S&P Capital IQ

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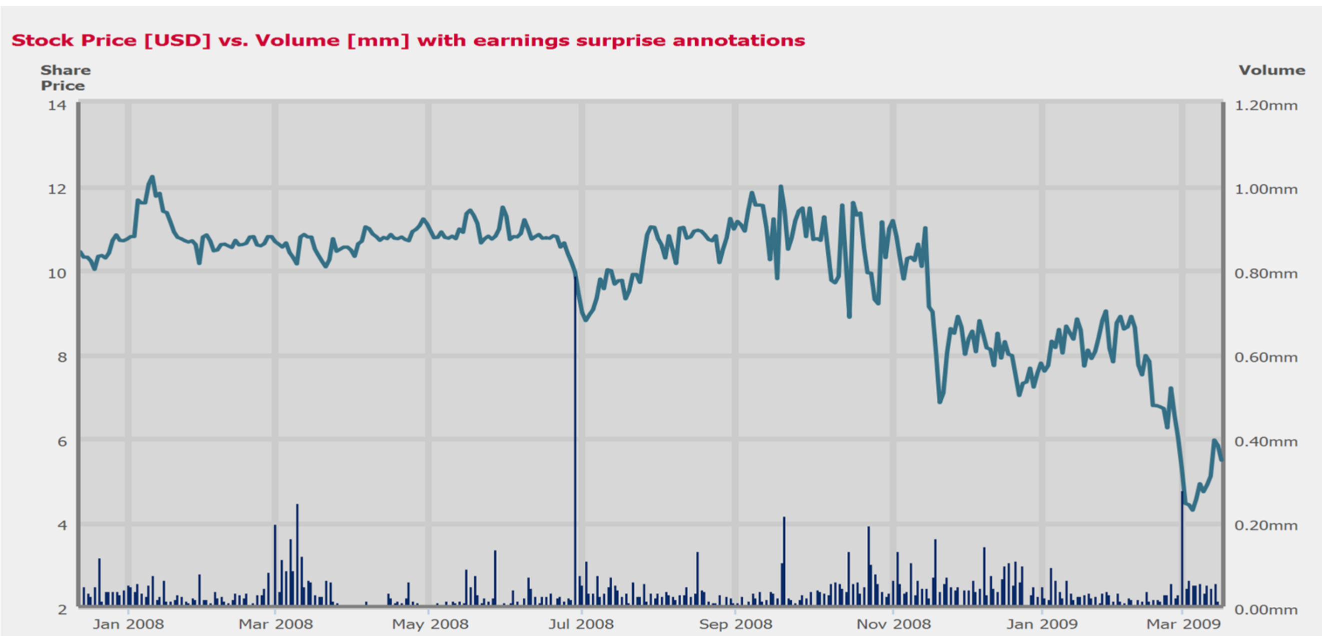

Call Participants

EXECUTIVES

Michael Gene Barnes
Executive Chairman

Sandra E. Bell
Chief Financial Officer

Presentation

Operator

Greetings, and welcome to the Tiptree Financial Inc. Second Quarter 2016 Earnings Call. [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Ms. Sandra Bell, Chief Financial Officer of Tiptree. Thank you, you may begin.

Sandra E. Bell
Chief Financial Officer

Good morning, and welcome to our second quarter 2016 earnings call. I am joined today by our Executive Chairman, Michael Barnes. We have posted the earnings release and presentation on our website at tiptreefinancial.com. The presentation provides supplemental information to our prepared remarks, which we will refer to by page during the call.

Our remarks today are qualified in their entirety by the disclaimers on Page 1 of the presentation. Prior to turning the call over to Michael, I just want to highlight a few of the key points. The presentation supplements are SEC filings, and is provided solely for information purposes. Throughout the presentation, there are forward-looking statements. Our businesses are subject to risks and uncertainties, which are outlined in our SEC filings, and which could impact our expectations of future results. Except as required by securities laws, we undertake no obligation to update any forward-looking statements.

We also use non-GAAP measures, which we believe provide additional information useful to investors. As these measures are not GAAP, they should not be used as a substitute for our GAAP disclosures. The appendix provides a reconciliation of each of these non-GAAP measures to their GAAP equivalent.

Having reviewed these disclaimers, let me turn the call over to Michael.

Michael Gene Barnes
Executive Chairman

Thanks, Sandra. Good morning, everyone, and thank you for joining us today. For the quarter, we continued to see positive trends across our businesses. On a consolidated basis, total revenues grew 32% year-over-year to $134 million, while contributing $7 million of net income, and $17.4 million of adjusted EBITDA from continuing operations. Both of these operating metrics were up significantly versus comparable periods in 2015.

We continue to execute against our strategic priorities. On Page 3, we summarized some of our key achievements for the second quarter. Fortegra continues to build positive momentum with another strong quarter. The insurance and warranty net-written premiums grew to $96 million for the first half, up 23% versus last year. Pretax income and adjusted EBITDA were $8.1 million and $11.4 million respectively, continuing the positive earnings trends from Q1.

With A.M. Best upgrade, Fortegra's CEO, Rick Kahlbaugh, and his team expect to see steady growth through expanding product originations, and adding clients. In addition, we are focused on investing the excess premium flow to enhance investment returns.

With our specialty finance segment, the mortgage business bounced back, originating $432 million of volume, up 30% over the first quarter. A stable housing market and low interest rates were key drivers for the increase, as refinancings and the home selling season supported origination.

Care, our senior housing business, contributed $15 million revenues, while expanding NOI margins, as actions taken to improve property occupancy levels, and stabilized costs are flowing through the bottom line. The senior housing pipeline remains strong, and we anticipate continued growth through new acquisitions and NOI improvements at existing properties.

We recently closed our third managed property acquisition of the year on August 1 for $29 million. Our Telos Asset Management business continues to produce steady cash flow, as we received nearly $12 million of cash from management fees and distributions on our subordinated note holdings year-to-date.

We saw positive results from our principal investments, with $7.5 million of revenue in the second quarter, primarily driven by our credit opportunities fund, and investments in nonperforming mortgages. These investments have been a big driver of our year-over-year increase in profits, as both investments were ceded in second quarter 2015.

From a capital allocation perspective, we had a busy quarter, reinvesting in our core businesses, as well as redeploying capital to increase shareholder value. For the core business, we invested approximately $11 million in NPL, bringing the total portfolio to $62 million. We allocated $26 million of capital from the Telos 7 warehouse for the launch of our 7 CLO. The largest transaction of the quarter was a block purchase of $5.6 million shares of Tiptree for $36.4 million. This transaction was completed at a 29% discount to book, accretive to both book value and earnings per share.

On the bottom of the page, we highlight book value for Class A share, which increased by 9.7% from $8.96 at year-end to $9.83 as of June 30. Growth in book value was the result of strong earnings, our share buyback program, and a large block purchase. On a pro forma basis, we estimate an additional $0.05 of earnings per Class A share, assuming that the repurchase that occurred on January 1.

With that, I will hand it back to Sandra, who will discuss the financial results.

Sandra E. Bell
Chief Financial Officer

Thank you, Michael. As Michael mentioned, our second quarter results were up across the board, with all of our segments contributing.

On a per share basis, earnings per Class A share, both overall and from continuing operations, was $0.17 per share. Earnings per Class A share from continuing operations were up $0.20 from the prior year, while overall net income for Class A share decreased over the prior year due to $21 million or $0.50 per share of discontinued operations in the second quarter of 2015. Of that amount, $16.3 million related to the gain on the sale of PFG.

While total stockholders equity is down on absolute terms since year end, primarily as a result of the block purchase that we executed at the end of June, book value per Class A share grew $0.87 or 9.7%, as a result of both earnings performance, and the block purchase below book.

Just a quick accounting note, the shares we bought back through the block purchase are held at subsidiary, but are treated as treasury shares under GAAP. These shares are being reserved for future uses, which range from potential acquisition currency to compensation.

On Page 5, we've laid out the components of our first half 2016 operating performance, which mirrors the second quarter trends. In short, each of our segments were also up double digits for revenue, pretax income, and adjusted EBITDA from continuing operations. In total, revenue has grown $75.5 million, pretax income from continuing operations was up $23.4 million, and adjusted EBITDA from continuing operations increased by $20.8 million versus the first half of 2015.

The high level themes are similar to the second quarter results. Fortegra's profits have increased, driven by growth in written premiums, net revenues, investment income, and margin expansion, stemming from disciplined cost management. Our senior housing performance is up as NOI margins have improved at existing properties, and acquisitions have increased our overall revenue and pretax earnings.

Improvement in volumes and margins in the mortgage business with the acquisition of Reliance, and growth in Siena's loan portfolio drove positive results in specialty finance. And principal investments are up substantially, primarily driven by realized and unrealized gains as well as earnings on the credit opportunities fund, and NPLs, which have helped to offset increased corporate costs. With that, we will now transition to a more detailed analysis of each segment's performance and outlook.

Page 7 highlights 4 metrics that we use to measure our insurance and insurance services segment, as adjusted revenue, as adjusted net revenues, adjusted EBITDA, and net written premiums.

The as-adjusted revenue measures are non-GAAP measures because they remove the purchase accounting adjustments from their comparable GAAP metrics. We use these metrics to analyze the relative performance of the business year-over-year.

For the quarter, adjusted EBITDA was $11.4 million, up 24% from the prior year, as adjusted net revenues were up approximately $1 million or 3%, as a result of improvements in investment income. Operating expenses were down $1.4 million due to the continued cost discipline.

For the first half, we saw year-over-year improvements in net revenues from credit protection and specialty products, slightly offset by ongoing competitive pressures in the mobile protection product. Net written premium, a volume metric, and a leading indicator of future revenues, increased by 23%, with all 3 product lines gaining momentum over the first half. This is particularly encouraging as warranty net written premiums reversed trend, and were up almost 27%. For the second half of the year, while we expect earnings growth to be supported by expansion in product revenue and investment income, the pace of growth may be tempered relative to that seen this quarter, and in the first half.

Moving to our specialty finance segment on Page 8, pretax income was $2.3 million for the second quarter, a $1.7 million increase over 2015. This was driven by the addition of Reliance and its mix of FHA/VA products, which also led to a 229 basis points increase in mortgage margins.

Single-family mortgage originations for the overall market were up 47% versus the first quarter of 2016, which was driven by favorable market conditions, and lower interest rates, but were flat versus the second quarter of 2015.

For the first half, pretax income is up 30%, as a result of increased originations, which were slightly offset by additional personnel and marketing expenses. We invested in additional loan officer headcount, which was up approximately 20% from last year, with the strategy to gain additional market share and volume in the second half of 2016 and beyond.

Siena, our middle market lending platform, also added to the improved performance with average earning assets up 25%.

Turning to the real estate segment on the following page, we continued to see improvements, as a result of additional acquisitions, and improving margins on existing properties. Pretax income improved by 41% in the quarter versus the same period in 2015, and was up 18.5% year-to-date, despite added depreciation from new acquisitions.

Adjusted EBITDA for the quarter was $2.3 million, up 15% from last year, driven by NOI increases of 21%. The acquisitions over the last 18 months were primarily managed properties, where we partner with existing operators to focus on the facilities that are undergoing enhancements to allow them to operate more efficiently.

On the bottom left of the page, you can see the improvements to date, as NOI margins on managed properties are up from 24.2% to 26%. As the newer facilities ramp up and stabilize, we expect our results to continue to improve. In addition to growing organically, we are continuing to invest, and we expect to acquire additional properties in the second half of 2016.

For asset management, on Page 10. The second quarter of -- for the second quarter of 2016, pretax income was up nearly $1 million year-over-year, primarily attributable to the normalization of our incentive compensation accruals versus 2015. We expect to see modest increases in fee revenue in subsequent quarters, as a result of the Telos 7 issuance, and are continuing to pursue opportunities to increase AUM for this segment.

Turning to the corporate and other segment on Page 11, our second quarter pretax income was up by $7.4 million from the prior year. Key drivers include improvements in our CLO equity performance of $5.1 million over the second quarter of 2015, as a result of increased distributions, and recovery of prior unrealized credit marks on our subordinated notes in Telos 5 and 6, earnings of $3.2 million from interest income on our credit investments, and sales of our remaining warehouse loans. $1.3 million from our NPL investments, as we begin to see the impact of early realizations and loan modifications, all of which was offset by increases in payroll of $0.3 million, as we have increased our staffing and augmented our SEC reporting expertise in the finance and accounting team, and increases in external costs of $3 million related to audit fees and additional stocks expenses.

For the first half, performance of our corporate segment was a big contributor, with increases in adjusted EBITDA of $11.8 million, driven by returns on principal investments added in the second half of 2015. Costs are up year-over-year, although we feel our infrastructure is vastly improved, and approximately $2 million of the cost increase was associated with material weakness remediation that should not repeat going forward.

Now I will pass it back to Michael for a wrap.

Michael Gene Barnes
Executive Chairman

For the summarized Tiptree's results for the quarter and the first half, we are pleased with our first half performance given the significant improvements in all of our performance measures related to continuing operations versus the prior year.

Our focus for our core business is to support growth of repeatable earnings. And we are optimistic that we will continue to see growth in our core businesses through the remainder of this year.

Our insurance sector was ahead of expectations. And with the A.M. Best upgrade, we are optimistic that revenues will grow through increased product originations, and returns on the investment pool.

Our real estate sector made further acquisitions to senior care facilities, and continues to increase revenue and NOI. Our asset management sector is stable. And in addition to CLOs, we are leveraging our strong performance and credit opportunities, to assess the potential for raising additional capital in other fund vehicles from managed accounts. Our specialty finance sector had a strong second quarter. We are investing in the expansion of the existing business by increasing our loan officers, which should yield improved production in the future.

Our corporate and other sector pretax earnings were positive, as the improved performance of our principal investments more than offset the growth in our company's administrative expenses. And importantly, for the second half of the year, we are focused on driving additional progress on this year's objectives of exiting noncore underperforming assets, reallocating that capital to existing core businesses, and further building out our infrastructure.
And now we're happy to take your questions.

Question and Answer

Operator

[Operator Instructions] Thank you. At this time, I'd like to turn the floor back over to Ms. Bell for any closing comments.

Sandra E. Bell
Chief Financial Officer

Thank you, Donna. And thanks to everyone for joining us today. If you have any questions, please feel free to reach out to me directly. We look forward to speaking with you again after the third quarter results are in. This concludes our conference call.

Operator
Ladies and gentlemen, thank you for your participation. This concludes today's teleconference. You may disconnect your lines at this time, and have a wonderful day.