

Hilltop Holdings Inc.
Form 10-Q
August 06, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2012

OR

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

Commission File Number: 1-31987

Hilltop Holdings Inc.

(Exact name of registrant as specified in its charter)

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MARYLAND
(State or other jurisdiction of incorporation or organization)

84-1477939
(I.R.S. Employer Identification No.)

200 Crescent Court, Suite 1330
Dallas, Texas
(Address of principal executive offices)

75201
(Zip Code)

(214) 855-2177

(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 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 No

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

Large accelerated filer

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

The number of shares of the Registrant's common stock outstanding at August 6, 2012 was 56,363,647.

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HILLTOP HOLDINGS INC.

FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2012

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Table of Contents**HILLTOP HOLDINGS INC.****CONSOLIDATED BALANCE SHEETS****AS OF JUNE 30, 2012 AND DECEMBER 31, 2011****(in thousands, except share and per share data)****(unaudited)**

| | June 30, 2012 | December 31, 2011 |
|--|--------------------------|------------------------------|
| Assets | | |
| Investments | | |
| Fixed maturities | | |
| Available for sale securities, at fair value (amortized cost of \$132,049 and \$135,166, respectively) | \$ 141,687 | \$ 144,801 |
| Equity securities | | |
| Available for sale securities, at fair value (cost of \$19,008 and \$16,813, respectively) | 19,610 | 19,022 |
| Other investments | | |
| Note receivable, at fair value (amortized cost of \$39,540 and \$38,641, respectively) | 40,672 | 38,588 |
| Warrants, at fair value (cost of \$12,068 and \$12,068, respectively) | 13,905 | 21,789 |
| Total investments | 215,874 | 224,200 |
| Cash and cash equivalents | 576,412 | 578,520 |
| Accrued interest and dividends | 1,494 | 1,576 |
| Premiums receivable | 26,792 | 24,390 |
| Deferred acquisition costs | 20,631 | 19,182 |
| Reinsurance recoverable, net of uncollectible amounts | 23,135 | 25,861 |
| Prepaid reinsurance premiums | 3,189 | 5,056 |
| Income taxes receivable | 77 | 77 |
| Deferred income taxes | 16,300 | 8,354 |
| Goodwill | 23,988 | 23,988 |
| Intangible assets, definite life | 5,490 | 6,074 |
| Intangible assets, indefinite life | 3,000 | 3,000 |
| Property and equipment, net | 2,115 | 2,128 |
| Loan origination costs, net | 2,380 | 2,471 |
| Other assets | 1,221 | 548 |
| Total assets | \$ 922,098 | \$ 925,425 |
| Liabilities and Stockholders Equity | | |
| Liabilities | | |
| Reserve for losses and loss adjustment expenses | \$ 52,087 | \$ 44,835 |
| Unearned premiums | 86,634 | 80,661 |
| Reinsurance payable | 3,057 | 2,845 |
| Accounts payable and accrued expenses | 7,293 | 8,121 |
| Notes payable | 131,450 | 131,450 |
| Other liabilities | 2,851 | 2,130 |
| Total liabilities | 283,372 | 270,042 |
| Stockholders Equity | | |
| Common stock, \$.01 par value, 100,000,000 shares authorized, 56,362,273 and 56,500,828 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively | 564 | 565 |

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| | | |
|--|------------|------------|
| Additional paid-in capital | 917,299 | 918,192 |
| Accumulated other comprehensive income | 8,586 | 13,983 |
| Accumulated deficit | (287,723) | (277,357) |
| Total stockholders' equity | 638,726 | 655,383 |
| Total liabilities and stockholders' equity | \$ 922,098 | \$ 925,425 |

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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HILLTOP HOLDINGS INC.
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011

(in thousands, except per share data)

(unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|-------------|------------------------------|-------------|
| | 2012 | 2011 | 2012 | 2011 |
| Revenue: | | | | |
| Net premiums earned | \$ 36,195 | \$ 32,568 | \$ 71,350 | \$ 63,500 |
| Net investment income | 3,223 | 2,229 | 6,482 | 4,310 |
| Other income | 1,851 | 1,723 | 3,562 | 3,348 |
| Net realized gains on investments | | | | |
| Other realized investment gains, net | 17 | 12 | 38 | 31 |
| Total realized investment gains, net | 17 | 12 | 38 | 31 |
| Total revenue | 41,286 | 36,532 | 81,432 | 71,189 |
| Expenses: | | | | |
| Loss and loss adjustment expenses | 39,071 | 41,101 | 61,613 | 57,105 |
| Policy acquisition and other underwriting expenses | 12,793 | 11,597 | 25,708 | 23,582 |
| General and administrative expenses | 2,913 | 1,612 | 4,557 | 3,485 |
| Depreciation and amortization | 330 | 426 | 690 | 858 |
| Interest expense | 2,131 | 2,245 | 4,270 | 4,421 |
| Total expenses | 57,238 | 56,981 | 96,838 | 89,451 |
| Loss before income tax benefit | (15,952) | (20,449) | (15,406) | (18,262) |
| Income tax benefit | 5,243 | 7,216 | 5,040 | 6,439 |
| Net loss attributable to common stockholders | \$ (10,709) | \$ (13,233) | \$ (10,366) | \$ (11,823) |
| Loss per share attributable to common stockholders | | | | |
| Basic loss per share | \$ (0.19) | \$ (0.23) | \$ (0.18) | \$ (0.21) |
| Diluted loss per share | \$ (0.19) | \$ (0.23) | \$ (0.18) | \$ (0.21) |
| Weighted average share information | | | | |
| Basic shares outstanding | 56,362 | 56,498 | 56,431 | 56,497 |
| Diluted shares outstanding | 56,362 | 56,498 | 56,431 | 56,497 |
| Other comprehensive (loss) income, before tax | | | | |
| Unrealized (losses) gains on available-for-sale securities | (3,071) | 918 | (8,303) | 288 |
| Income tax benefit (expense) | 1,075 | (321) | 2,906 | (101) |
| Other comprehensive (loss) income, net of tax | (1,996) | 597 | (5,397) | 187 |
| Comprehensive loss attributable to common stockholders | \$ (12,705) | \$ (12,636) | \$ (15,763) | \$ (11,636) |

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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HILLTOP HOLDINGS INC.
CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY
FOR THE SIX MONTHS ENDED JUNE 30, 2012

(in thousands)

(unaudited)

| | Common Stock Shares | Common Stock Amount | Additional Paid-in Capital | Accumulated Other Comprehensive Income | Accumulated Deficit | Total Stockholders Equity |
|--|------------------------|------------------------|----------------------------------|---|------------------------|---------------------------------|
| Balance, December 31, 2011 | 56,501 | \$ 565 | \$ 918,192 | \$ 13,983 | \$ (277,357) | \$ 655,383 |
| Net loss | | | | | (10,366) | (10,366) |
| Other comprehensive loss, net of tax benefit of \$2,906 | | | | (5,397) | | (5,397) |
| Total comprehensive loss | | | | | | (15,763) |
| Common stock issued to board members | 2 | | 24 | | | 24 |
| Repurchase of common stock | (141) | (1) | (1,161) | | | (1,162) |
| Stock compensation expense | | | 244 | | | 244 |
| Balance, June 30, 2012 | 56,362 | \$ 564 | \$ 917,299 | \$ 8,586 | \$ (287,723) | \$ 638,726 |

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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HILLTOP HOLDINGS INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2012 AND 2011

(in thousands)

(unaudited)

| | For the Six Months Ended June 30, | |
|---|--|-------------|
| | 2012 | 2011 |
| Cash flow from operating activities: | | |
| Net loss | \$ (10,366) | \$ (11,823) |
| Adjustments to reconcile net loss to net cash (used in) provided by operating activities: | | |
| Depreciation and amortization | 690 | 858 |
| Increase in deferred income taxes | (5,040) | (6,320) |
| Increase in unearned premiums | 5,973 | 9,304 |
| Increase in deferred acquisition costs | (1,449) | (2,380) |
| Realized gains on investments | (38) | (31) |
| Amortization of loan origination costs | 91 | 98 |
| Stock grant compensation expense | 268 | 34 |
| Decrease in payable to related party | | (263) |
| Increase in income taxes payable | | 21 |
| Increase in premiums receivable | (2,402) | (3,103) |
| Decrease in reinsurance recoverables | 2,726 | 3,734 |
| Increase in loss and loss adjustment expense reserves | 7,252 | 9,734 |
| Changes in other operating assets and liabilities | 723 | 226 |
| Net cash (used in) provided by operating activities | \$ (1,572) | \$ 89 |
| Cash flow from investing activities: | | |
| Purchases of available-for-sale securities | \$ (2,717) | \$ (16,321) |
| Proceeds from sales of available-for-sale securities | 2,075 | 2,392 |
| Proceeds from maturities of available-for-sale securities | 1,361 | 3,803 |
| Purchases of fixed assets | (93) | (242) |
| Net cash provided by (used in) investing activities | \$ 626 | \$ (10,368) |
| Cash flow from financing activities: | | |
| Repurchase of common stock | \$ (1,162) | \$ |
| Net cash used in financing activities | \$ (1,162) | \$ |
| Net decrease in cash and cash equivalents | (2,108) | (10,279) |
| Cash and cash equivalents, beginning of period | 578,520 | 649,439 |
| Cash and cash equivalents, end of period | \$ 576,412 | \$ 639,160 |
| Supplemental cash flow information: | | |
| Cash paid for interest | \$ 4,180 | \$ 4,386 |

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2012

(unaudited)

1. Business, Basis of Presentation and Summary of Significant Accounting Policies

Business

Hilltop Holdings Inc. is a holding company that is endeavoring to make opportunistic acquisitions or effect a business combination. In connection with this strategy, on May 8, 2012, we entered into a definitive agreement and plan of merger with PlainsCapital Corporation. In accordance with the merger agreement, PlainsCapital Corporation will become a wholly owned subsidiary of us. The purchase consideration to PlainsCapital Corporation shareholders includes approximately 27.5 million shares of our common stock and approximately \$318 million of cash. Consummation of the merger is subject to certain closing conditions, including approval of PlainsCapital Corporation's and our respective shareholders and regulatory approvals. No assurance can be given at this time as to when or if this transaction will be consummated.

We also conduct operations in the property and casualty insurance industry through our insurance subsidiaries, National Lloyds Insurance Company, or NLIC, and American Summit Insurance Company, or ASIC. National Lloyds Insurance Company commenced business in 1949 and currently operates in 14 states, with its largest market being the State of Texas. American Summit Insurance Company was formed in 1955 and currently operates in 12 states, its largest market being the State of Arizona. Both of these insurance companies carry a financial strength rating of A (Excellent) by A.M. Best, which was confirmed on March 30, 2012, and are regulated by the Texas Department of Insurance. Our products include fire and homeowners insurance to low value dwellings and manufactured homes primarily in Texas and other areas of the south, southeastern and southwestern United States.

Our common stock is listed on the New York Stock Exchange under the symbol HTH. We have no public trading history prior to February 12, 2004.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in conformity with generally accepted accounting principles in the United States of America (GAAP), and in conformity with the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP, however, have been condensed or omitted pursuant to Article 10 of Regulation S-X. The consolidated financial statements include the accounts of all wholly-owned subsidiaries of the Company. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements.

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In the opinion of management, these financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments necessary for the fair statement of the Company's financial position, results of operations and cash flows. These adjustments were of a normal, recurring nature. The results of operations for the interim periods ended June 30, 2012 may not be indicative of the results that may be expected for the year ended December 31, 2012. These financial statements should be read in conjunction with the financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2011.

We are required by GAAP to make estimates and assumptions that affect our reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of our financial statements and our reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates. These estimates and assumptions are particularly important in determining reserves for losses and loss adjustment expenses, deferred policy acquisition costs, reinsurance receivables and potential impairment of assets.

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HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2012

(unaudited)

Summary of Significant Accounting Policies

Recently Adopted Accounting Pronouncements

In October 2010, the FASB issued ASU-2010-26 to address the diversity in practice for the accounting for costs associated with acquiring or renewing insurance contracts. This guidance modifies the definition of acquisition costs to specify that a cost must be directly related to the successful acquisition of a new or renewal insurance contract in order to be deferred. If application of this guidance would result in the capitalization of acquisition costs that had not previously been capitalized by a reporting entity, the entity may elect not to capitalize those costs. The updated guidance is effective for periods beginning after December 15, 2011. The Company adopted this guidance prospectively on January 1, 2012, and it had no material impact on the Company's financial statements.

In May 2011, the FASB issued ASU-2011-04 to clarify ASC 820 and in some instances changed particular principles or requirements for measuring fair value or disclosing information about fair value measurements. The amendments in this update result in common fair value measurement and disclosure requirements in U.S. GAAP and International Financial Reporting Standards (IFRS). This updated guidance is effective for periods beginning after December 15, 2011. The adoption of this guidance on January 1, 2012 did not have a material impact on the Company's financial statements.

In June 2011, the FASB issued ASU-2011-05, which eliminates the current option to report other comprehensive income and its components in the statement of changes in equity. The new standard allows companies to report net income and other comprehensive income in a single, continuous statement, or in two separate, but consecutive statements. The statement(s) would need to be presented with equal prominence as the other primary financial statements. This updated guidance is effective for periods beginning after December 15, 2011. The adoption of this guidance on January 1, 2012 changed our current presentation of other comprehensive income; however, it did not have a material impact on the Company's financial statements.

In December 2011, the FASB issued ASU-2011-12, which amended ASU-2011-05 and defers guidance related to the presentation of reclassification adjustments out of accumulated other comprehensive income. All other requirements presented in ASU-2011-05 are not affected by this Update. This updated guidance is effective for periods beginning after December 15, 2011. The adoption of this guidance on January 1, 2012 changed our current presentation of other comprehensive income; however, it did not have a material impact on the Company's financial statements.

Table of Contents**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****JUNE 30, 2012****(unaudited)****2. Investments**

The amortized cost (original cost for equity securities), gross unrealized holding gains and losses, and fair value of available-for-sale securities by major security type and class of security at June 30, 2012 and December 31, 2011 were as follows (in thousands).

| | June 30, 2012 | | | |
|--|--------------------------------|---|--|-----------------------|
| | Cost/Amortized Cost | Gross Unrealized Holding Gains | Gross Unrealized Holding Losses | Fair Value |
| Available-for-sale securities: | | | | |
| Fixed maturities: | | | | |
| Government securities | \$ 27,756 | \$ 1,270 | \$ (1) | \$ 29,025 |
| Residential mortgage-backed securities | 10,373 | 797 | | 11,170 |
| Commercial mortgage-backed securities | 1,969 | 64 | | 2,033 |
| Corporate debt securities | 91,951 | 7,574 | (66) | 99,459 |
| | 132,049 | 9,705 | (67) | 141,687 |
| Equity securities | 19,008 | 608 | (6) | 19,610 |
| | 151,057 | 10,313 | (73) | 161,297 |
| Other investments: | | | | |
| Note receivable | 39,540 | 1,132 | | 40,672 |
| Warrants | 12,068 | 1,837 | | 13,905 |
| | \$ 202,665 | \$ 13,282 | \$ (73) | \$ 215,874 |

| | December 31, 2011 | | | |
|--|--------------------------------|---|--|-----------------------|
| | Cost/Amortized Cost | Gross Unrealized Holding Gains | Gross Unrealized Holding Losses | Fair Value |
| Available-for-sale securities: | | | | |
| Fixed maturities: | | | | |
| Government securities | \$ 27,729 | \$ 1,439 | \$ (3) | \$ 29,165 |
| Residential mortgage-backed securities | 11,708 | 944 | | 12,652 |
| Commercial mortgage-backed securities | 2,277 | 36 | (10) | 2,303 |

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| | | | | |
|---------------------------|------------|-----------|----------|------------|
| Corporate debt securities | 93,452 | 7,406 | (177) | 100,681 |
| | 135,166 | 9,825 | (190) | 144,801 |
| Equity securities | 16,813 | 2,462 | (253) | 19,022 |
| | 151,979 | 12,287 | (443) | 163,823 |
| Other investments: | | | | |
| Note receivable | 38,641 | | (53) | 38,588 |
| Warrants | 12,068 | 9,721 | | 21,789 |
| | \$ 202,688 | \$ 22,008 | \$ (496) | \$ 224,200 |

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HILLTOP HOLDINGS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2012

(unaudited)

The following tables summarize the length of time securities with unrealized losses at June 30, 2012 and December 31, 2011 have been in an unrealized loss position (in thousands).

| | Less than 12 Months | | June 30, 2012 12 Months or More | | Total | |
|--------------------------------|----------------------------|-------------------------------|------------------------------------|-------------------------------|----------------------------|-------------------------------|
| | Estimated Fair Value | Gross Unrealized Losses | Estimated Fair Value | Gross Unrealized Losses | Estimated Fair Value | Gross Unrealized Losses |
| Available-for-sale securities: | | | | | | |
| Fixed maturities: | | | | | | |
| Government securities | \$ 398 | \$ (1) | \$ | \$ | \$ 398 | \$ (1) |
| Corporate debt securities | 720 | (37) | 1,723 | (29) | 2,443 | (66) |
| | 1,118 | (38) | 1,723 | (29) | 2,841 | (67) |
| Equity securities | | | | | | |
| | | | 93 | (6) | 93 | (6) |
| | \$ 1,118 | \$ (38) | \$ 1,816 | \$ (35) | \$ 2,934 | \$ (73) |

| | Less than 12 Months | | December 31, 2011 12 Months or More | | Total | |
|---------------------------------------|----------------------------|-------------------------------|--|-------------------------------|----------------------------|-------------------------------|
| | Estimated Fair Value | Gross Unrealized Losses | Estimated Fair Value | Gross Unrealized Losses | Estimated Fair Value | Gross Unrealized Losses |
| Available-for-sale securities: | | | | | | |
| Fixed maturities: | | | | | | |
| Government securities | \$ 1,695 | \$ (3) | \$ | \$ | \$ 1,695 | \$ (3) |
| Commercial mortgage-backed securities | 487 | (10) | | | 487 | (10) |
| Corporate debt securities | 5,254 | (177) | | | 5,254 | (177) |
| | 7,436 | (190) | | | 7,436 | (190) |
| Equity securities | | | | | | |
| | 8,476 | (253) | | | 8,476 | (253) |
| | 15,912 | (443) | | | 15,912 | (443) |
| Other investments | | | | | | |
| Note receivable | 38,588 | (53) | | | 38,588 | (53) |
| | \$ 54,500 | \$ (496) | \$ | \$ | \$ 54,500 | \$ (496) |

For the three and six months ended June 30, 2012, the Company did not record any other-than-temporary impairments. While all of the investments are monitored for potential other-than-temporary impairment, our analysis and experience indicate that these investments generally do not present a greater risk of other-than-temporary impairment, as fair value should recover over time. Factors considered in our analysis include the reasons for the unrealized loss position, the severity and duration of the unrealized loss position, credit worthiness, and forecasted

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performance of the investee. While some of the securities held in the investment portfolio have decreased in value since the date of acquisition, the severity of loss and the duration of the loss position are not believed to be significant enough to warrant other-than-temporary impairment of the securities. The Company does not intend, nor is it likely that the Company will be required to sell these securities before the recovery of the cost basis; and, therefore, we do not believe any other-than-temporary impairments exist as of June 30, 2012.

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Gross realized investment gains and losses for the three and six months ended June 30, 2012 and 2011 are summarized as follows (in thousands).

| | Gross Gains | 2012 Gross Losses | Three Months Ended June 30, | | | |
|------------------|----------------|-------------------------|-----------------------------|----------------|-------------------------|-------|
| | | | Total | Gross Gains | 2011 Gross Losses | Total |
| Fixed maturities | \$ 19 | \$ (2) | \$ 17 | \$ 13 | \$ (1) | \$ 12 |
| | \$ 19 | \$ (2) | \$ 17 | \$ 13 | \$ (1) | \$ 12 |

| | Gross Gains | 2012 Gross Losses | Six Months Ended June 30, | | | |
|------------------|----------------|-------------------------|---------------------------|----------------|-------------------------|-------|
| | | | Total | Gross Gains | 2011 Gross Losses | Total |
| Fixed maturities | \$ 40 | \$ (2) | \$ 38 | \$ 33 | \$ (2) | \$ 31 |
| | \$ 40 | \$ (2) | \$ 38 | \$ 33 | \$ (2) | \$ 31 |

Sale of available-for-sale investment securities resulted in the following during the three and six months ended June 30, 2012 and 2011 (in thousands).

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--------------|-----------------------------|--------|---------------------------|----------|
| | 2012 | 2011 | 2012 | 2011 |
| Proceeds | \$ 1,080 | \$ 877 | \$ 2,075 | \$ 2,392 |
| Gross gains | \$ 19 | \$ 13 | \$ 40 | \$ 33 |
| Gross losses | \$ (2) | \$ (1) | \$ (2) | \$ (2) |

Table of Contents**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****JUNE 30, 2012****(unaudited)**

Expected maturities may differ from contractual maturities because certain borrowers may have the right to call or prepay obligations with or without penalties. The schedule of fixed maturities of available-for-sale securities at June 30, 2012 and December 31, 2011, by contractual maturity are as follows (in thousands).

| | June 30, 2012 | |
|---|---------------------------|-----------------------|
| | Amortized Cost | Fair Value |
| Available-for-sale fixed maturities: | | |
| Due within one year | \$ 28,682 | \$ 29,156 |
| Due after one year through five years | 53,382 | 56,644 |
| Due six years through ten years | 36,728 | 41,729 |
| Due after ten years | 915 | 955 |
| Mortgage-backed securities | 12,342 | 13,203 |
| | \$ 132,049 | \$ 141,687 |
| Other investments: | | |
| Due after one year through five years | \$ 51,608 | \$ 54,577 |
| | \$ 51,608 | \$ 54,577 |

| | December 31, 2011 | |
|---|---------------------------|-----------------------|
| | Amortized Cost | Fair Value |
| Available-for-sale fixed maturities: | | |
| Due within one year | \$ 12,608 | \$ 12,942 |
| Due after one year through five years | 69,594 | 73,300 |
| Due six years through ten years | 38,065 | 42,766 |
| Due after ten years | 914 | 838 |
| Mortgage-backed securities | 13,985 | 14,955 |
| | \$ 135,166 | \$ 144,801 |
| Other investments: | | |
| Due after one year through five years | \$ 50,709 | \$ 60,377 |
| | \$ 50,709 | \$ 60,377 |

Net investment income for the three and six months ended June 30, 2012 and 2011 is as follows (in thousands).

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| | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|-----------------------|-----------------------------|----------|----------|---------------------------|----------|----------|
| | 2012 | 2011 | Change | 2012 | 2011 | Change |
| Cash equivalents | \$ 206 | \$ 602 | \$ (396) | \$ 389 | \$ 1,219 | \$ (830) |
| Fixed maturities | 1,977 | 1,587 | 390 | 3,958 | 3,023 | 935 |
| Equity securities | 166 | 168 | (2) | 357 | 331 | 26 |
| Other Investments | 1,000 | | 1,000 | 2,000 | | 2,000 |
| | 3,349 | 2,357 | 992 | 6,704 | 4,573 | 2,131 |
| Investment expense | (126) | (128) | 2 | (222) | (263) | 41 |
| Net investment income | \$ 3,223 | \$ 2,229 | \$ 994 | \$ 6,482 | \$ 4,310 | \$ 2,172 |

At June 30, 2012, the Company had investments with carrying values totaling \$9.4 million on deposit with various state insurance departments.

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HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2012

(unaudited)

3. Fair Value Measurements

The Company's estimates of fair value for financial assets and financial liabilities are based on the framework established in ASC 820, *Fair Value Measurements and Disclosures*. The framework is based on the inputs used in valuation and gives the highest priority to quoted prices in active markets. It also requires that observable inputs be used in the valuations, when available. The disclosure of fair value estimates is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the Company's significant market assumptions. The three levels of the hierarchy are as follows:

- Level 1 - Unadjusted quoted market prices for identical assets or liabilities in active markets that the Company has the ability to access.
- Level 2 - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; or valuations based on models where the significant inputs are observable (e.g., interest rates, yield curves, prepayment speeds, default rates, loss severities, etc.) or can be corroborated by observable market data. Based on management's understanding of the methodologies used by our pricing service, all applicable investments have been valued in accordance with GAAP valuation principles.
- Level 3 - Valuations based on models where significant inputs are not observable. The unobservable inputs reflect the Company's own assumptions about the assumptions that market participants would use.

Table of Contents**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****JUNE 30, 2012****(unaudited)**

The following tables present the hierarchy of inputs used by the Company by financial asset type to determine their fair values at June 30, 2012 and December 31, 2011 (in thousands).

| | Total | As of June 30, 2012 | | Level 3 |
|--|-------------------|---------------------|-------------------|------------------|
| | | Level 1 | Level 2 | |
| Financial assets: | | | | |
| Cash and cash equivalents | \$ 576,412 | \$ 576,412 | \$ | \$ |
| Fixed maturities | | | | |
| Government securities | 29,025 | | 29,025 | |
| Residential mortgage-backed securities | 11,170 | | 11,170 | |
| Commercial mortgage-backed securities | 2,033 | | 2,033 | |
| Corporate debt securities | 99,459 | | 99,459 | |
| Equity securities | | | | |
| Common stock | 17,202 | 17,202 | | |
| Non-redeemable preferred stock | 2,408 | 2,408 | | |
| Other investments | | | | |
| Note receivable | 40,672 | | | 40,672 |
| Warrants | 13,905 | | | 13,905 |
| Total | \$ 792,286 | \$ 596,022 | \$ 141,687 | \$ 54,577 |

| | Total | As of December 31, 2011 | | Level 3 |
|--|-------------------|-------------------------|-------------------|------------------|
| | | Level 1 | Level 2 | |
| Financial assets: | | | | |
| Cash and cash equivalents | \$ 578,520 | \$ 578,520 | \$ | \$ |
| Fixed maturities | | | | |
| Government securities | 29,165 | | 29,165 | |
| Residential mortgage-backed securities | 12,652 | | 12,652 | |
| Commercial mortgage-backed securities | 2,303 | | 2,303 | |
| Corporate debt securities | 100,681 | | 100,681 | |
| Equity securities | | | | |
| Common stock | 18,774 | 18,774 | | |
| Non-redeemable preferred stock | 248 | 248 | | |
| Other investments | | | | |
| Note receivable | 38,588 | | | 38,588 |
| Warrants | 21,789 | | | 21,789 |
| Total | \$ 802,720 | \$ 597,542 | \$ 144,801 | \$ 60,377 |

Level 1 financial assets

The Company's Level 1 investments include cash and cash equivalent balances and actively-traded equity securities. Cash and cash equivalents are carried at amortized cost, which approximates fair value. Fair value of actively traded debt and equity securities are based on unadjusted quoted market prices. The Company receives the quoted market prices from a third party, nationally recognized, pricing service.

Level 2 financial assets

When quoted market prices are unavailable, the Company utilizes a third party pricing service to determine an estimate of fair value, which is mainly used for its fixed maturity investments, such as private and corporate debt securities, federal agency and municipal bonds, and non-government mortgage and asset-backed securities. The observable inputs utilized by the pricing service include interest rates, using either a market or income valuation approach to determine fair value. The extent of the use of each market input depends on the asset class and the market conditions; and, for some securities, additional inputs may be necessary. Based on management's understanding of the methodologies used by this pricing service, all applicable investments have been valued in accordance with GAAP valuation principles.

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HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2012

(unaudited)

As the Company is responsible for the determination of fair value, we have control processes designed to ensure that the fair values received from third-party pricing sources are reasonable and the valuation techniques and assumptions used appear reasonable and consistent with prevailing market conditions. As part of these controls, we perform monthly quantitative and qualitative analysis on the prices received from third parties to determine whether the prices are reasonable estimates of fair value. The Company's analysis includes: (i) a review of the methodology used by third party pricing services; (ii) where available, a comparison of multiple pricing services' valuations for the same security; (iii) a review of month to month price fluctuations; (iv) a review to ensure valuations are not unreasonably stale; and (v) back testing to compare actual purchase and sale transactions with valuations received from third parties. As a result of such procedures, the Company may conclude the prices received from third parties are not reflective of current market conditions. In those instances, we may request additional pricing quotes or apply internally developed valuations. However, the number of instances is insignificant and the aggregate change in value of such investments is not materially different from the original prices received.

Level 3 financial assets

The Company's Level 3 investments include the term loan issued to SWS Group, Inc., or SWS, and the warrants issued to us by SWS. Fair values are based on inputs that are unobservable and significant to the overall fair value measurement, and involve management judgment. Inputs used to determine fair value include market conditions, spread, volatility, structure and cash flows. The extent of the use of each market input depends on the asset class and the market conditions; and, for some securities, additional inputs may be necessary.

The SWS term loan cash flow model utilizes yield estimates based on comparable securities in the market. Interest rate is the most significant unobservable input. An increase or decrease in the discount rate would result in an increase or decrease in the fair value measurement of the term loan.

The warrants are valued utilizing a binomial model. SWS common stock price and its related volatility, an unobservable input, are the most significant inputs into the model and, therefore, increases or decreases to the stock price would result in a significant change in the fair value measurement of the warrants.

The following table is a roll-forward of the amounts at June 30, 2012 for financial instruments classified within Level 3. The classification of a financial instrument within Level 3 is based upon the significance of the unobservable inputs to the overall fair value measurement. The Company held no financial instruments classified within Level 3 during the six months ended June 30, 2011.

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Six Months Ended

| | | |
|------------------------------|----|---------|
| Balance at December 31, 2011 | \$ | 60,377 |
| Net transfers in | | |
| Purchases | | |
| Sales | | |
| Realized losses | | |
| Net unrealized losses | | (5,800) |
| Balance at June 30, 2012 | \$ | 54,577 |

All net unrealized losses in the table above are reflected in the accompanying financial statements. The Company had no transfers between Levels 1 and 2 for the six months ended June 30, 2012.

The following tables present the carrying value and fair value of liabilities where they differ in value at June 30, 2012 and December 31, 2011 (in thousands).

| | Carrying Value | Fair Value | June 30, 2012 | | | December 31, 2011 | |
|------------------------------|----------------|------------|---------------|------------|---------|-------------------|------------|
| | | | Level 1 | Level 2 | Level 3 | Carrying Value | Fair Value |
| Financial liabilities | | | | | | | |
| Notes payable | \$ 131,450 | \$ 133,293 | | \$ 133,293 | | \$ 131,450 | \$ 129,989 |

Table of Contents**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****JUNE 30, 2012****(unaudited)****4. Reserve for Unpaid Losses and Loss Adjustment Expenses**

A roll forward of the reserve for unpaid losses and loss adjustment expenses for the six months ended June 30, 2012 and 2011 is as follows (in thousands).

| | Six Months Ended June 30, | |
|-------------------------------|----------------------------------|-------------|
| | 2012 | 2011 |
| Balance at January 1 | \$ 44,835 | \$ 58,882 |
| Less reinsurance recoverables | (25,083) | (43,773) |
| Net balance at January 1 | 19,752 | 15,109 |
| Incurred related to: | | |
| Current Year | 59,340 | 56,775 |
| Prior Year | 2,273 | 330 |
| Total incurred | 61,613 | 57,105 |
| Payments related to: | | |
| Current Year | (38,845) | (37,059) |
| Prior Year | (11,798) | (6,700) |
| Total payments | (50,643) | (43,759) |
| Net balance at June 30 | 30,722 | 28,455 |
| Plus reinsurance recoverables | 21,365 | 40,161 |
| Balance at June 30 | \$ 52,087 | \$ 68,616 |

Incurred amounts related to prior years indicate that we experienced unfavorable development in incurred but not reported reserves as of December 31, 2011 and 2010, resulting in an expense in the six months ended June 30, 2012 and 2011, respectively. The development in 2012 is a result of late reported claims from the 2011 accident year. Primary lines of business contributing to the 2011 accident year development were homeowners and fire and allied claims.

5. Reinsurance Activity

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NLASCO, Inc., or NLASCO, our wholly-owned property and casualty insurance holding company, limits the maximum net loss that can arise from large risks or risks in concentrated areas of exposure by reinsuring (ceding) certain levels of risk. Substantial amounts of business are ceded; however, these reinsurance contracts do not relieve NLASCO from its obligations to policyholders. Such reinsurance includes quota share, excess of loss, catastrophe, and other forms of reinsurance on essentially all property and casualty lines of insurance. Net premiums earned, losses and loss adjustment expenses, or LAE, and policy acquisition and other underwriting expenses are reported net of the amounts related to reinsurance ceded to other companies. Amounts recoverable from reinsurers related to the portions of the liability for losses and LAE and unearned premiums ceded to them are reported as assets. Failure of reinsurers to honor their obligations could result in losses to NLASCO; consequently, allowances are established for amounts deemed uncollectible. NLASCO evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurer insolvencies. At June 30, 2012, we had reinsurance recoverables of approximately \$23 million, and no allowance.

NLASCO voluntarily participates as a Write Your Own carrier in the National Flood Insurance Program, or the NFIP. The NFIP is administered and regulated by the Federal Emergency Management Agency (FEMA). NLASCO operates as a fiscal agent of the Federal government in the selling and administering of the Standard Flood Insurance Policy. This involves writing the policy, collecting premiums and paying covered claims. All pricing is set by FEMA and all collections are made by the Company.

Table of Contents**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****JUNE 30, 2012****(unaudited)**

The Company cedes 100% of the policies written by the Company on the Standard Flood Insurance Policy to FEMA; however, if FEMA were unable to perform, the Company would have a legal obligation to the policyholders. The terms of the reinsurance agreement are standard terms, which require the Company to maintain its rating criteria, determine policyholder eligibility, issue policies on the Company's paper, endorse and cancel policies, collect from the insureds and process claims. NLASCO receives ceding commissions from NFIP for underwriting administration, claims management, commission and adjuster fees.

The effect of reinsurance on premiums written and earned for the three and six months ended June 30, 2012 and 2011 is as follows (in thousands).

| | Three Months Ended | | | | Six Months Ended | | | |
|-------------------------------|--------------------|-----------|---------------|-----------|------------------|-----------|---------------|-----------|
| | June 30, 2012 | | June 30, 2011 | | June 30, 2012 | | June 30, 2011 | |
| | Written | Earned | Written | Earned | Written | Earned | Written | Earned |
| Premiums from direct business | \$ 45,193 | \$ 41,602 | \$ 43,070 | \$ 36,460 | \$ 85,934 | \$ 80,287 | \$ 80,311 | \$ 71,156 |
| Reinsurance assumed | 1,666 | 1,417 | 1,401 | 1,271 | 3,104 | 2,776 | 2,671 | 2,521 |
| Reinsurance ceded | (5,230) | (6,824) | (5,348) | (5,163) | (9,847) | (11,713) | (10,158) | (10,177) |
| Net premiums | \$ 41,629 | \$ 36,195 | \$ 39,123 | \$ 32,568 | \$ 79,191 | \$ 71,350 | \$ 72,824 | \$ 63,500 |

The effect of reinsurance on incurred losses for the three and six months ended June 30, 2012 and 2011 is as follows (in thousands).

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|-----------|---------------------------|-----------|
| | 2012 | 2011 | 2012 | 2011 |
| Loss and loss adjustment expense (LAE) incurred | \$ 38,374 | \$ 43,204 | \$ 62,445 | \$ 61,150 |
| Reinsurance recoverables | 697 | (2,103) | (832) | (4,045) |
| Net loss and LAE incurred | \$ 39,071 | \$ 41,101 | \$ 61,613 | \$ 57,105 |

Multi-line excess of loss coverage

For all lines of business, the Company has excess of loss reinsurance covering \$775,000 in excess of \$225,000 retention on losses on any one risk.

Catastrophic coverage

As of January 1, 2012, the Company renewed its catastrophic reinsurance contract for its first and second layers of reinsurance. Per the contract renewal, the Company changed its underlying coverage at ASIC to \$6.5 million in excess of \$1.5 million retention. The Company has reinsurance for up to \$162 million in losses per event in excess of the \$8 million retention. The reinsurance from \$8 million to \$50 million loss is comprised of two layers of protection: \$17 million in excess of \$8 million loss; \$25 million in excess of \$25 million loss. The third layer provides coverage for \$50 million in excess of \$50 million loss; the fourth layer provides coverage of \$50 million in excess of \$100 million loss and the fifth layer provides coverage of \$20 million in excess of \$150 million loss. The fifth layer is not fully subscribed, with participants accounting for 79% of the total layer. Accordingly, NLASCO retains 21% of the losses in the fifth layer. NLIC and ASIC do not retain participation in any of the layers, other than the first \$8 million and \$1.5 million retention, respectively. During 2012, all five layers can be reinstated one time for 100% of the original premium. The third, fourth and fifth layer reinsurance contract renewed after June 30, 2012, in two layers, \$50 million in excess of \$50 million loss and \$70 million in excess of \$100 million loss, both of which are fully subscribed.

Table of Contents**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****JUNE 30, 2012****(unaudited)****6. Income Taxes**

The significant components of the provision for income taxes are as follows (in thousands).

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|----------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2012 | 2011 | 2012 | 2011 |
| Current tax benefit | \$ 29 | \$ 59 | \$ 7 | \$ 7 |
| Deferred tax benefit | 5,214 | 7,157 | 5,040 | 6,432 |
| Income tax benefit | \$ 5,243 | \$ 7,216 | \$ 5,040 | \$ 6,439 |

The decrease in income tax benefit is a direct result of the decreased loss from operations as the effective tax rate remained substantially unchanged.

7. Statutory Net Income and Capital and Surplus

The Company's insurance subsidiaries, which are domiciled in the State of Texas, prepare their statutory financial statements in accordance with accounting principles and practices prescribed or permitted by the Texas Department of Insurance, which Texas recognizes for determining solvency under Texas State Insurance Law. The Commissioner of the Texas Department of Insurance has the right to permit other practices that may deviate from prescribed practices. Prescribed statutory accounting practices are those practices that are incorporated directly or by reference in state laws, regulations, and general administrative rules applicable to all insurance enterprises domiciled in Texas. Permitted statutory accounting practices encompass all accounting practices that are not prescribed; such practices differ from state to state, may differ from company to company within a state, and may change in the future. The Company's insurance subsidiaries do not utilize permitted statutory accounting practices.

The Company's insurance subsidiaries' statutory financial statements are presented on the basis of accounting practices prescribed or permitted by the Texas Department of Insurance. Texas has adopted the National Association of Insurance Commissioners' (NAIC) statutory accounting practices as the basis of its statutory accounting practices with certain differences, which are not significant to the companies' statutory equity.

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Following is a summary of statutory capital and surplus and statutory net income of each insurance subsidiary for the three and six months ended June 30, 2012 and 2011 (in thousands).

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|------------------------------------|-------------|----------------------------------|-------------|
| | 2012 | 2011 | 2012 | 2011 |
| National Lloyds Insurance Company | | | | |
| Capital and surplus | \$ 86,882 | \$ 86,012 | \$ 86,882 | \$ 86,012 |
| Statutory net loss | (8,885) | (12,196) | (7,757) | (8,546) |
| American Summit Insurance Company | | | | |
| Capital and surplus | 24,136 | 23,753 | 24,136 | 23,753 |
| Statutory net loss | (663) | (831) | (570) | (1,555) |

Table of Contents**HILLTOP HOLDINGS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****JUNE 30, 2012****(unaudited)****8. Capital and Dividend Restrictions**

The funding of the cash requirements (including debt service) of NLASCO is primarily provided by cash dividends from NLASCO's wholly-owned insurance subsidiaries. Dividends paid by the insurance subsidiaries are restricted by regulatory requirements of the Texas Department of Insurance. Under Texas State Insurance Law for property and casualty companies, all dividends must be distributed out of earned surplus only. Furthermore, without the prior approval of the Commissioner, dividends cannot be declared or distributed which exceed the greater of ten percent of NLASCO's surplus, as shown by its last statement on file with the Commissioner, and 100% of net income for such period. At June 30, 2012, the maximum dividends that may be paid to NLASCO in 2012 without regulatory approval is approximately \$11.9 million.

Regulations of the Texas Department of Insurance require insurance companies to maintain minimum levels of statutory surplus to ensure their ability to meet their obligations to policyholders. At June 30, 2012, the Company's insurance subsidiaries had statutory surplus in excess of the minimum required.

Also, the NAIC has adopted the risk based calculation (RBC) formula (RBC ratio) for insurance companies that establishes minimum capital requirements relating to insurance risk, asset credit risk, interest rate risk and business risk. The formula is used by the NAIC and certain state insurance regulators as an early warning tool to identify companies that require additional scrutiny or regulatory action. At June 30, 2012, the Company's insurance subsidiaries' RBC ratio exceeded the level at which regulatory action would be required.

9. Loss per share

The following reflects the calculation of loss per share on a basic and diluted basis for the three and six months ended June 30, 2012 and 2011 (in thousands, except per share information).

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|------------------------------------|-------------|----------------------------------|-------------|
| | 2012 | 2011 | 2012 | 2011 |
| Loss per share from operations | | | | |
| Net loss from operations | \$ (10,709) | \$ (13,233) | \$ (10,366) | \$ (11,823) |
| Loss attributable to common stockholders | \$ (10,709) | \$ (13,233) | \$ (10,366) | \$ (11,823) |
| Basic loss per share from operations | \$ (0.19) | \$ (0.23) | \$ (0.18) | \$ (0.21) |

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| | | | | | | | | |
|--|----|--------|----|--------|----|--------|----|--------|
| Diluted loss per share from operations | \$ | (0.19) | \$ | (0.23) | \$ | (0.18) | \$ | (0.21) |
|--|----|--------|----|--------|----|--------|----|--------|

Weighted average share information:

| | | | | |
|----------------------------|--------|--------|--------|--------|
| Basic shares outstanding | 56,362 | 56,498 | 56,431 | 56,497 |
| Diluted shares outstanding | 56,362 | 56,498 | 56,431 | 56,497 |

Weighted average equivalent shares excluded from diluted loss per share because they would be anti-dilutive:

| | | | | |
|---------------------------|-------|-------|-------|-------|
| Senior exchangeable notes | 6,208 | 6,718 | 6,208 | 6,718 |
| Stock options | 700 | 100 | 700 | 100 |
| Total | 6,908 | 6,818 | 6,908 | 6,818 |

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HILLTOP HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2012

(unaudited)

10. Commitments and Contingencies

Liabilities for loss contingencies arising from claims, assessments, litigation, fines and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated.

We are a party to various legal actions resulting from our operating activities. These actions consist of litigation and administrative proceedings arising in the ordinary course of business, some of which are covered by liability insurance, and none of which is expected to have a material adverse effect on our financial condition, results of operations or cash flows taken as a whole.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the consolidated historical financial statements and notes appearing elsewhere in this Quarterly Report on Form 10-Q and the financial information set forth in the tables below.

Unless the context otherwise indicates, all references in this Management's Discussion and Analysis of Financial Condition and Results of Operations, or MD&A, to the Company, Hilltop, HTH, we, us, our or ours or similar words are to Hilltop Holdings Inc. (formerly known as Affordable Residential Communities Inc.) and its direct and indirect wholly-owned subsidiaries.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, as amended by the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical fact, included in this report that address results or developments that we expect or anticipate will or may occur in the future, that are preceded by, followed by or include the words believes, expects, may, will, would, could, should, seeks, approves, intends, plans, projects, estimates or anticipates or the negative of these words and phrases or similar words or phrases, including such things as our business strategy, our financial condition, our litigation, our efforts to make strategic acquisitions, our liquidity and sources of funding, our capital expenditures, our products, market trends, operations and business, are forward-looking statements.

These forward-looking statements are based on our beliefs, assumptions and expectations of our future performance taking into account all information currently available to us. These beliefs, assumptions and expectations are subject to risks and uncertainties and can change as a result of many possible events or factors, not all of which are known to us. If an event occurs or further changes, our business, business plan, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. Certain factors that could cause actual results to differ include, among others:

- fluctuations in the market price of our common stock and the related effect on the value of the merger consideration offered to PlainsCapital Corporation shareholders;
- business uncertainties and contractual restrictions while the contemplated merger with PlainsCapital Corporation is pending;
- the possibility that the proposed merger with PlainsCapital Corporation does not close when expected or at all because required regulatory, shareholder or other approvals and other conditions to closing are not received or satisfied on a timely basis or at all;
- required modifications to the terms of the proposed merger with PlainsCapital Corporation to obtain approvals or satisfy conditions;
- diversion of management time on merger related issues;
- changes in the financial condition and results of operations of PlainsCapital Corporation, including its failure to sustain its current revenues and earnings;

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- the adverse impact of external factors, such as changes in interest rates, inflation and consumer confidence;
- the condition of capital markets;
- actual outcome of the resolution of any conflict;
- our ability to use net operating loss carryforwards to reduce future tax payments;
- the impact of the tax code and rules on our financial statements;
- failure of NLASCO, Inc. s insurance subsidiaries to maintain their respective A.M. Best ratings;
- failure to maintain NLASCO, Inc. s current agents;
- lack of demand for insurance products;
- cost or availability of adequate reinsurance;
- changes in key management;
- severe catastrophic events in our geographic area;
- failure of NLASCO, Inc. s reinsurers to pay obligations under reinsurance contracts;
- failure of NLASCO, Inc. to maintain sufficient reserves for losses on insurance policies;

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- failure to successfully implement NLASCO, Inc.'s new information technology system; and
- failure of NLASCO, Inc. to maintain appropriate insurance licenses.

For a further discussion of these and other risks and uncertainties that could cause actual results to differ materially from those contained in our forward-looking statements, please refer to "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K, which was filed with the Securities and Exchange Commission on March 9, 2012. Consequently, all of the forward-looking statements made in this report are qualified by these cautionary statements and those risk factors, and there can be no assurance that the actual results or developments anticipated by us will be realized, or even substantially realized, and that they will have the expected consequences to, or effects on, us and our business or operations. Forward-looking statements made in this report speak as of the date of this report or as of the date specifically referenced in any such statement set forth in this report. Except to the extent required by law, we undertake no obligation to update or revise any forward-looking statements in this report.

GENERAL STRUCTURE OF THE COMPANY

We are a holding company that is endeavoring to make opportunistic acquisitions or effect a business combination. At June 30, 2012, Hilltop Holdings Inc. had approximately \$529 million of available cash and cash equivalents that could be used for this purpose. No assurances, however, can be given that we will be able to identify suitable targets, consummate acquisitions or a combination or, if consummated, successfully integrate or operate the acquired business.

Hilltop indirectly owns all of the outstanding shares of NLASCO, Inc., or NLASCO. NLASCO, in turn, owns National Lloyds Insurance Company, or NLIC, and American Summit Insurance Company, or ASIC, both of which are licensed property and casualty insurers operating in multiple states. In addition, NLASCO also owns the NALICO General Agency that operates in Texas. NLIC commenced business in 1949 and currently operates in 14 states with its largest market being the State of Texas. NLIC carries a financial strength rating of "A" (Excellent) by A.M. Best. ASIC was formed in 1955 and currently operates in 12 states, its largest market being the State of Arizona. ASIC carries a financial strength rating of "A" (Excellent) by A.M. Best. Both of these companies are regulated by the Texas Department of Insurance.

Our common stock is listed on the New York Stock Exchange, or the NYSE, under the symbol "HTH".

OVERVIEW OF RESULTS

For the three months ended June 30, 2012, net loss attributable to common stockholders was \$10.7 million, or \$0.19 per share, as compared to a net loss of \$13.2 million, or \$0.23 per share, for the same period in 2011. Net loss attributable to common stockholders decreased by \$2.5 million for the three months ended June 30, 2012, as compared to the same period in 2011, primarily due to higher net premiums earned of \$3.6 million, higher net investment income of \$1.0 million and lower loss and loss adjustment expenses of \$2.0 million, offset by higher policy acquisition and other underwriting expenses of \$1.2 million, higher general and administrative expenses of \$1.3 million and lower income tax benefit of \$2.0 million.

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For the six months ended June 30, 2012, net loss attributable to common stockholders was \$10.4 million, or \$0.18 per share, as compared to a net loss of \$11.8 million, or \$0.21 per share, for the same period in 2011. Net loss attributable to common stockholders decreased by \$1.5 million for the six months ended June 30, 2012, as compared to the same period in 2011, primarily due to higher net premiums earned of \$7.9 million, higher net investment income of \$2.2 million, offset by higher loss and loss adjustment expenses of \$4.5 million, higher policy acquisition and other underwriting expenses of \$2.1 million, higher general and administrative expenses of \$1.1 million and lower income tax benefit of \$1.4 million.

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BUSINESS OBJECTIVES AND OPERATING STRATEGIES

Strategic Acquisitions. Hilltop is seeking to make opportunistic acquisitions with its cash and, if necessary or appropriate, from additional equity or debt financing sources. In connection with this strategy, on May 8, 2012, we entered into a definitive agreement and plan of merger with PlainsCapital Corporation. In accordance with the merger agreement, PlainsCapital Corporation will become a wholly owned subsidiary of us. The purchase consideration to PlainsCapital Corporation shareholders includes approximately 27.5 million shares of our common stock and approximately \$318 million of cash. Consummation of the merger is subject to certain closing conditions, including approval of PlainsCapital Corporation's and our respective shareholders and regulatory approvals. No assurance can be given at this time as to when or if this transaction will be consummated.

Insurance Operations. NLASCO specializes in providing fire and homeowners insurance for low value dwellings and manufactured homes, primarily in Texas and other areas of the south, southeastern and southwestern United States. NLASCO targets underserved markets that require underwriting expertise that many larger carriers have been unwilling to develop given the relatively small volume of premiums produced by local agents. Within these markets, NLASCO attempts to capitalize on its superior local knowledge to identify profitable underwriting opportunities. NLASCO believes that it distinguishes itself from competitors by delivering products that are not provided by many larger carriers, providing a high level of customer service and responding quickly to the needs of its agents and policyholders. NLASCO applies a high level of selectivity in the risks it underwrites and uses a risk-adjusted return approach to capital allocation, which NLASCO believes allows it to consistently generate underwriting profits.

Many insurance buyers, agents and brokers use the ratings assigned by A.M. Best and other rating agencies to assist them in assessing the financial strength and overall quality of the companies from which they purchase insurance. A.M. Best assigned NLIC and ASIC a financial strength rating of A (Excellent). An A rating is the third highest of 16 rating categories used by A.M. Best. In evaluating a company's financial and operating performance, A.M. Best reviews a company's profitability, leverage and liquidity, as well as its book of business, the adequacy and soundness of its reinsurance, the quality and estimated market value of its assets, the adequacy of its liabilities for losses and loss adjustment expenses, or LAE, the adequacy of its surplus, its capital structure, the experience and competence of its management and its market presence. This rating is intended to provide an independent opinion of an insurer's ability to meet its obligations to policyholders and is not an evaluation directed at investors. This rating assignment is subject to the ability to meet A.M. Best's expectations as to performance and capitalization on an ongoing basis, including with respect to management of liabilities for losses and LAE, and is subject to revocation or revision at any time at the sole discretion of A.M. Best. NLASCO cannot ensure that NLIC and ASIC will maintain their present ratings.

RESULTS OF OPERATIONS

Comparison of the Three Months Ended June 30, 2012 to the Three Months Ended June 30, 2011

Revenue. Revenue for the three months ended June 30, 2012 was \$41.3 million, as compared to \$36.5 million for the same period in 2011. Net premiums earned were \$36.2 million for the three months ended June 30, 2012, as compared to \$32.6 million for the same period in 2011, primarily due to higher volume of earned premium of \$3.5 million and a decrease in the cost of reinsurance of \$0.1 million. Net investment income was \$3.2 million for the three months ended June 30, 2012, as compared to \$2.2 million for the same period in 2011, primarily due to interest earned on the note portion of the SWS investment at HTH parent only and higher yields on cash balances in 2012.

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Underwriting Results. The following table shows the components of the Company's underwriting loss for the three months ended June 30, 2012 and 2011. The Company's underwriting loss consists of net premiums earned, less loss and LAE and policy acquisition and other underwriting expenses. The underwriting results are discussed below (in thousands).

| | Three Months Ended June 30, | | Change | % Change |
|--|-----------------------------|-------------|----------|----------|
| | 2012 | 2011 | | |
| Direct premiums written | \$ 45,193 | \$ 43,070 | \$ 2,123 | 4.9% |
| Net premiums written | 41,629 | 39,123 | 2,506 | 6.4% |
| Net premiums earned | \$ 36,195 | \$ 32,568 | \$ 3,627 | 11.1% |
| Loss and LAE | 39,071 | 41,101 | (2,030) | -4.9% |
| Policy acquisition and other underwriting expenses | 12,793 | 11,597 | 1,196 | 10.3% |
| Underwriting loss | \$ (15,669) | \$ (20,130) | \$ 4,461 | -22.2% |
| Agency expenses | \$ (517) | \$ (453) | \$ (64) | -14.1% |
| Loss and LAE ratio | 107.9% | 126.2% | -18.3% | |
| Underwriting expense ratio | 33.9% | 34.2% | -0.3% | |
| Combined ratio | 141.8% | 160.4% | -18.6% | |

The loss and LAE ratio is loss and LAE divided by net premiums earned for the same period. The underwriting expense ratio is policy acquisition and other underwriting expense less agency expenses, divided by net premiums earned for the same period. Combined ratio gives you the sum of both ratios.

The second quarter is typically the most challenging for NLASCO, as Texas experiences seasonal severe weather. Tornado, wind and hail storms in Texas and the southwest produced losses of \$12.5 million in the three months ended June 30, 2012, compared to \$14.6 million in 2011. Losses from individual days of widely dispersed, exceptional weather events added \$2.6 million to losses in the three months ended June 30, 2012, as compared to \$7.1 million in 2011. Our net premiums earned also increased by 11.1% for the three months ended June 30, 2012, as compared to the same period in 2011. These factors contributed to our combined ratio of 141.8% for the three months ended June 30, 2012, declining from the 160.4% for the three months ended June 30, 2011.

The Company seeks to consistently generate underwriting profitability. Management evaluates NLASCO's loss and LAE ratio by bifurcating the losses to derive catastrophic and non-catastrophic loss ratios. The non-catastrophic loss ratio excludes Property Claims Services (PCS) events that exceed \$1.0 million of losses to NLASCO. Catastrophic events, including those that do not exceed our reinsurance retention, affect the Company's loss ratios. For the three months ended June 30, 2012, catastrophic events that did not exceed our reinsurance retention accounted for \$12.7 million of the total loss and loss adjustment expense, as compared to \$14.9 million for the same period in 2011. Excluding catastrophic events, our combined ratios for the three months ended June 30, 2012 and 2011 would have been 106.7% and 114.6%, respectively.

For the three months ended June 30, 2012, the Company incurred a benefit related to three catastrophes, Hurricane Ike, Hurricane Dolly and a 2010 Arizona storm, of \$0.2 million, as compared to losses of \$0.2 million for the same period in 2011. The benefit relates primarily to decreased reserves on previously settled hurricane claims and a reduction in reporting of Arizona claims. These losses have no effect on net loss and LAE incurred because the catastrophic events exceeded our retention and are fully recoverable from reinsurers. The primary financial effect is a benefit to reinstatement premiums for the three months ended June 30, 2012 of \$0.1 million, as compared to an expense of \$0.1 million for the same period in 2011.

Premiums. The property and casualty insurance industry is very competitive and is affected by soft and hard market business cycles. During a soft market, price competition tends to increase as insurers are willing to reduce premium rates in order to maintain growth in premium volume. The soft market makes it more difficult to attract new business, as well as retain exposures that are adequately priced. Although we recognize the need to remain competitive in the marketplace, the Company remains committed to its disciplined underwriting philosophy accepting only risks that are appropriately priced, while declining risks that it believes are under priced for the level of coverage provided.

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Direct premiums written by major product line for the three months ended June 30, 2012 and 2011, are presented in the table below (in thousands).

| | Three Months Ended June 30, | | | |
|---------------------------------|-----------------------------|-----------|----------|----------|
| | 2012 | 2011 | Change | % Change |
| Direct Premiums Written: | | | | |
| Homeowners | \$ 20,318 | \$ 19,464 | \$ 854 | 4.4% |
| Fire | 14,316 | 13,992 | 324 | 2.3% |
| Mobile Home | 8,108 | 7,167 | 941 | 13.1% |
| Commercial | 2,337 | 2,333 | 4 | 0.2% |
| Other | 114 | 114 | | 0.0% |
| | \$ 45,193 | \$ 43,070 | \$ 2,123 | 4.9% |

Total direct premiums written increased for the three months ended June 30, 2012 for all insurance products due to expanded distribution and growth on existing insurance products. Higher value homeowners and commercial insurance products generated \$0.3 million in direct premiums written for the three months ended June 30, 2012. Direct premiums written in Oklahoma, Georgia, Tennessee and Arizona increased a combined total of \$1.8 million in the three months ended June 30, 2012, as compared to the same period in 2011.

Net premiums written by major product line for the three months ended June 30, 2012 and 2011, are presented in the table below (in thousands).

| | Three Months Ended June 30, | | | |
|-----------------------------|-----------------------------|-----------|----------|----------|
| | 2012 | 2011 | Change | % Change |
| Net Premiums Written | | | | |
| Homeowners | \$ 18,715 | \$ 17,680 | \$ 1,035 | 5.9% |
| Fire | 13,188 | 12,710 | 478 | 3.8% |
| Mobile Home | 7,468 | 6,511 | 957 | 14.7% |
| Commercial | 2,152 | 2,119 | 33 | 1.6% |
| Other | 106 | 103 | 3 | 2.9% |
| | \$ 41,629 | \$ 39,123 | \$ 2,506 | 6.4% |

Total net premiums written increased for the three months ended June 30, 2012 for all insurance products, due to higher volume of direct written premiums and a decrease in catastrophic reinsurance costs of \$0.1 million.

Net premiums earned by major product line for the three months ended June 30, 2012 and 2011, are presented in the table below (in thousands).

| | Three Months Ended June 30, | | | |
|-----------------------------|-----------------------------|-----------|----------|----------|
| | 2012 | 2011 | Change | % Change |
| Net Premiums Earned: | | | | |
| Homeowners | \$ 16,294 | \$ 14,718 | \$ 1,576 | 10.7% |
| Fire | 11,470 | 10,580 | 890 | 8.4% |
| Mobile Home | 6,467 | 5,420 | 1,047 | 19.3% |
| Commercial | 1,871 | 1,764 | 107 | 6.1% |

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| | | | | |
|-------|-----------|-----------|----------|-------|
| Other | 93 | 86 | 7 | 8.1% |
| | \$ 36,195 | \$ 32,568 | \$ 3,627 | 11.1% |

Net premiums earned for the three months ended June 30, 2012 increased \$3.6 million, as compared to 2011. This increase is due to higher net written premiums of \$2.5 million and a decrease in change in net unearned premiums of \$1.1 million.

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Loss and Loss Adjustment Expenses. Loss and LAE are recognized based on formula and case basis estimates for losses reported with respect to direct business, estimates of unreported losses based on past experience and deduction of amounts for reinsurance placed with reinsurers. Loss and LAE for the three months ended June 30, 2012 was \$39.1 million, as compared to \$41.1 million for the same period in 2011. The decrease is primarily a result of lower widely dispersed, severe weather related losses of \$4.6 million, lower wind and hail storms that occurred in 2012 in Texas and Oklahoma of \$2.4 million, offset by higher non-catastrophic losses of \$4.8 million.

The loss and LAE ratio is calculated by taking the ratio of incurred losses and LAE to net premiums earned. The loss and LAE ratio for the three months ended June 30, 2012 and 2011 was 107.9% and 126.2%, respectively.

Policy Acquisition and Other Underwriting Expenses. Policy acquisition and other underwriting expenses for the three months ended June 30, 2012 and 2011 were as follows (in thousands).

| | 2012 | Three Months Ended June 30, | | | % Change |
|---|-----------|-----------------------------|----------|--|----------|
| | | 2011 | Change | | |
| Amortization of deferred policy acquisition costs | \$ 9,917 | \$ 8,489 | \$ 1,428 | | 16.8% |
| Other underwriting expenses | 2,876 | 3,108 | (232) | | -7.5% |
| Total policy acquisition and other underwriting expenses | 12,793 | 11,597 | 1,196 | | 10.3% |
| Agency expenses | (517) | (453) | (64) | | 14.1% |
| Total policy acquisition and other underwriting expenses less agency expenses | \$ 12,276 | \$ 11,144 | \$ 1,132 | | 10.2% |
| Net premiums earned | \$ 36,195 | \$ 32,568 | \$ 3,627 | | 11.1% |
| Underwriting expense ratio | 33.9% | 34.2% | -0.3% | | -0.9% |

Total policy acquisition and other underwriting expenses were \$12.8 million for the three months ended June 30, 2012, as compared to \$11.6 million for the same period in 2011, even though the underwriting expense ratio was favorable by 0.3%. Amortization of deferred policy acquisition costs increased \$1.4 million due to increase in direct written premiums of \$2.1 million during the three months ended June 30, 2012.

General and Administrative Expense. General and administrative expenses for the three months ended June 30, 2012 were \$2.9 million, as compared to \$1.6 million for the three months ended June 30, 2011, an increase of \$1.3 million. This increase was due to an increase in transaction fees of \$1.1 million related to the PlainsCapital Corporation transaction.

Depreciation and Amortization Expense. Depreciation and amortization expense for the three months ended June 30, 2012 was \$0.1 million less than the three months ended June 30, 2011, due to some equipment being fully depreciated.

Interest Expense. Interest expense for the three months ended June 30, 2012 was \$2.1 million, as compared to \$2.2 million for the same period in 2011, due to the reduction of \$6.9 million in debt.

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Income Taxes. The Company had a \$5.2 million income tax benefit for the three months ended June 30, 2012, compared to \$7.2 million benefit for the same period in 2011. The decrease in income tax benefit of \$2.0 million for the three months ended June 30, 2012, compared to the same period in 2011, is due to a decrease in net loss before income taxes of \$4.5 million, as the effective tax rate remained substantially unchanged.

Net Loss Attributable to Common Stockholders. As a result of the foregoing, our net loss attributable to common stockholders was \$10.7 million for the three months ended June 30, 2012, as compared to net loss of \$13.2 million for the three months ended June 30, 2011. The principal reasons for the loss in the second quarter of 2012 are incurred losses on wind and hail storms that occurred in Texas and Oklahoma and widely dispersed, exceptional weather related losses, which had incurred losses of \$12.5 million and \$2.6 million, respectively.

Table of Contents***Comparison of the Six Months Ended June 30, 2012 to the Six Months Ended June 30, 2011***

Revenue. Revenue for the six months ended June 30, 2012 was \$81.4 million, as compared to \$71.2 million for the same period in 2011. Net premiums earned were \$71.4 million for the six months ended June 30, 2012, as compared to \$63.5 million for the same period in 2011. The higher volume of earned premiums of \$7.9 million is primarily attributable to our expanded distribution and growth of our homeowners products, as well as a decrease in the cost of catastrophic reinsurance. Net investment income was \$2.2 million higher for the six months ended June 30, 2012, as compared to the same period in 2011, primarily due to the interest earned on the note portion of the SWS investment at HTH parent only and higher yields on cash and investments at NLASCO. Other income was \$3.6 million for the six months ended June 30, 2012, as compared to \$3.3 million for the same period in 2011 due to higher commission income from our agency operations. Total realized investment gains were \$38,000 for the six months ended June 30, 2012, as compared to an investment gain of \$31,000 for the same period in 2011.

Underwriting Results. The following table shows the components of the Company's underwriting loss for the six months ended June 30, 2012 and 2011. The Company's underwriting loss consists of net premiums earned, less loss and LAE and policy acquisition and other underwriting expenses. The underwriting results are discussed below (in thousands).

| | Six Months Ended June 30, | | | |
|--|----------------------------------|-------------|---------------|-----------------|
| | 2012 | 2011 | Change | % Change |
| Direct premiums written | \$ 85,934 | \$ 80,311 | \$ 5,623 | 7.0% |
| Net premiums written | 79,191 | 72,824 | 6,367 | 8.7% |
| Net premiums earned | \$ 71,350 | \$ 63,500 | \$ 7,850 | 12.4% |
| Loss and LAE | 61,613 | 57,105 | 4,508 | 7.9% |
| Policy acquisition and other underwriting expenses | 25,708 | 23,582 | 2,126 | 9.0% |
| Underwriting loss | \$ (15,971) | \$ (17,187) | \$ 1,216 | -7.1% |
| Agency expenses | \$ (964) | \$ (886) | \$ (78) | -8.8% |
| Loss and LAE ratio | 86.4% | 89.9% | -3.5% | |
| Underwriting expense ratio | 34.7% | 35.7% | -1.0% | |

The loss and LAE ratio is loss and LAE divided by net premiums earned for the same period. The underwriting expense ratio is policy acquisition and other underwriting expense less agency expenses, divided by net premiums earned for the same period. Combined ratio gives you the sum of both ratios.

Our combined ratio for the six months ended June 30, 2012 is 121.1%, as compared to 125.6% for the same period in 2011. The 4.5% decrease was due to an increase in net premiums earned of \$7.9 million, offset by an increase in loss and LAE and policy acquisition and other underwriting expenses of \$6.6 million. Net premiums earned increased 12.4% in the six months ended June 30, 2012, as compared to the same period in 2011, due to a \$12.2 million increase in volume of written premiums over the last twelve months. Loss and LAE increased 7.9% in the six months ended June 30, 2012, as compared to 2011, due to higher incurred losses associated with wind and hail storms that occurred in Texas and Oklahoma and additional losses associated with a 12.4% increase in earned premiums. Texas typically experiences seasonal wind and hail storms; however, NLASCO suffered significant losses from four storms that created \$12.5 million in incurred losses. Policy acquisition and other underwriting expenses increased 9.0% for the six months ended June 30, 2012, as compared to 2011, which is a result of increased direct written premiums, as the underwriting expense ratio was favorable by 1.0%.

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The Company seeks to consistently generate underwriting profitability. Management evaluates NLASCO's loss and LAE ratio by bifurcating the losses to derive catastrophic and non-catastrophic loss ratios. The non-catastrophic loss ratio excludes Property Claims Services (PCS) events that exceed \$1.0 million of losses to NLASCO. Catastrophic events, including those that do not exceed our reinsurance retention, affect the Company's loss ratios. For the six months ended June 30, 2012, catastrophic events that did not exceed our reinsurance retention accounted for \$14.0 million of the total loss and loss adjustment expense, of which \$12.5 million related to the 2012 accident year and \$1.5 million related to the 2011 accident year, as compared to \$15.8 million for the same period in 2011. Additionally, there were widely dispersed, exceptional weather related losses that added \$5.4 million in losses, as compared to \$7.1 million in 2011. Excluding catastrophic events, our combined ratios for the six months ended June 30, 2012 and 2011 would have been 101.5% and 101.1%, respectively.

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For the six months ended June 30, 2012, the Company incurred a benefit related to three catastrophes, Hurricane Ike, Hurricane Dolly and a 2010 Arizona storm, of \$0.6 million, as compared to a loss of \$3.2 million for the same period in 2011. The benefit in the six months ended June 30, 2012, relate primarily to decreased reserves on previously settled hurricane claims and a reduction in reporting on the Arizona storm. These losses have no effect on loss and LAE incurred because the catastrophic events exceeded our retention and are fully recoverable from reinsurers. The primary financial effect is the benefit to reinstatement premium payable to the affected reinsurers. For the six months ended June 30, 2012, the Company incurred a benefit to reinstatement premiums of \$0.1 million, as compared to an expense of \$0.5 million in 2011.

Premiums. The property and casualty insurance industry is very competitive and is affected by soft and hard market business cycles. During a soft market, price competition tends to increase as insurers are willing to reduce premium rates in order to maintain growth in premium volume. The soft market makes it more difficult to attract new business, as well as retain exposures that are adequately priced. Although we recognize the need to remain competitive in the marketplace, the Company remains committed to its disciplined underwriting philosophy accepting only risks that are appropriately priced, while declining risks that it believes are under priced for the level of coverage provided. Due to several catastrophic events and elevated reinsurance costs, NLASCO exited underwriting wind coverage along the Texas seacoast in March 2011.

Direct premiums written by major product line for the six months ended June 30, 2012 and 2011, are presented in the table below (in thousands).

| | Six Months Ended June 30, | | | |
|---------------------------------|---------------------------|-----------|----------|----------|
| | 2012 | 2011 | Change | % Change |
| Direct Premiums Written: | | | | |
| Homeowners | \$ 37,989 | \$ 35,769 | \$ 2,220 | 6.2% |
| Fire | 27,097 | 26,203 | 894 | 3.4% |
| Mobile Home | 16,218 | 13,844 | 2,374 | 17.1% |
| Commercial | 4,459 | 4,341 | 118 | 2.7% |
| Other | 171 | 154 | 17 | 11.0% |
| | \$ 85,934 | \$ 80,311 | \$ 5,623 | 7.0% |

Total direct premiums written increased for the six months ended June 30, 2012, for all insurance products, due to expanded distribution and growth of existing insurance products. Higher value homeowners and commercial insurance products generated \$1.3 million in direct written premiums for the six months ended June 30, 2012. Direct premiums written in Oklahoma, Georgia, Tennessee and Arizona increased \$4.4 million in the six months ended June 30, 2012, as compared to the same period in 2011.

Net premiums written by major product line for the six months ended June 30, 2012 and 2011, are presented in the table below (in thousands).

| | Six Months Ended June 30, | | | |
|-----------------------------|---------------------------|-----------|----------|----------|
| | 2012 | 2011 | Change | % Change |
| Net Premiums Written | | | | |
| Homeowners | \$ 35,008 | \$ 32,435 | \$ 2,573 | 7.9% |
| Fire | 24,971 | 23,760 | 1,211 | 5.1% |
| Mobile Home | 14,945 | 12,554 | 2,391 | 19.0% |
| Commercial | 4,109 | 3,936 | 173 | 4.4% |
| Other | 158 | 139 | 19 | 13.7% |
| | \$ 79,191 | \$ 72,824 | \$ 6,367 | 8.7% |

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Total net premiums written increased for the six months ended June 30, 2012 for all insurance products due to the result of higher direct written premiums and a decrease in reinsurance costs of \$0.3 million.

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Net premiums earned by major product line for the six months ended June 30, 2012 and 2011, are presented in the table below (in thousands).

| | Six Months Ended June 30, | | Change | % Change |
|-----------------------------|---------------------------|-----------|----------|----------|
| | 2012 | 2011 | | |
| Net Premiums Earned: | | | | |
| Homeowners | \$ 31,543 | \$ 28,283 | \$ 3,260 | 11.5% |
| Fire | 22,498 | 20,718 | 1,780 | 8.6% |
| Mobile Home | 13,465 | 10,946 | 2,519 | 23.0% |
| Commercial | 3,702 | 3,432 | 270 | 7.9% |
| Other | 142 | 121 | 21 | 17.4% |
| | \$ 71,350 | \$ 63,500 | \$ 7,850 | 12.4% |

Net premiums earned for the six months ended June 30, 2012 were up \$7.9 million, as compared to the same period of 2011, which is a result of higher net premiums written of \$6.4 million and a decrease in the change in net unearned premiums of \$1.5 million.

Loss and Loss Adjustment Expenses. Loss and LAE are recognized based on formula and case basis estimates for losses reported with respect to direct business, estimates of unreported losses based on past experience and deduction of amounts for reinsurance placed with reinsurers. Loss and LAE for the six months ended June 30, 2012 was \$61.6 million, as compared to \$57.1 million for the same period in 2011. The increase is primarily the result of higher non-catastrophic losses of \$8.6 million, offset by lower widely dispersed, severe weather related losses of \$1.7 million and lower wind and hail storms that occurred in 2012 in Texas and Oklahoma of \$1.8 million.

The loss and LAE ratio is calculated by taking the ratio of incurred losses and LAE to net premiums earned. The loss and LAE ratio for the six months ended June 30, 2012 and 2011 was 86.4% and 89.9%, respectively.

Policy Acquisition and Other Underwriting Expenses. Policy acquisition and other underwriting expenses for the six months ended June 30, 2012 and 2011 were as follows (in thousands).

| | Six Months Ended June 30, | | Change | % Change |
|---|---------------------------|-----------|----------|----------|
| | 2012 | 2011 | | |
| Amortization of deferred policy acquisition costs | \$ 19,146 | \$ 16,669 | \$ 2,477 | 14.9% |
| Other underwriting expenses | 6,562 | 6,913 | (351) | -5.1% |
| Total policy acquisition and other underwriting expenses | 25,708 | 23,582 | 2,126 | 9.0% |
| Agency expenses | (964) | (886) | (78) | 8.8% |
| Total policy acquisition and other underwriting expenses less agency expenses | \$ 24,744 | \$ 22,696 | \$ 2,048 | 9.0% |
| Net premiums earned | \$ 71,350 | \$ 63,500 | \$ 7,850 | 12.4% |
| Underwriting expense ratio | 34.7% | 35.7% | -1.0% | -2.8% |

Total policy acquisition and other underwriting expenses are up \$2.1 million due to the increase in amortization of deferred policy acquisition costs of \$2.5 million, offset by a decrease in other underwriting expenses of \$0.4 million. Amortization of deferred policy acquisition costs increased \$2.5 million due to an increase in direct written premium of \$5.6 million in the six months ended June 30, 2012 as compared to the same period in 2011.

General and Administrative Expense. General and administrative expenses for the six months ended June 30, 2012 were \$4.6 million, as compared to \$3.5 million for the six months ended June 30, 2011, an increase of \$1.1 million. This increase was due to an increase in transaction fees related to potential acquisitions of \$0.6 million and an increase in salaries and benefits of \$0.4 million.

Depreciation and Amortization Expense. Depreciation and amortization expense for the six months ended June 30, 2012 and 2011 was \$0.7 million and \$0.9 million, respectively. The decrease in 2012 is primarily due to some equipment being fully depreciated.

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Interest Expense. Interest expense for the six months ended June 30, 2012 and 2011 was \$4.3 million and \$4.4 million, respectively. The decrease is due to the reduction of \$6.9 million in debt.

Income Taxes. The Company had a \$5.0 million income tax benefit for the six months ended June 30, 2012, compared to a \$6.4 million benefit for the same period in 2011. The decrease in income tax benefit of \$1.4 million for the six months ended June 30, 2012, compared to the same period in 2011, is due to a decrease in operating loss of \$2.9 million, as the effective tax rate remained substantially unchanged.

Net Loss Attributable to Common Stockholders. As a result of the foregoing, our net loss attributable to common stockholders was \$10.4 million for the six months ended June 30, 2012, as compared to net loss of \$11.8 million for the six months ended June 30, 2011. The principal reasons for the loss in the second quarter of 2012 are incurred losses on wind and hail storms that occurred in Texas and Oklahoma and widely dispersed, exceptional weather related losses, which had incurred losses of \$14.0 million and \$5.4 million, respectively.

LIQUIDITY AND CAPITAL RESOURCES

General

Hilltop is a holding company whose assets primarily consist of the stock of its subsidiaries and invested assets with a combined value of approximately \$922 million at June 30, 2012. At June 30, 2012, the Company had invested approximately \$576 million in cash and cash equivalents, consisting of approximately \$529 million owned by the parent company and \$48 million owned by NLASCO and its subsidiaries. These deposits are in excess of the Federal Deposit Insurance Corporation insurance limit; however, the Company does not believe that it is exposed to any significant credit risk on cash based on the size and financial strength of the financial institutions in which the funds are held.

On May 8, 2012, we entered to a definitive merger agreement with PlainsCapital Corporation, whereby it will become a wholly owned subsidiary of us. The purchase consideration to PlainsCapital Corporation shareholders includes approximately 27.5 million shares of our common stock and approximately \$318 million of cash. After giving effect to the merger and its related transaction expenses, we expect to have approximately \$200 million of available cash at the parent company.

On the other hand, we will be required to pay PlainsCapital Corporation a termination of \$17.5 million if the merger agreement is terminated under certain circumstances, including, among others, our failure to receive stockholder approval. Accordingly, upon such an event, our available cash would be reduced by \$17.5 million.

At June 30, 2012, we had approximately \$576 million of cash and cash equivalents and \$216 million of investments, as compared to approximately \$579 million of cash and cash equivalents and \$224 million of investments as of December 31, 2011.

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As of June 30, 2012, our short-term liquidity needs included funds to pay our insurance claims and funds to service our debt.

Restrictions on Dividends and Distributions

Aside from investment income on Hilltop's invested assets and available cash, as a holding company, Hilltop relies on dividends and other permitted distributions from its subsidiaries. The payment of dividends from Hilltop's insurance subsidiaries, NLIC and ASIC, are subject to significant limitations under debt agreements, which limit their ability to declare and pay dividends in the event of a default.

Additionally, under Texas State Insurance Law for property and casualty companies, all dividends must be distributed out of earned surplus only. Furthermore, without the prior approval of the Commissioner of the Texas Department of Insurance, dividends cannot be declared or distributed that exceed the greater of ten percent of the company's surplus, as shown by its last statement on file with the Commissioner, and 100% of net income for such period. At June 30, 2012, the maximum dividends that may be paid in 2012, without regulatory approval, is approximately \$11.9 million.

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Regulations of the Texas Department of Insurance require insurance companies to maintain minimum levels of statutory surplus to ensure their ability to meet their obligations to policyholders. At June 30, 2012, the Company's insurance subsidiaries had statutory surplus in excess of the minimum required.

Also, the National Association of Insurance Commissioners, or NAIC, has adopted risk-based capital, or RBC, requirements for insurance companies that establish minimum capital requirements relating to insurance risk and assesses credit risk, interest rate risk and business risk. The formula is used by the NAIC and certain state insurance regulators as an early warning tool to identify companies that require additional scrutiny or regulatory action. At June 30, 2012, the Company's insurance subsidiaries' RBC ratio exceeded the level at which regulatory action would be required.

We believe that restrictions on the payments of dividends by our subsidiary companies will not have a material impact on our ability to carry out our normal business activities.

Sources and Uses of Funds

Our liquidity requirements are met primarily by positive cash flow from our normal operations, available cash, and investment activity. Primary sources of cash from insurance operations are premiums and other considerations, net investment income and investment sales and maturities. Primary uses of cash include payments of benefits, operating expenses, and purchases of investments.

Our insurance operating subsidiary, NLASCO, primary investment objective is to preserve capital. Our strategy is to purchase securities in sectors that represent the most attractive relative value. Bonds, cash and short-term investments constitute \$197 million, or 94.3%, of our investments at NLASCO at June 30, 2012. Although there is no intent to dispose of these investments at this time, our bonds are substantially in readily marketable securities.

Our management generally meets monthly to review the performance of investments and monitor market conditions for investments that would warrant any revision to investment guidelines.

Cash used in operations was \$1.6 million for the six months ended June 30, 2012, primarily due to a net loss of \$10.4 million, increases in deferred income taxes of \$5.0 million, increases in deferred acquisition costs of \$1.5 million and increases in premiums receivable of \$2.4 million, which were offset by depreciation and amortization of \$0.7 million, increase in unearned premiums of \$6.0 million, stock grant compensation expense of \$0.3 million, decrease in reinsurance recoverables of \$2.7 million, increase in loss and LAE reserves of \$7.3 million and other operating assets and liabilities of \$0.7 million. Cash provided by operations was \$0.1 million for the six months ended June 30, 2011, primarily due to a net loss of \$11.8 million, increases in deferred income taxes of \$6.3 million, \$2.4 million increase in deferred acquisition costs, \$0.3 million decrease in payable to related party, and \$3.1 million increase in premium and agents balances, offset by an increase in depreciation and amortization of \$0.9 million, unearned premiums increase of \$9.3 million, decrease in reinsurance recoverables of \$3.7 million, increase in loss and loss adjustment expense reserves of \$9.7 million and changes in operating assets and liabilities of \$0.2 million.

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Cash provided by investing activities was \$0.6 million in the six months ended June 30, 2012, primarily due to proceeds from sales and maturities of available-for-sale securities of \$3.4 million, offset by purchases of available-for-sale securities of \$2.7 million. Cash used in investing activities was \$10.4 million in the six months ended June 30, 2011 primarily due to purchases of available-for-sale securities of \$16.3 million, which was offset by proceeds from sales of available-for-sale securities of \$2.4 million and proceeds from maturities of available-for-sale securities of \$3.8 million.

Cash used in financing activities was \$1.2 million in the six months ended June 30, 2012, due to repurchase of common stock. There were no financing activities for the six months ended June 30, 2011.

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We believe that existing cash and investment balances, when combined with anticipated cash flows from operations and dividends from our insurance companies, will be adequate to meet our expected liquidity needs for the reasonably foreseeable future, including after giving effect to the proposed merger with PlainsCapital Corporation. We will continue to pursue and investigate possible strategic opportunities. In regards to strategic acquisitions, we may need to secure external financing. We cannot assure you that we will be successful in obtaining any such financing or in the implementation of our business plan.

Inflation

Inflation in the U.S. has been relatively low in recent years and did not have a material impact on our results of operations for the three months ended June 30, 2012 and 2011. Although the impact of inflation has been relatively insignificant in recent years, it remains a factor in the United States economy and may increase the cost of acquiring or replacing property and equipment and the costs of labor and utilities.

COMMITMENTS

NLASCO's loss reserves do not have contractual maturity dates. However, based on historical payment patterns, the following table estimates when management expects the loss reserves to be paid. The timing of claim payments is subject to significant uncertainty. NLASCO maintains a portfolio of investments with varying maturities to provide adequate cash flows for the payment of claims.

| | Reserves (in thousands) | |
|------------|------------------------------------|--------|
| 2012 | \$ | 19,429 |
| 2013 | | 17,345 |
| 2014 | | 7,448 |
| 2015 | | 4,479 |
| 2016 | | 2,188 |
| Thereafter | | 1,198 |
| | \$ | 52,087 |

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our future income, cash flows and fair values relevant to financial instruments are dependent upon market interest rates. Market risk relates to the risk of loss from adverse changes in market prices and interest rates. We may use some derivative financial instruments to manage, or hedge, interest rate risks related to our borrowings from time to time. We do not use derivatives for trading or speculative purposes and only enter into contracts with major financial institutions based on their credit rating and other factors. As of June 30, 2012, we did not have any derivative financial instruments.

As of June 30, 2012, our total debt outstanding was approximately \$131 million, comprised of \$83.9 million, or 64%, subject to fixed interest rates and \$47.5 million, or 36%, subject to variable interest rates.

If LIBOR and the prime rate were to increase by one eighth of one percent (0.125%), the increase in interest expense on the variable rate debt would decrease future earnings and cash flows by approximately \$59,000 annually.

Interest risk amounts were determined by considering the impact of hypothetical interest rates on our financial instruments. These analyses do not consider the effect of any change in overall economic activity that could occur in that environment. Further, in the event of a change of that magnitude, we may take actions to further mitigate our exposure to the change. However, due to the uncertainty of the specific actions that would be taken and their possible effects, these analyses assume no changes in our financial structure.

The fair value of debt outstanding as of June 30, 2012 was approximately \$133.3 million.

The following table sets forth certain information with respect to our indebtedness outstanding as of June 30, 2012 (in thousands).

| | Principal Commitments | | |
|------------------------|-----------------------|-----------|------------|
| | Fixed | Variable | Total |
| 2016 and Thereafter | 83,950 | 47,500 | 131,450 |
| Commitments | \$ 83,950 | \$ 47,500 | \$ 131,450 |

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ITEM 4. CONTROLS AND PROCEDURES

(a) Disclosure Controls and Procedures. The Company's management, with the supervision and participation of the Company's Chief Executive Officer and Chief Accounting Officer, has evaluated the effectiveness of the design and operation of Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based on such evaluation, the Company's Chief Executive Officer and Chief Accounting Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 and are effective in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Accounting Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in internal control over financial reporting. There have not been any changes in our internal control over financial reporting (as defined in Rule 13a-15(f) promulgated under the Securities Exchange Act of 1934) during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1A. RISK FACTORS

The pending merger with PlainsCapital Corporation is subject to closing conditions, the failure of any of which could result in our inability to consummate the transaction.

On May 8, 2012, we entered into an Agreement and Plan of Merger with PlainsCapital Corporation. The closing of the transaction is subject to the satisfaction of certain conditions, including the receipt of all necessary or advisable regulatory approvals and the approval of PlainsCapital Corporation's and our respective shareholders. No assurance can be given as to when or whether these approvals will be received.

Furthermore, if the merger agreement is terminated (i) by either party because Hilltop's stockholders failed to approve the stock issuance proposal at a meeting called for such purpose; or (ii) by PlainsCapital Corporation because Hilltop or the board of directors of Hilltop submits the stock issuance proposal to its stockholders without a recommendation for approval, or otherwise withdraws or materially and adversely modifies its recommendation, or recommends to its stockholders an alternate acquisition proposal, Hilltop will be required to pay PlainsCapital Corporation a termination fee of \$17.5 million.

We may fail to realize all of the anticipated benefits of our pending acquisition of PlainsCapital Corporation.

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The success of our pending acquisition of PlainsCapital Corporation will depend on, among other things, the ability to achieve certain operating results at PlainsCapital Corporation. If the financial condition or result of operations of PlainsCapital Corporation is materially different than those that we forecasted, the anticipated benefits of the acquisition may not be realized fully, or at all, or may take longer to realize than expected.

Hilltop and PlainsCapital Corporation have operated and, until the completion of the merger, will continue to operate, independently. The companies may have difficulty addressing possible differences in corporate cultures and management philosophies. It is also possible that clients, customers, depositors and counterparties of PlainsCapital Corporation could choose to discontinue their relationships with the company post-merger, which would adversely affect our future performance.

ITEM 6. EXHIBITS

(a) Exhibits:

See Exhibit Index

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SIGNATURES

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

HILLTOP HOLDINGS INC.

Date: August 6, 2012

By: /s/ DARREN PARMENTER
Darren Parmenter
Senior Vice President and Chief Accounting Officer
(Principal financial and accounting officer and duly
authorized officer)

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EXHIBIT INDEX

| Exhibit Number | Exhibit Title |
|---------------------------|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended. |
| 31.2 | Certification of Chief Accounting Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended. |
| 32.1 | Certification of Chief Executive Officer of Hilltop Holdings Inc., pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Chief Accounting Officer of Hilltop Holdings Inc., pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Labels Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |
