

FINAL TRANSCRIPT

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SIGI - Q1 2009 Selective Insurance Group, Inc. Earnings Conference Call

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PRESENTATION

Operator

Good day, everyone. Welcome to the Selective Insurance Group's first quarter 2009 earnings release conference call.

At this time, for opening remarks and introductions, I would like to turn the call over to Vice President, Investor Relations, Ms. Jennifer DiBerardino.

Jennifer DiBerardino - *Selective Insurance Group, Inc. - VP of IR*

Good morning, and welcome to Selective Insurance Group's first quarter 2009 conference call. This call is being simulcast on our website, and the replay will be available through May 29th, 2009. 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, at www.selective.com.

As stated in our quarterly release, we have revised our SEC reporting segment by reclassifying the Diversified Insurance Services segment, which contained Flood and Selective HR Solutions. As Flood is managed by insurance operations and included in insurance results by our competitors, it will now reside in that segment. Selective HR Solutions will be reported in its own segment, and the Investment segment remains the same. All financial information disclosed by the Company will reflect this change.

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Selective uses operating income, a non-GAAP measure, to analyze trends in operations. Operating income is net income excluding the after-tax impact of net realized investment gains or losses. 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 updating 10-Qs filed with the US 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, Chief Underwriting and Field Operations Officer; Mary Porter, Chief Claims Officer; Ron Zaleski, Chief Actuary; and Kerry Guthrie, Chief Investment Officer. Now I'll turn the call over to Dale to review the quarter results.

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

Thanks, Jen. Good morning. We reported solid insurance results in the quarter with a statutory combined ratio just over 100% and within overall expectations, despite incurring \$15 million in property losses over our budget. Results benefited from an overall \$4 million in favorable reserve development, as well as additional expense savings. Commercial lines new business was up 12% in the quarter to \$71 million, and we are very encouraged by the direction of our commercial lines pure pricing.

For the first quarter, we reported operating income per diluted share of \$0.05. The year-over-year decline was mainly due to the following after-tax items: Other investment income decline of \$14.5 million, driven by our alternative portfolio; an underwriting loss of \$1.9 million, driven by property volatility; and \$4 million less in tax benefit due to taxes booked in the first quarter, based on the full-year expected tax rate. This anomaly occurs when there's a quarter early in the year that is out of line with the profitability expected for the full year. This effect is expected to reverse in future quarters.

As expected in the first quarter, our alternative investments generated a loss of \$13.4 million after-tax compared to a slight gain of \$1.2 million after-tax in the same period in 2008. The losses reflect the general decline in all asset classes and the adoption of FAS 157 by many general partners. Given that the bulk of these investments report on a one quarter lag, the valuations reflect the tumultuous financial markets of the fourth quarter of 2008. Global real estate valuations were hit especially hard in 2008, particularly affecting three of our alternative investments. Although our alternative investment portfolio had a significant impact on our net investment income in the quarter, it only underperformed the S&P 500 index by 1%.

The property losses, mainly due to severe non-catastrophe winter weather, were \$15 million pretax higher than expected in the quarter, including \$6 million of prior year development related to the late reported property claims. This was lower than our initial estimate of \$17 million that we reported in March. The excess property losses reduced operating income after-tax by \$0.18 per share.

Invested assets were up 3% at March 31st, 2009 compared to December 31st, 2008, reflecting fair value increases on our available for sale portfolio, coupled with increased short-term investment balances. These increases were partially offset by the sale of equity investments. In the quarter, we transferred \$1.9 billion of fixed maturity securities into a held to maturity portfolio from an available for sale classification. In total, these transfers resulted in the presentation of stockholders equity during the quarter of \$34.6 million after-tax, as the fair value of these securities decreased approximately \$53.3 million.

Unrealized losses on our available for sale securities improved \$35.5 million after-tax, driven by a \$43.1 million after-tax improvement in fixed maturity securities, partially offset by a \$7.4 million after-tax decline in our equity portfolio. The net impact of these fluctuations amounted to \$0.67 per outstanding share. This was the primary driver in increasing our book value per share to \$17.23 at March 31st, partially offset by a net loss of \$0.24 and dividends of \$0.13.

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The markets continue to pose challenges regarding other than temporary impairments. We recorded a \$27.1 million pretax charge in the quarter, reflecting write downs on six fixed maturity securities, predominantly 2006 vintage Alt-A securities, representing \$26.3 million pretax, and three equity securities representing \$0.8 million pretax. We are also currently analyzing the impacts of the accounting guidance that was issued April 9th regarding fair value measurements and the impact of a distressed marketplace. We will adopt in the second quarter of 2009.

We have taken a number of actions in the quarter to reduce risk in our investment portfolio, including the following: A reduction in CMBS exposure by \$56 million or 25% while increasing our agency backed component from 32% to 53% through new purchases, significantly improving the credit characteristics of our CMBS portfolio. These are predominantly GNMA, with the full faith and credit of the US government; a \$91 million increase to government agencies raising our allocation from 7% to 9% of investment assets; the aforementioned movement of \$1.9 billion or approximately 60% of the fixed income portfolio into the held to maturity category to protect stockholders equity; a \$73 million increase in our short-term portfolio to \$271 million or 7% of investment assets; and a \$78 million reduction in our net equity exposure to \$57 million, bringing our exposure to a conservative 6% of stockholders' equity.

Our insurance operations continue to perform well. We were satisfied to report a 100.2% statutory combined ratio for the quarter. Our statutory combined ratio increased 1.9 points versus a year ago, driven by the previously mentioned property losses. Catastrophe losses were \$1.3 million or 0.4 points compared to CAT losses a year ago of \$4.7 million or 1.2 points.

Overall, prior year statutory lost and LAE favorable reserve development on a pretax basis for the quarter was approximately \$4 million, or 1 point on the combined ratio, compared to favorable development of \$3 million, or 0.8 points in the first quarter of 2008. This quarter's favorable development was primarily driven by Workers Compensation for accident years 2006 and prior, and one large personal injury claim in personal auto, partially offset by unfavorable property development.

As a result of the various expense savings initiatives we implemented in 2008 and 2009, the GAAP expense ratio for the quarter was down 2 points from a year ago to 31.4%. Our 2008 expense initiatives continue to benefit expenses in 2009, including ongoing commission savings. Additionally, in the first quarter, we made several charges that we expect to further reduce 2009 expenses by about \$9 million pretax. The largest savings came from the elimination of retiree life insurance benefits for active employees saving \$4 million, which was a one-time benefit in the first quarter. Other savings initiatives included 10% reduction in travel budgets and controlled hiring for the year, as we continue to proactively manage expenses.

Commercial lines reported a profitable 99.1% statutory combined ratio for the quarter. As mentioned, unanticipated property losses in the quarter added 3.4 points to commercial lines combined ratio. Workers' Compensation and commercial auto were both profitable, with 92.5% and 96.1% for statutory combined ratios, respectively. Commercial lines statutory net premium written declined 5% in the quarter; however, commercial lines new business increased a strong 12%. The decline in premium was mainly result of the economic downturn on audit and endorsement premium, primarily in Workers Compensation which required returns of \$17 million compared to \$3 million in the first quarter of 2008.

Reflecting our superior agency relationships, pure price was down just 0.8% in the quarter. More importantly, March held steady at 0%, our first month without negative pure price since April of 2005. We believe this positive new momentum is fueled by our excellent regional underwriting teams deploying business intelligence tools and leveraging our agency relationships. The results demonstrate discipline in a competitive marketplace.

Personal lines, which as Jennifer noted earlier about our segment changes, now includes flood operations. They posted a 107% statutory combined ratio for the first quarter versus 107.8% a year ago.

Personal lines premiums grew for the seventh consecutive quarter, with \$50 million in the first quarter, a 1% increase compared to 2008. New Jersey continues to put downward pressure on premium growth in our personal lines segment. Our decline in underpriced urban enterprise zoned business is outpacing our overall decline, which improve profitability long-term. In addition, the "Take-All-Comers" law has expired, allowing for true new business underwriting to take place for personal auto in the state.

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Homeowners profitability was negatively impacted by the severe weather in the first quarter; but as pricing moved into positive territory in 2008, we increased rates 7.4% overall on our personal lines book, adding about \$15 million in potential annualized premium.

Now I will turn the call over to Greg.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Thank you, Dale, and good morning. For the quarter, our insurance operations were strong in what is still a very competitive commercial lines marketplace. Our statutory combined ratio was slightly over 100. Our commercial lines new business was up 12% to \$71 million. Commercial lines pure pricing for the quarter was down only 0.8%, far better than any pricing surveys in the marketplace. A key statistic is that our renewal pure pricing for April through the 24th was a positive 0.4%, a significant achievement in these market and economic conditions.

Our Investor Day that was held on March 24th was very successful and highlighted these five keys to our success: Best in class underwriting and claim field models; sophisticated cycle management tools and profitable organic growth opportunities; a personal lines improvement plan; improving our cost of goods sold through various claims initiatives; and the benefits of Selective's high franchise value with 950 Ivy League independent agents through excellent company-wide relationships. We hosted an agency panel that provided a deeper insight into how agencies are managed and how they view their markets; in particular, their relationship with strong regional carriers like Selective. Takeaways from the panel included: the field underwriting or AMS model, coupled with strong technology, is why agents writing business with Selective; franchise value is huge with agents; while they acknowledge our broad underwriting appetite, agents want even more product depth and breadth from Selective; carrier financial strength is important to agents; and most importantly, agents can sell services like safety management and claims and do not necessarily have to provide the cheapest price.

Overall, relationships are critical; and the evidence of our best in class agency relationships is demonstrated in the improving first quarter commercial lines pricing and the positive pure price generated in April. From a new business standpoint, we are one of the few carriers providing agents with high quality new business leads, as well as strong producer and sales management development programs that provide the success -- that improves the success rate of producers in this difficult market.

In the first quarter, commercial lines new business was up 12%, and pricing and quality of the book also improved. Pricing on new business improved with the month of March at a positive 0.5%. The diamond score distribution improved as intended, with the percentage of four and five diamond business increasing from 58% to 64%; and in the one and two diamond business, down to 10%. New business growth by segment for the quarter was as follows: One & Done automated small business, \$18 million, up 5%; AMS, our middle market business, \$48 million, up 13%; Selected Risk Managers, our large account business, \$5 million, up 32%. We had our best quarter ever in small business One & Done premium production, averaging \$295,000 per business day. We set a new small business record of \$316,000 per day in March. We continue to increase our small business market share by expanding the One & Done(r) pipeline, leveraging strong agency relationships, and focusing the attention of our field technology representatives on writing small business. We have also gained traction in small business by widening the non-contracting pipeline with the inclusion of the garage and auto service, small manufacturing Workers Compensation, Lessor's Risk-only package policies, a competitive BOP program and Civic organizations. Non-contracting new business was up 17% in the quarter to \$163,000 per business day.

In the middle market, we are particularly pleased about the success we are having in new business written outside of our contracting Strategic Business Unit. Overall non-contracting commercial lines new business was up about 26%, much of which fell into the AMS or middle market sector; and particularly, our lead program that is starting to generate success in the marketplace. Overall in the quarter, middle markets wrote \$5 million in new business above our expectations.

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The large accounts unit increased new business 32% to \$5.4 million, and was basically on plan for the quarter. Submissions increased, and our hit ratio was approximately 20%. Renewal pure pricing was down 2.1%, while retention on a client basis was a strong 91%.

The two key initiatives that will drive underwriting improvement throughout our personal lines book as follows: (1) price increases, which on our in-force book amounted to \$15 million or 7.4% in 2008, and we expect another \$9 million or 4.3% in 2009; (2) our MATRIX models for both homeowners and automobile, which create organic growth opportunities with precision pricing capabilities.

From an insurance score standpoint, we are seeing a significant improvement in the quality of both homeowners and automobile business into the higher scored sectors that have better claim experience. In particular, our new homeowner MATRIX product includes by peril rating capability and allows us to more granularly price weather, wind, water, fire, theft and liability, among other factors.

Although we anticipate our personal lines results to continue to be somewhat lumpy, as we earn the \$24 million of filed rate increases over the next two year period, we are expecting significant improvement on our \$214 million personal lines book of business.

We have a number of initiatives underway to lower our claim costs that are focused around, (1) litigation management; (2) ongoing vendor consolidation; and (3) more effective integrated outcomes in the resolution of claims in Workers' Compensation and other casualty lines. In casualty, we are looking to reduce cycle time through focused litigation avoidance, file review initiatives and settlement efforts. In Workers Compensation, changes in case management utilization, centralized bill review, increased PPO penetration and return to work initiatives should produce better outcomes. In a very competitive market, cycle management tools are critical. We are successfully deploying our initiatives to write the highest quality new business, while at the same time granularly driving price increases on our renewal business.

Since we changed our SEC reporting segments this quarter, we are modifying financial guidance for 2009 to match the new segmentation. By moving flood into the insurance operations, there will be less of a difference between the GAAP and statutory combined ratios. Otherwise, guidance remains the same, as follows: A GAAP combined ratio below 103%; a statutory combined ratio below 102.5%; and catastrophe losses of 1.4 points. Now I will turn the call back to the operator for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Your first question is from David Lewis.

David Lewis - *Raymond James - Analyst*

Good morning, and thank you.

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

Good morning, David.

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Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Morning, David.

David Lewis - *Raymond James - Analyst*

A couple of question. First, Dale, let me clarify -- the 4 million favorable development is net of the 6 million of unfavorable, correct?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

That is correct.

David Lewis - *Raymond James - Analyst*

Okay. Just wanted to make sure. I guess I am trying to figure out maybe what the kind of combined ratio run rate is. If I look at the 100.8% that you are reporting, the 15 million of higher storms penalize you by about 4.1 points. The 4 million of favorable development helped you by a point. So even if you kind of net those two out -- and I guess I should say, then you had 4 million of kind of one-time favorable expenses, so you still ended up with about a 98.7% combined ratio if you net all of that out?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Dave, I think the way I would look at it in total, I would kind of focus on -- if you want to look at the property losses, \$15 million property losses had \$6 million of adverse development, so you are looking at about \$9 million of property losses. Let's just look at it above expected. And then you would -- if you net that down, then you have to look at \$4 million of favorable development just on a net basis as well, and that excludes the property aspects of it. And then when you --

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

It would be 10 million.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

10 million. Excuse me. Yes, that's what I thought. 10 million. And then you look at the expense savings of another few million, much of which gets amortized on a GAAP basis, when you look at it, they almost semi-net out.

David Lewis - *Raymond James - Analyst*

So if we kind of run through all the different variations, you're kind of running in that low 100% combined ratio?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Yes. That's probably the right way to look at it.

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David Lewis - *Raymond James - Analyst*

Okay. And just on the alternative investments, I know you don't have the details yet, but just from a general standpoint, I think you indicated that it only underperformed by 1% relative to the S&P 500. And I know historically there hasn't been, I guess, a close correlation to the S&P 500, but just a general thought. If the S&P 500 was down 13% in the first quarter of 2009, any guess -- I mean, are we probably looking at another double digit loss in the alternative investments for the first quarter?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Let me just say that our alternative investment portfolio significantly has outperformed the S&P 500. So I mean -- and let's just look at the full-year of 2008, the S&P was down around numbers somewhere in the 37% range. Our alternative investment portfolio was down about 9.9, somewhere in that neighborhood. And so when you look at it in that light, it is consistently year after year after year outperformed and -- or actually it has been additive -- having this suballocation to alternatives has added about \$30 million to our overall position as a result of having the suballocation into the alternative. So I just want to make sure that you get that point. I think in the first quarter, what you experiencing, when you look at our alternative portfolio, about a third of our loss in the quarter came from the real estate sector of the alternative, which represents approximately 13%. And I think what you are seeing there are some particularly hard hit e-values at the end of the year as a result of FAS157 and other factors. So it is very difficult to handicap this relative to what will happen in quarter two and three and four relative to what the S&P has done. But I just want to make sure it is clear that there has been consistent outperformance on this asset class relative to the S&P 500.

David Lewis - *Raymond James - Analyst*

And the alternative investments, remind me what the total dollar amount was?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

147 million at the end of March.

David Lewis - *Raymond James - Analyst*

Okay. That's all I have for now. Thank you.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Okay.

Operator

Your next question comes from Alison Jacobowitz with Bank of America.

Alison Jacobowitz - *Bank of America - Analyst*

Hi. I was sort of working along the same lines as David just did, but maybe just a couple of questions following that. On the expense ratio -- so you had the 1 point of help, then. Would you -- I didn't know if I heard you get it in there. Is 32 then sort of our new run rate before the new expense savings that you just mentioned? And then also in the other expenses, I don't think

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I heard it. Was that stock bonuses in the quarter? And maybe could you split out what was sort of a normalized number and what was maybe just one-time for the quarter?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Sure. Dale is getting that information for you right now, Allison. But with respect to the expense ratio -- you're looking GAAP expense ratio now? I want to make sure we're clear.

Alison Jacobowitz - *Bank of America - Analyst*

Yes.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Okay. Yes, you are looking at -- go ahead, Dale.

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

Well, on the other expenses within the quarter, the one item that -- the big item that is in there actually is the effective tax rate adjustment that we talked about earlier for about \$4 million out of the total of \$7.3 million in there. The actual -- the long-term incentive compensation actually is down from last year, just as a result of where the stock price has moved. Last year in the first quarter, you had a \$5 million expense related to long-term compensation that is stock-based. This quarter, you had only \$1.5 million in long-term. But the tax piece brought it back up. So basically, you are comparing a \$7.3 million number to a \$8 million number last year to the full total expenses there.

Alison Jacobowitz - *Bank of America - Analyst*

Oh, okay. And the tax piece is not going to reoccur. That was the one-time?

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

Right. I mean, basically, it is an old APB 28 -- not to turn you into an accounting geek -- but basically it amounts to -- you have to estimate your tax rate -- your marginal tax rate -- for the full year, and then you just book to that estimated number as opposed to doing a regular cut off tax calculation. So when you have got a first quarter that is out of line in terms of the expected profitability for the full year, you end up having this kind of a situation where you end up booking a higher tax.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

And then Allison, with respects to your question, relative to run rates, this reclassification is going to affect the run rate expense ratio on a GAAP basis. So you are going to need to narrow that down relative to -- because that had a tendency to widen out our GAAP expense ratio, and that's going to narrow that down about 50, 60 basis points, somewhere in that neighborhood; and then some of these other expense savings would be on top of that. And then that -- obviously, that assumes us starting to make sure we meet our overall top line revenue, and we don't get compression on the expenses relative to top line misses. But I would tell you overall for the quarter, we were very pleased with the balance of the new business, the renewal activity for the quarter; and if anything, what hurt our top line for the quarter was more economic in nature, in the sense that our returned premiums on audits and our endorsement premium were definitely above our expected levels.

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Alison Jacobowitz - Bank of America - Analyst

Okay. Thanks. And maybe I will follow-up offline but just -- I missed the first five seconds, literally. This reclass of the diversified line, is that -- that's going to be, then, completely gone going forward, or will some portion of it still wind up there?

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

You will have a separate segment that just indicates human resource administration outsourcing. So all of the other small components that were included within this are moved out. So the biggest one -- the biggest other one was the flood, which we're putting into our insurance operations -- which really matches the way all of our competitors end up reporting. So that was the difference that Greg was talking about in terms of the expense ratio, because the flood ends up netting down the expense ratio by about 5 to 6/10 of a point. So it narrows the difference between the GAAP and the stat combined ratio, and particularly the expense ratio component.

Alison Jacobowitz - Bank of America - Analyst

Okay. Great. Thanks. And if I want to go through my model, I reserve the right to call you offline.

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

Not a problem.

Alison Jacobowitz - Bank of America - Analyst

Thank you.

Operator

Your next question comes from Mike Grasher with Piper Jaffray.

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

Morning, Mike.

Michael Grasher - Piper Jaffray - Analyst

Good morning, everyone. I jumped on a couple of minutes late, so sorry if you addressed this in your opening remarks; but with risk to capital at 1.8 can you talk about capital levels relative to what maybe the agencies are thinking or saying, and how high you could potentially go here?

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

Well, our discussions with the rating agencies for years has been that our target level was to write premium at a 1.8 to 1 premium to surplus. We are currently at a 1.74. So we are right in that range. Obviously, everybody in the industry has had a depletion of capital as a result of what has happened in the financial markets. But at this point, we feel comfortable with our overall capitalization levels.

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Michael Grasher - Piper Jaffray - Analyst

And the agency then still holds to the 1.8 as far as the target level?

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

We have not had any discussions with them that would indicate otherwise.

Michael Grasher - Piper Jaffray - Analyst

Okay. Good to know. And then just wanted to ask about a few of the lines; in particular, the general liability and the BOP. Anything in particular in the quarter that occurred which drove those combined ratios higher?

Gregory Murphy - Selective Insurance Group, Inc. - Chairman, President & CEO

Sure. I mean, when you look at the BOP in particular, they had about \$3 million of water style damage claim that affected their performance. If you looked at the three major casualty lines and the commercial lines sector, which would include general liability comp and commercial auto; for the most part, when you look at those lines on an accident year basis, they're all pretty much running right in the 100. I think what you are seeing in the differential there relative to the calendar year numbers for the most part are either favorable or unfavorable development numbers that were booked in the quarter. And then the only other line that I've got to tell you really jumps out is the HO line, and that had about \$4 million, either large fire and/or water damage claims that occurred in the quarter that kind of blew that number out a little bit.

Michael Grasher - Piper Jaffray - Analyst

Okay. Got it. I wanted to ask about the -- specifically about the fire line, and then I guess as it regards homeowners as well.

Gregory Murphy - Selective Insurance Group, Inc. - Chairman, President & CEO

But Mike, if I may --

Michael Grasher - Piper Jaffray - Analyst

In terms of fraud or anything along those lines that maybe you are seeing or thinking?

Gregory Murphy - Selective Insurance Group, Inc. - Chairman, President & CEO

Yes. And I will let John talk to you about what we are doing relative to vacancy fraud and all of that; but just as another side note to let you know where our tremendous gains in pricing have occurred -- and I think this is important to know -- that when you look at our pricing -- for the pure pricing now -- so we're not giving you renewal pricing. We have always provided you pure pricing, which is really telling you what is actually happening on exposure basis. Some of the big gains that we made in the first quarter were in the area of commercial auto, liability and physical damage, where for the year we were running about minus 5%, and for the quarter, we were running at about an average of minus .5%. So tremendous gains in that line; and then the other line that has started to improve but yet needs more improvement is in the property -- commercial property line, where that ran for the full year at about a minus 57. And now that is running at a minus 21. And then with respects to BOP, we have done so many moments in what we have done to try to write the right business there, it is hard to really focus on that line in

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terms of pricing on a quarter by quarter basis. But I will let John kind of focus on the underwriting and other things that we are doing with respects to fraud and vacancy.

John Marchioni - *Selective Insurance Group, Inc. - Chief Underwriting Officer & Field Operations Officer*

Good morning. This is John Marchioni. Just a little further color on the property lines, in particular to your questions about fraud, we haven't necessarily seen an uptick in fraud activity. And I will tell you, I think we are as well-positioned as everybody to detect it with our field based claims model. We have CMSs out there across our footprint that are actually on site with these large fire and frozen pipe water losses within 24 hours. So their ability to detect fraud and hand it over to our very strong SIU I think unit positions us very well to detect it. And we really haven't seen that. I think what we have seen has been more of, as Greg indicated, economically driven factors; and in particular, in two of our commercial segments, being lessor's risk and hotels, what is happening with your increased vacancy rates in hotels -- on the hotel side, your increased vacancy rates, what you see happening is the top floor is being left vacated as they manage their rooms and that's causing some of these frozen pipe losses that happened in the first quarter.

Because when you look at the cold temperatures we saw and how far south they drifted, that really drove that. And I think at the end of the day, that becomes a management issue we are closely watching and underwriting for. And the same thing on the lessor's risk side with regard to vacancy percentages in those properties, we have got some very strict underwriting guidelines around vacancy which we certainly handle on new business, and our renewal underwriters are also aggressively managing vacancy rates on those classes of business on the renewal book as well. So more of an economic factor than it is a fraud factor from what we can see.

Michael Grasher - *Piper Jaffray - Analyst*

So then on the commercial side, with regard to the vacancies and that, you're just simply not seeing anything to this point?

John Marchioni - *Selective Insurance Group, Inc. - Chief Underwriting Officer & Field Operations Officer*

I'm sorry. From a fraud standpoint?

Michael Grasher - *Piper Jaffray - Analyst*

Yes.

John Marchioni - *Selective Insurance Group, Inc. - Chief Underwriting Officer & Field Operations Officer*

No, no.

Michael Grasher - *Piper Jaffray - Analyst*

Okay. Thank you. That's helpful.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Thanks, Mike.

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Operator

Your next question comes from Mark Dwelle with RBC Capital Markets.

Mark Dwelle - RBC Capital Markets - Analyst

Yes, good morning.

Gregory Murphy - Selective Insurance Group, Inc. - Chairman, President & CEO

Hi, Mark.

Mark Dwelle - RBC Capital Markets - Analyst

Several of my questions have been kind of already covered, but let me hit on a couple others that we haven't really gone through. Dale, you had gone through kind of a fairly lengthy litany of new business wins and different segments and so forth. By way of framing that up a little bit, who are you winning the business from? Are you beating other regionals, or are you beating mutuals? What's the source of the growth?

John Marchioni - Selective Insurance Group, Inc. - Chief Underwriting Officer & Field Operations Officer

This is John Marchioni. I will answer that question. And we have talked about in prior quarters as well. I think it really varies by state and by segment of business, the competitors set that we have -- whether it is a contractor class or some of our retail and service classes, or social service or golf course classes -- it really is a different set of competitors. So I would say, generally speaking, we are winning across the board on the non-contractor classes. I think we continue to win there as well; but the economy -- the economic impact on that class has really kept down opportunities. So it really is across the board. Our new business growth in the small area driven by some new manufacturing classes and auto services that have been there puts us in many cases against some of our national competitors. When you look at our other wins in the upper end of manufacturing in our specialty program classes of business, you tend to be matched up against some of the regional carriers. So I think we've had a fair amount of success in a number of different areas. And the only other comment I'll make on new business -- because I think you look at that number and realize how much progress we've made -- we monitor very closely the distribution of that business from a quality standpoint. We use diamond scoring, as we've talked about in the past. So we understand where that business comes from from a diamond distribution standpoint; and then as Greg indicated in his prepared comments, we measure new pure price very aggressively as well. So we are very comfortable with the pricing levels and the quality of that business, and it really is spread across a number of segments and up against a number of competitors.

Gregory Murphy - Selective Insurance Group, Inc. - Chairman, President & CEO

And I would say that when you listen to the agency panel, I mean, those points resonated loudly in terms of, they really want to have a relationship with the carrier that they've put their best business to; and what gives us a significant advantage in the marketplace is our superior field model, coupled with excellent technology, are what -- are the drivers of why agents want to put more and more of their best business with companies like Selective.

Mark Dwelle - RBC Capital Markets - Analyst

Okay. With that -- that's helpful detail. Thank you. Considering the new business growth and your early trends that some of the overall pure price is starting to tip a little bit positively, is it plausible that -- if the economy ceases being a negative drag on demand, is it plausible that you could actually see some top line growth by later in the year, or is that too optimistic?

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Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

I don't think that's necessarily too optimistic -- and obviously, there's a lot of moving parts in there. You are working still through some pretty good size amounts of inventory, where you have returned premiums as a result of lesser endorsement activity, less vehicles, less payroll. So those are some pretty big headwinds on the top line to overcome. But I think we are positioned well in terms of getting price increases. I think you heard me say that on an in-force basis, we have generated about \$24 million of revenue on the personal lines book, so that's quite a sizable increase because those are -- those rate increases compound, so you are going to get that rate level on the personal lines starting to work through.

And then in the commercial lines side, you have got to remember, quarter after quarter, we've had negative 3, negative 4, negative -- whatever, and price that we had to overcome. So to the extent that the price starts to move more into the positive territory, some of the negatives that have existed in prior quarters won't be there. Now, the other negative than that is maybe a little bit louder in the drum beat relative to that is some of the economic -- some of our customers that have less power units, that may be sizing down payroll; and obviously, those are things that we will need to overcome. But however, some of these other factors that were negative in the past are now positive, and I guess we are just going against the economic headwind.

Mark Dwelle - *RBC Capital Markets - Analyst*

Okay. That's very helpful. A question for Dale related to the reclassification of the investments to held for sale. You had commented that was a \$36.4 million benefit.

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

Right.

Mark Dwelle - *RBC Capital Markets - Analyst*

If I understand that correctly then, had you not done that, book value growth in the quarter effectively would have been flat or even slightly negative. This is -- it contributed to the rest of the portfolio producing an overall upside?

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

That is correct. That \$36 million would have been a negative in terms of our GAAP equity if we hadn't reclassified them as held to maturity.

Mark Dwelle - *RBC Capital Markets - Analyst*

Okay. And you had talked about the --

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

That is an after-tax number, \$36 million.

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Mark Dwelle - RBC Capital Markets - Analyst

Okay. Thank you. You had talked about the tax, unless I missed it. Did you actually give us a kind of run rate to use as far as the tax rate, or we can just solve that backwards from the benefit you implied?

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

Well, we didn't give you a run rate, and I don't have it right sitting here. But it's pretty -- given the way APB 28 works, it is pretty easy to calculate it. So calculate the marginal tax rate this quarter, and that's what our estimate is for the year -- because we have to book to that by accounting standard.

Mark Dwelle - RBC Capital Markets - Analyst

Okay. Okay, yes. That's all my questions. Thank you.

Operator

Your next question comes from Mike Grasher with Piper Jaffray.

Michael Grasher - Piper Jaffray - Analyst

Hi, Dale. Just wanted to follow-up with the -- with regard to capital; and just -- I'm looking over your debt to total capital ratio. What would be sort of the max that we can see you go to if need be, assuming capital remains flat?

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

Well, the conversations we've had -- again for years -- with the rating agencies has been about a 25% debt to cap. Currently, we are at a 23% on an unadjusted basis; but it's 17% adjusted for the equity credit that the rating agencies give us for the 60-year piece of hybrid that we put on. So 17%. Obviously, you could go up higher but that's -- the capital markets aren't open right now in any meaningful way.

Michael Grasher - Piper Jaffray - Analyst

Sure.

Dale Thatcher - Selective Insurance Group, Inc. - EVP & CFO

So it is not exactly a path that we would be pursuing in the near term. But obviously, there is room there on a debt to cap basis.

Michael Grasher - Piper Jaffray - Analyst

Okay. And then just -- I guess general comments around the dividend; and it is -- the yield obviously very nice here. If you did get into a situation where you needed to raise capital, would that be a source that you would look at, or is that pretty safe?

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Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

All I can say that that the Board looks at the dividend and assesses the dividend each and every quarter. There are many other capital management tools that we would look at first.

Michael Grasher - *Piper Jaffray - Analyst*

Okay. Thanks very much.

Operator

Your next question comes from Robert Paun with Sidoti & Company.

Robert Paun - *Sidoti & Company - Analyst*

Good morning.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Morning.

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

Good morning.

Robert Paun - *Sidoti & Company - Analyst*

I had a question on the comp -- the Workers' Comp book. You have seen some improvement there in the underwriting. Can you provide some more color on what you are experiencing there? Maybe you could comment on the frequency trends that you have seen?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

Sure. That's not a problem. I mean, what you are see there can in some cases is some improvement in some of the pricing going on in the book of business; but overall in the comp, you know, frequency has been down around -- on a fiscal year basis -- a fiscal year basis -- down around 14%, and surety has actually been up, and so our overall loss costs have been up around 2%. I think what you are starting to see in the comp overall -- and I know we are showing a very low combined ratio -- some of that is in total favorable development -- but when you look at the line on an accident year basis, it is running right around just under a -- right about 100 or so. And that's a significant improvement over where we were running it two or three years ago. And I think that just reflects the holistic efforts that we have done in terms of now starting to identify good business that we want to write as a result of our molding.

So we are starting to write some of that business. That's more profitable. We have been very effectively managing the inventory. We have done a lot in the area of claims in terms of some of the initiatives we have taken to improve there. So I think that is a holistic effort reflecting underwriting, underwriting changes, looking at loss leakage in the comp area for instance on the contracting side, so we have a big focus on loss leakage issues; and I think all of those things are what is starting to impact the book of business, and particularly now starting to grow it and writing profitable accounts in there.

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Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

And just to give you a touch more detail, Robert, on the -- the Workers' comp recorded a 92.5 combined for the quarter. But that included the \$7 million of favorable development that Greg indicated. So when you back that development out and put it on an accident year basis, again as Greg indicated, it is around a 101. So that's the more meaningful number to look at.

Robert Paun - *Sidoti & Company - Analyst*

Okay. So there was about 8 points of favorable development?

Dale Thatcher - *Selective Insurance Group, Inc. - EVP & CFO*

Correct.

Robert Paun - *Sidoti & Company - Analyst*

Okay. And also second question. Greg, in your prepared remarks you commented that retention was slightly down. Can we assume that's mostly due to pricing? Is that fair to say?

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

I think you are seeing -- some of that is the economy driven. You are seeing some consolidation of our customers. You are seeing some customers that have had trouble making it in these tough economic times. And I think to some extent -- and it is hard for us really to fully -- to fully put our finger on it, but the retention differential is so small it is not even worth overly analyzing it. Some of it could be the fact that we've put higher increases on what we perceive to be not as performing business as we like to see it. And maybe that business is finding other markets that is willing to write it -- maybe where our expiring premium was or even less than that. So -- but none of that, in my opinion, is really that significant to even really dwell on at this point.

Robert Paun - *Sidoti & Company - Analyst*

Okay. Thanks. That's all I have.

Operator

(Operator Instructions). There are no questions at this time.

Gregory Murphy - *Selective Insurance Group, Inc. - Chairman, President & CEO*

All right. Thank you, Operator. All right. Our first quarter results demonstrate discipline in a competitive marketplace. We believe the quarter's positive momentum is fueled by our excellent field underwriters deploying industry-leading business intelligence tools and leveraging our excellent agency relationships. We are competitively postured for a hardening market. Thank you for participating in the call this morning, and please give Jennifer or Dale a call with any follow-up questions you may have. So thank you very much.

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