



Mercury General (MCY)

Updated February 21st, 2022 by Jonathan Weber

Key Metrics

Current Price:	\$55	5 Year CAGR Estimate:	4.8%	Market Cap:	\$3.1B
Fair Value Price:	\$53	5 Year Growth Estimate:	1.5%	Ex-Dividend Date:	03/15/22
% Fair Value:	105%	5 Year Valuation Multiple Estimate:	-0.9%	Dividend Payment Date:	03/30/22
Dividend Yield:	4.6%	5 Year Price Target	\$57	Years Of Dividend Growth:	33
Dividend Risk Score:	D	Retirement Suitability Score:	C	Last Dividend Increase:	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 fourth quarter earnings results on February 15. The company reported net premiums earned of \$960 million for the quarter, which was up 4% compared to the previous year's period. Net premiums written rose by 4% year over year, to \$930 million. The fact that net written premiums were up year over year will likely mean that earned premiums should see some growth during the coming quarters. Mercury General's investment income and investment gains were flat year over year, coming in at a solid level of \$34 million. Mercury General's average annual yield on its investments declined slightly to 2.5%, compared to 2.8% during the previous year's quarter.

Mercury General's adjusted earnings-per-share totaled \$0.55 during the fourth quarter, beating the analyst consensus estimate. This can be attributed to lower-than-average catastrophe losses of \$19 million during the quarter. The coronavirus hasn't had a meaningful impact on Mercury General's profitability. 2021 was a strong year for Mercury, as earnings-per-share came in at an above-average \$5.03, although that was less than during the even stronger 2020. It is expected that 2022 and beyond will be weaker years again, which is why earnings-per-share will likely fall this year.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$2.13	\$2.18	\$2.28	\$2.34	\$1.73	\$1.64	\$1.80	\$2.60	\$5.54	\$5.03	\$3.50	\$3.77
DPS	\$2.44	\$2.45	\$2.46	\$2.47	\$2.48	\$2.49	\$2.50	\$2.51	\$2.52	\$2.53	\$2.54	\$2.60
Shares¹	54.9	55.0	55.1	55.2	55.3	55.3	55.3	55.3	55.4	55.4	55.5	56.0

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 recovered, however, due to lower catastrophe losses, but profits remained below the level that was hit in 2011, almost a decade earlier.

2019 had been a solid year for Mercury, but profits during 2020 rose to a way higher level, partially due to below-average catastrophe losses. The pandemic did not negatively impact the company's results during 2020, and the same can be expected for the current year, but higher losses for Mercury's ordinary business are expected for this year.

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 or hurricanes 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. These are not tied to the underlying strength of the economy, however, which is why Mercury's cyclicality is not tied to recessions.

¹ In Million

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	19.6	20.1	21.5	23.1	30.8	35.0	28.9	18.8	9.2	10.5	15.7	15.0
Avg. Yld.	5.8%	5.6%	5.0%	4.6%	4.7%	4.4%	5.1%	5.1%	5.0%	4.8%	4.6%	4.6%

Mercury General's shares traded at quite high valuations for many 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 2022, Mercury's shares trade slightly ahead of our fair value estimate.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	115%	112%	108%	106%	143%	152%	139%	96.5%	45.5%	50.3%	72.6%	69.1%

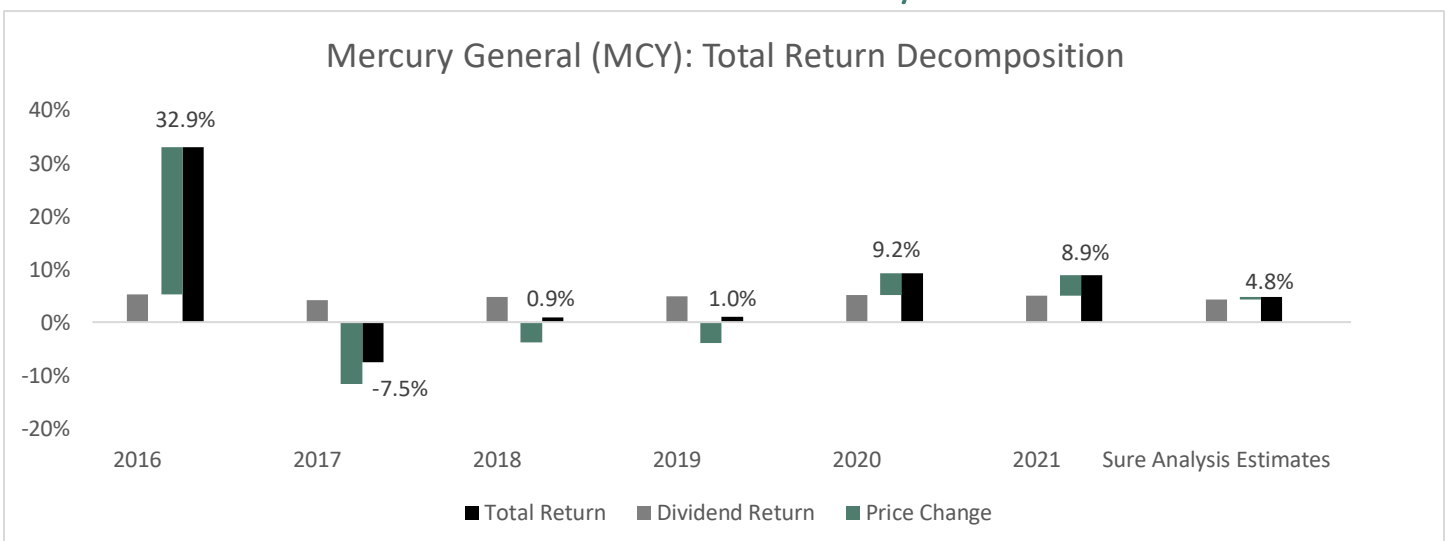
Mercury General has paid out more than 100% of its reported net earnings throughout most of the last decade. The company nevertheless managed to increase its dividend payout throughout the years, although the dividend growth rate was quite low in recent years, at less than 1% annually. Mercury General 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. But 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, however, and even though 2020 and 2021 were strong years, 2022 looks like it will be a weaker year again. Unforeseen catastrophes such as wildfires can impact results to a large degree. Due to unconvincing expected returns, we rate Mercury General a hold at the current level.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	2,783	2,821	3,012	3,009	3,228	3,416	3,380	3,973	3,785	3,993
D&A Exp.	37	31	28	48	53	55	59	65	68	79
Net Profit	117	112	178	74	73	145	(6)	320	375	248
Net Margin	4.2%	4.0%	5.9%	2.5%	2.3%	4.2%	-0.2%	8.1%	9.9%	6.2%
Free Cash Flow	133	191	220	170	275	322	355	480	566	460
Income Tax	18	20	69	(4)	(2)	22	(25)	58	84	51

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	4,190	4,315	4,600	4,629	4,789	5,101	5,434	5,889	6,328	6,772
Cash & Equivalents	158	267	290	264	220	291	314	294	348	336
Accounts Receivable	345	366	390	437	472	530	776	684	638	661
Goodwill & Int. Ass.	90	84	78	74	68	64	58	53	54	53
Total Liabilities	2,347	2,493	2,725	2,808	3,036	3,340	3,816	4,090	4,296	4,632
Accounts Payable	96	128	131	123	112	108	115	143	194	169
Long-Term Debt	140	190	290	290	320	371	372	372	373	373
Shareholder's Equity	1,842	1,822	1,875	1,821	1,752	1,761	1,618	1,800	2,033	2,140
LTD/E Ratio	0.08	0.10	0.15	0.16	0.18	0.21	0.23	0.21	0.18	0.17

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	2.8%	2.6%	4.0%	1.6%	1.6%	2.9%	-0.1%	5.7%	6.1%	3.8%
Return on Equity	6.3%	6.1%	9.6%	4.0%	4.1%	8.2%	-0.3%	18.7%	19.6%	11.9%
ROIC	5.9%	5.6%	8.5%	3.5%	3.5%	6.9%	-0.3%	15.4%	16.4%	10.1%
Shares Out.	54.9	55.0	55.1	55.2	55.3	55.3	55.3	55.3	55.4	55.4
Revenue/Share	50.68	51.33	54.74	54.51	58.36	61.74	61.08	71.76	68.36	72.12
FCF/Share	2.42	3.48	4.01	3.08	4.97	5.82	6.42	8.66	10.22	8.31

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

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