

Kinsale

4Q21: Strong Results Across the Board, Positive Operating Momentum Likely to Persist

KNSL had another strong quarter marked by healthy premium growth and robust underwriting margins. We view Kinsale as a high quality E&S franchise that we expect to perform well through the underwriting cycle, and we think there is likely to be upward momentum in its financial results over the medium term as it gradually unwinds the embedded economics in its book from the current hard market. Still, we remain Neutral on the stock given its valuation as well as the risk of multiple compression as the P&C pricing cycle continues to moderate (albeit more gradually than we had initially expected).

- EPS upside.** KNSL reported 4Q21 operating EPS of \$1.76, well above our \$1.39 estimate and consensus of \$1.36, driven primarily by a lower loss ratio (53.1% vs. 59.3%E). The expense ratio (21.4% vs. 21.5%E) and net written premium growth (+36.2% vs. +34.4%E) were modestly better. Within the loss ratio, both attritional losses (57.1% vs. 61.0%E) and catastrophe claims (-0.1% vs. +2.3%E) were responsible for the favorable variance. Prior year reserve releases were in-line. KNSL's results have exceeded our expectations for four consecutive quarters and we believe there is likely to be upside in our earnings estimates from a lower loss ratio assumption. However, we look to the earnings call to get more insight into any one-off factors (such as unusually low property losses) that could have benefited the accident year loss ratio in 4Q21. Given KNSL's casualty-focused mix, though, our view is that the 4Q21 result is probably more a reflection of management's loss picks (which in turn are informed by their view of pricing/terms and conditions vs. loss trends) and is therefore more likely than not to be trendable.
- Premium growth modestly better, margins were strong.** Net written premiums grew +36.2% y/y to \$177.5 mil., slightly above our \$175.1 mil. estimate (+34.4%), driven by continued healthy submission activity and higher prices. The CR of 74.5% was well below our 80.8% estimate, and results were also strong on an accident year basis (78.6% vs. 82.5%E). Net investment income was close to expectations.
- Given margin momentum, we think investor interest will likely shift to growth.** We think KNSL's growth outlook in 2022 and beyond will be more of a focus tomorrow on the earnings call given the clear margin momentum in its results. Related to this, we also expect KNSL's capital requirements vis-à-vis growth to be a discussion point. In the past, KNSL had signaled that it would fund its near-term capital requirements using debt. With a 20% debt-to-capital ratio as a constraint, we believe that Kinsale can issue upwards of \$150 million in debt. The company's net written premium to leverage ratio at year-end 2021 was roughly 1x equity.

Neutral

KNSL, KNSL US

Price (17 Feb 22): \$192.76

Price Target (Dec-22): \$225.00

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Quarterly Forecasts (FYE Dec)

Adj. EPS (\$)	2021A	2022E	2023E
Q1	1.11	1.44	
Q2	1.28	1.58	
Q3	1.59	1.38	
Q4	1.76	1.65	
FY	5.74	6.05	7.08

Style Exposure

Quant Factors	Current %Rank	Hist %Rank (1=Top)				
		6M	1Y	3Y	5Y	
Value	98	97	99	98	93	
Growth	4	5	6	16		
Momentum	34	83	59	24	11	
Quality	14	12	19	16	31	
Low Vol	79	38	43	74	76	
ESGQ	70	77	72	88	-	

4Q21 Results

EPS: \$1.76A vs. \$1.39E

NPW growth: +36.2% vs +34.4%E

Comb. ratio: 74.5% vs. 80.8%E

Positives

AY loss ratio

Expense ratio

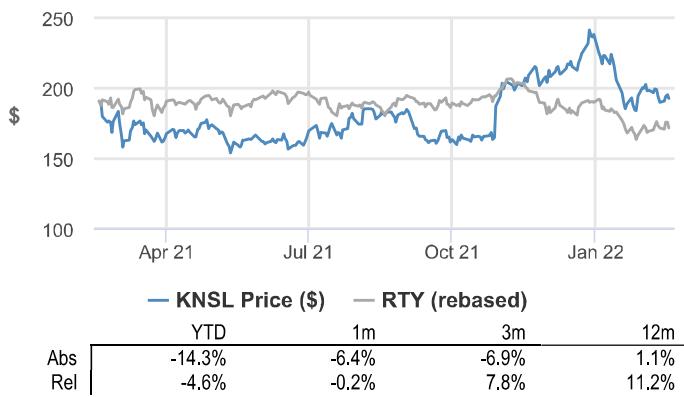
Premium growth

Sources for: Style Exposure – J.P. Morgan Quantitative and Derivatives Strategy; all other tables are company data and J.P. Morgan estimates.

See page 11 for analyst certification and important disclosures.

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Price Performance



Company Data

Shares O/S (mn)	23
52-week range (\$)	245.17-153.12
Market cap (\$ mn)	4,398.50
Exchange rate	1.00
Free float(%)	94.0%
3M - Avg daily vol (mn)	0.12
3M - Avg daily val (\$ mn)	25.4
Volatility (90 Day)	42
Index	RUSSELL 2000
BBG BUY HOLD SELL	4 4 0

Key Metrics (FYE Dec)

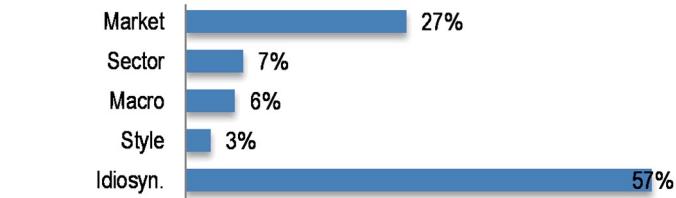
\$ in millions	FY21A	FY22E	FY23E
Financial Estimates			
NEP (Premium)	583	776	0
Underwriting income	134	141	(761)
Net investment income	57	36	40
Operating income	190	178	(721)
Adj. PBT	189	173	(726)
Adj. net income	132	140	164
Adj. EPS	5.74	6.05	7.08
BBG EPS	5.36	6.06	6.82
DPS	0.44	0.52	0.60
Investments	696	824	975
BVPS	30.65	36.28	42.87
NAVPS	-	-	-
Margins and Growth			
Adj. EPS growth	81.4%	5.4%	16.9%
Ratios			
Adj. tax rate	19.1%	19.0%	(5.3%)
Loss ratio	55.7%	60.6%	61.0%
Combined ratio	77.1%	81.8%	61.0%
Invest inc. % of Investments	-	-	-
Regulatory solvency ratio	-	-	-
Leverage (Debt/Debt+Equity)	-	-	-
ROE	20.8%	18.4%	18.2%
Valuation			
Dividend yield	0.2%	0.3%	0.3%
Adj. P/E	33.6	31.8	27.2
P/BV	6.3	5.3	4.5

Summary Investment Thesis and Valuation

Investment Thesis

KNSL is the only publicly traded P&C insurer that operates exclusively in the E&S insurance market with a focus on small commercial accounts. Our long-term outlook for KNSL is upbeat given its large addressable market, superior technology platform, and low cost base, which we view as a sustainable competitive advantage. Still, the stock's valuation seems full and we are concerned about the risk of multiple compression as the P&C pricing cycle continues to turn.

Performance Drivers



Factors	6M Corr	1Y Corr
Market: MSCI US	0.55	0.47
Sect: Financials	-0.33	-0.33
Ind: Insurance	-0.39	-0.29
Macro:		
US 10yr yield	-0.45	-0.39
Crude Oil	-0.39	-0.37
Credit Spread	0.11	0.22
Quant Styles:		
Quality	0.35	0.25
Momentum	0.27	0.24
Value	-0.22	-0.20

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Investment Thesis

Please see Page 5 for tables summarizing 4Q21 results.

KNSL will hold its earnings conference call at 9:00 AM Eastern on February 18, 2022.

The dial-in number for the call is 844-239-5282, code: 2881553.

The call replay will be available on <https://ir.kinsalecapitalgroup.com>.

We maintain our Neutral rating. In our opinion, KNSL is well-positioned to benefit from the hard P&C market on both volumes and margins. Also, we think that its low cost operating model is a sustainable competitive advantage in the E&S market across the pricing cycle, especially against higher cost competitors such as Lloyd's writers. On the other hand, the stock's valuation seems full versus commercial peers and specialist names, even after accounting for KNSL's growth potential and above-average margins. Furthermore, while favorable P&C market conditions have persisted longer than we had initially anticipated and will have positive implications for embedded margins, we think that the eventual turn in P&C pricing presents downside risk to KNSL's above-average multiple.

Well-Positioned to Capitalize on Favorable P&C Market

We expect the E&S market, where KNSL operates exclusively, to see continued strong new business flows and healthy price hikes in the near to medium term despite a handful of major underwriters increasing their focus on growth. We believe this favorable operating backdrop will give KNSL ample opportunities to continue driving strong premium growth. Similarly, the combination of price hikes and conservative reserving should allow KNSL to report healthy (and likely improving margins) for the foreseeable future. Looking beyond the current hard market, we see KNSL sustaining growth by continuing to build out its product offering, expanding distribution, and gaining incremental market share from other insurers that have less pricing flexibility to compete because of their much higher expense ratios.

Low Expenses a Durable Competitive Advantage

Kinsale operates with a proprietary and fully integrated technology platform that it built from the ground up, in contrast to many of its peers that use unwieldy hybrid systems consisting of legacy platforms and newer technologies. The net result has been an operating model that has the capacity to take on significant business volumes without sacrificing customer responsiveness, underwriting quality, and expense efficiency. We think that this operating leverage gives Kinsale the ability to outperform higher cost competitors (especially Lloyd's platforms, which constitute more than 20% of the E&S market) through the pricing cycle. During softer markets, KNSL has the ability to grow premiums as others pull back while maintaining above-average profitability. In hard markets, Kinsale can operate comfortably as a price taker and generate an even larger excess return relative to other companies.

Eventual Turn in Pricing Cycle is a Risk

The P&C industry is well into the current hard market and we expect price hikes to continue moderating modestly through 2022 and 2023 as re/insurers re-position themselves for growth and clients push back on rate-on-rate price hikes. This seems to be reflected in multiples for commercial P&C names, which are essentially flat versus pre-COVID levels, but less so for specialist names like KNSL, which are trading at a premium compared to historical levels. In our view, this presents the risk of multiple compression as pricing/volume swings tend to be more volatile in E&S given its function as a safety valve for the industry. Although we believe that KNSL will thrive even if prices soften, our view is that a reasonable valuation analysis will necessarily have to look several years out because of KNSL's above-average growth profile (our reference year is 2024), and would therefore have to account for how conditions in the P&C market are likely to be at that future time.

4Q21 Summary Results

The following tables and charts summarize KNSL's 4Q21 results as well as its operating performance over the past several years:

Table 1: 4Q21 Earnings: Actual versus Expected

\$ in millions, %, and bps

	JPM 4Q21E	Actual 4Q21	Actual v. Expected
<u>Underwriting Results</u>			
Net premiums written (\$)	175.1	177.5	1.4%
Net premiums earned (\$)	164.4	165.3	0.5%
Loss ratio			
AY loss ratio	59.3%	53.1%	-619 bps
Catastrophe losses	61.0%	57.1%	-387 bps
Unfavorable (favorable) PYD	2.3%	-0.1%	-234 bps
Expense ratio	-4.0%	-4.0%	2 bps
Combined ratio	21.5%	21.4%	-7 bps
AY combined ratio ex. cats	80.8%	74.5%	-627 bps
<u>Summary Income Statement</u>			
Underwriting income	31.7	42.2	33.2%
Net investment income	8.6	8.6	-0.2%
Taxes	(7.6)	(11.8)	55.2%
Operating income	32.7	39.0	19.3%
Operating EPS	\$1.39	\$1.76	26.7%

Source: Company reports and J.P. Morgan estimates.

Table 2: Historical Operating Performance

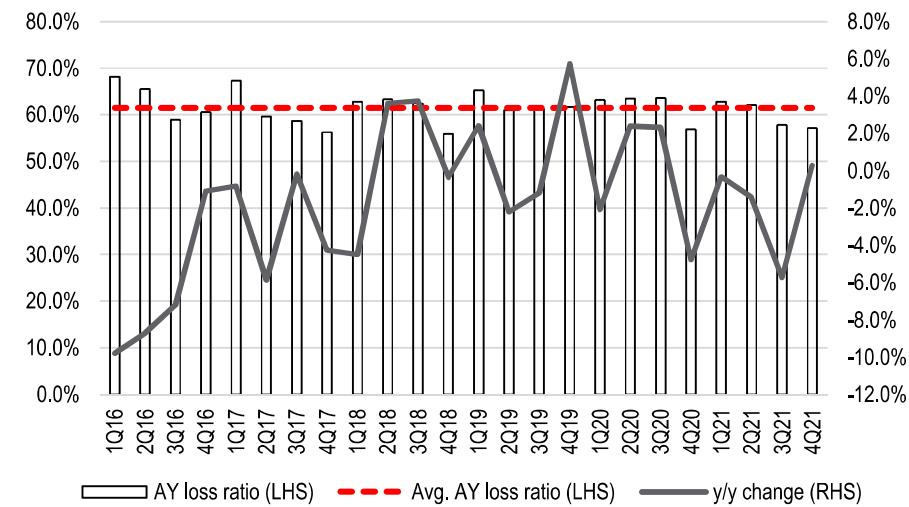
\$ in millions and %

	2016	2017	2018	2019	1Q20	2Q20	3Q20	4Q20	2020	1Q21	2Q21	3Q21	4Q21	2021
Premium Trends														
Gross written premiums	188.5	223.2	275.5	389.7	124.0	134.1	144.8	149.9	552.8	168.9	194.1	197.6	203.8	764.4
% ceded	11.3%	15.1%	14.5%	12.2%	12.9%	12.3%	15.6%	13.1%	13.5%	14.6%	13.6%	13.6%	12.9%	13.6%
Netwritten premiums	167.3	189.5	235.6	342.1	108.1	117.6	122.2	130.3	478.2	144.3	167.8	170.7	177.5	660.2
% growth y/y	99.1%	13.3%	24.4%	45.2%	47.9%	42.2%	40.9%	30.9%	39.8%	33.5%	42.6%	39.6%	36.2%	38.1%
Netearned premiums	133.8	176.1	212.7	283.0	89.8	97.0	108.2	117.8	412.8	123.0	137.7	156.9	165.3	582.9
% growth y/y	80.0%	31.6%	20.8%	33.0%	46.0%	46.7%	49.1%	42.3%	45.9%	37.1%	42.0%	44.9%	40.3%	41.2%
Underwriting Results														
AY loss ratio	63.0%	60.2%	60.9%	62.2%	63.1%	63.5%	63.5%	56.9%	61.5%	62.8%	62.0%	57.8%	57.1%	59.7%
Catastrophe losses	0.0%	5.0%	2.6%	1.1%	0.1%	0.4%	15.4%	5.1%	5.6%	0.1%	2.1%	3.7%	-0.1%	1.5%
Unfavorable (favorable) PYD	-10.0%	-6.4%	-3.3%	-3.3%	-3.4%	-3.7%	-2.8%	-3.1%	-3.2%	-5.7%	-6.6%	-5.9%	-4.0%	-5.5%
Loss ratio	53.0%	58.9%	60.2%	59.9%	59.9%	60.1%	76.2%	58.9%	63.9%	57.1%	57.5%	55.7%	53.1%	55.7%
Expense ratio	21.3%	25.1%	25.1%	24.8%	24.0%	23.7%	21.2%	22.8%	22.8%	22.9%	21.7%	20.1%	21.4%	21.4%
Combined ratio	74.4%	84.0%	85.3%	84.7%	83.9%	83.8%	97.3%	81.6%	86.8%	80.0%	79.2%	75.7%	74.5%	77.1%
AY combined ratio ex. cats	84.4%	85.3%	86.0%	87.0%	87.2%	87.1%	84.7%	79.6%	84.4%	85.7%	83.7%	77.9%	78.6%	81.1%
Investment Results														
Netinvestment income	7.5	10.6	15.7	20.1	6.0	6.6	7.0	6.5	26.1	6.9	7.4	8.1	8.6	31.0
% growth y/y	32.7%	41.2%	48.4%	28.3%	32.0%	38.3%	33.1%	17.1%	29.7%	16.5%	11.8%	15.5%	32.1%	18.9%
Duration	3.7	3.9	3.9	4.3	4.7	4.6	4.7	4.3	4.3	4.3	4.3	4.4	4.3	4.3
Gross yield ex. cash (YTD)	2.2%	2.4%	3.0%	3.1%	2.9%	3.0%	3.0%	2.9%	2.9%	2.6%	2.6%	2.5%	2.5%	2.5%
Cash and invested assets	480.3	561.1	643.1	908.2	955.0	1,100.0	1,200.0	1,300.0	1,300.0	1,400.0	1,500.0	1,600.0	1,700.0	1,700.0
% growth y/y	16.8%	14.6%	41.2%	34.9%	49.8%	38.1%	43.1%	43.1%	46.6%	36.4%	33.3%	30.8%	30.8%	30.8%

Source: Company reports and J.P. Morgan estimates.

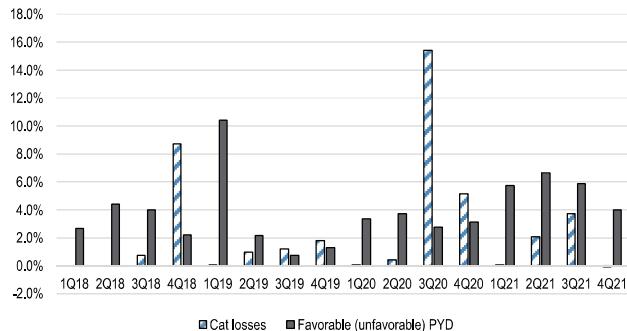
Figure 1: Historical AY Loss Ratio Trends

% of net earned premiums



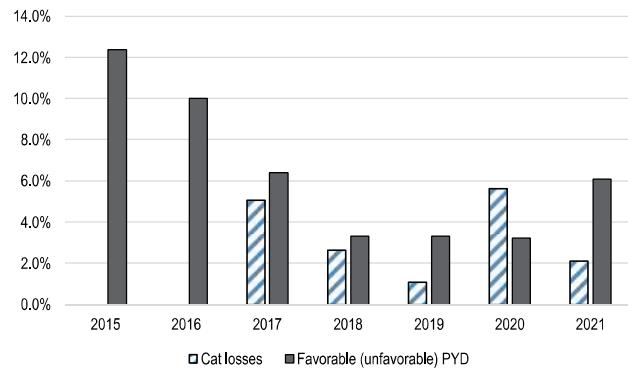
Source: Company reports and J.P. Morgan estimates.

Figure 2: Historical Catastrophe and PYD Trends (Quarterly)
 % of net earned premiums



Source: Company reports and J.P. Morgan estimates.

Figure 3: Historical Catastrophe and PYD Trends (Annual)
 % of net earned premiums



Source: Company reports and J.P. Morgan estimates.

Investment Thesis, Valuation and Risks

Kinsale Capital (*Neutral; Price Target: \$225.00*)

Investment Thesis

KNSL is the only publicly traded P&C insurer that operates exclusively in the E&S insurance market with a focus on small commercial accounts. Our long-term outlook for KNSL is positive given its large addressable market, superior technology platform, and low cost base, which we view as a sustainable competitive advantage. Still, the stock's valuation seems full at current levels and we are concerned about the risk of multiple compression as the P&C pricing cycle continues to moderate.

Valuation

We are maintaining our December 2022 price target at \$225. Our December 2022 target assumes a 4.5x P/BV target multiple on 2024 book value, which we believe is justified given KNSL's above-average growth over the long-term (+20% growth versus mid- to high-single-digit growth for most large commercial peers) and margin profile (80-85% combined ratio versus 85-90% for peers). KNSL trades at 6.3x book value, well above the specialty peer average (ex. PLMR) of 1.8x and commercial peers at 1.6x.

Risks to Rating and Price Target

We believe the main upside risks to our rating and price target are:

- **The hard P&C market lasts longer than expected.** Kinsale is seeing higher prices and greater submission flow because of dislocation in the P&C market. If current conditions persist longer than we assume, there could be upside to our forecasts and investor sentiment would likely improve.
- **Premium growth surpasses already elevated expectations.** In our view, part of KNSL's premium valuation is attributable to its above-average growth. We would expect KNSL's valuation multiple to expand if it consistently exceeds growth expectations in the next few years.
- **Margin improvement is greater than assumed.** The combination of earned pricing exceeding loss cost trends and management's conservative reserving suggests margin improvement in the next few years. If KNSL's margin improvement tracks higher than expectations, there could be upside to forecasts.

We believe the main downside risks to our rating and price target are:

- **Increased competition and/or push back from insurance clients dampens the pricing cycle.** The insurance industry is well into the hard market and clients are beginning to push back more strongly on price hikes while more insurers are deploying capital and positioning themselves for growth. If the cycle begins to turn, we believe there is a risk of multiple compression for insurers that have seen an outsized benefit from higher prices.
- **Adverse loss trends or social inflation re-emerge in casualty reserves.** Although unlikely to be a material risk for KNSL given its specific exposures and low limits, the re-opening of the economy and the court system could drive a surge in pent-up liability claims.

- **Unfavorable loss experience emerges from new lines of business.** Kinsale has a strong underwriting track record and it is entering new lines of business in a very strong part of the cycle. Still, given the long-tail nature of casualty coverage, the impact of badly underwritten risks is likely to persist.

Kinsale: Summary of Financials

Income Statement - Annual	FY21A	FY22E	FY23E	Income Statement - Quarterly	1Q22E	2Q22E	3Q22E	4Q22E
Earned premiums	-	-	-	Earned premiums	-	-	-	-
Policy charges and fee income	-	-	-	Policy charges and fee income	-	-	-	-
Net investment income	-	-	-	Net investment income	-	-	-	-
Other income	-	-	-	Other income	-	-	-	-
Total revenues	-	-	-	Total revenues	-	-	-	-
Insurance and annuity benefits	-	-	-	Insurance and annuity benefits	-	-	-	-
Interest credited	-	-	-	Interest credited	-	-	-	-
Interest expense	-	-	-	Interest expense	-	-	-	-
Acquisition & operating expenses	-	-	-	Acquisition & operating expenses	-	-	-	-
Amortization of acquisition costs (net)	-	-	-	Amortization of acquisition costs (net)	-	-	-	-
Other expenses	-	-	-	Other expenses	-	-	-	-
Total expenses	-	-	-	Total expenses	-	-	-	-
Pretax income	189	173	(726)	Pretax income	41	45	40	47
Income taxes	(36)	(33)	(38)	Income taxes	(8)	(9)	(8)	(9)
Total net income	132	140	164	Total net income	33	37	32	38
Total operating income	132	140	164	Total operating income	33	37	32	38
Weighted average diluted shares	23	23	23	Weighted average diluted shares	23	23	23	23
EPS - operating	5.74	6.05	7.08	EPS - operating	1.44	1.58	1.38	1.65
Balance Sheet and Capital Data	FY21A	FY22E	FY23E	Ratio Analysis	FY21A	FY22E	FY23E	FY24E
Shareholders' equity	-	-	-	EPS growth - operating	81.4%	5.4%	16.9%	-
Shareholders' equity ex. AOCI	-	-	-	Book value per share (ex. AOCI) growth	-	-	-	-
Shares outstanding	23	23	23	Return on equity (ROE) Return on equity (ex. AOCI)	20.8%	18.4%	18.2%	-
Book value per share	30.65	36.28	42.87		-	-	-	-
Book value per share (ex. AOCI)	-	-	-	Dividend payout ratio	7.7%	8.6%	8.5%	-
Capital for share repurchases	-	-	-	Total revenue growth	-	-	-	-
Capital for dividends	-	-	-	Total expense growth	-	-	-	-
Dividends	0.44	0.52	0.60	Tax rate	19.1%	19.0%	(5.3%)	-

Source: Company reports and J.P. Morgan estimates.

Note: \$ in millions (except per-share data).Fiscal year ends Dec

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Kinsale (KNSL, KNSL US) Price Chart



Date	Rating	Price (\$)	Price Target (\$)
03-May-19	OW	74.14	75
02-Aug-19	OW	89.98	105
08-Aug-19	OW	95.46	115
01-Nov-19	OW	105.72	125
20-Feb-20	OW	127.74	135
20-Apr-20	OW	114.01	125
31-Jul-20	OW	165.91	200
30-Oct-20	OW	208.26	220
18-Feb-21	OW	190.72	230
16-Apr-21	N	170.28	186
29-Apr-21	N	170.98	192
01-Jul-21	N	164.77	200
29-Jul-21	N	179.44	210
28-Oct-21	N	163.26	225

Source: Bloomberg Finance L.P. and J.P. Morgan; price data adjusted for stock splits and dividends.
 Initiated coverage Aug 22, 2016. All share prices are as of market close on the previous business day.

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