



# Mercury General (MCY)

Updated August 18<sup>th</sup>, 2020 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$45	<b>5 Year CAGR Estimate:</b>	12.8%	<b>Market Cap:</b>	\$2.5B
<b>Fair Value Price:</b>	\$65	<b>5 Year Growth Estimate:</b>	1.5%	<b>Ex-Dividend Date:</b>	09/14/20
<b>% Fair Value:</b>	70%	<b>5 Year Valuation Multiple Estimate:</b>	7.5%	<b>Dividend Payment Date:</b>	09/29/20
<b>Dividend Yield:</b>	5.6%	<b>5 Year Price Target</b>	\$69	<b>Years Of Dividend Growth:</b>	32
<b>Dividend Risk Score:</b>	C	<b>Retirement Suitability Score:</b>	B	<b>Last Dividend Increase:</b>	0.4%

## Overview & Current Events

Mercury General is an insurance company that is active in the following businesses: automobile, homeowners, renters & business insurance. Mercury was founded more than 50 years ago, in 1961. Personal automobile insurance is the most important business unit for Mercury General. The company is active in eleven states, with California being the most important market. Insurance is primarily sold through about 10,000 independent agents.

Mercury General reported its second quarter earnings results on August 4. The company reported net premiums earned of \$812 million, which was 13% less than Mercury's net earned premiums during the previous year's quarter. Net premiums written declined 13% year over year, to \$818 million. The fact that net written premiums were down year over year will likely mean that earned premiums will remain under pressure during the back half of the year. Mercury General's investment income improved by a lot from the first quarter's level, as the losses that were caused by the Q1 equity market selloff were reverted. Net investment income totaled \$34 million during the second quarter, which was on par with the previous year's level. Net realized investment gains stood at a very strong level of \$158 million.

Mercury General's adjusted earnings-per-share totaled \$1.86 during the second quarter, beating the analyst consensus estimate easily. The adjusted result already backs out one-time accounting gains during the quarter. The coronavirus does not have a meaningful impact on Mercury General's profitability so far. Thanks to a very strong first half of 2020, the outlook for fiscal 2020 is quite positive, and Mercury General will likely exceed 2019's profits this year.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>EPS</b>	\$2.09	\$2.79	\$2.13	\$2.18	\$2.28	\$2.34	\$1.73	\$1.64	\$1.80	\$2.60	<b>\$4.30</b>	<b>\$4.63</b>
<b>DPS</b>	\$2.37	\$2.41	\$2.44	\$2.45	\$2.46	\$2.47	\$2.48	\$2.49	\$2.50	\$2.51	<b>\$2.52</b>	<b>\$2.57</b>
<b>Shares<sup>1</sup></b>	54.8	54.9	54.9	55.0	55.1	55.2	55.3	55.3	55.3	55.3	<b>55.3</b>	<b>55.3</b>

Mercury's growth history is relatively weak. From 2009 to 2018 the company's earnings-per-share declined. 2016 and 2017 were two especially harsh years, primarily due to unusually high costs for catastrophes such as the California wildfires during the summer of 2017. During 2019 Mercury's earnings-per-share have recovered, however, due to lower catastrophe losses, but profits remained below the level that was hit in 2011, almost a decade earlier.

Following a solid 2019, analysts are forecasting an even better 2020, despite the current pandemic. Normalizing catastrophe losses, which were unusually high over the last couple of years, should be a tailwind for Mercury going forward. Analysts are not forecasting a major negative impact from the coronavirus crisis on Mercury's operations, apart from the accounting loss during the first quarter, which was reverted in Q2.

In the future, the company should be able to grow its profits slightly, we believe, although there likely will be big swings on a year-over-year basis, as there have been major changes in its profitability in the past. These cyclical results, caused by one-time impacts such as wildfires, are not unusual for insurance companies with a regional focus, and they are something investors have to live with when they want to invest into Mercury General.

<sup>1</sup> In Millions

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



# Mercury General (MCY)

Updated August 18<sup>th</sup>, 2020 by Jonathan Weber

## Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	20.1	14.5	19.6	20.1	21.5	23.1	30.8	35.0	28.9	18.8	10.5	15.0
Avg. Yld.	5.6%	6.0%	5.8%	5.6%	5.0%	4.6%	4.7%	4.4%	5.1%	5.1%	5.6%	3.7%

Mercury General's shares traded at quite high valuations throughout the last couple of years, with the company's price-to-earnings ratio being above 20 between 2013 and 2018. This was mostly due to the below-average profitability during those years. Based on current earnings forecasts for 2020, Mercury's shares are quite attractively valued.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	113%	86.4%	115%	112%	108%	106%	143%	152%	139%	96.5%	58.6%	55.5%

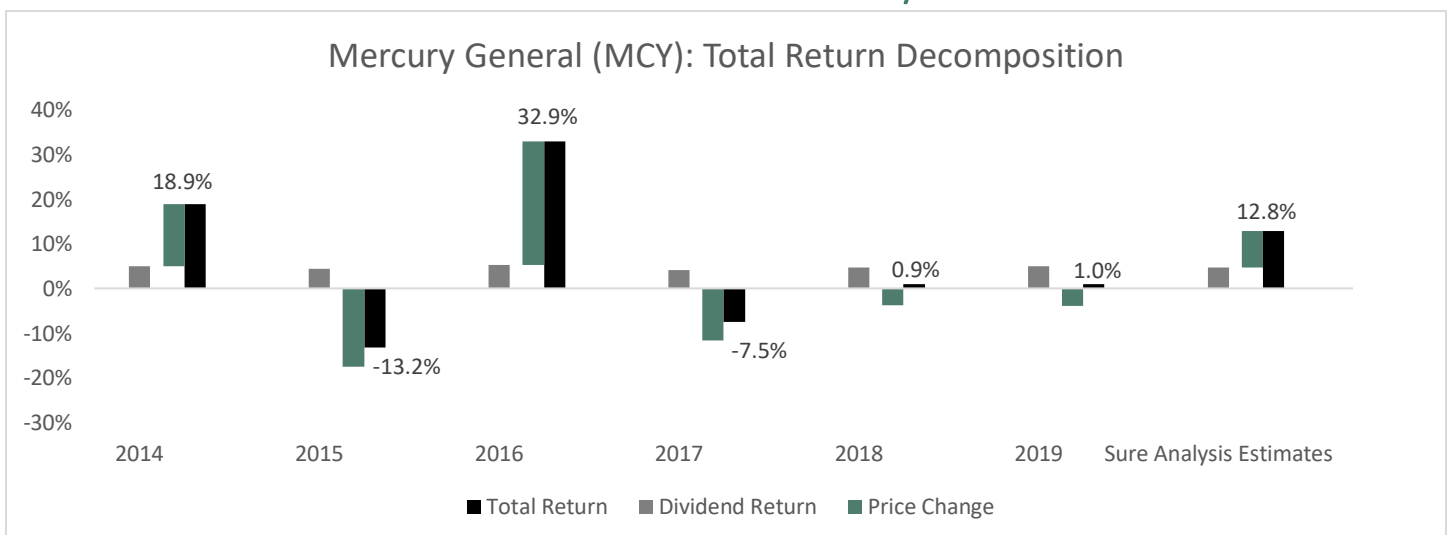
Mercury General has paid out more than 100% of its reported net earnings throughout most of the last decade. The company nevertheless managed to increase its dividend payout throughout the years, although the dividend growth rate was quite low in recent years, at less than 1% annually. Mercury General has been able to finance its dividend thanks to cash flows that are higher than the net profits that the company generates.

During the last financial crisis Mercury remained profitable, which can be explained by two key factors. First, even during times when the economy is weak, people still need insurance for their cars, property, and other belongings. Demand for Mercury's offerings is thus not overly dependent upon the economy. Second, Mercury did not invest in high-risk assets prior to the financial crisis, and therefore was able to avoid the huge losses many other financial corporations had to report. Mercury overall is recession-proof which is a plus during the current economic downturn, the company is significantly more impacted by catastrophes that affect its operations directly, such as 2017's huge California wildfires.

## Final Thoughts & Recommendation

Unlike most of its peers from the financial industry, Mercury General was relatively resilient during the last financial crisis. Mercury General's earnings growth has been very inconsistent, though, and even though analysts are forecasting a major earnings increase for 2020, unforeseen events such as wildfires or earthquakes can always lead to volatility. Due to the undervaluation and strong forecasted returns, we rate Mercury General a buy at the current level.

## Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



# Mercury General (MCY)

Updated August 18<sup>th</sup>, 2020 by Jonathan Weber

## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	2,776	2,777	2,783	2,821	3,012	3,009	3,228	3,416	3,380	3,973
D&A Exp.	41	41	37	31	28	48	53	55	59	65
Net Profit	152	191	117	112	178	74	73	145	(6)	320
Net Margin	5.5%	6.9%	4.2%	4.0%	5.9%	2.5%	2.3%	4.2%	-0.2%	8.1%
Free Cash Flow	63	140	133	191	220	170	275	322	355	
Income Tax	30	54	18	20	69	(4)	(2)	22	(25)	58

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	4,203	4,070	4,190	4,315	4,600	4,629	4,789	5,101	5,434	5,889
Cash & Equivalents	181	211	158	267	290	264	220	291	314	294
Accounts Receivable	281	289	345	366	390	437	472	530	776	684
Goodwill & Int. Ass.	103	97	90	84	78	74	68	64	58	53
Total Liabilities	2,409	2,213	2,347	2,493	2,725	2,808	3,036	3,340	3,816	4,090
Accounts Payable	107	95	96	128	131	123	112	108	115	143
Long-Term Debt	267	140	140	190	290	290	320	371	372	372
Shareholder's Equity	1,795	1,857	1,842	1,822	1,875	1,821	1,752	1,761	1,618	1,800
D/E Ratio	0.15	0.08	0.08	0.10	0.15	0.16	0.18	0.21	0.23	0.21

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	3.6%	4.6%	2.8%	2.6%	4.0%	1.6%	1.6%	2.9%	-0.1%	5.7%
Return on Equity	8.5%	10.5%	6.3%	6.1%	9.6%	4.0%	4.1%	8.2%	-0.3%	18.7%
ROIC	7.4%	9.4%	5.9%	5.6%	8.5%	3.5%	3.5%	6.9%	-0.3%	15.4%
Shares Out.	54.8	54.9	54.9	55.0	55.1	55.2	55.3	55.3	55.3	55.3
Revenue/Share	50.63	50.64	50.68	51.33	54.74	54.51	58.36	61.74	61.08	71.76
FCF/Share	1.15	2.56	2.42	3.48	4.01	3.08	4.97	5.82	6.42	

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

### Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.