Old Republic International Corp. (ORI)

Updated October 27th, 2018 by Josh Arnold

Key Metrics

Current Price:	$22	**5 Year CAGR Estimate:**	11.9%	**Volatility Percentile:**	10.4%
Fair Value Price:	$23	**5 Year Growth Estimate:**	7.0%	**Momentum Percentile:**	84.9%
% Fair Value:	94%	**5 Year Valuation Multiple Estimate:**	1.3%	**Growth Percentile:**	62.3%
Dividend Yield:	3.6%	**5 Year Price Target**	$33	**Valuation Percentile:**	55.4%
Dividend Risk Score:	A	**Retirement Suitability Score:**	A	**Total Return Percentile:**	63.1%

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 $6.6 billion.

Old Republic reported Q3 earnings on 10/25/18 and results beat expectations. General insurance net premiums rose 5% while title insurance premiums increased more than 7%. Claim costs also fell 19%, more than offsetting a 9% increase in SG&A costs. Old Republic is recovering nicely from a tough 2017 and Q3 results were very strong. In total, adjusted earnings-per-share came in at 56 cents versus just 9 cents in last year's Q3. We reiterate our estimate of $1.85 in earnings-per-share for this year as Old Republic continues to fire on all cylinders.

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***
Shares	241	241	259	259	259	260	261	262	263	269	***302***	***305***

As one 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 possible as the company looks to continue its low to mid-single digit growth in premiums, strong investment income as well as lower losses, like we saw in Q3. 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.

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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 has not 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%***

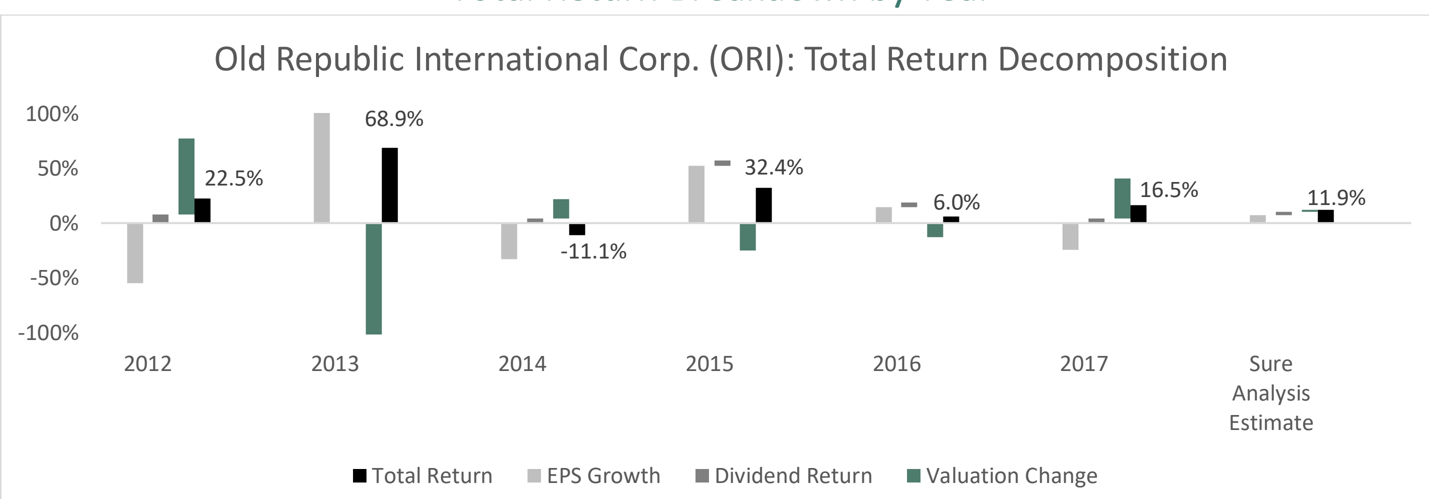
Given how unpredictable revenue and earnings have been, one is hardly surprised to see Old Republic's quality metrics have experienced tremendous volatility as well. Debt has remained flat over the years, something we do not expect to change, but its interest coverage continues to improve as earnings 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 compelling 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 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 and we rate it a buy based upon the high current yield and growth opportunities.

Total Return Breakdown by Year



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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.

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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	3238	3803.6	4102.6	4645.4	4969.8	5442.5	5530.5	5765.9	5900.3	6262.9
Net Profit	-558	-99.1	30.1	-140.5	-68.6	447.8	409.7	422.1	466.9	560.5
Net Margin	-17%	-2.6%	0.7%	-3.0%	-1.4%	8.2%	7.4%	7.3%	7.9%	8.9%
Free Cash Flow	565.6	532.9	-282.2	-94.9	532	686.7	-181.2	688.2	637.3	452.8
Income Tax	-261	-174.4	-2.5	-96.1	-59.8	225	199.7	209.6	219	164.8

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	13266	14190	15883	16050	16227	16534	16988	17102	18592	19404
Cash & Equivalents	63.9	77.3	127.3	93	101.2	153.3	136.7	159.8	145.7	125.9
Acc. Receivable	806.7	788.6	1022.9	4282.8	4371.7	4406.2	4710.1	4493.8	4621.7	4841.5
Total Liabilities	9526	10299	11761	12278	12631	12759	13064	13221	14131	14670
Accounts Payable	264.8	321.3	424	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Long-Term Debt	233	346.7	475	912.7	572.8	569.2	965	952.8	1528.5	1448.5
Total Equity	3740.3	3891.4	4121.4	3772.5	3596.2	3775	3924	3880.8	4460.6	4733.3
D/E Ratio	0.06	0.09	0.12	0.24	0.16	0.15	0.25	0.25	0.34	0.31

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	-4.2%	-0.7%	0.2%	-0.9%	-0.4%	2.7%	2.4%	2.5%	2.6%	3.0%
Return on Equity	-14%	-2.6%	0.8%	-3.6%	-1.9%	12.2%	10.6%	10.8%	11.2%	12.2%
ROIC	-13%	-2.4%	0.7%	-3.0%	-1.5%	10.5%	8.9%	8.7%	8.6%	9.2%
Shares Out.	241	241	259	259	259	260	261	262	263	269
Revenue/Share	13.99	16.14	17.00	18.21	19.43	18.53	18.74	19.47	19.91	20.92
FCF/Share	2.44	2.26	-1.17	-0.37	2.08	2.34	-0.61	2.32	2.15	1.51

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.