Assurant, Inc.
(AIZ-NYSE)

4Q15: Cutting Estimates Following a Disappointing Quarter

Recommendation: Our rating on shares of Assurant remains at Market Perform. The shares seem reasonably valued at nearly 10x our 2017 EPS estimate when compared with similar specialty insurers, particularly in light of volatile expense trends.

◆ Event: Assurant reported 4Q15 non-GAAP operating EPS was $0.97 versus $1.38 a year earlier, Street consensus of $1.51, and our $1.46 estimate. While risk results were generally good, the underperformance relative to our estimate was driven by higher operating expenses in Solutions (even after a $0.12 negative impact from prior-year accounting adjustments) and Specialty Property. Partially offsetting the higher expense levels was $0.09 per share of income from real estate investment partnerships.

◆ Specialty Property reported earnings of $57.8 million compared to $71.0 million a year ago and our forecast of $66.2 million. The expense ratio was 57.3% compared with our estimate of 52.1%. The company did note increased legal expenses. Cat losses this quarter of $15.1 million, pre-tax, compared to an expected $12.6 million, pre-tax. The non-cat loss ratio was lower than expected by 3.1 percentage points. Real estate investment income added $8.3 million, pre-tax, to earnings.

◆ Solutions recorded earnings of $29.6 million compared to our estimate of $54.9 million as operating expenses were $70.1 million, pre-tax, higher than expected. Expenses this quarter included costs related to program launches as well as a disclosed $12.6 million, pre-tax, prior-year accounting adjustment. The company also recorded a release of legal reserves in its U.K. business, offset by a remeasurement loss due to the depreciation of the Argentinian peso.

◆ Employee Benefits reported earnings of $15.5 million compared to $7.2 million a year ago and our $10.3 million forecast. The loss ratio decreased 470 bp sequentially while the expense ratio was up 200 bp. The sale of Employee Benefits to Sun Life remains on track to close in 1Q16.

◆ Estimates: Reflecting expense trends in the quarter and our best guess as to what they might look like going forward, we are reducing our 2016 and 2017 non-GAAP operating EPS estimates to $5.98 and $7.20, respectively, from $6.72 and $7.60 previously. Our estimates assume capital from the sale of the Employee Benefit business is deployed for share repurchase as of July 1, 2016; capital released from the run off of the Health business is deployed January 1, 2017.

<table>
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<th>Non-GAAP EPS</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>Q4</th>
<th>Full Year</th>
<th>GAAP EPS</th>
<th>Revenues (mil.)</th>
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Rows may not add due to rounding and changes in share count. Non-GAAP EPS reflects GAAP EPS less realized gains & losses on investments, non-operating benefits & charges, and discontinued operations.

Please read domestic and foreign disclosure/risk information beginning on page 5 and Analyst Certification on page 5.
Reports Disappointing Fourth Quarter Earnings

Reported non-GAAP operating EPS was $0.97 versus $1.38 a year earlier, Street consensus of $1.51, and our $1.46 estimate. While risk results were generally good, the underperformance relative to our estimate was driven by higher operating expenses in Solutions (even after a $0.12 negative impact from prior-year accounting adjustments) and Specialty Property. Partially offsetting the higher expense levels was $0.09 per share of income from real estate investment partnerships.

Solutions
Solutions recorded earnings of $29.6 million ($37.2 million excluding prior-period accounting adjustments) compared to $58.1 million a year ago and our $54.9 million estimate. The underperformance reflects higher than expected operating expenses — including about $6 million of costs associated with new program launches. The company also recorded a release of legal reserves in its U.K. business, offset by a remeasurement loss due to the depreciation of the Argentinian peso.

Revenues were flat from last year at $1.1 billion. The loss of a large mobile tablet program last year was mostly offset by growth in vehicle service contract business. Fee income increased 18.1% from last year, with the growth coming mostly from the company expansion of its repair and logistics offerings in mobile and auto.

Gross written premiums were $1.5 billion (excluding pre-need), up 6.5% y/y. Domestic Extended Service Contract gross written premiums were up 17.2% year-over-year to $1.0 billion. Domestic Credit (in run-off) gross written premiums were down 23.2% year-over-year and 5.6% sequentially to $55.1 million.

International Credit gross written premiums were down 14.2% on a year-over-year basis and 3.1% sequentially ($179.3 million), while International Extended Service Contract gross written premiums decreased 3.4% year-over-year but up 13.1% sequentially $202.1 million.

Pre-need face sales fell 0.8% from last year to $228.6 million.

Excluding pre-need, the overall combined ratio increased from 96.5% in 4Q14 to 100.5%. The domestic combined ratio rose to 100.1% from 92.9%, while the international combined ratio dropped to 101.4% from 103.4%.

General expenses increased to $821.7 million from $767.2 million in the fourth quarter of last year and from $721.5 million in the fourth quarter of last year at $1.0 billion. T

Specialty Property
Specialty Property reported earnings of $57.8 million compared to $71.0 million a year ago and our forecast of $66.2 million. Cat losses this quarter of $15.1 million, pre-tax, compared to an expected $12.6 million, pre-tax. The non-cat loss ratio was lower than expected by 3.1 percentage points. The expense ratio was 57.3% compared with our estimate of 52.1%. Real estate investment income added $8.3 million, pre-tax, to earnings.

The number of loans tracked decreased to 33.3 million from 33.9 million in 4Q14 and 33.4 million last quarter, while the placement rate fell 6 bp q/q to 2.28%.

Reflecting the sale of American Reliable and lower placement rate from REO policies, gross earned premiums decreased to $704.8 million from $822.4 million a year ago and down 2.4% from $722.2 million last quarter. Net earned premiums of $492.4 million decreased 24.8% from the $594.5 million recognized a year earlier but slightly up from $491.8 million in the third quarter.

The segment loss ratio for the quarter was 40.0%, below the 42.9% experienced a year earlier and our 42.5% estimate. The company benefitted from favorable non-catastrophe loss experience and lower catastrophe reinsurance costs. Cat losses this quarter of $15.1 million, pre-tax, compared to an expected $12.6 million, pre-tax. We had estimated a $12.6 million after-tax cat loss.

The expense ratio was up 6.7 percentage points y/y at 57.3%, well above our 52.1% forecast. The increase primarily reflects both continued mix shift as non-insurance, fee-based lines of business become a bigger piece of overall revenues as well as increased legal expenses. Management noted that it continued to expect the insurance expense ratio to remain in the mid-40% area.

Employee Benefits
The sale of Employee Benefits to Sun Life remains on track to close in 1Q16.
For the time being, however, Employee Benefits reported earnings of $15.5 million compared to $7.2 million a year ago and our $10.3 million forecast. The loss ratio decreased 470 bp sequentially while the expense ratio was up 200 bp.

Sales of $30.7 million were up from $28.7 million the same period last year.

Net earned premiums grew 0.5% year-over-year to $264.8 million from $263.5 million a year earlier. Group dental and group disability net earned premiums were flat y/y and down 3.0% y/y, respectively, while group life net earned premiums were up 1.0%.

The loss ratio was 63.9%, well below the 69.7% reported in the same period last year and our 69.0% assumption.

The expense ratio was 38.5%, up 60 bp from a year earlier and compared to our 37.0% projection.

**Corporate and Other**

Corporate and Other reported an operating loss of $37.6 million compared with a loss of $36.5 million a year ago and the $32.7 million loss we had projected. Results reflect a reversal of a tax benefit in the first quarter that should reverse throughout the remainder of the year.

**Health**

Health (now accounted for as a discontinued operation) recorded a loss of $15.8 million, reflecting severance and other expenses not included in the premium deficiency reserve.

**Investments and Capital Position**

Assurant experienced $6.3 million after tax of net realized investment gains during the quarter versus $4.0 million last quarter and $11.2 million of gains a year earlier.

Assurant’s fixed maturity portfolio contained $775 million of net unrealized gains versus $887 million at the end of last quarter.

Assurant contributed $260 million ($60 million more than originally expected) to the business in 4Q15 to maintain appropriate capital levels. Roughly $470 million of capital is expected to be released from the Health segment in the second half of 2016 with the potential for a bit more 2017.

Holding company excess capital was down from $520 million at the end of September to $460 million, with deployable capital at roughly $210 million ($60 million below last quarter) after adjusting for management’s desired $250 million buffer.

Book value per share was $67.92 as of quarter-end ($66.14 excluding accumulated other comprehensive income) versus $69.34 last quarter ($65.69 excluding AOCI).

During the quarter, the company repurchased 925,000 shares for $74.2 million. Through February 5, the company repurchased an additional 1.1 million shares for $90.0 million. $862.1 million remained on the current share repurchase authorization.

**Cutting Estimates to Reflect Higher Expenses**

Reflecting expense trends in the quarter and our best guess as to what they might look like going forward, we are reducing our 2016 and 2017 non-GAAP operating EPS estimates to $5.98 and $7.20, respectively, from $6.72 and $7.60 previously. Our estimates assume capital from the sale of the Employee Benefit business is deployed for share repurchase as of July 1, 2016; capital released from the run off of the Health business is deployed January 1, 2017.
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<th>U.S. Research</th>
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<th>Employee Benefits</th>
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Total EPS: 0.69

Source: Company reports and filings and Raymond James estimates.

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Market Perform (MP3) Expected to perform generally in line with the S&P 500 over the next 12 months.
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Market Perform (MP3) Expected to perform generally in line with the underlying country index.
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Market Perform (3) Expected to perform generally in line with the Stoxx 600 over the next 12 months.
Underperform (4) Expected to underperform the Stoxx 600 or its sector over the next 6 to 12 months.
Suspended (S) The rating and target price have been suspended temporarily. This action may be due to market events that made coverage impracticable, or to comply with applicable regulations or firm policies in certain circumstances, including when Raymond James may be providing investment banking services to the company. The previous rating and target price are no longer in effect for this security and should not be relied upon.

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Rating Distributions

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<th>Coverage Universe Rating Distribution*</th>
<th>Investment Banking Distribution</th>
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<td>Strong Buy and Outperform (Buy)</td>
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* Columns may not add to 100% due to rounding.

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Medium Risk/Income (M/INC) Lower to average risk equities of companies with sound financials, consistent earnings, and dividend yields above that of the S&P 500. Many securities in this category are structured with a focus on providing a consistent dividend or return of capital.
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<th>Company Name</th>
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<td>Assurant, Inc.</td>
<td>Raymond James &amp; Associates makes a market in shares of AIZ.</td>
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