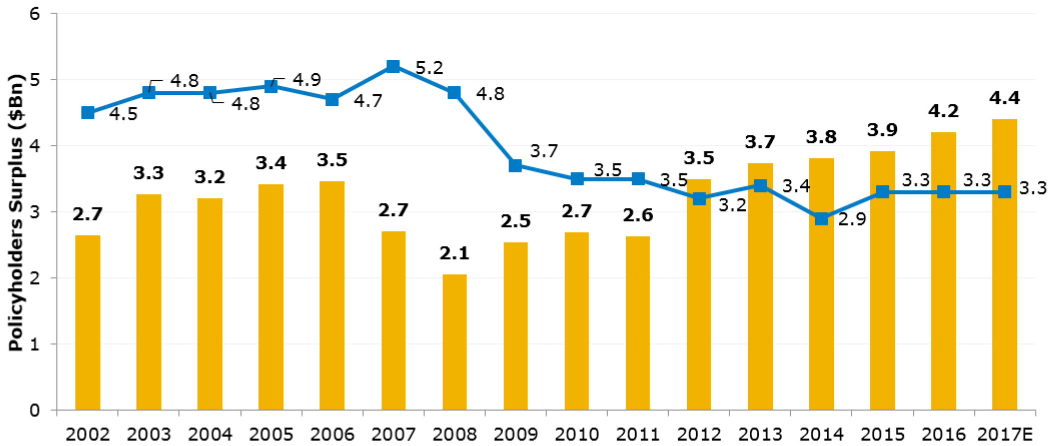
U.S. TITLE INSURERS 2018 OUTLOOK

Financial Institutions | Insurance Research

The U.S title insurance industry will enjoy another positive year in 2017, with robust surplus levels and seven consecutive years of net income. Since the industry's last net loss in 2010, title underwriters have generated close to $5 billion in net income. Through the third quarter of 2017, the title industry hit record policyholder surplus (PHS or surplus) levels at approximately $4.4 billion. Projections for year-end are also at $4.4 billion or just slightly under, as the fourth quarter typically experiences the highest reductions for dividends, leading to a healthy net premium to PHS ratio of about 3.3:1.

The industry has yet to achieve net income greater than $1 billion since before the financial crisis, which was achieved in 2003, 2004 and 2006, with net incomes of $1.11 billion, $1.09 billion, and $1.01 billion respectively. Kroll Bond Rating Agency (KBRA) expects net income to be around $750 million to $800 million in 2017, a decrease of between 12% and 17% from 2016. Net investment income has been generally consistent in recent years, averaging approximately $240 million over the past five years. However, this is considerably lower than prior to the financial crisis, when net investment income averaged over $500 million from 2003 through 2009. Going forward, KBRA expects net investment income to benefit from rising interest rates.

U.S. Title Insurance Industry - Policyholders Surplus and Net Written Premium to Policyholders Surplus



Source: ALTA.org - Title Industry Financial Data Books and KBRA Estimates

The industry continues to benefit from favorable loss experience due to lower claims volumes, with an expected industry loss ratio of around 5% in 2017. This approximates the recent three-year average and is down considerably from prior years. KBRA believes that claim experience has also improved in recent years in part due to a decrease in the level of foreclosure activity. Further, improved cost efficiencies along with the benefits from technological advances have improved expense ratios to approximately 95%, also down considerably from the past. Historical loss and expense ratios are available **here**. KBRA believes that further significant improvements in the expense ratio may be difficult to achieve, as a significant portion of a title insurer's cost structure is fixed.

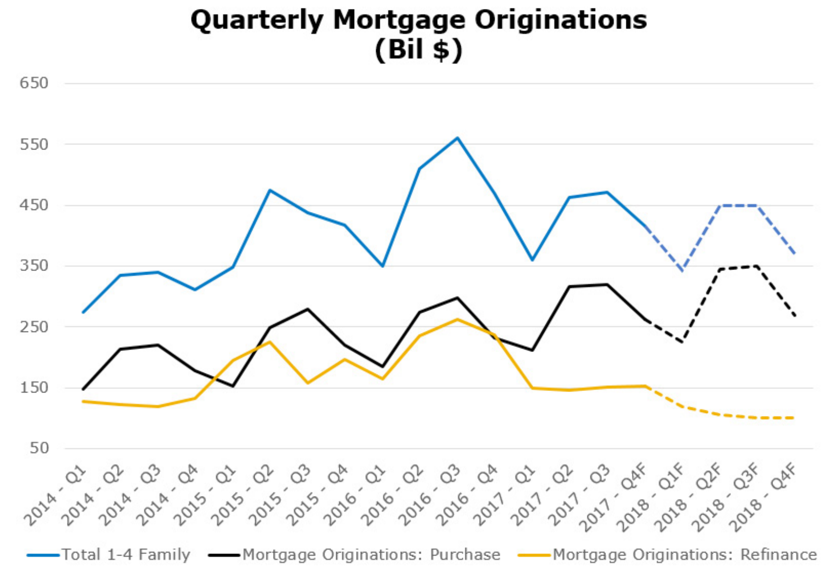
Industry Outlook is Stable

As a result of the recent favorable financial trends and the current financial condition of title underwriters, KBRA views the industry Outlook as Stable. Of the 47 title insurers with over $2 million of statutory surplus, KBRA expects close to 90% of title underwriters to have positive earnings in 2017, with over 75% increasing surplus. However, despite the industry's recent success, title insurers could face some headwinds in 2018. The Mortgage Bankers Association (MBA) is projecting further declines in mortgage volumes, with significant declines expected for mortgage refinances. Since premium volume and profitability for the title insurance industry is closely tied with real estate sales and mortgage refinancing activity, lower volumes could lead to lower profitability. The MBA's projected total mortgage originations are forecasted to decrease 12.3% in 2017 (+9.9% purchase originations and -36.6% for refinances), which is approximately the decline KBRA forecasts in net income. For 2018, the MBA projects an additional decline of 4.3%, with purchase originations increasing 8.3% and a further decline of 28.2% for refinances.

Quarterly Mortgage Originations Estimates

Quarter / Year	Total 1-4 Family	Mortgage Originations: Purchase	Mortgage Originations: Refinance
2014 - Q1	275	148	127
2014 - Q2	335	213	123
2014 - Q3	340	220	120
2014 - Q4	311	179	133
2015 - Q1	348	154	195
2015 - Q2	475	249	226
2015 - Q3	438	280	158
2015 - Q4	417	220	197
2016 - Q1	350	185	165
2016 - Q2	510	275	235
2016 - Q3	561	298	263
2016 - Q4	470	232	238
2017 - Q1	361	212	149
2017 - Q2	463	316	147
2017 - Q3	471	320	151
2017 - Q4F	415	262	153
2018 - Q1F	344	225	119
2018 - Q2F	450	345	105
2018 - Q3F	450	350	100
2018 - Q4F	370	270	100

Source: Mortgage Bankers Association



Source: Mortgage Bankers Association

However, as KBRA recently noted in its report titled, "**2017 Atlantic Hurricane Season Ends; Widespread Devastation Across Multiple Sectors Continue**," U.S. home building jumped to a one-year high in October of 1.29 million units which represents a 13.7% increase. This is likely attributable to disruptions caused by recent hurricanes in the South fading. Groundbreaking activity in the South, which accounts for almost half of U.S. residential construction, plummeted in the aftermath of the hurricanes. However, communities in the region have now started replacing houses damaged by flooding. The uptick in home construction reported by the Commerce Department was also driven by gains in the Northeast and Midwest regions. KBRA believes that the widespread destruction from the 2017 hurricanes and California fires could have a multi-year impact on reconstructions.

Homebuilder confidence has also steadily increased since September, as measured by the 'National Association of Home Builders/Wells Fargo Housing Market Index' (HMI). The HMI is an index based on a monthly survey of members belonging to the National Association of Home Builders (NAHB) that is designed to measure

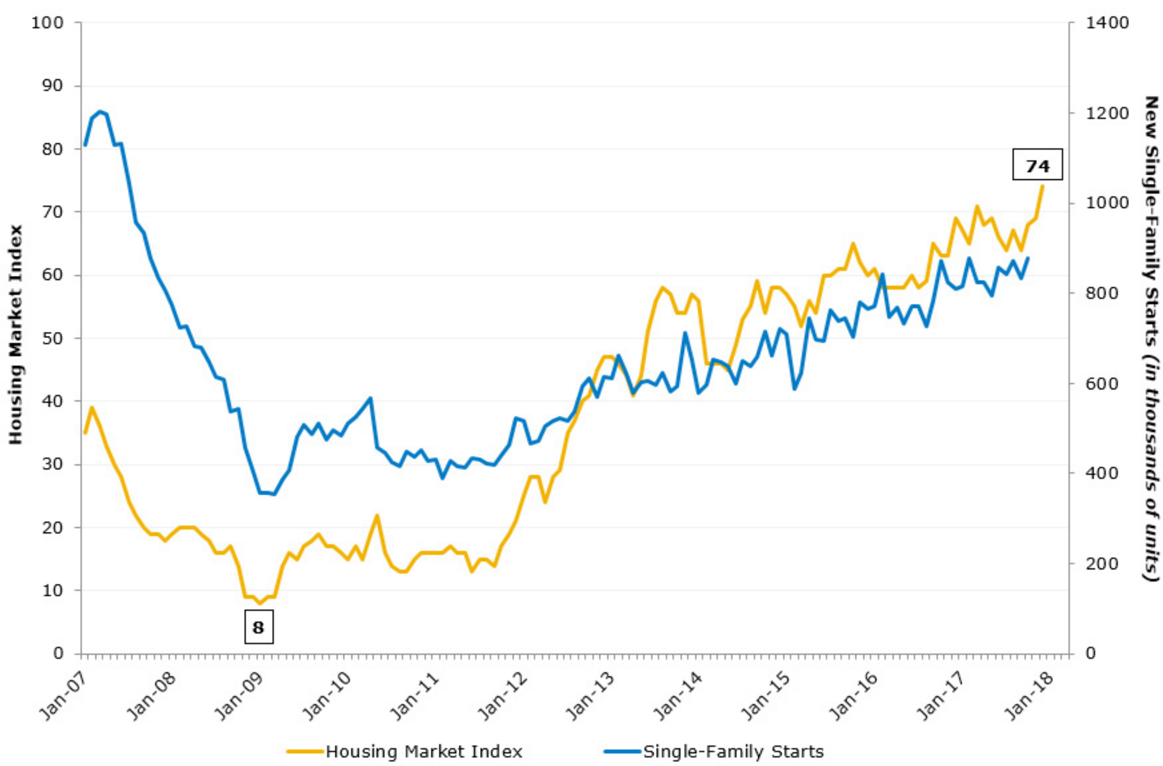
NAHB/Wells Fargo National and Regional Housing Market Index (HMI)

(Seasonally Adjusted)	2016	2017											
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov Revised	Dec Prelim.
Housing Market Index	**69**	**67**	**65**	**71**	**68**	**69**	**66**	**64**	**67**	**64**	**68**	**69**	**74**
Housing Market Index Components													
Single Family Sales: Present	75	72	71	77	74	75	72	70	74	70	75	77	**81**
Single Family Sales: Next 6 Months	78	76	73	78	75	78	75	73	77	73	78	76	**79**
Traffic of Prospective Buyers	52	51	46	53	52	51	49	48	48	47	48	50	**58**

Source: National Association of Home Buyers

sentiment for the U.S. single-family housing market. The NAHB HMI is a widely watched gauge of the outlook for the U.S. housing sector. The index is produced from a survey which asks the NAHB's 140,000-plus members to rate market conditions. The HMI is a weighted average of three components: Single Family Sales (present), Single Family Sales (next six months) and Traffic of Prospective Buyers. The index ranges between 0 and 100, with a reading over 50 indicating more builders view sales conditions as good compared with those who view them as poor. In December, the HMI reached 74, representing the highest level in 2017. The monthly HMI has only exceeded 74 six times since 1998, when it peaked at 78. The HMI reached a low of 8 in January, 2009.

NAHB/Wells Fargo Housing Market Index (HMI) and New Single-Family Starts

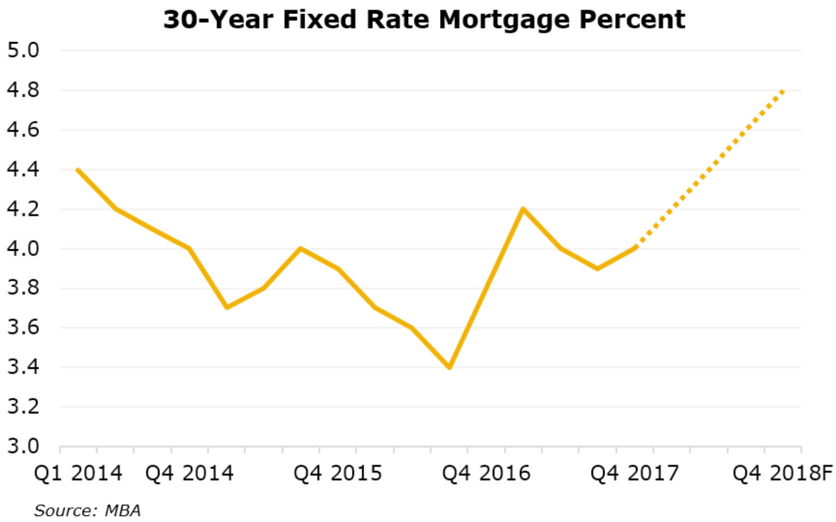


Source: NAHB/Wells Fargo Housing Market Index., U.S. Census Bureau.

Millennials Will Drive Sales

James M. Czapiga, president & CEO of Connecticut Attorneys Title Insurance Company (CATIC), also believes new home sales and housing inventory will be back up in 2018. CATIC is the 8th largest independent title insurer based on premium, and the market leader in Connecticut and Vermont. Mr. Czapiga notes that the "rise of the millennials" in home buying is one factor. According to the National Association of Realtors

(NAR), millennials are now the largest share of homebuyers. "Millennials are entering peak home-buying years, typically considered to be when consumers are between ages 25 and 45. This year, millennials are 20 to 36 years old. As they're having children, real estate experts say, millennials are moving to the suburbs, as well."[1] However, millennials are also facing a high level of student loan debt relative to their income. On the bright side, a poll by GFK Custom Research North America found 17% of parents of millennials expected to help them buy a home.



Regardless of being a millennial or not, one factor which always plays in the mix is the average 30-year fixed rate mortgage. The MBA expects the average rate to be 4.0% for year-end 2017 and then climb to 4.8% by year-end 2018. That's up from the low of 3.4% in the third quarter last year. But it's still lower than rates in the 6.5% range back in 2006. The NAR said its research indicates the median down payment for first-time buyers has been 6% for three years. The median down payment for repeat buyers has been 14% in three of the past four years.

M&A, Strategic Alternatives and Redomestications

Despite the lack of M&A among title underwriters in 2017, KBRA expects increased activity in 2018. Recent M&A activity was generally limited to agency consolidations and title underwriters acquiring title agencies. CATIC's Czapiga views this as a market play, with the acquirers seeking to increase market share through the acquisition of high volume and mostly multi-state agencies. KBRA notes many of the top independent title underwriters have been adding market share in recent years, and believes M&A could be the means to accelerate market share growth.

More noteworthy than agency acquisitions, however, was Stewart Information Services Corporation (Stewart) announcing it was considering strategic alternatives. "All options are on the table, including business combinations, a sale of the company and continued execution of our stand-alone business plan," said Matthew Morris, Stewart's CEO. This announcement came along with the release of their third quarter earnings, which were down significantly. Mr. Morris attributed the earnings decline partially due to Hurricane Harvey and declining refinancing orders.

KBRA believes that the size of Stewart could make a merger or sale within the title industry difficult. As the fourth largest title insurance group based on both premium and surplus, it could be difficult for another company to acquire them. There are already regulatory concerns that approximately 85% of the title industry's market share is controlled by the top four title insurance groups, which are comprised of thirteen operating companies. Stewart ranks behind Fidelity National, First American, and Old Republic. KBRA thinks that regulators would likely have a concern if one of the three larger groups acquire Stewart, having 85% of the market share lie within three groups.

[1] "Millennials finally embracing American Dream of home ownership", Susan Tompor, Detroit Free Press May 5, 2017

In last year's title outlook, KBRA noted the U.S. Government Accountability Office (GAO) issued a report describing certain troublesome aspects of title insurance, including a lack of price transparency and conflicts of interest among sellers. The GAO called for regulators to improve oversight, and the National Association of Insurance Commissioners (NAIC) also established a task force and working groups focused on a model guide for consumers; title insurance company reserve adequacy; and promoting competition in the title insurance market. The title insurance task force remained active at the 2017 NAIC winter meetings, continuing to focus on consumer protection, fraud and financial reporting.

On the other hand, Stewart is much larger than any of the independent title companies, which could also limit its options. However, KBRA believes Stewart could contemplate a merger of its two subsidiaries: Stewart Title Guarantee Co., domiciled in Texas, and Stewart Title Insurance Company, domiciled in New York. Like all insurance companies, title underwriters are regulated by its state of domicile. The majority of Stewart's business is regulated by Texas, which has one of the most conservative statutory premium reserve requirements in the country. If Stewarts merges its two entities and redomesticates to New York or another state, Stewart could potentially free up statutory premium reserves and allow increased premium writings.

KBRA believes redomestication is a viable option for Stewart and notes several redomestications in the title industry in 2017. Fidelity National Title Insurance Company redomesticated from California to Florida, while both Chicago Title Insurance Company and Commonwealth Land Title Insurance Company (Fidelity National subsidiaries) redomesticated from Nebraska to Florida.

Title Insurance Industry
Company Counts and Market Share

Period	# Active Companies[1]	# Group/Family Companies[2]	# Independent Companies	% Group/Family Market Share[3]	% Independent Market Share
2016	40	13	27	85.7%	14.3%
2015	41	14	27	86.9%	13.1%
2014	44	19	25	87.7%	12.3%
2013	45	18	27	88.6%	11.4%
2012	49	17	32	86.7%	13.2%
2011	52	18	34	88.2%	11.8%
2010	54	19	35	88.1%	11.9%
2009	65	30	35	90.3%	9.7%
2008	88	44	40	92.2%	7.8%
2007	94	47	37	93.0%	7.0%

Source: ALTA.Org

Notes: [1]Active companies represent underwriters with positive written premium.
[2]The numbers represented are the operating compnies within the four major title groups.
[3]Market share for 2016/2015 based on earned premium.
Market share for 2014 and prior based on written premium.

Technology and Title Insurance

As technology marches forward, KBRA believes the title insurance industry will benefit from the increase of eClosings, eMortgage and other related technology, such as blockchain. An eClosing is the partial or full electronic execution of all mortgage loan closing documents in a secure digital environment. Electronic closings enable a more efficient and streamlined closing experience for borrowers, originators, lenders, servicers, and title and real estate agents. Additional benefits include the lower potential for manual operational errors, such as missing signatures or documents, and it improves data quality and validation. With eClosings and blockchain, costs for electronic documents are typically less expensive to manage than traditional paper documents. In addition, associated shipping, copying, and storage costs are reduced. Some also contend eClosings provide additional peace of mind concerning the thoroughness of the title search, as it enhances the ability to review and approve documents prior to closing day.

One component of eClosings is eNotary services. Although regulations governing notarization of eMortgage loans is still evolving, its use will inevitably increase. In 2017, some borrowers completed their eClosings without a notary in the same room, including having an approved eNotary involved through FaceTime or Skype. DocuGuard, a provider of online documentation and closing related services contends, “Millions of dollars in claims are made every year as the result of fraudulent mortgage releases, deeds and powers of attorney acknowledged outside the presence of title company staff and lenders. The validity of documents notarized before and after settlements by parties unable to attend the closing have been an issue for decades.” DocuGuard’s objective is to end title insurance claims and mortgage lender losses resulting from notary fraud. DocuGuard records the acknowledgment of a document and makes it accessible on its website forever. DocuGuard secures evidence of who, what, where, when and what happened at the time the documents was notarized.

In summary, KBRA views the title industry Outlook as Stable. With seven consecutive years of strong net income and increased surplus, KBRA believes a few quarters of declining mortgage volumes projected by the MBA is manageable. In addition, the overall mortgage declines are largely related to refinances, with indications of new originations and new home sales increasing in 2018. Further, the industry’s aggregated PHS is more than double the PHS reported at year-end 2008 of $2.1 billion. Surplus is also up by more than 25% from the pre-crisis high of $3.5 billion at year-end 2006. Additionally, net written premium to PHS at 3.3 to 1 is favorable relative to historical levels. Lastly, KBRA believes title underwriters should experience some efficiencies through improved technology in 2018 and beyond.

Appendix A: Q3 2017 Title Insurer Statutory Filings

NAIC #	Q3 2017 Statutory Filings Company	State Of Domicile	Statutory Surplus	Year-to-Date Net Income
50814	First American Title Insurance Company	NE	$ 1,240,901,512	$ 94,345,357
50229	Chicago Title Insurance Company	FL	$ 969,592,636	$ 197,930,412
50121	Stewart Title Guaranty Company	TX	$ 561,306,008	$ 33,298,507
50520	Old Republic National Title Insurance Company	FL	$ 511,781,761	$ 86,667,449
51586	Fidelity National Title Insurance Company	FL	$ 476,989,929	$ 79,328,845
50083	Commonwealth Land Title Insurance Company	FL	$ 375,282,074	$ 30,674,926
50369	Investors Title Insurance Company	NC	$ 96,496,550	$ 9,255,130
50130	North American Title Insurance Company	CA	$ 82,791,544	$ 8,418,949
50164	BANKERS GUARANTEE TITLE & TRUST CO	OH	$ 62,687,006	$ 3,201,453
51020	National Title Insurance of New York Inc	NY	$ 53,288,268	$ 3,584,675
51420	Stewart Title Insurance Company	NY	$ 51,238,155	$ 7,012,322
50028	ACE Capital Title Reinsurance Company	NY	$ 46,660,567	$ 1,208,890
50004	Attorneys' Title Guaranty Fund, Inc. (IL) *(Q217 filing)	IL	$ 46,495,000	$ 973,000
50050	Westcor Land Title Insurance Company	CA	$ 38,745,773	$ 5,661,395
51268	Connecticut Attorneys Title Insurance Company	VT	$ 34,524,960	$ 1,137,867
11974	Amrock Title Insurance Company	TX	$ 29,192,203	$ 279,731
50016	Title Resources Guaranty Company	TX	$ 29,061,468	$ 14,227,110
51152	WFG National Title Insurance Company	SC	$ 28,078,547	$ 943,942
51411	American Guaranty Title Insurance Company	OK	$ 27,775,923	$ 3,660,925
51624	First American Title Guaranty Company fka United General Title Insurance Company	TX	$ 25,973,060	$ 7,364,792
50598	Alamo Title Insurance	TX	$ 23,128,316	$ 2,910,994
51578	AmTrust Title Insurance Company	NY	$ 19,380,070	$ 57,799
51365	American Security Title Insurance Co.	OK	$ 15,771,813	$ 610,848
51527	First American Title Insurance Company of Louisiana	LA	$ 15,591,960	$ 2,095,908
51209	Conestoga Title Insurance Co.	PA	$ 14,304,107	$ 633,179
50377	National Investors Title Insurance Company	TX	$ 12,944,453	$ 452,882
14240	First National Title Insurance Company	TX	$ 11,861,877	$ 2,673,339
51330	Ohio Bar Title Insurance Company	OH	$ 11,368,045	$ 612,042
50002	Land Title Insurance Corporation	CO	$ 9,289,872	$ 1,523,115
50026	Premier Land Title Insurance Company	TX	$ 7,898,965	$ 1,703,242
12309	Alliant National Title Insurance Company Inc.	CO	$ 7,752,621	$ 1,546,245
51632	EnTitle Insurance Company	OH	$ 6,403,010	$ (2,966,894)
NA	Title Guaranty Division of the Iowa Finance Authority (unincorporated)	IA	$ 6,314,000	$ 1,340,000
15781	California Members Title Insurance Company	CA	$ 6,155,182	$ (539,633)
50440	Real Advantage Title Insurance Company *(Q217 filing)	CA	$ 5,851,000	$ 384,000
50172	General Title Insurance Company	IN	$ 5,597,446	$ 487,171
50784	The Security Title Guarantee Corporation of Baltimore	MD	$ 5,362,195	$ 1,194,256
50001	American Eagle Title Insurance Company, Inc *(Q217 filing)	OK	$ 4,954,000	$ 624,000
11865	Arsenal Insurance Corporation	IN	$ 3,980,017	$ 784,005
12522	Agents National Title Insurance Company	MO	$ 3,734,873	$ (13,761)
12600	ARIS Title Insurance Corporation	NY	$ 3,535,037	$ (745,356)
12591	Sierra Title Insurance Guaranty Company	TX	$ 3,481,433	$ 196,370
15305	Southwest Land Title Insurance Company	TX	$ 3,459,323	$ 33,373
50261	The Title Guaranty & Trust Company of Chattanooga	TN	$ 3,112,122	$ 370,235
16169	National Consumer Title Insurance Company	FL	$ 2,989,286	$ (16,233)
50020	DAKOTA HOMESTEAD TITLE INSURANCE COMPANY	SD	$ 2,974,203	$ 89,545
51560	Attorneys Title Guaranty Fund Inc.	CO	$ 2,848,690	$ 438,014
	TOTAL INDUSTRY TOTALS Excluding Eliminations		$ 5,008,906,860	$ 605,654,362
	Estimated Eliminations		$ 580,000,000	$ 50,000,000
	Title Industry		$ 4,428,906,860	$ 555,654,362

Source: Company NAIC Filings

Note: NAIC filers with greater than $2 million in statutory surplus. Exlcudes 8 companies with less than $2 million in surplus.

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