Old Republic International Corp. (ORI)

Updated August 4th, 2018 by Josh Arnold

Key Metrics

Current Price:	$22	**5 Year CAGR Estimate:**	11.9%	**Volatility Percentile:**	12.4%
Fair Value Price:	$23	**5 Year Growth Estimate:**	7.0%	**Momentum Percentile:**	69.7%
% Fair Value:	94%	**5 Year Valuation Multiple Estimate:**	1.3%	**Valuation Percentile:**	72.5%
Dividend Yield:	3.6%	**5 Year Price Target**	$33	**Total Return Percentile:**	80.5%

Overview & Current Events

Old Republic was founded back in 1907 and the past 111 years have not 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 generates in excess of $6 billion in annual revenue and its market cap is $6.5 billion.

Old Republic reported second quarter earnings on 7/26/18 and results were quite strong. Total revenue was up 4.4% on strength in the general and title insurance businesses, which both saw mid-single digit increases. The company's RFIG run-off business contributed negatively to revenue growth but margins were robust. Pre-tax income rose 24% in Q2 as the flagship general insurance segment saw a 45% increase, more than offsetting a small decline in the title insurance business. In total, Old Republic's earnings-per-share nearly doubled from 35 cents to 66 cents; our estimates for this year remain unchanged at $1.85 per share in earnings.

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 would expect, Old Republic's earnings-per-share have been very volatile during the past decade. Insurers have notoriously unpredictable earnings and Old Republic is certainly no exception, having seen its earnings plummet and skyrocket multiple times in this period. However, it seems to have turned a corner when it comes to growth in earnings and as a result, we are forecasting 7% annual earnings-per-share growth going forward. This is a slight reduction compared to its long-term average but after years of sluggish performance, Old Republic looks poised to improve.

This rate of growth will be achieved as the company looks to continue its low to mid-single digit growth in premiums, strong investment income as well as lower losses from RFIG, like in in Q2. Further, margins should continue to move up in excess of revenue growth as its claims are falling from elevated levels. Keep in mind, however, that gains likely will not be linear as the insurance business is highly cyclical. Still, Old Republic looks poised for significant growth ahead.

The dividend will likely continue to grow at a relatively slow pace as 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. The stock'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	***11.7***	***12.5***
Avg. Yld.	5.5%	6.4%	5.4%	6.3%	7.3%	5.1%	4.7%	4.6%	4.1%	3.8%	***3.6%***	***2.7 %***

Old Republic's price-to-earnings multiple has been volatile in recent years but that has mostly been due to changes in earnings and not valuation resets from investors. The steady state price-to-earnings multiple for Old Republic is around 12.5, which is slightly higher than the current 11.7. We are therefore forecasting a modest 1.3% 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 3.6%, as we see it falling to 2.7% over time. 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%***

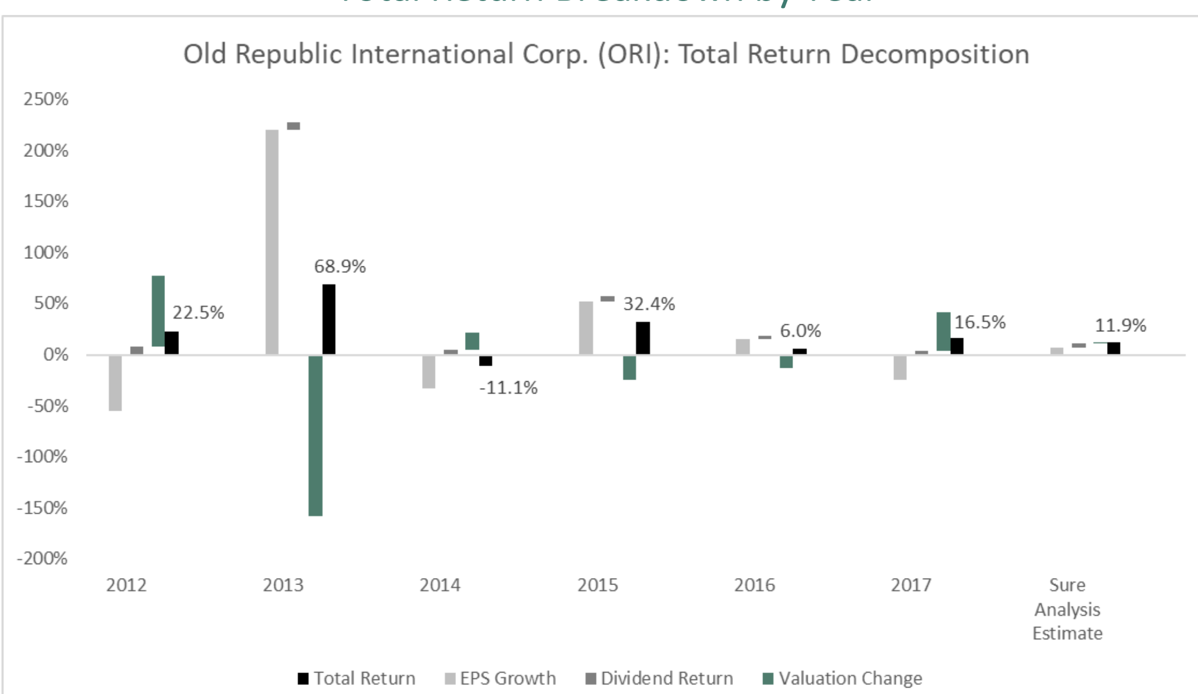
Given how unpredictable revenue and earnings have been, one is hardly surprised to see Old Republic's quality metrics have experienced tremendous volatility as well. Debt has remained flat over the years, something we do not expect to change, but its interest coverage continues to improve as earnings afford the company 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, Old Republic is in significantly better shape than it was a few years ago.

Old Republic 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. Investors would do well to remember that Old Republic, and indeed the insurance industry as a whole, will suffer during the next downturn.

Final Thoughts & Recommendation

Overall, Old Republic 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 11.9% in the coming years, consisting of the current 3.6% yield, 1.3% tailwind from the rising valuation and 7% earnings-per-share growth. That makes the stock attractive for income investors, value investors and those seeking growth. The only caveat is that owning any insurer is an exercise in patience as Old Republic's growth will likely be far from linear. However, if one can move past that, it looks attractive here and we rate it a buy based upon the high current yield and growth opportunities.

Total Return Breakdown by Year



Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.