



The Progressive Corporation (PGR)

Updated July 17th, 2021 by Nikolaos Sismanis

Key Metrics

| | | | | | |
|-----------------------------|------|--|-------|----------------------------------|-------------------------|
| Current Price: | \$96 | 5 Year CAGR Estimate: | 14.5% | Market Cap: | \$56.2 B |
| Fair Value Price: | \$96 | 5 Year Growth Estimate: | 10.0% | Ex-Dividend Date: | 10/06/2021 ¹ |
| % Fair Value: | 100% | 5 Year Valuation Multiple Estimate: | 0.0% | Dividend Payment Date: | 10/15/2021 |
| Dividend Yield: | 5.1% | 5 Year Price Target | \$155 | Years Of Dividend Growth: | 4 |
| Dividend Risk Score: | D | Retirement Suitability Score: | B | Last Dividend Increase: | 84.9% |

Overview & Current Events

Progressive, headquartered in Mayfield, Ohio, offers personal and commercial insurance throughout the United States. The company's Personal Lines segment writes insurance for personal autos, recreational and other vehicles. Its Commercial Lines business writes auto-related primary liability and physical damage insurance, and general liability and property insurance, primarily for small businesses. Finally, its Property business writes residential property insurance for homeowners, other property owners, and renters. The company generates around \$42 billion in annual revenues, and it based in Mayfield, Ohio.

On July 15th, 2021, Progressive reported its Q2-2021 results for the quarter ending June 30th, 2021. The company achieved record net premiums written of \$11.4 billion, a 13% increase year-over-year, while EPS came in at \$1.34, a 56% decline vs. Q2-2020. The increase in Progressive's premium was the result of higher net premiums and fees. However, the bottom line was compressed following the acquisition of Protective Insurance Corporation and its subsidiaries on June 1st.

Following this quarter's acquisition, we lower our FY2021 EPS estimate from \$11.00 to \$9.60. We have set our DPS expectations in line with last year's as the company's quarterly dividend has remained constant. Management's annual special dividend for the year could be more generous, though we remain prudent.

Growth on a Per-Share Basis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|----------------|
| EPS | \$1.61 | \$1.50 | \$1.95 | \$2.17 | \$2.16 | \$1.77 | \$2.74 | \$4.45 | \$6.75 | \$9.71 | \$9.60 | \$15.46 |
| DPS | \$0.41 | \$0.28 | \$0.49 | \$0.69 | \$0.89 | \$0.68 | \$1.12 | \$2.51 | \$2.65 | \$4.90 | \$4.90 | \$8.64 |
| Shares² | 637 | 608 | 604 | 595 | 589 | 585 | 586 | 587 | 587 | 588 | 586 | 550 |

Progressive is a best-of-breed insurer that has done a great job of capturing a substantial market share position in an industry known for its brutal competition. Its current market share of around 12% has grown significantly from around 9% three years ago, while through its recent acquisition it is likely to increase further. The company's expanded portfolio of insurance offerings not only contributes to diversification but also allows Progressive to cross-sell customers. Bundling is an old strategy, but it works great if you save clients' money. As a result, revenues have constantly been growing, while at the same time operating leverage and selling costs for existing customers are lower than acquiring a brand-new customer. The company's 5-year EPS and DPS growth rate have been north of 40%, although a good deal of that came from what may be a temporary boost from the pandemic in 2020. We estimate 10% growth from this point to reflect a reasonable slowdown in the medium term.

Our DPS forecast remains at 12%, as more rapid increases could be comfortably covered by EPS moving forward. Keep in mind that the company pays a small \$0.10 quarterly dividend and one large year-end dividend each year. This allows the

¹ Estimate.

² Share count is in millions.

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company to exhibit capital allocation flexibility, paying a much higher payment in good times or reducing the payment in lesser times.

Valuation Analysis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | Now | 2026 |
|------------------|------|------|------|------|------|------|------|------|------|------|-------------|-------------|
| Avg. P/E | 11.7 | 14.2 | 12.8 | 11.5 | 13.4 | 22.1 | 19.4 | 14.9 | 10.8 | 9.0 | 10.0 | 10.0 |
| Avg. Yld. | 2.2% | 1.3% | 2.0% | 2.8% | 3.1% | 1.7% | 2.1% | 3.8% | 3.6% | 5.6% | 5.1% | 5.6% |

Despite Progressive's solid profitability growth and dividend growth, the market has shown little appreciation for the stock over the years, attaching a humble valuation to it. The company is currently trading at around 10 times our expected EPS, lower than its historical average. We expect the P/E ratio to remain at these levels. The stock's high yield at the current ultra-low-rate environment could assist in a valuation expansion, though we remain conservative.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|---------------|------|------|------|------|------|------|------|------|------|------|------------|------------|
| Payout | 25% | 19% | 25% | 32% | 41% | 38% | 41% | 56% | 39% | 50% | 51% | 56% |

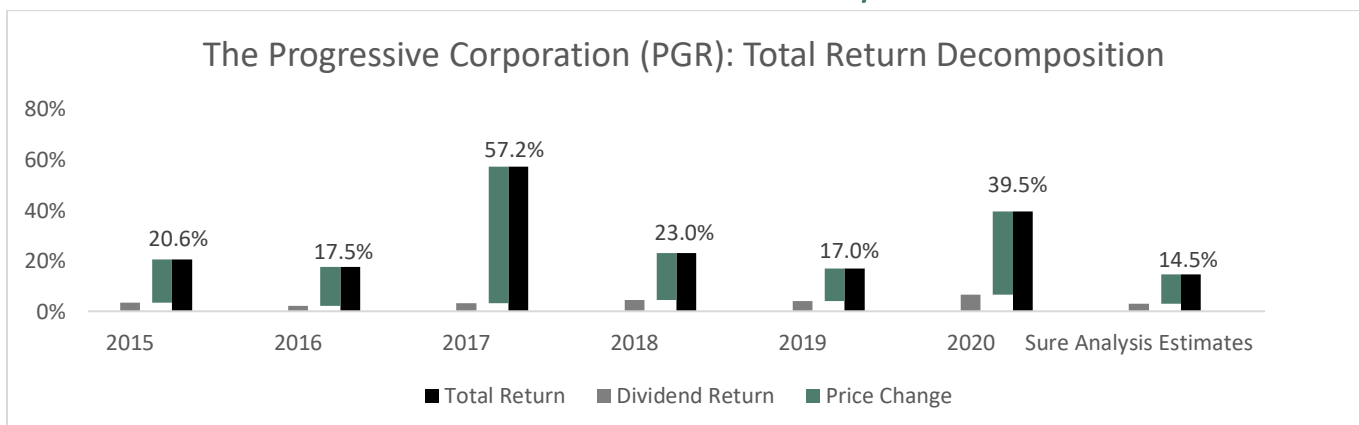
Progressive's current dividend payout should be quite safe, as the company retains around half of its net income, leaving a wide margin of error in the event of a temporary challenge. The company remains an industry-leader, while its financials are quite healthy, featuring a long-term debt/equity of just 30.3%. At the same time, however, we cannot ignore the fact the industry is highly competitive. In the future it could be massive disrupted by innovators such as the recently listed insurance disruptor Lemonade (LMND).

Another potential risk is small businesses possibly claiming that the pandemic has caused permanent interruption and therefore they must be covered by insurers. Despite commercial lines consisting of only 7.5% of Progressive's business, such a scenario could suppress its short-term profitability nonetheless. So far this has not been the case. Finally, a recession could significantly hurt the company's financials, as was the case during the Great Financials Crisis. Still, with its strong qualities the company should be able to recover quickly as proven over the past decade.

Final Thoughts & Recommendation

Progressive has managed to improve dramatically over the past few years. While Protective Insurance's acquisition may weigh slightly on this year's profitability, the company's growth story remains intact. We are forecasting 14.5% annualized returns, consisting of a 10% growth rate, 5.1% dividend yield, and constant valuation expectations. However, we do note that this thesis hinges on Progressive's growth being sustained. Shares earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|-----------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Revenue | 15,761 | 17,070 | 18,156 | 19,377 | 20,832 | 23,417 | 26,816 | 31,955 | 38,998 | 42,640 |
| D&A Exp. | 89 | 94 | 101 | 97 | 151 | 200 | 236 | 262 | 306 | 332 |
| Net Profit | 1,016 | 902 | 1,165 | 1,281 | 1,268 | 1,031 | 1,592 | 2,615 | 3,970 | 5,705 |
| Net Margin | 6.4% | 5.3% | 6.4% | 6.6% | 6.1% | 4.4% | 5.9% | 8.2% | 10.2% | 13.4% |
| Free Cash Flow | 1,419 | 1,564 | 1,760 | 1,618 | 2,162 | 2,518 | 3,601 | 6,019 | 5,898 | 6,682 |
| Income Tax | 472 | 415 | 555 | 626 | 611 | 414 | 541 | 543 | 1,180 | 1,469 |

Balance Sheet Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|-------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Total Assets | 21,845 | 22,695 | 24,408 | 25,788 | 29,819 | 33,428 | 38,701 | 46,575 | 54,895 | 64,100 |
| Cash & Equivalents | 156 | 179 | 75 | 108 | 224 | 212 | 265 | 70 | 226 | 77 |
| Acc. Receivable | 2,930 | 3,184 | 3,311 | 3,538 | 3,988 | 4,509 | 5,423 | 6,497 | 7,507 | 12,180 |
| Goodwill & Int. | --- | --- | --- | 13 | 943 | 882 | 819 | 747 | 681 | 624 |
| Total Liabilities | 16,038 | 16,688 | 18,219 | 18,859 | 22,530 | 25,470 | 29,416 | 35,753 | 41,222 | 47,060 |
| Accounts Payable | 1,771 | 1,684 | 1,785 | 1,894 | 2,068 | 2,496 | 3,481 | 5,047 | 5,963 | 4,956 |
| Long-Term Debt | 2,442 | 2,063 | 1,861 | 2,165 | 2,708 | 3,148 | 3,306 | 4,405 | 4,407 | 5,396 |
| Total Equity | 5,807 | 6,007 | 6,190 | 6,929 | 7,289 | 7,957 | 9,285 | 10,328 | 13,179 | 16,540 |
| D/E Ratio | 0.42 | 0.34 | 0.30 | 0.31 | 0.37 | 0.40 | 0.36 | 0.41 | 0.32 | 0.32 |

Profitability & Per Share Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Return on Assets | 4.7% | 4.1% | 4.9% | 5.1% | 4.6% | 3.3% | 4.4% | 6.1% | 7.8% | 9.6% |
| Return on Equity | 17.1% | 15.3% | 19.1% | 19.5% | 17.8% | 13.5% | 18.5% | 26.7% | 33.8% | 38.4% |
| ROIC | 12.5% | 11.1% | 14.5% | 14.9% | 13.3% | 9.8% | 13.4% | 18.8% | 23.8% | 28.2% |
| Shares Out. | 608 | 604 | 595 | 589 | 585 | 586 | 587 | 587 | 588 | 588 |
| Revenue/Share | 24.75 | 28.09 | 30.08 | 32.58 | 35.36 | 40.03 | 45.78 | 54.47 | 66.41 | 72.5 |
| FCF/Share | 2.23 | 2.57 | 2.92 | 2.72 | 3.67 | 4.30 | 6.15 | 10.26 | 10.04 | 11.37 |

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

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