

Selective Insurance(SIGI)

\$56.09 (As of 07/20/20)

Price Target (6-12 Months): **\$59.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 12/30/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: C

Growth: C

Momentum: B

Summary

Selective Insurance is poised to witness top-line growth backed by sustained premium growth across its segments. Premiums have benefited from the company's compelling portfolio, high retention ratio, pure renewal price increase and new business growth. Net investment income should benefit from active portfolio management. Geographic expansion plays a vital role in diversification and growth of the company. Shares of Selective Insurance have underperformed the industry in a year's time. Nevertheless, it boasts a solid capital position on which it returns value to shareholders in the form of dividend payments. However, the company is exposed to cat loss, which results in earnings volatility. Elevated expenses exert pressure on operating margin. The company's high debt to capital and lower times interest earned also remain concerns.

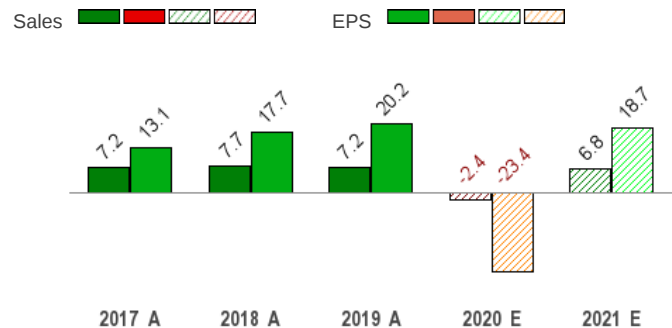
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$81.33 - \$37.48
20 Day Average Volume (sh)	270,518
Market Cap	\$3.3 B
YTD Price Change	-14.0%
Beta	0.73
Dividend / Div Yld	\$0.92 / 1.6%
Industry	Insurance - Property and Casualty
Zacks Industry Rank	Bottom 40% (150 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-12.5%
Last Sales Surprise	-3.3%
EPS F1 Est- 4 week change	-1.1%
Expected Report Date	07/29/2020
Earnings ESP	12.1%
P/E TTM	12.9
P/E F1	16.6
PEG F1	1.6
P/S TTM	1.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	715 E	733 E	747 E	758 E	2,952 E
2020	710 A	680 E	714 E	705 E	2,764 E
2019	686 A	701 A	713 A	730 A	2,832 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.83 E	\$1.03 E	\$0.90 E	\$1.16 E	\$4.00 E
2020	\$0.84 A	\$0.34 E	\$1.01 E	\$1.10 E	\$3.37 E
2019	\$0.90 A	\$1.16 A	\$0.97 A	\$1.37 A	\$4.40 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 07/20/2020. The reports text is as of 07/21/2020.

Overview

Headquartered in Branchville, NJ, Selective Insurance Group, Inc. was established in 1925. The company operates as a P&C insurer. It offers insurance products and services across the United States. Through its subsidiaries, the P&C insurer provides a wide range of insurance products and services, which includes property, casualty as well as flood insurances. The company caters to a wide set of clients including businesses, non-profit organizations, local government agencies as well as individuals.

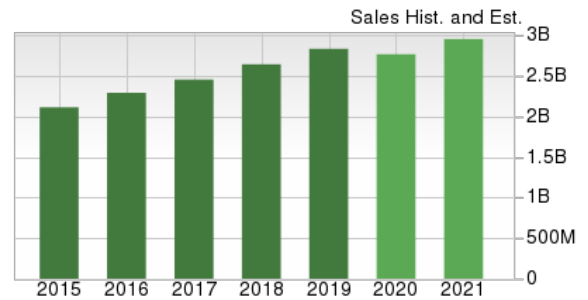
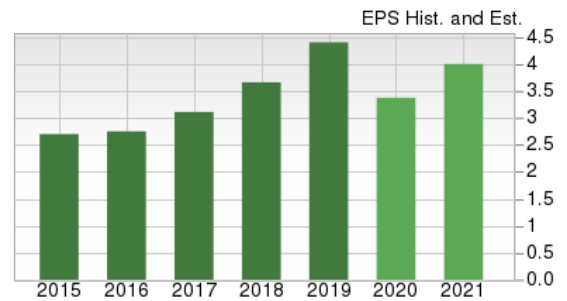
Selective Insurance classifies its operations through four segments, namely Standard Commercial Lines, Standard Personal Lines, Excess and Surplus (E&S) Lines plus Investments.

Standard Commercial Lines (79.8% of 2019 Net Premium Written)

— This segment offers insurance products and services to commercial enterprises including businesses, non-profit organizations and local government agencies. Presently, the segment represents 78% of the total insurance operations' net premiums written (NPW) and is sold across 25 states and the District of Columbia.

Standard Personal Lines (11.3%)— The segment offers products and services mainly to individuals, who have obtained coverage in the standard marketplace. The unit represents 13% of total insurance operations' NPW and is primarily sold in 13 Eastern and Midwestern states. The company boasts being the fifth largest writer of this coverage through the National Flood Insurance Program (NFIP) and writes flood business across all 50 states and the District of Columbia.

Excess and Surplus Lines (8.9%)— The segment provides insurance products and services to customers with not obtained coverage in the standard marketplace. Currently, the company writes commercial lines E&S coverages with the business forming 9% of the total insurance operations' NPW and sold in all 50 states and the District of Columbia.



Reasons To Buy:

▲ **Geographic Expansion** — The P&C insurer relies on geographic expansion for growth and diversification. Over the years, the company successfully expanded in New Hampshire along with presence in Southwest region such as Arizona, Colorado, Utah and Mexico. As a result, the company now has a total commercial lines presence in 27 states.

▲ **Improving Premiums** — Sustained premium growth across segments has helped the company's total premiums witness five-year CAGR (2015-2019) of 5.6%. However, net premiums written decreased 4% year over year in the first quarter of 2020 attributable to declines in both Commercial Lines and Personal Lines. The company expects pressure on premium growth for the next few quarters attributable to return audit premium adjustment and lower average policy size for new business. Nonetheless, we expect premiums written to increase, given the company's compelling portfolio, improved pricing, new business growth and high retention ratio.

Geographic expansions, improving premiums, improved rate environment leading to better investment income and solid capital position well poise Selective Insurance for long term growth.

Steady betterment of premiums has resulted in top-line improvement and over the past five years (2015-2019), total revenues witnessed a CAGR of 5.6%. The momentum continued through the first quarter of 2020 with revenues increasing 3.5% year over year.

▲ **Net Investment Income** — Despite a low interest rate environment in the past, the company managed to deliver impressive investment results. Net investment income rose 10% year over year in the first quarter of 2020, driven by alternative investment returns. For 2020, Selective Insurance projects an after-tax investment income of \$160 million, down from the prior guidance of \$185 million. However, as the company reports alternative investment returns on one-quarter lag, it expects second-quarter results to reflect the negative performance from the first quarter. Selective Insurance estimates after-tax loss of \$10 million to \$15 million for alternative investments for 2020.

▲ **Robust Capital Position** — Selective Insurance flaunts a sound capital structure and remains committed toward protecting the interests of its policyholders and shareholders alike while improving its financial strength and underwriting capabilities. Riding on a solid capital position, the company has been hiking dividends, which register a five-year CAGR (2014-2019) of nearly 12.09%. Such steadfast endeavors buoy confidence among investors, making it an attractive pick for yield-seeking investors. Its dividend yield of 1.6% appears attractive compared with the industry average of 0.5%.

▲ **Price Performance** — Shares of the company has lost 25.2% in the past year, wider than the industry's decline of 9.4%. Nevertheless, the company's favorable fundamentals should aid its shares.

Reasons To Sell:

- ▼ Stretched Valuation — Valuation remains stretched at the current level. Looking at the company's price-to-book ratio, which is the best multiple for valuing insurers, investors might not want to pay any further premium. The company currently has a trailing 12-month P/B ratio of 1.6x, higher than the industry average of 1.27x.
 - ▼ Exposure to Catastrophe Loss — Being a property and casualty (P&C) insurer, Selective Insurance remains exposed to catastrophe loss stemming from natural disasters and weather-related events. Such a massive loss poses an inherent risk to the P&C insurance business inducing volatility to its results. Combined ratio deteriorated 200 basis points on a year-over-year basis to 96.7% in the first quarter of 2020. For 2020, the company estimates combined ratio between 92% and 93%, an increase from the prior guidance of 91.5%, primarily due to expense ratio pressure from the estimated full-year impact of COVID-19 and 450 bps from catastrophe losses reflecting higher than expected cat losses through April and lower earned premium.
- The company estimated preliminary second-quarter net catastrophe losses of \$83 million, pre-tax. The expected loss could be due to the company's exposure to storms and civil unrest claims. It also estimated second-quarter combined ratio in the range of 98% to 99%, primarily due to higher-than expected losses from catastrophic events.
- ▼ Rising Expenses to Hurt Margin Expansion — Selective Insurance has been witnessing rising expenses over the years, primarily due to increasing loss and loss expense incurred and amortization of deferred policy acquisition costs. The metric increased 32% over the last five years and 3.7% in the first quarter of 2020. Increasing expenses have been weighing on net margin expansion. The first quarter of 2020 suffered 30 bps contraction in net margin. Hence, the company should strive to generate higher revenue growth rate compared with the rise in expenses. Also, expense ratio of 35.2% in the first quarter of 2020 deteriorated 190 bps from COVID-19-related bad debt expense and lower net premiums earned. Impact of COVID-19 outbreak is expected to continue affecting expense ratio.
 - ▼ Rising Debt Level: The company's debt has been increasing over the past many years inducing deterioration in debt to capital. Though at the end of the first quarter 2020, debt level was flat sequentially, debt to capital was 20.8%, up from 20% at the end of 2019. Also, long-term debt to capital of 20.8% compares unfavorably with the industry's measure of 1.3%. In addition, times interest earned, a measure to identify the company ability to service debt was 10.4% in the first quarter, down from 11% in the fourth quarter of 2019. This raises concerns as it indicates that its earnings are not sufficient to cover interest obligations.

Exposure to catastrophe loss due to natural disasters and weather-related events and elevated expenses continue to remain a concern for the company.

Last Earnings Report

Selective Insurance Q1 Earnings Miss, Decline Y/Y

Selective Insurance reported first-quarter 2020 operating income of 84 cents per share, missing the Zacks Consensus Estimate by 12.5%. Moreover, the bottom line deteriorated 6.7% from the year-ago period.

The reported quarter witnessed lower premiums written, higher catastrophic losses and expenses, offset by improved net investment income.

Quarter Ending **03/2020**

Report Date	May 05, 2020
Sales Surprise	-3.33%
EPS Surprise	-12.50%
Quarterly EPS	0.84
Annual EPS (TTM)	4.34

Behind the Headlines

Total revenues of \$710 million were up 3.5% from the year-ago quarter's figure. However, the top line missed the Zacks Consensus Estimate by 3.3%.

Net premiums written decreased 4% year over year to \$647.3 million attributable to declines in both Commercial Lines and Personal Lines. Net investment income rose 10% year over year to \$45.5 million, driven by alternative investment returns that benefited from strong returns from the fourth quarter of 2019 due to the one-quarter lag in reporting.

Total expenses increased 3.7% year over year to \$648.8 million primarily due to higher loss and loss expense incurred, amortization of deferred policy acquisition costs and other insurance expenses.

Combined ratio deteriorated 200 basis points (bps) on a year-over-year basis to 96.7%.

Segmental Results

Standard Commercial Lines net premiums written were down 5% year over year to \$518.4 million due to the \$75 million return audit and mid-term endorsement premium accrual.

Combined ratio deteriorated 190 bps to 96.7% from the prior-year quarter's level due to catastrophe losses of 4.0 percentage points that were partially offset by 1.9 percentage points of favorable prior-year casualty reserve development in the workers compensation line of business. Combined ratio increased 3.9 percentage points due to the COVID-19-related items.

Standard Personal Lines net premiums written were down 2% year over year to \$67.6 million due to a reduction in new business, which reflects an increasingly competitive marketplace. Combined ratio deteriorated 360 bps to 99.5% from the year-ago period's count due to the increase in the allowance for doubtful accounts due to the COVID-19 pandemic and higher catastrophe losses.

Excess & Surplus Lines net premiums written grew 8% year over year to \$61.3 million, driven by a 7% increase in new business. Combined ratio deteriorated 140 bps to 93.5% from the prior-year quarter's level due to higher non-catastrophe property losses and loss expenses, and an increase in the allowance for doubtful accounts due to the COVID-19 pandemic.

Financial Update

Selective Insurance exited the first quarter with total assets of \$8.9 billion, which climbed 2% above the level at the end of December 2019.

As of Mar 31, 2020, book value per share was \$35.11, having deteriorated 5% from the level as of 2019 end.

Annualized operating return on equity was 2.8% in the quarter under review, contracting 1040 points year over year.

2020 Guidance

Catastrophe losses of 4.5 points on the combined ratio have been estimated, indicating higher-than-expected cat losses through April combined with lower earned premium.

The company projects an after-tax net investment income of approximately \$160 million, down from the previous outlook of \$185 million principally due to an expected change in the full-year after-tax net investment income from alternative investments.

The company expects after-tax net investment loss from alternative investments between \$10 million and \$15 million against the previously mentioned gain of \$14 million.

Recent News

Selective Insurance Estimates Q2 Cat Loss, Updates Guidance - Jul 14, 2020

Selective Insurance estimates preliminary second-quarter net catastrophe losses of \$83 million, pre-tax. The expected loss could be due to the company's exposure to storms and civil unrest claims.

The company estimates second-quarter combined ratio in the range of 98% to 99%, primarily due to higher-than expected losses from catastrophic events.

Selective Insurance estimates net earnings per share ("EPS") for the second quarter in the range of 55 cents to 60 cents and operating EPS in the range of 35 cents to 40 cents, with the difference principally reflecting net realized and unrealized investment gains.

Valuation

Selective Insurance's shares are down 14% in the year-to-date period and 25.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 15.6% and 18.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 9.4% and 13.6%, respectively.

The S&P 500 index are up 0.3% in the year-to-date period and 8.7% in the past year.

The stock is currently trading at 1.6x trailing 12-month book value, which compares to 1.27x for the Zacks sub-industry, 2.37x for the Zacks sector and 4.41x for the S&P 500 index.

Over the past five years, the stock has traded as high as 2.4x and as low as 1.12x, with a 5-year median of 1.82x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$59 price target reflects 1.68x book value.

The table below shows summary valuation data for SIGI

Valuation Multiples - SIGI					
		Stock	Sub-Industry	Sector	S&P 500
P/B TTM	Current	1.6	1.27	2.37	4.41
	5-Year High	2.4	1.67	2.91	4.56
	5-Year Low	1.12	0.93	1.72	2.83
	5-Year Median	1.82	1.46	2.53	3.71
P/S F12M	Current	1.17	1.70	6.04	3.58
	5-Year High	1.62	11.26	6.7	3.58
	5-Year Low	0.81	1.39	4.96	2.53
	5-Year Median	1.31	1.85	6.07	3.02
P/E F12M	Current	15.08	24.61	16.38	22.83
	5-Year High	19.08	31.55	16.38	22.83
	5-Year Low	9.78	21.01	11.59	15.25
	5-Year Median	15.24	25.42	14.16	17.52

As of 07/21/2020

Industry Analysis Zacks Industry Rank: Bottom 40% (150 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
American Financial Group, Inc. (AFG)	Neutral	3
Axis Capital Holdings Limited (AXS)	Neutral	3
Hallmark Financial Services, Inc. (HALL)	Neutral	3
National General Holdings Corp (NGHC)	Neutral	3
Everest Re Group, Ltd. (RE)	Neutral	3
RenaissanceRe Holdings Ltd. (RNR)	Neutral	5
Alleghany Corporation (Y)	Neutral	2
Argo Group International Holdings, Ltd. (ARGO)	Underperform	4

Industry Comparison Industry: Insurance - Property And Casualty				Industry Peers		
	SIGI	X Industry	S&P 500	AFG	AXS	RNR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	5
VGM Score	C	-	-	A	F	D
Market Cap	3.35 B	1.15 B	22.29 B	5.41 B	3.34 B	7.94 B
# of Analysts	3	2	14	2	3	4
Dividend Yield	1.64%	1.33%	1.85%	2.99%	4.14%	0.78%
Value Score	C	-	-	A	C	D
Cash/Price	0.16	0.22	0.06	0.32	0.36	2.14
EV/EBITDA	7.92	5.16	13.06	3.57	8.98	-7.87
PEG Ratio	1.61	2.46	2.98	NA	19.18	0.90
Price/Book (P/B)	1.60	1.09	3.12	1.07	0.78	1.54
Price/Cash Flow (P/CF)	10.43	9.49	12.03	5.21	8.88	20.91
P/E (F1)	17.05	14.18	22.15	8.69	95.90	23.68
Price/Sales (P/S)	1.19	0.77	2.35	0.72	0.67	1.85
Earnings Yield	6.01%	6.87%	4.30%	11.50%	1.03%	4.22%
Debt/Equity	0.26	0.26	0.75	0.29	0.48	0.22
Cash Flow (\$/share)	5.38	3.12	6.94	11.57	4.47	8.62
Growth Score	C	-	-	B	F	C
Hist. EPS Growth (3-5 yrs)	11.89%	5.19%	10.82%	12.92%	-22.09%	-4.38%
Proj. EPS Growth (F1/F0)	-23.33%	-8.87%	-9.08%	-19.55%	-83.60%	-16.59%
Curr. Cash Flow Growth	21.30%	3.79%	5.51%	7.42%	-8.72%	3.81%
Hist. Cash Flow Growth (3-5 yrs)	13.47%	4.78%	8.55%	12.34%	-11.78%	-6.72%
Current Ratio	0.32	0.45	1.30	0.14	0.56	1.50
Debt/Capital	20.80%	20.54%	44.41%	22.59%	30.01%	43.45%
Net Margin	8.02%	3.85%	10.54%	3.57%	0.73%	9.16%
Return on Equity	12.30%	7.24%	15.74%	12.99%	-0.38%	6.06%
Sales/Assets	0.32	0.31	0.54	0.11	0.20	0.16
Proj. Sales Growth (F1/F0)	-2.28%	0.00%	-2.36%	-31.58%	-5.88%	11.78%
Momentum Score	B	-	-	A	F	F
Daily Price Chg	-0.39%	-0.34%	-0.77%	-2.78%	-2.94%	-1.16%
1 Week Price Chg	5.67%	2.81%	3.82%	4.57%	5.18%	4.68%
4 Week Price Chg	9.40%	1.31%	2.71%	-4.83%	-7.47%	1.95%
12 Week Price Chg	10.92%	4.70%	9.79%	-6.62%	13.32%	21.31%
52 Week Price Chg	-25.17%	-16.59%	-3.79%	-41.59%	-33.81%	1.30%
20 Day Average Volume	270,518	136,052	2,095,914	536,648	1,014,924	368,113
(F1) EPS Est 1 week change	0.90%	0.00%	0.00%	0.00%	-47.90%	-15.81%
(F1) EPS Est 4 week change	-1.08%	0.00%	0.09%	7.35%	-50.00%	-16.96%
(F1) EPS Est 12 week change	-15.81%	-16.21%	-4.60%	-7.94%	-90.43%	-47.42%
(Q1) EPS Est Mthly Chg	27.04%	0.00%	0.00%	-14.46%	-33.33%	-34.20%

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	C
Growth Score	C
Momentum Score	B
VGM Score	C

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.

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