



# Axis Capital Holdings Limited (AXS)

Updated February 6<sup>th</sup>, 2020 by Josh Arnold

## Key Metrics

|                             |      |  |       |                                  |                       |
|-----------------------------|------|--|-------|----------------------------------|-----------------------|
| <b>Current Price:</b>       | \$66 | <b>5 Year CAGR Estimate:</b>               | 4.1%  | <b>Market Cap:</b>               | \$5.4B                |
| <b>Fair Value Price:</b>    | \$56 | <b>5 Year Growth Estimate:</b>             | 5.0%  | <b>Ex-Dividend Date:</b>         | 03/27/20 <sup>1</sup> |
| <b>% Fair Value:</b>        | 118% | <b>5 Year Valuation Multiple Estimate:</b> | -3.3% | <b>Dividend Payment Date:</b>    | 04/16/20 <sup>2</sup> |
| <b>Dividend Yield:</b>      | 2.5% | <b>5 Year Price Target</b>                 | \$71  | <b>Years Of Dividend Growth:</b> | 18                    |
| <b>Dividend Risk Score:</b> | B    | <b>Retirement Suitability Score:</b>       | B     | <b>Last Dividend Increase:</b>   | 2.5%                  |

## Overview & Current Events

Axis Capital is a global insurer and reinsurer that was founded in 2001. It is split into Insurance and Reinsurance divisions, with the former making up about 55% of total revenue. It offers a broad range of risk transfer products for a diverse base of customers and has a market capitalization of \$5.4 billion with \$4.8 billion in annual revenue.

Axis reported Q4 and full-year earnings on January 29<sup>th</sup>, and while revenue beat consensus estimates, the bottom line came up a bit short. Gross premiums written declined by -0.2% on a reported basis, but was up 1% on a constant currency basis, to \$6.9 billion. The insurance segment posted a -3% decline that was partially offset by a 4% gain in the reinsurance segment.

The current accident year loss ratio excluding catastrophe and weather-related losses improved 110bps to 60.6% for the full year. Catastrophe and weather-related losses also improved 150bps to 7.5%, for a total current accident year loss ratio of 68.1% against 70.7% in 2018. However, a higher prior year reserve development ratio in 2019 offset those gains, and combined with higher acquisition costs and G&A expenses, Axis' combined ratio actually deteriorated 270bps to 102.6% for 2019.

Still, operating income was up from \$1.91 per share to \$2.52 year-over-year in 2019, and Axis boosted its book value, adjusted for dividends, by 15% over 2018.

Barring unforeseen catastrophes, Axis should produce \$5.40 or so in earnings-per-share for this year. In addition, we continue to forecast further book value gains as the company has proven to be quite adept at generating shareholder value, even in tough conditions.

## Growth on a Per-Share Basis

| Year                      | 2010    | 2011    | 2012    | 2013    | 2014    | 2015    | 2016    | 2017    | 2018    | 2019    | 2020           | 2025           |
|---------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|----------------|----------------|
| <b>BV/S</b>               | \$43.65 | \$37.79 | \$43.23 | \$46.32 | \$51.50 | \$54.54 | \$59.54 | \$54.91 | \$49.72 | \$55.79 | <b>\$58.58</b> | <b>\$74.76</b> |
| <b>EPS</b>                | \$4.60  | -\$0.90 | \$3.41  | \$5.49  | \$5.32  | \$4.02  | \$4.48  | -\$3.15 | \$1.92  | \$2.70  | <b>\$5.40</b>  | <b>\$6.89</b>  |
| <b>DPS</b>                | \$0.86  | \$0.93  | \$0.97  | \$1.02  | \$1.10  | \$1.22  | \$1.43  | \$1.53  | \$1.57  | \$1.61  | <b>\$1.64</b>  | <b>\$2.09</b>  |
| <b>Shares<sup>3</sup></b> | 117     | 131     | 122     | 112     | 101     | 96      | 86      | 84      | 84      | 84      | <b>84</b>      | <b>84</b>      |

Earnings-per-share have been tremendously volatile during the past decade, which is expected for an insurer. Axis' profits rise and fall based upon how efficiently it writes premiums along with factors that are out of its control, including claims, as we saw in 2019 once again. Axis has suffered of late due to higher claims from disasters such as typhoons and crop-related losses, but this should not reoccur moving forward.

Axis also benefits from higher interest rates as its investment income rises commensurately. We see moderate growth going forward as Axis continues to grow its business organically through prudent risk taking, in addition to further acquisitions like Novae. We are expecting 5% earnings-per-share growth ahead through a combination of continued premium growth, and investment income. There is potential room for additional upside should Axis avoid years like

<sup>1</sup> Estimated date

<sup>2</sup> Estimated date

<sup>3</sup> Share count in millions

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2017 in the future, or if it completes a sizable acquisition. Overall Axis looks well positioned for growth and in our view, continues to be well-managed.

We see the dividend growing at about the same rate as earnings and may reach \$2.09 or so in the next five years.

## Valuation Analysis

| Year      | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | Now         | 2025        |
|-----------|------|------|------|------|------|------|------|------|------|------|-------------|-------------|
| Avg. P/B  | 73%  | 85%  | 78%  | 95%  | 90%  | 99%  | 94%  | 113% | 111% | 106% | <b>112%</b> | <b>95%</b>  |
| Avg. Yld. | 2.7% | 2.9% | 2.9% | 2.3% | 2.4% | 2.3% | 2.6% | 2.5% | 2.9% | 2.7% | <b>2.5%</b> | <b>2.9%</b> |

The company's price-to-book ratio has moved around significantly as its fortunes have risen and fallen, similar to other insurance companies' valuations. Axis continues to enjoy a price-to-book ratio that is well above average and as a result, we see it as overvalued. The stock is still about as expensive as it has been in recent years after Axis spent much of the last decade at meaningful discounts to book value. We therefore see a -3.3% headwind to total returns from the valuation going forward as the price-to-book ratio moves back in line with its historical averages, closer to 95% from today's levels in excess of 110%.

As a result of a declining valuation, we see the dividend payment growing as a percentage of the share price, increasing the current yield from 2.5% to 2.9%. That yield would be near its historical high but given that its dividend is far more mature than it was several years ago, that is not entirely unexpected. The bottom line is that we expect Axis to remain a strong income stock.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year   | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020       | 2025       |
|--------|------|------|------|------|------|------|------|------|------|------|------------|------------|
| Payout | 19%  | ---  | 28%  | 19%  | 21%  | 30%  | 32%  | ---  | 82%  | 60%  | <b>30%</b> | <b>30%</b> |

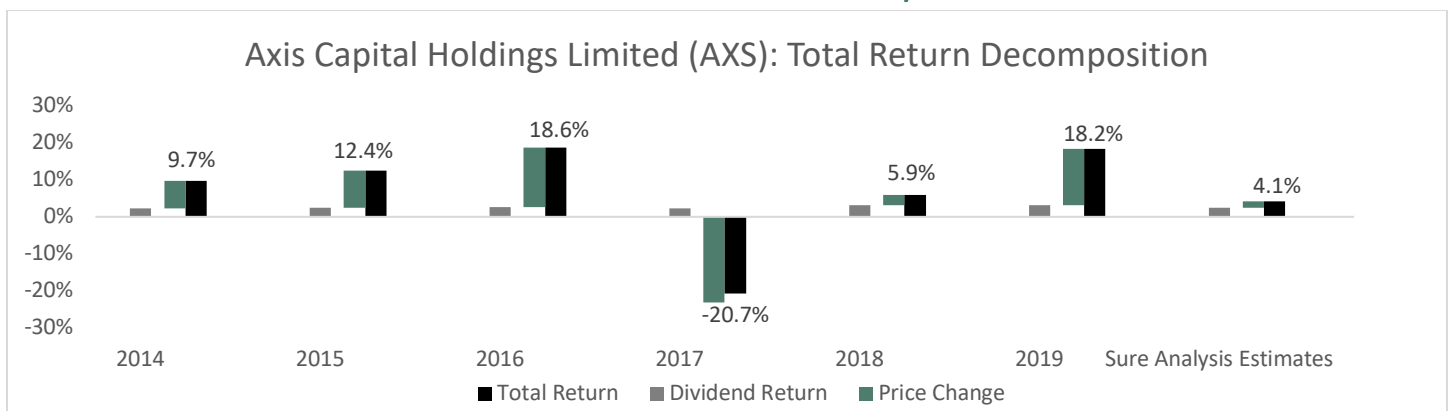
Axis' payout ratio is only about one-third of operating earnings in normalized years, so we find the dividend to be reasonably safe. The yield is less attractive than it has been simply because the share price is near its high.

Competitive advantages are tough to come by for insurers, and Axis is no different. On the bright side, recessions tend not to sway performance one way or the other, so there is a diversifying component to adding Axis to one's portfolio.

## Final Thoughts & Recommendation

We see Axis as overvalued and offering investors total annual returns of just 4.1% in the coming years. Axis' earnings-per-share growth of 5% could be somewhat offset by a headwind from the valuation, so more than half of its returns will result from the 2.5% yield. As a result of the current valuation, we rate Axis a sell despite its strong fundamentals.

## Total Return Breakdown by Year



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## Income Statement Metrics

| Year                  | 2010  | 2011 | 2012  | 2013  | 2014  | 2015  | 2016  | 2017  | 2018 | 2019 |
|-----------------------|-------|------|-------|-------|-------|-------|-------|-------|------|------|
| <b>Revenue</b>        | 3567  | 3846 | 3897  | 4170  | 4451  | 4233  | 4127  | 4442  | 5120 | 5185 |
| <b>SG&amp;A Exp.</b>  | 450   | 459  | 561   | 575   | 622   | 597   | 603   | 579   | 627  | 635  |
| <b>D&amp;A Exp.</b>   | 14    | 17   | 14    | 23    | 25    | 26    | 25    | 31    | 10   |      |
| <b>Net Profit</b>     | 857   | 46   | 547   | 727   | 811   | 642   | 513   | -369  | 43   | 323  |
| <b>Net Margin</b>     | 24.0% | 1.2% | 14.0% | 17.4% | 18.2% | 15.2% | 12.4% | -8.3% | 0.8% |      |
| <b>Free Cash Flow</b> | 1188  | 1190 | 1121  | 1097  | 862   | 791   | 407   | 259   | 11   |      |
| <b>Income Tax</b>     | 39    | 15   | 3     | 7     | 26    | 3     | 6     | -8    | -29  | 24   |

## Balance Sheet Metrics

| Year                          | 2010  | 2011  | 2012  | 2013  | 2014  | 2015  | 2016  | 2017  | 2018  | 2019  |
|-------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <b>Total Assets</b>           | 16446 | 17806 | 18852 | 19635 | 19956 | 19982 | 20814 | 24760 | 24133 | 25604 |
| <b>Cash &amp; Equivalents</b> | 930   | 982   | 760   | 923   | 922   | 988   | 1039  | 949   | 1233  | 1241  |
| <b>Acc. Receivable</b>        | 2,921 | 3,184 | 3,339 | 3,619 | 3,735 | 4,064 | 4,648 | 6,351 | 6,789 | 7,277 |
| <b>Goodwill &amp; Int.</b>    | 103   | 100   | 97    | 90    | 89    | 87    | 85    | 567   | 379   | 342   |
| <b>Total Liabilities</b>      | 10821 | 12362 | 13073 | 13767 | 14076 | 14115 | 14541 | 19419 | 19102 | 20060 |
| <b>Accounts Payable</b>       | 165   | 207   | 271   | 234   | 249   | 356   | 493   | 899   | 1,339 | 1,349 |
| <b>Long-Term Debt</b>         | 994   | 995   | 995   | 996   | 991   | 992   | 993   | 1,377 | 1,342 | 1,808 |
| <b>Total Equity</b>           | 5,125 | 4,944 | 5,277 | 5,190 | 5,193 | 5,239 | 5,146 | 4,566 | 4,255 | 4,769 |
| <b>D/E Ratio</b>              | 0.18  | 0.18  | 0.17  | 0.17  | 0.17  | 0.17  | 0.16  | 0.26  | 0.27  | 0.33  |

## Profitability & Per Share Metrics

| Year                    | 2010  | 2011  | 2012  | 2013  | 2014  | 2015  | 2016  | 2017  | 2018  | 2019  |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <b>Return on Assets</b> | 5.4%  | 0.3%  | 3.0%  | 3.8%  | 4.1%  | 3.2%  | 2.5%  | -1.6% | 0.2%  | 1.3%  |
| <b>Return on Equity</b> | 16.9% | 0.9%  | 10.7% | 13.9% | 15.6% | 12.3% | 9.9%  | -7.6% | 1.0%  | 7.2%  |
| <b>ROIC</b>             | 13.6% | 0.7%  | 8.3%  | 10.7% | 11.8% | 9.3%  | 7.3%  | -5.3% | 0.7%  | 4.7%  |
| <b>Shares Out.</b>      | 117   | 131   | 122   | 112   | 101   | 96    | 86    | 84    | 84    | 84    |
| <b>Revenue/Share</b>    | 26.19 | 30.02 | 31.52 | 36.16 | 42.10 | 42.48 | 45.08 | 52.81 | 60.94 | 61.39 |
| <b>FCF/Share</b>        | 8.72  | 9.29  | 9.06  | 9.51  | 8.16  | 7.94  | 4.44  | 3.08  | 0.13  |       |

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

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