S&P Global
Market Intelligence

The Hanover Insurance Group, Inc. NYSE:THG

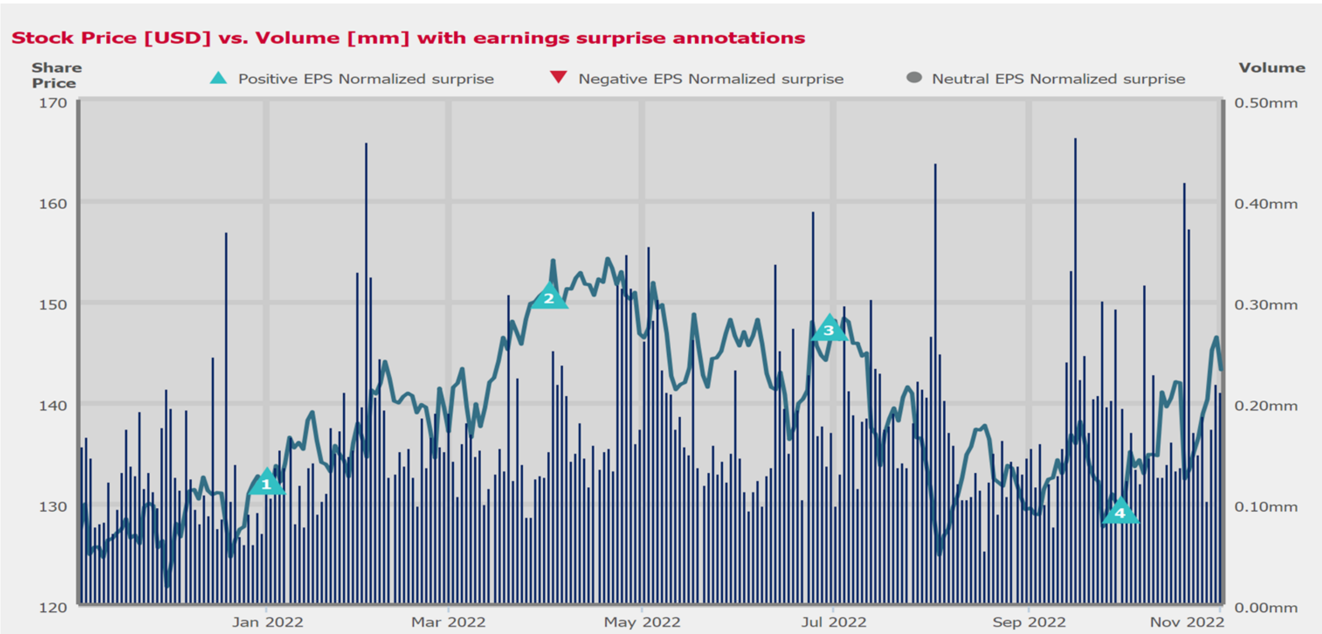
FQ3 2022 Earnings Call Transcripts

Wednesday, November 2, 2022 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2022-			-FQ4 2022-	-FY 2022-		-FY 2023-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	GUIDANCE	CONSENSUS
EPS Normalized	0.94	0.99	5.32	2.36	8.92	NA	NA
Revenue (mm)	1438.65	1505.40	4.64	1277.10	5397.59	NA	NA

Currency: USD
Consensus as of Nov-02-2022 1:05 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2021	2.54	3.38	1 32.55 %
FQ1 2022	3.07	3.26	2 6.19 %
FQ2 2022	2.15	2.32	3 7.91 %
FQ3 2022	0.94	0.99	4 5.32 %

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Call Participants

EXECUTIVES

Bryan James Salvatore
Executive VP & President of Specialty

Jeffrey Mark Farber
Executive VP & CFO

John Conner Roche
President, CEO & Director

Oksana Lukasheva
Senior Vice President of Corporate Finance

Richard William Lavey
Executive VP & President of Hanover Agency Markets

ANALYSTS

Grace Helen Carter
BofA Securities, Research Division

James Paul Bach
Keefe, Bruyette, & Woods, Inc., Research Division

Matthew John Carletti
JMP Securities LLC, Research Division

Michael Wayne Phillips
Morgan Stanley, Research Division

Paul Newsome
Piper Sandler & Co., Research Division

Presentation

Operator

Good day, and welcome to The Hanover Insurance Group Third Quarter Earnings Conference Call. My name is Keith, and I'll be your operator for today's call. [Operator Instructions] Please note, this event is being recorded. I would now like to turn the conference over to your host today, Oksana Lukasheva. Ms. Lukasheva, please begin.

Oksana Lukasheva
Senior Vice President of Corporate Finance

Thank you, operator. Good morning, and thank you for joining us for our quarterly conference call. We will begin today's call with prepared remarks from Jack Roche, our President and Chief Executive Officer; and Jeff Farber, our Chief Financial Officer. Available to answer your questions after our prepared remarks are Dick Lavey, President of Agency Markets; and Bryan Salvatore, President of Specialty Lines.

Before I turn the call over to Jack, let me note that our earnings press release, financial supplement and a complete slide presentation for today's call are available in the Investors section of our website at www.hanover.com. After the presentation, we will answer questions in the Q&A session. Our prepared remarks and responses to your questions today, other than statements of historical fact, include forward-looking statements as defined under the Private Securities Litigation Reform Act of 1995.

These statements can relate to, among other things, our outlook and guidance for 2022, economic conditions and related impacts, including inflation, supply chain disruption, evolving insureds behavior emerging from the pandemic and other risks and uncertainties that could affect company performance and/or cause actual results to differ materially from those anticipated. We caution you with respect to reliance on forward-looking statements, and in this respect, refer you to the forward-looking statements section in our press release, the presentation deck and our filings with the SEC.

Today's discussion will also reference certain non-GAAP financial measures such as operating income and accident year loss and combined ratios, excluding catastrophes, among others. A reconciliation of these non-GAAP financial measures to the closest GAAP measure on a historical basis can be found in the press release, the slide presentation or the financial supplement, which are posted on our website, as I mentioned earlier. With those comments, I will turn the call over to Jack.

John Conner Roche
President, CEO & Director

Thank you, Oksana, and good morning, everyone. I'll begin by providing some context on our third quarter performance, share my perspective on the current industry environment and outline our approach to address the prevailing economic and market pressures. Next, Jeff will review our financial and operating results by segment, outline our action plan in detail and provide an update to our financial expectations. And then we will open up the line and take your questions.

Before I comment on the results, on behalf of the entire Hanover team, I'd like to acknowledge all those who have been impacted by Hurricane Ian. Members of our claims organization are hard at work doing what they do best to help our customers recover as quickly as possible.

As always, I'm very proud of the important work we do every day to help our customers in their time of need. As evidenced by recent earnings reports, our industry is operating in a very dynamic macroeconomic environment, continuing inflation and supply chain disruptions, turbulent financial markets and losses from Hurricane Ian created a confluence of headwinds for the P&C industry in the third quarter.

As our track record demonstrates, we are executing very well on our catastrophe exposure management and continuing to diversify our portfolio over time. While our risk management discipline and strategic approach to the market enabled us to moderate the impact of recent macro challenges on our results, the accelerated pace of inflation and persistent supply chain issues surpassed our expectations.

As a result, we are making meaningful adjustments to our short-term pricing and underwriting approaches and are taking specific actions to mitigate the effects of inflation more aggressively, all to bring our company back to target profitability and deliver on our financial objectives. We have a very strong, highly regarded franchise and an excellent portfolio of businesses. Our company is built to generate superior performance over the long term. We've established a strong track record of profitability and assembled the skills, talent and capabilities to address these short-term loss trends head on. And we're confident the market is responding appropriately to these environmental issues, and we remain on track to achieve our long-term financial targets. We will continue to execute on our proven growth strategy focused on a differentiated agency and customer approach while also putting a laser focus on margin improvement in certain businesses to address the recent changes in the overall environment.

In the quarter, the effects of inflation were most pronounced in our personal auto homeowners and CMP property lines. Additionally, we experienced an increase in large losses in CMP with inflation and supply chain issues magnifying the effect on loss costs. Jeff will elaborate on the impact on each business in more detail. But to be clear, despite these temporary challenges, we remain very comfortable with the quality of our book of business, our risk selection and our underwriting discipline.

From that perspective, we are pleased with our overall performance year-to-date. Our resulting ROE of 10.5%, the execution of our strategic priorities and our top line results in the third quarter. We generated net written premium growth of 9.5% in the quarter with healthy production indicators across each of our segments. Our Core Commercial business grew 5.9% and led by renewal price increases of 11.2%, driven by double-digit increases in both our small and middle market businesses.

Rate increases accelerated 40 basis points sequentially to 7.3% and strong retention indicates we have additional opportunities to take even more rate in the future. Our specialty team continued to build on its momentum, achieving growth of 12.6%, underscoring the strength of our agent partnership model and our ability to access high-margin Specialty business. The investments we have made in our specialty capabilities have proven to be high-yielding, enhancing our relevancy and enabling us to pursue an even better balance between property and casualty risks over time.

In the third quarter, we achieved robust rate increases of 8% across our specialty book. with price increases, including exposure of 12.4%. This highly diversified and specialized portfolio enables us to offer our retail agents one of the broadest range of products in the small to midsized market. In that vein, we continue to expand our offerings. And we remain on track to complete the nationwide rollout of our specialty general liability product before year-end. Additionally, we were extremely pleased to see strong renewal retention and robust growth contributions from Surety, Specialty P&C and Marine. Moving to Personal Lines. This business grew net written premiums by 11.3%, with an average renewal pricing increase of 7.3%, sequential PIF growth of 1.5% and continued strong retention. Of course, we expect our personal lines policy growth and retention to moderate as we implement additional rate and other pricing actions in the coming quarters.

Looking ahead, we are working diligently on a series of actions designed to enable us to return to prior target margins in affected personal and Core Commercial property lines. As I indicated earlier, we have a high-quality book of business, but we need to make appropriate adjustments to address the current rapidly changing external environment. Many of these actions are already being executed. They are focused on three key areas: Pricing, insurance to value adjustments and targeted underwriting measures.

First, our most effective response to higher inflation is to increase rates, and we are aggressively stepping up these initiatives in property lines. Prospective rate increases must exceed loss trends for us to achieve our targeted combined ratios. We are moving quickly and have already stepped up our filings and made further automatic inflation adjustments for property exposures across all states.

We expect these actions to result in Personal Lines renewal price change of approximately 10% in the fourth quarter and to further accelerate to the low teens in 2023. A disciplined strategy is essential in the current environment, and our superior agent partnerships and market position will enable us to hit our pricing targets. Second, we are further implementing robust insurance to value adjustments in sectors and geographies that are most dramatically affected by the elevated costs.

These actions target insured value adjustments beyond those embedded in the automatic statewide inflation guard factors and are tailored to specific risks that are experiencing accelerated property valuations including elevated business interruption exposures. Third, we are implementing targeted underwriting actions to better position our quality book of business in light of the recent changes in the socioeconomic environment. These changes include enhancing underwriting guidelines, exclusions and targeted agency management.

We are also extensively using innovative tools and technology to increase our underwriting precision and reduce exposure to certain undesirable risks, those that will not meet our profitability expectations even with additional rate. We are intently focused on the personal lines and commercial property pricing environment as we execute on our plans to recapture industry-leading top-tier margins.

We do not see any signs of softening in the market conditions that would impact our portfolio. Inflation and supply chain issues are pervasive and impacting all primary insurers. Reinsurers are signaling shrinkage of property capacity, particularly after Hurricane Ian, which also bodes well for continued firming and discipline in the primary market.

In Personal Lines, we are experiencing one of the hardest markets in history, and we are well positioned to improve margins at an accelerated pace. In virtually any macroeconomic environment and particularly now, the market favors well-built companies with enduring business discipline through solid growth, a sound reserving philosophy and thoughtful financial stewardship, our company has consistently proven that discipline, and we'll continue to apply our superior skills and disciplined approach while we further work through inflation and other evolving pressures.

As we contemplate our past performance and our future opportunities, I have every confidence our experienced and talented team, our highly responsive and collaborative culture and our unique business strategy will enable us to drive superior performance well into the future. With that, I will turn the call over to Jeff.

Jeffrey Mark Farber
Executive VP & CFO

Thank you, Jack. Good morning, everyone. For the third quarter, after-tax operating income was $35.7 million or $0.99 per share. Our combined ratio was 101%, reflecting higher-than-expected inflation, supply chain pressures and the impact of catastrophes. Excluding catastrophes, the combined ratio was 94.2%. I'm going to walk you through the key drivers of what impacted our business in the quarter as well as the actions we are taking and their expected outcomes.

Catastrophe losses of $90 million or 6.8 points of net earned premium, included $28 million from Hurricane Ian and are likely better than the industry loss experience. our relatively modest Cat loss experience from Hurricane Ian, which was largely isolated to our commercial lines property book in Florida, underscores the effectiveness of the exposure management and portfolio diversification initiatives that we executed in prior years.

Our catastrophe risk premium in Florida is negligible, totaling less than 0.5% of our countrywide direct written premiums. Catastrophe losses in personal lines during the quarter were primarily related to wind and hail events in the Midwest. Our results in the third quarter included favorable prior year reserve development of $4 million primarily driven by specialty lines. We anticipate social inflation to reemerge fully in liability coverages.

And as such, our team continues to vigilantly monitor the litigation environment. We continue to believe that some of the macroeconomic headlines around medical and wage inflation weren't the utmost caution as we prudently set reserves in longer tail lines. Our expense ratio for the third quarter of 2022 was 30.4%, an improvement of 0.7 points from the prior year quarter, driven primarily by growth leverage and reduced incentive costs. We are pleased with the 50 basis point improvement in the year-to-date expense ratio from the prior year period, which reflects a beat to our expense ratio target.

Moving on to a discussion of our underlying underwriting performance. Our overall current accident year loss ratio, excluding catastrophes, was 64.1% in the quarter, which was approximately 5 points above our original early 2022 expectations and about 4 points higher relative to the outlook we provided in our second quarter 2022 earnings call. At a high level, out of the 5 points, personal auto contributed 2 points and home added 1.5 points, while CMP accounted for the balance, including large losses.

About 4 points of the 5 were driven by inflation and supply chain delays, of which about 1 point represented a reestimation of first and second quarter's claims on Personal Lines property. In summary, about 3.5 points of the loss ratio increased during the third quarter relative to our early 2022 expectation is the short-term challenge that needs to be addressed and it has our full focus.

Now looking at our results by business, starting with Core Commercial. The Core Commercial current accident year loss ratio, excluding catastrophes, was 61.7%, 50 basis points higher than the third quarter of 2021 as both periods included higher property large losses than our historical averages. Relative to our February 2022 expectations, the underlying loss ratio in the third quarter of 2022 was 4 points higher, driven by one increased property loss severity stemming from inflation and repair delays and the resulting elevated business interruption losses; and two, a higher incidence of property large losses in certain areas of the book.

Some of the large losses were aberrant, but we believe a portion of this loss activity reflects some recent environmental changes including commercial properties with reduced occupancy and an inexperienced workforce. Consistent with Jack's earlier comments, we are taking actions through pricing, insurance to value adjustments and some targeted underwriting changes. First, with respect to pricing, we achieved Core Commercial renewal price increases of 11.2% in the third quarter, consistent with the second quarter of 2022. Underlying property rate was 7.6%, with pricing up 11%.

We are continuing to seek substantial further rate increases, which we believe will be supported by the market in light of broader environmental challenges and lack of property capacity in the market. We upped automatic statewide exposure increases in many states. At the same time, we're using risk-specific insurance-to-value adjustments to complement renewal increases to certain property risks. Through various exposure adjustments, we've already added $28 million in premiums to date and expect to add an additional $6 million over the next 3 months.

Additionally, we continue to make enhancements to our underwriting strategies. We are tightening criteria within our targeted underwriting risk appetite to restrict new business and renewals in select challenged industry classes and updating underwriting guidelines. In the beginning of the year, we identified approximately $25 million of middle market commercial property business with unattractive characteristics which we have or are planning to nonrenewal from this portfolio. This should improve CMP profitability by approximately 1.5 points next year, all things equal.

We proactively manage portfolio risk in our property book of business through the use of proprietary analytics, risk solutions experts and third-party data, which result's in our ability to identify specific sectors and risk that we exclude from our underwriting appetite on an ongoing basis. Of course, property business is subject to volatility quarter-to-quarter, but we are confident that these actions will improve the underlying profitability of the Core Commercial portfolio. Turning to specialty. This business delivered excellent results for the quarter, while growing at double digits.

Current accident year loss ratio, excluding catastrophes, was 53.6% compared to 52.7% in the prior year quarter from lower-than-expected loss activity in our Marine and Specialty Industrial Property businesses in the third quarter of 2021. Like in other property lines, we are seeing the impact from inflation in this business but it is effectively offset by higher rates, exposure growth and is also helped by a highly diversified nature of underlying risks inside this business.

We have established an outstanding track record in specialty based on a prudent growth strategy, an enviable market position and above target returns. We are very pleased with the current profitability in Specialty underscored by a combined ratio of approximately 89% for the quarter and year-to-date. Turning to Personal Lines. The business delivered a combined ratio excluding catastrophes of 98.2%. And Personal Lines auto current accident year loss ratio, excluding catastrophes, was 78.8%, which is 6 points above our expectations for the quarter based on our updated assumptions exiting Q2.

It was primarily driven by a change in our inflation assumptions on auto property coverages. While used car prices seem to have softened slightly, the increased cost of repairs, specifically parts and labor, along with repair delays, contributed to higher severity in the third quarter. Additionally, in the third quarter, we lowered our subrogation recoverable assumptions for all three quarters of the current year.

Similar to many others, we previously attributed lower subrogation cash flows to delay in payments and turnover in staffing. However, we have seen indications that it is related to a shift in claims mix to a higher proportion of single-vehicle accidents with no subrogation opportunity. Approximately 3 points of the auto loss ratio in the third quarter was attributable to reestimation of first and second quarter 2022 claims, to align with our updated view of ultimate severity and subrogation assumptions.

Rate is the most effective tool at our disposal to improve profitability in personal auto. We took renewal pricing increases of 4.1% in the third quarter and additional pricing actions are already well underway beyond those we discussed in our Q2 call. We expect average renewal premium change of 7% in Q4 and double digits in 2023.

For the fourth quarter, we essentially doubled our rate filing activity as we push through barriers in historically more difficult regulatory states. Our largest markets, including Michigan, Massachusetts and most Northeast states are the most profitable. Our recent upper single-digit rate increases in these states are appropriate, and they will be reflected in our book of business for the next 6 to 12 months.

We will accelerate our rate filings in other states to bring price increases to mid-teens in some of these states with an expectation to increase our overall country-wide renewal premium change in auto to double digits in 2023. The market has clearly hardened in these geographies, and we are confident in our ability to execute this plan. New business pricing is also a critical driver for our auto plan. As we have shared in the past, we achieved aggressive new business increases through the first 2 quarters of the year. The third quarter marked a continuation of the upward trajectory with increases of approximately 12%. Looking ahead, we have increases of approximately 15% planned for the fourth quarter. These meaningful increases, albeit on about 15% of our book should drive about 2 points of the overall earned rate increase next year, contributing to the profitability of the line.

At the same time, we are pursuing non-rate actions to supplement the acceleration of our profitability improvement in auto, including increased nonrenewals, tightening underwriting, around accident and violation history and agent management. In homeowners, inflation-related severity and higher frequency of nonweather-related water losses drove an increase in the underlying loss ratio of about 7 points relative to our updated expectations exiting Q2 to 62.6%.

Increase in severity represented 4 points, which is inclusive of 2 points of first and second quarter claims reestimation. While we certainly expected increased inflationary pressures for the rest of the year, the 20%-plus increase we observed in paid severity in the third quarter was well above our expectation. Additionally, approximately 2 points of the variance was driven by higher frequency of nonweather water claims as the cost of repairs on more routine household incidents increased.

We have seen incidents that previously homeowners took care of themselves now more often result in claims. In response to these trends, we are accelerating pricing increases in homeowners beyond what we discussed in Q2, as evidenced by robust renewal premium change of 12.1% in Q3. We anticipate additional pricing increases of 15% in Q4 and 17% in Q1 2023.

We continue to lean into automatic state-by-state replacement cost increases to achieve the needed exposure changes, which is now about 9% compared to historical levels of 2% to 3%. Additionally, a subset of policies received specific adjustments on top of statewide adjustments. ITV alone on these policies is forecasted to yield up to 2.5 points of incremental renewal premium change for all homeowners over the next 12 months.

As an account writer, we look at overall profitability of the Personal Lines business. We have line of sight to steady improvement in this book of business from the current levels with rapid improvement in homeowners in 2023 and a more paced progression in auto as current and future rate actions continue to earn in, while some of the residual auto frequency benefit reduces from early 2022 levels.

Of course, this outlook is dependent on a more normal historical pace of inflation from here forward. Now moving to a discussion of our balance sheet and investment portfolio. Net investment income was $73 million for the quarter, up $2.5 million sequentially on the strength of higher-than-planned new money yields and increased cash flows.

Partnership income in the third quarter this year was in line with our original expectations despite lower equity multiples and wider credit spreads in the public markets in Q2 of this year, due to a sizable monetization of one of the partnership assets. We will be watching this asset class in the fourth quarter in view of the Q3 public market movements.

The current rising interest rate environment continues to be a very meaningful positive for net investment income over the longer term as the portfolio turns over and is reinvested at higher interest rates. As of today's call, new money yields are accumulating on the order of 300 basis points higher than what we expected in the beginning of the year, adding meaningfully to our fixed income expectation for next year.

Looking at fixed income portfolio valuations, we typically hold fixed income securities to maturity, and therefore, we are not overly concerned with temporary interest rate-driven movements in the market value of the portfolio. The increase in interest rates has allowed us to invest portfolio cash flows at attractive market yields and at higher quality.

The results in the quarter also reflect a nonoperating after-tax charge of $11.3 million of losses on intent to sell certain fixed income securities due to a planned transfer of investment management responsibilities of a small subset of the portfolio to an external manager. In terms of our internally managed portfolio, we have not made material changes to our long-term allocation and remain very comfortable with our positioning.

However, we have reduced duration and improved quality as investments mature. We continue to take a balanced approach, making prudent choices given rising risk of economic slowdown and ongoing market volatility. Looking at our equity and capital position, investment valuations continue to be reflected in our shareholders' equity. Lowering book value per share, 10.5% to $64.59 from June 30, 2022. Statutory capital remained relatively unchanged in the quarter at $2.7 billion, since the end of last year as investment losses on equity securities and a $100 million dividend payment to the parent was nearly offset by insurance company earnings. We remain disciplined and balanced on our capital management priorities and committed to being strong stewards of our capital.

Turning to guidance. We expect full year 2022 combined ratio excluding catastrophes, to be in the range of 92% to 92.5%. Our cat load for the fourth quarter is 4%. This outlook includes a typical seasonal decline in the home loss ratios and an increase in the auto loss ratios all things equal, continuation of loss trend and inflation levels as well as an expectation that some of the large loss experience will reoccur as pricing and underwriting actions are being executed.

To summarize, while considerable Swift changes in the macro environment created an adjustment to our previous short-term trajectory. Our underlying book of business is solid. Our action plan is robust and execution of the plan has our full and undivided focus. At the same time, with the current new money rate for investments so much higher than we had originally planned for 2022. Our investment portfolio provides a meaningful lift to net investment income in 2023 and even higher in 2024. As we look ahead, we are laser-focused on restoring our underwriting margins to target and also on our long-term targets for operating ROE to deliver increased value to our shareholders. With that, we will now open the line for questions. Operator?

Question and Answer

Operator

[Operator Instructions] And the first question comes from Matt Carletti with JMP Securities.

Matthew John Carletti
JMP Securities LLC, Research Division

First question, Jeff, I wanted to go back to your comments on expense ratio and how that to give us 50 bps of improvement is ahead of expectations. Can you expand on that a little bit? Are there some one-timers in there that kind of got you to where you are? Or does it make you -- or is it more sustainable, whether it be premium growth or otherwise kind of the leverage from it that makes you feel even better about kind of the guidance you've given on a go-forward basis being able to achieve it?

Jeffrey Mark Farber
Executive VP & CFO

Thanks, Matt. Notwithstanding the environment for talent and other pressures on cost. I think the earned premium growth that we're seeing in the quarter is really helping us out a lot on the expense ratio. And then on top of that, we had some reduced incentives, both agent and employee in the quarter relative to the current performance. So I think some of that is sustainable and some of that might be viewed as a onetime.

Matthew John Carletti
JMP Securities LLC, Research Division

Okay. Great. And then one more, if I could. Jack, you've spoken in the past about the specialty business, and I'm thinking about how you've had a lot of kind of existing Core Commercial customers that buy a lot of specialty products elsewhere and then that was viewed as a really good opportunity. Could you just update us on kind of the success that you've had there in terms of kind of bringing that package together for a number of customers or if a lot of the growth has been kind of new customers on a stand-alone basis and it hasn't been as successful?

John Conner Roche
President, CEO & Director

Yes. Thanks, Matt. I'll make a couple of comments but I'd love for Bryan to elaborate quickly. Our success in specialty really comes from a combination of both of those dimensions that you talked about. Much of our success comes from small to midsize customers that buy specialty coverages separately, but very much through the independent agency channel direct to carriers. And our operating models and the way in which we work together with our Core Commercial folks in the field is what gives us access to that business. We are increasing our success on cross-sell or multiline exposures. But really, our opportunity going forward is to continue really in both areas. So Bryan, I don't know if you want to say a few more words about that.

Bryan James Salvatore
Executive VP & President of Specialty

Yes, sure. And thanks again, Matt. Yes, so one thing I can share is that within our regions and our underwriting teams, there is an ongoing deliberate effort to bring what we call that total Hanover experience to our customers and agents and we're definitely seeing the progress. One thing that may be worth highlighting is when we think about new product development, that's one of the sort of the central drivers of it, right, is the ability to bring that total Hanover experience. And so just 2 data points, right? Two of our newest areas are retail E&S business and 1/3 of that business is written with customers that are existing Hanover customers. And then our newest area of specialty general liability, 50% of our policies are written with customers of Hanover. So we feel really good about the progress we're making there and then ongoing focus.

Operator

And the next question comes from Paul Newsome with Piper Sandler.

Paul Newsome
Piper Sandler & Co., Research Division

I wanted to ask a little bit for a little bit more color on the -- sort of the change that happened from an inflationary perspective across your book. And is it fair to say that essentially, what happened is that you had an assumption for claims inflation, but it accelerated further than you expected in the quarter, and that's what created the true-ups in the higher levels of expectation for claim perspective. Is that a fair assessment?

Jeffrey Mark Farber
Executive VP & CFO

I think that's pretty fair. Most of it was in auto and home and we had assumptions about gross severity in auto, and we had assumption about subrogation and salvage, and we revised those assumptions. We talked about that earlier in the prepared remarks and that there was a knock-on effect, which needed to be addressed for the first and second quarter. And then in home, it was a combination of some increased severity from materials and labor and things like that. It had its knock-on effect. And then we saw some elevated nonweather-related water type losses. Think about things like toilets or washing machines or other internal things that are leaking and causing damage and basements, things of that nature.

Paul Newsome
Piper Sandler & Co., Research Division

So as we look forward, is your expectations for both pricing and reserving having an expectation that you'll see a moderation in your claims inflation. It sounds like from your comments that, that's the case. Maybe you could talk about why we would see a moderation in claims inflation? And maybe just how much you think that moderation may happen.

John Conner Roche
President, CEO & Director

Yes, Paul, this is Jack. Let me get that response started. I think overall, what you should see is that we're going to exercise the proper level of humility around how the combination of inflation and supply chain and other factors are exacerbating some of the property and physical damage related trends. I think we're much more on top of not only those trends, but also some of the claim mix changes that we spoke to in our prepared remarks, that start to influence the severity beyond just the multiplying effect of inflation and supply chains. So I think we are clearly much more aware of how those -- all those changes are impacting our costs. We're not going to make any predictions about where inflation goes from here. We're going to assume in our pricing and our underwriting actions that the current environment is what it is. And frankly, we have a market by which we can move very, very quickly and enhance our pricing to deal with these at least short-term trends that we're experiencing. So I don't want you to mistake that -- to mean that we're not looking for how those trends evolve from here, both positively and negatively. But our assumptions and our actions right now are that the market where the environment is what it is, and we need to price aggressively to get there. So we have an action plan that's well underway. And our Personal Lines team and frankly, our Core Commercial team on the property side are going at it extremely hard.

Jeffrey Mark Farber
Executive VP & CFO

Paul, Jeff, just to add to that a little bit. So yes, as you know, our action plan is very specific. So we're going after strong renewal price change excellent new business increases, and those are really ramping up and have a tremendous year-over-year impact. We're getting ITV increases and inflation across the book, particularly in home and even in commercial and some selected underwriting actions. So we're optimistic about the trajectory and how we deal with the inflation going forward.

Operator

And the next question comes from Grace Carter with Bank of America.

Grace Helen Carter
BofA Securities, Research Division

The Specialty segment clearly did pretty well in the quarter. It's been doing pretty well year-to-date. I was just wondering if you could help us think through the risk of some of these inflationary pressures that we've seen in other segments start to spill into results in that segment as well? And just any sort of I guess, barriers to protect the margins in that segment relative to recent levels.

Bryan James Salvatore
Executive VP & President of Specialty

Yes. Thanks, Gray. I'll be the first to react to that. This is Bryan. So kind of like Jack mentioned it before, right? Our books certainly see some of the inflationary pressures. That said, it is a really diversified book. And that really helps that sort of sustainability of the results, right? We have 9 different businesses, over 20 different product areas that have a blend, the surety business, the professional liability, the management liability and that diversification has been -- has proven to be very helpful as we confront inflation. So -- but I will add, right, if you look at our rate change, we've been pushing rate change in the last on -- 8 quarters in the 8% range. And that was our being thoughtful about social inflation and trying to stay on top of it. And so we feel good about what we're doing there.

John Conner Roche
President, CEO & Director

Yes. I guess this is Jack. The only thing I would add to that is that when you look inside of our specialty portfolio, not only is it multiple products and multiple businesses. But even in Marine and our HSI business, our specialty industrial business. It's diversified within that and not all of those products and exposures are susceptible to inflation, as you would see, for example, in our Core Commercial business. One area that we pointed out in Core Commercial that is really exacerbating this business interruption exposure, and we really don't have that type of exposure, for example, in our large Marine business that gets exacerbated during this period. So it's a mixture of property and casualty diversification, but as well as different type of property business that resides in our specialty business.

Grace Helen Carter
BofA Securities, Research Division

Thank you. And on the Core Commercial side, I mean, you mentioned the reunderwriting actions going on in that book. It seems to have caused the net premiums written growth to be a little bit lower than the total pricing change that you achieved in the quarter. I guess, just looking forward, how should we think about sort of the top line and that book trend as we think about the tension between ongoing rate and pricing actions? And just the movement in reunderwriting different accounts that might need a little bit of margin help.

Richard William Lavey
Executive VP & President of Hanover Agency Markets

Yes. Thanks, Grace. This is Dick. So when we think about the growth of our Core Commercial business, you really need to think about the two different segments. Our small commercial business has been growing in the low double digits, and we expect that to continue with the investments that we've made in our platform and the engagement we have with our agents. And so that's all systems go. Our middle market book is the book that we've done some underwriting -- re-underwriting in, but it's a small percentage, the $25 million that was mentioned in the prepared remarks, gets at a very targeted segment. We'll -- you should expect to see growth in that segment in the mid-single-digit range going forward. We think that's prudent. We have thoughtful growth plans by geography, by industry segment, so it's very targeted, whereas our small commercial is a broader base set of classe's.

Operator

And the next question comes from James Bach with KBW.

James Paul Bach
Keefe, Bruyette, & Woods, Inc., Research Division

I wanted to go back to the Core Commercial lines pricing acceleration in some cases. I wanted to know across the book, which lines are rate increases are accelerating and outside of workers' compensation, which are potentially slowing.

John Conner Roche
President, CEO & Director

Yes, Jim, this is Jack. I'll just get started and ask Dick to quickly elaborate. I think one of the things we're most proud of is that even I think when many have been talking about Commercial Lines pricing and doing a little but for workers' comp, we really have not done that. We have been able to try to squeak out some pricing in workers' comp and not kind of use that as an excuse because we do believe the workers' comp trends will eventually become more normal, if you will, and you need to be thinking about pricing over those loss trends. That said, I think the biggest difference that Dick can elaborate on is the property coverages, right? We've been getting good solid pricing overall. But as we see the property coverages requiring more and more rate and some additional re-underwriting we're going at it extremely hard.

Richard William Lavey
Executive VP & President of Hanover Agency Markets

Yes. That's exactly right. Our property plan is to lean into those rates across the country both in small and middle market business. I would just say that the market is bearing the kinds of rates that we're putting forward, the retentions look good. So we know that the messaging we're hearing from the reinsurance providers are going to continue to push rate from their end and we'll do the same. So we're leaning into that heart.

James Paul Bach
Keefe, Bruyette, & Woods, Inc., Research Division

All right. And obviously, you cited the accelerating inflationary pressures. And then you also mentioned some caution with respect to medical inflation. I just want to get a sense of on how your views on medical inflation are potentially evolving in light of some of your other views on inflation.

John Conner Roche
President, CEO & Director

Yes. This is Jack, again. I would say that we're watching medical inflation more than seeing any concerning short-term trends. And so clearly, in areas like workers' compensation, we have fee schedules and other things that keep that from emerging too quickly. But in the liability lines, we're watching carefully to see whether there are some adjustments in the medical costs themselves or the types of procedures that end up exacerbating medical inflation over time. But I can't say that we've seen anything in the short term that is greatly concerning, but we've been prudent with our loss picks in both prior year and current year on the casualty lines to prepare for that, James.

Operator

And the next question comes from Michael Phillips with Morgan Stanley.

Michael Wayne Phillips
Morgan Stanley, Research Division

Anything you can share on the specialty side, on a little bit of a modest slowdown in retentions there. Anything I want to seeing you want to talk about?

John Conner Roche
President, CEO & Director

I'm sorry, Mike, you were talking about specialty retention?

Michael Wayne Phillips
Morgan Stanley, Research Division

Specialty retention, yes, yes.

Bryan James Salvatore
Executive VP & President of Specialty

Yes. This is Bryan. To your point, there was a slight slowdown. It's -- we're going to see variance in this quarter-over-quarter. We are watching it very, very closely. As I mentioned before, we continue to think that, that 8-ish percent rate change is appropriate. We continue to first towards that. And then we're just watching what's happening in the marketplace, watching what happens with our retention to see if there's any real slippage. But I tend to look at it -- at the quarter, but also really in the context of the full year. And so right now, I would say, overall, it's holding up pretty well.

John Conner Roche
President, CEO & Director

Mike, this is Jack. I think also -- I think we've said this in previous calls, there are aspects of our specialty book that are kind of anomalous in terms of how retention comes through. So for example, we write a lot of builders risk in Marine, which is not renewable premium surety in the way that, that business gets booked when new bonds are come through for existing customers. That has an impact on renewal retention. So what you'll see overall is that we have really robust retentions in specialty, but because of the nature of the products, they'll come through at a lower retention than, say, a Core Commercial part.

Michael Wayne Phillips
Morgan Stanley, Research Division

Okay. That makes sense. And Jeff, in your prepared remarks, you mentioned I think the phrase was some like you're pushing through some barriers in difficult states. Anything to elaborate there what you meant by that?

Jeffrey Mark Farber
Executive VP & CFO

It's always a process. We've got 20 different states for personal lines and obviously, every state for commercial. But at this point, we're feeling really good about the states that we're in and our ability to take rate, and we don't see any barriers there to get what we need.

Oksana Lukasheva
Senior Vice President of Corporate Finance

All right. It looks like there is no one else in the queue? Mike, what's your last question?

All right. So thank you very much for all of your participation today, and we're looking forward to talk to you next quarter.

Operator
Thank you. The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your lines.