



The Travelers Companies (TRV)

Updated January 26th, 2020 by Josh Arnold

Key Metrics

Current Price:	\$135	5 Year CAGR Estimate:	5.1%	Market Cap:	\$35B
Fair Value Price:	\$113	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	03/09/20
% Fair Value:	119%	5 Year Valuation Multiple Estimate:	-3.4%	Dividend Payment Date:	03/31/20
Dividend Yield:	2.4%	5 Year Price Target	\$152	Years Of Dividend Growth:	15
Dividend Risk Score:	B	Retirement Suitability Score:	B	Last Dividend Increase:	6.5%

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 generates \$30 billion in annual revenue and has a \$35 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 and full-year earnings on January 23rd, with a slight top line miss being overshadowed by a strong bottom line performance. Net income per diluted share came to \$3.32 on an adjusted basis for the fourth quarter, a year-over-year gain of 56%. Insurers tend to have volatile profits due to things like catastrophe losses, which are infrequent, generally not repeated, and take sizable portions of profit in periods where they occur.

Net income was up 4% for the year on a dollar basis to \$2.6 billion. However, thanks to share repurchase activity, Travelers saw earnings-per-share climb 11% for the full year.

Earnings growth drivers were stronger written premiums, which were up 6% for the quarter and 5% for the year. The company reported net written premium growth in all business segments. Particular strength was seen in domestic Business Insurance, which saw its renewal premium change rise 7.8%, which is the best value since 2013.

Catastrophe losses were just \$85 million in Q4 compared to \$610 million in the year-ago period. This drove the consolidated combined ratio to 92.4%, down 510bps from the year-ago period. The combined ratio is the ratio of expenses to revenue, so a lower value is better.

Travelers continued to return huge amounts of capital to shareholders, sending back \$376 million in share repurchases, and \$112 million in dividends during Q4. For the full year, those numbers were \$1.5 billion and \$0.9 billion, respectively.

We see continued strong earnings growth in 2020 barring unforeseen catastrophes, calling for \$10.30 per share.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$6.31	\$3.25	\$6.21	\$9.46	\$10.56	\$10.87	\$10.13	\$7.27	\$8.94	\$9.60	\$10.30	\$13.78
DPS	\$1.44	\$1.64	\$1.79	\$1.96	\$2.15	\$2.38	\$2.68	\$2.83	\$3.03	\$3.23	\$3.28	\$5.05
Shares¹	435	393	377	354	322	296	280	271	264	259	251	220

After strong growth coming out of the Great Recession, Travelers has failed to regain its 2015 high of \$10.87 in earnings-per-share. It appears that value will remain elusive in 2020 as well. In total, we are expecting 6% earnings-per-share growth annually in the coming years.

Travelers could achieve this growth primarily from higher underwritten premiums and the buyback program, although margins should play a part as well, as long as there aren't any large catastrophes. We see low single-digit gains from higher revenue as well as a similar tailwind from the company's 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

¹ Share count in millions

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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 is really 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 a pure income stock any longer given the higher share price, but its 2.4% yield is respectable, and the payout should continue to grow at a quicker pace than earnings.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2024
Avg. P/E	8.2	17.4	10.3	8.8	8.8	9.7	11.2	17.2	14.7	14.5	13.1	11.0
Avg. Yld.	2.8%	2.9%	2.8%	2.3%	2.3%	2.3%	2.4%	2.3%	2.3%	2.3%	2.4%	3.3%

Travelers' price-to-earnings multiple stands at 13.1 times this year's earnings estimate. We therefore see the stock as overvalued given that our estimate of fair value is 11 times earnings. That implies a moderate -3.4% headwind to total returns due to the valuation.

The yield is now somewhat higher than it has been in recent years, and we see the significant overvaluation in the shares as driving continued yield growth over time to the mid-3% area.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	22%	48%	28%	21%	20%	22%	25%	38%	34%	34%	32%	37%

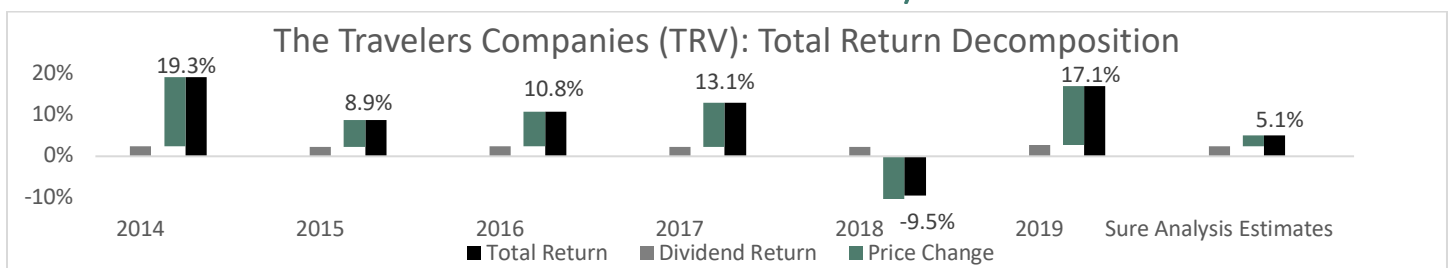
Travelers continues to be conservatively financed and does not have significant debt coming due in the next three years, so its balance sheet is in good shape and interest coverage remains robust. We believe the payout ratio should remain below 40% given that we are forecasting earnings and the dividend to grow at roughly congruent rates. The dividend is, therefore, very safe and we see many more years of increases on the horizon. Importantly, this continues to allow Travelers to buy back hundreds of millions of dollars of its own shares annually.

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. This makes Travelers a defensive play should the economy weaken materially, but we reiterate that insurance companies are susceptible to significant and unforeseen shocks, as Travelers has demonstrated in recent quarters.

Final Thoughts & Recommendation

Travelers looks like a safe financial services provider with a decent growth outlook that is trading above fair value. We see total annual return potential of 5.1% annually in the coming years, consisting of the current yield, 6% earnings-per-share growth and a modest headwind from movement in the valuation. We're reiterating Travelers at a hold rating as the stock is overvalued in our view.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	25112	25446	25740	26191	27174	26815	27625	28902	30282	31581
SG&A Exp.	3406	3556	3610	3757	3964	4094	4154	4170	4297	4365
D&A Exp.	812	802	827	867	864	818	826	813	803	763
Net Profit	3216	1426	2473	3673	3692	3439	3014	2056	2523	2622
Net Margin	12.8%	5.6%	9.6%	14.0%	13.6%	12.8%	10.9%	7.1%	8.3%	8.3%
Free Cash Flow	3054	2169	3230	3816	3693	3434	4469	4148	4380	5205
Income Tax	1090	-74	693	1272	1397	1301	1039	674	438	516

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets (\$B)	105.66	104.58	104.94	103.81	103.08	100.18	100.25	103.48	104.23	110.1
Cash & Equivalents	200	214	330	294	374	380	307	344	373	494
Acc. Receivable	5497	22071	21390	20166	19920	19721	19618	20228	20661	20763
Goodwill & Int.	3867	3798	3746	3985	3915	3852	3848	4293	4282	4291
Total Liabilities	80181	80098	79533	79016	78242	76586	77024	79752	81339	84179
Accounts Payable	407	5575	5152	4626	4698	4670	4882	5049	5074	4982
Long-Term Debt	6611	6605	6350	6346	6349	6344	6437	6571	6564	6558
Total Equity	25407	24477	25405	24796	24836	23598	23221	23731	22894	25943
D/E Ratio	0.26	0.27	0.25	0.26	0.26	0.27	0.28	0.28	0.29	0.25

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	3.0%	1.4%	2.4%	3.5%	3.6%	3.4%	3.0%	2.0%	2.4%	2.4%
Return on Equity	12.2%	5.7%	9.9%	14.6%	14.9%	14.2%	12.9%	8.8%	10.8%	10.7%
ROIC	9.7%	4.5%	7.9%	11.7%	11.8%	11.3%	10.1%	6.9%	8.4%	8.5%
Shares Out.	435	393	377	354	322	296	280	271	264	259
Revenue/Share	52.05	60.51	66.03	69.97	79.34	85.43	94.93	103.74	112.24	120.40
FCF/Share	6.33	5.16	8.29	10.20	10.78	10.94	15.36	14.89	16.23	19.84

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

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