S&P Capital IQ

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The Allstate Corporation NYSE:ALL

FQ4 2011 Earnings Call Transcripts

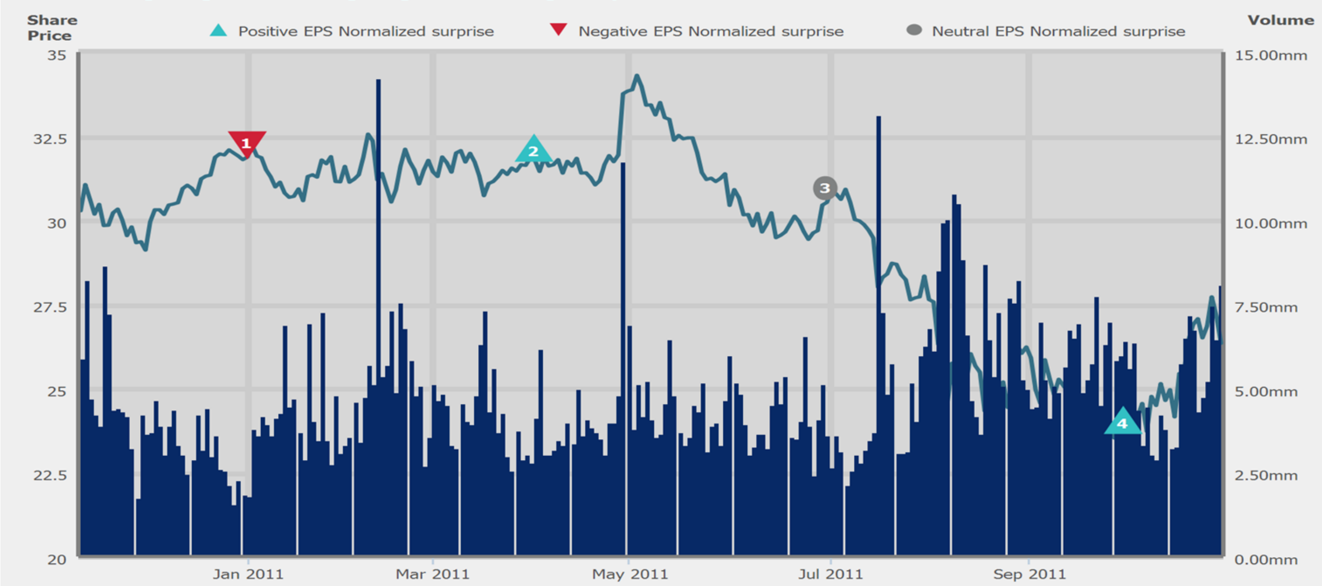
Thursday, February 02, 2012 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ4 2011-			-FQ1 2012-	-FY 2011-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	0.96	1.48	▲54.17	0.94	0.82	1.32
Revenue (mm)	6648.04	6605.00	▼(0.65 %)	6477.57	26493.64	25942.00

Currency: USD
Consensus as of Feb-02-2012 1:51 PM GMT

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



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2010	0.88	0.50	▼1 (43.18 %)
FQ1 2011	0.68	0.93	▲2 36.76 %
FQ2 2011	(1.55)	(1.23)	NM
FQ3 2011	0.12	0.16	▲3 33.33 %

Call Participants

EXECUTIVES

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Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Allstate Corporation Fourth Quarter 2011 Earnings Conference Call. [Operator Instructions] As a reminder, this conference call is being recorded. I would now like to introduce your host for today's conference, Mr. Robert Block, Senior Vice President of Investor Relations. Mr. Block, you may begin.

Robert Block

Thanks, Matt. Good morning, everyone, and thank you for joining us today for Allstate's Fourth Quarter 2011 Earnings Conference Call. This morning, Tom Wilson, Don Civgin and I will make a few opening remarks providing some context around our results for the fourth quarter and the year. We will follow those remarks with a question-and-answer session. Joining us for the Q&A session will be Judy Greffin, our Chief Investment Officer; Mark LaNeve, Senior Executive Vice President of Agency Operations and Chief Marketing Officer; Sam Pilch, our Controller; and Matt Winter, Senior Executive Vice President, Insurance Operations and President and Chief Executive Officer of Allstate Financial.

Yesterday, following the close of the market, we issued our press release and investor supplement for the fourth quarter 2011. We also posted a slide presentation that will be used this morning. You can find these documents on our website.

As noted on the first slide, this discussion may contain forward-looking statements regarding Allstate's operations. Actual results may differ materially from those statements. So please refer to our form 10-K for 2010, Form 8-K filed June 1, 2011, our 10-Q for the third quarter 2011 and our most recent press release for information on potential risks. We expect to file our 10-K for 2011 by February 29.

Also, this discussion will contain some non-GAAP measures for which there are reconciliations in our press release and on our website. This call is being recorded, and a replay will be available following the call. I will be available to answer any follow-up questions you may have once this call is completed.

Now I'll turn it over to Tom Wilson. Tom?

Thomas J. Wilson
Chairman & CEO

Good morning. I'll begin by reviewing our strategy and operating commitments for 2011, then I'll compare this to our results and then discuss our 2012 priorities. Bob and Don will then go through the underlying driver of our results.

Let's begin on Slide 2. Our strategy is to sell unique protection products to distinct customer segments, based on their preference for price, service and delivery channel. It's a long-term strategy designed to evolve with the changing marketplace and generate an operating return on equity of 13% by 2014. Our 3 near-term priorities for 2011 were: maintaining margins in the auto insurance business at industry-leading levels; secondly, improving returns in homeowners and Allstate Financial; and third, aggressively managing our capital. We're also hard at work on our longer-term initiatives to position our products and distribution platforms to meet the needs of our customers.

The chart on Slide 3 should be familiar to you. It's assigned to insurance market based on customer preferences around interaction and brand preference. Allstate does very well with customers in the lower left corner, who prefer to get more advice and assistance with their insurance needs and value of brand. We identified this group as personal touch loyalists. These customers prefer to buy multiple products such as Allstate Financial or a broad array of property liability protection products. This segment also has really good retention characteristics.

As you know, we acquired Esurance in the fourth quarter to serve customers who prefer to do this themselves, that's on the right side of the diagram. We're repositioning the Allstate brand and leveraging our claim and product expertise to compete directly with GEICO and Progressive Direct. We launched new Esurance advertising late in December, and we're making good progress in supporting this new team.

In the upper left, customers who want advice but are not as concerned about brand are served by Encompass. We acquired this business in 1999 when it had a combined ratio of well over 100, and we successfully improved profitability, which generated an attractive return on the acquisition price. More recently, this business has underperformed from a profit and growth standpoint. So late last year, we changed leadership and expect Encompass's results to improve.

If you turn to our financial results, they're on Page 4. For the year, we had net income of $788 million and $689 million of operating income despite incurring $3.8 billion in catastrophe losses. In the fourth quarter, we generated $724 million in net income, operating increased -- the operating income increased by $479 million to $750 million from the prior year as we experienced less catastrophe losses than in the prior year's quarter.

2011 was really -- was -- it had 2 distinct halves to it. In the middle quarters of the year, we incurred over $3.4 billion of catastrophe losses. In those 6 months, we had catastrophe losses that were more than 50% higher than we had in the entire 12 months of 2010. In the first and fourth quarters, catastrophe losses were more reasonable, and we earned about $2.40 per share in operating income. But through it all, we just -- we kept our focus on executing our strategy, which will drive long-term shareholder value.

If you look at our operating results, in Property-Liability, we maintained auto profitability with a combined ratio of 95.7 for the Allstate brand Standard Auto for 2011 compared to 95.5 for 2010. For the fourth quarter, the Allstate brand Standard Auto combined ratio was 95.5.

The combined ratio for Allstate brand Homeowners was 121.6, which included 50 points for those catastrophe losses which, as I said, were largely concentrated in the second and third quarters. We did make progress in improving returns with the underlying combined ratio, remember, that's the combined ratio excluding cats and prior reserve releases, was at 70.9, which is a 2-point improvement for the year. The total underlying combined ratio was 89.3 for 2011, within the range of 88 to 91 we provided at the beginning of 2011, and essentially, comparable to the number in 2010.

We also strengthened our agencies, so they'll continue to serve our agencies well. In 2011, the average size of Allstate agencies increased. And most importantly, the agency loyalty index, which is our measure of how well those agencies serve their customers, increased by almost 3 full points from 2010, and that's clearly a huge customer need and desire when you're looking at those personal touch loyalists.

We also introduced the Claim Satisfaction Guarantee and have now expanded that to over 30 states. We launched Good Hands Roadside as a way for our consumers to try our service and have signed up 390,000 new members last year. That's a unique offering in a marketplace. Nobody else offers that. And those results, those customer account don't show up in our policy counts.

Allstate Financial had net income of $586 million for 2011 and $529 million in operating income, which was 11% higher than 2010. In the fourth quarter, AF generated $140 million in net income and $138 million in operating income. Both were significantly higher than the prior fourth quarter, which, of course, is working on their goal of increasing returns on attributed equity. Very important, we also made great progress in executing the strategy to increase sales through Allstate agencies to those personal touch loyalists and shift the mix of business to underwritten products.

Our proactive management investments produced excellent results. Overall portfolio yields were relatively unchanged from 2010 despite the low interest rate environment. We remained long on corporate credit and further reduced our municipal bond exposure throughout the year. Unrealized net capital gains in the portfolio increased by $428 million after tax from the end of 2010, even as we realized about $0.5 billion in pretax capital gains during the year.

From a capital perspective, we returned almost $1.4 billion to shareholders in 2011 through both dividends and share repurchases. We completed one share repurchase program and initiated another $1 billion program in November, and we repurchased 4 million shares at a cost of a little over $100 million through the year-end. Our book value per share increased to $36.92, which is 4.5% higher than December 2010.

Our strategy of operating unique products to different customer segments does differentiate us from our customers -- or competitors. And so to further accelerate our success in that strategy, we have a clear focus on what we need to do in 2012 and you can see that on Slide 5. So we have to maintain profitability of our auto business. We'll do this by making further improvements in New York and Florida, being diligent about our costs and prices and providing Encompass and Esurance with the capabilities to improve their profitability.

Secondly, we must continue to raise returns from the homeowners and annuity businesses. At the same time, we need to grow insurance premiums. That means overcoming the negative impacts of improving results in those 2 big auto markets and in homeowners. We're going to do that by raising customer loyalty, growing a profitable auto and home markets, making sure we keep average premiums headed up and increasing the number of multiline households. Lastly, we have to proactively manage our investments and capital to generate attractive but balanced returns for our shareholders.

So Bob will now go through the business unit details with little more specificity.

Robert Block

Thanks, Tom. Turning to Slide 6. Property-Liability net premium written increased 2.9% to $6.4 billion in the fourth quarter and 0.3% for the year versus comparable periods in 2010. Excluding Esurance, the top line was flat with prior year for the quarter and down slightly for the year.

Allstate brand Standard Auto net premium written of $3.8 billion declined 0.8% in the quarter from the fourth quarter of 2010. A decline in units was partially offset by an increase in average premium, as profitability actions taken in Florida and New York negatively impacted the top line. New business applications fell 14.3% compared to the fourth quarter of 2010. Retention improved to 88.8 from 88.4 over comparable period in 2010. Policies enforced fell 1.5% from year-end 2010, but were flat excluding Florida and New York. The average gross premium increased in the quarter by 1.8%, driven in part by the rate increases approved in Florida and New York.

Allstate brand homeowners net premium written grew 2.8% in the quarter, as rate actions to improve profitability more than offset a reduction in units. We received approval for rate increases in 17 states, averaged -- averaging 7.8%. For the year, we averaged rate increases of 8.5% countrywide.

Our emerging businesses in Canada again contributed positively to the -- or contributed positive net premium written and unit growth in this quarter. Encompass net premium written was flat to prior year in the fourth quarter after declining in each of the first 3 quarters of 2011 compared to the prior year.

Midway down this exhibit, the combined ratio for Property-Liability was 90.7 in the fourth quarter compared to 100.8 in the fourth quarter 2010. The improvement of 10.1 points was primarily due to reduced impact of catastrophe losses of 7.3 points fourth quarter 2011 versus fourth quarter 2010. In the fourth quarter, we recorded $216 million of current quarter losses offset by favorable reserve reestimates of catastrophe losses that occurred earlier in 2011 of $118 million and $32 million favorable reserve reestimates from prior year. The underlying combined ratio for the fourth quarter 2011 was 90.5, an improvement from prior year of 1.5 points. The underlying combined ratio for the year was 89.3, well within the range we provided at the beginning of 2011.

The next slide provides loss cost trends for Allstate brand Standard Auto. On the left side of the slide, we show the level of frequency for bodily injury and property damage. 2011 results are the black line, and 2010 are in green. In the fourth quarter of 2011, both coverages declined relative to the prior year quarter with BI falling 3.5% and PD declining 2.6%. Rates have declined similar to the third quarter of 2011.

In the upper-right hand corner of the slide is a chart showing the percentage change for bodily injury and property damage paid severity. In the fourth quarter 2011, bodily injury paid severity increased 1.9%, and property damage paid severity increased by 5.8%. Much of the property damage paid severity increase reflected the impacts from rising prices for parts and used cars.

For the year, Allstate brand Standard Auto combined ratio was 95.7%, 0.2-point increase from 2010 as shown in the graph at the lower right-hand corner of the slide. With declining frequency essentially offsetting very modest increases in severity, we were able to maintain auto profitability while gaining approval for rate increases of 4.6%. We continue to focus on maintaining auto profitability.

On Slide 8, we have similar charts detailing loss cost trends for Allstate brand homeowners. Frequency, as shown in the upper left, increased 4.5%, but was partially offset by a decline in paid severity shown in the upper right. Thus, the increase in overall homeowner loss cost was less than the increase in earned premium. For the year, the underlying combined ratio improved by 2 points to 70.9%, and we continue to take actions to improve the profitability of this line of insurance. Looking forward, as reflected in our press release, we expect to produce an underlying Property-Liability combined ratio in the range of 88 to 91 for 2012.

Shifting to a discussion of Allstate Financial. Slide 9 provides the results for total premiums and contract charges, as well as the breakdown of income. These reflect the ongoing progress with the Allstate Financial strategy to improve overall business returns while shifting the focus from the spread-based products to underwritten products. Overall, premiums in contract charges increased in the fourth quarter by 7.3% over the fourth quarter 2010, and we're up 3.2% year-over-year in volume of $2.2 billion. The increase was in underwritten products and life-contingent annuities.

An important element of the strategic shift in product's mix is to drive greater participation in life and retirement sales by Allstate agencies. In the fourth quarter 2011, insurance -- life insurance applications issued through Allstate agencies increased 43% compared to the fourth quarter of 2010, a strong finish to the year where the increase was 33% over 2010's production level.

Allstate Financial produced net income of $140 million in the fourth quarter. 2011 is shown in the last line of this exhibit. This was an increase of $64 million from prior year, driven by increased operating income and capital gains realized in 2011 versus capital losses realized in 2010.

Operating income of $138 million increased $34 million from the fourth quarter 2010, primarily due to improvements in benefit spread and, to a lesser extent, investment spread. The improvement in benefit spread relates primarily to Allstate Benefits and was driven by a $38 million pretax reserve release associated with contract modification, better morbidity experienced and growth. The improvement in investment spread reflects actions taken to reposition the investment portfolio, as well as actions to lower crediting rates, which more than offset the managed decline in spread-based business enforced.

For the year, Allstate Financial produced net income of $586 million, operating income of $529 million and a return on attributed capital of 8.2% on both on operating and net income basis. The operating return increased 0.5 points, and the net income return increased 7.2 points compared to 2010. We've added an exhibit in the Investor Supplement this quarter, which breaks down income, attributed equity and operating returns by product to provide more transparency for Allstate Financial.

The value of the strategic shift to underwritten products becomes evident as these product groups generated higher returns than spread-based products. We also intend to improve returns in the immediate annuity business by diversifying the portfolio through reducing the allocation to fixed income investments and increasing allocations to limited partnerships in alternative investments that are expected to generate increased realized and unrealized gains.

In 2012, we will adopt new deferred policy acquisition cost or DAC accounting guidance on a retrospective basis. It is currently estimated to reduce shareholders' equity by $375 million after tax. We estimate that the new guidance will reduce Allstate Financial net income by approximately $40 million for the year after tax. We estimate that the new guidance will have an insignificant impact on Property-Liability net income. Looking forward, we will continue to execute on the strategy to shift the mix of business towards a more profitable underwritten products to generate improved returns in Allstate Financial.

And with that, I'll turn it over to Don.

Don Civgin
President of Emerging Businesses - Allstate Insurance Company

Thanks, Bob. Consistent with our past practice, we continue to proactively manage risk and return within the portfolio with the focus on protecting value and delivering solid returns. We continue to execute well as demonstrated by our results in the fourth quarter and for the full year. On Slide 10, you can see our portfolio returned 6.6% for 2011.

Also on that slide, you can see the size and composition of the overall portfolio of $95.6 billion at year-end 2011. The decline from the third quarter 2011 was in line with our expectations, as Allstate Financial continued its strategic reduction in spread-based liabilities, including the voluntary winding down of Allstate Bank.

During the quarter, we continue to reduced our exposure to the European Union while maintaining our allocation to corporate credit. As shown on the right side of this page, we continue to shift towards the middle portion of the interest rate curve by emphasizing our reinvestment activities in the 3- to 7-year maturities. Maturities in the 3 year or less range are primarily within Allstate Financial and will be used to fund liabilities withdrawals.

Net investment income for the quarter was $975 million, as shown on Slide 11, with a slight sequential decline, driven primarily by lower portfolio balances at Allstate Financial. Portfolio yields were stable despite the prolonged low interest rate environment with the total portfolio yield of 4.5% for the fourth quarter of 2011, consistent with the third quarter of 2011 and slightly higher than the 4.3% we have in the fourth quarter of 2010. The stable yields reflect our yield-enhanced actions, favorable limited partnership distributions and equity dividend, but are offset by lower interest rates.

On Slide 12, you can see that we generated $86 million of pretax net realized capital gains in the fourth quarter, down from $116 million for the fourth quarter of 2010. Realized gains in the quarter were primarily due to sales of fixed-income securities and favorable limited partnership valuations, partly offset by impairment write-downs and derivative valuation losses. For the year, pretax net realized capital gains were $503 million compared to 2010's net realized capital loss of $827 million.

The bottom of Slide 12 displays our pretax net unrealized capital gain position. We finished the year with approximately $2.9 billion of net unrealized gains, a $523 million improvement for the quarter and a $1.5 billion improvement for the year. This year, fixed income valuations benefited from lower interest rates, which were only partially offset by widening credit spreads and realized gains due to sales of fixed income securities.

Moving on to Slide 13. We finished 2011 with shareholders' equity of $18.7 billion, an increase from September 2011 of $0.6 billion. Statutory surplus at both AIC and Allstate Life Insurance remained strong, and deployable assets at the holding company level totaled $2.2 billion at year-end, reflecting the completion of the Esurance acquisition in October.

We initiated a $1 billion repurchase program in the fourth quarter and repurchased 4 million shares at a cost of $106 million under the new authorization by year-end. Total shares repurchased for 2011 totaled $946 million. We successfully prefunded $350 million of maturing senior notes with a $500 million 30-year senior unsecured note in early January with a 5.2% coupon. Lastly, book value per share ended the year at $36.92, an increase of $1.60 from year-end 2010, and an increase of $1.36 from the third quarter as well.

Now, let's open it up to your questions.

Robert Block
Matt, could you begin the Q&A?

Question and Answer

Operator

[Operator Instructions] Our first question comes from Bob Glasspiegel from Langen McAlenney.

Robert Ray Glasspiegel
Langen McAlenney

On the homeowners, I seem to be a little bit more excited about what's happening than you guys. The quarter underlying improved by 4.4 points. Third quarter was 1.7. So you had 2-point improvement for the year, but the fourth quarter seem to be better. Was there something either seasonality or non-cat weather that overstated the improvement, or is the mid-60s a good sort of run rate for underlying homeowners for 2012?

Thomas J. Wilson
Chairman & CEO

Bob, this is Tom. I'd like -- I'd rather look at it on a year basis where -- which is better by 2 points. In a quarter, you obviously get impacts of weather, but the other thing you get in a quarter is severity. And with a large difference in coverages, the amount of money you -- the average cost of the claim. So average cost of fire claim might be $30,000, average cost of a theft claim might be $25,000. So as you -- that mix changes, the severity bounces around a lot from quarter-to-quarter. So I think it's better to just look at it for the whole year. We're -- I'm pleased with where we're headed in homeowners. I don't think we've got it done yet, but it's just another sign that we're continuing -- our programs are continuing to work.

Robert Ray Glasspiegel
Langen McAlenney

Okay. My follow-up. I don't know that Gary is on the call or Don wants to address it, but I'd love some more Esurance data, sort of what the hit rate and response rate has been with the Allstate name. I noticed the expense ratio went up by 10 points from where it was at White Mountains. Is that average -- increased ad spin or accounting changes?

Thomas J. Wilson
Chairman & CEO

We're going to do Esurance as we move throughout this year when we actually have time to own it. We owned it for a couple of months. And as you know, we really did -- really launched a new program. I think it was like December 26 or something like that. So the increase is really due to intangibles. And, Don, you might want to talk about what you're doing about the insurance accounting on the intangible side of it.

Don Civgin
President of Emerging Businesses - Allstate Insurance Company

Yes. So when we closed the transaction in October, we completed the purchase accounting in accordance with GAAP, which requires us to fair value the assets we acquired. So we assigned about $353 million to intangibles. These are mostly customer relationships, trade names, technology. And we're going to amortize those over various periods depending on the asset, but it -- there is going to be heavy amortization in the early periods. We're excluding those from operating income combined ratio because they're noncash, so they're not reflective of the ongoing economics of the business. So we'll see those charges continue to go through. But as Tom said, we're making a lot of progress on Esurance and getting things going. But really, the marketing and the brand has only had a little bit of time to work, and you really wouldn't have seen any of those results yet in the fourth quarter.

Robert Ray Glasspiegel
Langen McAlenney

I don't think -- there was the 3:43 in the expense ratio. I'll follow-up with Bob afterwards.

Operator

Our next question is from Dan Johnson from Citadel.

Daniel B. Johnson
Citadel LLC

Great. I have 2 please. One, Tom, you've talked a bit over time about the progress so far and the plans in the future around driving more third-party participation in the homeowners product. Can you talk a little bit more about an update there? And maybe Matt could also highlight to what extent we are doing the same thing in the life business, and then I have a follow-up, please.

Thomas J. Wilson
Chairman & CEO

Okay. Dan, the overall arching theme that -- you're correct, what we've said is we can serve those personal touch loyalists completely without having to deploy our capital. So our strategy of serving them doesn't necessarily have to be linked to where we deploy our capital. We deploy our capital where we think we have skills and capabilities and where we think we can get a good return. So in total, we broker about -- a little over about $3.6 billion worth of stuff a year. The largest portion of that is in Allstate Financial. Matt, can talk about what we do there, where our skills and capabilities are and where we've grown it a lot this year, and you'll see his strategy embedded in that. In the Property-Liability subjects, I think it's like $1.1 billion or something like that. Most of that is homeowners or other property. We continue to be able to provide that -- those products to our customers and broker it through other people. We're actually restructuring some of those programs under Don Bailey, so we think we can improve both the choices for our customers and our economics. Matt, you want to talk about...

Matthew E. Winter
President and President of Allstate Insurance Company

Sure. Dan, so as Tom said, we've had pretty much a relatively long history at Allstate Financial of making decisions about which products we choose to manufacture and which products we choose to source from other carriers, knowing that we still had to provide a full suite of products for our distributors to be able to sell. So that started really with the outsourcing, on a major scale, of the variable annuity business when that block of business was sold to Prudential. And so right now, we do just under $1 billion of premium and deposits in the VA business. We do somewhere north of $400 million of mutual funds and about 140,000 -- I'm sorry $140 million on the book VA -- book value annuity. So we made a decision about 2 years ago, just after I got here, to stop manufacturing the book value annuity. We still manufacture the market value adjusted annuity. But we made the decision to source somebody else's product there, thinking that, for us, the risk return trade-off just didn't make sense. So we have a fairly robust brokering operation through our broker dealer. Now in addition to the major categories I mentioned, we also sourced a long-term care, some nonproprietary interest sensitive life, a small amount of variable universal life. But the major categories are the book value annuity, the VA and mutual funds.

Daniel B. Johnson
Citadel LLC

On both of these businesses, are we expecting to -- meaning -- protection and life, are we expecting a greater penetration of, I guess, outsourced capital usage this year?

Matthew E. Winter
President and President of Allstate Insurance Company

Well, I think that, as Tom mentioned, on the homeowner's side, we're taking a fairly granular look on a state-by-state basis of where it makes sense for us to manufacture that product and where it may make sense for us to use our Ivantage operation to source elsewhere. And I don't want to try to predict where we'll go with that, but it is our intention to offer the homeowner product -- a homeowner product to our customers in as many areas as possible. And we'll choose, based upon the individual economics, whether or not that's a manufactured product or a sourced product.

Daniel B. Johnson
Citadel LLC

Great. So maybe just a real quick second question on the insurance. The -- maybe if you could just lay out the parts that are being integrated and the parts that are specifically going to stay as freestanding as possible. And you don't need a litany. Just sort of interested more in things like sales versus claims versus advertising. Just a high level of stuff, how much this will be a stand-alone entity versus what parts you're trying to integrate.

Thomas J. Wilson
Chairman & CEO

Don will take you through some of the specifics, Dan. As you know, we've kept it separate as an organization. And you remember, the benefits of the acquisition for us is leveraging our brand name that will help them; secondly, improving their claim cost so reducing the variability of claim cost will enable us to improve profitability and put more money back in the business; and then broadening its product offering. Don can talk about how we're getting those skills and capabilities into Esurance.

Don Civgin
President of Emerging Businesses - Allstate Insurance Company

It's -- as Tom said, I mean, Dan, we are running it as a separate company. Their management team, which we were and continue to be very excited about, are running the business, and they're all still there. And Esurance is in San Francisco and Answer Financial is in Los Angeles, so they will maintain their offices. We have a lot of areas where can provide value to them, and actually somewhere there, we're learning from them as well. So the integration teams, which report, actually, at this point, to Gary Tolman, is more on a pull basis, as Tom has said in the past. So whether it's claims, purchasing, some product expansions, some state expansions and how they are able to use -- utilize our brand to improve consideration for the Esurance brand are basically being driven by them. We're providing whatever we can to make those things work well for them. And I -- what I tell you at this point is that's where a lot of the values is going to come from. It's going to be things like claims losses, buying scale, the additional products we're able to sell and, obviously, putting the Allstate endorsement on the Esurance brand so that their consideration and conversion will go up. Some of those we're making huge progress on I feel very, very good about. So the claims losses and scale product, we're working well and quickly on. The Esurance Allstate endorsement, really, people just heard about it for the first time at the end of December with the new ad. So that's going to take some time to drive up the retention and the conversion ratios. We expect kind of aggressive improvements in that, but it's really too early at this point to know how successful that has been or will be. But we're -- it's -- it is being continued to run separately and effectively, and we're just trying to add value where we can.

Operator

Our next question is from Alison Jacobowitz of Bank of America.

Alison Marnie Jacobowitz
BofA Merrill Lynch, Research Division

If I could ask 2. One is about the expense ratio for the total company, not specific to Esurance, but that's been rising over the past couple of years and I was just wondering if you can put some color on that. Do you expect that trend to continue? And the other is, is if you might be able to give maybe a little more specific an update on the profit issues in Florida, and if they're fully addressed and how that's doing?

Thomas J. Wilson
Chairman & CEO

First, on overall expenses. We're always about trying to reduce our expenses, so -- by line, so when you look at whether it's our technology expenses or our processing or headcount, we're always -- whether it's claims, we're always working on making sure we have the right level of expenses. Overall expenses were up some last year. The largest real driver of it would be a little more marketing spend, which we -- particularly in the fourth quarter, if you noticed the expense ratio was up. We've put a fair amount of money in terms of double-digit millions into launching Good Hands Roadside, which as I've said, is we got almost 400,000 new members. Those are -- they don't pay us anything. Remember that's -- you sign up for Roadside and it's pay-as-you-go when you need a tow or somebody to come to your car. So we're very excited about that, because we think it brings a lot of people into the company and gives us an opportunity to cross-sell them auto insurance and home insurance. But we spent some money on that last year seeking to grow. I think you'll continue to see some efforts on -- or some pressure on expenses as we both continue to advertise aggressively, and as we invest more money in technology. This business is rapidly becoming -- the technology's moving in -- out of sort of just the data management piece into the consumer connectivity piece. And we all have some work to do on that piece. Oh, Florida, sorry. Florida and New York are a little better than they were in the third quarter, as I said in the third quarter, they were profitable depending on which bases you wanted to look at. You go look at the exit, your statutory GAAP, they each had -- sort of had a measure under which they were profitable. They got a little better in the fourth quarter and they're going to continue to get better as we move throughout 2012. So they're out of the unprofitable zone, not yet to where we want them to be in terms of adequate returns, so you'll continue to see pressure on overall growth in the Standard Auto Allstate branded side because of New York and Florida.

Operator

Our next question is from Brian Meredith of UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

I got 2 for you. First one, Tom, you talked about increased marketing expenses and understand Florida and New York has caused some issues with PIP. But I'm curious if you could talk about how you're going to drive increased new business apps x Florida and New York, and how that's going to convert into PIP growth here going forward.

Thomas J. Wilson
Chairman & CEO

I want to be careful that I don't tell everybody else in the world what we're up to. So -- but I appreciate the question, Brian. So just give me -- when you look at where we are in the rest of the country, we've been flat in terms of items enforced, and we've had a very good combined ratio. So if you look at our combined ratio in total, at 95.7 and then you assume we'd lose money, or break even or something over the course of a whole year in New York and Florida in 2011, you'd say that it's obviously below, 95, in those other places so that's a very high attractive return. And so growing in those other markets is obviously a good thing for shareholder value. We're focused on doing that. There is -- one of the ways in which we believe we can do that is by broadening our risk appetite. Still staying in-line with this our sophisticated pricing, and not giving up large amounts of margin, but we could let that combined ratio go up a little bit so we'd grow. And as the Florida and New York combined ratio comes down, and then you add in Esurance on top of that, that's why when we'd look at the sort of underlying combined ratio, we say it'll be relatively flat. It's sort of a tale of 4 pieces, right? Homeownership come down, New York and Florida should come down. You'll see a slight drift in these other places, but those are bigger in terms of the overall volume of our combined ratio than either of the prior 2 pieces. And then Esurance, we'll put a little bit of pressure as we seek to invest and grow there and do more marketing. We will do more marketing on a more targeted basis in 2012. I know, Mark, if you want to talk about the marketing programs at all.

Mark R. LaNeve
Former Director, Chief Mktg Officer of Allstate Insurance Co. and SVP of Allstate Insurance Co.

Yes, over the last couple of years, obviously, the category has seen a dramatic increase in ad spend. If you look at our share voice we've maintained -- we've basically spent in the marketplace over the last several years an amount adequate to maintain a share voice at approximately what our market share is or slightly above it. One of the things we're -- with our strategy that Tom talked about, where we're really focused in the Allstate brand, on personal touch loyalists, those customers that enjoy and respect an agency relationship. By its very nature, it tells you this is local, so we are going to put more of our emphasis on local marketing next year. We're going to ship some dollars from what would've been national spend plus some increased dollars into the local markets, taking advantage of products like Claim Sat Guarantee, where we can be -- where we've broaden our pricing target to open ourselves up to a wider group of customers, making our marketing spend more effective. And we've seen that we've had some success in the fourth quarter with those kinds of programs, where we can really leverage the agents' efforts along with what we're doing locally. And if utilized radio, somewhat of an older medium, very successfully in these markets. So we think that we'll be able to keep pace, and as Tom mentioned, we've got real opportunities for growth in much of the country, and we'll be focused on continuing what we're doing with Mayhem and our Dennis Haysbert campaign, and then augmenting it with a strong local effort.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. And then just one other quick one here. Homeowners improvement, the underlying, I was wondering if you could drill down on that just a little bit more. Can you talk a little bit about how much of that improvement is coming from price or rate versus some of the underwriting initiatives that you've implemented? And as we go forward, look at your targets underlying combined, how much of that is going to be rate versus underlying-underwriting initiatives?

Thomas J. Wilson
Chairman & CEO

Brian, most of it would be coming from rate, at this point. The underwriting initiatives take a lot longer to rail through. So if you underwrite -- if the house isn't the right house, you know how the right price for it because your roof is bad or the porch is falling off or something, it doesn't necessarily turn into a loss, obviously, the next quarter. So that will take longer to burn in. It's incredibly important, though, to position in the long-term competitive position of business to get the right price for people. So we're continuing at it, we're putting a lot of effort on it, but most of it's price. And you'll see that as we go through next year as well. So of the 7 points that we've put into average price this year, you get a -- if you just think, okay, if we kind of do it equally throughout the year, you get about half this year and half next year, so we already have baked into next year about 3.5 points. So what Matt and his team will do to get -- to continue to improve pricing and he's got it segmented into a bunch of different good segments, which we can go into if someone in the call is interested. But it is mostly price, some of which is already there.

Operator

Our next question is from Michael Zaremski of Credit Suisse.

Michael Zaremski
Crédit Suisse AG, Research Division

In regards to pricing. It appears you've been pushing auto and home right increases above the national average. Would you expect that trend to continue, and can you comment on the competitive environment? And then I have a follow-up.

Thomas J. Wilson
Chairman & CEO

This is Tom. I would -- in terms of auto, I don't believe that's true. So if -- New York and Florida, obviously, have some impact on our overall, but if you just look at our average premium, like it's -- it's up like 1% or something like that. And if you look at average gross premium, you look at the country, you'd say it's probably in the 3% range. It's what you see from people like triple-I [ph] and stuff. So I don't believe we are -- I think we're competitive, some places we'll do 5 or 7, or this place in New York or Florida will hit it as hard as we need to hit it, but we feel like we're very competitive in the auto space. Homeowners, I believe, we were way ahead of the market, although I believe the market is catching up.

I can't really give you a sense for what everybody did in 2012. I can tell you, if you looked back -- if you look at the last 3 years in homeowners, our average gross premium's up by $160 per policy, which is about 18% or 19% over those 3 years. When I look at the industry stats, I don't see a number that big. I do see a lot of people taking fairly big increases in the last year, so my -- I suspect we were out early and other people are catching up. So we're not seeing any competitive pressure in raising homeowner prices. In total, this point -- I'm sure Matt, you have places, some places where it's a little tougher than others, but in general, everybody has the same kind of losses we do.

Matthew E. Winter
President and President of Allstate Insurance Company

Closing rates have stayed strong.

Thomas J. Wilson
Chairman & CEO

Yes. Excellent point, closing rates have stayed strong, retention rates have stayed strong. So we don't feel like we're out of the market on either of those.

Michael Zaremski
Crédit Suisse AG, Research Division

Okay, that's helpful. Then spread on the immediate fixed annuity book, and I believe on the other annuity book too, declined. Is it fair to say that, that'll continue to decline or I think in the prepared remarks, you talked about maybe improving it with alternative investments.

Matthew E. Winter
President and President of Allstate Insurance Company

Mike this is Matt. So let me clarify. The part that we're talking about, changing the investment strategy a bit on are the payout annuities that are extremely long-duration, very predictable cash flows that operate more like a pension liability. And so we have decided to treat our investment portfolio on a more granular level. And match the assets to that liability type in a more precise manner, and so we're going to look at some alternative investments that don't have the same liquidity characteristics as maybe some of our other blocks of business have, but they don't need those same liquidity characteristics. So you'll see us start to use some of those alternative investments to create the higher yield, long term, the total return, but maybe not on a pure, year-by-year net investment income basis. On the shore liability, deferred annuity block that is a little less predictable cash flow and we require additional liquidity, we're using the same leverage we've been using for the last several years. We've been managing the crediting rate as carefully as we can, consistent with our contractual terms and our compliance requirements. We're also being as precise as we can with the asset liability management on that block as well and trying to match durations. It is certainly challenging in the low interest rate environment, but as you've seen this past year, Judy's team has done an excellent job in getting those yields maintained. And so I'm cautiously optimistic that we'll have continued progress there.

Operator

Our next question is from Keith Walsh from Citi.

Keith F. Walsh
Citigroup Inc, Research Division

First for Tom, if you can just give us a little bit of more color behind the favorable reserve reestimate of $150 million, please. And then I've got a follow-up.

Thomas J. Wilson
Chairman & CEO

All right. Are you talking about catastrophes or are you talking about other coverages?

Keith F. Walsh

Citigroup Inc, Research Division

Just from the catastrophes in the press release on...

Thomas J. Wilson
Chairman & CEO

Yes, well, the catastrophe is obviously -- it's always hard to figure out exactly. Some decent part that came from the Arizona hailstorm that we had last year when you're trying to figure out how many roofers are coming out there, and you get a lot of light claims as people come back to their houses, and stuff like that. So as those types of events have become very situational and you have to just watch numbers, we have a philosophy that we want to have enough money and not be short. We don't over-reserve, but -- so in that particular case, we shot a little long. And the rest are just a variety of small additional changes per catastrophe. On the broader side of bodily injury and physical damage, both reserves and trends, we feel very good about reserves. Bodily injury paid costs looked, obviously, very good, if you look at our numbers. The incurred costs are what we think the ultimates will be. We're reserving a little bit higher level than that, as you would expect, because you have a lot of back-end stuff in the report year. Which years you're paying off have an impact on the pay, and so you get a little bit of a mix in there. So we're -- the paid are lower as the percentage increased than what we're ultimately reserving for. And then physical damage is pretty quick-- it kind of goes through. We thought that physical damage popped in the fourth quarter and paid, but mostly due to total losses. We're on top of it. For the year, it looked okay, but we're paying attention. And that, obviously the reserves, you get those claims paid off well, because it doesn't have a huge impact on reserves.

Keith F. Walsh
Citigroup Inc, Research Division

Okay. And then just for Matt on Allstate Financial. And I think you guys have talked about in the past about freeing up about $1 billion of capital, and we could see the business running down at least the fixed annuity, $6 billion of contract holder funds reduced in 2011. But the attributed equity is up year-over-year, and can you just help me understand these moving parts, I would have expected the equity dedicated to that business would actually be declining.

Matthew E. Winter
President and President of Allstate Insurance Company

I'm trying to understand your question. Can you just point me to where you're -- what you're looking at, you in the investor sup.

Keith F. Walsh
Citigroup Inc, Research Division

Well, I just -- within Allstate Financial on Page 34 of the supplement. You guys gave us this new disclosure about the attributed equity to the life business. And I'm just curious why that number's actually increasing year-over-year, when I would think it would be going in the other direction.

Matthew E. Winter
President and President of Allstate Insurance Company

We just didn't take any capital lot. I mean, the business is growing in -- and we're making profits in some capital intensive areas. The RBC is up because of our -- some of our investment portfolio moves in order to keep the returns where they need to be in this environment. And they are somewhat more capital intensive as we go from AAA corporates to some alternative investments, and that's driving some increased capital. Sam, anything else?

Samuel H. Pilch
Former Group Vice President and Controller

No, those are the reasons. Retention of profits, we're not taking any capital out of the company at this point.

Thomas J. Wilson
Chairman & CEO

We still don't have any intention to take capital out -- you're really looking at sort of quarterly swings. We don't -- on the RBC numbers, you wait until the statutory stuff gets done. That doesn’t get done really until like February or March. So we tend to let the capital in those subs ride until we get a better view of where they end up the year end.

Keith F. Walsh
Citigroup Inc, Research Division

Okay. And then just one final one on AF. With the $200 million decline in net investment income that you guys have in the presentation owing to the shrinking of the asset base, is that sort of a good run rate to think about throughout 2012?

Matthew E. Winter
President and President of Allstate Insurance Company

Well, it's always hard to predict those declines. Some of it's predictable declines, some is unpredictable and depends upon market movements. We don't see anything that occurred in 2011 that's that different than 2012 other than the Allstate Bank. And the decline in funds in Allstate Bank, obviously, happened in 2011 will not recur in 2012. But other than that, there should be fairly consistent flows.

Operator

Our next question is from Matthew Heimermann from JPMorgan.

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

First, just could you give us a little color and maybe outlook on the grow-to-win expenses just because of the $78 million you noted in the footnote of the supplement this quarter?

Matthew E. Winter
President and President of Allstate Insurance Company

I'm not -- Matt, what does it -- what do you mean, outlook on?

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

Well, just curious. Should we think about that being expenditures on that? Was that kind of a onetime, big, big pop relative to what you'd normally expect on that endeavor? Or is that indicative of kind of what we should expect going forward?

Thomas J. Wilson
Chairman & CEO

Yes, some of it was onetime, Matt, some of it will be continuing. Our grow-to-win was our effort to reengage the organization, our agencies on growth. Because earlier in the year, we had not been completely engaging growth. It included more advertising for auto insurance, which as long as it's economical, we'll continue to do that. It included about $25 million for Good Hands Roadside, a launch of that, which I don't think will be continuing. We want to find a way to continue to grow that business, but I don't think we have to do it through national advertising, the way we did to get it started. And then there were some other things we did in terms of local promotions. As long as those make money, we'll do it, but I would come back if you're concerned about the expense ratio. We pay attention to expense ratio, we make sure that every dollar we spend is economic, and if it's economic, then we make sure we can recover it in prices. And when you look at our average pay pure premium, which is, of course, just the total cost over time, that looks balanced relative to the price increases we're taking.

Matthew G. Heimermann

JP Morgan Chase & Co, Research Division

That's fair. And then just on the capital side, just a little color on the decline in stat surplus at ALIC this quarter. What factor drove that? And then also, in your capital plans for 2012, you talked about a potential preferred issue. Obviously, you've taken care of the debt refunding you talked about, so just curious to how to think about that and would be curious if earnings or capital ends up being a little bit better than we're expecting. Is that something that is -- potentially could come off the table?

Thomas J. Wilson
Chairman & CEO

And the last piece sounds like a third question, so I'm not exactly sure, but Don can talk about reserves and the debt. I'm not sure -- if we don't get to your questions, if there was a third question in there, maybe we can come back to it so we can get to the other people, but...

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

Just to clarify that last part was related just to saying with respect to the preferred, when you're addressing it, can you talk about whether or not that's an absolute plan or could be contingent upon how capital actually unfolds this year?

Thomas J. Wilson
Chairman & CEO

Yes. Okay, okay, I got it. Sorry.

Don Civgin
President of Emerging Businesses - Allstate Insurance Company

Actually, on the Allstate life insurance statutory surplus, it is down a little bit in the fourth quarter, in spite of the fact that they had a good fourth quarter from an earnings point of view. Most of that is because of reserve strengthening. If you recall, during the year, we took a fair amount of games-taking in the portfolio and the reinvestment rates required some level of strengthening of reserves. And then the other piece are just lower interest rates. With rates being lower in 2011, it's -- in our testing, required us to have more reserves up.

Thomas J. Wilson
Chairman & CEO

And as it relates to preferred, just the efficient -- let's say belt suspenders and alternative plans. So when we said we were going to do the $1 billion, we knew we had additional share repurchase, we knew we had $1 billion, at least, of excess capital at the holding company. We knew we would make money in 2012, and -- but we didn't want there to be any doubt that we could buy that $1 billion back, so we put in the authorization to do the preferred. And we'll do it if we think it makes sense, and depends what earnings are, but we fully intend to buy back the $1 billion worth of stock.

Matthew G. Heimermann
JP Morgan Chase & Co, Research Division

Okay, and then just maybe if you could give us some supplementary information on the Esurance and how you're accounting go-forward might contrast with the historical, that'd be great, too. Just...

Thomas J. Wilson
Chairman & CEO

Yes, we'll do that. And we're going to figure out how to help you see what we see on Esurance.

Operator

Our next question is from Jay Gelb of Barclays Capital.

Jay H. Gelb
Barclays PLC, Research Division

Two questions. First, can you give us your thoughts on marketing and advertising spending for 2012, and how that will compare to 2011? And then if we could get some insight on the impact of persistent low interest rates in the life insurance businesses, with the life currently running around the 8% return on equity for the full year, how much of the headwind will low rates be, going forward?

Thomas J. Wilson
Chairman & CEO

Let me take the first one. Judy, maybe you can talk about reinvestment, and Matt, you talk about it -- because I think the numbers, Jay, are off a little. If you look at, I think, it's Page 37, 38, we've broken out the life insurance -- Allstate Financial returns, it's a different bucket, so the 8% is not a number that resonates with me. That's what the deferred annuities are running at, but the life insurance business is low, is like 11% or something. And so you got to look at the components of it. In terms of marketing, advertising, we expect to maintain our share voice in the Allstate brand, and we expect to increase our share voice in the Esurance brand. And I think that's about where I'd like to leave it since other people listen to the call. And I don't want them to know sort of what kind of marketing we're doing. Matt, do you guys want...

Matthew E. Winter
President and President of Allstate Insurance Company

I'll start and then Judy can follow up. I think Tom was referring to the breakdown we have now on Page 39 of the Investors sup, which, Jay, shows the breakdown of operating income return on attributed equity. So really, the low interest rate environment affects the life insurance very little. It only affects some of the components of our Universal Life business with long-term guarantees and those products that are similar to that, it really doesn't impact the term business, which is really the vast majority of what we're growing right now. And if you look even on that breakdown under annuities, most of the work that we just described about the alternative investments on the payout annuity line is designed to prevent that low interest rate environment from taking that ROE down even further. So really, it's only leaving us with that deferred annuity block where we're making 8.7, and that's running off on a fairly predictable basis, and we're managing the in-force crediting rates very aggressively there. So, yes, it's a headwind on the work we're doing, but we don't think it's a long-term obstacle to it. It just creates some more work for us, and we have to get more creative in the way we manage the investment portfolio. But as I said, we feel pretty confident that with the change in the mix of business, and growing the mortality and morbidity, nonspread related businesses, as well as the alternative kind of pension investment strategy for long-term liabilities on the payout side. It leaves us with a manageable block to deal with to give some targeted, good return investment assets, too. And I'll let Judy follow up and talk a little bit more about that component.

Judith Pepple Greffin
Former Chief Investment Officer of Allstate Insurance Co. and EVP of Allstate Insurance Co.

So, as we've said earlier on the call, we have a fairly manageable reinvest for ALIC. We've done a pretty good job of matching the assets to the liabilities, so when we look at those contract holder funds that are going to be running off, it pretty much lines up with the maturities that we have in the portfolio. We still have a large portfolio that we're managing through a low rate environment, and we do several things to optimize that portfolio, given the liabilities. And Matt talked about one, with the payout annuities, where we're recognizing that the liabilities are very long and we want to put an asset strategy against those types of liabilities, but isn't necessarily as fixed income-oriented as it has been in the past.

Operator

Our next question is from Randy Binner from FBR.

Randolph Binner
FBR Capital Markets & Co., Research Division

Just a couple of follow-ups in the frequency area. One's on auto, one's on home. On auto, just there was a question on pricing earlier, and auto accident frequency has been favorable for Allstate and I think some other auto insurers. So is that -- I mean, definitely, should we worry about and from a pricing perspective in your ability to get price going forward?

Thomas J. Wilson
Chairman & CEO

Randy, this is Tom. If you look at our total frequency decline, you'd have to look at it in 2 chunks. New York and Florida, and then outside of New York and Florida. The largest component of our overall decline is in those 2 first states, which is both we've talked about one of the things we're doing to improve profitability. It is down slightly in the other states, but it's slightly -- and we don't see that as a problem in terms of having reduced rates, and nor does it look like it's -- it bounces around, though. I mean, the reason we give you all a range on combined ratio is frequency can move by 1 point in a year, and it's kind of sometimes it's weather, sometimes it's mileage, sometimes it just -- things happen. So it -- there is some variability around it, but we feel okay about it.

Randolph Binner
FBR Capital Markets & Co., Research Division

Okay, that's helpful. And then on the homeowner side, the xCAT frequency was up for the second quarter on a linked basis, and so it looks like a little bit higher trend. Is there anything driving that or is that just kind of year-over-year comparison as to when the severity -- I'm sorry, the frequency was lower?

Thomas J. Wilson
Chairman & CEO

I would -- when you look at homeowner frequency, there are -- I would say no. I think we're -- we feel like -- I mean, it varies by state. As you know, some states, we don't have -- some states we have severe weather problems, we've got to get more price to that. In some places, we have hurricane exposure, we got to make progress here. Other states, we have absolutely no problems at all and we should be growing and we're not. And then some states, we have what I would call normal frequency and severity issues where we have some progress right. Matt and his team have segmented it into those 4 segments, but we're managing in that way and so I feel comfortable that the way in which we're approaching the business, any trends in those 4 categories get reflected in the prices in those states. Maybe we could take one last question.

Operator

Our final question is from Adam Klauber of William Blair.

Adam Klauber
William Blair & Company L.L.C., Research Division

You talked a lot about the changes in the homeowners line, you've obviously done some really good work there. What inning do you think you're in, is this a 2-, 3-, 4-year process, I guess, where we at right now?

Thomas J. Wilson
Chairman & CEO

Some of my compatriots like to predict innings. I've always felt that's a bad thing because I can't predict the future. I would tell you, if you look back over the last 3 years, we've made a tremendous amount of progress, and we accelerated that progress, I believe, last year. And particularly it's not necessarily on price, but on the other things we will do. The next inning for us, which will be an important one, is launching a new product called house and home, which will deal with roof losses. So when you look at all the work we've done, it's working with our existing contracts and raising prices, trying to get the risk management right. And we're good at that and we've made a lot of -- we've had a lot of learnings over the last 3 years, and I feel like that game will continue to play out the next, I don't know if it's an inning, but the next thing we have to successfully accomplish is rolling out house and home, and Matt and Mark are working on that. What that does is it deals with roofs differently. So one of the big losses in severe weather are roofs. Some people just don't get their house -- their roofs fixed, and then a hailstorm comes and we replace a $20,000 roof when we're getting $1,000 from the customer, and it's obviously not a good trade. And so if the roof is 1 year old, it might have no damage to it, and $900 is the right price if the roof is 20 years old, then maybe we should be charging $2,000 or $3,000. So this new product gives us the opportunity to deal with roofs differently. That's really the next game and that will need to successfully accomplish that to get to our 13% return on equity by 2014. Matt, there are more...

Matthew E. Winter
President and President of Allstate Insurance Company

No, the only thing I would add, the other piece of that, as Tom mentioned at the beginning, is the decision on a granular level about selective brokering of other homeowner products in there. Because as we've now characterized the states into these categories of PML, PML in severe weather, and our ability to grow and successfully manufacture products for those states, we'll make decisions about whether they'll offer house and home or whether they'll offer a brokered product in there, so our agents have a homeowners product to offer their clients. And we have the risk profile that we want, as a company, in the homeowners area.

Robert Block

Okay. Thank you, all, very much. We'll talk to you next quarter.

Operator
Ladies and gentlemen, thank you for participating in today's conference. This concludes the program. You may now disconnect. Good day.