



The Hanover Insurance Group, Inc. (THG)

Updated February 28th, 2022, by Patrick Neuwirth

Key Metrics

Current Price:	\$140	5 Year CAGR Estimate:	16.3%	Market Cap:	\$5 B
Fair Value Price:	\$165	5 Year Growth Estimate:	11.0%	Ex-Dividend Date¹:	03/16/22
% Fair Value:	85%	5 Year Valuation Multiple Estimate:	3.4%	Dividend Payment Date¹:	03/30/22
Dividend Yield:	2.2%	5 Year Price Target	\$278	Years Of Dividend Growth:	17
Dividend Risk Score:	C	Retirement Suitability Score:	D	Last Dividend Increase:	7.1%

Overview & Current Events

The Hanover Insurance Group, Inc. (THG) is a holding company whose primary business is offering property and casualty insurance products and services. The company markets itself through independent agents and brokers in the United States. In 2021, Personal Lines accounted for approximately 40% of segmented revenues; Commercial Lines, 37%; Other Property & Casualty, 23%. The company operates an investment portfolio that is primarily exposed to fixed-income securities. The Hanover Insurance Group, Inc. was founded in 1852 and is headquartered in Worcester, Massachusetts.

On February 2nd, 2022, Hanover Insurance released its fourth-quarter and full-year 2021 results. For the quarter the company reported a net income of \$163.5 million (\$4.53 per diluted share) which is a small decrease compared to Q4-2020. The full-year 2021 ended with a total net income of \$418.7 million (\$11.49 per diluted share), up 17% compared to last year.

Commercial Lines net premiums written rose 9.6% in the last quarter of 2021 and 9% in the full year driven by rate and exposure increases. Personal Lines net premiums written were \$502.2 million in the fourth quarter of 2021, up 8.7% from the prior-year quarter, primarily driven by higher new business. Furthermore, net investment income in the last quarter was \$79.5 million, up 13.2% from the prior-year quarter.

The Hanover Insurance Group has a strong outlook for 2022 and presented ambitious financial targets for the next five years outlined during a recent investor day². The Board of Directors presented a long-term ROE target of ~14% and an EPS growth target of 12-13%. Expense leverage from growth is an important driver and the combination of a new software platform and operating model should improve claims cost efficiency.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$1.02	\$5.06	\$5.18	\$6.26	\$4.27	\$4.75	\$6.79	\$8.16	\$9.32	\$9.89	\$11.00	\$18.54
DPS	\$1.23	\$1.36	\$1.52	\$1.69	\$1.88	\$2.04	\$2.22	\$2.45	\$2.65	\$2.85	\$3.00	\$4.41
Shares³	44	44	44	43	42	43	42	38	36	36	35	35

The Hanover Insurance Group long-term earnings growth track record shows some instability, with the company's earnings-per-share having dropped in the fiscal years 2012 and 2016. However, in the last five years, the company has been able to grow its earnings-per-share at an 18.3% average annual rate. We expect Hanover Insurance to grow its earnings-per-share by 11% per year on average over the next five years, mainly driven by premium growth, assisted by optimizing costs, recording greater gains on its fixed-income investment positions and rising yields and interest rates. This growth rate is close to the company's expectations for double-digit growth for the next five years.

Hanover Insurance has a long history of paying dividends and has 17 consecutive years of annual dividend increases. In December 2021, the board increased the quarterly dividend by 7% to \$0.75. Over the last five years, the average annual growth rate is 8%.

¹ Estimated Date.

² Bank of America Securities Insurance Conference, February 16th, 2022

³ 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.



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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Avg. P/E	37.1	10.1	12.0	12.2	19.4	19.7	17.2	15.4	11.5	13.2	12.7	15.0
Avg. Yld.	1.9%	2.7%	2.4%	2.2%	2.3%	2.2%	1.9%	1.5%	2.5%	2.2%	2.2%	1.6%

The last few years Hanover Insurance's valuation has declined from the peak level (19.7) that it reached during 2017. During COVID, its share price declined to around \$83 before climbing back to \$140 in February of 2022. During the past decade shares of Hanover Insurance have traded with an average price-to-earnings ratio of about 15 times earnings. We are using 15 times earnings as a fair value baseline, implying the potential for a valuation tailwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

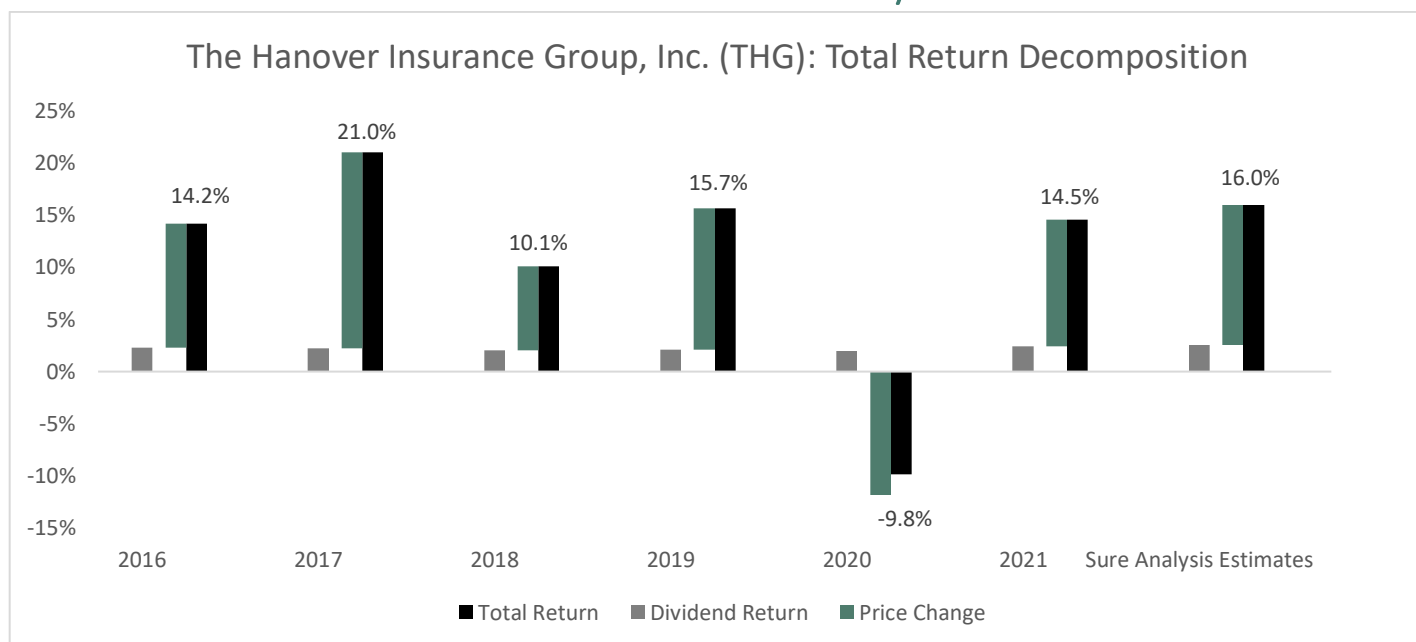
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	121%	27%	29%	27%	44%	43%	33%	30%	28%	29%	27%	24%

During the past five years the company's dividend payout ratio has averaged around 33%. With the current payout ratio of 27%, THG's dividend payments are well covered by earnings. Given the expected earnings growth, there is still room for the dividend to continue to grow moving forward while maintaining a payout ratio below 30%. The Hanover Insurance Group is a diversified and solid insurer with a differentiated P&C franchise in a fragmented market. With their differentiating strategy, such as specialized products and distinctive agency partnerships, the company can strengthen its competitive advantages. Furthermore, Hanover Insurance has a S&P and AM Best "A"-rating and a stable outlook.

Final Thoughts & Recommendation

The Hanover Insurance Group has a healthy balance sheet and ambitious financial targets for the next five years. The expected total returns for the shares are 16.3% per year, driven by 11% projected earnings growth, a 2.2% dividend yield, and the potential for a valuation tailwind. Although the stock price of Hanover Insurance is close to an all-time high, the company earns a buy rating based on its long-term growth potential.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	4,591	4,794	5,068	5,034	4,054	4,268	4,494	4,891	4,827	5,228
D&A Exp.	36	35	34	30	31	30	25	22	18	---
Net Profit	56	251	282	332	155	186	391	425	359	419
Net Margin	1.2%	5.2%	5.6%	6.6%	3.8%	4.4%	8.7%	8.7%	7.4%	8.0%
Free Cash Flow	387	361	554	425	728	686	538	590	693	---
Income Tax	(17)	83	96	109	(1)	77	44	93	83	101

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	13,485	13,379	13,760	13,781	14,220	15,470	12,400	12,491	13,444	14,254
Cash & Equivalents	565	486	373	339	283	298	1,021	216	121	231
Acc. Receivable	3,789	3,660	3,629	4,027	4,050	2,721	2,825	3,074	3,214	3,377
Goodwill & Int.	185	185	185	186	185	179	179	179	179	---
Total Liabilities	10,890	10,784	10,916	10,937	11,363	12,472	9,445	9,574	10,242	11,109
Accounts Payable	466	375	227	205	252	52	37	53	48	---
Long-Term Debt	849	904	904	803	786	787	778	653	781	782
Total Equity	2,595	2,595	2,844	2,844	2,858	2,998	2,955	2,916	3,202	3,145
LTD/E Ratio	0.33	0.35	0.32	0.28	0.28	0.26	0.26	0.22	0.24	0.25

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.4%	1.9%	2.1%	2.4%	1.1%	1.3%	2.8%	3.4%	2.8%	3.0%
Return on Equity	2.2%	9.7%	10.4%	11.7%	5.4%	6.4%	13.1%	14.5%	11.7%	13.2%
ROIC	1.6%	7.2%	7.8%	9.0%	4.3%	5.0%	10.4%	11.6%	9.5%	10.6%
Shares Out.	44	44	44	43	42	43	42	38	36	36
Revenue/Share	101.34	106.76	112.86	112.37	93.84	99.25	104.52	120.46	126.70	143.62
FCF/Share	8.54	8.04	12.33	9.49	16.84	15.95	12.52	14.52	18.18	---

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

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