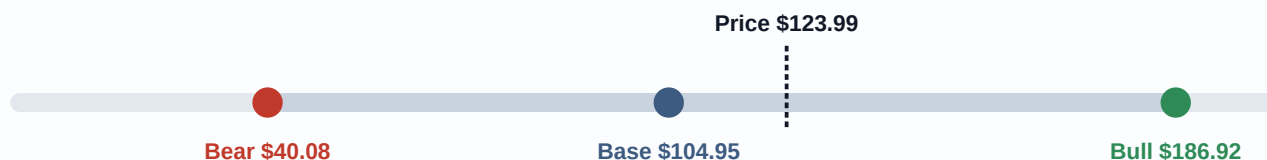


Initiated 2026-09-28 · Price \$123.99 (close 2026-09-25, stockanalysis.com) · Mkt cap \$3.25bn · Financials / specialty P&C insurance · Model: verified

Rating: Hold — Conviction: Low

Palomar is compounding fast: Q2 gross premium +27%, adjusted ROE 26%, and 2026 adjusted net income guidance raised to \$270–280mm. But earnings quality is slipping: commercial earthquake rates fell more than 20%, and growth comes from lower-margin crop, casualty and acquired surety. The stock looks cheap only on adjusted earnings, which exclude stock pay, intangible amortization and cat-bond costs. On GAAP it trades at ~16.7x trailing EPS and 3.3x book. The model's base case sits below the price, which rules out a Buy. Reported underwriting is still well inside the model's fade, so not a Sell. Conviction is Low.

MODEL VALUE RANGE VS PRICE



Business overview

Palomar writes specialty property and casualty insurance, mostly in the US. Q2 2026 gross written premium was \$630.5mm:

- **Casualty: \$197.5mm (31%).**
- **Inland marine and other property: \$169.7mm (27%).**
- **Earthquake: \$146.6mm (23%).** About 64% of the earthquake book is residential.
- **Crop: \$77.4mm (12%).**
- **Surety and credit: \$39.2mm (6%).** This is mainly The Gray Casualty & Surety Company, bought on 2026-01-31 for ~\$314mm with a new \$300mm term loan.

Palomar reinsures heavily: Q2 net written premium was 52% of gross. It carries \$3.92bn of earthquake limit above a \$20mm retention. Earnings turn on three things: earthquake and layered-property pricing, the mix shift toward lower-margin lines (the loss ratio was 33.9% in H1 against 24.7% a year earlier), and reinsurance cost.

Competition

- **Rivals.** In earthquake and E&S property: the Lloyd's market, Kinsale, RLI and, in residential, the California Earthquake Authority.
- **Where pressure shows first.** It is showing in price. Large commercial earthquake rates fell more than 20% in Q2 and layered property 16%. Residential earthquake held, with 96% retention (Q2 call, August 2026).

- **Valuation.** On stockanalysis (2026-09-28), Kinsale trades at 3.70x book and 15.5x forward earnings, Skyward at 1.92x and 10.5x, and RLI at 2.92x and 20.9x (RLI's forward figure is distorted by gains in the base year). Palomar trades at 3.31x book and 11.4x forward (adjusted consensus EPS).

Bull case

1. **Diversification compounds.** Casualty GWP rose 36.8%, crop guidance went to more than \$400mm (from ~\$320mm), and Gray Surety GWP rose 236% in its first full quarter. The "Palomar 2X" plan aims to double earnings while keeping ROE above 20%. Plays out if casualty and surety keep growing faster than earthquake shrinks. *Model: npe_growth*
2. **Underwriting discipline holds.** Management expects a mid-70s adjusted combined ratio for 2026 and renewed 14 treaties at "better or existing economics". It says it will "sacrifice premium for profitability". Plays out if earthquake pricing bottoms, as the CEO suggests, and cat losses stay near the \$8–12mm guide. *Model: combined_ratio*
3. **Float earns more.** Net investment income rose 49% in Q2, to a ~5.0% annualized yield on a portfolio that grew 25% in H1. Plays out if the 10Y stays near 5%. *Model: investment_yield, ia_growth*

Bear case

1. **Earthquake and property pricing keep falling.** Property is ~50% of the book. Commercial earthquake is already down more than 20% and layered property 16%, and management calls some new business sub-technical. Plays out if 2027 reinsurance and primary rates fall again. *Model: npe_growth*
2. **The mix gets worse.** Crop runs at ~100% net combined ratio. Casualty is unseasoned (84% IBNR) and growing 37%. The GAAP combined ratio already rose 7.7 points, to 83.8% in H1. Plays out if casualty develops adversely as it seasons. *Model: combined_ratio*
3. **Tail and reinsurance risk.** One large California earthquake would test the reinsurance tower and reprice it. The 0.38 beta does not capture that. *Model: cost_of_equity*

Valuation & balance sheet

Metric (definition)	Current	Own history (range or 5y avg)	Peers	Source, as-of
P/B (book \$37.46/share, June 2026)	3.31x (P/TBV ~4.4x on \$744mm tangible book)	\$15.37–\$35.54 BVPS FY2022–FY2025	KNSL 3.70x · RLI 2.92x · SKWD 1.92x	stockanalysis.com, 2026-09-28; Q2 release
Forward P/E (stockanalysis consensus, adjusted)	11.4x (12.2x on guidance midpoint \$275mm ÷ 27.06mm)	GAAP trailing 16.7x	KNSL 15.5x · RLI 20.9x · SKWD 10.5x	stockanalysis.com, 2026-09-28
Combined ratio (GAAP / adjusted)	83.8% / 76.3% H1 2026	76.1% / 70.9% H1 2025	n/a (unverified)	Q2 2026 release
ROE (TTM, GAAP)	22.2%	adjusted 26.3% Q2 annualized	KNSL 30.3% · RLI 25.2% · SKWD 17.3%	stockanalysis.com, 2026-09-28

Model-implied value range (from `model-summary.json` ; insurer module, residual income and justified P/BV, midpoints): Bear \$40.08 · Base \$104.95 · Bull \$186.92 per share, i.e. implied returns of –67.7% / –15.4% / +50.8% vs \$123.99. *These ranges show how the bull and bear drivers translate into value; they are not price targets.*

- **What the price implies.** It sits about a quarter of the way from base to bull. The market pays for margins holding near H1 levels rather than the base case's ~5-point fade.
- **Re-rating.** The two methods agree within 2% (residual income \$105.54, justified P/BV \$104.36). The base embeds a de-rating: a justified ~3.0x FY2025 book (\$34.84/share, est. as $\text{value}_b \div \text{FY0 book per share}$) against 3.56x today on the same book, a ~16% de-rating.

- **Tail.** A harsher case was run on a scratch copy, reflecting a pricing collapse plus an event year: NPE +30% / –5% / –5% / 0% / +3%; combined ratio 88%, 95%, 100%, 97%, 95%; investments flat after Y1; a 4.0% yield; and an 11% cost of equity. It gives \$14.67 (–88.2%).
- **Why Hold and not Sell.** The base-case fade is a forecast, not an observation. Palomar has beaten consensus EPS for 15 straight quarters and raised guidance again in Q2. The Q2 buyback averaged ~\$111, below today's price, so it says nothing either way.

Balance sheet:

- Debt: a \$295.8mm unsecured term loan (closed January 2026, amortizing quarterly). Its rate and final maturity are n/a (unverified); the model uses ~5.4% and 2031 (est.).
- Leverage: debt is 1.1x FY0 pre-tax earnings plus interest, and ~22% of debt plus book. Coverage is 16.9x.
- Cash and revolver: \$62.7mm of cash and a \$150mm revolver.
- Ratings: n/a (unverified).

Model note: tier **full**, status **built**, verification **verified** (LibreOffice recalculation matched all 2,846 formula cells). No assumptions without basis. Scenario consistency is **OK** on all 14 rows; S4's effect was corrected from + to ± after the model showed the cost-of-equity drag outweighs the yield gain.

- **Unverified inputs:** none flagged; the term-loan coupon and maturity are estimates affecting only credit figures.
- **Combined ratio.** The model runs ~3 points below GAAP, because intangible amortization (~\$37mm a year) is non-cash and runs off. Stock compensation and cat-bond expense stay in.
- **EPS.** Base Y1 EPS of \$7.78 sits 23% below the \$10.10 consensus, for two reasons. Consensus and guidance are adjusted: they exclude stock compensation (~\$32mm a year), intangible amortization, transaction and cat-bond costs, and gains. The model also projects no investment gains.

Scenario stress test

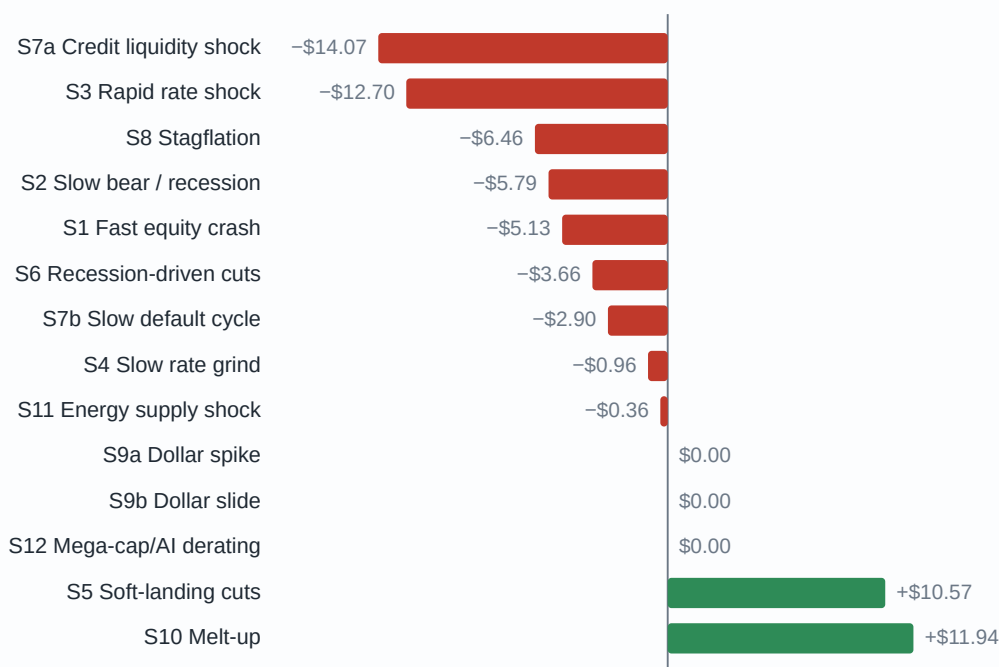
Reasoned from the bull/bear drivers above. The model column comes from the scenario overlays (Base case + shock).

Scenario	Effect	Mechanism	Magnitude	Model Δ value vs Base (\$/sh)
S1 Fast equity crash	–	Risk-premium spike; mostly fixed-income portfolio; no operating channel	Low	–\$5.13
S2 Slow bear / recession	–	Builder's risk and commercial exposures shrink, yields fall, surety losses rise. Much milder than Base – Bear (\$64.87) because the bear case is a pricing and reserve cycle, and recessions do not cause earthquakes or crop losses	Low	–\$5.79
S3 Rapid rate shock	±	Higher reinvestment yields vs a higher cost of equity; AOCI mark not modeled	Med	–\$12.70
S4 Slow rate grind	±	Higher reinvestment yields roughly offset by a higher cost of equity	Low	–\$0.96
S5 Soft-landing cuts	±	Lower yields vs a lower cost of equity	Med	+\$10.57
S6 Recession-driven cuts	–	Yields fall and the insured base shrinks	Low	–\$3.66
S7a Credit liquidity shock	–	Risk-off; bond marks proxied in a higher cost of equity	Med	–\$14.07
S7b Slow default cycle	–	Contractor defaults hit the Gray surety book; portfolio credit losses	Low	–\$2.90
S8 Stagflation	–	Replacement-cost inflation on property and builder's risk, and casualty loss trend, outrun pricing	Low	–\$6.46
S9a Dollar spike	0	No material effect, not modeled; domestic insurer	Low	\$0.00
S9b Dollar slide	0	No material effect, not modeled	Low	\$0.00

Scenario	Effect	Mechanism	Magnitude	Model Δ value vs Base (\$/sh)
S10 Melt-up	+	Risk appetite lowers the cost of equity	Med	+\$11.94
S11 Energy supply shock	-	Motor truck cargo and crop input costs; small	Low	-\$0.36
S12 Mega-cap/AI derating	0	No material effect, not modeled; fixed-income portfolio, no tech exposure	Low	\$0.00

No scenario moves base value by more than ~14%, so nothing is labelled High. **Currently active/on watch per the playbook:** S3 is partially active per `state.md`, and the macro log records all three legs crossed (10Y 5.17% on 2026-09-25). S8, S10 and S11 are on watch.

MODEL VALUE CHANGE VS BASE, BY SCENARIO



What would change the call

Upgrades if:

- The GAAP combined ratio holds at or below 84% through Q4 2026 as crop and casualty grow; or
- Management reports commercial earthquake rates stabilizing at the 2027 renewals; or
- The price falls toward the base case with guidance intact.

Downgrades if:

- Casualty shows adverse prior-year development; or
- The January or June 2027 renewals bring another double-digit earthquake rate cut; or
- 2026 adjusted net income lands below the \$270mm low end.

Watch items

- **W1:** GAAP combined ratio and loss ratio, against 83.8% and 33.9% in H1 2026. Source: Q3 2026 release (early November 2026). *Model: combined_ratio*
- **W2:** Earthquake GWP growth and commercial rate commentary, against >20% commercial rate declines in Q2. Source: Q3 and Q4 2026 calls. *Model: npe_growth*
- **W3:** 2026 adjusted net income against the \$270–280mm guide. Source: Q4 2026 release (February 2027). *Model: none*
- **W4:** Casualty prior-year development and IBNR share (84% in Q2). Source: Q3 2026 10-Q. *Model: combined_ratio*

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Independent single-name research. Directional characterization, not a price target, execution instruction, or portfolio recommendation.