

HANOVER INSURANCE GROUP, INC.
Form 10-Q
August 03, 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 1-13754

THE HANOVER INSURANCE GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware 04-3263626
(State or other jurisdiction of (I.R.S. Employer

incorporation or organization) Identification No.)

440 Lincoln Street, Worcester, Massachusetts 01653

(Address of principal executive offices) (Zip Code)

(508) 855-1000

(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, a 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

The number of shares outstanding of the registrant's common stock was 42,535,767 as of July 31, 2018.

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PART I - FINANCIAL INFORMATION

ITEM 1 - FINANCIAL STATEMENTS

THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(In millions, except per share data)	Three Months		Six Months Ended	
	Ended June 30, 2018	2017	June 30, 2018	2017
Revenues				
Premiums	\$1,272.9	\$1,181.2	\$2,536.5	\$2,362.5
Net investment income	78.7	72.3	161.6	143.4
Net realized and unrealized investment gains (losses):				
Net realized gains (losses) from sales and other	(0.4)	7.7	(0.1)	11.0
Net change in fair value of equity securities	6.0	—	(17.0)	—
Net other-than-temporary impairment losses on investments recognized in earnings	(1.9)	(1.8)	(2.6)	(3.2)
Total net realized and unrealized investment gains (losses)	3.7	5.9	(19.7)	7.8
Fees and other income	7.5	6.7	15.3	13.3
Total revenues	1,362.8	1,266.1	2,693.7	2,527.0
Losses and expenses				
Losses and loss adjustment expenses	783.6	725.0	1,569.4	1,491.5
Amortization of deferred acquisition costs	288.9	264.6	576.9	531.0
Interest expense	11.6	12.2	24.0	24.2
Other operating expenses	158.8	153.3	322.9	310.3
Total losses and expenses	1,242.9	1,155.1	2,493.2	2,357.0
Income before income taxes	119.9	111.0	200.5	170.0
Income tax expense (benefit):				
Current	17.3	4.9	37.5	38.8
Deferred	3.4	27.7	(4.0)	7.6
Total income tax expense	20.7	32.6	33.5	46.4
Income from continuing operations	99.2	78.4	167.0	123.6
Net gain from discontinued operations (net of tax benefit of \$0.1 for the six months ended June 30, 2018)	0.1	—	—	—
Net income	\$99.3	\$78.4	\$167.0	\$123.6
Earnings per common share:				
Basic:				
Income from continuing operations	\$2.33	\$1.85	\$3.93	\$2.91

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Net gain from discontinued operations	0.01	—	—	—
Net income per share	\$2.34	\$1.85	\$3.93	\$2.91
Weighted average shares outstanding	42.5	42.5	42.5	42.5
Diluted:				
Income from continuing operations	\$2.30	\$1.83	\$3.88	\$2.88
Net gain from discontinued operations	0.01	—	—	—
Net income per share	\$2.31	\$1.83	\$3.88	\$2.88
Weighted average shares outstanding	43.1	42.8	43.1	42.9

The accompanying notes are an integral part of these interim consolidated financial statements.

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THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

(In millions)	Three Months		Six Months	
	Ended June 30, 2018	2017	Ended June 30, 2018	2017
Net income	\$99.3	\$78.4	\$167.0	\$123.6
Other comprehensive income (loss), net of tax:				
Available-for-sale securities:				
Net (depreciation) appreciation during the period	(49.0)	19.4	(172.9)	38.3
Change in other-than-temporary impairment losses				
recognized in other comprehensive income (loss)	(0.1)	0.4	0.3	0.5
Total available-for-sale securities	(49.1)	19.8	(172.6)	38.8
Pension and postretirement benefits:				
Net change in net actuarial loss and prior service cost	0.9	2.4	(1.4)	4.7
Cumulative foreign currency translation adjustment:				
Amount recognized as cumulative foreign currency				
translation during the period	(0.5)	(4.5)	(1.0)	0.6
Total other comprehensive (loss) income, net of tax	(48.7)	17.7	(175.0)	44.1
Comprehensive income (loss)	\$50.6	\$96.1	\$(8.0)	\$167.7

The accompanying notes are an integral part of these interim consolidated financial statements.

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THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(In millions, except share data)	June 30, 2018	December 31, 2017
Assets		
Investments:		
Fixed maturities, at fair value (amortized cost of \$7,847.8 and \$7,688.8)	\$7,729.9	\$7,779.7
Equity securities, at fair value	554.0	576.5
Other investments	736.8	685.5
Total investments	9,020.7	9,041.7
Cash and cash equivalents	244.9	376.4
Accrued investment income	62.7	62.7
Premiums and accounts receivable, net	1,773.4	1,567.6
Reinsurance recoverable on paid and unpaid losses and unearned premiums	2,832.3	3,057.0
Deferred acquisition costs	564.5	550.2
Deferred income taxes	71.2	29.2
Goodwill	192.1	192.6
Other assets	539.2	504.2
Assets of discontinued operations	102.6	88.0
Total assets	\$15,403.6	\$15,469.6
Liabilities		
Loss and loss adjustment expense reserves	\$7,506.4	\$7,745.0
Unearned premiums	2,958.5	2,763.6
Expenses and taxes payable	643.3	716.2
Reinsurance premiums payable	452.9	344.8
Debt	787.1	786.9
Liabilities of discontinued operations	115.6	115.4
Total liabilities	\$12,463.8	12,471.9
Commitments and contingencies		
Shareholders' Equity		
Preferred stock, par value \$0.01 per share; 20.0 million shares authorized; none issued	—	—
Common stock, par value \$0.01 per share; 300.0 million shares authorized;		
60.5 million shares issued	0.6	0.6
Additional paid-in capital	1,864.2	1,857.0
Accumulated other comprehensive income (loss)	(169.1)	107.6
Retained earnings	2,200.4	1,975.0
Treasury stock at cost (18.0 million shares)	(956.3)	(942.5)
Total shareholders' equity	2,939.8	2,997.7
Total liabilities and shareholders' equity	\$15,403.6	\$15,469.6

The accompanying notes are an integral part of these interim consolidated financial statements.

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THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (UNAUDITED)

(In millions)	Six Months Ended June 30,	
	2018	2017
Preferred Stock		
Balance at beginning and end of period	\$—	\$—
Common Stock		
Balance at beginning and end of period	0.6	0.6
Additional Paid-in Capital		
Balance at beginning of period	1,857.0	1,846.7
Employee and director stock-based awards and other	7.2	5.3
Balance at end of period	1,864.2	1,852.0
Accumulated Other Comprehensive Income (Loss), net of tax		
Net Unrealized Appreciation (Depreciation) on Investments:		
Balance at beginning of period	205.4	186.0
Net appreciation (depreciation) on available-for-sale securities	(172.6)	38.8
Adoption of Accounting Standards Update 2016-01 and 2018-02	(81.6)	—
Balance at end of period	(48.8)	224.8
Defined Benefit Pension and Postretirement Plans:		
Balance at beginning of period	(79.5)	(102.5)
Net change in net actuarial loss and prior service cost	(1.4)	4.7
Adoption of Accounting Standards Update 2018-02	(16.2)	—
Balance at end of period	(97.1)	(97.8)
Cumulative Foreign Currency Translation Adjustment:		
Balance at beginning of period	(18.3)	(20.7)
Amount recognized as cumulative foreign currency translation during the period	(1.0)	0.6
Adoption of Accounting Standards Update 2018-02	(3.9)	—
Balance at end of period	(23.2)	(20.1)
Total accumulated other comprehensive income (loss)	(169.1)	106.9
Retained Earnings		
Balance at beginning of period	1,975.0	1,875.6
Cumulative effect of accounting change, net of taxes	104.3	—
Balance at beginning of period, as adjusted	2,079.3	1,875.6
Net income	167.0	123.6
Dividends to shareholders	(45.9)	(42.6)
Balance at end of period	2,200.4	1,956.6
Treasury Stock		
Balance at beginning of period	(942.5)	(928.2)
Shares purchased at cost	(25.3)	(28.0)
Net shares reissued at cost under employee stock-based compensation plans	11.5	12.6
Balance at end of period	(956.3)	(943.6)
Total shareholders' equity	\$2,939.8	\$2,972.5

The accompanying notes are an integral part of these interim consolidated financial statements.

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THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(In millions)	Six Months Ended June 30, 2018	2017
Cash Flows From Operating Activities		
Net income	\$ 167.0	\$ 123.6
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized and unrealized investment losses (gains)	19.4	(7.8)
Net amortization and depreciation	14.1	15.4
Stock-based compensation expense	7.6	7.3
Amortization of defined benefit plan costs	4.8	7.0
Deferred income tax (benefit) expense	(4.0)	7.6
Change in deferred acquisition costs	(14.3)	(29.6)
Change in premiums receivable, net of reinsurance premiums payable	(100.6)	(73.8)
Change in loss, loss adjustment expense and unearned premium reserves	249.3	384.7
Change in reinsurance recoverable	(53.3)	(72.7)
Change in expenses and taxes payable	(62.4)	(74.1)
Other, net	(48.1)	(37.8)
Net cash provided by operating activities	179.5	249.8

Cash Flows From Investing Activities		
Proceeds from disposals and maturities of fixed maturities	637.8	578.8
Proceeds from disposals of equity securities and other investments	51.2	65.8
Purchase of fixed maturities	(822.6)	(668.4)
Purchase of equity securities and other investments	(92.8)	(113.5)
Capital expenditures	(7.8)	(8.6)
Net cash used in investing activities	(234.2)	(145.9)
Cash Flows From Financing Activities		
Proceeds from exercise of employee stock options	11.1	10.3
Change in cash collateral related to securities lending program	(12.7)	(3.4)
Dividends paid to shareholders		