# Raising UNM to a Buy Based on Exceptional Premium Growth

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**Conclusion:** I am recommending the purchase of Unum Group (UNM) because my work suggests premium rate increases combined with voluntary benefits sales growth due to recent API integrations with major payroll providers will lead to much stronger than consensus earnings.

**Price Target:** I derive a one-year price target of $52.41, which is 21% above Monday’s (11/27) close of $43.12, by applying a 71% discount to the market multiple to my $9.53 FY’25 EPS estimate. Additionally, I utilized a discounted cash flow analysis, using an 8.74% cost of equity and a terminal growth rate of 1.75%, which yielded a valuation of $126.66. As a discounted cash flow analysis is not a common valuation method utilized by analysts that cover UNM, I have decided did not to include it in my one-year price target.

**What’s Changed:** My view regarding premium rate increases on Unum’s US Group Protection book and volume growth in the group’s voluntary benefit’s line motivates me to raise my FY’25 EPS estimates from $8.54 to $9.53, putting me 14% higher than consensus.

**Research:**

* I project a 12%increase in Unum’s US Group segment’s net earned premiums for FY’24, which is 7% above consensus. This premium growth results from a combination of rate hikes and an expansion in the segments voluntary benefits volume. Ultimately, these changes are driven by shifts in policyholder behavior stemming from the Covid-19 pandemic and corresponding adjustments in insurers' actuarial assumptions.
* I estimate a 5% increase in US Group (70% of revenue) premium rates over the next 12 months (17% increase in EPS). This was confirmed in an employer survey in which 225 employers expressed their anticipation of rate increases across various group benefits products at renewals. A benefits broker noted that the impact of these pricing adjustments is particularly pronounced within the small group market (companies with less than 500 employees). Discussions with a former Unum employee suggest that Unum's strong emphasis on small group clients will make it more susceptible to the effects of rate increases compared to its competitors. I believe the consensus view underestimates this impact.
* I anticipate a 15% increase in US Group voluntary benefits (50% of group operating income) policies in force, resulting in a 5% boost in earnings per share. This projection is largely attributed to Unum's position as one of the two major carriers offering API enrollment capabilities on major payroll administration platforms. According to my survey of 100 human resources professionals who use prominent payroll platforms, API enrollment is highly regarded by employers and benefits consultants, ranking second in importance only to price. Furthermore, an industry study indicates that one in three employers seek to transition to an API-based benefits administration solution. Additionally, my survey revealed that among the employers who do not currently offer voluntary benefits (representing 50% of the sample), 30% intend to introduce them during the upcoming enrollment period.
* Conversations with a group benefits executive at a competing firm and a voluntary benefits broker have confirmed Unum's dominant position in API connectivity within the voluntary benefits sector. This technological advantage sets them apart, and it's likely that competitors will need up to two years to catch up with this enrollment feature.

**Quantifying the Impact:** Specifically, I forecastpremium rate increases will result in a 6% higher EPS than consensus for FY’24. My current estimate is for rates to increase by 5% but could be as high as 12% if our more aggressive survey results prove indicative. This trend, paired with an increase in voluntary benefits policies in force will result in FY’25 EPS to be 14% higher than consensus.

**How I Differ:** My perspective diverges from the consensus view because I believe the market is overlooking the magnitude of the premium rate increases within the US Group, as well as the consequential impact these rate hikes will have on benefits ratios. Additionally, consensus expectations appear to underestimate both the potential earnings growth and the competitive advantage derived from Unum's API capabilities in the voluntary benefits sector. I believe that consensus will adopt my view after renewal at the end of Q1 ’24 when the effect of the premium rate increases and voluntary benefits growth result in EPS higher than consensus.

**Where Could I Be Wrong:** I have a high degree of conviction in my call because I conducted a variety of proprietary research that I ultimately utilized to establish this call. My downside scenario results in a stock price of $36.52 (15.6% below yesterday’s close) which could occur if the company fails to deliver growth in voluntary benefits, has stagnant premium rates, and sees an above consensus 5% increase in US Group benefits ratios. My upside scenario implies a stock price of $63.67 (47.5% above yesterday’s close) which would occur if the company recognized 12% premium rate increases across its US Group as well as 20% growth in voluntary benefits policies in force.

**Exhibit 1: Financial Forecasts**

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**Exhibit 2: How We Differ from Consensus**

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Exhibit 3: Key Financial Data, Valuation and Relative Performance

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# Appendix

## Valuation Rationale and Assumptions

Historically, UNM trades at a lower P/E than the broader market. This is not uncommon for life insurance companies as the current industry P/E multiple is around 8.0x compared to the S&P multiple of 18.9x. Utilizing the G10, we see that Unum’s NTM P/E is a 71% discount to the broader market. This gives us a P/E multiple of 5.5x. I arrived at my valuation by considering the current multiple applied to UNM's stock, which reflects the prevailing market uncertainty. Additionally, I factored in my above-consensus FY'25 EPS estimate. Although I acknowledge the potential for Unum's rerating due to its growth prospects, I believe that ongoing uncertainty in the life insurance industry may continue to weigh on the company's relative valuation.

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| **FY’25 EPS** | **P/E Multiple** | **Price Target** |
| **$9.53** | **5.5x** | **$52.41** |

Unum's price-to-book ratio is again below average in the life insurance sector. Given the newfound volatility among life insurance balance sheets with the introduction of LDTI and recent assumption unlocking’s, I believe that relative P/Bs may remain deflated in the future. To value UNM fairly, I examined its annual price-to-book ratios since 2013. These values ranged from a low of 0.43x to a high of 1.05x. I ultimately decided to use Unum’s current P/BV of 0.87x as I believe it reflects a fair valuation of the company’s prospects.

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| **FY’25 BVPS** | **P/B Multiple** | **Price Target** |
| **$56.05** | **0.87x** | **$52.87** |

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## Scenario Rational and Assumptions

**Base Rationale:** Voluntary BenefitsPolicy in force growth of 15% arriving at $2B of premiums in force by FY’24. Premium rate increases on US Group products of 5% for a gross premium per policy of $45.80. Benefits paid per policy in force at 3%, in line with consensus estimates. These assumptions have our net premiums earned growing at 12.4% in FY’24 and 3% in FY’25. These assumptions are driven by the scenario where UNM posts strong results following renewals and lapses and mortality rates do not exceed consensus expectations.

On the expense side, I forecast a US Group loss ratio of 59% for FY’24 and 58% for FY’25. Holding all other expenses constant in line with historical averages, we get US Group combined ratios of 80% for FY’24 and 81% for FY’25.

Our $52.41 base case price target was derived by applying a 5.5x P/E multiple to our above-consensus FY’25 EPS estimate of $9.53.

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| **FY’25 US Group Premiums** | **Total Net Premium Growth** | **FY’25 US Group Loss Ratio** |
| **$7,630** | **12.4%** | **58.5%** |

**Upside Rationale:** Voluntary BenefitsPolicy in force growth of 20% arriving at $2.4B of premiums in force by FY’24. Premium rate increases on US Group products of 12% for a gross premium per policy of $48.86. Benefits paid per policy in force at 3%, in line with consensus estimates. These assumptions have our net premiums earned growing at 22.5% in FY’24 and 3% in FY’25. These assumptions are driven by the scenario where UNM posts exceptionally strong results following renewals, premium growth rates meet the top quartile of my survey, and voluntary benefits growth exceeds expectations.

On the expense side, I forecast a US Group loss ratio of 55% for FY’24 and 55% for FY’25. Holding all other expenses constant in line with historical averages, I found US Group combined ratios of 79% for FY’24 and 78% for FY’25.

My $63.68 bull case price target was derived by applying a 5.5x P/E multiple to my above-consensus FY’25 EPS estimate of $11.65.

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| **FY’25 US Group Premiums** | **Total Net Premium Growth** | **FY’25 US Group Loss Ratio** |
| **$8,073** | **22.5%** | **55.9%** |

**Downside Rationale:** Voluntary BenefitsPolicy in force growth of 0% remaining at $1.6B of premiums in force by FY’24. Premium rate increases on US Group products of 0% for a gross premium per policy of $43.62. Benefits paid per policy in force at 5%, roughly 2% above consensus estimates. These assumptions have our net premiums earned declining at 2% in FY’24 and remaining flat in FY’25. These assumptions are driven by the scenario where UNM fails to derive a competitive advantage from is API connectivity, is unable to meaningfully expand pricing, and experiences above consensus loss ratios.

On the expense side, I forecast a US Group loss ratio of 63% for FY’24 and 64% for FY’25. Holding all other expenses constant in line with historical averages, I found US Group combined ratios of 86% for FY’24 and 87% for FY’25.

My $36.52 bear case price target was derived by applying a 5.5x P/E multiple to my above-consensus FY’25 EPS estimate of $6.68.

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| **FY’25 US Group Premiums** | **Total Net Premium Growth** | **FY’25 US Group Loss Ratio** |
| **$6,724** | **0%** | **63.4%** |

## Proprietary Research to Support Investment Thesis

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