Why Intact Financial Corporation Could Easily Cross $100

Description

Intact Financial Corporation (TSX:IFC) is having a pretty quiet year so far. Shares of Canada's largest property and casualty insurance company have lost roughly 3% year to date. A bigger part of the decline came after the company announced its plans to acquire **OneBeacon Insurance Group, Ltd** (NYSE:OB) earlier this month. While Bay Street appears to be unsure about what to do with Intact Financial shares, analysts at **Bank of Nova Scotia** just raised their price objective on the stock to $107, representing nearly 15% upside from current prices.

While I usually take analyst ratings with a grain of salt simply because they can change even before I book my next trade, I have to agree with Bank of Nova Scotia on Intact Financial's prospects. Yes, investors, Intact Financial looks compelling right now for three big reasons.

The acquisition could be a game-changer

On May 2, Intact announced it will acquire U.S.-based OneBeacon for an all-cash deal worth $2.3 billion. Intact maintains that the acquisition will be "neutral" to its net operating income per share (NOIPS) in 2018 and will generate mid-single digit NOIPS within two years of closing, which is what seems to have gotten the market wary. But investors need to consider the long-term potential.

The acquisition isn't a small one, and investors need to understand that integration takes times in such deals, especially when it's cross-border. OneBeacon, currently controlled by **White Mountains Insurance Group Ltd.** (NYSE:WTM), is present in 50 states across the U.S. It is primarily a specialty insurer that offers insurance for products that may not fall under the purview of traditional insurances, catering to customers in marine, technology, healthcare, transportation, entertainment, and financial institutions, among others.

So, I see a two-way benefit for Intact: the acquisition establishes a presence in the U.S. insurance market and strengthens its foothold in the high-margin specialty insurance market in Canada. That sounds like a win-win, as this chart from Intact's presentation also highlights.

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Chart showing how Intact will benefit from its OneBeacon acquisition.
Image source: Intact Financial

I also wouldn't be surprised if Intact lists itself on the U.S. stock exchange some years down the line because it'll be a much bigger entity than the already listed OneBeacon, which currently has a market capitalization of under US$2 billion.

Operational performance on track

Higher catastrophe losses have been denting Intact's bottom line in recent quarters, but its combined ratio for Q1 was still under 100% at 98.2%.

The combined ratio reflects the strength of an insurance company's operations, as it compares its claims and expenses as a percentage of its earned premiums. A ratio below 100% means premiums are higher and the core underwriting business is profitable. I use the word “core” here because insurance companies also earn from investments.

Intact’s Q1 premiums grew 4% year over year, return on equity stayed above the 10% mark, and book value per share grew 8% to $43.14. Book value is an important measure for insurance companies, and Intact isn’t disappointing on that front.

Attractive dividends

Despite fears that the OneBeacon acquisition could pressure Intact’s cash balance, I don’t see any reason for income investors to be wary. Intact has increased its dividend every year for more than a decade, doubling it in just eight years. It currently yields a good 2.7%.

Earlier this year, Intact hiked the dividend by 10%. Considering that management has had growth via acquisitions in mind for quite some time now, I don’t see why it would raise dividends, unless it’s confident it can maintain or grow them.

Overall, Intact is a complete package that long-term investors need in a stock. It’s a leader in its industry with an expanding book value, a strong history of returns on equity and dividends, and big growth catalysts ahead. The stock price should reflect these, giving you rich returns along the way.

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