The Allstate Corporation

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Earnings Call

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CALL PARTICIPANTS 2

PRESENTATION 3

QUESTION AND ANSWER 9

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Presentation

Operator

Thank you for standing by, and welcome to Allstate's First Quarter 2023 Earnings Conference Call. [Operator Instructions] As a reminder, today's program is being recorded.

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

Mark Nogal
Head of Investor Relations

Thank you, Jonathan.

Good morning. Welcome to Allstate's First Quarter 2023 Earnings Conference Call. After prepared remarks, we'll have a question-and-answer session.

Yesterday, following the close of the market, we issued our news release and investor supplement, filed our 10-Q and posted related material on our website at allstateinvestors.com. Our management team is here to provide perspective on these results.

As noted on the first slide of the presentation, our discussion will contain non-GAAP measures, for which there are reconciliations in the news release and investor supplement, and forward-looking statements about Allstate's operations. Allstate's results may differ materially from these statements, so please refer to our 10-K for 2022 and other public documents for information on potential risks.

As some of you know, this will be my final earnings call as the leader of our Investor Relations team, as I will be transitioning to a new role in our P&C finance area supporting National General. I'm leaving Investor Relations in the capable hands of Brent Vandermause, who will be a great partner for all of you going forward.

And now, I'll turn it over to Tom.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Good morning. We're excited for Mark, and we're completely confident that Brent is going to give you everything you need to help you decide how and why you want to invest in Allstate. So good morning. We appreciate the investment of your time in Allstate today.

Let's start with an overview results, and then Mario and Jesse are going to walk through the operating results and the actions that we're taking to increase shareholder value.

So let's start on Slide 2. Allstate's strategy, as you know, has 2 components: increase personal Property-Liability market share and expand Protection Services. Those are shown in the 2 ovals on the left.

If you go to the right-hand side of the slide, you can see a summary of the results for the first quarter. We had a net loss of $346 million in the first quarter, which reflects a Property-Liability underwriting loss which was only partially offset by strong investment income and profits from Protection Services and Health and Benefits. We're making good progress on executing comprehensive plans to improve auto insurance profitability, and of course, we'll have a substantive discussion on that today. Not to be overlooked, we also continue to advance Transformative Growth plan, which is to execute the top oval there, which is to increase Property-Liability market share. At the same time, Allstate Protection Plans in the lower oval continues to expand its product offering and geographic footprint.

Let's review the financial results on Slide 3. Revenues of $13.8 billion in the first quarter increased 11.8% or nearly $1.5 billion as compared to the prior year quarter. The increase was driven by higher average premiums in auto and homeowners insurance, resulting in a Property-Liability earned premium growth of

10.8%. In the auto insurance line, higher insurance premiums and lower expenses were essentially offset by increased loss costs, so the profit improvement plan had not yet returned margins to historical levels. The auto insurance line had an underwriting loss of $346 million in the quarter.

In homeowners, the story is really about $1.7 billion of catastrophes, which led to an underwriting loss of $534 million. The total underwriting loss was just under $1 billion.

Net investment income of $575 million benefited from higher yields, which mostly offset an income decline from performance-based investments. Protection Services and Health and Benefits generated adjusted net income of $90 million in the quarter. As a result, the adjusted net loss was $342 million or $1.30 a share.

Now let me turn it over to Mario to discuss Property-Liability results.

Mario Rizzo
President of Property & Liability and Director

Thanks, Tom, and good morning, everybody.

Let's flip to Slide 4. The chart on the left shows the Property-Liability recorded and underlying combined ratios since 2017. As you can see, Allstate has a long history of generating strong underwriting results though the current operating environment is challenging, with combined ratios over 100 last year and into the first quarter. The underlying combined ratio of 93.3 for the first quarter was slightly below the full year 2022.

The second chart compares the full year 2022 recorded combined ratio for all lines of business to the first quarter of this year, which removes the influence of intra-year severity changes that occurred throughout 2022. The first red bar shows the underlying loss ratio was essentially unchanged as higher premiums were offset by increased loss costs. The second red bar on the left shows most of the increase in the combined ratio was driven by higher catastrophe losses, reflecting the widespread severe weather in the first quarter of this year. Expenses were lower by 1.9 points of premiums and minimal non-catastrophe prior year reserve reestimates also had a positive impact.

Let's move to Slide 5 to review Allstate's auto insurance profitability in more detail. As you can see from the chart on the left, which shows the auto insurance recorded and underlying combined ratios from 2017 through the current quarter, we have a long history of sustained profitability in auto insurance as we've successfully leveraged our capabilities in pricing sophistication, underwriting and claims expertise and expense management to generate excellent returns in the auto insurance business. Since mid-2021, loss costs have increased rapidly, driving combined ratios above our mid-90s target. The profit improvement plan is designed to address these significant loss cost increases, and we're making good progress.

The chart on the right compares the recorded combined ratio of 104.4 in the first quarter to full year 2022 results. Starting on the left, higher average earned premiums drove a 5.7 point favorable impact, which is shown in the first green bar. The first red bar reflects a 6.5 point increase in underlying loss cost due to increased accident frequency and severity for the 2023 report year, with severity currently projected in the 9% to 11% range above the full prior report year. A lower expense ratio reflects expense reductions and higher earned premiums. The remaining difference was due to catastrophes and prior year reserve reestimates. All in, both the recorded and underlying combined ratios of 104.4 and 102.6, respectively, improved in the first quarter of 2023 compared to the full year 2022.

Slide 6 provides an update on the execution of our comprehensive approach to increase returns in auto insurance. There are 4 focus areas: raising rates; reducing expenses; implementing underwriting actions; and enhancing claim practices to manage loss costs.

Starting with rates. Following increases of 16.9% in 2022, the Allstate brand implemented an additional 1.7% of rate increases in the first quarter. We will continue to pursue rate increases in 2023 to restore auto insurance margins.

Reducing operating expenses is core to Transformative Growth. We have also temporarily reduced advertising to reflect a lower appetite for new business.

We implemented more restrictive underwriting actions on new business in locations and risk segments where we have not yet achieved adequate prices for the risk. As we move through 2023, it is likely that some of these restrictions will be removed where there are profitable growth opportunities.

Enhancing claim practices in a high inflation environment is key to delivering customer value. This includes leveraging strategic partnerships and scale with repair facilities and parts suppliers to mitigate the cost of repairing vehicles. In addition, settlement of pending bodily injury claims has been accelerated to avoid continued increases in costs and settlements.

Transitioning to Slide 7, let's discuss progress in 3 large states with a disproportionate impact on auto profitability. The table depicts Allstate brand auto new business production and rate actions for California, New York and New Jersey.

As a result of implemented profitability actions, new issued applications from the combination of California, New York and New Jersey declined by 40% compared to the prior year quarter. The decline in these 3 states meaningfully contributed to the 22% decline countrywide.

The right-hand portion of the table provides rate increases either taken or needed to improve margins. In California, we just received approval for a second 6.9% rate increase implemented in April, which will be effective in June. We continue to work closely with the California Department on the best path forward to getting rates to an adequate level and expect to file for an additional increase in the second quarter, which will reflect the balance of our full rate need.

In New York, we filed for additional rate in the first quarter that is currently pending with the Department of Financial Services.

In New Jersey, we attained a 6.9% rate increase in the first quarter and expect to pursue additional filings in the second quarter.

As mentioned earlier, we anticipate implementing additional rate across the country into 2023 to counteract persistent loss cost increases.

Slide 8 dives deeper into how we are improving customer value through expense reductions. The chart on the left shows the property liability underwriting expense ratio over time and highlights drivers of the 2.9 points of improvement in the first quarter compared to the prior year quarter.

The first green bar on the left shows the 2 point improvement impact from advertising spend, which has been reduced given a limited interest in new business at current rate levels. The last 2 green bars show a decline in operating and distribution costs mainly driven by lower agent- and employee-related costs and the impact of higher premiums.

Shifting to our longer-term target on the right, we remain on pace to reducing the adjusted expense ratio to 23 by year-end 2024 as part of Transformative Growth. This metric starts with our underwriting expense ratio excluding restructuring, coronavirus-related expenses, amortization and impairment of purchased intangibles and advertising. It then adds in our claims expense ratio, excluding costs associated with settling catastrophe claims because catastrophe-related costs tend to fluctuate.

Through innovation and strong execution, we've driven significant improvement relative to 2018, with a first quarter adjusted expense ratio of 24.9. We expect to drive additional improvement, achieving an adjusted expense ratio of approximately 23 by the end of next year, which represents a 6-point reduction compared to 2018.

The increase in average premiums certainly represents a tailwind. However, our intent in establishing the goal is to become more price competitive. This requires sustainable reduction in our cost structure with future focus on 3 principal areas, including: enhancing digitization and automation capabilities; improving operating efficiency through outsourcing, business model rationalization and centralized support; and enabling higher growth distribution at lower costs through changes in agency compensation structure and new agent models.

Now let's move to Slide 9 to review homeowner insurance results, which incurred an underwriting loss in the quarter despite favorable underlying performance due to elevated catastrophe losses. We have a superior business model that includes differentiated product, underwriting, reinsurance and a claims ecosystem that is unique in the industry. As you can see by the chart on the left, this approach consistently generates industry-leading underwriting results despite quarterly or yearly fluctuations in catastrophe losses.

The chart on the right shows key Allstate Protection homeowners insurance operating statistics for the first quarter. Net written premium increased 11.1% from the prior year quarter, predominantly driven by higher average gross written premium per policy in both the Allstate and National General brands and a 1.4% increase in policies in force.

The first quarter homeowners combined ratio of 119 increased by 35.1 points compared to the prior year quarter, reflecting higher catastrophe losses primarily related to 5 large wind events in March. These accounted for more than 70% of catastrophe losses in the quarter. The first quarter catastrophe loss ratio was significantly elevated compared to the prior year and 10-year historical average by 36.2 and 30.5 points, respectively.

The underlying combined ratio of 67.6 improved 0.4 points compared to the prior year quarter, driven by higher earned premium and a lower expense ratio partially offset by higher claim severity.

Slide 10 provides an update on Transformative Growth. Transformative Growth remains a focus and is being executed in parallel with our profit improvement actions. We continue to make good progress on this multiyear initiative that spans 5 main components: improving customer value; expanding customer access; increasing sophistication and investment in customer acquisition; modernizing the technology ecosystem; and driving organizational transformation.

The bottom half of the slide highlights recent progress by intended outcome. Providing the lowest cost insurance through expense reductions, broad distribution and pricing sophistication is key to growth. Our Allstate brand relative competitive position has deteriorated recently as rate increases have exceeded some competitors. We expect that those competitors will eventually raise rates, improving our competitive position and growth prospects.

Distribution has been expanded by launching middle market and preferred products through independent agents under the National General brand. These products are currently available in approximately 25% of the U.S. market, with a plan to be in nearly every market by the end of next year.

Our new affordable, simple and connected auto product creates a differentiated customer experience, which is expected to become available in approximately 1/3 of the U.S. through the direct distribution channel by the end of this year.

Deploying a new technology stack, integrating technology across brands and retiring legacy technology applications provides increased agility and lowers costs. This will be reflected in the sunset of the Esurance and Encompass technology platforms next year.

We believe Transformative Growth will lead to increased market share, and hence, higher company valuation multiples.

And now, I'll turn it over to Jesse to discuss the remainder of our results.

Jesse Edward Merten
Executive VP & CFO

All right. Thank you, Mario.

Let's start with Slide 11, which covers results for our Protection Services and Health and Benefits businesses. The chart on the left shows Protection Services revenues, excluding the impact of net gains and losses on investments and derivatives, which increased 7% to $671 million in the first quarter compared to the prior year quarter. The increase reflects growth in Allstate Protection Plans and Allstate Dealer Services, partially offset by a decline in Arity. By leveraging the Allstate brand, excellent customer service, expanded product offerings and partnerships with leading retailers, Protection Plans continues to generate profitable growth, resulting in a 17% increase in the first quarter compared to the prior year quarter.

In the table below the chart, you will see that adjusted net income of $34 million in the first quarter decreased $19 million compared to the prior year, primarily due to higher appliance and furniture claims severity and a higher mix of lower-margin business as we invest in growth at Allstate Protection Plans. We will continue to invest in these businesses which provide an attractive opportunity to meet our customers' needs and create value for shareholders.

Shifting to the chart on the right, Health and Benefits provides stable revenues and is consistently profitable while protecting more than 4 million customers. Revenues of $583 million in the first quarter of 2023 increased by $3 million compared to the prior year quarter as an increase in group health and other revenue was partially offset by a reduction in individual health and employee benefits. Health and Benefits operating systems are being rebuilt to lower costs and support growth, which will leverage the Allstate brand and customer base to generate shareholder value.

Adjusted net income of $56 million was in line with the prior year quarter.

Effective January 1, 2023, we adopted the FASB guidance, revising the accounting for certain long-duration insurance contracts in the Allstate Health and Benefits segment using the modified retrospective approach to the transition date of January 1, 2021. This had an immaterial impact on our results.

Now let's move to Slide 12, which depicts trends in our investment portfolio allocation. Our active portfolio management includes comprehensive monitoring of markets, sectors and individual names, and we proactively reposition based on our views of economic conditions, market opportunities and the risk/return trade-off.

Asset class holdings are shown on the left. Our $63.5 billion investment portfolio includes a large allocation to high-quality interest-bearing assets, which has increased in recent years. In response to increasing recession risk, we defensively positioned the portfolio in 2022 by reducing our exposure to below investment-grade bonds and public equity. We maintained this defensive position in the first quarter with additional reductions in our public equity exposure.

Our performance-based portfolio, shown in green and gray, enhances long-term returns and is broadly diversified with more than 400 assets. The portfolio is largely U.S. exposures that span vintage years, sponsors and sectors.

Exposure to real estate and commercial mortgage loans is modest at $2.8 billion or 4% of the portfolio and is focused on more resilient sectors such as industrial and multifamily. We hold only $230 million in office properties for mortgages.

In addition to real estate, we have selective exposure to the banking sector totaling about $4.5 billion and consists primarily of investment-grade, fixed income securities issued by large financial institutions. We hold $240 million of exposure to regional banks, primarily larger regional banks, and we did not realize significant losses related to recent bank failures. Our high-quality portfolio provides flexibility to take advantage of investment opportunities as economic conditions evolve while providing substantial liquidity to protect our customers.

Let's shift from investment allocation to performance on Slide 13. As shown in the table at the bottom of the chart on the left, total return on our portfolio was 2.4% in the first quarter and 1.2% over the last 12 months.

Net investment income, shown in the chart on the left, totaled $575 million in the quarter, which is $19 million below the first quarter of last year.

Market-based income of $507 million, shown in blue, was $184 million above the prior year quarter following the proactive decision to reposition the market-based portfolio into higher market yields and an increase in fixed income funded by our reduction in public equity.

Performance-based income of $126 million, shown in black, was $180 million below a strong prior year quarter. Volatility from quarter-to-quarter on these assets is expected. Our portfolio management and the allocation of risk capital to investments is highly integrated with the assessment of risk-adjusted return opportunities across the enterprise.

As you'll recall, in response to declines in auto insurance profitability, last year, we defensively positioned the portfolio against rising rates and reduced our exposure to recession-sensitive assets. As market rates rose, we began to increase the duration in the fourth quarter and ended the first quarter at 4 years. This duration extension locks in higher yields and income for longer while positioning the portfolio to benefit from potential future reductions in interest rates.

The chart on the right shows the fixed income earned yield continues to rise and was 3.4% at quarter end. Our portfolio yield is still below the current intermediate corporate bond yield of approximately 5.1%, reflecting an additional opportunity to increase yields if rates stay at these levels.

To close, let's turn to Slide 14 to discuss Allstate's strong financial position and prudent approach to capital management. In light of recent financial events impacting the banking industry, let's start with an overview of Allstate's liabilities.

As you can see in the chart on the left, our liabilities primarily consist of property casualty claim reserves and unearned premiums that are not subject to unpredictable or immediate demands for repayment. Our sophisticated economic capital framework quantifies enterprise risk to establish capital targets by business, product, geography and investment while also providing additional capital for stress events or contingencies.

The framework incorporates regulatory capital standards, proprietary econometric modeling, I struggle with that, rating agency criteria and other external assessments. It is used through the company from individual product and state-based decisions to establishing the appropriate amount of capital for each company and the overall corporation. Allstate's capital of $19.2 billion exceeds our target capital based on this framework.

Our ratings remain strong, with S&P and Moody's assigning an issuer credit rating of A minus and A3, respectively, to our recent senior debt offering.

Holding company assets of $4.2 billion as of the end of the first quarter represent approximately 2.5x our annual fixed charges.

We returned $377 million to shareholders in the quarter through dividends and share repurchases. As a sign of our financial strength and commitment to shareholder returns, the common dividend was increased by 4.7% in the first quarter and paid in early April.
With that as context, let's open up the line for questions.

Question and Answer

Operator

[Operator Instructions] And our first question comes from the line of Gregory Peters from Raymond James.

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

Well. A lot to unpack in your comments. I think what I'd like to do for my question and follow-up would be to focus on, first, Slide 5. And I was interested in your comments about the average underlying loss ratio, I think, up 6.5% in first quarter versus the average earned premium being a good guide for 5.7%. I guess the question would be is the expectation that 6.5% is going to continue? And when will the average earned premium go beyond where the underlying loss ratio deterioration is?

Thomas Joseph Wilson
Chairman of the Board, President & CEO

I'll get Mario to dig in on claim expenses.

When you look at the 5.7%, I'll remind you -- first, good morning, Greg. I'll remind you that remember, this is a number that's been trending up as the rates that we took in '21 and '22 start to be earned in. So we would expect that number to continue to increase as we earn in the rates we've already implemented, and so we think this.

In terms of claims severity, I'll let Mario give you an update on where we are and what we're thinking about.

Mario Rizzo
President of Property & Liability and Director

Yes. So in terms of claims severity, what we disclosed this quarter was across major coverages were running in the 9% to 11% range in both physical damage and in injury coverages. Really, the drivers of those costs, if you start with physical damage, we continue to see pretty persistent inflation, particularly in parts and labor costs to repair cars. Actually, used car prices or total values for used cars actually came down a little bit in the first quarter in our numbers, but we had a higher percentage of total loss frequency which impacted the mix, so those are really the drivers.

And on bodily injury, it's the same things we've been talking about. Medical inflation, medical consumption and attorney representation. So I think the drivers of severity continue to persist. In terms of where they're going forward, it's really anybody's guess, but I think our perspective is, and we've been pretty consistent on this point, we're going to continue to take prices up. We've been doing that really since the fourth quarter of 2021 throughout last year. That continued into the first quarter. We're going to continue to, on a forward-looking basis, implement rate increases to first catch up and then outpace loss cost trends. But our perspective on rates is we continue to need to push more price through the system, and we intend to do that throughout the balance of 2023.

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

Right. On Slide 7, you -- in your comments, you talked about those 3 states. And I guess a follow-up question would be, where do you think that's going to go from a rate perspective? I think you said in your comment, Mario, that you expect to file the balance of your full rate need in California, and won't that trigger a different process causing a delay in potential rate approvals? So give us some color on that slide, please.

Mario Rizzo
President of Property & Liability and Director

Sure. So first I'll start with as we talked about, we just got approval for a second 6.9% auto rate increase in California, so we're -- going back to the fourth quarter of last year, we've got approval for 2 6.9% rates, and we've done that by working closely with the department to lay out our data and our loss costs.

In those conversations, and I think you've seen some of this across the industry, the department is really encouraging carriers to file for the rate need that they have in their book as opposed to going forward with 6.9% rate increase filings, and it's really based on just the volume of rate filings they're getting. So as we talk to the commissioner and the department, we got -- we're able to secure approval for the 2 6.9% rate increases, and we intend on filing the balance of our rate need going forward.

Does that create risk in intervention? It does. But I think we need to get California auto prices back to where they need to be so that we can create the kind of availability for consumers, really, that they deserve in California. So we're going to work with the department closely, we're going to make that filing, and then we'll see where that takes us going forward.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

So Greg, I think embedded in your question is, will you be challenged on something above 6.9%? The strategy that Guy Hill and team put into place was take 6.9% -- get 6.9%, don't have to have a consumer advocate come in and look at it, get another 6.9% and then go for the full rate. So what you're seeing us do it in 3 chunks. Other people have tried to do it other ways. We think this is the right way for us.

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

Got it. In New York, New Jersey?

Mario Rizzo
President of Property & Liability and Director

Yes. We got some rate filings pending with the New York department that hopefully will get resolved soon. And then New Jersey, you see, we were able to implement a rate increase and we're going to come back and file another rate increase. So we're working hard to get these 3 states off of this page.

Operator

[Operator Instructions] And our next question comes from the line of Paul Newsome from Piper Sandler.

Jon Paul Newsome
Piper Sandler & Co., Research Division

I was hoping you could give us a little bit more additional color on the claims inflation rate. Is it fair to say that what we saw in the first quarter was an acceleration of frequency or severity trends that was unexpected? And if so, maybe you could talk about a little bit more the pieces that were that much worse that may have seemed to have caught some people in the industry off guard.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Paul, you were breaking up a little bit, so let me just make sure I get it. So we're talking about auto insurance severity trends first quarter versus -- is that a tick up from what you saw last year? Or is it the level -- I'll -- If that's the question, I'll just -- Mario can jump into that.

Jon Paul Newsome
Piper Sandler & Co., Research Division

Yes, you got it.

Mario Rizzo
President of Property & Liability and Director

Yes, Paul. I guess what I would say about severity, again, in that 9% to 11% range is it just remains persistently high, I think, is how I would describe it, and that's true across coverages. It's certainly lower than what our expectations were for severity last year, what our ultimate forecast is for 2022. But it still remains at elevated levels, which is why I go back to we're going to need to continue to push rate through the system through the balance of this year to combat that inflation.

Jon Paul Newsome
Piper Sandler & Co., Research Division

Is that -- should we interpret that as a further acceleration of rate? I mean, I think you were expecting to put rate -- more rate anyway, right? I guess the question is do we have a step function up a little bit from where we would have been 3 months ago?

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Yes. Paul, I think there's a little bit of -- I mean, when you're looking at the percentages, it gets a little confusing when you're in a high increase environment. So if you looked at the numbers that Mario was talking about, are the percentages up versus the full year of 2022, not versus the first quarter of last year. As you know, the percentages kept going up as we moved throughout the year and we adjusted our results. And so what we've decided to do is to talk about the percentages up versus the full year.

And I think Mario said it well, which is it continues to be high. And so we're trying to -- if you look at the percentage up versus what we thought it was in the first quarter, it would be higher than 10% to 11%, but it's not higher than what we thought the first quarter was at the end of last year. So as it relates to pricing, we're looking at just total loss cost frequency and severity, and we have to -- we believe we have to continue to increase prices this year. As Mario talked about, we were up almost 17% in the Allstate brand last year. I don't know. We don't have a target for what it will be this year. As Mario said, it's going to be what it needs to be.

Jon Paul Newsome
Piper Sandler & Co., Research Division

No, that's helpful. I always appreciate the help, and I'll let some other folks ask questions.

Operator

[Operator Instructions] And our next question comes from the line of Elyse Greenspan from Wells Fargo.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

My first question, I just wanted to talk about your RBC ratio. I mean, we see the cat losses and we can see the impact that that would have had on statutory income in the quarter. But you guys also did cut your equity investments in 1/2, which I think could have maybe a 20-point benefit in RBC. Is there a way for you guys to walk through the moving components of RBC in the quarter and give us a sense of where your RBC ratio would be within AIC at the end of the Q1?

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Elyse, thanks for the question. Let me provide a little overview and then Jesse can jump in for the specifics.

The headline would be, we don't just look at RBC. And so as Jesse said, so -- I mean, if you step back and say, what are the learnings from the recent bank failures? Having a capital problem is not something that just happens to you like an auto accident, right? It's a result of a series of choices made over time. So in terms of our series of choices, we had this really comprehensive set of processes around those choices that are highly analytical. We look at all kinds of scenarios. We look at it frequently, and as a result of that, we come up with what we think the right amount of capital is. It includes things like RBC. It includes things like the rating agencies. It includes, in some cases, we are more restrictive in terms of the amount of capital we think we need than other people. So we don't play the game of RBC arbitrage, so to speak, and fool ourselves.

With that, Jesse, do you want to talk about how you think about capital and where we're at?

Jesse Edward Merten
Executive VP & CFO

Yes. Thanks, Tom. I mean I think, as you and I have talked before at least, we try and take a look at our capital position using our sophisticated economic capital model and not just the RBC ratios. We don't -- just to be clear, to your specific question, we don't publish and have not published the RBC ratio for this quarter, and so I'm not in a position to take you through the bits and pieces on this call. I think directionally, you and others have noted what the RBC impacts would be.

But I think it's more important to think about the way that we manage capital and the way that we look at it on a comprehensive basis, not just an RBC basis. And I think you've seen reflected in the results that we continue to proactively manage our overall capital position.

So again, I go back to our economic capital model, the sophisticated and comprehensive way that we look at capital, including all different sources and uses, and feel confident in our capital position being, as I said in my prepared remarks, above our internal targeted levels.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

But you shouldn't take the fact that we have less equity as a statement that we thought we needed to save capital. We have less public equity holdings because we didn't think it was a good risk/return trade-off, which John will be happy to talk about if somebody wants to go through. But we think we have plenty of capital to run this business.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And then my second question, your personal auto underlying loss ratio did improve sequentially, right? There -- some noise, right, as there were some true-ups in the fourth quarter last year. And also, I thought that seasonally, Q1 for auto tends to be better. But I guess you put this all together and you guys are talking about taking -- still earning in some -- a good amount of rate increases, do you think that the personal auto loss ratio peaked in the first quarter? And should we expect it to improve from here?

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Well, first, we think the profit improvement plan is working. I would say, Elyse, that if you just summarize the first quarter, I would say we held serve. We held serve in the face of, if you're a tennis fan, 120-mile an hour serve, which was called continued high increase in severity. How will -- we've returned the ball, and as you point out, it's about where it was last year. It is improved sequentially in the fourth quarter, but you're absolutely right. And there were some other things going around in the fourth quarter related to the first, second and third quarter of last year. So it's not quite fair to say that it improved. I would just say we held serve.

We feel good about where we're going. It's -- in our mind, it's a question of when, not if we will get back to how we make profitability. And that's, of course, dependent on what happens with inflation and costs.

Operator

[Operator Instructions] And our next question comes from the line of Yaron Kinar from Jefferies.

Yaron Joseph Kinar
Jefferies LLC, Research Division

Maybe starting with the current capital position, the reallocation of some of the investments. Can you maybe talk about how you see the capital in maybe capital market stress scenarios? And I'm sure you run those internally. Any color you can offer around that would be much appreciated.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Yaron, I'm not exactly sure. Maybe you can give me another layer down in the question so we can get specific for you?

Yaron Joseph Kinar
Jefferies LLC, Research Division

Sure. So I think you're talking about, what, roughly $4 billion of liquidity or access of the holdco and I think $16 billion of liquidity. What happens to those if we find capital markets stressed? I don't know if there's another 25% decrease in the equity markets, maybe a credit cycle. I'm not exactly sure what kind of scenario to paint because I don't want to put you on the spot with a specific set of declines, but I'm sure you do test this excess capital availability against stresses in the system.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Yes. No, it's a good point. Let me get John to answer it better. I'll give you a little overview.

First, I would just say analytics everywhere. It [x4] how we run this place. So whether that's using sophisticated models this time, whether it's [total the] car or extending duration or what we're doing with capital. And so when we look at the extension of duration, I think John ran like 9 different scenarios, how to do it, what to do it, what -- so we're all over that.

When it comes to stress events in the capital markets, we look at all kinds of alternatives there. Everything from -- and what do we do if the the government defaults to what do we do if there's more bank failures. And so we have -- and John can tell you sort of how he's thinking about how we allocate assets in the portfolio relative to events in today's market.

I would say from an overall capital standpoint, which is we got plenty of money. Like you saw our liabilities, they're very predictable, and so nobody is going to run in and say give us back our $10 billion and we don't have it. At the same time, we have a really highly liquid portfolio because so much of it's investment-grade fixed income. If the fixed -- investment-grade fixed income markets completely shut down, we would still probably be fine. But no, probably we would be fine because we're having cash come in in terms of unearned premiums every day, so we don't really have any overall liquidity issues. But in terms of capital market stress and how you think about that from an investment decisions and where we're invested today, John can give you some perspective.

John Charles Pintozzi
Senior VP, Controller & Chief Accounting Officer

Yes. Yaron, thank you so much for the question. Just a piece of data. If we couldn't trade security, we'd have $5 billion of cash coming in in the next year just by things that are rolling off. It's highly integrated into the overall data and analytics and quantitative framework across the enterprise. So I'd -- and I answer this question, I feel confident that scores of people on the investment team could answer it too because it's part of the way that we think. We're not managing an investment portfolio separate from the way that we think about the enterprise.

Tom talked a little bit about the duration trade that we did that was highlighted in the materials. That's not taken in isolation of how all the other securities in the portfolio would perform, and it's not taken in isolation on how we think about the entire enterprise, what happens in underwriting and other areas. We run probably 100 different scenarios on a daily basis that look back at things that have happened in the past, things that could happen in the future, what that means for returns and what that means for capital. And we subscribe to getting the order of ready, aim, fire right, so we really aim a lot as we think about our investment profile.

Yaron Joseph Kinar
Jefferies LLC, Research Division

And then maybe shifting back to the auto book. Is the piece or the cadence of rate increases that you expect to file in auto kind of similar to where it was when we ended 2022? Or do you see maybe additional rate increases are necessary today relative to the plan at the beginning of the year?

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Versus the plans at the beginning of the year. So maybe I'll give an overview, Mario, with an analogy and you can [indiscernible]. We're running as fast and as hard as we can on rates everywhere. If we need them, we're really running fast and hard. If we think we're actually adequately priced in some states where we are today, we're still paying attention. We're still on the track. We're so warmed up and ready to run if we need to be.

Mario Rizzo
President of Property & Liability and Director

Yes. What I would add, Yaron, I'm going to go back to a comment I made earlier, which is we've been pretty consistent on this point of the need to take prices up going back to last year, and that hasn't changed. Now obviously, we react to new data, new information in real time, and the absolute amount of rate we take is going to be dependent on that updated data. As Tom mentioned earlier, we rely on heavy-duty analytics to manage the business and we respond to what's happening in real time, so the amount of rate we need will be dependent on how loss costs play out over time for us.

But we're going to continue to push rate through the system. We've been successful at that. I wouldn't get too hung up on quarter-to-quarter fluctuations because that quarterly number is going to bounce around in terms of the rates that were approved in a particular state and the size of those rates. But I think thematically, and we go back to what we've been saying now for -- over the last year, which is we're going to continue to take the rate that we need to get auto margins back to where they need to be, which is in the mid-90s targets that we have.

Yaron Joseph Kinar
Jefferies LLC, Research Division

And good luck, Mark, with the new role.

Mark Nogal
Head of Investor Relations

Thank you.

Operator

[Operator Instructions] And our next question comes from the line of Andrew Kligerman from Credit Suisse.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

I'm trying to unpack the earlier comment about used car prices coming down a bit because the Manheim Index was up about 8.6%, and that's kind of a forward-looking indicator. So maybe you could give a little color on what your expectation there is for used car prices? Does that kind of fit in your 9% to 11% or could it -- of projected severity increase? Or could it be materially higher as we look out in the year?

Mario Rizzo
President of Property & Liability and Director

Andrew, it's Mario. Thanks for the question. I guess what I'd start with, there's a number of indices for used car prices. I think you mentioned one with Manheim that tends to focus on wholesale prices. And I think as we all know, that metric was coming down most of last -- or certainly in the back half of last year, and then started to tick up in the end of the fourth quarter and has continued into this year.

What I was referring to earlier is actual total loss severity, which tends to lag the Manheim Index and is more a function of retail used car prices, which have improved, and that's what I was referring to in the quarter. What we saw was actually used car -- or, I'm sorry, total loss severity actually improved a little bit year-over-year.

In terms of the risk going forward, I think, yes. If you look at what's happening with the Manheim Index and other indices, certainly, they're headed in a different direction than they were headed for much of last year, which adds risk. We've tried to factor that into our severity expectations in terms of what we're recording that 9% to 11% range. But what we actually saw in the first quarter of this year was a modest improvement in total loss severity.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Got it. All right. And then it was interesting -- been interesting following National General with auto policies in force now of about $4.6 million off pretty significantly from $4.1 million last year. It looks like you're getting good rate increases. Your combined underlying was 94%, so -- which is pretty decent.

So looking forward, it sounds like you haven't fully rolled it out. Is this something that could really catapult your policy in force at a very responsible return? I mean, maybe a little color on how that -- what your expectations over the next year to -- for policy growth and doing so profitably?

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Andrew, thanks for focusing in on National General. For summary, we feel really good about the acquisition of National General. If you just start with the math, the numbers, it's exceeded our expectations and assumptions because as you'll remember, we mostly bought that so we could reduce our expenses in the independent agent channel by folding, basically having them reverse acquire Encompass, we just happened to buy them first. And so they've -- and that's ahead of plan and the numbers are bigger. So we're feeling really good about that, and that's the way we priced the deal.

You're -- strategically, which is where you're after, we're also getting the benefit of now having a solid platform and independent agent channel, which we did not before. We've been struggling to get a good platform. So they have good technology, good relationships, as you point out, mostly in the nonstandard stuff. And Mario, I think in his comments, mentioned how we're now taking those relationships and that technology platform and we're putting what we call mid-market, which is basically standard auto and homeowners, on that platform, and that's going to give us great growth opportunities because we're using the Allstate expertise in both standard auto and -- not to be underestimated, one bit really is our business model and homeowners. We think that's a great growth opportunity and which is basically icing on the cake relative to the acquisition.

So we feel really good about we're in that channel. It's part of Transformative Growth. It's part of increasing market share and personal profit liability, and we're pleased with the results.

Operator

[Operator Instructions] And our next question comes from the line of Josh Shanker from Bank of America.

Joshua David Shanker
BofA Securities, Research Division

I want to talk about segmentation and policy count. Obviously, the net decline in the auto policy count was quite high this quarter. Do you have some sort of advice or thoughts to think about how much policy count will decline over this repricing period?

But two, I also noted that homeowners policy count was flat which suggests in the segmentation, there's different policyholders you're keeping versus different policyholders you're losing. So I thought you might be able to touch on both things.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Good. Mario, why don't you talk about homeowners and what we're doing there to drive growth?

As it relates to auto insurance, we just talked about sort of the Allstate brand, I think, which may be the numbers you're referring to, which is down, versus Andrew's comment about National General, which is up. On the Allstate piece, there's obviously 2 components. One is, are you selling more new business? And then the second is what's happening with retention. And as it relates to new business, we've taken the approach that a prospective rate increase is like a new business penalty. So as you know, when you sell business, you're going to have -- you got expenses as you're getting the customers more to get them right upfront. And then the loss ratio is typically higher for new business than it is for existing business. If you need 10 points of rate on top of what you're currently selling it to, we've factored that into our growth projections on new business and said, well, that's -- at the very least, it's an additional 10 points of new business penalty. The worst is that when you raise your prices by 10%, all the money you spent getting the customer is wasted because they go away and you churn it.

So we've dialed back new business and advertising not so much because we're trying to manage the P&L but because we're managing the economic growth. And we think needing rate increases and going out and getting a new customer and saying, it's great, you bought it for $1,000. And then 6 months later saying, well, it was really $1,100 is not a good plan. So we've dialed back new business, and you see that really across the board. And Mario showed in some places, even more aggressively, like New York, New Jersey, and California, I've kidded Mario that like, he'll know every new business customer we get in New York if we keep this up personally. So that's basically an economic choice.

On retention, of course, that's the customer's choice and that depends what happens in the marketplace and what other people are doing. Our retention has gone down. We do model that out. It's really very difficult to take those old models though and give yourself any kind of good estimate on the current view because a couple of things have changed. One, these are much bigger increases than those models had in them. So those models are based on 5%, 6%, 7%, not on 10%, 12% or 15% or 40% in Texas. And at the same time, those models don't have the kind of competitive environment you're operating in where everybody else is raising rates at the same time. So we've shut down new business because we think it's economic and there's an increased new business penalty associated with being underpriced, and then we're managing through it.

What we want to do, of course, is we're highly focused on improving customer value because if people pay more, you got to do more for them. And so we're working hard on making sure we do insurance reviews, get our agents working.

Homeowners is another great story that I think we've kind of -- we get so focused on auto, we haven't really told it. It's a great business model. Mario can talk about what we're doing to grow that business.

Mario Rizzo
President of Property & Liability and Director

Yes. Thanks for the question, Josh. And homeowners, again, as I talked about in the prepared remarks, is a business that we continue to feel really good about in terms of where it's positioned from a profitable growth perspective. And what you saw in the quarter is that we actually increased policy count by about 1.4%. Retention actually picked up by a 1/10.

And I think there's a couple of things when you kind of unpack what's happening with retention in homeowners because much as Tom talked about, we're having to take prices up in auto, the way we're taking price increases is in a highly segmented and targeted way, and that's helping from a retention perspective on homeowners because those bundled customers tend to be our longest-tenured, most profitable customers.

We also bundle about 80% of homeowners' policies have a supporting auto line and the retention on a bundled customer, where a homeowner that has an auto policy, is meaningfully higher than a monoline homeowners, and we're continuing to see the benefit of that.

And we've put processes in place both in terms of economic incentives for our agents and sales processes in the call centers on the direct side to incent additional bundling. And we're seeing some nice trends in terms of bundling rates, which is certainly helping homeowner growth through homeowner retention.

We're going to continue to look for ways to grow the homeowner business. We think it provides a really compelling risk and return opportunity for us. The results are going to bounce around because there's volatility. This quarter is an example of that with catastrophe losses, but we continue to see our underlying combined ratio and loss ratio improve, and both through leveraging the tactics I talked about for retention and also looking to drive up production, particularly with bundled customers, we think we can continue to grow that line.

Joshua David Shanker
BofA Securities, Research Division

Are the bundlers having the same problem that they get quoted a rate an entire 6 months later? Or is your pricing such that you can comfortably quote a bundle right now and think that you're going to retain them for 12 months?

Mario Rizzo
President of Property & Liability and Director

Yes, we're obviously quoting bundled customers right now. And when you look at the business we are writing, we're seeing really nice improvements in terms of quality and lifetime value, which is indicative of that bundling rate. And so yes, we're quoting it.

And the other thing you got to remember, and this is true both from a retention and a new business perspective, bundling, it's an easier experience and a more streamlined experience for customers. There's discounts associated with bundling as well that can help offset higher auto rates and incent customers to stay with us.

Operator

[Operator Instructions] Our next question comes from the line of Brian Meredith from UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of questions here for you. First one, I'm just curious, I saw your expense ratio is down about 1 point ex ad spend. Where are we in this Transformational Growth as far as the expense ratio reduction? How much can we potentially see here additional going forward?

And then maybe on the -- as an add on to that, what's kind of a normalized ad spend as a percentage of earned premium, so we can kind of get a view on what our expense ratio should ultimately end up?

Mario Rizzo
President of Property & Liability and Director

Yes, Brian, this is Mario. Thanks for the question. Again, expenses, as much as Tom talked earlier about, earned premium and loss ratio, we kind of held serve there, we did see the benefit of a lower expense ratio both in terms of the underwriting expense ratio and the adjusted expense ratio.

Where we're at in the kind of continuum on the adjusted expense ratio, we set a goal to get that adjusted ratio down to about 23 by the end of 2024. And we're making really good progress on that. You saw continued progress on that this quarter. We certainly are being helped by higher earned premium which leveraged our cost. But we're continuing to see reductions in both operating costs and distribution-related costs, which are helping the expense ratio.

And I talked a little bit earlier about the areas we're focused on, whether it's automation, digitization, sourcing and continuing to drive both operating and distribution costs down. We're going to -- those are really going to be the levers we pull to push the expense ratio ultimately to that goal that we set with Transformative Growth. So we're making good progress, feel really good about that.

In terms of the level of marketing spend, certainly, we spent less this quarter on marketing than we did a year ago, and we've pulled that back. I think as Tom said earlier, really from an economic risk and return perspective, it doesn't make a lot of sense for us to invest aggressively in marketing at a time when our prices aren't adequate. But what we will do over time as more rates and -- or, I'm sorry, more states and more markets get to a rate level that we're comfortable with, we're going to surgically lean in. And as one of the components of Transformative Growth, we're going to look to both increase the level and the sophistication of the marketing investment that we make. And that will be commensurate with what we think the opportunity is to grow. So I can't sit here today and give you a specific dollar amount or a target that we're focused on. That's why we gave you the adjusted expense ratio, which excludes marketing costs because we're going to continue to invest in marketing when it makes economic sense and where it makes economic sense for us to lean in.

Thomas Joseph Wilson
Chairman of the Board, President & CEO

So let me just double click on the Transformative Growth piece. So the third piece of Transformative Growth is to increase the sophistication and investment in customer acquisition. We think we can and should be able to get new customers cheaper than we do today. There's lots of math we have around that. One of those is telematics. So we were the first out there with continuous telematics. We've been at it for over a decade. We're now taking telematics, and with Arity, we now think we can take telematics into new business, Brian. And actually, not have to have them download our app or put a device in their car to figure out how good a drive they are. We think we can use our sophisticated analytics to price them using telematics ahead of time, which will enable you to better manage your acquisition costs. So lots of work to go there, so plenty of opportunity to grow.

Brian Robert Meredith
UBS Investment Bank, Research Division

Can I just -- one quick follow-up here. If I think of kind of going forward here, when you're looking at putting rate increases through for the remainder of the year, what's your kind of base case with respect to how you're thinking about inflation here? Are you assuming that the current inflationary environment then is persisting through the remainder of 2023 as you're filing for rates?

Thomas Joseph Wilson
Chairman of the Board, President & CEO

Let me finish and make sure we respect for people's time on that question. So first, when you look at overall inflation, the numbers the Fed and everybody else sees, that's one set of numbers. If you look at the inflation in what we do, it's, of course, dramatically higher. And those are subject to different things. So whether the Fed tightens the economy or doesn't tighten the economy, probably isn't going to do a lot to keep people from having severe accidents, hurting themselves and needing a lot of medical care or then more lawyers getting involved in the case. Nor will it have a huge impact on what the OEs charge on parts. They tend to charge more in parts based on what they're doing to overall profitability and how many new cars are selling. So if we go into a recession, they sell new cars, I don't expect they're going to cut cars' prices. So we think inflation will persist in this business at a higher level than you see from the overall CPI, and that's why we're having to raise prices for our customers.

Thank you all for participating today. Thank you for being generous with your time. We're going a few minutes over. Our priorities, make sure we make money in auto insurance; continue to leverage our superior position in homeowners; start to grow and execute Transformative Growth, whether that's by getting our costs down, rolling out new products, expanding our National General platform; and then we didn't spend any time today on the great stories we have in the lower oval, which is expanding Protection Services.

So a lot of things we're working on hard to create more value for you. Thank you, and we'll see you next quarter.

Operator

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