Progressive

Outsized December 2023 premium growth: expect it to both continue and accelerate

Reiterate Rating: BUY | PO: 242.00 USD | Price: 178.76 USD

24 January 2024

Equity

Dec. ’23 op. EPS of $1.33 ($1.40 excl. non-cash NII charge)

The result came in well-ahead of Street consensus of $0.81 and our higher forecast of $0.88. The company comfortably exceeded its 96% guiding principle combined ratio for 2023 at 94.9% after a rocky start to the year due to high catastrophe losses and adverse prior-year loss development. The company beat our December 2023 expectations across the most closely watched measures: premium growth and underwriting margin. Policycount grew in December, which is atypical of the company, showing the growth trajectory has likely resumed. We are slightly increasing both our premium growth and revenue forecasts as we interpolate December 2023 results into our model.

Dec. ’23 net written premium surges 36% to $4.9bn

The December 2023 growth exceeded consensus expectations for 20.0% growth ($4.3bn) and our Street high forecast of 27.4% ($4.6bn). Partly feeding the growth (and already anticipated in our forecast) was an 11% boost to premium due to the adoption of Gregorian calendarization with a 31-day December instead of its former practice of typically treating December as a 28-day month. This reporting change will add much volatility in monthly reported revenue growth through September 2024 including acting as an 11% headwind for January 2024 results.

Written premium growth to accelerate in 2H24 vs. 1H24

While consensus forecast premium growth to decelerate in 2H24, we expect it likely to accelerate off already high levels. (We expect 16% growth in 1H24 and 20% in 2H24.) The key difference, we believe, is a failure to account for the disproportionate cash flow boost to written premium volumes during times of accelerating policycount growth. While we forecast policycount growth to accelerate modestly, “premium-months” are poised to surge as the company flips to policycount growth and faces easy comps from 2H23. Our forecasts nonetheless assume a decelerating growth in premium per policy.

Taking up our already high-on-the-Street forecast

Our EPS forecast rises modestly as we interpolate the stronger December results into our forecast. The modest increase in our EPS outlook combines with a higher P/E multiple of 18.1x (from 17.6x previously) based on parity with the S&P 500’s 2025 P/E multiple to take our price objective to $242 from $233. With healthy upside to our PO and a once-in-generation hard market for U.S. personal auto insurance, we continue to recommend investors buy shares of Progressive.

Estimates (Dec) (US$)	2022A	2023A	2024E	2025E	2026E
EPS	4.14	6.11	10.55	13.35	15.30
GAAP EPS	1.18	6.58	10.55	13.35	15.30
EPS Change (YoY)	14.0%	47.6%	72.7%	26.5%	14.6%
Consensus EPS (Bloomberg)			8.23	9.88	11.24
DPS	0.40	0.40	4.65	8.40	8.90
Valuation (Dec)					
P/E	43.2x	29.3x	16.9x	13.4x	11.7x
GAAP P/E	151.5x	27.2x	16.9x	13.4x	11.7x
Dividend Yield	0.2%	0.2%	2.6%	4.7%	5.0%

Key Changes

(US$)	Previous	Current
Price Obj.	233.00	242.00
2024E EPS	10.40	10.55
2025E EPS	13.20	13.35
2026E EPS	15.15	15.30

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Stock Data

Price	178.76 USD
Price Objective	242.00 USD
Date Established	24-Jan-2024
Investment Opinion	B-1-7
52-Week Range	110.92 USD -172.51 USD
Mrkt Val / Shares Out (mn)	104,628 USD / 585.3
Free Float	99.7%
Average Daily Value	407.99 USD
BofA Ticker / Exchange	PGR / NYS
Bloomberg / Reuters	PGR US / PGR.N
ROE (2024E)	27.9%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research’s equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to “BofA ESGMeter Methodology”.

Refer to important disclosures on page 19 to 21. Analyst Certification on page 17. Price Objective Basis/Risk on page 17. **12650140**

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Income Statement Data (Dec)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Total Earned Premiums	49,241	58,664	68,867	78,654	86,698
Net Investment Income	1,260	1,892	2,815	3,576	4,156
Total Revenue	**48,889**	**61,219**	**71,982**	**82,530**	**91,153**
Total Cost of Benefits and Claims	(38,123)	(45,650)	(50,935)	(57,963)	(63,840)
S,G & A (Including Commissions)	(9,055)	(10,018)	(12,662)	(14,010)	(15,256)
Total Operating Expenses	**(47,967)**	**(56,311)**	**(64,225)**	**(72,649)**	**(79,834)**
Pre-Tax Operating Earnings	**922**	**4,909**	**7,757**	**9,882**	**11,320**
Income Tax Expense	(201)	(1,001)	(1,545)	(1,983)	(2,269)
Operating Earnings After Tax	**2,430**	**3,591**	**6,203**	**7,859**	**9,011**
Net Income (Reported)	**2,457**	**3,628**	**6,212**	**7,899**	**9,051**
Diluted Shares	587	587	588	588	589
Operating Earnings Per Share	4.14	6.11	10.55	13.35	15.30
Net Income (Reported) Per Share	1.18	6.58	10.55	13.35	15.30

Balance Sheet Data (Dec)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Fixed Income Securities	NA	NA	NA	NA	NA
Total Cash and Investments	53,548	65,999	80,597	92,883	104,004
Total Assets	**75,465**	**88,691**	**100,627**	**111,955**	**124,440**
Reserves	30,359	34,389	38,795	43,806	49,323
LT Debt	6,388	6,889	7,389	8,389	9,389
Total Liabilities	**59,574**	**68,414**	**77,032**	**85,590**	**94,462**
Total Equity	**15,891**	**20,277**	**23,595**	**26,365**	**29,978**
Total Equity (Ex FAS 115)	**19,429**	**22,312**	**23,595**	**26,365**	**29,978**
Book Value per Share (Reported)	26.32	33.80	39.44	44.13	50.25
Book Value per Share (Ex FAS 115)	32.37	37.28	39.44	44.13	50.25

Ratios (Dec)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Expense Ratio	18.4%	17.1%	18.4%	17.8%	17.6%
Loss Ratio	77.4%	77.8%	74.0%	73.7%	73.6%
Combined Ratio	**95.8%**	**94.9%**	**92.4%**	**91.5%**	**91.2%**
Avg Assets / Avg Eq (Ex FAS 115) Ratio	3.9x	3.9x	4.1x	4.3x	4.2x

Growth Rates (YoY) (Dec)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Total Earned Premium	11.0%	19.1%	17.4%	14.2%	10.2%
Net Investment Income	46.4%	50.1%	48.8%	27.1%	16.2%
Total Revenue	4.0%	25.2%	17.6%	14.7%	10.4%
Operating Earnings per Share	14.0%	47.6%	72.7%	26.5%	14.6%
Asset	6.9%	17.5%	13.5%	11.3%	11.2%
Reported Book Value per Share	-13.3%	28.4%	16.7%	11.9%	13.9%

Performance Metrics (Dec)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Operating ROE	15.5%	21.4%	27.9%	30.1%	30.6%
Operating ROE (Ex FAS 115)	13.4%	18.0%	26.8%	30.1%	30.6%
Operating Return on Average Assets	3.3%	4.4%	6.6%	7.4%	7.6%
Operating Margin	5.0%	5.9%	8.6%	9.5%	9.9%
Long Term Debt to Cap Ratio (Ex FAS 115)	24.7%	23.6%	23.8%	24.1%	23.8%
Net Income % Operating Income	28.6%	107.8%	100.0%	100.0%	100.0%
Amtz of DAC % Pretax Profit bef Amtz of DAC	0%	0%	0%	0%	0%

Company Sector

Insurance - Non-Life

Company Description

Progressive derives most of its business from personal auto insurance policies. PGR operates in standard and preferred auto and is expanding distribution channels, which includes direct distribution and internet.

Investment Rationale

We believe that a combination of superior execution and a more rational competitive environment will allow Progressive to deliver on both premium growth and margins, a challenging balance to manage. In our view, the Street does not fully appreciate the earnings power or sustainability of Progressive's earnings, which is reflected in our above-consensus estimates.

Stock Data

Average Daily Volume	2,282,320

Quarterly Earnings Estimates

	2023	2024
Q1	0.65A	2.35E
Q2	0.40A	2.63E
Q3	2.09A	2.62E
Q4	2.96A	2.94E

In addition to Progressive's strong EPS result, the company posted 36.4% year-over-year net written premium growth overall compared with December 2022 and 35.9% for its Personal Lines segment (personal auto plus motorcycles, snowmobiles, etc.). The $4.88 billion in overall net written premium exceeded the consensus forecast of $4.29 billion (which implied 20.0% growth vs. December 2022) and the Personal Lines consensus forecast of $3.492 billion (21.7% year-over-year growth). The actual growth of 36% dramatically exceeded consensus expectations, but it also exceeded our high-on-the-Street December 2023 forecast of $4.55 billion (27.4% growth) overall and $3.69 billion (28.5% growth) in Personal Lines. The growth numbers were, by a notable margin, ahead of the range of expected outcomes.

This elevated growth, while ahead of even our expectations, nonetheless matches our generally positive outlook for Progressive. We have a high-on-the-Street growth forecast for net written premium volume overall in 2024 of $72.6 billion or 17.9% growth (or $59.0 billion or 21.5% growth for Personal Lines only). This compares with the consensus forecast of $69.5 billion or 13.2% growth (or $55.5 billion or 14.5% growth for Personal Lines only). Moreover, despite our forecast for very strong 2024 growth, we are expecting only single-digit year-over-year overall net written premium change in January 2024 (3.8% vs. January 2023). (Consensus is not available for a January-only forecast.) We then expect very strong year-over-year monthly Personal Auto premium growth to resume in February.

> Investors should be prepared for weak January 2024 premium growth, which we expect to be surround by strong premium growth in the surrounding months.

This strangeness in the pattern of monthly growth should suggest that there are many factors at work here that are being underappreciated by the sell-side, and probably the buy-side investors as well (including our expectation of accelerating net written premium volume in 2H24 off already strong 1H24 premium growth). We believe possible reasons for underestimating what we expect will be outsized premium volume growth fall into three main categories:

- Misunderstanding unit economics of growth
- Cash revenues vs. GAAP revenues
- The Gregorian calendar "intervention"

Our aim in this report will be to explain the impact of each of these three items in detail as we expect 1) overall premium growth is materially underestimated, and 2) Progressive's monthly revenue growth numbers are likely to fluctuate widely (and wildly) through September 2024.

Misunderstanding the Unit Economics

In the past, we argued that consensus numbers failed to consider the mechanics of unit economics in establishing its revenue forecasts. In our October 3, 2023 note entitled, "Addressing chronic mismodeling of Progressive's future earnings power," we addressed this issue in detail, but we will walk through some of the basics here. Simplistically, there are two drivers of revenue growth in most any business: price and units. A simple model for revenue growth is "how many more units were sold compared with the prior period" and "how much more/less was the price per unit compared with a year ago?" For most large-cap property & casualty insurance companies (Allstate, Chubb, CNA, Hartford, Travelers, etc.), unit growth—that is, number of policies—doesn't change so much year-to-year. As such, revenue growth (as expressed in net written premium) has adhered fairly closely to the pricing trend, while, further, EPS growth has largely been a function of sharecount reduction through repurchases. When looking at most of our spreadsheet models forecasting P&C insurance company revenues (but not Progressive, not Allstate), forward net written premium growth is calculated in an overly simple (and reductive) manner: by multiplying a growth rate forecast by the prior-period premium volume. But, at times of notable unit volume growth (or decline), this method of forecasting premium growth runs the risk of leading to the wrong answer. If a company increases its prices by 10% but also increases its unit volume by 10%, premium volume should grow by around 21% by multiplying units and price (10% x 10%). However, as unit volume approaches zero, the difference between growth in price and growth in premium becomes negligible.

> Because Progressive has strong unit volume growth unlike most of its P&C insurance peers, we believe there are unique factors that can cause its revenue growth to be underestimated.

However, Progressive is unusual among its large-cap P&C insurance peers. Unit volume really grows at Progressive, both consistently and materially. Personal Auto policycount growth has been 11.1%, 11.0%, 5.8%, 2.6% and 9.2% for each of the five years 2019-2023 (as well as in the many years preceding). In trying to "dissect" the two drivers of revenue growth, arguably, one can divide premium growth by unit growth to "back into" the change in price per policy (or "rate"). (While this is true, in theory, we will endeavor to smash that simplistic "theory" in the further two sections of this note.)

Our forecast for Personal Lines net written premium growth in full-year 2024 is 21.5% (compared with 23.7% in 2023). Our forecast for 2024 Personal Auto policycount growth is 12.4% (vs. 9.2% in 2023). Technically, however, premiums are "manufactured" as a byproduct of policies across the year, not just at year-end, so it is more accurate to measure the two periods' average Personal Auto policycounts against one another. Average policycount grew 10.8% average Personal Auto policycount growth in 2023 (as opposed to 9.2% as measured at year-end), and we forecast 8.7% growth in average policycount 2024 (as opposed to 12.4% at year end). We then argue average is more accurate as a denominator. Dividing premium growth by average policycount implies the price of the average Progressive Personal Auto policy rose 11.6% on average in 2023 and, on our numbers, is expected to rise to an average of 11.7% in 2024 (compared with a December 2023 U.S. Consumer Price Index for Motor Vehicle Insurance of up 20% year-over-year). (In actuality, the price change we induced above is the reverse of our process. We forecast unit volume and rate growth and multiply them together to determine premium growth.) This 11.7% number is higher than what we think rate will be on average for 2024, which will require some additional explanation in the sections to follow.

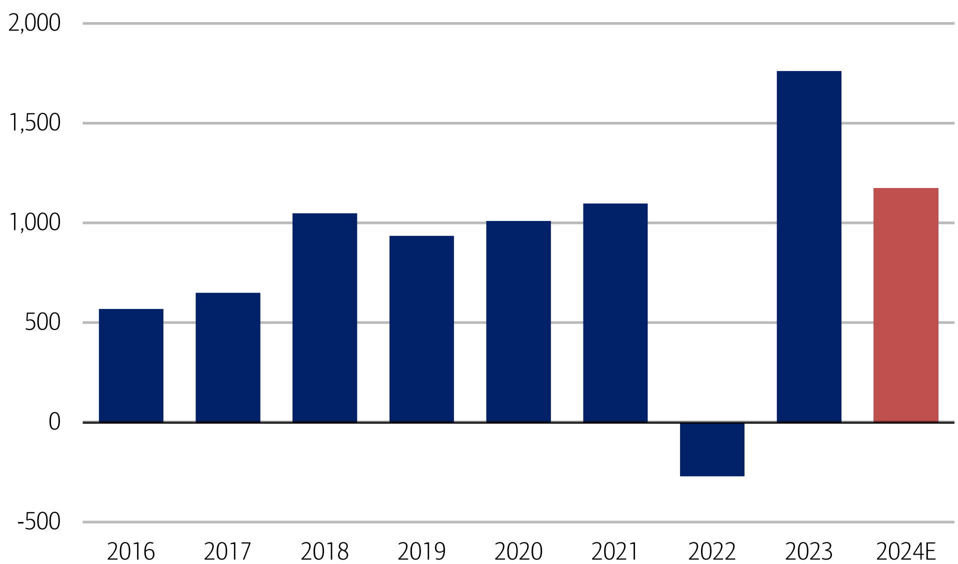
Since writing our October 3 note arguing that consensus numbers were materially mismodeling revenue for 2024, what we formerly viewed as material consensus revenue misforecasting appears to have corrected some (while the consensus average 2024 EPS estimate has risen 10% from $7.61 to $8.37). The consensus net written premium growth forecast for Progressive Personal Lines in 2024 is now $55.5 billion or 14.5% above 2023, according to Visible Alpha. Year-end consensus 2024 Personal Auto policycount is 21.4 million (and average 2024 policycount, the number more appropriate for the calculation of pricing is 20.5 million). This compares with year-end 2023 policycount of 19.5 million (with a 2023 average of 19.3 million). Divide premium growth of 14.5% by the year-over-year change in average policycount (6.5%), and it implies that the consensus forecast expects the average price change of a Progressive auto insurance policy to be about 7.5% over the 2023 price. (While U.S. CPI for motor vehicle indicates industry prices averaged up 17% in 2023 and exited the year up 20%, Progressive management commentary points to Progressive price per personal auto policy up around 12-14% at year-end). We do expect price increases to decelerate in 2024, and an average price increase of 7.5% does not seem unreasonable in our view (although maybe a touch light). From low double-digit levels to begin 2024, we would expect average price to converge toward the mid-single-digit range where it should average to across the cycle.

We argue that consensus numbers likely are underestimating policycount growth in 2024.

The gap between our 2024 Progressive Personal Lines net written premium growth of 21.5% is not as wide with consensus (now 14.5%) as it once was. The major gap between our forecast and consensus largely reflects two items: policycount to a lesser extent and the lack of recognition of what we would describe as the "premium-month" factor, which we will discuss in the next section. According to Visible Alpha, consensus expects Progressive Personal Auto policycount to be 20.6 million at June 30, 2024. This compares with 19.5 million at December 31, 2023, implying net policycount growth of 1.2 million in the first half of 2024. (The majority of Progressive's annual policycount growth tends to occur in the first half of the year.)

Exhibit 1: Progressive Personal Auto January-June net policycount additions (# in ks)

Consensus earnings forecasts predict a material decline in net policycount additions in 1H24 compared with 1H23, with 1H23 being essentially in-line with 2018-2021 level growth. We expect 1H23 net policycount additions will be similar to 1H23 levels.



2024E number represents the consensus forecast.
Source: Company filings and Visible Alpha

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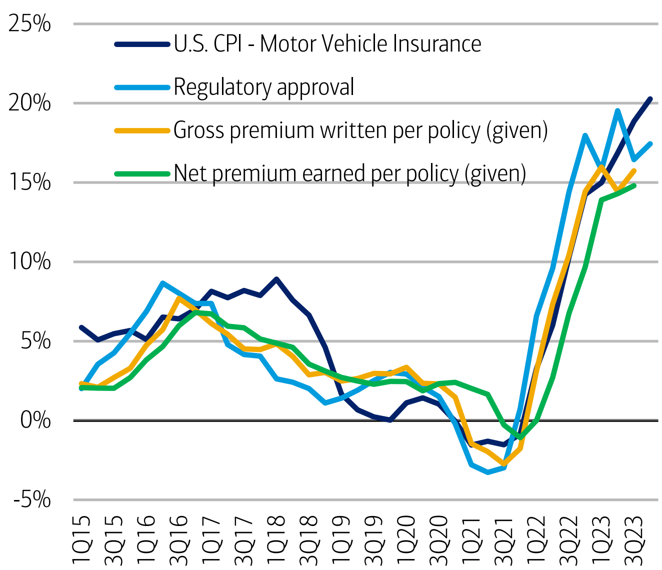
Consensus numbers seem to imply that first half of year Personal Auto policycount additions in 2024 (1.17 million net new policies) will be on par with where it was in 2018 and 2021 when the company was 60% and 85% of its current size, respectively. This represents a steep decline from 1.76 million net new policies added in 1H23 despite the fact that the U.S. personal lines market is currently experiencing its greatest dislocation since at least 2001-2002, but maybe even since 1976-1977. We expect policycount growth in 1H24 will be similar to 1H23. The consensus Personal Auto policycount growth forecast of 9.5% for 2024 runs 300bps below our policycount growth forecast and represents part of the gap between our forecast for premium revenue and that of consensus.

Cash revenues vs. GAAP revenues: “premium surge”

The section above revisits some work we’ve done in the past year, which remains correct in a “general” sense; however, over the past year, we have found that “price x unit” volume isn’t as predictive of net premium written volume as we might have originally thought. The “price” or “rate” side of the equation is difficult to comfortably estimate at Progressive based on how it has acted in the past.

How much to charge customers for coverage is a major component of the “secret sauce” in how personal auto carriers (and insurance carriers more broadly) effectively underwrite to a profit. Progressive does not disclose this information regularly (though some investors try to figure it out by closely watching rate filings in various states). Competitor Allstate makes this much easier for investors. The company discloses the impact regulatory rate filings have on its book on a monthly basis. (For years, the company disclosed this quarterly, and then, in 2020, the company decided to suspend this disclosure for competitive reasons. When its loss ratios began to deteriorate quickly in 2021, the company felt that investor trust required it to reimplement the rate impact disclosure and increased the frequency of the disclosure to a monthly rather than a quarterly rhythm.) In general, Allstate’s disclosure around pricing is about as specific as one could desire, the company includes the impact of rate filings, gross premium written per policy and net premium earned per policy. One can also calculate the change in net premium written and earned per policy by dividing premiums into average policycount.

Exhibit 2: Year-over-year change in Allstate brand personal auto rate
It is worthwhile to note that there is a lag from when Allstate receives regulatory approval to adjust its prices to its impact on the book of business overall. In cash terms, this shows up as the change in premium written 3-4 months after approval. Likewise, GAAP revenue changes (premiums earned) show up about 3-4 months after the change in written premium is recorded.



Source: Company filings

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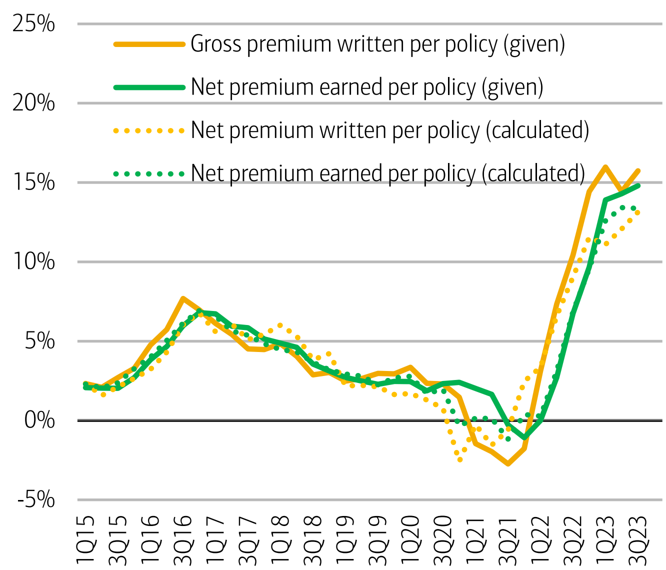
Exhibit 3: Year-over-year change in Allstate brand personal auto rate
Allstate gives investors the tools to understand the relationship between premium growth and pricing changes on a very granular basis. Also, aiming to reverse engineer these numbers by dividing average policycount into premiums leads investors to a similar conclusion, though disclosed premium per policy has exceeded the calculation of those same numbers in 2023.



Source: Company filings

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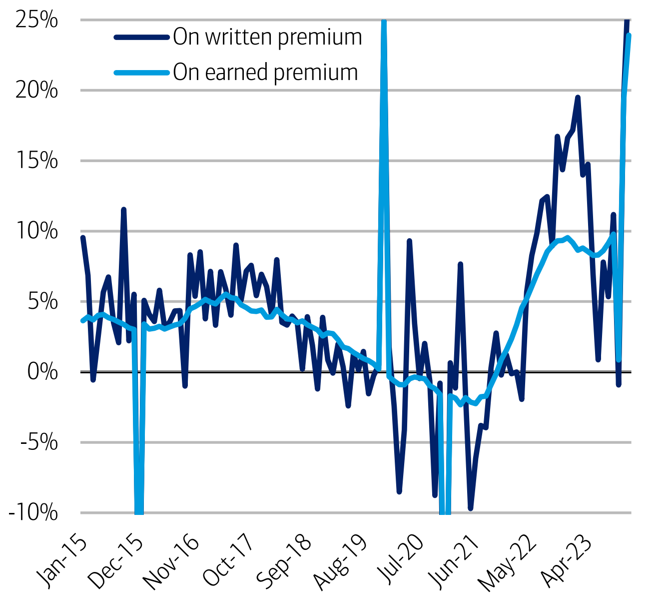
We bring up this disclosure at Allstate for illustrative purposes. In past notes, we have aimed to show, using this Allstate data, that the price change implied by regulatory rate change approvals precedes the change in price per policy on a written basis by 3-4 months, which, in turn, precedes the change in price per policy on an earned basis by another 3-4 months. This first lag occurs because, even after rate changes are improved, it will still be six months before all impacted policies experience the six-month anniversary of their policy coverage at which time they have to renew. And then, the second lag comes because it will take six months before a six-month policy amortizes the cash revenues associated with the policy into GAAP revenues. If this pattern fits for

Allstate, one might presume that it will work for Progressive as well and the "price x unit" volume forecasting would be a good predictor of revenue growth at Progressive. Unfortunately, the relationship among these numbers does not seem to hold up well for Progressive like it does for Allstate. Given that the numbers don't work well when solving for price per policy in the historical results at Progressive, we can hardly rely on them for predicting future revenue. One can see that the smoothness of the relationship among the Allstate numbers is not replicated among the Progressive numbers below.

Exhibit 4: Progressive Personal Auto change in Personal Lines premium per average Personal Auto policycount (year-over-year, monthly)

While measuring premium per policy on an earned basis shows a mostly smooth time series, this data is basically 3-4 months delayed in terms of indicating where Progressive pricing is. On a written basis, which would be more indicative, the results are extremely and confusingly volatile.



Source: Company filings

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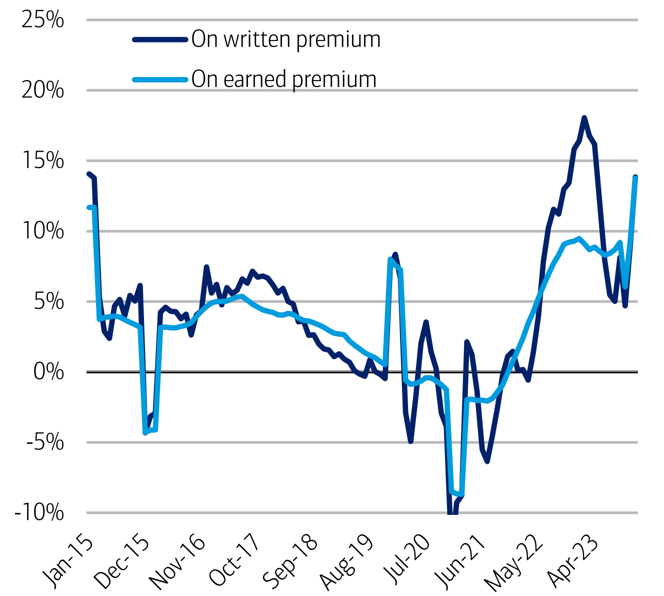
Exhibit 5: Progressive Personal Auto change in Personal Lines premium per avg. Personal Auto policycount (year-over-year, trailing 3 months)

Viewing this data on a trailing 3-month basis makes the time series more similar to how most companies report earnings: on a quarterly basis. Yet the volatility and asymmetry compared with the earned time series suggests shortcomings to "price x units" revenue forecasting.



Source: Company filings

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While the trend in net premium earned per policy seems to largely follow a smooth progression (excluding some very temporary major deviations in December once every few years that we will address in the next section) and in the ballpark of we know about Progressive's auto insurance pricing (on a six month lag), our "price x unit" volume heuristic had some trouble in being able to reasonably forecast net premium written. This began to become apparent to us last Spring (2023). In May, June and July of 2023 (when Progressive shares dipped and offered investors one of a handful of infrequent opportunities to buy the stock at more than a 10% discount to all-time highs), our forecasts for premium volume consistently overestimated Progressive's premium growth. For context, in Spring 2023, after experiencing too many losses from catastrophe activity and adverse prior-year development, the company cut back on marketing and restricted it underwriting appetite in service of aiming for its guiding principle of achieving a "96% or better" combined ratio for full-year 2023 (which was indeed achieved). Reflexively, one might argue that the company slowed its growth, so "of course" premium growth missed expectations.

However, it is not that simple. If Progressive "turns off the growth on April 30" and adds few next new customers in May, the change in the policycount growth rate would not be immediately perceptible. April results compare year-over-year with the prior April's policycount, boosted by all the net new customers added over the course of the year. May results compare year-over-year with the prior May's policycount, and, even though little growth would have occurred in the most recent May, the policycount is still boosted by the net new customers added over the preceding 11 months. Policycount growth doesn't change much from April to May. And rate? That takes many months to change. Rates need to be filed with their state regulators, and only a sixth of the portfolio experiences incremental rate change in a given month on a six-month policy (which represents the majority of Progressive's personal auto insurance policies). If the policycount growth isn't much changed and the effective rate isn't much changed, predicting premium growth shouldn't much change. Yet, we got our premium growth forecasts very wrong when Progressive pivoted away from growth in Spring 2023.

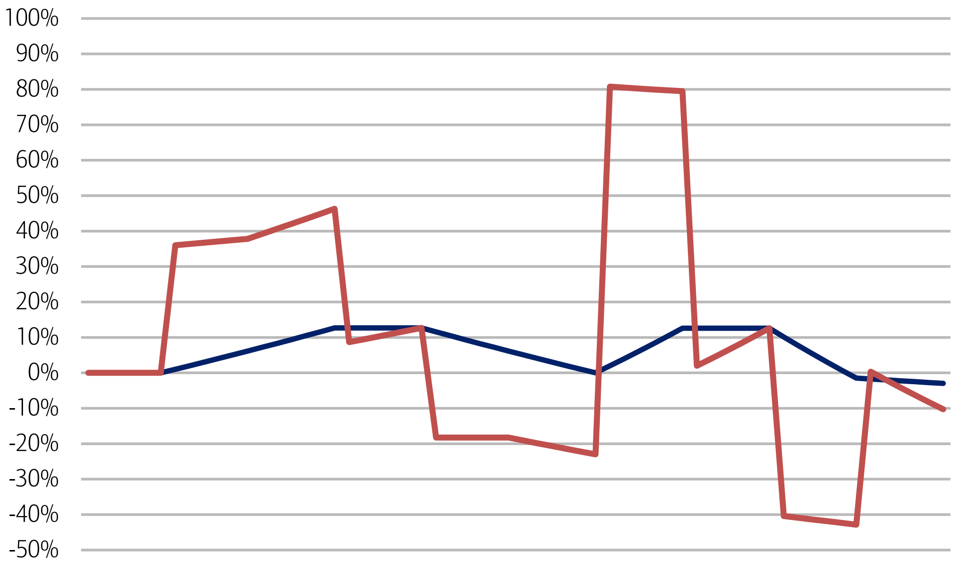
> It is difficult to track Progressive's change in premium per policy in real time using its net premium written disclosure.

To understand why, it may be useful to invent a new unit of measurement we will call "premium-months." Most Progressive personal auto policies are of a six-month duration. When Progressive writes a new auto policy it generally receives the full six months of premium upfront in cash (written premium), which amortizes into GAAP revenues in equal measure over the six-month policy life (earned premium). (This is not always the case. Progressive has some non-standard customers who pay for their coverage in monthly installments, and we would not be surprised if there were some preferred customers at Progressive who buy a special twelve-month policy.) It is probably not quite accurate but nonetheless reasonable to assume that policy renewals are spread equally across a six-month period. If a company like Progressive had a hypothetical twelve million personal auto policyholders, it would not be unreasonable to assume two million renew their six-month policies each month representing twelve million "premium-months" renewed in a given month or seventy-two million "premium-months" over the whole six-month period.

However, newly acquired policies do not appear to the company in a smooth pattern. The bulk of Progressive's annual new policycount growth tends to be disproportionately high in February through May, and it tends to grow faster when the company is heavily marketing and maximizing the aperture of its new policy embrace. Sometimes Progressive is growing quickly (as in 1Q23). Sometimes the company is conscientiously not growing (as in 2H23). When an insurer writes a new policy, it receives all the premium up front, or it receives six new "premium-months" (for six-month policies). This means that, during times of accelerated growth, the ratio of new "premium-months" to legacy renewing "premium-months" is noticeably higher than the ratio of new policies to legacy policies. Likewise, during phases of growth deceleration, the ratio of new-to-renewing "premium-months" will be lower than the ratio of new vs. renewing policies.

Exhibit 6: Relationship between annual change in hypothetical policycount and the change in "premium-months" assuming 100% retention and six-month policy life

During periods of policy growth, the year-over-year change in "premium-months" can rise very sharply. The blue line represents the change in the policycount, while the red line represents the change in 'premium-months.



Source: BofA Global Research

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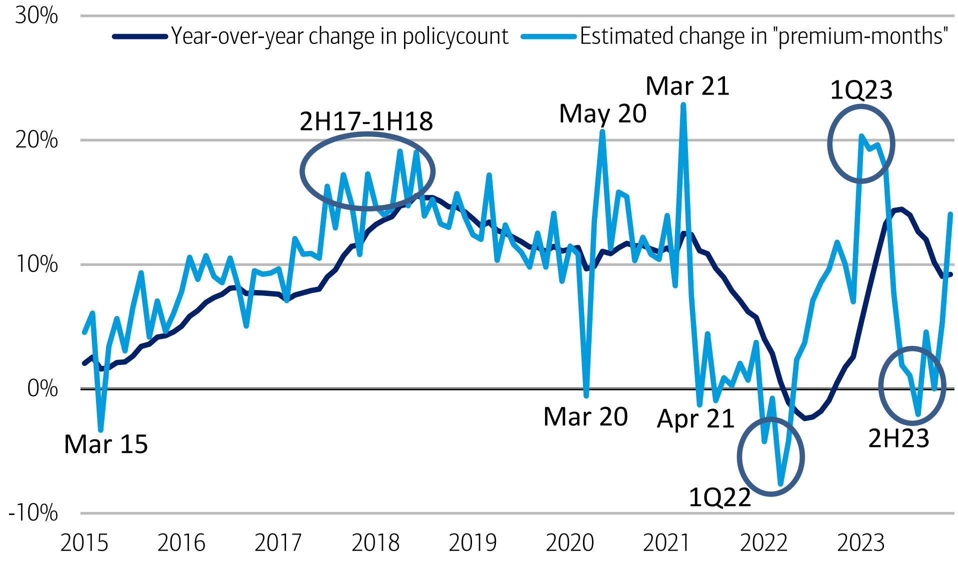
As a result, one should expect that net written premium growth would be poised to spike in excess of what "price x unit" volume would suggest during periods of policycount growth acceleration, while it will plummet during periods of deceleration in growth. And this is precisely what happened in the first third of 2023 where Progressive experienced some of the most rapid growth in the company's history only to pull the breaks on the growth in the middle part of the year as catastrophe losses and adverse prior-year development began to put the company's 96% guiding principle at risk for full-year 2023. Surging year-over-year "premium-month" growth in January through April were following by a steep drop in the year-over-year growth rate of "premium-month" growth in the middle part of the year despite the year-over-year change in pricing and policy count being fairly stable throughout. To accurately measure the policycount growth vs. "premium-month" growth, we would need to know Progressive's policycount retention, which we do not. However, we can make some assumptions that get us close to understanding the magnitude of the difference between these two variables.

Exhibit 7: Year-over-year change in Progressive Personal Auto policycount vs. "premium-months"

The calculation of net premiums written divided by policycount does not seem to accurately capture a proxy for the year-over-year change in rate. This may be because the outsized cash premium received at timed of accelerating growth, and the depressed cash premium received as growth decelerates. We believe our estimate of "premium-months" may better capture the unit volume growth rate for written premium or "cash" revenues.



Source: Company filings and BofA Global Research estimates

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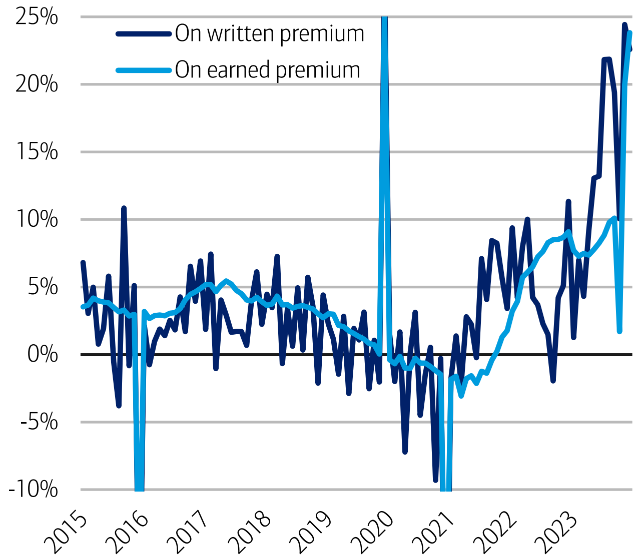
Switching from year-over-year change in policycount to estimated year-over-year change in "premium-months" helps in approximating the price per policy change as calculated by dividing into net premium written. When dividing growth in premium written by growth in estimated policy-months, it more closely resembles the number calculated by growth in net premium earned vs. policycount, AND it tends to produce an outcome where the rate on written premium is a predictor of the earned trend. One should compare Exhibits 8 and 9 (which use "premium-months" for written premium) against Exhibits 4 and 5 (raw data). Exhibits 8 and 9 help show a better approximation of the real trends.

Exhibit 8: Progressive Personal Auto change in Personal Lines premium per average Personal Auto "premium-months" (year-over-year, monthly)

Using "premium-months" as the denominator for solving for price using net premiums written shows a pattern that more closely conforms with the net premiums earned/policycount calculation AND tends to pre-date it by a few months.



Source: Company filings and BofA Global Research estimates

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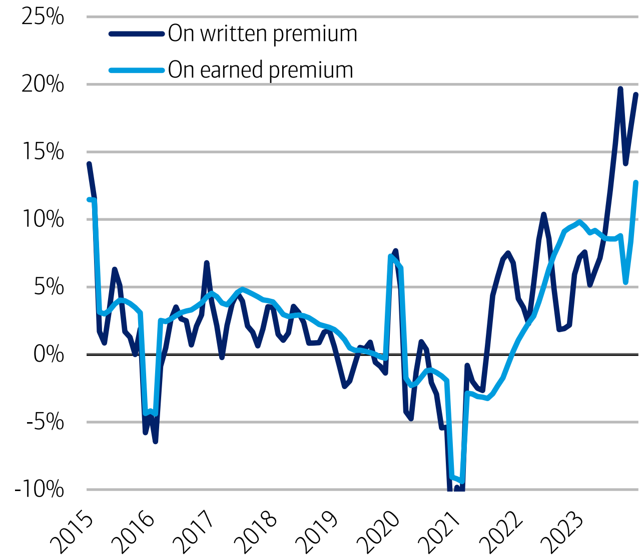
Exhibit 9: Progressive Personal Auto change in Personal Lines premium per average Personal Auto "premium-months" (year-over-year, trailing 3 months)

Using "premium-months" as the denominator for solving for price using net premiums written shows a pattern that more closely conforms with the net premiums earned/policycount calculation AND tends to pre-date it by a few months.



Source: Company filings and BofA Global Research estimates

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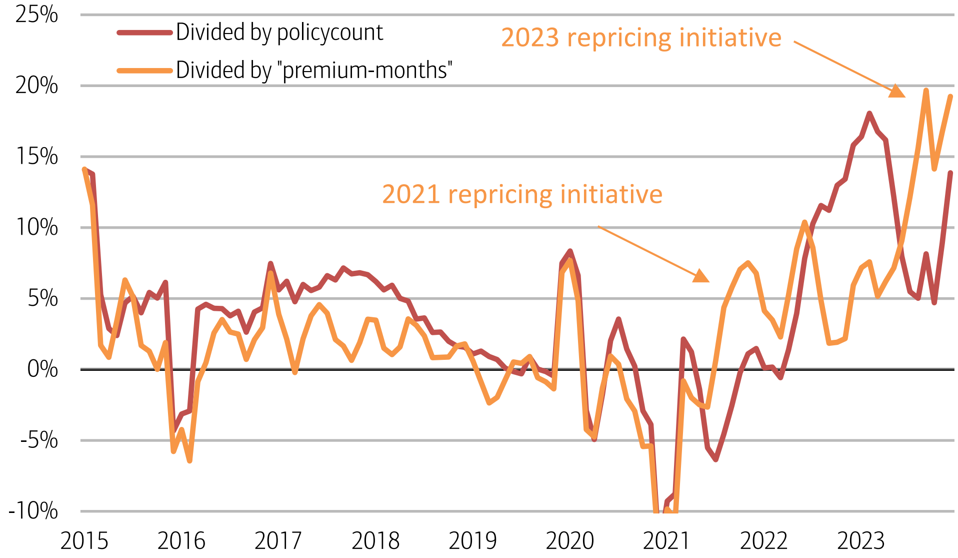
As evidence of the better accuracy of this method, one of the key things this change in methodology solves for is the correct timing of the repricing initiatives at Progressive. The company began a major repricing initiative in Spring 2021 and then again in Spring 2023. When dividing net premium written by policycount, it gives the impression of stagnant pricing in 2021, a pricing surge in 2022 and deceleration in 2023. We believe that the price acceleration in 2021 and 2023, which leads to GAAP revenue growth in 2022 and 2024 is the key feature on which investors should focus.

Exhibit 10: Progressive Personal Auto change in Personal Lines premium written per average Personal Auto policycount vs. per "premium-month" (year-over-year, trailing 3 months)

By tracking written rate as a function of "premium-months" as opposed to policycount, Progressive's pricing seems to track more closely with its commentary around pricing as well as broader market trends.



Source: Company filings and BofA Global Research estimates

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While this "premium-month" methodology is a better template for tracking the impact of pricing changes, it is far from perfect. There are several reasons for this: a) a slight mismatch in the numerator (Personal Lines premium, which includes motorcycles, snowmobiles, etc.) vs. the denominator (Personal Auto policycount, which excludes motorcycles, snowmobiles, etc.), b) a seasonality where it is unlikely that policies renewal in equal proportion year round, c) the impact of policy churn about which we only can estimate, d) the timing of holiday weekends where shopping propensity is different from other weekends and e) the noisy variability of short-term reporting (a single month). However, there is one other factor driving this variability: re-calendarization.

The Gregorian calendar "intervention"

On November 17, Progressive released its October 2023 earnings and included the following footnote to its results:

In October 2023, we converted our monthly accounting closing calendar to align with a traditional Gregorian calendar (e.g., January-31 days, February-28 or 29 days, March-31 days) as part of our multi-year financial enterprise resource planning effort to modernize certain of our financial systems and processes. Our prior fiscal financial closing calendar generally consisted of one 5-week month and two 4-week months in each quarter thus comprising a 52-week year. We do not expect that this change in the closing calendar will have a material impact on either our reported quarterly or annual underwriting results; however, it may impact year-over-year comparisons of monthly results from October 2023 through September 2024.

Historically, January premium numbers in Progressive's monthly releases were composed of 5 weeks (35 days) of revenue. February was 4 weeks (28 days) as was March and then April would again be 5 weeks (35 days). Four months with 5 weeks plus 8 months with 4 weeks led Progressive to report 52 weeks of earnings in a given year. Because 52 weeks is only 364 days and because February has a leap day every 4 years, December had a variable number of weeks depending on the year: in most years it was a 4-week month (28 days), but sometimes it had 5 weeks (35 days). This led to some unusual month-over-month results, particularly around the errant Decembers.

Exhibit 11: Days per month in Progressive premium disclosure

Progressive's new month reporting standard will create not-immaterial premium growth boosts and headwinds through September 2024.

	Prior	New	Impact
Oct. 23	35	31	-11.4%
Nov. 23	28	30	+7.1%
Dec. 23	28	31	+10.7%
Jan. 24	35	31	-11.4%
Feb. 24	28	29	+3.6%
Mar. 24	28	31	+10.7%
Apr. 24	35	30	-14.3%
May 24	28	31	+10.7%
June 24	28	30	+7.1%
July 24	35	31	-11.4%
Aug. 24	28	31	+10.7%
Sept. 24	28	30	+7.1%
Oct. 24	31	31	0.0%
Nov. 24	30	30	0.0%
Dec. 24	31	31	0.0%
Jan. 25	31	31	0.0%
Feb. 25	29	28	-3.4%

Source: Company filings

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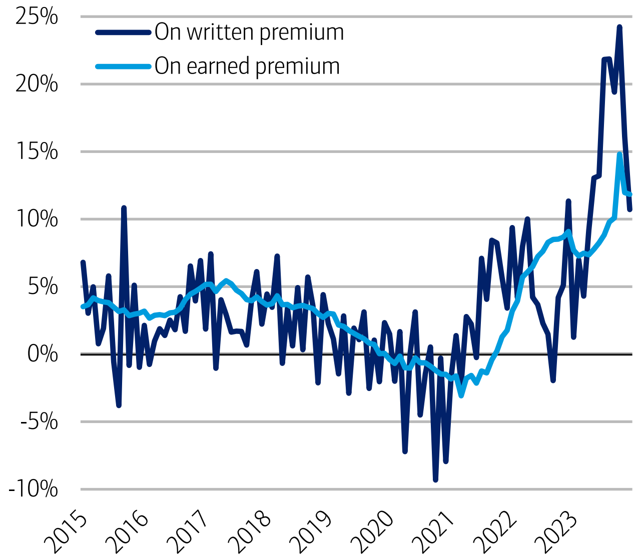
Going forward, months will have the number of days of premium revenue as equal to their number of days on the calendar. This means that January, formerly a 35-day month for Progressive, will now have 31 days (11.4% fewer days). February, which typically has 28 days and was formerly a 28-day month for Progressive, has a leap day in 2024 and will be a 29-day month (3.6% more days in 2024). March, formerly a 28-day month, will now be a 31-day month (10.7% more days in 2024), but April, formerly a 35-day month, will now have just 30 days going forward (14.2% fewer days in 2024). Through September 2024, these changes in the calendarization are going to have positive and negative impacts on Progressive's premium volume (and February 2025 will have one fewer day that February 2024, 3.4% fewer). Adjusting for this last quirk, we represent the same data in Exhibits 4/5 and 8/9. (In the future, this new calendarization will create a new quirk: a variable number of weekends in a 30-day or 31-day month. More people tend to shop for auto insurance on the weekends leading to more growth expected in a 5-weekend, 31-day month compared with a 4-weekend, 31-day month.)

Exhibit 12: Progressive Personal Auto change in Personal Lines premium per average Personal Auto "premium-month" (year-over-year, monthly, calendar-"corrected")

Monthly reporting still creates volatility in results, but the general trend for rate at Progressive is positive when making adjustments for the many quirks. We believe this augurs for a notable earned premium beat vs. consensus.



Source: Company filings and BofA Global Research estimates

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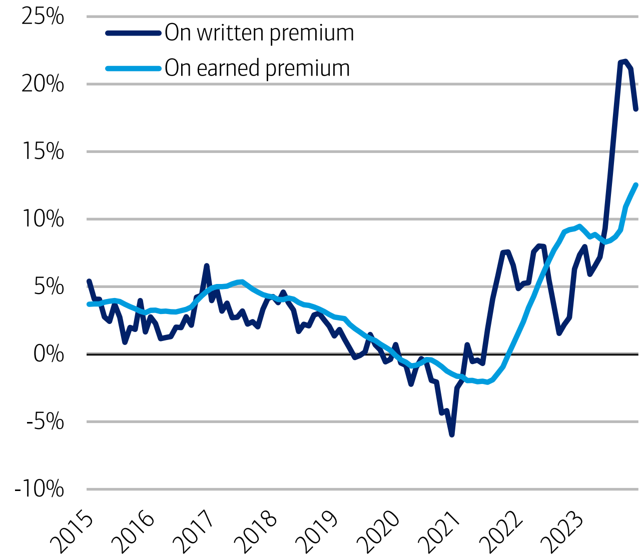
Exhibit 13: Progressive Personal Auto change in Personal Lines premium per average Personal Auto "premium-month" (year-over-year, trailing 3 months, calendar-"corrected")

Monthly reporting still creates volatility in results, but the general trend for rate at Progressive is positive when making adjustments for the many quirks. We believe this augurs for a notable earned premium beat vs. consensus.



Source: Company filings and BofA Global Research estimates

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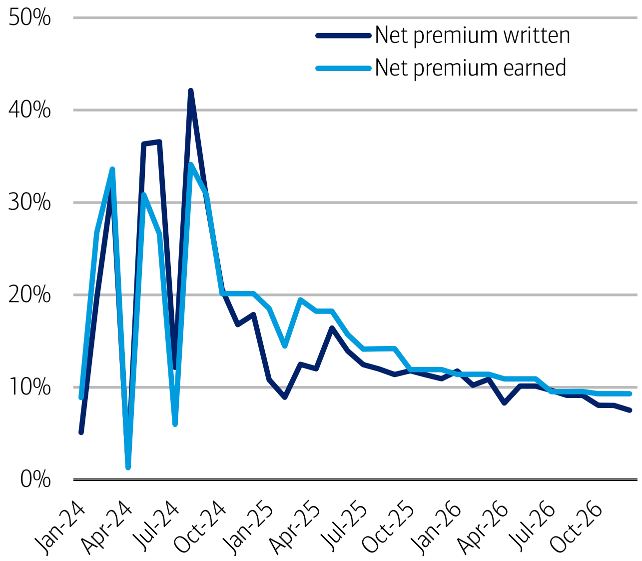
Headed into 2024, the rate that Progressive was writing in late 2023 will become rate that is earned into the income statement. We expect this to be positive for 2024 revenue and earnings as well as certainly higher than consensus.

Putting this all together: expect accelerating growth

This extended revenue analysis may seem picayune, but it does a lot to explain the material gap between our forecast and consensus results. Given our expectation of 21.5% Personal Lines net written premium growth vs. consensus of 14.5% in 2024, it may be worthwhile to highlight the variances. First, our forecast has some unusual quirks in the progression of the numbers. Given our forecast for single-digit premium growth in January, April and July 2024, the pattern should be made clear to investors in advance of what might otherwise be construed as January, April and July 2024 misses.

Exhibit 14: BofA forecast for Progressive Personal Auto premium (monthly)

We expect Progressive to handily exceed consensus revenue forecasts in 2024, but there is going to be a lot of volatility in the monthly results due to the adoption of the new calendarization.



Source: BofA Global Research estimates

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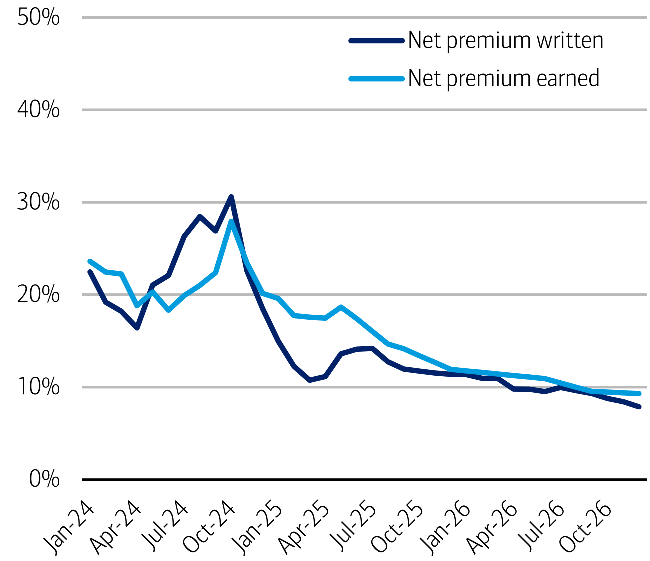
Exhibit 15: BofA forecast for Progressive Personal Auto premium (trailing 3 months)

The volatility is smoothed by looking at it on a trailing-3-month basis. It is worthwhile to note, unlike the consensus forecast, we believe revenue growth will accelerate in 2H24.



Source: BofA Global Research estimates

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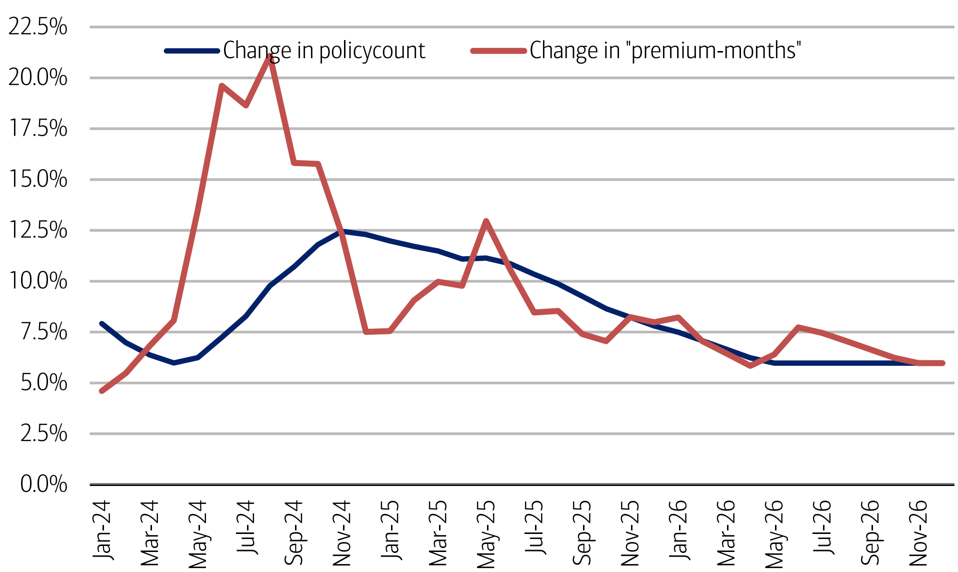
Cutting through the volatility, however, one will note that, while consensus anticipates premium volume (written and earned) to decelerate in 2H24, we expect it to accelerate. This is due to very easy prior year comparables in terms of "premium-months." Progressive chose to close its appetite to material new business in 2H23 and shrank. This means "premium-months" were depressed in 2H23. As Progressive reopens to new business in 2024 and presumable across the whole year, it will make for easy year-over-year comparables, particularly compared with the depress "premium-months" or 2H23.

Exhibit 16: Year-over-year change in policy unit: policycount vs. "premium-months"

To understand why our BofA growth forecast is so much higher than consensus, we would point investors to our expectation of a 2H24 surge in estimated "premium-months."



Source: BofA Global Research estimates

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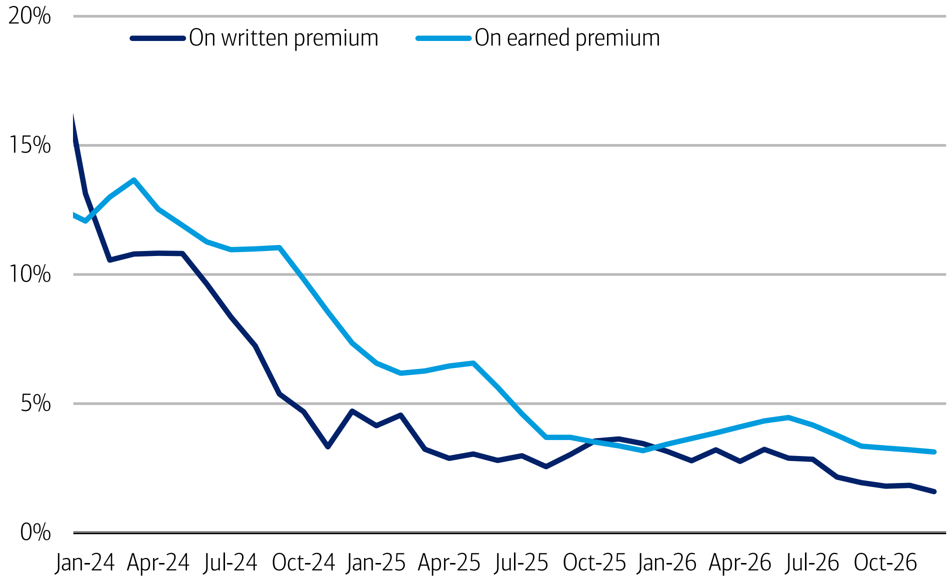
The increase is almost entirely “unit volume” (policycount and “premium-months”). On the basis of “rate,” we forecast material deceleration over the next three years.

Exhibit 17: Year-over-year price per policy change expectation in our Progressive premium forecast (trailing 3 months)

Our forecast assumes pricing at Progressive decelerates over the next 5 quarters, hovering in the 3-5% range beginning in 2Q25.



Source: BofA Global Research estimates

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We expect pricing to inflect to the low- to mid-single-digit range in mid-2025. Arguably, there could be upside to our forecast. We are assuming an end to the current hard market in U.S. auto insurance. This is based on believing that the cyclicality of the market will kick in. That said, we have no proprietary confidence in our estimate of the timing of that deceleration. If anything, our high-on-the-Street revenue forecast, we believe, runs the risk of being “too low.”

Price objective basis & risk

Progressive (PGR)

Our $242 price objective is based on the current S&P 500 P/E multiple for 2025 of 18.1x on our 2025E EPS forecast. Due to quickly accelerating EPS ahead of the market growth rate, as seen in 2016-2019, we believe Progressive shares should trade at a premium to market as its earnings accelerate. However, given a multiple valuation two years out, we only assume parity due to the necessarily decreased certainty in an out-year forecast.

Downside risks to our PO are 1) presented by the pressure from lower interest rates, causing a decline in earnings power and potentially leading the company to miss our EPS expectations, 2) the volatility associated with catastrophes, which also creates the risk of missing and exceeding our EPS outlook, 3) the impact of material pricing changes by major competitors, 4) the long-term impact of emergent technologies, such as ride-sharing applications and autonomously driven automobiles.

Analyst Certification

I, Joshua Shanker, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Insurance Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Aflac	AFL	AFL US	Joshua Shanker
	Allstate Corp.	ALL	ALL US	Joshua Shanker
	American International Group	AIG	AIG US	Joshua Shanker
	Arch Capital	ACGL	ACGL US	Joshua Shanker
	Assurant	AIZ	AIZ US	Grace Carter, CFA
	Axis Capital	AXS	AXS US	Joshua Shanker
	BRP Group, Inc.	BRP	BRP US	Joshua Shanker
	Cincinnati Financial Corporation	CINF	CINF US	Grace Carter, CFA
	Corebridge Financial	CRBG	CRBG US	Joshua Shanker
	Everest Group Ltd	EG	EG US	Joshua Shanker
	Intact Financial	YIFC	IFC CN	Grace Carter, CFA
	Intact Financial	IFCZF	IFCZF US	Grace Carter, CFA
	MetLife	MET	MET US	Joshua Shanker
	Progressive	PGR	PGR US	Joshua Shanker
	RenaissanceRe	RNR	RNR US	Joshua Shanker
	The Hartford	HIG	HIG US	Joshua Shanker
	Voya	VOYA	VOYA US	Joshua Shanker
	W.R. Berkley	WRB	WRB US	Joshua Shanker
NEUTRAL				
	Aon	AON	AON US	Joshua Shanker
	Brown & Brown	BRO	BRO US	Grace Carter, CFA
	CNA Financial	CNA	CNA US	Joshua Shanker
	Lincoln National	LNC	LNC US	Joshua Shanker
	Marsh McLennan	MMC	MMC US	Joshua Shanker
	Principal Financial Group	PFG	PFG US	Joshua Shanker
	Prudential Financial	PRU	PRU US	Joshua Shanker
	The Hanover	THG	THG US	Grace Carter, CFA
	Trupanion	TRUP	TRUP US	Joshua Shanker
	Unum	UNM	UNM US	Joshua Shanker
UNDERPERFORM				
	Arthur J. Gallagher & Co.	AJG	AJG US	Joshua Shanker
	Chubb Ltd	CB	CB US	Joshua Shanker
	Goosehead Insurance Inc.	GSHD	GSHD US	Joshua Shanker
	Selective	SIGI	SIGI US	Grace Carter, CFA

US - Insurance Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Travelers Cos	TRV	TRV US	Joshua Shanker
	Willis Towers Watson	WTW	WTW US	Joshua Shanker

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Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5 Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings	**Numerator**	**Denominator**
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt – Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit	**Numerator**	**Denominator**
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap = Current Share Price × Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price × Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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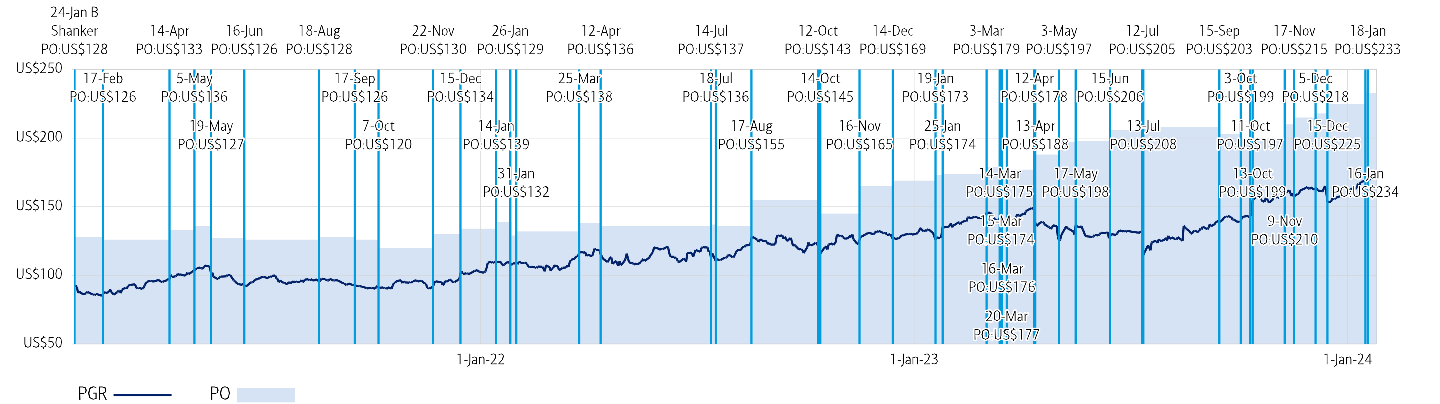
Disclosures

Important Disclosures

Progressive Corp (PGR) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Financial Services Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	156	53.79%	Buy	94	60.26%
Hold	72	24.83%	Hold	48	66.67%
Sell	62	21.38%	Sell	35	56.45%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

[R1] Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R2]
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R2] Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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