The Hanover Insurance Group, Inc. (THG)

Updated November 11th, 2023, by Patrick Neuwirth

Key Metrics

Current Price:	$113	**5 Year CAGR Estimate:**	13.0%	**Market Cap:**	$4.0 B
Fair Value Price:	$128	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date[1]:**	12/14/23
% Fair Value:	89%	**5 Year Valuation Multiple Estimate:**	2.4%	**Dividend Payment Date[1]:**	12/28/23
Dividend Yield:	2.9%	**5 Year Price Target**	$187	**Years Of Dividend Growth:**	18
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	Buy

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 2022, Personal Lines accounted for approximately 41% of segmented revenues; Commercial Lines, 36%; 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 November 1st, 2023, Hanover Insurance released its third quarter 2023 results for the period ending September 30th, 2023. For this quarter, the company reported a net income of $8.6 million ($0.24 per diluted share) compared to net income of $0.5 million ($0.01 per diluted share), in the prior-year quarter.

The company's third quarter combined ratio, excluding catastrophes, improved by 3.5 points compared to the same period in 2022, and improved by 2 points sequentially. This was driven by better property loss experience in Core Commercial and strong performance in the Specialty segment. The company also achieved renewal price changes of 14% for personal auto and 23% for home and delivered net investment income of $84.2 million in the quarter. The combined ratio, which measures the relationship between losses and expenses to premiums earned, was 104.4% for the quarter. This indicates that the company's expenses and losses exceeded the premiums earned, resulting in an underwriting loss. Overall net premiums written for the reported quarter increased by 6.0%, with strong growth from each segment. Renewal price increases of 18.0% were reported in Personal Lines, including 23.4% in homeowners, as well as increases of 12.9% in Specialty and 11.8% in Core Commercial. Rate increases were 10.7% in Personal Lines, 9.2% in Core Commercial, and 8.4% in Specialty. Furthermore, Net investment income of $84.2 million was up 15.3% from the prior-year quarter, primarily due to higher bond reinvestment rates and the continued investment of operational cashflows. The company expects higher interest rates to drive further growth in net investment income. Book value per share of $59.21, down 5.4% from June 30, 2023, primarily due to a decrease in the fair value of fixed maturity investments. The company presented ambitious financial targets for the next five years outlined during an investor day[2]. The Board of Directors presented a long-term ROE target of ~14% and an EPS growth target of 12% to 13%. The company's full year 2023 guidance remains unchanged. The company continues to anticipate its ex-CAT combined ratio to be at the higher end of the original guidance range of 91% to 92%. We are forecasting earnings power to determine of $8.50 for 2023 as EPS is expected to be very low this year.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS[3]	$5.06	$5.18	$6.26	$4.27	$4.75	$6.79	$8.16	$9.32	$8.73	$5.53	***$1.10***	***$12.49***
DPS	$1.36	$1.52	$1.69	$1.88	$2.04	$2.22	$2.45	$2.65	$2.85	$3.06	***$3.24***	***$4.76***
Shares[4]	44	44	43	42	43	42	38	36	36	35	***36***	***36***

[1] Estimated Date.

[2] Bank of America Securities Insurance Conference, February 15th, 2023

[3] Based on operating income

[4] In millions.

The Hanover Insurance Group, Inc. (THG)

Updated November 11th, 2023, by Patrick Neuwirth

The Hanover Insurance Group long-term earnings growth track record shows instability, with the company's earnings-per-share having dropped in the fiscal years 2016 and 2022. We expect Hanover Insurance recover from the 2022 & 2023 EPS dip and grow its earnings-per-share by 8% 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. This growth rate is more conservative compared to the company's expectations for double-digit growth for the next five years. The company has taken decisive action in response to elevated catastrophe loss trends, which we believe is essential to return to the target profitability objectives.

We choose to evaluate future returns using earnings power instead of earnings per share, especially since the company is experiencing a drastic decline for the current year. To normalize EPS, we applied the earnings power method involving total current assets multiplied by the average return on assets over the last decade, divided by the share count.

Hanover Insurance has a long history of paying dividends and has 18 consecutive years of annual dividend increases. In December 2022, the board increased the quarterly dividend by 8% from $0.75 to $0.81. Over the last five years, the average annual growth rate is 7.9%.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Avg. P/E	10.1	12.0	12.2	19.4	19.7	17.2	15.4	11.5	13.2	15.0	***13.3***	***15.0***
Avg. Yld.	1.9%	2.4%	2.2%	2.3%	2.2%	1.9%	1.5%	2.5%	2.2%	2.3%	***2.9%***	***2.5%***

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 $150 levels in April 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 also as a fair value baseline, implying the potential for a valuation tailwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

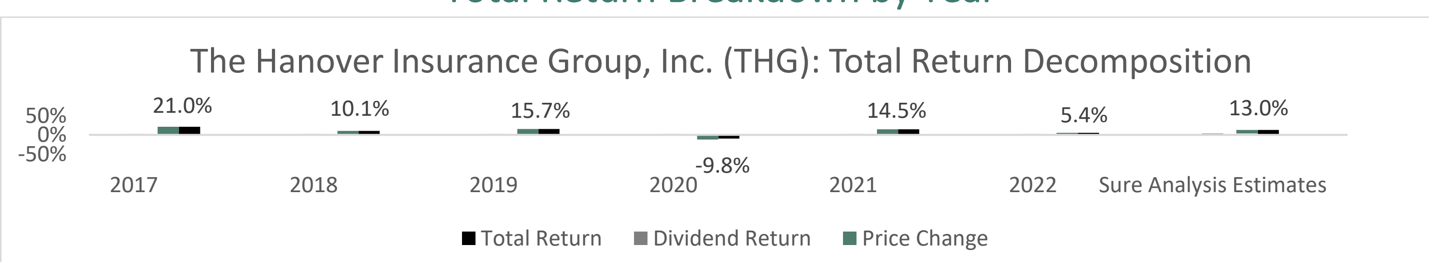
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	27%	29%	27%	44%	43%	33%	30%	28%	33%	55%	***38%***	***38%***

During the past five years the company's dividend payout ratio has averaged around 33%. With the current payout ratio of 38%, THG's dividend payments are just covered by earnings and is something to monitor. 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. However, the insurance industry is subject to fluctuations and volatility due to various factors, including weather events, regulatory changes, and economic conditions.

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 13.0% per year, driven by 8% projected earnings growth, a 2.9% dividend yield, and a valuation tailwind. The company earns a buy rating.

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.

The Hanover Insurance Group, Inc. (THG)

Updated November 11th, 2023, by Patrick Neuwirth

Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	4,794	5,068	5,034	4,054	4,268	4,494	4,891	4,827	5,228	5,469
D&A Exp.	35	34	30	31	30	25	22	18	---	13
Net Profit	251	282	332	155	186	391	425	359	419	116
Net Margin	5.2%	5.6%	6.6%	3.8%	4.4%	8.7%	8.7%	7.4%	8.0%	2.1%
Free Cash Flow	361	554	425	728	686	538	590	693	---	705
Income Tax	83	96	109	(1)	77	44	93	83	101	27

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	13,379	13,760	13,781	14,220	15,470	12,400	12,491	13,444	14,254	14,000
Cash & Equivalents	486	373	339	283	298	1,021	216	121	231	305
Acc. Receivable	3,660	3,629	4,027	4,050	2,721	2,825	3,074	3,214	3,377	3,566
Goodwill & Int.	185	185	186	185	179	179	179	179	---	179
Total Liabilities	10,784	10,916	10,937	11,363	12,472	9,445	9,574	10,242	11,109	11,670
Accounts Payable	375	227	205	252	52	37	53	48	---	70
Long-Term Debt	904	904	803	786	787	778	653	781	782	782
Total Equity	2,595	2,844	2,844	2,858	2,998	2,955	2,916	3,202	3,145	2,326
LTD/E Ratio	0.35	0.32	0.28	0.28	0.26	0.26	0.22	0.24	0.25	782

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	1.9%	2.1%	2.4%	1.1%	1.3%	2.8%	3.4%	2.8%	3.0%	0.8%
Return on Equity	9.7%	10.4%	11.7%	5.4%	6.4%	13.1%	14.5%	11.7%	13.2%	4.2%
ROIC	7.2%	7.8%	9.0%	4.3%	5.0%	10.4%	11.6%	9.5%	10.6%	3.3%
Shares Out.	44	44	43	42	43	42	38	36	36	36
Revenue/Share	106.76	112.86	112.37	93.84	99.25	104.52	120.46	126.70	143.62	151.48
FCF/Share	8.04	12.33	9.49	16.84	15.95	12.52	14.52	18.18	---	19.52

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