RLI Corporation (RLI)

Updated January 30th, 2020 by Jonathan Weber

Key Metrics

Current Price:	$94	**5 Year CAGR Estimate:**	-9.3%	**Market Cap:**	$4.2B
Fair Value Price:	$45	**5 Year Growth Estimate:**	3.0%	**Ex-Dividend Date:**	02/27/20[1]
% Fair Value:	209%	**5 Year Valuation Multiple Estimate:**	-13.7%	**Dividend Payment Date:**	03/20/20[2]
Dividend Yield:	1.0%	**5 Year Price Target**	$52	**Years Of Dividend Growth:**	44
Dividend Risk Score:	A	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	4.5%

Overview & Current Events

RLI Corp. is an insurance company that operates the following business units: Casualty (healthcare & transportation insurance), Property (fire, earthquake, difference in conditions, marine, etc.) and Surety (contract surety coverage, licenses, and bonds). RLI was founded in 1965 and is currently valued at $4.2 billion.

RLI Corporation reported its fourth quarter earnings results on January 23. The company reported revenues of $265 million during the quarter, which represents an increase of 54% compared to the revenues that RLI Corporation generated during the previous year's quarter. Gross written premiums rose by 8% year-over-year, while investment income rose by a strong 11% compared to the prior year's quarter. The massive revenue increase can be explained by the equity market downturn during the fourth quarter of 2018, which resulted in massive net realized losses during that quarter, which made for an easy comparison during 2019's fourth quarter.

RLI Corporation earned $0.63 per share on an adjusted basis, which was 58% more than the earnings-per-share that RLI Corporation generated during the fourth quarter of the previous year. The massive profit growth rate in Q4 was an outlier, mainly due to the easy comparison with the weak quarter during the previous year. RLI nevertheless managed to grow its earnings-per-share to $2.57 during all of 2019, which still represents a compelling increase versus fiscal 2018.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$2.66	$2.80	$2.02	$2.57	$2.62	$2.53	$2.08	$2.30	$2.05	$2.57	***$2.65***	***$3.07***
DPS	$0.57	$0.60	$0.63	$0.67	$0.71	$0.75	$0.79	$0.83	$0.87	$0.91	***$0.92***	***$1.17***
Shares[3]	41.9	42.3	42.5	43.0	43.1	43.5	44.0	44.2	44.5	45.4	***45.8***	***46.5***

RLI Corp. has not been able to grow its profits consistently over the last decade. Profitability remained high through the last financial crisis, which is a positive, but since then, earnings have gone up and down without any clear direction. This is, in large part, because low interest rates have reduced the income RLI can generate with its insurance float.

Rising interest rates were a positive for the company's profitability during the Fed's tightening cycle, but now that the Fed has gone back to a more dovish policy, this tailwind will likely disappear. Tax legislation changes are a tailwind for RLI Corporation, as this has increased the company's net earnings substantially, thanks to a drastic reduction in the company's tax rate. We believe that RLI Corporation should be able to grow its profits slightly going forward, as written premiums continue to grow, which provides some revenue growth tailwinds over the coming years. Due to the company's choppy earnings history, we do not forecast a high long-term earnings-per-share growth rate, though; instead we believe that 3% annual earnings-per-share growth is realistic.

RLI has increased its dividend, on average, by 6% annually through the last decade, which was primarily possible due to a steady increase in the company's dividend payout ratio. Since the payout ratio is still quite low, RLI should be able to

---

[1] Estimated date

[2] Estimated date

[3] In Millions

keep its dividends growing going forward, even with only modest expected earnings-per-share growth ahead. RLI has, in addition to its regular dividends, made many special dividend payments over the last couple of years.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	10.4	11.0	16.9	15.6	17.2	21.1	31.1	34.3	33.7	35.0	***35.5***	***17.0***
Avg. Yld.	2.1%	1.9%	1.8%	1.7%	1.6%	1.4%	1.2%	1.4%	1.3%	1.0%	***1.0%***	***2.2%***

RLI Corporation's price to earnings multiple has been moving in a very wide range over the last decade. Shares were valued at a low-double-digit price to earnings multiple shortly after the financial crisis, but the company's valuation exploded upwards over the last couple of years. Shares trade at a massive premium relative to how shares were valued in the past, which is why we see huge downside risk for RLI Corporation's share price.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	21.4%	21.4%	31.2%	26.1%	27.1%	29.6%	38.0%	49.7%	42.4%	35.4%	***34.7%***	***38.2%***

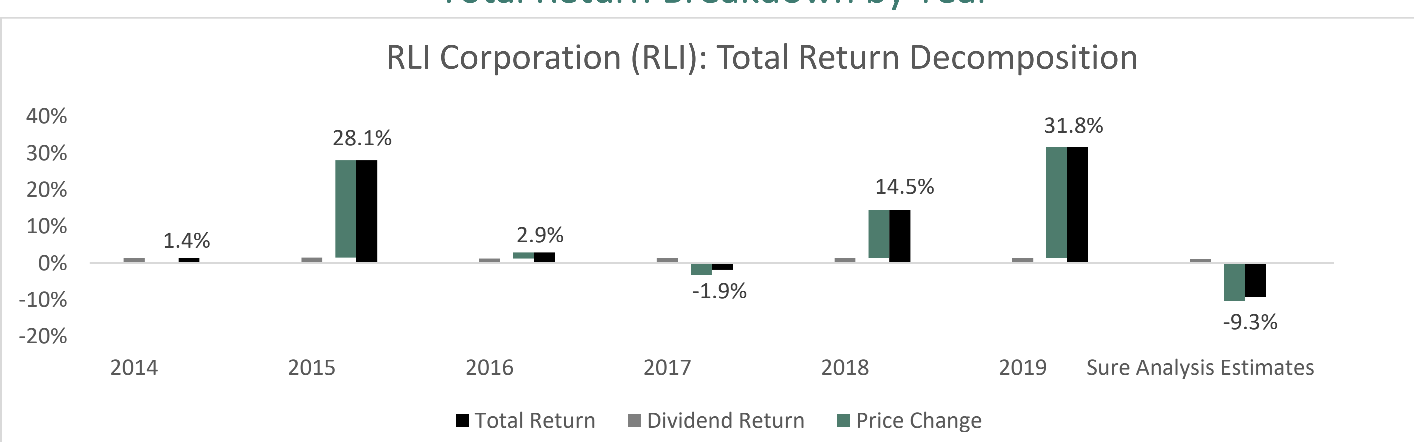
RLI Corporation has raised its regular dividend very steadily over the last couple of years, which was possible due to ongoing increases in the company's payout ratio. RLI Corporation still pays out just about one-third of its profits in the form of regular dividends, which makes the payout look sufficiently safe for the foreseeable future. Due to RLI Corporation's very low dividend yield we do not believe that shares are attractive for income investors.

Many financial corporations, including some insurers, experienced significant difficulty during the last recession. RLI remained profitable, and its earnings-per-share actually increased during the 2008 to 2010 time frame. We believe that RLI Corporation will be relatively stable during future recessions as well. Compared to other corporations from the financial industry, RLI Corporation thus looks like a more stable, lower-risk pick.

Final Thoughts & Recommendation

RLI Corporation is a smaller insurance company which produced strong underlying results during 2019, with written premiums and investment income rising substantially. Earnings will likely continue to grow during the next couple of years, but we see substantial deceleration in its earnings growth, as RLI Corporation does not have a strong long-term track record when it comes to generating earnings-per-share growth. We believe that shares are heavily overvalued today, and because of this, RLI Corporation earns a sell recommendation from Sure Dividend at current prices.

Total Return Breakdown by Year



Click here to rate and review this research report. Your feedback is important to us.

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.

RLI Corporation (RLI)

Updated January 30th, 2020 by Jonathan Weber

Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	547	583	621	663	708	777	796	818	801	820
SG&A Exp.	48	47	8	8	9	10	10	10	11	9
D&A Exp.	3	3	3	3	4	5	5	6	7	7
Net Profit	94	127	127	103	126	135	138	115	105	64
Net Margin	17.2%	21.8%	20.4%	15.6%	17.8%	17.4%	17.3%	14.1%	13.1%	7.8%
Free Cash Flow	127	98	113	21	117	116	143	158	188	211
Income Tax	39	51	57	39	49	54	59	42	-20	3

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	2539	2515	2655	2645	2740	2776	2735	2778	2947	3105
Cash & Equivalents	0	0	81	44	39	31	11	18	24	30
Accounts Receivable	84	107	478	499	507	490	442	415	436	518
Goodwill & Int. Ass.	26	26	60	76	75	73	71	64	59	55
Total Liabilities	1706	1723	1862	1848	1911	1930	1912	1954	2094	2298
Accounts Payable	22	24	51	44	47	38	38	18	22	23
Long-Term Debt	100	100	100	100	150	150	149	149	149	149
Shareholder's Equity	832	791	793	796	829	845	823	824	854	807
D/E Ratio	0.12	0.13	0.13	0.13	0.18	0.18	0.18	0.18	0.17	0.18

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	3.8%	5.0%	4.9%	3.9%	4.7%	4.9%	5.0%	4.2%	3.7%	2.1%
Return on Equity	12.2%	15.7%	16.0%	13.0%	15.5%	16.2%	16.5%	14.0%	12.5%	7.7%
ROIC	10.8%	14.0%	14.2%	11.6%	13.5%	13.7%	14.0%	11.8%	10.6%	6.6%
Shares Out.	42.5	41.9	42.3	42.5	43.0	43.1	43.5	44.0	44.2	44.5
Revenue/Share	12.58	13.73	14.49	15.35	16.26	17.73	18.05	18.41	18.00	18.30
FCF/Share	2.92	2.31	2.63	0.49	2.70	2.65	3.23	3.56	4.23	4.71

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