



The Travelers Companies (TRV)

Updated January 23rd, 2019 by Josh Arnold

Key Metrics

Current Price:	\$122	5 Year CAGR Estimate:	8.3%	Volatility Percentile:	11.4%
Fair Value Price:	\$121	5 Year Growth Estimate:	6.0%	Momentum Percentile:	42.2%
% Fair Value:	101%	5 Year Valuation Multiple Estimate:	-0.2%	Growth Percentile:	50.1%
Dividend Yield:	2.5%	5 Year Price Target	\$162	Valuation Percentile:	42.4%
Dividend Risk Score:	A	Retirement Suitability Score:	B	Total Return Percentile:	36.0%

Overview & Current Events

The Travelers Companies was founded in 1864 in Hartford, CT by two local businessmen. The company began with life and accident insurance but has expanded into various other types of coverage in the 150+ years since then. Today, it enjoys \$29 billion in annual revenue and a \$32 billion market capitalization. The company offers a wide and deep variety of protection products for auto, home and business customers. It is also a member of the Dow Jones Industrial Average, making it the only property casualty insurance provider in the prestigious index.

Travelers reported Q4 earnings on 1/22/19 and results were largely in-line with estimates, but weaker than the year-ago period thanks to the California wildfires and Hurricane Michael. Q4 core earnings-per-share came to \$2.13, missing estimates by a penny and ceding nearly 7% against the comparable period last year.

Total revenue was up 5% thanks mostly to a 4% gain in premiums underwritten. However, Travelers' combined ratio, which is a measure of profitability, deteriorated 200bps to 97.5% of revenue, thanks to higher claims. Likewise, core return on equity declined year-over-year from 11.1% to 10%.

Travelers saw particular strength in its Workers' Compensation products, as well as Surety, Management Liability and Personal Auto. Commercial Auto was a weak spot that was impacted negatively by higher loss estimates. Net investment income rose 5% year-over-year, earning the company \$630 million pre-tax thanks to better returns in its fixed income portfolio. The company also returned \$375 million to shareholders in Q4, including \$170 million of share repurchases.

We're out with an initial estimate of \$11 in earnings-per-share for 2019 as we expect higher revenue and more normalized losses, building upon the success of 2018.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$6.32	\$6.31	\$3.25	\$6.21	\$9.46	\$10.56	\$10.87	\$10.13	\$7.27	\$8.94	\$11.00	\$14.72
DPS	\$1.26	\$1.44	\$1.64	\$1.79	\$1.96	\$2.15	\$2.38	\$2.68	\$2.83	\$3.03	\$3.08	\$4.85
Shares	520	435	393	377	354	322	296	280	271	266	260	235

After strong growth coming out of the Great Recession, Travelers has failed to regain its 2014 high of \$10.56 in earnings-per-share. However, we believe that 2019 will be the year that occurs with our estimate of \$11. In total, we are expecting 6% earnings-per-share growth annually in the coming years, following a much higher rate of growth for 2019.

Travelers will achieve this growth primarily from higher underwritten premiums and the buyback, although margins should play a part as well, as long as there are not any enormous catastrophes. We see low single digit gains from higher revenue as well as a similar tailwind from the company's famous buyback, which has reduced the float by more than half in just the past decade alone. Recent reductions have been smaller in size given the higher share price, but Travelers is committed to reducing its share count over time. Lower operating expenses should also provide a bit of a boost to earnings, but the Travelers story really is about higher premiums, lower catastrophe losses, and a lower share count.

The dividend has been raised in the mid-single digit range annually and we expect that will continue for the foreseeable future. Travelers is not an income stock any longer given the higher share price, but its 2.5% yield is respectable, and the payout will continue to grow at roughly the pace of earnings, or perhaps slightly more.

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	7.0	8.2	17.4	10.3	8.8	8.8	9.7	11.2	17.2	14.7	11.1	11.0
Avg. Yld.	2.8%	2.8%	2.9%	2.8%	2.3%	2.3%	2.3%	2.4%	2.3%	2.3%	2.5%	3.0%

Travelers' price-to-earnings multiple has mostly stayed under 10 for the past decade but today, stands at 11.1. We therefore see the stock as fairly valued given that our estimate of fair value is 11. That implies essentially no impact to total returns due to the valuation.

The yield is near its historical lows at 2.5%, but we see the stagnating share price and rising dividend combining to send the yield to 3% in five years. Thus, we believe Travelers will become a strong income stock again

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	19%	22%	48%	28%	21%	20%	22%	25%	38%	34%	28%	33%

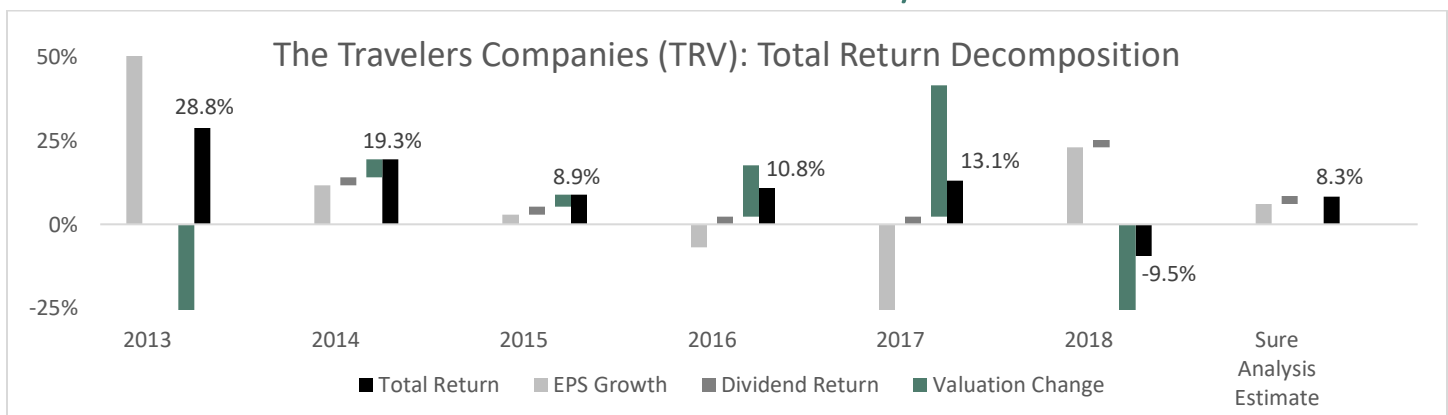
Travelers' quality metrics have oscillated over time along with its insurance losses. Underwriting margin peaked in the low-10% range but has not recovered. Travelers continues to be conservatively-financed and does not have significant debt coming due in the next three years, so its balance sheet is in good shape and interest coverage remains robust. The payout ratio should remain in the low-30% area given that we are forecasting earnings and the dividend to grow at roughly congruent rates. Note that Travelers should raise its payout in Q2 of 2019 for the June payment.

Travelers' main competitive advantages are in its immense scale and recognizable brand. Its size allows it to underwrite policies that others would not be able to and its brand is well-known from its long history. Travelers is more susceptible to catastrophes than recessions, as we saw in 2017 and again in 2018.

Final Thoughts & Recommendation

Travelers looks like a safe financial services provider with a decent growth outlook that is trading for fair value. We therefore see total annual returns of just 8.3% annually in the coming years, consisting of the current 2.5% yield, 6% earnings-per-share growth and a 0.2% headwind from essentially no movement in the valuation. While the valuation has improved since our last update, we still do not believe Travelers is cheap. Results continue to improve, but we believe most of this is already at least somewhat priced into the stock. We therefore rate the stock as a hold despite the improvement in the valuation, as we think investors will get a chance to buy the shares at a lower valuation in the relatively near term.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	24477	24680	25112	25446	25740	26191	27174	26815	27625	28902
SG&A Exp.	3518	3366	3406	3556	3610	3757	3964	4094	4154	4170
D&A Exp.	821	797	812	802	827	867	864	818	826	813
Net Profit	2924	3622	3216	1426	2473	3673	3692	3439	3014	2056
Net Margin	11.9%	14.7%	12.8%	5.6%	9.6%	14.0%	13.6%	12.8%	10.9%	7.1%
Free Cash Flow	3138	4231	3054	2169	3230	3816	3693	3434	4202	3762
Income Tax	792	1089	1090	-74	693	1272	1397	1301	1039	674

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets (\$B)	109.63	109.56	105.66	104.58	104.94	103.81	103.08	100.18	100.25	103.48
Cash & Equivalents	350	255	200	214	330	294	374	380	307	344
Acc. Receivable	5835	5471	5497	22071	21390	20166	19920	19721	19618	20228
Goodwill & Int.	4054	3953	3867	3798	3746	3985	3915	3852	3848	4293
Total Liabilities	84313	82145	80181	80098	79533	79016	78242	76586	77024	79752
Accounts Payable	528	546	407	5575	5152	4626	4698	4670	4882	5049
Long-Term Debt	6181	6527	6611	6605	6350	6346	6349	6344	6437	6571
Total Equity	25230	27336	25407	24477	25405	24796	24836	23598	23221	23731
D/E Ratio	0.24	0.24	0.26	0.27	0.25	0.26	0.26	0.27	0.28	0.28

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	2.6%	3.3%	3.0%	1.4%	2.4%	3.5%	3.6%	3.4%	3.0%	2.0%
Return on Equity	11.3%	13.8%	12.2%	5.7%	9.9%	14.6%	14.9%	14.2%	12.9%	8.8%
ROIC	9.2%	11.1%	9.7%	4.5%	7.9%	11.7%	11.8%	11.3%	10.1%	6.9%
Shares Out.	585	520	435	393	377	354	322	296	280	271
Revenue/Share	40.50	43.40	52.05	60.51	66.03	69.97	79.34	85.43	94.93	103.74
FCF/Share	5.19	7.44	6.33	5.16	8.29	10.20	10.78	10.94	14.44	13.50

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

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