S&P Global
Market Intelligence

The Allstate Corporation NYSE:ALL

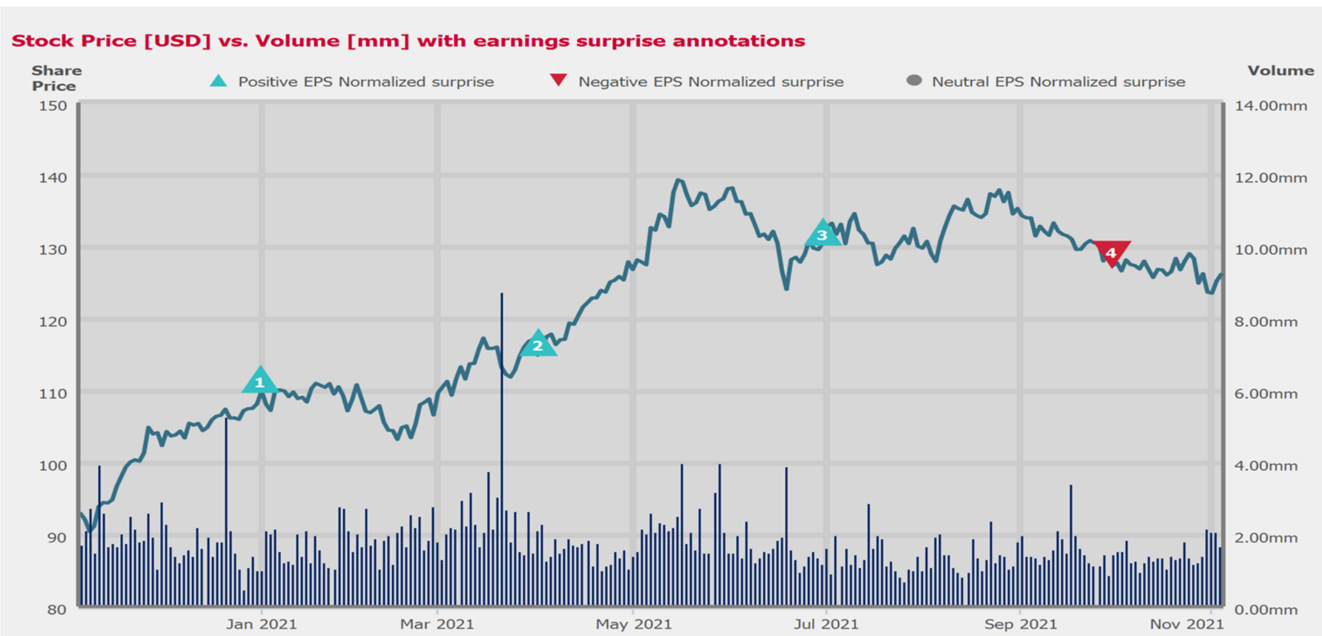
FQ3 2021 Earnings Call Transcripts

Thursday, November 04, 2021 1:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2021-			-FQ4 2021-	-FY 2021-	-FY 2022-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.75	0.73	(58.29 %)	2.48	14.23	NA
Revenue (mm)	10596.50	10615.00	0.17	10557.00	41297.08	NA

Currency: USD
Consensus as of Nov-04-2021 10:28 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2020	3.82	5.87	1 53.66 %
FQ1 2021	3.94	6.11	2 55.08 %
FQ2 2021	3.17	3.79	3 19.56 %
FQ3 2021	1.75	0.73	4 (58.29 %)

Table of Contents

Call Participants

EXECUTIVES

Glenn Thomas Shapiro
President of Personal Property-Liability of AIC

Mario Rizzo
Executive VP & CFO

Mark Nogal
Head of Investor Relations

Thomas Joseph Wilson
Board Chair, President & CEO

ANALYSTS

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

David Kenneth Motemaden
Evercore ISI Institutional Equities, Research Division

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

Joshua David Shanker
BofA Securities, Research Division

Michael Wayne Phillips
Morgan Stanley, Research Division

Presentation

Operator

Thank you for standing by, and welcome to the Allstate Third Quarter 2021 Earnings Conference Call. [Operator Instructions] As a reminder, today's program been is recorded.

would I now like to introduce your host for today's program, 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 Third Quarter 2021 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 and posted related materials to 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 the 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 2020 and other public documents for information on potential risks.

And now I'll turn it over to Tom.

Thomas Joseph Wilson
Board Chair, President & CEO

Well, good morning, and thank you for investing your time with us today.

Let's start on Slide 2. So this is Allstate's strategy on the left-hand side, which we've talked about before. We have 2 components: increase personal property-liability market share and expand the protection solution. Those are the 2 ovals you see on the left with the intersection between them. The key third quarter results are highlighted on the right-hand panel. Property-Liability policies in force increased by 12.5%. Allstate Protection Plans continue to grow rapidly by both broadening its product offering and expanding the network of retail providers. As a result, we now have almost 192 million policies in force across the enterprise.

Financially, the results were more mixed. Revenues were up substantially, but net income and adjusted net income declined from the prior year quarter. Underwriting income declined primarily due to higher loss costs in settling auto insurance claims. We've implemented price increases to proactively respond to the sharp rise in loss cost, and Transformative Growth continues to position us for long-term success, both of which we'll talk about in a couple of minutes. This was partially offset by the benefits from our long-term risk and return programs that include significant reinsurance recoverables. They were primarily related to Hurricane Ida, and a substantial increase in performance-based investment income.

Capital deployment results were excellent, with $1.5 billion of cash returned to shareholders in the quarter. We also completed the divestitures of our 2 largest life and annuity businesses, one in October and then one just earlier this week.

So let's go to Slide 3. Revenues of $12.5 billion in the quarter increased 16.9% compared to the prior year quarter, and that reflects both the higher earned [indiscernible] National General acquisition, Allstate brand, homeowners premium growth and higher net investment income. Property-Liability premiums and policies in force increased 13.5% and 12.5%, respectively.

Net investment income was $764 million, and that's up almost about $300 million compared to the prior year quarter, reflecting strong results from the performance-based portfolio. Net income was $508 million in the quarter, and that's compared to $1 billion in the prior quarter as lower underwriting income was partially offset by the higher investment income. Adjusted net income was $217 million or $0.73 per diluted share, and it's decreased [$683] million compared to the prior year quarter, reflecting the lower underwriting due to the higher auto and homeowners insurance loss costs. Net income for the first 9 months of 2021 was below the prior year, and that's largely due to the loss on the sale of the life annuity business, which we reported earlier in the year. Adjusted net income was $10.70 per share for the first 9 months, and that was above the prior year as higher investment income and lower expenses [audio gap] more than offset higher loss costs.

Let's turn to Slide 4. What I would do is put the pandemic in a longitudinal perspective because this created volatility for our results, and it obviously requires us to adapt quickly, which we do. But before we go through the impact on the third quarter results of the supply chain disruption, let's talk about the initial and subsequent impact of the pandemic. So in 2020, the economic lockdown resulted in fewer miles being driven and promoted -- and prompted an aggressive economic support response from, really, governments around the world. The impact on auto insurance was a dramatic drop in the number of accidents. And of course, due to this unprecedented driver in frequency, we proactively provided our customers with some money back, which increased customer retention.

Since then, since there was less road congestion and fewer accidents that occurred during commuting hours, the average speed and severity of auto claims increased, offsetting some of the frequency benefit. Nevertheless, underwriting margins improved dramatically, so we introduced a temporary Shelter-in-Place payback rather than take a permanent rate reduction and took some modest overall reductions in rate levels.

This year, as you can see from the right-hand column, the story has been just the opposite as it relates to frequency with large percentage increases. And while the overall level of accident frequency for the Allstate brand is still below prepandemic levels, the national and general nonstandard business is back to the levels before the pandemic. Auto severity this year, however, has been dramatically impacted by the supply chain disruption, and price increases on used cars and original equipment parts, and Mario will take you through that in a couple of slides.

From a pricing perspective, this results in moving from modest rate reductions to significant increases in auto insurance prices. From a growth standpoint, at the onset of the pandemic, we began to see a material increase in the consumer acceptance telematics, and we've really leaned into that with our Milewise product, which is really the only national product out there to pay for the mile, and that's led to substantial increase in our telematics product.

Now the pandemic has also had a significant impact on the investment portfolio, and this is the tale of the beginning and the end as well. So early in the crisis, equity valuations were down, and this had a negative impact on investment results. Then, of course, on -- and we have a broad-based long-term spread out over a decade really investing in these kinds of funds. And so we do it on a long-term basis, whether that's 3, 5 or 10 years. But -- so what's happened this year, of course, is we've had the opposite happen, which is with the economic stimulus, we've had equity valuations going up, and our returns have come back strongly.

In the market-based portfolio, lower interest rates at the onset of this pandemic did lead to an increase in the unrealized gains in the portfolio. But of course, what that does is reduce future interest rate income, which you see slight decline in this quarter. And many of our other businesses have been impacted some positively, some negatively, but it's our ability to adapt and seize the opportunities that are presented that create shareholder value.

So Mario will now go through the third quarter results in more detail and how Transformative Growth positions of Allstate for continued success.

Mario Rizzo
Executive VP & CFO

Thanks, Tom. Let's move to Slide 5 to review Property-Liability margin results in the third quarter. The recorded combined ratio of 105.3 increased 13.7 points compared to the prior year quarter. This was primarily driven by increased underlying losses as well as higher catastrophe losses and non catastrophe prior year reserve reestimates. The chart at the bottom of the slide quantifies the impact of each component in the third quarter compared to the prior year quarter.

As you can see, the personal auto underlying loss ratio drove most of the increase due to higher auto accident frequency and the inflationary impacts on auto severity. Higher catastrophe losses shown in the middle of the chart had a negative 1.4 point impact on the combined ratio as favorable reserve reestimates recorded in 2020 from wildfire subrogation settlements positively impacted the prior year quarter.

Gross catastrophe losses were higher but were reduced by nearly $1 billion of net reinsurance recoveries following Hurricane Ida, demonstrating the benefits of our long-term approach to risk and return management of the homeowners insurance business and our comprehensive reinsurance program.

Noncatastrophe prior year reserve strengthening of $162 million in the quarter drove an adverse impact of 0.8 points primarily from increases in auto and commercial lines. This also included $111 million of strengthening in the quarter related to asbestos, environmental and other reserves in the runoff Property-Liability segment following our annual comprehensive reserve review. This was partially offset by a lower expense ratio when excluding the impact of amortization of purchased intangibles primarily due to lower restructuring and related charges compared to the prior year quarter.

Moving to Slide 6. Let's go a bit deeper on auto insurance profitability. Allstate brand auto insurance underlying combined ratio finished at 97.5 for the quarter and 89.7 over the first 9 months of 2021. The increase to the prior year quarter reflects higher loss cost due to higher accident frequency, increased severity and competitive pricing enhancements implemented in late 2020 and earlier this year. While claim frequency increased relative to prior year, we continue to experience favorable trends relative to prepandemic levels. Allstate brand auto property damage frequency increased 16.6% compared to 2020 but decreased 16.8% relative to 2019.

The chart on the lower left compares the underlying combined ratio for the third quarter of 2019 to this quarter to remove some of the short-term pandemic volatility. The underlying combined ratio was 93.1 in 2019, which generates an attractive return on capital. Favorable auto frequency in the third quarter of 2021 lowered the combined ratio by 6.4 points compared to 2019.

Increased auto claim severity, however, increased the combined ratio by 12 points versus 2 years ago, as you can see from the red bar. The cost reductions implemented as part of Transformative Growth reduced expenses by 1.3 points, which favorably impacted 2021 results. As Tom mentioned, early in the pandemic, the severity increases were driven by higher average losses due to a reduction in low severity claims. This year, the increase reflects the impact of supply chain disruptions in the auto markets, which has increased used car prices and enabled original equipment manufacturers to significantly increase part prices.

The chart on the lower right shows used car values began increasing above the CPI in late 2020, which accelerated in 2021, resulting in an increase of 44% since the beginning of 2019. Similarly, OEM parts have also increased in 2021, roughly twice as much as core CPI. This has resulted in higher severities for both total loss vehicles and repairable vehicles.

Since these increases were accelerating throughout the second and third quarters of the year, we increased expected loss costs for the first 2 quarters of 2021, and this prior quarter strengthening shows up in the combined ratio for the third quarter. Increases in report year severities for auto insurance claims during the first 2 quarters of 2021 increased the third quarter combined ratio by 2.6 points, as you can see by the green bar on the lower left.

So let's flip to Slide 7, which lays out the steps we're taking to improve auto profitability. As you can see from the chart on the top, Allstate has maintained industry-leading auto insurance margins over a long period of time, with a combined ratio operating range in the mid-90s, exhibiting strong execution and operational expertise.

To maintain industry-leading results, we are increasing rates, improving claims effectiveness and continuing the lower costs. After lowering prices in early 2021 to reflect in part Allstate's lower expense ratio, we have proactively been responding with increases in the third quarter, with actions continuing into the fourth quarter and into 2022.

The chart on the right provides selected rate increases already implemented in the third and fourth quarter as well as publicly filed rates that have yet to be implemented in the fourth quarter. Those states denoted with the caret are top 10 states in terms of written premium as of year-end 2020. In the third quarter, we've received rate approvals for increases in 12 states, primarily in September. We adapted quickly to higher severities in the fourth quarter, with plans to file rates in an additional 20 states. We have already implemented rate increases in 8 states during the fourth quarter, with an average increase of 6.7% as of November 1. Looking ahead, we expect to pursue price increases in an additional 12 locations by year-end.

We are working closely with state regulators to provide detailed support and decrease the lag time between filing, implementation and premium generation. As we move into next year, it is likely auto insurance prices will continue to be increased to reflect higher severities. We also continue to leverage advanced claims capabilities and process efficiencies. Cost reductions as part of Transformative Growth will also continue to be implemented.

Let's turn to Slide 8 and discuss our expectations and commitment to further improve our cost structure through Transformative Growth. As you can see by the chart on the bottom of the slide, we've defined a new non-GAAP measure this quarter referred to as the adjusted expense ratio. This starts with our underwriting expense ratio, excluding restructuring, coronavirus-related expenses, amortization and impairment of purchased intangibles and investments in advertising. It then also adds in our claim expense ratio, excluding costs associated with settling catastrophe claims, which tend to be more variable. We believe this measure provides the best insight into the underlying expense trends within our Property-Liability business.

Through innovation and strong execution, we achieved 2.6 points of improvement when comparing 2020 to 2018, with further improvement occurring through the first 9 months of 2021. Over time, we expect to drive an additional 3 points of improvement from current levels, achieving an adjusted expense ratio of approximately 23 by year-end 2024. This represents about a 6-point reduction relative to 2018 or an average of 1 point per year over 6 years, enabling an improved price position relative to our competitors while maintaining attractive returns.

Future cost reductions center around continued digital enhancements to automate processes, enabling the retirement of legacy technology, operating efficiency gains from combining organization -- combining organizations and transforming the distribution model to higher growth and lower costs.

Transitioning to Slide 9, let's go up a level to show how Transformative Growth positions us for long-term success and how the components of Transformative Growth work together to create a flywheel of profitable growth. As you know, Transformative Growth is a multiyear initiative to increase personal Property-Liability market share by building a low-cost digital insurer with broad distribution. This will be accomplished by improving customer value, expanding customer access, increasing sophistication and investment in customer acquisition and deploying a new technology ecosystem. We've made significant progress to date across each component.

Starting at the top of the flywheel visual, our commitment to further lower our costs, improves customer value and enables a more competitive price position while maintaining attractive returns. Enhancing and expanding distribution puts us in a position to take advantage of more affordable pricing. Increasing the analytical sophistication of new customer acquisitions lets consumers know about this better value proposition. New technology platforms, lower costs and enable us to further broaden the solutions offered to property liability customers. This flywheel will enable us to increase market share and create additional shareholder value.

Turning to Slide 10. Let's look at the changes to the distribution system, which are also underway. As you can see in the chart on the left side of the slide, Property-Liability policies in force grew by 12.5% compared to the prior year quarter. National General, which includes Encompass, contributed growth of 4 million policies, and Allstate brand Property-Liability policies increased by 231,000 driven by growth across personal lines. Allstate brand auto policies in force increased slightly compared to the prior year quarter and sequentially for the third consecutive quarter, including growth of 142,000 policies compared to prior year-end, as you can see by the table on the lower left.

The chart on the right shows a breakdown of personal auto new issued applications compared to the prior year. [Audio gap] [38%] increase in the direct channel more than offset a slight decline from existing agents and volume that would have normally been generated by newly appointed agents. As you know, we've significantly reduced the number of new Allstate agents being appointed beginning in early 2020 since we are developing a new agent model to drive higher growth at lower cost. The addition of National General also added 502,000 new auto applications in the quarter.

Let me now turn it over to Mark to cover the remainder of the slides before we move to Q&A.

Mark Nogal
Head of Investor Relations

Thanks, Mario. Moving to Slide 11. Protection Services continues to grow revenue and profit. Revenues, excluding the impact of realized gains and losses, increased 23.3% to $597 million in the third quarter. Protection Plans and net written premium increased by $139 million due to the launch of the Home Depot relationship focusing on appliances. Our quarterly net written premium is now 5.5x the level of when the company was acquired in 2017.

Arity expanded revenues due to the integration of LeadCloud and Transparent.ly, which were acquired as part of the National General acquisition as well as increased device sales driven by growth in the Milewise products. Policies in force increased 12.5% to 150 million driven by growth in Allstate Protection Plans and Allstate Identity Protection. Adjusted net income was $45 million in the third quarter, representing an increase of $5 million compared to the prior year quarter driven by higher profitability at Allstate Identity Protection and Arity. This was partially offset by higher operating costs and expenses related to investments in growth.

Now let's shift to Slide 12, which highlights our investment performance. Net investment income totaled $764 million in the quarter, which was $300 million above the prior year quarter, driven by higher performance-based income, as shown in the chart on the left. Performance-based income totaled $437 million in the quarter, as shown in gray, reflecting increases in private equity investments.

As in prior quarters, several large idiosyncratic contributors had a meaningful impact on our results. These results represent a long-term and broad approach to growth investing, with nearly 90% of year-to-date performance-based income coming from assets with inception years of 2018 and prior.

Market-based income, shown in blue, was $6 million below the prior year quarter. The impact of reinvestment rates below the average interest-bearing portfolio yield was somewhat mitigated in the quarter by higher average assets under management and prepayment fee income.

Our total portfolio return was 1% in the third quarter and 3.3% year-to-date, reflecting income and changes in equity valuations, partially offset by higher interest rates. We take an active approach to optimizing our returns per unit risk for appropriate investment horizons. Our investment activities are integrated into our overall enterprise risk and return process and play an important role in generating shareholder value.

While the performance-based investment results continue to be strong in the third quarter, we manage the portfolio with a longer-term view on returns. On the right, we have provided our annualized portfolio return in total and by strategy over various time horizons.

Consistent with broader public and private equity markets, our portfolio has experienced returns above our historical trend over the last several quarters. While prospective returns will depend on future economic and market conditions, we do expect our performance-based returns to moderate in line with our longer-term results.

Now let's move to Slide 13, which highlights Allstate's strong capital position. Allstate's balance sheet strength and excellent cash flow generation provides strong cash returns to shareholders while investing in growth. Significant cash returns to shareholders, including $1.5 billion through a combination of share repurchases and common stock dividends, occurred during the third quarter. Common shares outstanding have been reduced by 5% over the last 12 months.

Already in the fourth quarter, we successfully completed the acquisition of SafeAuto on October 1 for $262 million to leverage National General's integration capabilities and further increased personal lines market share. We also recently closed on the divestitures of Allstate Life Insurance Company and Allstate Life Insurance Company in New York. These divestitures free up approximately $1.7 billion of deployable capital, which was factored into the $5 billion share repurchase program currently being executed.

Turning to Slide 14. Let's finish with a longer-term view of Allstate's focus on execution, innovation and sustainable value creation. Allstate has an excellent track record of serving customers, earning attractive returns on risks and delivering for shareholders, as you can see by the industry-leading statistics on the upper right.

f

Innovation is also critical to the execution, and our proactive implementation of Transformative Growth has positioned us well to address the macroeconomic challenges facing our business today and in the future. Sustainable value creation also requires excellent capital management and governance.

As an example, Allstate is in the top 15% of S&P 500 companies and cash returns to shareholders by providing an attractive dividend and repurchasing 25% and 50% of outstanding shares over the last 5 and 10 years, respectively. Execution, innovation and long-term value creation will continue to drive increased shareholder value.
With that context, let's open the line for your questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Josh Shanker from Bank of America.

Joshua David Shanker
BofA Securities, Research Division

I want to talk about bundles and homeowners and the pricing of the dual engine of homeowners and auto together. I guess there's 2 things I want to understand. One is when a customer sees their overall bundled price going up, what is the conversation like, especially as you're trying to more centralize your business with a greater direct relationship with your customers? And two, given Allstate's geographic footprint, can Allstate add incoming customers for homeowners without changing the cat footprint?

Thomas Joseph Wilson
Board Chair, President & CEO

Josh, this is Tom. I'll start and then Glenn can jump in. First, as you know, we've long been focused on bundling auto and homeowners because those are good, stable, long-term customers. You do get a discount for putting those 2 together. So there's an advantage to the customer from buying it and putting it all in one place besides just having one point of contact. And we've been good at that.

If you look at our growth in homeowners this year, it's higher than our growth in auto insurance, and that appears to be because we are doing more bundling of individual customers. It's a little hard to get the exact attribution, but we feel good about what our agents are doing to drive that.

As it relates to the growth of it, we've been -- we repositioned this business over multiple years back in the middle -- late 2000 -- the first decade of 2000. We've made, of course, a bunch of money since over the last 8 or 9 years, I think almost $9 billion of underwriting income on homeowners, which you need to do because we don't believe that a 4-point margin is attractive on homeowners for a couple of reasons. One is you don't get much investment income. Secondly, you got to put in more capital because the results are more volatile, and you have the big tail losses. So as we seek to grow it, we bring all of that math to bear on individual states is where we grow. And so if there's a state where -- even if there's a fair amount of catastrophe exposure, but we think we can get a good return that's got a margin on it that compensates us for the capital we have to put up and the reinsurance we have to buy, then we'll do that. And we're highly sophisticated in the way we run it. So the geographic focus is really we have a much a highly sophisticated model and do it.

On the direct business, you don't sell as much direct homeowners right now. We still need to crack the code on that. Before I -- Glenn will have some view on how we can continue to run the table in homeowners as we have so far, but the -- an upcoming thing that Glenn might want to touch on is what we're doing in the independent agent channel because of -- the National General platform gives us with our products, our expertise, our pricing, our claims management and our reinsurance programs gives us the ability to really serve a lot of customers.

Glenn, where would you go with that?

Joshua David Shanker
BofA Securities, Research Division

Yes. I just want to say, can you address retention and cat footprint as well?

Thomas Joseph Wilson
Board Chair, President & CEO

Yes. Glenn, why don't you take both of those?

Glenn Thomas Shapiro
President of Personal Property-Liability of AIC

Sure. So a few comments on homeowners leading into it, but we have a really strong homeowners business. And so we want to grow it, and we want to bundle it, as Tom said. So over the course of the past year, we've deepened bundling discounts. So we've made it more attractive for customers across 30 states. We've shifted our agency competition over the last couple of years to where it's more attractive for them to bundle, and the same is true in direct. As Tom said, we're looking to crack the code and write more there. We're writing some want to write more. And so some of the incentives for our direct team are around cross quoting and bundling.

To the point around cat footprint, we're in good shape. Like if you look at our ability to write business, we can write it pretty broadly. We can write in some cat-prone areas, but we tend to offset it and create the diversity of our book by writing in other areas. I mean, right now, we're on a 12-month view right now. We're at 93.8 combined ratio, made about $400 million underwriting profit in the last 12 months in spite of having some really big cat quarters. So it's a good business that we're able to consistently make money in. And so we're looking to grow it. But as Tom said, we have pretty stringent guidelines of where we write, how we write so that we don't overgrow in cat-prone areas, but we're able to grow without that.

And Tom mentioned something that I want to come back to in terms of the breadth of our distribution and growing, and that would be into our IA channel. The IA channel is a huge opportunity. Independent agents were in a lot of homeowners, and our National General and Allstate company as it will be branded is adding our middle market products, both auto and home, and we have sort of a whole new greenfield there to run in, and that would be a broad geographic spread, not just in cat-prone areas.

Thomas Joseph Wilson
Board Chair, President & CEO

Josh, let me just add something because I think I understand why you're trying to triangulate between sort of what's going on in the industry. First, we don't have a catastrophe exposure problem. We don't have a profitability problem, we believe, in homeowners. I mean we only made about -- we lost about [$16] million on $7.3 billion so far this year. So we'd like to make more money. But as Glenn pointed out, when you look over a longer period of time -- we've had a fair amount of ups and downs, but we still made underwriting profit on a sort of 12-month basis. So we don't have a catastrophe problem. So we don't have to restrict stuff and end up with what you're poking at is retention issues.

We have been there and done that, though. So -- and it was called the repositioning we did in the latter part of the decade I mentioned. And when you call a customer and say, I used to have -- used to be insured with us, and now I'm not going to share you with us -- and we're one of the biggest brokers of homeowners insurance product, I think, in the country, maybe [indiscernible] through our advantage. And even when you say to people, here's another company, it has some impact on your auto business so -- because people are like, well, I'll take my business someplace else or competitors decide they want to bundle and they'll go get those customers as well. So we had some issues with auto growth when we were downsizing.

We went down by 2 million policies in the homeowners business over a 4-5-year period. So it does hurt. It's manageable. I can't speak for what our competitors are going to do. What I do know is what Glenn said, which is we've got a good business. We know how to run it. We have growth opportunities, and we're looking forward to serving more customers and make more money for our shareholders along the way.

Operator

Our next question comes from the line of Greg Peters from Raymond James.

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

I'd like to turn your attention to Page 7, and I was particularly struck by your chart where you've identified the rate increases you've deployed and then one's that you're going to be implementing. And I was wondering if you could provide us some perspective on -- given the fact that severity has been so substantial, where you think that's going to go with other states? It feels like this is going to be an ongoing reset of pricing as we go through most of next year. And against that backdrop, just how you think about your competitive positioning when most of the industry is going to be raising rates?

Thomas Joseph Wilson
Board Chair, President & CEO

Let me start and then, Glenn, why don't you jump in on what you're doing individually? So I think you're right, Greg, that there seems to be this -- a threat going through the markets today that this is kind of a once and done. And we don't necessarily see it that way. I mean I think there's -- I'm never bold enough to decide in claims we're ahead of anybody else because, first, that assumes everybody is in the same place. Exactly I assume the same trends are going to happen them. And third is that those trends are going to end. And the answer is we don't know when they will do. What we do know is what we can do differently. And we do know that some of our competitors had frequency increases sooner than we did so that you would expect them to raise prices sooner than we did.

We do think that we have a good plan in place, and Glenn can take you through that, which is to make sure we get attractive returns in auto insurance, which is a key component of what we do in terms of delivering value for shareholders, and we're all over that, and we will go -- we're -- how that will move forward in terms of competitive position, that's also hard to tell. What I do know is that I'm really glad we started Transformative Growth 2 years ago. And so the cost reductions we already have in place certainly have benefited us. It's positioned us to be able to grow through many different venues, so we can dial a growth up if we choose to do that. So I'm really glad we are where we are, and we're positioned to take share in the future, which is, of course, our strategy, but we want to do that profitably.

Glenn, do you want to talk about your plans getting the auto insurance returns back where they have been historically?

Glenn Thomas Shapiro
President of Personal Property-Liability of AIC

Yes. Absolutely. So -- thanks, Greg, and you get a couple of important points that you're right about that everyone or close to everyone is going to have to take rate when you talk about competitive position. So we think about that as part of the process. But this is broad and this is going to be around for a while. Like everything you look at in terms of what the root cause is of severity, which is in its simplest terms, is the price of used cars. I'd like to talk about collision coverage as if the coverage that doesn't really have a policy limit that's stated other than the value of the vehicle itself. So in real terms, our policy limit on that coverage went up by 40-plus percent with no change in premium. And that experience happened to everybody across the industry. So it's a rarity where you have something is clear and clean as that, that is a root cause to your severity changes. So we think it'll be around for a bit, and we're going after rate to address that as one of the levers, and we've talked about our claims capabilities and certainly our expense reductions as other ones.

So in the third quarter, we took 12 price increases that went effective in the third quarter, another 8 in the fourth quarter so far, with more to come. So this is broad, and we'll be doing it just about everywhere. And I think the key from a competitive position is that we made a lot of progress. So our starting point, we made significant progress over the last year with the expenses we've taken out. And therefore, the competitive position we were in improved significantly. Our close rates improved significantly, leading to some of the greater new business that you saw.

And so as we take rates, and others do, it's our goal is certainly to keep that competitive position gain that we've made, but the primary goal is to get our margins back to where they need to be, and that's why we're going after rate, and we're doing it pretty proactively.

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

Great. I wanted to pivot to Slide 8, which is, I think, another really important slide in your presentation, and just to step back and recognize the long-term objective that you've introduced is pretty striking. I feel like when we get to 2024, if you've achieved that objective, that will put you clearly among the leaders in terms of lowest adjusted expense ratio in the marketplace. So I'm sure a lot of thought went into this. Can you give us some more color on where the improvement -- where you're going to get the most leverage in terms of the expense ratio improvements, where it's going to come from? And then I'll -- maybe also include some comments on the advertising expense because that's not included in this.

Thomas Joseph Wilson
Board Chair, President & CEO

Mario, do you want to start with the components of the cost reduction? And then I'll come back to advertising spend?

Mario Rizzo
Executive VP & CFO

Sure. So Greg, thanks for the question and the acknowledgment of the progress we've made. I guess where I'd start is maybe to just kind of go up a level and reiterate again what our objective in reducing costs really is, which is to enhance customer value by improving our competitive price position. And we're going to do that by continuing to drive down the expense component of our combined ratio, which is inclusive of both underwriting and claim expenses.

And to your point, we've made really good progress over the past several years. And in addition to the progress we've made, we've created plans and have line of sight to the additional 3-point objective that we've got by 2024 by focusing on things like digitizing processes to improve efficiency by continuing, as we do that, create opportunity to retire legacy technology to capture the synergies associated with the National General acquisition to continue to drive down distribution costs as we've talked about creating a -- kind of a more productive but lower cost distribution model. So we've got opportunity in both the -- from an operating cost perspective on both the underwriting and the claims side, and we've got a plan on how to get there. And that's why we established the goal. And we think once we can get the additional 3 points out of our cost structure, it's really going to position us well relative to our competitors to have a more competitive price point, to deliver higher customer value and really position ourselves to accelerate growth.

Thomas Joseph Wilson
Board Chair, President & CEO

So let me go to advertising, then let me, Greg, start with we didn't do Transformative Growth because of the pandemic. But boy, I'm sure glad we got started on Transformative Growth than we did because we were able to reposition the brand. We invested over $0.25 billion in repositioning the brand, new advertising, testing out new more sophisticated ways to do it. And we did it when frequency was low. So we were able to use some of that reduction in frequency, the margin it created to invest in long-term growth by repositioning the brand.

When you look at Transformative Growth, it's very simple, right? You get a more competitive price. You have more places to buy it. You let people know about that's the increase in advertising that I was talking about. What we do in the future will be depending how much we want to grow. So as we move forward, I think our advertising will be flat or come down some because we want to make sure we've got the pricing right in the point that came up earlier about the longevity of the -- how long will severity keep coming up. You want to make sure you've got that pricing right before you go out and get that flywheel going by doing more advertising.

That said, we're always going to do a lot of advertising because, as you know, it is a marketing war, really, out there between some of the large players. But the other part that's not as well known is it's getting every bit as sophisticated as auto insurance and home pricing. So you've really got to be good with your math on that. And whether it's upper front or lower front, or getting the right price to the right customer at the right time in the right space is -- it's complicated.

And so the other thing we've been working on is building out the sophistication so that every dollar of advertising investment we spend is well done. The reason we took it out of the expense ratio guidance was because it is more volatile and it'll depend on what kind of growth we're looking to achieve in that quarter. And this is a measure of really how effectively you running the business. Like how are you keeping your costs down for your customers so you can have that competitive price.

Operator

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 was on the growth in new business that you guys saw in direct in the quarter. I know from commentary, you guys started to take place during the quarter and then more is on the comp, but I'm just a little bit surprised with the level of growth you saw there just given the increase in the loss trend that you're mentioning. Can you just expand upon that? And would you expect the new business growth on the direct side to slow as you kind of push for additional rate through the system?

Thomas Joseph Wilson
Board Chair, President & CEO

Elyse, let me give that to Glenn and just -- but Glenn and his team have done a fabulous job in getting us better at direct. So some of the growth that you see is because of the advertising we talked about. Some of the growth you see is we're just getting a lot better at it. And so once we put the Allstate brand on it, and Glenn started to combine our capabilities, we just -- we're getting much more effective at what we closed on the web, what we closed in the call center.

Glenn, do you want to talk about the prospects for direct?

Glenn Thomas Shapiro
President of Personal Property-Liability of AIC

Yes. Yes, I agree with everything Tom just said. I think we've got really nice prospects because I would say we're making up ground in [indiscernible] because we have -- what, we're 20 years newer at doing direct of the Allstate brand than some of our competitors, but we're making up chunks of that capability as we move just 1.5 years into launching with Allstate brand in direct. So the effectiveness of our sales, whether it be our call centers or on the web, it's better. Our marketing sophistication, our partnership with marketing, all of those things getting better, and that helps move it up.

The other thing is, actually, in this price environment that's going to be disrupted, we're likely to see some tailwind in new business but some headwinds in retention because if we were in a situation where we're the only ones taking rate, you might expect the opposite. But with a whole bunch of people having to take rate, that will create a lot of shoppers. It'll create shoppers of our own, too, because it disrupts our own customers. And when people shop, they often find a better price or situation even in a rising environment like this. So there will be a lot of customers shopping ours and other companies. And so it's an opportunity, as Tom said, to leverage what we did and say we're really happy with the Transformative Growth than we did because we have more ways for customers to buy when that disruptive market happens.

Elyse Beth Greenspan
Wells Fargo Securities, LLC, Research Division

And then my second question, just in terms of rate, I believe the majority of your auto policies are 6 months. So correct me if I'm wrong there. But as we think about the rate going to the system, what you've done in the third quarter, the fourth quarter and expectations for next year, how long do you think it will take to get back to your target margins? Is this kind of a 6- to 12-month situation? I know you don't have specific target margins for Property-Liability, we've kind of gone to an overall ROE. But when you think about just putting your margins kind of at an acceptable level, would you think that, that would come over the next 6 to 12 months? Or can you give us a time range there?

Thomas Joseph Wilson
Board Chair, President & CEO

I don't think you can do a time range on it because I don't think we can predict what's going to happen in the future on the inflationary pressures. So what we can do is say we're going to go at this aggressively. As soon as we can get there, that will be when we like we're going to hustle [indiscernible] where, as he said, his priority is auto insurance margins on that part of the business. We've got lots of other priorities we're looking at.

But when you look at inflation, I'm not in the camp that the inflationary that like used car prices are suddenly going to go back down. I think you buy a car for $14,000, it used to cost you $10,000, like you're not thinking it's worth $10,000 no matter what the Fed and everybody else thinks about it being transitory. I think the same thing is true with when you look at parts prices. Parts prices, it's not like the oil market where prices are -- the system is built to go up and down every day. It gets embedded in there. The dealers buy inventory. People, distributors buy inventory. They price it. So we don't really see that being transitory and coming down.

How long it will take to work all the way through the system, what opportunities the OEs will take to push prices further up is really unknown at this part. So it's hard to determine when it will cross. What you do know is, Elyse, that top line is going to keep going up as long as we see movement in the bottom line, and it'll keep going up until the bottom line plans out that make the bottom line being loss cost. And that top line then we'll keep going past that point in time until we get back to the margins. But when we get back to the same underwriting margin on, let's call it, a dollar basis or a percentage basis on auto insurance, you can't really predict until you can have a better handle on where frequency and severity is going to shake out.

Glenn, anything you would add to that?

Glenn Thomas Shapiro
President of Personal Property-Liability of AIC

Yes. No, the only thing I would add would be that the tactical answer on the rates, because completely agree, and we don't know what the bottom line will do exactly. So we'll have to keep moving those and adjust. But the tactical answer on the rates, you're correct, Elyse, it's 6 months in almost all of our states and all of our policies. So it's about 6 months from the effective date to get all customers paying that and then another 6 months from the point they start paying it to where the full premium has been earned for 1 policy period. So you really start to see the effect of the rates starting at the beginning of the year but more impactfully in the second and third quarters of next year.

Operator

Our next question comes from the line of Michael Phillips from Morgan Stanley.

Michael Wayne Phillips
Morgan Stanley, Research Division

I think Glenn answered this question, but I just want to be sure. Going to ask first quarter, second quarter, you were taking some targeted rate cuts, and now you're not. And I think Glenn said the rate increases that are going to continue are going to be I think you said just about everywhere. So I want to confirm that because, I guess, the question would be, how much of an overlap would there be in states where you took previous rate cuts -- pretty recent rate cuts and now moving upward in those same states? Is there overlap there in those states? I'm asking because of what that means to consumer impact on maybe retentions, seeing gyrations down the back up again. And then also kind of if there is an overlap there, kind of what it means for something that Tom said and make sure we have pricing right to kind of confidence around the current rates?

Thomas Joseph Wilson
Board Chair, President & CEO

Glenn, do you want to take that?

Glenn Thomas Shapiro
President of Personal Property-Liability of AIC

Sure. So the short answer to your question would be, yes, there will be increases in places where there were modest decreases. I do think we waited a little while to really see what was happening with the frequency and ensure that it was long-standing, and it has remained a long-standing benefit before taking them. And we were modest in it. We've done some pretty significant givebacks in the shelter-in-place givebacks, which were onetime in that sort of durable discount. Actually changing rates and moving them down, we were more subtle with and more modest with. So I don't think people will see sort of a wild swing down and back up, but they will see it in same states.

And the simple fact is, as you saw on the chart, I believe, is on Page 7, that the used car prices spiked dramatically in the second quarter. And those sites and then people start having claims, and then those claims start to be paid and working their way into the loss cost, and you have this hyperinflationary environment on auto physical damage lines. So it's just the appropriate response at the appropriate time for it, and we'll do everything we can to maintain our retention. It's one of the wonderful things -- one of the many wonderful things about our agency force. Our agency force do a really good job of building relationships and talking to customers through changes in their policies and helping us through things like this.

Michael Wayne Phillips
Morgan Stanley, Research Division

Okay. The second question, kind of a different one then on Arity. I guess I'm curious, how you think about Arity? Do you think of it as either, a, more of a use it for our own pricing and telematics business or that plus kind of formed it off to others and having it more of a income-generating machine? It's still not giving you a lot of lift on that second piece. But do you think of it more that way longer term? We've seen more and more companies kind of go that route, and you're about the only one that isn't that go the route of farming that business off. I mean [Hartford] just announced it recently when they formed it off, and more and more companies are doing that. So how do you think about Arity? Is it more just for your own pricing? Or do you want to have it be more of a, again, income-generating machine as well?

Thomas Joseph Wilson
Board Chair, President & CEO

Michael, thank you for asking about something other than auto insurance margin because we have a lot of good things going in one, which is Arity, which is significant value has been created with Arity, both in the insurance business and outside the insurance business. And I don't think that's been reviewed by any analysts as if it was a separate company. I mean we have 600 billion miles of data. We were a risk score in operation. We help people do marketing more effectively and efficiently. And so we're really building quite a platform that will do a number of things. One is it does exactly what you talked about, which is in the way we started, it was telematics as a service for us. We needed somebody to collect the data. We needed to get a mobile app up. We need to put it in files and be able to do something with it. And so rather than do that inside the insurance company, we decided to do it outside the insurance company because we said this is -- at the point we said, this is basically a service that other insurance companies will need, and we can provide it to them. And we do. So Arity provides that service to some other insurance companies, and we're working to try to expand that effort for them. But it moved beyond what I would just call telematics as a service, help me pull data and figure out what my customers are doing, too.

We started collecting more data from ourselves and built a rating service organization so that we can help other insurance companies use telematics to price your insurance. We believe that they're going to get that capability anyway. So we think that we might as well do it through Arity and capture additional margin rather than just assuming we can take over 100% of the insurance industry by being a leader in telematics, which we are, but we don't think we can get the entire market share. So we created a rating services organization around that. It's then been expanded to include really lead generation because we started collecting more data. So we have data from the Allstate customers. We have data because we have our SDK embedded in other people's [indiscernible]. And we have hard data on -- I think it's over 25 million cars we're pulling every day, really high fidelity data that's in the same format. We also buy data that we're able to combine with that 25 million on an over another 75 million cars. So we're pulling data on 100 million cars per day right now. And so we're building this rating services organization for Allstate and other insurers so that we can not only do telematics as a service, we can do -- we think we can actually work to help people prequalify buyers, and it's called the Arity IQ. So significant value has been created.

I don't think that shows up in shareholder value today because I don't really see any of the analysts really looking hard and saying, what's it worth, but we think it's a substantial value, and we expect to continue to grow that business and expand its total addressable market.

Operator

Our next question comes from the line of David Motemaden from Evercore ISI.

David Kenneth Motemaden
Evercore ISI Institutional Equities, Research Division

I just had a question on I think it was Slide 7 where you show the around 7% rate increase that you are asking for. I guess that feels high to me, just especially considering that the loss ratio, if I take out the reserve charge, was only about 1.5 points higher than the third quarter of 2019 and then also just considering the expense initiatives that you guys have taken to date. I guess my thought was -- I thought that the expense plan would maybe sort of help reduce the amount of rate that you guys would need to take. I guess is that the right way of thinking about it? Or is it just too uncertain at this time and you guys just want to get in front of what might be coming down the road in terms of future loss cost increases?

Thomas Joseph Wilson
Board Chair, President & CEO

It's an accurate call out, David, that the future expense reductions will certainly help us manage profitability, but we're increasing the prices now because we do want to grow profitably. But being unclear as to where this inflation will sort out, we're being what we think is fair and appropriate as opposed to overly aggressive in increasing prices now.

As to the extent in the future, we don't need that as much, and our expenses come down, then we can improve our competitive position, which we've improved our competitive position pretty significantly in 2021. And we don't want to give that up, and we'd like to continue to improve it so we get that flywheel of growth going. But in this case, we're using the expense reductions for future competitive price improvement as opposed to saying we don't need to raise prices because loss costs are going up.

Glenn or Mario, anything you would add to that?

Glenn Thomas Shapiro
President of Personal Property-Liability of AIC

The only thing I'd add is it is pretty easy to get negative rates in approved and in market very quickly. And as we talked about in one of the prior answers, it takes time for them to earn in. So we're projecting future loss costs out over the course of the next year and years and taking rate that we think best reflects our best estimates of what we're going to need to deliver the right returns. So it would be a good situation to get into to where we were -- we slightly overshot and could dial it back. But as Tom said, there's a lot of questions still on where the severity will -- I'm sorry, the inflation to severity will end.

Thomas Joseph Wilson
Board Chair, President & CEO

At some point, Glenn, I mean, look, we need to make money in auto insurance, and we're going to do that.

I think we're out of time. So let me just say, as we move forward, you should expect us, as you've heard throughout this call, to expect to focus on improving the returns in auto insurance. At the same time, we're not letting up on any of the components of increasing our market share in personal Property-Liability or expanded circle protection, all of which we've had really good progress and success in this year and in this quarter. So you should expect us to continue to focus on a broad-based approach to increasing shareholder value.

So thank you for your engagement with us again, and we will talk to 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.