

# Tower Limited

## New Zealand General Insurance Digest

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The NZ 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 2.

### Insurance industry news and weather event update

- Conditions in the insurance market continue to stabilise. Despite NZ's rate of CPI for the September quarter hitting +7.2%, Stats NZ showed insurance inflation year-to-date for dwelling was +0.2%, contents +2.1% and vehicle +2.8%.
- MetService said 2022 saw an average number of severe weather events, but rainfall and temperatures broke records. November was the warmest on record, with the top three warmest Novembers on record all occurring since 2019.
- A cyber-attack at MAS, NZ's largest insurer of medical professionals, in December 2022 has highlighted data risks.
- Tower acquired Kiwibank's insurance portfolio in October 2022 for NZ\$5.9m.
- XRB and Chapter Zero's new NZ Climate-related Disclosures standards came into effect from 1 January 2023.
- In late November 2022, the RBNZ raised the Official Cash Rate (OCR) from 3.5% to 4.25%.
- The RBNZ is seeking feedback on insurance governance and supervisory processes before 21 February 2023.
- TWR reported its FY22 results, with GWP growing +13% over the year and reported NPAT of NZ\$18.9m relative to NZ\$19.3m in FY21. Christchurch earthquake costs and one-off policy remediation provisions impacted the result. At the underlying NPAT level, NPAT was up +31% to NZ\$27.3m from NZ\$20.8m in FY21.
- At the beginning of Q4 2022, mergers and acquisitions globally in the insurance industry were estimated to have decreased by -37%, according to insurance consultant Gallagher in its "Global M&A Insurance 2022 Review and 2023 Outlook" review.
- IAG said in early January 2023 that its reinsurance expenses for FY23 would range from A\$790m to A\$820m, up +20% to +25% as compared to FY22, resulting from extreme weather events in Australia, the United States and Europe. Despite the cost increases, cover was reduced materially.
- SUN, in its 10 November 2022 Investor Update, forecast that industry GWP growth out to 2030 in NZ would be +2.8% p.a. for motor and +3.9% p.a. for consumer home insurance.
- On 21 November 2022, in its Performance Update, QBE commented on the favourable rate environment but noted "higher than expected catastrophe costs".

### Stock Performances

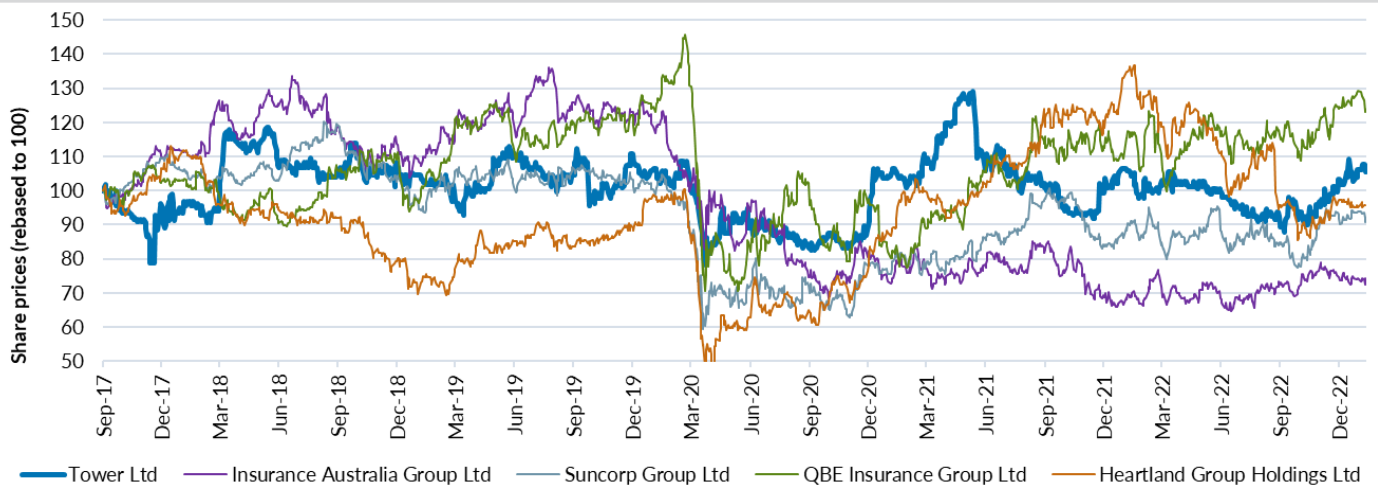
The listed Australasian insurance sector and TWR's financial peers have recently produced a wide range of performances. Over the last three months TWR (+14.3%) has been the top performer, closely followed by SUN (+12.9%), with IAG (+0.6%) producing the worst. Over twelve months, the performers were: IAG (+8.2%), QBE (+7.1%), SUN (+0.9%), TWR (+0.4%), and HGH (-29.8%).

**Tower Limited (TWR)**

<b>Market data (NZ\$)</b>						<b>Spot valuation (NZ\$)</b>					
Priced as at 11 Jan 2023					0.72	Total firm value					389
52 week high / low					0.75 / 0.60	PE relative					0.82
Market capitalisation (NZ\$m)					273.2	P/Book relative					0.79
<b>Key WACC assumptions</b>						<b>DCF valuation summary (NZ\$m)</b>					
Risk free rate					4.50%	(Net debt)/cash					2
Equity beta					1.10	Less: Capitalised operating leases					(52)
WACC					10.1%	Value of equity					339
Terminal growth					1.8%						
<b>Profit and Loss Account (NZ\$m)</b>						<b>Valuation Ratios</b>					
	2021A	2022A	2023E	2024E	2025E		2021A	2022A	2023E	2024E	2025E
Sales revenue (GEP)	395.5	418.3	472.5	520.7	556.6	EV/EBITDA (x)	n/a	n/a	n/a	n/a	n/a
<b>Normalised EBITDA</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	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)	16.2	16.2	9.1	7.7	7.3
<b>Normalised EBIT</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	Price/NTA (x)	1.3	1.6	2.1	2.4	2.6
Net interest	n/a	n/a	n/a	n/a	n/a	Free cash flow yield (%)	36.5	3.1	14.9	16.7	17.6
Associate income	0	0	0	0	0	Net dividend yield (%)	6.9	9.0	9.0	9.7	10.4
Tax	(9.1)	(7.5)	(13.8)	(16.2)	(17.3)	Gross dividend yield (%)	6.9	9.0	9.0	9.7	12.4
Minority interests	0.6	0.1	0	0	0	<b>Key Ratios</b>					
<b>Normalised NPAT</b>	<b>18.7</b>	<b>17.7</b>	<b>29.9</b>	<b>35.3</b>	<b>37.6</b>	Return on assets (%)	n/a	n/a	n/a	n/a	n/a
Abnormals/other	0	0	0	0	0	Return on equity (%)	5.4	5.8	11.4	14.1	15.5
<b>Reported NPAT</b>	<b>18.7</b>	<b>17.7</b>	<b>29.9</b>	<b>35.3</b>	<b>37.6</b>	Return on funds employed (%)	0.0	0.0	0.0	0.0	0.0
Normalised EPS (cps)	4.4	4.4	7.9	9.3	9.9	EBITDA margin (%)	n/a	n/a	n/a	n/a	n/a
DPS (cps)	5.0	6.5	6.5	7.0	7.5	EBIT margin (%)	n/a	n/a	n/a	n/a	n/a
<b>Growth Rates</b>						<b>Capital Structure</b>					
	2021A	2022A	2023E	2024E	2025E		2021A	2022A	2023E	2024E	2025E
Revenue (%)	6.2	5.8	13.0	10.2	6.9	Solvency capital	155.9	150.5	179.4	136.4	167.7
EBITDA (%)	n/a	n/a	n/a	n/a	n/a	Minimum solvency capital (MSC)	56.6	52.3	66.3	66.5	73.6
EBIT (%)	n/a	n/a	n/a	n/a	n/a	Total regulatory capital	106.6	102.3	83.3	91.3	91.3
Normalised NPAT (%)	57.1	-5.4	69.3	17.9	6.6	Solvency ratio (%)	275	287	271	205	228
Normalised EPS (%)	55.4	0.2	77.6	17.9	6.6	<b>Operating Performance</b>					
Ordinary DPS (%)	n/a	30.0	0.0	7.7	7.1		2021A	2022A	2023E	2024E	2025E
<b>Cash Flow (NZ\$m)</b>						Gross written premium	404.7	445.6	499.5	541.9	571.3
	2021A	2022A	2023E	2024E	2025E	<b>Gross earned premium</b>	<b>395.5</b>	<b>418.3</b>	<b>472.5</b>	<b>520.7</b>	<b>556.6</b>
<b>EBITDA</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	Reinsurance premium	(62.2)	(66.3)	(68.8)	(75.4)	(80.5)
Working capital change	n/a	n/a	n/a	n/a	n/a	<b>Net earned premium</b>	<b>333.3</b>	<b>352.1</b>	<b>403.7</b>	<b>445.3</b>	<b>476.1</b>
Interest & tax paid	0	0	0	0	0	Net claims expense	(204.3)	(224.9)	(257.9)	(285.6)	(306.4)
Other	0	0	0	0	0	* includes Large event claims of	(13.9)	(19.0)	(30.0)	(31.0)	(32.0)
<b>Operating cash flow</b>	<b>99.7</b>	<b>8.6</b>	<b>40.6</b>	<b>45.6</b>	<b>48.1</b>	Management & sales expenses	(123.3)	(129.9)	(142.9)	(152.1)	(158.5)
Capital expenditure	(12.0)	(17.3)	(13.9)	(15.1)	(15.9)	<b>Underwriting profit</b>	<b>28.0</b>	<b>23.6</b>	<b>32.3</b>	<b>37.0</b>	<b>40.7</b>
(Acquisitions)/divestments	(14.4)	(6.1)	4.1	0	0	Investment and other revenue	0.2	1.2	12.3	15.4	15.1
Other	(24.5)	(13.3)	(6.8)	(7.4)	(7.7)	Financing and other costs	(0.4)	(0.9)	(0.9)	(0.9)	(0.9)
<b>Funding available/(required)</b>	<b>48.7</b>	<b>(28.2)</b>	<b>24.0</b>	<b>23.1</b>	<b>24.4</b>	<b>Profit before tax</b>	<b>28.5</b>	<b>25.2</b>	<b>43.7</b>	<b>51.5</b>	<b>54.9</b>
Dividends paid	(10.5)	(20.0)	(24.7)	(26.6)	(28.5)	Tax expense	(9.1)	(7.5)	(13.8)	(16.2)	(17.3)
Equity raised/(returned)	0	(30.6)	0	0	0	<b>Profit after taxation (Reported)</b>	<b>19.3</b>	<b>17.7</b>	<b>29.9</b>	<b>35.3</b>	<b>37.6</b>
<b>(Increase)/decrease in net debt</b>	<b>38.2</b>	<b>(78.8)</b>	<b>(0.7)</b>	<b>(3.4)</b>	<b>(4.1)</b>	Abnormals	(1.1)	0	0	0	0
<b>Balance Sheet (NZ\$m)</b>						<b>Comprehensive profit</b>	<b>18.2</b>	<b>17.7</b>	<b>29.9</b>	<b>35.3</b>	<b>37.6</b>
	2021A	2022A	2023E	2024E	2025E	<b>Key ratios</b>					
Working capital	146.9	183.2	171.7	186.3	196.4	Tower Direct GWP growth %	26.4%	17.2%	11.2%	9.0%	5.0%
Fixed assets	9.4	5.4	6.9	8.3	9.5	Partnership GWP growth %	-30.0%	13.0%	14.0%	8.0%	7.0%
Intangibles	120.6	132.5	131.2	135.4	139.0	Total GWP growth %	7.3%	10.1%	12.1%	8.5%	5.4%
Right of use asset	25.6	23.3	20.6	17.9	15.2	Total claims ratio %	54.3%	54.1%	56.6%	57.5%	58.2%
Other assets	313.0	295.6	295.6	295.6	295.6	MER %	37.1%	36.0%	35.4%	34.2%	33.3%
<b>Total funds employed</b>	<b>615.5</b>	<b>640.0</b>	<b>626.0</b>	<b>643.5</b>	<b>655.7</b>	Combined ratio %	91.4%	90.1%	92.0%	91.7%	91.5%
Net debt/(cash)	(116.1)	(84.5)	(83.8)	(80.4)	(76.3)						
Lease liability	39.4	35.1	28.3	20.9	13.2						
Other liabilities	342.5	383.5	419.4	453.2	476.6						
Shareholder's funds	347.0	306.0	262.1	249.6	242.2						
Minority interests	2.7	0	0	0	0						
<b>Total funding sources</b>	<b>615.5</b>	<b>640.0</b>	<b>626.0</b>	<b>643.5</b>	<b>655.7</b>						

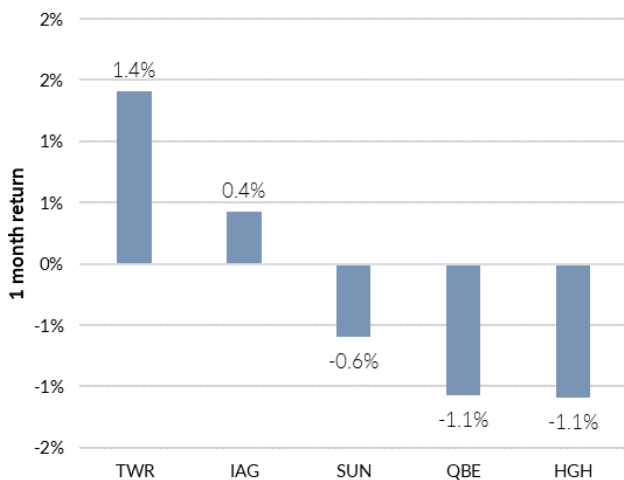
## Sector performance (of relevant peers)

Figure 1. Sector performance of relevant comparables (rebased to one since September 2017)



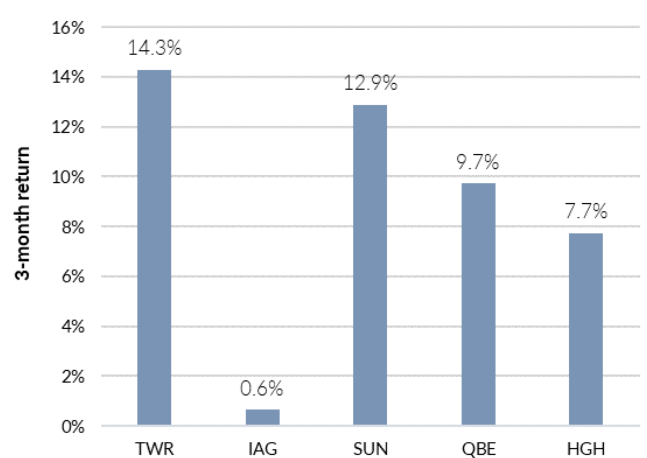
Source: Forsyth Barr analysis

Figure 2. Peer group returns over one month



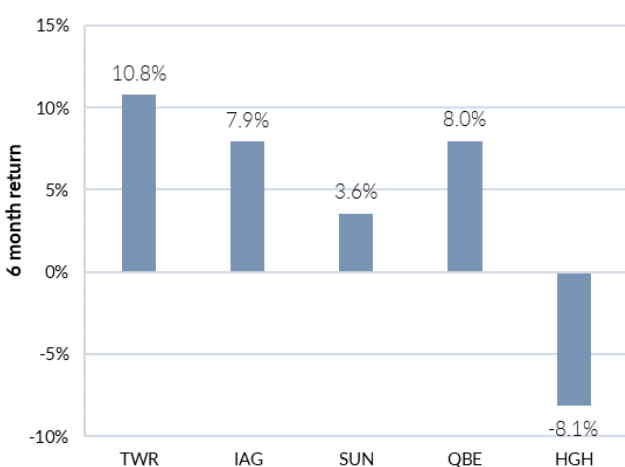
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

Figure 3. Peer group returns over three months



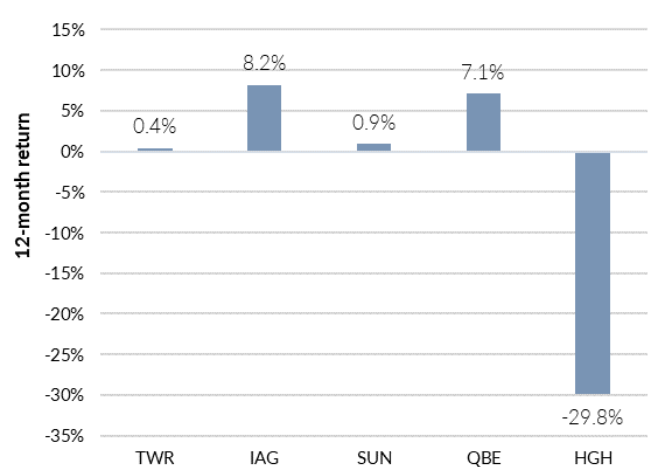
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

Figure 4. Peer group returns over six months



Source: Refinitiv, Bloomberg, Forsyth Barr analysis

Figure 5. Peer group returns over 12 months



Source: Refinitiv, Bloomberg, Forsyth Barr analysis

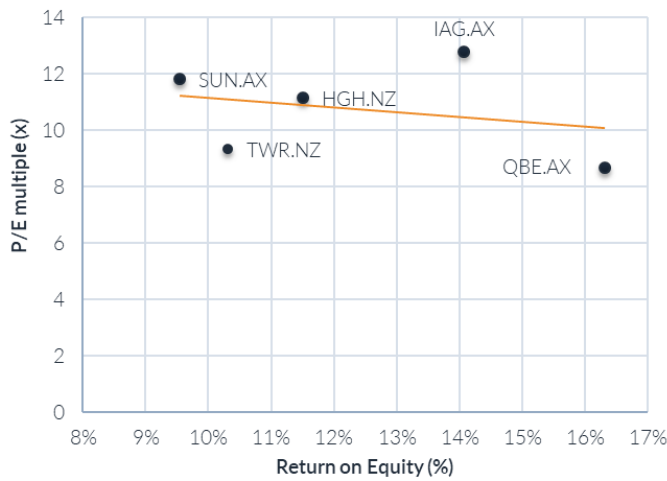
## Sector ratios (of relevant peers)

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 gross	1-yr fwd	2-yr fwd	1-yr fwd	2-yr fwd
TWR.NZ	30/09/2022	Tower	0.72	279	9.3	8.8	8.8	0.9	0.9	10.3	11.1
IAG.AX	30/06/2023	Insurance Australia	4.76	12,303	12.8	12.2	2.7	1.6	1.6	14.1	13.8
SUN.AX	30/06/2023	Suncorp Group	11.65	16,205	11.8	11.7	4.8	1.1	1.1	9.5	9.3
QBE.AX	31/12/2022	QBE Insurance	12.87	20,492	8.7	8.4	2.3	1.4	1.3	16.3	15.8
HGH.NZ	30/06/2023	Heartland Group	1.81	1,276	11.1	10.4	8.4	1.2	1.1	11.5	11.3
<b>Peer Median</b>					<b>11.8</b>	<b>11.0</b>	<b>3.8</b>	<b>1.3</b>	<b>1.2</b>	<b>12.8</b>	<b>12.6</b>

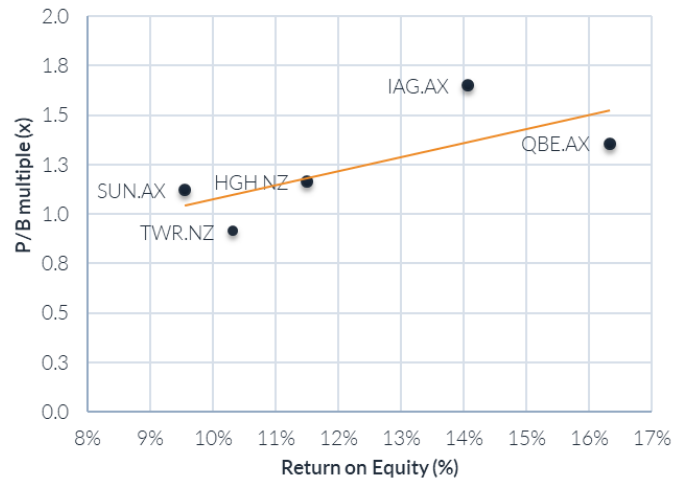
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

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



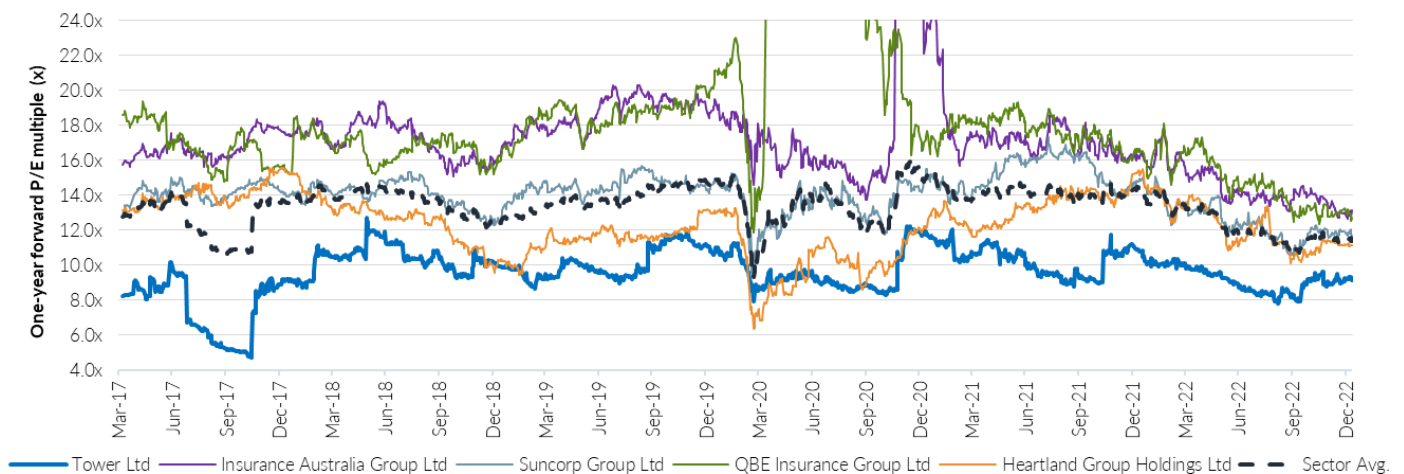
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

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



Source: Refinitiv, Bloomberg, Forsyth Barr analysis

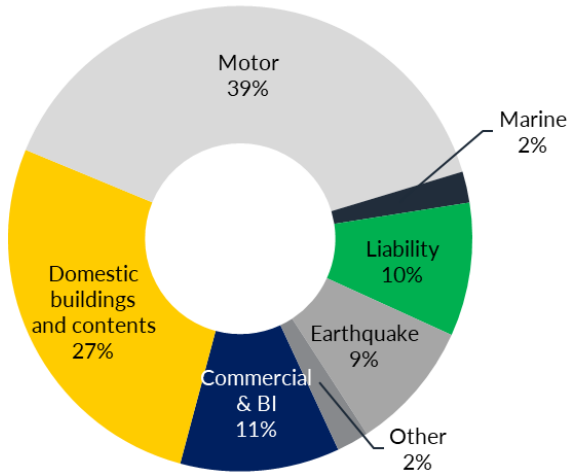
Figure 9. TWR relevant Australasian financials – one-year forward P/E multiple (x)



Source: Refinitiv, Forsyth Barr analysis

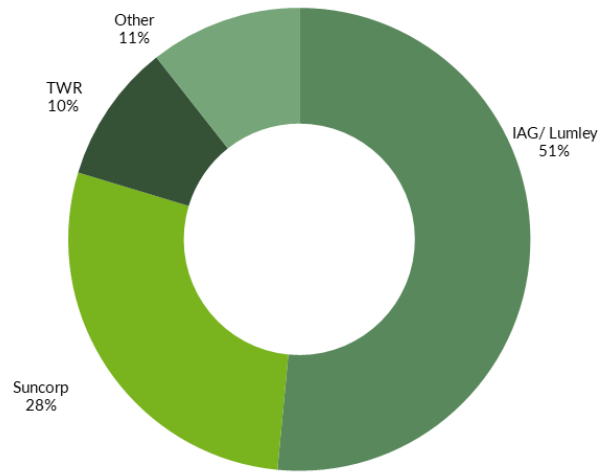
## Key New Zealand insurance industry charts

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



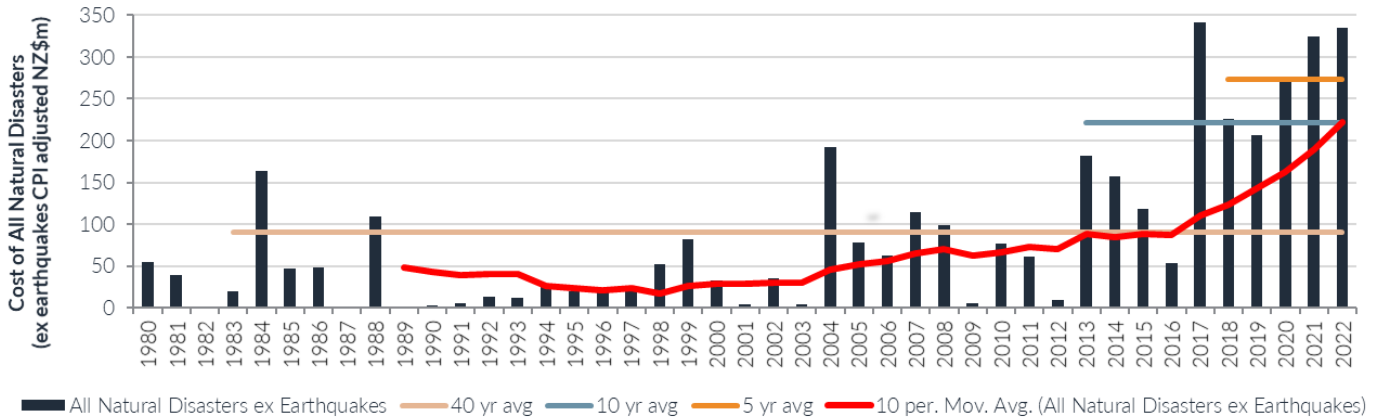
Source: ICANZ data for 2021

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



Source: Company reports, Forsyth Barr analysis

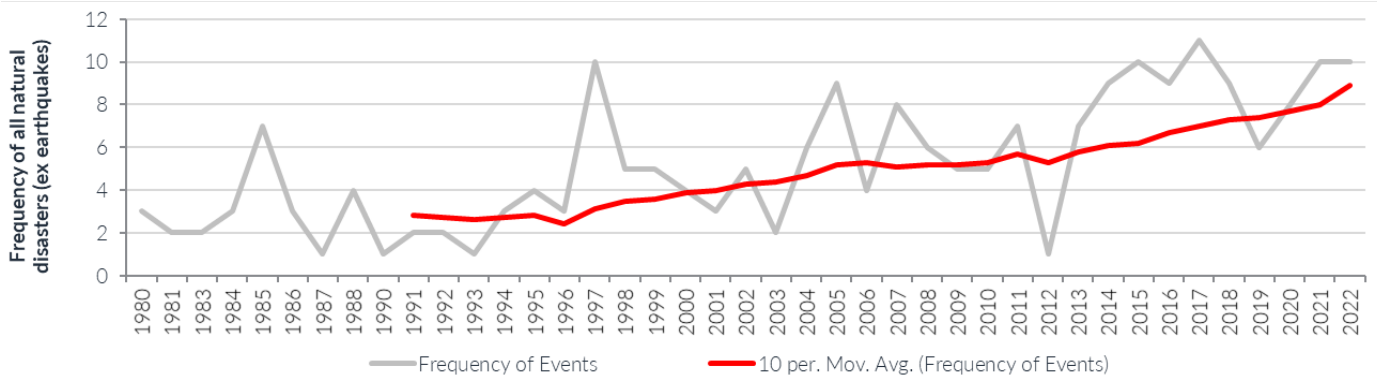
**Figure 12. Cost of All Natural Disasters excluding Earthquakes in NZ (CPI inflated, NZ\$m)**



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\$91m. More recently, the ten-year average industry cost is NZ\$222m per annum and the five-year average is NZ\$273m per annum. In Figure 13 below, the increasing frequency of events is displayed.

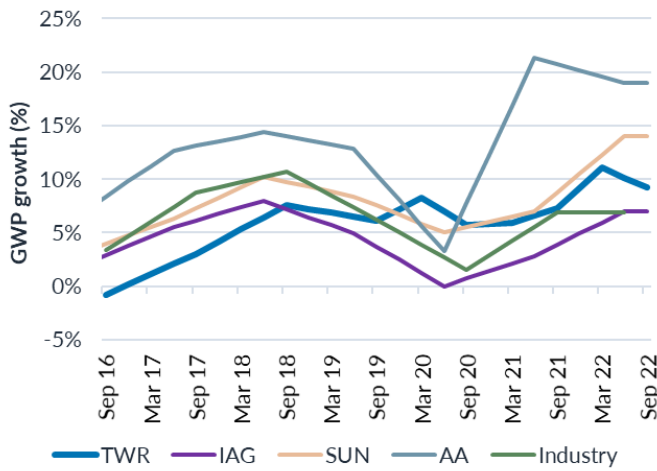
**Figure 13. Frequency of all natural disasters including earthquakes in NZ**



Source: ICNZ, Forsyth Barr analysis

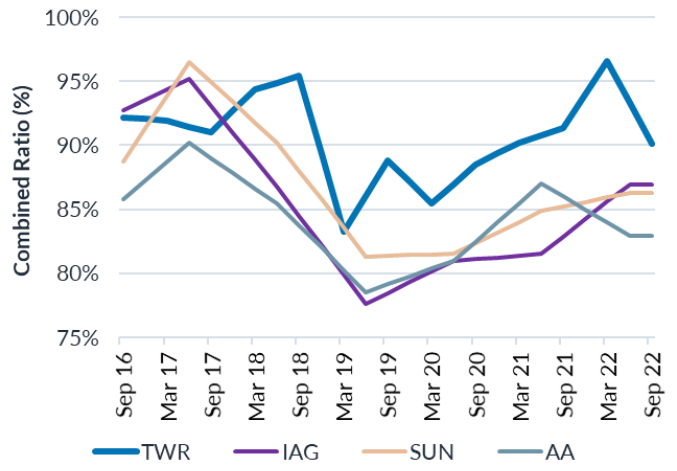


**Figure 14. GWP growth across NZ's leading personal insurers**



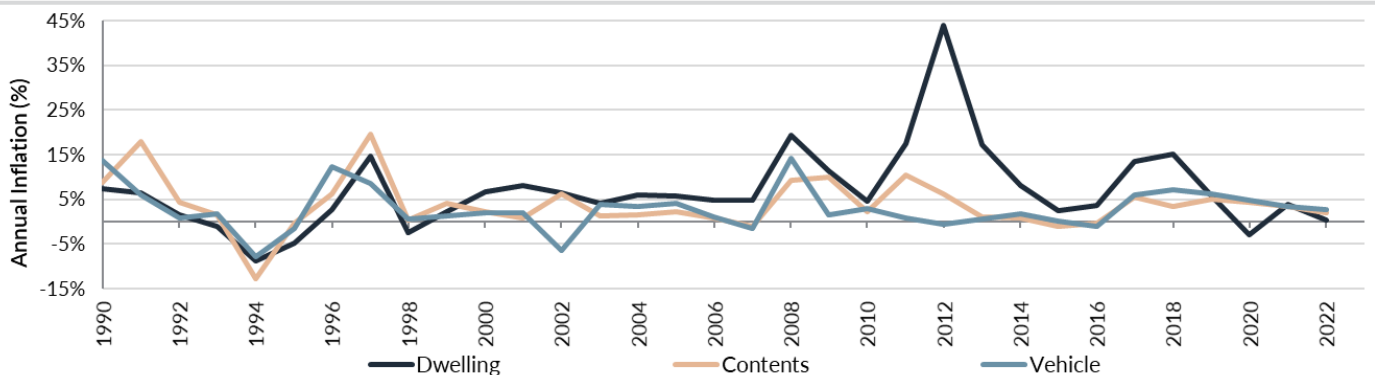
Source: Company reports, Forsyth Barr analysis

**Figure 15. Combined ratio across NZ's leading general insurers**



Source: Company reports, Forsyth Barr analysis

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



Source: Stats NZ, Forsyth Barr analysis

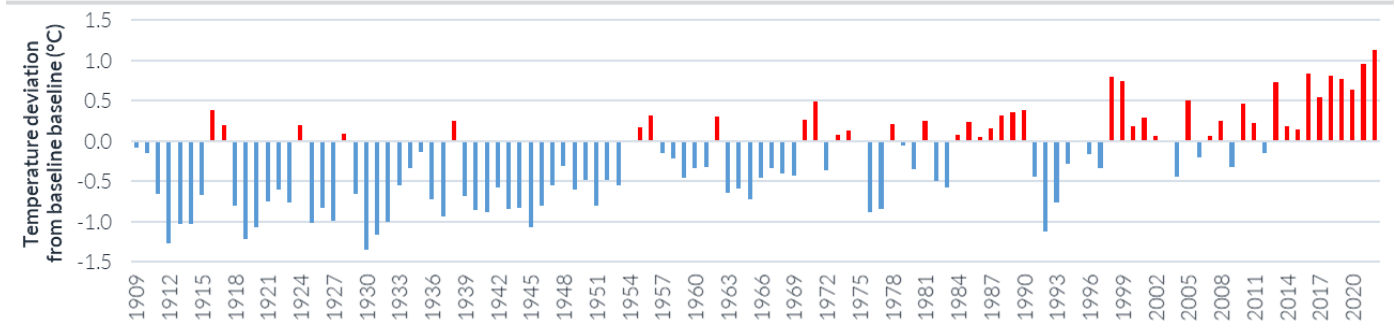
**Figure 17. Sector – Home & Contents customer ratings**

Rated brands	Overall Satisfaction*	Customer Service	Value for Money	Communication	Comprehensiveness of Cover	Cost
<b>FMG</b> Advice & Insurance	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<b>AA</b> Insurance	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★	★★★★★
<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

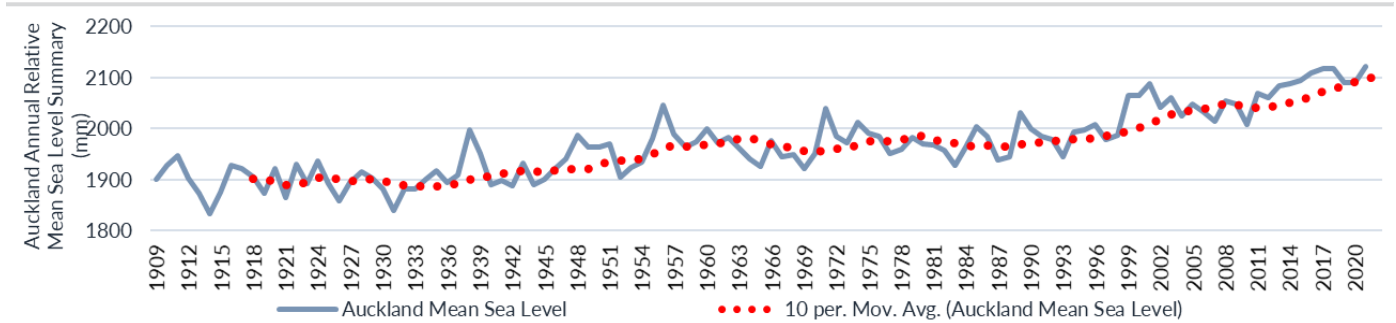
**Figure 18. NZ's average annual air temperatures relative to baseline**



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 **+1.50°C**. Two-thirds of this increase occurred over the last 50 years.

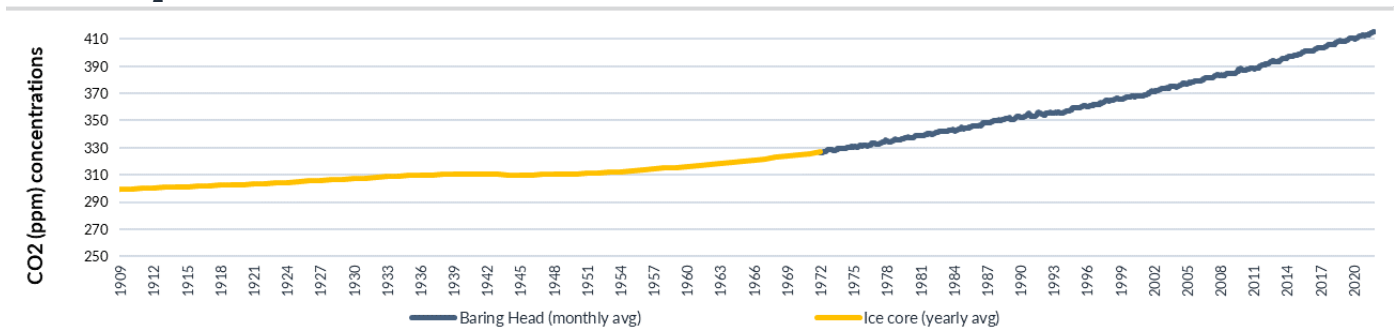
**Figure 19. Mean Sea Level (MSL) in Auckland**



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**

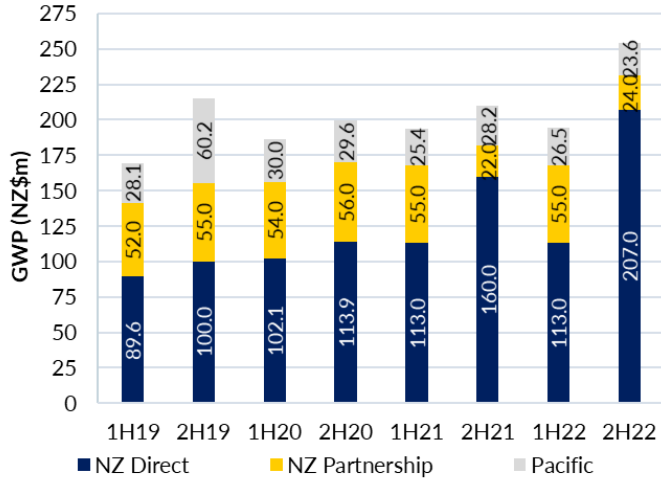


Source: CDIAC, NIWA, Forsyth Barr analysis

Atmospheric concentrations of carbon dioxide (CO<sub>2</sub>) influence how much energy the Earth traps, providing a valuable indicator of climate change. It is the longest-running series of data scientists have, with measurements dating 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 ~280ppm, with measurements ranging between 180–300ppm 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 for CO<sub>2</sub>, with measurements starting in 1972. We have utilised yearly averages for Antarctica's ice core data and the monthly average measurements for the NZ data.

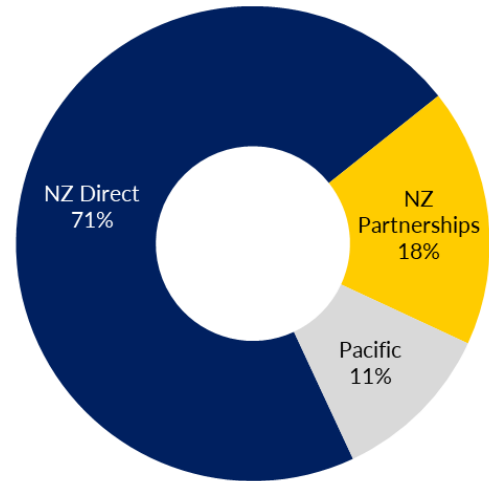
## Key TWR related charts

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



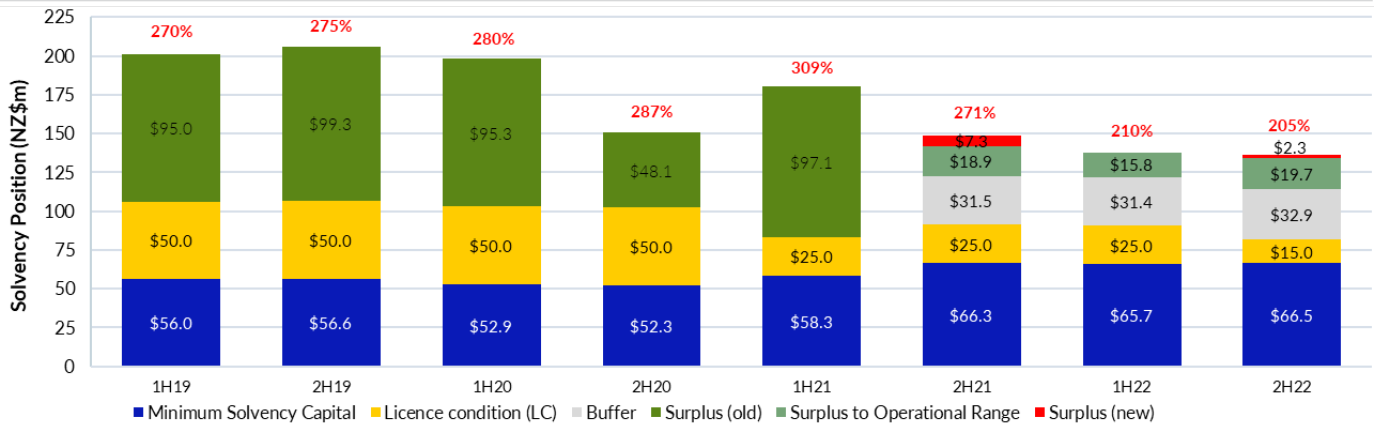
Source: Company data, Forsyth Barr analysis

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



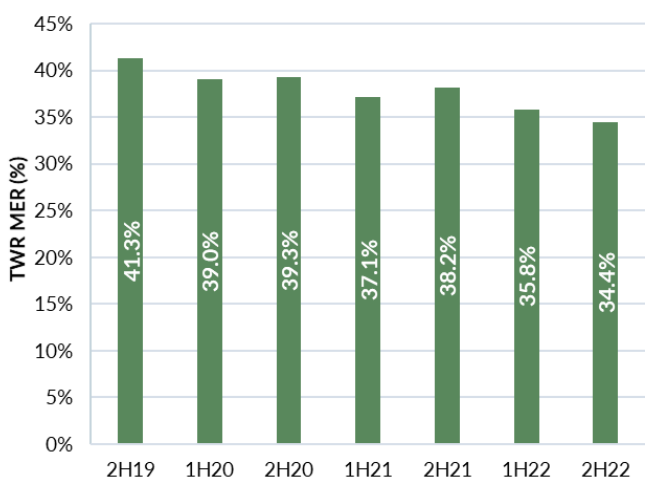
Source: Company data, Forsyth Barr analysis

Figure 23. TWR – Solvency Position



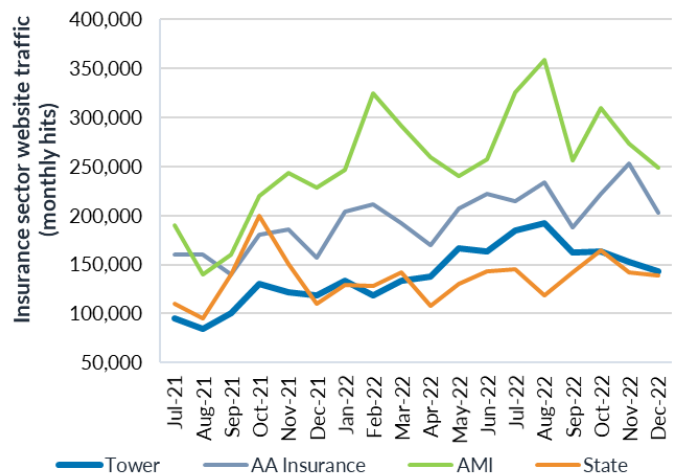
Source: Company data, Forsyth Barr analysis

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



Source: Company data, Forsyth Barr analysis

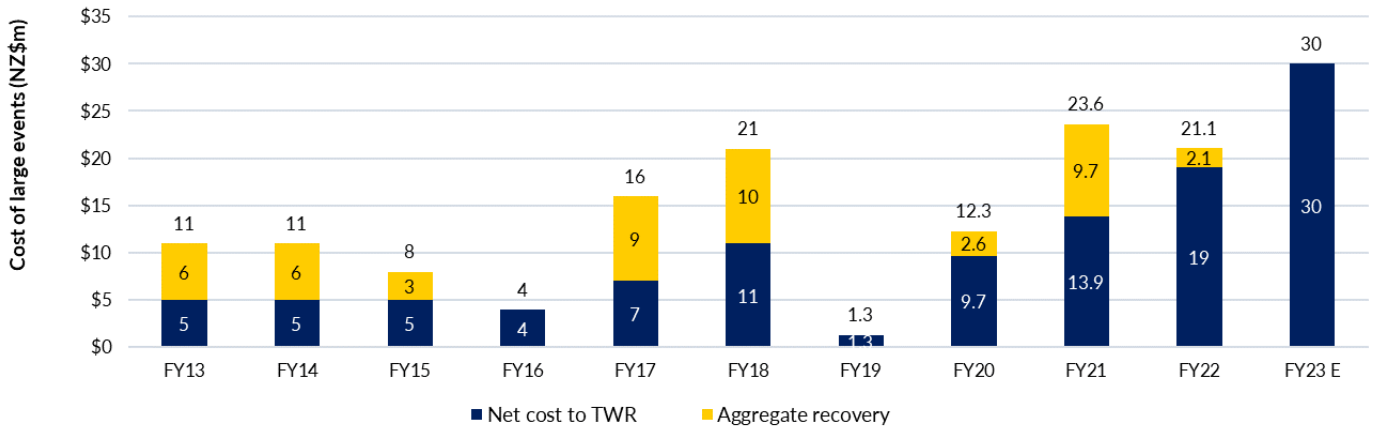
Figure 25. TWR – Website traffic of combative brands



Source: various online sources, Forsyth Barr analysis

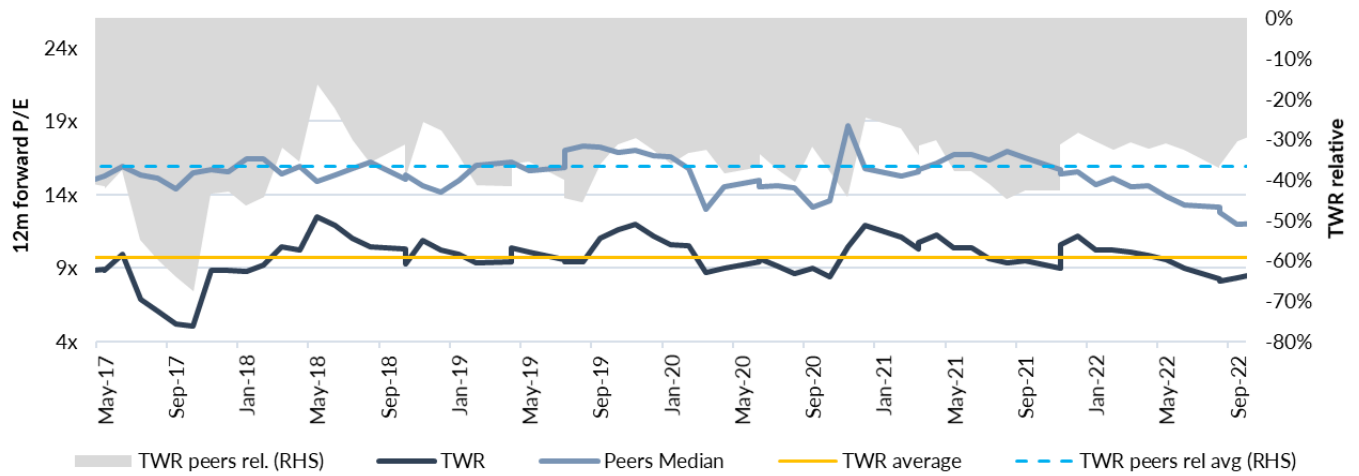


Figure 26. Ultimate estimated cost of large events (NZ\$m) – excluding reinsurance premium costs



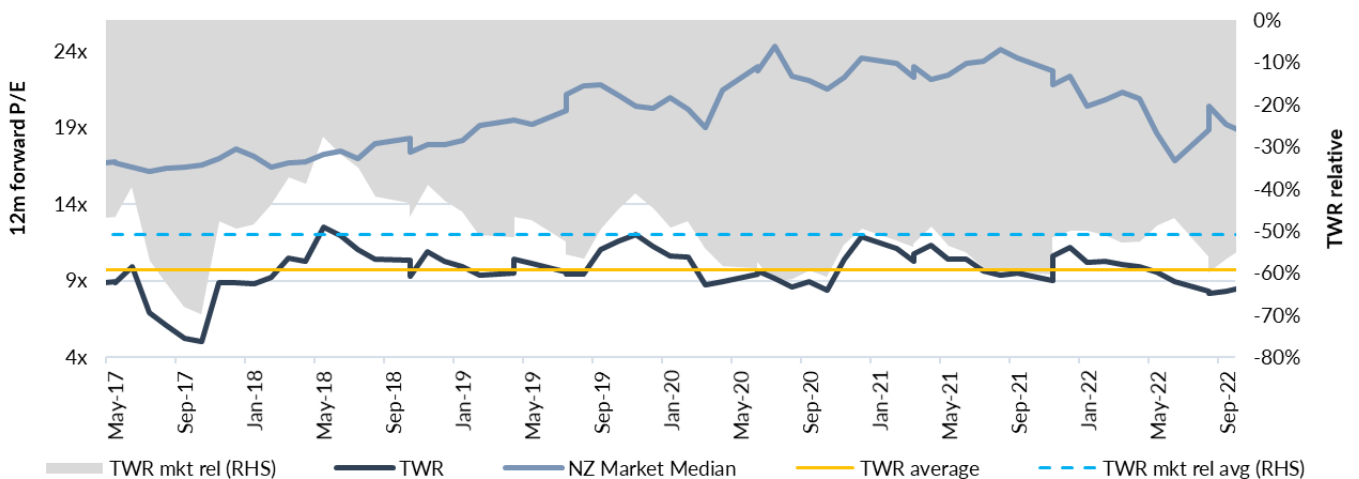
Source: Company data, Forsyth Barr analysis

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



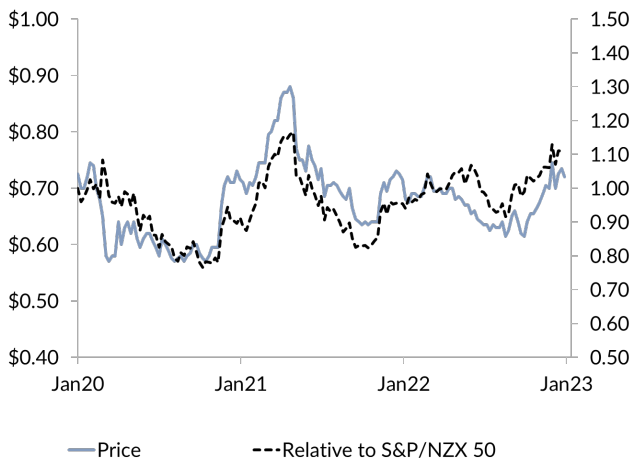
Source: Refinitiv, Forsyth Barr analysis

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

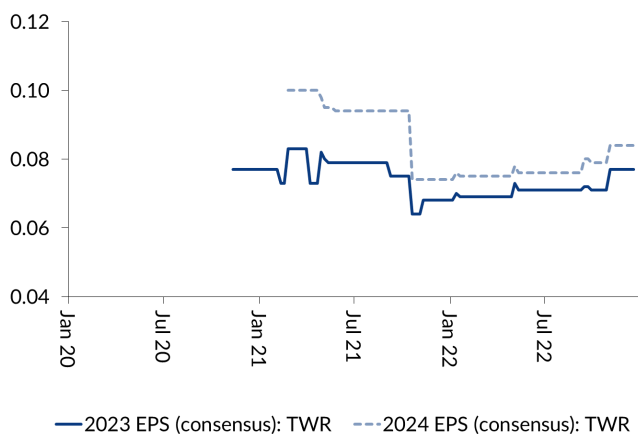
**Figure 31. International valuation comparisons**

Company	Code	Price	Mkt Cap (m)	PE		EV/EBITDA		EV/EBIT		Cash Yld 2024E
				2023E	2024E	2023E	2024E	2023E	2024E	
Tower Ltd	TWR NZ	NZ\$0.72	NZ\$273	9.1x	7.7x	n/a	n/a	n/a	n/a	9.7%
Heartland Group Holdings *	HGH NZ	NZ\$1.81	NZ\$1,277	11.0x	10.4x	n/a	n/a	n/a	n/a	7.0%
Insurance Australia Group	IAG AT	A\$4.76	A\$11,662	14.1x	12.6x	n/a	n/a	n/a	9.1x	6.1%
Suncorp Group	SUN AT	A\$11.65	A\$14,726	11.6x	11.4x	n/a	n/a	n/a	49.0x	6.7%
QBE INSURANCE GROUP	QBE AT	US\$8.88	US\$13,183	11.4x	8.4x	n/a	n/a	n/a	7.5x	6.6%
<b>Compco Average:</b>				<b>12.0x</b>	<b>10.7x</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>21.9x</b>	<b>6.6%</b>
<b>TWR Relative:</b>				<b>-24%</b>	<b>-28%</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>n/a</b>	<b>48%</b>

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

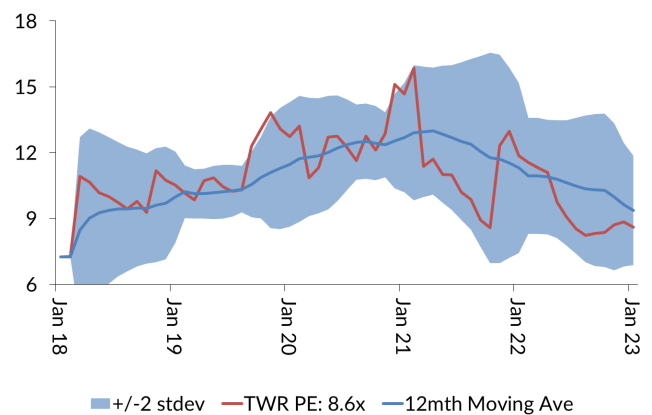
Source: \*Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (TWR) companies fiscal year end

**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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