First American Financial Corp (FAF)

Updated February 15th, 2023 by Quinn Mohammed

Key Metrics

Current Price:	$61	**5 Year CAGR Estimate:**	3.5%	**Market Cap:**	$6.3 B
Fair Value Price:	$47	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date[1]:**	03/07/2023
% Fair Value:	128%	**5 Year Valuation Multiple Estimate:**	-4.8%	**Dividend Payment Date[1]:**	03/15/2023
Dividend Yield:	3.4%	**5 Year Price Target:**	$60	**Years of Dividend Growth:**	11
Dividend Risk Score:	D	**Retirement Suitability Score:**	C	**Rating:**	Hold

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 Hong 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 $6.3 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 2022, First American Financial generated roughly $8 billion in revenue.

On August 24th, 2022, First American Financial raised its dividend 2% to $0.52 quarterly per share. This marked its 11th consecutive annual dividend increase. The company generated revenue of $1.7 billion, which was down 29% compared to the prior year quarter. Excluding net investment losses, total revenue was $1.8 billion, down 24% year-over-year. Net income per share was 54 cents, but excluding net investment losses of $0.83 was $1.35.

For the full fiscal 2022, FAF generated net income of $2.45 per diluted share, compared to $11.14 in 2021. Excluding net investment losses, FAF achieved $6.09 per share, compared to $8.16 in 2021.

During 2022, the company repurchased 7.5 million shares for $441 million at an average price of $58.65.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$1.71	$2.15	$2.62	$3.09	$3.76	$4.19	$6.22	$6.16	$11.14	$2.45	***$5.26***	***$6.71***
DPS	$0.48	$0.84	$1.00	$1.20	$1.44	$1.60	$1.68	$1.78	$1.94	$2.06	***$2.08***	***$2.41***
Shares[2]	106.0	107.5	109.1	110.0	110.9	111.5	112.5	113.0	111.4	104.9	***100.0***	***90.0***

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. In 2021, FAF generated very strong results but in 2022 the company suffered net investment losses which caused a downturn in its reported earnings. Excluding net investment losses, FAF grew their earnings by 15% and 10% annually over the last nine and five years on average. We believe going forward, FAF will continue growing earnings at roughly 5%. We also estimate that the dividend will grow in-line with earnings here, at 3%. FAF's markets have experienced higher revenue and increased transaction activity as a result of low interest rates. However, while low interest rates fueled the demand for home purchasing, and residential refinancing in the prior

[1] Estimate
[2] In millions

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.

year, rapidly rising rates now weigh on forecasted sales in 2023 and beyond. As a result, the company is putting more emphasis on expense management.

First American'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 it 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, such as the ServiceMac acquisition in 2021 and Mother Lode in 2022.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	14.3	13.1	14.1	12.4	12.1	12.7	8.9	8.4	7.8	7.8	***11.5***	***9.0***
Avg. Yld.	2.0%	3.0%	2.7%	3.1%	3.2%	3.0%	3.0%	3.5%	2.9%	3.4%	***3.4%***	***4.0%***

First American Financial Corp trades at 11.5 times this year's earnings expectations of $5.26 per share. This is above both the ten-year average P/E ratio and the five-year average ratio. Our estimated fair value of 9.0 times implies the potential for a valuation headwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

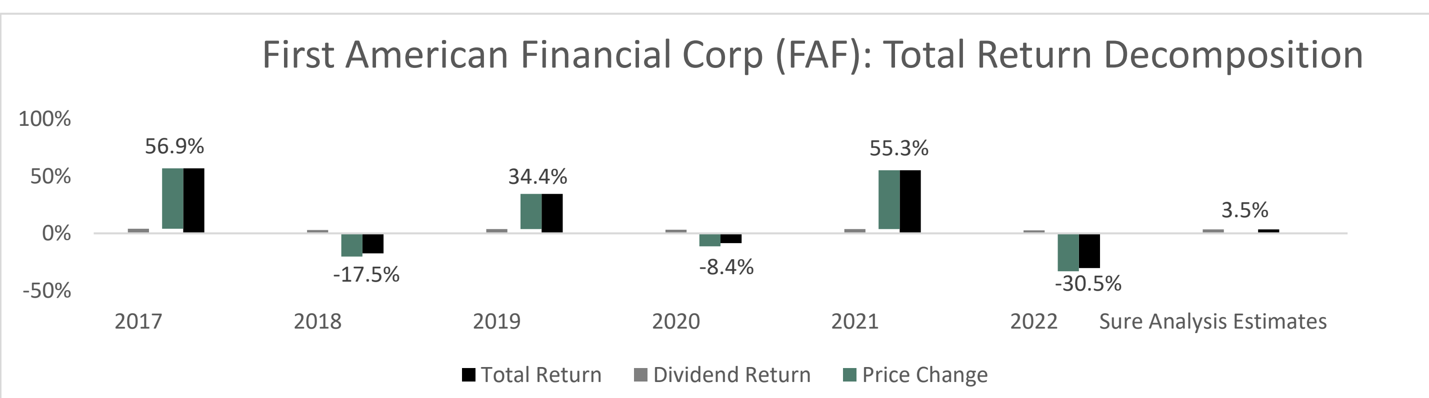
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	28%	39%	38%	39%	38%	38%	27%	29%	17%	84%	***40%***	***36%***

FAF has a fairly stable payout ratio in the 30% to 40% range on average. 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 5.0% and the 3.4% starting yield, offset by the potential for a valuation headwind. We forecast total annualized returns of 1.8% over the intermediate term and believe the company trades in excess of our estimate of fair value, thus we rate FAF as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	4,956	4,678	5,175	5,576	5,769	5,745	6,199	7,081	9,214	7,594
SG&A Exp.	1,489	1,436	1,595	1,655	1,724	1,749	1,806	1,941	2,350	2,340
D&A Exp.	75	86	86	99	128	126	129	149	158	167
Net Profit	186	234	288	343	423	474	707	696	1,241	263
Net Margin	3.8%	5.0%	5.6%	6.2%	7.3%	8.3%	11.4%	9.8%	13.5%	3.5%
Free Cash Flow	291	263	428	357	498	675	806	971	1,059	520
Provision for Tax	124	116	144	134	23	134	195	223	393	61

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	6,559	7,666	8,237	8,832	9,573	10,631	11,519	12,796	16,451	14,955
Cash & Equivalents	858	1,212	1,051	1,027	1,429	1,503	1,530	1,321	1,286	1,287
Accts Receivable	269	277	288	330	334	349	337	399	455	388
Goodwill & Intang.	892	1,016	1,012	1,096	1,213	1,254	1,243	1,573	1,806	1,992
Total Liabilities	4,103	5,090	5,484	5,817	6,090	6,885	7,094	7,874	10,668	10,267
Accounts Payable	26	26	56	59	68	47	59	56	87	51
Long-Term Debt	310	587	581	737	733	808	1,007	1,527	2,186	2,012
Total Equity	2,453	2,573	2,750	3,008	3,480	3,742	4,420	4,910	5,767	4,665
LTD/E Ratio	0.13	0.23	0.21	0.24	0.21	0.22	0.23	0.31	0.38	0.43

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	3.0%	3.3%	3.6%	4.0%	4.6%	4.7%	6.4%	5.7%	8.5%	1.7%
Return on Equity	7.8%	9.3%	10.8%	11.9%	13.0%	13.1%	17.3%	14.9%	23.2%	5.0%
ROIC	7.0%	7.9%	8.9%	9.7%	10.6%	10.8%	14.2%	11.7%	17.2%	3.6%
Shares Out.	106.0	107.5	109.1	110.0	110.9	111.5	112.5	110.4	111.4	107.3
Revenue/Share	45.43	43.04	47.12	50.16	51.31	50.72	54.54	62.65	82.71	70.77
FCF/Share	2.67	2.42	3.89	3.21	4.43	5.96	7.09	8.59	9.51	4.85

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