Randall & Quilter

New capital underpins ambitious growth strategy

10 December 2020

Recent newsflow illustrates the gathering momentum behind R&Q's growth. Negotiations are well underway for substantial legacy purchases, other transactions await regulatory approval, and both have been secured by the latest fundraising. Along with an equity issue in May, that means R&Q has added over US$200m in new capital this year.

R&Q intends to continue to capitalise upon the hardening insurance environment. The stronger balance sheet is reflected in the recent reiteration and extension of AM Best ratings to new Group entities.

Fundraising fuels expansion

R&Q has agreed to issue US$107.75m of 13-year unsecured subordinated notes. This will build its regulatory capital and put the finance in place to support its ongoing plans for both Program Management and Legacy. It continues to report **strong demand for its solutions in both divisions**.

The structure and terms of the fundraising match R&Q's current scale and appear to be an advantageous source of capital i.e., treated favourably within regulatory solvency and adjusted financial leverage positions. As subordinated debt (Tier 2 Ancillary Capital), the Notes will be subordinate to all policyholders and beneficiaries, and all non-subordinated creditors. The coupon is 3-month USD LIBOR (0.5% floor/2% cap), plus a 6.75% margin for the first ten years, 8.25% thereafter. That is in line with the market and R&Q's previous Tier 2 debt issues i.e., USD LIBOR plus 6.35% and 7.75%, with maturities in 2028 and 2023 respectively (FY19 accounts Note.22).

The Notes will be issued in a private placement which did not require a formal rating. They will be due in December 2033 and can be called after five years at par (at R&Q''s option). **They provide long term cost of capital certainty, improve the group's regulatory capital position, and enable it to grow by writing additional business.**

We have adjusted our forecasts to reflect the coupon, although not yet the income from prospective growth, which we anticipate will **generate considerably higher returns (c. 20% RoC).** The outlook remains attractive, underpinned by the new business pipeline, enhanced competitive positioning and the current 'hard' insurance market.

Undervalued

The forecast FY20e distribution of 9.5p is 3.3% up y-o-y, divisional forecasts are comfortably being met, and prospects are underpinned by balance sheet strength and recent investment. RQIH's current value at just 1.2x NAV is well below the average of 2.3x for Speciality Insurers over the past five years. Even moving to a conservative 25% discount to the peer group average would put RQIH shares at c 216p.

Summary forecasts

Year end 31 Dec	2018A	2019A	2020E	2021E
Operating Profit (EBIT) (£m)	18.6	47.6	42.0	56.0
Pre-tax (continuing) (£m)	14.3	38.1	32.8	44.5
EPS (p)	7.8	20.3	14.6	21.5
Yield on distribution (%)	5.1	5.2	5.4	5.8
Tangible NAV per share (p)	129	125	133	147

Source: Group report & accounts and ED estimates **final div paid in shares during the pandemic*

Company Data

EPIC	RQIH
Price	175p
52 weeks Hi/Lo	187p/113p
Market cap	£396m

Share Price, p

Source: ADVFN

Description

Randall & Quilter Investment Holdings Ltd. (R&Q) is a long-established UK and US insurance business led by an experienced and growing management team. It is focused on two core strategies: to drive commission income from writing niche books of business using its carriers licensed in all key regions and to grow an industry leading provider of exit solutions for legacy / run-off insurance assets to vendors in the US, Bermuda and Europe.

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Legacy acquisitions gathering steam

R&Q completed nine legacy transactions in H1 2020 and in September, announced a deal to reinsure the c US$400m casualty reserves of Bermudian RenRe's Lloyd's syndicate. It reported two transaction during November. R&Q Re (Bermuda) Ltd entered into a stock purchase agreement to acquire a Bermuda-domiciled captive insurance company, which is subject to regulatory approval. It also confirmed that the Oklahoma Insurance Commissioner had approved the Insurance Business Transfer of a portfolio of Sentry Insurance's reinsurance policies to a wholly owned R&Q subsidiary, National Legacy Insurance Company. Further deals of this type are expected to follow this path.

Other activity includes a potentially significant transaction for R&Q's Legacy division, reported by 'The Insurer' (3 December edition) and at this stage unconfirmed by R&Q. The scale, however, shows the Group's ambition. According to reports, R&Q is in exclusive discussions to acquire Soros-backed Vibe Syndicate Management Ltd. This would be a sizeable transaction i.e. a takeover of Lloyd's Syndicate 5678's **c £250m back year reserves**. The article says that Vibe sought an exit solution this summer. The book relates to the 2008-2019 years of account and covers multiple classes including A&H and general liability. It ceased underwriting on 31 December 2019.

A deal would follow R&Q's earlier agreement with Vibe Syndicate in August, when it agreed to acquire the entire issued share capital of Vibe-owned Inceptum Insurance Company, subject to regulatory approval. Inceptum was placed into run-off in September 2009 and sold by the HSBC group to Syndicate Holding in September 2011.

Portfolio Management outlook affirmed by AM Best ratings

In December R&Q's newly formed Excess & Surplus (E&S) lines carrier, Accredited Specialty Insurance Company (ASI), was assigned an **A.M. Best Financial Strength Rating of A- (Excellent)**, a **Financial Size Category of IX**, and a **Long-Term Issuer Credit Rating of "a-"**. Domiciled in Arizona, ASI's AM Best rating finalises R&Q's plan to establish an E&S program management company.

The US MGA market approaches **$60bn in annual premiums** and most MGAs operate within the E&S market. The rating completes the strategy to establish Accredited as a comprehensive program management solutions provider in all its major markets. As ASI is now both rated and licensed, it is in a position to take advantage of the opportunities in the E&S market and already reports a strong pipeline.

AM Best assigned an outlook of 'stable' and noted that the ratings *'reflect the consolidated balance sheet strength of R&Q'* which it categorises as *'very strong.'* It also recently affirmed the Financial Strength Ratings of A- (Excellent) and the Long-Term Issuer Credit Ratings of "a-" of R&Q's US Admitted Market program management company, Accredited Surety and Casualty Company, Inc., and its European program management company Accredited Insurance (Europe) Limited (Malta).

The new ratings and affirmations are key components of the group's position as a leading provider of high-quality program capacity to MGAs and reinsurers in both the US and Europe. A rating of A- and a Financial Size of IX means Accredited companies are among the best capitalised program managers

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