

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

- ☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the period ended March 31, 2020
- ☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from                      to  
Commission file number 001-36157

**ESSENT GROUP LTD.**

(Exact name of registrant as specified in its charter)

**Bermuda**

(State or other jurisdiction of  
incorporation or organization)

**Not Applicable**

(I.R.S. Employer  
Identification Number)

**Clarendon House  
2 Church Street**

**Hamilton HM11, Bermuda**

(Address of principal executive offices and zip code)

**(441) 297-9901**

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class              | Trading Symbol(s) | Name of each exchange on which registered |
|----------------------------------|-------------------|-------------------------------------------|
| Common Shares, \$0.015 par value | ESNT              | New York Stock Exchange                   |

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232-405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files.) Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

- |                         |                                     |                           |                          |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer         | <input type="checkbox"/> |
| Non-accelerated filer   | <input type="checkbox"/>            | Smaller reporting company | <input type="checkbox"/> |
|                         |                                     | Emerging growth company   | <input type="checkbox"/> |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒  
The number of the registrant's common shares outstanding as of May 1, 2020 was 98,623,303.

Essent Group Ltd. and Subsidiaries

Form 10-Q

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*Unless the context otherwise indicates or requires, the terms “we,” “our,” “us,” “Essent,” and the “Company,” as used in this Quarterly Report on Form 10-Q, refer to Essent Group Ltd. and its directly and indirectly owned subsidiaries, including our primary operating subsidiaries, Essent Guaranty, Inc. and Essent Reinsurance Ltd., as a combined entity, except where otherwise stated or where it is clear that the terms mean only Essent Group Ltd. exclusive of its subsidiaries.*

## **SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This Quarterly Report on Form 10-Q, or Quarterly Report, includes forward-looking statements pursuant to the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts or present facts or conditions, such as statements regarding our future financial condition or results of operations, our prospects and strategies for future growth, the introduction of new products and services, and the implementation of our marketing and branding strategies. In many cases, you can identify forward-looking statements by terms such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “potential” or the negative of these terms or other comparable terminology.

The forward-looking statements contained in this Quarterly Report reflect our views as of the date of this Quarterly Report about future events and are subject to risks, uncertainties, assumptions and changes in circumstances that may cause events or our actual activities or results to differ significantly from those expressed in any forward-looking statement. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future events, results, actions, levels of activity, performance or achievements. A number of important factors could cause actual results to differ materially from those indicated by the forward-looking statements, including, but not limited to, those factors described below, in Part I, Item 2 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Quarterly Report, and in Part I, Item 1A “Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2019 filed with the Securities and Exchange Commission. These factors include, without limitation, the following:

- the duration, spread and severity of the COVID-19 outbreak, which is currently ongoing and still evolving; the actions taken to contain the virus or treat its impact, including government and GSE actions to mitigate the economic impact of the outbreak; the nature and extent of the forbearance and modification options available to borrowers affected by the outbreak on mortgages we insure; reserve and other accounting estimates relating to the impact of the COVID-19 outbreak; borrower behavior in response to the outbreak and its economic impact; how quickly and to what extent normal economic and operating conditions can resume, including whether any future outbreaks interrupt economic recovery; how quickly and to what extent affected borrowers can recover from the negative economic impact of the outbreak; and whether and to what extent the outbreak and related economic conditions will exacerbate other risks and uncertainties facing our business, financial condition and business strategy;
- changes in or to Fannie Mae and Freddie Mac, which we refer to collectively as the GSEs, whether through Federal legislation, restructurings or a shift in business practices;
- failure to continue to meet the mortgage insurer eligibility requirements of the GSEs;
- competition for our customers or the loss of a significant customer;
- lenders or investors seeking alternatives to private mortgage insurance;
- increase in the number of loans insured through Federal government mortgage insurance programs, including those offered by the Federal Housing Administration;
- decline in the volume of low down payment mortgage originations;
- uncertainty of loss reserve estimates;
- decrease in the length of time our insurance policies are in force;
- deteriorating economic conditions;
- recently enacted U.S. Federal tax reform and its impact on us, our shareholders and our operations;

- the definition of “Qualified Mortgage” reducing the size of the mortgage origination market or creating incentives to use government mortgage insurance programs;
- the definition of “Qualified Residential Mortgage” reducing the number of low down payment loans or lenders and investors seeking alternatives to private mortgage insurance;
- the implementation of the Basel III Capital Accord, which may discourage the use of private mortgage insurance;
- management of risk in our investment portfolio;
- fluctuations in interest rates;
- inadequacy of the premiums we charge to compensate for our losses incurred;
- dependence on management team and qualified personnel;
- disturbance to our information technology systems;
- change in our customers’ capital requirements discouraging the use of mortgage insurance;
- declines in the value of borrowers’ homes;
- limited availability of capital or reinsurance;
- unanticipated claims arise under and risks associated with our contract underwriting program;
- industry practice that loss reserves are established only upon a loan default;
- disruption in mortgage loan servicing;
- risk of future legal proceedings;
- customers’ technological demands;
- our non-U.S. operations becoming subject to U.S. Federal income taxation;
- becoming considered a passive foreign investment company for U.S. Federal income tax purposes; and
- potential restrictions on the ability of our insurance subsidiaries to pay dividends.

Readers are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on these forward-looking statements. All of the forward-looking statements we have included in this Quarterly Report are based on information available to us on the date of this Quarterly Report. We undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise, except as otherwise required by law.

# PART I — FINANCIAL INFORMATION

## Item 1. Financial Statements (Unaudited)

### Essent Group Ltd. and Subsidiaries

#### Condensed Consolidated Balance Sheets (Unaudited)

| (In thousands, except per share amounts)                                                                           |           | March 31,<br>2020 | December 31,<br>2019 |
|--------------------------------------------------------------------------------------------------------------------|-----------|-------------------|----------------------|
| <b>Assets</b>                                                                                                      |           |                   |                      |
| Investments                                                                                                        |           |                   |                      |
| Fixed maturities available for sale, at fair value (amortized cost: 2020 — \$3,061,177; 2019 — \$2,967,225)        | \$        | 3,110,362         | \$ 3,035,385         |
| Short-term investments available for sale, at fair value (amortized cost: 2020 — \$595,173; 2019 — \$315,360)      |           | 595,165           | 315,362              |
| Total investments available for sale                                                                               |           | 3,705,527         | 3,350,747            |
| Other invested assets                                                                                              |           | 75,380            | 78,873               |
| Total investments                                                                                                  |           | 3,780,907         | 3,429,620            |
| Cash                                                                                                               |           | 31,055            | 71,350               |
| Accrued investment income                                                                                          |           | 18,572            | 18,535               |
| Accounts receivable                                                                                                |           | 41,228            | 40,655               |
| Deferred policy acquisition costs                                                                                  |           | 15,147            | 15,705               |
| Property and equipment (at cost, less accumulated depreciation of \$58,517 in 2020 and \$57,639 in 2019)           |           | 16,325            | 17,308               |
| Prepaid federal income tax                                                                                         |           | 261,885           | 261,885              |
| Other assets                                                                                                       |           | 21,815            | 18,367               |
| <b>Total assets</b>                                                                                                | <b>\$</b> | <b>4,186,934</b>  | <b>\$ 3,873,425</b>  |
| <b>Liabilities and Stockholders' Equity</b>                                                                        |           |                   |                      |
| Liabilities                                                                                                        |           |                   |                      |
| Reserve for losses and LAE                                                                                         | \$        | 73,341            | \$ 69,362            |
| Unearned premium reserve                                                                                           |           | 264,134           | 278,887              |
| Net deferred tax liability                                                                                         |           | 259,688           | 249,620              |
| Credit facility borrowings (at carrying value, less unamortized deferred costs of \$620 in 2020 and \$763 in 2019) |           | 424,380           | 224,237              |
| Other accrued liabilities                                                                                          |           | 58,317            | 66,474               |
| Total liabilities                                                                                                  |           | 1,079,860         | 888,580              |
| Commitments and contingencies (see Note 7)                                                                         |           |                   |                      |
| Stockholders' Equity                                                                                               |           |                   |                      |
| Common shares, \$0.015 par value:                                                                                  |           |                   |                      |
| Authorized - 233,333; issued and outstanding - 98,602 shares in 2020 and 98,394 shares in 2019                     |           | 1,479             | 1,476                |
| Additional paid-in capital                                                                                         |           | 1,117,286         | 1,118,655            |
| Accumulated other comprehensive income                                                                             |           | 46,113            | 56,187               |
| Retained earnings                                                                                                  |           | 1,942,196         | 1,808,527            |
| Total stockholders' equity                                                                                         |           | 3,107,074         | 2,984,845            |
| <b>Total liabilities and stockholders' equity</b>                                                                  | <b>\$</b> | <b>4,186,934</b>  | <b>\$ 3,873,425</b>  |

See accompanying notes to condensed consolidated financial statements.

**Essent Group Ltd. and Subsidiaries**

**Condensed Consolidated Statements of Comprehensive Income (Unaudited)**

| (In thousands, except per share amounts)                                                                                               | Three Months Ended March 31, |                   |
|----------------------------------------------------------------------------------------------------------------------------------------|------------------------------|-------------------|
|                                                                                                                                        | 2020                         | 2019              |
| <b>Revenues:</b>                                                                                                                       |                              |                   |
| Net premiums written                                                                                                                   | \$ 191,743                   | \$ 177,644        |
| Decrease in unearned premiums                                                                                                          | 14,753                       | 147               |
| Net premiums earned                                                                                                                    | 206,496                      | 177,791           |
| Net investment income                                                                                                                  | 20,633                       | 19,880            |
| Realized investment gains, net                                                                                                         | 3,135                        | 660               |
| Other income (loss)                                                                                                                    | (1,424)                      | 2,195             |
| <b>Total revenues</b>                                                                                                                  | <b>228,840</b>               | <b>200,526</b>    |
| <b>Losses and expenses:</b>                                                                                                            |                              |                   |
| Provision for losses and LAE                                                                                                           | 8,063                        | 7,107             |
| Other underwriting and operating expenses                                                                                              | 41,947                       | 41,030            |
| Interest expense                                                                                                                       | 2,132                        | 2,670             |
| <b>Total losses and expenses</b>                                                                                                       | <b>52,142</b>                | <b>50,807</b>     |
| Income before income taxes                                                                                                             | 176,698                      | 149,719           |
| Income tax expense                                                                                                                     | 27,175                       | 21,999            |
| <b>Net income</b>                                                                                                                      | <b>\$ 149,523</b>            | <b>\$ 127,720</b> |
| <b>Earnings per share:</b>                                                                                                             |                              |                   |
| Basic                                                                                                                                  | \$ 1.53                      | \$ 1.31           |
| Diluted                                                                                                                                | 1.52                         | 1.30              |
| <b>Weighted average shares outstanding:</b>                                                                                            |                              |                   |
| Basic                                                                                                                                  | 97,949                       | 97,595            |
| Diluted                                                                                                                                | 98,326                       | 98,104            |
| <b>Net income</b>                                                                                                                      | <b>\$ 149,523</b>            | <b>\$ 127,720</b> |
| <b>Other comprehensive income (loss):</b>                                                                                              |                              |                   |
| Change in unrealized (depreciation) appreciation of investments, net of tax (benefit) expense of (\$6,979) in 2020 and \$7,951 in 2019 | (10,074)                     | 38,366            |
| Total other comprehensive income (loss)                                                                                                | (10,074)                     | 38,366            |
| <b>Comprehensive income</b>                                                                                                            | <b>\$ 139,449</b>            | <b>\$ 166,086</b> |

See accompanying notes to condensed consolidated financial statements.

# Essent Group Ltd. and Subsidiaries

## Condensed Consolidated Statements of Changes in Stockholders' Equity (Unaudited)

| (In thousands)                                       | Three Months Ended March 31, |                     |
|------------------------------------------------------|------------------------------|---------------------|
|                                                      | 2020                         | 2019                |
| <b>Common Shares</b>                                 |                              |                     |
| Balance, beginning of period                         | \$ 1,476                     | \$ 1,472            |
| Issuance of management incentive shares              | 5                            | 6                   |
| Cancellation of treasury stock                       | (2)                          | (3)                 |
| Balance, end of period                               | 1,479                        | 1,475               |
| <b>Additional Paid-In Capital</b>                    |                              |                     |
| Balance, beginning of period                         | 1,118,655                    | 1,110,800           |
| Dividends and dividend equivalents declared          | 160                          | —                   |
| Issuance of management incentive shares              | (5)                          | (6)                 |
| Stock-based compensation expense                     | 4,780                        | 4,100               |
| Cancellation of treasury stock                       | (6,304)                      | (8,097)             |
| Balance, end of period                               | 1,117,286                    | 1,106,797           |
| <b>Accumulated Other Comprehensive Income (Loss)</b> |                              |                     |
| Balance, beginning of period                         | 56,187                       | (28,993)            |
| Other comprehensive (loss) income                    | (10,074)                     | 38,366              |
| Balance, end of period                               | 46,113                       | 9,373               |
| <b>Retained Earnings</b>                             |                              |                     |
| Balance, beginning of period                         | 1,808,527                    | 1,282,438           |
| Net income                                           | 149,523                      | 127,720             |
| Dividends and dividend equivalents declared          | (15,854)                     | —                   |
| Balance, end of period                               | 1,942,196                    | 1,410,158           |
| <b>Treasury Stock</b>                                |                              |                     |
| Balance, beginning of period                         | —                            | —                   |
| Treasury stock acquired                              | (6,306)                      | (8,100)             |
| Cancellation of treasury stock                       | 6,306                        | 8,100               |
| Balance, end of period                               | —                            | —                   |
| <b>Total Stockholders' Equity</b>                    | <b>\$ 3,107,074</b>          | <b>\$ 2,527,803</b> |

See accompanying notes to condensed consolidated financial statements.

**Essent Group Ltd. and Subsidiaries**

**Condensed Consolidated Statements of Cash Flows (Unaudited)**

| (In thousands)                                                                    | Three Months Ended March 31, |                  |
|-----------------------------------------------------------------------------------|------------------------------|------------------|
|                                                                                   | 2020                         | 2019             |
| <b>Operating Activities</b>                                                       |                              |                  |
| Net income                                                                        | \$ 149,523                   | \$ 127,720       |
| Adjustments to reconcile net income to net cash provided by operating activities: |                              |                  |
| Gain on the sale of investments, net                                              | (3,135)                      | (660)            |
| Equity in net loss (income) of other invested assets                              | 96                           | 159              |
| Distribution of income from other invested assets                                 | 339                          | —                |
| Depreciation and amortization                                                     | 878                          | 901              |
| Stock-based compensation expense                                                  | 4,780                        | 4,100            |
| Amortization of premium on investment securities                                  | 5,840                        | 3,551            |
| Deferred income tax provision                                                     | 17,047                       | 15,447           |
| Change in:                                                                        |                              |                  |
| Accrued investment income                                                         | (37)                         | (549)            |
| Accounts receivable                                                               | 805                          | (1,319)          |
| Deferred policy acquisition costs                                                 | 558                          | 392              |
| Other assets                                                                      | (2,877)                      | 2,370            |
| Reserve for losses and LAE                                                        | 3,979                        | 4,020            |
| Unearned premium reserve                                                          | (14,753)                     | (147)            |
| Other accrued liabilities                                                         | 88                           | (17,303)         |
| Net cash provided by operating activities                                         | 163,131                      | 138,682          |
| <b>Investing Activities</b>                                                       |                              |                  |
| Net change in short-term investments                                              | (279,803)                    | (56,422)         |
| Purchase of investments available for sale                                        | (294,746)                    | (192,530)        |
| Proceeds from maturity of investments available for sale                          | 29,472                       | 17,014           |
| Proceeds from sales of investments available for sale                             | 159,127                      | 79,714           |
| Purchase of other invested assets                                                 | (2,310)                      | (1,983)          |
| Return of investment from other invested assets                                   | 7,300                        | 179              |
| Purchase of property and equipment                                                | (466)                        | (1,011)          |
| Net cash used in investing activities                                             | (381,426)                    | (155,039)        |
| <b>Financing Activities</b>                                                       |                              |                  |
| Credit facility borrowings                                                        | 200,000                      | —                |
| Treasury stock acquired                                                           | (6,306)                      | (8,100)          |
| Dividends paid                                                                    | (15,694)                     | —                |
| Net cash provided by (used in) financing activities                               | 178,000                      | (8,100)          |
| Net decrease in cash                                                              | (40,295)                     | (24,457)         |
| Cash at beginning of year                                                         | 71,350                       | 64,946           |
| <b>Cash at end of period</b>                                                      | <b>\$ 31,055</b>             | <b>\$ 40,489</b> |
| <b>Supplemental Disclosure of Cash Flow Information</b>                           |                              |                  |
| Income tax payments                                                               | \$ —                         | \$ (5)           |
| Interest payments                                                                 | (1,641)                      | (2,532)          |

See accompanying notes to condensed consolidated financial statements.

## Essent Group Ltd. and Subsidiaries

### Notes to Condensed Consolidated Financial Statements (Unaudited)

In these notes to condensed consolidated financial statements, “Essent”, “Company”, “we”, “us”, and “our” refer to Essent Group Ltd. and its subsidiaries, unless the context otherwise requires.

#### Note 1. Nature of Operations and Basis of Presentation

Essent Group Ltd. (“Essent Group”) is a Bermuda-based holding company, which, through its wholly-owned subsidiaries, offers private mortgage insurance and reinsurance for mortgages secured by residential properties located in the United States. Mortgage insurance facilitates the sale of low down payment (generally less than 20%) mortgage loans into the secondary mortgage market, primarily to two government-sponsored enterprises (“GSEs”), Fannie Mae and Freddie Mac.

The primary mortgage insurance operations are conducted through Essent Guaranty, Inc. (“Essent Guaranty”), a wholly-owned subsidiary approved as a qualified mortgage insurer by the GSEs and is licensed to write mortgage insurance in all 50 states and the District of Columbia. Essent Guaranty reinsures 25% of new insurance written to Essent Reinsurance Ltd. (“Essent Re”), an affiliated Bermuda domiciled Class 3A Insurer licensed pursuant to Section 4 of the Bermuda Insurance Act 1978 that provides insurance and reinsurance coverage of mortgage credit risk. Essent Re also provides insurance and reinsurance to Freddie Mac and Fannie Mae. In 2016, Essent Re formed Essent Agency (Bermuda) Ltd., a wholly-owned subsidiary, which provides underwriting consulting services to third-party reinsurers. In accordance with certain state law requirements then in effect, Essent Guaranty also reinsures that portion of the risk that is in excess of 25% of the mortgage balance with respect to loans insured prior to April 1, 2019, after consideration of other reinsurance, to Essent Guaranty of PA, Inc. (“Essent PA”), an affiliate.

In addition to offering mortgage insurance, we provide contract underwriting services on a limited basis through CUW Solutions, LLC (“CUW Solutions”), a Delaware limited liability company, that provides, among other things, mortgage contract underwriting services to lenders and mortgage insurance underwriting services to affiliates.

We have prepared the condensed consolidated financial statements included herein pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). We have condensed or omitted certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) pursuant to such rules and regulations. In the opinion of management, the statements include all adjustments (which include normal recurring adjustments) required for a fair statement of financial position, results of operations and cash flows for the interim periods presented. These statements should be read in conjunction with the consolidated financial statements and notes thereto, including Note 1 and Note 2 to the consolidated financial statements, included in our Annual Report on Form 10-K for the year ended December 31, 2019, which discloses the principles of consolidation and a summary of significant accounting policies. The results of operations for the interim periods are not necessarily indicative of the results for the full year. We evaluated the need to recognize or disclose events that occurred subsequent to March 31, 2020 prior to the issuance of these condensed consolidated financial statements.

#### Note 2. Recently Issued Accounting Standards

##### *Accounting Standards Adopted During 2020*

In June 2016, the FASB issued ASU 2016-13, *Measurement of Credit Losses on Financial Instruments (Topic 326)*. This update is intended to provide financial statement users with more information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. The amendments in this ASU replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The new guidance requires financial assets measured at amortized cost to be presented at the net amount expected to be collected through the use of an allowance for credit losses. Credit losses relating to available-for-sale debt securities will also be recorded through an allowance rather than as a write-down of the amortized cost of the securities. The accounting for insurance losses and loss adjustment expenses (“LAE”) are not within the scope of this ASU. The provisions of this update were effective for annual and interim periods beginning after December 15, 2019 and we adopted this standard on January 1, 2020 using the modified retrospective approach. The adoption of this ASU did not have a material effect on the Company's consolidated operating results or financial position.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement*. The amendments in this update modify the disclosure requirements for fair value measurements by removing, modifying, or adding certain disclosures. The provisions of this update were effective for interim and annual periods beginning after December 15, 2019, with early adoption permitted for the removed disclosures. We adopted this standard on January 1, 2020. The adoption of this ASU did not have a material impact on our condensed consolidated financial statements.

*Accounting Standards Not Yet Adopted*

In March 2020, the FASB issued ASU No. 2020-04, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*. The amendments in this update provide temporary optional guidance to ease the potential burden in accounting for (or recognizing the effects of) reference rate reform. It provides optional expedients and exceptions for applying generally accepted accounting principles to contract, hedging relationships and other transactions affected by reference rate reform if certain criteria are met. The amendments in this update are effective as of March 12, 2020 through December 31, 2022. The Company is evaluating the impact the adoption of this ASU will have on our consolidated operating results and financial position.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**
**Note 3. Investments**

Investments available for sale consist of the following:

| <b>March 31, 2020 (In thousands)</b>           | <b>Amortized<br/>Cost</b> | <b>Unrealized<br/>Gains</b> | <b>Unrealized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|------------------------------------------------|---------------------------|-----------------------------|------------------------------|-----------------------|
| U.S. Treasury securities                       | \$ 224,192                | \$ 11,373                   | \$ —                         | \$ 235,565            |
| U.S. agency securities                         | 33,614                    | 278                         | —                            | 33,892                |
| U.S. agency mortgage-backed securities         | 838,547                   | 37,865                      | (114)                        | 876,298               |
| Municipal debt securities (1)                  | 398,245                   | 23,497                      | (2,054)                      | 419,688               |
| Non-U.S. government securities                 | 51,937                    | 1,504                       | (1,232)                      | 52,209                |
| Corporate debt securities (2)                  | 880,944                   | 15,992                      | (17,433)                     | 879,503               |
| Residential and commercial mortgage securities | 281,061                   | 6,596                       | (12,125)                     | 275,532               |
| Asset-backed securities                        | 352,637                   | 644                         | (15,606)                     | 337,675               |
| Money market funds                             | 595,173                   | —                           | (8)                          | 595,165               |
| Total investments available for sale           | <u>\$ 3,656,350</u>       | <u>\$ 97,749</u>            | <u>\$ (48,572)</u>           | <u>\$ 3,705,527</u>   |

  

| <b>December 31, 2019 (In thousands)</b>        | <b>Amortized<br/>Cost</b> | <b>Unrealized<br/>Gains</b> | <b>Unrealized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|------------------------------------------------|---------------------------|-----------------------------|------------------------------|-----------------------|
| U.S. Treasury securities                       | \$ 239,087                | \$ 3,526                    | \$ (407)                     | \$ 242,206            |
| U.S. agency securities                         | 33,620                    | 36                          | (51)                         | 33,605                |
| U.S. agency mortgage-backed securities         | 836,710                   | 13,956                      | (2,332)                      | 848,334               |
| Municipal debt securities (1)                  | 339,511                   | 22,245                      | (118)                        | 361,638               |
| Non-U.S. government securities                 | 52,230                    | 2,812                       | (47)                         | 54,995                |
| Corporate debt securities (2)                  | 856,638                   | 24,255                      | (592)                        | 880,301               |
| Residential and commercial mortgage securities | 282,840                   | 6,542                       | (1,101)                      | 288,281               |
| Asset-backed securities                        | 326,589                   | 857                         | (1,421)                      | 326,025               |
| Money market funds                             | 315,360                   | 2                           | —                            | 315,362               |
| Total investments available for sale           | <u>\$ 3,282,585</u>       | <u>\$ 74,231</u>            | <u>\$ (6,069)</u>            | <u>\$ 3,350,747</u>   |

(1) The following table summarizes municipal debt securities as of :

|                                    | <b>March 31,<br/>2020</b> | <b>December 31,<br/>2019</b> |
|------------------------------------|---------------------------|------------------------------|
| Special revenue bonds              | 73.7%                     | 74.5%                        |
| General obligation bonds           | 22.6                      | 21.3                         |
| Certificate of participation bonds | 3.0                       | 3.4                          |
| Tax allocation bonds               | 0.7                       | 0.8                          |
| Total                              | <u>100.0%</u>             | <u>100.0%</u>                |

(2) The following table summarizes corporate debt securities as of :

|                        | <b>March 31,<br/>2020</b> | <b>December 31,<br/>2019</b> |
|------------------------|---------------------------|------------------------------|
| Financial              | 34.1%                     | 34.4%                        |
| Consumer, non-cyclical | 20.3                      | 20.1                         |
| Communications         | 11.3                      | 10.3                         |
| Consumer, cyclical     | 7.9                       | 7.6                          |
| Energy                 | 7.3                       | 8.3                          |
| Utilities              | 6.7                       | 6.2                          |
| Technology             | 5.0                       | 4.8                          |
| Basic materials        | 3.8                       | 4.1                          |
| Industrial             | 3.6                       | 4.2                          |
| Total                  | <u>100.0%</u>             | <u>100.0%</u>                |

**Essent Group Ltd. and Subsidiaries**
**Notes to Condensed Consolidated Financial Statements (Unaudited)**

The amortized cost and fair value of investments available for sale at March 31, 2020, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Because most U.S. agency mortgage-backed securities, residential and commercial mortgage securities and asset-backed securities provide for periodic payments throughout their lives, they are listed below in separate categories.

| <b>(In thousands)</b>                          | <b>Amortized<br/>Cost</b> | <b>Fair<br/>Value</b> |
|------------------------------------------------|---------------------------|-----------------------|
| <b>U.S. Treasury securities:</b>               |                           |                       |
| Due in 1 year                                  | \$ 72,085                 | \$ 72,752             |
| Due after 1 but within 5 years                 | 84,353                    | 89,094                |
| Due after 5 but within 10 years                | 66,770                    | 72,529                |
| Due after 10 years                             | 984                       | 1,190                 |
| Subtotal                                       | 224,192                   | 235,565               |
| <b>U.S. agency securities:</b>                 |                           |                       |
| Due in 1 year                                  | 21,074                    | 21,125                |
| Due after 1 but within 5 years                 | 12,540                    | 12,767                |
| Subtotal                                       | 33,614                    | 33,892                |
| <b>Municipal debt securities:</b>              |                           |                       |
| Due in 1 year                                  | 589                       | 561                   |
| Due after 1 but within 5 years                 | 33,841                    | 35,210                |
| Due after 5 but within 10 years                | 205,608                   | 216,334               |
| Due after 10 years                             | 158,207                   | 167,583               |
| Subtotal                                       | 398,245                   | 419,688               |
| <b>Non-U.S. government securities:</b>         |                           |                       |
| Due in 1 year                                  | —                         | —                     |
| Due after 1 but within 5 years                 | 22,261                    | 22,575                |
| Due after 5 but within 10 years                | 24,229                    | 24,941                |
| Due after 10 years                             | 5,447                     | 4,693                 |
| Subtotal                                       | 51,937                    | 52,209                |
| <b>Corporate debt securities:</b>              |                           |                       |
| Due in 1 year                                  | 150,962                   | 151,107               |
| Due after 1 but within 5 years                 | 429,020                   | 432,300               |
| Due after 5 but within 10 years                | 277,323                   | 274,528               |
| Due after 10 years                             | 23,639                    | 21,568                |
| Subtotal                                       | 880,944                   | 879,503               |
| U.S. agency mortgage-backed securities         | 838,547                   | 876,298               |
| Residential and commercial mortgage securities | 281,061                   | 275,532               |
| Asset-backed securities                        | 352,637                   | 337,675               |
| Money market funds                             | 595,173                   | 595,165               |
| <b>Total investments available for sale</b>    | <b>\$ 3,656,350</b>       | <b>\$ 3,705,527</b>   |

Gross gains and losses realized on the sale of investments available for sale were as follows:

| <b>(In thousands)</b> | <b>Three Months Ended March 31,</b> |             |
|-----------------------|-------------------------------------|-------------|
|                       | <b>2020</b>                         | <b>2019</b> |
| Realized gross gains  | \$ 3,262                            | \$ 671      |
| Realized gross losses | 127                                 | 11          |

# Essent Group Ltd. and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

The fair value of investments available for sale in an unrealized loss position and the related unrealized losses were as follows:

|                                                | Less than 12 months |                         | 12 months or more |                         | Total             |                         |
|------------------------------------------------|---------------------|-------------------------|-------------------|-------------------------|-------------------|-------------------------|
|                                                | Fair Value          | Gross Unrealized Losses | Fair Value        | Gross Unrealized Losses | Fair Value        | Gross Unrealized Losses |
| <b>March 31, 2020 (In thousands)</b>           |                     |                         |                   |                         |                   |                         |
| U.S. agency mortgage-backed securities         | 14,136              | (63)                    | 2,265             | (51)                    | 16,401            | (114)                   |
| Municipal debt securities                      | 48,622              | (2,053)                 | 627               | (1)                     | 49,249            | (2,054)                 |
| Non-U.S. government securities                 | 10,302              | (1,232)                 | —                 | —                       | 10,302            | (1,232)                 |
| Corporate debt securities                      | 331,951             | (17,431)                | 1,423             | (2)                     | 333,374           | (17,433)                |
| Residential and commercial mortgage securities | 120,241             | (11,323)                | 3,011             | (802)                   | 123,252           | (12,125)                |
| Asset-backed securities                        | 213,185             | (9,029)                 | 69,388            | (6,577)                 | 282,573           | (15,606)                |
| Money market funds                             | 20,545              | (8)                     | —                 | —                       | 20,545            | (8)                     |
| <b>Total</b>                                   | <b>\$ 758,982</b>   | <b>\$ (41,139)</b>      | <b>\$ 76,714</b>  | <b>\$ (7,433)</b>       | <b>\$ 835,696</b> | <b>\$ (48,572)</b>      |

|                                                | Less than 12 months |                         | 12 months or more |                         | Total             |                         |
|------------------------------------------------|---------------------|-------------------------|-------------------|-------------------------|-------------------|-------------------------|
|                                                | Fair Value          | Gross Unrealized Losses | Fair Value        | Gross Unrealized Losses | Fair Value        | Gross Unrealized Losses |
| <b>December 31, 2019 (In thousands)</b>        |                     |                         |                   |                         |                   |                         |
| U.S. Treasury securities                       | \$ 29,013           | \$ (331)                | \$ 42,981         | \$ (76)                 | \$ 71,994         | \$ (407)                |
| U.S. agency securities                         | —                   | —                       | 25,605            | (51)                    | 25,605            | (51)                    |
| U.S. agency mortgage-backed securities         | 101,684             | (1,042)                 | 113,866           | (1,290)                 | 215,550           | (2,332)                 |
| Municipal debt securities                      | 10,651              | (112)                   | 624               | (6)                     | 11,275            | (118)                   |
| Non-U.S. government securities                 | 9,664               | (47)                    | —                 | —                       | 9,664             | (47)                    |
| Corporate debt securities                      | 83,013              | (576)                   | 14,531            | (16)                    | 97,544            | (592)                   |
| Residential and commercial mortgage securities | 59,341              | (1,059)                 | 3,442             | (42)                    | 62,783            | (1,101)                 |
| Asset-backed securities                        | 78,813              | (202)                   | 109,536           | (1,219)                 | 188,349           | (1,421)                 |
| <b>Total</b>                                   | <b>\$ 372,179</b>   | <b>\$ (3,369)</b>       | <b>\$ 310,585</b> | <b>\$ (2,700)</b>       | <b>\$ 682,764</b> | <b>\$ (6,069)</b>       |

At March 31, 2020 and December 31, 2019, we held 601 and 365 individual investment securities, respectively, that were in an unrealized loss position. We assess our intent to sell these securities and whether we will be required to sell these securities before the recovery of their amortized cost basis when determining whether to record an impairment on the securities in an unrealized loss position. In assessing whether the decline in the fair value at March 31, 2020 of any of these securities resulted from a credit loss or other factors, we made inquiries of our investment managers to determine that each issuer was current on its scheduled interest and principal payments. We reviewed the credit rating of these securities noting that over 98% of the securities at March 31, 2020 had investment grade ratings. For certain mortgage and asset-backed securities, we reviewed the available credit enhancement for the security, noting that each lot reviewed had enhancement available in the form of subordinated tranches and concluded that a credit loss had not been incurred as of March 31, 2020. For certain corporate debt securities, we obtained the current business outlook for the issuers from our investment managers, including whether an issuer's ability to make scheduled principal and interest payments had been impaired as of March 31, 2020. For the issuers reviewed, we concluded that their ability to make their scheduled principal and interest payments was not impaired as of March 31, 2020 and that a credit loss had not been incurred. Accordingly, we concluded that the decline in the market values experienced at March 31, 2020 was largely due to widening of credit spreads associated with COVID-19 along with a decline in trading activity for certain security types rather than due to credit impairment. To support our assessment, we obtained April 2020 fair values for the securities individually reviewed, noting that the fair value of virtually all those reviewed had increased since March 31, 2020. There was no other-than-temporary impairment recorded by the Company in the three months ended March 31, 2019.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

The Company's other invested assets at March 31, 2020 and December 31, 2019 totaled \$75.4 million and \$78.9 million, respectively. Other invested assets are comprised of limited partnership interests which are accounted for under the equity method of accounting with changes in value reported in other income. Due to the timing of receiving financial information from these partnerships, the results are generally reported on a one month or quarter lag.

The fair value of investments deposited with insurance regulatory authorities to meet statutory requirements was \$9.9 million at March 31, 2020 and \$9.4 million at December 31, 2019. In connection with its insurance and reinsurance activities, Essent Re is required to maintain assets in trusts for the benefit of its contractual counterparties. The fair value of the investments on deposit in these trusts was \$872.7 million at March 31, 2020 and \$805.5 million at December 31, 2019. Essent Guaranty is required to maintain assets on deposit in connection with its fully collateralized reinsurance agreements (see Note 4). The fair value of the assets on deposit was \$8.5 million at March 31, 2020 and \$6.4 million at December 31, 2019. Essent Guaranty is also required to maintain assets on deposit for the benefit of the sponsor of a fixed income investment commitment. The fair value of the assets on deposit was \$6.4 million at March 31, 2020 and \$6.4 million at December 31, 2019.

Net investment income consists of:

| (In thousands)          | Three Months Ended March 31, |           |
|-------------------------|------------------------------|-----------|
|                         | 2020                         | 2019      |
| Fixed maturities        | \$ 20,614                    | \$ 19,743 |
| Short-term investments  | 1,122                        | 1,058     |
| Gross investment income | 21,736                       | 20,801    |
| Investment expenses     | (1,103)                      | (921)     |
| Net investment income   | \$ 20,633                    | \$ 19,880 |

**Note 4. Reinsurance**

In the ordinary course of business, our insurance subsidiaries may use reinsurance to provide protection against adverse loss experience and to expand our capital sources. Reinsurance recoverables are recorded as assets, predicated on a reinsurer's ability to meet their obligations under the reinsurance agreements. If the reinsurers are unable to satisfy their obligations under the agreements, our insurance subsidiaries would be liable for such defaulted amounts.

The effect of reinsurance on net premiums written and earned is as follows:

| (In thousands)        | Three Months Ended March 31, |            |
|-----------------------|------------------------------|------------|
|                       | 2020                         | 2019       |
| Net premiums written: |                              |            |
| Direct                | \$ 205,980                   | \$ 183,682 |
| Ceded (1)             | (14,237)                     | (6,038)    |
| Net premiums written  | \$ 191,743                   | \$ 177,644 |
| Net premiums earned:  |                              |            |
| Direct                | \$ 220,733                   | \$ 183,829 |
| Ceded (1)             | (14,237)                     | (6,038)    |
| Net premiums earned   | \$ 206,496                   | \$ 177,791 |

(1) Net of profit commission.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**
**Quota Share Reinsurance**

Effective September 1, 2019, Essent Guaranty entered into a quota share reinsurance agreement with a panel of third-party reinsurers (the "QSR Agreement"). Each of the third-party reinsurers has an insurer financial strength rating of A or better by S&P Global Ratings, A.M. Best or both. Under the QSR Agreement, Essent Guaranty will cede premiums earned related to 40% of risk on eligible single premium policies and 20% of risk on all other eligible policies written September 1, 2019 through December 31, 2020, in exchange for reimbursement of ceded claims and claims expenses on covered policies, a 20% ceding commission, and a profit commission of up to 60% that varies directly and inversely with ceded claims. The QSR Agreement is scheduled to terminate on December 31, 2030. Essent Guaranty has certain termination rights under the QSR Agreement, including the option to terminate the QSR Agreement with no termination fee on December 31, 2021, and the option, subject to a termination fee, to terminate the QSR Agreement on December 31, 2022, or annually thereafter. Should Essent Guaranty not exercise its option to terminate the QSR Agreement on December 31, 2021, the maximum profit commission that Essent Guaranty could earn would increase to 63% in 2022 and thereafter. RIF ceded under the QSR Agreement was \$1.9 billion as of March 31, 2020.

**Excess of Loss Reinsurance**

Essent Guaranty has entered into fully collateralized reinsurance agreements ("Radnor Re Transactions") with unaffiliated special purpose insurers domiciled in Bermuda. For the reinsurance coverage periods, Essent Guaranty and its affiliates retain the first layer of the respective aggregate losses, and a Radnor Re special purpose insurer will then provide second layer coverage up to the outstanding reinsurance coverage amount. Essent Guaranty and its affiliates retain losses in excess of the outstanding reinsurance coverage amount. The reinsurance premium due to each Radnor Re special purpose insurer is calculated by multiplying the outstanding reinsurance coverage amount at the beginning of a period by a coupon rate, which is the sum of one-month LIBOR plus a risk margin, and then subtracting actual investment income collected on the assets in the related reinsurance trust during that period. The aggregate excess of loss reinsurance coverage decreases over a ten-year period as the underlying covered mortgages amortize. Essent Guaranty has rights to terminate the Radnor Re Transactions. The Radnor Re entities collateralized the coverage by issuing mortgage insurance-linked notes ("ILNs") in an aggregate amount equal to the initial coverage to unaffiliated investors. The notes have ten-year legal maturities and are non-recourse to any assets of Essent Guaranty or its affiliates. The proceeds of the notes were deposited into reinsurance trusts for the benefit of Essent Guaranty and will be the source of reinsurance claim payments to Essent Guaranty and principal repayments on the ILNs.

Essent Guaranty has also entered into reinsurance agreements with panels of reinsurers that provide aggregate excess of loss coverage immediately above or pari-passu to the coverage provided by the Radnor Re Transactions. The aggregate excess of loss reinsurance coverage decreases over a ten-year period as the underlying covered mortgages amortize. Essent Guaranty has rights to terminate these reinsurance agreements.

The following table summarizes Essent Guaranty's excess of loss reinsurance agreements as of March 31, 2020:

| Vintage Year | Reinsurer             | Effective Date    | Optional Termination Date  |
|--------------|-----------------------|-------------------|----------------------------|
| 2015 & 2016  | Radnor Re 2019-2 Ltd. | June 20, 2019     | June 25, 2024              |
| 2017         | Radnor Re 2018-1 Ltd. | March 22, 2018    | March 25, 2023 <b>(1)</b>  |
| 2017         | Panel of Reinsurers   | November 1, 2018  | October 1, 2023 <b>(2)</b> |
| 2018         | Radnor Re 2019-1 Ltd. | February 28, 2019 | February 25, 2026          |
| 2018         | Panel of Reinsurers   | February 28, 2019 | February 25, 2026          |
| 2019         | Radnor Re 2020-1 Ltd. | January 30, 2020  | January 25, 2027           |
| 2019         | Panel of Reinsurers   | January 30, 2020  | January 25, 2027           |

(1) If the reinsurance agreement is not terminated at the optional termination date, the risk margin component of the reinsurance premium increases by 50%.

(2) If the reinsurance agreement is not terminated at the optional termination date, the reinsurance premium increases by 50%.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

The following table summarizes Essent Guaranty's excess of loss reinsurance coverages and retentions as of March 31, 2020:

| (In thousands) | Vintage Year | Remaining Insurance in Force | Remaining Risk in Force | Remaining Reinsurance in Force |                   |              | Remaining First Layer Retention |
|----------------|--------------|------------------------------|-------------------------|--------------------------------|-------------------|--------------|---------------------------------|
|                |              |                              |                         | ILN                            | Other Reinsurance | Total        |                                 |
|                | 2015 & 2016  | \$ 25,025,497                | \$ 6,762,026            | \$ 244,105                     | \$ —              | \$ 244,105   | \$ 208,111                      |
|                | 2017         | 26,279,318                   | 6,665,183               | 280,180                        | 165,167 (4)       | 445,347      | 221,852                         |
|                | 2018         | 31,375,687                   | 7,923,964               | 377,509                        | 87,941 (5)        | 465,450      | 253,081                         |
|                | 2019 (3)     | 34,916,398                   | 8,826,958               | 495,889                        | 55,102 (6)        | 550,991      | 215,605                         |
|                | Total        | \$ 117,596,900               | \$ 30,178,131           | \$ 1,397,683                   | \$ 308,210        | \$ 1,705,893 | \$ 898,649                      |

(3) Reinsurance coverage on new insurance written from January 1, 2019 through August 31, 2019.

(4) Coverage provided immediately above the coverage provided by Radnor Re 2018-1 Ltd.

(5) Coverage provided pari-passu to the coverage provided by Radnor Re 2019-1 Ltd.

(6) Coverage provided pari-passu to the coverage provided by Radnor Re 2020-1 Ltd.

The amount of monthly reinsurance premium ceded to the Radnor Re entities will fluctuate due to changes in one-month LIBOR and changes in money market rates that affect investment income collected on the assets in the reinsurance trusts. As the reinsurance premium will vary based on changes in these rates, we concluded that the Radnor Re Transactions contain embedded derivatives that will be accounted for separately like freestanding derivatives.

In connection with the Radnor Re Transactions, we concluded that the risk transfer requirements for reinsurance accounting were met as each Radnor Re entity is assuming significant insurance risk and a reasonable possibility of a significant loss. In addition, we assessed whether each Radnor Re entity was a variable interest entity ("VIE") and the appropriate accounting for the Radnor Re entities if they were VIEs. A VIE is a legal entity that does not have sufficient equity at risk to finance its activities without additional subordinated financial support or is structured such that equity investors lack the ability to make significant decisions relating to the entity's operations through voting rights or do not substantively participate in the gains and losses of the entity. A VIE is consolidated by its primary beneficiary. The primary beneficiary is the entity that has both (1) the power to direct the activities of the VIE that most significantly affect the entity's economic performance and (2) the obligation to absorb losses or the right to receive benefits that could be potentially significant to the VIE. While also considering these factors, the consolidation conclusion depends on the breadth of the decision-making ability and ability to influence activities that significantly affect the economic performance of the VIE. We concluded that the Radnor Re entities are VIEs. However, given that Essent Guaranty (1) does not have the unilateral power to direct the activities that most significantly affect their economic performance and (2) does not have the obligation to absorb losses or the right to receive benefits that could be potentially significant to these entities, the Radnor Re entities are not consolidated in these financial statements.

The following table presents total assets of each Radnor Re special purpose insurer as well as our maximum exposure to loss associated with each Radnor Re entity, representing the fair value of the embedded derivative included in other assets (other accrued liabilities) on our condensed consolidated balance sheet and the estimated net present value of investment earnings on the assets in the reinsurance trust, each as of March 31, 2020:

| (In thousands)        | Total VIE Assets | Maximum Exposure to Loss |                     |          |
|-----------------------|------------------|--------------------------|---------------------|----------|
|                       |                  | On - Balance Sheet       | Off - Balance Sheet | Total    |
| Radnor Re 2018-1 Ltd. | \$ 280,180       | \$ 169                   | \$ 1,580            | \$ 1,749 |
| Radnor Re 2019-1 Ltd. | 377,509          | (2,441)                  | 1,967               | (474)    |
| Radnor Re 2019-2 Ltd. | 244,105          | (1,771)                  | 1,210               | (561)    |
| Radnor Re 2020-1 Ltd. | 495,889          | (1,918)                  | 6,059               | 4,141    |
| Total                 | \$ 1,397,683     | \$ (5,961)               | \$ 10,816           | \$ 4,855 |

**Notes to Condensed Consolidated Financial Statements (Unaudited)**
**Note 5. Reserve for Losses and Loss Adjustment Expenses**

The following table provides a reconciliation of the beginning and ending reserve balances for losses and loss adjustment expenses (“LAE”) for the three months ended March 31:

| (\$ in thousands)                                                     | 2020      | 2019      |
|-----------------------------------------------------------------------|-----------|-----------|
| Reserve for losses and LAE at beginning of period                     | \$ 69,362 | \$ 49,464 |
| Less: Reinsurance recoverables                                        | 71        | —         |
| Net reserve for losses and LAE at beginning of period                 | 69,291    | 49,464    |
| Add provision for losses and LAE, net of reinsurance, occurring in:   |           |           |
| Current period                                                        | 15,419    | 11,828    |
| Prior years                                                           | (7,356)   | (4,721)   |
| Net incurred losses and LAE during the current period                 | 8,063     | 7,107     |
| Deduct payments for losses and LAE, net of reinsurance, occurring in: |           |           |
| Current period                                                        | 1         | 15        |
| Prior years                                                           | 4,110     | 3,072     |
| Net loss and LAE payments during the current period                   | 4,111     | 3,087     |
| Net reserve for losses and LAE at end of period                       | 73,243    | 53,484    |
| Plus: Reinsurance recoverables                                        | 98        | —         |
| Reserve for losses and LAE at end of period                           | \$ 73,341 | \$ 53,484 |
| Loans in default at end of period                                     | 5,841     | 4,096     |

For the three months ended March 31, 2020, \$4.1 million was paid for incurred claims and claim adjustment expenses attributable to insured events of prior years. There has been a \$7.4 million favorable prior year development during the three months ended March 31, 2020. Reserves remaining as of March 31, 2020 for prior years are \$57.8 million as a result of re-estimation of unpaid losses and loss adjustment expenses. For the three months ended March 31, 2019, \$3.1 million was paid for incurred claims and claim adjustment expenses attributable to insured events of prior years. There was a \$4.7 million favorable prior year development during the three months ended March 31, 2019. Reserves remaining as of March 31, 2019 for prior years were \$41.7 million as a result of re-estimation of unpaid losses and loss adjustment expenses. In both periods, the favorable prior years' loss development was the result of a re-estimation of amounts ultimately to be paid on prior year defaults in the default inventory, including the impact of previously identified defaults that cured. Original estimates are increased or decreased as additional information becomes known regarding individual claims.

Due to business restrictions, stay-at-home orders and travel restrictions implemented as a result of COVID-19, unemployment in the United States has increased significantly. As unemployment is one of the most common reasons for borrowers to default on their mortgage, the increase in unemployment has the potential to increase the number of delinquencies and claim frequencies on the mortgages we insure. We expect to experience increased defaults beginning in the second quarter of 2020. COVID-19 has not materially affected our reserves as of March 31, 2020. The impact on our reserves in future periods will be dependent upon the amount of borrowers that default on their mortgage, our expectations at each reporting date for the losses we will experience on those delinquencies and the ultimate claims we pay.

**Note 6. Debt Obligations**
**Credit Facility**

Essent Group and its subsidiaries, Essent Irish Intermediate Holdings Limited and Essent US Holdings, Inc. (collectively, the "Borrowers"), are parties to a secured credit facility (the “Credit Facility”) with committed capacity of \$500 million. The Credit Facility provides for a \$275 million revolving credit facility, \$225 million of term loans and a \$100 million uncommitted line that may be exercised at the Borrowers’ option so long as the Borrowers receive commitments from the lenders. Borrowings under the Credit Facility may be used for working capital and general corporate purposes, including, without limitation, capital contributions to Essent’s insurance and reinsurance subsidiaries. Borrowings accrue interest at a

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

floating rate tied to a standard short-term borrowing index, selected at the Company's option, plus an applicable margin. A commitment fee is due quarterly on the average daily amount of the undrawn revolving commitment. The applicable margin and the commitment fee are based on the senior unsecured debt rating or long-term issuer rating of Essent Group to the extent available, or the insurer financial strength rating of Essent Guaranty. The annual commitment fee rate at March 31, 2020 was 0.25%. The obligations under the Credit Facility are secured by certain assets of the Borrowers, excluding the stock and assets of its insurance and reinsurance subsidiaries. The Credit Facility contains several covenants, including financial covenants relating to minimum net worth, capital and liquidity levels, maximum debt to capitalization level and Essent Guaranty's compliance with the PMIERS (see Note 14). The borrowings under the Credit Facility contractually mature on May 17, 2021. As of March 31, 2020, the Company was in compliance with the covenants and \$425 million had been borrowed under the Credit Facility with a weighted average interest rate of 2.87%. As of December 31, 2019, \$225 million had been borrowed with a weighted average interest rate of 3.51%.

**Note 7. Commitments and Contingencies****Obligations under Guarantees**

Under the terms of CUW Solutions' contract underwriting agreements with lenders and subject to contractual limitations on liability, we agree to indemnify certain lenders against losses incurred in the event that we make an error in determining whether loans processed meet specified underwriting criteria, to the extent that such error materially restricts or impairs the salability of such loan, results in a material reduction in the value of such loan or results in the lender repurchasing the loan. The indemnification may be in the form of monetary or other remedies. We paid less than \$0.1 million related to remedies for each of the three months ended March 31, 2020 and 2019, respectively. As of March 31, 2020, management believes any potential claims for indemnification related to contract underwriting services through March 31, 2020 are not material to our consolidated financial position or results of operations.

In addition to the indemnifications discussed above, in the normal course of business, we enter into agreements or other relationships with third parties pursuant to which we may be obligated under specified circumstances to indemnify the counterparties with respect to certain matters. Our contractual indemnification obligations typically arise in the context of agreements entered into by us to, among other things, purchase or sell services, finance our business and business transactions, lease real property and license intellectual property. The agreements we enter into in the normal course of business generally require us to pay certain amounts to the other party associated with claims or losses if they result from our breach of the agreement, including the inaccuracy of representations or warranties. The agreements we enter into may also contain other indemnification provisions that obligate us to pay amounts upon the occurrence of certain events, such as the negligence or willful misconduct of our employees, infringement of third-party intellectual property rights or claims that performance of the agreement constitutes a violation of law. Generally, payment by us under an indemnification provision is conditioned upon the other party making a claim, and typically we can challenge the other party's claims. Further, our indemnification obligations may be limited in time and/or amount, and in some instances, we may have recourse against third parties for certain payments made by us under an indemnification agreement or obligation. As of March 31, 2020, contingencies triggering material indemnification obligations or payments have not occurred historically and are not expected to occur. The nature of the indemnification provisions in the various types of agreements and relationships described above are believed to be low risk and pervasive, and we consider them to have a remote risk of loss or payment. We have not recorded any provisions on the condensed consolidated balance sheets related to indemnifications.

**Commitments**

We lease office space for use in our operations under leases accounted for as operating leases. These leases generally include options to extend them for periods of up to ten years. Our option to extend the term of our primary office locations at the greater of existing or prevailing market rates was not recognized in our right-of-use asset and lease liability. When establishing the value of our right-of-use asset and lease liability, we determine the discount rate for the underlying leases using the prevailing market interest rate for a borrowing of the same duration of the lease plus the risk premium inherent in the borrowings under our Credit Facility. Operating lease right-of-use assets of \$9.5 million and \$10.0 million as of March 31, 2020 and December 31, 2019, respectively, are reported on our consolidated balance sheet as property and equipment. Operating lease liabilities of \$11.9 million and \$12.6 million as of March 31, 2020 and December 31, 2019, respectively, are reported on our consolidated balance sheet as other accrued liabilities. Total rent expense was \$0.7 million and \$0.6 million for the three months ended March 31, 2020 and 2019, respectively.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

The following table presents lease cost and other lease information for the three months ended March 31, 2020 and 2019:

| (\$ in thousands)                                        | Three Months Ended<br>March 31, |               |
|----------------------------------------------------------|---------------------------------|---------------|
|                                                          | 2020                            | 2019          |
| Lease cost:                                              |                                 |               |
| Operating lease cost                                     | \$ 700                          | \$ 591        |
| Short-term lease cost                                    | 5                               | 42            |
| Sublease income                                          | (33)                            | (32)          |
| Total lease cost                                         | <u>\$ 672</u>                   | <u>\$ 601</u> |
| Other information:                                       |                                 |               |
| Weighted average remaining lease term - operating leases | 4.5 years                       | 5.5 years     |
| Weighted average discount rate - operating leases        | 4.0%                            | 4.1%          |

The following table presents a maturity analysis of our lease liabilities as follows at March 31, 2020:

|                                    |                  |
|------------------------------------|------------------|
| (In thousands)                     |                  |
| 2020 (April 1 through December 31) | \$ 2,229         |
| 2021                               | 2,999            |
| 2022                               | 3,003            |
| 2023                               | 2,752            |
| 2024                               | 1,334            |
| 2025 and thereafter                | 793              |
| Total lease payments to be paid    | 13,110           |
| Less: Future interest expense      | (1,173)          |
| Present value of lease liabilities | <u>\$ 11,937</u> |

**Note 8. Capital Stock**
**Dividends**

In February 2020, the Board of Directors declared a quarterly cash dividend of \$0.16 per common share which was paid on March 20, 2020. In May 2020, the Board of Directors declared a quarterly cash dividend of \$0.16 per common share payable on June 12, 2020, to shareholders of record on June 2, 2020.

**Note 9. Stock-Based Compensation**

In connection with the IPO in 2013, Essent Group's Board of Directors adopted, and Essent Group's shareholders approved, the Essent Group Ltd. 2013 Long-Term Incentive Plan (the "2013 Plan"), which was effective upon completion of the initial public offering. The types of awards available under the 2013 Plan include nonvested shares, nonvested share units, non-qualified share options, incentive stock options, share appreciation rights, and other share-based or cash-based awards. Nonvested shares and nonvested share units granted under the 2013 Plan have rights to dividends, which entitle holders to the same dividend value per share as holders of common shares in the form of dividend equivalent units ("DEUs"). DEUs are subject to the same vesting and other terms and conditions as the corresponding nonvested shares and nonvested share units. DEUs vest when the underlying shares or share units vest and are forfeited if the underlying share or share units forfeit prior to vesting.

# Essent Group Ltd. and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

The following table summarizes nonvested common share, nonvested common share unit and DEU activity for the three months ended March 31, 2020:

| (Shares in thousands)            | Time and Performance-Based Share Awards |                                        | Time-Based Share Awards |                                        | Share Units           |                                        | DEUs                      |                                        |
|----------------------------------|-----------------------------------------|----------------------------------------|-------------------------|----------------------------------------|-----------------------|----------------------------------------|---------------------------|----------------------------------------|
|                                  | Number of Shares                        | Weighted Average Grant Date Fair Value | Number of Shares        | Weighted Average Grant Date Fair Value | Number of Share Units | Weighted Average Grant Date Fair Value | Dividend Equivalent Units | Weighted Average Grant Date Fair Value |
| Outstanding at beginning of year | 394                                     | \$ 42.02                               | 169                     | \$ 41.31                               | 351                   | \$ 39.78                               | 5                         | \$ 51.11                               |
| Granted                          | 109                                     | 51.52                                  | 69                      | 51.52                                  | 312                   | 51.50                                  | 6                         | 26.83                                  |
| Vested                           | (140)                                   | 36.29                                  | (85)                    | 40.47                                  | (169)                 | 36.70                                  | (2)                       | 51.11                                  |
| Forfeited                        | —                                       | N/A                                    | —                       | N/A                                    | (8)                   | 49.23                                  | —                         | 42.06                                  |
| Outstanding at March 31, 2020    | 363                                     | \$ 47.09                               | 153                     | \$ 46.34                               | 486                   | \$ 48.21                               | 9                         | \$ 35.02                               |

In February 2020, certain members of senior management were granted nonvested common shares under the Essent Group Ltd. 2013 Long-Term Incentive Plan ("2013 Plan") that were subject to time-based and performance-based vesting. The time-based share awards granted in February 2020 vest in three equal installments on March 1, 2021, 2022 and 2023. The performance-based share awards granted in February 2020 vest based upon our compounded annual book value per share growth percentage during a three-year performance period that commenced on January 1, 2020 and vest on March 1, 2023. The portion of these nonvested performance-based share awards that will be earned based upon the achievement of compounded annual book value per share growth is as follows:

| Performance level | Compounded Annual Book Value Per Share Growth | Nonvested Common Shares Earned |
|-------------------|-----------------------------------------------|--------------------------------|
|                   | <13%                                          | 0%                             |
| <b>Threshold</b>  | 13%                                           | 10%                            |
|                   | 14%                                           | 35%                            |
|                   | 15%                                           | 60%                            |
|                   | 16%                                           | 85%                            |
| <b>Maximum</b>    | ≥17%                                          | 100%                           |

In the event that the compounded annual book value per share growth falls between the performance levels shown above, the nonvested common shares earned will be determined on a straight-line basis between the respective levels shown.

In January 2020, time-based share units were issued to all vice president and staff level employees and vest in three equal installments on January 2021, 2022 and 2023. In connection with our incentive program covering bonus awards for performance year 2019, in February 2020, time-based share units were issued to certain employees that vest in three equal installments on March 1, 2021, 2022 and 2023. In May 2020, 38,128 time-based share units were granted to non-employee directors that vest one year from the date of grant.

The total fair value on the vesting date of nonvested shares, share units or DEUs that vested was \$17.8 million and \$22.0 million for the three months ended March 31, 2020 and 2019, respectively. As of March 31, 2020, there was \$37.5 million of total unrecognized compensation expense related to nonvested shares or share units outstanding at March 31, 2020 and we expect to recognize the expense over a weighted average period of 2.4 years.

Employees have the option to tender shares to Essent Group to pay the minimum employee statutory withholding taxes associated with shares upon vesting. Common shares tendered by employees to pay employee withholding taxes totaled 139,853 in the three months ended March 31, 2020. The tendered shares were recorded at cost and included in treasury stock. All treasury stock has been cancelled as of March 31, 2020.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

Compensation expense, net of forfeitures, and related tax effects recognized in connection with nonvested shares was as follows:

| (In thousands)       | Three Months Ended March 31, |          |
|----------------------|------------------------------|----------|
|                      | 2020                         | 2019     |
| Compensation expense | \$ 4,780                     | \$ 4,100 |
| Income tax benefit   | 918                          | 765      |

**Note 10. Income Taxes**

As of March 31, 2020, the statutory income tax rates of the countries where the Company does business are 21% in the United States and 0.0% in Bermuda. The statutory income tax rate of each country is applied against the taxable income from each country to calculate the income tax expense. For the three months ended March 31, 2020, our provision for income taxes was not based on an estimated annual effective rate due to uncertainty regarding the potential impacts of COVID-19 on our results of operations. Due to that uncertainty, we were unable to make a reliable estimate of pretax income and the annual effective tax rate for the full year 2020. Accordingly, the provision for income taxes for the three months ended March 31, 2020 was based on the actual effective tax rate for the year to date period.

Income tax expense consists of the following components:

| (In thousands)           | Three Months Ended March 31, |           |
|--------------------------|------------------------------|-----------|
|                          | 2020                         | 2019      |
| Current                  | \$ 10,128                    | \$ 6,552  |
| Deferred                 | 17,047                       | 15,447    |
| Total income tax expense | \$ 27,175                    | \$ 21,999 |

Income tax expense is different from that which would be obtained by applying the applicable statutory income tax rates to income before taxes by jurisdiction (i.e. U.S. 21%; Bermuda 0.0%). The reconciliation of the difference between income tax expense and the expected tax provision at the weighted average tax rate was as follows:

| (\$ in thousands)                                 | Three Months Ended March 31, |                    |           |                    |
|---------------------------------------------------|------------------------------|--------------------|-----------|--------------------|
|                                                   | 2020                         |                    | 2019      |                    |
|                                                   | \$                           | % of pretax income | \$        | % of pretax income |
| Tax provision at weighted average statutory rates | \$ 27,376                    | 15.5 %             | \$ 23,938 | 16.0 %             |
| Non-deductible expenses                           | 714                          | 0.4                | 324       | 0.2                |
| Excess tax benefits from stock-based compensation | (620)                        | (0.3)              | (1,956)   | (1.3)              |
| Tax exempt interest, net of proration             | (342)                        | (0.2)              | (443)     | (0.3)              |
| Other                                             | 47                           | 0.0                | 136       | 0.1                |
| Total income tax expense                          | \$ 27,175                    | 15.4 %             | \$ 21,999 | 14.7 %             |

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

We provide deferred taxes to reflect the estimated future tax effects of the differences between the financial statement and tax bases of assets and liabilities using currently enacted tax laws. The net deferred tax liability was comprised of the following:

| (In thousands)             | March 31,<br>2020 | December 31,<br>2019 |
|----------------------------|-------------------|----------------------|
| Deferred tax assets        | \$ 27,863         | \$ 29,392            |
| Deferred tax liabilities   | (287,551)         | (279,012)            |
| Net deferred tax liability | \$ (259,688)      | \$ (249,620)         |

The components of the net deferred tax liability were as follows:

| (In thousands)                             | March 31,<br>2020 | December 31,<br>2019 |
|--------------------------------------------|-------------------|----------------------|
| Contingency reserves                       | \$ (277,496)      | \$ (261,855)         |
| Unearned premium reserve                   | 15,897            | 16,641               |
| Unrealized (gain) loss on investments      | (6,235)           | (13,214)             |
| Accrued expenses                           | 4,065             | 3,391                |
| Deferred policy acquisition costs          | (3,181)           | (3,298)              |
| Unearned ceding commissions                | 3,066             | 3,227                |
| Fixed assets                               | 1,383             | 1,502                |
| Start-up expenditures, net                 | 1,342             | 1,410                |
| Change in fair market value of derivatives | 1,252             | 370                  |
| Loss reserves                              | 440               | 416                  |
| Nonvested shares                           | 410               | 2,426                |
| Investments in limited partnerships        | (400)             | (400)                |
| Prepaid expenses                           | (131)             | (132)                |
| Loss reserves - TCJA transition adjustment | (108)             | (113)                |
| Organizational expenditures                | 8                 | 9                    |
| Net deferred tax liability                 | \$ (259,688)      | \$ (249,620)         |

As a mortgage guaranty insurer, we are eligible for a tax deduction, subject to certain limitations, under Section 832(e) of the IRC for amounts required by state law or regulation to be set aside in statutory contingency reserves. The deduction is allowed only to the extent that we purchase non-interest-bearing United States Mortgage Guaranty Tax and Loss Bonds ("T&L Bonds") issued by the Treasury Department in an amount equal to the tax benefit derived from deducting any portion of our statutory contingency reserves. During the three months ended March 31, 2020, we had not purchased or sold any T&L Bonds and for the year ended December 31, 2019, we had a net purchases of T&L Bonds in the amount of \$59.5 million. As of March 31, 2020 and December 31, 2019, we held \$261.9 million of T&L Bonds.

In evaluating our ability to realize the benefit of our deferred tax assets, we consider the relevant impact of all available positive and negative evidence including our past operating results and our forecasts of future taxable income. At March 31, 2020 and December 31, 2019, after weighing all the evidence, management concluded that it was more likely than not that our deferred tax assets would be realized.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**
**Note 11. Earnings per Share (EPS)**

The following table reconciles the net income and the weighted average common shares outstanding used in the computations of basic and diluted earnings per common share:

| (In thousands, except per share amounts)    | Three Months Ended<br>March 31, |            |
|---------------------------------------------|---------------------------------|------------|
|                                             | 2020                            | 2019       |
| Net income                                  | \$ 149,523                      | \$ 127,720 |
| Basic weighted average shares outstanding   | 97,949                          | 97,595     |
| Dilutive effect of nonvested shares         | 377                             | 509        |
| Diluted weighted average shares outstanding | 98,326                          | 98,104     |
| Basic earnings per share                    | \$ 1.53                         | \$ 1.31    |
| Diluted earnings per share                  | \$ 1.52                         | \$ 1.30    |

There were 353,230 and 142,642 antidilutive shares for the three months ended March 31, 2020 and 2019, respectively.

The nonvested performance-based share awards are considered contingently issuable for purposes of the EPS calculation. Based on the compounded annual book value per share growth as of March 31, 2020 and 2019, 100% of the performance-based share awards would be issuable under the terms of the arrangements at each date if March 31 was the end of the contingency period.

**Note 12. Accumulated Other Comprehensive Income (Loss)**

The following table presents the rollforward of accumulated other comprehensive income (loss) for the three months ended March 31, 2020 and 2019:

| (In thousands)                                                         | Three Months Ended March 31, |             |            |             |            |             |
|------------------------------------------------------------------------|------------------------------|-------------|------------|-------------|------------|-------------|
|                                                                        | 2020                         |             |            | 2019        |            |             |
|                                                                        | Before Tax                   | Tax Effect  | Net of Tax | Before Tax  | Tax Effect | Net of Tax  |
| Balance at beginning of period                                         | \$ 69,401                    | \$ (13,214) | \$ 56,187  | \$ (33,276) | \$ 4,283   | \$ (28,993) |
| Other comprehensive income (loss):                                     |                              |             |            |             |            |             |
| Unrealized holding gains (losses) on investments:                      |                              |             |            |             |            |             |
| Unrealized holding gains (losses) arising during the period            | (13,918)                     | 6,403       | (7,515)    | 46,977      | (8,071)    | 38,906      |
| Less: Reclassification adjustment for gains included in net income (1) | (3,135)                      | 576         | (2,559)    | (660)       | 120        | (540)       |
| Net unrealized gains (losses) on investments                           | (17,053)                     | 6,979       | (10,074)   | 46,317      | (7,951)    | 38,366      |
| Other comprehensive income (loss)                                      | (17,053)                     | 6,979       | (10,074)   | 46,317      | (7,951)    | 38,366      |
| Balance at end of period                                               | \$ 52,348                    | \$ (6,235)  | \$ 46,113  | \$ 13,041   | \$ (3,668) | \$ 9,373    |

(1) Included in net realized investment gains on our condensed consolidated statements of comprehensive income.

**Note 13. Fair Value of Financial Instruments**

We carry certain of our financial instruments at fair value. We define fair value as the current amount that would be exchanged to sell an asset or transfer a liability, other than in a forced liquidation.

**Notes to Condensed Consolidated Financial Statements (Unaudited)****Fair Value Hierarchy**

ASC No. 820 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market assumptions. The level within the fair value hierarchy to measure the financial instrument shall be determined based on the lowest level input that is significant to the fair value measurement. The three levels of the fair value hierarchy are as follows:

- Level 1 — Quoted prices for identical instruments in active markets accessible at the measurement date.
- Level 2 — Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and valuations in which all significant inputs are observable in active markets. Inputs are observable for substantially the full term of the financial instrument.
- Level 3 — Valuations derived from one or more significant inputs that are unobservable.

**Determination of Fair Value**

When available, we generally use quoted market prices to determine fair value and classify the financial instrument in Level 1. In cases where quoted market prices for similar financial instruments are available, we utilize these inputs for valuation techniques and classify the financial instrument in Level 2. In cases where quoted market prices are not available, fair values are based on estimates using discounted cash flows, present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rates and estimates of future cash flows and we classify the financial instrument in Level 3. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

We used the following methods and assumptions in estimating fair values of financial instruments:

- Investments available for sale — Investments available for sale are valued using quoted market prices in active markets, when available, and those investments are classified as Level 1 of the fair value hierarchy. Level 1 investments available for sale include investments such as U.S. Treasury securities and money market funds. Investments available for sale are classified as Level 2 of the fair value hierarchy if quoted market prices are not available and fair values are estimated using quoted prices of similar securities or recently executed transactions for the securities. U.S. agency securities, U.S. agency mortgage-backed securities, municipal debt securities, non-U.S. government securities, corporate debt securities, residential and commercial mortgage securities and asset-backed securities are classified as Level 2 investments.

We use independent pricing sources to determine the fair value of securities available for sale in Level 1 and Level 2 of the fair value hierarchy. We use one primary pricing service to provide individual security pricing based on observable market data and receive one quote per security. To ensure securities are appropriately classified in the fair value hierarchy, we review the pricing techniques and methodologies of the independent pricing service and believe that their policies adequately consider market activity, either based on specific transactions for the issue valued or based on modeling of securities with similar credit quality, duration, yield and structure that were recently traded. U.S. agency securities, U.S. agency mortgage-backed securities, municipal debt securities, non-U.S. government securities and corporate debt securities are valued by our primary vendor using recently executed transactions and proprietary models based on observable inputs, such as interest rate spreads, yield curves and credit risk. Residential and commercial mortgage securities and asset-backed securities are valued by our primary vendor using proprietary models based on observable inputs, such as interest rate spreads, prepayment speeds and credit risk. As part of our evaluation of investment prices provided by our primary pricing service, we obtained and reviewed their pricing methodologies which include a description of how each security type is evaluated and priced. We review the reasonableness of prices received from our primary pricing service by comparison to prices obtained from additional pricing sources. We have not made any adjustments to the prices obtained from our primary pricing service.

# Essent Group Ltd. and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

### Assets and Liabilities Measured at Fair Value

All assets measured at fair value are categorized in the table below based upon the lowest level of significant input to the valuations. All fair value measurements at the reporting date were on a recurring basis.

| March 31, 2020 (In thousands)                  | Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Instruments<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total               |
|------------------------------------------------|------------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|---------------------|
| <b>Recurring fair value measurements</b>       |                                                                                    |                                                           |                                                    |                     |
| Financial Assets:                              |                                                                                    |                                                           |                                                    |                     |
| U.S. Treasury securities                       | \$ 235,565                                                                         | \$ —                                                      | \$ —                                               | \$ 235,565          |
| U.S. agency securities                         | —                                                                                  | 33,892                                                    | —                                                  | 33,892              |
| U.S. agency mortgage-backed securities         | —                                                                                  | 876,298                                                   | —                                                  | 876,298             |
| Municipal debt securities                      | —                                                                                  | 419,688                                                   | —                                                  | 419,688             |
| Non-U.S. government securities                 | —                                                                                  | 52,209                                                    | —                                                  | 52,209              |
| Corporate debt securities                      | —                                                                                  | 879,503                                                   | —                                                  | 879,503             |
| Residential and commercial mortgage securities | —                                                                                  | 275,532                                                   | —                                                  | 275,532             |
| Asset-backed securities                        | —                                                                                  | 337,675                                                   | —                                                  | 337,675             |
| Money market funds                             | 595,165                                                                            | —                                                         | —                                                  | 595,165             |
| Total assets at fair value (1)                 | <u>\$ 830,730</u>                                                                  | <u>\$ 2,874,797</u>                                       | <u>\$ —</u>                                        | <u>\$ 3,705,527</u> |

(1) Does not include the fair value of embedded derivatives, which we have accounted for separately as freestanding derivatives and included in other assets or other accrued liabilities in our condensed consolidated balance sheet. See Note 4 for more information.

| December 31, 2019 (In thousands)               | Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Instruments<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total               |
|------------------------------------------------|------------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|---------------------|
| <b>Recurring fair value measurements</b>       |                                                                                    |                                                           |                                                    |                     |
| Financial Assets:                              |                                                                                    |                                                           |                                                    |                     |
| U.S. Treasury securities                       | \$ 242,206                                                                         | \$ —                                                      | \$ —                                               | \$ 242,206          |
| U.S. agency securities                         | —                                                                                  | 33,605                                                    | —                                                  | 33,605              |
| U.S. agency mortgage-backed securities         | —                                                                                  | 848,334                                                   | —                                                  | 848,334             |
| Municipal debt securities                      | —                                                                                  | 361,638                                                   | —                                                  | 361,638             |
| Non-U.S. government securities                 | —                                                                                  | 54,995                                                    | —                                                  | 54,995              |
| Corporate debt securities                      | —                                                                                  | 880,301                                                   | —                                                  | 880,301             |
| Residential and commercial mortgage securities | —                                                                                  | 288,281                                                   | —                                                  | 288,281             |
| Asset-backed securities                        | —                                                                                  | 326,025                                                   | —                                                  | 326,025             |
| Money market funds                             | 315,362                                                                            | —                                                         | —                                                  | 315,362             |
| Total assets at fair value (1)                 | <u>\$ 557,568</u>                                                                  | <u>\$ 2,793,179</u>                                       | <u>\$ —</u>                                        | <u>\$ 3,350,747</u> |

(1) Does not include the fair value of embedded derivatives, which we have accounted for separately as freestanding derivatives and included in other assets or other accrued liabilities in our condensed consolidated balance sheet. See Note 4 for more information.

**Notes to Condensed Consolidated Financial Statements (Unaudited)**
**Note 14. Statutory Accounting**

Our U.S. insurance subsidiaries prepare statutory-basis financial statements in accordance with the accounting practices prescribed or permitted by their respective state's department of insurance, which is a comprehensive basis of accounting other than GAAP. We did not use any prescribed or permitted statutory accounting practices (individually or in the aggregate) that resulted in reported statutory surplus or capital that was significantly different from the statutory surplus or capital that would have been reported had National Association of Insurance Commissioners' statutory accounting practices been followed. The following table presents Essent Guaranty's and Essent PA's statutory net income, statutory surplus and contingency reserve liability as of and for the three months ended March 31:

| (In thousands)                | 2020 |           | 2019 |         |
|-------------------------------|------|-----------|------|---------|
| Essent Guaranty               |      |           |      |         |
| Statutory net income          | \$   | 122,644   | \$   | 101,989 |
| Statutory surplus             |      | 1,074,153 |      | 905,534 |
| Contingency reserve liability |      | 1,270,864 |      | 981,207 |
| Essent PA                     |      |           |      |         |
| Statutory net income          | \$   | 1,627     | \$   | 2,093   |
| Statutory surplus             |      | 53,648    |      | 50,216  |
| Contingency reserve liability |      | 53,854    |      | 49,744  |

Net income determined in accordance with statutory accounting practices differs from GAAP. In 2020 and 2019, the more significant differences between net income determined under statutory accounting practices and GAAP for Essent Guaranty and Essent PA relate to policy acquisition costs and income taxes. Under statutory accounting practices, policy acquisition costs are expensed as incurred while such costs are capitalized and amortized to expense over the life of the policy under GAAP. We are eligible for a tax deduction, subject to certain limitations for amounts required by state law or regulation to be set aside in statutory contingency reserves when we purchase non-interest-bearing United States Mortgage Guaranty Tax and Loss Bonds ("T&L Bonds") issued by the Treasury Department. Under statutory accounting practices, this deduction reduces the tax provision recorded by Essent Guaranty and Essent PA and, as a result, increases statutory net income and surplus as compared to net income and equity determined in accordance with GAAP.

At March 31, 2020 and 2019, the statutory capital of our U.S. insurance subsidiaries, which is defined as the total of statutory surplus and contingency reserves, was in excess of the statutory capital necessary to satisfy their regulatory requirements.

Effective December 31, 2015, Fannie Mae and Freddie Mac, at the direction of the Federal Housing Finance Agency, implemented new coordinated Private Mortgage Insurer Eligibility Requirements, which we refer to as the "PMIERs." The PMIERs represent the standards by which private mortgage insurers are eligible to provide mortgage insurance on loans owned or guaranteed by Fannie Mae and Freddie Mac. The PMIERs include financial strength requirements incorporating a risk-based framework that require approved insurers to have a sufficient level of liquid assets from which to pay claims. The PMIERs also include enhanced operational performance expectations and define remedial actions that apply should an approved insurer fail to comply with these requirements. In 2018, the GSEs released revised PMIERs framework ("PMIERs 2.0") which became effective on March 31, 2019. As of March 31, 2020, Essent Guaranty, our GSE-approved mortgage insurance company, was in compliance with PMIERs 2.0. Due to business restrictions, stay-at-home orders and travel restrictions implemented as a result of COVID-19, we expect to experience increased defaults beginning in the second quarter of 2020. An increase in defaults increases our Minimum Required Assets under PMIERs, and, accordingly, we expect our Minimum Required Assets to increase in future periods.

Statement of Statutory Accounting Principles No. 58, *Mortgage Guaranty Insurance*, requires mortgage insurers to establish a special contingency reserve for statutory accounting purposes included in total liabilities equal to 50% of earned premium for that year. During the three months ended March 31, 2020, Essent Guaranty increased its contingency reserve by \$73.6 million and Essent PA increased its contingency reserve by \$0.9 million. This reserve is required to be maintained for a period of 120 months to protect against the effects of adverse economic cycles. After 120 months, the reserve is released to unassigned funds. In the event an insurer's loss ratio in any calendar year exceeds 35%, however, the insurer may, after

**Notes to Condensed Consolidated Financial Statements (Unaudited)**

regulatory approval, release from its contingency reserves an amount equal to the excess portion of such losses. Essent Guaranty and Essent PA did not release any amounts from their contingency reserves in the three months ended March 31, 2020 or 2019.

Under The Insurance Act 1978, as amended, and related regulations of Bermuda (the "Insurance Act"), Essent Re is required to annually prepare statutory financial statements and a statutory financial return in accordance with the financial reporting provisions of the Insurance Act, which is a basis other than GAAP. The Insurance Act also requires that Essent Re maintain minimum share capital of \$1 million and must ensure that the value of its general business assets exceeds the amount of its general business liabilities by an amount greater than the prescribed minimum solvency margins and enhanced capital requirement pertaining to its general business. At December 31, 2019, all such requirements were met.

Essent Re's statutory capital and surplus was \$1.0 billion as of March 31, 2020 and \$939.2 million as of December 31, 2019. Essent Re's statutory net income was \$49.5 million and \$39.5 million for the three months ended March 31, 2020 and 2019, respectively. Statutory capital and surplus as of March 31, 2020 and December 31, 2019 and statutory net income in the three months ended March 31, 2020 and 2019 determined in accordance with statutory accounting practices were not significantly different than the amounts determined under GAAP.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

*The following discussion should be read together with the "Selected Financial Data" and our audited consolidated financial statements and related notes included in our Annual Report on Form 10-K as of and for the year ended December 31, 2019 as filed with the Securities and Exchange Commission and referred to herein as the "Annual Report," and our condensed consolidated financial statements and related notes as of and for the three months ended March 31, 2020 included in Part I, Item 1 of this Quarterly Report on Form 10-Q, which we refer to as the "Quarterly Report." In addition to historical information, this discussion contains forward-looking statements that involve risks, uncertainties and assumptions that could cause actual results to differ materially from management's expectations. Factors that could cause such differences are discussed in the sections entitled "Special Note Regarding Forward-Looking Statements" in this Quarterly Report and Part I, Item 1A "Risk Factors" in our Annual Report. We are not undertaking any obligation to update any forward-looking statements or other statements we may make in the following discussion or elsewhere in this document even though these statements may be affected by events or circumstances occurring after the forward-looking statements or other statements were made.*

### Overview

We are an established and growing private mortgage insurance company. Essent Guaranty, Inc., our wholly-owned insurance subsidiary which we refer to as "Essent Guaranty," is licensed to write coverage in all 50 states and the District of Columbia. The financial strength ratings of Essent Guaranty are A3 with a stable outlook by Moody's Investors Service ("Moody's"), BBB+ with a negative outlook by S&P Global Ratings ("S&P") and A (Excellent) with a stable outlook by A.M. Best.

Our holding company is domiciled in Bermuda and our U.S. insurance business is headquartered in Radnor, Pennsylvania. We operate additional underwriting and service centers in Winston-Salem, North Carolina and Irvine, California. We have a highly experienced, talented team with 381 employees as of March 31, 2020. We generated new insurance written, or NIW, of approximately \$13.5 billion and \$11.0 billion for the three months ended March 31, 2020 and 2019, respectively. As of March 31, 2020, we had approximately \$165.6 billion of insurance in force.

We also offer mortgage-related insurance and reinsurance through our wholly-owned Bermuda-based subsidiary, Essent Reinsurance Ltd., which we refer to as "Essent Re." As of March 31, 2020, Essent Re provided insurance or reinsurance relating to GSE risk share and other reinsurance transactions covering approximately \$1.1 billion of risk. Essent Re also reinsures 25% of Essent Guaranty's NIW under a quota share reinsurance agreement. The insurer financial strength rating of Essent Re is BBB+ with a negative outlook by S&P and A (Excellent) with a stable outlook by A.M. Best.

### COVID-19

The novel coronavirus disease 2019 ("COVID-19") was first identified in December 2019 in Wuhan China. On March 11, 2020 the outbreak had spread to be declared a pandemic by the World Health Organization ("WHO"). Within a week of the WHO's declaration, most major economies had announced significant and increasing restrictions on the movement and interaction of people. By the end of March 2020 it was estimated that a quarter of the world's population was under some form of lockdown or stay-at-home order. Most state governments in the United States have implemented some form of travel and/or business restrictions to slow the spread of COVID-19. Business restrictions, stay-at-home orders and travel restrictions have resulted in a significant increase in unemployment in the United States, which has the potential to increase the number of delinquencies and claim frequencies on the mortgages we insure, as homeowners may not be able to make mortgage payments during extended periods of unemployment.

In response to the impact of COVID-19, the federal government has implemented unprecedented measures to assist borrowers in avoiding foreclosures and allow families to remain in their homes. Most notably, under the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act"), consumers with federally backed mortgages were granted two financial protections: (1) a temporary moratorium on foreclosures, and (2) mortgage forbearance, either in the form of a lower monthly payment or temporarily suspending payments. Under the new law, borrowers have the right to request forbearance for up to 360 days due to hardship caused by COVID-19. We believe that these measures will likely increase the overall duration of the default resolution process, which may result in increases in claim severities for loans that proceed to claim.

Over 95% of loans insured by Essent are federally backed by Fannie Mae or Freddie Mac. As a mortgage loan in forbearance is considered delinquent, we will provide loss reserves as loans in forbearance are reported to us as delinquent once the borrower has missed two consecutive payments. However, we believe providing borrowers time to recover from the adverse financial impact of the COVID-19 event may allow some families to be able to remain in their homes and avoid foreclosure.

For borrowers that have the ability to begin to pay their mortgage at the end of the forbearance period, mortgage servicers may work with them to modify the loans at which time the mortgage should be removed from delinquency status.

Essent has had a Pandemic Plan in place as part of its comprehensive Business Continuity Program for a number of years and invoked the Pandemic Plan in light of the COVID-19 event. Our workforce has been working in "full remote" mode since March 16, 2020. Through the use of technology, our national and regional account managers and customer service team have been in contact with our policyholders and their servicers, and we have made several COVID-19-related announcements which have been posted on our mortgage insurance website.

As of March 31, 2020, COVID-19 had not had a significant impact on our financial position or results of operations. As noted in "— Liquidity and Capital Resources," Essent had substantial liquidity and had Available Assets in excess of Minimum Required Assets under PMIERS 2.0 as of March 31, 2020. In order to maintain continuous MI coverage, mortgage servicers are required to advance MI premiums to us even if borrowers are in a forbearance plan. However, due to the increased unemployment noted above, we expect an increase in defaults, which will result in an increase in our provisions for loss and loss adjustment expenses compared to prior periods, reduced profit commission under our quota share reinsurance agreement with a panel of third-party reinsurers ("the QSR Agreement") and an increase in our Minimum Required Assets. In addition, it is possible that the volume of new mortgages could be negatively impacted by the stay-at-home orders which could result in lower NIW in future periods.

## **Legislative and Regulatory Developments**

Our results are significantly impacted by, and our future success may be affected by, legislative and regulatory developments affecting the housing finance industry. See Part I, Item 1 "Business—Regulation" and Part II, Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations—Legislative and Regulatory Developments" in our Annual Report for a discussion of the laws and regulations to which we are subject as well as legislative and regulatory developments affecting the housing finance industry.

The U.S. Internal Revenue Service and Department of the Treasury issued proposed regulations on July 10, 2019 relating to the tax treatment of passive foreign investment companies ("PFICs"). The proposed regulations provide guidance on various PFIC rules, including changes resulting from the 2017 Tax Cuts and Jobs Act. The Company is evaluating the potential impact of these proposed regulations to its shareholders and business operations.

## **Factors Affecting Our Results of Operations**

### ***Net Premiums Written and Earned***

Premiums associated with our U.S. mortgage insurance business are based on insurance in force ("IIF") during all or a portion of a period. A change in the average IIF during a period causes premiums to increase or decrease as compared to prior periods. Average net premium rates in effect during a given period will also cause premiums to differ when compared to earlier periods. IIF at the end of a reporting period is a function of the IIF at the beginning of such reporting period plus NIW less policy cancellations (including claims paid) during the period. As a result, premiums are generally influenced by:

- NIW, which is the aggregate principal amount of the new mortgages that are insured during a period. Many factors affect NIW, including, among others, the volume of low down payment home mortgage originations, the competition to provide credit enhancement on those mortgages, the number of customers who have approved us to provide mortgage insurance and changes in our NIW from certain customers;
- Cancellations of our insurance policies, which are impacted by payments on mortgages, home price appreciation, or refinancings, which in turn are affected by mortgage interest rates. Cancellations are also impacted by the levels of claim payments and rescissions;
- Premium rates, which represent the amount of the premium due as a percentage of IIF. Premium rates are based on the risk characteristics of the loans insured, the percentage of coverage on the loans, competition from other mortgage insurers and general industry conditions; and
- Premiums ceded or assumed under reinsurance arrangements. See Note 4 to our condensed consolidated financial statements.

Premiums are paid either on a monthly installment basis (“monthly premiums”), in a single payment at origination (“single premiums”), or in some cases as an annual premium. For monthly premiums, we receive a monthly premium payment which is recorded as net premiums earned in the month the coverage is provided. Monthly premium payments are based on the original mortgage amount rather than the amortized loan balance. Net premiums written may be in excess of net premiums earned due to single premium policies. For single premiums, we receive a single premium payment at origination, which is recorded as “unearned premium” and earned over the estimated life of the policy, which ranges from 36 to 156 months depending on the term of the underlying mortgage and loan-to-value ratio at date of origination. If single premium policies are cancelled due to repayment of the underlying loan and the premium is non-refundable, the remaining unearned premium balance is immediately recognized as earned premium revenue. Substantially all of our single premium policies in force as of March 31, 2020 were non-refundable. Premiums collected on annual policies are recognized as net premiums earned on a straight-line basis over the year of coverage. For the three months ended March 31, 2020 and 2019, monthly premium policies comprised 90% and 87% of our NIW, respectively.

Premiums associated with our GSE and other risk share transactions are based on the level of risk in force and premium rates on the transactions.

### ***Persistency and Business Mix***

The percentage of IIF that remains on our books after any 12-month period is defined as our persistency rate. Because our insurance premiums are earned over the life of a policy, higher persistency rates can have a significant impact on our profitability. The persistency rate on our portfolio was 73.9% at March 31, 2020. Generally, higher prepayment speeds lead to lower persistency.

Prepayment speeds and the relative mix of business between single premium policies and monthly premium policies also impact our profitability. Our premium rates include certain assumptions regarding repayment or prepayment speeds of the mortgages. Because premiums are paid at origination on single premium policies, assuming all other factors remain constant, if loans are prepaid earlier than expected, our profitability on these loans is likely to increase and, if loans are repaid slower than expected, our profitability on these loans is likely to decrease. By contrast, if monthly premium loans are repaid earlier than anticipated, our premium earned with respect to those loans and therefore our profitability declines. Currently, the expected return on single premium policies is less than the expected return on monthly policies.

### ***Net Investment Income***

Our investment portfolio was predominantly comprised of investment-grade fixed income securities and money market funds as of March 31, 2020. The principal factors that influence investment income are the size of the investment portfolio and the yield on individual securities. As measured by amortized cost (which excludes changes in fair market value, such as from changes in interest rates), the size of our investment portfolio is mainly a function of increases in capital and cash generated from or used in operations which is impacted by net premiums received, investment earnings, net claim payments and expenses. Realized gains and losses are a function of the difference between the amount received on the sale of a security and the security’s amortized cost, as well as any “other-than-temporary” impairments recognized in earnings. The amount received on the sale of fixed income securities is affected by the coupon rate of the security compared to the yield of comparable securities at the time of sale.

### ***Other Income***

Other income includes revenues associated with contract underwriting services and underwriting consulting services to third-party reinsurers. The level of contract underwriting revenue is dependent upon the number of customers who have engaged us for this service and the number of loans underwritten for these customers. Revenue from underwriting consulting services to third-party reinsurers is dependent upon the number of customers who have engaged us for this service and the level of premiums associated with the transactions underwritten for these customers.

In connection with the acquisition of our mortgage insurance platform, we entered into a services agreement with Triad Guaranty Inc. and its wholly-owned subsidiary, Triad Guaranty Insurance Corporation, which we refer to collectively as “Triad,” to provide certain information technology maintenance and development and customer support-related services. In return for these services, we receive a fee which is recorded in other income. Prior to December 1, 2019, this fee was adjusted monthly based on the number of Triad’s mortgage insurance policies in force and, accordingly, decreased over time as Triad’s existing policies were cancelled. Effective December 1, 2019, the services agreement was amended providing for a flat monthly fee through November 30, 2021. The services agreement provides for two subsequent one-year renewals at Triad’s option.

As more fully described in Note 4 to our condensed consolidated financial statements, the premiums ceded under certain reinsurance contracts with unaffiliated third parties varies based on changes in market interest rates. Under GAAP, these contracts contain embedded derivatives that are accounted for separately as freestanding derivatives. The change in the fair value of the embedded derivatives is reported in earnings and included in other income.

### ***Provision for Losses and Loss Adjustment Expenses***

The provision for losses and loss adjustment expenses reflects the current expense that is recorded within a particular period to reflect actual and estimated loss payments that we believe will ultimately be made as a result of insured loans that are in default.

Losses incurred are generally affected by:

- the overall state of the economy, which broadly affects the likelihood that borrowers may default on their loans and have the ability to cure such defaults;
- changes in housing values, which affect our ability to mitigate our losses through the sale of properties with loans in default as well as borrower willingness to continue to make mortgage payments when the value of the home is below or perceived to be below the mortgage balance;
- the product mix of IIF, with loans having higher risk characteristics generally resulting in higher defaults and claims;
- the size of loans insured, with higher average loan amounts tending to increase losses incurred;
- the loan-to-value ratio, with higher average loan-to-value ratios tending to increase losses incurred;
- the percentage of coverage on insured loans, with deeper average coverage tending to increase losses incurred;
- credit quality of borrowers, including higher debt-to-income ratios and lower FICO scores, which tend to increase incurred losses;
- the level and amount of reinsurance coverage maintained with third parties;
- the rate at which we rescind policies. Because of tighter underwriting standards generally in the mortgage lending industry and terms set forth in our master policy, we expect that our level of rescission activity will be lower than rescission activity seen in the mortgage insurance industry for vintages originated prior to the financial crisis; and
- the distribution of claims over the life of a book. As of March 31, 2020, 62% of our IIF relates to business written since January 1, 2018 and was less than three years old. As a result, based on historical industry performance, we expect the number of defaults and claims we experience, as well as our provision for losses and loss adjustment expenses ("LAE"), to increase as our portfolio seasons. See "— Mortgage Insurance Earnings and Cash Flow Cycle" below.

We establish loss reserves for delinquent loans when we are notified that a borrower has missed at least two consecutive monthly payments ("Case Reserves"), as well as estimated reserves for defaults that may have occurred but not yet been reported to us ("IBNR Reserves"). We also establish reserves for the associated loss adjustment expenses, consisting of the estimated cost of the claims administration process, including legal and other fees. Using both internal and external information, we establish our reserves based on the likelihood that a default will reach claim status and estimated claim severity. See Part II, Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Policies" included in our Annual Report for further information.

We believe, based upon our experience and industry data, that claims incidence for mortgage insurance is generally highest in the third through sixth years after loan origination. As of March 31, 2020, 62% of our IIF relates to business written since January 1, 2018 and was less than three years old. Although the claims experience on new insurance written by us to date has been favorable, we expect incurred losses and claims to increase as a greater amount of this book of insurance reaches its anticipated period of highest claim frequency. The actual default rate and the average reserve per default that we experience as our portfolio matures is difficult to predict and is dependent on the specific characteristics of our current in-force book (including the credit score of the borrower, the loan-to-value ratio of the mortgage, geographic concentrations, etc.), as well as

the profile of new business we write in the future. In addition, the default rate and the average reserve per default will be affected by future macroeconomic factors such as housing prices, interest rates and employment.

Due to business restrictions, stay-at-home orders and travel restrictions implemented as a result of COVID-19, unemployment in the United States has increased significantly. As unemployment is one of the most common reasons for borrowers to default on their mortgage, the increase in unemployment has the potential to increase the number of delinquencies on the mortgages we insure, and the claim frequency on existing delinquencies. We expect to experience increased defaults beginning in the second quarter of 2020. It is too early to tell how many claims we ultimately may have to pay associated with COVID-19-related defaults. There are many factors contributing to the uncertainty surrounding these insured loans. For borrowers that have the ability to begin to pay their mortgage at the end of the forbearance period, mortgage servicers will work with them to modify their loans at which time the mortgage will be removed from delinquency status. We believe that the forbearance process could have a favorable effect on the frequency of claims that we ultimately pay. In addition, as more fully described in Note 4 to our condensed consolidated financial statements, at March 31, 2020, we had over \$1.7 billion of excess of loss reinsurance covering NIW from January 1, 2015 to August 31, 2019 and a quota share reinsurance transaction on a portion of our NIW effective September 1, 2019 and continuing through December 31, 2020. COVID-19 has not materially affected our reserves as of March 31, 2020. The impact on our reserves in future periods will be dependent upon the amount of delinquent notices received from loan servicers and our expectations for the amount of ultimate losses on these delinquencies.

### ***Third-Party Reinsurance***

We use third-party reinsurance to provide protection against adverse loss experience and to expand our capital sources. When we enter into a reinsurance agreement, the reinsurer receives a premium and, in exchange, agrees to insure an agreed upon portion of incurred losses. These arrangements have the impact of reducing our earned premiums, but also reduce our risk in force ("RIF"), which provides capital relief, and may include capital relief under the PMIERS financial strength requirements. Our incurred losses are reduced by any incurred losses ceded in accordance with the reinsurance agreement. For additional information regarding reinsurance, see Note 4 to our condensed consolidated financial statements.

### ***Other Underwriting and Operating Expenses***

Our other underwriting and operating expenses include components that are substantially fixed, as well as expenses that generally increase or decrease in line with the level of NIW.

Our most significant expense is compensation and benefits for our employees, which represented 59% of other underwriting and operating expenses for the three months ended March 31, 2020, compared to 57% of other underwriting and operating expenses for the three months ended March 31, 2019. Compensation and benefits expense includes base and incentive cash compensation, stock compensation expense, benefits and payroll taxes.

Underwriting and other expenses include legal, consulting, other professional fees, premium taxes, travel, entertainment, marketing, licensing, supplies, hardware, software, rent, utilities, depreciation and amortization and other expenses. We anticipate that as we continue to add new customers and increase our IIF, our expenses will also continue to increase.

### ***Interest Expense***

Interest expense is incurred as a result of borrowings under our secured credit facility (the "Credit Facility"). Borrowings under the Credit Facility may be used for working capital and general corporate purposes, including, without limitation, capital contributions to Essent's insurance and reinsurance subsidiaries. Borrowings accrue interest at a floating rate tied to a standard short-term borrowing index, selected at the Company's option, plus an applicable margin.

### ***Income Taxes***

Income taxes are incurred based on the amount of earnings or losses generated in the jurisdictions in which we operate and the applicable tax rates and regulations in those jurisdictions. Our U.S. insurance subsidiaries are generally not subject to income taxes in the states in which we operate; however, our non-insurance subsidiaries are subject to state income taxes. In lieu of state income taxes, our insurance subsidiaries pay premium taxes that are recorded in other underwriting and operating expenses.

Essent Group Ltd. ("Essent Group") and its wholly-owned subsidiary, Essent Re, are domiciled in Bermuda, which does not have a corporate income tax. Essent Re reinsures 25% of Essent Guaranty's NIW under a quota share reinsurance agreement. Essent Re also provides insurance and reinsurance to Freddie Mac and Fannie Mae.

The amount of income tax expense or benefit recorded in future periods will be dependent on the jurisdictions in which we operate and the tax laws and regulations in effect.

### ***Mortgage Insurance Earnings and Cash Flow Cycle***

In general, the majority of any underwriting profit (premium revenue minus losses) that a book generates occurs in the early years of the book, with the largest portion of any underwriting profit realized in the first year. Subsequent years of a book generally result in modest underwriting profit or underwriting losses. This pattern generally occurs because relatively few of the claims that a book will ultimately experience typically occur in the first few years of the book, when premium revenue is highest, while subsequent years are affected by declining premium revenues, as the number of insured loans decreases (primarily due to loan prepayments), and by increasing losses.

### **Key Performance Indicators**

#### ***Insurance In Force***

As discussed above, premiums we collect and earn are generated based on our IIF, which is a function of our NIW and cancellations. The following table includes a summary of the change in our IIF for the three months ended March 31, 2020 and 2019 for our U.S. mortgage insurance portfolio. In addition, this table includes RIF at the end of each period.

| (In thousands)                | Three Months Ended March 31, |                |
|-------------------------------|------------------------------|----------------|
|                               | 2020                         | 2019           |
| IIF, beginning of period      | \$ 164,005,853               | \$ 137,720,786 |
| NIW - Flow                    | 13,549,299                   | 10,945,307     |
| NIW - Bulk                    | 151                          | 55,002         |
| Cancellations                 | (11,939,800)                 | (5,539,454)    |
| IIF, end of period            | \$ 165,615,503               | \$ 143,181,641 |
| Average IIF during the period | \$ 164,782,361               | \$ 140,137,045 |
| RIF, end of period            | \$ 38,290,022                | \$ 34,744,417  |

The following is a summary of our IIF at March 31, 2020 by vintage:

| (\$ in thousands)       | \$             | %      |
|-------------------------|----------------|--------|
| 2020 (through March 31) | \$ 13,456,039  | 8.1%   |
| 2019                    | 56,579,438     | 34.2   |
| 2018                    | 32,032,954     | 19.3   |
| 2017                    | 27,127,737     | 16.4   |
| 2016                    | 17,593,372     | 10.6   |
| 2015 and prior          | 18,825,963     | 11.4   |
|                         | \$ 165,615,503 | 100.0% |

#### ***Average Net Premium Rate***

Our average net premium rate is dependent on a number of factors, including: (1) the risk characteristics and average coverage on the mortgages we insure; (2) the mix of monthly premiums compared to single premiums in our portfolio; (3) cancellations of non-refundable single premiums during the period; (4) changes to our pricing for NIW; and (5) premiums ceded under third-party reinsurance agreements. For each of the three months ended March 31, 2020 and 2019, our average net premium rate was 0.48%. In 2019 and 2020, Essent Guaranty entered into third-party reinsurance agreements. We anticipate that the continued use of third-party reinsurance will reduce our average net premium rate in future periods.

### Persistency Rate

The measure for assessing the impact of policy cancellations on IIF is our persistency rate, defined as the percentage of IIF that remains on our books after any twelve-month period. See additional discussion regarding the impact of the persistency rate on our performance in “— Factors Affecting Our Results of Operations — Persistency and Business Mix.”

### Risk-to-Capital

The risk-to-capital ratio has historically been used as a measure of capital adequacy in the U.S. mortgage insurance industry and is calculated as a ratio of net risk in force to statutory capital. Net risk in force represents total risk in force net of reinsurance ceded and net of exposures on policies for which loss reserves have been established. Statutory capital for our U.S. insurance companies is computed based on accounting practices prescribed or permitted by the Pennsylvania Insurance Department. See additional discussion in “— Liquidity and Capital Resources — Insurance Company Capital.”

As of March 31, 2020, our combined net risk in force for our U.S. insurance companies was \$28.7 billion and our combined statutory capital was \$2.5 billion, resulting in a risk-to-capital ratio of 11.7 to 1. The amount of capital required varies in each jurisdiction in which we operate; however, generally, the maximum permitted risk-to-capital ratio is 25.0 to 1. State insurance regulators are currently examining their respective capital rules to determine whether, in light of the financial crisis, changes are needed to more accurately assess mortgage insurers’ ability to withstand stressful economic conditions. As a result, the capital metrics under which they assess and measure capital adequacy may change in the future. Independent of the state regulator and GSE capital requirements, management continually assesses the risk of our insurance portfolio and current market and economic conditions to determine the appropriate levels of capital to support our business.

### Results of Operations

The following table sets forth our results of operations for the periods indicated:

| Summary of Operations<br>(In thousands)   | Three Months Ended March 31, |                   |
|-------------------------------------------|------------------------------|-------------------|
|                                           | 2020                         | 2019              |
| <b>Revenues:</b>                          |                              |                   |
| Net premiums written                      | \$ 191,743                   | \$ 177,644        |
| Decrease in unearned premiums             | 14,753                       | 147               |
| Net premiums earned                       | 206,496                      | 177,791           |
| Net investment income                     | 20,633                       | 19,880            |
| Realized investment gains, net            | 3,135                        | 660               |
| Other income (loss)                       | (1,424)                      | 2,195             |
| Total revenues                            | 228,840                      | 200,526           |
| <b>Losses and expenses:</b>               |                              |                   |
| Provision for losses and LAE              | 8,063                        | 7,107             |
| Other underwriting and operating expenses | 41,947                       | 41,030            |
| Interest expense                          | 2,132                        | 2,670             |
| Total losses and expenses                 | 52,142                       | 50,807            |
| Income before income taxes                | 176,698                      | 149,719           |
| Income tax expense                        | 27,175                       | 21,999            |
| <b>Net income</b>                         | <b>\$ 149,523</b>            | <b>\$ 127,720</b> |

### Three Months Ended March 31, 2020 Compared to the Three Months Ended March 31, 2019

For the three months ended March 31, 2020, we reported net income of \$149.5 million, compared to net income of \$127.7 million for the three months ended March 31, 2019. The increase in our operating results in 2020 over the same period in 2019 was primarily due to the increase in net premiums earned associated with the growth of our IIF and the increases in net investment income and realized investment gains, partially offset by a decrease in other income and increases in the provision for losses and LAE, other underwriting and operating expenses and income tax expense.

### **Net Premiums Written and Earned**

Net premiums earned increased in the three months ended March 31, 2020 by 16%, compared to the three months ended March 31, 2019 primarily due to the increase in our average IIF from \$140.1 billion at March 31, 2019 to \$164.8 billion at March 31, 2020. The average net premium rate was 0.48% for each of the three months ended March 31, 2020 and 2019 as an increase in ceded premiums was offset by an increase in premiums earned on the cancellation of non-refundable single premium policies. In the three months ended March 31, 2020, ceded premiums increased to \$14.2 million, from \$6.0 million in the three months ended March 31, 2019 due to new third-party reinsurance agreements entered in 2020 and a full year of premiums ceded under third-party reinsurance agreements entered in 2019. In the three months ended March 31, 2020, premiums earned on the cancellation of non-refundable single premium policies increased to \$14.6 million, from \$4.3 million in the three months ended March 31, 2019 as a result of an increase in existing borrowers refinancing their mortgages due to favorable mortgage interest rates.

Net premiums written increased by 8% in the three months ended March 31, 2020 compared to the three months ended March 31, 2019. The increase in net written premiums in the three months ended March 31, 2020 was primarily due to an increase in average IIF in the respective period, partially offset by an increase in premiums ceded under third-party reinsurance agreements, a decrease in new single premium policies written, changes in the mix of mortgages we insure and changes in our pricing.

In the three months ended March 31, 2020 and 2019, unearned premiums decreased by \$14.8 million and \$0.1 million, respectively. The change in unearned premiums was a result of net premiums written on single premium policies of \$16.0 million and \$20.0 million, respectively, which was offset by \$30.8 million and \$20.1 million, respectively, of unearned premium that was recognized in earnings during the periods.

### **Net Investment Income**

Our net investment income was derived from the following sources for the periods indicated:

| (In thousands)          | Three Months Ended March 31, |           |
|-------------------------|------------------------------|-----------|
|                         | 2020                         | 2019      |
| Fixed maturities        | \$ 20,614                    | \$ 19,743 |
| Short-term investments  | 1,122                        | 1,058     |
| Gross investment income | 21,736                       | 20,801    |
| Investment expenses     | (1,103)                      | (921)     |
| Net investment income   | \$ 20,633                    | \$ 19,880 |

The increase in net investment income for the three months ended March 31, 2020 as compared to the same period in 2019 was due to the increase in the weighted average balance of our investment portfolio partially offset by a decrease in the pre-tax investment income yield. The average cash and investment portfolio balance increased to \$3.5 billion for the three months ended March 31, 2020 from \$2.9 billion for the three months ended March 31, 2019. The increase in the average cash and investment portfolio was primarily due to investing cash flows from operations. The pre-tax investment income yield decreased from 2.8% in the three months ended March 31, 2019 to 2.5% in the three months ended March 31, 2020 primarily due to an increase in the share of our investments allocated to cash, a general decline in investment yields due to declining interest rates and an increase in premium amortization on mortgage-backed and asset-backed securities. The pre-tax investment income yields are calculated based on amortized cost and exclude investment expenses. See “— Liquidity and Capital Resources” for further details of our investment portfolio.

### **Other Income**

Other income for three months ended March 31, 2019 was \$2.2 million compared to a loss of \$1.4 million for the three months ended March 31, 2020. The decrease in other income for the three months ended March 31, 2020 as compared to the same period in 2019 was primarily due to the changes in fair value of embedded derivatives contained in certain of our reinsurance agreements. In the three months ended March 31, 2020, we recorded an unfavorable decrease in the fair value of these embedded derivatives of \$4.2 million compared to a favorable increase in the fair value of the embedded derivatives of \$1.4 million in the three months ended March 31, 2019. Partially offsetting this decrease was an increase in fees earned for information technology and customer support services provided to Triad of \$1.6 million for the three months ended March 31, 2020 as compared to \$0.2 million for the three months ended March 31, 2019. Effective December 1, 2019, the Triad services

agreement was amended providing for a flat monthly fee through November 30, 2021. Other income also includes contract underwriting revenues and underwriting consulting services to third-party reinsurers.

### ***Provision for Losses and Loss Adjustment Expenses***

The increase in the provision for losses and LAE in the three months ended March 31, 2020 as compared to the same period in 2019 was primarily due to changes in the composition (such as mark-to-market loan-to-value ratios, risk in force, and number of months past due) of the underlying loans in default.

The following table presents a rollforward of insured loans in default for our U.S. mortgage insurance portfolio for the periods indicated:

|                                    | <b>Three Months Ended March 31,</b> |             |
|------------------------------------|-------------------------------------|-------------|
|                                    | <b>2020</b>                         | <b>2019</b> |
| Beginning default inventory        | 5,947                               | 4,024       |
| Plus: new defaults                 | 3,933                               | 2,918       |
| Less: cures                        | (3,914)                             | (2,749)     |
| Less: claims paid                  | (118)                               | (88)        |
| Less: rescissions and denials, net | (7)                                 | (9)         |
| Ending default inventory           | 5,841                               | 4,096       |

The increase in the number of defaults at March 31, 2020 compared to March 31, 2019 was primarily due to the increase in our IIF and policies in force and further seasoning of our insurance portfolio.

The following table includes additional information about our loans in default as of the dates indicated for our U.S. mortgage insurance portfolio:

|                                                      | <b>As of March 31,</b> |             |
|------------------------------------------------------|------------------------|-------------|
|                                                      | <b>2020</b>            | <b>2019</b> |
| Case reserves (in thousands) <b>(1)</b>              | \$ 67,097              | \$ 49,093   |
| Total reserves (in thousands) <b>(1)</b>             | \$ 73,325              | \$ 53,484   |
| Ending default inventory                             | 5,841                  | 4,096       |
| Average case reserve per default (in thousands)      | \$ 11.5                | \$ 12.0     |
| Average total reserve per default (in thousands)     | \$ 12.6                | \$ 13.1     |
| Default rate                                         | 0.83%                  | 0.65%       |
| Claims received included in ending default inventory | 140                    | 71          |

(1) The U.S. mortgage insurance portfolio reserves exclude reserves on GSE and other risk share risk in force at Essent Re of \$16 thousand as of March 31, 2020.

The decrease in the average case reserve per default was primarily due to improvements in economic fundamentals from the beginning of 2019 into the first quarter of 2020.

The following table provides a reconciliation of the beginning and ending reserve balances for losses and LAE:

| (In thousands)                                      | Three Months Ended March 31, |           |
|-----------------------------------------------------|------------------------------|-----------|
|                                                     | 2020                         | 2019      |
| Reserve for losses and LAE at beginning of period   | \$ 69,362                    | \$ 49,464 |
| Less: Reinsurance recoverables                      | 71                           | —         |
| Net reserve for losses and LAE at beginning of year | 69,291                       | 49,464    |
| Add provision for losses and LAE occurring in:      |                              |           |
| Current period                                      | 15,419                       | 11,828    |
| Prior years                                         | (7,356)                      | (4,721)   |
| Incurred losses and LAE during the current period   | 8,063                        | 7,107     |
| Deduct payments for losses and LAE occurring in:    |                              |           |
| Current period                                      | 1                            | 15        |
| Prior years                                         | 4,110                        | 3,072     |
| Loss and LAE payments during the current period     | 4,111                        | 3,087     |
| Net reserve for losses and LAE at end of period     | 73,243                       | 53,484    |
| Plus: Reinsurance recoverables                      | 98                           | —         |
| Reserve for losses and LAE at end of period         | \$ 73,341                    | \$ 53,484 |

The following tables provide a detail of reserves and defaulted RIF by the number of missed payments and pending claims for our U.S. mortgage insurance portfolio:

| (\$ in thousands)                     | As of March 31, 2020          |                                   |                    |                        |               |                                           |
|---------------------------------------|-------------------------------|-----------------------------------|--------------------|------------------------|---------------|-------------------------------------------|
|                                       | Number of Policies in Default | Percentage of Policies in Default | Amount of Reserves | Percentage of Reserves | Defaulted RIF | Reserves as a Percentage of Defaulted RIF |
| Missed payments:                      |                               |                                   |                    |                        |               |                                           |
| Three payments or less                | 3,043                         | 52%                               | \$ 15,128          | 23%                    | \$ 170,374    | 9%                                        |
| Four to eleven payments               | 2,140                         | 37                                | 30,493             | 45                     | 114,135       | 27                                        |
| Twelve or more payments               | 518                           | 9                                 | 15,235             | 23                     | 29,596        | 51                                        |
| Pending claims                        | 140                           | 2                                 | 6,241              | 9                      | 7,074         | 88                                        |
| Total case reserves (1)               | 5,841                         | 100%                              | 67,097             | 100%                   | \$ 321,179    | 21                                        |
| IBNR                                  |                               |                                   | 5,032              |                        |               |                                           |
| LAE                                   |                               |                                   | 1,196              |                        |               |                                           |
| Total reserves for losses and LAE (1) |                               |                                   | \$ 73,325          |                        |               |                                           |

(1) The U.S. mortgage insurance portfolio reserves exclude reserves on GSE and other risk share risk in force at Essent Re of \$16 thousand as of March 31, 2020.

| (\$ in thousands)                 | As of March 31, 2019          |                                   |                    |                        |               |                                           |
|-----------------------------------|-------------------------------|-----------------------------------|--------------------|------------------------|---------------|-------------------------------------------|
|                                   | Number of Policies in Default | Percentage of Policies in Default | Amount of Reserves | Percentage of Reserves | Defaulted RIF | Reserves as a Percentage of Defaulted RIF |
| Missed payments:                  |                               |                                   |                    |                        |               |                                           |
| Three payments or less            | 2,172                         | 53%                               | \$ 11,374          | 23%                    | \$ 117,607    | 10%                                       |
| Four to eleven payments           | 1,492                         | 36                                | 23,599             | 48                     | 80,842        | 29                                        |
| Twelve or more payments           | 361                           | 9                                 | 11,105             | 23                     | 20,526        | 54                                        |
| Pending claims                    | 71                            | 2                                 | 3,015              | 6                      | 3,517         | 86                                        |
| Total case reserves               | 4,096                         | 100%                              | 49,093             | 100%                   | \$ 222,492    | 22                                        |
| IBNR                              |                               |                                   | 3,682              |                        |               |                                           |
| LAE                               |                               |                                   | 709                |                        |               |                                           |
| Total reserves for losses and LAE |                               |                                   | \$ 53,484          |                        |               |                                           |

During the three months ended March 31, 2020, the provision for losses and LAE was \$8.1 million, comprised of \$15.4 million of current year losses partially offset by \$7.4 million of favorable prior years' loss development. During the three months ended March 31, 2019, the provision for losses and LAE was \$7.1 million, comprised of \$11.8 million of current year losses partially offset by \$4.7 million of favorable prior years' loss development. In both periods, the prior years' loss development was the result of a re-estimation of amounts ultimately to be paid on prior year defaults in the default inventory, including the impact of previously identified defaults that cured.

The following table includes additional information about our claims paid and claim severity as of the dates indicated:

| (\$ in thousands)     | Three Months Ended March 31, |          |
|-----------------------|------------------------------|----------|
|                       | 2020                         | 2019     |
| Number of claims paid | 118                          | 88       |
| Amount of claims paid | \$ 4,157                     | \$ 2,899 |
| Claim severity        | 77%                          | 78%      |

### ***Other Underwriting and Operating Expenses***

Following are the components of our other underwriting and operating expenses for the periods indicated:

| (\$ in thousands)                               | Three Months Ended March 31, |      |           |      |
|-------------------------------------------------|------------------------------|------|-----------|------|
|                                                 | 2020                         |      | 2019      |      |
|                                                 | \$                           | %    | \$        | %    |
| Compensation and benefits                       | \$ 24,866                    | 59%  | \$ 23,349 | 57%  |
| Premium taxes                                   | 4,433                        | 11   | 4,078     | 10   |
| Other                                           | 12,648                       | 30   | 13,603    | 33   |
| Total other underwriting and operating expenses | \$ 41,947                    | 100% | \$ 41,030 | 100% |
| Number of employees at end of period            | 381                          |      | 377       |      |

The significant factors contributing to the change in other underwriting and operating expenses are:

- Compensation and benefits increased in the three months ended March 31, 2020 as compared to the three months ended March 31, 2019 primarily due to increased stock compensation expense associated with shares granted in 2019 and 2020 and increased salaries and overtime associated with our increased NIW. Compensation and benefits includes salaries, wages and bonus, stock compensation expense, benefits and payroll taxes.
- Premium taxes increased primarily due to an increase in premiums written.
- Other expenses decreased as a result of ceding commission earned under the QSR Agreement. Other expenses include professional fees, travel, marketing, hardware, software, rent, depreciation and amortization and other facilities expenses.

### ***Interest Expense***

For the three months ended March 31, 2020, we incurred interest expense of \$2.1 million as compared to \$2.7 million for the three months ended March 31, 2019. The decrease was primarily due to a decrease in the weighted average interest rate for borrowings outstanding, partially offset by an increase in the average amounts outstanding under the Credit Facility. For the three months ended March 31, 2020, the average amount outstanding under the Credit Facility was \$236.0 million as compared to \$225.0 million for the three months ended March 31, 2019. For the three months ended March 31, 2020, the borrowings under the Credit Facility had a weighted average interest rate of 3.08% as compared to 4.49% for the three months ended March 31, 2019.

## ***Income Taxes***

Our subsidiaries in the United States file a consolidated U.S. Federal income tax return. Our income tax expense was \$27.2 million and \$22.0 million for the three months ended March 31, 2020 and 2019, respectively. For the three months ended March 31, 2020, our provision for income taxes was not based on an estimated annual effective rate due to uncertainty regarding the potential impacts of COVID-19 on our results of operations. Due to that uncertainty, we were unable to make a reliable estimate of pretax income and the annual effective tax rate for the full year 2020. Accordingly, the provision for income taxes for the three months ended March 31, 2020 was based on the actual effective tax rate of 15.4% for the year to date period. For the three months ended March 31, 2019, our income tax expense was calculated using an estimated annual effective tax rate of 16.0%. For the three months ended March 31, 2020 and 2019, income tax expense was reduced by excess tax benefits associated with the vesting of common shares and common share units of \$0.6 million and \$2.0 million, respectively. The tax effects associated with the vesting of common shares and common share units are treated as discrete items in the reporting period in which they occur and are not considered in the 2019 estimated annual effective tax rate above.

## **Liquidity and Capital Resources**

### ***Overview***

Our sources of funds consist primarily of:

- our investment portfolio and interest income on the portfolio;
- net premiums that we will receive from our existing IIF as well as policies that we write in the future;
- borrowings under our Credit Facility; and
- issuance of capital shares.

Our obligations consist primarily of:

- claim payments under our policies;
- interest payments and repayment of borrowings under our Credit Facility;
- the other costs and operating expenses of our business; and
- the payment of dividends on our common shares.

As of March 31, 2020, we had substantial liquidity with cash of \$31.1 million, short-term investments of \$595.2 million and fixed maturity investments of \$3.1 billion. We also had \$75 million available capacity under the revolving credit component of our Credit Facility, with \$425 million of borrowings outstanding under our Credit Facility. Borrowings under the Credit Facility contractually mature on May 17, 2021. At March 31, 2020, net cash and investments at the holding company were \$279.8 million. In addition, Essent Guaranty is a member of the Federal Home Loan Bank of Pittsburgh (the “FHLBank”) and has access to secured borrowing capacity with the FHLBank to provide Essent Guaranty with supplemental liquidity. Essent Guaranty had no outstanding borrowings with the FHLBank at March 31, 2020.

Management believes that the Company has sufficient liquidity available both at the holding company and in its insurance and other operating subsidiaries to meet its operating cash needs and obligations and committed capital expenditures for the next 12 months.

While the Company and all of its subsidiaries are expected to have sufficient liquidity to meet all their expected obligations, additional capital may be required to meet any new capital requirements that are adopted by regulatory authorities or the GSEs, or to respond to changes in the business or economic environment related to COVID-19, or to provide additional capital related to the growth of our risk in force in our mortgage insurance portfolio, or to fund new business initiatives including the insurance activities of Essent Re. We continually evaluate opportunities based upon market conditions to further increase our financial flexibility through the issuance of equity or debt, or other options including reinsurance or credit risk transfer transactions. There can be no guarantee that any such opportunities will be available on acceptable terms or at all.

At the operating subsidiary level, liquidity could be impacted by any one of the following factors:

- significant decline in the value of our investments;
- inability to sell investment assets to provide cash to fund operating needs;
- decline in expected revenues generated from operations;
- increase in expected claim payments related to our IIF; or
- increase in operating expenses.

Our U.S. insurance subsidiaries are subject to certain capital and dividend rules and regulations prescribed by jurisdictions in which they are authorized to operate and the GSEs. Under the insurance laws of the Commonwealth of Pennsylvania, the insurance subsidiaries may pay dividends during any twelve-month period in an amount equal to the greater of (i) 10% of the preceding year-end statutory policyholders' surplus or (ii) the preceding year's statutory net income. The Pennsylvania statute also requires that dividends and other distributions be paid out of positive unassigned surplus without prior approval. At March 31, 2020, Essent Guaranty had unassigned surplus of approximately \$368.8 million. Essent Guaranty of PA, Inc. ("Essent PA") had unassigned surplus of approximately \$14.6 million as of March 31, 2020. Essent Re is subject to certain dividend restrictions as prescribed by the Bermuda Monetary Authority and under certain agreements with counterparties. In connection with a quota share reinsurance agreement with Essent Guaranty, Essent Re has agreed to maintain a minimum total equity of \$100 million. As of March 31, 2020, Essent Re had total equity of \$1.0 billion. In connection with its insurance and reinsurance activities, Essent Re is required to maintain assets in trusts for the benefit of its contractual counterparties. See Note 3 to our condensed consolidated financial statements. At March 31, 2020, our insurance subsidiaries were in compliance with these rules, regulations and agreements.

### ***Cash Flows***

The following table summarizes our consolidated cash flows from operating, investing and financing activities:

| (In thousands)                                      | Three Months Ended March 31, |                    |
|-----------------------------------------------------|------------------------------|--------------------|
|                                                     | 2020                         | 2019               |
| Net cash provided by operating activities           | \$ 163,131                   | \$ 138,682         |
| Net cash used in investing activities               | (381,426)                    | (155,039)          |
| Net cash provided by (used in) financing activities | 178,000                      | (8,100)            |
| Net decrease in cash                                | <u>\$ (40,295)</u>           | <u>\$ (24,457)</u> |

### ***Operating Activities***

Cash flow provided by operating activities totaled \$163.1 million for the three months ended March 31, 2020, as compared to \$138.7 million for the three months ended March 31, 2019. The increase in cash flow provided by operating activities of \$24.4 million was primarily due to an increase in premiums collected during 2020.

### ***Investing Activities***

Cash flow used in investing activities totaled \$381.4 million and \$155.0 million for the three months ended March 31, 2020 and 2019, respectively. In both periods, cash flow used in investing activities related to investing cash flows from operations. Additionally, in 2020 cash flow used in investing activities included investing \$200 million of increased borrowings under the Credit Facility.

### ***Financing Activities***

Cash flow provided by financing activities totaled \$178.0 million for the three months ended March 31, 2020, primarily related to \$200 million of increased borrowings under the Credit Facility, partially offset by the quarterly cash dividend paid in March and treasury stock acquired from employees to satisfy tax withholding obligations. Cash flow used in financing activities totaled \$8.1 million for the three months ended March 31, 2019 primarily related to treasury stock acquired from employees to satisfy tax withholding obligations.

### ***Insurance Company Capital***

We compute a risk-to-capital ratio for our U.S. insurance companies on a separate company statutory basis, as well as for our combined insurance operations. The risk-to-capital ratio is our net risk in force divided by our statutory capital. Our net risk in force represents risk in force net of reinsurance ceded, if any, and net of exposures on policies for which loss reserves have been established. Statutory capital consists primarily of statutory policyholders' surplus (which increases as a result of statutory net income and decreases as a result of statutory net loss and dividends paid), plus the statutory contingency reserve. The statutory contingency reserve is reported as a liability on the statutory balance sheet. A mortgage insurance company is required to make annual contributions to the contingency reserve of 50% of net premiums earned. These contributions must generally be maintained for a period of ten years. However, with regulatory approval, a mortgage insurance company may make early withdrawals from the contingency reserve when incurred losses exceed 35% of net premiums earned in a calendar year.

During the three months ended March 31, 2020 and 2019, no capital contributions were made to our U.S. insurance subsidiaries.

Essent Guaranty has entered into reinsurance agreements that provide excess of loss reinsurance coverage for new defaults on portfolios of mortgage insurance policies issued in 2015 through 2019. The aggregate excess of loss reinsurance coverages decrease over a ten-year period as the underlying covered mortgages amortize. Effective September 1, 2019, Essent Guaranty entered into a quota share reinsurance agreement with a panel of third-party reinsurers (the "QSR Agreement"). Under the QSR Agreement, Essent Guaranty will cede premiums earned related to 40% of risk on eligible single premium policies and 20% of risk on all other eligible policies written September 1, 2019 through December 31, 2020, in exchange for reimbursement of ceded claims and claims expenses on covered policies, a 20% ceding commission, and a profit commission of up to 60% that varies directly and inversely with ceded claims. These reinsurance coverages also reduces net risk in force and PMIERS Minimum Required Assets. See Note 4 to our condensed consolidated financial statements.

Our combined risk-to-capital calculation for our U.S. insurance subsidiaries as of March 31, 2020 was as follows:

|                                                                |    |            |
|----------------------------------------------------------------|----|------------|
| <b>Combined statutory capital:</b><br><b>(\$ in thousands)</b> |    |            |
| Policyholders' surplus                                         | \$ | 1,128,012  |
| Contingency reserves                                           |    | 1,324,718  |
| Combined statutory capital                                     | \$ | 2,452,730  |
| Combined net risk in force                                     | \$ | 28,729,105 |
| Combined risk-to-capital ratio                                 |    | 11.7:1     |

For additional information regarding regulatory capital, see Note 14 to our condensed consolidated financial statements. Our combined statutory capital equals the sum of statutory capital of Essent Guaranty plus Essent PA, after eliminating the impact of intercompany transactions. The combined risk-to-capital ratio equals the sum of the net risk in force of Essent Guaranty and Essent PA divided by combined statutory capital. The information above has been derived from the annual and quarterly statements of our insurance subsidiaries, which have been prepared in conformity with accounting practices prescribed or permitted by the Pennsylvania Insurance Department and the National Association of Insurance Commissioners Accounting Practices and Procedures Manual. Such practices vary from accounting principles generally accepted in the United States.

Essent Re has entered into GSE and other risk share transactions, including insurance and reinsurance transactions with Freddie Mac and Fannie Mae. Essent Re also reinsures 25% of Essent Guaranty's NIW under a quota share reinsurance agreement. During the three months ended March 31, 2020 and 2019, Essent Re paid no dividends to Essent Group and Essent Group made no capital contributions to Essent Re. As of March 31, 2020, Essent Re had total stockholders' equity of \$1.0 billion and net risk in force of \$10.6 billion.

### ***Financial Strength Ratings***

The insurer financial strength rating of Essent Guaranty, our principal mortgage insurance subsidiary, is rated A3 with a stable outlook by Moody's Investors Service ("Moody's"), BBB+ with a negative outlook by S&P and A (Excellent) with

stable outlook by A.M. Best. The insurer financial strength rating of Essent Re is BBB+ with a negative outlook by S&P and A (Excellent) with stable outlook by A.M. Best.

### ***Private Mortgage Insurer Eligibility Requirements***

Effective December 31, 2015, Fannie Mae and Freddie Mac, at the direction of the FHFA, implemented new coordinated Private Mortgage Insurer Eligibility Requirements, which we refer to as the "PMIERs." The PMIERs represent the standards by which private mortgage insurers are eligible to provide mortgage insurance on loans owned or guaranteed by Fannie Mae and Freddie Mac. The PMIERs include financial strength requirements incorporating a risk-based framework that require approved insurers to have a sufficient level of liquid assets from which to pay claims. This risk-based framework provides that an insurer must hold a substantially higher level of required assets for insured loans that are in default compared to a performing loan. The PMIERs also include enhanced operational performance expectations and define remedial actions that apply should an approved insurer fail to comply with these requirements. In 2018, the GSEs released revised PMIERs framework ("PMIERs 2.0") which became effective on March 31, 2019. As of March 31, 2020, Essent Guaranty, our GSE-approved mortgage insurance company, was in compliance with PMIERs 2.0. As of March 31, 2020, Essent Guaranty's Available Assets were \$2.45 billion and its Minimum Required Assets were \$1.23 billion based on our interpretation of PMIERs 2.0.

Due to business restrictions, stay-at-home orders and travel restrictions implemented as a result of COVID-19, we expect to experience increased defaults beginning in the second quarter of 2020, although it is too early to tell how many of our insured mortgages will default as a result of COVID-19. An increase in defaults increases our Minimum Required Assets under PMIERs, and, accordingly, we expect our Minimum Required Assets to increase in future periods.

Consistent with the PMIERs, Essent will apply a 0.30 multiplier to the risk-based required asset amount factor for each insured loan in default backed by a property located in a Federal Emergency Management Agency ("FEMA") Declared Major Disaster Area that either 1) is subject to a forbearance plan executed in response to a FEMA Declared Major Disaster Area eligible for Individual Assistance, the terms of which are materially consistent with terms of forbearance plans offered by Fannie Mae or Freddie Mac, or 2) has an initial default date occurring up to either (i) 30 days prior to or (ii) 90 days following the COVID 19 pandemic event. In the case of the foregoing, the 0.30 multiplier shall be applied to the risk-based required asset amount factor for each insured loan in default for no longer than 120 days from the initial default date absent a forbearance plan described in 1) above.

Approximately 97% of Essent's outstanding primary mortgage insurance portfolio, as of March 31, 2020, has underlying properties located in FEMA Declared Major Disaster Areas eligible for Individual Assistance. Accordingly, we believe that the majority of the non-performing loans that will be reported to the Company subsequent to March 31, 2020, will fall into categories 1) and 2) above and receive the 0.30 multiplier in calculating the PMIERs required assets.

## **Financial Condition**

### ***Stockholders' Equity***

As of March 31, 2020, stockholders' equity was \$3.1 billion, compared to \$3.0 billion as of December 31, 2019. This increase was primarily due to net income generated in 2020, partially offset by a decrease in accumulated other comprehensive income related to a decrease in our unrealized investment gains.

### ***Investments***

As of March 31, 2020, investments totaled \$3.8 billion compared to \$3.4 billion as of December 31, 2019. In addition, our total cash was \$31.1 million as of March 31, 2020, compared to \$71.4 million as of December 31, 2019. The increase in investments was primarily due to investing net cash flows from operations and a \$200 million credit facility borrowing during the three months ended March 31, 2020.

## Investments Available for Sale by Asset Class

| Asset Class<br>(\$ in thousands)               | March 31, 2020      |               | December 31, 2019   |               |
|------------------------------------------------|---------------------|---------------|---------------------|---------------|
|                                                | Fair Value          | Percent       | Fair Value          | Percent       |
| U.S. Treasury securities                       | \$ 235,565          | 6.4%          | \$ 242,206          | 7.2%          |
| U.S. agency securities                         | 33,892              | 0.9           | 33,605              | 1.0           |
| U.S. agency mortgage-backed securities         | 876,298             | 23.7          | 848,334             | 25.3          |
| Municipal debt securities(1)                   | 419,688             | 11.3          | 361,638             | 10.8          |
| Non-U.S. government securities                 | 52,209              | 1.4           | 54,995              | 1.7           |
| Corporate debt securities(2)                   | 879,503             | 23.7          | 880,301             | 26.3          |
| Residential and commercial mortgage securities | 275,532             | 7.4           | 288,281             | 8.6           |
| Asset-backed securities                        | 337,675             | 9.1           | 326,025             | 9.7           |
| Money market funds                             | 595,165             | 16.1          | 315,362             | 9.4           |
| <b>Total Investments Available for Sale</b>    | <b>\$ 3,705,527</b> | <b>100.0%</b> | <b>\$ 3,350,747</b> | <b>100.0%</b> |

| (1) The following table summarizes municipal debt securities as of : | March 31,<br>2020 | December 31,<br>2019 |
|----------------------------------------------------------------------|-------------------|----------------------|
| Special revenue bonds                                                | 73.7%             | 74.5%                |
| General obligation bonds                                             | 22.6              | 21.3                 |
| Certificate of participation bonds                                   | 3.0               | 3.4                  |
| Tax allocation bonds                                                 | 0.7               | 0.8                  |
| Total                                                                | 100.0%            | 100.0%               |

| (2) The following table summarizes corporate debt securities as of : | March 31,<br>2020 | December 31,<br>2019 |
|----------------------------------------------------------------------|-------------------|----------------------|
| Financial                                                            | 34.1%             | 34.4%                |
| Consumer, non-cyclical                                               | 20.3              | 20.1                 |
| Communications                                                       | 11.3              | 10.3                 |
| Consumer, cyclical                                                   | 7.9               | 7.6                  |
| Energy                                                               | 7.3               | 8.3                  |
| Utilities                                                            | 6.7               | 6.2                  |
| Technology                                                           | 5.0               | 4.8                  |
| Basic materials                                                      | 3.8               | 4.1                  |
| Industrial                                                           | 3.6               | 4.2                  |
| Total                                                                | 100.0%            | 100.0%               |

### Investments Available for Sale by Rating

| Rating(1)                                   | March 31, 2020      |               | December 31, 2019   |               |
|---------------------------------------------|---------------------|---------------|---------------------|---------------|
| (\$ in thousands)                           | Fair Value          | Percent       | Fair Value          | Percent       |
| Aaa                                         | \$ 2,177,097        | 58.7%         | \$ 1,817,905        | 54.2%         |
| Aa1                                         | 109,937             | 3.0           | 109,122             | 3.3           |
| Aa2                                         | 152,322             | 4.1           | 145,282             | 4.3           |
| Aa3                                         | 200,368             | 5.4           | 159,599             | 4.8           |
| A1                                          | 199,762             | 5.4           | 206,643             | 6.2           |
| A2                                          | 199,109             | 5.4           | 183,780             | 5.5           |
| A3                                          | 188,393             | 5.1           | 191,933             | 5.7           |
| Baa1                                        | 227,067             | 6.1           | 232,490             | 6.9           |
| Baa2                                        | 173,772             | 4.7           | 179,664             | 5.4           |
| Baa3                                        | 43,374              | 1.2           | 65,119              | 1.9           |
| Below Baa3                                  | 34,326              | 0.9           | 59,210              | 1.8           |
| <b>Total Investments Available for Sale</b> | <b>\$ 3,705,527</b> | <b>100.0%</b> | <b>\$ 3,350,747</b> | <b>100.0%</b> |

(1) Based on ratings issued by Moody's, if available. S&P or Fitch Ratings ("Fitch") rating utilized if Moody's not available.

### Investments Available for Sale by Effective Duration

| Effective Duration                          | March 31, 2020      |               | December 31, 2019   |               |
|---------------------------------------------|---------------------|---------------|---------------------|---------------|
| (\$ in thousands)                           | Fair Value          | Percent       | Fair Value          | Percent       |
| < 1 Year                                    | \$ 1,372,660        | 37.0%         | \$ 1,038,782        | 31.0%         |
| 1 to < 2 Years                              | 508,923             | 13.7          | 306,148             | 9.1           |
| 2 to < 3 Years                              | 402,111             | 10.9          | 348,708             | 10.4          |
| 3 to < 4 Years                              | 330,719             | 8.9           | 361,147             | 10.8          |
| 4 to < 5 Years                              | 298,753             | 8.1           | 443,382             | 13.2          |
| 5 or more Years                             | 792,361             | 21.4          | 852,580             | 25.5          |
| <b>Total Investments Available for Sale</b> | <b>\$ 3,705,527</b> | <b>100.0%</b> | <b>\$ 3,350,747</b> | <b>100.0%</b> |

### Top Ten Investments Available for Sale Holdings

| Rank<br>(\$ in thousands)                 | March 31, 2020                  |                   |                   |                 |                  |
|-------------------------------------------|---------------------------------|-------------------|-------------------|-----------------|------------------|
|                                           | Security                        | Fair Value        | Amortized Cost    | Unrealized Gain | Credit Rating(1) |
| 1                                         | Fannie Mae 3.500% 1/1/2058      | \$ 29,953         | \$ 28,590         | \$ 1,363        | Aaa              |
| 2                                         | Freddie Mac 4.000% 11/1/2048    | 27,834            | 27,283            | 551             | Aaa              |
| 3                                         | U.S. Treasury 2.625% 6/30/2023  | 21,207            | 19,666            | 1,541           | Aaa              |
| 4                                         | U.S. Treasury 5.250% 11/15/2028 | 20,966            | 18,844            | 2,122           | Aaa              |
| 5                                         | Ginnie Mae 4.000% 4/20/2049     | 19,226            | 18,828            | 398             | Aaa              |
| 6                                         | U.S. Treasury 1.500% 8/15/2026  | 18,523            | 17,447            | 1,076           | Aaa              |
| 7                                         | Fannie Mae 4.500% 5/1/2048      | 16,379            | 15,399            | 980             | Aaa              |
| 8                                         | Freddie Mac 4.500% 4/1/2049     | 15,968            | 15,433            | 535             | Aaa              |
| 9                                         | U.S. Treasury 2.625% 7/15/2021  | 15,197            | 14,740            | 457             | Aaa              |
| 10                                        | Freddie Mac 4.000% 5/15/2050    | 14,406            | 13,711            | 695             | Aaa              |
| Total                                     |                                 | <u>\$ 199,659</u> | <u>\$ 189,941</u> | <u>\$ 9,718</u> |                  |
| Percent of Investments Available for Sale |                                 | <u>5.4%</u>       |                   |                 |                  |

(1) Based on ratings issued by Moody's, if available. S&P or Fitch rating utilized if Moody's not available.

| Rank<br>(\$ in thousands)                 | December 31, 2019               |                   |
|-------------------------------------------|---------------------------------|-------------------|
|                                           | Security                        | Fair Value        |
| 1                                         | Fannie Mae 3.500% 1/1/2058      | \$ 30,112         |
| 2                                         | U.S. Treasury 5.250% 11/15/2028 | 29,480            |
| 3                                         | Freddie Mac 4.000% 11/1/2048    | 28,530            |
| 4                                         | U.S. Treasury 2.625% 6/30/2023  | 20,465            |
| 5                                         | U.S. Treasury 1.500% 8/15/2026  | 17,161            |
| 6                                         | Fannie Mae 4.500% 5/1/2048      | 16,972            |
| 7                                         | Freddie Mac 4.500% 4/1/2049     | 16,585            |
| 8                                         | U.S. Treasury 2.625% 7/15/2021  | 14,978            |
| 9                                         | Freddie Mac 4.000% 5/15/2050    | 14,700            |
| 10                                        | Fannie Mae 4.000% 5/1/2056      | 13,079            |
| Total                                     |                                 | <u>\$ 202,062</u> |
| Percent of Investments Available for Sale |                                 | <u>6.0%</u>       |

The following tables include municipal debt securities for states that represent more than 10% of the total municipal bond position as of March 31, 2020:

| (\$ in thousands)                                                       | Fair Value       | Amortized Cost   | Credit Rating (1), (2) |
|-------------------------------------------------------------------------|------------------|------------------|------------------------|
| <b>Texas</b>                                                            |                  |                  |                        |
| University of Houston                                                   | \$ 6,440         | \$ 6,364         | Aa2                    |
| Texas A&M University                                                    | 6,255            | 5,940            | Aaa                    |
| State of Texas                                                          | 5,755            | 5,525            | Aaa                    |
| City of Houston TX Combined Utility System Revenue                      | 5,125            | 4,659            | Aa2                    |
| City of Austin TX Electric Utility Revenue                              | 2,358            | 2,150            | Aa3                    |
| Dallas/Fort Worth International Airport                                 | 2,335            | 2,181            | A1                     |
| City of Houston TX                                                      | 2,254            | 2,118            | Aa3                    |
| North Texas Municipal Water District                                    | 2,049            | 1,962            | Aaa                    |
| North Texas Tollway System                                              | 1,894            | 1,763            | A2                     |
| City of Dallas TX                                                       | 1,843            | 1,679            | Aa3                    |
| City of Fort Worth TX Water & Sewer System Revenue                      | 1,532            | 1,480            | Aa1                    |
| Tarrant Regional Water District                                         | 1,527            | 1,454            | Aaa                    |
| City of San Antonio TX Airport System                                   | 1,313            | 1,194            | A1                     |
| City of Corpus Christi TX Utility System Revenue                        | 1,164            | 1,079            | A1                     |
| Harris County Toll Road Authority                                       | 1,066            | 1,035            | Aa2                    |
| Central Texas Turnpike System                                           | 1,032            | 1,014            | Baa1                   |
| Metropolitan Transit Authority of Harris County Sales & Use Tax Revenue | 919              | 912              | Aaa                    |
| County of Fort Bend TX                                                  | 854              | 803              | Aa1                    |
| Austin-Bergstrom Landhost Enterprises, Inc.                             | 631              | 591              | A3                     |
| San Jacinto Community College District                                  | 584              | 547              | Aa3                    |
| Austin Independent School District                                      | 277              | 302              | Aaa                    |
|                                                                         | <u>\$ 47,207</u> | <u>\$ 44,752</u> |                        |

| (\$ in thousands)                                                       | Fair Value       | Amortized Cost   | Credit Rating (1), (2) |
|-------------------------------------------------------------------------|------------------|------------------|------------------------|
| <b>New York</b>                                                         |                  |                  |                        |
| Metropolitan Transportation Authority                                   | \$ 7,605         | \$ 7,303         | A1                     |
| State of New York Personal Income Tax Revenue                           | 7,193            | 6,945            | Aa1                    |
| City of New York NY                                                     | 7,109            | 6,521            | Aa1                    |
| The Port Authority of New York and New Jersey                           | 5,984            | 5,586            | Aa3                    |
| New York City Transitional Finance Authority Future Tax Secured Revenue | 5,021            | 4,688            | Aa1                    |
| City of Yonkers NY                                                      | 2,344            | 2,305            | A2                     |
| TSASC, Inc.                                                             | 2,236            | 2,195            | A2                     |
| County of Nassau NY                                                     | 2,206            | 2,011            | A2                     |
| Long Island Power Authority                                             | 1,893            | 1,766            | A2                     |
| New York City Transitional Finance Authority Building Aid Revenue       | 1,565            | 1,485            | Aa2                    |
| Town of Oyster Bay NY                                                   | 1,092            | 1,047            | Aa2                    |
|                                                                         | <u>\$ 44,248</u> | <u>\$ 41,852</u> |                        |

(1) Certain of the above securities may include financial guaranty insurance or state enhancements. The above ratings include the effect of these credit enhancements, if applicable.

(2) Based on ratings issued by Moody's, if available. S&P or Fitch rating utilized if Moody's not available.

## **Off-Balance Sheet Arrangements**

Essent Guaranty has entered into fully collateralized reinsurance agreements ("Radnor Re Transactions") with unaffiliated special purpose insurers domiciled in Bermuda. The Radnor Re special purpose insurers are special purpose variable interest entities that are not consolidated in our condensed consolidated financial statements because we do not have the unilateral power to direct those activities that are significant to their economic performance. As of March 31, 2020, our estimated off-balance sheet maximum exposure to loss from the Radnor Re entities was \$10.8 million, representing the estimated net present value of investment earnings on the assets in the reinsurance trusts. See Note 4 to our condensed consolidated financial statements for additional information.

## **Critical Accounting Policies**

As of the filing date of this report, there were no significant changes in our critical accounting policies from those discussed in our 2019 Form 10-K. See Note 2 to our condensed consolidated financial statements for recently issued accounting standards adopted or under evaluation.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

We own and manage a large investment portfolio of various holdings, types and maturities. Investment income is one of our primary sources of cash flow supporting operations and claim payments. The assets within the investment portfolio are exposed to the same factors that affect overall financial market performance. While our investment portfolio is exposed to factors affecting markets worldwide, it is most sensitive to fluctuations in the drivers of U.S. markets.

We manage market risk via defined investment policy implemented by our treasury function with oversight from our board of directors and our senior management. Important drivers of our market risk exposure monitored and managed by us include but are not limited to:

- *Changes to the level of interest rates.* Increasing interest rates may reduce the value of certain fixed-rate bonds held in the investment portfolio. Higher rates may cause variable-rate assets to generate additional income. Decreasing rates will have the reverse impact. Significant changes in interest rates can also affect persistency and claim rates which may in turn require that the investment portfolio be restructured to better align it with future liabilities and claim payments. Such restructuring may cause investments to be liquidated when market conditions are adverse.
- *Changes to the term structure of interest rates.* Rising or falling rates typically change by different amounts along the yield curve. These changes may have unforeseen impacts on the value of certain assets.
- *Market volatility/changes in the real or perceived credit quality of investments.* Deterioration in the quality of investments, identified through changes to our own or third-party (e.g., rating agency) assessments, will reduce the value and potentially the liquidity of investments.
- *Concentration Risk.* If the investment portfolio is highly concentrated in one asset, or in multiple assets whose values are highly correlated, the value of the total portfolio may be greatly affected by the change in value of just one asset or a group of highly correlated assets.
- *Prepayment Risk.* Bonds may have call provisions that permit debtors to repay prior to maturity when it is to their advantage. This typically occurs when rates fall below the interest rate of the debt.

Market risk is measured for all investment assets at the individual security level. Market risks that are not fully captured by the quantitative analysis are highlighted. In addition, material market risk changes that occur from the last reporting period to the current are discussed. Changes to how risks are managed will also be identified and described.

At March 31, 2020, the effective duration of our investments available for sale was 2.6 years, which means that an instantaneous parallel shift (movement up or down) in the yield curve of 100 basis points would result in a change of 2.6% in fair value of our investments available for sale. Excluding short-term investments, our investments available for sale effective duration was 3.1 years, which means that an instantaneous parallel shift (movement up or down) in the yield curve of 100 basis points would result in a change of 3.1% in fair value of our investments available for sale.

### Item 4. Controls and Procedures

#### Disclosure Controls and Procedures

Our management carried out an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer, of the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report. Based on this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective as of March 31, 2020, the end of the period covered by this Quarterly Report.

#### Changes in Internal Control Over Financial Reporting

During our most recent fiscal quarter, there has not been any change in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II — OTHER INFORMATION

### Item 1. Legal Proceedings

We are not currently subject to any material legal proceedings.

### Item 1A. Risk Factors

Risk factors that affect our business and financial results are discussed in Part I, Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2019. There have been no material changes in our risk factors from those previously disclosed in our Annual Report. You should carefully consider the risks described in our Annual Report, which could materially affect our business, financial condition or future results. The risks described in our Annual Report are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition, and/or operating results. If any of the risks actually occur, our business, financial condition, and/or results of operations could be negatively affected.

#### Risks relating to the impact of COVID-19

An outbreak of COVID-19 is currently spreading throughout the world, including in Asia, Europe and the United States. This outbreak is unprecedented in modern history and continues to rapidly evolve and disrupt the global economy and financial markets, including the U.S. housing and mortgage markets. On March 11, 2020, the World Health Organization declared the outbreak to be a pandemic, and on March 13, 2020, U.S. President Donald Trump declared the outbreak to be a national emergency. The rapid spread has resulted in authorities around the world implementing numerous measures to contain the virus, such as travel bans and restrictions, quarantines, shelter-in-place orders and business shutdowns. The pandemic and these containment measures have had, and are expected to continue to have, a substantial negative impact on businesses around the world and on global, regional and national economies.

The emergence of the COVID-19 pandemic and the resulting containment measures have caused economic and financial disruptions that have adversely affected, and are expected to continue to materially adversely affect, our business, results of operations, financial condition and liquidity. The extent to which the pandemic will continue to materially adversely affect our business, results of operations, financial condition and liquidity will depend on numerous evolving factors and future developments that we are not able to predict, including the duration, spread and severity of the outbreak; the nature, extent and effectiveness of containment measures; the extent and duration of the effect on the economy, unemployment, consumer confidence and consumer and business spending; and how quickly and to what extent normal economic and operating conditions can resume.

Since the outbreak of the pandemic, there have been a number of governmental and GSE efforts to implement programs designed to assist individuals and businesses impacted by the virus. On March 27, 2020, the Coronavirus Aid, Relief and Economic Security Act, referred to as the CARES Act, was signed into law. The CARES Act provides financial assistance for businesses and individuals and targeted regulatory relief for financial institutions, was signed into law. Among many other things, the CARES Act suspends foreclosures and evictions for at least 60 days from March 18, 2020, on mortgages purchased or securitized by the GSEs. In addition, the CARES Act enacts into law a requirement to provide payment forbearance on such mortgages to borrowers experiencing a hardship during the COVID-19 emergency. Forbearance under the CARES Act allows for a mortgage payment to be suspended for up to 360 days due to hardship caused by COVID-19. The CARES Act also provides for enhanced unemployment benefits and direct aid to individuals, among other things.

Fannie Mae and Freddie Mac, the primary purchasers of mortgages we insure, have adopted relief measures consistent with the CARES Act to assist borrowers impacted by COVID-19. Under forbearance plans announced by the GSEs and implemented by their servicers, eligible homeowners who are adversely impacted by COVID-19 are permitted to temporarily reduce or suspend their mortgage payments for up to 12 months. The GSEs have announced that, at the end of the forbearance plan, the homeowner may not be required to pay back their reduced or suspended mortgage payments in one lump sum, but may be eligible for a number of different options offered by their mortgage servicer, including repayment plans, resuming normal payments or lowering the monthly loan payment through a modification. However, there can be no assurances that homeowners will be able to remain current on their mortgages once the forbearance period ends, and a significant percentage could ultimately default and result in a mortgage insurance claim despite the GSE and other programs.

The COVID-19 pandemic and containment measures have contributed to, among other things:

- The risk that policy losses and loss adjustment expenses we ultimately incur as a result of COVID-19 and the related economic impact may be substantially different than the loss reserves established on our financial statements at the end of each period. In accordance with industry practice and statutory accounting rules applicable to mortgage guaranty insurance companies, we establish loss reserves only for loans reported to us in default, including forbearance-related defaults. These reserves are established using estimated claim rates and claim amounts in estimating the ultimate loss, which estimates are subject to significant uncertainty given the unprecedented nature and magnitude of the COVID-19 pandemic. In addition, because our reserving method does not account for the impact of future losses that could occur from loans that are not yet delinquent, our obligation for ultimate losses that we expect to occur under our policies in force at any period end is not reflected in our financial statements, except in the case where a premium deficiency exists. As of March 31, 2020, we have been notified by mortgage servicers of only a limited number of mortgage defaults, however, we expect the number of COVID-19-related defaults reported to us, and consequently our reserves for losses and loss adjustment expenses as a result of COVID-19, to increase significantly over time.
- A deterioration in the ability and willingness of homeowners to continue to make mortgage payments on loans that we insure, which could result in an increase in the amount of insurance regulatory and PMIERS capital we are required to hold for delinquent loans, including forbearance-related delinquencies, as well as an increase in claims ultimately made with respect to such mortgage loans. Mortgage delinquencies are typically affected by a variety of borrower-specific factors, such as job loss, illness, death and divorce, and macroeconomic factors, such as rising unemployment, market deterioration and home price depreciation, many of which are likely exacerbated by the COVID-19 pandemic.
- A potential reduction in the number of new mortgage loans available for us to insure, and consequently, on our future volumes of new insurance written, with the degree of the impact dependent in large part on the extent and duration of the economic contraction.
- Adverse impacts on capital, credit and reinsurance market conditions, which may limit our ability to issue ILNs, purchase reinsurance or access traditional financing methods. Such adverse impacts may increase our cost of capital and affect our ability to meet liquidity needs.
- An increased strain on our risk management policies generally, including, but not limited to, the effectiveness and accuracy of our models, given the lack of data inputs and comparable precedent.
- An increased risk to the value of our investments and other assets, which has the potential to result in impairment charges.
- Adverse impacts on our daily business operations and our employees' ability to perform necessary business functions, including as a result of illness or as a result of restrictions on movement.
- Adverse impacts on our costs structure, including the need for increased staffing in certain segments of our business, increased spending on our business continuity efforts, such as technology, and readiness efforts for returning to our offices, which may in turn limit our ability to make investments in other areas.
- An increased risk of an information or cyber-security incident, fraud, a failure to maintain the uninterrupted operation of our information systems or a failure in the effectiveness of our anti-money laundering and other compliance programs due to, among other things, an increase in remote work.

The above impacts of the COVID-19 pandemic and containment measures are likely to continue and in some cases, may worsen. The pandemic and containment measures may cause us to modify our strategic plans and business practices, and we may take further actions that we determine are in the best interests of our employees, customers and business partners. As a result of the above risks, COVID-19 could materially and adversely impact our business, results of operations, financial position and liquidity.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds****Repurchases of Securities**

The table below sets forth information regarding repurchases of our common shares during the three months ended March 31, 2020. All of the shares represent common shares that were tendered to the Company by employees in connection with the vesting of restricted shares to satisfy tax withholding obligations. We do not consider these transactions to be a share buyback program.

| Period                         | Total<br>Number of<br>Shares<br>Purchased | Average Price<br>Paid Per Share | Total Number of<br>Shares Purchased<br>as Part of Publicly<br>Announced Plans<br>or Programs | Maximum Number<br>of Shares that<br>May Yet Be<br>Purchased Under<br>the Plans or<br>Programs |
|--------------------------------|-------------------------------------------|---------------------------------|----------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------|
| January 1 - January 31, 2020   | —                                         | N/A                             | —                                                                                            | —                                                                                             |
| February 1 - February 29, 2020 | —                                         | N/A                             | —                                                                                            | —                                                                                             |
| March 1 - March 31, 2020       | 86,404                                    | \$ 43.64                        | —                                                                                            | —                                                                                             |
| Total                          | 86,404                                    |                                 | —                                                                                            | —                                                                                             |

**Item 6. Exhibits**

(a) Exhibits:

| <b>Exhibit<br/>No.</b> | <b>Description</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
|------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <a href="#">31.1</a>   | Certification of Chief Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                                                                                     |
| <a href="#">31.2</a>   | Certification of Chief Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                                                                                     |
| <a href="#">32.1</a>   | Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                                                                                                                  |
| 101                    | The following financial information from this Quarterly Report on Form 10-Q for the quarter ended March 31, 2020, formatted in Inline XBRL: (i) the Condensed Consolidated Balance Sheets (Unaudited); (ii) the Condensed Consolidated Statements of Comprehensive Income (Unaudited); (iii) the Condensed Consolidated Statements of Changes in Stockholders' Equity (Unaudited); (iv) the Condensed Consolidated Statements of Cash Flows (Unaudited); and (v) the Notes to Condensed Consolidated Financial Statements (Unaudited). |

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, on the date indicated.

**ESSENT GROUP LTD.**

Date: May 8, 2020

/s/ MARK A. CASALE

Mark A. Casale

President, Chief Executive Officer and Chairman  
(Principal Executive Officer)

Date: May 8, 2020

/s/ LAWRENCE E. MCALEE

Lawrence E. McAlee

Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

Date: May 8, 2020

/s/ DAVID B. WEINSTOCK

David B. Weinstock

Vice President and Chief Accounting Officer  
(Principal Accounting Officer)

## CERTIFICATION

I, Mark A. Casale, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Essent Group Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 8, 2020

/s/ MARK A. CASALE

Mark A. Casale

President, Chief Executive Officer and Chairman

(Principal Executive Officer)

## CERTIFICATION

I, Lawrence E. McAlee, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Essent Group Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 8, 2020

/s/ LAWRENCE E. MCALEE

Lawrence E. McAlee

Senior Vice President and Chief Financial Officer

(Principal Financial Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS  
ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

The undersigned, Mark A. Casale, President, Chief Executive Officer and Chairman of Essent Group Ltd. (the “Company”), and Lawrence E. McAlee, Senior Vice President and Chief Financial Officer of the Company, each hereby certify, pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of his knowledge:

- (1) the Quarterly Report on Form 10-Q of the Company for the quarter ended March 31, 2020 (the “Report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 8, 2020

/s/ MARK A. CASALE

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Mark A. Casale

President, Chief Executive Officer and Chairman

/s/ LAWRENCE E. MCALEE

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Lawrence E. McAlee

Senior Vice President and Chief Financial Officer