change at the granular level that we can in other businesses to provide that breakout. It's not that it's not an appropriate question, it's that the business dynamics under it operate differently and, therefore, really can't be parsed with quite as much precision.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

This is Doreen. We do look at it, to Jay's point, but we find the combination of them with renewal premium change to be the more meaningful way to look at the business and we've never really disclosed that level. So we can look at it, but we didn't want to make sure...

Jay S. Fishman
Former Executive Chairman

In most -- yes, in most cases, in our Personal lines of business, fundamental exposure is not changing and it is the total price change that is really reflective. And Doreen, you can talk about the bond.

Jay Steven Benet
Vice Chairman and Chief Financial Officer

You can get deductible -- you can get changes, but we don't just parse it at that level.

Jay S. Fishman
Former Executive Chairman

Bond?

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

On the bond side, I would say -- and we talked a little bit about the -- in Management Liability in particular on RPC and rate, it's such, again, to Jay's point of combined concepts of what the limits are, the attachment points, the term of the policy. So we look at them blended together, not that we don't look at them, it's just more meaningful for us to combine them for us, for the business performance.

Operator

Our next question comes from the line of Meyer Shields of KBW.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Doreen, has there been any change in the competitive environment for Personal lines, specifically Auto, over the course of the year?

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

What we've seen and we've watched this pretty closely to see, particularly with our commission changes and Quantum 2.0, what's going on out there. And I would say, in the independent agency channel, we've seen some very targeted but not broad, follows in terms of a little bit of people changing commission, a little bit of targeting specifically on price reduction. What we haven't seen in that channel is anybody really address broadly the cost structure. And so, no, it's not a major change. We just continue to watch it.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, that's good news. Jay, you talked earlier about the other factors that can drive margin improvement aside from the GAAP between rate increases and loss cost trends. I was wondering, are those other issues -- is that expected trends changing at all?

Jay S. Fishman
Former Executive Chairman

Is that expected trend changing at all. Help me with -- I don't understand quite the question.

Meyer Shields
Keefe, Bruyette, & Woods, Inc., Research Division

I'm asking it poorly. Is the impact of other factors besides the rate, loss trend gap and its impact on margin expansion, is that -- translate -- given the improvements that you've had so far, for example, in the granularity of pricing and so on, should we expect less margin expansion from those other factors going forward than we have in the past couple of years?

Jay Steven Benet
Vice Chairman and Chief Financial Officer

I got it. The answer is, I sure don't think so. The reason for the caution is simply because it would be I think, inappropriate to leap to a conclusion that 4% versus 3.3% will, in effect, by definition, result in a narrowing margin. It may. I'm not saying it's not, but there are other factors that go in to whether the margin gets bigger or smaller and you're in the range now of the gap between these 2 numbers that is loss trend and rate, to be such that these other factors, which always operate, they always operate, could actually produce a different outcome than this simple arithmetic would demonstrate. And again, the example I used before with rate of 7% and loss trend of 4%, this is just a loss trend of only -- please, it's an easy call and with loss trend of 4% and rate of 1%, it would also be an easy call. But you're at a range now where it's not an easy call. I'm not saying from the outside looking in, by the way. I'm saying even from the inside, it's not an easy call to absolutely say it's going to expand or it's going to contract. It is on the line in effect right now and we don't know how to be any more precise than we're being with you. This is as good as we have to offer.

Operator

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

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

Just recently, I was doing an agent tour and they were talking about a little bit more aggressiveness in the spread between new business and old -- and renewal business on the commercial business. And I wanted to see if you perceived any change there in that, either in Travelers or in the marketplace,.

Alan David Schnitzer
Chairman of the Board & CEO

Hey, Paul, it's Alan. Let me comment on us, and I'm not sure we're going to comment more broadly on the market, but it's always dangerous, I think, to take one conversation with an agent and extrapolate from that. I would say from our data, we see that over the last couple of years, 7 or 8 quarters has been a pretty consistent gap between new and renewal, but if you look back over a longer period of time, I'd say that gap is reasonably tight at the moment on a longer-term view.

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

And then as a separate question, it's been a long time since we've talked about some of the direct channels and other experimentation that you have been working on over several years. And I'd like to know if Quantum 2.0 is sort of where we're at with respect to what we're looking at for the future of Travelers for the next couple of years or if there are some ongoing efforts still to build out other channels.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

This is Doreen. I'll just speak to that. So I will tell you that Quantum 2.0 is definitely a positive for direct-to-consumer as well as the agency channel. It was a product that we thought would be attractive across channels. So as we look at our metrics around conversion and sales, we believe that, that Quantum 2.0 has definitely had a positive on that. In addition to that, we always look for process improvement. We've also been very focused on looking at digital marketing and how to use our dollars in a very targeted way for direct. We also have plans, and I think we've talked to all of you in the past, this is not just direct, but we will continue to look at where we can enhance the property products, as well as looking at how we bring accounts together and that will be both a benefit for the agency channel as well as direct.

Operator

Our last question comes from the line of Josh Stirling from Sanford Bernstein.

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

So Jay, pricing has been slowing. It's come off, what, 3% in the past year. And if you sort of simplistically project forward another year, at last year's pace, pricing probably would be 0 or maybe even a slight decline. And so I think big picture of what we're just trying to figure out whether the industry's pricing decline is going to stop at something like inflation, does it go to 0 or does it go negative? And I recognize you guys don't want to talk about other companies, but to keep you focused on Travelers. And if I understand all the sort of back and forth around the margin outlook and Alan's comments, I think you're basically saying that you'll keep pricing more or less in line with inflation over the next year. So is that right?

Jay S. Fishman
Former Executive Chairman

Well I can certainly tell you what our strategy is. I have no problem sharing that, and obviously, the ability to execute in a business environment, we may succeed, we may not. We haven't changed anything about the way we're approaching individual accounts. We -- I remind everybody of this all the time. Right now, there's an underwriter in Kansas City who is seated right now, who's sitting with an agent, having a conversation about one account, and they're not thinking about the overall market, they're not thinking about inflation, they're thinking about the return on that account and how do I improve it. So you got to start with the premise that this really does start at the bottom and work its way up. As accounts have become -- as increasing number of accounts have now had several years of increases and are now producing profitability returns, however you like to look at it, that really fall into that, boy, we're glad we have that account category, we ask our people to be thoughtful, to be judicious about the way they approach every individual account. It doesn't have to be a straight line. It can be a stair step. It can be driven by the local market. It can be driven by the relationship with an agent. It can be driven by the size of the book that we have with the agent. It can be driven by whether there's been claim problems or not on that account. All of those things go into the pricing of an individual account. Now what we're trying to get to is a point where over time and come back to over time all the time, that we manage to offset the impact of loss cost by either rising prices or self-help through efficiency or expense reduction -- I point the kinds of things that Greg Toczydlowski and the group have done in Personal Insurance. That -- $1 saved in expense is as good as $1 raised at the point-of-sale in rate. In fact, arguably even better. I -- and I will speak really just personally because I'm not sure I'd be speaking for the whole place. I am hopeful, maybe even cautiously optimistic, that we will not -- and I said this, by the way, 10 years ago, maybe not 10, maybe 8 years ago -- I personally believe that the Property and Casualty business will have a meaningfully lower level of cyclicality. Never said 0, but always said a less or lower amplitude of that cyclicality. There are a host of reasons why I believe that, analytics and data are just one, but it's very important one. And I think it's proven on the way down before we entered into this cycle, I think it's been proven here on the way up. I'm hopeful, maybe even optimistic, that it will -- that, that will turn out to be true on the way down. We don't see anything in the way in which business is done at the point-of-sale in the market that would suggest that we are at a precipice that would suggest that something fundamentally is going to change next month, next quarter or frankly, even next year.

Now we could be dead wrong about all of this. It's possible. We could be dead wrong. But we're focused on over time maintaining our margins. It doesn't mean that an individual account has to have a price increase every year. It doesn't mean that in the quarter, the rate won't come under loss trend. I'd like to know where the mix of business is that's coming up for renewal, the answer to the success for us is in the granular analysis more than the headline number. So I'm -- that's honestly how -- never anything, but honest -- but that's how we see the marketplace environment. That's how we intend to operate. We'll see if it's sustainable. I'm -- again, I'm hopeful and maybe even optimistic. There was a thoughtfulness -- we understand -- but we're not unique in this. We certainly understand the world of risk-taking. I have a lot of respect for a lot of other companies out there because I see how they operate and they also had a great respect for risk-taking. And that, I think, is kind of different than it was perhaps 15 years ago. It's -- there's a different level, I think, of understanding and perception of what it means to commit your shareholders' capital to a risk or a series of risks and turn out to be dead wrong. I think there's a healthy regard for that and in that -- that has resulted in a set of industry-wide, better analytics, better risk-taking profile, that I think, by the way, is good for the customer. I think it's good for the agent, and I think it's good for the markets. While cyclicality, up or down, is actually bad for everybody and better insight, better data, better analytics is actually better for everybody, you get better analysis, you get better -- more thoughtful pricing related to risks. So that's a somewhat fulsome answer. But that's our feel about it.

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

That's really helpful, Jay. I guess, just one other question. Related to the Personal lines business. You guys have made big inroads of Quantum 2.0, sort of stabilizing your volumes there, getting a more competitive product in the market. I'm wondering what your plans are for Homeowners. It's been -- I mean, a decade ago probably wasn't a very good business, but it sure seems like a very profitable one now, but it's been shrinking for many years. And I'm wondering what -- when maybe we see you guys turn the corner there and start to use this as a growth engine.

Jay S. Fishman
Former Executive Chairman

I'm going to ask Doreen to answer, but just because I'm allowed to be so proud of what the organization has done. So as far back as we see the data having, I'll say integrity, and that's at least 10 years and maybe more on a comparable basis, we had 1 year in our Homeowners business with a combined ratio of over 100 and that was 2011. That was the Joplin storms and the Tuscaloosa storms. So whether it was Ike, Gustav and Dolly or Rita, Katrina, Wilma, it didn't matter. This -- the way that business has --

actually, I'll come back to my previous comment about risk-taking, I am just so proud, candidly, of the way the whole organization has operated and thought about risk-taking. So we love the business, and it's been a terrific performer for us and actually, I personally think, in the future, as the potential shift between Auto and Homeowners, I think it could very well do some shifting over the next 10 years, I love where we are. But with that, Doreen, you can take the rest.

Doreen Spadorcia
Former Vice Chairman of Technology, Claim Svcs, Ops & Risk Control

Thank you. And obviously, following on what Jay said, I'll tell you that we spent -- and it goes back to, I think, one of the earlier questions just about looking at weather and you probably recall, we looked at pricing, we looked at underwriting, we looked at concentration and we feel really that we're operating now from a position of really great returns and we see that when we have a competitive Auto product that also helps drive home, and we are going to look for those opportunities where we can tune the products so that in those areas that we think it makes sense to grow, that we will. So again, we were planning just -- we talked about Auto where we thought we were going to be flat to comparing ourselves in the fourth quarter to the -- to last year. We knew Home was going to lag a little bit behind that. So everything we're looking at with production is really according to what our expectations were. But as Jay said, we really were a property underwriter, we like the products and we're going to look for the opportunities going forward.

Gabriella Nawi
Senior Vice President of Investor Relations

Yes, this will conclude our call. As always, I am available in Investor Relations for any follow-up questions. Thank you for joining, and have a great day.

Operator
Ladies and gentlemen, that does conclude the conference call for today. We thank you for your participation and ask that you please disconnect your lines.