Taking Stock: Markel a marvel

by Malcolm_Berko

Dear Mr. Berko: Please tell me about Markel Insurance that sells for $449 a share. I'd like to buy 30 shares as a long-term investment. My broker/brother says it's like a mini-Berkshire Hathaway in the style of Warren Buffet. But I need your recommendation and thoughts in helping me decide to invest $15,000 here.

N.R.

Bend, Ore.

Dear N.R.: Markel Corp. (MKL-$449) is home ported in Glen Allen, Va., sandwiched between the dreamy, poetic American towns of Mechanicsville and Ashland. This bucolic thorp of 13,000 American's has 6,000 homes with good schools and libraries. Glen Allen boasts two Marriotts, a drive-in movie, several McDonald's, a bowling alley and 610 homes posted on the Multiple Listing Service. Glen Allen feels like a good place to raise children, to be one of the 2,000 MKL employees, raise a family, own a house with a white picket fence, bring a covered dish to the annual American Legion picnic, celebrate the 4th of July and March in the Labor Day parade.

MKL has been in the specialty insurance business since 1930, came public in 1986 at $10 and the stock has never split. It first broke the $100 price barrier in 1997 and in the last dozen months its stock price ranged between $450 and $554 a share. There are only 10 million shares outstanding so MKL is considered a mid-cap stock with a market capitalization of $4.7 billion.

MKL underwrites specialty insurance products and programs for almost every specialty and niche market. MKL sells coverage that competitors are reluctant to insure.

For example, its excess and surplus lines (58 percent of premiums) insure bars, skating rinks, restaurants, product liability, public toilets, animal shelters, fitness centers, private schools, movie theaters, professional liability (physicians, dentists, lawyers, architects, engineers, etc.). The specialty admitted market (13 percent of premiums) writes property and casualty insurance on yachts, summer camps, sports camps, snowmobiles, earthquake coverage, horse farms, floods, motorcycles, parades, etc. And MKL writes business on both direct and subscription basis in the London market, which accounts for 29 percent of premiums.

Management seeks small markets with low annual premiums and avoids competing with the big boys like American International Group, Chubb, Travelers or Marsh McLennan. MKL's unique success is an extensive "specific knowledge" database enabling the company to underwrite unusual risks that are unattractive to the giants. MKL has quite an impressive proprietary database on myriad risk scenarios that the competition would

be hard-pressed to duplicate.

Meanwhile, management continues to build its presence in the London market, which is the second-largest insurance market in the world, and from which it expects to earn significant revenue growth over the next dozen years. MKL believes it should earn $34.50 in 2007 and due to an expected flat premium market in 2008 MKL believes its earnings will come in a bit lower at about $33.25 a share.

Book value has increased in 15 of the past 17 years and this year's book is expected to come in at $290 a share, up from 2007's $260. Most specialty insurers usually trade at two times book. And KeyBanc Capital Markets rates MKL a "BUY" with a price target of $600 in the next 12 months. I think KeyBanc may be a bit too sanguine, but since some of our aggressively managed accounts have owned MKL for a few years, I'll take it.

Still MKL is an unusual company. Its management is encouraged to be spontaneous - "let's hear what you think" or "do it now" rather than "give me a written analysis" or "let's plan in stages." The MKL people are a different breed; they abhor bureaucracy but respect authority. They're flexible, imaginative and encouraged to take the initiative.

Perhaps that's why MKL also has impressive successes in its private equity investments. It owns interests in various small businesses such as First Market Bank, AMF Bakeries and Terra Nova to name a few. MKL will continue to acquire well-researched, independent companies for its private equity portfolio. MKL will provide private capital when necessary and allow current management to continue their successful ways. Not quite up to Berkshire Hathaway numbers, but getting there.

I don't have a single objection to a 30-share purchase providing you intend to keep MKL for at least 10 years. Imagine owning Berkshire Hathaway in 1997 at $35,000 a share; today it's trading at $143,000 a share. Since coming public at $10 in 1986, MKL stock has outperformed the Dow by almost 100 percent with an average annual stock return of 21 percent. And if the past is prologue, this might give you some dandy returns by 2018.

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