S&P Global
Market Intelligence

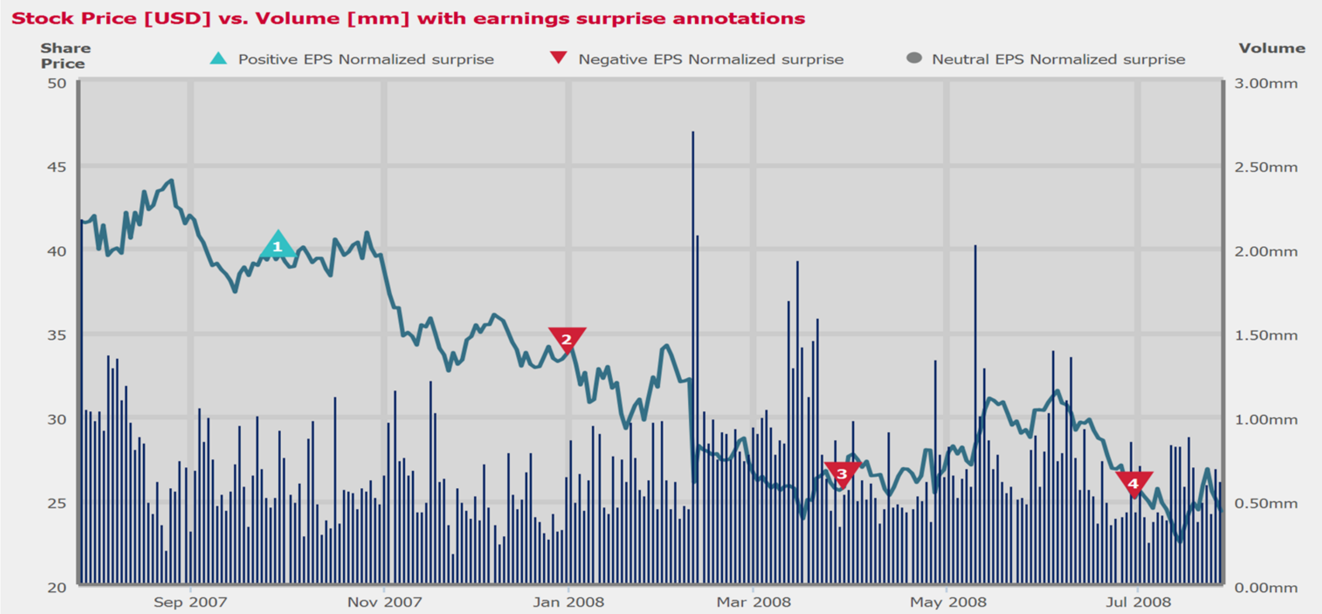
CNA Financial Corporation NYSE:CNA
FQ3 2008 Earnings Call Transcripts

Monday, October 27, 2008 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2008-			-FQ4 2008-	-FY 2008-	-FY 2009-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.69	0.31	▲(55.07 %)	0.80	3.31	3.55
Revenue	-	-	▲0.13	-	-	-
Revenue (mm)	1596.00	1598.00	-	-	6462.00	6268.00

Currency: USD
Consensus as of Oct-15-2008 11:59 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2007	0.68	0.78	▲1 14.71 %
FQ4 2007	1.02	0.82	▼2 (19.61 %)
FQ1 2008	1.01	0.82	▼3 (18.81 %)
FQ2 2008	0.96	0.93	▼4 (3.12 %)

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Call Participants

EXECUTIVES

D. Craig Mense

James R. Lewis

Nancy M. Bufalino

Stephen W. Lilienthal

ANALYSTS

Jay Cohen
Merrill Lynch

Matthew Carletti
Fox-Pitt Kelton

Robert Glasspiegel
Langen McAlenney

Ron Bobbin
Capital Returns

Unidentified Analyst

Presentation

Operator

Good day, and welcome to the CNA Financial Corporation's Third Quarter 2008 Earnings Conference Call. Today's call is being recorded.

At this time, I would like to the conference over to Ms. Nancy Bufalino. Please go ahead ma'am.

Nancy M. Bufalino

Thank you, Patrick and good morning. Welcome to CNA's third quarter 2008 discussion of our financial result. Hopefully, everyone has got an opportunity to review the press release and financial supplement, which we released earlier this morning and can be found on CNA website.

With us this morning to discuss our financial results are Steve Lilienthal, Chairman and CEO; Craig Mense, CFO; and Jim Lewis, President and CEO of P&C Operations.

Before we get started, I'd like to advice everyone that during this call there maybe forward-looking statements made in references to non-GAAP financial measures. Please see the section of the earnings release available on CNA's website contains forward-looking statements in regard to both.

In addition, the forward-looking statements speak as of today October 27, 2008. CNA expressly disclaims any obligation to update or revise any forward-looking statements made during this call. This call is being recorded and webcast. During the next week, this call may be accessed on CNA's website at www.cna.com. Following the conclusion of today's prepared remarks by CNA's senior management, we'll be happy to take questions from the investment community.

With that, I'll turn the call over to CNA's Chairman and CEO, Steve Lilienthal.

Stephen W. Lilienthal

Thank you, Nancy, and good morning everybody. Thanks for joining us today. This was a complex and challenging quarter on all fronts. Economic conditions remain stagnant, the global financial markets experienced the most severe pressure in memory if not in history, and the insurance marketplace remain competitive... excuse me, further aggravated by significant catastrophe activities.

CNA has continued to operate in a disciplined fashion, consistent with previous quarters and consistent with our head on proactive approach to other issues.

During the course of this morning's call, we will discuss the following: the financial results for the quarter and year-to-date, the CNA Financial and for our business segments, the impact of the global meltdown in the financial markets on our investments portfolio, and we will discuss the details of our comprehensive capital plan.

We believe that by taking these proactive steps, we further augment our solid capital base and are well positioned to both meet the challenges and act on the opportunities that are likely to emerge in the marketplace.

In addition to bolstering the statutory capital by the $1 billion in our insurance company, we had a significant level of cash on hand at the holding company and the details of this plan are included in the press release. And Craig will discuss this in a few minutes. We will also discuss our P&C Operations and our disciplined cautious conservative approach in the difficult market.

Premium levels have reduced a bit inline with market conditions, retentions are holding solid at just over 80, the rate levels are running at about minus 4% on average and are inline with market if not a little bit better.

As an additional note, we are not significant players in the large cap casualty market segment, which appears to be the most aggressive at this time.

New business at 17% of the total is very appropriate for the market and exactly where we said it would be four to five years ago. The combined ratio of a 107 for the quarter includes approximately 16 points of catastrophe activity. It still remains at just over a 100 combined for the year and well under a 100 excluding caps in the quarter.

Our expense ratio, which has been consistently managed to reflect the changing size of the business remains in the 30% range year-to-date despite investments made in certain key business segments in both standard and special lines. The strategy going forward, as it has been in the past, is to leverage a very, very diversified product portfolio by moving and shifting in and out of segments and cross selling our existing customer base through a very solid distribution network.

Overall, in a market that keeps getting tougher, CNA is sticking to and delivering on the fundamentals. And Jim Lewis will give you the details on that in a few minutes.

Before I turning this call over to Jim Lewis and Craig Mense, let me add a final note regarding our leadership succession plan. As you will recall, when we announced Tom Motamed, my successor to be last June, he had a 12 month 9/15 covenant in his employment arrangement with Chubb. Knowing and respecting that I agreed to stay on until June '09 even though I had intended to retire when my contract expired at year-end 2008.

We had hoped that at some point Chubb would be agreeable to allowing Tom to join CNA at an earlier date. I'm happy to report that we've reached an agreement with Chubb for Tom for time to join CNA on January 1, 2009 as Chairman and Chief Executive Officer.

Tom is an extraordinary individual. We are delighted to welcome him sooner rather than later. And I'm looking forward to working with Tom through the transition. This will certainly eliminate any possibility of organizational loss of focus. And we feel that this is a very well planned and executed succession plan.

In summary, our ability to withstand and navigate through the pressures of the third quarter speaks of a very solid business we have built over the past several years. With good work on the fundamentals and a smooth leadership transition, we are very well positioned to stay on our profitable course.

With that, let me hand it over to Craig.

D. Craig Mense

Thanks Steve. Good morning everyone. As Steve mentioned, the markets have made this a very challenging quarter. It's obviously a challenging time for all of us, but it's one that we are certain that we're up to meeting.

As we look at our company, we see one that has a well established record of generating meaningful operating income, is a disciplined participant in the insurance market, is generating significant positive cash flow and has more than ample liquidity.

While our capital levels have been pressured by the extreme evaluations of our invested assets in today's dysfunctional market, we have acted preemptively to eliminate any concerns about our financial strength and to further bolster our already strong capital and holding company cash position. As result, we are well positioned to act on opportunities that may emerge over the near and longer term.

Now, let me take a moment to give you a bit more detail on the financials. For the third quarter, net operating income from continuing operations was $83 million or $0.31 per diluted share, compared with $212 million or $0.78 per diluted share in the prior year period.

The net loss for the quarter, which includes the impact of realized investment gains and losses as well as discontinued operations, was $331 million or $1.23 per diluted share. This compares to $174 million of net income or $0.64 per diluted share last year.

Year-to-date, net operating income from continuing operations was $554 million or $2.06 per diluted share, compared with $837 million or $3.08 per diluted share in the first nine months of 2007.

Year-to-date net income was $37 million or $0.14 per diluted share, compared with $687 million or $2.53 per diluted share for the prior year period.

Property & Casualty Operations produced third quarter net operating income of $92 million, compared with $331 million in the prior year period. The primary drivers of the decline were higher catastrophe losses and lower net investment income. After-tax catastrophe losses were $168 million this quarter, compared with $7 million in the prior year period. Year-to-date cat losses were $233 million after-tax. This compares with $37 million in all of 2007.

With respect to the non-core segment, Life & Group produced a third quarter net operating loss of $36 million, compared with a $131 million loss in the prior period. Last year's result included an after-tax loss of $108 million related to a reinsurance arbitration settlement.

The corporate segment had third quarter up... net operating income of $27 million, compared with $12 million in the prior year period. The current period benefited from a $27 million after tax relief from an allowance for uncollectible reinsurance receivables. We continued to closely manage all our run-up operations to mitigate earnings risks.

Third quarter pre-tax investment income was $439 million, down from $580 million in the prior year period. These results include $23 million of losses from our trading portfolio in the current period, as compared to $2 million of trading losses in the previous period.

Excluding the impact of trading, gains and losses, the primary drivers of decreased results were our limited partnership investments and the effect of lower short-term interest rates.

Limited partnership losses were $77 million or a negative 3.5% return, compared with LP income of $90 million in the third quarter of '07 and $46 million in this year's second quarter.

Our portfolio of limited partnerships continues to be a very attractive investment despite recent earnings volatility. These holdings bring diversification to the overall portfolio, with less volatility and higher absolute returns and equities. The volatility is expected and we are confident that they will perform well over the longer term just as they have over the last decade.

After tax net realized investment losses were $423 million this quarter, compared with losses of $38 million in the prior year period. Those realized losses included after tax impairments of $380 million this quarter. The majority of which were driven by credit issues.

The realized losses and impairments were primarily related to preferred securities and corporate bonds, including securities issued by Fannie Mae, Freddie Mac, Washington Mutual and two Icelandic banks.

The net unrealized loss position of our investments was $3.4 billion at the end of the quarter, an adverse change of $1.9 billion from June 30th of 2008. This change affected virtually all asset classes and accelerated in the last ten trading days of the quarter, which accounted for approximately 75% of the total quarterly change in unrealized loss. The market freeze up at the end of September was especially tough on evaluation of our corporate and municipal bond portfolios.

We regard the unrealized loss position as temporary and based on current circumstances are very confident in its ultimate recovery. In light of our unrealized loss position, is worth noting that the abnormal conditions in the fixed income market. Credit spreads and pricing marks are extreme. We believe there is a no appreciable change to the credit quality of our portfolio.

CNA has the intent and ability to hold these assets in an unrealized loss position until they recover their value. The combination of positive operating cash flow and principle payment is generating over $2.5 billion annually of investible cash. As yields returned to historical norms, we expect our unrealized position to improve substantially. In the meantime, we are able to deploy our investible cash flow at very attractive rates.

In light of financial market uncertainty, we also felt it was prudent to move ahead in a plan to supplement our capital base. The details of the capital actions are in our press release, so I will confine my remarks to the few high level observations.

The course of the plan is a $1.25 billion preferred stock issue to be purchased by loans. The proceeds will fund a $1 billion surplus no transaction with Continental Casualty, our major insurance subsidiary to strengthen statutory surplus.

Our risk based capital levels are strong, and this addition provides an added level of comfort at a time of financial uncertainty. The remainder of the proceeds $250 will be held at the CNA upholding company level and we'll bolster cash and increase our financial flexibility. These funds are in addition to the more than $700 million in short-term investments already held at the holding company level. We expect to have approximately $1 billion of cash at the holding company level when we complete this transaction.

Between the addition to statutory capital and the enhanced liquidity at the holding company level, our view is that we are very well positioned to withstand further financial market stress and as importantly to act on emerging opportunities. By the way, our thought here relates to the prospects for organic growth, not acquisitions.

Finally, we will discontinue the quarterly common stock dividend they are getting this quarter to further conserve cash and capital.

Next, let me add a few comments about our securities lending program. In light of external concerns about securities lending, it is important to note that we only lend securities for purposes of enhancing investment income.

We require borrowers of these securities to maintain collateral with us of at least a 102% of the fair value of the securities loan. We only accept U.S. Government Securities Agencies or Ginnie Mae Securities as collateral. We do not utilize collateral received for operating or financing purposes.

Our securities lending programs are managed as a matchbook portfolio, where the collateral is invested to substantially match the term of the loan, with some limits risk. We have never experienced a loss from our securities lending activities.

I trust that you recognize that CNA is a company that is producing steady, meaningful operating income, has ample liquidity, is generating significant positive cash flow, has acted prudently to eliminate uncertainties, is well-positioned to sustain additional financial market stresses, and as importantly, to take advantage of emerging market opportunities.

With that, I'll turn it over to Jim.

James R. Lewis

Good morning, everyone. The soft market, hurricanes and a sluggish economy didn't make it easy for property casualty insurers in the third quarter. But as you heard from Steve and Craig, property and casualty operations continues to perform well.

Our focus on catastrophe exposure management helped contain our losses to a manageable level. I'm also pleased to say that as soon as possible, after each stone passes since, our claims teams were on the ground, serving our customers professionally and efficiently. This type of operational discipline is completely consistent with our focus on the fundamental.

As I have mentioned before, we continue to focus on portfolio optimization to maximize risk adjusted returns, data driven decision-making for improved risk selection and pricing, field and distribution management aligned with business strategies, cross-sell to leverage our broad portfolio, and performance monitoring tools and government's processes to navigate the market cycle. In short, we continued to push hard on the key drivers of our business.

Now let's turn to a few of our key operating metrics, starting with premium. Operating and cash, the operation's metric and premium volume decreased 3% for the third quarter, and 4% year-to-date.

In standard volumes, net working premium decreased approximately 4% for the quarter, and 7% year-to-date. Specialty Lines was essentially flat for the quarter and year-to-date.

Our premium volume reflects three major factors: market pressure across our portfolio especially, on Standard Lines; very solid retention of renewal accounts; and a disciplined approach for new business in a soft market. I'll touch on the latter two items in a moment.

With respect to market pressure, it's not letting up. So, while we pay attention to the top-line we are not top-line driven. We continue to focus on the quality and mix of our business. In Specialty Lines just a matter of adjusting and refining an already high quality profitable portfolio.

In Standard Line just more of a matter of strengthening our fundamental. Through segmentation, sub-segmentation and predictive analytics, we are improving the quality of our middle-market book.

In small business, we're building a franchise with enhanced products, award winning agency interface and expanded distribution outreach. In addition, we're already well positioned in business like boiler and machinery, in the marine, excess and surplus lines and others. By adding staff and resources to these specialized businesses, we expect to balance out our more mainstream commercial insurance risk. Overall, we feel very good about our progress in Standard Lines.

Now, let's look at rate and retention metric. For the third quarter average rates decreased by little less than 4%, a slight improvement over the previous three quarters. The average rate decreases for Standard Lines was approximately 5%, for Specialty Lines it was 3%. This is the sixth consecutive quarter that rate changed across our portfolio has run in the range of negative 3% to 5%.

In the south market of the late nineties, rates fell off a cliff. This time around we continued to see a steady gradual decline. It is still very challenging, but with our diversified portfolio, strong distribution relationships and business quality metrics, CNA is well positioned to deal with this type of market pressure.

For our retention, we are run at approximately 82%, very solid and inline with the past few quarters. Underlined retention was 80% during the third quarter, with Specialty Lines running at 84%.

Overall, our rate and retention numbers that were underscore the importance of managing the risk of adverse selection. Our renewal efficiency metrics are critical in this regard. Favorable rate and retention also reflects strong distribution relationships, which enables us to get out ahead of renewal accounts before they go to market. These close working relationships are critical for retaining quality accounts without given away the store.

Now, let's turn to new businesses. We wrote approximately $264 million made in new business in the third quarter. This represents approximately 17% of production, appropriate for the market and right where we've been all year. Overall, I would characterize our new business strategy as controlled, selective and forward-looking.

As with renewals, we tracked the quality of new business with the range of metrics. With respect to the selectivity, our new business strategy is in direct support of our portfolio optimization, most new business in our target classes.

In addition, cross-sale continues to provide a nice boost to our new business; $86 million in the third quarter or 32% of all new business.

And finally, despite market competitions, we're beginning to realize modest growth in our target classes. At the same time, we're increased in our understanding of customer needs in these classes and build in a franchise with our agents. So, when the market eventually hardens, we'll be in a better position for growth.

Turning to loss ratio, our third quarter 2008 net common year loss ratio reflects the heavy cat overlay on the sound underwriting focus. P&C up loss ratio of 76% includes approximately 15 point of catastrophe losses and four points of favorable development. Most of the cat losses came in Standard Lines, which had a net account year loss ratio of approximately 96%, including 31 points of cat loss and 1 point of unfavorable development.

Specialty Lines loss ratio of 59% including 1 point of cat losses and 8 points of favorable development. The impact of cats and development is fully broken out on page 10 and 12 of our financial supplement.

On a net tax, net year basis in 2008 loss ratio for property and casualty operation is approximately 73% versus 67% for 2007. Again catastrophe losses were the main two drivers of change, adding seven points to the current year ratio.

As mentioned in previous calls, we are very vigilant when comes to our loss ratio. I already mentioned catastrophe exposure management portfolio management and predictive modeling. With these, I would add three others. First, a very disciplined process of underwriting controls and grants of authority; second, clients involvement in every stage of underwriting management, which led trust to trends and coverage interpretations and emerging hazards. And finally, risk control experts who specialize in the industries we serve. Their assessment of account quality helps improve our risk selection and pricing.

Now, let's turn to our combined ratio. With the third quarter property and casualty operations came in at a 107%, the 15% increase from the prior year period is primarily related to the loss ratio that previously discussed.

Year-to-date, the P&C Operations combined ratio was approximately 101%. This includes approximately seven points per catastrophe, which puts our non-cash combined ratio on the range we've been running for the past few quarters. The Standard Lines, the third quarter combined ratio was approximately 129%. Specialty Lines came in with a very respectable combined ratio of 88%.

Turning to expenses for a moment, property and casualty operations had a third quarter expense ratio of approximately 32%. This includes approximately 1 point from wind storm assessments. We continued to mange expenses aggressively, but as we've said before market pressures will challenge our ratios going forward. In addition, we continued to invest in CNA's future, for instant adding underwriter at the point of sale and upgrading our claims operation.

Before wrapping up, I would like to say a few words about our outlook for the rest of year and into '09. Overall, I am cautious about the market, but cautious in our direction. CNA is well diversified by product, account size and geography.

Our distribution relationships are solid. We have a track record of building strong sustainable market positions. I feel very good about our Specialty Lines businesses, where we're leveraging our strong positions in health pro, professional liability and management liability to related market niches. Our small business operation continues to gain traction.

In lower market, we're growing a core book of more profitable construction and general industry business. I'm encouraged by the potential of the more specialized Standard Lines businesses, but we're building out what we already have a profitable operations.

Finally, there is our award winning claims operation. We treat out claims by size and complexity. Our expressed inter churns around less complex claims professionally and efficiently. But with respect to medical claims management, our integrated approach goes at every driver of medical and indemnity cost.

We also have an excellent record of favorable settlements and verdicts. It's all about excellence in execution, which we continued to enhance with investments and imaging, product control and certification of our step. In short, I continued to feel good about our ability to maneuver through the market cycle.

In summary, the third quarter was another solid quarter; catastrophe losses notwithstanding. We continued to optimize our portfolio, self and underwriting discipline, manage expenses for our investment selectively, and leverage our strong franchise and our chosen industry segment. As I said at the beginning, we're executing well on our business drivers.

With that, I'll turn it back to the operator.

Question And Answer

Question and Answer

Operator

[Operator Instructions]. We will take our first question from Jay Cohen with Merrill Lynch.

Jay Cohen
Merrill Lynch

Hi. Good morning. Question relates to the capital raise. I guess I was although surprised by it and two questions actually. First, how much is this related to the statutory surplus in your life insurance companies?

D. Craig Mense

None of it related to statutory surplus in the Life Company's Jay, its Craig.

Jay Cohen
Merrill Lynch

Okay. But it seems on the property and casualty side, maybe I am using the wrong metrics, but it always seemed like you had a reasonable cushion. And even though you had some decent realized losses there, it seemed like you had that cushion.

D. Craig Mense

That's true. And I'd say that would continue to be the case, and would have been the case before we did the capital raise. So, our objective here in the capital raise was as I said, eliminate any question's uncertainty, and to position us to really withstand any stresses, as well as really act on opportunities that we thought were more likely to emerge, whether on the investing side or on the particularly, on the organic growth side and the business going forward.

So, a day before the capital raise our targeted... I know we've... I've talked to you before about kind of ignoring or saying how crude the premium surplus ratios were. But, I think maybe another, more standard ratio to look at is risk based capital, in terms of raise were minimums. And our target has always been to be somewhere in the 325 to 350 range.

So, before the range we were in... we were at on minimum, down to 325. And after the range, we're really closer to 373, 375. So we are at historical... near at historical highs, really across any measures. And we've done it more to be anticipatory than anything.

Jay Cohen
Merrill Lynch

And, have you had a dialogue with the rating agencies? For example, did they have any say, essentially in the capital raise?

D. Craig Mense

Well, no they had no say in the capital raise.

Jay Cohen
Merrill Lynch

Maybe I phrased that wrong. Maybe... were they part of the rationale for raising capital?

D. Craig Mense

No. They weren't part of the rationale... I mean, we, I guess be clear, they certainly weren't the impetus or the catalyst for raising capital. Let me be clear, that was ours. Among the capital measures and metrics we've look at, are all the rating agencies capital models, as well as our own economic capitals, where we're premium to surplus, as well as RBC. And again, this rates puts us at or near historic highs, on any of those measures.

I think that maybe what you are also getting at and, let them speak for themselves. But, we had certainly had conversations with them, each and every one of them about these decisions, and about the raise and the specifics of it. I would say they were very complementary of our preemptive action and how comprehensive the thought process and the plan was, and we're hopeful that they're all supportive of it.

Jay Cohen
Merrill Lynch

I assume that Life Company, I mean, look like the June surplus, that you guys show is about a little over $500 million. And, yet if you look at the realized losses, which is reported net loss for the Life Company, much of it was realized losses, you lost about $230 million, which suggest a less half a capital in the Life operation. So, I was really surprised you said none of it related to Life Company, is look you have less the capital there, the statutory capital. Am I thinking about that incorrectly?

D. Craig Mense

Yes, I think that the... what you're looking at relative to those numbers, remember that long-term care little bit different than what's in the statutory entity, which... remember that does not have long-term care. Long-term care results are in the CCC, the Continental Casualty Company. So really the capital... stat capital in the Life Company is still at very healthy levels.

Jay Cohen
Merrill Lynch

Okay. And then last question if you don't mind. On the Life side, given that it isn't run-off and obviously give some credit risk in there, any thought about just selling that business as a run off entity and not having the deal with any other risk?

D. Craig Mense

I can't really comment on that Jay.

Jay Cohen
Merrill Lynch

Okay, thanks.

Operator

We take our question from Bob Glasspiegel with Langen McAlenney.

Robert Glasspiegel
Langen McAlenney

Good morning. Just trying to tie all this together, I mean you're short of cutting the dividend and delayed raising dilutive capital, just sort of sending a discouraging sign to the capital markets. But the spin on it is we're raising this to be proactive for opportunities. But Jim Lewis's commentary seems grumpy and sober.

I guess I was hoping that you might be a little bit more positive about where the current environment is to justify raising this dilutive capital if it is offensive. Jim, I mean, can you give me a little bit of confidence that you look more optimistic or where are you seeing pockets of the opportunity today, where this offensive capital can be used?

James R. Lewis

Yes.As you look at our overall premium volume, you can see that our net written premium actually has improved in the third quarter. And I think a lot of that has to do with the traction that we are now driven in our Standard Lines portfolio. In some of the places there I have indicated earlier, that we have sub-segment, our middle market book. And we're now starting to see traction there. We've made investments in some of our specialized businesses that I've talked earlier such as boiler and machinery are excess and surplus finds our in marine part of our portfolio.

Our Specialty portfolio is still performing extremely well. And, quite frankly, as I look at this market rate now, our overall rate levels seem to have leveled out. At least, they are continuing to drop any further and they've been in the minus 3% to minus 5% level. For the quarter, they were down minus 4 overall for P&C compared to minus 5 in the previous period.

Our book of business is more signatory to small to middle market part of the book itself. We're not much of a player in the large lines, but quite frankly we still have market pressures and there is still is competition from the market standpoint.

I do think there is the potential for our reach to harden, especially as you look at lower investment income, the fact that there are higher loss ratios and you are not able to really cover overall loss costs. But there is a higher cost of capital today. And there is actually a reduced level of excess capital. I think over time, all of those will have some variant to-date, we really haven't seen that. And so I can't count on that. So, when you talk about my comments being sober, I'm just being realistic that this is the marketplace that we are in right now. I am assuming that marketplace is going to be one we're going to continue with and we're doing all the appropriate things with portfolio optimization, sub-segment and in segment in our portfolio using data driven decision making within the portfolio, all with the intense position that the current market is. If it changes, then we'll be in a very strong position to take advantage of the market.

Stephen W. Lilienthal

Yes Bob, this is Steve. I beg if I could add to Jim's comments. I mean, we have always taken a rather conservative and cautious approach to the market. And we've not seen anything yet that would have caused a compelling change in the insurance marketplace, absent everything is going on the financial, the economic side.

But no carrier has started to jettison business. As we commented earlier in the call, there is no real new source of growth that's out there. So, the game continues to be one of displacement. I think some of the events of the quarter have caused rates to firm at the level that they're at right now. But, there is nothing that has fundamentally changed that has caused any carrier to move up aggressively and their prices with any success.

And that being said, we constantly give instructions to our underwriters across both Standard and Special Lines to test the market, so we're constantly looking at opportunities to raise prices and then we kind look at retention. We've hope to win the new business marketplace, to see if the spreads between new business and renewal pricing is starting to close. That doesn't seem to have happened yet. So, we still remained very... we remained hopeful, but we remained conservative in terms of how we actually operate the business.

Robert Glasspiegel
Langen McAlenney

Some of your competitors have de-risked the portfolio. I assume that's not where you guys have been coming from. I know last quarter you were dipping in a little bit some riskier assets carefully. It's... where does de-risking the portfolio stand, and finally to what extent was Tom involved in the capital decisions?

Stephen W. Lilienthal

Let me take the last one first one first, Tom Motamed was not involved in any decision-making or had any input on the capital decision, or any other discussion that taken place with anything going on at CNA. He was prohibited very, very clearly, and we understood that very, very clearly, when we hired him last May.

The approach to Chubb in mid-to-late October was something that we had thought about all along just to see if we can shorten up the transitional period from 12 months down to seven. And also shorten up or avoid the possibility of any organizational loss of focus, given the length of the transition.

So, he had no input whatsoever, and he will not be involved in decision making or strategic direction until he assumes his position as Chairman and CEO in January. So that's the first one. Now, with respect to de-risking of the portfolio, you're talking about the P&C insurance portfolio, or the investment portfolio?

Robert Glasspiegel
Langen McAlenney

Both, yes.

Stephen W. Lilienthal

How long you have? You want to talk about the insurance portfolio, first or you want to talk investments?

Robert Glasspiegel
Langen McAlenney

Well, let's go the investments.

D. Craig Mense

Okay. This is Craig, Bob. Maybe first to come back to another comment you made about the preferred, it's not dilutive. There are no warrants with it, okay. By the way, there is no call premium.

Robert Glasspiegel
Langen McAlenney

Will you be able to get more than 10% with money?

D. Craig Mense

There is no embedded options that are common in today's market, the things in today's market.

Robert Glasspiegel
Langen McAlenney

Should you be able invest it as higher than 10% rate?

D. Craig Mense

No, I didn't say that.

Robert Glasspiegel
Langen McAlenney

It's dilutive then right? So there would be earnings.

D. Craig Mense

But remember also that we have... we'll take those dollars as well as the 2.5 billion of other cash that we're generating that we do have available to us, and available to us to invest in today's attractive rates. Now, relative to de-risking the portfolio, I'd remind you that we've always maintained very high liquidity in the portfolio. So, over 92% of our assets are either in cash short-term or public debt... public bonds. And 89% of that is investment grade.

We've made very little change over the course of this quarter in terms of asset allocations, maybe a slight tickup in governments and a slight tickup immunity, so not much different than that. We have not been a net buyer of sub-prime like we were last quarter, although, I'd tell you that those things... those investments are using have played out very well for us so far.

Stephen W. Lilienthal

Again Bob, just to add on the insurance portfolio, I mean, we did that several years ago. And I think we've talked about that at length. And I'll ask Jim Lewis if you want to add anything further my comments. But, if you recall, we did a major shift in the workers comp portfolio, which took it down by about 40% and shifted the penetration in the states that we're in. We virtually added large cap, our cat new market, and shifted that on Specialty Lines, we shifted out a lot of the large cap Specialty Lines also.

We took down a tremendous amount of our closure exposure. We have managed limits rather aggressively over the past several years so that we're less... we are not at all dependent on reinsurance. We are less... much, much less dependent on reinsurance than we were before.

And I think... and we also have managed terms on these policies. So, we didn't... we had limited severely the number of multiyear policies that we were involved with. Now, that's in addition to the controls and the monitoring that we put in place across the organization. Now, Jim if you want to add anything else?

James R. Lewis

The only thing I'd add is on the word comp order, work comp used to be well in excess of 20 plus percent of our portfolio. Now, closer to the 25%, it's now down to 12%. So, that's an area that we aggressively attacked when we got here. And we now have at remains the level that we're very comfortable with.

Stephen W. Lilienthal

I think Bob that's also one of the reasons why we feel, we can exploit some of the opportunities that we present ourselves, because we are not overloaded in a lot of these areas. So, yes we can kind of cautiously find ourselves exploring the large property market. A companion to that is the boiler market and as well in the marine market. And we already have in excess of surplus lines operation that we are looking to expand.

So, I think the fact that we have devitalized the property casualty portfolio some time ago allows us to kind of move around a little bit and take eight pieces as we feel appropriate against our risk tolerance on a going forward basis. So, yes. That's on the investment side and on the PC side.

Robert Glasspiegel
Langen McAlenney

Thank you Steve for answer. I encourage you again to consider that your November analysts meeting to give some color on value-added long-term investment numbers.

Stephen W. Lilienthal

Okay. Thank you, Bob.

Operator

We'll take our next question from Matt Carletti with Fox-Pitt Kelton.

Matthew Carletti
Fox-Pitt Kelton

Hey, good morning. Thanks for taking my question. Two questions actually; first is on the capital raise, has AM best commented on how to treat that equity versus debt. And the second is that you mentioned the kind of unrealized movements in the quarter end of the last 10 days were the hardest hit. How is that booked if you provide some color since 9/30, I guess October, months till date?

D. Craig Mense

This is Craig again. So all... we've heard from all of the agencies and I think they we'll all be commenting independently. So you can see it. There is a comment from Moody's already out, where they are affirming their financial ratings and they are affirming the outlook as stable. So, I would refer you to their press releases which I expect to be forthcoming over the course of today and tomorrow about all those things.

As far as the changes on realized since the end of the quarter, I mean you all know what's going on in the market. And I think if you also are very well aware of the composition of our portfolio. So, given your knowledge of our portfolio composition I think you can expect that it's moved inline with market conditions, although I would tell you that the last week was certainly better than the first three weeks of the month.

Matthew Carletti
Fox-Pitt Kelton

Okay. And just on the rating agencies, I mean I understand the kind of the reiterating the outlooks, thinking well on the lines of just... earlier this year your idea of how they're going to treat it in terms of debt versus equity credit given the structure of the product?

D. Craig Mense

Well, we are, I mean we believe... we'll be treating it as equity on our financial statements. I think that Moody's has announced that they are treating at its more debt like than equity like. And I don't know if we were looking to answer, we end up we heard from AM Best. AM Best is treating it to be 80% equity.

Matthew Carletti
Fox-Pitt Kelton

Alright, thanks a lot.

Operator

[Operator Instructions]. We'll take our next question from Ray Wicklander with Friedman's Global Investments [ph].

Unidentified Analyst

Hi. This week 25 RBC ratio was that for CCC or was that consolidated number?

D. Craig Mense

That's CCC.

Unidentified Analyst

Okay. And that's 375 after?

D. Craig Mense

Yes.

Unidentified Analyst

Okay. So, for your level of rating I guess 325 you can see so pretty high. So, how much is the rating agencies the anxiety was caused by the OCI... the AOCI I should say?

Stephen W. Lilienthal

Well, maybe we're not exactly sure what you're driving at there but if I could just remind that we developed and presented this plan to rating agencies without any instigation or provocation from them, I mean this was our feeling as to the best way to approach the conditions that we're presenting themselves in the market place to us. And as Craig said earlier to make sure that there was no level of uncertainty regarding the financial strength of CNA and also to position us to deal with the opportunities that we felt would present themselves going forward. So, I'm hoping that answers your question.

Unidentified Analyst

Yes, its does. But we to see a moving targets from the rating agencies and for couple of other companies where OCI seems to be much more important now. But, alright that's fine. And then the second question I think you alluded to a bit, were you purchasers of sub-prime or Alt-A in the quarter?

Stephen W. Lilienthal

No. We're not.

Unidentified Analyst

Okay, alright. Thanks guys.

Operator

We'll take our next question from Ron Bobbin with Capital Returns.

Ron Bobbin
Capital Returns

Hi, thanks and good morning. The... I think the press release talks about preferred rate being reset, I understand the fifth anniversary. I want to know what are the terms that drive the rate being resets and also the investments from Lowe's, is it coming in the form of cash. Thanks.

Stephen W. Lilienthal

We're having a little bit of hard time hearing you, it wasn't very really clear. Do you mind repeating your question?

Ron Bobbin
Capital Returns

Sure. I thought, I read in the press release with respect to the Lowe's preferred purchase that the rate on the preferred stock starts at 10%. But I think that after five years that the rates gets reset?

Stephen W. Lilienthal

That's correct.

Ron Bobbin
Capital Returns

And I wanted to know what are terms of the reset, what is it... is it some floating number over an index is the adjustment factor determining can tell us where it is? And then the second part of my question $3 billion purchase of preferred, are they paying cash in effect or using some other form of payments?

Stephen W. Lilienthal

As far as the reset, so it is reset after five years in its 700 basis points over the 10 year treasury. Those meant to be a market risk adjustment but there is a 10% for on the preferred dividend.

Ron Bobbin
Capital Returns

And that's the one and only reset date from thereon it's perpetual that have really over that point?

Stephen W. Lilienthal

No, it's every five. It would be reset every five years.

Ron Bobbin
Capital Returns

Thanks. And how about the form of payments?

Stephen W. Lilienthal

Cash.

Ron Bobbin
Capital Returns

Okay. Thanks a lot, best of luck.

Stephen W. Lilienthal

Thank you.

Operator

We have a follow-up question from Jay Cohen with Merrill Lynch.

Jay Cohen
Merrill Lynch

Actually my question was answered. Thank you.

Operator

[Operator Instructions]. And we have no additional questions at this time. I'll like to turn the call back over to our speakers for any closing remarks.

Nancy M. Bufalino

Thank you, Patrick and thank you all for joining us today. Once again, I call your attention to disclosures concerning forward-looking statements and non-GAAP measure. I'd also like to remind everyone that CNA's senior management will be speaking at the Lowe's investor meeting in the morning of Wednesday, November 5th at the Peer Hotel in New York City.

If you're interested in attending, please contact CNA or Lowe, so we can send you the registration information. A take replay of today's conference call will be available for one week immediately following this call until November 3rd. Please view the earnings release for details and thank you all for your participation today.

Operator
This concludes today's conference. We thank everyone for there participation. You may now disconnect your lines. .