REINSURANCE GROUP OF AMERICA INC
Form 10-Q
November 04, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2011

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File Number 1-11848

REINSURANCE GROUP OF AMERICA, INCORPORATED

(Exact name of Registrant as specified in its charter)

MISSOURI	**43-1627032**
(State or other jurisdiction of incorporation or organization)	**(IRS employer identification number)**

1370 Timberlake Manor Parkway

Chesterfield, Missouri 63017

(Address of principal executive offices)

(636) 736-7000

(Registrant s telephone number, including area 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 x 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x 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 and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer	x	Accelerated Filer	¨
Non-Accelerated Filer	¨	Smaller Reporting Company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of October 31, 2011, 73,267,641 shares of the registrant s common stock were outstanding.

REINSURANCE GROUP OF AMERICA, INCORPORATED AND SUBSIDIARIES

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REINSURANCE GROUP OF AMERICA, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

	September 30, 2011	December 31, 2010
	(Dollars in thousands, except share data)	
Assets		
Fixed maturity securities:		
Available-for-sale at fair value (amortized cost of $13,926,899 and $13,345,022 at September 30, 2011 and December 31, 2010, respectively)	$ 15,557,032	$ 14,304,597
Mortgage loans on real estate (net of allowances of $10,062 and $6,239 at September 30, 2011 and December 31, 2010, respectively)	934,694	885,811
Policy loans	1,228,890	1,228,418
Funds withheld at interest	5,445,886	5,421,952
Short-term investments	81,747	118,387
Other invested assets	1,020,043	707,403
Total investments	24,268,292	22,666,568
Cash and cash equivalents	802,651	463,661
Accrued investment income	190,298	127,874
Premiums receivable and other reinsurance balances	1,060,631	1,037,679
Reinsurance ceded receivables	727,290	769,699
Deferred policy acquisition costs	3,787,257	3,726,443
Other assets	347,035	289,984
Total assets	$ 31,183,454	$ 29,081,908
Liabilities and Stockholders Equity		
Future policy benefits	$ 9,445,222	$ 9,274,789
Interest-sensitive contract liabilities	8,378,159	7,774,481
Other policy claims and benefits	2,826,297	2,597,941
Other reinsurance balances	136,298	133,590
Deferred income taxes	1,662,806	1,396,747
Other liabilities	776,239	637,923
Short-term debt	199,997	199,985
Long-term debt	1,414,546	1,016,425
Collateral finance facility	681,004	850,039
Company-obligated mandatorily redeemable preferred securities of subsidiary trust holding solely junior subordinated debentures of the Company		159,421
Total liabilities	25,520,568	24,041,341
Commitments and contingent liabilities (See Note 8)		
Stockholders Equity:		
Preferred stock (par value $.01 per share; 10,000,000 shares authorized; no shares issued or outstanding)		
Common stock (par value $.01 per share; 140,000,000 shares authorized; shares issued: 79,137,758 and 73,363,523 at September 30, 2011 and December 31, 2010, respectively)	791	734
Warrants		66,912
Additional paid-in-capital	1,719,683	1,478,398
Retained earnings	2,989,231	2,587,403

Treasury stock, at cost; 5,870,872 and 328 shares at September 30, 2011 and December 31, 2010, respectively	(352,106)	(295)
Accumulated other comprehensive income	1,305,287	907,415
Total stockholders equity	5,662,886	5,040,567
Total liabilities and stockholders equity	$ 31,183,454	$ 29,081,908

See accompanying notes to condensed consolidated financial statements (unaudited).

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REINSURANCE GROUP OF AMERICA, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	Three months ended September 30, 2011	Three months ended September 30, 2010	Nine months ended September 30, 2011	Nine months ended September 30, 2010
	(Dollars in thousands, except per share data)			
Revenues:				
Net premiums	$ 1,776,165	$ 1,647,300	$ 5,300,971	$ 4,857,781
Investment income, net of related expenses	268,210	287,504	976,686	883,433
Investment related gains (losses), net:				
Other-than-temporary impairments on fixed maturity securities	(11,911)	(4,904)	(19,049)	(15,823)
Other-than-temporary impairments on fixed maturity securities transferred to (from) accumulated other comprehensive income	3,089	26	3,381	2,231
Other investment related gains (losses), net	(130,778)	(11,902)	27,076	150,989
Total investment related gains (losses), net	(139,600)	(16,780)	11,408	137,397
Other revenues	90,132	37,515	192,254	108,990
Total revenues	1,994,907	1,955,539	6,481,319	5,987,601
Benefits and Expenses:				
Claims and other policy benefits	1,514,765	1,393,891	4,504,227	4,076,310
Interest credited	35,251	94,776	237,510	230,879
Policy acquisition costs and other insurance expenses	149,228	157,058	741,663	760,509
Other operating expenses	94,029	85,409	297,340	259,755
Interest expense	27,025	25,191	77,412	65,781
Collateral finance facility expense	3,069	2,041	9,372	5,807
Total benefits and expenses	1,823,367	1,758,366	5,867,524	5,399,041
Income before income taxes	171,540	197,173	613,795	588,560
Provision for income taxes	24,155	68,941	172,706	210,870
Net income	$ 147,385	$ 128,232	$ 441,089	$ 377,690
Earnings per share:				
Basic earnings per share	$ 2.00	$ 1.75	$ 5.99	$ 5.17
Diluted earnings per share	$ 1.98	$ 1.72	$ 5.94	$ 5.06
Dividends declared per share	$ 0.18	$ 0.12	$ 0.42	$ 0.36

See accompanying notes to condensed consolidated financial statements (unaudited).

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REINSURANCE GROUP OF AMERICA, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine months ended September 30, 2011	2010
	(Dollars in thousands)	
Cash Flows from Operating Activities:		
Net income	$ 441,089	$ 377,690
Adjustments to reconcile net income to net cash provided by operating activities:		
Change in operating assets and liabilities:		
Accrued investment income	(64,464)	(68,755)
Premiums receivable and other reinsurance balances	(86,339)	(98,274)
Deferred policy acquisition costs	(104,267)	(45,525)
Reinsurance ceded receivable balances	42,409	(74,410)
Future policy benefits, other policy claims and benefits, and other reinsurance balances	669,174	1,385,629
Deferred income taxes	68,059	14,579
Other assets and other liabilities, net	(46,320)	38,453
Amortization of net investment premiums, discounts and other	(100,328)	(104,878)
Investment related gains, net	(11,408)	(137,397)
Gain on repurchase of collateral finance facility securities	(55,840)	
Excess tax benefits from share-based payment arrangement	(4,418)	(1,379)
Other, net	86,630	44,546
Net cash provided by operating activities	833,977	1,330,279
Cash Flows from Investing Activities:		
Sales of fixed maturity securities available-for-sale	2,338,405	2,533,344
Maturities of fixed maturity securities available-for-sale	195,582	107,648
Purchases of fixed maturity securities available-for-sale	(3,104,714)	(3,664,819)
Cash invested in mortgage loans	(117,697)	(97,947)
Cash invested in policy loans	(8,928)	(38,996)
Cash invested in funds withheld at interest	(23,784)	(90,282)
Principal payments on mortgage loans on real estate	60,764	18,923
Principal payments on policy loans	8,456	2,412
Change in short-term investments and other invested assets	(86,895)	20,334
Net cash used in investing activities	(738,811)	(1,209,383)
Cash Flows from Financing Activities:		
Dividends to stockholders	(31,039)	(26,340)
Repurchase of collateral finance facility securities	(111,831)	
Net proceeds from long-term debt issuance	394,388	
Proceeds from redemption and remarketing of trust preferred securities	154,588	
Maturity of trust preferred securities	(159,473)	
Purchases of treasury stock	(380,345)	(718)
Excess tax benefits from share-based payment arrangement	4,418	1,379
Exercise of stock options, net	8,680	8,804
Change in cash collateral for derivative positions	163,250	121,054
Deposits on universal life and other investment type policies and contracts	328,903	130,510
Withdrawals on universal life and other investment type policies and contracts	(119,180)	(247,856)
Net cash provided by (used in) financing activities	252,359	(13,167)
Effect of exchange rate changes on cash	(8,535)	14,319

Change in cash and cash equivalents	338,990	122,048
Cash and cash equivalents, beginning of period	463,661	512,027
Cash and cash equivalents, end of period	$ 802,651	$ 634,075
Supplementary information:		
Cash paid for interest	$ 57,821	$ 61,327
Cash paid for income taxes, net of refunds	$ 110,075	$ 41,368

See accompanying notes to condensed consolidated financial statements (unaudited).

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REINSURANCE GROUP OF AMERICA, INCORPORATED AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Organization and Basis of Presentation

Reinsurance Group of America, Incorporated (RGA) is an insurance holding company that was formed on December 31, 1992. The accompanying unaudited condensed consolidated financial statements of RGA and its subsidiaries (collectively, the Company) have been prepared in conformity with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. Results for the three and nine months ended September 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. There were no subsequent events that would require disclosure or adjustments to the accompanying condensed consolidated financial statements through the date the financial statements were issued. These unaudited condensed consolidated financial statements include the accounts of RGA and its subsidiaries and should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s 2010 Annual Report on Form 10-K (2010 Annual Report) filed with the Securities and Exchange Commission on February 28, 2011.

The Company has reclassified the presentation of certain prior-period information to conform to the current presentation. Such reclassifications include separately disclosing the deposits and the withdrawals on universal life and other investment type policies and contracts in the condensed consolidated statements of cash flows. All intercompany accounts and transactions have been eliminated.

2. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share on net income (in thousands, except per share information):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Earnings:				
Net income (numerator for basic and diluted calculations)	$ 147,385	$ 128,232	$ 441,089	$ 377,690
Shares:				
Weighted average outstanding shares (denominator for basic calculation)	73,856	73,162	73,680	73,117
Equivalent shares from outstanding stock options(1)	398	1,258	527	1,457
Denominator for diluted calculation	74,254	74,420	74,207	74,574
Earnings per share:				
Basic	$ 2.00	$ 1.75	$ 5.99	$ 5.17
Diluted	$ 1.98	$ 1.72	$ 5.94	$ 5.06

(1) Year-to-date amounts are the weighted average of the individual quarterly amounts.

The calculation of common equivalent shares does not include the impact of options having a strike or conversion price that exceeds the average stock price for the earnings period, as the result would be antidilutive. The calculation of common equivalent shares also excludes the impact of outstanding performance contingent shares, as the conditions necessary for their issuance have not been satisfied as of the end of the reporting period. For the three months ended September 30, 2011, approximately 1.1 million stock options and approximately 0.8 million performance contingent shares were excluded from the calculation. For the three months ended September 30, 2010, approximately 1.7 million stock options and approximately 0.7 million performance contingent shares were excluded from the calculation.

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3. Comprehensive Income

The following table presents the components of the Company s comprehensive income (dollars in thousands):

	Three months ended		Nine months ended	
	September 30, 2011	September 30, 2010	September 30, 2011	September 30, 2010
Net income	$ 147,385	$ 128,232	$ 441,089	$ 377,690
Other comprehensive income (loss), net of income tax:				
Unrealized investment gains, net of reclassification adjustment for gains included in net income	354,709	362,408	470,473	729,749
Reclassification adjustment for other-than-temporary impairments	(2,008)	(17)	(2,198)	(1,450)
Currency translation adjustments	(112,810)	68,701	(71,683)	31,808
Unrealized pension and postretirement benefit adjustment	708	325	1,280	443
Comprehensive income	$ 387,984	$ 559,649	$ 838,961	$ 1,138,240

The balance of and changes in each component of accumulated other comprehensive income (loss) for the nine months ended September 30, 2011 are as follows (dollars in thousands):

	Accumulated Other Comprehensive Income (Loss), Net of Income Tax			
	Accumulated Currency Translation Adjustments	Unrealized Appreciation of Securities	Pension and Postretirement Benefits	Total
Balance, December 31, 2010	$ 270,526	$ 651,449	$ (14,560)	$ 907,415
Change in component during the period	(71,683)	468,275	1,280	397,872
Balance, September 30, 2011	$ 198,843	$ 1,119,724	$ (13,280)	$ 1,305,287

4. Investments

The Company had total cash and invested assets of $25.1 billion and $23.1 billion at September 30, 2011 and December 31, 2010, respectively, as illustrated below (dollars in thousands):

	September 30, 2011	December 31, 2010
Fixed maturity securities, available-for-sale	$ 15,557,032	$ 14,304,597
Mortgage loans on real estate	934,694	885,811
Policy loans	1,228,890	1,228,418
Funds withheld at interest	5,445,886	5,421,952
Short-term investments	81,747	118,387
Other invested assets	1,020,043	707,403
Cash and cash equivalents	802,651	463,661
Total cash and invested assets	$ 25,070,943	$ 23,130,229

All investments held by the Company are monitored for conformance to the qualitative and quantitative limits prescribed by the applicable jurisdiction s insurance laws and regulations. In addition, the operating companies boards of directors periodically review their respective investment portfolios. The Company s investment strategy is to maintain a predominantly investment-grade, fixed maturity securities portfolio, which will provide adequate liquidity for expected reinsurance obligations and maximize total return through prudent asset management. The Company s asset/liability duration matching differs between operating segments. Based on Canadian reserve requirements, the Canadian liabilities are matched with long-duration Canadian assets. The duration of the Canadian portfolio exceeds twenty years. The average duration for all portfolios, when consolidated, ranges between eight and ten years.

The Company participates in a securities borrowing program whereby securities, which are not reflected on the Company s condensed consolidated balance sheets, are borrowed from a third party. The Company is required to maintain a minimum of 100% of the market value of the borrowed securities as collateral. The Company had borrowed securities with an amortized cost of $150.0 million and a market value of $149.1 million as of September 30, 2011. The borrowed securities are used to provide collateral under an affiliated reinsurance transaction. There were no securities borrowed as of December 31, 2010.

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Investment Income, Net of Related Expenses

Major categories of investment income, net of related expenses consist of the following (dollars in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Fixed maturity securities available-for-sale	$ 190,990	$ 179,130	$ 566,581	$ 532,259
Mortgage loans on real estate	14,474	13,406	41,801	37,567
Policy loans	16,454	18,271	49,549	56,150
Funds withheld at interest	41,267	69,677	306,028	245,249
Short-term investments	393	1,142	2,201	3,520
Other invested assets	11,470	11,926	31,680	26,694
Investment revenue	275,048	293,552	997,840	901,439
Investment expense	(6,838)	(6,048)	(21,154)	(18,006)
Investment income, net of related expenses	$ 268,210	$ 287,504	$ 976,686	$ 883,433

Investment Related Gains (Losses), Net

Investment related gains (losses), net consist of the following *(*dollars in thousands*)*:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Fixed maturity and equity securities available for sale:				
Other-than-temporary impairment losses on fixed maturities	$ (11,911)	$ (4,904)	$ (19,049)	$ (15,823)
Portion of loss recognized in accumulated other comprehensive income (before taxes)	3,089	26	3,381	2,231
Net other-than-temporary impairment losses on fixed maturities recognized in earnings	(8,822)	(4,878)	(15,668)	(13,592)
Impairment losses on equity securities			(3,680)	(32)
Gain on investment activity	34,840	39,371	92,423	74,833
Loss on investment activity	(7,182)	(7,773)	(20,749)	(21,967)
Other impairment losses and change in mortgage loan provision	(2,370)	(5,087)	(4,980)	(7,482)
Derivatives and other, net	(156,066)	(38,413)	(35,938)	105,637
Net gains (losses)	$ (139,600)	$ (16,780)	$ 11,408	$ 137,397

The net other-than-temporary impairment losses on fixed maturity securities recognized in earnings of $8.8 million and $15.7 million in the third quarter and first nine months of 2011, respectively, are primarily due to a decline in value of structured securities with exposure to mortgages and corporate bankruptcies. The impairment losses on equity securities of $3.7 million in the first nine months of 2011 are primarily due to the financial condition of European financial institutions. The impaired equity securities are hybrid securities that contain equity-like features. The derivative losses for the first three and nine months ended September 30, 2011 are primarily due to an increase in the fair value of embedded derivative liabilities associated with modified coinsurance and funds withheld treaties and guaranteed minimum benefit riders.

During the three months ended September 30, 2011 and 2010, the Company sold fixed maturity securities and equity securities with fair values of $57.2 million and $97.6 million at gross losses of $7.2 million and $7.8 million, respectively, or at 88.9% and 92.6% of amortized cost, respectively. During the nine months ended September 30, 2011 and 2010, the Company sold fixed maturity securities and equity securities with fair values of $388.9 million and $497.0 million at gross losses of $20.7 million and $22.0 million, respectively, or at 94.9% and 95.8% of amortized cost, respectively. The Company generally does not engage in short-term buying and selling of securities.

Other-Than-Temporary Impairments

The Company identifies fixed maturity and equity securities that could potentially have credit impairments that are other-than-temporary by monitoring market events that could impact issuers credit ratings, business climates, management changes, litigation, government actions and other similar factors. The Company also monitors late payments, pricing levels, rating agency actions, key financial ratios, financial statements, revenue forecasts and cash flow projections as indicators of credit issues.

The Company reviews all securities to determine whether an other-than-temporary decline in value exists and whether losses should be recognized. The Company considers relevant facts and circumstances in evaluating whether a credit or interest rate-related impairment of a security is other-than-temporary. Relevant facts and circumstances considered include: (1) the extent and length of time the fair value has been below cost; (2) the reasons for the decline in fair value; (3) the issuer s financial position and access to capital and (4) for fixed maturity securities, the Company s intent to sell a security or whether it is more likely than not it will be required to sell the security before the recovery of its amortized cost which, in some cases, may extend to maturity and for equity securities, the Company s ability and intent to hold the security for a period of time that allows for the recovery in value. To the extent the Company determines that a security is deemed to be other-than-temporarily impaired, an impairment loss is recognized.

Impairment losses on equity securities are recognized in net income. Recognition of impairment losses on fixed maturity securities is dependent on the facts and circumstances related to a specific security. If the Company intends to sell a security or it is more likely than not that it would be required to sell a security before the recovery of its amortized cost, it recognizes an other-than-temporary impairment in net income for the difference between amortized cost and fair value. If the Company does not expect to recover the amortized cost basis, it does not plan to sell the security and if it is not more likely than not that it would be required to sell a security before the recovery of its amortized cost, the recognition of the other-than-temporary impairment is bifurcated. The Company recognizes the credit loss portion in net income and the non-credit loss portion in accumulated other comprehensive income (AOCI).

The Company estimates the amount of the credit loss component of a fixed maturity security impairment as the difference between amortized cost and the present value of the expected cash flows of the security. The present value is determined using the best estimate cash flows discounted at the effective interest rate implicit to the security at the date of purchase or the current yield to accrete an asset-backed or floating-rate security. The techniques and assumptions for establishing the best estimate cash flows vary depending on the type of security. The asset-backed securities cash flow estimates are based on security-specific facts and circumstances that may include collateral characteristics, expectations of delinquency and default rates, loss severity and prepayment speeds and structural support, including subordination and guarantees. The corporate fixed maturity security cash flow estimates are derived from scenario-based outcomes of expected corporate restructurings or the disposition of assets using security specific facts and circumstances including timing, security interests and loss severity.

In periods after an other-than-temporary impairment loss is recognized on a fixed maturity security, the Company will report the impaired security as if it had been purchased on the date it was impaired and will continue to estimate the present value of the estimated cash flows of the security. Accordingly, the discount (or reduced premium) based on the new cost basis is accreted into net investment income over the remaining term of the fixed maturity security in a prospective manner based on the amount and timing of estimated future cash flows.

The following tables set forth the amount of credit loss impairments on fixed maturity securities held by the Company as of the dates indicated, for which a portion of the other-than-temporary impairment (OTTI) loss was recognized in AOCI, and the corresponding changes in such amounts (dollars in thousands):

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