

Mossberg's Investor Digest

Best Idea Profile:

Hallmark Financial Services (NYSE:HALL)

DESCRIPTION:

Headquartered in Fort Worth, Texas; Hallmark Financial is a diversified property/casualty insurance group that serves businesses and individuals in specialty and niche markets. The Company offers standard commercial insurance, specialty commercial insurance and personal insurance in selected market subcategories that are characteristically low-severity and short-tailed risks. Hallmark focuses on marketing, distributing, underwriting and servicing property/casualty insurance products that require specialized underwriting expertise or market knowledge. The insurance policies Hallmark produces are written by its five insurance company subsidiaries as well as unaffiliated insurers.

KEY INVESTMENT CONSIDERATIONS:

Proven Track Record – Started as a “Texas only” mono-line insurer in 1990, Hallmark Financial has a proven platform and a successful track record of operating results and expansion. Since 2004 the Company has expanded into 4 to 5 states per year and has added a number of new business lines. Hallmark has consistency run an efficient and disciplined organization with efficiency ratios in the low 20's and a 5 year growth rate of book value of 15%.

ROE – Hallmark has a record of delivering a strong ROE for investors. From 2006 through 2010 the Company had an average ROE of 10.4%.

Opportunistic Entry Point – Hallmarks performance has been severely impacted by the Company's 2009 entrance into the Florida personal lines market. Losses increased in FY2010 due to lower production and widespread claim fraud. For the Q1FY2011 Hallmark reported an \$11.2 million net loss. Hallmark reported that \$9.7 million of this loss was a result of adverse prior year loss reserve development in the Personal Lines Segment in Florida. Hallmark has addressed the problems in Florida by hiring additional senior claim managers and increasing premiums. The Company also hired Paul Harrison, former president of Imperial Fire and Casualty Insurance Company as its Personal Lines business unit Chief Operating Officer. Also, Hallmark's Florida exposure should be dramatically reduced. Hallmark reports that out of the net premiums written in Florida, just \$3.5 million remained in unearned premium reserves as of March 31, 2011, and Hallmark expects this remainder to run-off by the end of this year. During Q2FY2011 Hallmark suspended all new business in Florida.

Share Buyback Program – Hallmark repurchased 875,712 shares or 4.5% of its outstanding common stock for a total cost of \$6.4 million during the second quarter to date, including shares purchased subsequent to quarter end. Since inception of the company's buyback program, total shares repurchased are 1.6 million or 8% of outstanding common stock. The total cost of shares repurchased to date is \$11.7 million or \$7.17 per share, equivalent to 64% of Hallmarks second quarter book value per share of \$11.23. There are approximately 2.4 million shares remaining authorized under the company's current stock buyback program.

Growth Opportunities – With the exception of its Florida problems, Hallmark has strong metrics and has delivered strong results for its investors. The company's high efficiency niche product line platform has demonstrated merit and the company has opportunities to grow with new products lines in a number of new states.

VALUATION

Hallmark Financial currently trades for \$6.68 per share which equates to a 41% discount to book value. As the Company reports more normalized returns the stock should experience a narrowing discount to book value.

(Hallmark Financial : NASDAQ:HALL)

Investment Data (as of 8/26/11)

Recent Price	\$6.68
52-Week Range	\$6.32 - \$9.64
Fiscal Year End	Dec
Dividend	NA
Yield	NA
Shares Outstanding	19MM
Average Trading Volume (3 mos)	55.4k
Market Capitalization	\$129MM
Cash	\$51MM
Long Term Debt	\$59MM
Enterprise Value (EV)	\$137MM
BV/ Share	\$11.23
TTM Revenue	\$311MM
P/ Revenue	\$0.4x
TTM EPS	\$(0.49)
P/ EPS	NA
TTM EBITDA	NA
EV/ EBITDA	NA

We attempt to provide subscribers with reasoned opinions based on our analysis of publicly available information from sources believed to be reliable, but make no representations as to its accuracy or completeness. Best Idea profiles are not based upon individual needs of subscribers nor are they an offer to buy or sell securities. Additional disclosures can be found under the Disclosures portion of the Mossberg's Investor Digest website.