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160-Year Old Hanover Retaking Its Place as P/C Industry Leader

Eight out of 160 years of history may not seem like a big deal but for Hanover Insurance Group, founded in 1852, the last eight years have seen a series of big deals.

Eight years ago in 2004, the $2.4 billion heavily personal lines super-regional insurer was trying to regain momentum after a big venture into life insurance and annuities by its parent company at the time, Allmerica Financial, went sour.

Today, the Worcester, Mass.-based company has $4 billion in revenues, writes only property/casualty, conducts business on a nationwide basis, underwrites a balanced book of personal, commercial and specialty lines business, and is one of the country's fastest-growing P/C insurers.

In recent years, the company has been expanding its footprint, diversifying its products, partnering with select independent agents, adding international and excess/surplus capabilities, and earning strong ratings – executing notes it has played to varying degrees of success since its founding 160 years ago.

"I tell people that one of the parts of our journey right now is taking our place again as one of the lead companies in the marketplace and it's not the first time we did it," Frederick Eppinger, CEO, told *Insurance Journal* in a recent wide-ranging interview.

In excerpts from the interview with Insurance Journal's Andy Simpson, Eppinger discusses among other issues Hanover's history, its recent acquisitions, his company's regional approach, his appreciation for independent agents, and whether the late Steve Jobs of Apple would have made it in the property/casualty insurance business.

After eight years of deals shedding the life and annuity businesses then adding new property/casualty products and expertise by buying business from OneBeacon and London-based Chaucer and others, Eppinger thinks now is a good time for Hanover to grow organically – and reflect.

"We are at a milestone as a company. We're now a couple years into the expansion out West. With Chaucer we have the Lloyd's connection again. I feel like it's not a bad time to step back and reflect on where we are and where we're going and why I think we're going to be quite successful," he said.

"I reflect on the last four years with a horrible recession and all the others things, the financial crisis, and for us to be growing and being upgraded and really thriving in a difficult time, to me it all comes together into a nice story about where the company is."

Hanover's History

Hanover Insurance was founded in 1852 in Hanover Square in New York City, which makes it older than big players Allstate, W.R. Berkley, Chubb, CNA and Travelers. It's one of the 40 oldest companies on the New York Stock Exchange – a fact the company celebrated by the ringing of the bell on the floor of the NYSE on

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April 3. Eppinger was joined on the bell platform by Marita Zuraitis, president of Hanover's property/casualty companies, and the company's executive leadership team.

Hanover started as a fire insurance company. It later added auto, marine and surety, then workers' compensation, general liability and other casualty lines. It did business with Lloyd's in London as far back as 1880 and did business in China back in 1920.

Hanover moved its headquarters to central Massachusetts in 1969, the same year it expanded its business in the Midwest with its affiliation with Citizens Insurance Co., based in Michigan.

The insurer has weathered the 1872 Chicago fire, the 1906 San Francisco earthquake, the 1929 stock market crash, and the 2004-2005 hurricanes including Katrina. It also survived the 2008 financial crisis – the only insurer in the country that had its ratings upgraded during this period by A.M. Best, Moody's and Standard & Poor's. In 2011, it survived a record $362 million in catastrophe losses.

One of Hanover's biggest challenges in its history had nothing to do with its property/casualty business. For a period starting in 1992, Hanover came under the umbrella of Allmerica Financial, which included State Mutual, one of the oldest and biggest life insurers. In addition to selling fixed life products, Allmerica became one of the hottest sellers of variable annuities in the late '90s. It got into deep trouble, however, after the stock market collapsed following the Sept. 11, 2001, terrorist attacks. The company began struggling to generate investment returns sufficient to meet the guaranteed return it promised the holders of its variable annuities.

Allmerica President and CEO John F. O'Brien, who championed the variable annuity sales, resigned in October 2002. In 2003, the company made the big decision to sell its fixed life insurance business and in August of that year hired Eppinger to take over the company.

Under Eppinger, by 2005, the company had completed restructuring and reinsurance deals that led to its eventual exit from the variable life and annuity businesses. The company also returned to its property/casualty roots and restored its name, Hanover Insurance Group.

The Hanover Insurance Group is now the holding company for a group of insurers that includes The Hanover Insurance Co., based in Worcester, Mass., and Citizens Insurance Company of America, headquartered in Howell, Michigan, and Chaucer Holdings plc, based in London, and their affiliates.

The current news of Hartford Financial Services getting out of the life insurance and annuities business to focus on property/casualty is a déjà vu for Hanover veterans including Eppinger, who himself worked in Hartford's property/casualty division before returning to his hometown of Worcester and taking over Hanover in 2003.

OneBeacon Deal

Under Eppinger, the company left the life business behind, focusing instead on expanding and diversifying its property/casualty business largely through acquisitions.

While he has overseen about eight acquisitions since he joined Hanover, Eppinger's deal to acquire the renewal rights to business from OneBeacon Insurance Group in 2009 was one of his biggest and boldest. Hanover acquired the renewal rights to $400 million in small and middle market business. The deal enabled Hanover to not only expand its specialty lines and middle market appeal but also advance its reach into western states.

When the OneBeacon opportunity came up, Eppinger said he saw three advantages: good products, good agent relationships and good talent.

"The product side of it, to me, was very intriguing," Eppinger told Insurance Journal, referring to the fact that OneBeacon's core business was industry product lines from the old Atlantic Mutual.

OneBeacon also offered "advantages for their spread and scale, particularly in small commercial, and they had some depth of relationships with some agents in the West and really good agents that really helped us," he said.

"Then, just broadly, their talent, in my view, was really extraordinary.

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Part of what I wanted to get at was the talent that they had in these geographies and these product areas."

Eppinger had been looking into expanding to the West and this deal would give Hanover access to about $100 million business there.

Believing that the people were key, Eppinger did something he thinks not many other CEOs would have done. Before a penny of revenue had been put on the books, he hired 165 of the OneBeacon people, right away. He also took on about 200 new agents in the deal.

Taking on the expense of hiring people before knowing how much business was going to be won is risky. Eppinger said competition for renewal rights business is typically fierce because "once you announce one of these you put a bull's eye on that business with every competitor in the world." Every competitor knows the accounts will have to transfer to another company so they all go after them.

"It's competitive business so usually it's a little bit tricky. What our agents did is they worked with us policy by policy to make sure that the insured knew the company and what we were trying to do. It was a real partnership right out of the gate. Again, for us, when history is written on this decade and the next, it was a really critical step for us," Eppinger said.

The deal has paid off better than Eppinger thought it would. Typical success on renewals is about 50 percent, he said, but Hanover sailed to an 80 percent renewal on the business plus enough new business from agents to cover for the 20 percent that did not renew with Hanover.

"I would argue it's all because the people came," he said.

Eppinger said "it's remarkable in a soft market where people are shrinking" that after just two years Hanover already writes $400 million out West.

In fact, the West has been so welcoming to Hanover that the company just announced it is creating a second western regional division to handle more business.

Chaucer

In July 2011, Hanover took another giant leap forward with its acquisition of Chaucer Holdings, a leading Lloyd's specialty insurance group, in a $474 million deal. Chaucer has expanded Hanover's specialty capabilities and is providing additional product and geographic diversification.

Chaucer writes almost $1 billion in property, marine, aviation and energy products, along with a personal and commercial motor business within the United Kingdom.

Many of today's Main Street risks have global exposures and Chaucer can help Hanover's agents with these risks, according to Eppinger.

Eppinger also likes several of the industries Chaucer serves. "Clearly, it has some great skill sets in about 13 categories that I'm interested in, like energy and marine and aviation…. all interesting categories [that] are parts of the economy that are growing, if you will, like alternative energy and stuff. It's really quite interesting," he said.

Eppinger also sees Hanover using its Chaucer connection to extend or supplement some of what Hanover already does for certain markets, making it unnecessary for an agent to go to a wholesaler. For example, Hanover writes a lot of marine business but has not had the international coverage needed for fine arts; now with Chaucer it does. The same can be done with healthcare, political risk and others.

"Well, now, we'll do an extension of our product set to our partners in some of these categories. So over time, what we're going to be able to do is just like we've done with OneBeacon, create some solutions out of those skills to provide to our agents," Eppinger said. "It makes our relationship more important with the folks that we do business with."

In Chaucer's first six months as part of Hanover, it delivered $429 million in net written premium, resulting in pretax income of $32 million.

Business Mix

Under Eppinger, the company has diversified its business along with expanding geographically.

Eight years ago in 2004, two-thirds of Hanover's business was personal lines. Today its mix is almost one-third personal, one-third commercial

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and one-third specialty. Personal lines is at 34 percent; commercial lines, 27 percent; U.S. specialty lines, 15 percent; and, thanks to the acquisition of Chaucer, it also has 15 percent in international specialty lines. Reinsurance and some UK motor insurance make up the rest.

Hanover's core commercial lines business generates $1.1 billion in premiums targeting small and middle market accounts. The most commonly written accounts have less than $250,000 of premium. These products include a standard business owners policy (BOP), commercial packages, property, general liability, workers' compensation and umbrellas.

The company's U.S. specialty commercial lines business reached $600 million in 2011. Specialized products include those for marine, surety, industrial property, professional liability, management liability, healthcare and commercial umbrellas and excess.

London-based Chaucer brings even more specialty capabilities in property, marine and aviation, and energy as well as liability coverage for professionals, financial institutions and directors and officers. About 24 percent of Chaucer's nearly $1 billion in business is marine and aviation, 22 percent is property, and 5 percent is energy.

In personal lines, Hanover stresses account-oriented selling of auto and homeowners along with additional companion products for things like identity theft, valuable items, watercraft, home care services, dwelling fire and umbrellas. The personal lines segment produces $1.5 billion in business, 60 percent of which is auto. Nearly 70 percent of all personal lines is account business. To manage this line, it has been implementing personal lines rate increases for several years and reducing concentrations of business in certain areas including Florida, Louisiana and Rhode Island.

The company today is licensed to sell property/casualty insurance in all states and the District of Columbia. It actively markets commercial lines policies in 36 states and in D.C and personal lines policies in 19 states.

More than 30 percent of its total business is in two states: Michigan with 22.8 percent and Massachusetts with 9.6 percent. After Michigan and Massachusetts, its biggest states for business are New York, California, New Jersey, Illinois, Florida, Connecticut, Texas and Maine.

Hanover's geographic footprint is changing as it capitalizes on the inroads in the West made through the OneBeacon deal and deepens its relationships with select independent agents in regions where it sees opportunity.

'As Simple As That'

Having independent agents representing the company is a strategy as old as the company itself. Samuel Sage of Cleveland became the company's first agent in 1852. By 1865, Hanover had another 44 agents and by 1871, it had 400.

Successfully partnering with independent agents is also a strategy that Eppinger believes will define Hanover's future success.

"We grow when other people don't grow because we solve more problems for the typical agent than most companies. It's as simple as that," Eppinger said.

The company has a total of about 2,500 agents nationwide but many of those are legacy and heavily personal lines agents. Hanover does not necessarily want a lot of agents. It increasingly favors doing business with a select group.

The company has its deepest relationships with about 800 top agents to whom the company gives what Eppinger calls "franchise value." This group of agents is responsible for $3 billion of Hanover's $4 billion of business. They get an assurance that the company won't appoint any nearby agents to compete with them and they get the new products and the attention from Hanover's professionals in local offices.

The strategy is about more than just contracting with the best agents; it's about giving them value.

"Our whole vision is that we combine innovation and this franchise value with agents with this notion of local adults that have authority. We give our professionals authority," he said. "Sure we have efficient

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models and we have automation like everybody else, but we're not one of the companies that says the black box runs this place."

While some small commercial lines carriers are centralizing their underwriting or decision-making, Eppinger said Hanover is redistributing its underwriters to its various regions. Each regional vice president is responsible for about 40 to 50 agents and is available to work with them to solve problems.

"Yes, a lot of it comes in automated, like everybody else, but when you have a problem, when there's a kick out, when there's a risk that needs some discussion or alteration we have local underwriters. It's the complete opposite of everybody else," Eppinger said.

"What happens is at the end of the day there's no machine that can really understand the risk, particularly on middle market or low end to middle market risk. You need somebody that actually knows the territory, knows the category, knows the risk."

This approach opens up opportunities for Hanover to pick up business when certain competitors under pressure in today's market issue across-the-board decisions regarding, for instance, small commercial accounts.

"So there's a lot of places where people have said no more X, whatever line of business it is. Everybody's going to get a 14 percent increase or a 20 percent increase. To me, that is just like saying I'm going to do a hiring freeze, where I can't think about where I need people and where I don't. Everybody's stopped thinking," said Eppinger.

Instead, he said, Hanover will work with agents to re-underwrite and price these accounts to see "who needs the rate, who doesn't need the rate, and can we solve the problem?"

What Best Agents Are Doing

Hanover has been emphasizing its portfolio of specialty commercial lines products in response to what the country's best agents want, according to Eppinger.

"When you look at the industry, in almost every geography the best agents and brokers are doing the same thing," he said. "They're saying what I need to invest in is areas of expertise. I've got to know things like not-for-profits or healthcare or whatever it is."

He said agents in all parts of the country are concluding that "just being generic" is not the way to be successful; rather they are saying "to really be the most successful my folks, my producers, have to know things."

That puts pressure on a carrier to be able to respond in the areas where these agents decide to specialize.

"You have to pick your spots. What you have to do is be clear on what you're good at and what you're not good at. The reason why they're independent agents is that obviously they're going to have a portfolio of companies that they partner with for their solutions," Eppinger said.

He said a lot of agents are interested in the professional lines, small lawyers, accountants, not-for-profits, private schools, churches and industrial risks coverages that Hanover has developed.

Hanover also tries to be smart about which products it lets which agencies sell.

"Instead of saying for private schools, anybody can sell private schools, we say no, the agents that actually know how to do that are the people that get the product, which our agents love because that means that, for them, they're not competing against people or somebody going direct," he said.

'Silly Notion'

Eppinger spends a lot of time trying to understand agency economics and trends and is convinced independent agents have a bright future. To think otherwise is "just crazy," said the CEO, who, of course, would be crazy to pin his own company's future on independent agents if he did not believe in them.

"[W]hat's happening in the agency channel is there's some consolidation within agents. But the stronger agents are getting stronger. I mean their ability to add value is getting better. My view is that the world is not less complex; it's getting more complex. And the notion that buyers don't need help is just crazy; it's silly. It's a silly notion," he said.

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He said from personal lines, to professional lines, to weather-related risks along with coverage variations and limits, people need more, not less, help.

"You know, most of us don't want to be experts in insurance. We want to run our business and live our lives. What you're seeing is that agents have become more and more efficient providers of advice. I mean that's what I believe. I believe that the value that they provide is getting greater because they're being more and more efficient in delivering it, and it's more needed," Eppinger told Insurance Journal.

How's Hanover Doing?

Despite the soft market, financial crisis, recession and catastrophes, Hanover has grown revenue for five straight years and, according to Dowling & Partners, been the fastest-growing P/C insurer.

By year-end 2010, with OneBeacon in the fold, Hanover grew to be a $3 billion company; it was at $2.4 billion in 2004, Eppinger's first full year at the helm.

By the end of 2011, with Chaucer on board, revenues were $3.9 billion.

Hanover, like many P/C insurers, ran into some rough spots in 2011, a year with record-setting catastrophes worldwide. Hanover still posted net income of $37.1 million, although that was down 76 percent from 2010. The company's combined ratio for the year 2011 came in at 104.6, about 10 points of that attributable to catastrophe losses including higher-than-expected losses from floods in Thailand. But even with that, it outperformed the industry average on combined ratio.

Book value per share took a dive in the financial crisis year of 2008 but since then it has been rising and in 2011, Hanover achieved the highest value ($56.24) in its history.

Eppinger does not see additional major acquisitions for Hanover in the near future. Now is the time for execution.

"Obviously, you think about the journey, there was the phase at the beginning that was really fixing a lot. Then we moved into building out these capabilities and enhancing the portfolio and the value propositions of our agents," he said. "What I believe right now is we're in a period of executing against the priorities as far as delivering value to our partners. That's going to lead to a lot of additional growth."

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