S&P Global
Market Intelligence

The Allstate Corporation NYSE:ALL

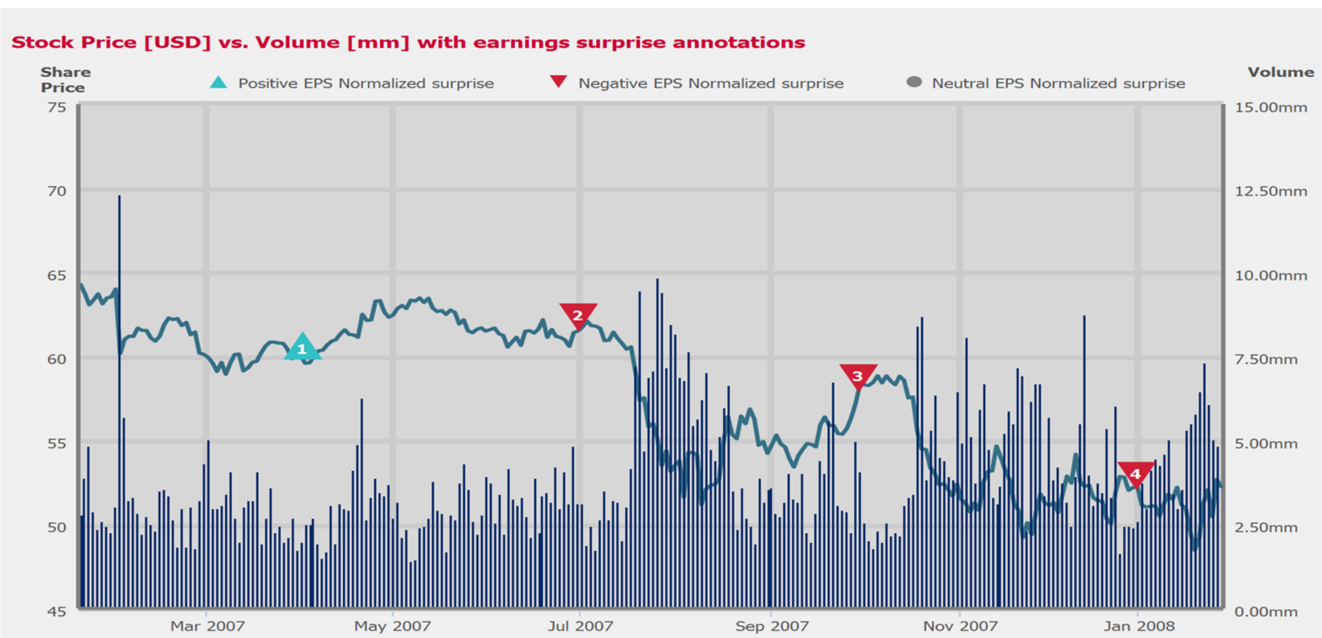
FQ1 2008 Earnings Call Transcripts

Thursday, April 24, 2008 1:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2008-			-FQ2 2008-	-FY 2008-	-FY 2009-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.62	1.33	(17.90 %)	1.53	5.95	6.06
Revenue	-	-	0.26	-	-	-
Revenue (mm)	6746.63	6764.00	-	6822.02	27241.59	27603.77

Currency: USD
Consensus as of Apr-24-2008 1:30 PM GMT



	- EPS NORMALIZED -		
	CONSENSUS	ACTUAL	SURPRISE
FQ1 2007	1.86	1.93	1 3.76 %
FQ2 2007	1.80	1.76	2 (2.22 %)
FQ3 2007	1.70	1.54	3 (9.41 %)
FQ4 2007	1.32	1.28	4 (3.03 %)

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Call Participants

EXECUTIVES

Eric A. Simonson

George E. Ruebenson

James E. Hohmann

Robert Block

Samuel H. Pilch

Thomas J. Wilson

ANALYSTS

Brian Meredith
UBS

Charles Gates
Credit Suisse

David Lewis
Raymond James & Associates

David Small
Bear Stearns & Co.

Gary Ransom
Fox-Pitt Kelton

Jay Cohen
Merrill Lynch & Company

Jay Gelb
Lehman Brothers

Joshua Shanker
Citigroup

Matthew Heimermann
J.P. Morgan

Michael Phillips
Stifel Nicolaus & Company, Inc.

Paul Newsome
Sandler O'Neill & Partners

Robert Glasspiegel
Langen McAlenney

Unidentified Analyst

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Allstate Corporation First Quarter 2008 Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will be given that time. [Operator Instructions]. As a reminder, this conference call is being recorded.

I would now like to introduce to your host for today's conference Mr. Robert Block, Vice President of Investor Relation. Sir, you may begin.

Robert Block

Thank you. Good morning everyone and welcome to Allstate's first quarter earnings conference call. Joining me today are Tom Wilson and Sam Pilch, who will share their comments on the quarter. Jim Hohmann, Head of Allstate Financial; George Ruebenson, Head of Allstate Protection; and Rick Simonson, Head of Allstate Investments are also hear and would be available for questions following the prepared remarks.

During the Q&A session we ask that you limit yourself to one question and one follow-up so that we can get to as many inquiries as possible in the time available. We know that there is another call immediately following ours, so we will finish this call on time.

Note that the following discussion may contain forward-looking statements regarding Allstate and its operations. Actual results may differ materially. For information on factors that could cause such differences refer to our 2007 Form 10-K and yesterday's press release. We may discuss some non-GAAP measures for which you will find reconciliations in the press release, in investor's supplements on allstate.com.

This call is being recorded and your participation will constitute consent to any recording, publication, webcast, or broadcast of your name, voice and comments by Allstate. If you do not agree with these terms, please disconnect now. A replay will be available shortly following the conclusion of the call. Our remarks are current only as the time and date of the call. And finally, Investor Relations will be available to handle any further inquiries you may have after we have concluded this call.

We'll begin now with comments from Tom Wilson. Tom?

Thomas J. Wilson

Good morning. Thank you for joining us. We had two significant challenges in the first quarter; catastrophes and weak investment markets, both of which we overcame as a result of our strategy. You remember our strategy is to reinvent protection or retirement for the consumer, and there are four operating priorities that support that goal; operational excellence, consumer focus, enterprise risk of return, and capital management.

So here are key takeaways from the quarter. Operating income declined to $747 million, a $450 million decline, as we experienced one of the worst first quarters ever catastrophe loses. A large part of that was caused by tornados as a number of which was about double what is normal.

Our focus on operational excellence, however, generated an underlying combined ratio of 85.8% better than the full year expectations we said at the beginning of the year. That resulted from declining frequencies and our disciplined pricing philosophy of not chasing growth with price reductions, and that was of course partially offset by a rise in current year severities. Our consumer focus is what enables us to avoid price reductions as a primary driver of our strategy.

Allstate standard auto unit volumes continue to be relatively flat, although, net written premium is up slightly. We also continued to have success with the Your Choice Auto. Allstate Blue is contributing to growth in non-standard auto in the new business written premiums. Encompass auto premium which is of course our independent agency offering is starting to see a real growth due to the introduction of Encompass Edge. We're also starting to see some growth in our redesigned emerging lines... emerging business lines, although that's not likely to offset reductions in our commercial business.

Our focus on enterprise risk and return enable us to avoid large losses due to concentrations in any one asset class. Our diversified high-quality portfolio was negatively impacted by turmoil in the credit markets; however, as we took $655 million of pre-tax realized capital loses in the quarter. As a result, net income declined to $348 million.

Impairment write-downs in the investment portfolio in losses due to settlement in evaluation and derivatives were the primary driver of those losses. And majority of the impairments relate to securities that are performing in line with anticipated or contractual cash flows. Sam will cover both of these in more detail.

Lastly, we remain a financially strong well-capitalized company. During the quarter we increased our dividend for the fourteenth year in a row. We completed our $4 billion share repurchase program initiated another $2 billion program. Our strategy continues to serve us well and what has been a challenging quarter. The underlying business remained stronger, and we expect to do well in the future.

Now Bob and Sam will give you a deeper look at the numbers before we go to Q&A.

Robert Block

Thanks, Tom. Because we provide you with an enormous amount of financial... detailed financial information, I plan on hitting the highlights of property liability, underwriting income trends and Allstate Financial results.

In property liability our top line remained relatively flat, a trend that we have seen over the last several quarters. We continue to see positive growth in Allstate brand, in standard auto net premium written as the effects of the rates taken in the back half of 2007 more than offset to slowdown in unit growth caused by lower retention and reduced new business sales.

We also experienced favorable results in new business premium for non-standard auto, particularly in the states, where we've introduced Allstate Blue and in Encompass auto where we have introduced Encompass Edge. These favorable results were overshadowed by the declines in our property lines due to primarily to actions aimed at reducing exposure to mega caps.

From an underwriting income perspective, we posted a combined ratio of 94%, an increase from first quarter 2007 of 9.4 points. The majority of that point variance was due to increased catastrophe losses worth about 6 points and reduced favorable prior year reserve re-estimates worth about 1.7 points. As Tom indicated, the underlying rhythm of the business remains very strong with an underlying combined ratio of 85.5%, a level better than our full-year outlook we provided in our last January.

Essentially, combing the decreases in frequency with very modest increases and current year severity, the resulting loss cost trends are well within our pricing assumptions. Thus with pricing actions we took in 2007 and continue to execute in 2008, our margins remained within our expectations.

Specifically in standard auto, bodily injury frequency declined 6.5% from prior year quarter, continuing a trend that goes back for several years. In fact, according to data compiled by the research entity, Insurance Research Council, BI frequency for the industry has declined each year since 1995. This trend is something to keep in mind when evaluating injury loss cost trends for auto insurance.

Now back to our quarterly results. The drop in frequency helped offset the rise in BI severity. For the quarter, BI paid severity rose 8.6% from the first quarter 2007, reflecting continued inflationary pressure in medical care and hospital-related charges as well as some operational issues that we have identified in our addressing.

Property damage frequency also fell in the quarter by 2.4%, reversing the trend we saw throughout 2007. Unfortunately, the paid severity for property damage increased a little faster than the 2007 trends, coming in at 4.1%. But again, when you combine the two factors to get the overall loss cost trend, the results remain modest and within pricing assumptions.

Homeowner loss trends excluding catastrophe losses also showed a significant moderation from prior trends with frequency and paid severity increasing 1.5% and 3.1% respectively from the first quarter 2007.

Turning to Allstate Financial, we saw an increase in premiums and deposits of 15.9% from the prior year quarter, primarily due to a $460 million increase in the issuance of institutional products. We also experienced modest increases in our life products and deferred fixed annuities. Allstate Financial products sold through the Allstate Agency system grew 6% during this quarter compared to last year's first quarter.

Later this quarter, in the second quarter, we will be introducing a new suite of products as part of our strategy to reinvent retirement for the consumer. From an operating income perspective, Allstate Financial results were $13 million less than the first quarter 2007 at $143 million. Lower investments spread and slightly increased operating expenses were the primary causes of the decline.

The decline in investment spreads were from lower investment income results driven by reduced asset balances as a result of dividends paid in 2007, increased short-term balances to provide additional liquidity during this period of disruptive capital markets, and lower investment yields. Allstate Financial continues to focus on improving returns while developing new and innovative products for the consumer.

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

Samuel H. Pilch

Thank you, Bob. I'd like to begin with a brief summary of our catastrophe losses and the prior year reserve re-estimates. After that I'll spend most of time reviewing our investments.

For the quarter catastrophes totaled $568 million or about 8.4% of our earned premium. And that was $407 million or 3.5 times more than for the first quarter of 2007. We experienced 27 cats in 2008 compared to 18 in 2007. This increase was primarily related to severe winter weather experienced across the country, in part due to unusually high tornado activity.

Included in those quarter cat loses was $117 million of prior year reserve strengthening related to litigation in the Louisiana for hurricane Katrina. As you may recall the deadline for filing litigation in Louisiana was August of 2007. Including the $117 million related to prior year catastrophes, total property liability reserve re-estimates for the quarter amounted to $101 million strengthening of reserves. That compared with a favorable prior year reserve re-estimate in the first quarter of 2007 of $129 million or for an unfavorable change of $230 million.

Turning to our investment performance, initially I described our investment strategies. We follow long-term investment strategies that differ for profit liability in Allstate Financial. The proper liability we focus on after-tax returns, which has led to a higher level of municipal bonds. We are also concerning the liquidity needs related to catastrophes and claim settlements, which has led to holdings of equity securities and public debt including corporate bonds.

In Allstate Financial, we follow asset liability management focused on the need for risk adjusted spreads, leading to a selection of assets that performed favorably on a long-term basis. The portfolios are broadly diversified, which enables us to avoid losses from concentrations. With the diversity of our investments, when you have a broad-based market decline, there is a possibility of more with smaller losses being incurred.

We carry most of our investments at fair value but not our liabilities. As a result, the volatility experienced in unrealized gains and losses on investments is not offset with corresponding changes in the fair value of the liabilities.

Next, I'll review the investment portfolio position. As of the end of the first quarter, our investment portfolios totaled $115 billion, which was 3% less than the end of 2007. The decline was primarily related to a reduction in our net unrealized capital gain loss position, realized capital losses, and slight decline in Allstate Financial contract-holder funds and collateral received in securities lending and derivatives.

The unrealized position occasionally has large quarterly changes, which are relatively small as a percentage of the total portfolio, but large anomaly. For example, the largest quarterly decline in the most recent five years was $3.4 billion or 3% of investments in the second quarter of 2004, and the largest increase is $2.3 billion or 2% of the investments in the third quarter of 2006. This quarter our unrealized position declined by $2.5 billion or 2%.

Now to go through the make up, our net unrealized capital gain and loss position at March 31 was a net unrealized capital loss of approximately $600 million compared to a net unrealized capital gain of approximately $1.9 billion at the end of the year or a decline of $2.5 billion.

The change was primarily due to a decline of unrealized capital gains on investment grade, fixed income securities of approximately $1.9 billion. As yields used to determine fair values increased resulting from widening credit spreads that more than offset the effects of decline risk free interest rates.

Additionally, approximately $600 million reduction in unrealized gains and equities securities occurred. $200 million of the unrealized gains was a result of sales of equity securities during the quarter. The change in the fixed income unrealized capital gain position was primarily attributable to lower fair values on our asset backed and commercial backed holdings.

As I mentioned before, valuation movement of our assets does not result in accounting recognition of the valuation movement of our liabilities, but this is occurring economically.

The next area I'll cover on investments is our net investment income, our realized capital gains and loss results. Net investment income declined 2.9% compared to the first quarter of last year. Moreover net investment income for both businesses was driven by lower portfolio yields and lower average balances. Income from limited partnerships was higher for Allstate Financial and lower for property liability.

Net realized capital loses for the quarter was $655 million on a pre-tax basis and included $60 million of net gains related to dispositions, $415 million losses from write-downs and $300 million of net losses due to derivative changes, and evaluation settlements in the quarter.

Impairment write-downs totaled $347 million for fixed income securities, primarily related to residential mortgages and other structured securities, and $52 million for equity securities. Approximately 70% of the fixed income write-downs relate to securities that are currently performing in line with anticipated or contractual cash flows, which were written down primarily because of expected deterioration in the performance of the underlying collateral. The remaining 30% are primarily related to securities currently experiencing a significant departure from anticipated residual cash flows.

The net $300 million realized capital loss from derivative instruments for the quarter comprised $103 million for the risk reduction programs that we have and $162 million for the valuation of embedded equity options and fixed income securities. Losses from the risk reduction programs, primarily in our duration management programs were related to changing interest rates and credit spreads as rates declined during the period.

Next some background on how we determine the losses on embedded derivatives. In our portfolio we are invested in convertibles and equity linked notes. We develop fair value for these securities in total. However derivative accounting requires us to separately value the embedded options and to report the change in value in realized capital gains and losses.

The difference between the total fair value changes and the change determined for the embedded options is the change in the value of the host which is reported as unrealized capital gains and losses.

At March 31, our securities with embedded options totaled $2.1 billion and decreased in fair value by $132 million comprising a realized capital loss of $162 million and an unrealized capital gain reported other comprehensive income of $28 million.

Total fair value exceeded total book value by $52 million at March 31. Valuation gains and losses are converted to cash with securities with embedded option upon our election to sell these securities. In the event that the economic value of the options us not realized we will recover the part of value if held to maturity. Total fair value exceeded par value by $84 million, while we were in a gain position as of March 31.

Now I'll wrap up my discussion with a few additional comments on capital management actions and related balance sheet metrics on our combined ratio outlook. In the area of capital management actions, during the quarter, we completed our $4 billion repurchase program that began in November 2006 and commenced a $2 billion share repurchase program that is expected to be completed by March 31, 2009.

Our book value at the end of the first quarter was $36.45 per share comparable to $36.54 per share reported in the first quarter of the previous year. Excluding unrealized net gains and fixed income securities, book value increased by $2.44 or 7%.

Finally, we expect our property liability combined ratio excluding the effect of catastrophes and prior year reserved estimates will be within the range of 87 to 89 for the full year 2008.

Frequency was better than expected in the first quarter. We will continue to monitor trends, and if appropriate, we will revisit our outlook. We believe that the continued strong underwriting performance at this level should translate into a stock price performance within our historical valuation range.

Through our earnings release and other reports, we continue to strive for greater transparency of our results. I hope our efforts meet your expectations and needs.

I'm turning back to Tom.

Thomas J. Wilson

Matt, I think we are ready to start the Q&A session.
Question And Answer

Question and Answer

Operator

Thank you, sir. [Operator Instructions]. Our first question is from David Lewis of Raymond James. Your question please.

David Lewis
Raymond James & Associates

Thank you and good morning. Reflecting a high level of catastrophe losses over the past several quarters, has Allstate considered buying more reinsurance to reduce that quarterly earnings volatility, particularly in light of the reduced reinsurance costs? And I believe in the fourth quarter you indicated that reinsurance costs would likely decline from $900 million in '07 to roughly $660 million in '08? Then I have a follow-up.

Thomas J. Wilson

David, thank you. Good morning. We have... as you know, we substantially raised our reinsurance program over the last three or four years, so we are now probably one of the largest buyers of reinsurance in the country. That reinsurance has really been focused on mega catastrophes. So, if you go around and look at our programs, it really goes from the northeast all the way around through up to Texas, everywhere on the coast. We have programs in place for, just for individual states or groups of states at lower levels and then we of course have our $2 billion over $2 billion program, which is if catastrophe losses in total exceed $2 billion after reinsurance, we have another $2 billion to cover.

The cat losses that we have been seeing in the last couple of quarters have really been what... tornadoes, hail storms, some of which is due to inclement weather, which looks out of pattern. But we haven't yet moved to the place where we think we need to by reinsurance to ship that part away from the company. We... those... we get decent price increases on those and we can take care of our customers pretty well with them. So, that has not been part of our program. And right, now we're not thinking about buying reinsurance at lower levels to take the quarterly earnings volatility.

David Lewis
Raymond James & Associates

Tom, just to follow-up, we are kind of hearing that auto pricing trends are probably more on the rise than in decline on a state-by-state basis. Can you tell us kind of where you are seeing your rate activity versus competitors?

Thomas J. Wilson

Sure. Maybe we'll get George to take that one.

George E. Ruebenson

Basically, as we said in the press release, we have taken auto rate increases in the first quarter in 12 states for an average of 4.5%, in property, about twice that rate and in about nine different states. What we have noticed over the last three quarters is that instead of taking rate decreases, many of our competitors are now being more aggressive on taking rate increases. As you saw from their results of the end of '07, their combined ratios are materially higher on average than ours. And in the first quarter, they continued that by taking more rate increases than decreases. We'd like the fact that our combined ratios are in good range. We are going to continue to monitor them. We'll take rate increases where necessary, but we do think our competitors will probably have to take more increases than we will.

David Lewis
Raymond James & Associates

Thank you very much.

Operator

Our next question is from Charles Gates of Credit Suisse. Your question please.

Charles Gates
Credit Suisse

Hi, good morning. My first question, to what extent do you believe that the favorable frequency trend, a function of sharply higher gas prices, as well as the fact that what 11% of this rise in unemployment in the United States are probably your insureds?

Thomas J. Wilson

Good morning, Charlie. I would say we were happy that the trend on frequency turned negative after last year where it bumped up and everybody was worried about it being a long-term trend. Reversal from what we have had over the last 20 years, I think it is probably too early to call. I mean I think there was a good question; those are clearly drivers of frequency, both gas prices and unemployment, we think, do impact a number of miles driven. But it is a little too hard to tell for just one quarter.

Charles Gates
Credit Suisse

Okay. My second or my follow-up question, on page two of your news release, you talk about something called ballpark estimating tool in how this integrates the various distribution channels. What does that mean?

Thomas J. Wilson

Well, let me step back first and give you slightly... start with our consumer focus. What is it we are trying to do, trying to meet customers' needs. In my words, I would like to say eliminate the human motive, which is where you call us, you give us data, we listen to it, it goes through our brains into our fingertips, and we tap it into computer, and you don't need to pay us to do that. That's not high value added. So, what we have been doing is trying to find ways to eliminate that and be... and have the conversation really be about what kind of protection do you need? Talk about value, so it's not all about price. Those people who are human modems and only sell on price won't have value... won't provide value to customers on long-term basis. So, we are trying to shift it. That's why we have products like Your Choice Auto so you can actually talk about what kind of coverage and features do you want, what kind of risk profile are you.

The ballpark estimating tool is a way that we use. We can pre-populate our computers with data that we buy as opposed to making you give it to us. And then we kind of... we can verify it as opposed to input it directly. When we say integrate it with all the channels, what we find is when we tend... a lot of people look at this business and try to say, well, you have got direct and then you have agencies and this. We sell a lot of business direct. We just happen to sell it out of 13,000 local offices, who happen to be there in case someone needs them or they can have a personal relationship. But not everybody who buys from us walks into the office, obviously. A lot of them buy direct over the phone.

So, we tend to look at it and say, how do you serve your customers? Well, so, a number of people come to us on the web. We use that ballpark estimating tool. And a greater than majority of those people will end up in our local agencies buying business. So that's what we mean by integrating. So, they come into the allstate.com website. They do the quick two and a half minute quote, boom, all of a sudden, they end up with an agency as opposing to having to buy it over the web.

Charles Gates
Credit Suisse

Thank you.

Operator

Our next question is from Bob Glasspiegel of Langen McAlenney. Your question please.

Robert Glasspiegel
Langen McAlenney

Good morning and I apologize in advance for this question. But given that you are the first PC company to provide expanded disclosure of FAS 157, I'm going to need some education. Specifically, the level 3 assets where you are valuing using internal models and broker calls at $22.7 billion, is large relative to your capital base. How do you handle the situation in today's world where markets... models are saying one thing and markets are saying things that seem to be quite in conflict with the what internal models are. How do you resolve those conflicts in an environment where there are no markets?

Thomas J. Wilson

Hey Bob, maybe you could just give me a little more clarification. What do you mean? What's the conflict that you are poking at?

Robert Glasspiegel
Langen McAlenney

Well, some of the companies like AIG, and Citigroup, that we are using mark to model on some of these complex securities. When they made a transition to mark to market, there was a pretty big hit to the book value. And they were publicly saying that the market... before they made the change, that the markets really weren't reflecting what their internal models would suggest. So, I think over the last few years, there has been a divergence in the sort of level 1 assets the companies that had been ahead at adopting sort of disentanglement [ph] of what the models would suggest and what the markets would say.

Thomas J. Wilson

Let me make a general comment, and maybe Sam can walk you through what we have in level 3. First as always, Bob, you are thoughtful and ahead of the game. I did read your piece some early hour this morning. I would not automatically say that level 3 assets are low quality.

Robert Glasspiegel
Langen McAlenney

Right.

Thomas J. Wilson

Level 3 are different valuation methods, not necessarily low quality. So, I'm not sure that the comparison of what you have in level 3 to capital levels is the right way to look at that. Clearly, you want to make sure that people have the stuff valued and that's what that accounting standard is for. But I don't think it necessarily implies that because they are hard to value, they are low quality. I think our stuff we have in level 3... I can't speak for everybody else, but the stuff we have in level 3 is stuff we have been in for a long time, we have great experience in, and maybe Sam, you can just go through the three sort of main categories of that. And then if you have any follow-up, Rick is here if you want to talk about any of the categories of our skills and the type of stuff we invest in.

Samuel H. Pilch

Thank you, Tom. I can't really comment too much about AIG. But you may recall, what you were citing is the reporting at year end, and with respect to that, they had not yet adopted FAS 157. So, that wasn't yet to be an influence.

Robert Glasspiegel
Langen McAlenney

I understand, yes

Samuel H. Pilch

With respect to it, they do have a different investment strategy than we have. They were heavily engaged in CDOs. With respect to the components of level 3, just as Tom said, first off, we didn't change assets going from the end of the year to the current quarter. We followed mostly of the same valuation practices that we have historically. We had introduced categories. In the final level 3, it really appears a blend of each of the types of valuation techniques that we follow. There are some assets that have been valued by our servicers and they provided objective information with respect to it on the market. And we used that information in valuing those securities and we put them into level 3 because of the deep discounts that have occurred in the marketplace.

There are also other assets that have been priced by brokers and it is a non-binding quote and we placed those into level 3 as well. And finally, the largest category, which is the private placements, which there isn't sources externally, we priced those using models. And we are using expected cash flows and we have a lot of knowledge, experience with these because many of these we have held for a long time and they're a discounted evaluation approach.

Robert Glasspiegel
Langen McAlenney

But you... can I just interrupt, you mentioned private placements is a big... I think it was $12 billion of these assets. Is there some general type of assets that would have been in that category that you just described?

Thomas J. Wilson

Maybe Rick can just tell you what the size of portfolio types average of that.

Robert Glasspiegel
Langen McAlenney

Yes, that would be great.

Samuel H. Pilch

One common characteristic is that they do not have ratings by rating organizations. Whereas some of the ones... the ones in level 2 private placement do have ratings and they could be values, based off of those ratings. The ones in level 3 don't. That's the one common component.

Eric A. Simonson

Bob, it's Rick Simonson. The private placement model that we use is a model that is very, very similar to models that have been used by life insurance companies for the last 30 years. They are expected cash flow models, that we apply discount rates. We look for comparables. We look for industry sector comparables and develop an algorithm that produces a valuation. This is nothing new. The credits in the private placement portfolio are a cross section of corporate America, industry sectors. And it's the least sort of troublesome or problematic or difficult, for that matter, to value... not difficult to value.

The other stuff that Sam referred to that we either are dependent on independent pricing sources or more challenging, often times, are the broker quotes. That is where we spend disproportionate amounts of our valuation time at the end of every month.

Robert Glasspiegel
Langen McAlenney

Every type of [ph] investment private placements

Eric A. Simonson

For private placement? Yes, $20 million to $25 million is the average size of each fixed income private placement. The credit quality is a BBB plus to low A weighted average quality.

Thomas J. Wilson

Is that helpful Bob?

Robert Glasspiegel
Langen McAlenney

Very helpful. Appreciate it.

Thomas J. Wilson

Okay.

Operator

Our next question is from Jay Gelb of Lehman Brothers. Your question please.

Jay Gelb
Lehman Brothers

Thanks and good morning. I want to touch base on some of the credit related issues. Can you give us a sense whether you've had any rating agency feedback on the impact from the unrealized and realized investment losses and whether you may thank that could slow the pace of the share buybacks?

Thomas J. Wilson

Sam might have a specific comment about rating agencies. We had a couple yesterday to talk about the life company. But it's going to have no impact on the share buybacks, Jay. I mean we're well capitalized. We have excess capital. When we put the $2 billion program in place, we had recognized both the increase in the dividends and that the requirements they had on cash flow and thought about the potential for continued deterioration of capital markets. So, we are in good shape.

Jay Gelb
Lehman Brothers

And... I'm sorry. Go ahead.

Samuel H. Pilch

With respect to the rating agencies, they have seen in our industry, both the property liability as well as financial services, a lot of period-to-period changes in valuation. And this particular period was really no different with respect to the unrealized. The realized we did take losses and they will reduce the surplus available, but we have in place sufficient capital at the operating level to cover that.

Jay Gelb
Lehman Brothers

And given, Tom, you mentioned the rating agencies being in on the life company, I don't know if there were any initial thoughts

Thomas J. Wilson

It was just a normally scheduled thing. More the losses that Sam pointed out from a book value show up in the life company, because that's where the liabilities are. Now, we don't mark those liabilities to market the way we do unrealized gains or losses which if we did, would offset a lot as far as that. But it was a normally scheduled thing. I didn't mean to imply that they showed up here because they were nervous about.

Jay Gelb
Lehman Brothers

Okay. And then on the frequency trend, I just want to circle back on that, because we saw with Allstate today the auto frequency improved sequentially, whereas with Travelers, they reported this morning, they said basically not much in the way of improvement. And I believe you referenced an industry study that you said overall was down. So, I am just wondering, is there anything specific about Allstate where you would, that could have driven the sequential improvement in auto frequency?

Thomas J. Wilson

I don't know that I could compare it to Travelers, Jay. Everybody's got their own book of business, both geographically and by risk type. I would say that geographically, George, as we've looked at, it's pretty much everywhere.

George E. Ruebenson

Yes.

Thomas J. Wilson

A wide variety of states have done well on declining frequency, so, but I can't speak for why those were up [ph].

Jay Gelb
Lehman Brothers

Okay, and my final question is

Thomas J. Wilson

Is this a follow-up, Jay, or is

Jay Gelb
Lehman Brothers

Sorry, it's my follow up to my follow up. If there is any commentary you can provide on the Florida situation that would be helpful.

Thomas J. Wilson

We're working hard to try to resolve that situation in Florida.

Jay Gelb
Lehman Brothers

Alright. Thanks very much.

Operator

Our next question is from Josh Shanker of Citi. Your question, please.

Joshua Shanker
Citigroup

Thank you very much. I was wondering... a more numbers question. In the previous disclosures that you gave us from prior quarters, you gave us a very helpful image of the sort of unrealized loss by accounts in a number of asset classes that you haven't given in the most recent disclosure. I'm wondering if we could get that perhaps, a read through on some numbers.

Thomas J. Wilson

Josh, Jay was saying [ph] a little bit more, which are you talking ?

Joshua Shanker
Citigroup

It was on page six in the fourth quarter press release and then on page six of this quarter's, you gave us some of the information but not all. Would you tell us what your mark to market? The numbers I've been looking for, and obviously, you can come back to this. Are your unrealized gains or losses on the corporate securities, MBSs, sovereigns, preferred stocks and derivative securities?

Thomas J. Wilson

Okay. What... maybe, Sam, do you want to spend a minute on the RMBS portfolio. And then Josh, if you have very specific, the other parts, sovereigns of that, maybe Bob, you can follow-up with Bob, is that all right?

Joshua Shanker
Citigroup

That's fine.

Samuel H. Pilch

In the 10-Q will be providing all the details by major asset types. So, they will be in a couple weeks. But with respect to RMBS and some of the other assets that deem to be part of an eloquent market, there has been some movement. We did provide some information in the earnings release. Overall, we hold $4.85 billion of RMBS, ABS, CDOs, Alt-A, commercial real estate CDOs, that's less than 5% of our asset base. The largest piece is RMBS, that's little bit above $3 billion. We have 85% of them are actual AAA or AA rated. The carrying value that we have right now is 79% of the amortized costs. The unrealized loss position on those is $870 million for the quarter moved $370 million.

We'd like to point out we are continuing to receive principal repayments on the RMBS as we noted, $150 million in the quarter. And just as a reminder, last year for the year, we received $946 million. In addition, we also get paid the interest due and some of the other categories we didn't make note of the repayments that were occurring. We did take some write-downs in these areas and they show up as the RMBS $35 million, but we also took a loss on sales. On the ABS CDOs we took a write-down of $60 million. We only have $17 million remaining in the portfolio after... at this time. So it's our maximum remaining exposure, if any. We also took $89 million of write-downs on Alt-A. So those are the largest activities within the portfolio and they showed up in the unrealized as well as the realized area.

Joshua Shanker
Citigroup

I appreciate it. I will send you a small piece, maybe you can fill in some holes that I'm still missing.

Thomas J. Wilson

Okay, just send it to me Josh.

Joshua Shanker
Citigroup

Great. And then the other question is, this is a matter of I guess opinion. Compared to some of the other financials which took major kitchen-sink [ph] quarters in the fourth quarter, obviously, the first quarter here at Allstate seems like a much more severe pairing back than the fourth quarter. I'm wondering to the extent the FASB 157 influenced this, or just in the end, the assets you happened to hold held up much better in the fourth quarter, and this quarter here, there are showing the deterioration.

Samuel H. Pilch

This is Sam. Clearly, it was market driven valuations declined during the quarter throughout, I think that we have seen that in the companies that have reported so far, the banks and brokers. So we are participating [ph] in that trend. With FAS 157 there is a lot more attention on valuation processes and techniques. But the fact of the matter is, by its design, it was not intended to result in a change in valuation, it was intended to be improved disclosure about the securities in the valuation techniques.

Thomas J. Wilson

I can't speak I don't have in front of me a chart of all the write-downs people took in the fourth quarter. But I think I would go back to a comment that both Sam and I made which is, some of those firms had large concentrated positions in single asset classes that, particularly the CDOs that they took big shots on. We hardly owned

Samuel H. Pilch

160 at the beginning.

Thomas J. Wilson

Yes, 160 at the beginning of the process now down to $16 million or $17 million, much to or chagrin [ph]. But the good news is we didn't have large concentrated multi-billion portfolios in those asset classes that took the shot in the fourth quarter. Of course, as you all know, January and February, the contagion spread to many other asset classes reducing liquidity and market prices which is what you see in our portfolio. But again, because we have such a highly diversified portfolio and we always stayed that the upper end of the credit rating scales, it's all manageable for us. We prefer it go up, but it's all manageable.

Joshua Shanker
Citigroup

Well, I look forward to it going up, then

Thomas J. Wilson

Yes, me too.

Joshua Shanker
Citigroup

Just a disclosure.

Thomas J. Wilson

Thank you.

Operator

Our next question is from the Gary Ransom of Fox-Pitt Kelton. Your question please.

Gary Ransom
Fox-Pitt Kelton

Yes, I just had a question about, more on the competitive environment again. Your policies in force actually declined very slightly, yet others are supposedly raising rates. I guess I would have generally thought that the raising of rates might have helped. Raising rates at other competitors might have helped PIF growth. Can you just comment about how your PIF growth relates to the competitive environment in this quarter?

George E. Ruebenson

Yes, Gary, this is George. The rates that we have been seeing that the competitors have been taking have been improving our competitive environment. But the economic climate is very problematic. Car sales are down about 7% and it's just more difficult for us to grow. There is no real unit growth in the industry. We don't have the final numbers in, but last year, I think we did increase our market share a little bit as we did in '06. So, I think it's just more of a factor of the market than anything else. I do think that with continued pressure on combined ratios for our competitors, if we they do take the rates we think they will, it will improve our competitive position, obviously, should help our growth prospects.

Gary Ransom
Fox-Pitt Kelton

Okay. Thank you very much.

Operator

Our next question from Michael Phillips of Stifel Nicolaus. Your question, please.

Michael Phillips
Stifel Nicolaus & Company, Inc.

Hi, thanks. Good morning. Continuing with the operating environment, if I could kind of throw down two state specific questions. I'm curious what you are seeing specifically in New Jersey on the auto side and then, secondly, in California. I guess in retrospect, anything you would have done differently in your dealings with the department there?

Thomas J. Wilson

Well maybe we can talk a little... New Jersey, I think, George is doing very well out there.

George E. Ruebenson

Yes, we are growing and we are making money. Yes. It's been a very good market for us over the last several years.

Michael Phillips
Stifel Nicolaus & Company, Inc.

I guess the question there is, are you seeing the same kind of upward pressure on the rates that you are seeing throughout the rest of the country?

George E. Ruebenson

I'm sorry.

Thomas J. Wilson

In New Jersey?

Michael Phillips
Stifel Nicolaus & Company, Inc.

Yes in New Jersey.

Thomas J. Wilson

In New Jersey, we took rates over a year ago.

George E. Ruebenson

Yes, we did.

Thomas J. Wilson

We haven't taken much in last year. We took rates a year ago. GEICO, you remember GEICO kind of came into the market, what, three years ago.

George E. Ruebenson

Yes, three years ago, right.

Thomas J. Wilson

We held firm, didn't reduce our rates, took some rates up about a year ago and we are capturing a lot of business right there right now. On California, I would just say, we don't like to get into sort of looking in the rear-view mirror about what you would do differently. It is not our intention to end up in disputes with regulators around the country. That said we do have... there are laws and regulations that we and everybody is supposed to abide by. If we think that we need to protect our shareholders and our customers by doing the right thing, we'll do that. We would like to resolve the thing in California as well and just keep moving. We have offered to lower our rates in California. We'd like to do that. But I wouldn't go back in the rear-view mirror in that one.

Michael Phillips
Stifel Nicolaus & Company, Inc.

Okay, fair enough. Thanks very much.

Operator

Our next question is from Brian Meredith of UBS. Your question, please.

Brian Meredith
UBS

Yes. Good morning. Two questions here. The first one, can we talk about some of the severity trends going on in your business? One, have you gotten any more, dug any more into what's going on with respect to the BI severity, and any outlook as far as when that may decline here? And then on the PD severity, it did tick-up. I'm wondering if you're seeing any pressure from auto parts inflation given the rise you have seen in steel prices and plastic prices or could we see that here in future quarters?

Thomas J. Wilson

I will stay away from making any predictions about the direction of future severity trends in either BI or PD. But in BI, again, what we are seeing is inflationary pressures on the medical costs on hospital waiver type charges, earnings if exit [ph] and we are looking at some operational issues that, where we can perhaps work to offset some of the inflationary pressures on the bodily injury. As those are successfully executed, they should show up in the results.

On PD the severity has returned back to a level that it was running similar to in 2006 in a 3% to 4% range. The inflationary factors, oil prices and plastic prices and things of that nature will impact the industry in terms of the repair of cars going forward. But again, the real issue is how does this work in your loss cost trend, how it look and how do you work it into your pricing. So, at this point, when you look at the overall loss cost trend line, it seems to be well within our expectation.

Brian Meredith
UBS

Great. And then second question, I guess would come [ph], can we talk a little bit about potential for M&A activity? Obviously, there was a big transaction yesterday. Any desire to increase your platform domestically in the U.S. or even kind of looking overseas, are there any opportunities potentially to maybe take the Allstate platform and look at overseas?

Thomas J. Wilson

Well, as we have talked about before, we don't comment on specific acquisitions, so thank you for not asking about specifically. I will tell you that we look at just about everything that comes across the table. We always evaluate whether we think first, it will fit strategically, will it help us reinvent protection retirement for the consumer, do we think we could get a good return on it, what kind of operational efficiencies we have? We could clearly afford, and have capital to do acquisitions of the size you are talking about, but haven't seen anything that we think makes sense for us at this point in the property casualty businesses, I assume where you are focused.

Brian Meredith
UBS

Yes.

Thomas J. Wilson

And as I said, if we see something we like, we'll buy it. But to date, we haven't seen anything we like. If you go to general prices, the good news is that the prices are down. The bad news is that our price is down too. So, we always have to evaluate, is this a good use of capital to buy somebody else, expand their strategic platform, which we would like to do, or should we continue to buy back stock which is also attractive for our shareholders. So, we kind of look at it with that... from all those different angles.

Brian Meredith
UBS

Alright. Thank you.

Operator

Our next question is from Matthew Heimermann of J.P. Morgan. Your question, please.

Matthew Heimermann
J.P. Morgan

Hi. Good morning, everyone. Two questions. The first was, just with respect to advertising it seems, and maybe this is a New York centric comment, because that's where I watch TV. But it seems like the advertising message for Allstate as well as State Farm has shifted from kind of a value pitch to will also save you money. And I just was trying to reconcile that versus what seems to be, in some cases, rates stabilizing or increasing?

Thomas J. Wilson

I can't speak for State Farm's advertising. Maybe take you way up for a second and I'll come down quickly to advertising. When you look at consumers and you segment them, you find that about 40% of consumers really want price. About 40% of the people want value and different features and 20% are agnostic. Our target is clearly toward those people who want value. We also, obviously because of our size and scale, get a number of people who want good price and the people who want value also don't want to overpay.

So, price is always a part of the equation, but price is not the sole driver of our value proposition. In fact, ours is about -- if you look at our advertising, it's really more about choice. So, we've banged away, Joan Walker and the team have great advertising which is really around choice, Your Choice Auto which differentiates us in the marketplace has raised consideration.

So, while we might talk about an opportunity to save, whether that be Your Choice Auto gives you some discounts and things going forward, that's not intended to be the core message that we're giving in our advertising, and that's not the way consumers see it. I can't speak which advertisements you have seen. Obviously price is important, but that's not our lead sale. We are not, give me two and a half minutes and I'll save you 15%. We are not in that category.

Matthew Heimermann
J.P. Morgan

Okay. And then the second question is just, the rate increases that you are seeing, and this is for George, the rate increases you are seeing, are these significant enough that they are impacting shopping behavior?

George E. Ruebenson

No. We are still getting a large number of people shopping. I think what is happening is that we are seeing more people who are inclined to shop rather than to buy. But no, our quotes are up considerably. I think part of it has to do with the economy. As things get tighter, people look for different ways to save money. So they are out searching, but I don't really think it's having a big impact.

Matthew Heimermann
J.P. Morgan

Okay. Thank you.

Operator

Our next question is from Jay Cohen of Merrill Lynch. Your question please.

Jay Cohen
Merrill Lynch & Company

Yes. My question related to the newly issued applications which were down almost 14%. I know that number jumps around a lot. But I was wondering if there is anything behind that or is it just related to the comment you made PIF, that the account's not growing. I just think with Your Choice Auto and the marketing platform, that number would probably be going up or not down as much?

George E. Ruebenson

Yes. This is George. Yes, the comments are the same as about PIF. The fact is that the market right now is not growing very much. And I think as the year unfolds, hopefully the economy gets a little better and we'll get more car sales, which is really the engine for our new business sales.

Thomas J. Wilson

Jay, we obviously would like to see them go up too. But I think... what we try to say is, we have a balanced approach. We bang away at advertising. We have good products, we differentiated the products. We have our local agencies and it's just a tougher market today. But we are not going to move off our strategy to discount price to drive that number up, because we think that would be a bad choice.

Jay Cohen
Merrill Lynch & Company

Got it. Thanks.

Operator

Our next question is from David Small of Bear Stearns. Your question please.

David Small
Bear Stearns & Co.

Good morning. Could you just touch on your investment strategy, particularly as it goes to the investments that are behind your fixed annuity business? And also in the quarter, did you... were you buying asset backed RMBS. I was just going through the math here, and kind of if I take out all the unrealized losses, the realized losses, it looks like you might have been buying some of those types of securities in the quarter.

Eric A. Simonson

This is Rick. The strategy, the investment strategy behind Allstate Financial's businesses, including fixed annuities are largely risk-adjusted spread strategies, oriented toward providing good, quality, stable income. To do that, we generally invest in the BBB plus to low A sweet spot. During the first quarter, origination spreads were over 300 basis points to treasuries. This is the first time, many, many years that we have had the chance to put money to work at that kind of economic value. We did not buy during the first quarter, any ABS, RMBS. We did not buy any Alt-A. We did not... certainly didn't buy and CDO paper, and I'd have to look at the numbers to make sure that I'm tracking with you. Maybe we can get back to you on that.

David Small
Bear Stearns & Co.

Okay, great. So your view about the fixed annuity business hasn't changed, given the credit environment.

James E. Hohmann

This is Jim Holman. Thank you for asking. As far as the fixed annuity environment is concerned, fixed annuities are actually up, quite a bit up. I think up about 40% in the marketplace in the first quarter. That said, the market is probably as challenging as it's ever been as it's gotten very, very competitive. Our fixed annuities are up about 7.5% and quite frankly, that's a reflection of our pricing discipline as we are in the marketplace. So, we continue to participate in the marketplace. We like the marketplace, but it's extraordinarily competitive.

David Small
Bear Stearns & Co.

Okay. Thank you.

Operator

Our next question is from Paul Newsome of Sandler O'Neill. Your question please.

Paul Newsome
Sandler O'Neill & Partners

My question was just asked. Thanks.

Thomas J. Wilson

Okay. Thanks Paul.

Operator

Our final question today is from Tony Dilatiana [ph] of John Hancock. Your question.

Unidentified Analyst

Yes. Thank you very much. Just have a question follow-up to the gentleman on the investment side. I'm looking at page 21 on the press release where you talk about your investments. And you got the estimated fair value, and I know you gave some general comment about 79% and I don't know what the carrying value is versus I guess book, I guess versus par. But I guess could you quickly go down those major categories and give us that answer for the categories. And I guess in terms of vintage type disclosure, could you comment on vintage in some of the more esoteric asset classes like the CMBS and the RMBS. And obviously, just a brief comment on the... to other CDOs and other asset-backed securities, what basically are they in? But certainly, the price that you have versus the par value will be an indication of how you marking these things and that would be helpful.

Thomas J. Wilson

I'm sorry. Tony, it sounds like a pretty specific question. I'm going to suggest maybe that we work through a table with you, with Bob. We'd be happy to do that. We obviously... I mean, if your question is really, have you marked it down enough from par so that we have some sense that the values are really there. I think you get a little bit of flavor from what we talked about. We've written off almost all of the CDOs which started to

Unidentified Analyst

But that 79% comment you gave, what was that applying to? Was that to the whole $7.3 billion? Was it just a particular thing?

Thomas J. Wilson

No, it was, I guess

Unidentified Analyst

And just looking at the, I'd like to look at each individual line there to get a sense of is it just one area that's causing a lot of the angst. And certainly I can follow-up on those particular items.

Thomas J. Wilson

Let Sam... Sam will answer your question, Tony, and if you have follow-up we can get you specifics with Bob. Is that alright?

Unidentified Analyst

Yes.

Thomas J. Wilson

Okay, great.

Samuel H. Pilch

For the four securities that we have detail on, that's on page 22, you can compute the book value percentage by taking the value, let's take that RMBS of $3.3 billion and the total loss, the unrealized loss is $870 million. Just add it to it. $3.3 billion divided by roughly 4.2 is 79. That algorithm can be applied for each of the four.

Unidentified Analyst

And in terms of vintages, just so, investors look at that to try to see the vintages. I know you talk about, '05, '07, whatever I guess, you do specific year by year type of analysis anywhere?

Thomas J. Wilson

We have the summary. But again, Bob can walk you through the individual years.

Unidentified Analyst

Okay. Thank you.

Thomas J. Wilson

Okay. Alright. I'd like to close since I know you are all... many of you are headed for another call. So as always, we appreciate your participation, your questions, feedback. Let me close with two thoughts. Allstate's strategy is working in what has been a challenging quarter and a challenging market. This is a great franchise. We have both operational excellence and a differentiated consumer focused strategic. And that combination will continue to deliver great results both for our customers and our shareholders. So, thank you and we'll talk to you next quarter.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes the program. You may now disconnect. Good day.