S&P Global
Market Intelligence

Kemper Corporation NYSE:KMPR

FQ3 2019 Earnings Call Transcripts

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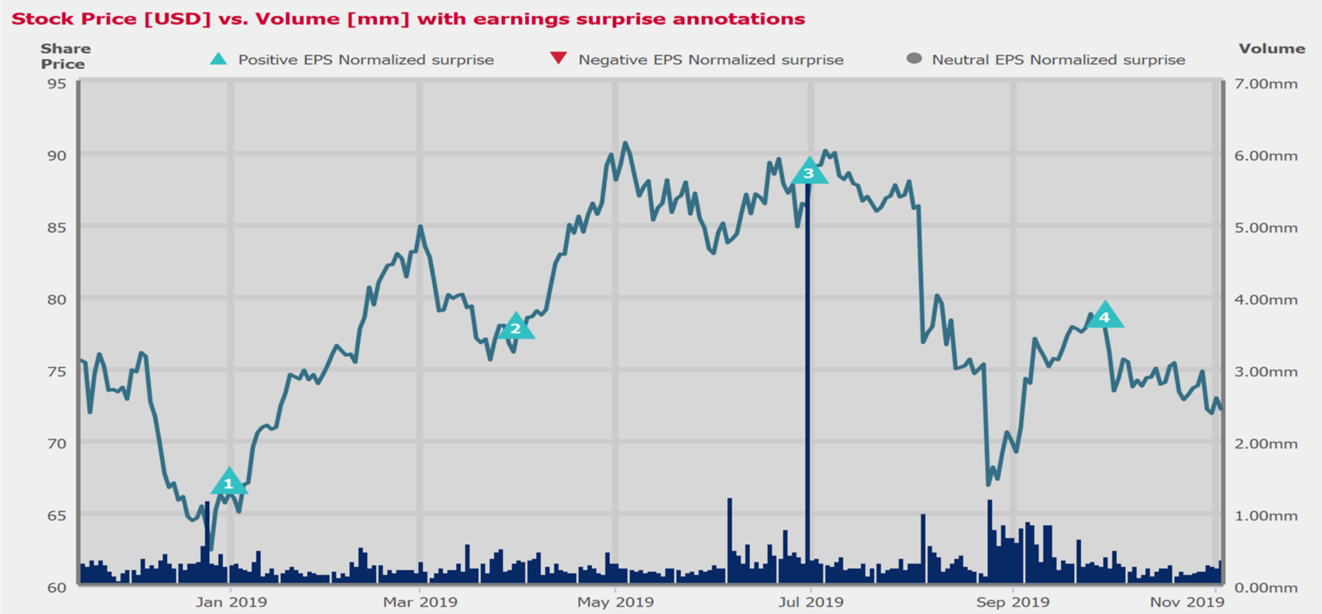
S&P Global Market Intelligence Estimates

	-FQ3 2019-			-FQ4 2019-	-FY 2019-	-FY 2020-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.39	1.93	▲38.85	1.36	5.61	6.02
Revenue (mm)	1223.59	1234.10	▲0.86	1237.88	4909.72	5126.27

Currency: USD
Consensus as of Oct-29-2019 11:14 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2018	0.78	0.91	▲15.19 %
FQ1 2019	1.38	1.50	▲8.70 %
FQ2 2019	1.33	1.38	▲3.76 %
FQ3 2019	1.39	1.93	▲38.85 %

Table of Contents

Call Participants	....	3
Presentation	....	4
Question and Answer	....	9

Call Participants

EXECUTIVES

Christine Patrick
Vice President of Investor Relations

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

James J. McKinney
Senior VP & CFO

Joseph Patrick Lacher
President, CEO & Director

ANALYSTS

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

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

Matthew John Carletti
JMP Securities LLC, Research Division

Seth A. Rosenberg
UBS Investment Bank, Research Division

Presentation

Operator

Good afternoon, ladies and gentlemen, and welcome to Kemper's Third Quarter 2019 Earnings Conference Call. My name is Chuck, and I will be your coordinator today. [Operators Instructions] As a reminder, the conference call is being recorded for replay purposes.

I would now like to introduce your host for today's call, Christine Patrick, Kemper's Vice President and Investor Relations. Ms. Patrick, you may begin.

Christine Patrick
Vice President of Investor Relations

Thank you, Chuck. Good afternoon, everyone, and welcome to Kemper's discussion of our third quarter 2019 results. This afternoon, you'll hear from Joe Lacher, Kemper's President and Chief Executive Officer; Jim McKinney, Kemper's Executive Vice President and Chief Financial Officer; and Duane Sanders, Kemper's Executive Vice President and the Property & Casualty Division President. We'll make a few opening remarks to provide context around our third quarter results. And then we will open up the call for a question-and-answer session.

During the interactive portion of the call, our presenters will be joined by John Boschelli, Kemper's Executive Vice President and Chief Investment Officer; and Mark Green, Kemper's Executive Vice President and Life & Health Division President.

After the market close this afternoon, we issued our earnings release and published our third quarter earnings presentation and financial supplement. In addition, we filed our Form 10-Q with the SEC. You can find these documents on the Investors section of our website at kemper.com.

Our discussion today may contain forward-looking statements. Our actual results may differ materially from these statements. For information on potential risks associated with relying on forward-looking statements, please refer to our 2018 Form 10-K as well as our third quarter 2019 Form 10-Q and earnings release.

This afternoon's discussion also includes non-GAAP financial measures that we believe are meaningful to investors. One such measure that I would like to highlight again is as adjusted for acquisition. It is clearly important to understand our reported results, including the impact the Infinity acquisition has to Kemper overall. However, investors have also expressed an interest in understanding the underlying organic performance of the combined businesses.

Since our as-reported financials don't include Infinity's historical information prior to the closing of the acquisition and our current results include the impact of purchase accounting, the underlying trends are not easily visible.

In an effort to provide insight into the underlying performance of the combined businesses, we also display our financials as adjusted for acquisition. This view removes the impact of purchase accounting and includes historical Infinity information for periods prior to the closing of the acquisition to more easily provide a meaningful year-over-year comparison.

In our financial supplement, presentation and earnings release, we have defined and reconciled all non-GAAP financial measures to GAAP where required in accordance with SEC rules. You can find these documents on the Investors section of our website at kemper.com.

Finally, all comparative references will be to corresponding 2018 period, unless otherwise stated.

I'll now turn the call over to Joe.

Joseph Patrick Lacher
President, CEO & Director

Thank you, Christine. Good afternoon, everyone, and thanks for joining us on today's call. I'm pleased to announce yet another strong quarter of financial and operational performance.

You can see this when looking at Page 4. This quarter, we made $129 million of net income and $136 million of net income adjusting for the acquisition of Infinity, which you'll see on the following slide. These numbers are up 40% and 3%, respectively. This translates on a per share basis to $1.91 and $2.01, respectively.

Additionally, this resulted in a 37% increase in tangible book value per share and a return on average equity, excluding unrealized gains, of 13%. Overall, Kemper generated industry-leading organic growth. We maintained very strong margins, and we strengthened our balance sheet.

Our strategy and business model continue to perform well. The opportunity for expansion within our Specialty auto business remains strong, which coupled with Kemper's diversified business portfolio, should continue to drive industry-leading top line organic growth while producing strong profitability and creating significant long-term shareholder value.

The Specialty P&C segment reported very strong results. We generated 10% top line growth, with accelerating sequential quarter policies-in-force growth. We did this while maintaining an adjusted underlying combined ratio of 91%. We continue to outperform our competition. The strength of our model comes from a specialized and tailored focus on our target customers, a sustainable and expanding cost advantage and increasing product sophistication. These 3 advantages are interconnected. Our success amplifies these advantages and should enable future outperformance.

You can see evidence of this increasing strength and our ability to generate growth across a more diverse set of geographies. This quarter, we had double-digit profitable growth outside of California and it's accelerating. Our combined company platform has created strong opportunities within the Specialty auto market, and we expect that dynamic to continue.

Our Life & Health business returned to a more normal level of earnings and delivered modest growth. The stable cash flows and diversification benefits it provides to Kemper continue to enhance shareholder value.

Our Preferred P&C business turnaround continues despite all of the positive changes we are introducing. Given the modest size of this business, we continue to expect a higher level of ongoing quarterly volatility in both underlying and catastrophe results.

From a financial strength standpoint, we currently maintain roughly $830 million of available and committed contingent liquidity. This liquidity, coupled with our current debt-to-capital ratio of 16.7%, provides us with significant financial flexibility.

We also took action this quarter to further fortify our balance sheet through the contribution of roughly $55 million to our pension, bringing the liability within a fully funded range.

With that, I'll hand the call over to Jim to discuss the consolidated quarterly financial results in more detail.

James J. McKinney
Senior VP & CFO

Thank you, Joe, and good afternoon to everyone on the call. Let's turn to Page 5 to discuss the third quarter financial results. This quarter was another solid quarter for Kemper with top-quartile results leading to strong growth in earned premium, adjusted consolidating net operating income per share and net income per share.

Earned premium grew 7.8% to $1.1 billion. Excluding the impact of purchase accounting, net income per share was flat and adjusted consolidated net operating income per share declined 8%, which when normalized for onetime discrete items, would have increased 22%. We will discuss this point in more detail on the next page.

These numbers drive ultimate shareholder value creation, reflected in this quarter's 21% growth in tangible net book value per share, excluding net unrealized gains on fixed maturities, and a 20% return on tangible equity.

Turning to Page 6. I'd like to remind you that the third quarter of 2018 was positively impacted by a partial satisfaction of an arbitration judgment and the benefit from tax reform. Excluding those items and a few discrete items in 2019, adjusted consolidated net operating income grew by a robust 22%.

Moving to Page 7. Here, we isolate the key sources of volatility in our earnings. Adjusting for these sources of volatility, our underlying operating performance continues to increase substantially over the previous year. The combined company operating platform is helping to drive strong shareholder value creation. This is largely a result of market share gain and strong profitability related to our Kemper Auto platform.

In addition, we are pleased with the increase in Life sales and the long-term stability of the cash flows this provides our operating model.

I'll now turn the call over to Duane to discuss the results of our P&C segments.

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Thank you, Jim, and good afternoon, everyone. Let's start with the Specialty P&C insurance segment results on Page 8. Our top line continues to see strong growth. Earned premiums increased to $783 million for the quarter, up 10% over the third quarter of 2018. Policies-in-force increased 7%, demonstrating Kemper's leading competitive position within the Specialty Auto market. Our third quarter year-to-date as-adjusted underlying combined ratio was 92%, a 1 point improvement over the 6 months ended June 30.

As Joe mentioned earlier, we are outperforming the competition. We believe this is driven by the 3 interconnected strengths of our model. First, our Specialty market focus targets a combination of nonstandard and Hispanic customers and customers in challenging geographies. Our deep understanding of their needs and the nuances that drive success in these markets provide a competitive advantage.

We're also a low-cost provider, focused on achieving expense efficiencies and effectively manage loss costs, which are our products' ultimate cost of goods sold. This is combined with leading product sophistication, which allows us to more accurately price within our Specialty markets.

We are more fully realizing the benefits of our franchise as these distinct advantages mutually strengthen each other and deliver a systematic, sustainable competitive advantage, and enable us to continue to drive industry-leading results.

On Page 9, you can see the results of our Preferred P&C Insurance segment. Earned premiums were $191 million for the quarter, growing 4% over the third quarter of 2018 primarily reflecting the impact of rate actions taken over the past year. The underlying combined ratio for the quarter was 95%, up slightly from the third quarter of 2018.

Turning to catastrophes. Many of our competitors reported elevated losses this quarter. Our experience, however, was relatively benign, reporting $12 million in losses compared to $18 million in the third quarter of 2018. This quarter is another example of what we've noted in the past. Based on the size and distribution of our book, combining overall industry losses and market share is not a good predictor of our catastrophe results.

This quarter also included a benefit from the negotiated sale of our subrogation rights from 2017 and 2018 California wildfires, which was recognized as $15 million in favorable prior year catastrophe development. While underwriting results in this segment remain below our profitability goals, we expect improved actions in claims, pricing and underwriting will move us towards our desired results.

I'll now turn the call back to Jim.

James J. McKinney

Senior VP & CFO

Thank you, Duane. Our Life & Health division's results are on Page 10 of the presentation. Our continued focus on improving distribution capabilities resulted in earned premium growth of 2%. This quarter, the operating profit for the business returned to more typical levels with a benefit expense ratio within a normal range of volatility.

During the quarter, we released $15 million in reserves related to ongoing outreach efforts in our Life Insurance policy payment claims process.

Turning to investments on Page 11. Our portfolio remains diversified and highly rated, as demonstrated on the bottom left of the page. Looking at the chart on the upper left, you can see the investment performance over the past 5 quarters. This quarter, we produced $92 million in net investment income, largely in line with our performance in the third quarter of 2018. The liquidity that our operating model creates from the Life Insurance business permits us to match-fund P&C liabilities. The net result is a decrease in short-term portfolio yield volatility and its corresponding impact on net investment income. The pretax equivalent annualized book yield of 4.4%, down from 5.2% in the third quarter of 2018, is due to a shift in asset mix in connection with the addition of the Infinity portfolio.

Also, we increased our investments in corporate-owned Life Insurance. This contributed $3 million through the other income line compared with $1 million over the prior year. This allocation enhances investment returns with attractive risk characteristics, and an example of how we continue to evaluate all options to maximize shareholder value.

On Page 12, we highlight our strong capital and liquidity position. In the third quarter, operating cash flows increased $22 million to $367 million compared to the third quarter of last year. Our increased scale and disciplined operational and financial management continue to enable these results.

Turning our attention to the chart in the upper right of Page 12, you can see that our insurance groups are well capitalized. In the upper left-hand corner, we present parent company liquidity. At quarter end, we had substantial financial flexibility, with $169 million in cash and investments and $660 million in borrowings available from our revolver and our subsidiaries.

Our debt-to-capital ratio was 16.7%, somewhat below our normal range. The combination of all of these items provide substantial flexibility to support continued growth and shareholder value creation.

With that, I'll turn the call back to Joe for closing comments.

Joseph Patrick Lacher
President, CEO & Director

Thank you, Jim. I'd like to take a moment to note the other press release we issued today. When I arrived at Kemper 4 years ago, we needed to fix a number of things in the organization and needed the talent to get moving on those fixes quickly. Mark Green was one of the first people we brought on board, and he took on 2 core responsibilities: leading the Life & Health division in a broad business development role. We've now reached the point in our evolution where each area will benefit from focused leadership. As such, I'd asked Mark to assume a new position with responsibility for business development and reinsurance. This role leverages Mark's strong entrepreneurial background and many of the skills he's developed over his career. He'll continue to lead the Life & Health division while we search for a leader in that role. I greatly appreciate Mark's efforts over the past 3 years, and I look forward to continued success.

In conclusion, this quarter demonstrated the continuation of our focus to build Kemper's overall value. Our profile of specialized businesses continues to produce revenue growth, solid earnings and attractive shareholder returns.

Thanks to the ongoing efforts of our committed team, this quarter's results confirm that our strategy and business model continue to perform well. We're expanding Kemper's reach in our ability to serve specialty markets with easy-to-use, affordable and appropriate insurance and financial solutions.

Now we'll turn the call back to the operator to take your questions.

Question and Answer

Operator

[Operator Instructions] And our first question will come from Greg Peters with Raymond James.

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

I had a couple of questions. First of all, just stepping back from a big-picture perspective. I think it would be appropriate for your management team to weigh-in on some of the frequency and severity trends that we've heard others comment on, both in California and outside of California. And Joe, maybe you can dovetail that with your comments and clarification around your growth outside of California and Specialty P&C.

Joseph Patrick Lacher
President, CEO & Director

Sure, Greg. I'll take a shot at it, and then we'll see if anybody else wants to add on top of it. And I'll do them almost in reverse order. Our growth outside of California has been a strategic focus of ours. It's not that we don't like California, we do like it. We continue to perform well there. It's an important state for us, and we continue to grow inside of California. We saw a distinct opportunity to take the strength of our franchise and grow outside of California, and have been doing that. We described that -- prior to the Infinity transaction, after the Infinity transaction, it's been a focus of the organization.

One of the things we expect, it might take a little bit of time after the transaction to fully realize some of the internal synergies we needed to get, not expense synergies, but capability synergies. And we're seeing those bear fruit and come to fruition, and are excited about that growth opportunity, again, outside of California. It's got nothing to do with not liking the state.

Relative to -- I'm sorry, go ahead.

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

Is that -- is the outside of California -- I'm sorry, to interrupt you, Joe. That was rude, but...

Joseph Patrick Lacher
President, CEO & Director

No. Go ahead, Greg. I was shifting comments, so go ahead.

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

Yes. I just wanted to clarify. Is that within existing geographies? Or did you -- are there new geographies involved?

Joseph Patrick Lacher
President, CEO & Director

It's largely existing geographies with the definition that they were existing at either Kemper or Infinity prior to the transaction. But in some cases, they were relatively newer states. We've got significant growth in Florida and Texas. We've also got very significant growth in Georgia, to lesser degrees, Louisiana, Arizona, some other spots around that. So we're seeing that it's not just one state. All of those states had activity begun prior to our transaction with affinity -- Infinity, someone more sizable than others. And as such, the smaller ones are having much bigger growth rates, but it's more than one. And I think that answers your question.

Charles Gregory Peters

Raymond James & Associates, Inc., Research Division

Yes, it does. You were going to do a little bit more on frequency and severity, I think, though.

Joseph Patrick Lacher
President, CEO & Director

Yes, frequency and severity. In general, we're seeing similar trends to what people are describing, other folks have described on frequency. We're seeing modest upticks on severity, a little more in California, a little more in BI. We're not particularly seeing anything that I would describe as crazy outsized. We've seen a lot of folks talk about social inflation, and that's interesting. A lot of folks jumping on the bandwagon. We're just not seeing it run through our numbers to the point where we would have looked to coin a phrase and blame it on something. It's just a little normal uptick that's running there.

We believe that, perhaps, if other folks are seeing it and maybe why we're not, our specialized focus might have a customer group that's a little less exposed to it. We've got a lower limits profile. There may be any number of reasons that have us seeing something a little different, but it wouldn't be something we would have poked at to highlight.

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

Got it. Got it. Just another follow-on on the Specialty. The improvement was violent and substantial. I think somewhere in your comments, one of you mentioned the possibility for volatility going forward. And also, maybe you can dovetail that in with comments around where are you on the cost savings? I think it said 80% of your cost savings have been achieved, et cetera.

Joseph Patrick Lacher
President, CEO & Director

Okay. So help me understand, Greg. So either we got a little background noise or I got lost in your question. I thought -- the volatility comment we were describing was relative to our Preferred business which is smaller. You -- what were you asking about Specialty?

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

The -- there was a violent improvement in the results. And so I guess, ultimately, what I'm looking for is the sustainability of these results going forward.

Joseph Patrick Lacher
President, CEO & Director

So which results are you specifically pointing? Are you looking at the underlying combined ratio on Specialty?

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

Yes. That's exactly where I'm focused.

Joseph Patrick Lacher
President, CEO & Director

Hey, Greg. And -- we highlighted this last quarter and we'll highlight it again this quarter. I think the way to read the numbers is to look at the year-to-date numbers for the loss picks and the other elements. You've got a little bit of intra-year development, favorable intra-year development that's rolling through the quarter this quarter. Doesn't overly change what our loss pick is for the entire year. You're seeing -- if you go to Page 36 and 37 of the supplement, or 37 and 38, relatively in line with year-over-year results and relatively in line with kind of first quarter picks. So not a whole lot of volatility. It's just about how that intra-year rolls through.

And really, to put a really fine point on it, Greg, in the second quarter, we thought we were seeing a little bit of a temperature for the year. You got a little bit of intra-year development from the first quarter and we were wrong, and so you get the positive version of that in the third quarter. So the year-to-date number is really the right way to look at that. And if you think of those together, what you see is a fairly consistent view on profitability throughout the year.

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

Right. I'll [indiscernible] kind of [indiscernible] Page 37 or 38, you had...

Joseph Patrick Lacher
President, CEO & Director

You're breaking up a little bit, Greg. Can you restate that?

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

I'm sorry, I think [indiscernible] those questions.

Joseph Patrick Lacher
President, CEO & Director

37 and 38 will show you, if that was your question.

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

Yes.

Joseph Patrick Lacher
President, CEO & Director

Greg, there, just to highlight, your as-adjusted numbers for the 9 months are 92.5% and 91.7% for the quarter. If you look at that relative to prior year of 92.6%, relatively flat when you're thinking about the Specialty Auto business. If you include CV in the results on a year-over-year basis, we've improved roughly 1 point in terms of the total combined ratio. Pretty steady.

Operator

And our next question will come from Paul Newsome of Sandler O'Neill.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

Congratulations on the quarter. I was hoping we'd just give a little bit more color on the competitive environment in both the nonstandard auto business as well as the Preferred, maybe if there's any contrast between the 2.

Joseph Patrick Lacher
President, CEO & Director

So you're a little faint, Paul. I think what you said was looking for color commentary on the competitive environment on separately nonstandard and Preferred and a recognition that they were likely different competitive environments, and just confirming that.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

Yes. Sorry about that if I'm...

Joseph Patrick Lacher

President, CEO & Director

No problem. No problem. Duane, you want to take a shot?

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Yes. Got it. Thanks, Joe. So I'd say on the Specialty side, I would -- first, between the 2, I'd say they're very different because your players in both of those spaces are primarily different players. But on the Specialty side, it's -- it is a dynamic that changes across from state to state. And you'll see -- we'll take Florida, for example, you'll see some competitors that have not had good results or taking significant rate increases, others that have done well, introducing new products. So there's a lot of variation across that.

But no -- outside of maybe just a few, no real large swings. It's -- I'd say, it's nuanced and it's marginal up and down. And then, of course, inside the Preferred space, you've got a lot of sophisticated players there. And again, based on limit distribution and the things that Joe mentioned where some of that social trend kind of activity is taking place, you might see a little bit more than what we're finding and where Specialty products are -- have a lower [limit] distribution and may not be seeing as much of that adverse impact.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

Great. And just a quick -- did you fully book all of the subrogation right -- returns from the wildfire? Or is there a piece that may come later?

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

No. That's the full net impact results that we're expecting to receive, Paul.

Joseph Patrick Lacher
President, CEO & Director

Paul, just to touch just one second on -- and to add a little bit to Duane, when he transitioned. One thing that I think to highlight in terms of that competitive environment, and as Duane kind of said, relatively stable from what we've seen kind of in the past and the other, I think what's important to point out is that our relative competitive strength as a company had increased during that period of time, both because of the scale that we have, our loss cost management capability, our product sophistication and just our overall cost discipline, and the net result to that is I think you're seeing us continue to be an increasing force with -- inside this space. And I think it's important to look at it on that relative basis versus just purely what the competitive environment is on its own.

Operator

Our next question will come from Seth Rosenberg of UBS.

Seth A. Rosenberg
UBS Investment Bank, Research Division

Couple of questions for you. So -- and maybe this dovetails with what Greg was asking in Specialty, on the frequency and severity. But looking at the results you had in Commercial Auto this quarter, they are very strong, you're not seeing any of the same trends that others are talking about in regards to attorney involvement and higher severity there? Maybe you can remind us what's in that book?

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Yes. I would say, yes. I think the descriptor that we gave and as Joe kind of explained, that is consistent. Our profile there, too, is very similar to what we've -- to what we write on the Specialty side. So I think -- again, we're not immune to it, but certainly, the activity is more prominent where you've got bigger limits. And we're -- we don't have fleet business, it's a 1, it's a 2-car, it's an artisan contractor with a pickup truck. So we're finding ourselves in a pretty good spot right now. Again, I'm not telling you we're immune to it, but everything we're seeing today, we're not -- that's not showing up.

Joseph Patrick Lacher
President, CEO & Director

We manage the book, Seth, as much more like a personal lines book of business, given that they're 1, 2, sometimes 3 vehicles and we run it and operate it that way. Where some of the broader industry might look at commercial vehicle, and they're thinking about it as a big commercial auto policy, where they're either fleets or there's bigger books and they're trying to do individual account underwriting. And it's just a different way of selecting the risks, pricing and limits profiles and produces a different result. We're highly confident that we can continue to achieve these results because of the way we're managing the business and selecting the policies and the customers. And it, to some degree, is a different market than the [GU] that you see when you just look at a stat line of commercial vehicle.

Seth A. Rosenberg
UBS Investment Bank, Research Division

Got it. Makes sense. And then it looks like it's small in terms of discount, but just thinking about the sale of the classic auto book. How should we think about that moving forward? I mean does that have any material impact on to the loss ratio versus expense ratio mix?

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Minimally at all. I mean it's a $16 million book. We cease to write new business on -- actually, November 1, renewals will start to transition out March 1. And again, it's a very minor percentage of the -- to the book overall.

Seth A. Rosenberg
UBS Investment Bank, Research Division

Got it. And then just one...

Joseph Patrick Lacher
President, CEO & Director

If I can follow on it. The -- you're asking a great question, and I think Duane highlighted it well, to answer your specific question on sort of its impact on the numbers. The bigger issue is just how do we think about things strategically. We looked at that business and we said we're pretty good at it. We're making a reasonable margin. But when we looked at it, we said it's not better with us than it would be somewhere else, moving that business to Hagerty, probably did a better job for customers. They were going to do a better job with it overall. And our ability to create a specialty there, we weren't going to generate long-term outsized growth and shareholder value creation. So it was more of a hobby for us than a strategic focus. So it was time to let it thrive with somebody else. The bigger item there is less what it does to our numbers and more how we think about the strategy.

Seth A. Rosenberg
UBS Investment Bank, Research Division

Got it. It makes sense. And then just one last one, if I can. So I thought you made a good point that given the makeup of the book, it's not really effective to look at state geographies when you're thinking about cat losses. So just any early indications on how you guys are thinking about the fourth quarter wildfires in California?

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Yes. This is Duane. Yes, I would say they're within expectations. We're not seeing anything outsized there in terms of either count or size in terms of the individual losses. So nothing really to report.

Operator

[Operators Instructions] And our next question will come from Christopher Campbell of KBW.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

So a quick question for you guys on the P&C expense ratio. It looks like that's normalized, and you guys aren't seeing as much of the [BI] gap stuff in there year-over-year. Now should -- it looks more normal where I would expect it. So is like 17% to 18% like a good way we should be thinking about that going forward?

James J. McKinney
Senior VP & CFO

Yes, I think that's a reasonable expectation. And to your point, we highlighted both at the time of acquisition, and then in subsequent quarters, that there was a really quick runoff of kind of the ROBA amortization just due to the overall policy life of the book of business as a whole. I think you'll see that, both again in Pages 37 and 38. I think the expense ratios that you're referencing, kind of that 17%, 18%, is a reasonable range to kind of think about what's a normal kind of expense load for us to incur.

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Yes. There's, I think, Page 20 as well and the supplement will give you some insight on that, too.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Great. And -- sorry, go ahead.

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

No. That was it.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Great. And then I mean should we expand -- I mean, as you're growing that, like what would be the potential like upside for like scale-driven economies on that number? Or is that pretty lean where you're at right now?

James J. McKinney
Senior VP & CFO

Chris, I would highlight, it's fairly lean. Obviously, there'll be additional dollars that we get. But in terms of -- on a ratio basis, it's impacting -- thinking about an additional 1 point or 0.5 point, if you're just kind of thinking about a book of business that's over $3 billion, that would be a $30 million-plus number to kind of move that point. I think you should think about it more as kind of the incremental dollars that we'll add. So if there's 5, 10 over time, we'll accrue those things. But in terms of that having a 0.5 point, 1 point impact on the ratio, I wouldn't -- I'm not forecasting that. I think you should really think about it in that 17% to 18% type range.

Joseph Patrick Lacher
President, CEO & Director

Said differently, Chris, at this point, we think that's a very reasonable range and we've got attractive margins. If we were to find more expense savings and synergies, we would likely be deploying that into growing the business rather than expanding the margin because we believe that growing the business at those attractive margins grows earnings per share and grows book value per share and creates more shareholder value than it would be to be pushing the margin down. And when we do that, that ratio may move around a little bit based on how we're dealing with pricing. But we're at a point where we believe shareholder value creation is by expanding -- is best served by expanding our growth in these margins. So I would encourage you not to be trying to model that expense ratio going down because it's just not how we're thinking about driving the business. It may as we work mixes of different things, but the primary goal is the growth piece at these margins.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. That makes sense. I'm sorry? Okay. Well -- and then dovetailing on the growth, right? So the earned premiums are up by $70 million in that segment but then the noncat loss ratios or like the current accident year loss ratios are down 20 bps. Now I would have expected there to be kind of a new business penalty. So I guess, like what's the dynamic happening there? Were you able to grow premiums by like 10%? And then you're getting lower on accident year margin.

Joseph Patrick Lacher
President, CEO & Director

I think, Chris, you're hitting right on the fact that we've got an attractive business model. And Duane sort of went through those points, the specialized focus, being good at the target customers, being good at our target geographies, bringing on the benefits of scale into our product sophistication, the sizable expense advantage we have now and it's increasing, our ability to do a better job on loss cost management. Every one of those items works together to allow us to be a stronger organization, and that allows us to generate stronger growth and do that at attractive margins. All of those things play together. And once you have the advantages, it allows you to accelerate.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Got it. And then if I'm just thinking about like your target market, I mean are there areas where you're starting to get saturated? Or is there just that much like greenfield ahead of you? I guess I don't really have like a good way of like thinking about the nonstandard market in some of your geographies, and like what your market share is versus what the potential could be.

Joseph Patrick Lacher
President, CEO & Director

I think probably we're at a point, Chris, when we sit and look at it, we can ride this horse for a long time. We are very thoughtfully growing outside of the California where you might have looked and said, "Boy, that's where we might have the most concentration." We're leveraging our strengths to grow outside of those geographies and continuing to be successful there. I think we're probably a long way from being capped out on growth at our size. Give us $25 billion or $30 billion, and I'll start worrying about it.

Christopher Campbell
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. Perfect. And then just one last numbers' question on the Preferred P&C auto piece. The underlying combined ratio was up 250 bps year-over-year. I guess any color on what's driving that?

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Yes. This is Duane. Yes. And I think there, you're seeing a little bit of pressure on the new business side. As you recall, we've introduced a new platform and new product. We actually rolled in our last product in May of this year. So we're now in everywhere we're going to be in. And of course, now that it's in, we got to go back and we're going to dial it in. So we've got a little bit of new business penalty that's in there, and the gang's working hard in terms of understanding what those drivers are and making those corrections.

Joseph Patrick Lacher

President, CEO & Director

It really is a perfect example, Chris, of the 2 questions in combination where that Preferred business, we're still working on enhancing our capabilities there, and we don't have the same strength of competitive advantages that we do in Specialty. And the new business penalty you'd expect to see, you're seeing there, and it will work its way in. We've got a longer average customer life. So we've got a longer period of time for that to work its way through. So we can get comfortable that, that may be a value-added transaction over the long term. But you're seeing the real strength of the Specialty franchise when you compare the 2.

Operator

Our next question will come from Matthew Carletti of JMP Securities.

Matthew John Carletti
JMP Securities LLC, Research Division

Just a quick one. A follow-up, I think, on Chris' last question there. Joe or Duane, can you kind of pull in Preferred together. Can you give us an idea of kind of, in the old proverbial baseball analogy, kind of what inning are we in? Or kind of how should we think about how much progress has been made, how much more kind of path there is ahead to where you get to a point that you feel you have those competitive advantages, and the business' kind of run rate?

Duane Allen Sanders
Senior VP and President of Property & Casualty Division

Yes. Good question. I think from the -- in terms of the efforts and the progress, I'd say we've made some huge strides, albeit in terms of getting it to where we want it, I would -- I'd say we're probably in the middle innings, the fourth, fifth inning of the game with more work to do. I think any time you launch a new product, and Joe mentioned on an annual policy basis, you've got to get market feedback and you've got to get results. And so we're still truing those up. But with what we've done in terms of the build, the segmentation and all the effort that went in to get it into the marketplace, we now have more insight in terms of what we need to do, and that's where we're spending our time.

Joseph Patrick Lacher
President, CEO & Director

When we put the -- we dealt with the issues early on, Matt. The first thing the business needed was a different policy administration system. And you've been following the organization long enough to recall that the company had written off its first version at a more sophisticated policy administration system. Fortunately, we've recovered most of that from our arbitration award. So that -- but we didn't recover the time. We've put in Guidewire as a policy administration system. That enables us to be much more nimble and much more effective. That had to be done before we could start deploying some of these capabilities, so that's in. We've taken a first shot in our new and updated product and are having the new business penalties we would normally expect running through. We're having the disruption that occurs when you normally convert programs from one rating system and one rating program to a new system and a new program. So that's running through right now. We expect that to take probably another 12 months to get through the system.

And we will continue to improve our capabilities inside of that space. We're going to get, hopefully, some tailwind help from the claims side because we use parts of our claim department between Specialty Auto and Preferred. We clearly have a focus on some parts of this that are Specialty, and some that are uniquely Preferred, but there are some pieces like the physical damage adjustments when you're dealing with the metal on vehicles, that very much works back and forth between the 2 groups. Some of that scale advantage that we're getting and strength in the Specialty side will have a halo effect and eventually work its way into Preferred. And as Duane said, it just moves a little bit slower with 12-month policies.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Joe Lacher for any closing remarks.

Joseph Patrick Lacher
President, CEO & Director

Thank you, operator. And thanks, everyone, for your time today and your interest in Kemper. We look forward to speaking with you again next quarter. Thanks.

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