

Alleghany Corporation(Y)

\$487.11 (As of 05/18/20)

Price Target (6-12 Months): **\$416.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 02/19/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:D

Value: C

Growth: F

Momentum: A

Summary

Alleghany's first-quarter 2020 bottom line missed estimates attributable to soft performance at the Reinsurance segment. Exposure to catastrophe loss induces earnings volatility. Lower return on equity poses financial risk. Also, higher expenses continue to weigh on the company's margin. Shares of Alleghany have underperformed the industry year to date. Nonetheless, strong performance across insurance and reinsurance operations and better pricing will continue to boost premium revenues. Alleghany strives to grow via inorganic and organic means. It strives to achieve a solid balance sheet with higher liquidity and lower debt. Continued strong underwriting performances by TransRe, RSUI, CapSpecialty and PacificComp should drive results in the near term. Robust capital position should enable the company to deploy capital effectively.

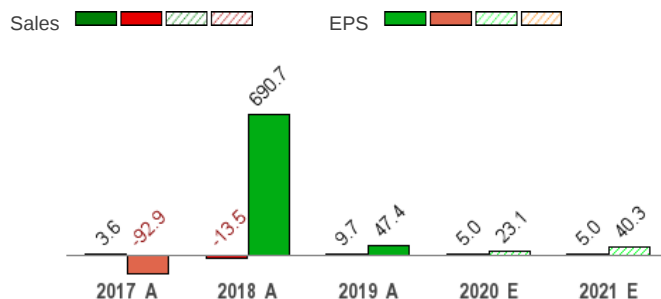
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$847.95 - \$426.87
20 Day Average Volume (sh)	74,229
Market Cap	\$7.0 B
YTD Price Change	-39.1%
Beta	0.65
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Insurance - Property and Casualty
Zacks Industry Rank	Bottom 43% (144 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-49.7%
Last Sales Surprise	NA
EPS F1 Est- 4 week change	-21.8%
Expected Report Date	08/04/2020
Earnings ESP	0.0%
P/E TTM	25.8
P/E F1	16.7
PEG F1	NA
P/S TTM	0.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					6,625 E
2020	2,024 A				6,309 E
2019	1,934 A	2,103 A	1,534 A	1,565 A	6,009 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$10.65 E	\$10.89 E	\$7.57 E	\$11.95 E	\$41.05 E
2020	\$4.99 A	\$4.65 E	\$5.97 E	\$10.38 E	\$29.25 E
2019	\$9.66 A	\$12.40 A	\$7.61 A	-\$6.09 A	\$23.77 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 05/18/2020. The reports text is as of 05/19/2020.

Overview

Established in 1929 and headquartered in New York, Alleghany Corporation and its subsidiaries engage in property and casualty (P&C) reinsurance and insurance businesses in the United States and internationally. The company was incorporated in Delaware in 1984.

Although the primary sources of revenues and earnings are reinsurance and insurance operations and investments, the company also generates revenues and earnings from a diverse portfolio of middle-market businesses that are owned and managed through its wholly-owned subsidiary Alleghany Capital.

Alleghany reports through three segments – **Reinsurance, Insurance and Alleghany Capital**.

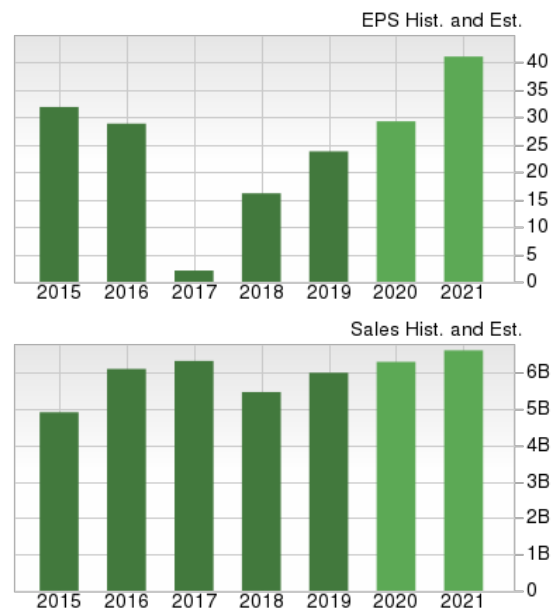
The Reinsurance segment (78.2% of 2019 net premiums written) consists of P&C reinsurance operations conducted by TransRe's reinsurance operating subsidiaries and is further reported through two major product lines – property and casualty & other. TransRe has been a subsidiary since March 2012.

The Insurance segment (21.8%) consists of P&C insurance operations conducted in the United States by AIHL through its insurance operating subsidiaries, RSUI and CapSpecialty. RSUI also writes a modest amount of assumed reinsurance business, which is included in the insurance segment. RSUI has been a subsidiary of AIHL since July 2003. CapSpecialty has been a subsidiary of AIHL since January 2002.

AIHL Re, a captive reinsurance company, which provides reinsurance to Alleghany's current and former insurance operating subsidiaries and affiliates, has been a wholly-owned subsidiary of Alleghany since its formation in May 2006. RSUI is headquartered in Atlanta, GA; CapSpecialty, is headquartered in Middleton, WI. AIHL Re, the Vermont-domiciled captive reinsurance company, provides reinsurance to current and former insurance operating subsidiaries and affiliates.

The insurance segment constitutes a smaller portion of the company's consolidated net premiums written and is reported through RSUI and CapSpecialty subsidiaries.

Prior to Dec 31, 2017, AIHL's insurance operations also included PacificComp.



Reasons To Sell:

- ▼ Shares of the company have lost 39.1% year to date, compared to the industry's decline of 23.6%. Exposure to cat loss, increasing expenses are likely to weigh on price.
- ▼ As a property and casualty insurer, Alleghany is exposed to catastrophe loss, causing volatility in underwriting results. Catastrophe loss in the first quarter of 2020 was \$181.6 million, much higher than \$3.4 million incurred in the year-ago quarter. Higher losses induced underwriting loss of \$24 million against the year-ago quarter profit of \$85 million. Combined ratio deteriorated 820 bps year over year in the first quarter of 2020. Given the unpredictability of cat occurrences, the underwriting results are always exposed to volatility.
- ▼ Alleghany has been experiencing an increase in expenses due to higher losses and loss adjustment expenses, operating expense and commissions, brokerage and other underwriting expenses. In the last five years the company witnessed an increase of 86% in expenses, with net margin contracting 170 basis points. In the first quarter of 2020, expenses rose 10.9% and net margin contracted 330 bps. The company must strive to generate revenue growth more than the magnitude increase in expenses; else margin will continue to erode.
- ▼ Alleghany's return on equity is 3.3%, lower than the industry average of 6.5%. The company's lower profitability reflects in relative inefficiency in utilizing shareholder's funds.

Exposure to catastrophe losses causing volatility in underwriting results and increase in expenses weighing on margin expansion can induce volatility in earnings results.

Risks

- Alleghany's top line has been improving over the past few years, driven by increasing gross premium written. This momentum continued in the first quarter of 2020 with revenues rising 4.6% and gross premiums written increasing 10.2%. Moreover, we expect continued strong underwriting performances by TransRe and RSUI, CapSpecialty and PacificComp should continue to drive the results.

Solid performances at TransRe and RSUI, CapSpecialty and PacificComp, helps them pay dividend to the parent company that is used to make acquisitions at Alleghany Capital, reduce debt, or repurchase shares.

- Alleghany considers strategic buyouts a prudent approach to ramp up its growth profile. Past buyouts of RSUI, CapSpecialty and PacificComp – responsible for insurance operations – were a testimony to the company's long-term growth strategy. In May 2018, Alleghany Capital, a subsidiary of Alleghany, announced buyouts of Russ Berrie and Applause brands from Larsen & Bowman Holdings Ltd. and Maple Licensing Ltd. through Jazwares' affiliate – Zag Toys, a division of Zacks Enterprises, Inc. The buyout will enable Alleghany to widen its product base by entering into the consumer products industry. Last month, it acquired a majority interest in Wilbert Funeral Services, Inc. Hence, the company through its subsidiaries pursues acquisitions that not only expands its geographical presence but also add capabilities to its portfolio.
- For a considerable period of time, the company's investment results were affected by a persistently low interest environment. However, the company witnessed a turnaround in 2017, which continued through 2019. Though net investment income declined 8.9% in the first quarter of 2020 attributable to losses on credit-related partnership investments, we expect it to be back on growth track and aid top-line improvement at a steady pace.
- Alleghany boasts a solid balance sheet with high liquidity and improving leverage. With modest leverage (debt to equity was 16.2%, improving 40 bps sequentially and comparing favorably with the industry average of 21.8%) and a decent capitalized base, Alleghany is well-positioned to support its subsidiaries in taking advantage of growth opportunities. Though its times interest earned of 1.8, a measure to identify a company's ability to service debt, was lower sequentially, its cash balance of \$1.6 billion (up 31.9% from 2019 end level) at first-quarter 2020 end suggests that the company has sufficient cash reserves to meet its debt obligations.

The company has doubled its book value per share since the financial crisis of 2008. Book value per share was \$463.9, up 11.8% from 2019 end.

- Banking on its strong capital position, Alleghany is engaged in share buybacks, which in turn, enhances shareholder value. Though the company does not resort to paying dividends, the board of directors paid out a special dividend of \$15 per share in March 2020. The company had \$582.9 million remaining under repurchase authorization as on Mar 31, 2020.
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Last Earnings Report

Alleghany Q1 Earnings Miss Estimates, Revenues Rise Y/Y

Alleghany reported first-quarter 2020 adjusted income of \$4.99 per share, which missed the Zacks Consensus Estimate by nearly 5%. The bottom line plunged 48.3% year over year.

The company witnessed better results at Insurance segment but the performance of the Reinsurance segment was soft.

Operational Update

Operating revenues improved 4.6% year over year to \$2 billion on higher net premiums earned.

Net premiums written rose 10.7% year over year to \$1.5 billion.

Net investment income came in at \$112 million, down 8.9% year over year, attributable to losses on credit-related partnership investments.

Underwriting loss was \$24 million against the year-ago quarter's profit of \$85 million. Losses include \$153 million of catastrophe losses at TransRe related to the COVID-19 pandemic.

Total costs and expenses increased 10.4% to \$1.9 billion.

Alleghany Capital's pretax earnings were \$0.3 million, down from \$30.2 million in the year-ago quarter.

Segment Update

Reinsurance Segment: Net premiums written improved 9.3% to \$1.2 billion owing to an increase in various domestic casualty lines of business written, including general liability, professional liability and umbrella lines of business, partially offset by a slight decrease in property lines of business written globally and the impact of changes in foreign currency exchange rates.

Underwriting loss was \$1678.9 million against year-ago quarter's income of \$40 million. Combined ratio deteriorated 1090 basis points to 107%, reflecting catastrophe losses, largely related to the Pandemic.

Insurance Segment: Net premiums written increased 16% to \$322.7 million, driven by growth at RSUI.

Underwriting income of \$54.5 million improved 21.9% year over year. The combined ratio of the reported segment improved 90 basis points to 82.5%.

Financial Update

Cash balance was \$1.6 billion, up 31.9% from 2019 end level.

Debt balance of \$1.5 billion decreased 13.5% from 2019-end level.

Allegheny's shareholder equity at the end of the first quarter increased 14.1% to \$7.9 billion down 10.5% from 2019 end level.

Book value per share was \$549.07 as of Mar 31, 2020, down 7.7% from the level as of Dec 31, 2019.

Cash outflow from operating activities was \$7.3 billion, lower than \$66.4 billion outflow in year ago quarter.

Share Repurchase Update

Allegheny bought back shares worth \$44 million in the quarter.

As of Mar 31, 2020, the company had \$583 million remaining under its share repurchase authorization.

Quarter Ending 03/2020

Report Date	May 05, 2020
Sales Surprise	NA
EPS Surprise	-49.70%
Quarterly EPS	4.99
Annual EPS (TTM)	18.91

Recent News

Alleghany Offers 3.625% \$500 Million Senior Unsecured Notes - May 13, 2020

Alleghany announced the pricing of \$500 million aggregate principal amount of senior unsecured notes. The notes carry an interest rate of 3.625% and are scheduled to mature in 2030.

The company aims to deploy the net proceeds for general corporate purposes, which may include the repayment of existing debt.

Alleghany's Unit Closes Buyout of Squishmallows Owner Kellytoy – Apr 1, 2020

Alleghany Corporation's wholly-owned subsidiary Alleghany Capital Corporation declared that its subsidiary, Jazwares, LLC has acquired a majority stake in Kelly Toys Holdings, LLC and Kelly Amusement Holdings, LLC, formerly known as Kellytoy Worldwide, Inc. and Kellytoy (USA), Inc., collectively known as Kellytoy.

With the acquisition of Kellytoy, Jazwares will get the opportunity to grow into a leading toy industry platform with the combination of Jazwares' unique operating capabilities and Alleghany Capital's financial backing.

Alleghany's Subsidiary Acquires Majority Stake in Wilbert – Apr 1, 2020

Alleghany Corporation's unit Alleghany Capital has acquired a majority stake in Wilbert. Notably, Alleghany Capital signed a deal to buy a 45% equity stake in Wilbert in the year 2017.

Wilbert's solid business model will enable Alleghany Capital to leverage potential growth opportunities prevailing in noninsurance markets.

Valuation

Alleghany Corporation shares are down 39.1% in the year-to-date period and 28.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 23.6% and 26.1% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 16.7% and 18.9%, respectively.

The S&P 500 index are down 8.2% in the year-to-date period and up 3.8% in the past year.

The stock is currently trading at 0.89x trailing 12-month tangible book value, which compares to 1.09x for the Zacks sub-industry, 2.25x for the Zacks sector and 3.91x for the S&P 500 index.

Over the past five years, the stock has traded as high as 1.38x and as low as 0.74x, with a 5-year median of 1.08x. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$416 price target reflects 0.75x tangible book value.

The table below shows summary valuation data for Y

Valuation Multiples - Y					
		Stock	Sub-Industry	Sector	S&P 500
P/B TTM	Current	0.89	1.09	2.25	3.91
	5-Year High	1.38	1.67	2.90	4.56
	5-Year Low	0.74	0.93	1.71	2.83
	5-Year Median	1.08	1.46	2.53	3.65
P/S F12M	Current	1.27	1.40	5.81	3.34
	5-Year High	1.8	11.26	6.7	3.44
	5-Year Low	1.24	1.40	4.99	2.53
	5-Year Median	1.6	1.87	6.05	3.01

As of 05/18/2020

Industry Analysis Zacks Industry Rank: Bottom 43% (144 out of 254)



Top Peers

Company (Ticker)	Rec	Rank
American Financial Group, Inc. (AFG)	Neutral	3
Cincinnati Financial Corporation (CINF)	Neutral	4
First American Financial Corporation (FAF)	Neutral	4
Fidelity National Financial, Inc. (FNF)	Neutral	4
Markel Corporation (MKL)	Neutral	4
Everest Re Group, Ltd. (RE)	Neutral	4
W.R. Berkley Corporation (WRB)	Neutral	3
Arch Capital Group Ltd. (ACGL)	Underperform	5

Industry Comparison Industry: Insurance - Property And Casualty				Industry Peers		
	Y	X Industry	S&P 500	AFG	MKL	RE
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	4	-	-	3	4	4
VGM Score	D	-	-	A	D	B
Market Cap	6.97 B	1.14 B	20.09 B	5.21 B	11.63 B	9.07 B
# of Analysts	1	2	14	3	4	2
Dividend Yield	0.00%	1.26%	2.1%	3.10%	0.00%	3.44%
Value Score	C	-	-	A	D	B
Cash/Price	0.32	0.22	0.07	0.36	0.41	0.15
EV/EBITDA	4.76	4.75	12.13	3.43	3.86	7.31
PEG Ratio	NA	1.75	2.72	NA	NA	NA
Price/Book (P/B)	0.89	0.96	2.75	1.03	1.19	1.06
Price/Cash Flow (P/CF)	15.11	8.12	10.86	5.02	14.40	8.14
P/E (F1)	16.50	12.76	20.10	8.38	49.40	10.55
Price/Sales (P/S)	0.85	0.72	2.05	0.70	1.57	1.10
Earnings Yield	6.00%	7.14%	4.77%	11.93%	2.02%	9.48%
Debt/Equity	0.19	0.26	0.76	0.29	0.37	0.08
Cash Flow (\$/share)	32.24	3.12	7.01	11.57	58.60	22.15
Growth Score	F	-	-	B	C	C
Hist. EPS Growth (3-5 yrs)	-15.93%	4.86%	10.87%	12.92%	6.49%	-18.46%
Proj. EPS Growth (F1/F0)	23.05%	-2.01%	-10.31%	-19.68%	-56.08%	-19.87%
Curr. Cash Flow Growth	25.33%	5.61%	5.51%	7.42%	13.53%	310.65%
Hist. Cash Flow Growth (3-5 yrs)	-8.44%	7.31%	8.55%	12.34%	9.05%	-5.41%
Current Ratio	0.33	0.45	1.28	0.14	0.60	0.32
Debt/Capital	17.98%	20.55%	44.46%	22.59%	27.81%	7.36%
Net Margin	0.69%	3.92%	10.59%	3.57%	-2.61%	8.25%
Return on Equity	3.26%	7.52%	16.29%	12.99%	6.33%	8.48%
Sales/Assets	0.31	0.31	0.55	0.11	0.20	0.31
Proj. Sales Growth (F1/F0)	0.00%	0.00%	-2.49%	0.00%	5.56%	10.09%
Momentum Score	A	-	-	D	D	F
Daily Price Chg	6.24%	5.64%	5.21%	6.56%	1.50%	6.76%
1 Week Price Chg	-13.57%	-5.25%	-4.56%	-17.19%	-4.39%	-4.45%
4 Week Price Chg	-10.77%	-4.99%	4.12%	-13.62%	-9.03%	-5.33%
12 Week Price Chg	-37.23%	-23.41%	-16.39%	-45.48%	-36.06%	-36.28%
52 Week Price Chg	-28.79%	-26.23%	-5.84%	-41.59%	-20.19%	-27.71%
20 Day Average Volume	74,229	132,317	2,651,378	742,212	65,388	475,463
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-2.77%	0.00%	-8.62%
(F1) EPS Est 4 week change	-21.84%	-9.45%	-4.48%	-11.59%	-57.26%	-29.47%
(F1) EPS Est 12 week change	-36.48%	-18.82%	-16.39%	-26.00%	-57.02%	-32.88%
(Q1) EPS Est Mthly Chg	-56.83%	-9.84%	-9.90%	-39.54%	-23.17%	-63.13%

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	F
Momentum Score	A
VGM Score	D

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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