



# Old Republic International Corp. (ORI)

Updated July 29<sup>th</sup>, 2019 by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$23	<b>5 Year CAGR Estimate:</b>	11.3%	<b>Volatility Percentile:</b>	11.8%
<b>Fair Value Price:</b>	\$24	<b>5 Year Growth Estimate:</b>	7.0%	<b>Momentum Percentile:</b>	60.9%
<b>% Fair Value:</b>	96%	<b>5 Year Valuation Multiple Estimate:</b>	0.8%	<b>Growth Percentile:</b>	66.3%
<b>Dividend Yield:</b>	3.5%	<b>5 Year Price Target</b>	\$33	<b>Valuation Percentile:</b>	68.3%
<b>Dividend Risk Score:</b>	C	<b>Retirement Suitability Score:</b>	C	<b>Total Return Percentile:</b>	70.5%

## Overview & Current Events

Old Republic was founded back in 1907, and the past 112 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 capitalization is \$7 billion.

Old Republic reported Q2 earnings on 7/25/19 and results were largely in-line with expectations. Total revenue was up 3.2% to \$1.6 billion as net premiums and fees were up 2.8% and net investment income increased 5.7%. All of the company's operating segments produced higher revenue with general insurance leading the way at +5.1% year-over-year to \$850 million.

Operating expenses rose 4% year-over-year as claim costs rose 4.6%, sales and general expense rose 3.5%, and interest and other charges were up 4%. This led to operating income falling year-over-year from \$247 million to \$205 million. Old Republic's composite ratio, which is the amount it spends on expenses and claim costs as a percentage of revenue, rose from 94.3% to 95.2% thanks to higher operating expenses.

This sent earnings-per-share on an operating basis down from \$0.47 to \$0.45 in Q2. Headline earnings-per-share, which includes investment gains, was \$0.55 against \$0.66 in the year-ago period. Last year's Q2 included 19 cents of investment gains while this year's Q2 contained just 10 cents.

After a largely as expected Q2, we don't see any cause to reduce our earnings-per-share estimate for this year, and have left it unchanged at \$1.90.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	-\$0.67	-\$0.16	-\$0.86	-\$0.39	\$1.25	\$0.84	\$1.28	\$1.47	\$1.11	\$1.86	<b>\$1.90</b>	<b>\$2.66</b>
<b>DPS</b>	\$0.68	\$0.69	\$0.70	\$0.71	\$0.72	\$0.73	\$0.74	\$0.75	\$0.76	\$0.78	<b>\$0.80</b>	<b>\$0.96</b>
<b>Shares</b>	241	259	259	259	260	261	262	263	269	303	<b>310</b>	<b>350</b>

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, with Q1 results somewhat indicative of this. 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, particularly if equity markets remain strong.

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.

*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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## Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	---	---	---	---	11.2	18.6	12.5	12.6	18.0	11.4	<b>12.0</b>	<b>12.5</b>
Avg. Yld.	6.4%	5.4%	6.3%	7.3%	5.1%	4.7%	4.6%	4.1%	3.8%	3.7%	<b>3.5%</b>	<b>2.9%</b>

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. Our estimate of fair value for Old Republic is 12.5 times earnings, which is slightly higher than the current 12, and lower than its average of 14. We are therefore forecasting a modest 0.8% tailwind to annual total returns from the valuation over the coming years.

In addition, we see the yield falling as improving earnings growth could send the stock price higher without the benefit of similar growth in the dividend. That combination would produce a much lower yield in the coming years from today's level of 3.5%, as we see it falling to 2.9% 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	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	---	---	---	---	58%	87%	59%	51%	68%	42%	<b>42%</b>	<b>36%</b>

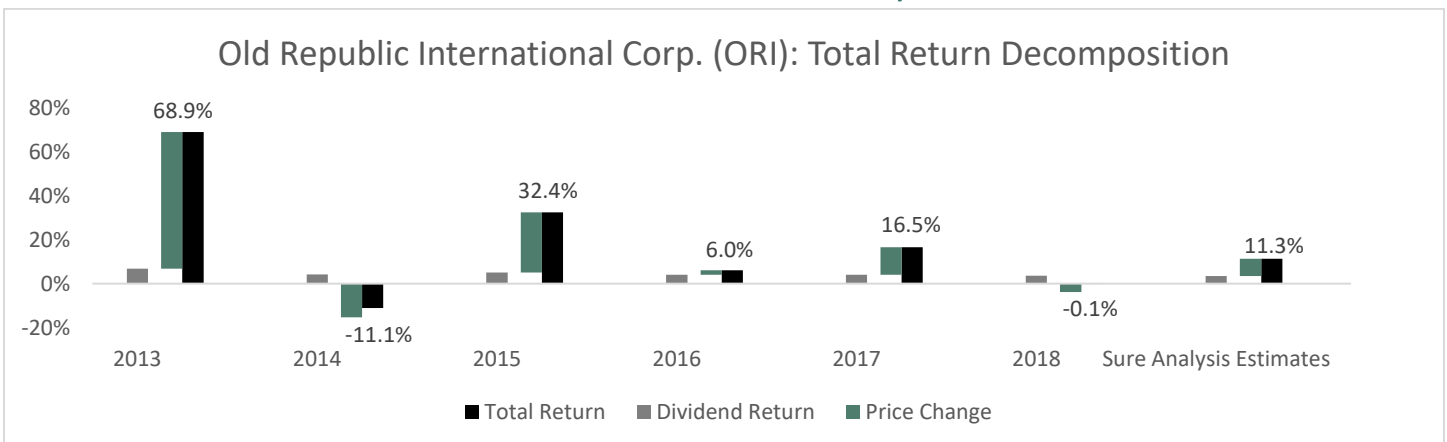
The payout ratio has fallen significantly in recent years, given slow payout growth coupled with strong earnings; that trend should continue. Overall, Old Republic is in significantly better shape than it was a few years ago.

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 now essentially fairly valued and offers robust forecast total annual returns of 11.3% in the coming years, consisting of the current 3.5% yield, 0.8% 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 constant. However, if one can move past that, it looks attractive and we continue to rate it a buy based upon the high current yield and growth opportunities.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Revenue</b>	3804	4103	4645	4970	5443	5531	5766	5900	6263	6022
<b>Net Profit</b>	-99	30	-141	-69	448	410	422	467	561	371
<b>Net Margin</b>	-2.6%	0.7%	-3.0%	-1.4%	8.2%	7.4%	7.3%	7.9%	8.9%	6.2%
<b>Free Cash Flow</b>	533	-282	-95	532	687	-181	688	637	453	761
<b>Income Tax</b>	-174	-3	-96	-60	225	200	210	219	165	68

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets</b>	14190	15883	16050	16227	16534	16988	17102	18592	19404	19327
<b>Cash &amp; Equivalents</b>	77	127	93	101	153	137	160	146	126	100
<b>Acc. Receivable</b>	789	1023	4283	4372	4406	4710	4494	4622	4842	4984
<b>Total Liabilities</b>	10299	11761	12278	12631	12759	13064	13221	14131	14670	14181
<b>Long-Term Debt</b>	347	475	913	573	569	965	953	1529	1449	981
<b>Total Equity</b>	3891	4121	3773	3596	3775	3924	3881	4461	4733	5146
<b>D/E Ratio</b>	0.09	0.12	0.24	0.16	0.15	0.25	0.25	0.34	0.31	0.19

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Return on Assets</b>	-0.7%	0.2%	-0.9%	-0.4%	2.7%	2.4%	2.5%	2.6%	3.0%	1.9%
<b>Return on Equity</b>	-2.6%	0.8%	-3.6%	-1.9%	12.2%	10.6%	10.8%	11.2%	12.2%	7.5%
<b>ROIC</b>	-2.4%	0.7%	-3.0%	-1.5%	10.5%	8.9%	8.7%	8.6%	9.2%	6.0%
<b>Shares Out.</b>	241	259	259	259	260	261	262	263	269	303
<b>Revenue/Share</b>	16.14	17.00	18.21	19.43	18.53	18.74	19.47	19.91	20.92	20.00
<b>FCF/Share</b>	2.26	-1.17	-0.37	2.08	2.34	-0.61	2.32	2.15	1.51	2.53

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

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