

PROGRESSIVE CORP/OH/
Form 10-Q
July 31, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2018

or
 Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission File Number: 1-9518

THE PROGRESSIVE CORPORATION
(Exact name of registrant as specified in its charter)

Ohio 34-0963169
(State or other jurisdiction of (I.R.S.
incorporation or organization) Employer
Identification
No.)

6300 Wilson Mills Road, Mayfield Village, Ohio 44143
(Address of principal executive offices) (Zip Code)
(440) 461-5000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Shares, \$1.00 par value: 582,512,182 outstanding at June 30, 2018

PART I—FINANCIAL INFORMATION

Item 1. Financial Statements.

The Progressive Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income
(unaudited)

| Periods Ended June 30, (millions — except per share amounts) | Three Months | | | Six Months | | |
|---|--------------|-----------|-------------|------------|------------|-------------|
| | 2018 | 2017 | % Change | 2018 | 2017 | % Change |
| Revenues | | | | | | |
| Net premiums earned | \$7,634.2 | \$6,313.3 | 21 | \$14,808.2 | \$12,340.0 | 20 |
| Investment income | 192.1 | 138.8 | 38 | 358.4 | 268.0 | 34 |
| Net realized gains (losses) on securities: | | | | | | |
| Net realized gains (losses) on security sales | (9.6) | 45.5 | (121) | 97.4 | 97.6 | 0 |
| Net holding period gains (losses) on securities | 53.5 | 0.4 | NM | (101.7) | 1.2 | NM |
| Net impairment losses recognized in earnings | (11.1) | (13.8) | (20) | (11.1) | (14.8) | (25) |
| Total net realized gains (losses) on securities | 32.8 | 32.1 | 2 | (15.4) | 84.0 | (118) |
| Fees and other revenues | 116.0 | 88.8 | 31 | 219.8 | 174.0 | 26 |
| Service revenues | 42.9 | 32.7 | 31 | 77.1 | 61.2 | 26 |
| Other gains (losses) | 0 | 0 | NM | 0 | 0.2 | (100) |
| Total revenues | 8,018.0 | 6,605.7 | 21 | 15,448.1 | 12,927.4 | 19 |
| Expenses | | | | | | |
| Losses and loss adjustment expenses | 5,375.3 | 4,614.9 | 16 | 10,246.1 | 8,878.3 | 15 |
| Policy acquisition costs | 630.8 | 514.2 | 23 | 1,227.0 | 1,017.1 | 21 |
| Other underwriting expenses | 1,046.9 | 845.0 | 24 | 2,027.1 | 1,690.6 | 20 |
| Investment expenses | 6.2 | 6.6 | (6) | 12.2 | 12.2 | 0 |
| Service expenses | 37.0 | 27.0 | 37 | 66.3 | 52.9 | 25 |
| Interest expense | 41.7 | 43.4 | (4) | 78.5 | 80.2 | (2) |
| Total expenses | 7,137.9 | 6,051.1 | 18 | 13,657.2 | 11,731.3 | 16 |
| Net Income | | | | | | |
| Income before income taxes | 880.1 | 554.6 | 59 | 1,790.9 | 1,196.1 | 50 |
| Provision for income taxes | 178.9 | 181.9 | (2) | 359.9 | 393.1 | (8) |
| Net income | 701.2 | 372.7 | 88 | 1,431.0 | 803.0 | 78 |
| Net (income) loss attributable to noncontrolling interest (NCI) | 3.0 | (5.1) | (159) | (8.8) | (11.1) | (21) |
| Net income attributable to Progressive | \$704.2 | \$367.6 | 92 | \$1,422.2 | \$791.9 | 80 |
| Other Comprehensive Income (Loss) | | | | | | |
| Changes in: | | | | | | |
| Total net unrealized gains (losses) on securities | \$(50.1) | \$92.6 | (154) | \$(204.6) | \$225.0 | (191) |
| Net unrealized losses on forecasted transactions | 0.2 | (8.0) | (103) | 0.4 | (5.7) | (107) |
| Foreign currency translation adjustment | 0 | (0.1) | (100) | 0 | 0.2 | (100) |
| Other comprehensive income (loss) | (49.9) | 84.5 | (159) | (204.2) | 219.5 | (193) |
| Other comprehensive (income) loss attributable to NCI | 0.6 | (1.3) | (146) | 4.6 | (2.2) | (309) |
| Comprehensive income attributable to Progressive | \$654.9 | \$450.8 | 45 | \$1,222.6 | \$1,009.2 | 21 |
| Computation of Per Share Earnings Available to Progressive Common Shareholders | | | | | | |
| Net income attributable to Progressive | \$704.2 | \$367.6 | 92 | \$1,422.2 | \$791.9 | 80 |
| Less: Preferred share dividends | 6.7 | 0 | NM | 7.9 | 0 | NM |

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| | | | | | | |
|--|---------|---------|----|-----------|---------|----|
| Net income available to common shareholders | \$697.5 | \$367.6 | 90 | \$1,414.3 | \$791.9 | 79 |
| Average common shares outstanding - Basic | 582.0 | 580.5 | 0 | 582.0 | 580.4 | 0 |
| Net effect of dilutive stock-based compensation | 3.8 | 3.3 | 15 | 3.6 | 3.1 | 16 |
| Total average equivalent common shares - Diluted | 585.8 | 583.8 | 0 | 585.6 | 583.5 | 0 |
| Basic: Earnings per common share | \$1.20 | \$0.63 | 89 | \$2.43 | \$1.36 | 78 |
| Diluted: Earnings per common share | \$1.19 | \$0.63 | 89 | \$2.42 | \$1.36 | 78 |
| Dividends declared per common share ¹ | \$0 | \$0 | | \$0 | \$0 | |

NM = Not Meaningful

¹ Progressive maintains an annual variable common share dividend program. See Note 9 – Dividends for further discussion.

See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries
Consolidated Balance Sheets
(unaudited)

| (millions) | June 30, 2018 | 2017 | December 31, 2017 |
|--|------------------|------------|----------------------|
| Assets | | | |
| Available-for-sale securities, at fair value: | | | |
| Fixed maturities (amortized cost: \$24,061.8, \$18,311.7, and \$20,209.9) | \$23,789.2 | \$18,388.1 | \$20,201.7 |
| Short-term investments (amortized cost: \$3,231.2, \$3,729.7, and \$2,869.4) | 3,231.2 | 3,729.7 | 2,869.4 |
| Total available-for-sale securities | 27,020.4 | 22,117.8 | 23,071.1 |
| Equity securities, at fair value: | | | |
| Nonredeemable preferred stocks (cost: \$677.0, \$666.0, and \$698.6) | 758.6 | 783.1 | 803.8 |
| Common equities (cost: \$1,314.0, \$1,472.3, and \$1,499.0) | 3,142.2 | 3,077.5 | 3,399.8 |
| Total equity securities | 3,900.8 | 3,860.6 | 4,203.6 |
| Total investments | 30,921.2 | 25,978.4 | 27,274.7 |
| Cash and cash equivalents | 154.8 | 161.0 | 265.0 |
| Restricted cash | 2.9 | 0.8 | 10.3 |
| Total cash, cash equivalents, and restricted cash | 157.7 | 161.8 | 275.3 |
| Accrued investment income | 146.3 | 112.1 | 119.7 |
| Premiums receivable, net of allowance for doubtful accounts of \$210.5, \$175.8, and \$210.9 | 6,230.2 | 5,091.3 | 5,422.5 |
| Reinsurance recoverables, including \$117.6, \$79.2, and \$103.3 on paid losses and loss adjustment expenses | 2,410.7 | 2,027.1 | 2,273.4 |
| Prepaid reinsurance premiums | 289.8 | 212.6 | 203.3 |
| Deferred acquisition costs | 895.7 | 727.2 | 780.5 |
| Property and equipment, net of accumulated depreciation of \$984.7, \$894.7, and \$940.6 | 1,116.4 | 1,152.1 | 1,119.6 |
| Goodwill | 452.7 | 452.7 | 452.7 |
| Intangible assets, net of accumulated amortization of \$211.7, \$140.5, and \$175.7 | 330.6 | 401.8 | 366.6 |
| Other assets | 412.2 | 372.7 | 412.9 |
| Total assets | \$43,363.5 | \$36,689.8 | \$38,701.2 |
| Liabilities | | | |
| Unearned premiums | \$10,245.9 | \$8,407.7 | \$8,903.5 |
| Loss and loss adjustment expense reserves | 14,070.8 | 12,060.4 | 13,086.9 |
| Net deferred income taxes | 46.0 | 191.8 | 135.0 |
| Accounts payable, accrued expenses, and other liabilities | 3,922.3 | 3,153.2 | 3,481.0 |
| Debt ¹ | 3,859.5 | 3,383.4 | 3,306.3 |
| Total liabilities | 32,144.5 | 27,196.5 | 28,912.7 |
| Redeemable noncontrolling interest (NCI) ² | 218.2 | 501.8 | 503.7 |
| Shareholders' Equity | | | |
| Serial Preferred Shares (authorized 20.0) | | | |
| Serial Preferred Shares, Series B, no par value (cumulative, liquidation preference \$1,000 per share) (authorized, issued, and outstanding 0.5, 0, and 0) | 493.9 | 0 | 0 |
| Common shares, \$1.00 par value (authorized 900.0; issued 797.5, including treasury shares of 215.0, 216.5, and 215.8) | 582.5 | 581.0 | 581.7 |
| Paid-in capital | 1,425.9 | 1,351.0 | 1,389.2 |
| Retained earnings | 8,720.4 | 5,908.8 | 6,031.7 |
| Accumulated other comprehensive income: | | | |

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| | | | |
|--|------------|------------|-------------|
| Net unrealized gains (losses) on securities | (210.9 |) 1,164.6 | 1,295.0 |
| Net unrealized losses on forecasted transactions | (17.6 |) (15.1 |) (14.8 |
| Foreign currency translation adjustment | 0 | (0.9 |) 0 |
| Accumulated other comprehensive (income) loss attributable to NCI | 6.6 | 2.1 | 2.0 |
| Total accumulated other comprehensive income attributable to Progressive | (221.9 |) 1,150.7 | 1,282.2 |
| Total shareholders' equity | 11,000.8 | 8,991.5 | 9,284.8 |
| Total liabilities, redeemable NCI, and shareholders' equity | \$43,363.5 | \$36,689.8 | \$ 38,701.2 |

¹ Consists of long-term debt. See Note 4 – Debt for further discussion.

² See Note 12 – Redeemable Noncontrolling Interest for further discussion.

See notes to consolidated financial statements.

3

The Progressive Corporation and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
(unaudited)

| Six Months Ended June 30, (millions — except per share amounts) | 2018 | 2017 |
|---|-------------------|------------------|
| Serial Preferred Shares, No Par Value | | |
| Balance, Beginning of period | \$0 | \$0 |
| Issuance of Serial Preferred Shares, Series B | 493.9 | 0 |
| Balance, End of period | \$493.9 | \$0 |
| Common Shares, \$1.00 Par Value | | |
| Balance, Beginning of period | \$581.7 | \$579.9 |
| Treasury shares purchased | (0.7) | (0.7) |
| Net restricted equity awards issued/vested | 1.5 | 1.8 |
| Balance, End of period | \$582.5 | \$581.0 |
| Paid-In Capital | | |
| Balance, Beginning of period | \$1,389.2 | \$1,303.4 |
| Treasury shares purchased | (1.7) | (1.5) |
| Net restricted equity awards issued/vested | (1.5) | (1.8) |
| Amortization of equity-based compensation | 37.5 | 52.2 |
| Reinvested dividends on restricted stock units | (0.8) | 0.1 |
| Adjustment to carrying amount of redeemable noncontrolling interest | 3.2 | (1.4) |
| Balance, End of period | \$1,425.9 | \$1,351.0 |
| Retained Earnings | | |
| Balance, Beginning of period | \$6,031.7 | \$5,140.4 |
| Net income attributable to Progressive | 1,422.2 | 791.9 |
| Treasury shares purchased | (37.0) | (21.9) |
| Reinvested dividends on restricted stock units | 0.8 | (0.1) |
| Cumulative effect of change in accounting principle ¹ | 1,300.2 | 0 |
| Reclassification of disproportionate tax effects ¹ | 4.3 | 0 |
| Other, net | (1.8) | (1.5) |
| Balance, End of period | \$8,720.4 | \$5,908.8 |
| Accumulated Other Comprehensive Income Attributable to Progressive | | |
| Balance, Beginning of period | \$1,282.2 | \$933.4 |
| Attributable to noncontrolling interest | 4.6 | (2.2) |
| Other comprehensive income | (204.2) | 219.5 |
| Cumulative effect of change in accounting principle ¹ | (1,300.2) | 0 |
| Reclassification of disproportionate tax effects ¹ | (4.3) | 0 |
| Balance, End of period | \$(221.9) | \$1,150.7 |
| Total Shareholders' Equity | \$11,000.8 | \$8,991.5 |

¹ See Note 14 – New Accounting Standards for further discussion.

There are 5.0 million Voting Preference Shares authorized; no such shares have been issued.

See notes to consolidated financial statements.

| The Progressive Corporation and Subsidiaries | | |
|---|------------|-----------|
| Consolidated Statements of Cash Flows | | |
| (unaudited) (millions) | | |
| Six Months Ended June 30, | 2018 | 2017 |
| Cash Flows From Operating Activities | | |
| Net income | \$1,431.0 | \$803.0 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 86.6 | 84.0 |
| Amortization of intangible assets | 36.0 | 31.0 |
| Net amortization of fixed-income securities | 23.2 | 44.1 |
| Amortization of equity-based compensation | 38.5 | 53.9 |
| Net realized (gains) losses on securities | 15.4 | (84.0) |
| Net (gains) losses on disposition of property and equipment | 1.7 | 3.2 |
| Other (gains) losses | 0 | (0.2) |
| Changes in: | | |
| Premiums receivable | (807.7) | (582.0) |
| Reinsurance recoverables | (137.3) | (142.4) |
| Prepaid reinsurance premiums | (86.5) | (42.1) |
| Deferred acquisition costs | (115.2) | (76.0) |
| Income taxes | 2.0 | (64.3) |
| Unearned premiums | 1,342.4 | 939.0 |
| Loss and loss adjustment expense reserves | 983.9 | 692.3 |
| Accounts payable, accrued expenses, and other liabilities | 700.4 | 430.2 |
| Other, net | (31.1) | (67.1) |
| Net cash provided by operating activities | 3,483.3 | 2,022.6 |
| Cash Flows From Investing Activities | | |
| Purchases: | | |
| Fixed maturities | (10,780.0) | (6,803.3) |
| Equity securities | (136.4) | (89.5) |
| Sales: | | |
| Fixed maturities | 3,916.1 | 2,359.9 |
| Equity securities | 460.0 | 133.3 |
| Maturities, paydowns, calls, and other: | | |
| Fixed maturities | 2,936.2 | 2,413.5 |
| Equity securities | 15.0 | 50.0 |
| Net sales (purchases) of short-term investments | (343.8) | (146.8) |
| Net unsettled security transactions | 367.9 | 259.3 |
| Purchases of property and equipment | (102.0) | (73.2) |
| Sales of property and equipment | 6.7 | 12.5 |
| Acquisition of additional shares of ARX Holding Corp. | (295.9) | 0 |
| Acquisition of an insurance company, net of cash acquired | 0 | (18.1) |
| Net cash used in investing activities | (3,956.2) | (1,902.4) |
| Cash Flows From Financing Activities | | |
| Net proceeds from issuance of Serial Preferred Shares, Series B | 493.9 | 0 |
| Net proceeds from debt issuance | 589.5 | 841.1 |
| Payments of debt | (37.1) | (12.5) |
| Redemption/reacquisition of subordinated debt | 0 | (594.4) |
| Dividends paid to common shareholders | (654.9) | (395.4) |
| Proceeds from exercise of equity options | 3.3 | 0.5 |

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| | | |
|---|----------|----------|
| Acquisition of treasury shares for restricted stock tax liabilities | (39.0) | (24.1) |
| Acquisition of treasury shares acquired in open market | (0.4) | 0 |
| Net cash provided by (used in) financing activities | 355.3 | (184.8) |
| Decrease in cash, cash equivalents, and restricted cash | (117.6) | (64.6) |
| Cash, cash equivalents, and restricted cash – January 1 | 275.3 | 226.4 |
| Cash, cash equivalents, and restricted cash – June 30 | \$157.7 | \$161.8 |

See notes to consolidated financial statements.

The Progressive Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Note 1 Basis of Presentation — The accompanying consolidated financial statements include the accounts of The Progressive Corporation and ARX Holding Corp. (ARX), and their respective wholly owned insurance and non-insurance subsidiaries and affiliates in which Progressive or ARX has a controlling financial interest. The Progressive Corporation owned 86.7% of the outstanding capital stock of ARX at June 30, 2018 and 69.0% at June 30, 2017 and December 31, 2017. The increase in Progressive's ownership of ARX at June 30, 2018, is due to the minority ARX shareholders who "put" 204,527 of their ARX shares during the second quarter 2018, including exercised stock options, to Progressive pursuant to the stockholders' agreement. All intercompany accounts and transactions are eliminated in consolidation.

The consolidated financial statements reflect all normal recurring adjustments that, in the opinion of management, were necessary for a fair statement of the results for the interim periods presented. The results of operations for the period ended June 30, 2018, are not necessarily indicative of the results expected for the full year. These consolidated financial statements and the notes thereto should be read in conjunction with Progressive's audited financial statements and accompanying notes included in Exhibit 13 to our Annual Report on Form 10-K for the year ended December 31, 2017 ("2017 Annual Report to Shareholders").

Other assets on the consolidated balance sheets include properties that are considered "held for sale," if any. The fair value of these properties, less the estimated cost to sell them, was \$17.4 million at June 30, 2018 and \$5.3 million at December 31, 2017. No properties were held for sale at June 30, 2017.

Note 2 Investments — The following tables present the composition of our investment portfolio by major security type, consistent with our classification of how we manage, monitor, and measure the portfolio. Our securities are reported in our Consolidated Balance Sheets at fair value, with all of our equity securities having a readily determinable fair value. The changes in fair value for our fixed-maturity securities (other than hybrid securities) are reported as a component of accumulated other comprehensive income, net of deferred income taxes, in our Consolidated Balance Sheets.

The net holding period gains (losses) reported below represent the inception-to-date changes in fair value. The changes in the net holding period gains (losses) between periods for the hybrid securities and, beginning in 2018, equity securities are recorded as a component of net realized gains (losses) on securities in our Consolidated Statements of Comprehensive Income. Prior to 2018, the change in fair value of our equity securities was part of accumulated other comprehensive income (see Note 14 – New Accounting Standards for further discussion).

| (\$ in millions) | Cost | Gross Unrealized Gains | Gross Unrealized Losses | Net Holding Period Gains (Losses) | Fair Value | % of Total Fair Value |
|--|------------|------------------------------|-------------------------------|---|---------------|--------------------------------|
| June 30, 2018 | | | | | | |
| Available-for-sale securities: | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | \$8,005.8 | \$ 0.9 | \$ (141.3) | \$0 | \$7,865.4 | 25.4 % |
| State and local government obligations | 1,678.9 | 4.3 | (15.9) | 0 | 1,667.3 | 5.4 |
| Foreign government obligations | 0 | 0 | 0 | 0 | 0 | 0 |
| Corporate debt securities | 7,422.4 | 4.2 | (94.3) | (2.0) | 7,330.3 | 23.7 |
| Residential mortgage-backed securities | 819.6 | 8.4 | (5.4) | 0 | 822.6 | 2.7 |
| Commercial mortgage-backed securities | 2,725.5 | 2.9 | (31.5) | 0 | 2,696.9 | 8.7 |
| Other asset-backed securities | 3,189.2 | 2.0 | (13.7) | 0.1 | 3,177.6 | 10.3 |
| Redeemable preferred stocks | 220.4 | 14.1 | (2.0) | (3.4) | 229.1 | 0.7 |
| Total fixed maturities | 24,061.8 | 36.8 | (304.1) | (5.3) | 23,789.2 | 76.9 |
| Short-term investments | 3,231.2 | 0 | 0 | 0 | 3,231.2 | 10.5 |
| Total available-for-sale securities | 27,293.0 | 36.8 | (304.1) | (5.3) | 27,020.4 | 87.4 |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 677.0 | 0 | 0 | 81.6 | 758.6 | 2.4 |
| Common equities | 1,314.0 | 0 | 0 | 1,828.2 | 3,142.2 | 10.2 |
| Total equity securities | 1,991.0 | 0 | 0 | 1,909.8 | 3,900.8 | 12.6 |
| Total portfolio ^{1,2} | \$29,284.0 | \$ 36.8 | \$ (304.1) | \$1,904.5 | \$30,921.2 | 100.0 % |

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| (\$ in millions) | Cost | Gross Unrealized Gains | Gross Unrealized Losses | Net Holding Period Gains (Losses) | Fair Value | % of Total Fair Value |
|--|------------|------------------------|-------------------------|-----------------------------------|------------|-----------------------|
| June 30, 2017 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | \$4,166.4 | \$ 4.4 | \$ (15.8) | \$ 0 | \$4,155.0 | 16.0 % |
| State and local government obligations | 2,473.3 | 32.5 | (5.9) | 0.2 | 2,500.1 | 9.7 |
| Foreign government obligations | 22.5 | 0 | 0 | 0 | 22.5 | 0.1 |
| Corporate debt securities | 4,991.6 | 29.4 | (7.6) | 0.4 | 5,013.8 | 19.3 |
| Residential mortgage-backed securities | 1,260.3 | 10.9 | (5.9) | 2.3 | 1,267.6 | 4.8 |
| Commercial mortgage-backed securities | 2,364.9 | 19.8 | (9.7) | 0 | 2,375.0 | 9.1 |
| Other asset-backed securities | 2,843.3 | 6.4 | (2.5) | 0.2 | 2,847.4 | 11.0 |
| Redeemable preferred stocks | 189.4 | 19.0 | (1.7) | 0 | 206.7 | 0.8 |
| Total fixed maturities | 18,311.7 | 122.4 | (49.1) | 3.1 | 18,388.1 | 70.8 |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 666.0 | 123.6 | (6.5) | 0 | 783.1 | 3.0 |
| Common equities | 1,472.3 | 1,611.7 | (6.5) | 0 | 3,077.5 | 11.8 |
| Short-term investments | 3,729.7 | 0 | 0 | 0 | 3,729.7 | 14.4 |
| Total portfolio ^{1,2} | \$24,179.7 | \$ 1,857.7 | \$ (62.1) | \$ 3.1 | \$25,978.4 | 100.0 % |

| (\$ in millions) | Cost | Gross Unrealized Gains | Gross Unrealized Losses | Net Holding Period Gains (Losses) | Fair Value | % of Total Fair Value |
|--|------------|------------------------|-------------------------|-----------------------------------|------------|-----------------------|
| December 31, 2017 | | | | | | |
| Fixed maturities: | | | | | | |
| U.S. government obligations | \$6,688.8 | \$ 1.1 | \$ (44.0) | \$ 0 | \$6,645.9 | 24.4 % |
| State and local government obligations | 2,285.6 | 20.7 | (9.3) | 0.1 | 2,297.1 | 8.4 |
| Foreign government obligations | 0 | 0 | 0 | 0 | 0 | 0 |
| Corporate debt securities | 4,997.2 | 14.8 | (14.4) | 0.1 | 4,997.7 | 18.3 |
| Residential mortgage-backed securities | 828.8 | 11.3 | (3.4) | 0 | 836.7 | 3.1 |
| Commercial mortgage-backed securities | 2,760.1 | 11.8 | (13.3) | 0 | 2,758.6 | 10.1 |
| Other asset-backed securities | 2,454.5 | 4.5 | (4.5) | 0.2 | 2,454.7 | 9.0 |
| Redeemable preferred stocks | 194.9 | 17.8 | (1.5) | (0.2) | 211.0 | 0.8 |
| Total fixed maturities | 20,209.9 | 82.0 | (90.4) | 0.2 | 20,201.7 | 74.1 |
| Equity securities: | | | | | | |
| Nonredeemable preferred stocks | 698.6 | 114.0 | (8.8) | 0 | 803.8 | 2.9 |
| Common equities | 1,499.0 | 1,901.0 | (0.2) | 0 | 3,399.8 | 12.5 |
| Short-term investments | 2,869.4 | 0 | 0 | 0 | 2,869.4 | 10.5 |
| Total portfolio ^{1,2} | \$25,276.9 | \$ 2,097.0 | \$ (99.4) | \$ 0.2 | \$27,274.7 | 100.0 % |

¹Our portfolio reflects the effect of unsettled security transactions; at June 30, 2018 and 2017, we had \$362.1 million and \$287.1 million, respectively, included in "other liabilities," compared to \$5.8 million included in "other assets" at December 31, 2017.

²The total fair value of the portfolio at June 30, 2018 and 2017, and December 31, 2017, included \$1.7 billion, \$1.1 billion, and \$1.6 billion, respectively, of securities held in a consolidated, non-insurance subsidiary of the holding company, net of any unsettled security transactions.

Short-Term Investments Our short-term investments may include commercial paper and other investments that are expected to mature or are redeemable within one year.

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We did not have any open repurchase or reverse repurchase transactions in our short-term investment portfolio at June 30, 2018 and 2017, or December 31, 2017. To the extent we enter into repurchase or reverse repurchase transactions, and consistent with past practice, we would elect not to offset these transactions and would report them on a gross basis on our balance sheets despite the option to elect to offset these transactions as long as they were with the same counterparty and subject to an enforceable master netting arrangement.

Hybrid Securities Included in our fixed-maturity securities are hybrid securities, which are reported at fair value:

| (millions) | June 30, | | December 31, 2017 |
|--|----------|---------|----------------------|
| | 2018 | 2017 | |
| Fixed maturities: | | | |
| State and local government obligations | \$3.6 | \$6.6 | \$ 6.1 |
| Corporate debt securities | 170.3 | 61.3 | 99.8 |
| Residential mortgage-backed securities | 0 | 189.7 | 0 |
| Other asset-backed securities | 5.5 | 7.7 | 6.7 |
| Redeemable preferred stocks | 67.3 | 0 | 30.3 |
| Total hybrid securities | \$246.7 | \$265.3 | \$ 142.9 |

Certain securities in our portfolio are accounted for as hybrid securities because they contain embedded derivatives that are not deemed to be clearly and closely related to the host investments. Since the embedded derivative (e.g., change-in-control put option, debt-to-equity conversion, or any other feature unrelated to the credit quality or risk of default of the issuer that could impact the amount or timing of our expected future cash flows) does not have an observable intrinsic value, we have elected to record the change in fair value of the entire security through income as a realized gain or loss.

Fixed Maturities The composition of fixed maturities by maturity at June 30, 2018, was:

| (millions) | Cost | Fair Value |
|----------------------|------------|---------------|
| Less than one year | \$3,805.2 | \$3,809.2 |
| One to five years | 15,190.7 | 14,999.1 |
| Five to ten years | 4,939.7 | 4,855.4 |
| Ten years or greater | 126.2 | 125.5 |
| Total | \$24,061.8 | \$23,789.2 |

Asset-backed securities are classified in the maturity distribution table based upon their projected cash flows. All other securities which do not have a single maturity date are reported based upon expected average maturity. Contractual maturities may differ from expected maturities because the issuers of the securities may have the right to call or prepay obligations.

Gross Unrealized Losses As of June 30, 2018, we had \$304.1 million of gross unrealized losses in our fixed-maturity securities. A review of our fixed-maturity securities indicated that the issuers were current with respect to their interest obligations and that there was no evidence of deterioration of the current cash flow projections that would indicate we would not receive the remaining principal at maturity.

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The following tables show the composition of gross unrealized losses by major security type and by the length of time that individual securities have been in a continuous unrealized loss position:

| (\$ in millions) | Total No. of Sec. | Total Fair Value | Gross Unrealized Losses | Less than 12 Months | | 12 Months or Greater | | Unrealized Losses | |
|--|-------------------|------------------|-------------------------|---------------------|------------|----------------------|------------|-------------------|-----------|
| | | | | No. of Sec. | Fair Value | No. of Sec. | Fair Value | | |
| June 30, 2018 | | | | | | | | | |
| Fixed maturities: | | | | | | | | | |
| U.S. government obligations | 70 | \$7,503.2 | \$(141.3) | 33 | \$4,543.5 | \$(73.6) | 37 | \$2,959.7 | \$(67.7) |
| State and local government obligations | 355 | 1,050.9 | (15.9) | 219 | 631.9 | (7.1) | 136 | 419.0 | (8.8) |
| Corporate debt securities | 391 | 6,153.5 | (94.3) | 322 | 5,439.3 | (77.2) | 69 | 714.2 | (17.1) |
| Residential mortgage-backed securities | 227 | 380.3 | (5.4) | 52 | 188.6 | (0.9) | 175 | 191.7 | (4.5) |
| Commercial mortgage-backed securities | 142 | 2,300.9 | (31.5) | 85 | 1,371.4 | (14.4) | 57 | 929.5 | (17.1) |
| Other asset-backed securities | 219 | 2,479.7 | (13.7) | 148 | 2,055.1 | (8.5) | 71 | 424.6 | (5.2) |
| Redeemable preferred stocks | 3 | 30.2 | (2.0) | 1 | 4.6 | (0.2) | 2 | 25.6 | (1.8) |
| Total fixed maturities | 1,407 | \$19,898.7 | \$(304.1) | 860 | \$14,234.4 | \$(181.9) | 547 | \$5,664.3 | \$(122.2) |
| (\$ in millions) | Total No. of Sec. | Total Fair Value | Gross Unrealized Losses | Less than 12 Months | | 12 Months or Greater | | Unrealized Losses | |
| | | | | No. of Sec. | Fair Value | No. of Sec. | Fair Value | | |
| June 30, 2017 | | | | | | | | | |
| Fixed maturities: | | | | | | | | | |
| U.S. government obligations | 41 | \$2,781.8 | \$(15.8) | 39 | \$2,725.1 | \$(15.1) | 2 | \$56.7 | \$(0.7) |
| State and local government obligations | 222 | 818.7 | (5.9) | 138 | 479.8 | (3.3) | 84 | 338.9 | (2.6) |
| Corporate debt securities | 143 | 1,905.2 | (7.6) | 122 | 1,599.6 | (5.3) | 21 | 305.6 | (2.3) |
| Residential mortgage-backed securities | 220 | 535.7 | (5.9) | 126 | 197.8 | (1.1) | 94 | 337.9 | (4.8) |
| Commercial mortgage-backed securities | 74 | 905.6 | (9.7) | 52 | 679.5 | (5.7) | 22 | 226.1 | (4.0) |
| Other asset-backed securities | 160 | 2,077.8 | (2.5) | 145 | 1,823.8 | (1.9) | 15 | 254.0 | (0.6) |
| Redeemable preferred stocks | 1 | 10.8 | (1.7) | 0 | 0 | 0 | 1 | 10.8 | (1.7) |
| Total fixed maturities | 861 | 9,035.6 | (49.1) | 622 | 7,505.6 | (32.4) | 239 | 1,530.0 | (16.7) |
| Equity securities: | | | | | | | | | |
| Nonredeemable preferred stocks | 3 | 73.1 | (6.5) | 0 | 0 | 0 | 3 | 73.1 | (6.5) |
| Common equities | 80 | 73.1 | (6.5) | 74 | 72.3 | (6.5) | 6 | 0.8 | 0 |
| Total equity securities | 83 | 146.2 | (13.0) | 74 | 72.3 | (6.5) | 9 | 73.9 | (6.5) |
| Total portfolio | 944 | \$9,181.8 | \$(62.1) | 696 | \$7,577.9 | \$(38.9) | 248 | \$1,603.9 | \$(23.2) |
| (\$ in millions) | Total No. of Sec. | Total Fair Value | Gross Unrealized Losses | Less than 12 Months | | 12 Months or Greater | | Unrealized Losses | |
| | | | | No. of Sec. | Fair Value | No. of Sec. | Fair Value | | |
| December 31, 2017 | | | | | | | | | |
| Fixed maturities: | | | | | | | | | |
| | 58 | \$5,817.0 | \$(44.0) | 41 | \$4,869.3 | \$(34.6) | 17 | \$947.7 | \$(9.4) |

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| | | | | | | | | | |
|--|-------|------------|----------|-------|------------|----------|-------|-----------|----------|
| U.S. government obligations | | | | | | | | | |
| State and local government obligations | 358 | 1,200.3 | (9.3) |) 230 | 737.6 | (4.4) |) 128 | 462.7 | (4.9) |
| Corporate debt securities | 222 | 2,979.4 | (14.4) |) 171 | 2,072.9 | (9.1) |) 51 | 906.5 | (5.3) |
| Residential mortgage-backed securities | 201 | 300.9 | (3.4) |) 30 | 75.1 | (0.2) |) 171 | 225.8 | (3.2) |
| Commercial mortgage-backed securities | 105 | 1,682.3 | (13.3) |) 63 | 1,221.2 | (5.9) |) 42 | 461.1 | (7.4) |
| Other asset-backed securities | 197 | 1,837.3 | (4.5) |) 134 | 1,377.8 | (3.3) |) 63 | 459.5 | (1.2) |
| Redeemable preferred stocks | 2 | 21.8 | (1.5) |) 1 | 10.8 | (0.1) |) 1 | 11.0 | (1.4) |
| Total fixed maturities | 1,143 | 13,839.0 | (90.4) |) 670 | 10,364.7 | (57.6) |) 473 | 3,474.3 | (32.8) |
| Equity securities: | | | | | | | | | |
| Nonredeemable preferred stocks | 4 | 127.8 | (8.8) |) 1 | 56.5 | (0.5) |) 3 | 71.3 | (8.3) |
| Common equities | 19 | 13.4 | (0.2) |) 18 | 13.4 | (0.2) |) 1 | 0 | 0 |
| Total equity securities | 23 | 141.2 | (9.0) |) 19 | 69.9 | (0.7) |) 4 | 71.3 | (8.3) |
| Total portfolio | 1,166 | \$13,980.2 | \$(99.4) |) 689 | \$10,434.6 | \$(58.3) |) 477 | \$3,545.6 | \$(41.1) |

Since both June 30, 2017 and December 31, 2017, the number of securities in our fixed-maturity portfolio with unrealized losses increased, primarily the result of rising interest rates during the latter part of 2017 and early 2018. We had no material decreases in valuation as a result of credit rating downgrades and all of the securities in the table above are current with respect to required principal and interest payments.

Other-Than-Temporary Impairment (OTTI) The following table shows the total non-credit portion of the OTTI recorded in accumulated other comprehensive income, reflecting the original non-credit loss at the time the credit impairment was determined (i.e., unadjusted for valuation changes subsequent to the original write-down):

| (millions) | June 30, | | December 31, |
|--|----------|----------|--------------|
| | 2018 | 2017 | 2017 |
| Fixed maturities: | | | |
| Residential mortgage-backed securities | \$(19.7) | \$(19.7) | \$ (19.7) |
| Commercial mortgage-backed securities | (0.3) | (0.5) | (0.3) |
| Total fixed maturities | \$(20.0) | \$(20.2) | \$ (20.0) |

The following tables provide rollforwards of the amounts related to credit losses recognized in earnings for the periods ended June 30, 2018 and 2017, for which a portion of the OTTI losses were also recognized in accumulated other comprehensive income at the time the credit impairments were determined and recognized:

| (millions) | Three Months Ended | | |
|---|--------------------|------------|--------|
| | June 30, 2018 | | |
| | Mortgage-Backed | | |
| | Residential | Commercial | Total |
| Balance at March 31, 2018 | \$ 0 | \$ 0.5 | \$ 0.5 |
| Reductions for securities sold/matured | 0 | 0 | 0 |
| Change in recoveries of future cash flows expected to be collected ¹ | 0.3 | 0 | 0.3 |
| Balance at June 30, 2018 | \$ 0.3 | \$ 0.5 | \$ 0.8 |

| (millions) | Six Months Ended June | | |
|---|-----------------------|------------|--------|
| | 30, 2018 | | |
| | Mortgage-Backed | | |
| | Residential | Commercial | Total |
| Balance at December 31, 2017 | \$ 0 | \$ 0.5 | \$ 0.5 |
| Reductions for securities sold/matured | 0 | 0 | 0 |
| Change in recoveries of future cash flows expected to be collected ¹ | 0.3 | 0 | 0.3 |
| Balance at June 30, 2018 | \$ 0.3 | \$ 0.5 | \$ 0.8 |

| (millions) | Three Months Ended June 30, 2017 | | |
|---|----------------------------------|------------|---------|
| | Mortgage-Backed | | |
| | Residential | Commercial | Total |
| Balance at March 31, 2017 | \$11.4 | \$ 0.1 | \$11.5 |
| Reductions for securities sold/matured | (11.4) | 0 | (11.4) |
| Change in recoveries of future cash flows expected to be collected ¹ | 0.2 | 0 | 0.2 |
| Balance at June 30, 2017 | \$0.2 | \$ 0.1 | \$0.3 |

| (millions) | Six Months Ended June 30, 2017 | | |
|---|--------------------------------|------------|---------|
| | Mortgage-Backed | | |
| | Residential | Commercial | Total |
| Balance at December 31, 2016 | \$11.1 | \$ 0.4 | \$11.5 |
| Reductions for securities sold/matured | (10.9) | (0.3) | (11.2) |
| Change in recoveries of future cash flows expected to be collected ¹ | 0 | 0 | 0 |
| Balance at June 30, 2017 | \$0.2 | \$ 0.1 | \$0.3 |

¹Reflects the current period change in the expected recovery of prior impairments that will be accreted into income over the remaining life of the security.

Although we determined it is more likely that we will not be required to sell the securities prior to the recovery of their respective cost bases (which could be maturity), we are required to measure the amount of potential credit losses on the securities that were in an unrealized loss position. In that process, we considered a number of factors and inputs related to the individual securities. The methodology and significant inputs used to measure the amount of credit losses in our portfolio included: current performance indicators on the business model or underlying assets (e.g., delinquency rates, foreclosure rates, and default rates); credit support (via current levels of subordination); historical credit ratings; and updated cash flow expectations based upon these performance indicators. In order to determine the amount of credit loss, if any, the net present value of the cash flows expected (i.e., expected recovery value) was calculated using the current book yield for each security, and was compared to its current amortized value. In the event that the net present value was below the amortized value, a credit loss would be deemed to exist, and the security would be written down. We did not have any credit impairment write-downs for the six months ended June 30, 2018 or 2017.

Realized Gains (Losses) The components of net realized gains (losses) for the three and six months ended June 30, were:

| (millions) | Three Months | | Six Months | |
|--|--------------|--------|------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| Gross realized gains on security sales | | | | |
| Available-for-sale securities: | | | | |
| U.S. government obligations | \$1.7 | \$4.5 | \$1.7 | \$4.9 |
| State and local government obligations | 0.6 | 2.6 | 9.2 | 3.1 |
| Corporate and other debt securities | 0.3 | 7.3 | 0.4 | 11.4 |
| Residential mortgage-backed securities | 0 | 20.9 | 0 | 21.0 |
| Commercial mortgage-backed securities | 0.3 | 1.2 | 2.0 | 2.4 |
| Other asset-backed securities | 0.1 | 0 | 0.1 | 0.3 |
| Redeemable preferred stocks | 3.2 | 0 | 4.3 | 0.3 |
| Total available-for-sale securities | 6.2 | 36.5 | 17.7 | 43.4 |
| Equity securities: | | | | |
| Nonredeemable preferred stocks | 0 | 6.2 | 3.6 | 51.6 |
| Common equities | 18.5 | 9.9 | 138.4 | 17.3 |
| Total equity securities | 18.5 | 16.1 | 142.0 | 68.9 |
| Subtotal gross realized gains on security sales | 24.7 | 52.6 | 159.7 | 112.3 |
| Gross realized losses on security sales | | | | |
| Available-for-sale securities: | | | | |
| U.S. government obligations | (29.9) | (0.4) | (38.8) | (3.6) |
| State and local government obligations | (0.6) | 0 | (1.9) | (0.1) |
| Corporate and other debt securities | (1.0) | (1.9) | (4.1) | (2.8) |
| Residential mortgage-backed securities | 0 | (0.3) | 0 | (0.3) |
| Commercial mortgage-backed securities | 0 | (0.7) | (6.3) | (3.1) |
| Other asset-backed securities | (0.9) | 0 | (1.0) | 0 |
| Total available-for-sale securities | (32.4) | (3.3) | (52.1) | (9.9) |
| Equity securities: | | | | |
| Nonredeemable preferred stocks | (1.9) | (4.6) | (2.3) | (5.8) |
| Common equities | 0 | 0 | (7.9) | (0.1) |
| Total equity securities | (1.9) | (4.6) | (10.2) | (5.9) |
| Subtotal gross realized losses on security sales | (34.3) | (7.9) | (62.3) | (15.8) |
| Net realized gains (losses) on security sales | | | | |
| Available-for-sale securities: | | | | |
| U.S. government obligations | (28.2) | 4.1 | (37.1) | 1.3 |
| State and local government obligations | 0 | 2.6 | 7.3 | 3.0 |
| Corporate and other debt securities | (0.7) | 5.4 | (3.7) | 8.6 |
| Residential mortgage-backed securities | 0 | 20.6 | 0 | 20.7 |
| Commercial mortgage-backed securities | 0.3 | 0.5 | (4.3) | (0.7) |
| Other asset-backed securities | (0.8) | 0 | (0.9) | 0.3 |
| Redeemable preferred stocks | 3.2 | 0 | 4.3 | 0.3 |
| Total available-for-sale securities | (26.2) | 33.2 | (34.4) | 33.5 |
| Equity securities: | | | | |
| Nonredeemable preferred stocks | (1.9) | 1.6 | 1.3 | 45.8 |
| Common equities | 18.5 | 9.9 | 130.5 | 17.2 |
| Total equity securities | 16.6 | 11.5 | 131.8 | 63.0 |
| Litigation settlements and other gains (losses) | 0 | 0.8 | 0 | 1.1 |

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| | | | | |
|--|---------|---------|----------|---------|
| Subtotal net realized gains (losses) on security sales | (9.6) | 45.5 | 97.4 | 97.6 |
| Net holding period gains (losses) | | | | |
| Hybrid securities | (2.3) | 0.4 | (5.5) | 1.2 |
| Equity securities | 55.8 | 0 | (96.2) | 0 |
| Subtotal net holding period gains (losses) | 53.5 | 0.4 | (101.7) | 1.2 |
| Other-than-temporary impairment losses | | | | |
| Equity securities: | | | | |
| Common equities | 0 | (2.6) | 0 | (3.6) |
| Subtotal investment other-than-temporary impairment losses | 0 | (2.6) | 0 | (3.6) |
| Other asset impairment | (11.1) | (11.2) | (11.1) | (11.2) |
| Subtotal other-than-temporary impairment losses | (11.1) | (13.8) | (11.1) | (14.8) |
| Total net realized gains (losses) on securities | \$32.8 | \$32.1 | \$(15.4) | \$84.0 |

Gross realized gains were predominantly the result of sales in our indexed common stock portfolio in order to reduce the overall portfolio risk, while gross realized losses were predominantly in our available-for-sale securities and were the result of changes in credit spreads and interest rates. Also included are holding period change in valuation gains and losses on equity securities and hybrid securities, recoveries from litigation settlements related to investments, and write-downs for securities determined to be other-than-temporarily impaired. The other asset impairment relates to renewable energy investments, which

are reflected in “other assets” on the balance sheet, under which the future pretax cash flows are expected to be less than the carrying value of the assets.

The following table reflects our holding period realized gains (losses) on equity securities recognized for the three and six months ended June 30, 2018 for equity securities held at quarter end:

| (millions) | Three Months 2018 | Six Months 2018 |
|--|-------------------------|-----------------------|
| Total net gains (losses) recognized during the period on equity securities | \$ 72.4 | \$ 35.6 |
| Less: Net gains (losses) recognized on equity securities sold during the period | 16.6 | 131.8 |
| Net holding period gains (losses) recognized during the period on equity securities held at period end | \$ 55.8 | \$ (96.2) |

Note: Comparative disclosure for the prior year period is not meaningful.

Net Investment Income The components of net investment income for the three and six months ended June 30, were:

| (millions) | Three Months | | Six Months | |
|--|--------------|---------|------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| Available-for-sale securities: | | | | |
| Fixed maturities: | | | | |
| U.S. government obligations | \$45.9 | \$17.0 | \$85.7 | \$29.7 |
| State and local government obligations | 9.1 | 13.1 | 19.1 | 26.4 |
| Foreign government obligations | 0 | 0.1 | 0 | 0.2 |
| Corporate debt securities | 51.8 | 31.3 | 88.0 | 60.9 |
| Residential mortgage-backed securities | 6.6 | 10.3 | 13.5 | 19.9 |
| Commercial mortgage-backed securities | 20.2 | 18.3 | 41.4 | 37.1 |
| Other asset-backed securities | 16.1 | 11.8 | 29.7 | 21.7 |
| Redeemable preferred stocks | 2.9 | 2.9 | 5.5 | 6.3 |
| Total fixed maturities | 152.6 | 104.8 | 282.9 | 202.2 |
| Short-term investments | 14.9 | 8.8 | 25.0 | 15.8 |
| Total available-for-sale securities | 167.5 | 113.6 | 307.9 | 218.0 |
| Equity securities: | | | | |
| Nonredeemable preferred stocks | 10.4 | 10.6 | 21.3 | 22.1 |
| Common equities | 14.2 | 14.6 | 29.2 | 27.9 |
| Total equity securities | 24.6 | 25.2 | 50.5 | 50.0 |
| Investment income | 192.1 | 138.8 | 358.4 | 268.0 |
| Investment expenses | (6.2) | (6.6) | (12.2) | (12.2) |
| Net investment income | \$185.9 | \$132.2 | \$346.2 | \$255.8 |

The amount of investment income (interest and dividends) we recognize varies from year to year based on the average assets held during the year and the book yields of the securities in our portfolio. The increase in net investment income on a year-over-year basis for the three and six months ended June 30, 2018, was due to a combination of an increase in average assets and an increase in portfolio yields. The increase in average assets was due to strong underwriting growth and profitability, as well as the \$600 million debt and \$500 million preferred stock issuances in the first quarter of 2018. The increase in portfolio yields was a result of our decision to increase the portfolio duration from 2.3 years at the end of the second quarter 2017 to 2.6 years at the end of the second quarter 2018 and a general rise in interest rates.

Trading Securities At June 30, 2018 and 2017, and December 31, 2017, we did not hold any trading securities and did not have any net realized gains (losses) on trading securities for the three and six months ended June 30, 2018 and 2017.

Derivative Instruments

At June 30, 2018 and 2017, and December 31, 2017, we had no open derivative positions. During March 2017, we entered into a forecasted debt issuance hedge, against a possible rise in interest rates, in conjunction with the \$850 million of 4.125% Senior Notes due 2047 issued in April 2017. Upon issuance, we closed the hedge and recognized, as part of accumulated other comprehensive income, a pretax unrealized loss of \$8.0 million in April 2017.

See Note 4 – Debt for further discussion.

Note 3 Fair Value — We have categorized our financial instruments, based on the degree of subjectivity inherent in the method by which they are valued, into a fair value hierarchy of three levels, as follows:

Level 1: Inputs are unadjusted quoted prices in active markets for identical instruments at the measurement date (e.g., U.S. government obligations, which are continually priced on a daily basis, active exchange-traded equity securities, and certain short-term securities).

Level 2: Inputs (other than quoted prices included within Level 1) that are observable for the instrument either directly or indirectly (e.g., certain corporate and municipal bonds and certain preferred stocks). This includes: (i) quoted prices for similar instruments in active markets, (ii) quoted prices for identical or similar instruments in markets that are not active, (iii) inputs other than quoted prices that are observable for the instruments, and (iv) inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Inputs that are unobservable. Unobservable inputs reflect our subjective evaluation about the assumptions market participants would use in pricing the financial instrument (e.g., certain structured securities and privately held investments).

Determining the fair value of the investment portfolio is the responsibility of management. As part of the responsibility, we evaluate whether a market is distressed or inactive in determining the fair value for our portfolio. We review certain market level inputs to evaluate whether sufficient activity, volume, and new issuances exist to create an active market. Based on this evaluation, we concluded that there was sufficient activity related to the sectors and securities for which we obtained valuations.

The composition of the investment portfolio by major security type and our outstanding debt was:

| (millions) | Fair Value | | | Total | Cost |
|---|------------|------------|---------|------------|------------|
| | Level 1 | Level 2 | Level 3 | | |
| June 30, 2018 | | | | | |
| Fixed maturities: | | | | | |
| U.S. government obligations | \$7,865.4 | \$0 | \$0 | \$7,865.4 | \$8,005.8 |
| State and local government obligations | 0 | 1,667.3 | 0 | 1,667.3 | 1,678.9 |
| Foreign government obligations | 0 | 0 | 0 | 0 | 0 |
| Corporate debt securities | 0 | 7,330.3 | 0 | 7,330.3 | 7,422.4 |
| Subtotal | 7,865.4 | 8,997.6 | 0 | 16,863.0 | 17,107.1 |
| Asset-backed securities: | | | | | |
| Residential mortgage-backed | 0 | 822.6 | 0 | 822.6 | 819.6 |
| Commercial mortgage-backed | 0 | 2,696.9 | 0 | 2,696.9 | 2,725.5 |
| Other asset-backed | 0 | 3,177.6 | 0 | 3,177.6 | 3,189.2 |
| Subtotal asset-backed securities | 0 | 6,697.1 | 0 | 6,697.1 | 6,734.3 |
| Redeemable preferred stocks: | | | | | |
| Financials | 0 | 67.7 | 0 | 67.7 | 65.3 |
| Utilities | 0 | 4.6 | 0 | 4.6 | 4.8 |
| Industrials | 10.1 | 146.7 | 0 | 156.8 | 150.3 |
| Subtotal redeemable preferred stocks | 10.1 | 219.0 | 0 | 229.1 | 220.4 |
| Total fixed maturities | 7,875.5 | 15,913.7 | 0 | 23,789.2 | 24,061.8 |
| Short-term investments | 2,954.2 | 277.0 | 0 | 3,231.2 | 3,231.2 |
| Total available-for-sale securities | 10,829.7 | 16,190.7 | 0 | 27,020.4 | 27,293.0 |
| Equity securities: | | | | | |
| Nonredeemable preferred stocks: | | | | | |
| Financials | 77.4 | 676.2 | 0 | 753.6 | 672.0 |
| Industrials | 0 | 0 | 5.0 | 5.0 | 5.0 |
| Subtotal nonredeemable preferred stocks | 77.4 | 676.2 | 5.0 | 758.6 | 677.0 |
| Common equities: | | | | | |
| Common stocks | 3,141.9 | 0 | 0 | 3,141.9 | 1,313.7 |
| Other risk investments | 0 | 0 | 0.3 | 0.3 | 0.3 |
| Subtotal common equities | 3,141.9 | 0 | 0.3 | 3,142.2 | 1,314.0 |
| Total equity securities | 3,219.3 | 676.2 | 5.3 | 3,900.8 | 1,991.0 |
| Total portfolio | \$14,049.0 | \$16,866.9 | \$5.3 | \$30,921.2 | \$29,284.0 |
| Debt | \$0 | \$3,959.0 | \$0 | \$3,959.0 | \$3,859.5 |

| (millions) | Fair Value | | | Total | Cost |
|--|------------|------------|---------|------------|------------|
| | Level 1 | Level 2 | Level 3 | | |
| June 30, 2017 | | | | | |
| Fixed maturities: | | | | | |
| U.S. government obligations | \$4,155.0 | \$0 | \$0 | \$4,155.0 | \$4,166.4 |
| State and local government obligations | 0 | 2,500.1 | 0 | 2,500.1 | 2,473.3 |
| Foreign government obligations | 22.5 | 0 | 0 | 22.5 | 22.5 |
| Corporate debt securities | 0 | 5,013.8 | 0 | 5,013.8 | 4,991.6 |
| Subtotal | 4,177.5 | 7,513.9 | 0 | 11,691.4 | 11,653.8 |
| Asset-backed securities: | | | | | |
| Residential mortgage-backed | 0 | 1,267.6 | 0 | 1,267.6 | 1,260.3 |
| Commercial mortgage-backed | 0 | 2,375.0 | 0 | 2,375.0 | 2,364.9 |
| Other asset-backed | 0 | 2,847.4 | 0 | 2,847.4 | 2,843.3 |
| Subtotal asset-backed securities | 0 | 6,490.0 | 0 | 6,490.0 | 6,468.5 |
| Redeemable preferred stocks: | | | | | |
| Financials | 0 | 64.1 | 0 | 64.1 | 60.4 |
| Utilities | 0 | 32.2 | 0 | 32.2 | 30.5 |
| Industrials | 0 | 110.4 | 0 | 110.4 | 98.5 |
| Subtotal redeemable preferred stocks | 0 | 206.7 | 0 | 206.7 | 189.4 |
| Total fixed maturities | 4,177.5 | 14,210.6 | 0 | 18,388.1 | 18,311.7 |
| Equity securities: | | | | | |
| Nonredeemable preferred stocks: | | | | | |
| Financials | 85.3 | 697.8 | 0 | 783.1 | 666.0 |
| Industrials | 0 | 0 | 0 | 0 | 0 |
| Subtotal nonredeemable preferred stocks | 85.3 | 697.8 | 0 | 783.1 | 666.0 |
| Common equities: | | | | | |
| Common stocks | 3,077.2 | 0 | 0 | 3,077.2 | 1,472.0 |
| Other risk investments | 0 | 0 | 0.3 | 0.3 | 0.3 |
| Subtotal common equities | 3,077.2 | 0 | 0.3 | 3,077.5 | 1,472.3 |
| Total fixed maturities and equity securities | 7,340.0 | 14,908.4 | 0.3 | 22,248.7 | 20,450.0 |
| Short-term investments | 2,448.0 | 1,281.7 | 0 | 3,729.7 | 3,729.7 |
| Total portfolio | \$9,788.0 | \$16,190.1 | \$0.3 | \$25,978.4 | \$24,179.7 |
| Debt | \$0 | \$3,564.4 | \$114.8 | \$3,679.2 | \$3,383.4 |

| (millions) | Fair Value | | | Total | Cost |
|--|------------|------------|---------|------------|------------|
| | Level 1 | Level 2 | Level 3 | | |
| December 31, 2017 | | | | | |
| Fixed maturities: | | | | | |
| U.S. government obligations | \$6,645.9 | \$0 | \$0 | \$6,645.9 | \$6,688.8 |
| State and local government obligations | 0 | 2,297.1 | 0 | 2,297.1 | 2,285.6 |
| Foreign government obligations | 0 | 0 | 0 | 0 | 0 |
| Corporate debt securities | 0 | 4,997.7 | 0 | 4,997.7 | 4,997.2 |
| Subtotal | 6,645.9 | 7,294.8 | 0 | 13,940.7 | 13,971.6 |
| Asset-backed securities: | | | | | |
| Residential mortgage-backed | 0 | 836.7 | 0 | 836.7 | 828.8 |
| Commercial mortgage-backed | 0 | 2,758.6 | 0 | 2,758.6 | 2,760.1 |
| Other asset-backed | 0 | 2,454.7 | 0 | 2,454.7 | 2,454.5 |
| Subtotal asset-backed securities | 0 | 6,050.0 | 0 | 6,050.0 | 6,043.4 |
| Redeemable preferred stocks: | | | | | |
| Financials | 0 | 64.1 | 0 | 64.1 | 61.3 |
| Utilities | 0 | 11.4 | 0 | 11.4 | 10.1 |
| Industrials | 0 | 135.5 | 0 | 135.5 | 123.5 |
| Subtotal redeemable preferred stocks | 0 | 211.0 | 0 | 211.0 | 194.9 |
| Total fixed maturities | 6,645.9 | 13,555.8 | 0 | 20,201.7 | 20,209.9 |
| Equity securities: | | | | | |
| Nonredeemable preferred stocks: | | | | | |
| Financials | 80.6 | 718.2 | 0 | 798.8 | 693.6 |
| Industrials | 0 | 0 | 5.0 | 5.0 | 5.0 |
| Subtotal nonredeemable preferred stocks | 80.6 | 718.2 | 5.0 | 803.8 | 698.6 |
| Common equities: | | | | | |
| Common stocks | 3,399.5 | 0 | 0 | 3,399.5 | 1,498.7 |
| Other risk investments | 0 | 0 | 0.3 | 0.3 | 0.3 |
| Subtotal common equities | 3,399.5 | 0 | 0.3 | 3,399.8 | 1,499.0 |
| Total fixed maturities and equity securities | 10,126.0 | 14,274.0 | 5.3 | 24,405.3 | 22,407.5 |
| Short-term investments | 1,824.4 | 1,045.0 | 0 | 2,869.4 | 2,869.4 |
| Total portfolio | \$11,950.4 | \$15,319.0 | \$5.3 | \$27,274.7 | \$25,276.9 |
| Debt | \$0 | \$3,606.5 | \$37.1 | \$3,643.6 | \$3,306.3 |

Our portfolio valuations, excluding short-term investments, classified as either Level 1 or Level 2 in the above tables are priced exclusively by external sources, including: pricing vendors, dealers/market makers, and exchange-quoted prices. We did not have any transfers between Level 1 and Level 2 during 2018 or 2017.

Our short-term security holdings classified as Level 1 are highly liquid, actively marketed, and have a very short duration, primarily 90 days or less to redemption. These securities are held at their original cost, adjusted for any accretion of discount, since that value very closely approximates what an active market participant would be willing to pay for such securities. The remainder of our short-term securities are classified as Level 2 and are not priced externally since these securities continually trade at par value. These securities are classified as Level 2 since they are primarily longer-dated securities issued by municipalities that contain either liquidity facilities or mandatory put features within one year.

At June 30, 2018, vendor-quoted prices represented 72% of our Level 1 classifications (excluding short-term investments), compared to 58% and 66% at June 30, 2017 and December 31, 2017, respectively. The securities quoted by vendors in Level 1 primarily represent our holdings in U.S. Treasury Notes, which are frequently traded, and the quotes are considered similar to exchange-traded quotes. The balance of our Level 1 pricing comes from quotes obtained directly from trades made on active exchanges.

At June 30, 2018 and 2017, and December 31, 2017, vendor-quoted prices comprised 98%, 99%, and 98%, respectively, of our Level 2 classifications (excluding short-term investments), while dealer-quoted prices represented 2%, 1%, and 2%, respectively. In our process for selecting a source (e.g., dealer, pricing service) to provide pricing for securities in our portfolio, we reviewed documentation from the sources that detailed the pricing techniques and methodologies used by these sources and determined if their policies adequately considered market activity, either based on specific transactions for the particular security type or based on modeling of securities with similar credit quality, duration, yield, and structure that were recently transacted. Once a source is chosen, we continue to monitor any changes or modifications to their processes by reviewing their documentation on internal controls for pricing and market reviews. We review quality control measures of our sources as they become available to determine if any significant changes have occurred from period to period that might indicate issues or concerns regarding their evaluation or market coverage.

As part of our pricing procedures, we obtain quotes from more than one source to help us fully evaluate the market price of securities. However, our internal pricing policy is to use a consistent source for individual securities in order to maintain the integrity of our valuation process. Quotes obtained from the sources are not considered binding offers to transact. Under our policy, when a review of the valuation received from our selected source appears to be outside of what is considered market level activity (which is defined as trading at spreads or yields significantly different than those of comparable securities or outside the general sector level movement without a reasonable explanation), we may use an alternate source's price. To the extent we determine that it may be prudent to substitute one source's price for another, we will contact the initial source to obtain an understanding of the factors that may be contributing to the significant price variance, which often leads the source to adjust their pricing input data for future pricing.

To allow us to determine if our initial source is providing a price that is outside of a reasonable range, we review our portfolio pricing on a weekly basis. When necessary, we challenge prices from our sources when a price provided does not match our expectations based on our evaluation of market trends and activity. Initially, we perform a review of our portfolio by sector to identify securities whose prices appear outside of a reasonable range. We then perform a more detailed review of fair values for securities disclosed as Level 2. We review dealer bids and quotes for these and/or similar securities to determine the market level context for our valuations. We then evaluate inputs relevant for each class of securities disclosed in the preceding hierarchy tables.

For our structured debt securities, including commercial, residential, and asset-backed securities, we evaluate available market-related data for these and similar securities related to collateral, delinquencies, and defaults for historical trends and reasonably estimable projections, as well as historical prepayment rates and current prepayment assumptions and cash flow estimates. We further stratify each class of our structured debt securities into more finite sectors (e.g., planned amortization class, first pay, second pay, senior, subordinated, etc.) and use duration, credit quality, and coupon to determine if the fair value is appropriate.

For our corporate debt and preferred stock (redeemable and nonredeemable) portfolios, as well as the notes and debentures issued by The Progressive Corporation (see Note 4 – Debt), we review securities by duration, coupon, and credit quality, as well as changes in interest rate and credit spread movements within that stratification. The review also includes recent trades, including: volume traded at various levels that establish a market, issuer specific fundamentals, and industry specific economic news as it comes to light.

For our municipal securities (e.g., general obligations, revenue, and housing), we stratify the portfolio to evaluate securities by type, coupon, credit quality, and duration to review price changes relative to credit spread and interest rate changes. Additionally, we look to economic data as it relates to geographic location as an indication of price-to-call or maturity predictors. For municipal housing securities, we look to changes in cash flow projections, both historical and reasonably estimable projections, to understand yield changes and their effect on valuation. Lastly, for our short-term securities, we look at acquisition price relative to the coupon or yield. Since our short-term securities are typically 90 days or less to maturity, with the majority listed in Level 2 being 30 days or less to redemption, we believe that acquisition price is the best estimate of fair value.

We also review data assumptions as supplied by our sources to determine if that data is relevant to current market conditions. In addition, we independently review each sector for transaction volumes, new issuances, and changes in

spreads, as well as the overall movement of interest rates along the yield curve to determine if sufficient activity and liquidity exists to provide a credible source for our market valuations.

During each valuation period, we create internal estimations of portfolio valuation (performance returns), based on current market-related activity (i.e., interest rate and credit spread movements and other credit-related factors) within each major sector of our portfolio. We compare our internally generated portfolio results with those generated based on quotes we receive externally and research material valuation differences. We compare our results to index returns for each major sector adjusting

for duration and credit quality differences to better understand our portfolio's results. Additionally, we review on a monthly basis our external sales transactions and compare the actual final market sales prices to previous market valuation prices. This review provides us further validation that our pricing sources are providing market level prices, since we are able to explain significant price changes (i.e., greater than 2%) as known events occur in the marketplace and affect a particular security's price at sale.

This analysis provides us with additional comfort regarding the source's process, the quality of its review, and its willingness to improve its analysis based on feedback from clients. We believe this effort helps ensure that we are reporting the most representative fair values for our securities.

Except as described below, our Level 3 securities are also priced externally; however, due to several factors (e.g., nature of the securities, level of activity, and lack of similar securities trading to obtain observable market level inputs), these valuations are more subjective in nature. Certain private equity investments and fixed-income investments included in the Level 3 category are valued using external pricing supplemented by internal review and analysis.

After all the valuations are received and our review is complete, if the inputs used by vendors are determined to not contain sufficient observable market information, we will reclassify the affected security valuations to Level 3. At June 30, 2018 and 2017, and December 31, 2017, we did not have any securities in our fixed-maturity portfolio listed as Level 3.

At June 30, 2018 and December 31, 2017, we held one private nonredeemable preferred security with a value of \$5.0 million that was priced internally. The security was purchased during the third quarter 2017 and the value at both periods equals the cost at acquisition. A review of their latest available financial statements did not reveal any significant changes that would impact the security's fair value. We did not hold any internally priced securities at June 30, 2017.

We review the prices from our external sources for reasonableness using internally developed assumptions to derive prices for the securities, which are then compared to the prices we received. During 2018 or 2017, there were no material assets or liabilities measured at fair value on a nonrecurring basis. Based on our review, all prices received from external sources remained unadjusted.

We did not have any material changes in fair value associated with Level 3 assets for the three and six months ended June 30, 2018 and 2017. Due to the relative size of the Level 3 securities' fair values compared to the total portfolio's fair value, any changes in pricing methodology would not have a significant change in valuation that would materially impact net or comprehensive income.

Note 4 Debt — Debt at each of the balance sheet periods consisted of:

| (millions) | June 30, 2018 | | June 30, 2017 | | December 31, 2017 | |
|------------------------------|----------------|------------|----------------|------------|-------------------|------------|
| | Carrying Value | Fair Value | Carrying Value | Fair Value | Carrying Value | Fair Value |
| 3.75% Senior Notes due 2021 | \$498.9 | \$506.4 | \$498.6 | \$528.0 | \$498.8 | \$520.7 |
| 2.45% Senior Notes due 2027 | 496.3 | 451.3 | 496.0 | 474.2 | 496.1 | 477.9 |
| 6 5/8% Senior Notes due 2029 | 296.2 | 364.4 | 296.0 | 389.0 | 296.1 | 382.3 |
| 6.25% Senior Notes due 2032 | 395.4 | 492.5 | 395.2 | 522.7 | 395.3 | 516.9 |
| 4.35% Senior Notes due 2044 | 346.6 | 356.7 | 346.5 | 376.5 | 346.5 | 388.7 |
| 3.70% Senior Notes due 2045 | 395.3 | 363.9 | 395.2 | 389.7 | 395.2 | 402.9 |
| 4.125% Senior Notes due 2047 | 841.3 | 831.5 | 841.1 | 884.3 | 841.2 | 917.1 |
| 4.20% Senior Notes due 2048 | 589.5 | 592.3 | 0 | 0 | 0 | 0 |
| Other debt instruments | 0 | 0 | 114.8 | 114.8 | 37.1 | 37.1 |
| Total | \$3,859.5 | \$3,959.0 | \$3,383.4 | \$3,679.2 | \$3,306.3 | \$3,643.6 |

During the first quarter 2018, ARX repaid its term loans, in their entirety, in the aggregate principal amount of \$37.1 million and, during the third quarter 2017, redeemed its junior subordinated notes and senior notes, in their entirety, in the aggregate principal amount of \$65.2 million. Both the repayment and the redemptions were funded in part with proceeds from fixed-rate loans made by The Progressive Corporation. These intercompany transactions were eliminated in consolidation.

The Progressive Corporation Debt

The Progressive Corporation issued \$600 million of 4.20% Senior Notes due 2048 (the “4.20% Senior Notes”) in March 2018, and \$850 million of 4.125% Senior Notes due 2047 (the “4.125% Senior Notes”) in April 2017, in underwritten public offerings. The net proceeds from these issuances, after deducting underwriters’ discounts, commissions, and other issuance costs, were approximately \$589.5 million and \$841.1 million, respectively. In addition, upon issuance of the 4.125% Senior Notes, we closed a forecasted debt issuance hedge, which was entered into to hedge against a possible rise in interest rates, and recognized an \$8.0 million pretax unrealized loss as part of accumulated other comprehensive income (loss), which is being amortized as an adjustment to interest expense over the life of the 4.125% Senior Notes. Consistent with the other senior notes issued by Progressive, interest on the 4.20% Senior Notes and 4.125% Senior Notes is payable semiannually and both are redeemable, in whole or in part, at any time.

The Progressive Corporation Line of Credit

During the second quarter 2018, The Progressive Corporation entered into a new line of credit with PNC Bank, National Association (PNC) in the maximum principal amount of \$250 million. The prior line of credit, entered into in April 2017, had expired. The line of credit is on the same terms and conditions as the previous line of credit. Subject to the terms and conditions of the line of credit documents, advances under the line of credit (if any) will bear interest at a variable rate equal to the higher of PNC’s Prime Rate or the sum of the Federal Funds Open Rate plus 50 basis points. Each advance must be repaid on the 30th day after the advance or, if earlier, on April 30, 2019, the expiration date of the line of credit. Prepayments are permitted without penalty. The line of credit is uncommitted and, as such, all advances are subject to PNC’s discretion. We had no borrowings under either line of credit during the first six months of 2018 or throughout 2017.

Note 5 Income Taxes — Deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax bases of assets and liabilities at the enacted tax rates. We review our deferred tax assets regularly for recoverability. At June 30, 2018 and 2017, and December 31, 2017, we determined that we did not need a valuation allowance on our gross deferred tax assets. Although realization of the deferred tax assets is not assured, management believes that it is more likely than not the deferred tax assets will be realized based on our expectation that we will be able to fully utilize the deductions that are ultimately recognized for tax purposes.

For deferred taxes on items that are reported in accumulated other comprehensive income, our policy is to release the income tax effects related to these items on an aggregate portfolio approach. For this purpose, we consider our available-for-sale fixed maturity securities and hedges on forecasted transactions as separate portfolios.

For the six months ended June 30, 2018, there have been no material changes in our uncertain tax positions.

The effective tax rate for the three and six months ended June 30, 2018 were 20.3% and 20.1% respectively, compared to 32.8% and 32.9% for the same periods in 2017. The current year effective tax rate is lower primarily due to the reduction in the U.S. corporate income tax rate from 35% to 21%, effective January 1, 2018.

As of June 30, 2018, we have not fully completed our accounting for the tax effects of the enactment of the legislation commonly known as the Tax Cuts and Jobs Act of 2017 with regard to the deductibility of compensation expense for certain covered executives due to uncertainty surrounding the appropriate tax treatment of outstanding performance-based awards, and uncertainty surrounding the discount factors to be applied for loss reserve discounting. We are waiting for the Internal Revenue Service to publish additional guidance or information for both items.

Note 6 Loss and Loss Adjustment Expense Reserves — Activity in the loss and loss adjustment expense reserves is summarized as follows:

| (millions) | June 30, | |
|--|------------|------------|
| | 2018 | 2017 |
| Balance, Beginning of period | \$13,086.9 | \$11,368.0 |
| Less reinsurance recoverables on unpaid losses | 2,170.1 | 1,801.0 |
| Net balance, Beginning of period | 10,916.8 | 9,567.0 |
| Incurred related to: | | |
| Current year | 10,164.6 | 8,804.1 |
| Prior years | 81.5 | 74.2 |
| Total incurred | 10,246.1 | 8,878.3 |
| Paid related to: | | |
| Current year | 5,533.7 | 4,951.0 |
| Prior years | 3,851.5 | 3,381.8 |
| Total paid | 9,385.2 | 8,332.8 |
| Net balance, End of period | 11,777.7 | 10,112.5 |
| Plus reinsurance recoverables on unpaid losses | 2,293.1 | 1,947.9 |
| Balance, End of period | \$14,070.8 | \$12,060.4 |

We experienced unfavorable reserve development of \$81.5 million and \$74.2 million for the first six months of 2018 and 2017, respectively, which is reflected as “Incurred related to prior years” in the table above.

Year-to-date June 30, 2018

Approximately \$72 million of the unfavorable prior year reserve development was attributable to accident years 2017 and 2016.

Our personal auto business incurred about \$57 million of unfavorable loss and loss adjustment expense (LAE) reserve development, with the Agency and Direct auto businesses contributing about \$36 million and \$21 million, respectively, of unfavorable development. The unfavorable development was primarily due to an increase in reopened personal injury protection (PIP) claims.

Our Commercial Lines business experienced about \$17 million of unfavorable development primarily due to late reported losses and higher LAE than anticipated.

Our Property business recognized unfavorable development of about \$7 million, while our special lines products had minimal development during the first half of the year.

Year-to-date June 30, 2017

Approximately \$56 million of the unfavorable prior year reserve development was attributable to accident year 2016 with the balance attributable to accident year 2015.

Our commercial and personal auto businesses incurred about \$102 million of unfavorable loss and LAE reserve development for the first six months of 2017, partially offset by the favorable loss and LAE reserve development of about \$28 million in our special lines and Property businesses.

Our Agency and Direct personal auto businesses incurred about \$65 million and \$29 million, respectively, of the total unfavorable reserve development, primarily due to an increase in costs related to property damage, more late reported bodily injury claims than anticipated, and higher LAE costs.

Our Property business experienced about \$20 million in favorable development primarily due to the identification of prior year losses eligible to be ceded under our catastrophe bond reinsurance program.

Note 7 Supplemental Cash Flow Information — Cash and cash equivalents include bank demand deposits and daily overnight reverse repurchase commitments of funds held in bank demand deposit accounts on ARX’s subsidiaries, which are primarily collateralized by U.S. Treasury notes. The amount of reverse repurchase commitments held by ARX’s subsidiaries at June 30, 2018 and 2017, and December 31, 2017, were \$155.9 million, \$130.2 million, and \$247.2 million, respectively.

Restricted cash on our consolidated balance sheets represents cash that is restricted to pay flood claims under the National Flood Insurance Program’s “Write Your Own” program, for which American Strategic Insurance and other subsidiaries of ARX (ASI) are administrators.

We paid the following in the respective periods:

| | Six Months Ended June 30, | |
|--------------|------------------------------|---------|
| (millions) | 2018 | 2017 |
| Income taxes | \$358.9 | \$452.9 |
| Interest | 70.9 | 73.3 |

Income taxes paid for the six months ended June 30, 2017, was revised to correct the amount of tax payments disclosed for that period; there was no overall impact on the decrease in cash, cash equivalents, and restricted cash that was reported in our consolidated statement of cash flows for the six months ended June 30, 2017.

Note 8 Segment Information — Our Personal Lines segment writes insurance for personal autos and recreational vehicles (our special lines products). Our Commercial Lines segment writes primary liability and physical damage insurance for automobiles and trucks owned and/or operated predominantly by small businesses in the business auto, for-hire transportation, contractor, for-hire specialty, tow, and for-hire livery markets. Our Property segment writes residential property insurance for homeowners, other property owners, and renters. Our other indemnity businesses include our run-off businesses. Our service businesses provide insurance-related services, including processing Commercial Automobile Insurance Procedures/Plans (CAIP) business and serving as an agent for homeowners, general liability, and workers’ compensation insurance, among other products, through our programs with ASI and unaffiliated insurance companies. All segment revenues are generated from external customers; all intercompany transactions, including those between Progressive and ASI, are eliminated in consolidation.

Following are the operating results for the respective periods:

| (millions) | Three Months Ended June 30, | | | | Six Months Ended June 30, | | | |
|--------------------------------------|-----------------------------|-------------------------|-----------|-------------------------|---------------------------|-------------------------|------------|-------------------------|
| | 2018 | | 2017 | | 2018 | | 2017 | |
| | Revenues | Pretax Profit (Loss) | Revenues | Pretax Profit (Loss) | Revenues | Pretax Profit (Loss) | Revenues | Pretax Profit (Loss) |
| Personal Lines | | | | | | | | |
| Agency | \$3,225.7 | \$360.9 | \$2,752.5 | \$205.5 | \$6,289.5 | \$770.0 | \$5,384.0 | \$455.2 |
| Direct | 3,211.8 | 287.9 | 2,650.0 | 162.7 | 6,228.1 | 585.9 | 5,173.7 | 338.0 |
| Total Personal Lines ¹ | 6,437.5 | 648.8 | 5,402.5 | 368.2 | 12,517.6 | 1,355.9 | 10,557.7 | 793.2 |
| Commercial Lines | 884.3 | 100.3 | 671.7 | 56.2 | 1,692.9 | 195.1 | 1,317.2 | 123.6 |
| Property ² | 312.4 | (51.9) | 239.1 | 3.7 | 597.7 | (23.4) | 465.1 | 11.5 |
| Other indemnity | 0 | 0 | 0 | (0.1) | 0 | 0.2 | 0 | (0.3) |
| Total underwriting operations | 7,634.2 | 697.2 | 6,313.3 | 428.0 | 14,808.2 | 1,527.8 | 12,340.0 | 928.0 |
| Fees and other revenues ³ | 116.0 | NA | 88.8 | NA | 219.8 | NA | 174.0 | NA |
| Service businesses | 42.9 | 5.9 | 32.7 | 5.7 | 77.1 | 10.8 | 61.2 | 8.3 |
| Investments ⁴ | 224.9 | 218.7 | 170.9 | 164.3 | 343.0 | 330.8 | 352.0 | 339.8 |
| Other gains (losses) | 0 | 0 | 0 | 0 | 0 | 0 | 0.2 | 0.2 |
| Interest expense | NA | (41.7) | NA | (43.4) | NA | (78.5) | NA | (80.2) |
| Consolidated total | \$8,018.0 | \$880.1 | \$6,605.7 | \$554.6 | \$15,448.1 | \$1,790.9 | \$12,927.4 | \$1,196.1 |

NA = Not applicable

¹ Personal auto insurance accounted for 94% of the total Personal Lines segment net premiums earned during the three and six months ended June 30, 2018, and 93% for the same periods in 2017; insurance for our special lines products (e.g., motorcycles, ATVs, RVs, watercraft, and snowmobiles) accounted for the balance of the Personal Lines net premiums earned.

² For the three and six months ended June 30, 2018, pretax profit (loss) includes \$18.0 million and \$36.0 million, respectively, of amortization expense predominately associated with the acquisition of a controlling interest in ARX and \$15.5 million and \$31.0 million for the same periods in 2017. Although this expense is included in our Property segment, it is not reported in the consolidated results of ARX and, therefore, will not affect the value of net income (loss) attributable to noncontrolling interest.

³ Pretax profit (loss) for fees and other revenues is attributable to operating segments.

⁴ Revenues represent recurring investment income and total net realized gains (losses) on securities; pretax profit is net of investment expense.

Our management uses underwriting margin and combined ratio as primary measures of underwriting profitability. Underwriting profitability is calculated by subtracting losses and loss adjustment expenses, policy acquisition costs, and other underwriting expenses from the total of net premiums earned and fees and other revenues. The underwriting margin is the pretax underwriting profit (loss) expressed as a percentage of net premiums earned (i.e., revenues from underwriting operations). Combined ratio is the complement of the underwriting margin. Following are the underwriting margins/combined ratios for our underwriting operations for the respective periods:

| | Three Months Ended June 30, | | | | Six Months Ended June 30, | | | |
|-------------------------------|-----------------------------|-------------------|-------------------------|-------------------|---------------------------|-------------------|-------------------------|-------------------|
| | 2018 | | 2017 | | 2018 | | 2017 | |
| | Under-writing Margin | Combined Ratio | Under-writing Margin | Combined Ratio | Under-writing Margin | Combined Ratio | Under-writing Margin | Combined Ratio |
| Personal Lines | | | | | | | | |
| Agency | 11.2 | % 88.8 | 7.5 | % 92.5 | 12.2 | % 87.8 | 8.5 | % 91.5 |
| Direct | 9.0 | 91.0 | 6.1 | 93.9 | 9.4 | 90.6 | 6.5 | 93.5 |
| Total Personal Lines | 10.1 | 89.9 | 6.8 | 93.2 | 10.8 | 89.2 | 7.5 | 92.5 |
| Commercial Lines | 11.3 | 88.7 | 8.4 | 91.6 | 11.5 | 88.5 | 9.4 | 90.6 |
| Property ¹ | (16.6) | 116.6 | 1.5 | 98.5 | (3.9) | 103.9 | 2.5 | 97.5 |
| Total underwriting operations | 9.1 | 90.9 | 6.8 | 93.2 | 10.3 | 89.7 | 7.5 | 92.5 |

¹ Included in the three and six months ended June 30, 2018 is 5.8 points and 6.0 points, respectively, of amortization expense predominately associated with the acquisition of a controlling interest in ARX and 6.5 points and 6.7 points, respectively, for the three and six months ended June 30, 2017.

Note 9 Dividends

Annual Variable Common Share Dividends

We maintain a policy of paying an annual variable dividend on our common shares that, if declared, would be payable shortly after the close of the year. This annual variable dividend is based on a target percentage of after-tax underwriting income (using the statutory tax rate) multiplied by a performance factor (Gainshare factor), which is determined by reference to the Agency auto, Direct auto, special lines, Commercial Lines, and Property business units, with minor exclusions and adjustments, and subject to the limitations discussed below. The target percentage is determined by our Board of Directors on an annual basis and announced to shareholders and the public. In December 2017, the Board determined the target percentage for 2018 to be 33-1/3% of annual after-tax underwriting income, which is unchanged from the 2017 target percentage.

The Gainshare factor can range from zero to two and is determined by comparing our operating performance for the specified business units for the year to certain predetermined profitability and growth objectives approved by the Compensation Committee of the Board. This Gainshare factor is also used in the annual cash incentive program currently in place for our employees (our "Gainsharing program"). On a year-to-date basis, as of June 30, 2018, the Gainshare factor was 1.91. Since the final factor will be determined based on our results for the full year, the final factor may vary from the current factor.

Our annual dividend program will result in a variable payment to shareholders each year, subject to certain limitations. If the Gainshare factor is zero or if our comprehensive income is less than after-tax underwriting income, no dividend would be payable under our annual variable dividend policy. In addition, the ultimate decision on whether or not a dividend will be paid is in the discretion of the Board of Directors. The Board could decide to alter our policy, or not to pay the annual variable dividend, at any time prior to the declaration of the dividend for the year. Such an action by the Board could result from, among other reasons, changes in the insurance marketplace, changes in our performance or capital needs, changes in the U.S. federal income tax laws, disruptions of national or international capital markets, or other events affecting our business, liquidity, or financial position.

Following is a summary of our shareholder dividends that were declared in the last two years:

| (millions, except per share amounts) | Amount of Common Share Dividends |
|--------------------------------------|----------------------------------|
|--------------------------------------|----------------------------------|

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| Dividend Type | Declared | Paid | Per Share | Accrued ¹ | Paid ¹ |
|-------------------|---------------|---------------|-----------|----------------------|-------------------|
| Annual – Variable | December 2017 | February 2018 | \$ 1.1247 | \$ 655.1 | \$ 654.9 |
| Annual – Variable | December 2016 | February 2017 | 0.6808 | 395.4 | 395.4 |

¹ Variance between accrued and paid, if any, reflects the difference between the number of estimated and actual shares outstanding as of the record date.

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Preferred Share Dividends

In the first quarter 2018, we issued 500,000 Series B Fixed-to-Floating Rate Cumulative Perpetual Serial Preferred Shares, without par value (the “Series B Preferred Shares”), with a liquidation preference of \$1,000 per share (the “stated amount”). Holders of the Series B Preferred Shares will be entitled to receive cumulative cash dividends semi-annually in March and September, if and when declared by the Board of Directors. Until March 15, 2023 (the “fixed-rate period”), the annual dividend rate is fixed at 5.375% of the stated amount per share. Beginning March 15, 2023, the annual dividend rate switches to a floating rate equal to the three-month LIBOR rate plus a spread of 2.539% applied to the stated amount per share. After the fixed-rate period and up until redemption of the Series B Preferred Shares, the dividends would be payable quarterly, if and when declared by the Board of Directors. The Series B Preferred Shares are perpetual and have no stated maturity date. After the fixed-rate period, we may redeem the Series B Preferred Shares at the stated amount plus all accrued and unpaid dividends.

Note 10 Other Comprehensive Income (Loss) — The components of other comprehensive income (loss), including reclassification adjustments by income statement line item, were as follows:

| (millions) | Components of Changes in Accumulated Other Comprehensive Income (after tax) | | | | | | |
|---|---|-------------------------------|--|---|---|---|-----------------------------------|
| | Pretax total other comprehensive income | Total tax (provision) benefit | After tax total other comprehensive income | Total net unrealized gains (losses) on securities | Net unrealized gains on forecasted transactions | Foreign currency translation adjustment | (Income) loss attributable to NCI |
| Balance at March 31, 2018 | \$ (218.6) | \$ 46.0 | \$ (172.6) | \$ (160.8) | \$ (17.8) | \$ 0 | \$ 6.0 |
| Other comprehensive income (loss) before reclassifications: | | | | | | | |
| Investment securities | (90.4) | 18.8 | (71.6) | (71.6) | 0 | 0 | 0 |
| Forecasted transactions | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Foreign currency translation adjustment | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Loss attributable to noncontrolling interest (NCI) | 0.7 | (0.1) | 0.6 | 0 | 0 | 0 | 0.6 |
| Total other comprehensive income (loss) before reclassifications | (89.7) | 18.7 | (71.0) | (71.6) | 0 | 0 | 0.6 |
| Less: Reclassification adjustment for amounts realized in net income by income statement line item: | | | | | | | |
| Net impairment losses recognized in earnings | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net realized gains (losses) on securities | (27.2) | 5.7 | (21.5) | (21.5) | 0 | 0 | 0 |
| Interest expense | (0.3) | 0.1 | (0.2) | 0 | (0.2) | 0 | 0 |
| Total reclassification adjustment for amounts realized in net income | (27.5) | 5.8 | (21.7) | (21.5) | (0.2) | 0 | 0 |
| Total other comprehensive income (loss) | (62.2) | 12.9 | (49.3) | (50.1) | 0.2 | 0 | 0.6 |
| Balance at June 30, 2018 | \$ (280.8) | \$ 58.9 | \$ (221.9) | \$ (210.9) | \$ (17.6) | \$ 0 | \$ 6.6 |

| (millions) | Components of Changes in Accumulated Other Comprehensive Income (after tax) | | | | | | |
|---|---|-------------------------------|--|---|---|---|-----------------------------------|
| | Pretax total accumulated other comprehensive income | Total tax (provision) benefit | After tax total accumulated other comprehensive income | Total net unrealized gains (losses) on securities | Net unrealized gains on forecasted transactions | Foreign currency translation adjustment | (Income) loss attributable to NCI |
| Balance at December 31, 2017 | \$ 1,977.8 | \$ (695.6) | \$ 1,282.2 | \$ 1,295.0 | \$ (14.8) | \$ 0 | \$ 2.0 |
| Cumulative effect adjustment ¹ | (2,006.0) | 705.8 | (1,300.2) | (1,300.2) | 0 | 0 | 0 |
| Reclassification of disproportionate tax effect ² | 0 | (4.3) | (4.3) | (1.1) | (3.2) | 0 | 0 |
| Adjusted balance at December 31, 2017 | (28.2) | 5.9 | (22.3) | (6.3) | (18.0) | 0 | 2.0 |
| Other comprehensive income (loss) before reclassifications: | | | | | | | |
| Investment securities | (293.8) | 61.6 | (232.2) | (232.2) | 0 | 0 | 0 |
| Forecasted transactions | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Foreign currency translation adjustment | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Loss attributable to noncontrolling interest (NCI) | 5.8 | (1.2) | 4.6 | 0 | 0 | 0 | 4.6 |
| Total other comprehensive income (loss) before reclassifications | (288.0) | 60.4 | (227.6) | (232.2) | 0 | 0 | 4.6 |
| Less: Reclassification adjustment for amounts realized in net income by income statement line item: | | | | | | | |
| Net impairment losses recognized in earnings | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net realized gains (losses) on securities | (34.9) | 7.3 | (27.6) | (27.6) | 0 | 0 | 0 |
| Interest expense | (0.5) | 0.1 | (0.4) | 0 | (0.4) | 0 | 0 |
| Total reclassification adjustment for amounts realized in net income | (35.4) | 7.4 | (28.0) | (27.6) | (0.4) | 0 | 0 |
| Total other comprehensive income (loss) | (252.6) | 53.0 | (199.6) | (204.6) | 0.4 | 0 | 4.6 |
| Balance at June 30, 2018 | \$ (280.8) | \$ 58.9 | \$ (221.9) | \$ (210.9) | \$ (17.6) | \$ 0 | \$ 6.6 |

¹Reflects the fair value changes on equity securities as of December 31, 2017, which are reported as realized gains (losses) under the new accounting guidance. See Note 14 – New Accounting Standards for additional information.

²Reflects the effect of the change in the U.S. federal tax rate on our available-for-sale fixed maturity securities and our hedges on forecasted transactions as of December 31, 2017. See Note 14 – New Accounting Standards for additional information.

| (millions) | Components of Changes in Accumulated Other Comprehensive Income (after tax) | | | | | | |
|---|---|-------------------------------------|---|--|---|--|--|
| | Pretax total accumulated other comprehensive income | Total tax (provision) benefit | After tax total accumulated other comprehensive income | Total net unrealized gains (losses) on securities | Net unrealized gains on forecasted transactions | Foreign currency translation adjustment | (Income)loss attributable to NCI |
| Balance at March 31, 2017 | \$ 1,645.9 | \$ (578.4) | \$ 1,067.5 | \$ 1,072.0 | \$ (7.1) | \$ (0.8) | \$ 3.4 |
| Other comprehensive income (loss) before reclassifications: | | | | | | | |
| Investment securities | 177.2 | (62.1) | 115.1 | 115.1 | 0 | 0 | 0 |
| Forecasted transactions | (12.0) | 4.2 | (7.8) | 0 | (7.8) | 0 | 0 |
| Foreign currency translation adjustment | (0.2) | 0.1 | (0.1) | 0 | 0 | (0.1) | 0 |
| Loss attributable to noncontrolling interest (NCI) | (1.9) | 0.6 | (1.3) | 0 | 0 | 0 | (1.3) |
| Total other comprehensive income (loss) before reclassifications | 163.1 | (57.2) | 105.9 | 115.1 | (7.8) | (0.1) | (1.3) |
| Less: Reclassification adjustment for amounts realized in net income by income statement line item: | | | | | | | |
| Net impairment losses recognized in earnings | (2.6) | 0.9 | (1.7) | (1.7) | 0 | 0 | 0 |
| Net realized gains (losses) on securities | 37.2 | (13.0) | 24.2 | 24.2 | 0 | 0 | 0 |
| Interest expense | 0.3 | (0.1) | 0.2 | 0 | 0.2 | 0 | 0 |
| Total reclassification adjustment for amounts realized in net income | 34.9 | (12.2) | 22.7 | 22.5 | 0.2 | 0 | 0 |
| Total other comprehensive income (loss) | 128.2 | (45.0) | 83.2 | 92.6 | (8.0) | (0.1) | (1.3) |
| Balance at June 30, 2017 | \$ 1,774.1 | \$ (623.4) | \$ 1,150.7 | \$ 1,164.6 | \$ (15.1) | \$ (0.9) | \$ 2.1 |

| (millions) | Components of Changes in Accumulated Other Comprehensive Income (after tax) | | | | | | |
|---|---|-------------------------------|--|---|---|---|-----------------------------------|
| | Pretax total accumulated other comprehensive income | Total tax (provision) benefit | After tax total accumulated other comprehensive income | Total net unrealized gains (losses) on securities | Net unrealized gains on forecasted transactions | Foreign currency translation adjustment | (Income) loss attributable to NCI |
| Balance at December 31, 2016 | \$ 1,439.5 | \$ (506.1) | \$ 933.4 | \$ 939.6 | \$ (9.4) | \$ (1.1) | \$ 4.3 |
| Other comprehensive income (loss) before reclassifications: | | | | | | | |
| Investment securities | 431.7 | (151.3) | 280.4 | 280.4 | 0 | 0 | 0 |
| Forecasted transactions | (8.0) | 2.8 | (5.2) | 0 | (5.2) | 0 | 0 |
| Foreign currency translation adjustment | 0.3 | (0.1) | 0.2 | 0 | 0 | 0.2 | 0 |
| Loss attributable to noncontrolling interest (NCI) | (3.4) | 1.2 | (2.2) | 0 | 0 | 0 | (2.2) |
| Total other comprehensive income (loss) before reclassifications | 420.6 | (147.4) | 273.2 | 280.4 | (5.2) | 0.2 | (2.2) |
| Less: Reclassification adjustment for amounts realized in net income by income statement line item: | | | | | | | |
| Net impairment losses recognized in earnings | (3.6) | 1.3 | (2.3) | (2.3) | 0 | 0 | 0 |
| Net realized gains (losses) on securities | 88.8 | (31.1) | 57.7 | 57.7 | 0 | 0 | 0 |
| Interest expense | 0.8 | (0.3) | 0.5 | 0 | 0.5 | 0 | 0 |
| Total reclassification adjustment for amounts realized in net income | 86.0 | (30.1) | 55.9 | 55.4 | 0.5 | 0 | 0 |
| Total other comprehensive income (loss) | 334.6 | (117.3) | 217.3 | 225.0 | (5.7) | 0.2 | (2.2) |
| Balance at June 30, 2017 | \$ 1,774.1 | \$ (623.4) | \$ 1,150.7 | \$ 1,164.6 | \$ (15.1) | \$ (0.9) | \$ 2.1 |

In an effort to manage interest rate risk, we often enter into forecasted transactions on Progressive's debt issuances. We expect to reclassify \$1.0 million (pretax) into interest expense during the next 12 months, related to net unrealized losses on forecasted transactions (see Note 4 – Debt for further discussion).

Note 11 Litigation — The Progressive Corporation and/or its insurance subsidiaries are named as defendants in various lawsuits arising out of claims made under insurance policies written by our insurance subsidiaries in the ordinary course of business. We consider all legal actions relating to such claims in establishing our loss and loss adjustment expense reserves. In addition, The Progressive Corporation and/or its subsidiaries are named as defendants in a number of class action or individual lawsuits that challenge certain of the operations of the subsidiaries.

These cases include those alleging damages as a result of our subsidiaries' practices in evaluating or paying medical or injury claims or benefits, including, but not limited to, personal injury protection, medical payments, and bodily injury benefits; the utilization, content, or appearance of policy documents; labor rates paid to auto body repair shops; wage and hour issues; and cases challenging other aspects of our subsidiaries' claims, marketing, or sales practices, or other business operations. Other insurance companies face many of these same issues.

The nature and volume of litigation to which The Progressive Corporation is subject is similar to that which was disclosed in Note 12 – Litigation in our 2017 Annual Report to Shareholders.

We plan to contest the pending lawsuits vigorously, but may pursue settlement negotiations in some cases, if appropriate. The outcomes of pending cases are uncertain at this time. We establish accruals for these lawsuits when it is probable that a loss has been or will be incurred and we can reasonably estimate potential loss exposure, which may include a range of loss. As to lawsuits for which the loss is considered neither probable or estimable, or is considered probable but not estimable, we do not establish an accrual. Nevertheless, we continue to evaluate this pending litigation to determine if any losses not deemed probable and estimable become so, at which point we would establish an accrual at our best estimate of the loss or range of loss.

With respect to our pending lawsuits that are not related to claims under insurance policies, the accruals that we have established, if any, were not material at June 30, 2018 or 2017, and there were no material settlements during the first six months of 2018 or 2017. For most of these lawsuits, we do not consider any losses to be both probable and estimable, and we are unable to estimate a meaningful range of loss, if any, at this time, due to the factors discussed in Note 12 – Litigation in our 2017 Annual Report to Shareholders. In the event that any one or more of these lawsuits results in a substantial judgment against or settlement by us, or if our accruals (if any) prove to be inadequate by a significant amount, the resulting liability could have a material adverse effect on our consolidated financial condition, cash flows, and/or results of operations. For a further discussion on our pending litigation and related reserving policies, see Note 12 – Litigation in our 2017 Annual Report to Shareholders.

Note 12 Redeemable Noncontrolling Interest — In connection with the April 2015 acquisition of a controlling interest in ARX, The Progressive Corporation entered into a stockholders’ agreement with the other ARX stockholders. As part of the stockholders’ agreement, the minority ARX stockholders had the right to “put” a portion of their ARX shares to Progressive in 2018, and have the right to put all of their remaining shares to Progressive in 2021. During the second quarter 2018, the minority ARX stockholders put 204,527 shares, including 5,483 shares that were issued upon the exercise of outstanding stock options, bringing Progressive’s total ownership interest in ARX to 86.7%. Progressive acquired these additional shares, in a cash transaction, for a total cost of \$295.9 million. If ARX stockholders do not put all of their shares to Progressive in 2021, Progressive has the ability to “call” all of the outstanding shares shortly thereafter and to bring its ownership stake to 100% in 2021. See Note 15 – Redeemable Noncontrolling Interest in our 2017 Annual Report to Shareholders for a discussion of the purchase price for shares to be purchased by Progressive pursuant to these put or call rights.

Since these securities are redeemable upon the occurrence of an event that is not solely within the control of Progressive, we have recorded the redeemable noncontrolling interest (NCI) as mezzanine equity on our consolidated balance sheets, which represents the minority shares at the current estimated purchase price pursuant to the put and call provisions of the stockholders’ agreement. The estimated purchase price is based, in part, on the change in tangible net book value of ARX from December 31, 2014 to the balance sheet dates.

In addition to these minority shares, at June 30, 2018, ARX employees held options to purchase 16,067 ARX shares. These options and any shares issued upon exercise are subject to the stockholders’ agreement, including the “put” and “call” rights described above. Until the options are exercised, the underlying obligation of approximately \$23.2 million is not recorded as part of redeemable NCI. See Note 9 – Employee Benefit Plans in our 2017 Annual Report to Shareholders for a discussion of our employee stock options.

The changes in the components of redeemable NCI during the six months ended June 30, 2018 and 2017, and the year ended December 31, 2017, were:

| (millions) | June 30, 2018 | June 30, 2017 | December 31, 2017 |
|---|---------------------|---------------------|----------------------|
| Balance, Beginning of period | \$503.7 | \$483.7 | \$ 483.7 |
| Net income attributable to NCI | 8.8 | 11.1 | 5.9 |
| Other comprehensive income (loss) attributable to NCI | (4.6) | 2.2 | 2.3 |
| Exercise of employee stock options | 9.4 | 3.4 | 3.4 |
| Purchase of ARX shares | (295.9) | 0 | 0 |
| Change in redemption value of NCI | (3.2) | 1.4 | 8.4 |
| Balance, End of period | \$218.2 | \$501.8 | \$ 503.7 |

Note 13 Goodwill and Intangible Assets

Goodwill

During the six months ended June 30, 2018, there were no changes to the carrying amount of goodwill. Goodwill recorded at June 30, 2018 and 2017, and December 31, 2017 was \$452.7 million. No accumulated goodwill impairment losses exist.

Intangible Assets

The following table is a summary of the net carrying amount of other intangible assets as of June 30, 2018 and 2017, and December 31, 2017:

| (millions) | June 30, 2018 | June 30, 2017 | December 31, 2017 |
|---|---------------------|---------------------|-------------------------|
| Intangible assets subject to amortization | \$318.2 | \$389.4 | \$ 354.2 |
| Indefinite-lived intangible assets ¹ | 12.4 | 12.4 | 12.4 |
| Total | \$330.6 | \$401.8 | \$ 366.6 |

¹ Indefinite-lived intangible assets are comprised of state insurance and agent licenses. State insurance licenses were previously subject to amortization under superseded accounting guidance and have \$0.6 million of accumulated amortization for all periods presented.

Intangible assets subject to amortization consisted of the following:

| (millions) | June 30, 2018 | | | June 30, 2017 | | | December 31, 2017 | | |
|----------------------|-----------------------------|-----------------------------|---------------------------|-----------------------------|-----------------------------|---------------------------|-----------------------------|-----------------------------|---------------------------|
| Category | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
| Policies in force | \$256.2 | \$ 119.0 | \$ 137.2 | \$256.2 | \$ 82.4 | \$ 173.8 | \$256.2 | \$ 100.7 | \$ 155.5 |
| Agency relationships | 159.2 | 37.0 | 122.2 | 159.2 | 25.6 | 133.6 | 159.2 | 31.3 | 127.9 |
| Software rights | 79.1 | 34.7 | 44.4 | 79.1 | 24.1 | 55.0 | 79.1 | 29.4 | 49.7 |
| Trade name | 34.8 | 20.4 | 14.4 | 34.8 | 7.8 | 27.0 | 34.8 | 13.7 | 21.1 |
| Total | \$529.3 | \$ 211.1 | \$ 318.2 | \$529.3 | \$ 139.9 | \$ 389.4 | \$529.3 | \$ 175.1 | \$ 354.2 |

Amortization expense was \$18.0 million and \$36.0 million for the three and six months ended June 30, 2018, respectively, compared to \$15.5 million and \$31.0 million during the same periods last year.

During the third quarter 2017, we revised our estimate of the economic useful life of our trade name intangible asset from an original life of 10 years to a remaining life of 2 years. The decrease in the useful life represents the estimated length of time that it is expected to take to transition the branding of our Property products from the ASI trade name to the Progressive brand. As of June 30, 2018, the remaining average life of all of our intangible assets is 4.4 years.

Note 14 New Accounting Standards

Issued

In January 2018, the Financial Accounting Standards Board (FASB) proposed an Accounting Standards Update (ASU), which would provide targeted improvements to the new lease accounting guidance issued by the FASB in February 2016 (the "2016 ASU"). The 2016 ASU, which eliminates the off-balance-sheet accounting for leases, will require lessees to report their operating leases as both an asset and liability on the statement of financial position and to disclose key information about leasing arrangements in the financial statement footnotes. Under the 2016 ASU, there will be no change to the recognition of lease expense in our results of operations. The 2016 ASU will be effective for fiscal years (including interim periods within those fiscal years) beginning after December 15, 2018 (2019 for calendar-year companies). Under the proposed guidance, companies would have the option to apply the new lease requirements either as of the effective date (i.e., January 1, 2019), with comparative information presented in accordance with the previous standard, or on a modified retrospective basis, which would restate all financial statement information as of the beginning of the earliest period presented and is the transition method under the 2016 ASU. Based on our lease portfolio at June 30, 2018, and in accordance with the accounting elections available in the 2016 ASU, we would have recorded an increase to assets and liabilities of approximately \$140 million, and there

would have been no impact on our results of operations or cash flows. Therefore, we do not expect this standard to have a material impact on our financial condition.

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In March 2017, the FASB issued an ASU related to premium amortization on purchased callable debt securities. The intent of the standard is to shorten the amortization period for certain purchased callable debt securities held at a premium. Under the ASU, the premium is required to be amortized to the earliest call date. The ASU more closely aligns interest income recorded on bonds held at a premium with the economics of the underlying instrument. The ASU, which is required to be applied on a modified retrospective basis, is effective for fiscal years beginning after December 15, 2018 (2019 for calendar-year companies), and interim periods within those fiscal years. Since we have historically used a yield-to-worst scenario for our securities that were purchased at a premium, and the first call on a premium security most often produces the lowest and most conservative yield, we do not expect this standard to have a significant impact on our financial condition, cash flows, or results of operations.

In January 2017, the FASB issued an ASU, which eliminates the requirement to determine the implied fair value of goodwill in measuring an impairment loss. Upon adoption, the measurement of a goodwill impairment will represent the excess of the reporting unit's carrying value over fair value, limited to the carrying value of goodwill. This ASU is effective for goodwill impairment tests in fiscal years beginning after December 15, 2019 (2020 for calendar-year companies), with early adoption permitted. We do not expect this standard to have a material impact on our financial position or results of operations.

In June 2016, the FASB issued an ASU intended to improve the timing, and enhance the accounting and disclosure, of credit losses on financial assets. Additionally, this update will modify the existing accounting guidance related to the impairment evaluation for available-for-sale debt securities and will result in the creation of an allowance for credit losses as a contra asset account. The ASU will require cumulative-effect changes to retained earnings in the period of adoption, if any occur, and will also require prospective changes on previously recorded impairments. This ASU is effective for fiscal years (including interim periods within those fiscal years) beginning after December 15, 2019 (2020 for calendar-year companies), with early adoption permissible (including interim periods within that fiscal year) beginning after December 15, 2018 (2019 for calendar-year companies). While the ASU creates additional accounting complexities related to the recognition of the impairment losses, and subsequent recoveries, through an allowance for credit losses account, we do not expect the ASU to have a material impact on our current method of evaluating securities for credit losses or the timing or recognition of the amounts of the impairment losses.

Adopted

On January 1, 2018, we adopted the ASU intended to improve the recognition and measurement of financial instruments. Under this update, the changes in fair value of equity securities are recognized as a component of net income. Upon adoption, we recorded a cumulative-effect adjustment of \$1.3 billion, which is net of taxes. The cumulative-effect adjustment represents the amount of after-tax net unrealized gains on equity securities that was recorded as part of accumulated other comprehensive income at December 31, 2017. The adoption of this ASU had no impact on comprehensive income. Consistent with our historical presentation, cash flows on equity securities will be reflected as investing activities in the Consolidated Statements of Cash Flows.

In the first quarter 2018, we adopted the ASU related to the reclassification of certain tax effects from accumulated other comprehensive income. This update provided companies with the option to reclassify disproportionate tax effects in accumulated other comprehensive income caused by the legislation commonly known as the Tax Cuts and Jobs Act of 2017 to retained earnings. We opted to make the reclassification, which resulted in a decrease to accumulated other comprehensive income and an offsetting increase to retained earnings of \$4.3 million. This reclass was solely due to the effect of the change in the U.S. federal tax rate on our available-for-sale fixed-maturity securities and our hedges on forecasted transactions. There were no disproportionate tax effects related to our equity securities subsequent to adopting the ASU related to classification and measurement discussed above.

Note 15 Reclassification — For the three and six months ended June 30, 2017, we reclassified the change in the net holding period gains (losses) on hybrid securities held at June 30, 2017 to “net holding period gains (losses) on securities” out of “net realized gains (losses) on security sales” to conform with the current-year Consolidated Statements of Comprehensive Income presentation. There was no overall impact on total net realized gains (losses) on securities. We also reclassified the classification and presentation of restricted cash in our Consolidated Statements of Cash

Flows in accordance with the accounting guidance we adopted for the year ended December 31, 2017 relating to this item; there was no overall impact on the increase in cash, cash equivalents, and restricted cash as a result of this reclassification. In addition, on our Consolidated Balance Sheets for December 31, 2017, we reclassified our “dividends payable” into “accounts payable, accrued expenses, and other liabilities” to be consistent with the current period presentation.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

I. OVERVIEW

The Progressive Corporation's insurance subsidiaries recognized strong growth in both premiums and policies in force in the second quarter 2018, compared to the same period last year. During the quarter, we generated \$8.1 billion of net premiums written, which is an increase of \$1.3 billion, or 20%, compared to the second quarter 2017. In addition, on a quarter-over-prior-year quarter basis, companywide net premiums earned increased 21% and policies in force grew 13%. We ended the quarter with 19.6 million total policies in force. For the second quarter 2018, we produced an underwriting margin of 9.1%, 2.3 points better than the second quarter last year, and a 63% increase in our pretax underwriting profitability. The increase in profitability for the second quarter 2018, on a year-over-year basis, in part reflects our increase in average written premium per policy along with decreases in our auto claims frequency and fewer catastrophe losses in 2018.

On a year-over-year basis, net income attributable to Progressive increased 92% for the second quarter and 80% for the first six months, primarily due to growth in our underwriting profitability and the lower effective tax rate in 2018, which reflects the change in the statutory tax rate to 21% from 35%. Comprehensive income attributable to Progressive increased 45% for the quarter and 21% year-to-date on a year-over-year basis. Comprehensive income includes a decrease in the value of our investment portfolio during 2018, compared to an increase in the portfolio valuation during the same periods last year. Due to a change in accounting guidance, as of January 1, 2018, the change in value of our equity securities is reported as a component of net income, instead of being a component of "other comprehensive income," while the change in value of fixed-maturity securities remains part of "other comprehensive income." This accounting change may cause more volatility in net income based on equity market conditions.

Therefore, comprehensive income may be a more beneficial measure of our overall performance.

During the second quarter 2018, our total capital (debt plus shareholders' equity) increased \$0.7 billion, to \$14.9 billion, primarily reflecting income during the quarter.

A. Insurance Operations

Our Personal and Commercial Lines operating segments were profitable during the second quarter 2018, while our Property business generated an underwriting loss, primarily due to catastrophe losses incurred during the quarter. All three segments contributed to our solid premium and policy in force growth during the second quarter on a year-over-year basis.

Our Personal Lines underwriting profit margin was 10.1% and Commercial Lines was 11.3%, while Property had an underwriting loss margin of 16.6%, which included 26.1 points of catastrophe losses, net of reinsurance, as well as 5.8 points of amortization expense, predominately related to our acquisition of a controlling interest of ARX Holding Corp. (ARX) in 2015. Our special lines products were also profitable in the second quarter, but their results had a minimal impact on our total Personal Lines combined ratio.

On a year-over-year basis, our catastrophe losses for the quarter were down 1.0 point. About 70% of the catastrophe losses in the second quarter 2018, both on the vehicle and Property businesses, were due to storms in Texas and Colorado. For the quarter, our companywide prior accident years development had a 0.3 point unfavorable impact, compared to a 0.6 point favorable impact in the second quarter 2017. Our overall incurred personal auto frequency was down around 2.6%, while severity was up about 2.3%. While we priced for the increase in severity, we were not anticipating the continued decrease in frequency, which contributed to the underwriting profitability in the quarter. During the second quarter 2018, we renewed our catastrophe reinsurance coverage, which is in addition to our aggregate stop-loss agreement that was renewed at the beginning of the year and our multi-year reinsurance coverage still in effect. Under our catastrophe reinsurance, we increased our retention level to \$60 million, from the \$50 million retention we had in place last year. The increase reflects our decision to retain more of the catastrophe losses given our premium and regulatory capital growth during the year.

During the quarter, total new personal auto applications (i.e., issued policies) increased 27% on a year-over-year basis, including a 21% and 32% increase in our Agency auto and Direct auto businesses, respectively. The significant increase in Direct auto applications reflects, in part, lower growth during the second quarter 2017. On a year-over-year basis, the personal auto businesses benefited from increased advertising spend, as well as competitive product

offerings and position in the marketplace. We will continue to spend on marketing when we believe that it is an efficient use of our dollars. We continued to generate strong new business application growth in our bundled auto and home customers (i.e., Robinsons) in both the Agency and Direct channels. New applications for our special lines products were up 2% during the second quarter 2018, compared to the same period last year.

For the Commercial Lines business, new applications increased 9% on a year-over-year basis during the second quarter 2018. Most of the underwriting restrictions that were implemented in the first quarter of 2018 were lifted during the second quarter 2018. We will continue to monitor our rate levels with a view toward continuing to grow profitably while providing high-quality customer service.

The Property business had an 81% increase in new applications for the second quarter 2018, compared to the same period last year and growth is strong in both the agency and direct channels. Our home/condo products grew nearly 60%, while the balance was due to an increase in our renters, umbrella, and manufactured home products. We have increased our state footprint since the second quarter last year for both the homeowners and renters products. In addition, our product offerings were more competitive during the second quarter and we saw growth through HomeQuote Explorer® (HQX), our online quoting platform for home insurance. Where available, we incorporated HQX into our online bundled auto and home quoting experience. We have also added the ability to buy select products online through HQX to meet our customers needs. The “buy button” is currently only in one state but we plan to roll out to other states over time.

During the quarter, on a year-over-year basis, our written premium per policy for our personal auto businesses increased about 5%, primarily reflecting a shift in the mix of business toward higher premium coverages and the rate increases taken during the last 12 months. Written premium per policy increased 4% for our special lines products and increased 12% for our Commercial Lines business. The Commercial Lines increase reflects rate actions throughout 2017, as well as shifts in our mix of businesses to higher premium products. The total written premium per policy for the Property business decreased 5%, reflecting the renters business, which has lower premiums per policy, comprising a greater proportion of the total Property business. For our core Property business (e.g., home and condo insurance), the written premium per policy increased slightly. We continue to manage rate levels in our Property business to help meet our profitability targets in this segment.

We ended the second quarter 2018 with 12.8 million personal auto policies in force, with Agent auto and Direct auto growing 14% and 17%, respectively, over the the same period last year. Our special lines products policies in force grew 1% over the second quarter last year, Commercial Lines grew 9%, and Property grew 35%. On a year-over-year basis, total Personal Lines increased policies in force by about 1.7 million policies, Commercial Lines increased policies by just over 53,000, and Property increased policies by 455,500.

To grow policies in force, it is critical that we retain our customers for longer periods. Consequently, increasing retention is one of our most important priorities, and our efforts to increase our share of multi-product households continue to be a key initiative to support that goal. Policy life expectancy, which is our actuarial estimate of the average length of time that a policy will remain in force before cancellation or lapse in coverage, is our primary measure of customer retention in our vehicle businesses. Policy life expectancy has increased in Personal Lines, with our trailing 12-month total auto policy life expectancy up 10% over the second quarter last year and special lines was flat. Our Agency auto and Direct auto policy life expectancy were up 11% and 9%, respectively. These increases reflect the competitive markets as well as our Destination Era initiatives, where we have experienced an increase in customers who bundle their auto coverage with other products, which tends to translate to longer relationships with these customers. For Commercial Lines, our policy life expectancy increased 2% year over year.

B. Investments

The fair value of our investment portfolio was \$30.9 billion at June 30, 2018. Our asset allocation strategy is to maintain 0%-25% of our portfolio in Group I securities, with the balance (75%-100%) of our portfolio in Group II securities (the securities allocated to Group I and II are defined below under Results of Operations – Investments). At June 30, 2018, 16% of our portfolio was allocated to Group I securities and 84% to Group II securities, compared to 17% and 83%, respectively, at December 31, 2017.

Our recurring investment income generated a pretax book yield of 2.7% for the second quarter 2018, compared to 2.3% for the same period in 2017. Our investment portfolio produced a fully taxable equivalent (FTE) total return of 0.6% for the second quarter 2018, compared to 1.3% for the same period in 2017. Our fixed-income and common stock portfolios had FTE total returns of 0.3% and 3.1%, respectively, for the second quarter 2018, compared to 1.1% and 3.5%, respectively, last year.

At June 30, 2018, the fixed-income portfolio had a weighted average credit quality of AA- and a duration of 2.6 years, compared to AA- and 2.5 years, respectively, at December 31, 2017. We lengthened our portfolio duration modestly during the first half of the year in response to higher interest rates as the risk/reward to our portfolio's value at higher rate levels moved toward a more balanced position. However, our duration remains below the mid-point of our range as a means to limit any decline in portfolio value from an increase in rates from current low levels.

II. FINANCIAL CONDITION

A. Liquidity and Capital Resources

Progressive's insurance operations create liquidity by collecting and investing premiums from new and renewal business in advance of paying claims. Operations generated positive cash flows of about \$3.5 billion and \$2.0 billion for the first six months of 2018 and 2017, respectively. The year-over-year increase primarily reflects the increase in premiums collected in excess of paid losses due to strong growth during the period.

Our unsecured discretionary line of credit (the "Line of Credit") with PNC Bank, National Association (PNC) in the maximum principal amount of \$250 million was renewed during April 2018, on the same terms and conditions, and will expire on April 30, 2019. We did not engage in any short-term borrowings, including under our discretionary Line of Credit, to fund our operations or for liquidity purposes during the reported periods.

During the second quarter, in accordance with our stockholders' agreement related to the ARX acquisition, The Progressive Corporation increased its share ownership of ARX to 86.7% when the minority ARX stockholders put 204,527 shares to Progressive, at a total cost of \$295.9 million. The Progressive Corporation has the ability to achieve 100% ownership of ARX by the end of the second quarter of 2021. See Note 12 – Redeemable Noncontrolling Interest for further discussion.

Our total capital (debt plus shareholders' equity) was \$14.9 billion, at book value, at June 30, 2018, compared to \$12.4 billion at June 30, 2017 and \$12.6 billion at December 31, 2017. The increase since year end reflects the increase in comprehensive income during that period as well as the issuance of \$600 million of 4.20% Senior Notes due 2048 and \$500 million of Series B Fixed-to-Floating Rate Cumulative Perpetual Serial Preferred Shares (the "Series B Preferred Shares"), in underwritten public offerings, during the first quarter 2018.

Our repurchases of common stock were not material during the second quarter of 2018, and we repurchased 702,255 shares at a total cost of \$39.4 million on a year-to-date basis. No dividends were declared during the six months ended June 30, 2018. During the first quarter, we paid \$654.9 million of common share dividends, which were declared in December 2017. Also, during the first quarter 2018, ARX repaid in full its term loans in the aggregate principal amount of \$37.1 million. At June 30, 2018, ARX has no external borrowings outstanding.

Our debt-to-total capital ratio remained below 30% during all reported periods, consistent with our financial policy. This ratio, which reflects debt as a percent of debt plus shareholders' equity and excludes redeemable noncontrolling interest, was 26.0% at June 30, 2018, 27.3% at June 30, 2017, and 26.3% at December 31, 2017.

We seek to deploy capital in a prudent manner and use multiple data sources and modeling tools to estimate the frequency, severity, and correlation of identified exposures, including, but not limited to, catastrophic and other insured losses, natural disasters, and other significant business interruptions, to estimate our potential capital needs. During the first six months of 2018 and at all times during 2017, our total capital exceeded the sum of our regulatory capital layer plus our self-constructed extreme contingency layer, as described in our Annual Report to Shareholders for the year ended December 31, 2017.

Based upon our capital planning and forecasting efforts, we believe that we have sufficient capital resources and cash flows from operations to support our current business, scheduled principal and interest payments on our debt, dividends on our Series B Preferred Shares, our contractual obligations, and other expected capital requirements for the foreseeable future. Nevertheless, depending on our levels of premium growth and regulatory capital needs, underwriting profitability, including hurricane activity and other catastrophic storms and events, investment returns, and capital outlays through dividends, among other factors, we may need to raise additional capital in the next 12 months to satisfy our capital needs. It is possible that a capital-raising transaction involving debt securities could cause our debt-to-total capital ratio to exceed our published financial policy for a period of time.

B. Commitments and Contingencies

Contractual Obligations

During the first six months of 2018, our contractual obligations have not changed materially from those discussed in our Annual Report on Form 10-K for the year ended December 31, 2017, other than the debt and preferred share issuance transactions described above.

Off-Balance-Sheet Arrangements

Our off-balance-sheet leverage includes operating leases and purchase obligations. There have been no material changes in the off-balance-sheet items since the discussion in the notes to the financial statements in Progressive's Annual Report on Form 10-K for the year ended December 31, 2017.

III. RESULTS OF OPERATIONS – UNDERWRITING

A. Segment Overview

We report our underwriting operations in three segments: Personal Lines, Commercial Lines, and Property. As a component of our Personal Lines segment, we report our Agency and Direct business results to provide further understanding of our products by distribution channel. Our other indemnity businesses include our run-off businesses. The following table shows the composition of our companywide net premiums written, by segment, for the respective periods:

| | Three Months Ended June 30, 2018 | | Six Months Ended June 30, 2017 | |
|-----------------------------------|--|------|---|------|
| Personal Lines | | | | |
| Agency | 42 % | 43 % | 42 % | 43 % |
| Direct | 40 | 40 | 42 | 42 |
| Total Personal Lines ¹ | 82 | 83 | 84 | 85 |
| Commercial Lines | 13 | 13 | 12 | 11 |
| Property | 5 | 4 | 4 | 4 |
| Total underwriting operations | 100% | 100% | 100% | 100% |

¹ Personal auto insurance accounted for 91% and 93% of the total Personal Lines segment net premiums written during the three and six months ended June 30, 2018, respectively, and 89% and 92% for the same periods in 2017; insurance for our special lines products accounted for the balance.

Our Personal Lines business writes insurance for personal autos and special lines products (e.g., motorcycles, watercraft, and RVs). We currently write our Personal Lines products in all 50 states. We also offer our personal auto product (not special lines products) in the District of Columbia. Our personal auto policies are primarily written for 6-month terms, while the special lines products are written for 12-month terms.

Our Commercial Lines business writes primary liability, physical damage, and other auto-related insurance for automobiles and trucks owned and/or operated predominantly by small businesses. While the majority of our Commercial Lines business is written through the independent agency channel, the amount of business written through the direct channel continues to grow and represented about 12% of premiums written for the first six months of 2018. We write Commercial Lines business in all 50 states and the majority of our policies are written for 12-month terms.

Our Property business writes residential property insurance (single family homes, condominium unit owners, rental coverage, etc.) for homeowners, other property owners, and renters. Our Property business primarily consists of the operations of the ARX organization. ARX wholly owns or controls the insurance companies that we refer to in the aggregate as "ASI." We write the majority of our Property business through the independent agency channel; however, we continue to expand the distribution of our Property product offerings in the direct channel. Property policies are written for a 12-month term. ASI writes residential property in 43 states and the District of Columbia, with Vermont being the latest state where we began writing business. ASI also writes flood insurance in 44 states and the District of Columbia, and ASI and Progressive write renters insurance in 44 states and the District of Columbia. Florida and

Texas remain the largest states for the Property business comprising just over 40% of the year-to-date premium volume. We continue to transition ASI products from the ASI trade name to the Progressive brand. We expect to complete the transition in both our agency and direct channels over the next year.

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B. Profitability

Profitability for our underwriting operations is defined by pretax underwriting profit, which is calculated as net premiums earned plus fees and other revenues less losses and loss adjustment expenses, policy acquisition costs, and other underwriting expenses. We also use underwriting margin, which is underwriting profit or loss expressed as a percentage of net premiums earned, to analyze our results. For the respective periods, our underwriting profitability results were as follows:

| | Three Months Ended June 30, | | | Six Months Ended June 30, | | | | |
|-------------------------------|-----------------------------|---------|---------------|---------------------------|---------------|--------|---------------|--------|
| | 2018 | | 2017 | | 2018 | | 2017 | |
| | Underwriting | | Underwriting | | Underwriting | | Underwriting | |
| | Profit (Loss) | | Profit (Loss) | | Profit (Loss) | | Profit (Loss) | |
| (\$ in millions) | \$ | Margin | \$ | Margin | \$ | Margin | \$ | Margin |
| Personal Lines | | | | | | | | |
| Agency | \$360.9 | 11.2 % | \$205.5 | 7.5 % | \$770.0 | 12.2 % | \$455.2 | 8.5 % |
| Direct | 287.9 | 9.0 | 162.7 | 6.1 | 585.9 | 9.4 | 338.0 | 6.5 |
| Total Personal Lines | 648.8 | 10.1 | 368.2 | 6.8 | 1,355.9 | 10.8 | 793.2 | 7.5 |
| Commercial Lines | 100.3 | 11.3 | 56.2 | 8.4 | 195.1 | 11.5 | 123.6 | 9.4 |
| Property ¹ | (51.9) | (16.6) | 3.7 | 1.5 | (23.4) | (3.9) | 11.5 | 2.5 |
| Other indemnity ² | 0 | NM | (0.1) | NM | 0.2 | NM | (0.3) | NM |
| Total underwriting operations | \$697.2 | 9.1 % | \$428.0 | 6.8 % | \$1,527.8 | 10.3 % | \$928.0 | 7.5 % |

¹ For the three and six months ended June 30, 2018, amounts include \$18.0 million and \$36.0 million, respectively, of amortization expense predominately associated with the acquisition of a controlling interest in ARX, and \$15.5 million and \$31.0 million for the respective periods last year. The increase in amortization expense reflects a change in the economic useful life of the trade name intangible asset; see Note 13 – Goodwill and Intangible Assets for further discussion.

² Underwriting margins for our other indemnity businesses are not meaningful (NM) due to the lack of premiums earned by, and the variability of loss costs in, such businesses.

Our underwriting profit margin increased in both the second quarter and first six months of 2018, compared to the same periods last year. The increase was driven by higher written premium per policy on both our personal and commercial auto products, lower than anticipated frequency, and lower catastrophe losses, as compared to last year.

Further underwriting results for our Personal Lines business, including results by distribution channel, the Commercial Lines business, the Property business, and our underwriting operations in total, were as follows:

| | Three Months Ended | | | Six Months Ended | | |
|---|--------------------|------|--------|------------------|------|--------|
| | June 30, | | | June 30, | | |
| | 2018 | 2017 | Change | 2018 | 2017 | Change |
| Underwriting Performance ¹ | | | | | | |
| Personal Lines—Agency | | | | | | |
| Loss & loss adjustment expense ratio | 69.4 | 73.0 | (3.6) | pts. 68.6 | 71.9 | (3.3) |
| Underwriting expense ratio | 19.4 | 19.5 | (0.1) | pts. 19.2 | 19.6 | (0.4) |
| Combined ratio | 88.8 | 92.5 | (3.7) | pts. 87.8 | 91.5 | (3.7) |
| Personal Lines—Direct | | | | | | |
| Loss & loss adjustment expense ratio | 70.9 | 75.0 | (4.1) | pts. 70.3 | 73.8 | (3.5) |
| Underwriting expense ratio | 20.1 | 18.9 | 1.2 | pts. 20.3 | 19.7 | 0.6 |
| Combined ratio | 91.0 | 93.9 | (2.9) | pts. 90.6 | 93.5 | (2.9) |
| Total Personal Lines | | | | | | |
| Loss & loss adjustment expense ratio | 70.2 | 74.0 | (3.8) | pts. 69.4 | 72.8 | (3.4) |
| Underwriting expense ratio | 19.7 | 19.2 | 0.5 | pts. 19.8 | 19.7 | 0.1 |
| Combined ratio | 89.9 | 93.2 | (3.3) | pts. 89.2 | 92.5 | (3.3) |
| Commercial Lines | | | | | | |
| Loss & loss adjustment expense ratio | 68.7 | 69.4 | (0.7) | pts. 68.0 | 68.5 | (0.5) |
| Underwriting expense ratio | 20.0 | 22.2 | (2.2) | pts. 20.5 | 22.1 | (1.6) |
| Combined ratio | 88.7 | 91.6 | (2.9) | pts. 88.5 | 90.6 | (2.1) |
| Property | | | | | | |
| Loss & loss adjustment expense ratio | 79.9 | 63.6 | 16.3 | pts. 68.0 | 61.5 | 6.5 |
| Underwriting expense ratio ² | 36.7 | 34.9 | 1.8 | pts. 35.9 | 36.0 | (0.1) |
| Combined ratio ² | 116.6 | 98.5 | 18.1 | pts. 103.9 | 97.5 | 6.4 |
| Total Underwriting Operations ³ | | | | | | |
| Loss & loss adjustment expense ratio | 70.4 | 73.1 | (2.7) | pts. 69.2 | 72.0 | (2.8) |
| Underwriting expense ratio | 20.5 | 20.1 | 0.4 | pts. 20.5 | 20.5 | 0 |
| Combined ratio | 90.9 | 93.2 | (2.3) | pts. 89.7 | 92.5 | (2.8) |
| Accident year loss & loss adjustment expense ratio ⁴ | 70.1 | 73.7 | (3.6) | pts. 68.6 | 71.4 | (2.8) |

¹ Ratios are expressed as a percentage of net premiums earned; fees and other revenues are netted with underwriting expenses in the ratio calculations.

² Included in the three and six months ended June 30, 2018 are 5.8 points and 6.0 points, respectively, of amortization expense predominately associated with our acquisition of a controlling interest in ARX, and 6.5 points and 6.7 points for the respective periods last year. Excluding these additional expenses, for the three months ended June 30, 2018 and 2017, the Property business would have reported expense ratios of 30.9 and 28.4, respectively, and combined ratios of 110.8 and 92.0. For the six months ended June 30, 2018 and 2017, excluding these additional expenses, the Property business would have reported expense ratios of 29.9 and 29.3, respectively, and combined ratios of 97.9 and 90.8.

³ Combined ratios for the other indemnity businesses are not presented separately due to the low level of premiums earned by, and the variability of loss costs in, such businesses.

⁴ The accident year ratios include only the losses that occurred during the period noted. As a result, accident period results will change over time, either favorably or unfavorably, as we revise our estimates of loss costs when payments are made or reserves for that accident period are reviewed.

Losses and Loss Adjustment Expenses (LAE)

| (millions) | Three Months Ended June 30, | | Six Months Ended June 30, | |
|-------------------------------------|-----------------------------|-----------|---------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Change in net loss and LAE reserves | \$585.7 | \$334.0 | \$860.9 | \$545.5 |
| Paid losses and LAE | 4,789.6 | 4,280.9 | 9,385.2 | 8,332.8 |
| Total incurred losses and LAE | \$5,375.3 | \$4,614.9 | \$10,246.1 | \$8,878.3 |

Claims costs, our most significant expense, represent payments made, and estimated future payments to be made, to or on behalf of our policyholders, including expenses needed to adjust or settle claims. Claims costs are a function of loss severity and frequency and, for our vehicle businesses, are influenced by inflation and driving patterns, among other factors, some of which are discussed below. In our Property business, severity is primarily a function of construction costs and the age of the structure. Accordingly, anticipated changes in these factors are taken into account when we establish premium rates and loss reserves. Loss reserves are estimates of future costs and our reserves are adjusted as underlying assumptions change and information develops.

Our total loss and LAE ratio decreased 2.7 points for the second quarter 2018, compared to the second quarter 2017, and 2.8 points on a year-to-date basis, due to higher average premiums, lower auto frequency, and diligent expense management. In addition, our catastrophe losses, as a percentage of earned premiums, were lower for both the second quarter and first six months of 2018, compared to the same periods last year.

The following table shows our consolidated catastrophe losses, excluding loss adjustment expenses, incurred during the periods:

| (\$ in millions) | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|----------|---------------------------|----------|
| | 2018 | 2017 | 2018 | 2017 |
| Vehicle businesses | \$124.9 | \$162.0 | \$150.4 | \$223.4 |
| Property business, net of reinsurance (excluding ASL) | 122.8 | 132.2 | 147.4 | 225.1 |
| Reinsurance recoverable on ASL ¹ | (41.2) | (58.6) | (42.0) | (101.9) |
| Property business, net | 81.6 | 73.6 | 105.4 | 123.2 |
| Total net catastrophe losses incurred | \$206.5 | \$235.6 | \$255.8 | \$346.6 |
| Increase to combined ratio | 2.7 pts. | 3.7 pts. | 1.7 pts. | 2.8 pts. |

¹ Represents the reinsurance recoverable recorded on the losses under our aggregate stop-loss agreements (ASL); see table below for further information.

In the second quarter 2018, approximately 70% of the catastrophe losses were due to wind and hail storms and flooding in Texas and Colorado. We have responded, and will continue to respond, promptly to catastrophic events when they occur in order to provide exemplary claims service to our customers.

We do not have catastrophe-specific reinsurance for our vehicle businesses. We reinsure most of our Property business against various risks, including, but not limited to, catastrophic losses through excess of loss reinsurance and an aggregate stop-loss agreement.

The table above reports the reinsurance recoverables under our aggregate stop-loss agreements related to 2018 losses and development on 2017 losses. The aggregate stop-loss agreement for 2018 covers all accident year losses and allocated loss adjustment expenses (ALAE) that occur during 2018, except those from named storms and liability claims, and provides \$200 million of coverage if ASI's applicable loss and ALAE ratio for the full accident year were to exceed 63%. The aggregate stop-loss agreement for 2017 had substantially the same terms as the 2018 agreement. The following table shows the total reinsurance recoverables under the aggregate stop-loss agreement by accident year:

| (\$ in millions) | Three Months Ended June 30, | | Six Months Ended June 30, | |
|------------------------------------|-----------------------------|--------|---------------------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| Reinsurance recoverables on losses | | | | |
| 2018 | \$37.7 | \$— | \$37.7 | \$— |
| 2017 | 3.5 | 58.6 | 4.3 | 101.9 |
| Total | 41.2 | 58.6 | 42.0 | 101.9 |
| Reinsurance recoverables on ALAE | | | | |
| 2018 | 4.1 | — | 4.1 | — |
| 2017 | 0.5 | 6.2 | 0.5 | 11.0 |
| Total | 4.6 | 6.2 | 4.6 | 11.0 |
| Total reinsurance recoverables | | | | |
| 2018 | 41.8 | — | 41.8 | — |
| 2017 | 4.0 | 64.8 | 4.8 | 112.9 |
| Total | \$45.8 | \$64.8 | \$46.6 | \$112.9 |

During the second quarter 2018, we renewed about 40% of our catastrophe reinsurance coverage under similar terms as the prior coverage; the remainder is covered by multi-year contracts that are still in effect. Upon renewal, however, we increased our retention threshold for losses and LAE from a single catastrophic event to \$60 million, compared to the \$50 million retention level under the prior agreement. We believe that this increased retention level is appropriate given our growth in both premiums and regulatory capital.

The following discussion of our severity and frequency trends in our personal auto businesses excludes comprehensive coverage because of its inherent volatility, as it is typically linked to catastrophic losses generally resulting from adverse weather. Comprehensive coverage insures against damage to a customer's vehicle due to various causes other than collision, such as windstorm, hail, theft, falling objects, and glass breakage.

Total personal auto incurred severity (i.e., average cost per claim, including both paid losses and the change in case reserves) on a calendar-year basis increased about 2% and 3% for the three and six months ended June 30, 2018, respectively, compared to the same periods last year. Following are the changes we experienced in severity in our auto coverages on a year-over-year basis:

- Collision increased about 6% and 7% for the second quarter and the first six months of 2018, respectively, in part due to an increase in the severity of total loss claims and higher costs to repair newer vehicles.

- Bodily injury and auto property damage both increased about 2% - 3% for both periods.

- Personal injury protection (PIP) decreased about 7% and 4% for the second quarter and the first six months of 2018, respectively.

It is a challenge to estimate future severity, especially for bodily injury and PIP claims, but we continue to monitor changes in the underlying costs, such as medical costs, health care reform, and jury verdicts, along with regulatory changes and other factors that may affect severity.

Our incurred frequency of auto accidents, on a calendar-year basis, decreased about 3% and 2% for the three and six months ended June 30, 2018, respectively, compared to the same periods last year. Following are our frequency changes by coverage on a year-over-year basis:

- PIP, auto property damage, and bodily injury decreased about 2% - 3% for both periods presented.

Collision decreased about 2% and 1% for the second quarter and the first six months of 2018, respectively.

We closely monitor the changes in frequency, but the degree or direction of near-term frequency change is not something that we are able to predict with any certainty. We analyze trends to distinguish changes in our experience from external factors, such as changes in the number of vehicles per household, miles driven, gasoline prices, advances in vehicle safety, and unemployment rates, versus those resulting from shifts in the mix of our business, to allow us to reserve more accurately for our loss exposures.

The table below presents the actuarial adjustments implemented and the loss reserve development experienced in the following periods on a companywide basis:

| (\$ in millions) | Three Months Ended | | Six Months Ended June | |
|---|--------------------|----------|-----------------------|-------------|
| | June 30, 2018 | 2017 | 30, 2018 | 2017 |
| ACTUARIAL ADJUSTMENTS | | | | |
| Reserve decrease (increase) | | | | |
| Prior accident years | \$(7.0) | \$45.5 | \$(0.8) | \$70.9 |
| Current accident year | 6.2 | (2.9) | 13.9 | (16.4) |
| Calendar year actuarial adjustment | \$(0.8) | \$42.6 | \$13.1 | \$54.5 |
| PRIOR ACCIDENT YEARS DEVELOPMENT | | | | |
| Favorable (unfavorable) | | | | |
| Actuarial adjustment | \$(7.0) | \$45.5 | \$(0.8) | \$70.9 |
| All other development | (18.9) | (8.5) | (80.7) | (145.1) |
| Total development | \$(25.9) | \$37.0 | \$(81.5) | \$(74.2) |
| (Increase) decrease to calendar year combined ratio | (0.3) pts. | 0.6 pts. | (0.6) pts. | (0.6) pts. |

Total development consists of both actuarial adjustments and “all other development.” The actuarial adjustments represent the net changes made by our actuarial staff to both current and prior accident year reserves based on regularly scheduled reviews. Through these reviews, our actuaries identify and measure variances in the projected frequency and severity trends, which allow them to adjust the reserves to reflect the current cost trends. For our Property business, 100% of the outstanding reserves are reviewed monthly and, as such, include any development on catastrophe losses as part of the actuarial adjustments. For the vehicle businesses, only a subset of our reserves is reviewed monthly as part of the actuarial adjustment process. Development for catastrophe losses for the vehicle businesses would be reflected in “all other development,” discussed below, to the extent they related to prior year reserves. We report these actuarial adjustments separately for the current and prior accident years to reflect these adjustments as part of the total prior accident years development.

“All other development” represents claims settling for more or less than reserved, emergence of unrecorded claims at rates different than anticipated in our incurred but not recorded (IBNR) reserves, and changes in reserve estimates on specific claims. Although we believe the development from both the actuarial adjustments and “all other development” generally results from the same factors, we are unable to quantify the portion of the reserve development that might be applicable to any one or more of those underlying factors.

Our objective is to establish case and IBNR reserves that are adequate to cover all loss costs, while incurring minimal variation from the date that the reserves are initially established until the losses are fully developed. See Note 6 – Loss and Loss Adjustment Expense Reserves, for a more detailed discussion of our prior accident years development. We continue to focus on our loss reserve analysis, attempting to enhance accuracy and to further our understanding of our loss costs.

Underwriting Expenses

Progressive’s underwriting expenses increased 24% for the second quarter and 20% for the first six months of 2018, compared to the same periods last year. Nevertheless, the underwriting expense ratio (i.e., policy acquisition costs and other underwriting expenses, net of fees and other revenues, expressed as a percentage of net premiums earned) was only 0.4 points higher for the second quarter 2018 and was flat for the first six months of 2018, in part reflecting the increase in earned premium per policy we realized during the same periods. The increase in advertising spend was the primary driver of the increase in total underwriting expenses. During the second quarter and first six months of 2018, our advertising expenditures increased 55% and 44%, respectively, compared to the same periods last year. We will

continue to invest in advertising as long as we generate sales at a cost below the maximum amount we are willing to spend to acquire a new customer.

C. Growth

For our underwriting operations, we analyze growth in terms of both premiums and policies. Net premiums written represent the premiums from policies written during the period, less any premiums ceded to reinsurers. Net premiums earned, which are a function of the premiums written in the current and prior periods, are earned as revenue over the life of the policy using a daily earnings convention. Policies in force, our preferred measure of growth since it removes the variability due to rate changes or mix shifts, represents all policies under which coverage was in effect as of the end of the period specified.

| (\$ in millions) | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|-------------------------------|-----------------------------|-----------|----------|---------------------------|------------|----------|
| | 2018 | 2017 | % Growth | 2018 | 2017 | % Growth |
| NET PREMIUMS WRITTEN | | | | | | |
| Personal Lines | | | | | | |
| Agency | \$3,384.6 | \$2,916.4 | 16 % | \$6,719.9 | \$5,737.1 | 17 % |
| Direct | 3,268.3 | 2,681.7 | 22 | 6,677.8 | 5,474.3 | 22 |
| Total Personal Lines | 6,652.9 | 5,598.1 | 19 | 13,397.7 | 11,211.4 | 20 |
| Commercial Lines | 1,045.2 | 857.1 | 22 | 1,972.1 | 1,518.0 | 30 |
| Property | 397.2 | 290.9 | 37 | 694.3 | 507.7 | 37 |
| Total underwriting operations | \$8,095.3 | \$6,746.1 | 20 % | \$16,064.1 | \$13,237.1 | 21 % |
| NET PREMIUMS EARNED | | | | | | |
| Personal Lines | | | | | | |
| Agency | \$3,225.7 | \$2,752.5 | 17 % | \$6,289.5 | \$5,384.0 | 17 % |
| Direct | 3,211.8 | 2,650.0 | 21 | 6,228.1 | 5,173.7 | 20 |
| Total Personal Lines | 6,437.5 | 5,402.5 | 19 | 12,517.6 | 10,557.7 | 19 |
| Commercial Lines | 884.3 | 671.7 | 32 | 1,692.9 | 1,317.2 | 29 |
| Property | 312.4 | 239.1 | 31 | 597.7 | 465.1 | 29 |
| Total underwriting operations | \$7,634.2 | \$6,313.3 | 21 % | \$14,808.2 | \$12,340.0 | 20 % |
| June 30, | | | | | | |
| (thousands) | 2018 | 2017 | % Growth | | | |
| POLICIES IN FORCE | | | | | | |
| Agency auto | 6,107.4 | 5,350.3 | 14 % | | | |
| Direct auto | 6,650.9 | 5,692.6 | 17 | | | |
| Total auto | 12,758.3 | 11,042.9 | 16 | | | |
| Special lines ¹ | 4,387.4 | 4,356.3 | 1 | | | |
| Personal Lines - total | 17,145.7 | 15,399.2 | 11 % | | | |
| Commercial Lines | 678.9 | 625.7 | 9 % | | | |
| Property | 1,766.6 | 1,311.1 | 35 % | | | |

¹ Includes insurance for motorcycles, watercraft, RVs, and similar items.

During the first half of 2018, we added 1.4 million policies in force and added approximately 2.3 million since June 30, 2017. The increases reflect both an increase in new applications and lengthening retention.

Although new policies are necessary to maintain a growing book of business, we continue to recognize the importance of retaining our current customers as a critical component of our continued growth. As shown in the tables below, we measure retention by policy life expectancy. We disclose our changes in policy life expectancy using a trailing 12-month period, since we believe this measure is indicative of recent experience, mitigates the effects of month-to-month variability, and addresses seasonality. We also review our customer retention for our personal auto products using a trailing 3-month period. Although using a trailing 3-month measure does not address seasonality and can reflect more volatility, this measure is more responsive to current experience and can be an indicator of how our

retention rates are moving.

To analyze growth, we review new policies, rate levels, and the retention characteristics of our segments.

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D. Personal Lines

The following table shows our year-over-year changes for our Personal Lines business:

| | Growth Over Prior Year | | | | |
|-----------------------------------|------------------------|------|--------------|------|---|
| | Quarter | | Year-to-date | | |
| | 2018 | 2017 | 2018 | 2017 | |
| APPLICATIONS | | | | | |
| New | 21 | % 9 | % 21 | % 7 | % |
| Renewal | 9 | % 6 | % 10 | % 6 | % |
| WRITTEN PREMIUM PER POLICY - AUTO | 5 | % 6 | % 5 | % 6 | % |
| RETENTION MEASURES - AUTO | | | | | |
| Policy life expectancy | | | | | |
| Trailing 3-months | 5 | % 4 | % | | |
| Trailing 12-months | 10 | % 5 | % | | |

In our Personal Lines business, the increase in both new and renewal applications resulted from increases in our personal auto products. In the auto businesses, the increase in new applications was primarily attributable to our competitive product offerings and position in the marketplace and reflects our increase in advertising spend during the first half of 2018. For the second quarter 2018, on a year-over-year basis, our auto new applications were up 27% and our special lines products increase in new applications was 2%. For the first six months of 2018, auto new applications were up 26% and special lines saw a decrease of 1%. The Direct business contributed more to our auto growth for both periods, primarily due to lower new applications in the second quarter and first six months of 2017, following a reduction of our advertising spend during the second half of 2016. Rate increases taken in our auto businesses over the trailing 12-month period, in addition to a shift in business mix, contributed to the increase we experienced in written premium per policy for the second quarter and first six months of 2018. Our Destination Era efforts continue to have a positive impact on our retention.

We report our Agency and Direct business results separately as components of our Personal Lines segment to provide further understanding of our products by distribution channel.

The Agency Business

| | Growth Over Prior Year | | | | |
|--|------------------------|------|--------------|------|---|
| | Quarter | | Year-to-date | | |
| | 2018 | 2017 | 2018 | 2017 | |
| Auto: new applications | 21 | % 17 | % 20 | % 16 | % |
| renewal applications | 10 | % 7 | % 11 | % 6 | % |
| written premium per policy | 5 | % 6 | % 5 | % 6 | % |
| Auto retention measures: | | | | | |
| policy life expectancy - trailing 3-months | 5 | % 6 | % | | |
| trailing 12-months | 11 | % 6 | % | | |

The Agency business includes business written by more than 35,000 independent insurance agencies that represent Progressive, as well as brokerages in New York and California. New and renewal applications increased during the second quarter and the six months ended June 30, 2018, primarily reflecting our competitiveness in the marketplace as a result of many of our competitors taking higher rate increases than we have over the trailing 12-month period.

During the second quarter, we continued to experience new business application growth and strong policy in force growth in each of our consumer segments (e.g., inconsistently insured, consistently insured and maybe a renter, homeowners who do not bundle auto and home, and homeowners who bundle auto and home) with the largest increase coming from our bundled auto and home product (i.e., Robinsons), albeit on a smaller base. During the year, we generated new auto application growth in 45 states, including nine of our top 10 largest Agency states.

We have continued to see an increase in demand from agents as evidenced by about a 5% increase in quote volume during the second quarter and first six months of 2018, compared to the same periods last year. Our Agency auto rate of conversion (i.e., converting a quote to a sale) increased about 14% for both the second quarter and the six months ended June 30, 2018, compared to last year. Written premium per policy for new and renewal Agency auto business

increased 5% for the second quarter and first six months of 2018, as compared to the same periods last year, primarily reflecting rate increases previously discussed.

The Direct Business

| | Growth Over Prior Year | | | | |
|--|------------------------|------|--------------|------|---|
| | Quarter | | Year-to-date | | |
| | 2018 | 2017 | 2018 | 2017 | |
| Auto: new applications | 32 | % 8 | % 31 | % 3 | % |
| renewal applications | 13 | % 8 | % 13 | % 9 | % |
| written premium per policy | 5 | % 5 | % 5 | % 6 | % |
| Auto retention measures: | | | | | |
| policy life expectancy - trailing 3-months | 4 | % 1 | % | | |
| trailing 12-months | 9 | % 2 | % | | |

The Direct business includes business written directly by Progressive on the Internet, through mobile devices, and over the phone. During the year, we generated new Direct auto application growth in 49 states, including all of our top 10 largest Direct states. New and renewal applications increased during the second quarter and the six months ended June 30, 2018, primarily reflecting our competitiveness in the marketplace. In addition, we increased our advertising spend, on a year-over-year basis, for the second quarter and the first six months of 2018, which helped drive new business growth and also contributed to the total increase in our Direct business expense ratios during both periods. Similar to our Agency business, during the second quarter, we continued to grow our new Direct auto applications double digits across all consumer segments and, with the marketing investments that continued to target auto/home bundlers, we saw the greatest growth in our Robinsons consumer segment. Our Direct auto quote volume increased 15% and 12%, on a year-over-basis, for the second quarter and first six months of 2018, respectively, and the rate of conversion increased about 16% for the second quarter and 18% for the six months ended June 30, 2018, compared to last year. Written premium per policy for new and renewal Direct auto business increased 4% and 5%, respectively, for the second quarter 2018, and 4% and 5%, for the first six months, as compared to the same periods last year, primarily reflecting rate increases previously discussed.

E. Commercial Lines

| | Growth Over Prior Year | | | | |
|---|------------------------|--------|--------------|---------|---|
| | Quarter | | Year-to-date | | |
| | 2018 | 2017 | 2018 | 2017 | |
| New applications | 9 | %(4)% | 17 | %(12)% | |
| Renewal applications | 5 | % 10 | % 4 | % 10 | % |
| Written premium per policy | 12 | % 11 | % 13 | % 8 | % |
| Policy life expectancy - trailing 12-months | 2 | % 0 | % | | |

Our Commercial Lines business operates in the business auto, for-hire transportation, contractor, for-hire specialty, tow, and for-hire livery markets and is primarily written in the agency channel. Commercial Lines experienced solid year-over-year new application growth in the second quarter and first six months of 2018, reflecting increased quote volume, a generally strong economy and limited options for commercial auto customers and agents. We continue to monitor the growth and profitability across all of our business market targets and will impose underwriting restrictions when we believe it is necessary to meet our profitability objectives. We removed a number of underwriting restrictions early in the second quarter 2018; however, some truck underwriting restrictions remain in select markets. During 2018, we added three additional states bringing the total to four states where we insure transportation network company business. Albeit from a smaller base, the net premiums earned on this business during the second quarter 2018 are up nearly 120% from the first quarter 2018. We continued to increase our understanding of the pricing for this product and may increase the number of states where we provide coverage. We have also seen greater market acceptance of Smart Haul[®], our usage-based insurance program for our for-hire transportation policyholders. With the enforcement of the federal electronic logging device mandate, we believe we are well positioned to offer competitive rates to the best owners/operators and small fleets.

During the three and six months ended June 30, 2018, we increased rates and experienced shifts in business mix, which contributed to the increase in our written premium per policy. Despite higher rates, the increase in policy life expectancy was primarily attributable to a shift in business mix and competitors taking higher rate increases.

F. Property

| | Growth Over Prior Year | | | |
|----------------------------|------------------------|------|--------------|------|
| | Quarter | | Year-to-date | |
| | 2018 | 2017 | 2018 | 2017 |
| New applications | 81 | % 35 | % 83 | % 33 |
| Renewal applications | 21 | % 19 | % 20 | % 20 |
| Written premium per policy | (5) |)(7) | (5) |)(8) |

Our Property business writes residential property insurance for homeowners, other property owners, and renters, primarily in the agency channel. The significant growth in new applications is attributable to state expansion that occurred during the last 12 months in both Property business written by ARX and Progressive's renters business, more competitive product offerings, as well as momentum in growing Robinsons through our Platinum agency offering.

In addition, the Property growth is benefiting from HomeQuote Explorer[®], our direct online homeowner insurance shopping experience that was launched in March 2017. During the second quarter 2018, ASI began offering the ability to buy Progressive Home online through the HQX platform. The online buy button functionality is currently offered in one state and we plan to expand to other states over time.

The decrease in premium per policy continues to reflect a relatively higher percentage of renters policies, which have lower premiums per policy. Our core Property policies (e.g., home and condo insurance) had a slight increase in written premiums per policy for both periods on a year-over-year basis.

G. Income Taxes

A deferred tax asset or liability is a tax benefit or expense that is expected to be realized in a future tax year. At June 30, 2018 and 2017, and December 31, 2017, we reported net deferred tax liabilities. At June 30, 2018 and 2017, and December 31, 2017, we had net current income taxes payable of \$60.5 million, \$17.9 million, and \$23.8 million, respectively, which were reported as part of "other liabilities."

Our effective tax rate was 20% for the second quarter and first six months of 2018, compared to 33% for the same periods last year. The decrease primarily reflects the reduction in the federal corporate income tax rate to 21%, from the previous rate of 35%, under the legislation commonly known as the Tax Cuts and Jobs Act of 2017. See Note 5 – Income Taxes for further discussion.

There were no material changes in our uncertain tax positions during the three months ended June 30, 2018.

IV. RESULTS OF OPERATIONS – INVESTMENTS

A. Investment Results

We report total return to reflect our management philosophy governing the portfolio and our evaluation of investment results. The fully taxable equivalent (FTE) total return includes recurring investment income, adjusted to a fully taxable amount for certain securities that receive preferential tax treatment (e.g., municipal securities), and total net realized, and changes in total net unrealized, gains (losses) on securities.

Our investment portfolio produced an FTE total return of 0.6% for the three months ended June 30, 2018, compared to 1.3% for the same period in 2017. Our fixed-income and common stock portfolios had FTE total returns of 0.3% and 3.1%, respectively, for the three months ended June 30, 2018, and 1.1% and 3.5%, respectively, for the same period in 2017. Interest rates rose during the quarter. However, we did not change our fixed-income portfolio duration of 2.6 years. We generated a small positive return in the fixed-income portfolio this quarter as coupon income was able to offset the rise in interest rates and mixed spread movements across sectors. The equity market rebounded from its first quarter drop and ended the second quarter higher year-to-date. Our indexed portfolio return was in line with the overall market, while our actively managed portfolio lagged with a negative return.

The following summarizes investment results for the periods ended June 30:

| | Three Months | | Six Months | |
|---|--------------|-------|------------|-------|
| | 2018 | 2017 | 2018 | 2017 |
| Pretax recurring investment book yield (annualized) | 2.7 % | 2.3 % | 2.6 % | 2.3 % |
| Weighted average FTE book yield (annualized) | 2.8 % | 2.5 % | 2.7 % | 2.6 % |
| FTE total return: | | | | |
| Fixed-income securities | 0.3 % | 1.1 % | 0 % | 2.2 % |
| Common stocks | 3.1 % | 3.5 % | 2.7 % | 9.8 % |
| Total portfolio | 0.6 % | 1.3 % | 0.3 % | 3.1 % |

A further break-down of our FTE total returns for our portfolio, including any net gains (losses) on our derivative positions, for the periods ended June 30, follows:

| | Three Months | | Six Months | |
|--|--------------|-------|------------|--------|
| | 2018 | 2017 | 2018 | 2017 |
| Fixed-income securities: | | | | |
| U.S. Treasury Notes | 0 % | 0.8 % | (0.7 %) % | 1.4 % |
| Municipal bonds | 0.8 % | 1.6 % | 0.6 % | 3.4 % |
| Corporate bonds | 0.3 % | 1.0 % | (0.3 %) % | 2.0 % |
| Residential mortgage-backed securities | 0.6 % | 1.7 % | 1.1 % | 2.8 % |
| Commercial mortgage-backed securities | 0.5 % | 1.5 % | 0.5 % | 2.8 % |
| Other asset-backed securities | 0.5 % | 0.5 % | 0.7 % | 1.0 % |
| Preferred stocks | 0.5 % | 4.2 % | 0.5 % | 9.6 % |
| Short-term investments | 0.5 % | 0.3 % | 0.9 % | 0.5 % |
| Common stocks: | | | | |
| Indexed | 3.4 % | 3.4 % | 2.8 % | 10.0 % |
| Actively managed | (1.5 %) % | 5.3 % | 2.3 % | 7.5 % |

B. Portfolio Allocation

The composition of the investment portfolio was:

| (\$ in millions) | Fair Value | % of Total Portfolio | Duration (years) | Rating ¹ |
|--------------------------------|------------|----------------------|------------------|---------------------|
| June 30, 2018 | | | | |
| Fixed maturities | \$23,789.2 | 76.9 | % 2.9 | AA- |
| Nonredeemable preferred stocks | 758.6 | 2.4 | 3.1 | BBB- |
| Short-term investments | 3,231.2 | 10.5 | 0.1 | AA- |
| Total fixed-income securities | 27,779.0 | 89.8 | 2.6 | AA- |
| Common equities | 3,142.2 | 10.2 | na | na |
| Total portfolio ^{2,3} | \$30,921.2 | 100.0 | % 2.6 | AA- |
| June 30, 2017 | | | | |
| Fixed maturities | \$18,388.1 | 70.8 | % 2.6 | A+ |
| Nonredeemable preferred stocks | 783.1 | 3.0 | 3.6 | BBB- |
| Short-term investments | 3,729.7 | 14.4 | <0.1 | AA |
| Total fixed-income securities | 22,900.9 | 88.2 | 2.3 | A+ |
| Common equities | 3,077.5 | 11.8 | na | na |
| Total portfolio ^{2,3} | \$25,978.4 | 100.0 | % 2.3 | A+ |
| December 31, 2017 | | | | |
| Fixed maturities | \$20,201.7 | 74.1 | % 2.8 | AA- |
| Nonredeemable preferred stocks | 803.8 | 2.9 | 3.3 | BBB- |
| Short-term investments | 2,869.4 | 10.5 | <0.1 | AA- |
| Total fixed-income securities | 23,874.9 | 87.5 | 2.5 | AA- |
| Common equities | 3,399.8 | 12.5 | na | na |
| Total portfolio ^{2,3} | \$27,274.7 | 100.0 | % 2.5 | AA- |

na = not applicable

¹Represents ratings at period end. Credit quality ratings are assigned by nationally recognized statistical rating organizations. To calculate the weighted average credit quality ratings, we weight individual securities based on fair value and assign a numeric score of 0-5, with non-investment-grade and non-rated securities assigned a score of 0-1. To the extent the weighted average of the ratings falls between AAA and AA+, we would assign an internal rating of AAA-.

²Our portfolio reflects the effect of unsettled security transactions; at June 30, 2018 and 2017, we had \$362.1 million and \$287.1 million, respectively, included in "other liabilities," compared to \$5.8 million included in "other assets" at December 31, 2017.

³The total fair value of the portfolio at June 30, 2018 and 2017, and December 31, 2017, included \$1.7 billion, \$1.1 billion, and \$1.6 billion, respectively, of securities held in a consolidated, non-insurance subsidiary of the holding company, net of any unsettled security transactions.

Our asset allocation strategy is to maintain 0%-25% of our portfolio in Group I securities, with the balance (75%-100%) of our portfolio in Group II securities.

We define Group I securities to include:

- common equities
- nonredeemable preferred stocks
- redeemable preferred stocks, except for 50% of investment-grade redeemable preferred stocks with cumulative dividends, which are included in Group II, and
- all other non-investment-grade fixed-maturity securities.

Group II securities include:

short-term securities, and
all other fixed-maturity securities, including 50% of the investment-grade redeemable preferred stocks with
cumulative dividends.

We believe this asset allocation strategy allows us to appropriately assess the risks associated with these securities for capital purposes and is in line with the treatment by our regulators.

The following table shows the composition of our Group I and Group II securities:

| (\$ in millions) | June 30, 2018 | | June 30, 2017 | | December 31, 2017 | |
|--|---------------|----------------------|---------------|----------------------|-------------------|----------------------|
| | Fair Value | % of Total Portfolio | Fair Value | % of Total Portfolio | Fair Value | % of Total Portfolio |
| Group I securities: | | | | | | |
| Non-investment-grade fixed maturities | \$802.2 | 2.6 | % \$387.6 | 1.5 | % \$404.8 | 1.5 |
| Redeemable preferred stocks ¹ | 156.3 | 0.5 | 144.5 | 0.6 | 147.4 | 0.5 |
| Nonredeemable preferred stocks | 758.6 | 2.4 | 783.1 | 3.0 | 803.8 | 2.9 |
| Common equities | 3,142.2 | 10.2 | 3,077.5 | 11.8 | 3,399.8 | 12.5 |
| Total Group I securities | 4,859.3 | 15.7 | 4,392.7 | 16.9 | 4,755.8 | 17.4 |
| Group II securities: | | | | | | |
| Other fixed maturities ² | 22,830.7 | 73.8 | 17,856.0 | 68.7 | 19,649.5 | 72.1 |
| Short-term investments | 3,231.2 | 10.5 | 3,729.7 | 14.4 | 2,869.4 | 10.5 |
| Total Group II securities | 26,061.9 | 84.3 | 21,585.7 | 83.1 | 22,518.9 | 82.6 |
| Total portfolio | \$30,921.2 | 100.0 | % \$25,978.4 | 100.0 | % \$27,274.7 | 100.0 |

¹Includes non-investment-grade redeemable preferred stocks of \$83.5 million, \$82.3 million, and \$83.8 million at June 30, 2018 and 2017, and December 31, 2017, respectively.

²Includes investment-grade redeemable preferred stocks, with cumulative dividends, of \$72.8 million, \$62.2 million, and \$63.6 million at June 30, 2018 and 2017, and December 31, 2017, respectively.

To determine the allocation between Group I and Group II, we use the credit ratings from models provided by the National Association of Insurance Commissioners (NAIC) for classifying our residential and commercial mortgage-backed securities, excluding interest-only securities, and the credit ratings from nationally recognized statistical rating organizations (NRSRO) for all other debt securities. NAIC ratings are based on a model that considers the book price of our securities when assessing the probability of future losses in assigning a credit rating. As a result, NAIC ratings can vary from credit ratings issued by NRSROs. Management believes NAIC ratings more accurately reflect our risk profile when determining the asset allocation between Group I and Group II securities.

Unrealized Gains and Losses

As of June 30, 2018, our fixed-maturity portfolio had pretax net unrealized losses, recorded as part of accumulated other comprehensive income, of \$267.3 million, compared to net unrealized gains of \$73.3 million at June 30, 2017 and net unrealized losses of \$8.4 million at December 31, 2017. The changes for both periods reflect valuation declines in nearly all sectors during the first six months of 2018, most notably in our U.S. Treasury and corporate portfolios, partially offset by net realized losses on sales of securities primarily in our U.S. Treasury portfolio. See Note 2 – Investments for a further break-out of our gross unrealized gains and losses.

Holding Period Gains and Losses

The following table provides the inception-to-date gross and net holding period gains (losses) for our hybrid fixed-maturity securities and our equity securities as of June 30, 2018:

| (millions) | Gross Holding Period Gains | Gross Holding Period Losses | Net Holding Period Gains (Losses) |
|---|-------------------------------------|--------------------------------------|---|
| Hybrid fixed maturities: | | | |
| State and local government obligations | \$0 | \$0 | \$0 |
| Corporate debt securities | 0 | (2.0) | (2.0) |
| Other asset-backed securities | 0.1 | 0 | 0.1 |
| Redeemable preferred stocks | 0 | (3.4) | (3.4) |
| Total hybrid fixed maturities | 0.1 | (5.4) | (5.3) |
| Equity securities: | | | |
| Nonredeemable preferred stocks | 92.8 | (11.2) | 81.6 |
| Common equities | 1,836.5 | (8.3) | 1,828.2 |
| Total equity securities | 1,929.3 | (19.5) | 1,909.8 |
| Total holding period securities at June 30, 2018 | \$1,929.4 | \$(24.9) | \$1,904.5 |
| Total holding period securities at June 30, 2017 ¹ | \$1,738.5 | \$(13.1) | \$1,725.4 |
| Total holding period securities at December 31, 2017 ¹ | \$2,015.6 | \$(9.4) | \$2,006.2 |

¹For comparative purposes, the holding period securities at June 30, 2017 and December 31, 2017 include the hybrid fixed maturities with holding period gains (losses) and the equity securities with unrealized gains (losses).

Other-Than-Temporary Impairment (OTTI)

Net realized gains (losses) may include write-downs of securities determined to have had other-than-temporary declines in fair value. In light of the new accounting guidance effective for 2018, we no longer need to analyze our equity securities for OTTI.

We routinely monitor our fixed-maturity portfolio for pricing changes that might indicate potential impairments and perform detailed reviews of securities with unrealized losses. In such cases, changes in fair value are evaluated to determine the extent to which such changes are attributable to: (i) fundamental factors specific to the issuer, such as financial conditions, business prospects, or other factors, (ii) market-related factors, such as interest rates or equity market declines (e.g., negative return at either a sector index level or at the broader market level), or (iii) credit-related losses, where the present value of cash flows expected to be collected is lower than the amortized cost basis of the security.

Fixed-maturity securities with declines attributable to issuer-specific fundamentals are reviewed to identify available evidence, circumstances, and influences to estimate the potential for, and timing of, recovery of the investment's impairment. An other-than-temporary impairment loss is deemed to have occurred when the potential for recovery does not satisfy the criteria set forth in the current accounting guidance.

When a security in our fixed-maturity portfolio has an unrealized loss and it is more likely than not that we will be required to sell the security, we write-down the security to its current fair value and recognize the entire unrealized loss through the comprehensive income statement as a realized loss. If a fixed-maturity security has an unrealized loss and it is more likely than not that we will hold the debt security until recovery (which could be maturity), then we determine if any of the decline in value is due to a credit loss (i.e., where the present value of cash flows expected to be collected is lower than the amortized cost basis of the security) and, if so, we will recognize that portion of the impairment in net income as part of the comprehensive income statement as a realized loss; any remaining unrealized loss on the security is considered to be due to other factors (e.g., interest rate and credit spread movements) and is reflected in other comprehensive income as part of shareholders' equity, along with unrealized gains or losses on

securities that are not deemed to be other-than-temporarily impaired.

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The write-down activity recorded in the comprehensive income statements was as follows:

| (millions) | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|----------------------------|-----------------------------|--------------------------------|--|---------------------------|--------------------------------|--|
| | Total Write-downs | Write-downs on Securities Sold | Write-downs on Securities Held at Period End | Total Write-downs | Write-downs on Securities Sold | Write-downs on Securities Held at Period End |
| 2018 | | | | | | |
| Common equities | \$0 | \$ 0 | \$ 0 | \$0 | \$ 0 | \$ 0 |
| Total investment portfolio | 0 | 0 | 0 | 0 | 0 | 0 |
| Other assets ¹ | 11.1 | 0 | 11.1 | 11.1 | 0 | 11.1 |
| Total write-downs | \$11.1 | \$ 0 | \$ 11.1 | \$11.1 | \$ 0 | \$ 11.1 |
| 2017 | | | | | | |
| Common equities | \$2.6 | \$ 0 | \$ 2.6 | \$3.6 | \$ 0 | \$ 3.6 |
| Total investment portfolio | 2.6 | 0 | 2.6 | 3.6 | 0 | 3.6 |
| Other assets ¹ | 11.2 | 0 | 11.2 | 11.2 | 0 | 11.2 |
| Total write-downs | \$13.8 | \$ 0 | \$ 13.8 | \$14.8 | \$ 0 | \$ 14.8 |

¹Reflects an impairment of a renewable energy investment under which the future pretax cash flows are expected to be less than the carrying value of the asset.

The following table stratifies the gross unrealized losses in our fixed-maturity portfolio at June 30, 2018, by duration in a loss position and magnitude of the loss as a percentage of the cost of the security:

| (millions) | Fair Value | Total Gross Unrealized Losses | Decline of Investment Value | | | |
|--|------------|-------------------------------|-----------------------------|--------|--------|------|
| | | | >15% | >25% | >35% | >45% |
| Fixed maturity: | | | | | | |
| Unrealized loss for less than 12 months | \$14,234.4 | \$ 181.9 | \$0.1 | \$ 0.1 | \$ 0.1 | \$ 0 |
| Unrealized loss for 12 months or greater | 5,664.3 | 122.2 | 0 | 0 | 0 | 0 |
| Total | \$19,898.7 | \$ 304.1 | \$0.1 | \$ 0.1 | \$ 0.1 | \$ 0 |

We completed a thorough review of the existing securities in these loss categories and determined that, applying the procedures and criteria discussed above, these securities were not other-than-temporarily impaired. We also determined that it is more likely that we will not be required to sell these securities, for the periods of time necessary to recover the respective cost bases of these securities, and that there are no additional credit-related impairments on our debt securities.

Since total unrealized losses are already a component of other comprehensive income and included in shareholders' equity, any recognition of these losses as additional OTTI losses would have no effect on our comprehensive income, book value, or reported investment total return.

Fixed-Income Securities

The fixed-income portfolio is managed internally and includes fixed-maturity securities, short-term investments, and nonredeemable preferred stocks. A primary exposure for the fixed-income portfolio is interest rate risk, which includes the change in value resulting from movements in the underlying market rates of debt securities held. We manage this risk by maintaining the portfolio's duration (a measure of the portfolio's exposure to changes in interest rates) between 1.5 and 5 years. The duration of the fixed-income portfolio was 2.6 years at June 30, 2018, compared to 2.3 years at June 30, 2017 and 2.5 years at December 31, 2017. The change from June 30, 2017 through June 30, 2018 reflects our proactive monitoring and reacting to the changing interest rate environment while maintaining a conservative duration position to limit potential declines in portfolio value from increases in rates. The distribution of duration and convexity (i.e., a measure of the speed at which the duration of a security is expected to change based on a rise or fall in interest rates) is monitored on a regular basis.

The duration distribution of our fixed-income portfolio, excluding short-term investments, represented by the interest rate sensitivity of the comparable benchmark U.S. Treasury Notes, was:

| Duration Distribution | June 30, 2018 | June 30, 2017 | December 31, 2017 |
|------------------------------|---------------|---------------|-------------------|
| 1 year | 21.9 | % 24.1 | % 19.8 |
| 2 years | 18.1 | 14.5 | 15.7 |
| 3 years | 24.9 | 25.9 | 27.0 |
| 5 years | 19.3 | 24.3 | 24.1 |
| 7 years | 10.2 | 8.0 | 8.7 |
| 10 years | 5.6 | 3.3 | 4.7 |
| 20 years | 0 | (0.1 |) 0 |
| 30 years | 0 | 0 | 0 |
| Total fixed-income portfolio | 100.0 | % 100.0 | % 100.0 |

The negative duration in the 20-year category at June 30, 2017 arose from the variable rate nature of the dividends on some of our preferred stocks. If not called at their call dates, the dividends on these securities would reset from a fixed rate to a lower floating rate, which could cause these securities to trade at a discount and, therefore, with a negative duration as the securities' valuation would likely rise if the floating rate moves higher.

Another primary exposure related to the fixed-income portfolio is credit risk. This risk is managed by maintaining an A+ minimum weighted average portfolio credit quality rating, as defined by NRSROs, which was successfully maintained during the first six months of 2018 and all of 2017.

The credit quality distribution of the fixed-income portfolio was:

| Rating | June 30, 2018 | June 30, 2017 | December 31, 2017 |
|---|---------------|---------------|-------------------|
| AAA | 47.3 | % 40.8 | % 45.8 |
| AA | 11.7 | 17.7 | 13.6 |
| A | 11.1 | 12.1 | 12.2 |
| BBB | 24.7 | 24.6 | 23.2 |
| Non-investment grade/non-rated ¹ | | | |
| BB | 3.3 | 3.4 | 3.6 |
| B | 1.5 | 0.7 | 1.0 |
| CCC and lower | 0.1 | 0.1 | 0.1 |
| Non-rated | 0.3 | 0.6 | 0.5 |
| Total fixed-income portfolio | 100.0 | % 100.0 | % 100.0 |

¹The ratings in the table above are assigned by NRSROs. The non-investment-grade fixed-income securities based upon our Group I classification represented 3.9% of the total fixed-income portfolio at June 30, 2018, compared to 3.3% at June 30, 2017 and 2.6% at December 31, 2017.

The changes in credit quality profile from June 30, 2017 were the result of transactions in our portfolio that shifted the mix within the various credit categories.

Our portfolio is also exposed to concentration risk. Our investment constraints limit investment in a single issuer, other than U.S. Treasury Notes or a state's general obligation bonds, to 2.5% of shareholders' equity, while the single issuer guideline on preferred stocks and/or non-investment-grade debt is 1.25% of shareholders' equity. Additionally, the guideline applicable to any state's general obligation bonds is 6% of shareholders' equity. We also consider sector concentration a risk, and we frequently evaluate the portfolio's sector allocation with regard to internal requirements and external market factors. We consider concentration risk both overall and in the context of individual asset classes, including but not limited to common equities, residential and commercial mortgage-backed securities, municipal bonds, and high-yield bonds. We were within all of the constraints described above during all reported periods. We monitor prepayment and extension risk, especially in our structured product and preferred stock portfolios. Prepayment risk includes the risk of early redemption of security principal that may need to be reinvested at less attractive rates. Extension risk includes the risk that a security will not be redeemed when anticipated, and that the security that is extended will have a lower yield than a security we might be able to obtain by reinvesting the expected redemption principal. Our holdings of different types of structured debt and preferred securities help manage this risk. During the first six months of 2018 and all of 2017, we did not experience significant prepayment or extension of principal relative to our cash flow expectations in the portfolio.

Liquidity risk is another risk factor we monitor. Our overall portfolio remains very liquid and we believe that it is sufficient to meet expected near-term liquidity requirements. The short-to-intermediate duration of our portfolio provides a source of liquidity, as we expect approximately \$1.7 billion, or 10.4%, of principal repayment from our fixed-income portfolio, excluding U.S. Treasury Notes and short-term investments, during the remainder of 2018. Cash from interest and dividend payments provides an additional source of recurring liquidity.

The duration of our U.S. government obligations, which are included in the fixed-income portfolio, was comprised of the following at June 30, 2018:

| (\$ in millions) | Fair Value | Duration (years) |
|---------------------------|------------|------------------|
| U.S. Treasury Notes | | |
| Less than one year | \$217.2 | 0.4 |
| One to two years | 1,563.6 | 1.5 |
| Two to three years | 1,723.1 | 2.4 |
| Three to five years | 2,982.4 | 3.9 |
| Five to seven years | 594.2 | 5.9 |
| Seven to ten years | 784.9 | 8.3 |
| Total U.S. Treasury Notes | \$7,865.4 | 3.6 |

As of June 30, 2018, we had no interest rate swaps or treasury futures.

ASSET-BACKED SECURITIES

Included in the fixed-income portfolio are asset-backed securities, which were comprised of the following at the balance sheet dates listed:

| (\$ in millions) | Fair Value | Net Unrealized Gains (Losses) | % of Asset-Backed Securities | Duration (years) | Rating (at period end) |
|---|------------|-------------------------------|------------------------------|------------------|------------------------|
| June 30, 2018 | | | | | |
| Residential mortgage-backed securities: | | | | | |
| Collateralized mortgage obligations | \$444.9 | \$ (2.1) | 6.7 | % 1.1 | AA |
| Home equity (sub-prime bonds) | 377.7 | 5.1 | 5.6 | 0.3 | BBB+ |
| Residential mortgage-backed securities | 822.6 | 3.0 | 12.3 | 0.7 | A+ |
| Commercial mortgage-backed securities | 2,696.9 | (28.6) | 40.3 | 2.7 | A+ |
| Other asset-backed securities: | | | | | |
| Automobile | 1,358.6 | (4.7) | 20.3 | 0.9 | AAA- |
| Credit card | 513.8 | (0.2) | 7.6 | 0.9 | AAA |
| Student loan | 521.8 | (0.6) | 7.8 | 1.0 | AA |
| Other ¹ | 783.4 | (6.2) | 11.7 | 1.7 | AA- |
| Other asset-backed securities | 3,177.6 | (11.7) | 47.4 | 1.1 | AA+ |
| Total asset-backed securities | \$6,697.1 | \$ (37.3) | 100.0 | % 1.7 | AA- |

| (\$ in millions) | Fair Value | Net Unrealized Gains (Losses) | % of Asset-Backed Securities | Duration (years) | Rating (at period end) |
|---|------------|-------------------------------|------------------------------|------------------|------------------------|
| June 30, 2017 | | | | | |
| Residential mortgage-backed securities: | | | | | |
| Collateralized mortgage obligations | \$715.4 | \$ (1.6) | 11.0 | % 0.8 | A |
| Home equity (sub-prime bonds) | 552.2 | 6.6 | 8.5 | 0.3 | BBB |
| Residential mortgage-backed securities | 1,267.6 | 5.0 | 19.5 | 0.6 | A- |
| Commercial mortgage-backed securities | 2,375.0 | 10.1 | 36.6 | 3.6 | A |
| Other asset-backed securities: | | | | | |
| Automobile | 1,288.7 | (0.5) | 19.9 | 0.6 | AAA- |
| Credit card | 366.4 | (0.1) | 5.6 | 0.4 | AAA |
| Student loan | 609.4 | 4.7 | 9.4 | 1.2 | AA- |
| Other ¹ | 582.9 | (0.2) | 9.0 | 2.2 | AA- |
| Other asset-backed securities | 2,847.4 | 3.9 | 43.9 | 1.0 | AA+ |
| Total asset-backed securities | \$6,490.0 | \$ 19.0 | 100.0 | % 1.9 | A+ |

| (\$ in millions) | Fair Value | Net Unrealized Gains (Losses) | % of Asset-Backed Securities | Duration (years) | Rating (at period end) |
|---|------------|-------------------------------|------------------------------|------------------|------------------------|
| December 31, 2017 | | | | | |
| Residential mortgage-backed securities: | | | | | |
| Collateralized mortgage obligations | \$404.3 | \$ 0 | 6.7 | % 1.1 | A+ |
| Home equity (sub-prime bonds) | 432.4 | 7.9 | 7.1 | 0.2 | BBB+ |
| Residential mortgage-backed securities | 836.7 | 7.9 | 13.8 | 0.7 | A- |
| Commercial mortgage-backed securities | 2,758.6 | (1.5) | 45.6 | 2.9 | A |
| Other asset-backed securities: | | | | | |
| Automobile | 1,182.2 | (1.8) | 19.5 | 0.7 | AAA- |
| Credit card | 95.8 | (0.1) | 1.6 | 0.5 | AAA |
| Student loan | 538.7 | 2.3 | 8.9 | 1.1 | AA- |
| Other ¹ | 638.0 | (0.4) | 10.6 | 2.2 | A+ |
| Other asset-backed securities | 2,454.7 | 0 | 40.6 | 1.2 | AA+ |
| Total asset-backed securities | \$6,050.0 | \$ 6.4 | 100.0 | % 1.9 | A+ |

¹Includes equipment leases, whole business securitizations, and other types of structured debt.

The increase in asset-backed securities since December 31, 2017, is primarily due to purchases in the other asset-backed sector partially offset by maturities in the residential mortgage-backed sector and sales and maturities in the commercial mortgage-backed sector. See below for a further discussion of our residential and commercial mortgage-backed securities. The other asset-backed securities category is not included in the discussions below due to the high credit quality, short duration, and security structure of those instruments.

Residential Mortgage-Backed Securities (RMBS) The following table details the credit quality rating and fair value of our RMBSs, along with the loan classification and a comparison of the fair value at June 30, 2018, to our original investment value (adjusted for returns of principal, amortization, and write-downs):

| (\$ in millions) | Collateralized Mortgage Obligations | | | | | | Total | % of Total |
|---------------------------------|-------------------------------------|------------------|------------------|--------------------|-----------------------------|---------|-------|------------|
| | Home Equity | Agency Pass-Thro | Non-Agency Prime | Alt-A ² | Government/GSE ³ | | | |
| Rating ¹ | | | | | | | | |
| AAA | \$35.7 | \$30.1 | \$ 221.8 | \$6.8 | \$ 50.2 | \$344.6 | 41.9 | % |
| AA | 77.8 | 0 | 22.2 | 22.9 | 0.8 | 123.7 | 15.0 | |
| A | 109.2 | 0 | 3.6 | 0 | 0 | 112.8 | 13.7 | |
| BBB | 33.0 | 0 | 8.6 | 0 | 0 | 41.6 | 5.1 | |
| Non-investment grade/non-rated: | | | | | | | | |
| BB | 36.7 | 0 | 3.3 | 1.9 | 0 | 41.9 | 5.1 | |
| B | 48.0 | 0 | 2.8 | 0.8 | 0 | 51.6 | 6.3 | |
| CCC and lower | 13.6 | 0 | 6.3 | 0 | 0 | 19.9 | 2.4 | |
| Non-rated | 23.7 | 0 | 14.9 | 47.9 | 0 | 86.5 | 10.5 | |
| Total fair value | \$377.7 | \$30.1 | \$ 283.5 | \$80.3 | \$ 51.0 | \$822.6 | 100.0 | % |
| Increase (decrease) in value | 1.4 | % (4.0) | %) (0.4) |)% 2.4 | % (3.0) |)% 0.4 | % | |

¹The credit quality ratings in the table above are assigned by NRSROs; when we assign the NAIC ratings for our RMBSs, \$177.8 million of our non-investment-grade securities are rated investment-grade and classified as Group II and \$22.1 million, or 2.7% of our total RMBSs, are not rated by the NAIC and are classified as Group I.

²Represents structured securities with primary residential loans as collateral for which documentation standards for loan approval were less stringent than conventional loans; the collateral loans are often referred to as low documentation or no documentation loans.

³The securities in this category are insured by a Government Sponsored Entity (GSE) and/or collateralized by mortgage loans insured by the Federal Housing Administration (FHA) or the U.S. Department of Veteran Affairs (VA).

Our collateralized mortgage obligation (CMO) portfolio is primarily composed of non-GSE/FHA/VA mortgage securities. The majority of our portfolio consists of older deals with predictable prepayment speeds, high levels of subordination, and stable delinquency trends. During the second quarter 2018, we purchased well-structured older vintage and new issue positions backed by high quality collateral. Our home-equity loan-backed security portfolio decreased in value during the quarter due to repayments of principal.

Commercial Mortgage-Backed Securities (CMBS) The following table details the credit quality rating and fair value of our CMBSs, along with a comparison of the fair value at June 30, 2018, to our original investment value (adjusted for returns of principal, amortization, and write-downs):

Commercial Mortgage-Backed Securities (at June 30, 2018)

| Rating ¹ | Multi-Borrower | Single-Borrower | Total | % of Total | |
|---------------------------------|----------------|-----------------|-----------|------------|---|
| AAA | \$ 242.8 | \$ 481.2 | \$724.0 | 26.9 | % |
| AA | 34.2 | 630.4 | 664.6 | 24.6 | |
| A | 0 | 464.4 | 464.4 | 17.2 | |
| BBB | 0 | 631.9 | 631.9 | 23.4 | |
| Non-investment grade/non-rated: | | | | | |
| BB | 14.4 | 168.2 | 182.6 | 6.8 | |
| B | 0.8 | 28.6 | 29.4 | 1.1 | |
| Total fair value | \$ 292.2 | \$ 2,404.7 | \$2,696.9 | 100.0 | % |
| Increase (decrease) in value | (0.1)% | (1.2)% | (1.0)% | | |

¹The credit quality ratings in the table above are assigned by NRSROs; when we assign the NAIC ratings for our CMBSs, \$180.4 million of our non-investment-grade securities are rated investment-grade and classified as Group II and \$31.6 million, or 1.2% of our total CMBSs, are not rated by the NAIC and are classified as Group I.

During the quarter, we continued to focus on single-borrower CMBS, which represented 89.2% of the portfolio at June 30, 2018, because we believed these transactions provided an opportunity to select investments based on real estate and underwriting criteria that fit our preferred credit risk and duration profile. Our multi-borrower, fixed-rate CMBS portfolio is concentrated in vintages with conservative underwriting. During the quarter, we increased our CMBS bond portfolio by \$435.7 million on a cost basis. We increased the duration in our CMBS portfolio from 2.4 to 2.7 years during the quarter as new issue fixed-rate securities were added. The average credit quality was A+ at June 30, 2018, compared to A at March 31, 2018.

MUNICIPAL SECURITIES

Included in the fixed-income portfolio at June 30, 2018 and 2017, and December 31, 2017, were \$1,667.3 million, \$2,500.1 million, and \$2,297.1 million, respectively, of state and local government obligations. These securities had a duration of 2.7 years at June 30, 2018, compared to 2.9 years at June 30, 2017 and 2.7 years at December 31, 2017; the weighted average credit quality rating (excluding the benefit of credit support from bond insurance) was AA for all three periods. These securities had net unrealized losses of \$11.6 million at June 30, 2018, compared to net unrealized gains of \$26.6 million at June 30, 2017 and \$11.4 million at December 31, 2017.

The following table details the credit quality rating of our municipal securities at June 30, 2018, without the benefit of credit or bond insurance:

Municipal Securities (at June 30, 2018)

| (millions) Rating | General Obligations | Revenue Bonds | Total |
|-------------------|---------------------|---------------|---------|
| AAA | \$ 228.4 | \$395.8 | \$624.2 |
| AA | 352.9 | 558.1 | 911.0 |
| A | 1.0 | 98.4 | 99.4 |
| BBB | 29.9 | 2.8 | 32.7 |

Total \$ 612.2 \$1,055.1 \$1,667.3

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Included in revenue bonds were \$786.3 million of single family housing revenue bonds issued by state housing finance agencies, of which \$562.4 million were supported by individual mortgages held by the state housing finance agencies and \$223.9 million were supported by mortgage-backed securities. Of the programs supported by mortgage-backed securities, approximately 25% were collateralized by Fannie Mae and Freddie Mac mortgages; the remaining 75% were collateralized by Ginnie Mae loans, which are fully guaranteed by the U.S. government. Of the programs supported by individual mortgages held by the state housing finance agencies, the weighted average credit quality rating was AA+. Most of these mortgages were supported by FHA, VA, or private mortgage insurance providers.

We reduced our holdings of tax-exempt municipal bonds during 2018, with the majority of the sales occurring during the first quarter. The new corporate tax rate we use to value our tax-exempt holdings rendered these bonds less attractive relative to alternative taxable investments. At current valuations, we expect to hold the majority of our housing bonds and bonds we hold for premium tax abatement purposes, in addition to other bonds that for credit or structural reasons we still find attractive.

CORPORATE SECURITIES

Included in our fixed-income securities at June 30, 2018 and 2017, and December 31, 2017, were \$7,330.3 million, \$5,013.8 million, and \$4,997.7 million, respectively, of corporate securities. These securities had a duration of 3.3 years at June 30, 2018, compared to 2.4 years at June 30, 2017 and 2.6 years at December 31, 2017, and a weighted average credit quality rating of BBB for all three periods. These securities had net unrealized losses of \$90.1 million at June 30, 2018, compared to net unrealized gains of \$21.8 million at June 30, 2017 and \$0.4 million at December 31, 2017.

Our allocation to corporate bonds increased during the second quarter as we took advantage of market volatility to add to the portfolio and increase duration at attractive levels.

The table below shows the exposure break-down by sector and rating:

Corporate Securities (at June 30, 2018)

| (millions) Rating | Consumer | Industrial | Communication | Financial Services | Agency | Technology | Basic Materials | Energy | Total |
|------------------------------------|------------|------------|---------------|-----------------------|--------|------------|--------------------|----------|------------|
| AAA | \$ 0 | \$ 0 | \$ 0 | \$50.1 | \$ 0.5 | \$ 0 | \$ 0 | \$ 0 | \$50.6 |
| AA | 0 | 0 | 0 | 237.7 | 1.2 | 0.1 | 0 | 27.4 | 266.4 |
| A | 282.5 | 222.5 | 42.7 | 504.6 | 0 | 2.2 | 31.2 | 9.7 | 1,095.4 |
| BBB | 2,361.4 | 904.1 | 361.5 | 684.2 | 0 | 635.6 | 53.4 | 207.9 | 5,208.1 |
| Non-investment grade/non-rated: | | | | | | | | | |
| BB | 23.5 | 117.2 | 98.1 | 14.8 | 0 | 100.9 | 27.7 | 25.5 | 407.7 |
| B | 105.5 | 79.1 | 40.4 | 46.3 | 0 | 9.5 | 17.2 | 4.1 | 302.1 |
| Total fair value | \$ 2,772.9 | \$ 1,322.9 | \$ 542.7 | \$ 1,537.7 | \$ 1.7 | \$ 748.3 | \$ 129.5 | \$ 274.6 | \$ 7,330.3 |

At June 30, 2018, we held \$1,496.2 million of U.S. dollar-denominated corporate bonds issued by companies that are domiciled, or whose parent companies are domiciled, in the U.K. (\$260.5 million) and other European countries (\$1,235.7 million), primarily in the consumer, financial, and industrial industries.

PREFERRED STOCKS – REDEEMABLE AND NONREDEEMABLE

We hold both redeemable (i.e., mandatory redemption dates) and nonredeemable (i.e., perpetual with call dates) preferred stocks. At June 30, 2018, we held \$229.1 million in redeemable preferred stocks and \$758.6 million in nonredeemable preferred stocks, compared to \$206.7 million and \$783.1 million, respectively, at June 30, 2017, and \$211.0 million and \$803.8 million at December 31, 2017. At June 30, 2018, our preferred stock portfolio had net unrealized gains of \$12.1 million and net holding period gains of \$78.2 million recorded as part of net realized gains (losses), compared to \$134.4 million and \$121.5 million of net unrealized gains at June 30, 2017 and December 31, 2017, respectively.

Our preferred stock securities had a small positive return in the second quarter of 2018 as their high level of income was able to offset declines in prices due to higher rates and wider spreads. Changes in the corporate tax rate have made other sectors more attractive relative to preferreds. In combination with that, spreads are still somewhat tight on a longer-term basis. With slightly wider spreads and growth in the overall fixed-income portfolio, we added to a few positions during the quarter to keep our allocation relatively steady at this lower level.

Our preferred stock portfolio had a duration of 2.9 years at June 30, 2018, compared to 2.8 years at June 30, 2017, and 2.9 years at December 31, 2017. The majority of our preferred securities have fixed-rate dividends until a call date and then, if not called, convert to floating-rate dividends. The interest rate duration of our preferred securities is calculated to reflect the call, floor, and floating-rate features. Although a preferred security will remain outstanding if not called, its interest rate duration will reflect the variable nature of the dividend. The overall credit quality rating was BBB- for all three periods. Our non-investment-grade preferred stocks were primarily with issuers that maintain investment-grade senior debt ratings.

The table below shows the exposure break-down by sector and rating at quarter end:

Preferred Stocks (at June 30, 2018)

| (millions) Rating | Financial Services | | | | | | Total |
|---------------------------------|--------------------|---------------|-----------|---------|-------------|-----------|---------|
| | U.S. Banks | Foreign Banks | Insurance | Other | Industrials | Utilities | |
| A | \$56.4 | \$ 0 | \$ 0 | \$10.1 | \$ 0 | \$ 0 | \$66.5 |
| BBB | 388.7 | 0 | 65.6 | 54.8 | 116.0 | 4.6 | 629.7 |
| Non-investment grade/non-rated: | | | | | | | |
| BB | 158.8 | 5.1 | 42.7 | 0 | 40.8 | 0 | 247.4 |
| B | 0 | 0 | 0 | 39.1 | 0 | 0 | 39.1 |
| Non-rated | 0 | 0 | 0 | 0 | 5.0 | 0 | 5.0 |
| Total fair value | \$603.9 | \$ 5.1 | \$ 108.3 | \$104.0 | \$ 161.8 | \$ 4.6 | \$987.7 |

We also face the risk that dividend payments on our preferred stock holdings could be deferred for one or more periods or skipped entirely. As of June 30, 2018, all of our preferred securities continued to pay their dividends in full and on time. Approximately 80% of our preferred stock securities pay dividends that have tax preferential characteristics, while the balance pay dividends that are fully taxable.

At June 30, 2018, we held \$102.6 million of U.S. dollar-denominated preferred stocks (\$5.1 million nonredeemable and \$97.5 million redeemable) issued by financial institutions that are domiciled, or whose parent companies are domiciled, in foreign countries.

Common Equities

Common equities, as reported on the balance sheets, were comprised of the following:

| (\$ in millions) | June 30, 2018 | | June 30, 2017 | | December 31, 2017 | |
|------------------------|---------------|--------|---------------|--------|-------------------|--------|
| Indexed common stocks | \$2,985.7 | 95.0 % | \$2,931.5 | 95.3 % | \$3,248.4 | 95.6 % |
| Managed common stocks | 156.2 | 5.0 | 145.7 | 4.7 | 151.1 | 4.4 |
| Total common stocks | 3,141.9 | 100.0 | 3,077.2 | 100.0 | 3,399.5 | 100.0 |
| Other risk investments | 0.3 | 0 | 0.3 | 0 | 0.3 | 0 |
| Total common equities | \$3,142.2 | 100.0% | \$3,077.5 | 100.0% | \$3,399.8 | 100.0% |

In our indexed common stock portfolio, our individual holdings are selected based on their contribution to the correlation with the index. For all three periods reported in the table above, the GAAP basis total return was within the desired tracking error of +/- 50 basis points when compared to the Russell 1000 Index. We held 816 out of 988, or 83%, of the common stocks comprising the Russell 1000 Index at June 30, 2018, which made up 93% of the total market capitalization of the index.

We reduced our exposure to common equities during the first quarter of 2018 by approximately 10% by selling securities in our indexed common stock portfolio and re-allocating the funds to our fixed-maturity portfolio.

The actively managed common stock portfolio is managed by one external investment manager. At June 30, 2018, the fair value of the actively managed portfolio was \$156.2 million, compared to an adjusted cost basis of \$123.1 million.

Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995: Investors are cautioned that certain statements in this report not based upon historical fact are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements often use words such as “estimate,” “expect,” “intend,” “plan,” “believe,” and other words and terms of similar meaning, or are tied to future periods, in connection with a discussion of future operating or financial performance. Forward-looking statements are based on current expectations and projections about future events, and are subject to certain risks, assumptions and uncertainties that could cause actual events and results to differ materially from those discussed herein. These risks and uncertainties include, without limitation, uncertainties related to estimates, assumptions, and projections generally; inflation and changes in general economic conditions (including changes in interest rates and financial markets); the possible failure of one or more governmental, corporate, or other entities to make scheduled debt payments or satisfy other obligations; our ability to access capital markets and financing arrangements when needed to support growth or other capital needs, and the favorable evaluations by credit and other rating agencies on which this access depends; the potential or actual downgrading by one or more rating agencies of our securities or governmental, corporate, or other securities we hold; the financial condition of, and other issues relating to the strength of and liquidity available to, issuers of securities held in our investment portfolios and other companies with which we have ongoing business relationships, including reinsurers and other counterparties to certain financial transactions or under certain government programs; the accuracy and adequacy of our pricing, loss reserving, and claims methodologies; the competitiveness of our pricing and the effectiveness of our initiatives to attract and retain more customers; initiatives by competitors and the effectiveness of our response; our ability to obtain regulatory approval for the introduction of products to new jurisdictions, for requested rate changes and the timing thereof and for any proposed acquisitions; the effectiveness of our brand strategy and advertising campaigns relative to those of competitors; legislative and regulatory developments at the state and federal levels, including, but not limited to, matters relating to vehicle and homeowners insurance, health care reform and tax law changes; the outcome of disputes relating to intellectual property rights; the outcome of litigation or governmental investigations that may be pending or filed against us; severe weather conditions and other catastrophe events; the effectiveness of our reinsurance programs; changes in vehicle usage and driving patterns, which may be influenced by oil and gas prices, changes in residential occupancy patterns, and the effects of the emerging “sharing economy”; advancements in vehicle or home technology or safety features, such as accident and loss prevention technologies or the development of autonomous or partially autonomous vehicles; our ability to accurately recognize and appropriately respond in a timely manner to changes in loss frequency and severity trends; technological advances; acts of war and terrorist activities; our ability to maintain the uninterrupted operation of our facilities, systems (including information technology systems), and business functions, and safeguard personal and sensitive information in our possession, whether from cyber-attacks, other technology events or other means; our continued access to and functionality of third-party systems that are critical to our business; our continued ability to access cash accounts and/or convert securities into cash on favorable terms when we desire to do so; restrictions on our subsidiaries’ ability to pay dividends to The Progressive Corporation; possible impairment of our goodwill or intangible assets if future results do not adequately support either, or both, of these items; court decisions, new theories of insurer liability or interpretations of insurance policy provisions and other trends in litigation; changes in health care and auto and property repair costs; and other matters described from time to time in our releases and publications, and in our periodic reports and other documents filed with the United States Securities and Exchange Commission. In addition, investors should be aware that generally accepted accounting principles prescribe when a company may reserve for particular risks, including litigation exposures. Accordingly, results for a given reporting period could be significantly affected if and when a reserve is established for one or more contingencies. Also, our regular reserve reviews may result in adjustments of varying magnitude as additional information regarding claims activity becomes known. Reported results, therefore, may be volatile in certain accounting periods.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

The duration of the financial instruments held in our portfolio that are subject to interest rate risk was 2.6 years at June 30, 2018 and 2.5 years at December 31, 2017. The weighted average beta of the equity portfolio was 1.00 at June 30, 2018, compared to 1.05 at December 31, 2017. Although components of the portfolio have changed, no material changes have occurred in the total interest rate or market risk when compared to the tabular presentations of our interest rate and market risk sensitive instruments in our Annual Report on Form 10-K for the year ended December 31, 2017.

Item 4. Controls and Procedures.

Progressive, under the direction of our Chief Executive Officer and our Chief Financial Officer, has established disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. The disclosure controls and procedures are also intended to ensure that such information is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

Our Chief Executive Officer and our Chief Financial Officer reviewed and evaluated Progressive's disclosure controls and procedures as of the end of the period covered by this report. Based on that review and evaluation, the Chief Executive Officer and Chief Financial Officer concluded that Progressive's disclosure controls and procedures are effectively serving the stated purposes as of the end of the period covered by this report.

We are not aware of any material change in Progressive's internal control over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II—OTHER INFORMATION

Item 1A. Risk Factors.

The risk factors affecting our business are discussed in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2017. There have been no material changes in the risk factors that were discussed in that report.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

(c) Share Repurchases

ISSUER PURCHASES OF EQUITY SECURITIES

| 2018 Calendar Month | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares That May Yet be Purchased Under the Plans or Programs |
|-----------------------------|---|---------------------------------------|---|---|
| April | 1,861 | \$ 60.22 | 1,523,523 | 23,476,477 |
| May - prior authorization | 30,467 | 60.23 | 1,553,990 | — |
| May - current authorization | 435 | 60.10 | 435 | 24,999,565 |
| June | 3,676 | 62.33 | 4,111 | 24,995,889 |
| Total | 36,439 | \$ 60.44 | | |

On May 16, 2018, the Company publicly announced that its Board of Directors renewed the authorization for the Company to repurchase up to 25 million of its common shares. This authorization, which does not have an expiration date, terminated the 23,446,010 shares that remained under the Board's prior authorization to repurchase 25 million common shares, which was originally announced on May 12, 2017.

Share repurchases under this authorization may be accomplished through open market purchases, through privately negotiated transactions, pursuant to our equity incentive plans, or otherwise, and may include trading plans entered into with one or more brokerage firms in accordance with Rule 10b5-1 under the Securities Exchange Act of 1934. During the second quarter 2018, all repurchases were accomplished in conjunction with our incentive compensation plans at the then-current market prices; there were no open market purchases during the quarter. Progressive's financial policies state that we will repurchase shares to neutralize dilution from equity-based compensation in the year of issuance and as an option to effectively use underleveraged capital.

Item 5. Other Information.

I. OTHER

President and CEO Susan Patricia Griffith's letter to shareholders with respect to our second quarter 2018 results is included as Exhibit 99 to this Quarterly Report on Form 10-Q. The letter is also posted on Progressive's website at progressive.com/annualreport.

Item 6. Exhibits.

See exhibit index on page 61.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

THE PROGRESSIVE CORPORATION
(Registrant)

Date: July 31, 2018 By: /s/ John P. Sauerland
John P. Sauerland
Vice President and Chief Financial Officer

EXHIBIT INDEX

| Exhibit No. Under Reg. S-K, Item 601 | Form 10-Q Exhibit Number | Description of Exhibit | If Incorporated by Reference, Documents with Which Exhibit was Previously Filed with SEC |
|--------------------------------------|--------------------------|--|--|
| 10 | 10 | <u>Executive Deferred Compensation (2018 Amendment and Restatement)</u> | Filed herewith |
| 31 | 31.1 | <u>Rule 13a-14(a)/15d-14(a) Certification of the Principal Executive Officer, Susan Patricia Griffith</u> | Filed herewith |
| 31 | 31.2 | <u>Rule 13a-14(a)/15d-14(a) Certification of the Principal Financial Officer, John P. Sauerland</u> | Filed herewith |
| 32 | 32.1 | <u>Section 1350 Certification of the Principal Executive Officer, Susan Patricia Griffith</u> | Furnished herewith |
| 32 | 32.2 | <u>Section 1350 Certification of the Principal Financial Officer, John P. Sauerland</u> | Furnished herewith |
| 99 | 99 | <u>Letter to Shareholders from Susan Patricia Griffith, President and Chief Executive Officer (Regulation FD Disclosure)</u> | Furnished herewith |
| 101 | 101.INS | XBRL Instance Document | Filed herewith |
| 101 | 101.SCH | XBRL Taxonomy Extension Schema Document | Filed herewith |
| 101 | 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | Filed herewith |
| 101 | 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document | Filed herewith |
| 101 | 101.LAB | XBRL Taxonomy Extension Label Linkbase Document | Filed herewith |
| 101 | 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | Filed herewith |