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Tiptree Inc. NasdaqCM:TIPT

FQ2 2019 Earnings Call Transcripts

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S&P Global Market Intelligence Estimates

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Table of Contents

Call Participants

EXECUTIVES

Michael Gene Barnes
Executive Chairman of the Board

Sandra E. Bell
Chief Financial Officer

ANALYSTS

Walter M. Schenker
MAZ Capital Advisors, LLC

Presentation

Operator

Greetings, and welcome to the Tiptree's Second Quarter 2019 Earnings Call. [Operator Instructions] As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Sandra Bell. Please go ahead.

Sandra E. Bell
Chief Financial Officer

Good morning, and welcome to our second quarter 2019 earnings call. We are joined today by our Executive Chairman, Michael Barnes; and our CEO, Jonathan Ilany. We have posted the earnings release and presentation on our website at tiptreeinc.com. Our remarks today are qualified in their entirety by the disclaimers on Page 1 of the presentation. This presentation supplements our SEC filings and is provided solely for information purposes. Throughout the presentation, we make forward-looking statements. Our businesses are subject to risks and uncertainties, which are outlined in our SEC filings and which could impact our expectations of future results. Except as required by securities laws, we undertake no obligation to update any forward-looking statements.

In addition, we use non-GAAP measures, which we believe provides supplemental information about our business and are useful to investors. As these measures are not GAAP, they should not be used as a substitute for GAAP disclosures. The appendix in the presentation provides a reconciliation to each of these measures to their GAAP equivalent.

With that, we will turn the call over to Michael.

Michael Gene Barnes
Executive Chairman of the Board

Thank you, Sandra, and good morning to everyone. As we enter the second half of the year, we are pleased with our first half financial performance and overall execution against our strategic objectives. We continue to grow our insurance business top line at double-digit rates and continue to refine our investments in Tiptree Capital with the goal of long-term value creation.

Our year-to-date return to shareholders was 7%, measured by growth in book value per share and dividends paid. As noted in our second quarter earnings release, we announced a $0.04 dividend for the second quarter, which represents a 14.3% increase from 2018 dividend.

At a macro level, we anticipate some slowing of the global economies over the next 2 years, although we remain long-term positive on the stability and continued expansion of the U.S. and the outlook for global trade. With this as our backdrop, we believe our core businesses are well positioned to benefit from a stable economy and a relatively healthy consumer base. Our focus on insurance and warranty origination at Fortegra is well positioned to grow, and we continue to look for acquisitions to expand our existing platform.

Away from insurance, certain market sectors, such as shipping, present attractive opportunities based on near-term technicals and long-term fundamentals. However, other sectors such as high-yield corporate credit present reasons to be cautious as we near the potential shift of a decade-long credit recovery cycle.

With this concern in mind, we have taken steps to reduce our exposure to corporate credit, but feel well positioned to take advantage of what we believe will be increasing opportunities over the coming years in stressed and distressed corporate credit. But to be clear, we are positive in our long-term outlook and see Tiptree's core businesses well positioned to continue to prosper.

With that, I'll pass it to Sandra, who will take you through the second quarter financial results in more detail.

Sandra E. Bell
Chief Financial Officer

Thank you, Michael. On Page 4, we present the company's key metrics for the second quarter of 2019. Net income was $12.2 million, an increase of $11.3 million over the prior year period. The increase was primarily driven by 2 factors: continued growth in insurance underwriting operations and $12.4 million of pretax gains on investments versus $3.8 million of mark-to-market losses in the second quarter of 2018. Included in the pretax gain on investments is a $7.6 million gain recorded on the sale of our Telos CLO asset management business in the second quarter. Net income for the year-to-date period was $16.5 million, down significantly given the prior year gain on sale of our senior living operations.

Excluding that gain and income from discontinued operations, net income before noncontrolling interest was up $21.1 million. The primary drivers of this increase can be attributed to similar factors as the quarter.

Operating EBITDA for the quarter was $12.7 million, down from the prior year, due primarily to the repositioning of our investment portfolio and the resulting buildup of cash still to be deployed.

Operating EBITDA for the year-to-date period was $25.3 million, up 5.9% from the prior year period. While both periods were impacted by the realignment of the insurance investment portfolio, the year-to-date results were more than offset by insurance underwriting growth and contributions from shipping operations.

On the bottom of the page, we show a [walk] from operating EBITDA to total pretax income, highlighting the key differences between the 2 metrics. Book value per share increased to $11.47, up $0.68 from year-end 2018, driven by improved earnings in addition to share buybacks over the past 4 quarters at an average 40% discount to book.

Turning to Page 5. We highlight our capital allocated between insurance and Tiptree Capital, along with the respective returns to assist investors in understanding Tiptree's enterprise value. When considering capital allocation decisions, we look at total capital, which includes corporate debt held at both the holding company and our insurance subsidiary. We valuate our return on capital using trailing 12-month operating EBITDA, which, for the most recent period, was $56.3 million. Our total return of approximately 8.4% is composed of 13.9% return in specialty insurance and an 8.6% return in Tiptree Capital. The key drivers of our returns for the period were growth in insurance operating EBITDA across all product lines, consistent and stable dividends from our Invesque shares, positive contributions from shipping operations in Tiptree Capital and relatively stable corporate expenses.

Now let's turn to our specialty insurance results. On Page 7, we highlight our underwriting performance, and then on the following page, returns from the investment portfolio. We continue to see positive top line growth across our product lines, including our European warranty program. For the first half of 2019, gross written premiums grew $67 million year-over-year, up 17%, and net written premiums grew 34%. We believe that there are number of fundamental factors, which provide support to continue this growth moving forward.

Within warranty, our opportunities exist, partly because of the size and growth trajectory of the overall market. We have made great strides penetrating this sector and believe it has a long runway for growth.

Second, the nature of the claims we incur in our product lines do not change substantially through different economic cycles. And typically, consumers keep their cars and appliances longer in a slowing economy, which we believe may increase demand for extended service contracts.

Underwriting margin was up 11%, and our combined ratio held steady at 93.2%, demonstrating our ability to continue to grow profitably in our insurance business. This quarter, I would also like to highlight that we have built a substantial balance of $726 million of unearned premiums and deferred revenues on our balance sheet, up 23% from this time last year. This growth is key to our future earnings, both from underwriting profits as well as contributions from the growing investment portfolio of paid in premium.

Turning to the investment portfolio on Page 8. Our net investments grew by $79 million year-over-year, up 19%, driven by our growth in net written premiums. Year-to-date, net investment income was $7.7 million, down $1.4 million as we reduced our exposure to corporate loans, thus decreasing our interest income. We ended the quarter with $124 million of cash in the insurance portfolio, which is available for investments. Net portfolio income was $12.9 million, up approximately $8.2 million versus the prior year. The improved performance was driven by 2019 unrealized gains versus losses in the prior year period, combined with lower asset-based interest expense.

On Page 10, we present the results of Tiptree Capital, which primarily consists of our Invesque shares and shipping operations. Over time, we would expect that our investments could shift as we recognize returns in 1 asset class or business and reinvest in others. Our senior living results are included in our 2018 results to facilitate period-over-period comparison.

As of the end of the second quarter, our Invesque position represents a $119 million, of which $99 million is held in Tiptree Capital, the remainder is in our insurance portfolio. The final transfer restrictions on our Invesque shares expired on August 1, 2019. The remaining discount will accrete into income over the third quarter. Year-to-date, real assets operating EBITDA was $6.8 million, which includes dividends on our Invesque shares and the results from our shipping operations. Specialty finance operating EBITDA was stable, while pretax income declined due to a $1.6 million mark-to-market loss on our MSR portfolio, as mortgage interest rates declined.

Now we will turn the call back to Michael to conclude our prepared remarks.

Michael Gene Barnes
Executive Chairman of the Board

Thanks, Sandra. The first half was a solid start to the year. Our book value increased plus dividends produced a return of 7%, and operating EBITDA improved over the prior year. Our announced dividend increase and share buybacks reflect our positive view of the cash flow that our business can generate. For the remainder of 2019, we expect to see continued growth in our insurance business, both organically and selectively through acquisitions should we find the right ones. We will also look to grow our insurance investment portfolio in line with the business and to enhance its total return over the long term. And within Tiptree Capital, we will continue to seek opportunistic capital allocations that present attractive long-term returns.

With that, we'll open the line for questions.

Question and Answer

Operator

Our first question comes from Walter Schenker with MAZ Partners.

Walter M. Schenker
MAZ Capital Advisors, LLC

It is a strategic question trying to understand given your investment expertise and the values you maintain in the business, why the stock buyback, which was 1.5 million shares, so we'll call it $10 million roughly, a little bit more, has not been substantially more aggressive? I understand there's liquidity issue, but there'll always be a liquidity issue. You have a lot of cash. And it would seem the most accretive thing you can do and the return at $6 or $7 a share on buying back your stock as such that there isn't a lot in your portfolio that gives you a higher long-term return and in short-term accretes value at a greater rate for shareholders?

Michael Gene Barnes
Executive Chairman of the Board

Thank you, Walter. I think that's a fair comment. And in fact, we are always trying to balance the question of make -- allocating capital available to new investments that will further grow our platform, grow our business, produce potentially attractive returns as opposed to buying back shares, which at the discount at which we're trading, I would agree, is -- has the potential to be very accretive and represents a good use of capital potentially. So we're always evaluating that and trying to balance that. We do have investments earmarked -- that we've earmarked capital for and that we want to be very careful in terms of having that capital that goes out of the company when buying back shares. We have been fairly active, I'd say, over the last 4 years in buying back shares and have purchased a substantial portion of our outstanding float back at a discount of approximately 40% to our GAAP book value.

So I think we have been fairly aggressive in buying back shares. We're going to continue to look for opportunities to buy back shares. To be frank, as legacy investors of Tiptree have exited, the ability to buy back shares in a large amount at a substantial discount has diminished. And so some of the larger holders, although they may have interest in selling shares, would only do so at a much higher price, which makes it less attractive. So as we've bought back shares, a lot of it has been in the more liquid float, which isn't always a great thing. It's very much our objective to grow the business and to create a larger enterprise value. And so we're always trying to balance that. But we take your comments to our heart and we are always looking to buy back shares at attractive prices with -- if we have available capital.

Operator

There are no further questions, I would like to turn the floor over to Sandra for closing comments.

Sandra E. Bell
Chief Financial Officer
Thank you, Stacy, and thanks, everyone, for joining us today. If you have any questions, please feel free to reach out to me directly. This concludes our second quarter 2019 conference call.