

# Tower Limited

## New Zealand General Insurance Digest

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The New Zealand General Insurance Digest provides a snapshot of relevant information for the general insurance industry. We detail information pertinent to Tower (TWR), local financial comparables and Australasian listed insurance peers. Edition 1.

### Insurance industry news and weather event update

- Insurance companies continue to see the impacts of COVID-19, the Russia-Ukraine conflict and global supply chain issues, leading to high claims inflation as the cost of repairs and replacements continues to rise. Anecdotal evidence, however, is that building cost inflation is moderating.
- The five-year average claims cost across all natural disasters (excluding earthquakes) for all insurers is NZ\$256m per annum. This compares with the ten-year average of NZ\$213m per annum and forty year average of NZ\$89m.
- S&P predicts the overall NZ insurance industry's combined ratio to remain between 87% and 90% over the next two to three years.
- Statistics NZ has released coastal data going back 120 years that highlights sea levels have been rising faster in the past 60 years.
- There have been eight significant insurance events this year-to-date, as experienced by all insurance companies, including:
  - New Zealand weather (August), costing ~NZ\$12m
  - South Island weather (July), costing ~NZ\$16m
  - New Zealand weather (July), costing ~NZ\$15m
  - North and South Island Storm (June), costing ~NZ\$15m
- In early September, TWR signed two partnership agreements with advisory firm Kiwi Adviser Network (KAN) and Ray White.
- A report published by AA Insurance saw thefts and attempted thefts of motor vehicles in New Zealand rising by +37% for the year ended 30 June 2022, with Auckland experiencing a +43% year-on-year increase in vehicle thefts, driven by the surge of ram raids.
- In August, TWR announced it would use a risk-based pricing model for coastal erosion, in what is being regarded as a significant step by the industry to combat climate change.
- Mergers and acquisitions in the global insurance industry hit their highest rate in ten years in the first half of 2022, reported international law firm Clyde & Co.

### Stock Performances

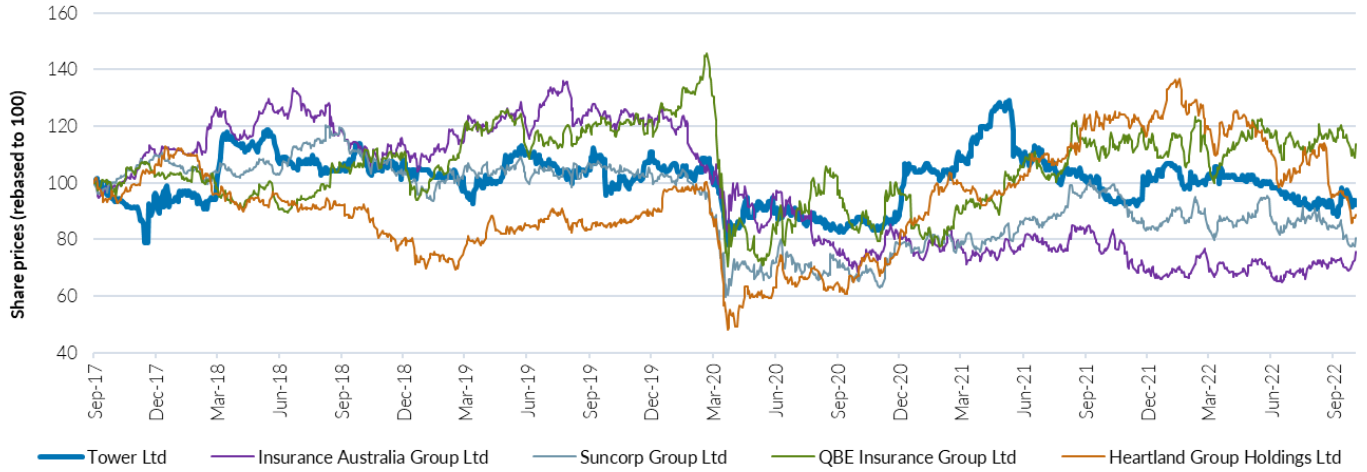
The listed Australasian insurance sector and TWR's financial peers have recently produced a wide range of performances. Over the last three months, IAG (+11.5%) is the only comparable company to have produced a positive return, with Heartland Bank (HNZ) producing the worst (-14.7%). This compared to TWR at -3.8% over three months. Over twelve months: QBE (+3.3%), IAG (-2.2%), TWR (-3.4%), SUN (-18.0%), and HGH (-27.3%).

**Tower Limited (TWR)**

<b>Market data (NZ\$)</b>						<b>Spot valuation (NZ\$)</b>					
Priced as at 04 Oct 2022					<b>0.63</b>	PE relative					<b>0.79</b>
52 week high / low					0.73 / 0.60	P/Book relative					0.74
Market capitalisation (NZ\$m)					239.1	DCF					0.71
											0.95
<b>Key WACC assumptions</b>						<b>DCF valuation summary (NZ\$m)</b>					
Risk free rate					4.00%	Total firm value					450
Equity beta					1.10	(Net debt)/cash					0
WACC					10.1%	Less: Capitalised operating leases					(48)
Terminal growth					1.5%	Value of equity					402
<b>Profit and Loss Account (NZ\$m)</b>						<b>Valuation Ratios</b>					
Sales revenue (GEP)	2020A	2021A	2022E	2023E	2024E	EV/EBITDA (x)	2020A	2021A	2022E	2023E	2024E
Normalised EBITDA	n/a	n/a	n/a	n/a	n/a	EV/EBIT (x)	n/a	n/a	n/a	n/a	n/a
Depreciation and amortisation	n/a	n/a	n/a	n/a	n/a	PE (x)	22.1	14.2	10.6	8.2	7.0
Normalised EBIT	n/a	n/a	n/a	n/a	n/a	Price/NTA (x)	1.2	1.2	1.3	1.2	1.2
Net interest	n/a	n/a	n/a	n/a	n/a	Free cash flow yield (%)	7.9	42.2	19.5	27.1	27.9
Associate income	0	0	0	0	0	Net dividend yield (%)	0.0	7.9	8.7	9.5	10.3
Tax	(7.9)	(9.1)	(12.1)	(14.9)	(17.3)	Gross dividend yield (%)	0.0	7.9	8.7	9.5	10.3
Minority interests	0.4	0.6	0.1	0	0						
Normalised NPAT	11.9	18.7	23.6	29.3	34.3	<b>Key Ratios</b>					
Abnormals/other	0	0	0	0	0	Return on assets (%)	2020A	2021A	2022E	2023E	2024E
Reported NPAT	11.9	18.7	23.6	29.3	34.3	Return on equity (%)	n/a	n/a	n/a	n/a	n/a
Normalised EPS (cps)	2.9	4.4	5.9	7.7	9.1	Return on funds employed (%)	3.4	5.4	7.5	9.1	10.4
DPS (cps)	0	5.0	5.5	6.0	6.5	EBITDA margin (%)	0.0	0.0	0.0	0.0	0.0
						EBIT margin (%)	n/a	n/a	n/a	n/a	n/a
						Capex to sales (%)	n/a	n/a	n/a	n/a	n/a
						Capex to depreciation (%)	2.8	3.0	3.1	3.1	3.1
						Imputation (%)	n/a	n/a	n/a	n/a	n/a
						Pay-out ratio (%)	0	0	0	0	0
							0	113	93	78	72
<b>Growth Rates</b>						<b>Capital Structure</b>					
Revenue (%)	2020A	2021A	2022E	2023E	2024E	Solvency capital	2020A	2021A	2022E	2023E	2024E
EBITDA (%)	8.0	6.2	7.9	11.1	9.8	Minimum solvency capital (MSC)	155.9	150.5	179.4	171.2	174.0
EBIT (%)	n/a	n/a	n/a	n/a	n/a	Total regulatory capital	56.6	52.3	66.3	73.5	73.2
Normalised NPAT (%)	n/a	n/a	n/a	n/a	n/a	Solvency ratio (%)	106.6	102.3	83.3	91.3	91.3
Normalised EPS (%)	-28.2	57.1	26.4	24.1	17.2		275	287	271	233	238
Ordinary DPS (%)	-39.7	55.4	33.9	30.2	17.2						
	n/a	n/a	10.0	9.1	8.3	<b>Operating Performance</b>					
						2020A	2021A	2022E	2023E	2024E	
<b>Cash Flow (NZ\$m)</b>						Gross written premium	377.2	404.7	448.6	499.8	542.0
EBITDA	2020A	2021A	2022E	2023E	2024E	Gross earned premium	372.6	395.5	426.6	474.2	520.9
Working capital change	n/a	n/a	n/a	n/a	n/a	Reinsurance premium	(57.2)	(62.2)	(67.0)	(68.6)	(75.5)
Interest & tax paid	0	0	0	0	0	Net earned premium	315.3	333.3	359.6	405.5	445.4
Other	0	0	0	0	0	Net claims expense	(181.1)	(204.3)	(216.3)	(259.9)	(287.5)
Operating cash flow	18.9	100.9	46.6	64.8	66.8	* includes Large event claims of	(9.7)	(13.9)	(20.0)	(30.0)	(31.5)
Capital expenditure	(10.5)	(12.0)	(13.3)	(14.9)	(16.1)	Management & sales expenses	(126.6)	(123.3)	(130.3)	(134.9)	(139.4)
(Acquisitions)/divestments	(9.5)	(14.4)	(4.4)	0	0	Underwriting profit	31.8	28.0	36.0	33.7	41.5
Other	(9.4)	(24.5)	(2.8)	(3.2)	(3.4)	Investment and other revenue	5.3	0.2	0.5	11.4	11.1
Funding available/(required)	(10.5)	49.9	26.1	46.8	47.3	Financing and other costs	(1.1)	(0.4)	(0.9)	(0.9)	(0.9)
Dividends paid	0	(10.5)	(20.9)	(22.8)	(24.7)	Profit before tax	20.3	28.5	35.7	44.2	51.7
Equity raised/(returned)	44.9	0	(30.4)	0	0	Tax expense	(7.9)	(9.1)	(12.1)	(14.9)	(17.3)
(Increase)/decrease in net debt	34.4	39.4	(25.2)	24.0	22.6	Profit after taxation (Reported)	12.3	19.3	23.6	29.3	34.3
						Abnormals	(1.3)	(1.1)	0	0	0
						Comprehensive profit	11.0	18.2	23.6	29.3	34.3
<b>Balance Sheet (NZ\$m)</b>						<b>Key ratios</b>					
Working capital	2020A	2021A	2022E	2023E	2024E	Tower Direct GWP growth %	13.7%	26.4%	11.8%	11.5%	9.0%
Fixed assets	184.1	146.9	154.2	171.8	186.3	Partnership GWP growth %	2.8%	-30.0%	13.0%	14.0%	8.0%
Intangibles	10.0	9.4	10.5	11.8	13.0	Total GWP growth %	5.7%	7.3%	10.8%	11.4%	8.4%
Right of use asset	119.6	120.6	125.5	129.2	133.1	Total claims ratio %	49.3%	54.3%	53.8%	58.4%	59.4%
Other assets	7.2	25.6	23.2	20.8	18.4	MER %	39.2%	37.1%	36.2%	33.3%	31.3%
Total funds employed	277.6	313.0	313.0	313.0	313.0	Combined ratio %	88.5%	91.4%	90.0%	91.7%	90.7%
Net debt/(cash)	598.6	615.5	626.4	646.6	663.9						
Lease liability	(80.1)	(116.1)	(90.9)	(115.0)	(137.5)						
Other liabilities	8.7	39.4	36.6	33.4	30.0						
Shareholder's funds	322.9	342.5	365.8	406.7	440.3						
Minority interests	345.0	347.0	314.9	321.5	331.2						
Total funding sources	598.6	615.5	626.4	646.6	663.9						

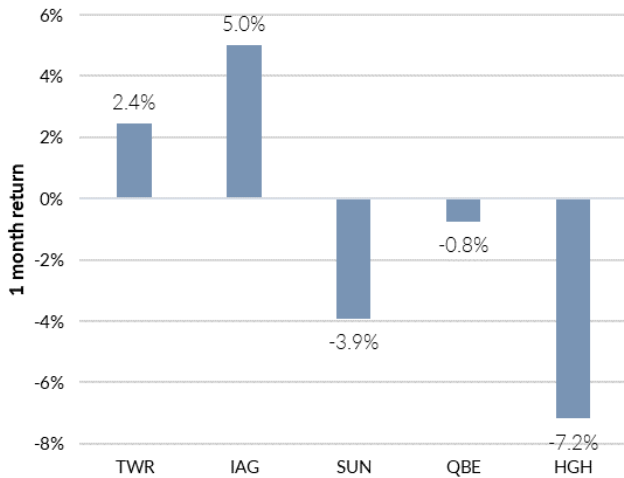
## Sector performance (of relevant peers)

Figure 1. Sector performance of relevant comparables



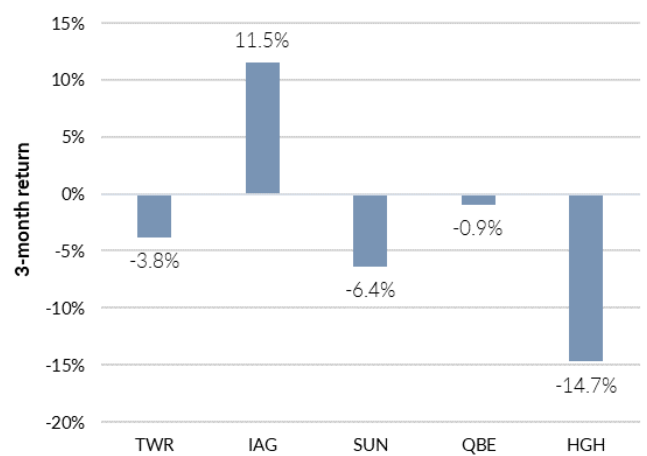
Source: Forsyth Barr analysis

Figure 2. Peer group returns over one month



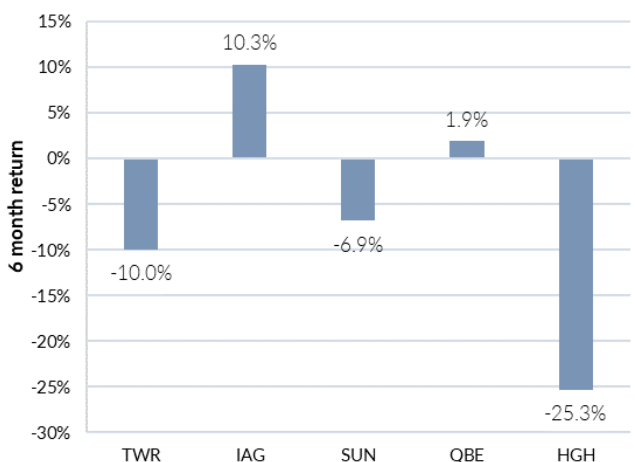
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

Figure 3. Peer group returns over three months



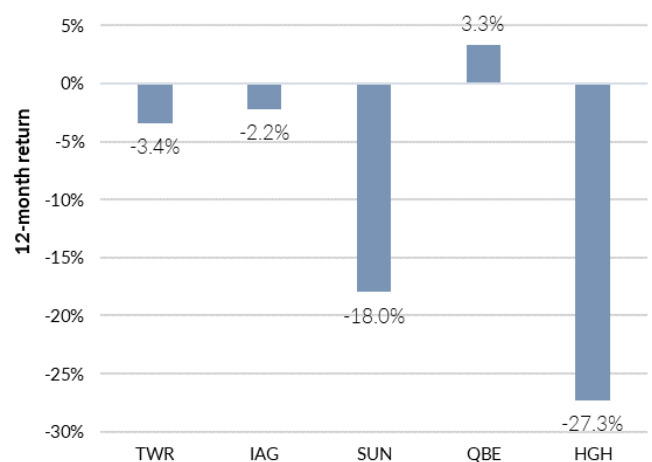
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

Figure 4. Peer group returns over six months



Source: Forsyth Barr analysis

Figure 5. Peer group returns over 12 months



Source: Forsyth Barr analysis

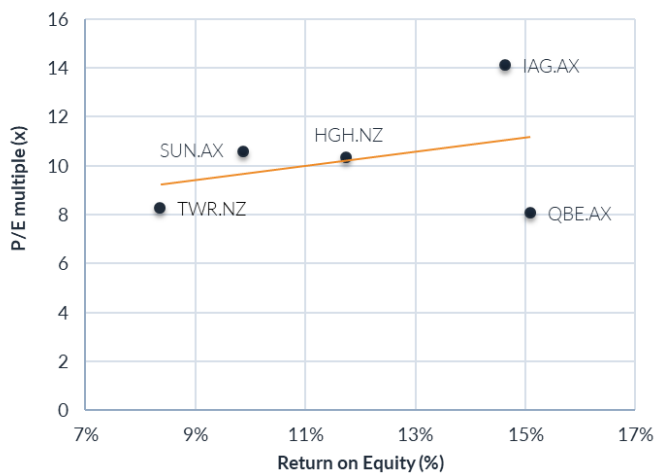
## Sector ratios (of relevant peers)

Figure 6. Table of relevant peers

Ticker	Next Bal. Date	Company	Share Price	Market Cap (NZ\$m)	PE (x)		Div Yield (%)	P/B (x)		ROE %	
					1-yr fwd	2-yr fwd		1-yr fwd	2-yr fwd	1-yr fwd	2-yr fwd
TWR.NZ	30/09/2022	Tower	0.63	237	10.6	8.2	8.7	0.7	0.7	8.4	8.8
IAG.AX	30/06/2023	Insurance Australia	4.80	12,800	29.5	14.8	2.7	1.7	1.6	14.6	14.7
SUN.AX	30/06/2023	Suncorp Group	10.29	14,089	17.2	11.0	5.7	1.0	0.9	9.9	9.5
QBE.AX	31/12/2022	QBE Insurance	11.76	19,109	15.4	9.6	2.6	1.1	1.1	15.1	15.9
HGH.NZ	30/06/2023	Heartland Group	1.68	1,145	10.4	10.2	9.2	1.1	1.0	11.7	11.2
<b>Peer Median</b>					<b>18.1</b>	<b>11.4</b>	<b>4.2</b>	<b>1.1</b>	<b>1.1</b>	<b>13.2</b>	<b>13.0</b>

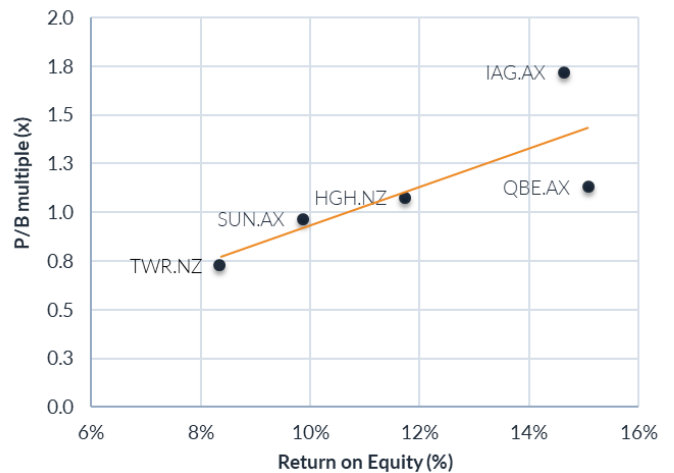
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

Figure 7. TWR relevant Australasian financials – P/E versus ROE one-year forward



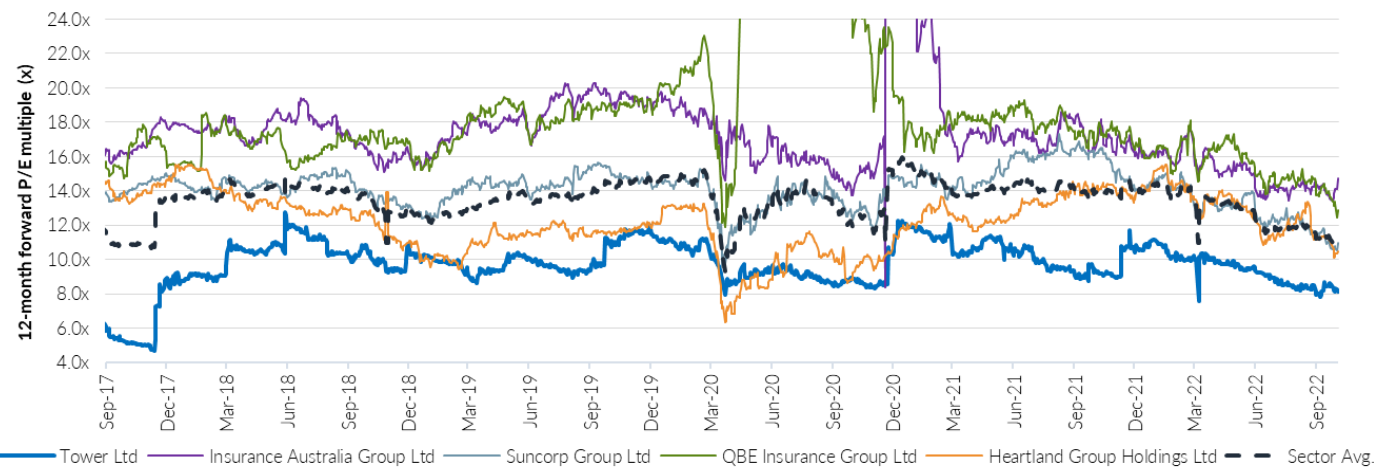
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

Figure 8. TWR relevant Australasian financials – Price to Book versus ROE one-year forward



Source: Refinitiv, Bloomberg, Forsyth Barr analysis

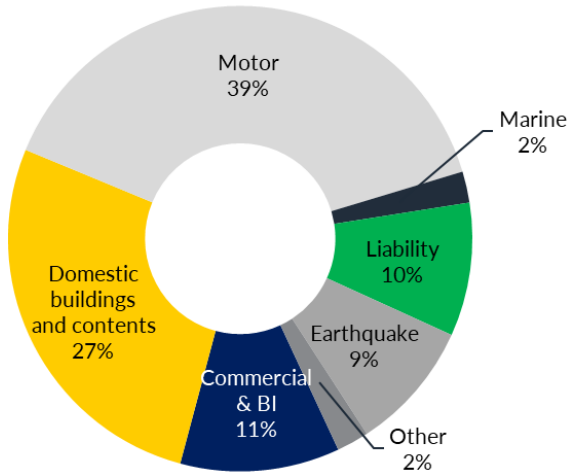
Figure 9. TWR relevant Australasian financials – 12-month forward P/E multiple (x)



Source: Refinitiv, Forsyth Barr analysis

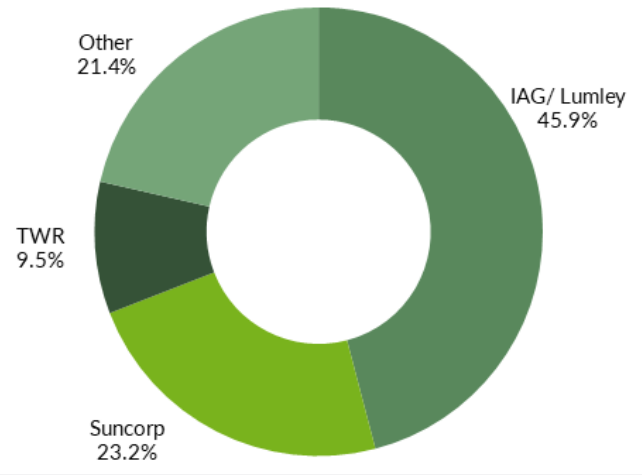
## Key New Zealand insurance industry charts

Figure 10. NZ insurance sector – Net Written Premiums (NWP) by insurance class



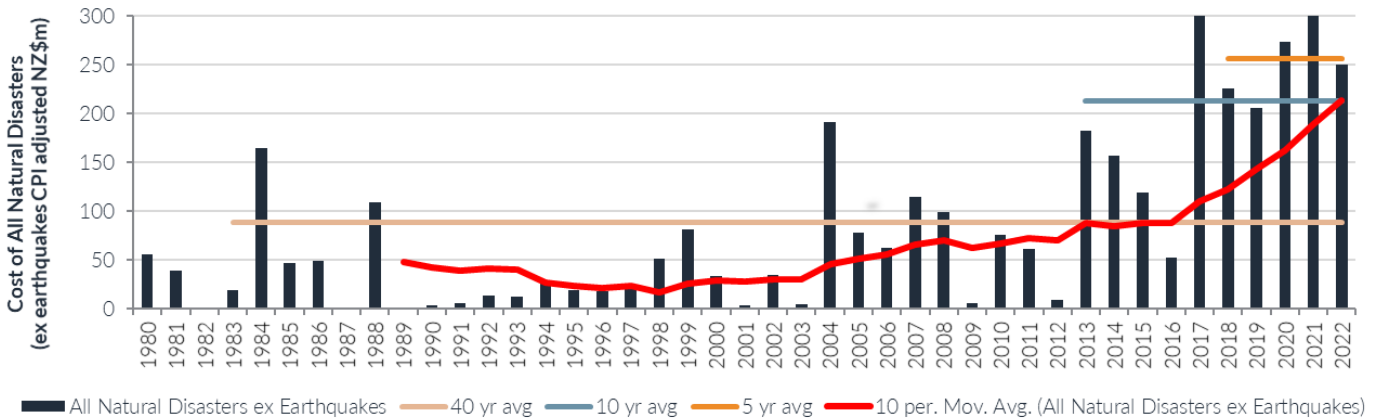
Source: ICANZ data for 2021

Figure 11. NZ Personal lines insurance market shares (30 September 2022 estimate)



Source: Company reports, Forsyth Barr analysis

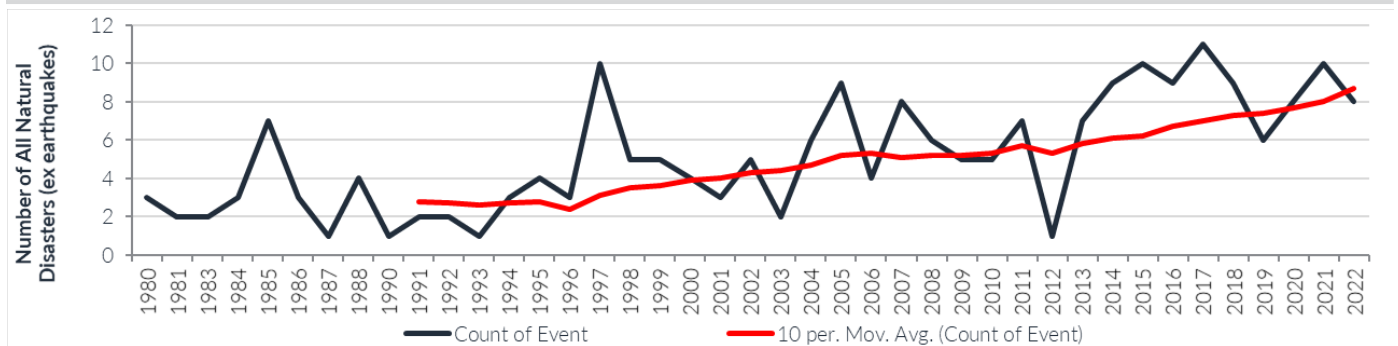
Figure 12. Cost of All Natural Disasters excluding Earthquakes in NZ (CPI inflated, NZ\$m)



Source: ICNZ, Forsyth Barr analysis

Figure 12, above, displays a trend of the increasing cost of natural disasters (excluding earthquakes) in New Zealand across all insurers, driven partly by climate change. Over the past 40 years the average cost in New Zealand of all-natural disasters, excluding earthquakes, has been NZ\$89m. More recently, the ten-year average industry cost is NZ\$213m per annum and the five-year average of NZ\$256m per annum. In Figure 13 below, the increasing frequency of events is displayed.

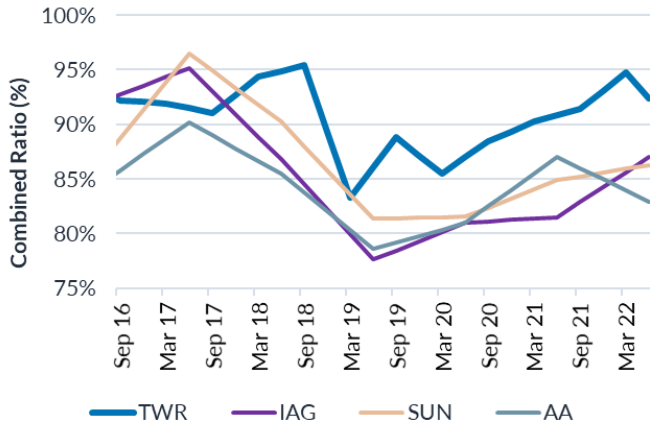
Figure 13. Frequency of all natural disasters including earthquakes in NZ



Source: ICNZ, Forsyth Barr analysis

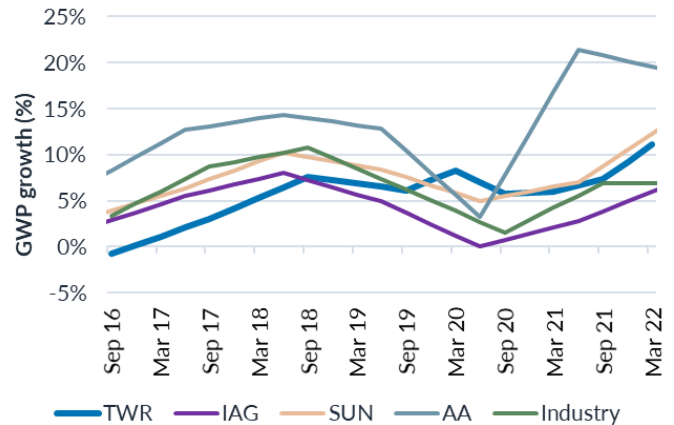


**Figure 14. Combined ratio across NZ's leading general insurers**



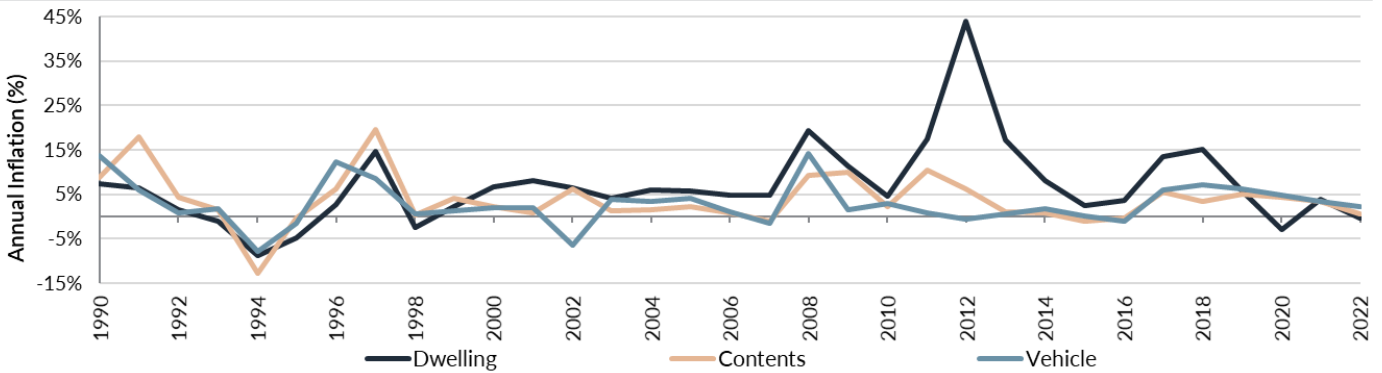
Source: Company reports, Forsyth Barr analysis

**Figure 15. GWP Growth across NZ's leading personal insurers**



Source: Company reports, Forsyth Barr analysis

**Figure 16. NZ General Insurance Market (CPI to June by category)**



Source: Stats NZ, Forsyth Barr analysis

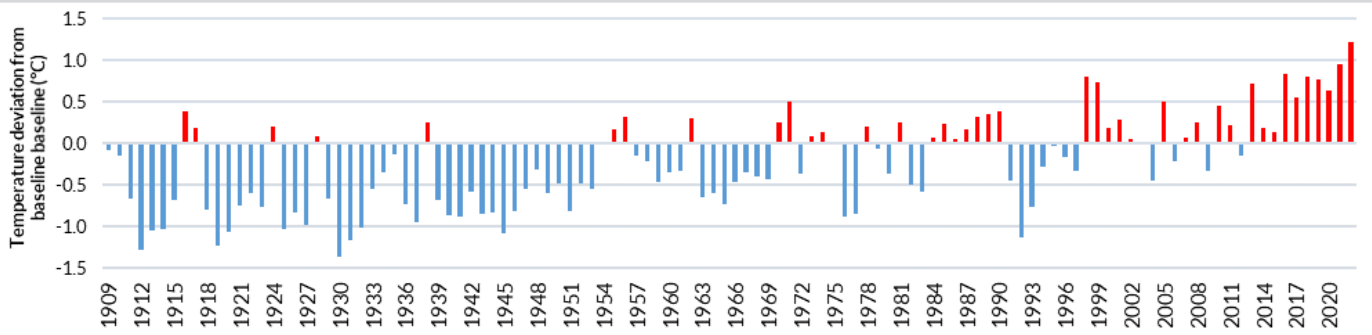
**Figure 17. Sector – Home & Contents customer ratings**

Rated brands	Overall Satisfaction*	Customer Service	Value for Money	Communication	Comprehensiveness of Cover	Cost
<b>FMG</b> Advice & Insurance	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>AA Insurance</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>N+1</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>STATE</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>TOWER</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>bnz</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>amj</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>Westpac</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>ASB</b> ONE STEP AHEAD	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>vero</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>AMP</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>ANZ</b>	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★

Source: Canstar

## Key environmental factor charts

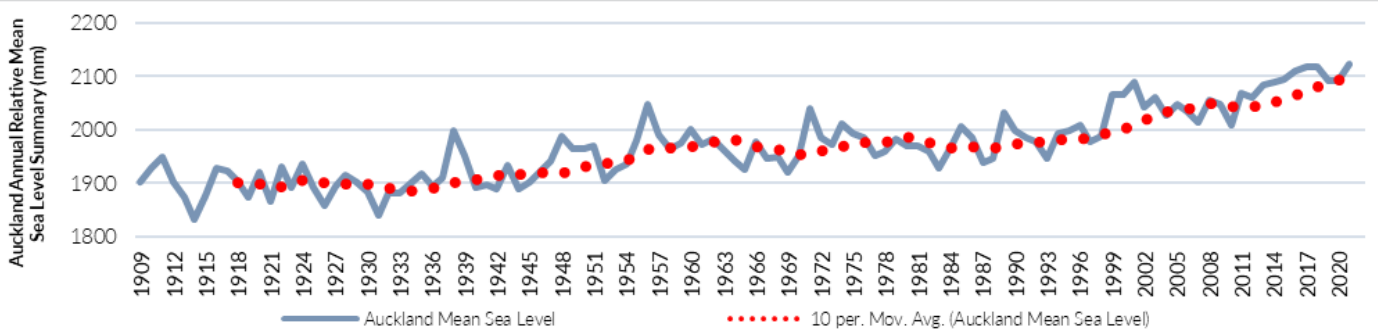
Figure 18. NZ's average annual air temperatures relative to baseline



Source: NIWA, series relative to the annual mean temperature between 1981–2010 of 12.61°C.

The absolute rise in temperature between the average of the first five years in the series above (1909 to 1914) and the last five years (2018 to 2022) is **+1.52°C**. Two-thirds of this increase occurred over the last 50 years.

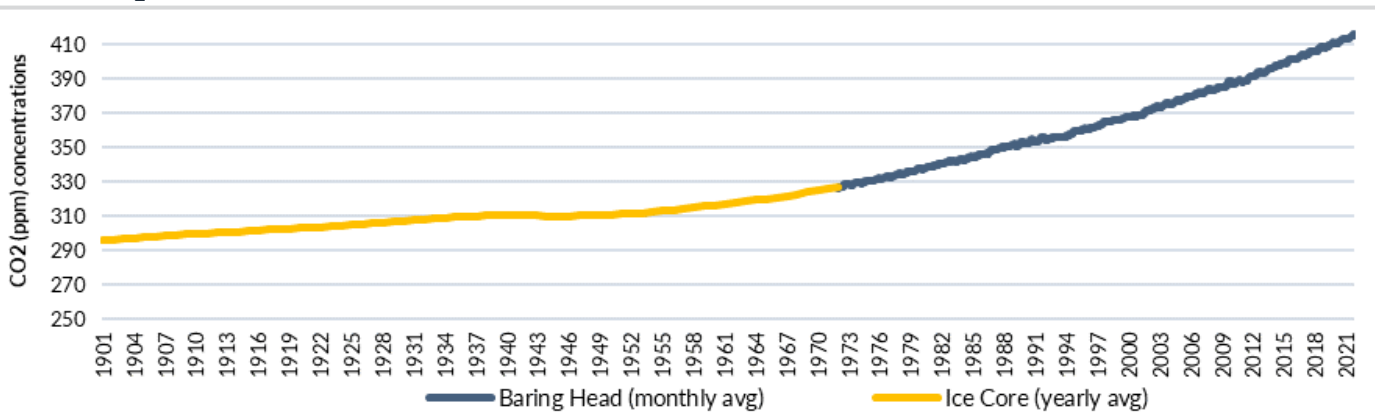
Figure 19. Mean Sea Level (MSL) in Auckland



Source: Paul Denys of Otago University "Sea Level Rise in New Zealand: The Effect of Vertical Land Motion on Century-Long Tide Gauge Records in a Tectonically Active Region", Ports of Auckland, University of Hawaii Sea Level Center and The Permanent Service for Mean Sea Level (PSMSL), Forsyth Barr analysis

The mean Relative Sea Level rise for Auckland between 1909 and 2021 is approximately **+2.0 mm/year**.

Figure 20. CO<sub>2</sub> concentrations at Baring Head and ice core data

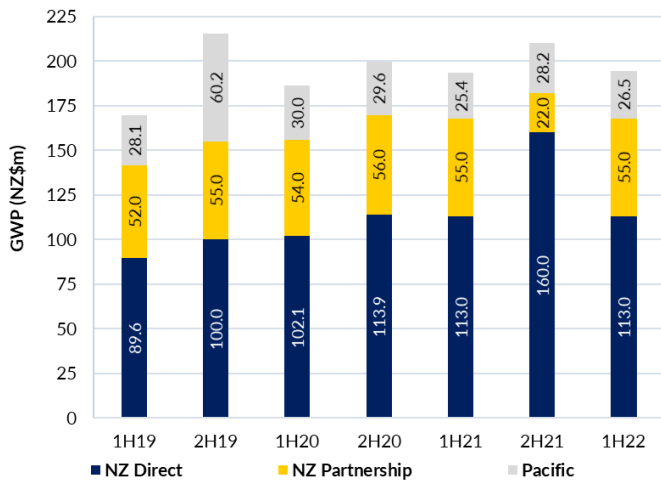


Source: CDIAC, NIWA, Forsyth Barr analysis

Atmospheric concentrations of carbon dioxide (CO<sub>2</sub>) influence how much energy Earth traps, providing a valuable indicator of climate change. It is the longest-running series of data scientists have, with measurements going back 800,000 years based on ice core samples. As a comparison, the pre-industrial level of CO<sub>2</sub> in the atmosphere was ~280 ppm, with measurements ranging between 180–300 ppm; over the last 800,000 years. More recently, CO<sub>2</sub> concentrations have been growing at +0.3% per annum since 1909 and at +0.5% per annum for the last 50 years. The Baring Head records, NIWA's clean air station near Wellington, are the longest-running recorded monthly data series in the Southern Hemisphere of CO<sub>2</sub>, with measurements starting in 1972. We have utilised yearly averages for Antarctica's ice core data and the monthly averaged measurements for the NZ data.

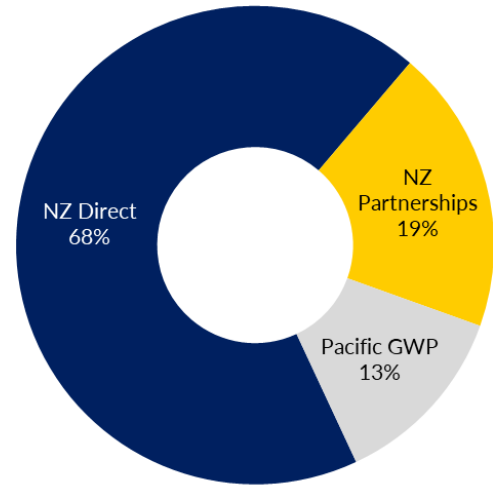
## Key TWR related charts

Figure 21. TWR – GWP by Division (half-on-half growth)



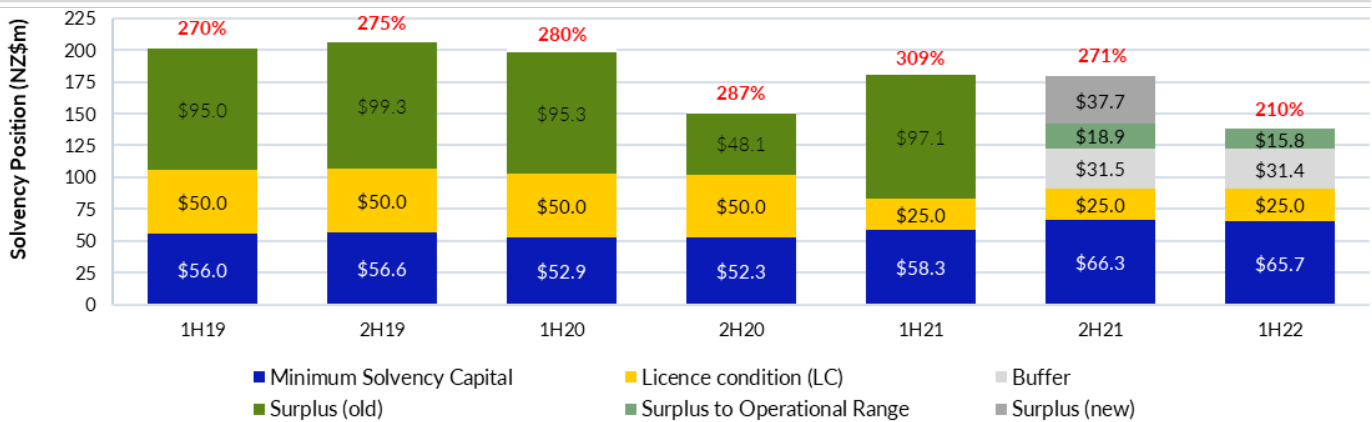
Source: Company data, Forsyth Barr analysis

Figure 22. TWR – GWP Segmental Split (FY22 estimate)



Source: Company data, Forsyth Barr analysis

Figure 23. TWR – Solvency Position



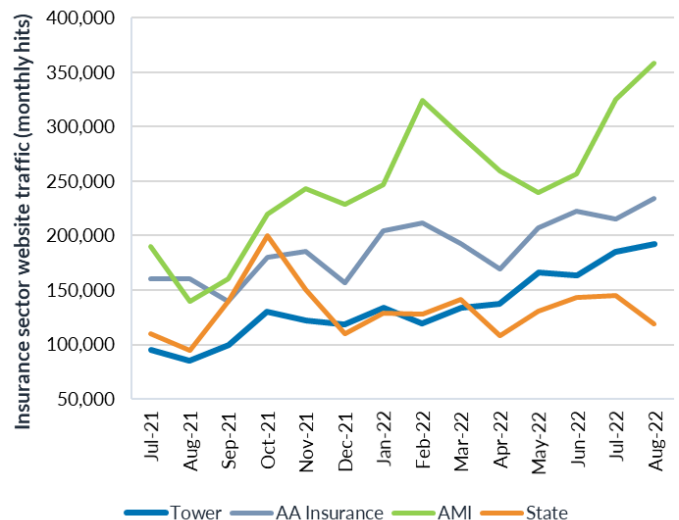
Source: Company data, Forsyth Barr analysis

Figure 24. TWR – Group MER Half-on-half (% of NEP)



Source: Company data, Forsyth Barr analysis

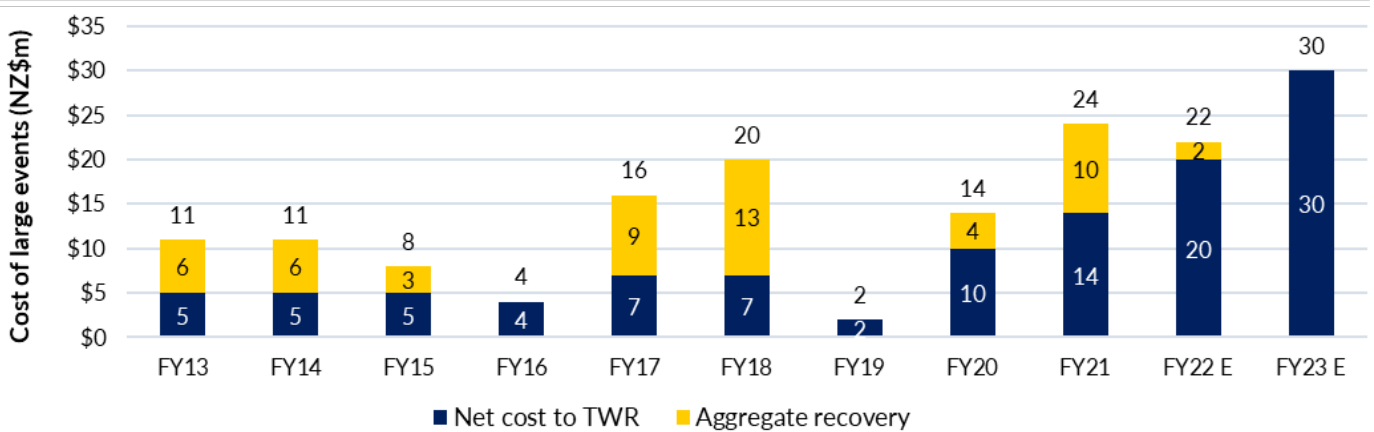
Figure 25. TWR – Website traffic of combative brands



Source: various online sources, Forsyth Barr analysis

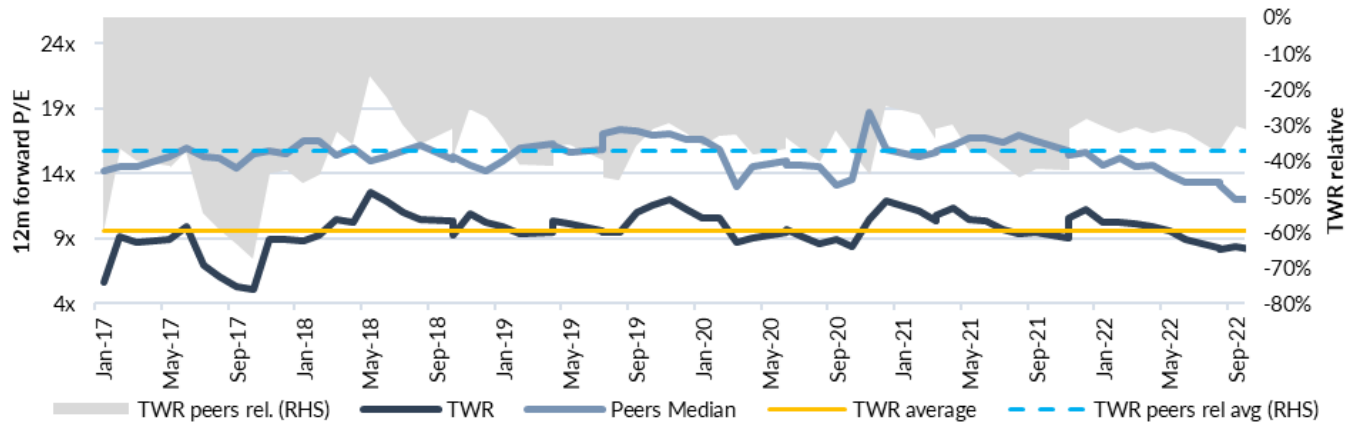


Figure 26. Ultimate estimated cost of large events (NZ\$m) – excluding reinsurance premium costs



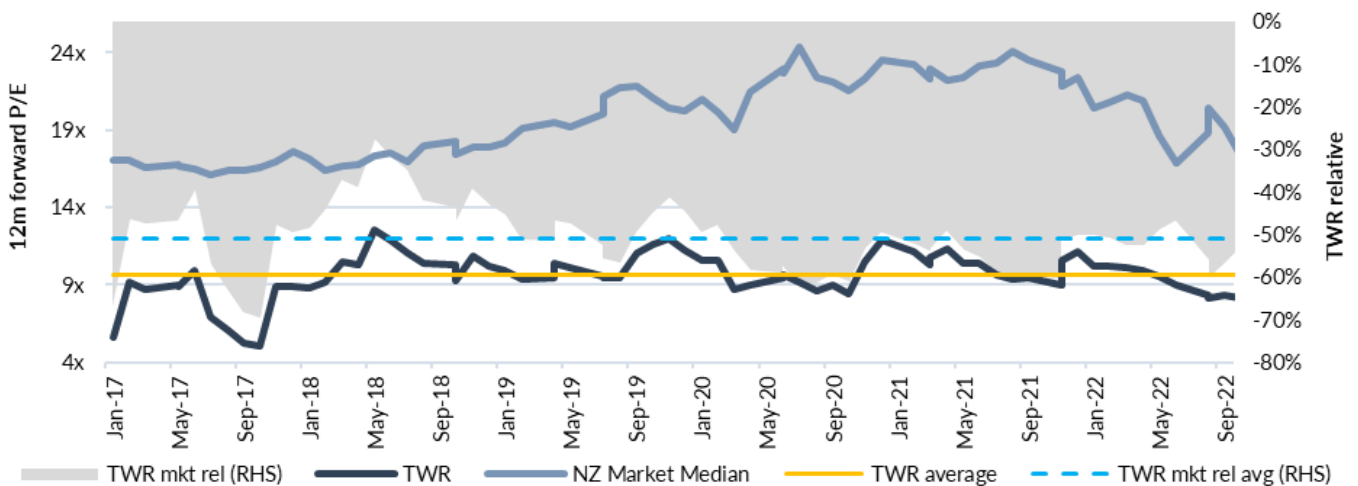
Source: Company data, Forsyth Barr analysis

Figure 27. TWR – Forward P/E against the peers market and history



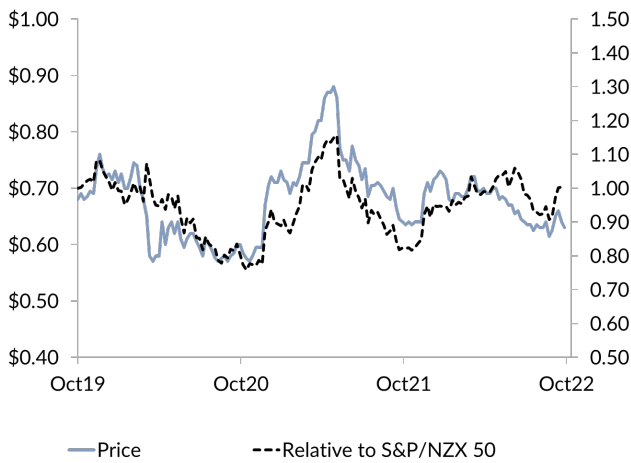
Source: Refinitiv, Forsyth Barr analysis

Figure 28. TWR – Forward P/E against the market and history



Source: Refinitiv, Forsyth Barr analysis

**Figure 29. Price performance**



Source: Forsyth Barr analysis

**Figure 30. Substantial shareholders**

Shareholder	Latest Holding
Bain Capital Credit LP	20.0%
ACC	9.6%
Salt Funds Management	7.0%
Investment Services Group	5.4%
NZ Funds Management	5.2%

Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

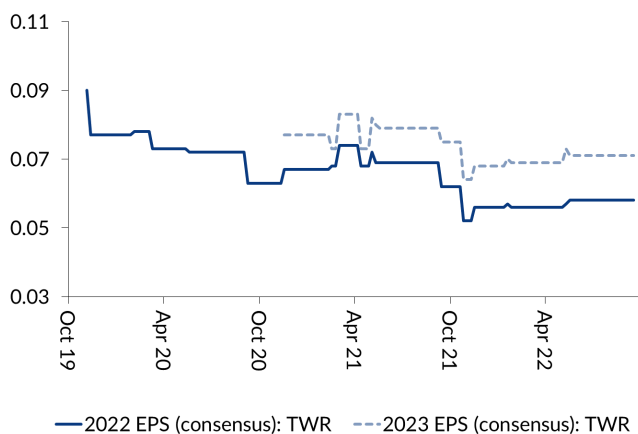
**Figure 31. International valuation comparisons**

Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2023E
				2022E	2023E	2022E	2023E	2022E	2023E	
Tower Ltd	TWR NZ	NZ\$0.63	NZ\$239	10.6x	8.2x	n/a	n/a	n/a	n/a	9.5%
Heartland Group Holdings *	HGH NZ	NZ\$1.68	NZ\$1,185	10.4x	10.2x	n/a	n/a	n/a	n/a	7.2%
Insurance Australia Group	IAG AT	A\$4.83	A\$11,906	29.5x	14.8x	n/a	n/a	n/a	10.4x	5.3%
Suncorp Group	SUN AT	A\$10.32	A\$13,045	17.2x	11.0x	n/a	n/a	n/a	47.5x	7.0%
QBE INSURANCE GROUP	QBE AT	US\$7.64	US\$11,340	15.4x	9.6x	n/a	n/a	n/a	8.1x	5.8%
<b>Compco Average:</b>				<b>18.1x</b>	<b>11.4x</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>22.0x</b>	<b>6.3%</b>
<b>TWR Relative:</b>				<b>-41%</b>	<b>-29%</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>50%</b>

EV = Mkt cap+net debt+lease liabilities+min interests-investments

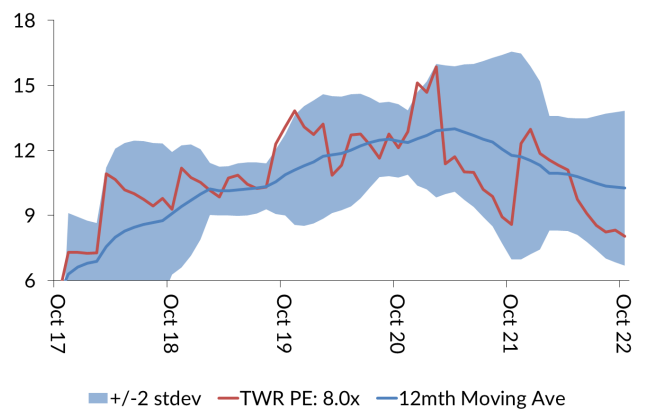
Source: \*Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (TWR) companies fiscal year end

**Figure 32. Consensus EPS momentum (NZ\$)**



Source: Forsyth Barr analysis

**Figure 33. One year forward PE (x)**



Source: Forsyth Barr analysis

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