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Selective Insurance Group, Inc. *(SIGI)*

Q1 2012 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, everyone. Welcome to the Selective Insurance Group's First Quarter 2012 Earnings Release Conference Call. At this time, for opening remarks and introductions, I'd like to turn the call over to Senior Vice President, Investor Relations and Treasurer, Ms. Jennifer DiBerardino.

Jennifer W. DiBerardino
Treasurer & Senior VP-Investor Relations, Selective Insurance Group, Inc.

Good morning, and welcome to Selective Insurance Group's First Quarter 2012 Conference Call. This call's being simulcast on our website and a replay will be available through May 25, 2012. A supplemental investor package, which includes GAAP reconciliations of non-GAAP financial measures referred to on this call, is available on the Investors 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 Report 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.

I'd like to take this opportunity to mention that we will be hosting Investor Day for institution investors and analysts the afternoon of the May 14 in New York City. A board group of our management team will present and we will hold a panel discussion with several of our independent agents. The event will be webcasted and can be accessed through our website beginning at 1:30 p.m. that afternoon. Please contact me if you would like to attend.

Joining me today on the call is the following members of Selective's Executive management team: Greg Murphy, CEO; Dale Thatcher, CFO; and John Marchioni, EVP, Insurance Operations; and Ron Zaleski, Chief Actuary.

Now, I'll turn the call over to Dale to review first quarter results.

Dale Allen Thatcher

Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.

Thanks, Jen. Good morning. Continued improving Commercial and Personal Lines pricing and a quiet catastrophe quarter drove first quarter results for writing an overall statutory combined ratio of 99.1%. In addition, both Commercial and Personal Lines turned in combined ratios on a statutory basis under 100, and we achieved our 12th consecutive quarter of Commercial Lines price increases.

For the quarter, we reported operating income per diluted share of $0.28 as compared to $0.30 a year ago. Improved underwriting profitability drove the results, partially offset by lower net investment income. The first quarter statutory combined ratio of 99.1% was a 3.5 point improvement from the year ago quarter.

Catastrophe losses in the quarter were $7 million pre-tax or 1.8 points. This was below our annual budget of 2.5 points but more in line with our longer term historic average. Favorable prior-year casualty development of $3 million or 0.8 points and an improvement in Personal Lines profitability drove results.

The statutory -- total statutory net premiums written were up 16% in the quarter with Commercial Lines net premium written up 18%. Commercial Lines growth included the E&S business, which contributed $26 million in the quarter along with audit and endorsement additional premium of $5.7 million. Audit and endorsement premium has now been positive for four quarters in a row.

Commercial Lines renewal pure price was up 5.1% for the quarter and retention improved 3 points to 83% from a year ago. Our granular pricing strategy has allowed us to achieve higher price increases while retention has also moved higher. The Commercial Line statutory combined ratio was 99.2% in the quarter. Commercial property and Commercial auto continued to perform very well in the quarter, reporting combined ratios of 83.9% and 96.6%, respectively.

The BOP line reported a first quarter statutory combined ratio of 99.4%, including favorable prior year casualty development of 5.9 points. The increase in the first quarter expense ratio is largely related to additional underwriting expenses associated with our E&S business, which added 1 point to both the statutory and GAAP expense ratios, half of which is related to first year acquisition expenses.

Upon acquisition, MUSIC's unearned premiums were fully seeded, which results in a GAAP underwriting expense ratio being under some additional pressure until the premium that we write is earned and is able to support the ongoing expenses of these operations. This will be the case throughout the balance of 2012.

Personal Lines net premium written grew 7% in the quarter to $66 million. And the statutory combined ratio was 97.7%, which included 4.4 points of catastrophe losses. For Personal Lines, catastrophe losses were higher by about 1.6 points driven primarily by tornado and thunderstorm activity in the South and Midwest. We were encouraged by the underlying improvement in our Personal Lines results.

Turning to investments, first quarter after tax net investment income declined 23% from a year ago to $25 million. The decline was largely driven by alternative investments, which produced after-tax income of $1.5 million in the quarter versus $7.6 million last year. While the majority of our alternative investments report on a one quarter lag, equity market performance is not entirely predictive of the performance of our alternative portfolio. This is largely due to the mix of our investments, which include energy, mezzanine debt, real estate and private equity.

The after-tax yield on fixed maturity securities was 2.6% for the quarter, down about 20 basis points from both the fourth quarter and the year ago period, reflecting the continued low interest rate environment.

Invested assets increased 5% from a year ago to $4.2 billion. Our overall fixed income portfolio maintains a high credit quality of AA minus and a duration of 3.2 years, including short-term. We began to redeploy the short-term investment position acquired from a MUSIC transaction through the purchase of corporates and selectively reentering the municipal bond market with investments in high quality issuers.

Compared to a year ago, the portfolio unrealized gain position improved to $165 million pre-tax at March 31, 2012 from $75 million. Also noteworthy is the quarter end unrecognized gaining position in the fixed income held the maturity portfolio of $45 million pre-tax or $0.53 per share after-tax.

Surplus and shareholders equity remains strong at $1.1 billion at March 31. Book value per share increased 4% to $19.76 from $19.06 at March 31, 2011, which has been restated to reflect the adoption of the deferred acquisition costs accounting change on January 1, 2012.

The restatement resulted in an approximate $1 per share reduction in historic book value per share numbers. Our premium to surplus ratio remains flat with last quarter at 1.4 to 1. We continually review options to maximize shareholder return and are encouraged by the improving insurance market conditions for growth opportunities.

Now, I'll turn the call over to John Marchioni to review the insurance operations.

John J. Marchioni

Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.

Thanks, Dale. Good morning. The market is clearly firming and we continue to find less resistance to price increases in Commercial Lines. As a result, we achieved our 12th consecutive quarter of Commercial Lines price increases with a positive 5.1%. The trend remained positive throughout the quarter with 4.5% in January, 5.3% in February and 6% in March. We fully expect this trend to continue.

We believe we're on an excellent position to take advantage of the improving Commercial Lines marketplace. We've spent years implementing pricing and underwriting tools that allow our underwriters to have the information they need at their fingertips to make and form decisions in real-time on their account portfolios.

We're on a third generation of Commercial Lines productive models. Carriers that are rolling out modeling for the first time could struggle against companies like Selective, who have had models in place and refine them over time.

The predictive model output is just one of the many tools our underwriters have to make sound policy level decisions on both rate and retention. We rolled out our dynamic portfolio manager to renew our underwriters in

2010. This tool has numerous inputs, including modeling, that assist the underwriter in maximizing results in their account portfolio. It provides what if analysis capabilities for renewal that result in optimal pricing guidance while demonstrating the loss benefit impact on the underwriters' entire portfolio. On the lesser quality business, it gives them a much better sense of true walk away pricing. This is a very strong tool and it's been embraced by our underwriters as invaluable.

Standard Commercial Lines Direct new business was up 48% to $70 million compared to the first quarter of 2011. As we continue to introduce new and expanded products to our agents and customers, we are seeing increased take-up rates for these products with our current customer base as well as helping us win new business.

New Commercial Lines business for the quarter breaks down as follows. Small account new business was up 24% to $20.3 million. Middle Market & Large Account business was up 61% to $49.6 million. As other carriers are raising rate across the board regardless of account quality, we are getting opportunities at agent control business due to the excellent relationships we have with our agency partners. This allows us to utilize our underwriting tools and sophisticated pricing capabilities to put new business on the books at actuarially sound rates. As a result, our hit ratios have improved and the number of new policy issued is up year-on-year, although still below 2010 levels. We are exercising underwriting and pricing discipline and growing in a controlled fashion.

Personal Lines premium grew 7% in the quarter while new business was down 6%. Filed rate increases that were effective for the quarter averaged 5.9% while retention improved 1 point from a year ago to 87%. We achieved profitability in the quarter and feel good about the progress we have made in changing the mix of business and maximizing rates. New business was down in the quarter due to our underwriting initiatives which are designed to drive greater profitability.

In 2012, we will continue to push rate in both the auto and homeowners books and are on track to achieve 55 weight increases with the potential for an impact of $23 million in additional premium on our in-force book. We are pleased with the growth of our new E&S contract binding authority platform which resulted in $26 million and additional premium written in the first quarter.

I'm especially pleased with how smoothly both operations have been incorporated into our operations. Effective April 1, we'll begin writing the Alterra renewal rights books of business on our own paper through Mesa Underwriter Specialty Insurance Company or MUSIC. We are looking forward to renewing a significant portion of the $120 million combined book as we deepen our partnerships with our new wholesale agency force and take advantage of the $300 million to $400 million in premium potential from our current retail agency base.

Now, I'll turn the call over to Greg.

Gregory Edward Murphy

Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.

Thanks, John, and good morning. Overall, we're pleased with our first quarter performance and the progress we continue to drive throughout the organization. There's clear evidence of a more rationale Commercial Lines pricing, terms and conditions, by almost all competitors who are now seeking increases [indiscernible] (12:54) business, with some being significant. In certain cases, they're still willing to reduce price to retain business, but in many they are holding line.

Most importantly, the conditions in the marketplace are aligned for opportunity for Selective. Our nimbleness, combined with pricing sophistication and outstanding agency relationships, provides us with high quality growth and underwriting opportunities. We benefit from other carriers who are increasing Commercial Lines price on an across-the-board or socialized basis, mainly because they're underestimating their price requirements for the worst end of the market place and overstating for the best. With our sophisticating underwriting tools, we can identify and write the best business. We're paying close attention as to who the incumbent carrier is as one needs to be cautious about the quality of the Commercial Lines business that is currently being shopped. Less sophisticated companies will ultimately become a market for adverse selection as there are a significant amount of under-performing business being pushed into the market place.

For the quarter, Commercial Lines new business was up 48% to $70 million over a weak new business production in the first quarter of 2011. Another advantage is our ability to obtain rate which is bolstered by most competitors taking an across-the-board, non-negotiable approach to rate increases. Commercial Lines rates continue to elevate which makes us much less than an outlier in the industry as we've been driving rate for three years.

Our underwriters continue to work diligently to focus on rate, on the lines, segments and accounts that are most deserving while working with our agents to obtain the best most profitable accounts. When we drive rate an excess of 10% on the lowest quality business, renewal retention drops to between 60% and 65%, whereas higher quality business that is priced around 3% to 5% retained at a solid 83% to 86% level. Again for the quarter, our Commercial Lines retention was up 3 points to 83%. Our tools enable underwriters to see the impact on their book of business of the decisions they make on price and retention on a day-to-day basis and to look ahead and plan a course of action by agent, segment and territory. We talked to our underwriters often to test the market, push for more rate increases where necessary and appropriate and to find the breaking point between price of retention.

I cannot say enough about our outstanding agency relationships. When we were driving rate back in 2009, agents closely managed our renewal books and retention remained stable. From 2009 to 2011, we did see a slowdown in new business but there is not a lot of high quality new business in the marketplace. We feel this as a sweet spot in the marketplace for us where we can achieve 5% to 7% overall rate while still maintaining strong retention and experiencing new business growth. A significant portion of premium growth, $26 million or 7 points in the quarter, was generated from our newly acquired E&S operations.

To date, we've spent a significant amount of time on the transition from a technology and processing standpoint. Now we can focus our efforts on premium growth particularly with our own agents as businesses migrating into the E&S market and pricing is starting to firm. We continue to proactively manage our cost of goods sold through a number of initiatives. We have implemented predicted modeling for both claims fraud analytics and recoveries which help us avoid fraudulent payments and to identify payments that we maybe able to recover due to fraud. These are powerful tools that are part of our overall projected three point loss reduction in claims by the end of 2013.

We expect ongoing positive renewal price increases and new business growth over the remaining three quarters in the year based on our ability to strategically utilize our sophisticated underwriting tools and strong agency relationships.

In the first quarter, there were some positive variances in underwriting and some negative variances investments. But overall, earnings came in as we expected. After only one quarter, we are maintaining our 2012 expectations as follows: a statutory combined ratio of 101.5; a GAAP combined ratio of 102.5, which do not include any additional reserve development assumptions either favorable or unfavorable; the cash fee losses of 2.5 points, about a point higher than a historical average to reflect the more severe weather patterns. Investment income is expected to be approximately flat with 2011 levels and weighted average shares outstanding of 55.6 million.

Now I'll turn the call over to the operator for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] And our first question comes from Ray Iardella from Macquarie. Your line is open.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Thanks, good morning. So couple of quick questions. I guess first maybe John or John or Greg, your commentary regarding pricing sort of your expectations, pricing would continue the momentum that you've seen over the past couple of months. Do you have any early indications sort of what you're seeing in April yet?

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.

A

Ray, this is John. We don't have an indication that we're comfortable sharing relative to April. We certainly see internally what's happening with each of our renewal inventories. But I think if you look at the trend in the first quarter and how pure price built for month-to-month during the course of the quarter and then look at the corresponding retention to reach of those time periods, it's that. Those two metrics that we look and say that we feel comfortable about where the market is and why we feel good about the trajectory we're on. And again, there's always things that could change and drive the marketplace in a different direction going forward, but everything we're seeing points to a continued firming and a strengthening of the market over the course of 2012.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Okay. That's helpful.

Gregory Edward Murphy
Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.

A

Ray, if I could add to that, John, obviously John [indiscernible] (20:09) we've got a great view and lens into what's happening. And the reason why we're uncomfortable getting a number for April is the fact that some of the tougher accounts that get negotiated go right to the end of the wire. So that creates a lot of push and pull and what happens to rate. But to give a sense of our capability, our focus know exactly what's happening and where they are. It's just the fact that some of these tougher negotiations go right to the end.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Understood, understood. And maybe talk a little bit about the E&S business. I mean is the rate that you're getting on that book, is that basically in line with the rest of the commercial book or is that better, worse? Any color would be helpful.

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.

A

Ray, this is John again. We certainly expect to see pricing firming going forward in the E&S market. We haven't reported our E&S results separately. We certainly monitor that business. We've been very focused on the transition. And again, recall that this is a renewal rights transaction. So the historical performance is not necessarily something that we monitor closely, but we certainly look at pricing relative to base rate levels and make sure those are moving in the right direction.

So I would say that we expect them to move in tandem although it won't be perfectly tight to what we were seeing in the center commercial lines market, but you're starting to see business move from the standard market into the E&S market, and certainly you are seeing more and more talk of E&S companies putting higher rate levels out on the street. They tend to stick and we would to see the same dynamic in that marketplace as well.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Okay. That's helpful. And it seems like you guys are first focused based on the commentary that on sort of getting the acquisition in place, and now it seems like you're turning your focus towards sort of your existing distribution. Is that not sort of baked into first quarter of the growth that you've seen on E&S side or is that something we can kind of see ramp up over time?

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.

A

That's something that you would see ramp up over time. We certainly have been focused on getting the transition completed, getting the technology up and running. And just in terms of our growth outlook going forward for that particular segment, there's clearly growth opportunity that we expect through deepening relationships with the wholesalers that we have with both MUSIC and STONECREEK across all 50 states. And then we think over the next several quarters, you will start to see somewhat some benefit coming through from our retail agency partners as they start to develop deeper relationships with these wholesalers and feed business to us through that means. So that – you haven't seen that really drive the production to this point, but we fully expect that to happen at future quarters.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Okay. That's helpful.

Gregory Edward Murphy
Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.

A

Yeah. Ray, I'm only going to add to that. I think you are right. That's been the focus. And even on the pricing and monitoring tools, those are some of the things that we're currently making sure we have baked into product process. So I think you said it well that this is – this first quarter was a foundational quarter, making sure we had all the processes and other things done. And then, as John mentioned, more towards the third quarter timeframe, we've got some incentives that we'll be adding to our own agents for production.

So I look at this as a three prong growth effort. One is a rate initiative that you indicated that is starting to ramp-up a little bit more in the E&S sector. The second is the normal migration in our hardening market between business moving fungibly from primary market into the E&S space. And then third will be our own agents in terms of one – or they have our incentive to sit there and consolidate more of their business with our identified wholesalers. But that doesn't mean it's guaranteed that we're going to get that business, but it's a good opportunity for us for growth.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Understood, understood. And then, maybe for Dale on the portfolio side, can you maybe talk about one, you know, the dividend income in the quarter? And then secondly, sort of the level of returns you guys expect longer term on the alternative investments and sort of how that relates to the kinds in 2012? And I'll re-queue after this. Thanks.

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.

A

Okay, sure. Well, the dividends were up because remember last year, we put in place a high dividend yield equity strategy. So that was put in place over the course of the year. So that's why you have substantially more dividends in the first quarter of 2012 versus 2011. Basically as we looked out at the marketplace and the bonds yields that were available, it was clear that – basically go into a high dividend yields strategy was adventitious given the tax advantage nature of them and just a relative yield compared with the bond portfolio, but that's why those were up.

As far as the alternative investments go, that ends up being a very lumpy type of investment. If you look at our alternatives for last year, they delivered about $20 million over the course of the year, about $11 million in the first quarter. So there's no guarantee as to which quarter things will come in or how it will come in, but we feel very comfortable with how they're performing and what we have there. So that's the one thing that we always council our analysts that it's the most difficult piece of the puzzle to prognosticate what level of income is going to be generated on a quarter-to-quarter basis.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Okay. And then I guess, the dividend income relative to 4Q, was there anything particular in fourth quarter of 2011? I guess it was $2.2 million. Were there any onetime special dividends or...

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.

A

Not one time special, but traditionally, the fourth quarter tends to be a heavier dividend quarter for equities. So it's just kind of a natural boost in that regard.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Okay. Thanks for the color.

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.

A

Thanks, Ray.

Operator: Thank you. Our next question comes from Bob Farnam from KBW. Your line is open.

Robert Farnam
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Hi, there. Good morning.

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.

A

Good morning, Bob.

Robert Farnam
Analyst, Keefe, Bruyette & Woods, Inc.
Q

Back to E&S book, just want to -- how much of that book are you renewing or is that going according to plan?

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.
A

Generally speaking, the E&S space tends to have a much lower retention level because obviously keep in mind, it's a little bit like the non-standard auto business in some ways. So people, when they are in the E&S marketplace, strive to get into the primary space. So generally speaking, retention there is about 60% historically. We're seeing retentions that are as expected, so we feel pretty good about the way we're generating business there.

Robert Farnam
Analyst, Keefe, Bruyette & Woods, Inc.
Q

Okay. And I figure it's pretty early but I understand the business as higher expense ratios, but I'm curious of the – if the loss ratio has been performing as expected. But again I [ph] pretty much understand (27:03) maybe pretty early for that?

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.
A

Yeah. It's basically too early to start talking about numbers within the E&S base with regards to that. It's all I can say basically is that it's performing as we expected to at this stage of the game.

Robert Farnam
Analyst, Keefe, Bruyette & Woods, Inc.
Q

Okay, fair enough. So how are the rate increases overall relative to the loss cost trends? We know – what impact are we going to have in the loss ratio going forward?

Gregory Edward Murphy
Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.
A

Well, I think I can tell you that the loss trends for us are in the just below 3%, right in that neighborhood, and that continues to hold pretty firm. And then rate level overall, we're earning at about that rate level or about that level or slightly higher, and then we're writing at, as John mentioned, we're at 5.1 for the quarter. And when you look at what we actually did in the month of March, it was 6. And I think when you do comparables for the Street, I would compare our numbers and retention most closely to the things that I've seen publicly which would really be traveler select program where their rate level was somewhere in – when you interpolate that graph – somewhere in the 5.5, 6 range with a 75% retention. And I think that's probably the most straight up comp out there in the marketplace. So I would say that we're overall pleased where we are relative to trend. We would like to get a little more, and as John mentioned, we expect to see that elevate as we move through the rest of the year.

Robert Farnam
Analyst, Keefe, Bruyette & Woods, Inc.
Q

All right, okay. And last question from me, was there any reserved development in Personal lines this quarter?

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.
A

There was a favorable development of $1 million in homeowners.

Robert Farnam
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Great, thank you.

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.

A

Thanks.

Operator: Thank you. Our next question or comment comes from Scott Heleniak from RBC Capital Markets. Your line is open.

Scott G. Heleniak
Analyst, RBC Capital Markets Equity Research

Q

Hi, good morning.

Gregory Edward Murphy
Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.

A

Good morning.

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.

A

Good morning.

Scott G. Heleniak
Analyst, RBC Capital Markets Equity Research

Q

Just one of you talk about the retentions. Obviously, we're pretty nicely and a lot of your competitors are reporting kind of a decline in retentions. So I'm just curious if you could talk about kind of what you're hearing from your customers and how you're able to drive this. And is there any particular areas where you feel like you're not getting enough rate and you're pulling back? It didn't really seem like that too much, but just wondering if you could touch on the retention improvement?

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.

A

Sure, this is John. I'll take that question. So we take a lot of pride – and you heard this in the prepared comments – we take a lot of pride in driving rate on a very granular basis. So when you look at how we segment our business, there's a whole host of ways we do that, and we target business based on certain risk characteristics, certain model output scores, line of business strategy, segment strategies. And if you were to look at what we would consider to be our highest target rate segments, you do see much lower retentions in that area. So that's part of it. So I would say the granular pricing strategy that we've deployed since 2009 is a big driver in that. The other big driver in that – and you've heard a little bit of this in the prepared comments as well – is relationships, and we know a lot of companies talk about relationships out there. But if you look at our ability to manage retention with price ahead of the marketplace over the last three years, that's because we go out with a granular approach.

But then we're able to have very specific conversations with our agency partners to understand where the competition is on certain accounts. But also we have a good sense as to what real walk-away pricing is on the tougher accounts. And the challenge for many companies is, when you think about performance going forward, you can't just look at past lost ratios on an account level and determine what's good business and bad business. So you could probably tools together to try to project experience going forward. And that's really where the art is – is in the work that we're talking about here. So I would put it down to great tools and a granular pricing approach along with great agency partnerships where the dialog is constantly ongoing at a portfolio level.

Gregory Edward Murphy
Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.
A

And another thing – I think I want to add to that – As the market continues to elevate in rate, I would say that in our late call in the middle quality business, they're probably is opportunity to drive more rate, but that's more market centric because you don't want to be too far out. Now you got – that's the balance that John's really talking about on a lower end. We're putting on a lot – some [ph] big (31:40) rate increases just not renewing. So you don't see that hold and stick in our rate level. But it is in our non-renewal which is in our profit improvement plan. But it's that little market that you really – I say "really" with John's "really" – how you pushed that where the market is and that's where you want to make sure you retain that business which also you want to make sure you maximizing the rate. And I think that's really what we're talking about.

Scott G. Heleniak
Analyst, RBC Capital Markets Equity Research
Q

Okay. And the – obviously, the new business was up pretty nicely. I know you've [ph] perched (32:10) that out between small and middle. I just wondering if you could break that out a little bit more just kind of by line or by class. And also I know we talk about price a little bit too, but what are you seeing as far as new business pricing, and obviously you probably not getting the same sort of rate? But just wondering if you could talk about sort of the differential between renewal retention pricing and new business pricing and kind of how you're looking at that in business.

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.
A

So this is John again. There's a few different pieces to that question. So let me just start with the type of business first. So I would say from a line of business perspective, it's pretty reflective of our enforced inventory. You don't really see major swings in terms of mix by line of business. Clearly, we continue to see some growth, some stronger growth in some of our less matured territories. So geographically, a little bit more of a mix in that direction.

And then from a segment basis, we continue to see a lot more growth outside of contractors. So that's been a concerted effort to continue to diversify. And Contractors has been great segment for us overtime. It's causality driven, so it certainly helps in terms of managing cat exposure. And we can see it to be a strong player there, but we've also made a concerted effort to diversify into non-contracting segments. And you really seen that bear proof over the last couple of years.

On the pricing side, as we talked about in prior quarters, it's much more difficult to measure pure price on the new business side because you don't have the same basket of policies to evaluate from one time period to the next. However, we have different measures in place that our underwriters use to measure both quality and pricing because the big gap, when you think about trying to evaluate that, is you could look at pricing for one period to another.

But if you don't have the same basket of polices, you have to find a way to introduce change in quality. And if you believe your quality of business is improving, which we certainly do, you would assume to be a little bit more downward pressure on pricing as a result of that. So you going to try to incorporate that into the analysis. So pricing generally on new business is under more pressure than renewal books, and that's just the dynamic of the marketplace we're in. So our risk selection quality is critically important. So we look at it. We don't report it because it's not an exact number that you can calculate like you do on your renewal book. But I can tell you that when you look at where the production's coming from, the quality of the accounts and the pricing relative to unit of exposure, we feel good about the business that we've been riding in the new business arena.

The other point to make there is while on a year-to-year basis it is clearly up. It's not nearly where it was just a few years ago. So at $70 million – and if you extrapolate that out over a year and think about what that would look like – that is not still at the levels we mentioned in 2010 in the prepared comments as a comparison. These are still not very big new business levels compared to what we've done in prior years.

Scott G. Heleniak — Q
Analyst, RBC Capital Markets Equity Research

Okay. And then my final question was just if you could touch on the reserve releases that were $3 million. Was there any area of Commercial where – you [ph] have always said (35:21) Personal Lines, you had a little bit [ph] favorable zone (35:23). Was there any areas in Commercial Lines where we had a negative development at all? And if you could touch on any change in loss cost trends, frequency or severity anywhere?

Dale Allen Thatcher — A
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.

We did not have any adverse development within any overall line of business. We had favorable development of about $1 million in the BOP line which was included in some of our prepared comments and also $1 miillion in the Commercial Auto Line and then the $1 million that we've talked about before in the homeowners.

So of that obviously, you have some accident years to develop adversely, some that develop favorably, but on an overall basis, it was all favorable development. But again, very modest at $3 million.

Scott G. Heleniak — Q
Analyst, RBC Capital Markets Equity Research

All right. Thanks a lot.

Operator: Thank you. [Operator Instructions] Our next question or comment comes from Alison Jacobowitz from Merrill Lynch. Your line is open.

Alison Jacobowitz — Q
Analyst, Bank of America Merrill Lynch

Hi. Thanks. Two questions. I was wondering on the non- cat weather I didn't hear it all there. If I missed it, I'm sorry. But was it better than expected given the mild winter? And then I was wondering if you could talk just a little more about alternative investment income. I know it doesn't exactly move with the S&P but if you could just talk about maybe some of the asset classes and what maybe held back the performance a little bit this quarter relative to the market.

John J. Marchioni — A
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.

On the properties – it's John – on the property side, you see the cat numbers but we also had a solid quarter from a non-cat property standpoint in both personalized and then commercial property.

Dale Allen Thatcher
Chief Financial Officer & Executive Vice President, Selective Insurance Group, Inc.
A

And as far as the alternative investments, where we are, we've got – there's real estate. There's mezzanine financing. There's the stress debt. There's private equity. There's secondary private equity. And there's also energy. I wouldn't say that there's anything particularly that held it back. Obviously, the dollars weren't nearly as strong as we had in the first quarter of last year. You just didn't have as much M&A activity during the quarter. And as – if you look at our alternative portfolio, we have not invested new money into the portfolio in a few years. Therefore, most of these are more in the harvesting stage of their lifecycle. Therefore, if you've got reduced M&A activity, you're going to see less income in those kind of quarters.

Alison Jacobowitz
Analyst, Bank of America Merrill Lynch
Q

Okay, thanks. And one other question if I can ask. In the Personal Lines to the price increases – I don't know if you can give it or generally talk about it, and again if I – if it was in there and I missed it, I'm sorry – but the homeowners versus the auto rate increases, if you could put a number around what you're seeing there or what you're doing there?

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.
A

Yeah. So for – this is John. In Personal Lines the total was 5.9% and that broke down to 5.5% on Auto and 7% on Home.

Alison Jacobowitz
Analyst, Bank of America Merrill Lynch
Q

Thank you.

Operator: Thank you. Our next question or comment comes from Ray Iardella from Macquarie. Your line is open.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.
Q

Thanks for taking my follow-up. Just wanted to maybe touch on some of the claims initiatives you guys are working on. And I guess certainly you're going to get some improvement, I think, from the rate side, but maybe can you talk about – is there anything you guys have been learning from the claim initiatives? And do you still I think – I believe the thought process is 3 points of improvement to the loss ratio by 2013?

John J. Marchioni
Executive Vice President-Insurance Operations, Selective Insurance Group, Inc.
A

Yeah. This is John. I can certainly start with that and then Greg could add if need be. So I – there's really a series of initiatives across all major lines of business that are designed to drive that improvement. We have actually seen some of it manifest itself already and continue to see that into 2012, but if we just look at the major lines and you start with Worker's Comp, there's clearly lot of effort around improving medical management, and the that's a big driver of loss experience on the Worker's Comp side. So improve networks, improve case managing capabilities. But then the other change that we've implemented – and this applies to both comp and liability – is a higher degree of specialization.

So if we look at comp, the ability to have your claim adjusters well trained in a specific area, be it your fast track short term medical claims, your loss time claims versus your longer term resolution type work. And the key there would be not just having people who are well trained in a specific area of claims handling, but then making sure you [ph] treat our (40:07) process, get the claim for the right person as early in the claim life cycle as possible. So I think that's been a big part of we've done on the comp side. You combine that with the medical management improvements. And then the same concept on the liability side where we've created a complex claims unit to make sure that we're getting those more complex liability claims, again, into the hands of a well-schooled and well-trained complex claim handler as early in the process as possible. So there's other initiatives around making sure that you're managing your property losses and your contents of repricing perspective that we've done. So a series of other initiatives that drive down loss cost, but I would say those in the liability and comp area, we would expect to be the big drivers. And we think we are very well on track to that three points by '13 that Greg alluded to in the prepared comments.

Gregory Edward Murphy
Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.

A

And then I will add to that Ray. Even some the – I touched on, a little bit, some of the analytics that we're doing and been very exciteful relative to fraud, relative to recovery. And now even on the fraud side, you're looking for tendencies in your own inventory, but now we're also starting to kind of use that data and look at claims that are being presented to us on the liability side where we're getting claims information later on in the process. This is again providing that supplemental knowledge base that help to feed some of these tight types of cases. And then even, as John touched on, even on the expense side, how we're managing our panelist debt counsel, the things that we're doing on recovery relative to better managing that cost structure. So I want to say it's holistic and we feel very good about our positioning in the marketplace relative to the initiatives.

Ray Iardella
Analyst, Macquarie Capital (USA), Inc.

Q

Great. Thanks for all your answers.

Operator: Thank you. [Operator Instructions] One moment while we wait for questions. And I'm currently showing no further questions or comments at this time.

Gregory Edward Murphy
Chairman, President & Chief Executive Officer, Selective Insurance Group, Inc.

Well, thank you for participating in the call, and I would strongly encourage you to attend our upcoming investor day on May 14 where you'll have an opportunity to see for yourself some [indiscernible] (42:47) of our management team and spend time with four of our superior independent agents. For the details on this event, please call Jennifer. Thank you very much.

Operator: That concludes today's conference call. Thank you for your participation. You may disconnect at this time.