S&P Capital IQ

CONTENTS

Selective Insurance Group, Inc. NasdaqGS:SIGI

FQ3 2011 Earnings Call Transcripts

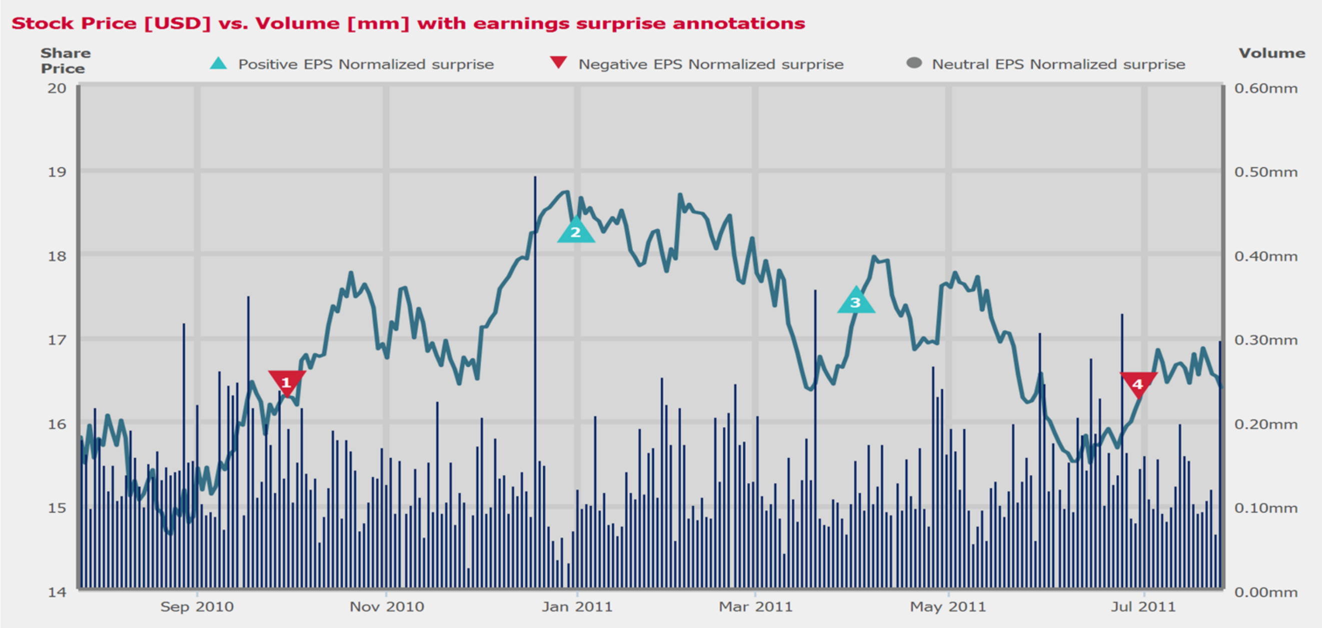
Thursday, October 27, 2011 12:30 PM GMT

S&P Capital IQ Estimates

	-FQ3 2011-			-FQ4 2011-	-FY 2011-	-FY 2012-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	(0.45)	(0.34)	NM	0.29	0.24	1.53
Revenue (mm)	399.57	394.07	(1.38 %)	408.45	1423.00	1618.88

Currency: USD

Consensus as of Oct-27-2011 3:01 AM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ3 2010	0.38	0.35	1 (7.89 %)
FQ4 2010	0.38	0.48	2 26.32 %
FQ1 2011	0.29	0.32	3 10.34 %
FQ2 2011	0.02	0.01	4 (50.00 %)

Call Participants

EXECUTIVES

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

Gregory E. Murphy
Chairman and Chief Executive Officer

Jennifer W. DiBerardino
Former Senior Vice President of Investor Relations

John J. Marchioni
President and Chief Operating Officer

ANALYSTS

Alison Jacobowitz

Doug Mewhirter

Michael Grasher

Robert Edward Farnam
Keefe, Bruyette, & Woods, Inc., Research Division

Presentation

Operator

Good day, everyone. Welcome to the Selective Insurance Group's Third Quarter 2011 Earnings Release Conference Call. At this time, for opening remarks and introductions, I would like to turn the call over to Senior Vice President, Investor Relations and Treasurer, Ms. Jennifer DiBerardino. Ma'am you may begin.

Jennifer W. DiBerardino
Former Senior Vice President of Investor Relations

Thank you. Good morning, welcome to Selective Insurance Group's Third Quarter 2011 Conference Call. This call is being simulcast on our website and the replay will be available through November 28th, 2011. A supplemental investor package, which includes GAAP reconciliations of non-GAAP financial measures referred to on this call, is available on the Investor's page of our website www.selective.com.

Selective uses operating income, a non-GAAP measure, to analyze trends and operations. Operating income is net income excluding the after-tax impact of net realized investment gains or losses, as well as the after-tax results of discontinued operations. We believe that providing this non-GAAP measure makes it easier for investors to evaluate our insurance business.

As a reminder, some of the statements and projections that will be made during this call are forward-looking statements, as defined by the Private Securities Litigation Reform Act of 1995. Forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties. We refer you to Selective's Annual Reports on Form 10-K and any subsequent Form 10-Qs filed with the U.S. Securities and Exchange Commission for a detailed discussion of these risks and uncertainties. Please note that Selective undertakes no obligation to update or revise any forward-looking statements.

Joining me today on the call are the following members of Selective's Executive Management Team: Greg Murphy, CEO; Dale Thatcher, CFO; John Marchioni, EVP Insurance Operations; and Ron Zaleski, Chief Actuary. Now I'll turn the call over to Dale to review the quarter results.

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

Thanks, Jen. Good morning. 2011 has proved to be a year of significant capacity losses for the BMC industry, and Selective's solid share was third quarter catastrophe losses of $67 million. In spite of that, we witnessed a continuation of positive underlying trends we saw in the second quarter. We achieved our tenth consecutive quarter of positive Commercial Lines price at 2.7%, and Commercial Lines premium grew 10% in the quarter. Commercial Lines' direct new business increased 15%, and audit and endorsement premiums continued to benefit the top line.

While the majority of our catastrophe losses in the quarter were from Hurricane Irene, Topical Storm Lee, six other weather events and $10.4 million in development primarily from the tornado activity in the second quarter accounted for the rest. Hurricane Irene now represents the largest storm loss in our history with gross losses including IV&R estimated at $48 million or $40 million on a net basis. In addition, we incurred $740,000 in re-instatement premium on the first layer of our capacity free treaty.

For the quarter, we reported an operating loss per dilute share of $0.34 compared to operating income of $0.35 a year ago. While catastrophe losses reduced earnings by $0.81 a share, higher net investment income from alternative investments in favorable prior-year casualty development partially offset these losses.

Since the quarter was in a loss position, basic shares are required to be used for the calculation of earnings per share as the effect of common stock equivalence would have yielded a smaller per share loss.

The third quarter statutory combined ratio was 166.4%, an increase of 16.1 points from a year ago. Catastrophe losses accounted for 18.8 points, partially offset by favorable prior-year casualty reserve development of $10 million or 2.8 points. Excluding the impact of catastrophe and reserve development, the combined ratio for the quarter was 100.4%.

Total statutory net premiums written were up 9% in the quarter, driven by Commercial Lines net premiums written growth of 10%, our second sequential quarter of growth. Our recent expansion into the Excess and Surplus lines contributed $8.4 million in net premiums written in the quarter. Much of the remaining premium increase in Commercial Lines was driven by continued improvement in audit and endorsement premiums to a positive $4.4 million in the quarter, compared to almost $11 million in return premium in the third quarter of 2010.

The Commercial Lines statutory combined ratio was 110.7% in the third quarter, including 13.5 points of catastrophe losses. Commercial property excluding catastrophe losses continued to perform well with an 81.2% combined ratio.

Commercial Auto and General Liability each had a good quarter, reporting statutory combined ratio of 95.9% including favorable prior-year casualty development of 2.9 and 6.3 points respectively.

Workers' compensation results showed some improvement in the quarter reporting a statutory combined ratio of 114.2% versus 130.2% a year ago. Results benefited from positive audit and endorsement premium of $1.6 million. There was no prior-year development in the quarter as we are seeing some stabilization in the line. While we can't say yet that this is a trend, we monitor our reserve positions very closely through a ground up analysis of reserves every quarter.

In Personal lines, net premiums written grew 4% in the quarter to $73 million as we saw renewal pure price increases of 5.9%. The Personal lines statutory combined ratio was 141.4%, driven by 41.9 points of catastrophe losses. Additional non-catastrophe property losses added 9.5 points to a combined ratio compared to a third quarter of 2010. The majority of the non-cap losses was primarily weather related, but did not fall into the PCS timeframe for named storms.

Turning to investments, third quarter after tax net investment income increased 7% from a year ago to $27 million. Pre-tax alternative investment income of $4.5 million drove the increase. Recognizing that the majority of the alternative investments report on a one quarter lag, we believe that the third quarter equity market declines are not completely predictive of alternative performance in the fourth quarter. Our seasoned portfolio includes investments in segments that are not as susceptible to equity market volatility such as energy and mezzanine depth.

Reflecting the continued low interest rate environment, the after tax yield on fixed maturity securities was 2.7% for the quarter, flat with last quarter and down slightly from a year-ago period. Invested assets increased 2% from a year-ago to $4.1 billion.

Our fixed income portfolio has an overall credit rating of AA- and duration of 3.2 years including short-term investments. The AA- rating reflects the recent S&P downgrade of U.S. debt. We continue to invest primarily in high quality corporate bonds while maintaining elaborate maturity schedule. Our municipal portfolio continues to be very high quality with an average AA rating. We have no investment in sovereign debt in Greece, Portugal, Spain, Italy or Ireland.

Equity exposure at September 30, 2011 was 3.4% of invested assets, up almost 2% from a year ago as we deployed our high dividend yield equity strategy. While equity market returns were negative in the third quarter, this strategy continues to outperform the broad market. We have an unrealized gaining position of $118 million pre-tax at September 30 2011, up from $102 million last quarter. The unrecognized gain position in the fixed income held a maturity portfolio was $49 million pre-tax or $0.58 per share after tax.

Surplus remains strong at $1 billion the September 30 while stockholder equity was flat with a year ago at $1.1 billion. Both value per share increased to $20.04 from $19.95 in December 31, 2010. Our premium to surplus ratio increased slightly to 1.4x in the quarter. We believe we have adequate capital to fully participate in an improving industry market place.

The dividend yield is currently 3.3% while the stock trades of 79% of book value.

Now I will turn the call over to John Marchioni to review insurance operations.

John J. Marchioni
President and Chief Operating Officer

Thanks Dale. Good morning. The Commercial Lines market place dividend increase discipline in the third quarter allowing for broader achievement of positive price. We are proud of our tenth consecutive quarter of positive Commercial Lines price which was up 2.7% as we remain focused on improving our underlying profitability to deployment of our granular pricing tools. We believe our pricing granularity is competitive advantage. We will continue to test market conditions as we push for higher rates on more of our policy inventory.

For the third quarter, accounts less than $20,000 in premium had point of renewal retention of 88.7% at a pure price increase of 3%. Accounts greater than $20,000 in premium, had point of renewal retention of 83.8% and a pure price increase of 2.4%. In addition, overall commercial year-on-year retention improved 2 points to 82% this quarter as our underwriters and agents continue to balance our pricing strategies with retention of our best accounts.

Commercialized new business in the quarter was up 15% compared to the third quarter of 2010, driven by our middle market and large account business which grew by 29% from a year ago.

The combination of a more rational market place and new product deployment generated this growth. New business has been strong and our community and public services segment, as we've seen very good demand for our new Para-transit in schools product. In addition, our new E&S operations generated $8.4 million of written premiums in the quarter. Year-to-date however, Commercial Lines new business was down 5% compared to 2010 as follows: one and done automated new business was down 18% to $48 million and middle market and larger account new business up 2% to $112 million.

Workers compensation results continue to be under pressure industry-wide and AMS is forecasting an Industry combined ratio of 121.5 for 2011. Several states have recently approved increased rates in this line. While Workers compensation results are still unsatisfactory, we saw some improvement in our results in the third quarter. To facilitate better results, we have been deploying numerous workers compensation claims and underwriting initiatives. While pricing still needs to move higher, we achieved 1 point greater pure rate increase on this line than our overall book.

In claims, we are well on our way to achieving our overall goal of three points in loss cost savings over 3 years. In fact, we have already achieved our full year target of $8 million in savings in the first 9 months. We believe that the stabilization this quarter and Workers compensation result is a direct result of initiatives such as specialized handling of complex Workers compensation claims and proactive medical management.

Personalized net premiums written grew 4% in the quarter while new business was down 22%. We are achieving positive rate and at the same time refining our underwriting approach to improve Auto profitability. We have implemented 30-rate increases this year and are on track for the implementation of another 16-rate increases by year end. In total these rate increases put January an additional $18 million on our enforced book. In the quarter, our renewal pure rate increases were 6.1% for Personal Auto and 5.9% for Homeowners. Our personalized book continues to show a strong retention at 87%, up two points from the third quarter of 2010.

As you would expect, the third quarter catastrophe is also resulted in significant flooding activity throughout the North Eastern and Middle Atlantic States. But the income we generated from handling flood claims in the write-your-own program increased 6 fold compared to last year's third quarter to $4.9 million. The impact of flood is included in our Personal Lines underwriting results.

We remain focused on our strategy to introduce new and expanded products to our agents and customers. The renewal rights transaction with Alterra, which closed August 1st, contributed $8.4 million in written premiums in the third quarter.

The acquisition announced this September for the E&S subsidiary MUSIC from Montpelier Re provides us the platform needed to fully execute our E&S strategy. MUSIC take 50 state license E&S Company with the systems required to underwrite and sell our claims in order to begin writing the contract binding authority business on our own paper. MUSIC also gives us a western presence as we intend to retain the full complement of underwriters and claims specialists in Scottsville, Arizona to manage and grow the book.

Both books of E&S business are comprised of approximately 75% casualty lines, mainly General Liability with no Workers compensation and 25% property. The 55 MUSIC wholesale agents have virtually no overlap with the 40 wholesales that did business with Alterra prior to the Read or Write transaction.

The $125 million in renewal premium opportunity from these acquisitions provides us with a good baseline. When we consider the potential for growth to the $300 to $400 million of contract binding authority, E&S coverage our 990 independent agency partners currently placed elsewhere. We think we have a solid platform to expand our franchise value model to our new wholesale agency partners.

I am pleased to welcome Richard Nenaber, his team in Scottsdale and our new wholesale general agency partners who will join the selective team after regulatory approvals and closing anticipated in the fourth quarter. Along with our wholesale Pennsylvania operations, they will form our entry into the higher margin Excess and Surplus market. The combined years of experience from both operations will provide us with superior market knowledge as we expand our product offerings into this new space.

Now I will turn the call over to Greg.

Gregory E. Murphy
Chairman and Chief Executive Officer

Thank you, John. Good morning. The story in 2011 has clearly been significant industry-wide catastrophe losses. PCS estimates US catastrophe losses for the 9 months at $30 billion with $6 billion from Hurricane Irene. Due to the adversity we have had the opportunity to demonstrate our service preposition which sponsors everything. Our dedicate claims and flood operations have been working around the clock, helping individuals and businesses in need recover from the devastating tornados, hurricanes and flooding across our footprint. This has been the worst catastrophe loss in Selective's 85-year history, but it's remained an earnings event. Our strong capital position should allow us to take full advantage of entering the cycle. If there is any doubt that the commercialized industry was in need of pricing discipline, the catastrophe losses should make it even more obvious.

The commercialized market place continues to firm as indicated by the Telling-House quips second quarter survey in which pricing increased 1.4% in the third quarter owing to the pricing moved higher again including a 3.2% increase for the month of September as our retention levels also edged upwards.

We have the experience working with our agents to raise price in a very granular way and we've been doing it for the past two-and-half years. Our multi-year price increases for both Commercial Lines and Personal Lines means we are earning rate increases in excess of our expected loss trends. However, given today's lower interest rate environment, coupled with higher expectations for country-wide catastrophe losses such as wind, chaos, tornados and the coastal hurricane threat, we believe pricing must move higher across the board.

For Personal Lines, we continue to achieve rate increases across our footprints. The plan rate increases for 2011 are expected to generate an additional $18 million in annual premiums. To improve the long term profitability of our Homeowners' book, our focus will be on additional rate increases as well as the potential of higher deductibles that will promote better consumer cost sharing.

We have successfully grown the top line in a disciplined manner over the past 2 quarters and we are encouraged about our future growth opportunities due to the following: most importantly our granular pricing capability which helped us deliver the tenth consecutive quarter of renewal price increases. Better than expected retention levels. The stabilizing economy has resulted in positive order premium for the past two quarters, the new business success, due to new product offerings and the improving head ratios for middle market and large accounts and our excessive surplus line, small business contracting binding authority acquisitions.

We believe our superior agency relationships, sophisticated underwriting tools and crisis strategies, allow us to outperform our peers and the industry over the long term, while delivering strong shareholder returns. Given the elevated catastrophe losses we're experiencing today, we're revising our overall 2011 guidance to achieve a statutory and GAAP combined ratio of approximately 180. Our guidance includes a two-point catastrophe loss assumption for the fourth quarter, but does not include any expectations for additional favorable or unfavorable reserve development. Weighted average shares year-end are expected to be 55 million.
Now I'll turn the call back to the operator for your questions.

Question and Answer

Operator

Thank you. [Operator instructions] Our first question comes from Mike Grasher. Your line is open, sir.

Michael Grasher

Thank you. Good morning everyone. First question just around your reinsurance program. Can you remind us the renewal period?

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

It's January 1 renewal for our Cat program. It's July 1 for our property and our casualty pro-risk program.

Michael Grasher

Okay. And I guess how are you thinking about the Cat program at this point? You've just experienced the largest event in the company's history with Irene. Does it pretty much perform in line with expectations and would you look to tweak it in any way?

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

I don't really think at the current time that there's any particular tweaks that we have in mind, although obviously we're always evaluating the marketplace and how the reinsurers react with regards to pricing and structure, but we don't have any current plans underway. We have a $40 million retention on our program. Irene had gross losses estimated at $48 million. So, so far so good, everything has performed as we would have expected for our Cat program.

Michael Grasher

And then just capital levels where they are, we expect to be no issues around that in terms of changing any of the programs?

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

Right. I would agree. I mean basically as Greg pointed out in his prepared comments, in spite of the unbelievable capacity losses that we had this year, it's still an earnings event. We had positive earnings through nine months. So it wasn't any kind of capital depletion event at all. So we feel pretty good about everything.

Michael Grasher

Okay and then I think, Greg, you were saying something about -- just want to clarify the point, 18 million expected increase in premiums for 2012. Was that commercial or personal lines or?

Gregory E. Murphy
Chairman and Chief Executive Officer

Mike, that was the personal lines expectations as a result of rate increases already taken in their annual impact on premium. So that number was and then obviously we've made no prognostications yet in terms of what our overall rate level for 2012 will be. But obviously given the market conditions in home, I think there's two areas that we're going to push on. One is going to be rate and the other are going to be deductibles to promote as I indicated before, a better cost sharing between the consumer and ourselves.

Michael Grasher

Okay, but that specifically was related to the personal lines.

Gregory E. Murphy
Chairman and Chief Executive Officer

That was specifically rated to the personal lines, yes.

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

And Mike, that was specifically rated to the impact of already taking price increases. So it’s not any kind of a growth prediction on the overall personal lines.

Michael Grasher

Understood.

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

Just want to make sure that was clear.

Michael Grasher

That’s clear and then finally, just in terms of getting more rates on the commercial side, maybe the pressure in orders comp. Does it seem like you’re just sort of getting started there, that there’s a lot more opportunity to come forward? I understand results right now are not the best, but what does that say about the future pricing of the line itself?

John J. Marchioni
President and Chief Operating Officer

Mike, this is John. I’ll take that question. So in the quarter, workers comp actually, as we said in the prepared comments, exceeded our overall price number by about a full point, came in at about 3.6%. Now, part of that is our ability to work on individual schedule mods that we have on business. The part we’re relying on is for the various state rate bureaus to take rate increases which we’ve actually started to see over the last 12 to 18 months. So our expectation is with the industry results where they are, you will continue to see hardwire rate increases come through at a state by state level and then we’ll also continue to manage our individual schedule mod usage in order to achieve a higher overall rate number. But clearly, in addition to the medical cost management work we’ve done in the claim side and some other underwriting initiatives with regard to specific segments, that line needs more rate than its currently getting industry wide and we’ll continue to push that ahead of our overall price targets.

Gregory E. Murphy
Chairman and Chief Executive Officer

And Mike, I would add too that when you really start to think about it, as the competitive landscape continues to change, a lot of our competitors have been using comp as the entry point into an account. We are an account underwriters so let’s be clear, we’re not writing mono line comp, but it is a line like John indicated that’s under the most CPI inflationary need and I think as the market starts to move, that is the line that probably needs the heaviest rate level in terms. But I think we feel pretty good about the fact that we will continue to make movement and that will be where a lot of the movement is focused in as well as some of the property indications relative to the higher storm activity.

Michael Grasher

Okay, appreciate that. Thanks very much.

Operator

Our next question comes from Doug Mewhirter. Your line is open.

Doug Mewhirter

Hi, good morning. 2 questions. The first one is about auto premiums. I noticed that the auto premiums were roughly flat with same quarter last year. Is that basically an effect of your rate increasage maybe biting a little bit into new business? You might be a little, I guess what, competitive or you might be actually getting less of the people maybe you don't want. I just want - because auto and homeowners have been tracking pretty well with growth and auto seemed to be tailing off in the last quarter.

Gregory E. Murphy
Chairman and Chief Executive Officer

I'm sorry, Doug. Did you say audit or auto?

Doug Mewhirter

Auto insurance.

John J. Marchioni
President and Chief Operating Officer

Yes, this is John again. I'll address that. Auto has been an area that we've taken - I would say we've been ahead of the market in the rate that we've taken across our footprint and you saw what the number was for the quarter. The other thing we've done is taken some pretty significant underwriting actions, which has put pressure on our new business. So the drop off you're seeing in auto is driven through the most part by new business. Retentions are still very good. Rate is still very positive, but those are designed activities to change -- improve our mix of business. From an account standpoint, we continue to see more and more improvement in terms of cross selling. So the amount of business we write that's a combination auto and home continues to increase which is also a positive indication in terms of improving mix of business. But the drop off in auto is our rate stance which has been slightly ahead of the market and some underwriting actions that we've taken to improve our mix of business.

Doug Mewhirter

Okay, thanks. That's a helpful answer. My second question, I guess 2-part question about your growing E&S business. First, with the Alterra business, the renewal rates, what's the ramp on that? I saw you did 8.5 million roughly this quarter. Is that pretty much pro rata of what we could look at for the following quarters or there are going to be more of an acceleration as you get more comfortable with the book and the underwriters?

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

Well, the book, Doug, was a $77 million book that we purchased and obviously we're exercising our renewal rights and our underwriting capabilities on that. So our expectation is to actually see that probably be a little bit less than that over the course of the year, but that positions us well we think for growth on a go-forward basis.

Doug Mewhirter

And quick follow up on that, were those policies I guess run straight through you or is there any kind of fronting arrangement while you're still transitioning?

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

Because we don't have a legal entity that's licensed for E&S, that's a fronting arrangement on the Alterra book until we're able to close on the MUSIC acquisition and then obviously with transition we'll be able to start using their paper then ultimately to renew the Alterra business onto our own legal entity at that point in time.

Gregory E. Murphy
Chairman and Chief Executive Officer

And Doug, just one other point to add. I think when you start to look into the fourth quarter, you'll get a sense of what a normalized kind of quarter run rate will be based on as we work through some of the transitional issues, some of the lag time from when business is written down by a retailer and it actually gets to one of our wholesaling agents and then ultimately to us. So I think the fourth quarter E&S premium will kind of provide a better lens as to the volume metric activity that you're going to see kind of going forward. But that doesn't include really any of the incremental penetration that we're planning for our own agents in terms of other things that we're looking at to try to move that business into that plant as well.

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

The other thing I'd point out, Doug, is that will also not include any business from MUSIC. Remember the MUSIC acquisition also comes with its own book of business of about $48 million. So we won't have any of that premium until after closing which we expect to occur sometime in the fourth quarter, possibly as late as 1-1 of 2012.

Doug Mewhirter

And actually you answered most of my follow up about MUSIC, what the volume was and just to remind, was the MUSIC, did you buy the balance sheet or is it again just the renewal rights and the licenses?

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

We bought the legal entity and all of the insurance liabilities were reinsured by Montpelier. So we didn't take any of the insurance liability portion of the balance sheet. Your normal accounts payables and things like that we took.

Doug Mewhirter

Okay, great. Thanks. That's all my questions.

Operator

Our next question comes from Bob Farnam. Your line is open.

Robert Edward Farnam
Keefe, Bruyette, & Woods, Inc., Research Division

Yes, hi there. A couple of more questions on the E&S topic. So it sounds like you're going to be renewing a pretty good portion. How are you seeing the market conditions right now? Is that relative to the standard business right now?

John J. Marchioni
President and Chief Operating Officer

This is John. We would fully expect, although the market is just now starting to firm on the admitted or standard market side, we would fully expect as that continues to firm and standard market companies start to take underwriting action on the renew book, in addition to pricing action, you will start to see business flowing out of the admitted market into the non-admitted market and as a result of that, that will also help rate and price firming on the E&S side as well. So there's going to be a little bit of lag in that regard, but as the standard market starts to firm we would fully expect over the next 12 to 18 months you're going see increased opportunity on the E&S side as a result of that.

Robert Edward Farnam
Keefe, Bruyette, & Woods, Inc., Research Division

Right. That's going to be - kind of the growth there could be more significant than it is in the standard book because you're getting the rates and more business looks I guess?

John J. Marchioni

President and Chief Operating Officer

The way we look at it.

Robert Edward Farnam
Keefe, Bruyette, & Woods, Inc., Research Division

Okay and in terms of the systems that you acquired, is the pricing there as granular as your core book and you speak of the granular pricing capability and the corporate, so I just want to know the new systems, are you just going to use them as is or you're planning on switching them over to the core platform?

John J. Marchioni
President and Chief Operating Officer

We plan on using the system capability that is in place at MUSIC. It is a very different business model from a pricing granularity perspective. That business does tend to be rated on a class basis with very little pricing flexibility from account to account. So unlike in the standard market where you could really differentiate yourself in the market by modifying your base price structure based on individual risk characteristics, that business the rates are established generally higher than ISO rate levels and not really deviated from one account to another within a given class of business.

Robert Edward Farnam
Keefe, Bruyette, & Woods, Inc., Research Division

Right. Okay, thank you.

Operator

[Operator instructions] Our next question comes from Jay Cohen. Your line is open.

Alison Jacobowitz

Thanks, it's Alison Jacobowitz. Good morning. A few questions for you. One is, are there any proposed changes in workers' comp regulation in your key states that could help your results? And then the second is, is it possible for you to give any more insight into the alternative income that we might see next quarter given the lag?

John J. Marchioni
President and Chief Operating Officer

I'll take the comp question first. There's really nothing of substance that we see on the near-term horizon in any of our states that we would expect to materially impact the results and obviously in many cases when you see the state wall change, it requires regulations to be promulgated which will delay the impact some, but I would say that we're looking more at our internal efforts on the claims underwriting and pricing side to improve our results and not expecting that improvement to come from state law regulatory changes.

Gregory E. Murphy
Chairman and Chief Executive Officer

Yes, I would say Alison, the only thing that wasn't in comp but it was in New Jersey there is some pit reform and a lot of the CPT codes and things like that they're working on, but that is - our concern is -- schedules, better protection from cost sharing that will happen within the healthcare space and that like John indicated, we're trying to do everything that we can in our own internal operations, but we are trying to push for more holistic fee schedules, better insulating of that to protect ourselves from future cost shipping that may happen into the private payers like ourselves down the road.

Dale A. Thatcher
Former Chief Financial Officer, Executive Vice President and Treasurer

And then on the alternative investments, I guess the only thing I can do is provide a little bit more color on the guidance we already provided in our prepared comments and that is, keep in mind that we did sell about $20 million worth of those alts last year end and we believe that that has decreased the correlation of our alternative performance with the broad SMP marketplace. So even though SMP is down substantially in the third quarter of this year, that one quarter lag, we don't expect to see that same kind of decrease in value for the alternatives in the fourth quarter. But obviously it all remains to be seen because there's only so much prognostication that we're able to make on those alternative investments.

Alison Jacobowitz

That's great. Thank you.

Operator

I'm showing no further questions.

Gregory E. Murphy
Chairman and Chief Executive Officer

Alright. Well, thank you all very much. If you have any follow up issues just contact Jennifer and or Dale. So thank you very much for your participation today.

Operator
Thank you for your participation. You may disconnect at this time.