First American Financial Corp (FAF)

Updated October 25th, 2021 by Quinn Mohammed

Key Metrics

Current Price:	$75	**5 Year CAGR Estimate:**	9.3%	**Market Cap:**	$8.2 B
Fair Value Price:	$82	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date[1]:**	12/07/2021
% Fair Value:	91%	**5 Year Valuation Multiple Estimate:**	2.0%	**Dividend Payment Date[2]:**	12/15/2021
Dividend Yield:	2.6%	**5 Year Price Target:**	$105	**Years of Dividend Growth:**	10
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	10.9%

Overview & Current Events

First American Financial Corporation traces its roots back to 1889 when two firms opened to handle title matters in the brand-new county of Orange County, California. In 1894, these two entities merged into the Orange County Title Company, the immediate predecessor to what is known today as First American Title Insurance Company, the largest subsidiary of First American Financial Corporation. In 1988, First American opened title insurance offices in Canada. Shortly after, they used a similar business model to develop international operations across the globe. First American was the first title insurance provider in Mexico, Korea, and Honk Kong and today has the leading market share in Australia and England.

First American trades on the NYSE under the ticker FAF and has a market capitalization of $8.2 billion. FAF provides insurance through two segments: title insurance and related services and specialty insurance. Title insurance and related services include real estate insurance, property closing services, escrow, risk mitigation, real estate data products and related real estate transaction services. The title insurance sector provides insurance to residential and commercial customers. In 2020, FAF generated $7.1 billion in revenue.

FAF released third quarter results on October 21st. The company generated total revenue of $2.6 billion, up 34% compared to last year. The corporation closed title orders were down 13%, however the revenue per title order closed rose 31% year-over-year. Average revenue per order grew 44.4%, driven by the shift in the order mix from lower premium residential refinance transactions to higher-premium commercial and purchase transactions. The Title Insurance and Services segment pretax margin of 16.4% was driven by record commercial and agency revenues which outweighed the decline in refinance activity. Net income of $445 million grew 145% compared to the same prior year period's $182 million. Net income per diluted share rose 147% from $1.62 to $4.00.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$0.94	$2.77	$1.71	$2.15	$2.62	$3.09	$3.76	$4.19	$6.22	$6.16	**$7.48**	**$9.55**
DPS	$0.24	$0.36	$0.48	$0.84	$1.00	$1.20	$1.44	$1.60	$1.68	$1.78	**$1.94**	**$2.48**
Shares[3]	105.4	107.2	106.0	107.5	109.1	110.0	110.9	111.5	112.5	110.4	**109.0**	**108.0**

Earnings per share, while somewhat bumpy at times, trended upwards strongly into 2019, and the COVID pandemic did not cause major distress for the firm in 2020. FAF was able to grow their earnings by 23.2% and 18.6% annually over the last nine and five years on average, due to the upward momentum experienced in recent years. We believe going forward, and off the back of these tremendous earnings forecast, that FAF will continue growing earnings at roughly 5%. We also estimate that the dividend will grow in-line with earnings here, at 5%. FAF's markets are experiencing higher revenue and increased transaction activity, bolstered by low interest rates. Additionally, low interest rates will continue fueling the demand for home purchasing, and also residential refinancing.

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[1] Estimate

[2] Estimate

[3] In millions

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FAF's growth strategy revolves around three pillars: profitably grow the core title and settlement business, strengthen the enterprise through data and process advantage, and manage and actively invest in complementary business where FAF has a strategic advantage. The company will also make value-creating investments in the core business and acquire or invest in businesses that fit within their strategy.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	15.5	6.7	14.3	13.1	14.1	12.4	12.1	12.7	8.9	8.4	**10.0**	**11.0**
Avg. Yld.	1.6%	1.9%	2.0%	3.0%	2.7%	3.1%	3.2%	3.0%	3.0%	3.5%	**2.6%**	**2.4%**

First American Financial Corp trades at 10.0 times this year's earnings expectations of $7.48. This is 15% below the 9-year average PE of 11.8, and 8% below the 5-year average PE of 10.9. Our estimated fair value of 11 times would result in gains of 2.0% due to the valuation expansion. With a higher valuation, we expect the yield to drop slightly, down to 2.4%, still higher than the S&P 500's sub-2% yield.

Safety, Quality, Competitive Advantage, & Recession Resiliency

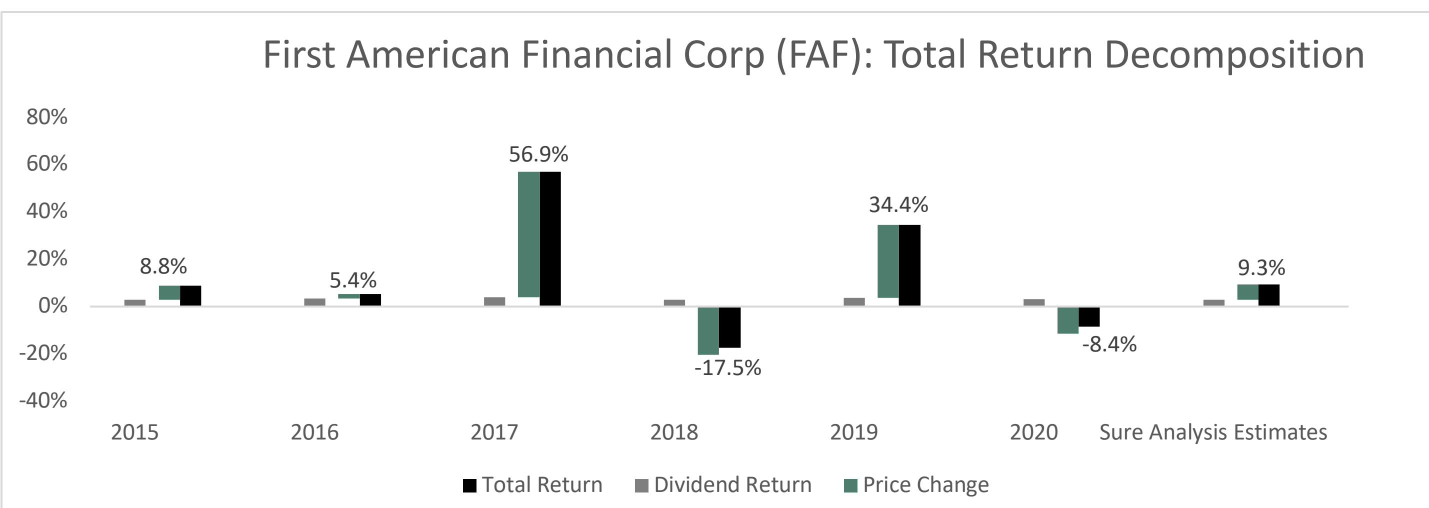
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	26%	13%	28%	39%	38%	39%	38%	38%	27%	29%	**26%**	**26%**

FAF has a fairly stable payout ratio in the 30% to 40% range on average, however in the past couple of years the payout has dropped as earnings grew significantly. FAF was not a public company during the great financial crisis, however it's entrenchment into the housing market which had great difficulties in that recession would have likely caused problems in the company's earnings, so we don't consider FAF to be recession resistant. FAF has a data advantage amongst its peers, which they can leverage to achieve market-leading title automation. Additionally, FAF is geographically diversified and was even the first title insurer in some countries, and in others they possess the leading market share.

Final Thoughts & Recommendation

First American Financial Corporation has more than one hundred years in the title insurance business and is investing into technology to raise their top and bottom lines. The company will produce total returns through EPS growth of roughly 5%, the strong yield of 2.6%, and also valuation expansion of 2.0%. We estimate that FAF can produce total returns of 9.3% over the near term and believe the company trades at roughly 91% of fair value, thus we rate FAF a Buy.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	3,821	4,542	4,956	4,678	5,175	5,576	5,769	5,745	6,199	7,081
SG&A Exp.	1,178	1,335	1,489	1,436	1,595	1,655	1,724	1,749	1,806	1,941
D&A Exp.	77	75	75	86	86	99	128	126	129	149
Net Profit	78	301	186	234	288	343	423	474	707	696
Net Margin	2.0%	6.6%	3.8%	5.0%	5.6%	6.2%	7.3%	8.3%	11.4%	9.8%
Free Cash Flow	67	346	291	263	428	357	498	675	806	971
Provision for Tax	52	166	124	116	144	134	23	134	195	223

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	5,362	6,051	6,559	7,666	8,237	8,832	9,573	10,631	11,519	12,796
Cash & Equivalents	475	698	858	1,212	1,051	1,027	1,429	1,503	1,530	1,321
Accts Receivable	258	291	269	277	288	330	334	349	337	399
Goodwill & Intang.	878	903	892	1,016	1,012	1,096	1,213	1,254	1,243	1,573
Total Liabilities	3,327	3,699	4,103	5,090	5,484	5,817	6,090	6,885	7,094	7,874
Accounts Payable	28	28	26	26	56	59	68	47	59	56
Long-Term Debt	300	230	310	587	581	737	733	808	1,007	1,527
Total Equity	2,029	2,348	2,453	2,573	2,750	3,008	3,480	3,742	4,420	4,910
D/E Ratio	0.15	0.10	0.13	0.23	0.21	0.24	0.21	0.22	0.23	0.31

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	1.4%	5.3%	3.0%	3.3%	3.6%	4.0%	4.6%	4.7%	6.4%	5.7%
Return on Equity	3.9%	13.8%	7.8%	9.3%	10.8%	11.9%	13.0%	13.1%	17.3%	14.9%
ROIC	3.4%	12.2%	7.0%	7.9%	8.9%	9.7%	10.6%	10.8%	14.2%	11.7%
Shares Out.	105.4	107.2	106.0	107.5	109.1	110.0	110.9	111.5	112.5	110.4
Revenue/Share	35.74	41.84	45.43	43.04	47.12	50.16	51.31	50.72	54.54	62.65
FCF/Share	0.63	3.19	2.67	2.42	3.89	3.21	4.43	5.96	7.09	8.59

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