

Palomar Holdings Inc. (PLMR)

\$106.02 (As of 08/20/20)

Price Target (6-12 Months): **\$111.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 10/14/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:F

Value: F

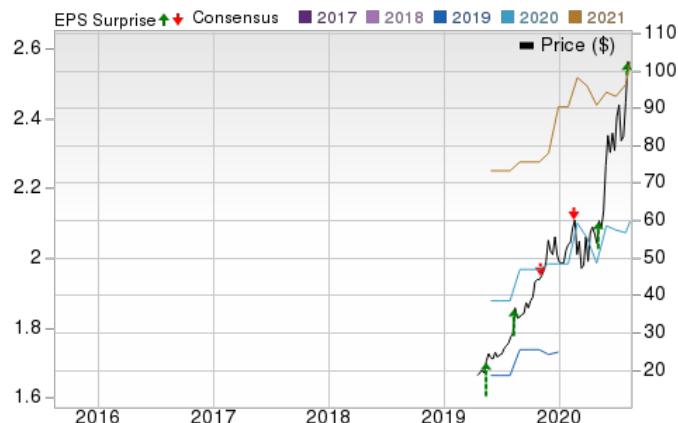
Growth: D

Momentum: D

Summary

Shares of Palomar Holdings have outperformed the industry in the past year. It is well-poised on solid revenue growth and balance sheet. Focus on new business, strong premium retention rates for existing business, renewals of existing policies bode well. Net investment income is expected to continue to grow on the back of higher average balance of investments. Higher return on equity indicates efficient utilization of shareholders' value. Based on operational excellence, it has affirmed prior guidance of adjusted net income between \$50.5 million and \$53 million, indicating year-over-year growth of 33% to 40%. However, exposure to cat loss induces underwriting volatility. Also, high costs can strain margin expansion. Its earnings of 52 cents per share beat the Zacks Consensus Estimate by 8.3% and improved 44.4% from the prior-year quarter.

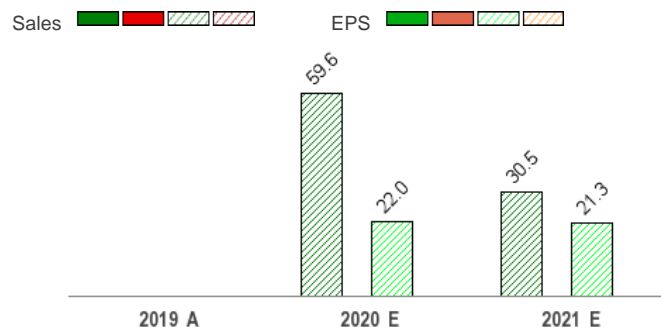
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$108.00 - \$32.57
20 Day Average Volume (sh)	258,172
Market Cap	\$2.7 B
YTD Price Change	110.0%
Beta	-0.13
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Insurance - Property and Casualty
Zacks Industry Rank	Top 49% (124 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	8.3%
Last Sales Surprise	8.1%
EPS F1 Est- 4 week change	1.6%
Expected Report Date	11/02/2020
Earnings ESP	0.3%

P/E TTM	55.8
P/E F1	50.3
PEG F1	NA
P/S TTM	18.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	52 E	55 E	58 E	61 E	227 E
2020	38 A	42 A	46 E	49 E	174 E
2019	22 A	25 A	30 A	33 A	109 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.57 E	\$0.58 E	\$0.66 E	\$0.73 E	\$2.56 E
2020	\$0.50 A	\$0.52 A	\$0.53 E	\$0.57 E	\$2.11 E
2019	\$0.52 A	\$0.36 A	\$0.40 A	\$0.48 A	\$1.73 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/20/2020. The reports text is as of 08/21/2020.

Overview

Headquartered in La Jolla, CA, Palomar Holdings, Inc. formerly known as GC Palomar Holdings (GCPH), was officially founded in 2014 by acquiring Palomar Specialty Insurance Company (PSIC) from Pacific Indemnity Company in a stock purchase transaction. Palomar Holdings is an insurance holding company that was incorporated in Delaware in March 2019.

Palomar Holdings is a rapidly growing and profitable company focused on the provision of catastrophe insurance for personal and commercial property. It provides specialty property insurance products in their target markets to both individuals and businesses. Its products are distributed through multiple channels, including retail agents, program administrators, wholesale brokers and in partnership with other insurance companies. The market opportunity, its distinctive products and differentiated business model will enable the company to grow its business profitably.

Palomar is uniquely positioned to address over \$30 billion of the \$600 billion U.S. property and casualty insurance market. It has grown into the fifth largest writer of earthquake insurance in California.

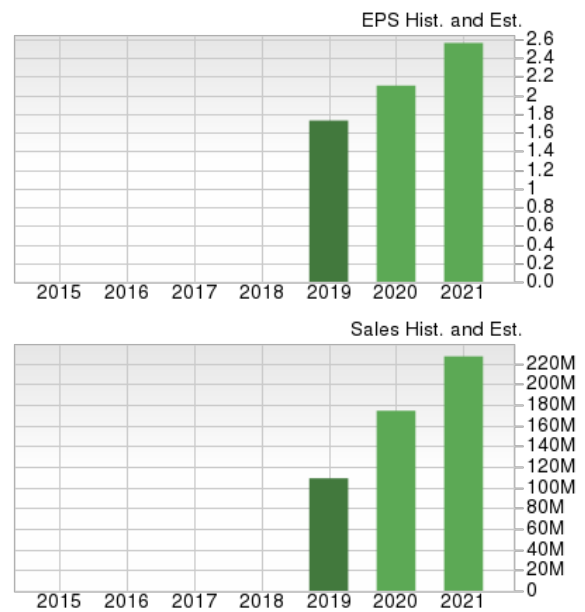
The company's wholly owned operating subsidiaries are Palomar Insurance Holdings, Inc. (PIH), which wholly owns Palomar Specialty Insurance Company (PSIC), Prospect General Insurance Agency, Inc. (PGIA) and Palomar Specialty Reinsurance Company Bermuda Ltd. (PSRE).

Its primary lines of business include Residential Earthquake, Commercial Earthquake, Specialty Homeowners, Commercial All Risk, Hawaii Hurricane and Residential Flood.

Residential and Commercial Earthquake products are priced at a granular level and offer flexible product features. Residential Earthquake products seek to expand the residential earthquake insurance market by attracting buyers who may not otherwise acquire protection.

For Commercial All Risk products, the company uses detailed technical analysis to identify a subset of target occupancies and developed a proprietary risk pricing methodology that will enable it to select and price risk appropriately.

Palomar has a single operating segment, the property and casualty insurance business. It offers primarily earthquake, wind, and flood insurance products.



Reasons To Buy:

▲ **Share Performance:** Shares of Palomar Holdings have gained 209.3%, against the industry's decline of 3.4% in a year's time. The company's operational efficiencies and solid capital position will continue to drive shares.

▲ **Strong Premium Growth:** Palomar has been displaying a good track record of net written premiums. Consistent premium growth has been boosting results, enabling the company to maintain sustained revenue growth over the past few years. Net written premiums increased at a two-year CAGR (2017-2019) of 40%. Premium growth was primarily due to an increased volume of policies written across the lines of business, driven by new business generated with existing partners, strong premium retention rates for existing business, expansion of their products' geographic and distribution footprint, and new partnerships. Net written premiums improved 55.1% year over year to \$95.6 million in the first half of 2020, primarily due to an increase in gross written premiums in commercial all risk and commercial earthquake lines. Premiums should continue to benefit from its solid product portfolio (short tail in nature) as well as geographic expansion, appointment of new producers, strategic partnerships with other insurance carriers and rate increases.

▲ **Investment Income:** Despite low interest rate environment, investment income increased at a two-year CAGR (2017-2019) of 67.7% owing to higher average balance of investments. The momentum continued through the first half of 2020, with the metric increasing 69.8% year over year to \$4.1 million. The increase was primarily due to a higher average balance of investments during the six months ended Jun 30, 2020 largely due to proceeds from April 2019 IPO, investing of cash generated from operations and proceeds from January 2020 secondary offering. High-quality fixed income securities and increase in fixed-income yields should continue to drive the momentum going forward.

▲ **Revenue Growth:** Revenues have been increasing over the last several years on the back of higher premiums, net investment income and commission and other income. The momentum continued in the first half of 2020 as well, with the metric rising 76.4% year over year to \$81.2 million. High premium retention and strong renewal rates should continue to retain the momentum going forward.

▲ **Combined Ratio:** Palomar has been witnessing substantial improvement in the combined ratio of its P&C business over the past few years due to lower catastrophe events and improved loss ratio. A company's combined ratio reflects its underwriting profitability. The adjusted combined ratio improved 160 basis points (bps) year over year to 63.4% in the first half of 2020. Palomar has been able to maintain combined ratio below 95% for three years. The company expects the combined ratio and adjusted combined ratio to increase about 2 to 2.5 points in the second half of 2020.

The company strives to protect earnings and balance sheet with reinsurance program that mitigates the impact of major events on overall profitability. The company completed the reinsurance programs in May 2020, in which it obtained \$200 million of incremental limit for California earthquakes, approximately \$300 million of incremental limit for all earthquake zones and approximately \$80 million of incremental windstorm limit. Effective June 2020, reinsurance coverage exhausts at \$1.4 billion for earthquake events and \$600 million for hurricane events. This reinsurance program will provide adequate support to the company's growth initiatives and appropriate levels of protection in the event of a major catastrophe.

▲ **Solid Balance Sheet:** Backed by a sustained operational performance, the company has maintained a solid capital position. Palomar generated solid cash flows, which surged 45% year over year to \$24.4 million in the first half of 2020. Its balance sheet remains solid given \$90.2 million capital infusion from public offering. The company also boasts a debt-free balance sheet with no exposure to the equity markets. Its cash and cash equivalents increased at a two-year CAGR (2017-2019) of 75.3%. As of Jun 30, 2020, it surged 230% from 2019-end figure. This suggests that the company has sufficient cash reserves to ensure financial stability.

▲ **Profitability:** Return on equity, a measure of profitability reflecting how efficiently the company is utilizing its shareholders' value. Return on equity is 17.5%, which compares favorably with the industry average of 6.2%.

Palomar Holdings remains focused on higher premium growth. Improving combined ratio and higher investment income are tailwinds

Reasons To Sell:

- ▼ **Escalating Expenses:** Palomar Holdings has been experiencing an increase in expenses due to higher incurred losses and loss adjustment expenses, interest expense and acquisition expenses and other underwriting expenses. In the second quarter of 2020, total expenses increased 59.8% to \$27.8 million, mainly due to higher losses and loss adjustment expenses, acquisition expenses and other underwriting expenses. The company should strive to generate higher revenue growth rate compared with the rise in expenses, else margin will be dented going forward.
- ▼ **Catastrophe Loss:** Palomar being a property and casualty insurer remains exposed to catastrophe loss, stemming from earthquakes, hurricanes, windstorms, floods and other severe events. The occurrence of such catastrophes could affect the financial condition and results of operations. Additionally, increased severity of such weather events, including hurricanes, could adversely impact the company's ability to predict, quantify, reinsure and manage catastrophe risk and may materially increase the losses resulting from such catastrophe events.
- ▼ **Stretched Valuation:** Valuation of the company remains stretched and expensive at current level. Looking at its price-to-book (P/B) ratio, the best multiple for valuing insurers, investors might not want to pay any further premium. Palomar Holdings currently has a trailing 12-month P/B ratio of 6.48, higher than the industry average of 1.24.

Exposure to cat loss that induces underwriting volatility and rising expenses due to higher losses and loss adjustment expenses, interest expense and acquisition expenses are concerns.

Last Earnings Report

Palomar Surpasses Q2 Earnings and Revenue Estimates

Palomar Holdings, Inc.'s second-quarter 2020 operating earnings of 52 cents per share beat the Zacks Consensus Estimate by 8.3% and improved 44.4% from the prior-year quarter.

Palomar witnessed improved premiums along with increase in net investment income and underwriting income in the reported quarter.

Behind the Q2 Headlines

Total revenues improved 68% year over year to \$42 million, mainly attributable to higher premiums, net investment income and commission and other income. Moreover, the top line exceeded the Zacks Consensus Estimate by 8.1%

Gross written premiums increased 43.6% year over year to \$83.8 million. Net written premiums grew 59% year over year to \$53.6 million owing to an increase in gross written premiums.

Net investment income increased 42.5% year over year to \$2.1 million. The increase was primarily due to a higher average balance of investments held during the three months ended Jun 30, 2020, due primarily to proceeds from the company's April 2019 IPO, investing of cash generated from operations and proceeds from the company's January 2020 secondary offering.

Palomar witnessed underwriting gain of \$12.4 million, up 73.7% from the year-earlier period.

Total expenses increased 59.8% to \$27.8 million, mainly due to higher losses and loss adjustment expenses, acquisition expenses and other underwriting expenses.

Adjusted combined ratio deteriorated 130 basis points (bps) year over year to 65.1%.

Financial Update

As of Jun 30, 2020, Palomar Holdings had assets worth \$584 million, up 47.7% from the level at 2019 end.

Cash and cash equivalents surged 230% from 2019-end level to about \$109.3 million.

Shareholder equity at the end of the reported quarter increased 71.6% from 2019-end to \$375.2 million.

Annualized adjusted return on equity was 16.4% in the second quarter of 2020, reflecting a contraction of 480 bps year over year.

2020 Outlook

Palomar Holdings affirmed its prior guidance of adjusted net income of \$50.5 to \$53.0 million, equating to a growth rate of 33% to 40% from 2019.

Quarter Ending 06/2020

Report Date	Aug 04, 2020
Sales Surprise	8.13%
EPS Surprise	8.33%
Quarterly EPS	0.52
Annual EPS (TTM)	1.90

Recent News

Palomar Holdings' Unit Gets Rating Action From A.M. Best – Jul 28, 2020

AM Best has assigned a Financial Strength Rating of A- (Excellent) and a Long-Term Issuer Credit Rating of "a-" to Palomar Excess and Surplus Insurance Company. The outlook of the ratings is stable.

Palomar Holdings Declares Pricing of Common Stock – Jun 23, 2020

Palomar Holdings announced the pricing of 1 million shares of its common stock whose par value is 0.01 cent per share. The shares are priced at \$82.00 per share. The company intends to deploy the net proceeds from the offering of shares for general corporate purposes, which include making contributions to the capital of Palomar Excess and Surplus Insurance Company, and to fund future growth.

Palomar Formed Palomar Excess and Surplus Insurance Company – Jun 23, 2020

Palomar Holdings formed Palomar Excess and Surplus Insurance Company (PESIC), a newly established surplus lines insurance company subsidiary.

Valuation

Palomar's shares are up 109.9% in the year-to-date period and 209.3% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 11.2% and 16.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 3.4% and 7.9%, respectively.

The S&P 500 index are up 4.7% in the year-to-date period and 15.7% in the past year.

The stock is currently trading at 6.85x trailing 12-month book value, which compares to 1.24x for the Zacks sub-industry, 2.46x for the Zacks sector and 4.53x for the S&P 500 index.

Over the past five years, the stock has traded as high as 7.84x and as low as 2.8x, with a 5-year median of 5.32x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$111 price target reflects 7.17x book value.

The table below shows summary valuation data for PLMR

Valuation Multiples - PLMR					
		Stock	Sub-Industry	Sector	S&P 500
P/B TTM	Current	6.85	1.24	2.46	4.53
	5-Year High	7.84	1.67	2.91	4.56
	5-Year Low	2.8	0.93	1.72	2.83
	5-Year Median	5.32	1.45	2.53	3.75
P/S F12M	Current	12.99	1.70	6.22	3.7
	5-Year High	13.41	11.26	6.67	3.7
	5-Year Low	4.11	1.39	4.97	2.53
	5-Year Median	7.59	1.84	6.06	3.05
P/E F12M	Current	44.23	25.04	16.5	22.77
	5-Year High	44.24	31.55	16.5	22.77
	5-Year Low	13.05	21.01	11.6	15.25
	5-Year Median	24.81	25.42	14.26	17.58

As of 08/20/2020

Industry Analysis Zacks Industry Rank: Top 49% (124 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
First American Financial Corporation (FAF)	Outperform	1
Axis Capital Holdings Limited (AXS)	Neutral	4
Chubb Limited (CB)	Neutral	3
Conifer Holdings, Inc. (CNFR)	Neutral	3
Everest Re Group, Ltd. (RE)	Neutral	3
Selective Insurance Group, Inc. (SIGI)	Neutral	3
W.R. Berkley Corporation (WRB)	Neutral	3
American International Group, Inc. (AIG)	Underperform	4

Industry Comparison Industry: Insurance - Property And Casualty				Industry Peers		
	PLMR	X Industry	S&P 500	AIG	CB	SIGI
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	4	3	3
VGM Score	F	-	-	B	C	C
Market Cap	2.70 B	1.26 B	23.46 B	25.09 B	55.72 B	3.34 B
# of Analysts	4	2	14	6	7	2
Dividend Yield	0.00%	1.31%	1.65%	4.39%	2.53%	1.65%
Value Score	F	-	-	B	B	B
Cash/Price	0.04	0.27	0.07	1.13	0.10	0.11
EV/EBITDA	125.05	5.17	13.34	2.96	9.79	8.26
PEG Ratio	NA	1.98	3.00	1.13	1.72	8.61
Price/Book (P/B)	6.85	0.97	3.12	0.40	1.02	1.45
Price/Cash Flow (P/CF)	65.09	10.37	12.60	2.79	10.47	10.37
P/E (F1)	49.54	13.87	21.61	11.28	17.16	16.01
Price/Sales (P/S)	18.46	0.81	2.44	0.52	1.56	1.20
Earnings Yield	1.99%	5.80%	4.43%	8.86%	5.83%	6.24%
Debt/Equity	0.00	0.24	0.76	0.63	0.25	0.24
Cash Flow (\$/share)	1.63	3.12	6.93	10.45	11.78	5.38
Growth Score	D	-	-	B	D	C
Hist. EPS Growth (3-5 yrs)	NA%	3.85%	10.44%	2.87%	-1.69%	11.01%
Proj. EPS Growth (F1/F0)	21.68%	-3.84%	-5.53%	-43.72%	-28.83%	-20.80%
Curr. Cash Flow Growth	103.81%	3.77%	5.20%	41.46%	0.06%	21.30%
Hist. Cash Flow Growth (3-5 yrs)	NA%	4.81%	8.52%	-3.88%	8.77%	13.47%
Current Ratio	0.93	0.43	1.33	0.34	0.31	0.31
Debt/Capital	0.00%	20.03%	44.50%	38.47%	20.32%	19.32%
Net Margin	28.80%	5.15%	10.13%	-9.46%	6.10%	6.73%
Return on Equity	17.46%	6.81%	14.67%	3.28%	5.98%	9.90%
Sales/Assets	0.33	0.31	0.51	0.09	0.20	0.31
Proj. Sales Growth (F1/F0)	56.56%	0.00%	-1.54%	-7.51%	2.60%	1.00%
Momentum Score	D	-	-	D	C	D
Daily Price Chg	1.09%	0.00%	-0.59%	-2.44%	-0.40%	-0.21%
1 Week Price Chg	-1.97%	0.07%	1.09%	1.08%	0.15%	-2.62%
4 Week Price Chg	25.42%	2.76%	1.91%	-8.60%	-8.79%	-3.08%
12 Week Price Chg	41.81%	5.77%	6.82%	-6.39%	-0.22%	4.99%
52 Week Price Chg	209.28%	-13.18%	1.47%	-45.81%	-20.47%	-30.79%
20 Day Average Volume	258,172	134,397	1,873,576	6,773,497	1,683,890	282,921
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-0.64%	-0.02%	-1.18%
(F1) EPS Est 4 week change	1.57%	2.35%	1.79%	-0.70%	3.86%	1.11%
(F1) EPS Est 12 week change	0.60%	-0.52%	3.35%	-10.82%	-27.77%	2.20%
(Q1) EPS Est Mthly Chg	0.48%	3.56%	0.42%	-0.54%	3.13%	7.51%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	F
Growth Score	D
Momentum Score	D
VGM Score	F

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

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