Selective Insurance(SIGI)

$56.76 (As of 08/21/20)

Price Target (6-12 Months): **$60.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 12/30/19) Prior Recommendation: Underperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5) Zacks Style Scores: Value: B | Growth: C | Momentum: D	**3-Hold** VGM:B

Summary

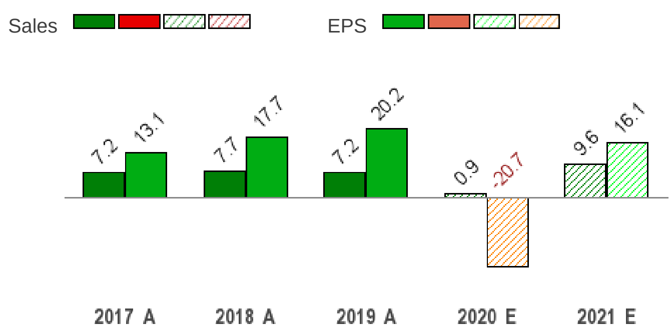
Selective Insurance's second quarter earnings of 40 cents per share beat the Zacks Consensus Estimate by 8.1% but declined 65.5% year over year. It is poised to witness top-line growth backed by sustained premium growth across its segments. Premiums have benefited from the company's compelling portfolio, 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 company's growth. Shares have underperformed the industry in the past year. Nevertheless, it boasts solid capital position on which it deploys capital effectively. However, it is exposed to cat loss, inducing earnings volatility. High costs exert pressure on operating margin. Its high debt level and lower times interest earned remain concern.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	$80.65 - $37.48
20 Day Average Volume (sh)	282,921
Market Cap	$3.4 B
YTD Price Change	-12.9%
Beta	0.72
Dividend / Div Yld	$0.92 / 1.6%
Industry	Insurance - Property and Casualty
Zacks Industry Rank	Top 48% (121 out of 252)
Last EPS Surprise	8.1%
Last Sales Surprise	-3.8%
EPS F1 Est- 4 week change	1.1%
Expected Report Date	NA
Earnings ESP	0.0%
P/E TTM	15.9
P/E F1	16.3
PEG F1	1.5
P/S TTM	1.2

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	764 E	776 E	790 E	802 E	3,132 E
2020	710 A	670 A	748 E	746 E	2,857 E
2019	686 A	701 A	713 A	730 A	2,832 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	$0.91 E	$1.04 E	$0.95 E	$1.15 E	$4.05 E
2020	$0.84 A	$0.40 A	$1.15 E	$1.10 E	$3.49 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 08/21/2020. The reports text is as of 08/24/2020.

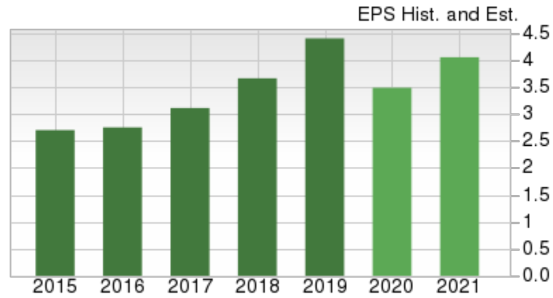
Overview

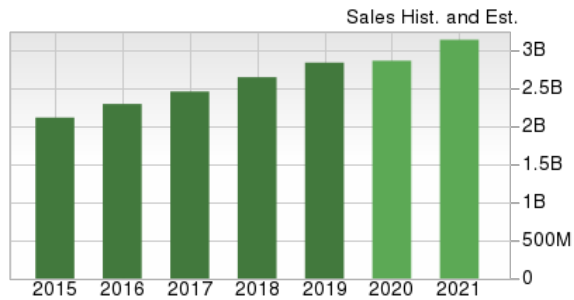
Headquartered in Branchville, NJ, Selective Insurance Group, Inc. was established in 1925. The company operates as a P&C insurer. It offers insurance products and services across the United States. Through its subsidiaries, the P&C insurer provides a wide range of insurance products and services, which 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:

▲ **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 remained flat from the year-ago period in the first half of 2020 as it was impacted by a $75 million accrual for estimated return audit and mid-term endorsement premiums. Nonetheless, we expect premiums written to increase, given the company's compelling portfolio, improved pricing, new business growth and high retention ratio.

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 half of 2020 with revenues remaining almost flat year over year.

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

▲ **Net Investment Income** — Despite a low interest rate environment in the past, the company managed to deliver impressive investment results. However, net investment income decreased 17% year over year in the first half of 2020 to $74 million due to losses from other investments portfolio. Nevertheless, for 2020, Selective Insurance projects an after-tax investment income of $170 million, up from the prior guidance of $160 million. Selective Insurance estimates $5 million in after-tax net investment income from alternative investments.

▲ **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.

▲ **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 12.1%. 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 28.2% in the past year, wider than the industry's decline of 2.5%. Nevertheless, the company's favorable fundamentals should aid its shares.

Reasons To Sell:

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

- **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 1.48, higher than the industry average of 1.24.

- **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 370 basis points on a year-over-year basis to 97.6% in the first half of 2020. For 2020, the company estimates combined ratio, excluding catastrophe losses, between 90% and 91%, an improvement from its first-quarter 2020 guidance, which was between 92% and 93%, and 600 bps from catastrophe losses, reflecting wider-than-expected losses through the first half of the year.

- **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 3.6% in the first half of 2020 to $1.3 billion. Increasing expenses have been weighing on net margin expansion. In the second quarter, net margin contracted 130 bps sequentially and 200 bps year over year. Hence, the company should strive to generate higher revenue growth rate compared with the rise in expenses. Also, expense ratio of 34.7% in the first half of 2020 deteriorated 130 bps due to the earned impact of the COVID-19 related premium items, which reduced premiums earned and increase in allowance for bad debt. The expense ratio is expected to face upward pressure due to operating costs being spread over a smaller premium base. Also, if the customers' finances are further impacted, the company has to increase allowance for bad debt, which would further affect the expense ratio in the remaining quarters.

- **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 second quarter 2020, debt level was flat from 2019-end level, total debt to total capital of 25.9% deteriorated 580 basis points from 2019-end and compared unfavorably with the industry's measure of 21.3%. In addition, times interest earned, a measure to identify the company ability to service debt was 8.6 in the second quarter, down from 11 in the fourth quarter of 2019 and compared unfavorably with the industry's measure of 8.5. This raises concerns as it indicates that its earnings are not sufficient to cover interest obligations.

Last Earnings Report

Selective Insurance's Q2 Earnings Beat, Plunge Y/Y

Quarter Ending	06/2020
Report Date	Jul 29, 2020
Sales Surprise	-3.77%
EPS Surprise	8.11%
Quarterly EPS	0.40
Annual EPS (TTM)	3.58

Selective Insurance Group, Inc. reported second-quarter 2020 operating income of 40 cents per share, beating the Zacks Consensus Estimate by 8.1%. However, the bottom line declined 65.5% from the year-ago period’s number.

Selective Insurance witnessed higher net premium written, offset by higher catastrophe losses and decline in alternative investment income, which is reported on a one-quarter lag.

Behind the Headlines

Total revenues of $670 million were down 4.4% from the year-ago quarter’s figure, primarily due to lower premiums earned and net investment income. Moreover, the same missed the Zacks Consensus Estimate by 3.7%.

Net investment income decreased 40% year over year to $28.5 million due to alternative investment losses of $16 million pre-tax, or $13 million after-tax, which are reported on a one-quarter lag, and reflected the market decline during the first quarter.

Net premiums written increased 3% year over year to $724.8 million attributable to increase in both Commercial Lines and Excess & Surplus Lines.

Total expenses increased 3.5% year over year to $639.8 million primarily due to higher loss and loss expense incurred, amortization of deferred policy acquisition costs and interest expenses.

Catastrophe losses increased 182% year over year to $83.2 million, primarily due to $43 million of losses related to two April storms and $20 million of losses related to civil unrest claims. Combined ratio deteriorated 530 basis points (bps) on a year-over-year basis to 98.4% in the quarter under review, primarily due to COVID-19-related underwriting items of $9.6 million and higher level of catastrophe losses. It is partially offset by the impact of net prior year favorable casualty reserve development, lower non-catastrophe property losses compared to the prior-year quarter and ongoing expense management initiatives.

Segmental Results

Standard Commercial Lines net premiums written were up 5% year over year to $583.3 million, attributable to increase in retention and solid renewal pure price rise. Combined ratio deteriorated 400 bps to 96.7% from the prior-year quarter’s level due to higher catastrophe losses.

Standard Personal Lines net premiums written declined 5% year over year to $78.2 million due to COVID-19-related personal automobile premium credits of $4.3 million, which was partially offset by increase in new business, renewal pure price and higher retention. Combined ratio deteriorated 1470 bps on a year-over-year basis to 108.8% in the quarter under review due to higher catastrophe losses, partially offset by a reduction in non-catastrophe property losses.

Excess & Surplus Lines net premiums written grew 3% year over year to $63.2 million, primarily attributable to increase in renewal pure price and new business. Combined ratio also deteriorated 590 bps to 100.9% due to higher catastrophe losses.

Financial Update

Selective Insurance exited the second quarter with total assets of $9.3 billion, which was 6% above the level at December 2019 end. As of Jun 30, 2020, book value per share was $38.43, up 4.1% from the level as of 2019 end. Annualized operating return on equity was 6.2% in the quarter under review, down 830 basis points year over year.

2020 Guidance

The company estimates GAAP combined ratio, excluding catastrophe losses, in the range of 90% to 91%, indicating an improvement from the earlier guidance of 92%-93% provided in the first quarter.

Catastrophe losses of 6.0 points on the combined ratio have been estimated, reflecting higher-than-expected losses through the first half of the year. As COVID-19 has not been designated a catastrophe event by the Insurance Services Office's Property Claims Services unit, such losses are not included in this ratio.

The company projects an after-tax investment income of $170 million, $10 million higher than first-quarter 2020 guidance of $160 million. It now expects up to $5 million in after-tax net investment income from alternative investments.

Overall effective tax rate is expected to be approximately 18.5%, which includes an effective tax rate of 18.5% for net investment income, indicating a tax rate of 5.25% for tax-advantaged municipal bonds and a tax rate of 21% for all other items.

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 12.9% in the year-to-date period and 28.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 10.8% and 17.1% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 2.5% and 7%, respectively.

The S&P 500 index are up 5.4% in the year-to-date period and 18.3% in the past year.

The stock is currently trading at 1.48x trailing 12-month book value, which compares to 1.24x for the Zacks sub-industry, 2.45x for the Zacks sector and 4.56x 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 $60 price target reflects 1.56x 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	1.48	1.24	2.45	4.56
	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	1.45	2.53	3.75
P/S F12M	Current	1.12	1.70	6.22	3.71
	5-Year High	1.62	11.26	6.67	3.71
	5-Year Low	0.81	1.39	4.97	2.53
	5-Year Median	1.3	1.84	6.06	3.05
P/E F12M	Current	14.74	25.07	16.4	22.85
	5-Year High	19.08	31.55	16.4	22.85
	5-Year Low	9.78	21.01	11.6	15.25
	5-Year Median	15.25	25.42	14.26	17.58

As of 08/21/2020

Industry Analysis Zacks Industry Rank: Top 48% (121 out of 252)

Top Peers

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

Industry Comparison Industry: Insurance - Property And Casualty

Industry Peers

	SIGI	X Industry	S&P 500	AFG	AXS	RNR
Zacks Recommendation (Long Term)	Neutral	-	-	Outperform	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	4	3
VGM Score	B	-	-	B	C	C
Market Cap	3.39 B	1.26 B	23.62 B	5.76 B	3.79 B	8.84 B
# of Analysts	2	2	14	2	3	4
Dividend Yield	1.62%	1.30%	1.65%	2.77%	3.64%	0.81%
Value Score	B	-	-	A	C	C
Cash/Price	0.11	0.27	0.07	0.47	0.43	2.10
EV/EBITDA	8.39	5.18	13.29	3.40	8.55	-9.05
PEG Ratio	1.54	1.97	3.03	NA	23.08	0.78
Price/Book (P/B)	1.48	0.93	3.11	0.94	0.80	1.30
Price/Cash Flow (P/CF)	10.55	10.35	12.69	5.62	10.08	20.02
P/E (F1)	16.36	13.80	21.51	9.42	115.41	19.58
Price/Sales (P/S)	1.22	0.80	2.43	0.77	0.77	1.92
Earnings Yield	6.13%	5.87%	4.46%	10.62%	0.87%	5.10%
Debt/Equity	0.24	0.24	0.76	0.31	0.38	0.17
Cash Flow ($/share)	5.38	3.12	6.93	11.57	4.47	8.62
Growth Score	C	-	-	D	B	D
Hist. EPS Growth (3-5 yrs)	11.01%	3.85%	10.44%	11.69%	-22.66%	-5.59%
Proj. EPS Growth (F1/F0)	-20.80%	-3.84%	-5.53%	-19.95%	-84.52%	-3.45%
Curr. Cash Flow Growth	21.30%	3.77%	5.20%	7.42%	-8.72%	3.81%
Hist. Cash Flow Growth (3-5 yrs)	13.47%	4.81%	8.52%	12.34%	-11.78%	-6.72%
Current Ratio	0.31	0.43	1.33	0.15	0.59	1.62
Debt/Capital	19.32%	20.03%	44.50%	23.79%	25.37%	38.10%
Net Margin	6.73%	5.15%	10.13%	3.13%	-0.41%	13.02%
Return on Equity	9.90%	6.81%	14.67%	11.34%	-1.85%	5.21%
Sales/Assets	0.31	0.31	0.51	0.11	0.19	0.17
Proj. Sales Growth (F1/F0)	1.00%	0.00%	-1.54%	-34.34%	-6.60%	24.10%
Momentum Score	D	-	-	C	D	B
Daily Price Chg	1.76%	-0.36%	-0.15%	-1.26%	-1.12%	-0.80%
1 Week Price Chg	-2.62%	0.07%	1.09%	2.56%	4.33%	-5.68%
4 Week Price Chg	-1.37%	1.34%	1.64%	2.98%	8.75%	-4.32%
12 Week Price Chg	6.83%	5.00%	6.72%	2.10%	15.23%	2.09%
52 Week Price Chg	-29.57%	-13.56%	1.00%	-35.89%	-31.16%	-8.30%
20 Day Average Volume	282,921	134,397	1,873,576	390,099	1,069,059	292,779
(F1) EPS Est 1 week change	-1.18%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	1.11%	2.35%	1.79%	-1.95%	-5.65%	15.76%
(F1) EPS Est 12 week change	2.20%	-0.52%	3.35%	-0.34%	-59.59%	-0.69%
(Q1) EPS Est Mthly Chg	7.51%	3.56%	0.42%	11.51%	-18.52%	14.37%

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	B
Growth Score	C
Momentum Score	D
VGM Score	B

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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