Old Republic International Corp. (ORI)

Updated April 25th, 2018 by Josh Arnold

Key Metrics

Current Price:	$21	**5 Year CAGR Estimate:**	12.4%	**Quality Percentile:**	N/A
Fair Value Price:	$23	**5 Year Growth Estimate:**	7.0%	**Momentum Percentile:**	N/A
% Fair Value:	92%	**5 Year Valuation Multiple Estimate:**	1.7%	**Total Return Percentile:**	N/A
Dividend Yield:	3.7%	**5 Year Price Target**	$33	**Valuation Percentile:**	N/A

Overview & Current Events

Old Republic was founded back in 1907 and the past 111 years haven't always been easy. But the company has persevered and today, it markets, underwrites and provides risk management services for a variety of general and title insurances. It does in excess of $6B in annual revenue and its market cap is $6.3B.

The company's recent Q4 saw 14% higher pretax income on growth in its investment gains as well as continued improvement in its RFIG run-off segment. ORI has been dwindling its RFIG business steadily and each quarter sees lower asset values. With that comes lower losses and thus, higher pretax income. RFIG's Q4 showed some of its growth potential through a combination of prudent investments, strong premium growth and lower losses from RFIG.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$0.81	$0.67	$0.16	$0.86	$0.39	$1.25	$0.84	$1.28	$1.47	$1.11	***$1.85***	***$2.60***
DPS	$0.67	$0.68	$0.69	$0.70	$0.71	$0.72	$0.73	$0.74	$0.75	$0.76	***$0.78***	***$0.88***

As you'd expect, ORI's EPS has been all over the place in the past decade. Insurers have notoriously volatile earnings and ORI is certainly no exception, having seen its earnings plummet and skyrocket multiple times in this period. However, ORI seems to have turned a corner when it comes to growth in earnings and as a result, we are forecasting 7% annual EPS growth going forward. This is a slight reduction compared to its long-term average but after years of sluggish performance, ORI looks poised to improve.

This rate of growth will be achieved as ORI looks to continue its low to mid-single digit growth in premiums, strong investment income as well as lower losses from RFIG. Further, ORI's margins should continue to move up in excess of revenue growth as its claims continue to fall from elevated levels. Keep in mind, however, that gains likely will not be linear as the insurance business is highly cyclical. Still, ORI looks poised for significant growth ahead.

The dividend will likely continue to grow at a relatively slow pace as ORI's dividend increases in the past decade have been very small. It did pay a $1 special dividend early in 2018 but that is unlikely to become a normal practice. ORI's yield is still very strong even with its sluggish payout growth, so income investors will likely find it attractive.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	14.9	15.0	79.7	12.2	24.4	11.2	18.6	12.5	12.6	18.0	***11.5***	***12.5***
Avg. Yld.	5.5%	6.4%	5.4%	6.3%	7.3%	5.1%	4.7%	4.6%	4.1%	3.8%	***3.7%***	***2.7 %***

ORI's PE multiple has moved around a bunch but that has mostly been due to volatile earnings and not valuation resets from investors. The steady state P/E multiple for ORI is around 12.5, which is slightly higher than the current 11.5. We are therefore forecasting a small 1.7% tailwind to annual total returns from the valuation over the coming years.

In addition, we see the yield falling as improving earnings growth should send the stock price higher without the benefit of similar growth in the dividend. That combination should produce a much lower yield in the coming years from today's level of 3.7%, as we see it falling to 2.7% over time. ORI's improving earnings could spur management to boost the increases in the dividend, but that hasn't happened yet, as they instead opted for the special dividend in January.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
Op Mrgn	-25.3%	-7.2%	0.7%	-5.1%	-2.6%	12.4%	11.0%	11.0%	11.6%	11.6%	***12.5%***	***14.0%***
Debt/A	72%	73%	74%	76%	78%	77%	77%	77%	76%	76%	***76%***	***75%***
Int. Cov.	NMF	(12.3)	0.9	(4.6)	(3.7)	29.1	21.5	14.7	13.5	11.2	***14.0***	***18.0***
Payout	83%	101%	431%	81%	182%	58%	87%	59%	51%	68%	***42%***	***34%***
Std. Dev.	90.0%	51.6%	29.0%	35.9%	29.5%	21.5%	20.4%	19.5%	18.7%	16.6%	***21.0%***	***33.0%***

Given how volatile ORI's revenue and earnings have been, one is hardly surprised to see its quality metrics have experienced tremendous volatility as well. Its operating margins have been well into negative territory for years, but of late, ORI's recovery in earnings has produced strong operating margins that we expect will continue to gradually increase for the reasons stated above. Its debt has remained flat over the years, something we don't expect will change, but its interest coverage continues to improve as earnings afford ORI more breathing room with financing costs. The payout ratio has fallen significantly in recent years and given slow payout growth but strong earnings, that trend should continue. Overall, ORI is in significantly better shape than it was a few years ago.

ORI operates in a tremendously competitive field, making advantages hard to come by. However, it sets itself apart with its strong premiums against claims, the product of prudent underwriting. This has afforded it a compelling turnaround in recent years, something that was needed given the very tough time it had with the Great Recession. Keep in mind that for all its growth potential, investors would do well to remember that ORI will suffer during the next downturn.

Final Thoughts & Recommendation

Overall, ORI looks pretty compelling here if one can stomach the potential risk of owning an insurer. The stock is fairly valued and offers forecast total annual returns of 12.4% in the coming years, consisting of the current 3.7% yield, 1.7% tailwind from the rising valuation and 7% EPS growth. That makes ORI attractive for income investors, value investors and those seeking growth. The only caveat is that owning any insurer is an exercise in patience as ORI's growth will likely be far from linear. However, if one can move past that, it looks compelling here.

Total Return Breakdown by Year