

MGIC INVESTMENT CORP
Form 10-Q
May 08, 2018

FORM 10-Q
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

QUARTERLY REPORT PURSUANT TO
 SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018

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 1-10816

MGIC Investment Corporation

(Exact name of registrant as specified in its charter)

WISCONSIN

(State or other jurisdiction of incorporation or organization)

39-1486475

(I.R.S. Employer Identification No.)

250 E. KILBOURN AVENUE

MILWAUKEE, WISCONSIN

(Address of principal executive offices)

(414) 347-6480

(Registrant's telephone number, including area code)

53202

(Zip Code)

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting 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. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company (Do not check if a smaller reporting company)

Emerging growth company 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).

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YES NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| CLASS OF STOCK | PAR VALUE | DATE | NUMBER OF SHARES |
|----------------|-----------|----------------|------------------|
| Common stock | \$1.00 | April 30, 2018 | 371,347,632 |

Forward Looking and Other Statements

All statements in this report that address events, developments or results that we expect or anticipate may occur in the future are “forward looking statements.” Forward looking statements consist of statements that relate to matters other than historical fact. In most cases, forward looking statements may be identified by words such as “believe,” “anticipate” or “expect,” or words of similar import. The risk factors referred to in “Forward Looking Statements and Risk Factors – Location of Risk Factors” in Management’s Discussion and Analysis of Financial Condition and Results of Operations below, may cause our actual results to differ materially from the results contemplated by forward looking statements that we may make. We are not undertaking any obligation to update any forward looking statements or other statements we may make 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. Therefore no reader of this document should rely on these statements being current as of any time other than the time at which this document was filed with the Securities and Exchange Commission.

Table of contents

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES

FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2018

Table of contents

Page

PART I — FINANCIAL INFORMATION

Item 1 Financial Statements:

| | |
|---|-----------|
| <u>Consolidated Balance Sheets - March 31, 2018 (Unaudited) and December 31, 2017</u> | <u>7</u> |
| <u>Consolidated Statements of Operations (Unaudited) - Three Months Ended March 31, 2018 and 2017</u> | <u>8</u> |
| <u>Consolidated Statements of Comprehensive Income (Unaudited) - Three Months Ended March 31, 2018 and 2017</u> | <u>9</u> |
| <u>Consolidated Statements of Shareholders' Equity (Unaudited) - Three Months Ended March 31, 2018 and 2017</u> | <u>10</u> |
| <u>Consolidated Statements of Cash Flows (Unaudited) - Three Months Ended March 31, 2018 and 2017</u> | <u>11</u> |
| <u>Notes to Consolidated Financial Statements (Unaudited)</u> | <u>12</u> |
| <u>Note 1 - Nature of Business and Basis of Presentation</u> | <u>12</u> |
| <u>Note 2 - New Accounting Pronouncements</u> | <u>12</u> |
| <u>Note 3 - Debt</u> | <u>15</u> |
| <u>Note 4 - Reinsurance</u> | <u>15</u> |
| <u>Note 5 - Litigation and Contingencies</u> | <u>17</u> |
| <u>Note 6 - Earnings Per Share</u> | <u>18</u> |
| <u>Note 7 - Investments</u> | <u>19</u> |
| <u>Note 8 - Fair Value Measurements</u> | <u>22</u> |
| <u>Note 9 - Other Comprehensive Income</u> | <u>25</u> |
| <u>Note 10 - Benefit Plans</u> | <u>26</u> |
| <u>Note 11 - Income Taxes</u> | <u>26</u> |
| <u>Note 12 - Loss Reserves</u> | <u>27</u> |
| <u>Note 13 - Shareholders' Equity</u> | <u>31</u> |
| <u>Note 14 - Share-Based Compensation</u> | <u>32</u> |
| <u>Note 15 - Statutory Information</u> | <u>32</u> |

| | |
|---|-----------|
| <u>Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | <u>34</u> |
|---|-----------|

| | |
|--|-----------|
| <u>Item 3 Quantitative and Qualitative Disclosures about Market Risk</u> | <u>65</u> |
|--|-----------|

| | |
|---------------------------------------|-----------|
| <u>Item 4 Controls and Procedures</u> | <u>65</u> |
|---------------------------------------|-----------|

PART II — OTHER INFORMATION

| | |
|---------------------------------|-----------|
| <u>Item 1 Legal Proceedings</u> | <u>67</u> |
|---------------------------------|-----------|

| | |
|-----------------------------|-----------|
| <u>Item 1A Risk Factors</u> | <u>67</u> |
|-----------------------------|-----------|

| | |
|------------------------|-----------|
| <u>Item 6 Exhibits</u> | <u>76</u> |
|------------------------|-----------|

| | |
|--------------------------|-----------|
| <u>INDEX TO EXHIBITS</u> | <u>76</u> |
|--------------------------|-----------|

| | |
|-------------------|-----------|
| <u>SIGNATURES</u> | <u>77</u> |
|-------------------|-----------|

Table of contents

Glossary of terms and acronyms

/ A

ARMs

Adjustable rate mortgages

ABS

Asset-backed securities

ASC

Accounting Standards Codification

Available Assets

Assets, as designated under the PMIERS, that are readily available to pay claims, and include the most liquid investments

/ B

Book or book year

A group of loans insured in a particular calendar year

BPMI

Borrower-paid mortgage insurance

/ C

CECL

Current expected credit losses

CFPB

Consumer Financial Protection Bureau

CLO

Collateralized loan obligations

CMBS

Commercial mortgage-backed securities

/ D

DAC

Deferred insurance policy acquisition costs

Debt-to-income (“DTI”) ratio

The ratio, expressed as a percentage, of a borrowers’ total debt payments to gross income

Direct

When referring to insurance or risk written or in force, “direct” means before giving effect to reinsurance

/ F

Fannie Mae

Federal National Mortgage Association

FCRA
Fair Credit Reporting Act

FEMA
Federal Emergency Management Agency

FHA
Federal Housing Administration

FHFA
Federal Housing Finance Agency

FHLB
Federal Home Loan Bank of Chicago, of which MGIC is a member

FICO score
A measure of consumer credit risk provided by credit bureaus, typically produced from statistical models by Fair Isaac Corporation utilizing data collected by the credit bureaus

Freddie Mac
Federal Home Loan Mortgage Corporation

/ G
GAAP
Generally Accepted Accounting Principles in the United States

GSEs
Collectively, Fannie Mae and Freddie Mac

/ H
HAMP
Home Affordable Modification Program

HARP
Home Affordable Refinance Program

HOPA
Homeowners Protection Act

/ I
IADA
Individual Assistance Disaster Area

Table of contents

IBNR

Losses incurred but not reported

IIF

Insurance in force, which for loans insured by us, is equal to the unpaid principal balance, as reported to us

/ J

JCT

Joint Committee on Taxation

/ L

LAE

Loss adjustment expenses

Legacy book

Mortgage insurance policies written prior to 2009

Loan-to-value ("LTV") ratio

The ratio, expressed as a percentage, of the dollar amount of the first mortgage loan to the value of the property at the time the loan became insured and does not reflect subsequent housing price appreciation or depreciation. Subordinate mortgages may also be present.

Long-term debt:

5.75% Notes

5.75% Senior Notes due on August 15, 2023, with interest payable semi-annually on February 15 and August 15 of each year

9% Debentures

9% Convertible Junior Subordinated Debentures due on April 1, 2063, with interest payable semi-annually on April 1 and October 1 of each year

FHLB Advance or the Advance

1.91% Fixed rate advance from the FHLB due on February 10, 2023, with interest payable monthly

Loss ratio

The ratio, expressed as a percentage, of the sum of incurred losses and loss adjustment expenses to NPE

Low down payment loans or mortgages

Loans with less than 20% down payments

LPMI

Lender-paid mortgage insurance

/ M

MBS

Mortgage-backed securities

MD&A

Management's discussion and analysis of financial condition and results of operations

MGIC

Mortgage Guaranty Insurance Corporation, a subsidiary of MGIC Investment Corporation

MIC

MGIC Indemnity Corporation, a subsidiary of MGIC

Minimum Required Assets

The greater of \$400 million or the total of the minimum amount of Available Assets that must be held under the PMIERs based upon a percentage of RIF weighted by certain risk attributes

MPP

Minimum Policyholder Position, as required under certain state requirements. The "policyholder position" of a mortgage insurer is its net worth or surplus, contingency reserve and a portion of the reserves for unearned premiums

/ N

N/A

Not applicable for the period presented

NAIC

The National Association of Insurance Commissioners

NIW

New Insurance Written, is the aggregate original principal amount of the mortgages that are insured during a period

N/M

Data, or calculation, deemed not meaningful for the period presented

Table of contents

NPE

The amount of premiums earned, net of premiums assumed and ceded under reinsurance agreements

NPL

Non-performing loan, which is a delinquent loan, at any stage in its delinquency

NPW

The amount of premiums written, net of premiums assumed and ceded under reinsurance agreements

/ O

OCI

Office of the Commissioner of Insurance of the State of Wisconsin

/ P

Persistency

The percentage of our insurance remaining in force from one year prior

PMI

Private Mortgage Insurance (as an industry or product type)

PMIERS

Private Mortgage Insurer Eligibility Requirements issued by the GSEs

Premium Yield

The ratio of NPE divided by the average IIF outstanding for the period measured

/ Q

QSR Transaction

Quota share reinsurance transaction

/ R

REMIC

Real Estate Mortgage Investment Conduit

RESPA

Real Estate Settlement Procedures Act

RIF

Risk in force, which for an individual loan insured by us, is equal to the unpaid loan principal balance, as reported to us, multiplied by the insurance coverage percentage. RIF is sometimes referred to as exposure

Risk-to-capital

Under certain state regulations, the ratio of RIF, net of reinsurance and exposure on policies currently in default and for which loss reserves have been established, to the level of statutory capital

RMBS

Residential mortgage-backed securities

/ S

State Capital Requirements

Under certain state regulations, the minimum amount of statutory capital relative to risk in force (or similar measure)

/ T

Tax Act

The U.S. tax reform enacted on December 22, 2017 and commonly referred to as the “Tax Cuts and Jobs Act”

/ U

Underwriting expense ratio

The ratio, expressed as a percentage, of the underwriting and operating expenses, net and amortization of DAC of our combined insurance operations (which excludes underwriting and operating expenses of our non-insurance subsidiaries) to NPW

Underwriting profit

NPE minus incurred losses and underwriting expenses

USDA

U.S. Department of Agriculture

/ V

VA

U.S. Department of Veterans Affairs

Table of contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

MGIC INVESTMENT
CORPORATION AND
SUBSIDIARIES
CONSOLIDATED BALANCE
SHEETS

(In thousands) Note March 31, 2018 December 31, 2017

ASSETS (Unaudited)

Investment portfolio:

Fixed income, available

for sale, at fair value

(amortized cost, 2018

- \$4,930,063 \$4,983,315
- \$4,974,616; 2017

- \$4,946,278) Equity securities,

at fair value

(cost, 2018 / 8 4,099 7,246

- \$4,143; 2017

- \$7,223)

Other invested

assets / 8 3,100 —

at cost

Total investment portfolio 4,937,262 4,990,561

| | | |
|---|-------------|-------------|
| Cash and cash | 177,488 | 99,851 |
| equivalents | | |
| Accrued investment income | 45,123 | 46,060 |
| Reinsurance recoverable on loss reserves | 45,474 | 48,474 |
| Reinsurance recoverable on paid losses | 3,718 | 3,872 |
| Premiums receivable | 52,701 | 54,045 |
| Home office and equipment, net | 48,382 | 44,936 |
| Deferred insurance policy acquisition costs | 18,928 | 18,841 |
| Deferred income taxes, net | 211,994 | 234,381 |
| Other assets | 75,273 | 78,478 |
| Total assets | \$5,616,343 | \$5,619,499 |

LIABILITIES
AND
SHAREHOLDERS'
EQUITY

Liabilities:

| | | |
|---------------------------------|-----------|-----------|
| Loss reserves | \$924,171 | \$985,635 |
| Unearned premiums | 397,688 | 392,934 |
| Federal Home Loan Bank | 155,000 | 155,000 |

| | | |
|---------------|------------|-----------|
| advance | | |
| Senior | | |
| notes | 418,848 | 418,560 |
| Convertible | | |
| junior | | |
| subordinated | 256,872 | 256,872 |
| debentures | | |
| Other | | |
| liabilities | 232,361 | 255,972 |
| Total | | |
| liabilities | 2,384,940 | 2,464,973 |
| Contingencies | | |
| Shareholders' | | |
| equity: | | |
| Common | | |
| stock | | |
| (one | | |
| dollar | | |
| par | | |
| value, | | |
| shares | | |
| authorized | | |
| 1,000,000; | | |
| shares | | |
| issued | | |
| 2018 | | |
| - | 371,348 | 370,567 |
| 371,348; | | |
| 2017 | | |
| - | | |
| 370,567; | | |
| shares | | |
| outstanding | | |
| 2018 | | |
| - | | |
| 371,348; | | |
| 2017 | | |
| - | | |
| 370,567) | | |
| Paid-in | | |
| capital | 1,847,000 | 1,850,582 |
| Accumulated | | |
| other | | |
| comprehensive | | |
| loss, | (107,760) | (43,783) |
| net | | |
| of | | |
| tax | | |
| Retained | | |
| earnings | 1,120,815 | 977,160 |
| | 3,231,403 | 3,154,526 |

Total
shareholders'
equity

Total
liabilities

and \$5,616,343 \$5,619,499

shareholders'
equity

See accompanying notes to consolidated financial statements.

MGIC Investment Corporation - Q1 2018 | 7

Table of contents

MGIC INVESTMENT
CORPORATION AND
SUBSIDIARIES
CONSOLIDATED
STATEMENTS OF
OPERATIONS (Unaudited)

Three Months Ended
March 31,

(In
thousands,
except
Note 2018 2017
per
share
data)
Revenues:
Premiums
written:
Direct \$270,034 \$265,823
Assumed 0 1,288
Ceded (33,220) (30,409)
Net
premiums 236,906 236,702
written
Increase
in
unearned 64,799) (7,599)
premiums,
net
Net
premiums 232,107 229,103
earned
Investment
income,
net 32,121 29,477
of
expenses
Net
realized
investment 7 (329) (125)
losses
Other
revenue 1,871 2,425
Total 265,770 260,880
revenues

| | | |
|---|------------|-----------|
| Losses and expenses: | | |
| Losses incurred | 23,850 | 27,619 |
| net Amortization of deferred policy acquisition costs | 2,572 | 2,230 |
| Other underwriting and operating expenses, net | 46,090 | 40,765 |
| Interest expense | 13,233 | 16,309 |
| Total losses and expenses | 85,745 | 86,923 |
| Income before tax | 180,025 | 173,957 |
| Provision for income taxes | 36,388 | 84,159 |
| Net income | \$ 143,637 | \$ 89,798 |

| | | |
|---------------------|---------|---------|
| Earnings per share: | | |
| Basic | \$ 0.39 | \$ 0.26 |
| Diluted | \$ 0.38 | \$ 0.24 |

| | | |
|--|---------|---------|
| Weighted average common shares outstanding | 370,908 | 341,009 |
| - basic | | |
| Weighted average common shares | 401,562 | 402,175 |

outstanding

-

diluted

See accompanying notes to consolidated financial statements.

MGIC Investment Corporation - Q1 2018 | 8

Table of contents

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (Unaudited)

| (In thousands) | Note | Three Months Ended | |
|--|------|--------------------|------------|
| | | March 31, 2018 | 2017 |
| Net income | | \$ 143,637 | \$ 89,798 |
| Other comprehensive (loss) income, net of tax: | 9 | | |
| Change in unrealized investment gains and losses | 7 | (64,453) | 12,121 |
| Benefit plan adjustments | | 494 | (153) |
| Foreign currency translation adjustment | | — | 31 |
| Other comprehensive (loss) income, net of tax | | (63,959) | 11,999 |
| Comprehensive income | | \$ 79,678 | \$ 101,797 |

See accompanying notes to consolidated financial statements

MGIC Investment Corporation - Q1 2018 | 9

Table of contents

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (Unaudited)

| (In thousands) | Note | Three Months Ended March 31, | |
|--|----------|---------------------------------|--------------------|
| | | 2018 | 2017 |
| Common stock | | | |
| Balance, beginning of period | | \$370,567 | \$359,400 |
| Net common stock issued under share-based compensation plans | | 781 | 771 |
| Balance, end of period | | 371,348 | 360,171 |
| Paid-in capital | | | |
| Balance, beginning of period | | 1,850,582 | 1,782,337 |
| Net common stock issued under share-based compensation plans | | (8,854) | (7,493) |
| Equity compensation | | 5,272 | 3,461 |
| Balance, end of period | | 1,847,000 | 1,778,305 |
| Treasury stock | | | |
| Balance, beginning of period | | — | (150,359) |
| Balance, end of period | | — | (150,359) |
| Accumulated other comprehensive (loss) income | | | |
| Balance, beginning of period | <u>2</u> | (43,801) | (75,100) |
| Other comprehensive income, net of tax | <u>2</u> | (63,959) | 11,999 |
| Balance, end of period | | (107,760) | (63,101) |
| Retained earnings | | | |
| Balance, beginning of period | <u>2</u> | 977,178 | 632,717 |
| Net income | | 143,637 | 89,798 |
| Balance, end of period | | 1,120,815 | 722,515 |
| Total shareholders' equity | | \$3,231,403 | \$2,647,531 |

See accompanying notes to consolidated financial statements.

Table of contentsMGIC INVESTMENT CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

| (In thousands) | Three Months Ended | |
|---|--------------------|------------|
| | March 31, 2018 | 2017 |
| Cash flows from operating activities: | | |
| Net income | \$143,637 | \$89,798 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 15,833 | 17,079 |
| Deferred tax expense | 39,388 | 48,932 |
| Net realized investment losses | 329 | 125 |
| Change in certain assets and liabilities: | | |
| Accrued investment income | 937 | 287 |
| Reinsurance recoverable on loss reserves | 3,000 | 3,835 |
| Reinsurance recoverable on paid losses | 154 | (165) |
| Premium receivable | 1,344 | 485 |
| Deferred insurance policy acquisition costs | (87) | (477) |
| Profit commission receivable | 377 | (3,395) |
| Loss reserves | (61,464) | (103,771) |
| Unearned premiums | 4,754 | 7,585 |
| Return premium accrual | (5,500) | (4,800) |
| Income taxes payable - current | (3,117) | 34,654 |
| Other, net | (5,619) | (12,703) |
| Net cash provided by operating activities | 133,966 | 77,469 |
| Cash flows from investing activities: | | |
| Purchases of investments: | | |
| Fixed income securities | (209,477) | (187,077) |
| Equity securities | (20) | (19) |
| Proceeds from sales of fixed income securities | 10,844 | 33,980 |
| Proceeds from maturity of fixed income securities | 155,605 | 199,234 |
| Net increase in payable for securities | — | 10,336 |
| Additions to property and equipment | (5,208) | (4,014) |
| Net cash (used in) provided by investing activities | (48,256) | 52,440 |
| Cash flows from financing activities: | | |
| Proceeds from revolving credit facility | — | 150,000 |
| Payment of debt issuance costs | — | (1,523) |
| Payment of withholding taxes related to share-based compensation net share settlement | (8,073) | (6,722) |
| Net cash (used in) provided by financing activities | (8,073) | 141,755 |
| Net increase in cash and cash equivalents | 77,637 | 271,664 |
| Cash and cash equivalents at beginning of period | 99,851 | 155,410 |
| Cash and cash equivalents at end of period | \$177,488 | \$427,074 |

See accompanying notes to consolidated financial statements.

Table of contents

MGIC INVESTMENT CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2018
(Unaudited)

Note 1. Nature of Business and Basis of Presentation

MGIC Investment Corporation is a holding company which, through Mortgage Guaranty Insurance Corporation (“MGIC”) is principally engaged in the mortgage insurance business. We provide mortgage insurance to lenders throughout the United States and to government sponsored entities to protect against loss from defaults on low down payment residential mortgage loans. An insurance subsidiary of MGIC provides credit insurance for certain mortgages under Fannie Mae and Freddie Mac (the “GSEs”) credit risk transfer programs.

The accompanying unaudited consolidated financial statements of MGIC Investment Corporation and its wholly-owned subsidiaries have been prepared in accordance with the instructions to Form 10-Q as prescribed by the Securities and Exchange Commission (“SEC”) for interim reporting and do not include all of the other information and disclosures required by accounting principles generally accepted in the United States of America (“GAAP”). These statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2017 included in our Annual Report on Form 10-K. As used below, “we,” “our” and “us” refer to MGIC Investment Corporation’s consolidated operations or to MGIC Investment Corporation, as the context requires.

In the opinion of management, the accompanying financial statements include all adjustments, consisting primarily of normal recurring accruals, necessary to fairly state our consolidated financial position and consolidated results of operations for the periods indicated. The consolidated results of operations for the interim period may not be indicative of the results that may be expected for the year ending December 31, 2018.

Substantially all of our insurance written since 2008 has been for loans purchased by the GSEs. We operate under the Private Mortgage Insurer Eligibility Requirements (“PMIERS”) of the GSEs that became effective December 31, 2015 and which have been amended from time to time. The financial requirements of the PMIERS require a mortgage insurer’s “Available Assets” (generally only the most liquid assets of an insurer) to equal or exceed its “Minimum Required Assets” (which are based on an insurer's book of insurance in force, calculated from tables of factors with several risk dimensions and subject to a floor amount). Based on our interpretation of the PMIERS, as of March 31, 2018, MGIC’s Available Assets are in excess of its Minimum Required Assets; and MGIC is in compliance with the financial requirements of the PMIERS and eligible to insure loans purchased by the GSEs.

Reclassifications

Certain reclassifications to 2017 amounts have been made in the accompanying financial statements to conform to the 2018 presentation.

Subsequent events

We have considered subsequent events through the date of this filing.

Share repurchase program

On April 26, 2018, our Board of Directors authorized a share repurchase program under which we may repurchase up to \$200 million of our common stock through the end of 2019. Repurchases may be made from time to time on the open market or through privately negotiated transactions. The repurchase program may be suspended for periods or discontinued at any time.

Table of contents

Note 2. New Accounting Pronouncements

Accounting standards effective in 2018, or early adopted, and relevant to our financial statements

Table 2.1 shows the relevant amendments to accounting standards that have been implemented for the fiscal year beginning January 1, 2018; none had a material impact on our consolidated financial statements or disclosures.

Table 2.1

| Standard / Interpretation | Amended Standards | Effective date |
|---------------------------|---|-----------------|
| | ASC 718 Compensation - Stock Compensation | |
| | •ASU 2017-09 - Scope of Modification Accounting | January 1, 2018 |
| | ASC 310 Receivables - Nonrefundable Fees and Other Costs | |
| | •ASU 2017-08 - Premium Amortization on Purchased Callable Debt Securities | January 1, 2019 |
| | ASC 715 Compensation - Retirement Benefits | |
| | •ASU 2017-07 - Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost | January 1, 2018 |
| | ASC 825 Financial Instruments - Overall | |
| | •ASU 2016-01 - Recognition and Measurement of Financial Assets and Financial Liabilities | January 1, 2018 |

Stock Compensation - Scope of Modification Accounting

In May 2017, the FASB issued updated guidance related to a change in the terms or conditions (modification) of a share-based award. The updated guidance provides that an entity should account for the effects of a modification unless the fair value and vesting conditions of the modified award and the classification of the award (equity or liability instrument) are the same as the original award immediately before the modification. The updated guidance addresses the current diversity in practice on applying modification accounting, as some entities evaluate whether changes to awards are substantive, which is not prescribed within the current accounting guidance. The updated guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those annual periods. Early adoption is permitted, including adoption in any interim period.

Adoption impact: The adoption of this guidance had no impact on our consolidated financial statements or disclosures.

Premium Amortization on Purchased Callable Debt Securities

In March 2017, the FASB issued updated guidance to amend the amortization period for certain purchased callable debt securities held at a premium shortening the amortization period to the earliest call date. Under current GAAP, there is diversity in practice in the amortization period for premiums of callable debt securities and in how the potential for exercise of a call is factored into current impairment assessments. This updated guidance aligns with how callable debt securities, in the United States, are generally quoted, priced, and traded assuming a model that incorporates consideration of calls (also referred to as “yield-to-worst” pricing). The updated guidance is effective for annual periods beginning after December 15, 2018, including interim periods within those annual periods.

Adoption impact: We adopted this guidance as of January 1, 2018 with no impact to our consolidated financial statements or disclosures as our accounting practice adhered to the updated guidance.

Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost

In March 2017, the FASB issued updated guidance that improves the reporting of net benefit cost in the financial statements. The updated guidance requires that an employer report the service cost component in the same financial statement caption as other compensation costs arising from services rendered by employees during the period. The other components of net benefit cost are required to be presented in the statement of operations separately from the service cost component and outside a subtotal of income from operations, if one is presented. Current guidance does not prescribe where the amount of net benefit cost

Table of contents

should be presented in an employer’s statement of operations and does not require entities to disclose by line item the amount of net benefit cost that is included in the statement of operations. The updated guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those annual periods.

Adoption impact: The adoption of this guidance had no impact on our consolidated financial statements or disclosures as the service cost component is reported in the same financial statement caption as other compensation costs and we do not present a subtotal of income outside of income from operations. The service cost component of our benefit plans is disclosed in Note 10 - “Benefit Plans” to our consolidated financial statements.

Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued updated guidance to address the recognition, measurement, presentation, and disclosure of certain financial instruments. The updated guidance requires equity investments, except those accounted for under the equity method of accounting, that have a readily determinable fair value to be measured at fair value with changes in fair value recognized in net income. Equity investments that do not have readily determinable fair values may be remeasured at fair value either upon the occurrence of an observable price change or upon identification of an impairment. A qualitative assessment for impairment is required for equity investments without readily determinable fair values. The updated guidance also eliminates the requirement to disclose the method and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost on the balance sheet. Further, the updated guidance clarifies that entities should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entities’ other deferred tax assets. The updated guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those annual periods and will require recognition of a cumulative effect adjustment at adoption.

Adoption impact: The adoption of this guidance resulted in an immaterial cumulative effect adjustment to our 2018 beginning accumulated other comprehensive (loss) income and retained earnings to recognize unrealized gains on equity investments. At December 31, 2017, equity investments were classified as available-for-sale on the consolidated balance sheet. Upon adoption the updated guidance eliminated the available-for-sale balance sheet classification for equity securities.

In February 2018, the FASB issued a separate update for technical corrections and improvements to clarify certain aspects of the guidance issued above. This update clarifies the presentation of investments in Federal Home Loan Bank stock and prohibits the investment from being shown with equity securities.

Adoption impact: As of March 31, 2018, the value of our investment in Federal Home Loan Bank of Chicago (“FHLB”) stock, which is carried at cost, is presented within “Other invested assets” on our consolidated balance sheet.

Prospective Accounting Standards

Table 2.2 shows the relevant new amendments to accounting standards, which are not yet effective or adopted.

Table 2.2

| Standard / Interpretation | Amended Standards | Effective date |
|---------------------------|---|-----------------|
| | ASC 326 Financial Instruments - Credit Losses | |
| | • ASU 2016-13 - Measurement of Credit Losses on Financial Instruments | January 1, 2020 |

Measurement of Credit Losses on Financial Instruments

In June 2016, the FASB issued updated guidance that requires immediate recognition of estimated credit losses expected to occur over the remaining life of many financial instruments. Entities will be required to utilize a current

expected credit losses (“CECL”) methodology that incorporates their forecasts of future economic conditions into their loss estimate unless such forecast is not reasonable and supportable, in which case the entity will revert to historical loss experience. Any allowance for CECL reduces the amortized cost

Table of contents

basis of the financial instrument to the amount an entity expects to collect. Credit losses relating to available-for-sale fixed maturity securities are to be recorded through an allowance for credit losses, rather than a write-down of the asset, with the amount of the allowance limited to the amount by which fair value is less than amortized cost. In addition, the length of time a security has been in an unrealized loss position will no longer impact the determination of whether a credit loss exists. The updated guidance is not prescriptive about certain aspects of estimating expected credit losses, including the specific methodology to use, and therefore will require significant judgment in application. The updated guidance is effective for annual periods beginning after December 15, 2019, including interim periods within those annual periods. Early adoption is permitted for annual and interim periods in fiscal years beginning after December 15, 2018. We are currently evaluating the impacts the adoption of this guidance will have on our consolidated financial statements, but do not expect it to have a material impact on our consolidated financial statements or disclosures.

Note 3. Debt

Debt obligations

The par value of our long-term debt obligations and their aggregate carrying values as of March 31, 2018 and December 31, 2017 are presented in table 3.1 below.

| | Table 3.1 | | |
|--------------------------------|---------------|----------------|-------------------|
| Long-term debt obligations | (In millions) | March 31, 2018 | December 31, 2017 |
| FHLB Advance | | \$ 155.0 | \$ 155.0 |
| 5.75% Notes | | 425.0 | 425.0 |
| 9% Debentures ⁽¹⁾ | | 256.9 | 256.9 |
| Long-term debt, par value | | 836.9 | 836.9 |
| Debt issuance costs | | (6.2) | (6.5) |
| Long-term debt, carrying value | | \$ 830.7 | \$ 830.4 |

Convertible at any time prior to maturity at the holder's option, at an initial conversion rate, which is subject to adjustment, of 74.0741 shares per \$1,000 principal amount, representing an initial conversion price of approximately \$13.50 per share. If a holder elects to convert their debentures, deferred interest owed on the debentures being converted is also converted into shares of our common stock. The conversion rate for any deferred interest is based on the average price that our shares traded at during a 5-day period immediately prior to the election to convert. In lieu of issuing shares of common stock upon conversion of the debentures, we may, at our option, make a cash payment to converting holders for all or some of the shares of our common stock otherwise issuable upon conversion.

The 5.75% Notes, 9% Debentures, and any amounts drawn on our revolving credit facility, are obligations of our holding company, MGIC Investment Corporation, and not of its subsidiaries. In addition to interest on amounts drawn, the unused portion of our revolving credit facility is subject to recurring commitment fees, which is charged to interest expense. The Federal Home Loan Bank Advance (the "FHLB Advance") is an obligation of MGIC.

Table 3.2 below presents interest payments on our debt obligations.

| | | Table 3.2 | |
|---------------------------------------|------------------|---------------------------------------|--------|
| | | Three Months Ended March 31, | |
| Interest payments on debt obligations | (In millions) | 2018 | 2017 |
| Revolving credit facility | | \$0.2 | \$— |
| FHLB Advance | | 0.7 | 0.7 |
| 5.75% Notes | | 12.2 | 12.9 |
| Total interest payments | | \$13.1 | \$13.6 |

Table of contents

Note 4. Reinsurance

The reinsurance agreements we have entered into, excluding captive agreements (which were immaterial), are discussed below. The effect of all of our reinsurance agreements on premiums earned and losses incurred is shown in table 4.1 below.

| Table 4.1 | | Three Months Ended | |
|----------------------|-----------|--------------------|--|
| Reinsurance | March 31, | | |
| (In thousands) | 2018 | 2017 | |
| Premiums earned: | | | |
| Direct | \$265,251 | \$259,428 | |
| Assumed | 121 | 98 | |
| Ceded | (33,265) | (30,423) | |
| Net premiums earned | \$232,107 | \$229,103 | |
| Losses incurred: | | | |
| Direct | \$31,501 | \$32,413 | |
| Assumed | 90 | 105 | |
| Ceded | (7,741) | (4,899) | |
| Losses incurred, net | \$23,850 | \$27,619 | |

Quota share reinsurance

We utilize quota share reinsurance to manage our exposure to losses resulting from our mortgage guaranty insurance policies and to provide reinsurance capital credit under the PMIERS. Each of the reinsurers under our QSR Transactions has an insurer financial strength rating of A- or better by Standard and Poor's Rating Services, A.M. Best or both.

2018 QSR Transaction. We entered into a 2018 QSR Transaction with a group of unaffiliated reinsurers to manage our exposure to losses resulting from the covered mortgage guaranty insurance policies and to provide reinsurance capital credit under the PMIERS. The 2018 QSR Transaction has an effective date of January 1, 2018, and provides coverage on new business written in 2018 that meets certain eligibility requirements. Under the 2018 QSR Transaction, we will cede losses incurred and premiums on or after the effective date through December 31, 2029, at which time the agreement expires. Early termination of the agreement can be elected by us effective December 31, 2021, and annually thereafter, for a fee, or under specified scenarios for no fee upon prior written notice, including if we will receive less than 90% of the full credit amount under the PMIERS for the risk ceded in any required calculation period.

The structure of the 2018 QSR Transaction is a 30% quota share for all policies covered, with a 20% ceding commission as well as a profit commission. Generally, under the 2018 QSR Transaction, we will receive a profit commission provided that the loss ratio on the loans covered under the agreement remains below 62%.

2015 and 2017 QSR Transactions.

Our 2017 quota share reinsurance agreement (“2017 QSR Transaction”) provides coverage on new business written January 1, 2017 through December 29, 2017 that meets certain eligibility requirements. Under the agreement we cede losses incurred and premiums on or after the effective date through December 31, 2028, at which time the agreement expires. Early termination of the agreement can be elected by us effective December 31, 2021 for a fee, or under specified scenarios for no fee upon prior written notice including if we will receive less than 90% of the full credit amount under the PMIERS for the risk ceded in any required calculation period.

Our 2015 quota share reinsurance agreement (“2015 QSR Transaction”) covers eligible risk in force written before 2017. The 2015 QSR Transaction cedes losses incurred and premiums through December 31, 2024, at which time the agreement expires. Early termination of the agreement can be elected by us effective December 31, 2018 for a fee, or under specified scenarios for no fee upon prior written notice,

Table of contents

including if we will receive less than 90% of the full credit amount under the PMIERS for the risk ceded in any required calculation period.

The structure of both the 2017 QSR Transaction and 2015 QSR Transaction is a 30% quota share for all policies covered, with a 20% ceding commission as well as a profit commission. Generally, under the QSR Transactions, we will receive a profit commission provided that the loss ratio on the loans covered under the agreement remains below 60%.

Table 4.2 below presents a summary of our quota share reinsurance agreements, excluding captive agreements (which were immaterial), for the three months ended March 31, 2018 and 2017.

| Quota share reinsurance (In thousands) | Three Months Ended March 31, | |
|--|---------------------------------|----------|
| | 2018 | 2017 |
| Ceded premiums written and earned, net of profit commission ⁽¹⁾ | \$33,036 | \$28,895 |
| Ceded losses incurred | 7,788 | 4,687 |
| Ceding commissions ⁽²⁾ | 12,645 | 12,003 |
| Profit commission | 30,189 | 31,117 |

(1) Under our QSR Transactions, premiums are ceded on an earned and received basis as defined in the agreements.

(2) Ceding commissions are reported within Other underwriting and operating expenses, net on the consolidated statements of operations.

Under the terms of QSR Transactions, ceded premiums, ceding commission and profit commission are settled net on a quarterly basis. The ceded premium due after deducting the related ceding commission and profit commission is reported within “Other liabilities” on the consolidated balance sheets.

The reinsurance recoverable on loss reserves related to our QSR Transactions was \$43.5 million as of March 31, 2018 and \$39.3 million as of December 31, 2017. The reinsurance recoverable balance is secured by funds on deposit from the reinsurers which are based on the funding requirements of PMIERS that address ceded risk.

Note 5. Litigation and Contingencies

Before paying an insurance claim, we review the loan and servicing files to determine the appropriateness of the claim amount. When reviewing the files, we may determine that we have the right to rescind coverage on the loan. We refer to insurance rescissions and denials of claims collectively as “rescissions” and variations of that term. In addition, our insurance policies generally provide that we can reduce or deny a claim if the servicer did not comply with its obligations under our insurance policy. We call such reduction of claims “curtailments.” In recent quarters, an immaterial percentage of claims received in a quarter have been resolved by rescissions. In each of 2017 and the first quarter of 2018, curtailments reduced our average claim paid by approximately 5.6% and 7.3%, respectively.

Our loss reserving methodology incorporates our estimates of future rescissions, curtailments, and reversals of rescissions and curtailments. A variance between ultimate actual rescission, curtailment and reversal rates and our estimates, as a result of the outcome of litigation, settlements or other factors, could materially affect our losses.

When the insured disputes our right to rescind coverage or curtail claims, we generally engage in discussions in an attempt to settle the dispute. If we are unable to reach a settlement, the outcome of a dispute ultimately would be determined by legal proceedings.

Under ASC 450-20, until a liability associated with settlement discussions or legal proceedings becomes probable and can be reasonably estimated, we consider our claim payment or rescission resolved for financial reporting purposes and do not accrue an estimated loss. Where we have determined that a loss is probable and can be reasonably estimated, we have recorded our best estimate of our probable loss. If we are not able

Table of contents

to implement settlements we consider probable, we intend to defend MGIC vigorously against any related legal proceedings.

In addition to matters for which we have recorded a probable loss, we are involved in other discussions and/or proceedings with insureds with respect to our claims paying practices. Although it is reasonably possible that when these matters are resolved we will not prevail in all cases, we are unable to make a reasonable estimate or range of estimates of the potential liability. We estimate the maximum exposure associated with matters where a loss is reasonably possible to be approximately \$282 million, although we believe (but can give no assurance that) we will ultimately resolve these matters for significantly less than this amount. This estimate of our maximum exposure does not include interest or consequential or exemplary damages.

Mortgage insurers, including MGIC, have been involved in litigation and regulatory actions related to alleged violations of the anti-referral fee provisions of the Real Estate Settlement Procedures Act, which is commonly known as RESPA, and the notice provisions of the Fair Credit Reporting Act, which is commonly known as FCRA. While these proceedings in the aggregate have not resulted in material liability for MGIC, there can be no assurance that the outcome of future proceedings, if any, under these laws would not have a material adverse affect on us. In addition, various regulators, including the CFPB, state insurance commissioners and state attorneys general may bring other actions seeking various forms of relief in connection with alleged violations of RESPA. The insurance law provisions of many states prohibit paying for the referral of insurance business and provide various mechanisms to enforce this prohibition. While we believe our practices are in conformity with applicable laws and regulations, it is not possible to predict the eventual scope, duration or outcome of any such reviews or investigations nor is it possible to predict their effect on us or the mortgage insurance industry.

Through a non-insurance subsidiary, we utilize our underwriting skills to provide an outsourced underwriting service to our customers known as contract underwriting. As part of the contract underwriting activities, that subsidiary is responsible for the quality of the underwriting decisions in accordance with the terms of the contract underwriting agreements with customers. That subsidiary may be required to provide certain remedies to its customers if certain standards relating to the quality of our underwriting work are not met, and we have an established reserve for such future obligations. Claims for remedies may be made a number of years after the underwriting work was performed. The underwriting remedy expense for 2017 and the first three months of 2018 was immaterial to our consolidated financial statements.

In addition to the matters described above, we are involved in other legal proceedings in the ordinary course of business. In our opinion, based on the facts known at this time, the ultimate resolution of these ordinary course legal proceedings will not have a material adverse effect on our financial position or consolidated results of operations.

See Note 11 – “Income Taxes” for a description of federal income tax contingencies.

Note 6. Earnings per Share

Basic earnings per share (“EPS”) is calculated by dividing net income by the weighted average number of shares of common stock outstanding. Diluted EPS includes the components of basic EPS and also gives effect to dilutive common stock equivalents. We calculate diluted EPS using the treasury stock method and if-converted method. Under the if-converted method, diluted EPS reflects the potential dilution that could occur if our convertible debt instruments result in the issuance of common stock. The determination of potentially issuable shares does not consider the satisfaction of the conversion requirements and the shares are included in the determination of diluted EPS as of the beginning of the period, if dilutive. During the quarter ended March 31, 2018, we had 9% Debentures outstanding that could result in potentially issuable shares. For purposes of calculating basic and diluted EPS, vested restricted stock and restricted stock units (“RSUs”) are considered outstanding.

Table of contents

Table 6.1 reconciles the numerators and denominators used to calculate basic and diluted EPS.

| | | Table 6.1 | |
|--------------------|---|-----------------|-----------|
| | | Three Months | |
| | | Ended March 31, | |
| Earnings per share | (In thousands, except per share data) | 2018 | 2017 |
| | Basic earnings per share: | | |
| | Net income | \$ 143,637 | \$ 89,798 |
| | Weighted average common shares outstanding | 370,908 | 341,009 |
| | - basic | | |
| | Basic earnings per share | \$ 0.39 | \$ 0.26 |
| | Diluted earnings per share: | | |
| | Net income | \$ 143,637 | \$ 89,798 |
| | Interest expense, net of tax (1): | | |
| | 2% Notes | — | 823 |
| | 5% Notes | — | 1,282 |
| | 9% Debentures | 4,566 | 3,757 |
| | Diluted income available to common shareholders | \$ 148,203 | \$ 95,660 |
| | Weighted average common shares outstanding | 370,908 | 341,009 |
| | - basic | | |
| | Effect of dilutive securities: | | |

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| | | |
|--|---------|---------|
| Unvested RSUs | 1,626 | 1,488 |
| 2% Notes | — | 29,859 |
| 5% Notes | — | 10,791 |
| 9% Debentures | 19,028 | 19,028 |
| Weighted average common shares outstanding - diluted | 391,562 | 402,175 |
| Diluted earnings per share | \$0.38 | \$0.24 |

(1) The three months ended March 31, 2018 and 2017 were tax effected at a rate of 21% and 35%, respectively.

Note 7. Investments

Fixed maturities

The amortized cost, gross unrealized gains and losses, and fair value of investments in fixed income securities classified as available-for-sale at March 31, 2018 and December 31, 2017 are shown in tables 7.1a and 7.1b below.

Table 7.1a

| | March 31, 2018 | | | | |
|--|---|----------------|------------------------|--|------------|
| | (In thousands) | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses ⁽¹⁾ | Fair Value |
| Details of fixed income investments by category - current year | U.S. Treasury securities and obligations of U.S. government corporations and agencies | \$ 191,018 | \$ 256 | \$ (2,212) | \$ 189,062 |
| | Obligations of U.S. states and political subdivisions | 2,093,901 | 27,926 | (19,130) | 2,102,697 |
| | Corporate debt securities | 2,087,977 | 1,921 | (33,819) | 2,056,079 |
| | Asset backed securities (“ABS”) | 9,451 | — | (29) | 9,422 |
| | Residential mortgage backed securities (“RMBS”) | 182,050 | 48 | (10,558) | 171,540 |
| Commercial mortgage | 302,434 | 722 | (9,800) | 293,356 | |

| | | | | |
|---|-----------|--------|---------|-------------|
| backed securities (“CMBS”) | | | | |
| Collateralized loan obligations (“CLO”) | 107,785 | 163 | (41 |) 107,907 |
| Total fixed income securities | 4,974,616 | 31,036 | (75,589 |) 4,930,063 |

Table of contents

| | | Table 7.1b | | | | |
|--|---|-------------------|----------------|------------------------|--|------------|
| | | December 31, 2017 | | | | |
| | | (In thousands) | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses ⁽¹⁾ | Fair Value |
| Details of fixed income investments by category - prior year-end | U.S. Treasury securities and obligations of U.S. government corporations and agencies | | \$ 179,850 | \$ 274 | \$ (1,278) | \$ 178,846 |
| | Obligations of U.S. states and political subdivisions | | 2,105,063 | 56,210 | (8,749) | 2,152,524 |
| | Corporate debt securities | | 2,065,475 | 10,532 | (9,169) | 2,066,838 |
| | ABS | | 4,925 | — | (2) | 4,923 |
| | RMBS | | 189,153 | 60 | (7,364) | 181,849 |
| | CMBS | | 301,014 | 1,204 | (4,906) | 297,312 |
| | CLOs | | 100,798 | 304 | (79) | 101,023 |
| | Total fixed income securities | | 4,946,278 | 68,584 | (31,547) | 4,983,315 |

(1) At March 31, 2018 and December 31, 2017, there were no other-than-temporary impairment losses recorded in other comprehensive income.

The amortized cost and fair values of fixed income securities at March 31, 2018, by contractual maturity, are shown in table 7.2 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 ABS, RMBS, CMBS, and CLOs provide for periodic payments throughout their lives, they are listed in separate categories.

| | | Table 7.2 | |
|---|----------------|----------------|------------|
| | | March 31, 2018 | |
| | | (In thousands) | Fair Value |
| Fixed income securities maturity schedule | Amortized Cost | | |
| Due in one year or less | \$ 650,415 | | \$ 649,088 |
| Due after one year through five years | 1,507,245 | | 1,487,678 |
| Due after five years through ten | 909,711 | | 893,329 |

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| | | |
|-------------|-------------|-------------|
| years | | |
| Due after | | |
| ten years | 1,305,525 | 1,317,743 |
| | \$4,372,896 | \$4,347,838 |
| ABS | 9,451 | 9,422 |
| RMBS | 182,050 | 171,540 |
| CMBS | 302,434 | 293,356 |
| CLOs | 107,785 | 107,907 |
| Total as of | | |
| March 31, | \$4,974,616 | \$4,930,063 |
| 2018 | | |

Proceeds from sales of fixed income securities classified as available-for-sale were \$10.8 million and \$34.0 million during the three months ended March 31, 2018 and 2017, respectively. Gross gains of \$0.1 million and \$0.2 million and gross losses of \$0.3 million and \$0.3 million were realized on those sales during the three months ended March 31, 2018 and 2017, respectively.

Table of contents

Equity securities

The cost and fair value of investments in equity securities at March 31, 2018 and December 31, 2017 are shown in tables 7.3a and 7.3b below. As described in Note 2 - "New Accounting Pronouncements," updated guidance regarding the "Recognition and Measurement of Financial Assets and Financial Liabilities" became effective on January 1, 2018, which prohibits our investment in FHLB stock from being presented with equity securities. The amount of our FHLB stock investment has been reclassified and presented in "Other invested assets" on our consolidated balance sheet as of March 31, 2018.

Table 7.3a

| Details of equity security investments - current year | (In thousands) | March 31, 2018 | | | Fair Value |
|---|----------------|----------------|-------------|--------------|------------|
| | | Cost | Gross Gains | Gross Losses | |
| Equity securities | | \$4,143 | \$ 8 | \$ (52) | \$4,099 |

Table 7.3b

| Details of equity security investments - prior year-end | (In thousands) | December 31, 2017 | | | Fair Value |
|---|----------------|-------------------|-------------|--------------|------------|
| | | Cost | Gross Gains | Gross Losses | |
| Equity securities | | \$7,223 | \$ 39 | \$ (16) | \$7,246 |

For the three months ended March 31, 2018, we recognized \$0.1 million of net losses on equity securities still held as of March 31, 2018.

Other invested assets

Other invested assets include an investment in FHLB stock that is carried at cost, which due to its nature approximates fair value. Ownership of FHLB stock provides access to a secured lending facility, and our current FHLB Advance amount is secured by eligible collateral whose fair value is maintained at least at 102% of the outstanding principal balance. As of March 31, 2018, that collateral consisting of fixed income securities is included in our total investment portfolio amount with a total fair value of \$165.6 million.

Unrealized investment losses

Tables 7.4a and 7.4b below summarize, for all available-for-sale investments in an unrealized loss position at March 31, 2018 and December 31, 2017, the aggregate fair value and gross unrealized loss by the length of time those securities have been continuously in an unrealized loss position. The fair value amounts reported in tables 7.4a and 7.4b are estimated using the process described in Note 8 - "Fair Value Measurements" to these consolidated financial statements and in Note 3 - "Significant Accounting Policies" of the notes to the consolidated financial statements in our 2017 Annual Report on Form 10-K.

Table 7.4a

| Investments unrealized losses - current year | (In thousands) | March 31, 2018 | | | | Total Fair Value | Unrealized Losses |
|---|----------------|--------------------------------|--|-------------------|----------|------------------|-------------------|
| | | Less Than 12 Months Fair Value | 12 Months or Greater Unrealized Fair Value | Unrealized Losses | Total | | |
| U.S. Treasury securities and obligations of U.S. government | | \$77,510 | \$(1,532) | \$31,491 | \$(680) | \$109,001 | \$(2,212) |

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| | | | | | | |
|--|-------------|-------------|-----------|-------------|-------------|-------------|
| corporations and agencies Obligations of U.S. states and political subdivisions | 905,755 | (11,622) | 201,094 | (7,508) | 1,106,849 | (19,130) |
| Corporate debt | 1,743,627 | (26,797) | 148,468 | (7,022) | 1,892,095 | (33,819) |
| securities | | | | | | |
| ABS | 9,423 | (29) | — | — | 9,423 | (29) |
| RMBS | 14,226 | (416) | 156,842 | (10,142) | 171,068 | (10,558) |
| CMBS | 114,206 | (2,162) | 126,941 | (7,638) | 241,147 | (9,800) |
| CLOs | — | — | 1,936 | (41) | 1,936 | (41) |
| Total | \$2,864,747 | \$(42,558) | \$666,772 | \$(33,031) | \$3,531,519 | \$(75,589) |

MGIC Investment Corporation - Q1 2018 | 21

Table of contents

| Investments unrealized losses - prior year-end | Table 7.4b (In thousands) | December 31, 2017 | | | | | |
|---|------------------------------|---------------------|-------------------|----------------------|-------------------|--------------|-------------------|
| | | Less Than 12 Months | | 12 Months or Greater | | Total | |
| | | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| U.S. Treasury securities and obligations of U.S. government corporations and agencies | | \$ 144,042 | \$ (796) | \$ 31,196 | \$ (482) | \$ 175,238 | \$ (1,278) |
| Obligations of U.S. states and political subdivisions | | 505,311 | (3,624) | 211,684 | (5,125) | 716,995 | (8,749) |
| Corporate debt securities | | 932,350 | (4,288) | 200,716 | (4,881) | 1,133,066 | (9,169) |
| ABS | | 4,923 | (2) | — | — | 4,923 | (2) |
| RMBS | | 14,979 | (280) | 166,329 | (7,084) | 181,308 | (7,364) |
| CMBS | | 51,096 | (358) | 138,769 | (4,548) | 189,865 | (4,906) |
| CLOs | | 14,243 | (7) | 3,568 | (72) | 17,811 | (79) |
| Equity securities | | 226 | (2) | 431 | (14) | 657 | (16) |
| Total | | \$ 1,667,170 | \$ (9,357) | \$ 752,693 | \$ (22,206) | \$ 2,419,863 | \$ (31,563) |

The unrealized losses in all categories of our investments at March 31, 2018 and December 31, 2017 were primarily caused by changes in interest rates between the time of purchase and the respective fair value measurement date. There were 788 and 586 securities in an unrealized loss position at March 31, 2018 and December 31, 2017, respectively. During each of the three months ended March 31, 2018 and 2017 there were no other-than-temporary impairments (“OTTI”) recognized.

Note 8. Fair Value Measurements

Recurring fair value measurements

In accordance with fair value accounting guidance, we applied the following fair value hierarchy to measure fair value for assets and liabilities:

Level 1 - Quoted prices for identical instruments in active markets that we can access. Financial assets utilizing Level 1 inputs primarily include U.S. Treasury securities and equity securities.

Level 2 - Quoted prices for similar instruments in active markets that we can access; quoted prices for identical or similar instruments in markets that are not active; and inputs, other than quoted prices, that are observable in the marketplace for the instrument. The observable inputs are used in valuation models to calculate the fair value based on the type of instrument. Financial assets utilizing Level 2 inputs primarily include obligations of U.S. government corporations and agencies, corporate bonds, mortgage-backed securities, asset-backed securities, and most municipal bonds.

Level 3 - Valuations derived from valuation techniques in which one or more significant inputs or value drivers are unobservable. The inputs used to derive the fair value of Level 3 securities reflect our own assumptions about the assumptions a market participant would use in pricing an asset or liability. Our non-financial assets that are classified as Level 3 securities consist of real estate acquired through claim settlement. The fair value of real estate acquired is the lower of our acquisition cost or a percentage of the appraised value. The percentage applied to the appraised value is based upon our historical sales experience adjusted for current trends.

Table of contents

Assets measured at fair value, by hierarchy level, as of March 31, 2018 and December 31, 2017 as shown in tables 8.1a and 8.1b below are estimated using the process described above, and more fully in Note 3 - "Significant Accounting Policies" of the notes to the consolidated financial statements in our 2017 Annual Report on Form 10-K.

Table 8.1a

| Fair value hierarchy - current year | (In thousands) | March 31, 2018 | | | |
|---|----------------|------------------|--|---|---|
| | | Total Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. Treasury securities and obligations of U.S. government corporations and agencies | | \$ 189,062 | \$ 81,418 | \$ 107,644 | \$ — |
| Obligations of U.S. states and political subdivisions | | 2,102,697 | — | 2,102,443 | 254 |
| Corporate debt securities | | 2,056,079 | — | 2,056,079 | — |
| ABS | | 9,422 | — | 9,422 | — |
| RMBS | | 171,540 | — | 171,540 | — |
| CMBS | | 293,356 | — | 293,356 | — |
| CLOs | | 107,907 | — | 107,907 | — |
| Total fixed income securities | | 4,930,063 | 81,418 | 4,848,391 | 254 |
| Equity securities ⁽¹⁾ | | 4,099 | 2,931 | — | 1,168 |
| Total investments at fair value | | \$ 4,934,162 | \$ 84,349 | \$ 4,848,391 | \$ 1,422 |
| Real estate acquired ⁽²⁾ | | \$ 10,078 | \$ — | \$ — | \$ 10,078 |

Equity securities in Level 3 are carried at cost, which approximates fair value. See "Reconciliations of Level 3 assets" below for information regarding a change in presentation of amounts previously included in Level 3 Equity securities.

⁽²⁾ Real estate acquired through claim settlement, which is held for sale, is reported in Other assets on the consolidated balance sheets.

Table 8.1b

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| Fair value hierarchy - prior year-end (In thousands) | December 31, 2017 | | | |
|---|-------------------|--|---|---|
| | Total Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. Treasury securities and obligations of U.S. government corporations and agencies | \$ 178,846 | \$ 81,598 | \$ 97,248 | \$ — |
| Obligations of U.S. states and political subdivisions | 2,152,524 | — | 2,152,253 | 271 |
| Corporate debt securities | 2,066,838 | — | 2,066,838 | — |
| ABS | 4,923 | — | 4,923 | — |
| RMBS | 181,849 | — | 181,849 | — |
| CMBS | 297,312 | — | 297,312 | — |
| CLOs | 101,023 | — | 101,023 | — |
| Total fixed income securities | 4,983,315 | 81,598 | 4,901,446 | 271 |
| Equity securities ⁽¹⁾ | 7,246 | 2,978 | — | 4,268 |
| Total investments at fair value | \$ 4,990,561 | \$ 84,576 | \$ 4,901,446 | \$ 4,539 |
| Real estate acquired ⁽²⁾ | \$ 12,713 | \$ — | \$ — | \$ 12,713 |

⁽¹⁾ Equity securities in Level 3 are carried at cost, which approximates fair value.

⁽²⁾ Real estate acquired through claim settlement, which is held for sale, is reported in Other assets on the consolidated balance sheets.

Table of contents

Reconciliations of Level 3 assets

For assets measured at fair value using significant unobservable inputs (Level 3), a reconciliation of the beginning and ending balances for the three months ended March 31, 2018 and 2017 is shown in tables 8.2a and 8.2b below. As described in Note 2 - "New Accounting Pronouncements," updated guidance regarding the Recognition and Measurement of Financial Assets and Financial Liabilities became effective on January 1, 2018, which requires that our investment in FHLB stock not be presented with equity securities. Prior to the updated guidance, our FHLB stock was included in our Level 3 equity securities. As shown in table 8.2a below, for the three months ended March 31, 2018, we have transferred our FHLB stock out of Level 3 assets, and they are carried at cost, which approximates fair value on our consolidated balance sheet as of March 31, 2018. The amount of FHLB stock is presented in "Other invested assets" as of March 31, 2018. There were no losses included in earnings for those periods attributable to the change in unrealized losses on assets still held at the end of the applicable period.

Table 8.2a

| | (In thousands) | Three Months Ended March 31, 2018 | | | |
|--|---|-----------------------------------|-------------------|-------------------|----------------------|
| | | Debt Securities | Equity Securities | Total Investments | Real Estate Acquired |
| Development of assets and liabilities classified within level 3 - current year quarter | Balance at December 31, 2017 | \$271 | \$ 4,268 | \$ 4,539 | \$12,713 |
| | Transfers out of Level 3 | — | (3,100) | (3,100) | — |
| | Total realized/unrealized gains (losses): | | | | |
| | Included in earnings and reported as losses incurred, net | — | — | — | 341 |
| | Purchases | — | — | — | 5,894 |
| | Sales | (17) | — | (17) | (8,870) |
| | Balance at March 31, 2018 | \$254 | \$ 1,168 | \$ 1,422 | \$10,078 |

Table 8.2b

| | (In thousands) | Three Months Ended March 31, 2017 | | | |
|--|---|-----------------------------------|-------------------|-------------------|----------------------|
| | | Debt Securities | Equity Securities | Total Investments | Real Estate Acquired |
| Development of assets and liabilities classified within level 3 - prior year quarter | Balance at December 31, 2016 | \$691 | \$ 4,268 | \$ 4,959 | \$11,748 |
| | Total realized/unrealized gains (losses): | | | | |
| | Included in earnings and reported as losses incurred, net | — | — | — | (163) |
| | Purchases | — | — | — | 8,683 |
| | Sales | (8) | — | (8) | (9,538) |

| | | | | |
|------------------------------|-------|----------|----------|----------|
| Balance at March 31, 2017 | \$683 | \$ 4,268 | \$ 4,951 | \$10,730 |
|------------------------------|-------|----------|----------|----------|

Authoritative guidance over disclosures about the fair value of financial instruments requires additional disclosure for financial instruments not measured at fair value. Certain financial instruments, including insurance contracts, are excluded from these fair value disclosure requirements. The carrying values of cash and cash equivalents (Level 1) and accrued investment income (Level 2) approximated their fair values. Additional fair value disclosures related to our investment portfolio are included in Note 7 – “Investments.”

Financial liabilities not measured at fair value

We incur financial liabilities in the normal course of our business. Table 8.3 presents the carrying value and fair value of our financial liabilities disclosed, but not carried, at fair value at March 31, 2018 and December 31, 2017. The fair values of our 5.75% Notes and 9% Debentures were based on observable market prices. The fair value of the FHLB Advance was estimated using discounted cash flows on current incremental borrowing rates for similar borrowing arrangements. In all cases the fair values of the financial liabilities below are categorized as Level 2.

Table of contents

| | | Table 8.3 | | | |
|---------------------------------------|----------------|----------------|------------|-------------------|------------|
| | | March 31, 2018 | | December 31, 2017 | |
| Fair value measurements - liabilities | (In thousands) | Carrying Value | Fair Value | Carrying Value | Fair Value |
| | FHLB Advance | | 155,000 | 149,756 | \$155,000 |
| 5.75% Notes | | 418,848 | 446,730 | 418,560 | 465,473 |
| 9% Debentures | | 256,872 | 350,897 | 256,872 | 353,507 |
| Total financial liabilities | | \$830,720 | \$947,383 | \$830,432 | \$971,104 |

Note 9. Other Comprehensive Income

The pretax and related income tax (expense) benefit components of our other comprehensive income (loss) for the three months ended March 31, 2018 and 2017 are included in table 9.1 below.

| | | Table 9.1 | |
|---|--|------------------------------|-----------|
| | | Three Months Ended March 31, | |
| | | 2018 | 2017 |
| Components of other comprehensive (loss) income | (In thousands) | | |
| | Net unrealized investment (losses) gains arising during the period | \$ (81,587) | \$ 18,647 |
| | Income tax benefit (expense) | 17,134 | (6,526) |
| | Net of taxes | (64,453) | 12,121 |
| | Net changes in benefit plan assets and obligations | 625 | (234) |
| | Income tax (expense) benefit | (131) | 81 |
| | Net of taxes | 494 | (153) |
| | Net changes in unrealized foreign currency translation adjustment | — | 45 |
| | Income tax (expense) | — | (14) |
| | Net of taxes | — | 31 |

| | | |
|---|------------|----------|
| Total other comprehensive (loss) income | (80,962) | 18,458 |
| Total income tax benefit (expense) | 17,003 | (6,459) |
| Total other comprehensive (loss) income, net of tax | \$(63,959) | \$11,999 |

The pretax and related income tax benefit (expense) components of the amounts reclassified from our accumulated other comprehensive loss (“AOCL”) to our consolidated statements of operations for the three months ended March 31, 2018 and 2017 are included in table 9.2 below.

Table 9.2

| Reclassifications from AOCL | Three Months Ended March 31, | |
|---|------------------------------|---------|
| | 2018 | 2017 |
| (In thousands) | | |
| Reclassification adjustment for net realized (losses) gains ⁽¹⁾ | \$(91) | \$(747) |
| Income tax benefit | 19 | 261 |
| Net of taxes | (72) | (486) |
| Reclassification adjustment related to benefit plan assets and obligations ⁽²⁾ | (625) | 234 |
| Income tax benefit (expense) | 131 | (81) |
| Net of taxes | (494) | 153 |
| Total reclassifications | (716) | (513) |
| Total income tax benefit | 150 | 180 |
| Total reclassifications, net of tax | \$(566) | \$(333) |

⁽¹⁾ Increases (decreases) Net realized investment (losses) gains on the consolidated statements of operations.

⁽²⁾ Decreases (increases) Other underwriting and operating expenses, net on the consolidated statements of operations.

Table of contents

A rollforward of AOCL for the three months ended March 31, 2018, including amounts reclassified from AOCL, are included in table 9.3 below.

| | | Three Months Ended March 31, 2018 | | |
|---------------------|---|--|--|-------------|
| | | Net unrealized gains and losses on available-for-sale securities | Net benefit plan assets and obligations recognized in shareholders' equity | Total AOCL |
| Rollforward of AOCL | (In thousands) | | | |
| | Balance, December 31, 2017, net of tax | \$29,257 | \$ (73,058) | \$(43,801) |
| | Other comprehensive income before reclassifications | (64,525) | — | (64,525) |
| | Less: Amounts reclassified from AOCL | (72) | (494) | (566) |
| | Balance, March 31, 2018, net of tax | \$(35,196) | \$ (72,564) | \$(107,760) |

Note 10. Benefit Plans

Table 10.1 provides the components of net periodic benefit cost for our pension, supplemental executive retirement and other postretirement benefit plans for the three months ended March 31, 2018 and 2017.

| | | Three Months Ended March 31, | | | |
|---|------------------------------------|---|----------|------------------------------------|-----------|
| | | Pension and Supplemental Executive Retirement Plans | | Other Postretirement Benefit Plans | |
| (In thousands) | | 2018 | 2017 | 2018 | 2017 |
| Components of net periodic benefit cost | Service cost | \$2,562 | \$2,294 | \$270 | \$187 |
| | Interest cost | 3,782 | 3,858 | 214 | 167 |
| | Expected return on plan assets | (5,570) | (5,036) | (1,588) | (1,312) |
| | Recognized net actuarial loss | 1,785 | 1,535 | (46) | — |
| | Amortization of prior service cost | (87) | (107) | (1,026) | (1,662) |
| | | | \$2,472 | \$2,544 | \$(2,176) |

Net periodic
benefit cost
(benefit)

We currently intend to make contributions totaling \$11 million to our qualified pension plan and supplemental executive retirement plan in 2018.

Note 11. Income Taxes

We have approximately \$585.7 million of net operating loss (“NOL”) carryforwards as of March 31, 2018. Any unutilized carryforwards are scheduled to expire at the end of tax years 2032 through 2033.

We evaluate the realizability of our deferred tax assets including our NOL carryforwards on a quarterly basis. Based on our analysis, we have concluded that all of our deferred tax assets are fully realizable and therefore no valuation allowance existed at March 31, 2018 and December 31, 2017.

Tax Contingencies

As previously disclosed, the Internal Revenue Service (“IRS”) completed examinations of our federal income tax returns for the years 2000 through 2007 and issued proposed assessments for taxes, interest and penalties related to our treatment of the flow-through income and loss from an investment in a portfolio of residual interests of Real Estate Mortgage Investment Conduits (“REMICs”). The IRS indicated that it did not believe that, for various reasons, we had established sufficient tax basis in the REMIC residual interests to deduct the losses from taxable income. We appealed these assessments within the IRS and in August 2010, we reached a tentative settlement agreement with the IRS which was not finalized.

In 2014, we received Notices of Deficiency (commonly referred to as “90 day letters”) covering the 2000-2007 tax years. The Notices of Deficiency reflect taxes and penalties related to the REMIC matters of \$197.5 million and at March 31, 2018, there would also be interest related to these matters of approximately \$209.7 million.

Table of contents

In 2007, we made a payment of \$65.2 million to the United States Department of the Treasury which will reduce any amounts we would ultimately owe. The Notices of Deficiency also reflect additional amounts due of \$261.4 million, which are primarily associated with the disallowance of the carryback of the 2009 net operating loss to the 2004-2007 tax years. We believe the IRS included the carryback adjustments as a precaution to keep open the statute of limitations on collection of the tax that was refunded when this loss was carried back, and not because the IRS actually intends to disallow the carryback permanently. Depending on the outcome of this matter, additional state income taxes and state interest may become due when a final resolution is reached. As of March 31, 2018, those state taxes and interest would approximate \$87.4 million. In addition, there could also be state tax penalties. Our total amount of unrecognized tax benefits as of March 31, 2018 is \$143.7 million, which represents the tax benefits generated by the REMIC portfolio included in our tax returns that we have not taken benefit for in our financial statements, including any related interest.

We reached agreement with the IRS to settle all issues in the case and the IRS subsequently submitted documentation reflecting the terms of the agreement to the Joint Committee on Taxation (“JCT”) for its review, which must be performed before a settlement can be completed. In the second quarter of 2018, we were notified that the JCT had no objection to the terms of the agreement and that the IRS was working toward finalizing the matter. The expected impact of the agreed upon settlement was previously reflected in our consolidated financial statements.

Although we expect the settlement to be completed, should a settlement not be completed, ongoing litigation to resolve our dispute with the IRS could be lengthy and costly in terms of legal fees and related expenses. We would need to make further adjustments, which could be material, to our tax provision and liabilities if our view of the probability of success in this matter changes, and the ultimate resolution of this matter could have a material negative impact on our effective tax rate, results of operations, cash flows, available assets and statutory capital. In this regard, see Note 15 - “Statutory Information.”

The total amount of the unrecognized tax benefits, related to our aforementioned REMIC issue that would affect our effective tax rate is \$125.0 million. We recognize interest accrued and penalties related to unrecognized tax benefits in income taxes. As of March 31, 2018 and December 31, 2017, we had accrued \$52.9 million and \$52.0 million, respectively, for the payment of interest.

Note 12. Loss Reserves

We establish reserves to recognize the estimated liability for losses and loss adjustment expenses (“LAE”) related to defaults on insured mortgage loans. Loss reserves are established by estimating the number of loans in our inventory of delinquent loans that will result in a claim payment, which is referred to as the claim rate, and further estimating the amount of the claim payment, which is referred to as claim severity.

Estimation of losses is inherently judgmental. The conditions that affect the claim rate and claim severity include the current and future state of the domestic economy, including unemployment and the current and future strength of local housing markets; exposure on insured loans; the amount of time between default and claim filing; and curtailments and rescissions. The actual amount of the claim payments may be substantially different than our loss reserve estimates. Our estimates could be adversely affected by several factors, including a deterioration of regional or national economic conditions, including unemployment, leading to a reduction in borrowers’ income and thus their ability to make mortgage payments, and a drop in housing values which may affect borrower willingness to continue to make mortgage payments when the value of the home is below the mortgage balance. Changes to our estimates could result in a material impact to our consolidated results of operations and financial position, even in a stable economic environment.

The “Losses incurred” section of table 12.1 below shows losses incurred on delinquencies that occurred in the current year and in prior years. The amount of losses incurred relating to delinquencies that occurred in the current year

represents the estimated amount to be ultimately paid on such delinquencies. The amount of losses incurred relating to delinquencies that occurred in prior years represents the difference between the actual claim rate and severity associated with those delinquencies resolved in the current year compared to the estimated claim rate and severity at the prior year-end, as well as a re-estimation of amounts to be ultimately paid on delinquencies continuing from the end of the prior year. This re-estimation of the claim rate and severity is the result of our review of current trends in the delinquent inventory, such as percentages of

Table of contents

delinquencies that have resulted in a claim, the amount of the claims relative to the average loan exposure, changes in the relative level of delinquencies by geography and changes in average loan exposure.

Losses incurred on delinquencies that occurred in the current year decreased in the first three months of 2018 compared to the same period in 2017, primarily due to a decrease in the estimated claim rate on recently reported delinquencies and a decrease in the number of new delinquencies, net of related cures.

For the three months ended March 31, 2018 and 2017, we experienced favorable loss reserve development on previously received delinquencies, in large part, due to the resolution of approximately 31% and 29%, respectively, of the prior year delinquent inventory, with improved cure rates. The favorable loss reserve development resulting from a reduction in the estimated claim rate was partially offset in each of the three months ended March 31, 2018 and 2017 by an increase in our severity assumption on previously received delinquencies.

The “Losses paid” section of table 12.1 below shows the amount of losses paid on delinquent notices received in the current year and losses paid on delinquent notices received in prior years. For several years, the average time it took to receive a claim associated with a delinquency had increased significantly from our historical experience of approximately twelve months. This was, in part, due to new loss mitigation protocols established by servicers and to changes in some state foreclosure laws that may include, for example, a requirement for additional review and/or mediation processes. In recent quarters, we have experienced a decline in the average time servicers are utilizing to process foreclosures, which has reduced the average time to receive a claim associated with new delinquent notices that do not cure. All else being equal, the longer the period between delinquency and claim filing, the greater the severity.

During the first three months of 2018, our losses paid included \$7 million paid upon commutation of coverage on pools of non-performing loans (“NPLs”). The commutations reduced our delinquent inventory by 224 delinquencies. These commutations had no material impact on our losses incurred, net.

Our estimate of premiums to be refunded on expected claim payments is accrued for separately in “Other Liabilities” on our consolidated balance sheets and approximated \$56 million and \$61 million at March 31, 2018 and December 31, 2017, respectively.

Table of contents

Table 12.1 provides a reconciliation of beginning and ending loss reserves as of and for the three months ended March 31, 2018 and 2017.

| | Table 12.1 | |
|---|--|-----------------------|
| | Three Months Ended March 31, | |
| | 2018 | 2017 |
| Development of reserves for losses and loss adjustment expenses | (In thousands) | |
| | | |
| | Reserve at beginning of period | \$985,635 \$1,438,813 |
| | Less reinsurance recoverable | 48,474 50,493 |
| | Net reserve at beginning of period | 937,161 1,388,320 |
| | Losses incurred: | |
| | Losses and LAE incurred in respect of delinquency notices received in: | |
| | Current year | 59,070 80,416 |
| | Prior years ⁽¹⁾ | (35,220) (52,797) |
| | Total losses incurred | 23,850 27,619 |
| | Losses paid: | |
| | Losses and LAE paid in respect of delinquency notices received in: | |
| | Current year | 95 331 |
| | Prior years | 81,983 127,224 |
| | Reinsurance terminations | 236 — |
| | Total losses paid | 82,314 127,555 |
| | Net reserve at end of period | 878,697 1,288,384 |
| | | 45,474 46,658 |

Plus
 reinsurance
 recoverables
 Reserve at end of period \$924,171 \$1,335,042

(1) A negative number for prior year losses incurred indicates a redundancy of prior year loss reserves. See the following table for more information about prior year loss development.

The prior year development of the reserves in the first three months of 2018 and 2017 is reflected in table 12.2 below.

Table 12.2

| | Three Months Ended March 31, | |
|--|---------------------------------------|--------|
| (in millions) | 2018 | 2017 |
| Reserve development on previously received delinquencies | | |
| Decrease in estimated claim rate on primary defaults | \$(47) | \$(54) |
| Increase in estimated severity on primary defaults | 16 | 4 |
| Change in estimates related to pool reserves, LAE reserves and reinsurance | (4) | (3) |
| Total prior year loss development | \$(35) | \$(53) |

(1) A negative number for prior year loss development indicates a redundancy of prior year loss reserves.

Default inventory

A rollforward of our primary delinquent inventory for the three months ended March 31, 2018 and 2017 appears in table 12.3 below. The information concerning new notices and cures is compiled from monthly reports received from loan servicers. The level of new notice and cure activity reported in a particular month can be influenced by, among other things, the date on which a servicer generates its report, the accuracy of the data provided by servicers, the number of business days in a month, transfers of servicing between loan servicers and whether all servicers have provided the reports in a given month.

Table of contents

| | | Table 12.3 | |
|----------------------------------|--|-----------------|----------|
| | | Three Months | |
| | | Ended March 31, | |
| | | 2018 | 2017 |
| Delinquent inventory rollforward | Delinquent inventory at beginning of period | 46,556 | 50,282 |
| | New notices | 14,623 | 14,939 |
| | Cures | (18,073) | (17,128) |
| | Paids (including those charged to a deductible or captive) | (1,571) | (2,635) |
| | Rescissions and denials | (68) | (95) |
| | Other items removed from inventory | (224) | (14) |
| | Delinquent inventory at end of period | 41,243 | 45,349 |
| | | | |
| | | | |
| | | | |

The decrease in the primary delinquent inventory experienced during 2018 and 2017 was generally across all markets and primarily in book years 2008 and prior. Historically as a default ages it becomes more likely to result in a claim.

Hurricane activity

New delinquent notice activity increased in the fourth quarter of 2017 because of hurricane activity that primarily impacted Puerto Rico, Texas, and Florida in the third quarter of 2017. In response to the hurricanes, the Federal Emergency Management Agency has declared Individual Assistance Disaster Areas (“IADA”), and during the fourth quarter of 2017 we received 9,294 new notices from the IADA. As a result, the number of loans delinquent three months or less was a higher percentage of our total inventory as of December 31, 2017 than it had been as of March 31, 2017. Many of the loans in the IADA first reported as delinquent in the fourth quarter of 2017 remained delinquent through the period ending March 31, 2018 and are shown as 4-11 months delinquent in table 12.4 below. Correspondingly, the combined number of loans in our delinquent inventory with up to eleven missed payments was elevated as of December 31, 2017, compared to March 31, 2017, and remained elevated as of March 31, 2018 as shown in table 12.5 below.

Table 12.4 below shows the number of consecutive months a borrower is delinquent.

Table 12.4

| March 31, 2018 | December 31, 2017 | March 31, 2017 |
|-------------------|----------------------|-------------------|
|-------------------|----------------------|-------------------|

Delinquent inventory - consecutive months in default

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| | | | | | | |
|---|--------|------|--------|------|--------|------|
| 3 months or less | 8,770 | 21 % | 17,119 | 37 % | 9,184 | 20 % |
| 4-11 months | 16,429 | 40 % | 12,050 | 26 % | 13,617 | 30 % |
| 12 months or more ⁽¹⁾ | 16,044 | 39 % | 17,387 | 37 % | 22,548 | 50 % |
| ⁽²⁾ Total primary delinquent inventory | 41,243 | 100% | 46,556 | 100% | 45,349 | 100% |
| Primary claims received inventory included in ending delinquent inventory: | 819 | 2 % | 954 | 2 % | 1,390 | 3 % |

Approximately 44%, 45%, and 48% of the primary delinquent inventory delinquent for 12 consecutive months or more has been delinquent for at least 36 consecutive months as of March 31, 2018, December 31, 2017, and March 31, 2017, respectively.

⁽²⁾ The majority of items removed from our delinquent inventory were due to commutations of NPLs during the three months ended March 31, 2018 were delinquent for 12 consecutive months or more as of December 31, 2017.

Table of contents

The number of months a loan is in the delinquent inventory can differ from the number of payments that the borrower has not made or is considered delinquent. These differences typically result from a borrower making monthly payments that do not result in the loan becoming fully current. Table 12.5 below shows the number of payments that a borrower is delinquent.

| | March 31, 2018 | December 31, 2017 | March 31, 2017 |
|---|-------------------|----------------------|-------------------|
| 3 payments or less | 16,023 39 % | 21,678 46 % | 15,692 35 % |
| 4-11 payments | 13,734 33 % | 12,446 27 % | 12,275 27 % |
| 12 payments or more ⁽¹⁾ | 11,486 28 % | 12,432 27 % | 17,382 38 % |
| ⁽²⁾ Total primary delinquent inventory | 41,243 100% | 46,556 100% | 45,349 100% |

(1) Approximately 42%, 43%, and 45% of the primary delinquent inventory with 12 payments or more delinquent has at least 36 payments delinquent as of March 31, 2018, December 31, 2017, and March 31, 2017, respectively.

(2) The majority of items removed from our delinquent inventory were due to commutations of NPLs during the three months ended March 31, 2018 had 12 or more payments delinquent as of December 31, 2017.

Pool insurance delinquent inventory decreased to 1,200 at March 31, 2018 from 1,309 at December 31, 2017, and 1,714 at March 31, 2017.

Claims paying practices

Our loss reserving methodology incorporates our estimates of future rescissions and curtailments. A variance between ultimate actual rescission and curtailment rates and our estimates, as a result of the outcome of litigation, settlements or other factors, could materially affect our losses. Our estimate of premiums to be refunded on expected future rescissions is accrued for separately and is included in "Other liabilities" on our consolidated balance sheets. For information about discussions and legal proceedings with customers with respect to our claims paying practices see Note 5 – "Litigation and Contingencies."

Note 13. Shareholders' Equity

Change in accounting principle

As described in Note 2 - "New Accounting Pronouncements," during the first quarter of 2018 the updated guidance of "Recognition and Measurement of Financial Assets and Financial Liabilities" became effective. The application of this guidance resulted in an immaterial cumulative effect adjustment to our 2018 beginning accumulated other comprehensive (loss) income and retained earnings to recognize unrealized gains on equity securities.

Shareholders Rights Agreement

Our Amended and Restated Rights Agreement dated July 23, 2015 ("the 2015 Agreement") seeks to diminish the risk that our ability to use our NOLs to reduce potential future federal income tax obligations may become substantially limited and to deter certain abusive takeover practices. The benefit of the NOLs would be substantially limited, and the timing of the usage of the NOLs could be substantially delayed, if we were to experience an "ownership change" as defined by Section 382 of the Internal Revenue Code.

Under the 2015 Agreement, each outstanding share of our Common Stock is accompanied by one Right. The “Distribution Date” occurs on the earlier of ten days after a public announcement that a person has become an “Acquiring Person,” or ten business days after a person announces or begins a tender offer in which consummation of such offer would result in a person becoming an “Acquiring Person.” An “Acquiring Person” is any person that becomes, by itself or together with its affiliates and associates, a beneficial owner of 5% or more of the shares of our Common Stock then outstanding, but excludes, among others, certain exempt and grandfathered persons as defined in the Agreement. The Rights are not exercisable until the Distribution Date. Each Right will initially entitle shareholders to buy one-tenth of one share of our Common Stock at a Purchase Price of \$45 per full share (equivalent to \$4.50 for each one-tenth share), subject to adjustment. Each exercisable Right (subject to certain limitations) will entitle its holder to purchase, at the Rights’ then-current Purchase Price, a number of our shares of Common Stock (or if after the Shares Acquisition Date, we are acquired in a business combination, common shares of the acquiror) having a market value at the time equal

Table of contents

to twice the Purchase Price. The Rights will expire on August 1, 2018, or earlier as described in the 2015 Agreement. The Rights are redeemable at a price of \$0.001 per Right at any time prior to the time a person becomes an Acquiring Person. Other than certain amendments, the Board of Directors may amend the Rights in any respect without the consent of the holders of the Rights.

On April 26, 2018, our Board of Directors approved amendments to the 2015 Agreement described above (as amended and restated, the “2018 Agreement”). The only material amendment made to the 2015 Agreement was an extension of the final expiration date until March 1, 2020. The approval and effectiveness of the 2018 Agreement is subject to shareholder approval at the Annual Meeting of Shareholders, scheduled to be held in July 2018. Until such shareholder approval, the 2015 Rights Agreement remains in effect.

Note 14. Share-Based Compensation

We have certain share-based compensation plans. Under the fair value method, compensation cost is measured at the grant date based on the fair value of the award and is recognized over the service period which generally corresponds to the vesting period. Awards under our plans generally vest over periods ranging from one to three years.

Table 14.1 shows the number of shares granted to employees and the weighted average fair value per share during the periods presented (shares in thousands).

Table 14.1

| Restricted stock grants | Three months ended March 31, | | | |
|--|------------------------------|---|-------------------|---|
| | 2018 | | 2017 | |
| | Shares Granted | Weighted Average Share Fair Value | Shares Granted | Weighted Average Share Fair Value |
| RSUs subject to performance conditions | 1,239 | \$ 15.80 | 1,237 | \$ 10.41 |
| RSUs subject only to service conditions | 412 | 15.71 | 395 | 10.41 |

Note 15. Statutory Information

Statutory Capital Requirements

The insurance laws of 16 jurisdictions, including Wisconsin, our domiciliary state, require a mortgage insurer to maintain a minimum amount of statutory capital relative to the risk in force (or a similar measure) in order for the mortgage insurer to continue to write new business. We refer to these requirements as the “State Capital Requirements.” While they vary among jurisdictions, the most common State Capital Requirements allow for a maximum risk-to-capital ratio of 25 to 1. A risk-to-capital ratio will increase if (i) the percentage decrease in capital exceeds the percentage decrease in insured risk, or (ii) the percentage increase in capital is less than the percentage increase in insured risk. Wisconsin does not regulate capital by using a risk-to-capital measure but instead requires a minimum policyholder position (“MPP”). The “policyholder position” of a mortgage insurer is its net worth or surplus, contingency reserve and a portion of the reserves for unearned premiums.

At March 31, 2018, MGIC’s risk-to-capital ratio was 9.4 to 1, below the maximum allowed by the jurisdictions with State Capital Requirements, and its policyholder position was \$2.2 billion above the required MPP of \$1.2 billion. In

calculating our risk-to-capital ratio and MPP, we are allowed full credit for the risk ceded under our reinsurance transactions with a group of unaffiliated reinsurers. It is possible that under the revised State Capital Requirements discussed below, MGIC will not be allowed full credit for the risk ceded to the reinsurers. If MGIC is not allowed an agreed level of credit under either the State Capital Requirements or the financial requirements of the PMIERS, MGIC may terminate the reinsurance transactions, without penalty. At this time, we expect MGIC to continue to comply with the current State Capital Requirements; however, you should read the rest of these financial statement footnotes for information about matters that could negatively affect such compliance.

At March 31, 2018, the risk-to-capital ratio of our combined insurance operations (which includes a reinsurance affiliate) was 10.3 to 1. Reinsurance agreements with an affiliate permit MGIC to write insurance

Table of contents

with a higher coverage percentage than it could on its own under certain state-specific requirements. A higher risk-to-capital ratio on a combined basis may indicate that, in order for MGIC to continue to utilize reinsurance agreements with its affiliate, additional capital contributions to the reinsurance affiliate could be needed.

The NAIC plans to revise the minimum capital and surplus requirements for mortgage insurers that are provided for in its Mortgage Guaranty Insurance Model Act. In May 2016, a working group of state regulators released an exposure draft of a risk-based capital framework to establish capital requirements for mortgage insurers, although no date has been established by which the NAIC must propose revisions to the capital requirements and certain items have not yet been completely addressed by the framework, including the treatment of ceded risk, minimum capital floors, and action level triggers. Currently, we believe that the PMIERS contain the more restrictive capital requirements in most circumstances.

While MGIC currently meets the State Capital Requirements of Wisconsin and all other jurisdictions, it could be prevented from writing new business in the future in all jurisdictions if it fails to meet the State Capital Requirements of Wisconsin, or it could be prevented from writing new business in a particular jurisdiction if it fails to meet the State Capital Requirements of that jurisdiction, and in each case MGIC does not obtain a waiver of such requirements. It is possible that regulatory action by one or more jurisdictions, including those that do not have specific State Capital Requirements, may prevent MGIC from continuing to write new insurance in such jurisdictions.

If we are unable to write business in all jurisdictions, lenders may be unwilling to procure insurance from us anywhere. In addition, a lender's assessment of the future ability of our insurance operations to meet the State Capital Requirements or the PMIERS may affect its willingness to procure insurance from us. A possible future failure by MGIC to meet the State Capital Requirements or the PMIERS will not necessarily mean that MGIC lacks sufficient resources to pay claims on its insurance liabilities. While we believe MGIC has sufficient claims paying resources to meet its claim obligations on its insurance in force on a timely basis, you should read the rest of these financial statement footnotes for information about matters that could negatively affect MGIC's claims paying resources.

Dividend restrictions

In the first quarter of 2018, MGIC paid a \$50 million dividend to our holding company. MGIC is subject to statutory regulations as to payment of dividends. The maximum amount of dividends that MGIC may pay in any twelve-month period without such dividends being subject to regulatory disapproval by the OCI is the lesser of adjusted statutory net income or 10% of statutory policyholders' surplus as of the preceding calendar year end. Adjusted statutory net income is defined for this purpose to be the greater of statutory net income, net of realized investment gains, for the calendar year preceding the date of the dividend or statutory net income, net of realized investment gains, for the three calendar years preceding the date of the dividend less dividends paid within the first two of the preceding three calendar years. The OCI recognizes only statutory accounting principles prescribed, or practices permitted by the State of Wisconsin for determining and reporting the financial condition and results of operations of an insurance company. The OCI has adopted certain prescribed accounting practices that differ from those found in other states. Specifically, Wisconsin domiciled companies record changes in the contingency reserves through the income statement as a change in underwriting deduction. As a result, in periods in which MGIC is increasing contingency reserves, statutory net income is lowered. For the year ended December 31, 2017, MGIC's statutory net income was reduced by \$473 million to account for the increase in contingency reserves.

Table of contents

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

Introduction

The following is management’s discussion and analysis of the financial condition and results of operations of MGIC Investment Corporation for the first quarter of 2018. As used below, “we” and “our” refer to MGIC Investment Corporation’s consolidated operations. This form 10-Q should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our Annual Report on Form 10-K for the year ended December 31, 2017. See the “Glossary of terms and acronyms” for definitions and descriptions of terms used throughout this MD&A. The Risk Factors contained in Item 1A discuss trends and uncertainties affecting us and are an integral part of the MD&A.

Forward Looking and Other Statements

As discussed under “Forward Looking Statements and Risk Factors” below, actual results may differ materially from the results contemplated by forward looking statements. 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. Therefore no reader of this document should rely on these statements being current as of any time other than the time at which this document was filed with the Securities and Exchange Commission.

Through our subsidiary MGIC, we are a leading provider of PMI in the United States, as measured by \$197.5 billion of primary IIF at March 31, 2018.

Table of contents

Overview

| | Three Months Ended March 31, | | |
|--|---|---------|-------------|
| | (In millions, except per share data, unaudited) | | |
| | 2018 | 2017 | % Change |
| Summary financial results of MGIC Investment Corporation | | | |
| Selected statement of operations data | | | |
| Total revenues | \$265.8 | \$260.9 | 2 |
| Losses incurred, net | 23.9 | 27.6 | (13) |
| Other underwriting and operating expenses, net | 46.1 | 40.8 | 13 |
| Income before tax | 180.0 | 174.0 | 3 |
| Provision for income taxes | 36.4 | 84.2 | (57) |
| Net income | 143.6 | 89.8 | 60 |
| Diluted income per share | \$0.38 | \$0.24 | 58 |
| Non-GAAP Financial Measures ⁽¹⁾ | | | |
| Adjusted pre-tax operating income | \$180.4 | \$174.1 | 4 |
| Adjusted net income | 144.6 | 117.1 | 23 |

operating
income
Adjusted
net
operating
income \$0.38 \$0.31 23
per
diluted
share

(1) See “Explanation and reconciliation of our use of Non-GAAP financial measures.”

Summary of first quarter 2018 results

Comparative quarterly results

We recorded first quarter 2018 net income of \$143.6 million, or \$0.38 per diluted share. Net income increased by \$53.8 million compared with net income of \$89.8 million in the prior year, primarily reflecting the non-recurring additional tax provision recorded in the prior year period for the expected settlement of our IRS litigation and the lower statutory income tax rate in the current year period. In addition, our diluted weighted average shares outstanding decreased from the prior year due to reductions in our convertible debt outstanding. These factors resulted in a 58% increase in diluted income per share.

Adjusted net operating income for the first quarter 2018 was \$144.6 million (Q1 2017: \$117.1 million) and adjusted net operating income per diluted share was \$0.38 (Q1 2017: \$0.31). The 23% increase in adjusted net operating income reflects the lower statutory income tax rate in the current year period and lower losses incurred, net. In addition to the increase in adjusted net operating income, our diluted weighted average shares outstanding decreased from the prior year. These factors resulted in a 23% increase in adjusted net operating income per diluted share.

Losses incurred, net were \$23.9 million, down 13% compared to the prior year primarily due to an estimated claim rate of 9% on new delinquent notices received in the current year period, which declined from 10.5% in the prior year period. Our estimated claim rate on new notices reflects the current economic environment and anticipated cure activity on the notices received.

Other underwriting and operating expenses, net were \$46.1 million, an increase of 13% compared to the prior year driven by higher share-based compensation expenses and non-executive compensation.

The decrease in our provision for income taxes in the first quarter of 2018 as compared to the same period in the prior year was due to the additional provision recorded in the first quarter of 2017 for the expected settlement of our IRS litigation and a decrease in the statutory income tax rate.

In March 2018, MGIC paid a dividend of \$50 million to our holding company and we expect MGIC to continue to pay quarterly dividends of at least the amount paid in the first quarter.

See “Consolidated Results of Operations” below for additional discussion of our results for the three months ended March 31, 2018 compared to the prior year period.

Table of contents

Capital

Share repurchase program

On April 26, 2018, our board of directors authorized a share repurchase program under which we may repurchase up to \$200 million of our common stock through the end of 2019. Repurchases may be made from time to time on the open market or through privately negotiated transactions. The repurchase program may be suspended for periods or discontinued at any time. As of March 31, 2018, our holding company had approximately \$257 million in cash and investments and we expect to fund the purchases with these resources. As of March 31, 2018, we had approximately 371.3 million shares of common stock outstanding.

GSEs

We must comply with the PMIERS to be eligible to insure loans purchased by the GSEs and insured with PMI. In addition to their financial requirements, the PMIERS include business, quality control and certain transaction approval requirements.

If MGIC ceases to be eligible to insure loans purchased by one or both of the GSEs, it would significantly reduce the volume of our NIW. Factors that may negatively impact MGIC's ability to continue to comply with the financial requirements of PMIERS include the following:

On December 18, 2017, we received a summary of proposed changes to the PMIERS that are being recommended to the FHFA by the GSEs. Once the PMIERS are finalized, we expect a six-month implementation period before the revised PMIERS are effective. We expect that effectiveness will not be earlier than the fourth quarter of 2018. If the GSE-recommended changes are adopted with an effective date in the fourth quarter of 2018, we expect that at the effective date, MGIC would continue to have an excess of Available Assets over Minimum Required Assets, although this excess would be materially lower than it was at March 31, 2018 under the existing PMIERS, and that MGIC would continue to be able to pay quarterly dividends to our holding company at the \$50 million quarterly rate at which they were paid in the first quarter of 2018.

We have non-disclosure obligations to each of the GSEs and cannot provide further comment on the specific provisions of the GSE-recommended changes other than as described above. Until the GSEs and/or FHFA provide public disclosure of proposed or final changes to the existing PMIERS, we do not plan to update or correct any of the disclosure above or provide any additional disclosure regarding any modifications that may occur in the GSE-recommended changes to PMIERS.

- Our future operating results may be negatively impacted by the matters discussed in our risk factors. Such matters could decrease our revenues, increase our losses or require the use of assets, thereby creating a shortfall in Available Assets.

• Should capital be needed by MGIC in the future, capital contributions from our holding company may not be available due to competing demands on holding company resources, including for repayment of debt.

While on an overall basis, the amount of Available Assets MGIC must hold in order to continue to insure GSE loans increased under the PMIERS over what state regulation currently requires, our reinsurance transactions mitigate the negative effect of the PMIERS on our returns.

State Regulations

The insurance laws of 16 jurisdictions, including Wisconsin, our domiciliary state, require a mortgage insurer to maintain a minimum amount of statutory capital relative to its RIF (or a similar measure) in order for the mortgage insurer to continue to write new business. We refer to these requirements as the "State Capital Requirements." While they vary among jurisdictions, the most common State Capital Requirements allow for a maximum risk-to-capital ratio of 25 to 1. A risk-to-capital ratio will increase if (i) the percentage decrease in capital exceeds the percentage decrease in insured risk, or (ii) the percentage increase in capital is less than the percentage increase in insured risk. Wisconsin does not regulate capital by using a risk-to-capital measure but instead requires an MPP.

Table of contents

At March 31, 2018, MGIC's risk-to-capital ratio was 9.4 to 1, below the maximum allowed by the jurisdictions with State Capital Requirements, and its policyholder position was \$2.2 billion above the required MPP of \$1.2 billion. In calculating our risk-to-capital ratio and MPP, we are allowed full credit for the risk ceded under our reinsurance transactions with a group of unaffiliated reinsurers. It is possible that under the revised State Capital Requirements discussed below, MGIC will not be allowed full credit for the risk ceded to the reinsurers. If MGIC is not allowed an agreed level of credit under either the State Capital Requirements or the PMIERS, MGIC may terminate the reinsurance transactions, without penalty. At this time, we expect MGIC to continue to comply with the current State Capital Requirements; however, refer to our risk factor titled "State capital requirements may prevent us from continuing to write new insurance on an uninterrupted basis" for more information about matters that could negatively affect such compliance.

At March 31, 2018, the risk-to-capital ratio of our combined insurance operations (which includes a reinsurance affiliate) was 10.3 to 1. Reinsurance transactions with our affiliate permit MGIC to write insurance with a higher coverage percentage than it could on its own under certain state-specific requirements.

The NAIC plans to revise the minimum capital and surplus requirements for mortgage insurers that are provided for in its Mortgage Guaranty Insurance Model Act. A working group of state regulators has been considering since 2016 a risk-based capital framework to establish capital requirements for mortgage insurers, although no date has been established by which the NAIC must propose revisions to the capital requirements and certain items have not yet been completely addressed by the framework, including the treatment of ceded risk, minimum capital floors, and action level triggers. Currently we believe that the PMIERS contain the more restrictive capital requirements in most circumstances.

GSE reform

The FHFA has been the conservator of the GSEs since 2008 and has the authority to control and direct their operations. The increased role that the federal government has assumed in the residential housing finance system through the GSE conservatorship may increase the likelihood that the business practices of the GSEs change in ways that have a material adverse effect on us and that the charters of the GSEs are changed by new federal legislation. In the past, members of Congress have introduced several bills intended to change the business practices of the GSEs and the FHA; however, no legislation has been enacted. The Administration has indicated that the conservatorship of the GSEs should end; however, it is unclear whether and when that would occur and how that would impact us. As a result of the matters referred to above, it is uncertain what role the GSEs, FHA and private capital, including PMI, will play in the residential housing finance system in the future or the impact of any such changes on our business. In addition, the timing of the impact of any resulting changes on our business is uncertain. Most meaningful changes would require Congressional action to implement and it is difficult to estimate when Congressional action would be final and how long any associated phase-in period may last.

For additional information about the business practices of the GSEs, see our risk factor titled "Changes in the business practices of the GSEs, federal legislation that changes their charters or a restructuring of the GSEs could reduce our revenues or increase our losses."

Loan modifications and other similar programs

The federal government, including through the U.S. Department of the Treasury and the GSEs, and several lenders have modification and refinance programs to make outstanding loans more affordable to borrowers with the goal of reducing the number of foreclosures. These programs included HAMP, which expired at the end of 2016, and HARP, which is scheduled to expire at the end of 2018. The GSEs have introduced other loan modifications programs to replace HAMP.

From 2008 through 2012, we were notified of modifications that cured delinquencies that, had they become paid claims, would have resulted in a material increase in our incurred losses. More recently, the number of modifications

has decreased significantly. Nearly all of the reported loan modifications were for loans insured in 2009 and prior.

Table of contents

We cannot determine the total benefit we may derive from loan modification programs, particularly given the uncertainty around the re-default rates for defaulted loans that have been modified. Our loss reserves do not account for potential re-defaults of current loans.

As shown in the following table, as of March 31, 2018 approximately 15% of our primary RIF has been modified.

| Modifications | Policy year | HARP Modifications ⁽¹⁾ | | HAMP & Other Modifications | |
|----------------|-------------|-----------------------------------|---|----------------------------|---|
| 2003 and prior | 2003 | 10.9 | % | 41.5 | % |
| 2004 | 2004 | 19.2 | % | 44.6 | % |
| 2005 | 2005 | 25.3 | % | 42.4 | % |
| 2006 | 2006 | 29.1 | % | 40.3 | % |
| 2007 | 2007 | 40.6 | % | 31.6 | % |
| 2008 | 2008 | 56.1 | % | 18.9 | % |
| 2009 | 2009 | 37.8 | % | 5.8 | % |
| 2010 | 2010 | | | | |
| - Q1 2018 | - Q1 2018 | — | % | 0.2 | % |
| Total | Total | 7.7 | % | 7.2 | % |

⁽¹⁾ Includes proprietary programs that are substantially the same as HARP.

As of March 31, 2018, based on loan count, the loans associated with 97.1% of HARP modifications and 77.5% of HAMP and other modifications were current.

Factors affecting our results

Our results of operations are affected by:

Premiums written and earned

Premiums written and earned in a year are influenced by:

NIW, which increases IIF. Many factors affect NIW, including the volume of low down payment home mortgage originations and competition to provide credit enhancement on those mortgages from the FHA, the VA, other mortgage insurers, GSE programs that may reduce or eliminate the demand for mortgage insurance and other alternatives to mortgage insurance. NIW does not include loans previously insured by us that are modified, such as loans modified under HARP.

Cancellations, which reduce IIF. Cancellations due to refinancings are affected by the level of current mortgage interest rates compared to the mortgage coupon rates throughout the in force book, current home values compared to values when the loans in the in force book were insured and the terms on which mortgage credit is available. Home price appreciation can give homeowners the right to cancel mortgage insurance on their loans if sufficient home equity is achieved. Cancellations also result from policy rescissions, which require us to return any premiums received on the rescinded policies and claim payments, which require us to return any premium received on the related policies from the date of default on the insured loans. Cancellations of single premium policies, which are generally non-refundable, result in immediate recognition of any remaining unearned premium.

•

Premium rates, which are affected by product type, competitive pressures, the risk characteristics of the insured loans, the percentage of coverage on the insured loans, and PMIERs capital requirements. The substantial majority of our monthly and annual mortgage insurance premiums are under premium plans for which, for the first ten years of the policy, the amount of premium is determined by multiplying the initial premium rate by the original loan balance; thereafter, the premium rate resets to a lower rate used for the remaining life of the policy. However, for loans that have utilized HARP, the initial ten-year period resets as of the date of the HARP transaction. The remainder of our monthly and annual premiums are under premium plans for which premiums are determined by a fixed percentage of the loan's amortizing balance over the life of the policy.

Table of contents

• Premiums ceded, net of a profit commission, under reinsurance agreements. See Note 4 - “Reinsurance” to our consolidated financial statements for a discussion of our reinsurance agreements.

Premiums are generated by the insurance that is in force during all or a portion of the period. A change in the average IIF in the current period compared to an earlier period is a factor that will increase (when the average in force is higher) or reduce (when it is lower) premiums written and earned in the current period, although this effect may be enhanced (or mitigated) by differences in the average premium rate between the two periods as well as by premiums that are returned or expected to be returned in connection with claim payments and rescissions, and premiums ceded under reinsurance agreements. Also, NIW and cancellations during a period will generally have a greater effect on premiums written and earned in subsequent periods than in the period in which these events occur.

Investment income

Our investment portfolio is composed principally of investment grade fixed income securities. The principal factors that influence investment income are the size of the portfolio and its yield. As measured by amortized cost (which excludes changes in fair value, such as from changes in interest rates), the size of the investment portfolio is mainly a function of cash generated from (or used in) operations, such as NPW, investment income, net claim payments and expenses, and cash provided by (or used for) non-operating activities, such as debt or stock issuances or repurchases.

Losses incurred

Losses incurred are the current expense that reflects estimated payments that will ultimately be made as a result of delinquencies on insured loans. As explained under “Critical Accounting Policies” in our 10-K MD&A, except in the case of a premium deficiency reserve, we recognize an estimate of this expense only for delinquent loans. The level of new delinquencies has historically followed a seasonal pattern, with new delinquencies in the first part of the year lower than new delinquencies in the latter part of the year, though this pattern can be affected by the state of the economy and local housing markets. Losses incurred are generally affected by:

• The state of the economy, including unemployment and housing values, each of which affects the likelihood that loans will become delinquent and whether loans that are delinquent cure their delinquency.

• The product mix of the in force book, with loans having higher risk characteristics generally resulting in higher delinquencies and claims.

• The size of loans insured, with higher average loan amounts tending to increase losses incurred.

• The percentage of coverage on insured loans, with deeper average coverage tending to increase losses incurred.

The rate at which we rescind policies or curtail claims. Our estimated loss reserves incorporate our estimates of future rescissions of policies and curtailments of claims, and reversals of rescissions and curtailments. We collectively refer to such rescissions and denials as “rescissions” and variations of this term. We call reductions to claims “curtailments.”

The distribution of claims over the life of a book. Historically, the first few years after loans are originated are a period of relatively low claims, with claims increasing substantially for several years subsequent and then declining, although persistency, the condition of the economy, including unemployment and housing prices, and other factors can affect this pattern. For example, a weak economy or housing value declines can lead to claims from older books increasing, continuing at stable levels or experiencing a lower rate of decline. See further information under “Mortgage insurance earnings and cash flow cycle” below.

• Losses ceded under reinsurance agreements. See Note 4 - “Reinsurance” to our consolidated financial statements for a discussion of our reinsurance agreements.

Table of contents

Underwriting and other expenses

Most of our operating expenses are fixed, with some variability due to contract underwriting volume. Contract underwriting generates fee income included in “Other revenue.” Underwriting and other expenses are net of any ceding commission associated with our reinsurance agreements. See Note 4 - “Reinsurance” to our consolidated financial statements for a discussion of our reinsurance agreements.

Interest expense

Interest expense reflects the interest associated with our outstanding debt obligations discussed in Note 3 - “Debt” to our consolidated financial statements and under “Liquidity and Capital Resources” below.

Other

Certain activities that we do not consider being part of our fundamental operating activities, may also impact our results of operations and are described below.

Net realized investment gains (losses)

Realized gains and losses are a function of the difference between the amount received on the sale of a security and the security’s cost basis, as well as any “other than temporary” impairments (“OTTI”) 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.

Loss on debt extinguishment

At times, we may undertake activities to enhance our capital position, improve our debt profile and/or reduce potential dilution from our outstanding convertible debt. Extinguishing our outstanding debt obligations early through these discretionary activities may result in losses primarily driven by the payment of consideration in excess of our carrying value.

Refer to “Explanation and reconciliation of our use of Non-GAAP financial measures” below to understand how these items impact our evaluation of our core financial performance.

Mortgage insurance earnings and cash flow cycle

In general, the majority of any underwriting profit 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 following the year the book was written. Subsequent years of a book may result in either underwriting profit or underwriting losses. This pattern of results typically 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 increasing losses. The typical pattern is also a function of premium rates generally resetting to lower levels after ten years.

Table of contents

Explanation and reconciliation of our use of non-GAAP financial measures

Non-GAAP financial measures

We believe that use of the Non-GAAP measures of adjusted pre-tax operating income (loss), adjusted net operating income (loss) and adjusted net operating income (loss) per diluted share facilitate the evaluation of the company's core financial performance thereby providing relevant information to investors. These measures are not recognized in accordance with GAAP and should not be viewed as alternatives to GAAP measures of performance.

Adjusted pre-tax operating income (loss) is defined as GAAP income (loss) before tax, excluding the effects of net realized investment gains (losses), gain (loss) on debt extinguishment, net impairment losses recognized in income (loss) and infrequent or unusual non-operating items where applicable.

Adjusted net operating income (loss) is defined as GAAP net income (loss) excluding the after-tax effects of net realized investment gains (losses), gain (loss) on debt extinguishment, net impairment losses recognized in income (loss), and infrequent or unusual non-operating items where applicable. The amounts of adjustments to components of pre-tax operating income (loss) are tax effected using a federal statutory tax rate of 21% for 2018 and 35% for 2017.

Adjusted net operating income (loss) per diluted share is calculated in a manner consistent with the accounting standard regarding earnings per share by dividing (i) adjusted net operating income (loss) after making adjustments for interest expense on convertible debt, whenever the impact is dilutive by (ii) diluted weighted average common shares outstanding, which reflects share dilution from unvested restricted stock units and from convertible debt when dilutive under the "if-converted" method.

Although adjusted pre-tax operating income (loss) and adjusted net operating income (loss) exclude certain items that have occurred in the past and are expected to occur in the future, the excluded items represent items that are: (1) not viewed as part of the operating performance of our primary activities; or (2) impacted by both discretionary and other economic or regulatory factors and are not necessarily indicative of operating trends, or both. These adjustments, along with the reasons for their treatment, are described below. Trends in the profitability of our fundamental operating activities can be more clearly identified without the fluctuations of these adjustments. Other companies may calculate these measures differently. Therefore, their measures may not be comparable to those used by us.

Net realized investment gains (losses). The recognition of net realized investment gains or losses can vary (1) significantly across periods as the timing of individual securities sales is highly discretionary and is influenced by such factors as market opportunities, our tax and capital profile, and overall market cycles.

Gains and losses on debt extinguishment. Gains and losses on debt extinguishment result from discretionary (2) activities that are undertaken to enhance our capital position, improve our debt profile, and/or reduce potential dilution from our outstanding convertible debt.

Net impairment losses recognized in earnings. The recognition of net impairment losses on investments can vary (3) significantly in both size and timing, depending on market credit cycles, individual issuer performance, and general economic conditions.

Infrequent or unusual non-operating items. Income tax expense related to our IRS dispute is related to past (4) transactions which are non-recurring in nature and are not part of our primary operating activities.

Table of contents

| | | | | | | |
|---|---|-------------------------|-----------------|------------|-------------------------|-----------------|
| Non-GAAP reconciliations | Reconciliation of Income before tax / Net income to Adjusted pre-tax operating income / Adjusted net operating income | | | | | |
| | Three Months Ended March 31, | | | | | |
| | 2018 | | | 2017 | | |
| (In thousands, except per share amounts) | Pre-tax | Tax provision (benefit) | Net (after-tax) | Pre-tax | Tax provision (benefit) | Net (after-tax) |
| Income before tax / Net income | \$ 180,025 | \$ 36,388 | \$ 143,637 | \$ 173,957 | \$ 84,159 | \$ 89,798 |
| Adjustments: | | | | | | |
| Additional income tax provision related to IRS litigation | — | (708) | 708 | — | (27,224) | 27,224 |
| Net realized investment losses | 329 | 69 | 260 | 125 | 44 | 81 |
| Adjusted pre-tax operating income / Adjusted net operating income | \$ 180,354 | \$ 35,749 | \$ 144,605 | \$ 174,082 | \$ 56,979 | \$ 117,103 |
| | Reconciliation of Net income per diluted share to Adjusted net operating income per diluted share | | | | | |
| Weighted average diluted shares outstanding | | | 391,562 | | | 402,175 |
| Net income per diluted share | | | \$ 0.38 | | | \$ 0.24 |
| Additional income tax provision related to IRS litigation | | | — | | | 0.07 |
| Net realized investment losses | | | — | | | — |
| Adjusted net operating income per diluted share | | | \$ 0.38 | | | \$ 0.31 |

Table of contents

Mortgage Insurance Portfolio

New insurance written

According to Inside Mortgage Finance and GSE estimates, total mortgage originations for the first quarter of 2018 decreased from the respective prior year period primarily due to a decline in refinance originations. The total amount of mortgage originations is generally influenced by the level of new and existing home sales, the percentage of homes purchased for cash, and the level of refinance activity. PMI market share of total mortgage originations is generally influenced by the mix of purchase and refinance originations as PMI market share is 3-4 times higher for purchase originations than refinance originations. PMI market share is also impacted by the market share of total originations for FHA, VA, and USDA.

NIW for the first quarter of 2018 was \$10.6 billion (Q1 2017: \$9.3 billion) and continued to have what we believe are favorable underlying risk characteristics. The percentage of NIW with DTI ratios greater than 45% was approximately 20% during the first quarter of 2018, which was relatively consistent with the fourth quarter of 2017, but up significantly from approximately 6% in the first quarter of 2017. Under our 2018 QSR Transactions, we may cede risk associated with NIW with DTI ratios between 45% and 50%; however, the amount of risk we may cede in connection with such NIW in any quarter is limited to a percentage of all risk written and that percentage is materially below the percentage of risk written represented by such loans in the first quarter of 2018. To mitigate our risk from the increase in NIW written on loans with DTI ratios greater than 45%, effective in March 2018 we changed our underwriting guidelines to require loans with DTI ratios greater than 45% to have a FICO score of at least 700. As a result of this change and a change in GSE underwriting requirements, we expect loans with DTI ratios greater than 45% will be a lower percentage of our NIW. We are continuing to monitor our exposure to such loans and may take further action. The percentage of purchase mortgages insured increased in the three months ended March 31, 2018 compared to the same period of the prior year because the level of refinance transactions declined as mortgage interest rates, on average, have increased during the first quarter of 2018.

The following tables present characteristics of our NIW for the three months ended March 31, 2018 and 2017.

| Primary NIW by FICO score | Three Months Ended March 31, | |
|---------------------------|------------------------------------|----------------------------------|
| | (% of primary NIW) 2018 | (% of primary NIW) 2017 |
| 760 and greater | 41.4% | 42.4% |
| 740 - 759 | 17.1% | 16.5% |
| 720 - 739 | 14.6% | 14.2% |
| 700 - 719 | 11.7% | 11.8% |
| 680 - 699 | 7.7 % | 7.9 % |
| 660 - 679 | 4.0 % | 4.0 % |
| 640 - 659 | 2.3 % | 2.3 % |
| | 1.1 % | 0.9 % |

639 and
less

| Loan-to-Value | Three Months Ended March 31, | |
|----------------------------------|------------------------------------|-------|
| (% of primary NIW) | 2018 | 2017 |
| 95.01% and above 90.01% | 13.1% | 7.9% |
| to 95.00% | 44.1% | 47.2% |
| 85.01% to 90.00% | 29.0% | 30.3% |
| 80.01% to 85% | 13.8% | 14.6% |

Table of contents

| Policy payment type | Three Months Ended March 31, | |
|--------------------------|------------------------------------|-------|
| | 2018 | 2017 |
| (% of primary NIW) | | |
| Monthly premiums | 80.4% | 83.1% |
| Single premiums | 19.4% | 16.6% |
| Annual premiums | 0.2 % | 0.3 % |

| Type of mortgage | Three Months Ended March 31, | |
|--------------------------|------------------------------------|-------|
| | 2018 | 2017 |
| (% of primary NIW) | | |
| Purchases | 88.2% | 83.4% |
| Refinances | 11.8% | 16.6% |

Insurance and risk in force

The amount of our IIF and RIF is impacted by the amount of NIW and cancellations of primary IIF during the period. Cancellation activity is primarily due to refinancing activity, but is also impacted by rescissions, cancellations due to claim payment, and policies cancelled when borrowers achieve the required amount of home equity. Refinancing activity has historically been affected by the level of mortgage interest rates and the level of home price appreciation. Cancellations generally move inversely to the change in the direction of interest rates, although they generally lag a change in direction.

Persistency

Our persistency was 80.2% at March 31, 2018 compared to 80.1% at December 31, 2017 and 76.9% at March 31, 2017. Since 2000, our year-end persistency ranged from a high of 84.7% at December 31, 2009 to a low of 47.1% at December 31, 2003. With the current and expected level of mortgage interest rates we expect a low level of refinance activity and that our persistency will increase gradually in subsequent periods.

| IIF and RIF | Three Months Ended March 31, | |
|----------------------------|---------------------------------|---------|
| | 2018 | 2017 |
| (In billions) | | |
| NIW | \$10.6 | \$9.3 |
| Cancellations | (8.0) | (7.8) |
| Increase in primary IIF | \$2.6 | \$1.5 |
| (In billions) | 2018 | 2017 |
| Direct primary IIF | \$197.5 | \$183.5 |

as of March
 31,
 Direct
 primary RIF \$50.9 \$47.5
 as of March
 31,

Credit profile of our primary RIF

The proportion of our total primary RIF written after 2008 has been steadily increasing in proportion to our total primary RIF. Our 2009 and later books possess significantly improved risk characteristics when compared to our 2005-2008 origination years. The loans we insured beginning in 2009, on average, have substantially higher FICO scores and lower LTVs than those insured in 2005-2008. The credit profile of our pre-2009 RIF has benefited from programs such as HARP. HARP allows borrowers who are not delinquent, but who may not otherwise be able to refinance their loans under the current GSE underwriting standards due to, for example, the current LTV exceeding 100%, to refinance and lower their note rate. Loans associated with 97.1% of all of our HARP modifications were current as of March 31, 2018. The aggregate of our 2009-2018 books and our HARP modifications accounted for approximately 87% of our total primary RIF at March 31, 2018.

Table of contents

| Primary RIF (\$ in billions) | March 31, 2018 | | December 31, 2017 | | March 31, 2017 | |
|------------------------------|-------------------|-------------|----------------------|-------------|-------------------|-------------|
| | RIF | % of RIF | RIF | % of RIF | RIF | % of RIF |
| 2009+ | \$40,350 | 79 % | \$39,248 | 78 % | \$34,298 | 72 % |
| 2005 - 2008 (HARP) | 3,642 | 7 % | 3,773 | 7 % | 4,353 | 9 % |
| Other years (HARP) | 291 | 1 % | 308 | 1 % | 378 | 1 % |
| Subtotal | 44,283 | 87 % | 43,330 | 86 % | 39,029 | 82 % |
| 2005- 2008 (Non-HARP) | 5,612 | 11 % | 5,894 | 12 % | 7,093 | 15 % |
| Other years (Non-HARP) | 1,044 | 2 % | 1,095 | 2 % | 1,399 | 3 % |
| Subtotal | 6,656 | 13 % | 6,989 | 14 % | 8,492 | 18 % |
| Total Primary RIF | \$50,939 | 100 % | \$50,319 | 100 % | \$47,521 | 100 % |

Pool insurance

MGIC has written no new pool insurance since 2008, however, for a variety of reasons, including responding to capital market alternatives to PMI and customer demands, MGIC may write pool risk in the future. Our direct pool risk in force was \$455 million (\$233 million on pool policies with aggregate loss limits and \$222 million on pool policies without aggregate loss limits) at March 31, 2018 compared to \$471 million (\$236 million on pool policies with aggregate loss limits and \$235 million on pool policies without aggregate loss limits) at December 31, 2017. If claim payments associated with a specific pool reach the aggregate loss limit, the remaining IIF within the pool would be cancelled and any remaining delinquencies under the pool would be removed from our delinquent inventory.

Table of contents

Consolidated Results of Operations

The following section of the MD&A provides a comparative discussion of MGIC Investment Corporation's Consolidated Results of Operations for the three months ended March 31, 2018 and 2017.

Revenues

| Revenues (in millions) | Three Months Ended March 31, | | |
|--|---------------------------------|---------|-------------|
| | 2018 | 2017 | % Change |
| Net premiums written | \$236.9 | \$236.7 | — |
| Net premiums earned | \$232.1 | \$229.1 | 1 |
| Investment income, net of expenses | 32.1 | 29.5 | 9 |
| Net realized investment losses | (0.3) | (0.1) | N/M |
| Other revenue | 1.9 | 2.4 | (21) |
| Total revenues | \$265.8 | \$260.9 | 2 |

Net premiums written and earned

NPW and NPE were relatively unchanged from the prior year as lower premium rates partially offset a larger average IIF and the amount of ceded premiums increased. The increase in ceded premiums was driven by a higher percentage of our NIW having LTVs 95% or greater and/or DTI ratios greater than 45%, both of which have higher premiums, and we ceded a higher percentage of such loans under our 2018 QSR Transaction than under our other QSR Transactions.

See "Overview - Factors Affecting Our Results" above for additional factors that influenced the amount of net premiums written and earned during the period.

Premium yield

Premium yield (NPE divided by average IIF) decreased from the prior year period to 47.3 basis points (Q1 2017: 50.1 basis points) and is influenced by a number of key drivers, which have a varying impact from period to period.

The decline in our premium yield compared to the prior year period reflects:

- A larger percentage of our IIF from book years with lower premium rates due to a decline in premium rates in recent periods and certain policies undergoing premium rate resets on their ten-year anniversaries; offset in part by,
- less of an adverse impact from premium refunds primarily due to lower claim activity.

In April 2018 we announced a reduction to our borrower-paid premium rates, which will contribute to a lower effective premium yield in future periods. Based upon the mix of our NIW in the first quarter of 2018, approximately 78% of that NIW would have been subject to the price reduction, and the weighted average direct premium rate on that portion of our NIW would have been approximately 11% lower. Applying the reduced premiums would have resulted in an overall direct premium rate decrease for all NIW in the first quarter of 2018 of approximately 9%. The new borrower paid premium rates are scheduled to become effective on June 4, 2018. Lender-paid single premium rates were not changed by our announcement.

Table of contents

The following table reconciles our premium yield for the three months ended March 31, 2018 from the respective prior year period.

| | | |
|--|-------------------|-------|
| Premium yield | (in basis points) | |
| Premium yield | | |
| - March 31, 2017 | | 50.1 |
| Reconciliation: | | |
| Change in premium rates | | (3.6) |
| Change in premium refunds and accruals | | 0.8 |
| Single premium policy persistency | | 0.1 |
| Reinsurance | | (0.1) |
| Premium yield | | |
| - March 31, 2018 | | 47.3 |

Reinsurance agreements

Our quota share reinsurance affects various lines of our statements of operations and therefore we believe it should be analyzed by reviewing its total effect on our pre-tax income, described as follows.

• We cede a fixed percentage of premiums on insurance covered by the agreements.

We receive the benefit of a profit commission through a reduction in the premiums we cede. The profit commission varies directly and inversely with the level of losses on a “dollar for dollar” basis and is eliminated at levels of losses that we do not expect to occur. As a result, lower levels of losses result in a higher profit commission and less benefit from ceded losses; higher levels of losses result in more benefit from ceded losses and a lower profit commission (or for levels of losses we do not expect, its elimination).

• We receive the benefit of a ceding commission through a reduction in underwriting expenses equal to 20% of premiums ceded (before the effect of the profit commission).

• We cede a fixed percentage of losses incurred on insurance covered by the agreements.

The blended pre-tax cost of reinsurance under our different transactions is less than 6% (but will decrease if losses are materially higher than we expect). This blended pre-tax cost is derived by dividing the reduction in our pre-tax net income on loans covered by reinsurance by our direct (that is, without reinsurance) premiums from such loans. Although the pre-tax cost of the reinsurance under each transaction is generally constant, the effect of the reinsurance on the various components of pre-tax income discussed above will vary from period to period, depending on the level of ceded losses.

The amount of our NIW subject to our QSR Transactions as shown in table below will vary from period to period due to loan level exclusion terms. For example, our 2018 QSR Transaction excludes loans with LTV ratios of 85% and below, but increases the percentage of risk written with the following loan level characteristics subject to coverage when compared to our 2017 QSR Transaction: (1) LTV ratios of 95% and greater, and (2) DTI ratios greater than 45%. Our QSR Transactions contain coverage limits that may be triggered depending on the mix of our risk written during the period. The number of loans we insured with DTI ratios greater than 45% increased in the second half of 2017 after the requirements of the GSE underwriting guidelines were made more liberal, and remained elevated through the first quarter of 2018. Despite the increased limit in our 2018 QSR Transaction, the risk written in the first quarter of 2018 on loans with DTI ratios greater than 45% exceeded the coverage limit under our 2018 QSR Transaction which contributed to the decline in the percentage of NIW covered in first quarter of 2018 compared with the prior year period.

Table of contents

The following tables provide additional information related to our reinsurance agreements for 2018 and 2017.

| Quota share reinsurance | As of and For the Three Months Ended March 31, | | |
|---|--|----------|---|
| (\$ in thousands, unless otherwise stated) | 2018 | 2017 | |
| NIW subject to quota share reinsurance agreements | 73 | % 87 | % |
| IIF subject to quota share reinsurance agreements | 78 | % 77 | % |
| Statements of operations: | | | |
| Ceded premiums written, net | \$33,036 | \$28,895 | |
| % of direct premiums written | 12 | % 11 | % |
| Ceded premiums earned, net | \$33,036 | \$28,895 | |
| % of direct premiums earned | 12 | % 11 | % |
| Profit commission | \$30,189 | \$31,117 | |
| Ceding commissions | \$12,645 | \$12,003 | |
| Ceded losses incurred | \$7,788 | \$4,687 | |
| Mortgage insurance portfolio: | | | |
| Ceded RIF (in millions) | \$12,008 | \$10,924 | |
| Captive reinsurance | As of and For the Three Months | | |

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| | Ended March 31, | |
|---|-----------------|----------|
| (\$ in thousands) | 2018 | 2017 |
| IIF subject to captive reinsurance agreements | 1 | % 1 % |
| Statements of operations: | | |
| Ceded premiums written | \$ 138 | \$ 1,424 |
| % of direct premiums written | 0.1 | % 0.8 % |
| Ceded premiums earned | \$ 183 | \$ 1,438 |
| % of direct premiums earned | 0.1 | % 0.8 % |
| Ceded losses incurred | \$(47) | \$ 213 |

Investment income

Net investment income in the first quarter of 2018 was \$32.1 million, up from \$29.5 million in the prior year period. The increase in investment income was due to an increase in the average balance of the investment portfolio along with higher investment yields over the periods.

Other revenue

Other revenue for the first quarter of 2018 was \$1.9 million, down from \$2.4 million in the prior year primarily due to a decline in contract underwriting fees.

Table of contents

Losses and expenses

| Losses and expenses | Three Months Ended March 31, | |
|---|---------------------------------------|--------|
| (in millions) | 2018 | 2017 |
| Losses incurred, net | \$23.9 | \$27.6 |
| Amortization of deferred policy acquisition costs | 2.6 | 2.2 |
| Other underwriting and operating expenses, net | 46.1 | 40.8 |
| Interest expense | 13.2 | 16.3 |
| Total losses and expenses | \$85.8 | \$86.9 |

Losses incurred, net

As discussed in “Critical Accounting Policies” in our 10-K MD&A and consistent with industry practices, we establish loss reserves for future claims only for loans that are currently delinquent. The terms “delinquent” and “default” are used interchangeably by us. We consider a loan to be delinquent when it is two or more payments past due. Loss reserves are established based on estimating the number of loans in our delinquent inventory that will result in a claim payment, which is referred to as the claim rate, and further estimating the amount of the claim payment, which is referred to as claim severity.

Estimation of losses is inherently judgmental. The conditions that affect the claim rate and claim severity include the current and future state of the domestic economy, including unemployment, and the current and future strength of local housing markets. The actual amount of the claim payments may be substantially different than our loss reserve estimates. Our estimates could be adversely affected by several factors, including a deterioration of regional or national economic conditions, including unemployment, leading to a reduction in borrower income and thus their ability to make mortgage payments, and a drop in housing values that could result in, among other things, greater losses on loans, and may affect borrower willingness to continue to make mortgage payments when the value of the home is below the mortgage balance. Historically, losses incurred have followed a seasonal trend in which the second half of the year has weaker credit performance than the first half, with higher new notice activity and a lower cure rate. Our estimates are also affected by any agreements we enter into regarding our claims paying practices, such as the settlement agreements discussed in Note 5 – “Litigation and Contingencies” to our consolidated financial statements. Changes to our estimates could result in a material impact to our consolidated results of operations and financial position, even in a stable economic environment.

Losses incurred, net in the first quarter of 2018 decreased 14% to \$24 million compared to \$28 million in the prior year. The decrease was due to a decrease in losses and LAE incurred on defaults reported in the current year. Losses incurred on current year defaults declined primarily due to a lower claim rate on recently received delinquencies. Favorable development on prior year defaults occurred in the first quarter of 2018 and 2017 primarily due to a lower

claim rate on previously received delinquencies.

| Composition of losses incurred | Three Months Ended | | |
|--------------------------------|--------------------|---------|-------------|
| | March 31, | | |
| | 2018 | 2017 | % Change |
| Current year / New notices | \$59.1 | \$80.4 | (26) |
| Prior year reserve development | (35.2) | (52.8) | (33) |
| Losses incurred, net | \$23.9 | \$27.6 | (13) |

Table of contents

Loss ratio Three Months Ended March 31,

The loss ratio is the ratio, expressed as a percentage, of the sum of incurred losses and loss adjustment expenses to net premiums earned. The decline in the loss ratio in the three months ended March 31, 2018 compared to the respective prior year periods was primarily due to a lower level of losses incurred, net.

New notice claim rate - total Three Months Ended March 31,

⁽¹⁾ Claim rate is the approximate quarterly rate.

New notice claim rate - loans insured 2008 and prior Three Months Ended March 31,

New notice activity continues to be primarily driven by loans insured in 2008 and prior, which continue to experience a cycle whereby many loans default, cure, and re-default. This cycle, along with the duration that defaults may ultimately remain in our notice inventory, results in significant judgment in establishing the estimated claim rate.

Claims severity

Factors that impact claim severity include the exposure on the loan (the unpaid principal balance of the loan times our insurance coverage percentage), the amount of time between delinquency and claim filing (which impacts the amount of interest and expenses, with a longer period between delinquency and claim filing generally increasing severity), and curtailments. As discussed in Note 12 - "Loss Reserves", the average time for servicers to process foreclosures has recently shortened. Therefore, we expect the average number of

Table of contents

missed payments at the time a claim is received to be approximately 18 to 24 for new notices received, compared to an average of 35 to 38 missed payments for claims received in recent periods. Our loss reserves estimates take into consideration trends over time, because the development of the delinquencies may vary from period to period without establishing a meaningful trend.

The majority of loans prior to 2009 (which represent the majority of loans in the delinquent inventory) are covered by master policy terms that, except under certain circumstances, do not limit the number of years of interest that an insured may include when filing a claim. Under our current master policy terms, an insured may include accumulated interest when filing a claim only for the first three years the loan is delinquent. In each case, the insured must comply with its obligations under the terms of the applicable master policy.

| Claims severity trend | Average exposure on claim paid | Average claim paid | % Paid to exposure | Average number of missed payments at claim received date |
|-----------------------|--------------------------------|--------------------|--------------------|--|
| Q1 2018 | \$45,597 | \$51,069 | 112.0 % | 38 |
| Q4 2017 | 44,437 | 49,177 | 110.7 % | 36 |
| Q3 2017 | 43,313 | 46,389 | 107.1 % | 35 |
| Q2 2017 | 44,747 | 49,105 | 109.7 % | 35 |
| Q1 2017 | 44,238 | 49,110 | 111.0 % | 35 |
| Q4 2016 | 43,200 | 48,297 | 111.8 % | 35 |
| Q3 2016 | 43,747 | 48,050 | 109.8 % | 34 |
| Q2 2016 | 43,709 | 47,953 | 109.7 % | 35 |
| Q1 2016 | 44,094 | 49,281 | 111.8 % | 34 |

Note: Table excludes material settlements. Settlements include amounts paid in settlement disputes for claims paying practices and commutations of pools of NPLs.

In considering the potential sensitivity of the factors underlying our estimate of loss reserves, it is possible that even a relatively small change in our estimated claim rate or severity could have a material impact on reserves and, correspondingly, on our consolidated results of operations even in a stable economic environment. For example, as of March 31, 2018, assuming all other factors remain constant, a \$1,000 increase/decrease in the average severity reserve factor would change the reserve amount by approximately +/- \$17 million. A 1 percentage point increase/decrease in the average claim rate reserve factor would change the reserve amount by approximately +/- \$23 million.

See Note 12 – “Loss Reserves” to our consolidated financial statements for a discussion of our losses incurred and claims paying practices (including curtailments).

Net losses and LAE paid

Net losses and LAE paid in the three months ended March 31, 2018 declined 36%, compared to the same period in the prior year due to lower claim activity on our primary business. We believe losses and LAE paid will continue to decline as the credit profile of our RIF continues to improve and our delinquent inventory declines.

MGIC Investment Corporation - Q1 2018 | 51

Table of contents

The following table presents our net losses and LAE paid for the three months ended March 31, 2018 and 2017.

| Net losses and LAE paid (In millions) | Three Months Ended March 31, | |
|--|---------------------------------------|-------|
| | 2018 | 2017 |
| Total primary (excluding settlements) | \$80 | \$130 |
| Claims paying practices and NPL settlements ⁽¹⁾ | 7 | — |
| Pool | 2 | 2 |
| Direct losses paid | 89 | 132 |
| Reinsurance | (11) | (9) |
| Net losses paid | 78 | 123 |
| LAE | 4 | 5 |
| Net losses and LAE paid | \$82 | \$128 |

(1) See Note 12 - "Loss Reserves" for additional information on our settlements of disputes for claims paying practices and commutations of NPLs.

Primary claims paid for the top 15 jurisdictions (based on 2018 losses paid) and all other jurisdictions for the three months ended March 31, 2018 and 2017 appears in the following table.

| Paid losses by jurisdiction (In millions) | Three Months Ended March 31, | |
|--|---------------------------------------|------|
| | 2018 | 2017 |
| New Jersey | \$14 | \$17 |
| New York | 10 | 10 |
| Florida | 6 | 16 |
| Maryland | 5 | 7 |
| Illinois | 5 | 8 |
| Pennsylvania | 3 | 8 |
| Ohio | 2 | 4 |
| California | 2 | 3 |
| Massachusetts | 2 | 4 |
| Georgia | 2 | 4 |

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| | | |
|---------------------------------------|------|-------|
| Virginia | 2 | 3 |
| Connecticut | 2 | 3 |
| North Carolina | 1 | 2 |
| Indiana | 1 | 3 |
| Michigan | 1 | 3 |
| All other jurisdictions | 22 | 35 |
| Total primary (excluding settlements) | \$80 | \$130 |

The primary average claim paid can vary materially from period to period based upon a variety of factors, including the local market conditions, average loan amount, average coverage percentage, the amount of time between delinquency and claim filing, and our loss mitigation efforts on loans for which claims are paid.

2017 hurricane activity

Hurricane activity primarily impacting Texas, Florida, and Puerto Rico in the third quarter of 2017 increased the number of new notices of delinquency reported to us in the fourth quarter of 2017. The number of delinquent loans remain elevated in those jurisdictions while the amount of paid losses for the three months ended March 31, 2018 decreased in each of those jurisdictions compared to the same period of the prior year. Paid losses on all loans, including those not affected by hurricanes, decreased in part because foreclosure moratoriums in the Texas and Florida IADA's through December 31, 2017 and Puerto Rico through May 31,

Table of contents

2018 impact all delinquent loans in those areas, including those not affected by hurricanes. Based on our analysis and past experience, we expect the majority of delinquencies that we estimated to be caused by the hurricanes to cure and to not result in a material increase in our incurred losses or losses paid.

The primary average claim paid for the top 5 states (based on 2018 losses paid) for the three months ended March 31, 2018 and 2017 appears in the following table.

| Primary average claim paid | Three Months | |
|----------------------------|-----------------|----------|
| | Ended March 31, | |
| | 2018 | 2017 |
| New Jersey * | \$93,249 | \$86,900 |
| New York * | 97,446 | 86,417 |
| Florida * | 55,746 | 66,904 |
| Maryland | 78,073 | 79,355 |
| Illinois * | 41,200 | 49,785 |
| All other jurisdictions | 39,123 | 38,795 |
| All jurisdictions | 51,069 | 49,110 |

Note: Asterisk denotes jurisdictions in the table above that predominately use a judicial foreclosure process, which generally increases the amount of time it takes for a foreclosure to be completed.

The primary average RIF on delinquent loans at March 31, 2018, December 31, 2017 and March 31, 2017 and for the top 5 jurisdictions (based on 2018 losses paid) appears in the following table.

| Primary average RIF - delinquent loans | March 31, December 31, March 31, | | |
|--|----------------------------------|-----------|-----------|
| | 2018 | 2017 | 2017 |
| New Jersey | \$ 65,968 | \$ 65,684 | \$ 65,024 |
| New York | 70,967 | 71,260 | 69,506 |
| Florida | 55,226 | 54,872 | 54,120 |
| Maryland | 66,776 | 66,266 | 66,165 |
| Illinois | 41,451 | 40,794 | 41,769 |
| All other jurisdictions | 40,289 | 39,848 | 39,773 |
| All jurisdictions | 45,569 | 45,153 | 44,980 |

The primary average RIF on all loans was \$49,610, \$49,142, and \$47,633 at March 31, 2018, December 31, 2017 and March 31, 2017, respectively.

Loss reserves

Our primary delinquency rate at March 31, 2018 was 4.02% (YE 2017: 4.55%, March 31, 2017: 4.55%). Our primary delinquent inventory was 41,243 loans at March 31, 2018, representing a decrease of 11% from December 31, 2017 and 9% from March 31, 2017. The reduction in our primary delinquent inventory is the result of the total number of delinquent loans: (1) that have cured; (2) for which claim payments have been made; or (3) that have resulted in rescission, claim denial, or removal from inventory due to settlements of claims paying disputes or commutations of coverage of pools of NPLs, collectively, exceeding the total number of new delinquencies on insured loans. In recent periods, we have experienced improved cure rates and the number of delinquencies in inventory with twelve or more

missed payments has been declining. Generally, a defaulted loan with fewer missed payments is less likely to result in a claim.

Table of contents

The gross reserves at March 31, 2018, December 31, 2017 and March 31, 2017 appear in the table below.

| Gross reserves | March 31, 2018 | December 31, 2017 | March 31, 2017 |
|---|----------------|----------------------|----------------|
| Primary: | | | |
| Direct loss reserves (in millions) | \$853 | \$913 | \$1,236 |
| IBNR and LAE | 57 | 58 | 75 |
| Total primary loss reserves | \$910 | \$971 | \$1,311 |
| Ending delinquent inventory | 41,243 | 46,556 | 45,349 |
| Percentage of loans delinquent (delinquency rate) | 4.02 % | 4.55 % | 4.55 % |
| Average total primary loss reserves per delinquency | \$22,060 | \$20,851 | \$28,911 |
| Primary claims received inventory included in ending delinquent inventory | 819 | 954 | 1,390 |
| Pool ⁽¹⁾ : | | | |
| Direct loss reserves (in millions): | | | |
| With aggregate loss limits | \$9 | \$10 | \$17 |
| Without aggregate loss limits | 5 | 4 | 6 |
| Total pool direct loss reserves | \$14 | \$14 | \$23 |

| | | | |
|--|-------|-------|-------|
| Ending default inventory: | | | |
| With aggregate loss limits | 847 | 952 | 1,252 |
| Without aggregate loss limits | 353 | 357 | 462 |
| Total pool ending delinquent inventory | 1,200 | 1,309 | 1,714 |
| Pool claims received inventory included in ending delinquent inventory | 28 | 42 | 64 |
| Other gross reserves (in millions) | \$— | \$1 | \$1 |

- (1) Since a number of our pool policies include aggregate loss limits and/or deductibles, we do not disclose an average direct reserve per delinquency for our pool business.

2017 hurricane activity

Hurricane activity primarily impacting Texas, Florida, and Puerto Rico in the third quarter of 2017 increased the number of new notices of delinquency reported to us in the fourth quarter of 2017. Based on our analysis and past experience, we expect the majority of the delinquent notices in the hurricane affected areas that we estimated to be caused by the hurricane to cure and to not result in a material increase in our incurred losses or losses paid. For those notices we estimated to be caused by the hurricanes, we established our loss reserves with a lower estimated claim rate than the claim rate we applied to other notices in our delinquent inventory. As a result, the average total primary reserves per delinquency declined as of March 31, 2018 and December 31, 2017, respectively, when compared to March 31, 2017. When excluding the impact of those notices we estimated to be caused by the hurricanes, the average total primary loss reserves per delinquency was approximately \$24,000 at both March 31, 2018 and December 31, 2017. See our risk factors titled “Recent hurricanes may impact our incurred losses, the amount and timing of paid claims, our inventory of notices of default and our Minimum Required Assets under PMIERS” and “Downturns in the domestic economy or declines in the value of borrowers’ homes from their value at the time their loans closed may result in more homeowners defaulting and our losses increasing, with a corresponding decrease in our returns” for factors that could cause our actual results to differ from our expectations expressed in this paragraph.

Table of contents

The primary delinquent inventory for the top 15 jurisdictions (based on 2018 losses paid) at March 31, 2018, December 31, 2017 and March 31, 2017 appears in the following table.

| Primary delinquent inventory by jurisdiction | March 31, December 31, March 31, | | |
|--|----------------------------------|--------|--------|
| | 2018 | 2017 | 2017 |
| New Jersey * | 1,530 | 1,749 | 2,337 |
| New York * | 2,228 | 2,387 | 2,935 |
| Florida * | 5,568 | 6,501 | 3,738 |
| Maryland | 929 | 1,026 | 1,195 |
| Illinois * | 1,974 | 2,136 | 2,411 |
| Pennsylvania * | 2,189 | 2,403 | 2,722 |
| Ohio * | 1,850 | 2,025 | 2,308 |
| California | 1,319 | 1,402 | 1,498 |
| Massachusetts | 696 | 759 | 1,018 |
| Georgia | 1,376 | 1,550 | 1,628 |
| Virginia | 676 | 731 | 776 |
| Connecticut * | 552 | 574 | 641 |
| North Carolina | 1,094 | 1,189 | 1,361 |
| Indiana * | 1,069 | 1,178 | 1,340 |
| Michigan | 1,167 | 1,260 | 1,313 |
| All other jurisdictions | 17,026 | 19,686 | 18,128 |
| Total primary delinquent inventory | 41,243 | 46,556 | 45,349 |

Note: Asterisk denotes jurisdictions in the table above that predominately use a judicial foreclosure process, which generally increases the amount of time it takes for a foreclosure to be completed.

The primary delinquent inventory by policy year at March 31, 2018, December 31, 2017 and March 31, 2017 appears in the following table.

| Primary delinquent inventory by policy year | March 31, December 31, March 31, | | |
|---|----------------------------------|--------|--------|
| | 2018 | 2017 | 2017 |
| Policy year: | | | |
| 2004 and prior | 7,754 | 8,739 | 10,032 |
| 2005 | 4,374 | 4,916 | 5,173 |
| 2006 | 6,724 | 7,719 | 8,156 |
| 2007 | 11,248 | 12,807 | 14,167 |
| 2008 | 3,086 | 3,455 | 3,755 |
| 2009 | 273 | 315 | 372 |
| 2010 | 174 | 199 | 190 |
| 2011 | 234 | 266 | 214 |
| 2012 | 479 | 549 | 349 |
| 2013 | 843 | 957 | 645 |
| 2014 | 1,534 | 1,757 | 1,071 |

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| | | | |
|------------------------------|--------|--------|--------|
| 2015 | 1,808 | 1,992 | 886 |
| 2016 | 1,790 | 1,930 | 339 |
| 2017 | 922 | 955 | — |
| 2018 | — | — | — |
| Total | | | |
| primary delinquent inventory | 41,243 | 46,556 | 45,349 |

The delinquent inventory for most policy years includes delinquencies from hurricane impacted areas that have not cured. As a result, delinquencies, including in our most recent policy years, were greater than they otherwise would have been as of March 31, 2018 and December 31, 2017. Within the hurricane impacted

Table of contents

areas, there were 10,198, 12,446, and 6,531 loans in our ending primary delinquent inventory as of March 31, 2018, December 31, 2017, and March 31, 2017, respectively.

Delinquent inventory mix by book year

The losses we have incurred on our 2005 through 2008 books have exceeded our premiums from those books. Although uncertainty remains with respect to the ultimate losses we may experience on those books, as we continue to write new insurance, those books have become a smaller percentage of our total mortgage insurance portfolio. Our 2005 through 2008 books represented approximately 18% and 19% of our total primary RIF at March 31, 2018 and December 31, 2017, respectively. Approximately 39% of the remaining primary RIF on our 2005 through 2008 books of business benefited from HARP as of both March 31, 2018 and December 31, 2017.

On our primary business, the highest claim frequency years have typically been the third and fourth year after loan origination. However, the pattern of claim frequency can be affected by many factors, including persistency and deteriorating economic conditions. Deteriorating economic conditions can result in increasing claims following a period of declining claims. As of March 31, 2018, 47% of our primary RIF was written subsequent to December 31, 2015, 61% of our primary RIF was written subsequent to December 31, 2014, and 69% of our primary RIF was written subsequent to December 31, 2013.

Underwriting and other expenses, net

Underwriting and other expenses includes items such as employee compensation costs, fees for professional services, depreciation and maintenance expense, and premium taxes, and are reported net of ceding commissions.

Underwriting and other expenses, net for the three months ended March 31, 2018 were \$46.1 million up from \$40.8 million in the respective prior year periods. The increase was primarily due to higher share-based compensation and non-executive compensation.

Table of contents

Underwriting expense ratio Three Months Ended March 31,

The underwriting expense ratio is the ratio, expressed as a percentage, of the underwriting and operating expenses, net and amortization of DAC of our combined insurance operations (which excludes underwriting and operating expenses of our non-insurance subsidiaries) to NPW. The underwriting expense ratio in the three months ended March 31, 2018 increased compared to the respective prior year period. The increase in the ratio was primarily due to higher compensation expenses in the current year period.

Interest expense

Interest expense for the three months ended March 31, 2018 was \$13.2 million, down from \$16.3 million in the prior year period. The decrease was due to the maturity of the 5% Notes and conversion of the 2% Notes in 2017.

Provision for income taxes and effective tax rate

| | Three Months Ended March 31, | | | |
|---|------------------------------|---------|---------|----------|
| | (in millions, except rate) | 2018 | 2017 | % Change |
| Income tax provision and effective tax rate | | | | |
| Income before tax | | \$180.0 | \$174.0 | 3 % |
| Provision for income taxes | | \$36.4 | \$84.2 | (57)% |
| Effective tax rate | | 20.2 % | 48.4 % | N/M |

The difference between our statutory tax rate of 21% and our effective tax rate of 20.2% for the three months ended March 31, 2018 was primarily due to the benefits of tax preferred securities. The difference between our statutory rate of 35% and our effective tax rate of 48.4% for the three months ended March 31, 2017 was primarily due to the additional provision recorded for the expected settlement of our IRS litigation.

See Note 11 – “Income Taxes” to our consolidated financial statements for a discussion of our tax position.

Table of contents

Balance Sheet Review

Total assets, liabilities, and shareholders' equity

As of March 31, 2018, total assets were \$5.6 billion, approximately the same as year-end 2017, and total liabilities were \$2.4 billion, down approximately \$0.1 billion from year-end 2017. Shareholders' equity increased approximately \$0.1 billion primarily due to net income in the first three months of 2018, offset in part by a decrease in the fair value of our investment portfolio.

The following sections mainly focus on our cash and cash equivalents, deferred income taxes, net, and loss reserves as these reflect the major developments in our assets and liabilities since December 31, 2017.

Consolidated balance sheets - Assets
as of March 31, 2018 (In thousands)

| | |
|----------------------------|------------|
| Cash and cash equivalents | \$ 177,488 |
| Investments | 4,937,262 |
| Premiums receivable | 52,701 |
| Deferred income taxes, net | 211,994 |
| Other assets | 236,898 |

Cash and cash equivalents - Our cash and cash equivalents balance increased as net cash generated from operating activities was only partly offset by net cash used in investing and financing activities.

Deferred income taxes, net - The decrease in our deferred income taxes, net was primarily due to the utilization of federal net operating loss carryforwards as we generated net income during the first three months of 2018.

Consolidated balance sheets - Liabilities and equity
as of March 31, 2018 (In thousands)

| | |
|----------------------|------------|
| Loss reserves | \$ 924,171 |
| Unearned premiums | 397,688 |
| Long-term debt | 830,720 |
| Other liabilities | 232,361 |
| Shareholders' equity | 3,231,403 |

Loss reserves - Our loss reserves include: (1) reserves representing estimates of losses and settlement expenses on reported delinquencies and (2) IBNR. Our gross reserves are reduced by reinsurance recoverable on our estimated losses and settlement expenses to calculate a net reserve balance. The net reserve balance decreased by 6% to \$879 million as of March 31, 2018, from \$937 million as of December 31, 2017. Reinsurance recoverables on our estimated losses and settlement expenses were \$45 million and \$48 million as of March 31, 2018 and December 31, 2017, respectively. The overall decrease in our loss reserves during the first three months of 2018 was due to a higher level of losses paid (\$82 million) relative to losses incurred (\$24 million) and favorable development on previously received delinquencies.

Table of contents

Investment portfolio

The average duration and investment yield of our investment portfolio as of March 31, 2018, December 31, 2017, and March 31, 2017 are shown in the table below.

| | | March 31, 2018 | December 31, 2017 | March 31, 2017 |
|--|---|----------------|-------------------|----------------|
| Portfolio duration and embedded investment yield | Duration (in years) | 4.2 | 4.3 | 4.6 |
| | Pre-tax yield ⁽¹⁾ (% of average investment portfolio assets) | 2.8% | 2.7% | 2.6% |
| | After-tax yield ⁽¹⁾ (% of average investment portfolio assets) | 2.4% | 2.0% | 1.9% |
| | | | | |

⁽¹⁾ Embedded investment yield is calculated on a yield-to-worst basis.

The increase in the investment portfolio's after-tax yield as of March 31, 2018, relative to the prior periods presented is being driven by the decrease in the statutory income tax rate.

The security ratings of our fixed income investments as of March 31, 2018, December 31, 2017, and March 31, 2017 are shown in the table below.

| Fixed income security ratings | Period | Security Ratings ⁽¹⁾ | | | |
|-------------------------------|-------------------|---------------------------------|-----|-----|-----|
| | | AAAAA | A | BBB | |
| | March 31, 2018 | 21% | 25% | 36% | 18% |
| | December 31, 2017 | 21% | 26% | 36% | 17% |
| | March 31, 2017 | 24% | 29% | 33% | 14% |

⁽¹⁾ Ratings are provided by one or more of: Moody's, Standard & Poor's and Fitch Ratings. If three ratings are available, the middle rating is utilized; otherwise the lowest rating is utilized.

Table of contents

Liquidity and Capital Resources

Consolidated Cash Flow Analysis

We have three primary types of cash flows: (1) operating cash flows, which consist mainly of cash generated by our insurance operations and income earned on our investment portfolio, less amounts paid for claims, interest expense and operating expenses, (2) investing cash flows related to the purchase, sale and maturity of investments and purchases of property and equipment and (3) financing cash flows generally from activities that impact our capital structure, such as changes in debt and shares outstanding. The following table summarizes our consolidated cash flows from operating, investing and financing activities:

| Summary of consolidated cash flows | (In thousands) | Three Months Ended March 31, | |
|---------------------------------------|----------------|---------------------------------|------------|
| | | 2018 | 2017 |
| Total cash provided by | | | |
| (used in): | | | |
| Operating activities | | \$ 133,966 | \$ 77,469 |
| Investing activities | | (48,256) | 52,440 |
| Financing activities | | (8,073) | 141,755 |
| Increase in cash and cash equivalents | | \$ 77,637 | \$ 271,664 |

Net cash provided by operating activities for the three months ended March 31, 2018 increased compared to the same period of 2017 primarily due to a lower level of losses paid, net.

Net cash used in investing activities for the three months ended March 31, 2018 reflects purchases of fixed income securities in an amount that exceeded our proceeds from sales and maturities of fixed income securities during the quarter as cash from operations was available for additional investment, as well as amounts spent on property and equipment.

Net cash from investing activities for the three months ended March 31, 2017 reflects proceeds from sales and maturities of fixed income securities, and unsettled investment activity, that exceeded purchases of fixed income securities during the quarter, offset in part by amounts spent on property and equipment.

Net cash used in financing activities for the three months ended March 31, 2018 reflects the payment of withholding taxes related to share-based compensation net share settlement.

Net cash provided by financing activities for the three months ended March 31, 2017 includes the proceeds from amounts borrowed under our revolving credit facility, less expenses paid to establish the revolving credit facility and the payment of withholding taxes related to share-based compensation net share settlement.

Capitalization

Debt at our holding company and holding company liquidity

Debt - holding company

As of March 31, 2018, our holding company's debt obligations were \$814.5 million in aggregate principal consisting of our 5.75% Notes and 9% Debentures. MGIC's ownership of \$132.7 million of our holding company's 9% Debentures is eliminated in consolidation, but they remain outstanding obligations owed by our holding company to MGIC.

Liquidity analysis - holding company

As of March 31, 2018, we had approximately \$257 million in cash and investments at our holding company. These resources are maintained primarily to service our debt interest expense, pay debt maturities, and to settle intercompany obligations. While these assets are held, we generate investment income that serves to offset a portion of our interest expense. Investment income and the payment of dividends from our insurance subsidiaries are the principal sources of holding company cash inflow. MGIC is the principal source of dividends, and their payment is restricted by insurance regulation. See Note 15 - "Statutory Information" to our

Table of contents

consolidated financial statement for additional information about MGIC's dividend restrictions. The payment of dividends from MGIC is also influenced by our view of the appropriate level of PMIERS Available Assets to maintain an excess over Minimum Required Assets. Other sources of holding company liquidity include any unused capacity on our unsecured revolving credit facility (\$175 million) and raising capital in the public markets. The ability to raise capital in the public markets is subject to prevailing market conditions, investor demand for the securities to be issued, and our deemed creditworthiness.

We may also use available holding company cash to repurchase shares of our common stock or to repurchase our outstanding debt obligations. Such repurchases may be material, may be made for cash (funded by debt) and/or exchanges for other securities, and may be made in open market purchases, privately negotiated acquisitions or other transactions. See "Overview - Capital" of this MD&A for a discussion of the share repurchase program authorized on April 26, 2018.

In the first quarter of 2018, our holding company cash and investments increased by \$40 million, to \$257 million as of March 31, 2018. Cash inflows during the quarter included \$50 million of dividends received from MGIC and other inflows of \$2 million. Cash outflows during the quarter at our holding company included \$12 million of interest payments on our 5.75% Notes. We expect MGIC to continue to pay quarterly dividends of at least \$50 million per quarter for the remainder of 2018.

The net unrealized losses on our holding company investment portfolio were approximately \$3 million at March 31, 2018 and the portfolio had a modified duration of approximately 1.8 years.

Subject to certain limitations and restrictions, holders of each of the 9% Debentures may convert their notes into shares of our common stock at their option prior to certain dates under the terms of their issuance, in which case our corresponding obligation will be eliminated.

See Note 7 – "Debt" to our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2017 for additional information about the conversion terms of our 9% Debentures and the terms of our indebtedness, including our option to defer interest on our 9% Debentures. The description in Note 7 - "Debt" to our consolidated financial statements in our Annual Report on Form 10-K is qualified in its entirety by the terms of the notes and debentures.

Although not anticipated in the near term, we may also contribute funds to our insurance operations to comply with the PMIERS or the State Capital Requirements. See "Overview - Capital" above for a discussion of these requirements. See discussion of our non-insurance contract underwriting services in Note 5 – "Litigation and Contingencies" to our consolidated financial statements for other possible uses of holding company resources.

Debt at subsidiaries

MGIC is a member of the FHLB, which provides MGIC access to an additional source of liquidity via a secured lending facility. MGIC has \$155.0 million of debt outstanding in the form of a fixed rate advance from the FHLB. Interest on the Advance is payable monthly at an annual rate, fixed for the term of the Advance, of 1.91%. The principal of the Advance matures on February 10, 2023. MGIC may prepay the Advance at any time. Such prepayment would be below par if interest rates have risen after the Advance was originated, or above par if interest rates have declined. The Advance is secured by eligible collateral whose fair value is maintained at least at 102% of the outstanding principal balance. MGIC provided eligible collateral from its investment portfolio.

Capital Adequacy
PMIERS

We operate under the PMIERS of the GSEs that became effective December 31, 2015. The PMIERS were most recently revised in December 2016, but the revision had no impact on our calculation of Available Assets or Minimum Required Assets, or on our operations. Refer to “Overview - Capital - GSEs” of this MD&A for further discussion of PMIERS.

Table of contents

As of March 31, 2018, MGIC's Available Assets under PMIERS totaled approximately \$4.8 billion, an excess of approximately \$0.9 billion over its Minimum Required Assets; and MGIC is in compliance with the requirements of the PMIERS and eligible to insure loans purchased by the GSEs. Maintaining a sufficient level of Available Assets will allow MGIC to remain in compliance with the PMIERS financial requirements, including, we believe, to the extent they are revised. Our QSR Transactions provided an aggregate of approximately \$0.8 billion of PMIERS capital credit as of March 31, 2018. Refer to Note 4 - "Reinsurance" to our consolidated financial statements for additional information on our QSR Transactions.

We plan to continuously comply with the PMIERS through our operational activities or through the contribution of funds from our holding company, subject to demands on the holding company's resources, as outlined above.

Risk-to-capital

We compute our risk-to-capital ratio on a separate company statutory basis, as well as on a combined insurance operation basis. The risk-to-capital ratio is our net RIF divided by our policyholders' position. Our net RIF includes both primary and pool risk in force, and excludes risk on policies that are currently in default and for which loss reserves have been established, and those covered by reinsurance. The risk amount includes pools of loans with contractual aggregate loss limits and without these limits. Policyholders' position 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, and a portion of the reserves for unearned premiums. The statutory contingency reserve is reported as a liability on the statutory balance sheet. A mortgage insurance company is required to make annual additions to the contingency reserve of approximately 50% of net earned premiums. 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 earned premiums in a calendar year.

MGIC's separate company risk-to-capital calculation is shown in the table below.

| | (In millions, except ratio) | March 31, 2018 | December 31, 2017 |
|---|--------------------------------|-------------------|----------------------|
| Risk-to-capital - MGIC separate company | | | |
| RIF - net ⁽¹⁾ | | \$ 31,789 | \$ 31,144 |
| Statutory policyholders' surplus | | 1,620 | 1,620 |
| Statutory contingency reserve | | 1,773 | 1,654 |
| Statutory policyholders' position | | \$ 3,393 | \$ 3,274 |
| Risk-to-capital | | 9.4:1 | 9.5:1 |

⁽¹⁾ RIF – net, as shown in the table above is net of reinsurance and exposure on policies currently delinquent for which loss reserves have been established.

Our combined insurance companies' risk-to-capital calculation (which includes a reinsurance affiliate) is shown in the table below. Reinsurance transactions with our affiliate permit MGIC to write insurance with a higher coverage percentage than it could on its own under certain state-specific requirements.

| | (In millions, except ratio) | March 31, 2018 | December 31, 2017 |
|--|--------------------------------|-------------------|----------------------|
| Risk-to-capital - Combined insurance companies | | | |

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| | | |
|--------------------------------------|-----------|-----------|
| RIF - net ⁽¹⁾ | \$ 37,510 | \$ 36,818 |
| Statutory policyholders' surplus | 1,622 | 1,622 |
| Statutory contingency reserve | 2,031 | 1,897 |
| Statutory policyholders' position | \$ 3,653 | \$ 3,519 |
| Risk-to-capital | 10.3:1 | 10.5:1 |

⁽¹⁾ RIF – net, as shown in the table above, is net of reinsurance and exposure on policies currently delinquent (\$2.0 billion at March 31, 2018 and \$2.3 billion at December 31, 2017) for which loss reserves have been established.

Table of contents

The reductions in MGIC's and our combined insurance companies' risk-to-capital in the first three months of 2018 were primarily due to an increase in statutory policyholders' position due to an increase in statutory contingency reserves, partially offset by an increase in net RIF in both calculations. Our RIF, net of reinsurance, increased in the first three months of 2018, due to an increase in our IIF. Our risk-to-capital ratio will decrease if the percentage increase in capital exceeds the percentage increase in insured risk.

For additional information regarding regulatory capital see Note 15 – “Statutory Information” to our consolidated financial statements as well as our risk factor titled “State Capital requirements may prevent us from continuing to write new insurance on an uninterrupted basis.”

Financial Strength Ratings

| MGIC financial strength ratings | Rating Agency | Rating | Outlook |
|---------------------------------|-------------------------------------|--------|---------|
| | Moody's Investor Services | Baa2 | Stable |
| | Standard and Poor's Rating Services | BBB+ | Stable |

For further information about the importance of MGIC's ratings, see our risk factor titled “Competition or changes in our relationships with our customers could reduce our revenues, reduce our premium yields and / or increase our losses.”

Table of contents

Contractual Obligations

At March 31, 2018, the approximate future payments under our contractual obligations of the type described in the table below are as follows:

| Contractual obligations (In millions) | Payments due by period | | | | |
|---|------------------------|------------------------|--------------|--------------|-------------------------|
| | Total | Less than 1 year | 1-3 years | 3-5 years | More than 5 years |
| Long-term debt obligations | \$2,039.2 | \$51.3 | \$101.8 | \$255.7 | \$1,630.4 |
| Operating lease obligations | 2.3 | 0.8 | 1.4 | 0.1 | — |
| Tax obligations | 56.0 | 56.0 | — | — | — |
| Purchase obligations | 14.3 | 13.4 | 0.9 | — | — |
| Pension, SERP and other post-retirement plans | 326.1 | 29.8 | 65.9 | 67.0 | 163.4 |
| Other long-term liabilities | 924.2 | 346.6 | 419.6 | 158.0 | — |
| Total | \$3,362.1 | \$497.9 | \$589.6 | \$480.8 | \$1,793.8 |

Our long-term debt obligations as of March 31, 2018 include their related interest and are discussed in Note 3 - “Debt” to our consolidated financial statements and under “Liquidity and Capital Resources” above. Our operating lease obligations include operating leases on certain office space, data processing equipment and autos, as discussed in Note 16 - “Leases” to our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2017. Tax obligations primarily relate to our current dispute with the IRS, as discussed in Note 11 - “Income Taxes.” Purchase obligations consist primarily of agreements to purchase items related to our ongoing infrastructure projects and information technology investments in the normal course of business. See Note 11 - “Benefit Plans” to our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2017 for a discussion of expected benefit payments under our benefit plans.

Our other long-term liabilities represent the loss reserves established to recognize the liability for losses and LAE related to existing defaults on insured mortgage loans. The timing of the future claim payments associated with the established loss reserves was determined primarily based on two key assumptions: the length of time it takes for a notice of delinquency to develop into a received claim and the length of time it takes for a received claim to be ultimately paid. The future claim payment periods are estimated based on historical experience, and could emerge differently than this estimate, in part, due to uncertainty regarding how certain factors, such as loss mitigation protocols established by servicers and changes in some state foreclosure laws that may include, for example, a requirement for additional review and/or mediation process.

See Note 12 - “Loss Reserves” to our consolidated financial statements. In accordance with GAAP for the mortgage insurance industry, we establish loss reserves only for delinquent loans. Because our reserving method does not take account of the impact of future losses that could occur from loans that are not 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 consolidated financial statements or in the table above.

Table of contents

Forward Looking Statements and Risk Factors

General: Our business, results of operations, and financial condition could be affected by the risk factors referred to under “Location of Risk Factors” below. These risk factors are an integral part of Management’s Discussion and Analysis.

These factors may also cause actual results to differ materially from the results contemplated by forward looking statements that we may make. Forward looking statements consist of statements which relate to matters other than historical fact. Among others, statements that include words such as we “believe,” “anticipate” or “expect,” or words of similar import, are forward looking statements. We are not undertaking any obligation to update any forward looking statements we may make even though these statements may be affected by events or circumstances occurring after the forward looking statements were made. Therefore no reader of this document should rely on these statements being current as of any time other than the time at which this document was filed with the Securities and Exchange Commission.

While we communicate with security analysts from time to time, it is against our policy to disclose to them any material non-public information or other confidential information. Accordingly, investors should not assume that we agree with any statement or report issued by any analyst irrespective of the content of the statement or report, and such reports are not our responsibility.

Location of Risk Factors: The risk factors are in Item 1 A of our Annual Report on Form 10-K for the year ended December 31, 2017, as supplemented by Part II, Item 1 A of this Quarterly Report on Form 10-Q. The risk factors in the 10-K, as supplemented by this 10 Q and through updating of various statistical and other information, are reproduced in Exhibit 99 to this Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Our investment portfolio is essentially a fixed income portfolio and is exposed to market risk. Important drivers of the market risk are credit spread risk and interest rate risk.

Credit spread risk is the risk that we will incur a loss due to adverse changes in credit spreads. Credit spread is the additional yield on fixed income securities above the risk-free rate (typically referenced as the yield on U.S. Treasury securities) that market participants require to compensate them for assuming credit, liquidity and/or prepayment risks.

We manage credit risk via our investment policy guidelines which primarily place our investments in investment grade securities and limit the amount of our credit exposure to any one issue, issuer and type of instrument. Guideline and investment portfolio detail is available in "Business – Section C, Investment Portfolio" in Item 1 of our Annual Report on Form 10-K for the year ended December 31, 2017.

Interest rate risk is the risk that we will incur a loss due to adverse changes in interest rates relative to the characteristics of our interest bearing assets.

One of the measures used to quantify this exposure is modified duration. Modified duration measures the price sensitivity of the assets to the changes in spreads. At March 31, 2018, the modified duration of our fixed income investment portfolio was 4.2 years, which means that an instantaneous parallel shift in the yield curve of 100 basis points would result in a change of 4.2% in the fair value of our fixed income portfolio. For an upward shift in the yield curve, the fair value of our portfolio would decrease and for a downward shift in the yield curve, the fair value would increase. See Note 7 – “Investments” to our consolidated financial statements for additional disclosure surrounding our investment portfolio.

Item 4. Controls and Procedures

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Our management, with the participation of our principal executive officer and principal financial officer, has evaluated our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended), as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our principal executive officer and principal financial officer concluded that such controls and procedures were effective as of the end of such period. There was no change in our internal control over

MGIC Investment Corporation - Q1 2018 | 65

Table of contents

financial reporting that occurred during the first quarter of 2018 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

MGIC Investment Corporation - Q1 2018 | 66

Table of contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In the second quarter of 2018, we were notified that the Joint Committee on Taxation had no objection to the terms of the agreement reached between us and the Internal Revenue Service ("IRS") with respect to our previously disclosed U.S. Tax Court case, and that the IRS was working toward finalizing the matter.

Item 1 A. Risk Factors

With the exception of the changes described and set forth below, there have been no material changes in our risk factors from the risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. The risk factors in the 10-K, as supplemented by this 10-Q, and through updating of various statistical and other information, are reproduced in their entirety in Exhibit 99 to this Quarterly Report on Form 10-Q. Competition or changes in our relationships with our customers could reduce our revenues, reduce our premium yields and / or increase our losses.

Our private mortgage insurance competitors include:

Arch Mortgage Insurance Company,
Essent Guaranty, Inc.,
Genworth Mortgage Insurance Corporation,
National Mortgage Insurance Corporation, and
Radian Guaranty Inc.

The private mortgage insurance industry is highly competitive and is expected to remain so. We believe that we currently compete with other private mortgage insurers based on pricing, underwriting requirements, financial strength (including based on credit or financial strength ratings), customer relationships, name recognition, reputation, the strength of our management team and field organization, the ancillary products and services provided to lenders and the effective use of technology and innovation in the delivery and servicing of our mortgage insurance products.

Much of the competition in the industry in the last few years has centered on pricing practices which have included: (i) reductions in standard filed rates for borrower-paid mortgage insurance policies ("BPMI"); (ii) use by certain competitors of a spectrum of filed rates to allow for formulaic, risk-based pricing (commonly referred to as "black-box" pricing); and (iii) use of customized rates (discounted from published rates) that are made available to many, but not all, lenders. On April 9, 2018, we announced we will be reducing our BPMI premium rates effective June 4, 2018, to enable all lenders and borrowers to benefit from lower premium rates. There can be no assurance that our competitors will not offer BPMI premium rates lower than our new rates. In addition, the Freddie Mac pilot program discussed in our risk factor titled "The amount of insurance we write could be adversely affected if lenders and investors select alternatives to private mortgage insurance" could lead to reductions in LPMI premium rates.

In each of 2017 and the first quarter of 2018, approximately 4%, of our new insurance written was for loans for which one lender was the original insured. Our relationships with our customers could be adversely affected by a variety of factors, including if our premium rates are higher than those of our competitors, our underwriting requirements result in our declining to insure some of the loans originated by our customers, or our insurance policy rescissions and claim curtailments affect the customer.

Table of contents

Certain of our competitors have access to capital at a lower cost of capital than we do (including, as a result of off-shore reinsurance vehicles, which are also tax-advantaged). As a result, they may be better positioned to compete outside of traditional mortgage insurance, including by participating in the pilot program referred to above and other alternative forms of credit enhancement pursued by the GSEs. In addition, because of their tax advantages, certain competitors may be able to achieve higher after-tax rates of return on their NIW compared to us, which could allow them to leverage reduced pricing to gain market share.

Substantially all of our insurance written since 2008 has been for loans purchased by the GSEs. The current PMIERS of the GSEs require a mortgage insurer to maintain a minimum amount of assets to support its insured risk, as discussed in our risk factor titled "We may not continue to meet the GSEs' private mortgage insurer eligibility requirements and our returns may decrease as we are required to maintain more capital in order to maintain our eligibility." The PMIERS do not require an insurer to maintain minimum financial strength ratings; however, our financial strength ratings can affect us in the following ways:

A downgrade in our financial strength ratings could result in increased scrutiny of our financial condition by the GSEs and/or our customers, potentially resulting in a decrease in the amount of our new insurance written.

Our ability to participate in the non-GSE mortgage market (which has been limited since 2008, but may grow in the future), could depend on our ability to maintain and improve our investment grade ratings for our mortgage insurance subsidiaries. We could be competitively disadvantaged with some market participants because the financial strength ratings of our insurance subsidiaries are lower than those of some competitors. MGIC's financial strength rating from Moody's is Baa2 (with a stable outlook) and from Standard & Poor's is BBB+ (with a stable outlook).

Financial strength ratings may also play a greater role if the GSEs no longer operate in their current capacities, for example, due to legislative or regulatory action. In addition, although the PMIERS do not require minimum financial strength ratings, the GSEs consider financial strength ratings to be important when utilizing forms of credit enhancement other than traditional mortgage insurance, including the pilot program referred to above, and as discussed in our risk factor titled "The amount of insurance we write could be adversely affected if lenders and investors select alternatives to private mortgage insurance."

If we are unable to compete effectively in the current or any future markets as a result of the financial strength ratings assigned to our insurance subsidiaries, our future new insurance written could be negatively affected.

The amount of insurance we write could be adversely affected if lenders and investors select alternatives to private mortgage insurance.

Alternatives to private mortgage insurance include:

- lenders using FHA, VA and other government mortgage insurance programs,
- investors using risk mitigation and credit risk transfer techniques other than private mortgage insurance,
- lenders and other investors holding mortgages in portfolio and self-insuring, and
- lenders originating mortgages using piggyback structures to avoid private mortgage insurance, such as a first mortgage with an 80% loan-to-value ratio and a second mortgage with a 10%, 15% or 20% loan-to-value ratio (referred to as 80-10-10, 80-15-5 or 80-20 loans, respectively) rather than a first mortgage with a 90%, 95% or 100% loan-to-value ratio that has private mortgage insurance.

In the first quarter of 2018, Freddie Mac began marketing a pilot program to lenders that would have loan level mortgage default coverage provided by various (re)insurers that are not mortgage insurers and that are not selected by the lenders. We view the pilot program as competing with traditional LPMI. The pilot offers pricing below prevalent LPMI rates. Inside Mortgage Finance reported that sources told it Fannie Mae is working on a similar initiative.

Table of contents

The GSEs (and other investors) have used other forms of credit enhancement other than private mortgage insurance, such as engaging in credit-linked note transactions executed in the capital markets, or using other forms of debt issuances or securitizations that transfer credit risk directly to other investors; using other risk mitigation techniques in conjunction with reduced levels of private mortgage insurance coverage; or accepting credit risk without credit enhancement.

The FHA's share of the low down payment residential mortgages that were subject to FHA, VA, USDA or primary private mortgage insurance was 35.6% in 2017, 35.5% in 2016, and 39.3% in 2015. In the past ten years, the FHA's share has been as low as 17.1% in 2007 and as high as 68.7% in 2009. Factors that influence the FHA's market share include relative rates and fees, underwriting guidelines and loan limits of the FHA, VA, private mortgage insurers and the GSEs; lenders' perceptions of legal risks under FHA versus GSE programs; flexibility for the FHA to establish new products as a result of federal legislation and programs; returns expected to be obtained by lenders for Ginnie Mae securitization of FHA-insured loans compared to those obtained from selling loans to Fannie Mae or Freddie Mac for securitization; and differences in policy terms, such as the ability of a borrower to cancel insurance coverage under certain circumstances. We cannot predict how the factors that affect the FHA's share of new insurance written will change in the future.

The VA's share of the low down payment residential mortgages that were subject to FHA, VA, USDA or primary private mortgage insurance was 24.1% in 2017, 26.6% in 2016, and 23.9% in 2015. In the past ten years, the VA's share has been as low as 5.4% in 2007 and as high as 26.6% in 2016. We believe that the VA's market share has generally been increasing because of an increase in the number of borrowers that are eligible for the VA's program, which offers 100% loan-to-value ratio ("LTV") loans and charges a one-time funding fee that can be included in the loan amount, and because eligible borrowers have opted to use the VA program when refinancing their mortgages. Changes in the business practices of the GSEs, federal legislation that changes their charters or a restructuring of the GSEs could reduce our revenues or increase our losses.

The GSEs' charters generally require credit enhancement for a low down payment mortgage loan (a loan amount that exceeds 80% of a home's value) in order for such loan to be eligible for purchase by the GSEs. Lenders generally have used private mortgage insurance to satisfy this credit enhancement requirement. (For information about a GSE pilot program initiated in the first quarter of 2018 that provides loan level default coverage by various (re)insurers that are not mortgage insurers, see our risk factor titled "The amount of insurance we write could be adversely affected if lenders and investors select alternatives to private mortgage insurance.") Because low down payment mortgages purchased by the GSEs have generally been insured with private mortgage insurance, the business practices of the GSEs greatly impact our business and include:

- private mortgage insurer eligibility requirements of the GSEs (for information about the financial requirements included in the PMIERS, see our risk factor titled "We may not continue to meet the GSEs' private mortgage insurer eligibility requirements and our returns may decrease as we are required to maintain more capital in order to maintain our eligibility"),

- the capital and collateral requirements for participants in the GSEs' alternative forms of credit enhancement discussed in our risk factor titled "The amount of insurance we write could be adversely affected if lenders and investors select alternatives to private mortgage insurance,"

- the level of private mortgage insurance coverage, subject to the limitations of the GSEs' charters (which may be changed by federal legislation), when private mortgage insurance is used as the required credit enhancement on low down payment mortgages,

- the amount of loan level price adjustments and guaranty fees (which result in higher costs to borrowers) that the GSEs assess on loans that require private mortgage insurance,

- whether the GSEs influence the mortgage lender's selection of the mortgage insurer providing coverage and, if so, any transactions that are related to that selection,

Table of contents

- the underwriting standards that determine which loans are eligible for purchase by the GSEs, which can affect the quality of the risk insured by the mortgage insurer and the availability of mortgage loans,
- the terms on which mortgage insurance coverage can be canceled before reaching the cancellation thresholds established by law,
- the programs established by the GSEs intended to avoid or mitigate loss on insured mortgages and the circumstances in which mortgage servicers must implement such programs,
- the terms that the GSEs require to be included in mortgage insurance policies for loans that they purchase,
- the terms on which the GSEs offer lenders relief on their representations and warranties made at the time of sale of a loan to the GSEs, which creates pressure on mortgage insurers to limit their rescission rights to conform to such relief,
- and the extent to which the GSEs intervene in mortgage insurers' claims paying practices, rescission practices or rescission settlement practices with lenders, and
- the maximum loan limits of the GSEs compared to those of the FHA and other investors.

The Federal Housing Finance Agency ("FHFA") has been the conservator of the GSEs since 2008 and has the authority to control and direct their operations. The increased role that the federal government has assumed in the residential housing finance system through the GSE conservatorship may increase the likelihood that the business practices of the GSEs change in ways that have a material adverse effect on us and that the charters of the GSEs are changed by new federal legislation. In the past, members of Congress have introduced several bills intended to change the business practices of the GSEs and the FHA; however, no legislation has been enacted. The Administration has indicated that the conservatorship of the GSEs should end; however, it is unclear whether and when that would occur and how that would impact us. As a result of the matters referred to above, it is uncertain what role the GSEs, FHA and private capital, including private mortgage insurance, will play in the residential housing finance system in the future or the impact of any such changes on our business. In addition, the timing of the impact of any resulting changes on our business is uncertain. Most meaningful changes would require Congressional action to implement and it is difficult to estimate when Congressional action would be final and how long any associated phase-in period may last.

We may not continue to meet the GSEs' private mortgage insurer eligibility requirements and our returns may decrease as we are required to maintain more capital in order to maintain our eligibility.

We must comply with the PMIERS to be eligible to insure loans purchased by the GSEs. The PMIERS include financial requirements, as well as business, quality control and certain transaction approval requirements. The financial requirements of the PMIERS require a mortgage insurer's "Available Assets" (generally only the most liquid assets of an insurer) to equal or exceed its "Minimum Required Assets" (which are based on an insurer's book of insurance in force and are calculated from tables of factors with several risk dimensions and are subject to a floor amount). Based on our interpretation of the PMIERS, as of March 31, 2018, MGIC's Available Assets totaled \$4.8 billion, or \$0.9 billion in excess of its Minimum Required Assets. MGIC is in compliance with the PMIERS and eligible to insure loans purchased by the GSEs.

If MGIC ceases to be eligible to insure loans purchased by one or both of the GSEs, it would significantly reduce the volume of our new business writings. Factors that may negatively impact MGIC's ability to continue to comply with the financial requirements of the PMIERS include the following:

On December 18, 2017, we received a summary of proposed changes to the PMIERS that are being recommended to the FHFA by the GSEs. Once the PMIERS are finalized, we expect a six-month implementation period before the revised PMIERS are effective. We expect that effectiveness will not be earlier than the fourth quarter of 2018. If the GSE-recommended changes are adopted with an effective date in the fourth quarter of 2018, we expect that at the effective date, MGIC would continue to have an excess of Available Assets over Minimum Required Assets, although this excess would be materially lower than it was at March 31, 2018 under the existing PMIERS, and that MGIC would continue to be able

Table of contents

to pay quarterly dividends to our holding company at the \$50 million quarterly rate at which they were paid in the first quarter of 2018.

We have non-disclosure obligations to each of the GSEs and cannot provide further comment on the specific provisions of the GSE-recommended changes other than as described above. Until the GSEs and/or FHFA provide public disclosure of proposed or final changes to the existing PMIERS, we do not plan to update or correct any of the disclosure above or provide any additional disclosure regarding any modifications that may occur in the GSE-recommended changes to PMIERS.

Our future operating results may be negatively impacted by the matters discussed in the rest of these risk factors. Such matters could decrease our revenues, increase our losses or require the use of assets, thereby creating a shortfall in Available Assets.

Should capital be needed by MGIC in the future, capital contributions from our holding company may not be available due to competing demands on holding company resources, including for repayment of debt.

While on an overall basis, the amount of Available Assets MGIC must hold in order to continue to insure GSE loans increased under the PMIERS over what state regulation currently requires, our reinsurance transactions mitigate the negative effect of the PMIERS on our returns. In this regard, see the first bullet point above. In addition, reinsurance may not always be available to us or available on similar terms, and it subjects us to counterparty credit risk.

The benefit of our net operating loss carryforwards may become substantially limited.

As of March 31, 2018, we had approximately \$585.7 million of net operating losses for tax purposes that we can use in certain circumstances to offset future taxable income and thus reduce our federal income tax liability. Any unutilized carryforwards are scheduled to expire at the end of tax years 2032 through 2033. Our ability to utilize these net operating losses to offset future taxable income may be significantly limited if we experience an "ownership change" as defined in Section 382 of the Internal Revenue Code of 1986, as amended (the "Code"). In general, an ownership change will occur if there is a cumulative change in our ownership by "5-percent shareholders" (as defined in the Code) that exceeds 50 percentage points over a rolling three-year period. A corporation that experiences an ownership change will generally be subject to an annual limitation on the corporation's subsequent use of net operating loss carryovers that arose from pre-ownership change periods and use of losses that are subsequently recognized with respect to assets that had a built-in-loss on the date of the ownership change. The amount of the annual limitation generally equals the fair value of the corporation immediately before the ownership change multiplied by the long-term tax-exempt interest rate (subject to certain adjustments). To the extent that the limitation in a post-ownership-change year is not fully utilized, the amount of the limitation for the succeeding year will be increased.

While we have adopted our Amended and Restated Rights Agreement (the "2015 Agreement") to minimize the likelihood of transactions in our stock resulting in an ownership change, future issuances of equity-linked securities or transactions in our stock and equity-linked securities that may not be within our control may cause us to experience an ownership change. If we experience an ownership change, we may not be able to fully utilize our net operating losses, resulting in additional income taxes and a reduction in our shareholders' equity.

On April 26, 2018, our Board of Directors approved amendments to the 2015 Agreement described above (as amended and restated, the "2018 Agreement"). The only material amendment made to the 2015 Agreement was an extension of the final expiration date until March 1, 2020. The approval and effectiveness of the 2018 Agreement is subject to shareholder approval at the Annual Meeting of Shareholders, scheduled to be held in July 2018. Until such shareholder approval, the 2015 Rights Agreement remains in effect and will expire by its terms on August 1, 2018.

Table of contents

Resolution of our dispute with the Internal Revenue Service could adversely affect us.

The Internal Revenue Service (“IRS”) completed examinations of our federal income tax returns for the years 2000 through 2007 and issued proposed assessments for taxes, interest and penalties related to our treatment of the flow-through income and loss from an investment in a portfolio of residual interests of Real Estate Mortgage Investment Conduits (“REMICs”). We appealed these assessments within the IRS and in August 2010, we reached a tentative settlement agreement with the IRS which was not finalized.

In 2014, we received Notices of Deficiency (commonly referred to as “90 day letters”) covering the 2000-2007 tax years. The Notices of Deficiency reflect taxes and penalties related to the REMIC matters of \$197.5 million and at March 31, 2018, there would also be interest related to these matters of approximately \$209.7 million. In 2007, we made a payment of \$65.2 million to the United States Department of the Treasury which will reduce any amounts we would ultimately owe. The Notices of Deficiency also reflect additional amounts due of \$261.4 million, which are primarily associated with the disallowance of the carryback of the 2009 net operating loss to the 2004-2007 tax years. We believe the IRS included the carryback adjustments as a precaution to keep open the statute of limitations on collection of the tax that was refunded when this loss was carried back, and not because the IRS actually intends to disallow the carryback permanently. Depending on the outcome of this matter, additional state income taxes and state interest may become due when a final resolution is reached. As of March 31, 2018, those state taxes and interest would approximate \$87.4 million. In addition, there could also be state tax penalties. Our total amount of unrecognized tax benefits as of March 31, 2018 is \$143.7 million, which represents the tax benefits generated by the REMIC portfolio included in our tax returns that we have not taken benefit for in our financial statements, including any related interest.

We reached agreement with the IRS to settle all issues in the case and the IRS subsequently submitted documentation reflecting the terms of the agreement to the Joint Committee on Taxation (“JCT”) for its review, which must be performed before a settlement can be completed. In the second quarter of 2018, we were notified that the JCT had no objection to the terms of the agreement and that the IRS was working toward finalizing the matter. The expected impact of the agreed upon settlement was previously reflected in our consolidated financial statements.

Although we expect the settlement to be completed, should it not be completed, ongoing litigation to resolve our dispute with the IRS could be lengthy and costly in terms of legal fees and related expenses. We would need to make further adjustments, which could be material, to our tax provision and liabilities if our view of the probability of success in this matter changes, and the ultimate resolution of this matter could have a material negative impact on our effective tax rate, results of operations, cash flows, available assets and statutory capital. In this regard, see our risk factors titled “We may not continue to meet the GSEs’ private mortgage insurer eligibility requirements and our returns may decrease as we are required to maintain more capital in order to maintain our eligibility” and “State capital requirements may prevent us from continuing to write new insurance on an uninterrupted basis.”

The mix of business we write affects our Minimum Required Assets under the PMIERS, our premium yields and the likelihood of losses occurring.

The Minimum Required Assets under the PMIERS are, in part, a function of the direct risk-in-force and the risk profile of the loans we insure, considering loan-to-value ratio, credit score, vintage, Home Affordable Refinance Program (“HARP”) status and delinquency status; and whether the loans were insured under lender-paid mortgage insurance policies or other policies that are not subject to automatic termination consistent with the Homeowners Protection Act requirements for borrower paid mortgage insurance. Therefore, if our direct risk-in-force increases through increases in new insurance written, or if our mix of business changes to include loans with higher loan-to-value ratios or lower FICO scores, for example, or if we insure a higher percentage of loans under lender-paid mortgage insurance policies, all other things equal, we will be required to hold more Available Assets in order to maintain GSE eligibility.

The minimum capital required by the risk-based capital framework contained in the exposure draft released by the NAIC in May 2016 would be, in part, a function of certain loan and economic factors, including property location, loan-to-value ratio and credit score; general underwriting quality in the market at the time of loan

Table of contents

origination; the age of the loan; and the premium rate we charge. Depending on the provisions of the capital requirements when they are released in final form and become effective, our mix of business may affect the minimum capital we are required to hold under the new framework.

Beginning in 2014, we have increased the percentage of our business from LPMI policies. Depending on the actual life of a single premium policy and its premium rate relative to that of a monthly premium policy, a single premium policy may generate more or less premium than a monthly premium policy over its life.

We have in place quota share reinsurance ("QSR") transactions with a group of unaffiliated reinsurers that cover most of our insurance written from 2013 through 2018, and a portion of our insurance written prior to 2013. Although the transactions reduce our premiums, they have a lesser impact on our overall results, as losses ceded under the transactions reduce our losses incurred and the ceding commissions we receive reduce our underwriting expenses. The blended pre-tax cost of reinsurance under our different transactions is less than 6% (but will decrease if losses are materially higher than we expect). This blended pre-tax cost is derived by dividing the reduction in our pre-tax income on loans covered by reinsurance by our direct (that is, without reinsurance) premiums from such loans. Although the pre-tax cost of the reinsurance under each transaction is generally constant, the effect of the reinsurance on the various components of pre-tax income will vary from period to period, depending on the level of ceded losses. Although the GSEs have approved the terms of our QSR transactions, they will be reviewed under the PMIERS at least annually.

We may not receive full credit under the PMIERS in future periods for the risk ceded under our QSR transactions. In addition to the effect of reinsurance on our premiums, we expect a decline in our premium yield resulting from the premium rates themselves: the books of business we wrote before 2009, which have a higher average premium rate than subsequent books of business, are expected to continue to decline as a percentage of the insurance in force; and the average premium rate on these books of business is also expected to decline as the premium rates reset to lower levels at the time the loans reach the ten-year anniversary of their initial coverage date. However, for loans that have utilized HARP, the initial ten-year period was reset to begin as of the date of the HARP transaction. As of March 31, 2018, approximately 1% of our total primary insurance in force was written in 2008, has not been refinanced under HARP and is subject to a reset after ten years.

The circumstances in which we are entitled to rescind coverage have narrowed for insurance we have written in recent years. During the second quarter of 2012, we began writing a portion of our new insurance under an endorsement to our then existing master policy (the "Gold Cert Endorsement"), which limited our ability to rescind coverage compared to that master policy. To comply with requirements of the GSEs, we introduced our current master policy in 2014. Our rescission rights under our current master policy are comparable to those under our previous master policy, as modified by the Gold Cert Endorsement, but may be further narrowed if the GSEs permit modifications to them. Our current master policy is filed as Exhibit 99.19 to our quarterly report on Form 10-Q for the quarter ended September 30, 2014 (filed with the SEC on November 7, 2014). All of our primary new insurance on loans with mortgage insurance application dates on or after October 1, 2014, was written under our current master policy. As of March 31, 2018, approximately 76% of our flow, primary insurance in force was written under our Gold Cert Endorsement or our current master policy. The FHFA and the GSEs have proposed revised GSE rescission relief principles to, among other things, further limit the circumstances under which mortgage insurers may rescind coverage. It has been proposed that these principles be incorporated into new master policies which the GSEs have indicated should be effective for new business written in 2019, subject to state regulatory approvals. These proposed principles, if adopted, are likely to further reduce our ability to rescind insurance coverage in the future, potentially resulting in higher losses than would be the case under our existing master insurance policies.

From time to time, in response to market conditions, we change the types of loans that we insure and the requirements under which we insure them. We also change our underwriting guidelines, in part through aligning some of them with Fannie Mae and Freddie Mac for loans that receive and are processed in accordance with certain approval recommendations from a GSE automated underwriting system. We also make exceptions to our underwriting requirements on a loan-by-loan basis and for certain customer programs. As a result of changes to our underwriting guidelines and requirements (including those related to debt to income ("DTI") ratios, credit scores, and the manner in which income levels and property values are determined) and other factors, our business written beginning in the second half of 2013 is expected to have a

Table of contents

somewhat higher claim incidence than business written in 2009 through the first half of 2013, but materially below that on business written in 2005-2008. However, we believe this business presents an acceptable level of risk. Our underwriting requirements are available on our website at <http://www.mgic.com/underwriting/index.html>.

Even when home prices are stable or rising, mortgages with certain characteristics have higher probabilities of claims. These characteristics include higher LTV ratios, lower FICO scores, limited underwriting, including limited borrower documentation, or higher DTI ratios, as well as loans having combinations of higher risk factors. As of March 31, 2018, mortgages with these characteristics in our primary risk in force included mortgages with LTV ratios greater than 95% (13.9%), loans with borrowers having FICO scores below 620 (2.9%), mortgages with borrowers having FICO scores of 620-679 (11.2%), mortgages with limited underwriting, including limited borrower documentation (2.7%), and mortgages with borrowers having DTI ratios greater than 45% (or where no ratio is available) (13.7%), each attribute as determined at the time of loan origination. An individual loan may have more than one of these attributes. A material number of these loans were originated in 2005 - 2007 or the first half of 2008. For information about our classification of loans by FICO score and documentation, see footnotes (5) and (6) to the Characteristics of Primary Risk in Force table under "Business - Our Products and Services" in Item 1 of our Annual Report on Form 10-K filed with the SEC on February 23, 2018.

As of March 31, 2018, approximately 1% of our primary risk in force consisted of adjustable rate mortgages which allow for adjustment of the initial interest rate during the five years after the mortgage closing ("ARMs"). We classify as fixed rate loans adjustable rate mortgages with an initial interest rate that is fixed during the five years after the mortgage closing and loans with temporary interest rate adjustments during the initial five years, commonly referred to as "buydowns," that convert to a fixed rate for the duration of the loan term. If interest rates should rise between the time of origination of such loans and when their interest rates may be reset, claim rates on such loans may be substantially higher than for loans without variable interest rate features. In addition, we have insured "interest-only" loans, which may also be ARMs, and loans with negative amortization features, such as pay option ARMs. We believe claim rates on these loans will be substantially higher than on loans without scheduled payment increases that are made to borrowers of comparable credit quality.

If state or federal regulations or statutes are changed in ways that ease mortgage lending standards and/or requirements, or if lenders seek ways to replace business in times of lower mortgage originations, it is possible that more mortgage loans could be originated with higher risk characteristics than are currently being originated, such as loans with lower FICO scores and higher DTIs. Lenders could pressure mortgage insurers to insure such loans, which are expected to experience higher claim rates. Although we attempt to incorporate these higher expected claim rates into our underwriting and pricing models, there can be no assurance that the premiums earned and the associated investment income will be adequate to compensate for actual losses even under our current underwriting requirements. We do, however, believe that our insurance written beginning in the second half of 2008 will generate underwriting profits.

Our holding company debt obligations materially exceed our holding company cash and investments.

At March 31, 2018, we had approximately \$257 million in cash and investments at our holding company and our holding company's debt obligations were \$815 million in aggregate principal amount, consisting of \$425 million of 5.75% Senior Notes due in 2023 ("5.75% Notes") and \$390 million of 9% Debentures (of which approximately \$133 million was purchased, and is held, by MGIC, and is eliminated on the consolidated balance sheet). Annual debt service on the 5.75% Notes and 9% Debentures outstanding as of March 31, 2018, is approximately \$60 million (of which approximately \$12 million will be paid to MGIC and will be eliminated on the consolidated statement of operations).

The 5.75% Senior Notes and 9% Debentures are obligations of our holding company, MGIC Investment Corporation, and not of its subsidiaries. The payment of dividends from our insurance subsidiaries which, other than investment income and raising capital in the public markets, is the principal source of our holding company cash inflow, is restricted by insurance regulation. MGIC is the principal source of dividend-paying capacity. In the first quarter of 2018 and in 2017, MGIC paid a total of \$50 million and \$140 million, respectively, in dividends to our holding company. We expect MGIC to continue to pay quarterly dividends. We

Table of contents

ask the OCI not to object before MGIC pays dividends. On April 26, 2018, our Board of Directors authorized a share repurchase program under which we may repurchase up to \$200 million of our common stock through the end of 2019. Repurchases may be made from time to time on the open market or through privately negotiated transactions. The repurchase program may be suspended for periods or discontinued at any time. If any additional capital contributions to our subsidiaries were required, such contributions would decrease our holding company cash and investments. As described in our Current Report on Form 8-K filed on February 11, 2016, MGIC borrowed \$155 million from the Federal Home Loan Bank of Chicago. This is an obligation of MGIC and not of our holding company.

Our success depends, in part, on our ability to manage risks in our investment portfolio.

Our investment portfolio is an important source of revenue and is our primary source of claims paying resources. Although our investment portfolio consists mostly of highly-rated fixed income investments, our investment portfolio is affected by general economic conditions and tax policy, which may adversely affect the markets for credit and interest-rate-sensitive securities, including the extent and timing of investor participation in these markets, the level and volatility of interest rates and credit spreads and, consequently, the value of our fixed income securities, and as such, we may not achieve our investment objectives. Volatility or lack of liquidity in the markets in which we hold securities has at times reduced the market value of some of our investments, and if this worsens substantially it could have a material adverse effect on our liquidity, financial condition and results of operations.

For the significant portion of our investment portfolio that is held by MGIC, to receive full capital credit under insurance regulatory requirements and under the PMIERS, we generally are limited to investing in investment grade fixed income securities whose yields reflect their lower credit risk profile. Our investment income is dependent upon the size of the portfolio and its reinvestment at prevailing interest rates. A prolonged period of low investment yields would have an adverse impact on our investment income as would a decrease in the size of the portfolio. Further, the PMIERS impact our investment choices; changes could negatively impact our investment income and could reduce our Available Assets through mark-to-market adjustments.

In addition, we structure our investment portfolio to satisfy our expected liabilities, including claim payments in our mortgage insurance business. If we underestimate our liabilities or improperly structure our investments to meet these liabilities, we could have unexpected losses resulting from the forced liquidation of fixed income investments before their maturity, which could adversely affect our results of operations.

Table of contents

Item 6. Exhibits

The accompanying Index to Exhibits is incorporated by reference in answer to this portion of this Item, and except as otherwise indicated in the next sentence, the Exhibits listed in such Index are filed as part of this Form 10-Q. Exhibit 32 is not filed as part of this Form 10-Q but accompanies this Form 10-Q.

(Part II, Item 6)

Index to exhibits

| Exhibit Number | Description of Exhibit | Incorporated by reference | |
|-------------------|--|---------------------------|------------------------------------|
| | | Form | Exhibit(s) Filing Date |
| 4.9 | Amended and Restated Rights Agreement, dated as of April 26, 2018, between MGIC Investment Corporation and Equiniti Trust Company, as successor rights agent, which includes as Exhibit A thereto the Form of Right Certificate | 8-A12B/A | <u>4.1</u> April 27, 2018 |
| <u>12</u> | Ratio of Earnings to Fixed Charges † | | |
| <u>31.1</u> | Certification of CEO under Section 302 of Sarbanes-Oxley Act of 2002 † | | |
| <u>31.2</u> | Certification of CFO under Section 302 of Sarbanes-Oxley Act of 2002 † | | |
| <u>32</u> | Certification of CEO and CFO under Section 906 of Sarbanes-Oxley Act of 2002 (as indicated in Item 6 of Part II, this Exhibit is not being “filed”) †† | | |
| <u>99</u> | Risk Factors included in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2017, as supplemented by Part II, Item 1A of this Quarterly Report on Form 10-Q , and through updating of various statistical and other information † | | |
| <u>101.INS</u> | XBRL Instance Document | | |
| <u>101.SCH</u> | XBRL Taxonomy Extension Schema Document | | |
| <u>101.CAL</u> | XBRL Taxonomy Extension Calculation Linkbase Document | | |
| <u>101.DEF</u> | XBRL Taxonomy Extension Definition Linkbase Document | | |
| <u>101.LAB</u> | XBRL Taxonomy Extension Label Linkbase Document | | |
| <u>101.PRE</u> | XBRL Taxonomy Extension Presentation Linkbase Document | | |

† Filed herewith.

†† Furnished herewith.

Table of contents

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 May 8, 2018.

MGIC INVESTMENT CORPORATION

/s/ Timothy J. Mattke
Timothy J. Mattke
Executive Vice President and
Chief Financial Officer

/s/ Julie K. Sperber
Julie K. Sperber
Vice President, Controller and Chief Accounting Officer

MGIC Investment Corporation - Q1 2018 | 77