

Equity Research

May 8, 2015

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Financials

Essent Group Ltd.

ESNT Reports 1Q15 Earnings Beat as Robust Growth Story Remains Intact, Credit Quality Still Stellar

While Essent Group (ESNT) is still a relatively young company, having entered the U.S. mortgage insurance market in 2010, it would be reasonable to expect that the company would begin to see an uptick in losses at this point. However, as ESNT has continued to grow its portfolio such an uptick has yet to materialize and the lack of significant loss development has helped to buoy its profitability.

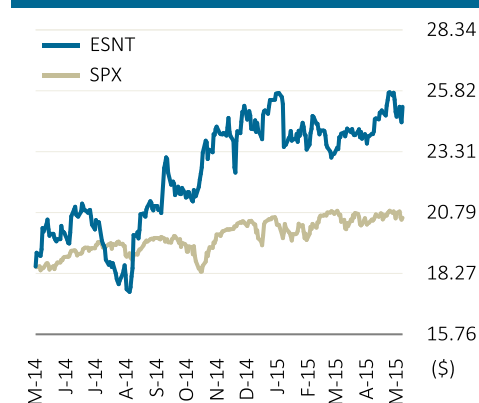
- ▶ ESNT this morning reported 1Q15 earnings per diluted share of \$0.38, beating the consensus estimate of \$0.35 and our estimate of \$0.36 as net premiums earned jumped 11% sequentially to \$75.0mm.
- ▶ At the same time, ESNT's credit quality remained stellar as its provision for loan losses and loss adjustment expense declined to \$2.0mm in 1Q15 from \$3.0mm in 4Q14 and the percentage of loans in default remained tiny at 0.21%.
- ▶ **We are reiterating our Buy recommendation on ESNT and price target of \$31** based on 14.5X our 16E EPS of \$2.14. We believe the company's solid growth prospects, lack of legacy exposures and predictable future earnings stream merit a premium valuation.
- ▶ While ESNT's share of a competitive U.S. mortgage insurance market remained stable in 1Q15, it continued to set the stage for future growth by adding 25 customers during the quarter, bringing its total to 1,025.
- ▶ In addition to its legacy-free balance sheet and investment grade credit rating, another factor that differentiates ESNT from its peers is
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- ▶ **Valuation:** Our \$31 price target for ESNT is based on 14.5X our 16E EPS of \$2.14.

ESNT **\$25.16**
12 month target \$31.00
Upside 23.2%

BUY

52 week range \$17.51 - \$25.76
Market Cap (m) \$2,302

Price Performance



Source: IDC

Estimates

	1Q14 A	2Q14 A	3Q14 A	4Q14 A	FY14 A	1Q15 A	2Q15 E	3Q15 E	4Q15 E	FY15 E	FY16 E
Diluted EPS (Adj.)	0.18	0.23	0.29	0.33	1.01	0.38	0.40	0.43	0.47	1.68	2.14
BVPS (Ex-AOCI)	8.74	9.07	9.35	10.87	10.87	10.88	11.28	11.71	12.18	12.18	14.33
Operating Income	23	30	39	44	136	51	53	57	62	223	287

Source: BTIG Research Estimates and Company Documents (\$ in millions, except per share amount)

Please Read: Important disclosures and analyst's certification appear in Appendix

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its ability to enter into GSE risk share transactions via its Bermuda-based insurer, Essent Re. The unit in 1Q15 continued to leverage the reinsurance entity by participating in Freddie Mac's Agency Credit Insurance Structure (ACIS) 2015-2 and 2015-3 transactions and insured \$20.7mm of risk that Freddie Mac had retained as part of its STACR 2014-DN₃ and STACR 2014-DN₄ deals.

Income Statement

Operating Model - ESNT (\$ millions)	Dec-13 2013A	Mar-14 1Q14A	Jun-14 2Q14A	Sep-14 3Q14A	Dec-14 4Q14A	Dec-14 2014A	Mar-15 1Q15A	Jun-15 2Q15E	Sep-15 3Q15E	Dec-15 4Q15E	Dec-15 2015E	Dec-16 2016E
Net premiums written	258.87	52.19	63.51	77.86	83.22	276.78	82.26	88.36	94.03	100.16	364.80	446.88
Increase in unearned premiums	(93.70)	(7.44)	(13.16)	(17.54)	(15.41)	(53.55)	(7.22)	(9.82)	(10.45)	(11.13)	(38.61)	(49.65)
Net premiums earned	165.16	44.75	50.34	60.32	67.81	223.23	75.04	78.54	83.58	89.03	326.19	397.23
Net investment income	4.64	1.90	3.08	3.41	3.90	12.29	4.28	4.60	4.95	5.32	19.14	26.16
Realized investment gains	0.17	0.40	0.07	0.15	0.31	0.93	0.65	-	-	-	0.65	-
Other income	10.15	0.77	0.79	0.74	0.72	3.03	0.04	0.05	0.05	0.05	0.19	0.24
Revenue	180.12	47.82	54.28	64.62	72.74	239.47	80.01	83.19	88.57	94.40	346.17	423.63
Provision for losses and LAE	3.79	0.90	0.97	1.39	3.05	6.31	2.00	2.10	2.20	2.31	8.62	10.97
Other underwriting and operating expenses	132.18	23.46	23.65	24.47	25.66	97.23	27.50	28.19	28.89	29.61	114.19	126.04
Losses and expenses	135.97	24.36	24.61	25.86	28.71	103.54	29.50	30.28	31.09	31.93	122.80	137.01
Loss before income taxes	44.15	23.46	29.67	38.76	44.04	135.93	50.51	52.90	57.48	62.48	223.37	286.62
Income tax expense (benefit)	(7.72)	8.45	10.11	13.69	15.17	47.43	15.68	16.40	17.82	19.37	69.26	88.85
Net income	51.87	15.01	19.56	25.07	28.87	88.50	34.84	36.50	39.66	43.11	154.11	197.77
Diluted EPS	0.60	0.18	0.23	0.29	0.33	1.01	0.38	0.40	0.43	0.47	1.68	2.14
Diluted shares outstanding	87.02	84.70	84.71	85.03	87.95	87.95	91.51	91.61	91.71	91.81	91.81	92.21
Book value per share	8.30	8.74	9.07	9.35	10.87	10.87	10.88	11.28	11.71	12.18	12.18	14.33
Tax rate	-17.48%	36.04%	34.09%	35.32%	34.45%	34.89%	31.03%	31.00%	31.00%	31.00%	31.01%	31.00%

Source: BTIG Research Estimates and Company Documents

Appendix: Analyst Certification and Other Important Disclosures

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I, Mark Palmer, hereby certify that the views about the companies and securities discussed in this report are accurately expressed and that I have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

I, Giuliano Bologna, hereby certify that the views about the companies and securities discussed in this report are accurately expressed and that I have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report.

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Stocks in coverage as of the end of the most recent calendar quarter (March 31, 2015): 142

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Essent Group Ltd. (ESNT)

Valuation

Our price target of \$31 for ESNT is based on 14.5X our 16E EPS of \$2.14

Risks

Risks to our recommendation include legislative or regulatory actions or decisions to change the role of the GSEs in the U.S. housing market, actions to decrease or discontinue the use of mortgage insurance or changes in the GSEs' eligibility requirements for mortgage insurers that could reduce ESNT's revenues or adversely affect its profitability and returns; a reduced amount of insurance ESNT may be able to write if lenders and investors select alternatives to private mortgage insurance; the negative impact on revenues, profitability and returns if ESNT were to lose a significant customer; the potential adverse impact on ESNT's business prospects and operating results if the Consumer Financial Protection Bureau's final rule defining a qualified mortgage (QM) reduces the size of the origination market or creates incentives to use government-supported mortgage insurance programs; a potential increase in ESNT's losses if a downturn in the U.S. economy or a decline in the value of borrowers' homes from their value at the time their loans close results in more homeowners defaulting.

Essent Group Ltd. (ESNT)



Note: Closing Price and Target Price have been adjusted for corporate actions.

Date	Closing Price (\$)	Target Price (\$)	Analyst	Rating
31-Oct-13	21	28	Mark Palmer	BUY
13-Feb-15	24.18	31	Mark Palmer	BUY

Other Disclosures

Additional Information Available Upon Request

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