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Horace Mann Educators Corp. (HMN)

Q2 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings, and welcome to the Horace Mann Second Quarter Earnings Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

I'd now like to turn the conference over to your host, Ryan Greenier, Vice President of Investor Relations. Please go ahead, sir.

Ryan E. Greenier
Vice President-Investor Relations, Horace Mann Educators Corp.

Thank you, Rob, and good morning, everyone. Welcome to Horace Mann's discussion of our second quarter 2017 results. Yesterday, we issued our earnings release and investor financial supplement. Copies are available on the Investors page of our website.

Our speakers today are Marita Zuraitis, President and Chief Executive Officer, and Bret Conklin, Executive Vice President and Chief Financial Officer. Bill Caldwell, Executive Vice President of Property and Casualty, and Matt Sharpe, Executive Vice President of Life and Retirement are also available for the question-and-answer session that follows our prepared comments.

Before turning it over to Marita, I want to note that our presentation today includes forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. The company cautions investors that any forward-looking statements include risks and uncertainties and are not guarantees of future performance. These forward-looking statements are based on management's current expectations, and we assume no obligation to update them. Actual results may differ materially due to a variety of factors, which are described in our press release and SEC filings.

In our prepared remarks, we may use some non-GAAP measures. Reconciliations of these measures to the most comparable GAAP measures are available in the supplemental section of our press release.

And now, I'll turn the call over to Marita Zuraitis.

Marita Zuraitis

President, Chief Executive Officer & Director, Horace Mann Educators Corp.

Thanks, Ryan. Good morning, everyone, and welcome to our call. Last evening, we reported second quarter operating income of $0.02 per share. This result reflects another quarter of elevated weather volatility for the entire P&C industry and does not reflect the underlying earnings power of our business.

The convective storm activity we saw in Colorado, Texas, Minnesota and other areas of the Midwest created unprecedented levels of hail and wind damage. In fact, the Colorado storm has been estimated as the costliest hail event in the states' history. And while these storms clearly affected our bottom line, it also underscores why we are here.

At Horace Mann, we help educators protect what they have today and plan for a successful tomorrow. As a result of this significant amount of adverse weather in the quarter, we've delivered on that promise for thousands of customers.

I'm confident that the significant efforts of our entire claims team continue to provide industry-leading customer satisfaction. After all, this is why we are in the P&C business to help educators put their lives back together after the unthinkable.

That said, the earnings impact for the quarter was significant. The volatile weather impacted both our second quarter catastrophe losses, which were the second highest in our company's history, as well as non-cat weather impacting our underlying auto and property loss ratios.

Given the significant weather related loss impacts, I think it's important to note that our prior year loss experience also contained heavier than normal weather related losses. But even with those impacts, we still have a profitable book of property business that ended 2016 with a 90.1% combined ratio. This is a strong profitable result given the significant impact weather had on the entire industry last year.

As a P&C insurer that writes property exposure, we know there is an inherent volatility in quarterly results. It's important to analyze and react to quarterly volatility appropriately. But what is important is the [ph] sum of the tapes (03:51). And despite the difficult start to the year, we remain optimistic that our property book will have a reported combined ratio around 100% in 2017, provided third and fourth quarter weather follows historic patterns and is similar to what we saw over the past few years.

In addition, we are encouraged that when you look past the weather impacts in the quarter, our underlying auto results are moving in the right direction. Our Life and Retirement business continues to grow. These two divisions contributed $17.4 million or $0.42 per share to this quarter's results, underscoring the earnings diversity of our multi-line business model.

Looking more closely at the P&C results in the quarter, we experienced 16 catastrophe events, which resulted in $32.4 million or $0.51 per share of catastrophe losses. In May, the Denver area experienced baseball-sized hail, which generated $8 million in losses. And in June, a series of large convective storms hit the upper Midwest, mainly Minnesota, which alone generated another $10 million in losses.

I think it's important to note that there were 29 PCS-declared catastrophes in the first half of 2017. This is the largest amount in the first half of the year since we've been tracking PCS catastrophes.

In addition to significant catastrophe losses, there was also historic level of non-cat weather events in the quarter. We have consistently used a strict PCS definition for named storms and specific states impacted to determine our catastrophe losses. As a result, in the quarter where you have record levels of smaller but still potent convective storms, you would expect to see an increase in non-cat weather related losses. And we like other carriers that use a similar catastrophe definition clearly have seen these impacts.

Non-cat property losses increased nearly 10 points compared to a favorable experience we saw for non-cat weather in the second quarter of the prior year. To put this in perspective, based on our historic loss patterns, we typically see around 25 points of non-cat wind, water and hail.

In 2016, we had one of the lowest level of losses related to these perils in recent history at 20 points. This year that trend flipped to one of the highest quarters at 30 points. This 10-point increase is worth $0.08 of earnings and was the significant contributor to the results in the quarter.

Unfortunately much of the weather related loss activity across the country this quarter occurred in geographies where we have a strong market presence. Based on broader industry data, we believe our losses are in line with our market share in these impacted geographies.

For example, Minnesota is our fourth largest state in terms of premium volume. As a result when there is a significant weather event that affects this entire state, we're going to have a sizable weather related loss and you saw that dynamic this quarter.

But it doesn't mean that we're over-penetrated in Minnesota. We always monitor exposure maps and review sub zip code concentrations. But when an event is so large, it's hard to avoid the widespread damage.

As a personal lines carrier with a national footprint, it's also important to have a wide spread of exposures across many states, including those states that historically have low catastrophe exposure. We have been working on building our premium base in markets where we have historically been underrepresented.

For example, we have identified target growth states such as Pennsylvania that have strong P&C profitability, lower than average weather related volatility and educators with higher than average disposable income that can support greater levels of retirement savings and larger life insurance purchases.

In addition to targeting marketing campaigns, we have prioritized agent recruitment in these markets. We're confident that over time, this intense focus on a more diversified geographic mix and a deliberate focus on the most profitable educator segments will help reduce the quarterly volatility that we do see in periods with heavy convective storm activity.

But spread is one component of managing a profitable P&C book. The others include strong product management, disciplined underwriting and an appropriate rate action that outpaces loss cost.

Over the past few years, we've increased the use of higher deductibles in markets prone to convective storm activity, implemented sizable property rate increases to account for weather related volatility, and tightened our underwriting appetite in certain markets. And these efforts are what drove the strong property performance last year when we achieved a 90% combined ratio.

Given the peril mix that drove property results in the quarter, we did see a similar uptick in weather related losses in auto. The frequency of weather related claims increased, and similar to last quarter, we attribute 1 to 2 points for the increase in this underlying loss ratio to weather related causes.

Looking at underlying auto results through the first six months of the year, the combined ratio of 105.7% is running about 2 points higher than the previous year. This is entirely attributable to an increase in the frequency of weather related claims. Non-weather related frequencies and severities have stabilized in the low single-digit range consistent with our pricing models. Unfortunately, this quarter's weather related results will pressure our ability to generate a 1 point improvement in the underlying auto loss ratio for the full year of 2017.

We remain laser focused on moving our auto book back to the high 90s and are taking even further rate and underwriting actions as we continue to grow in profitable markets. We responded early to elevated auto frequency and severity trends in 2015 taking decisive action to increase our rate plan, tightened underwriting and improved our clams operations. And over the course of 2015 and 2016, we continue to increase or exceed our rate plan, moving from an annual plan of 4% in 2015, 6% in 2016 and setting a 2017 plan of 8%.

Given the additional weather volatility, an unprecedented level of industry-wide auto catastrophe losses, we continue to take even more rate beyond our original plan and are on track for an 11% rate increase in 2017. While this additional rate will impact written premium in 2017, it will take some time to earn in. As a result, we now expect margin improvement in auto to emerge in 2018, which is a few quarters longer than we originally anticipated. Our confidence is strengthened by the improvement that we already see in our underlying auto loss results when you exclude the historic weather related impacts.

Despite these rate actions, our retention is holding for preferred educator business. That said, we are seeing modest retentive impacts as we are shedding business that no longer meets our profitability targets.

Auto business with lower policy limits, non-educator auto or auto in states that are challenging from a regulatory or a loss cost trend perspective can be placed with a partner carrier either progressive or through our Horace Mann general agency relationships, and therefore, we can retain the customer relationship.

Through June, the consumer price index data indicates auto rates have increased by nearly 8% for U.S. customers compared to the prior year. This is a meaningful increase and illustrates we're not alone in our rate actions. Clearly, the combination of distracted driving, higher miles driven and an increase in the frequency and severity of convective storm activity has resulted in an industry-wide need for continued rate increases.

With average auto insurance costs increasing at rates higher than inflation, it is critical that our educator customers understand the drivers behind the rate increases. In order to maintain strong customer satisfaction and retention, on that front, we launched a multi-channel rate change education campaign to advance the dialog about how macroeconomic trends and consumer behaviors are affecting auto insurance rates.

We believe these customer-centric efforts will mitigate the potentially disruptive impact of double-digit rate increases may create. But more importantly, we believe this discussion will be critical in changing perceptions and attitudes around distracted driving.

Before turning to Life and Retirement, I want to reiterate that improving P&C profitability is our number one priority. We like the broader industry are experiencing historic levels of weather related losses and are clearly seeing troubling weather trends. More severe convective storms continue to increase in frequency.

While this data will work its way into pricing over time, we are keenly focused on ensuring our rate plan includes adequate increases to account for this volatility and incorporates recent trends in our pricing models. Our 2017 rate plan for auto and property was influenced by the heightened weather volatility in 2016. But given the results for the first half of 2017, as I said, we will clearly push more.

We will continue to take rate, further tighten our underwriting in certain segments and geography, while also doubling down on growth initiatives in target states with accretive loss ratios. And while the expense ratio was modestly lower in the quarter due to the timing of certain expenses, we continue to look carefully at expenses and we'll take targeted actions where appropriate.

Life and Retirement results were a bright spot in the quarter. Insurance in force for Life businesses continue to grow. Sales were solid and earnings were up 20%. Earnings benefited from favorable mortality in the quarter, as well as solid investment income.

In April, we launched our new suite of individual annuity products, Personal Retirement Protector as well as the new custodial IRA platform. In addition to the product launch, we also launched our proprietary educational tool [indiscernible] (14:51) in June.

This tool which is administered by our agency force aggregates the customer's household and financial information and helps our agents make product recommendations that will allow a customer to achieve their financial goals. It will also review P&C and life insurance coverage levels, given household income, assets and retirement goals.

For those customers with more sophisticated financial planning needs, we also launched an internal team that can partner with our agents to provide financial planning services and recommendations for those educators who have wealth planning needs that are more clearly aligned to the emerging and mass affluent markets.

This multi-pronged approach will provide a level of consistency to the Horace Mann agency experience and replicate the sales practices of some of our most successful financial services agents.

We have been training our agency force on the new products and sales process and agent reaction has been favorable. This new approach combined with the compensation changes and product redesign allows us to provide consistent, holistic solutions to all of our educator clients and significantly advances our products, distribution and infrastructure.

We've been making good products and progress on PDI enhancements for quite some time. Last year, we launched our open architecture 403(b) group platform, then modernized our individual product offerings. And this year, we have moved to a fee-based compensation model and refined our sales processes to better align with providing customized recommendations and solutions.

We also overhauled our infrastructure to offer simple, user friendly online, phone and agent-led enrollment opportunities. Our institutional team continues to make headway introducing our innovative Horace Mann group Retirement Advantage product to more and more school districts. The sales pipeline for institutional business is longer than our retail products, and we expect our investments in this team to produce meaningful increases in assets under management in 2018 and beyond.

Overall, the innovations we've made over the past few years in our Retirement business were the required investments to transform Horace Mann into a nimble, customer-centric solutions provider that can serve the needs of both school districts and individual educators, regardless of their channel preferences and wealth planning needs. We're confident these investments will accelerate our asset gathering abilities, attract more agents and advisors to our unique value proposition and allow us to continue to take share in the 403(b) retirement space.

While this quarter's reported results were disappointing, I remain confident we are on the right path. Looking past the sizable weather related impacts, our auto profitability improvement initiatives are taking hold, and we are seeing strong results in Life and Retirement. Those strong results provide ballast in what has turned out to be a historic level of weather related losses in the first and second quarters of 2017.

By focusing on the educator and putting their unique needs at the center of everything we do, we are differentiating ourselves in the marketplace and are establishing Horace Mann as the preferred insurance and financial service provider to educators. Our unique value proposition is sound and we're making the right investments to attract more school districts, educators and agents to Horace Mann, which will over time accelerate profitable growth.

Thanks. And now I'll turn the call over to Bret.

Bret A. Conklin

Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.

Thanks, Marita. And good morning, everyone. Second quarter operating income of $0.02 per diluted share was $0.23 lower than the prior year quarter, with nearly all of the difference related to higher weather related losses in the P&C segment.

As a result of the sizable weather impacts in the quarter, we have revised our annual earnings guidance to $1.45 to $1.65 per diluted share. These revisions reflect the elevated catastrophe and non-catastrophe losses incurred in the first half of the year.

Our estimates for weather related losses for the second half of the year remain consistent with historic averages, which are significantly less volatile than the first half of the year. We have updated key driver guidance as well. And I will provide more details as we cover each business segment.

The P&C segment had an after tax loss of $13.9 million in the quarter, compared to a loss of $4.5 million in the prior year quarter. On a reported basis, the combined ratio was 118.5%, catastrophe losses of 20.2 points were 2.5 points higher than the prior year. The underlying loss ratio increased by nearly 5 points. The increase for both was related to adverse weather.

The expense ratio declined modestly in the quarter largely related to the timing of non-capitalized systems modernization expenses. Similar to last quarter, prior accident year property reserves continue to develop favorably and accounted for all of the releases in the quarter.

Within auto, we are seeing non-weather related loss trends stabilize. The underlying combined ratio for the first half of the year was 105.7%, 0.5 point higher than our full year 2016 results, despite the first half of 2017 having over 2 points of weather related losses. In a more normalized weather period, we would have expected to see improvement.

While our profitability improvement initiatives are taking hold and our rate plan is accelerating, the impacts of weather related claims in the first half of the year will impede our ability to generate 1 point of underlying loss ratio improvement in 2017.

We remain on track, but our path to a lower underlying combined ratio is now a quarter or two longer, and we expect to see improvement in 2018. As a result, we expect the full year 2017 underlying combined ratio to be similar to 2016 results.

The underlying combined ratio for property was 82.5% for the quarter. On a year-to-date basis, the reported property combined ratio is 118.6%, a level we expect to come down in the second half of 2017 as typically our second half property results are stronger than the first half. On a full year basis, we now expect the reported property combined ratio to be around 100%, which reflects the year-to-date adverse weather results.

P&C written premiums increased 5% to $168 million, largely due to rate actions. As Marita mentioned, we continue to increase our rate plan and now expect 11% for auto and over 4% for property in 2017. This will further increase written premium. However, much of the margin expansion related to these increases will occur in 2018 as the increases earn in. In addition, customer retention remains high at 83% in auto and 87% in property.

P&C sales increased 6% in the quarter with auto up 7% and property increasing 4%. Much of the increase was driven by rate, as sales were relatively flat on a unit basis compared to the prior year. We remain focused on ensuring new business is profitable and our focusing marketing efforts in profitable geographies and segments, while further tightening our underwriting appetite in certain markets.

Life segment operating earnings excluding DAC unlocking were $5.5 million, a 22% increase from the prior year period. Mortality costs were nearly $1 million favorable compared to the prior year, and net investment income was modestly higher.

Life sales of recurring premium products were solid, in line with the prior quarter at $1.9 million. Single premium sales were modestly lower at $1.8 million, and for the first six months of the year, Life sales were up 18%. We continue to expect double-digit growth in Life sales, as one of our key strategies is to continue to grow the life insurance business, thereby increasing the share of mortality-based earnings for the company.

In the Retirement segment, operating income excluding DAC unlocking was $12 million, a $1.3 million decrease compared to the prior year. The annualized net interest spread of 189 basis points improved 4 basis points compared to the prior year and reflects continued strong investment portfolio performance.

Alternative investment returns were on track with our 7% annual return assumption in the quarter, and prepayment activity was similar to the level we saw in 2016. Offsetting the higher net investment income and growth in contract charges earned was a $3.2 million increase in operating expenses. These expenses are related to the build-out of our new modernized Retirement product suite, of which DOL compliant expenses is a component, as well as the addition of the institutional sales team.

Retirement assets under management grew 7% to $6.5 billion, reflecting continued sales momentum, strong recurring deposits, and market appreciation for our variable annuity accounts.

Consolidated net investment income increased modestly to $92 million. For the quarter, alternative returns were positive and on target, but below prior year. The combination of lower interest rates and tighter credit spreads challenged our ability to put money to work in the quarter resulting in a new money reinvestment rate that was in line with our 4% target. Our purchases this quarter focused on conservative asset balances, like agency debt, investment grade corporates, taxable munis and high quality structured securities.

Given the continued growth of online retailing, the retail sector has been a focus in the news lately. We have approximately $230 million of retail related exposure in our portfolio with a net unrealized gain of $6.5 million, which is primarily investment grade and has spread across various asset classes. We are very comfortable with our retail exposure and continue to work with our investment managers to monitor the changing landscape.

Overall, on a reported basis, book value per share increased to $33.49. The net unrealized gain position on investments was $433 million, an increase of nearly $82 million during the quarter, largely due to lower interest rates and tighter spreads.

In summary, our results for the first half of 2017 do not represent the normalized earnings power of our business model. Historic levels of weather related losses significantly impacted P&C operating results and obscured progress we are making in improving auto profitability.

Our Life and Retirement businesses continue to profitably grow. We are confident that the investments we are making today will result in appropriate sales growth, which over time will result in improved ROEs as we add scale. Retirement sales continue to be solid, and we are encouraged by a growing institutional RFP pipeline. And our Life segment is clearly performing well.

Despite the significant weather impacts in the quarter, I am confident that we remain on the right track for long-term profitable growth, and we are successfully executing our vision to be the preferred insurance and financial services provider to the nation's K-12 educators.

Thanks. And I will turn the call back over to Ryan to start the Q&A.

Ryan E. Greenier
Vice President-Investor Relations, Horace Mann Educators Corp.

Thanks, Bret. Rob, please open the line up to begin the Q&A portion of the call.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Thank you. Our first question today is coming from the line of Chris Campbell with KBW. Please go ahead with your question.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Yes, hi. Good morning.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

Good morning.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.

Q

My first question is just if I'm looking at the sequential change in the auto loss ratio, that was about up 590 bps, and if you just back out (sic) [back out of the past cat's] that's 280 bps. So that gives you 310 bps delta. Now if non-cat weather was a similar 100 bps, 200 bps headwind this quarter, I mean how bad would it have been excluding the auto rate actions that you've taken to this point?

William J. Caldwell
Executive Vice President-Property & Casualty, Horace Mann Educators Corp.

A

So just to back up with the 105.7%, that was about 0.5 point above our year-end results. Our rate actions were planned for 8%. We're now at 9.5%, we're at 11%. I will say those rate actions are front-loaded. So when you think about the 11%, 40% of that is in the last quarter.

Those to go back and back out the rate actions for the first half results would be difficult. But I will say that I like the progress that I'm seeing from an earned premium perspective. We're getting the rate that we want filed and approved and implemented. It's just a matter of translating that written premium into earned premium.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

Yeah. And the only thing I'd say is what we said in the script, clearly, when you back out cat and non-cat weather on a year-to-date basis, we are on track for that 1 point improvement that we had talked about. Obviously, the weather impact for the first half of the year is nothing that any one planned for.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Right. Now is it possible to get a breakdown of that targeted combined ratio by attritional losses, cats, non-cats weather and expenses for auto?

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

I mean certainly, we have all that data, we'd be glad to follow up with the specific detail, we have it all.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Perfect. Very, very helpful. And just one more question on auto – I'm sorry, go ahead.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

I said no problem at all.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. Is there any significance in the absence of any favorable auto development this quarter?

Bret A. Conklin
Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.

A

No, I think that's – this is Bret, Chris. As is typical, certainly, the first half of this year we've only released – we have reserved releases on the Property segment. Auto, obviously, we've had pressure there, as we talked about on the last call. We'll book it if we see it. But certainly, we're weaving that into our price increases. But until we see the development, we're not booking anything.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

And I think it's also important to reiterate that what we have said consistently hasn't changed. We are conservative reservers, we remain conservative reservers and we tend to pick well above the mid range of many of the models that we run in our reserving and that level of conservatism, hard word to say, hasn't changed and won't change.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Thanks. That's very helpful. And then on the tax rate on the P&C net investment income, is there anything special going on there? And we know it's obviously a little bit lower this quarter.

Bret A. Conklin
Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.

A

No. And Chris, I think as you look out to the full year too obviously with the significant losses we took in the quarter, probably a more normalized rate that you'd probably want to use for your full year, for the consolidated basis might be in a range of more 20% to 22% effective rate. As you recall, last year, our consolidated tax rate was about 26%. So I think as you look to year end 2017, 20% to 22% would be the kind of range of effective tax rate you want to use.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. And just one final one on the Life segment, what was driving the favorable mortality this quarter?

Matthew P. Sharpe
Executive Vice President, Life and Retirement Division, Horace Mann Educators Corp.

A

The mortality is – I can't point to any specific cause for the mortality. The favorable mortality has the similar trend that we saw the last quarter. I mean it's not anything specific to our book, I don't think.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.
A

And still within the model, the actuarial range that we model over the whole book.

Christopher Campbell
Analyst, Keefe, Bruyette & Woods, Inc.
Q

Okay. Thanks. That's very helpful. Thanks for all the answers and best of luck in third quarter.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.
A

Thank you.

Ryan E. Greenier
Vice President-Investor Relations, Horace Mann Educators Corp.
A

Thank you.

Operator: Our next question is from the line of Robert Glasspiegel with Janney. Please proceed with your question.

Robert Glasspiegel
Analyst, Janney Montgomery Scott LLC
Q

Good morning, Horace Mann.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.
A

Hey, Bob.

Bret A. Conklin
Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.
A

Morning.

Robert Glasspiegel
Analyst, Janney Montgomery Scott LLC
Q

Is there something going on in auto beyond non-cat and cat, whether couple attacks at this I mean, it was just unlucky, but driving the first half, you're pushing rate harder than you thought you were going to push. So are you needing to price for something else?

And put another way, yeah, your underlying is up a couple points year-over-year in the first half, but the second half comparisons are up against about 107%-ish and underlying. And it seems like you're saying you can't do a 105% in the second half underlying which would be 106%, 107% with cats. It seems like your second half underlying targets are pretty unambitious, given how much rates you're getting. So is there something else going on besides weather that's making you chase upstream on the auto?

William J. Caldwell
Executive Vice President-Property & Casualty, Horace Mann Educators Corp.

A

Yeah, Bob. It's Bill. As we said in the script, there's about 2 points here of weather related. Excluding that, we like the trends that we're seeing. We're seeing the earned rate impact come in. We're seeing it retain. We like the underwriting actions that we're taking. Our claims actions are holding. We're seeing severities hold in the low single digit range. So the underlying trends I think are good. We're just overcoming about 2 points of weather activity in the first half of the year.

Robert Glasspiegel
Analyst, Janney Montgomery Scott LLC

Q

Why do you need to step up your – I'm sorry.

William J. Caldwell
Executive Vice President-Property & Casualty, Horace Mann Educators Corp.

A

Yeah, we do need to – we do and we have stepped up our rate actions. We plan for 8% this year. We're forecasting now 11%. 40% of that is in the last quarter. So from an implemented to written to earned timeline, that will really be a 2018 impact for that incremental rate. But certainly, the 8% percent was aggressive and now we're 11%. We'll continue to identify, diagnose and react as we continue to see these adverse trends.

Robert Glasspiegel
Analyst, Janney Montgomery Scott LLC

Q

I guess, my question though is if you're on track ex bad luck, why push rate further, why the need to push rate further?

William J. Caldwell
Executive Vice President-Property & Casualty, Horace Mann Educators Corp.

A

Well, we don't expect that these weather activities won't continue. So when they do occur, we put them into our analysis and they convert into rate at some point.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

Yeah. Not to mention the fact that the weather's already occurred, it's there. When you look at the consumer price index, when you look at all the data that we have as well as what we're seeing from competitors, it seemed prudent to push that level of rate, especially considering the retention that we have across our book.

When you look at the rates that we pushed, the 4%, the 6%, the 8%, we got it with very minimal impact on retention. And then you look across what we're hearing from our competitors in the states and it seems prudent to push that level of rate. Bob, you know that you always look at the percentage of new business. You look at your retention and you look at your ability to push that rate and it's there. So it seems to make sense that we continue to push what's appropriate, and you got to pay for that whether, it happened.

Bret A. Conklin
Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.

A

Yeah. And maybe to dovetail on that, certainly, as we told the Street, our plan was to get 1 point improvement to arrive at 104%, but certainly that is not our long-term combined ratio goal. So we've got to eat away at it. But as we've said before, we'd like the total P&C to be in the mid 90s, with auto probably in the high 90s and the property in the low 90s. So it's – our plan was 104%, but that certainly is not the long-term plan.

Marita Zuraitis A
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

Absolutely, right.

Robert Glasspiegel Q
Analyst, Janney Montgomery Scott LLC

Let me try one last try. You're getting more rate than you thought. Has your underlying second half assumption improved from where you went into the year?

Bret A. Conklin A
Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.

Our second half assumptions are in line with our plan. We're assuming normal weather activity. It's typically later in the third and fourth quarter. As you know, Bob, fourth quarter is typically not a great quarter for our auto book. We expect that to be consistent with prior years. But nothing unusual about the back half...

Robert Glasspiegel Q
Analyst, Janney Montgomery Scott LLC

But I'm saying there's more rate in the second half than you thought you were going to have...

Marita Zuraitis A
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

Yeah, but like we said in the...

Robert Glasspiegel Q
Analyst, Janney Montgomery Scott LLC

So I would think the underlying would be in better shape for the second half than you thought unless...

Marita Zuraitis A
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

So like we said in the script, Bob, that will have minimal effect and it'll take longer for those rate increases to earn in, which is why we think you'll begin to see that emergence in the first couple of quarters of 2018.

Robert Glasspiegel Q
Analyst, Janney Montgomery Scott LLC

Okay. I'll follow up online. I'm still a little confused. I'm sorry. On the expense ratio, have you changed your target for the year? You actually improved year-over-year through six months.

Bret A. Conklin A
Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.

Yeah. Bob, this is Bret. We have not changed our target for the year at 27.5%. I believe, June to June, we're basically pretty much spot on 27.3% versus 27.3%. So, we'll have some timing issues from quarter-to-quarter. But no, we're still targeting 27.5% for the full year.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

And like I said in the script, Bob, we'll continue to look for opportunities to tighten our belt. After a quarter like this, you do have a fair amount of losses. I think it's prudent for us to look for those places where we can tighten our belt, be a little more conservative from an expense standpoint, but we're not changing any of our plans or targets.

Robert Glasspiegel
Analyst, Janney Montgomery Scott LLC

Q

Okay. Thank you very much.

Marita Zuraitis
President, Chief Executive Officer & Director, Horace Mann Educators Corp.

A

Thanks, Bob.

Bret A. Conklin
Executive Vice President and Chief Financial Officer, Horace Mann Educators Corp.

A

Thanks.

Operator: [Operator Instructions] Thank you. I'd like to turn the floor back to Ryan for further remarks.

Ryan E. Greenier
Vice President-Investor Relations, Horace Mann Educators Corp.

Thanks. And thank you all for joining us this morning on Horace Mann second quarter earnings call. If anyone does have any further questions, don't hesitate to reach out to me or Kristi Niles. Thank you very much.

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