S&P Capital IQ

CONTENTS

The Hanover Insurance Group, Inc. NYSE:THG

FQ4 2014 Earnings Call Transcripts

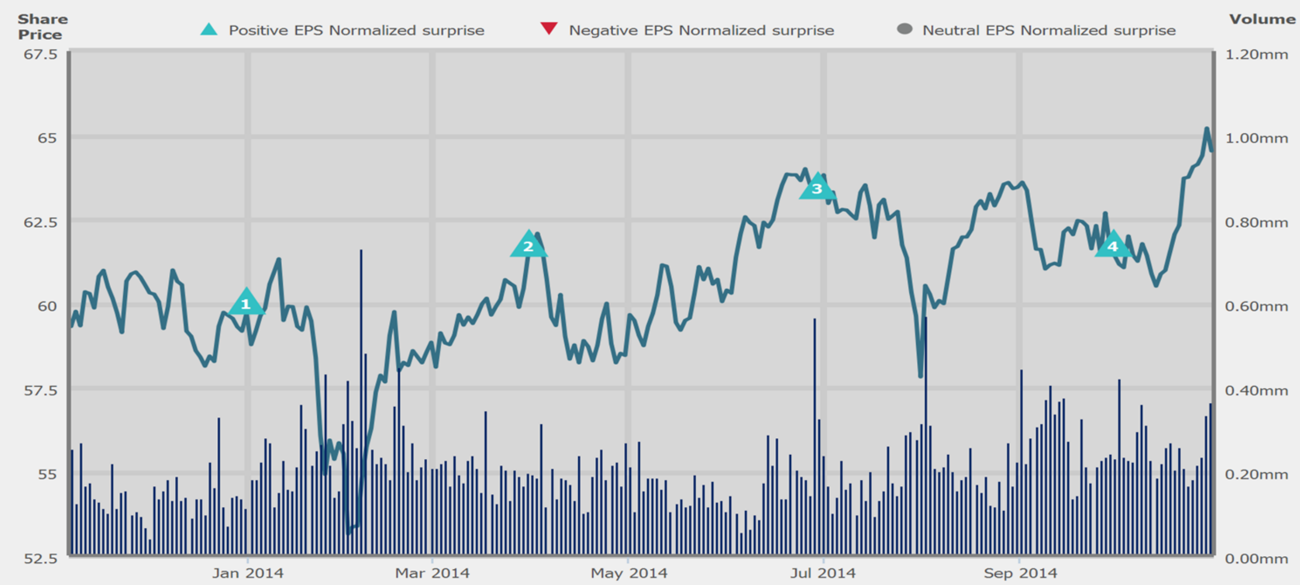
Thursday, February 05, 2015 3:00 PM GMT

S&P Capital IQ Estimates

	-FQ4 2014-			-FQ1 2015-	-FY 2014-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	1.50	1.77	18.00	1.44	4.91	5.19
Revenue (mm)	-	-	-	1205.60	-	-

Currency: USD
Consensus as of Feb-05-2015 10:46 AM GMT

Stock Price [USD] vs. Volume [mm] with earnings surprise annotations



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ4 2013	1.08	1.33	1 23.15 %
FQ1 2014	0.94	1.05	2 11.70 %
FQ2 2014	1.18	1.30	3 10.17 %
FQ3 2014	0.91	1.06	4 16.48 %

Call Participants

EXECUTIVES

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

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President of Hanover Agency Markets

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Richard W. Lavey
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ANALYSTS

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Sterne Agee & Leach Inc., Research Division

Unknown Analyst

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Presentation

Operator

Good day ladies and gentlemen, and welcome to the Q4 2014 The Hanover Insurance Group, Inc. Earnings Conference Call. My name is Joyce, and I will be your operator for today. [Operator Instructions] As a reminder, this conference is being recorded for replay purposes.

I would now like to turn the conference over to your host for today, Oksana Lukasheva. Please proceed.

Oksana Lukasheva
Vice President of Investor Relations

Thank you, Joyce. Good morning, and thank you for joining our fourth quarter conference call. We will begin today's call with prepared remarks from Fred Eppinger, our President and Chief Executive Officer; and David Greenfield, our Executive Vice President and CFO. Available to answer your questions after our prepared remarks are Dick Lavey, our recently appointed President of Personal Lines; Andrew Robinson, President of Specialty Lines; Jack Roche, President of Business Insurance; and Bob Stuchbery, President of International Operations and Chief Executive Officer of Chaucer.

Before I turn the call over to Fred, let me note that our earnings press release, financial supplement and a complete slide presentation for today's call are available in the Investors section of our website at www.hanover.com. After the presentation, we will answer questions in the Q&A session.

Our prepared remarks and responses to your questions today, other than statements of historical fact, include forward-looking statements, including our earnings guidance for 2015. There are certain factors that could cause actual results to differ materially from those anticipated by this press release, slide presentation and conference call. We caution you with respect to reliance on forward-looking statements and, in this respect, refer you to the Forward-Looking Statements section in our press release, Slide 2 of the presentation deck and our filings with the SEC.

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

With those comments, I will turn the call over to Fred.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Thank you, Oksana. Good morning, everyone, and thank you for joining our fourth quarter earnings call. 2014 was a strong year for our company. We are very pleased to report record results for the full year and for the fourth quarter.

We delivered net income per share of $6.28, the highest annual income in the history as a public company. Operating income per share was $5.19 in 2014, yielding an operating ROE of 9%. And our combined ratio, excluding catastrophes, was 92%, in line with our original 2014 guidance. Results of the fourth quarter were also strong, with operating income of $1.77 per share and an ROE of 12.7%.

In 2014, we took an important step on our path to achieve target returns, fundamentally repositioning our portfolio, driving needed rate and achieving greater penetration with our partners, coming out of the year with 6% net premium growth and 1.5 point improvement in ex-cat combined ratio compared to 2013.

We feel good about our market position, the fundamentals of our business and the progress we have made on all our strategic priorities. As important, given our current market position and financial condition, we have confidence in our ability to continue to generate profitable growth and earnings accretion going forward. This confidence is based on our success thus far, our market momentum and the multiple earnings levers at work in our business as we enter 2015.

I will have more on these items after David reviews our financials.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Thank you, Fred, and good morning, everyone. We had an excellent quarter, and we're pleased to report our highest full year and quarterly earnings, a product of the team's relentless focus on making the most of our profitability levers and improving the underlying strength of our operation.

Net income for the fourth quarter was $90 million or $2 per diluted share compared to $70 million or $1.57 per diluted share in the prior year quarter. Operating income was $80 million or $1.77 per diluted share compared to $60 million or $1.33 per diluted share in the fourth quarter of last year.

For the full year, net income was $282 million or $6.28 per diluted share compared to $251 million or $5.59 per diluted share in 2013. Operating income was $233 million in 2014 or $5.19 per diluted share compared to $227 million or $5.06 per diluted share last year.

Turning to underwriting results. I'm going to focus my comments on the full year, with references to the quarter results where appropriate. Our 2014 combined ratio was 96.9%, in line with the prior year ratio of 96.7%. This slight increase was fully attributed to higher catastrophe losses of the current year, which were largely offset with improved ex-cat performance. At 4.7% of net earned premiums, catastrophe losses essentially were in line with our assumptions at the beginning of the year, and 1.6 points higher than we reported in 2013. The combined ratio, excluding catastrophes, improved by 1.4 points, reflecting a 2-point improvement in the domestic business, with Chaucer remaining relatively unchanged.

We are proud of what we accomplished in our domestic operations in 2014. The 2-point improvement in ex-cat combined ratio stems from the decrease in the loss ratio, with contributions from both Commercial and Personal Lines, along with the decline in the Commercial Lines' expense ratio. Together, these improvements drove a meaningful increase in our ex-cat underwriting margin of $75 million as compared to 2013.

On the Commercial Lines side, our continued focus on writing small- and mid-sized accounts would help -- which helps support more consistent pricing increases, along with ongoing mix management initiatives and expansion of our product portfolio, drove roughly a 2-point improvement in the loss ratio from 60.2% to 58.5%.

The accident year loss ratio in other commercial lines, which includes surety and other domestic specialty business, improved by 4 points in 2014, driven by continuing business maturation, along with mix management and pricing actions. We are very pleased with the traction these businesses have established, as they continue to support the overall margin expansion and top line growth of the company.

The CMP line also continued to perform well, as we remain diligent in our rate and non-rate actions. In auto, we are encouraged by the recent underlying trends in our books in response to our persistent pricing actions and changes in the severity profile of the business. Our loss ratio in 2014 remained relatively stable compared to 2013 as we continue to take a cautious approach to this line, given our experience in recent periods and ongoing industry trends.

In workers' compensation, although we experienced some normal quarterly fluctuations throughout the year, our full year loss ratio was relatively in line with 2013 actuals and our 2014 expectations. We continue to be very pleased with the performance of our smaller-sized, lower-risk profile book.

Additionally, we delivered a full year commercial line expense ratio of 37%, representing a 1-point improvement over 2013, as we guided. This improvement was driven by growth leverage and operating model efficiencies.

In Personal Lines, the underlying loss ratio for the year was 62.4%, nearly 1 point better than the 63.3% we reported in 2013.

Our pricing and mix initiatives continue to drive the overall quality of the business, as demonstrated by a 2-point decline in the auto accident year loss ratio.

The homeowners line was about 1 point higher, as we experienced heavier non-catastrophe weather in the first half of 2014 compared to lighter-than-usual activity in the first half of 2013.

Adjusting for this impact, the accident year loss ratio in homeowners also improved by approximately 2 points. Our rate increases continue to run above loss cost levels, providing confidence in our ability to generate further margin accretion in 2015.

Chaucer delivered another strong year and quarter of results, with a combined ratio of 90% and 88%, respectively. Full year pretax operating income reached $178 million compared to $150 million in 2013. Lower catastrophe losses helped offset a slightly higher incidence of large losses in 2014.

Chaucer's expense ratio was 38% for the full year, in line with our expectations and with the prior year. The expense ratio ticked up in the fourth quarter compared to our expectations and guidance, driven by higher performance compensation expenses and foreign exchange movements.

Although Chaucer exceeded historical averages and delivered annual results above our forecast, we believe the current -- given the current challenging market conditions and with the return to a more normal loss environment, it will trend back to a historical combined ratio of about 95% going forward.

Moving on to the top line. Overall net premium written growth of over 5% for the year reflected growth of 7% in Commercial Lines, 10% in Chaucer and moderation of premium decreases in Personal Lines of 0.4% for the year. As the majority of the exposure management and profitability improvement actions in our domestic businesses were completed during 2014, we are pleased with solid growth for the year and particularly with the return to growth of Personal Lines in the second half of the year.

Commercial Lines experienced robust growth, while we continue to adjust the portfolio mix. At Chaucer, growth for the year was driven mostly by political risk lines in marine and casualty. The premium growth also reflects the increased underwriting participation after we eliminated certain capital arrangements, as well as the impact of foreign exchange movements. Overall, both our bottom line and top line performance met, and in some instances, exceeded our expectations for 2014.

In 2015, we will maintain our focus on sustaining combined ratio improvement and driving the organization to achieve target returns.

Moving on to investment results. At year end, cash and invested assets were $8.6 billion, with fixed-income securities and cash representing 90% of the total. Roughly 94% of our fixed-income securities were investment grade, and the average duration of the portfolio was 4.2 years. Our investment portfolio remains high quality and well-laddered.

Our quarterly net investment income increased to $68.8 million from $68.1 million in the prior year quarter. Our net investment income for the year was $270.3 million, up slightly over the prior year.

While lower new money yields continue to impact our returns, we more than offset this impact with a higher level of assets from positive operating cash flow and deployment of operating cash into the portfolio. The earned yield on our fixed-maturity portfolio was 3.65% in the quarter and 3.71% for the year compared to 3.86% in the prior year quarter and 3.95% in 2013.

As I've mentioned on previous calls, we continue to prudently expand our portfolio mix into non-fixed-income instruments. We believe this will help offset some of the yield pressures that exist in this low-rate environment, which together with higher cash flows, should drive a slightly higher net investment income in 2015.

Net unrealized investment gains were approximately $310 million at the end of the fourth quarter compared to $222 million at the beginning of the year and $293 million at the end of the third quarter. In this very fluid time in the marketplace, we expect additional volatility in our net unrealized gains' position going forward.

I'll finish up with a few comments on the strength of our balance sheet and capital position. We ended the quarter with $3.7 billion in total capital, over $2 billion in U.S. statutory capital, the highest it's ever been, and a debt-to-total capital ratio of 24%, the lowest since March 2011.

And in the further confirmation of our progress, last week, Standard & Poor's recognized the strength of our capital position and the operating progress we made on our overall franchise by upgrading our financial strength ratings to A with a stable outlook.

At December 31, book value per share was $64.85, up 2% in the quarter and up 9% since December 2013. Excluding net unrealized investment gains, book value grew 7% in 2014, reflecting strong earnings throughout the year, partially offset by the impact of capital management actions.

For the full year, we repurchased approximately 350,000 common shares for $20 million or an average of $58.90 per share, which represents approximately 0.8% of our shares outstanding. We did not repurchase any shares in the fourth quarter. And we have $117 million remaining in our stock repurchase program.

Looking ahead to 2015, we expect we will continue to be opportunistic when considering stock repurchases. However, we believe our capital is best deployed as a tool to support the growth of our business, as well as capitalize on the current market conditions. We entered 2015 with a very strong balance sheet position, providing us with a great foundation for business growth and development.

And with that, I'll turn the call back to Fred.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Thanks, David. As we reflect on our progress and turn our focus to 2015, we are confident that we will capitalize on the improvements we've made across our organization and the forward momentum we have established in the market.

Looking back on 2014, we significantly advanced our journey, making progress on all our strategic priorities. We enhanced the distinctiveness and quality of our product portfolio and service capabilities, while improving our position with our agent and broker partners.

I'll review some of the key areas of progress in each business segment and why our current position is a source of confidence for continued improvement in 2015.

Starting with Personal Lines. 2014 was an important transition year for this business. We began the year with a focus on exposure management initiatives and rolling out our Platinum Experience platform. We ended the year with momentum, accelerating new business and increasing retention for the last 2 quarters.

Net written premiums grew 3% for the quarter, and we were basically flat for the year as we nearly completed our exposure management actions, ending the drag on growth from this business.

Rate increases for the year were 6%, with the fourth quarter indicators being slightly lower at 5%. With good transparency into 2015 rates, we believe the increases will hold at the same level at about 5%.

Our underlying retention, which excludes the impact of voluntary premium reduction, continued to improve and stood at 81% at the close of the fourth quarter 2014. A combination of mix management and pricing initiatives drove solid profitability improvement in our Personal Lines book, as demonstrated by the decline in ex-cat loss ratio from 64% in 2013 to 62% in 2014.

Given our retention levels in pricing, which remains above loss cost, we believe we are well-positioned to get additional rate to drive performance improvement in 2015.

Another important reason for our confidence lies in the success of our Platinum product. Platinum is the most relevant, full-account offering available to independent agents that are focused on selling value. While some of our competitors now realize the need for bundled product and upscaled services for their target customers, we are already successfully addressing this market need through Platinum, which now covers most of our Personal Lines footprint.

Our agent partners have been very receptive to our Platinum offering in the early going. In fact, approximately 70% of our total new business in states where we have introduced Platinum is driven by this new offering. Agency feedback has been excellent. Not only does Platinum provide comprehensive coverages at an attractive surface package to our customers, it also addresses important agency needs.

Through rate stability, dedicated customer service and self-service capabilities, agents are able to manage their existing business more effectively and be more targeted in their new business generation. We believe we can continue to build on the success of Platinum across our partner agency network in 2015.

As mentioned on previous calls, Platinum is associated with higher umbrella penetration, better retention, anchoring assets and enhanced business mix, which should drive improved profitability over time. We are extremely excited with our current position and opportunities at Personal Lines, and we believe we should see low single-digit growth and strong profit in 2015.

In Commercial Lines, our focus in 2014 was twofold: We continued to adjust business mix through rate and non-rate actions; and we also advanced our position with partner agents, achieving greater shelf space with established and more recently developed products. The combination of both of these factors gives us a clear view into more profitable growth going forward.

For the quarter, our pricing in core commercial was just under 7%, fundamentally in line with recent trends. We recognized there was pressure in the marketplace and plan for our price increases to lessen in 2015. But we believe we will continue to see pricing in excess of loss trends into the near future.

In commercial auto, we ended the year with better pricing increases than we started, which has ultimately contributed to more than 20% in cumulative pricing gains achieved since the end of 2011. We also repositioned this line through a number of targeted re-underwriting initiatives. We believe these actions are helping us to address issues in this line, and we are encouraged by our underlying trends. However, we remain vigilant and cautious due to the adverse development we and our competitors have seen.

Our mix management initiatives were not limited to commercial auto. We executed portfolio actions in the broadest sense, including working on property exposure concentrations and repositioning the risk profile on some specialty businesses, which together impacted our growth for the year by about 2% or $50 million in premium.

Although, we forfeited some growth, we believe our book of business is more stable and is of higher quality, which is demonstrated by our numbers. Our Commercial Lines underlying loss ratio improved by 1.5 points in 2014. Our results indicate that we are able to achieve better pricing and drive important changes in our book without compromising on our growth momentum with agents.

Our Commercial Lines growth in 2014 was strong, a strong 7%, led by specialty. Underlying retention remains stable, as expected, with the relatively small size of our accounts supporting pricing consistency. Growth is obviously very helpful to our expense ratio, which improved by 1 point, 2014, and we have visibility to at least another 0.5 point of improvement in 2015.

We approach the market differently than others in the industry. While many competitors are commoditizing their business, we've developed unique capabilities to effectively sell value. In 2014, we continued to invest in product innovation. For example, we finalized our work on possible allied health and technology offerings, we made meaningful additions to our miscellaneous professional liability product.

We continue to successfully execute our approach of building deeper business insight and deeper relationships with a limited number of agents, agents that are growing their business and whose portfolio aligns with our strategy. Deeper penetration with these agents is critical to our growth. We progressed this year increasing shelf space with our partners, especially with our small commercial platform, which is -- which offers top-of-the-line technology, as well as tailored underwriting expertise.

Our franchise value with our partners is excellent and will create a significant number of opportunities, as we continue to execute our value proposition and grow profitability with this targeted agency base.

We have strong leverage to grow and further improve profitability in Commercial Lines. We operate segments which are less price-sensitive, while we continue to refine the business mix to focus on more profitable classes. We now have greater earnings persistency in our book, and equally important, pricing continues to run at acceptable levels, putting us in a position where profitable mid- to high-single-digit growth is sustainable in 2015.

At Chaucer, our focus in 2014 was to successfully navigate a challenging market and leverage our distinctive market positions and underwriting capabilities to maintain a strong book of business. Once again, we delivered outstanding results, ending the year with $178 million of pretax operating income and a 10% net premium growth, as we effectively delivered on our priorities that benefited from a favorable loss environment.

We actively managed our diversified product portfolio to protect, and where possible, enhance underwriting margins in this dynamic market. Our underwriting maintained highly disciplined, while we effectively deployed capital and underwriting capabilities in some targeted opportunities that arose.

Our underwriting expertise, coupled with a well-diversified portfolio, positions us among the strongest of all these writers, best able to navigate the current market successfully. But given the challenging environment, we expect limited net premium growth out of Chaucer in 2015.

Overall, as evident through our 2014 results, our strategies in each business segment are aligned to drive further success. We believe the persistency of rate and the strong positions we have developed with our partners will allow us to sustain momentum and profitably grow in all of our domestic businesses.

With our rate and profit management actions and ability to improve our business mix, we expect underlying margins will also continue to improve. And although Chaucer's future performance will likely yield results more in line with our long-term target of 95% combined ratio, we think we have visibility to produce another 1 point of overall underwriting margin accretion in 2015. And I am optimistic about the many opportunities that lie ahead.

Before we open up to questions, let me just take a moment to discuss 2015 and provide some thoughts relating to our 2015 financial outlook. Our operating earnings expectations for 2015 is in the range of $5.70 to $6 per share. As the basis for this outlook, we anticipate written premium growth of mid-single digits, net investment income growth of approximately 5% compared to 2014 and an overall combined ratio of around 96% that assumes catastrophe losses slightly below 5% of earned premium.

In closing, I'd like to emphasize how pleased we are with our results in the quarter and the year, as we have executed on our financial and strategic goals. Due to the continued progress we have made, we are confident that we will continue to deliver strong results in 2015.
Operator, can you please open the line for questions?

Question and Answer

Operator

[Operator Instructions] The first question comes from the line of Dan Farrell of Sterne Agee.

Daniel D. Farrell
Sterne Agee & Leach Inc., Research Division

Just a question, as it relates to your guidance. If I look at the midpoint of that, and correct me if I'm thinking wrong in this math, it looked like it would imply something just below about a 9.5% cost base ROE. How do you think about that level versus your ultimate goal of getting close to an 11% ROE? What do you think the ability is to get there, and sort of the path and time that you think you might be able to do that?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes, I think that's right, Dan. So I think the midpoint for us, the way we think about it, is at about right at about a 10%, because -- as we think about our operating ROE. And I believe that where we are is really within the range. So by the run rate in the fourth quarter, I see us to be very close to or at that range that we always talk about. So I feel pretty good about that. Obviously, the yields have been surprisingly low as far as stickiness, staying low. But I feel pretty good about where we are and the continued improvement of our earnings, and feel that we're going to be very close to the range as we close out next year.

Daniel D. Farrell
Sterne Agee & Leach Inc., Research Division

Okay, great. And then I have a question regarding the auto segment. As you guys transition towards more of a growth outlook, how do you think about your ability to maintain the nice profitability gains that you have achieved in that business? And maybe if you could talk a little bit more about the Platinum product, is that related to key other characteristics of that business that allow it to be more profitable than new business that comes on?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes. So -- and I'll let Dick Lavey, who's joined us, to supplement what I'm talking about. We are thrilled, actually, by the Personal Lines. We think we hit something here. We've worked pretty hard over the last 3 years to get to an account-focused approach and have changed the demographics of our book. And we believe we have really good market insight into what our target market is. And so we talk about that 78% of our business is now this full account, but it's also a very attractive demographic, call it, middle market, right? So we've built up a terrific value offering for this middle-market market. And what you're seeing is our ability to sustain pretty good rate. So we have, as you can imagine, Personal Lines, because you file way ahead and you kind of get the policies out way ahead. We have pretty good transparency to this 5% level, almost across our business in pricing, because a lot of our corrective actions and concentration and weather, you remember 2 years ago, 2.5 years ago, we said we were going to take our weather assumptions up on our overall business, and we did that. But what you're seeing is really nice persistency and, frankly, growth now with our target agents around this segment and this profit kind of, what I would say, profitable kind of middle-market approach to the business. And we're pretty happy with it. I've mentioned at the earnings call, we believe that it's about a $90 billion business in the agency channel, and about $70 billion of that is this value-added segment we're going after, and there's a significant amount of it in our agency channel. And we've been able to identify that with our partners. And it had pretty good success, moving against that and transitioning that business to us with a number of our partners. So we believe we can get the rate. We believe the profitability of the lines are good. And more importantly, we believe they're stable.

Richard W. Lavey

Chief Growth Innovation Officer

So -- and absolutely not to be redundant with what Fred said, but the rate that we have flowing into the book gives us great confidence that we will be at targeted returns, and of course, you have to do that at a state-by-state basis. And in each of our states, we feel confident. Of course, we'll watch loss cost trends carefully, but we think at kind of a stable 5% rate for the foreseeable future, that that's going to sustain our ability to continue to see improvement in loss ratio -- or combined ratio. Just to echo what Fred said, the quality of our business, we couldn't feel better about. The segment that we go after and because of our agent distribution strategy, we know where that business is. We have tight relationships with our agents, so they understand the target segment that we were interested in. And we have more than a handful of quality metrics that give us a lot of confidence. So our umbrella penetration is upwards of 15% to 20% better. Our coverage A curves are higher, our BI limits are higher. And so all of that, just says we've got the right customer segment that we'll be able to kind of see consistent price increases without impacting retention.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes. And I think the other point that I then gave a little bit in my script tonight and we talked in our earnings call, we also believe how you service this segment. A lot of other people that we compete against have not invested in the self-service tools, the center tools, the proactive ability to reach out to these clients and serve them better. And that helps our agents' economics and ours. And I think that's why we're seeing a nice little uptick. So I'm pretty -- I think as this unfolds, we'll keep watching it, focusing on it. But I think we've added another growth part of our business.

Richard W. Lavey
Chief Growth Innovation Officer

And maybe the last important point on this is, we've been at this for 5 years, right? So we believe we're ahead of much of our competition in the sense that we have the market-leading product out there, we've done the mix management that we need to do. So as Fred said, just 80% of our business is this nice, high-quality customer segment in an account -- it's an account book. And so we start from that great position. And from here, we think we just build upon it. The business that's coming on the book has really high-quality mix. And so we're -- we believe we've got a running start against the competition. As you see, there's a lot of folks talking about this market segment and the value of pulling the accounts together, and we feel like we're several pieces ahead of that.

Operator

Line of Vincent DeAugustino with KBW.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Just a bit of a, I guess, a longer-term question. And so just looking back over the last few years, it's been quite an awesome trajectory. And so I'm kind of curious about on the guidance, that can be really helpful when there's substantial flux in the business. And now that you've arrived, so to speak, what I'm curious about is if you would -- if you plan on continuing to provide guidance in the future, or at this point have you reached a kind of level where the results start to speak for themself? And the reason I ask because we've seen some of your peers kind of go down that path of not giving guidance once they've kind of come to the conclusion of a turnaround. And so I just wanted to kind of get your philosophy on that now versus maybe a year from now.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

So Vincent, I think I'd first start to say that we don't have a sunset date by which we're planning to no longer give guidance. But to your question, as you might imagine, we kick it around and talk about it pretty regularly. And I think to some degree, you're right, that as our results and our performance are more normal and more easily projectable, you might be able to not have to provide guidance because it will be simply to estimate. But I would just say for now, for the foreseeable future, that's not our plan to stop giving guidance. And we'll continue to do so. And if we do change, we'll give plenty of notice to that.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, good. Fred, so maybe a quick question for you or maybe perhaps Dick. So when we think about Hanover's agency model, there's probably 2 other competitors that I'd put in the same group mentally, as far as that focus on the agency franchise, evaluating how Hanover plays into that. And I guess, what I'm kind of curious about is here, we've seen both of those kind of other 2 step up their game as far as their commitment to that service level. And so what I'm curious about is if there's anything on the competitive landscape where some of these other players that are really agency-focused would need to redouble their agency service efforts.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes. I mean, what's fascinating -- if you go -- if you think about it both Personal Lines or let me go broadly. If I go broadly, first, with commercial, I believe we have one of the handful, so I'm talking less than 5 world-class agency networks. And our network is as narrower than the big national guys that have built, over the years, strong penetration at the retail agent level and they've gone broader then we've chosen to stay with the winners a little bit better. And what you're seeing is we have built a lot more insight, as we talked at the Investor Day, about that channel where the business is, how attractive it is, et cetera. What we've decided to do and lay on top of it, and Personal Lines is a great example, is the notion of about really trying to get at the most profitable business, the best business, the most -- the business we think that would allow us to kind of hold and retain it for a longer period of time. So we've done a lot on saying, where are the segments where we can provide value-added. So whether it's the schmiddle [ph], small and the middle market, and our industry solutions or it's in Personal Lines, we worked with our agents and say, "Okay, this is where we can actually help your economics to create more sustainability, but also to -- ability to share shift -- shift shelf space to us." So Personal Lines is a great example. We believe that this segment is very good, but is underserved. So I would tell you that a good 2/3 of the agency of Personal Lines business is in companies, it's with our competitors that are less than $1 billion in premium, many under $500 million. Their ability to invest in service centers that are effective or self-service or tools, is very much -- much more challenging for them to do that, to them people with scale. And so we kind of raised the stakes a little bit, and we've given our agents a little bit of advantage because we've given them both franchise value, but we've raised the stakes on some of these kind of servicing tools. But I would argue that that's -- it's working in Personal Lines and it's raising the stakes for our competitors. But it's the same thing we're doing in schmiddle business. You're hearing people talk about the stuff that's non-commodity, small commercial. Well, we've been doing that for 3, 4 years, and it's really working well because our ability to -- like at the end of the year, if you look at what we did at the end of the year, how much of our business in middle market was contained to in what we call pipeline, which is in collaboration with our agents, looking at their business, what matches our appetite, what do we need to do. So we've got more looks this year than ever before, which allows us to be very targeted on the business we write. But that comes from both our investment in the data tools, but also in these solutions that we have by industry that allow an agent to say, "This business, I'm going to scare you away and give you a good look at it." So I think you're right, I think we've kind of -- there's a lot of our competition, but clearly the regional companies that just don't have, in my view, the wherewithal to use the data and then invest in their offering. And what you're starting to see from us is ability to kind of call steady growth, right, because we're getting good looks, we're working with our guys to get the business in. And in an environment that we'll probably see for the next 2 years, where you often have huge rate increases. And so you're not going to see a lot of turmoil and churn in the business, just because, right? So there's a lot of stability, which you're going to see a lot of people not get good looks. So our ability to be proactive, have value offerings, and then get the agents to work with us. The pipeline is an enormous advantage that I just -- I have a hard time believing that a lot of the smaller folks will be able to do that. So you'll see a lot more people, their growth kind of go away and their rate go down, up a little loss cost.

And I think we have an ability to do that right now, but not just Personal Lines, but also in some of our other businesses as well.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Vincent, I think the one other thing I would add to that is that -- trying to sort of project on the 2 competitors you are thinking about, there is a very material difference in our product capabilities, which is part of the fundamental difference, whether it be specialty industrial, marine, technology, professional liability, health care. We see a bit of executive protection from a couple of those more agency-focused competitors, but it's pretty perfunctory relative to what we do. So I think a big part of this is about the sophistication of our organization is much more comparable as it relates to Commercial Lines to the very best, most-sophisticated players in our industry. And I do think that that's really one of the defining differences in addition to the points that Fred talked about.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. It sounds like you guys are actually or might be some of the impetus behind some of the other commentary, so definitely thanks for that. Shifting over to Chaucer, just 2 quick ones, hopefully. But Bob, I guess, has there been any change in the net economic trade-off between U.K. motor returns and the capital benefit that motor provides to the other lines of business?

Robert Arthur Stuchbery
Former Chief Executive Officer and Executive Director

No, I mean, that remains as it is. And the more that we're doing that in certain motors we've got subject to, we've delivered on Solvency II, is still coming out with that same benefit. So the extreme, specifically, the 1 in 200 capital number, we get diverse protection credit from writing the U.K. motor against their other lines. That hasn't changed.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay, good. And then just on Jan 1 renewals, anything from the Chaucer side that kind of surprised your -- anything kind of stand out?

Robert Arthur Stuchbery
Former Chief Executive Officer and Executive Director

No, I think we've always guided that 2015, we expect to see sort of negligible growth. We planned for that. And from what we see now, analyzing, sort of doing a post review among ones, nothing that's come out of that -- particularly out of Lloyd's business, nothing has come out of that. Surprised us so. We still think we're in line with our expectations.

Operator

[Operator Instructions] The next question comes from the line of Larry Greenberg of Janney Capital.

Unknown Analyst

It's actually Lou [indiscernible], calling in for Larry. We had a couple of questions. In your reserve strengthening in commercial, was that just all commercial auto or was there anything else there?

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

It's -- sorry, I think you mentioned reserve strengthening. At commercial auto, there were some development in that line.

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

That was with the math, most of it was. Yes.

David B. Greenfield
Former Chief Financial Officer, Principal Accounting Officer and Executive Vice President

Yes. In just in auto, yes.

Unknown Analyst

In just in auto, okay. Do you guys see any change in trends there or just see a continuation of what's been going on recently?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

I think, again, one of the interesting things -- well, obviously, we've been talking about this since '11, and definitely, there was a lot of talk about it in the industry. What we feel pretty good about it is a couple of things. We've been at it for a couple of years here. And the ability to get rate and do the underwriting has allowed us to kind of have some transparency, and we feel really good about our book going forward. Obviously, the industry has had some kind of, what I would say, frequency of severity, if you will. But we feel like we've been on top of it, and we're in a pretty good place right now. In new business, it's interesting, pricing in the environment is much more realistic right now. You're seeing the new business pricing is really solid. And so it's -- the industry has recognized what the issues are. And so I think that's one thing that, in my view, has changed in this last year is that -- the industry has really adjusted price levels. And you can kind of, in my view, go into it with your eyes open and have it build a good book of business, or at least maintain a good book of business, given where our competitors have -- how they've reacted. So is there anything, Jack, you want to...

John C. Roche
President of Hanover Agency Markets

No, I think to your question, Lou, that we -- what we are seeing is that this has been a trend that's taking a couple, 3 years to really fully emerge. Many companies are -- have been watching this. Others have just recently acknowledged what some of us have seen for a couple of years. But remember, this is kind of a new level of BI severity driven by a number of factors. So it was really difficult to be able to try to declare where the final resting point was going to be for some of this severity. So we think we're at that stage now, particularly in the second half of '14, where we've seen some improvement in our large loss activity that's driving that severity. We are cautious, as David said earlier to take too much credit for it. Remember, the duration of the severity and the litigation that surround it pushed out over last couple of years. So you go to be careful about reading too much into kind of present-day trends. But at least our large loss activity appears to be reacting to some of the re-underwriting. And to what Fred said, we're covering up enough price now that even the same large loss activity is going to get better paid for. So we feel like we're at that point of improvement opportunity, but we're going to remain very cautious about how we account for this line.

Unknown Analyst

Great. That's super helpful. We have one more question. What are your expectations for expense ratio in Commercial and Personal? I think Fred mentioned 50 bps of improvement in Commercial, is that correct?

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Yes. Right now to that, given the work we've done. Yes.

Unknown Analyst

Okay. And for Personal, that was...

Frederick H. Eppinger
Former Chief Executive Officer, President and Director

Should be stable to slightly flat...

Unknown Analyst

Flat year-over-year. All right.

Operator

We have a follow-up question from Vincent DeAugustino with KBW.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

I have some 2 on workers' comp. Just on the top line growth, that's been bouncing around a good bit, at least relative to kind of where I've been modeling it. But I was just curious if new business is moving around, renewals, audit premiums or any kind of items like that would be moving the needle?

John C. Roche
President of Hanover Agency Markets

Yes, I think -- this is Jack. Clearly, you've seen a bumping around there from a top line perspective. Some of that is exactly as you described. We have some comparisons on the audit, for example, fourth quarter 2013, we had a particularly strong audit APs that came through, so the comparisons have a bit of an impact on the fourth quarter numbers. We also had some booking anomalies that kind of moved the numbers around. But I think what you're seeing overall is that workers' comp growth is really going to be in line with our overall growth. We're going to continue to be cautious in the auto line, but you should see us to be a total account player, particularly in the low end of middle market and small commercial. And from a profit perspective, we think we had a little bit of bumpiness in '14 regarding a couple of large losses, but the underlying trends in workers' comp continue to look favorable for us, and we have pretty good prospects moving forward.

Vincent M. DeAugustino
Keefe, Bruyette, & Woods, Inc., Research Division

Okay. And this may just be a bit of a curveball on workers' comp. But I guess, one of the things that we've heard about is that health care reform can cause some shifts in or more towards part-time workers. And so from a loss cost standpoint, I'm kind of trying to think through that because, arguably, this is maybe less experience from the workers' standpoint. And then even if the premium was the same for a 40 hours' worth of work versus 2 shifts of 20, I'm thinking the margin performance may not be the same. And so I'd just be curious if you guys have kind of thought through any of that or if it's kind of just too early to tell?

Richard W. Lavey
Chief Growth Innovation Officer

Well, we think through it regularly. I think that it is too early to tell. I think there is competing views here that more insured people, through their health care system, will have a positive impact on how many people show up in a workers' comp claim environment. But there is also the possibility that the disadvantages, quite frankly, in the workers' comp system vis-à-vis of costs can drive a certain amount of behavior into the workers' comp system. So we are -- one of the things we would say is that we believe we've driven our portfolio towards a risk profile that minimizes the impact one way or the other, quite frankly. We're down in the kind of the low- to no-loss sector, if you will, through the small commercial environment. And where you can really see volatility in your results in workers' comp is when you're in the high-frequency kind of area where that -- where those disadvantages in fee schedules and the overall claim management issue can come back to haunt you. So I think we're going to be in a stable place here for a while in the workers' comp system. And it's really driving the right mix and getting price over loss trend, and we like the trends that we have going in both of those categories.

Operator

There are no further questions in queue. At this time, I would like to turn the call back over to Oksana Lukasheva.

Oksana Lukasheva
Vice President of Investor Relations

Thank you, all, for your participation today, and we are looking forward to speaking to you next quarter.

Operator
Ladies and gentlemen, this concludes today's conference. Thank you for your participation. You may now disconnect. Have a great day.