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Greetings. And welcome to First American Financial Corporation First Quarter 2020 Earnings Conference Call. (Operator Instructions) A copy of today’s press release is available on First American’s website at www.firstam.com/investor. Please note the call is being recorded and will be available for replay from the company’s investor website and for a short time, by dialing (877) 660-6853 or (201) 612-7415, and you’ll enter conference ID 13701584.

We will now turn the call over to Craig Barberio, Vice President of Investor Relations, to make an induction and -- oh my gosh, an introductory statement.

Craig Barberio First American Financial Corporation - Director of IR

Good morning, everyone, and welcome to First American’s Earnings Conference call for the First Quarter of 2020. Joining us today will be our Chief Executive Officer, Dennis Gilmore; and Mark Seaton, Executive Vice President and Chief Financial Officer. Some of the statements made today may contain forward-looking statements that do not relate strictly to historical or current fact. These forward-looking statements speak only as of the date they are made, and the company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made.

Risks and uncertainties exist that may cause results to differ materially from those set forth in these forward-looking statements. For more information on the risks and uncertainties, please refer to this morning’s earnings release and the risk factors discussed in our Form 10-K and subsequent SEC filings.

Our presentation today also contains certain non-GAAP financial measures that we believe provide additional insight into the operational efficiency and performance of the company relative to earlier periods and relative to the company’s competitors. For more details on these non-GAAP financial measures, including presentation with and reconciliation to the most directly comparable GAAP financials, please refer to this morning’s earnings release, which is available on our website at www.firstam.com.

I’ll now turn the call over to Dennis Gilmore.
Good morning, and thank you for joining our call. Today, I will comment on First American’s response to the pandemic and its impact on our business. Mark will comment on our first quarter earnings, financial expectations for 2020 and capital management.

Throughout the pandemic, our first priority has been to keep our employees and their families safe. Early in the process, we activated our business continuity plan, which includes giving our employees the ability to work from home. Today, the vast majority of our workforce is working remotely. For those who do come to the office, we are taking extra precautions and following CDC guidelines. Consistent with our people first philosophy, we have committed to our employees that we will not make any layoffs through the end of the second quarter. We strongly believe that this is the right approach given these unique circumstances. We’ve taken a long-term perspective, and although this action will negatively impact our short-term results, we believe the benefits to our people, our customers and ultimately, our shareholders will be worth the investment. However, if the economy continues to deteriorate for an extended period, we will review all measures to control expenses as we have done consistently in the past.

Our second priority has been to maintain service levels to our customers. The settlement services we provide are critical, and we have been deemed in essential service across nearly all states. Individuals, businesses and lenders need title and closing services for the transfer of real estate or to secure a mortgage, and we have worked tirelessly to maintain business continuity despite the disruption caused by the pandemic.

We’ve experienced minor disruption to our operation when the stay-at-home orders were first announced, but those issues were quickly resolved. These stay-at-home orders have come at a time when refinance volumes are surging, amplifying the strain on the industry.

Throughout 2019, we have launched a number of automation efforts, leveraging our deep data assets, including clear to go, an engine designed for our central refinance channel that has been expanded to our branch and agency operations covering a significant portion of our refinance transactions. This has helped us increase productivity and manage service levels at a time when volumes have soared. We will continue to focus on the advancement of numerous automation efforts across the business.

I’d like to shift gears now and discuss the current market environment. Our purchase business was off to a strong start in 2020 until mid-March when orders fell sharply. For the first 3 weeks of April, open purchase orders are down 43% relative to the same 3 weeks of 2019. We’ve seen west coast markets decline approximately 50%, while other places such as the midwest have fallen only 35%. The good news is, although orders have fallen severely, they appear to have stabilized. The 43% drop we are currently experiencing has been consistent since the beginning of April, and it appears we’ve reached a floor.

For the first 3 weeks in April, refinance open orders have averaged 3,000 per day, up 120% over last year. This strong volume is serving as a natural hedge to our declining resale business. So far in April, revenues in our commercial business have dropped sharply, down 44% from the same period of 2019.

Commercial transactions in industries such as retail, hotels, multifamily have slowed considerably due to the uncertainty of underlying cash flows. In other areas of our business, low mortgage rates have triggered strong growth in volumes. Our data business has benefited from strong demand as refinance volume has more than offset the decline in purchase. Our Docutech acquisition, which we closed March 2, has seen transaction volumes up over 150% compared to 2019. Docutech advances our ability to provide lender customers with end-to-end digital mortgage and settlement services. The events of the last few weeks have accelerated the adoption curve for eClose and First American is well positioned for this industry change. Our home warranty business continues to perform well.

With purchase transactions declining, we continue to focus on the direct-to-consumer channel as well as policy retention efforts. Our revenue growth is in line with our expectation, and we have seen a slight reduction in loss rate.

Regarding title claims, we have not seen any increase in incurred claims. However, since the current economic conditions could result in an increase in claims, we have elected to raise our title loss provision rate to 5% this quarter. We continue to have a strong reserve position on our balance sheet, and Mark will comment on the title loss provision rate in detail in his comments. Our team is rising to meet the challenge of providing great...
service to our customers, and we believe customers increasingly want to do business with a company that’s built to last. We entered this crisis with a strong balance sheet, and we can put our capital to work in this market by continuing to fund our innovation efforts and by making opportunistic investments when others can’t.

For the last several years, we have been on a journey to digitally transform our business, and the recent events have validated that our strategic path is the right one. We will continue to expand our data assets, further automate our title production and continue to digitize our closing process. While we don’t know when business will return to normal, we are confident that we will emerge in an even stronger leadership position when it does.

I’d now like to turn the call over to Mark.

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Thank you, Dennis. I’ll comment on our first quarter earnings, financial expectations for 2020 and capital management. In the first quarter, we earned $0.55 per diluted share. Excluding net realized investment losses of $65 million, primarily related to a decline in the value of equity securities, we earned $1.06 per diluted share.

In the title segment, pretax margin was 5.6% or 10.3% excluding net realized investment losses. To date, we have not seen an uptick in claims as a result of the current market environment. In fact, claims were significantly below our expectation in the first quarter of 2020. Our incurred title claims in the first quarter were 26% below our actuarial expectation and 6% lower than prior year. However, title claims generally increase when economic conditions deteriorate. We don’t expect our loss rate to approach the levels experienced from 2005 to 2008, but we do expect some increase in claims. It’s quite possible that since we entered 2020 in such a strong reserve position, that existing reserves will be adequate to cover this expected increase in claims. But given market uncertainties, we believe it’s prudent to raise the loss rate to 5%. Our current expectation is to maintain a 5% loss rate until we have more visibility into how the current environment will affect our claims experience.

Turning to the Specialty Insurance segment. Pretax margin was 10.5% or 13.0%, excluding net realized investment losses. Both the home warranty and property and casualty business lines achieved lower claim loss rates leading to a decline in the overall loss rate for this segment to 52% this quarter compared with 55% in the prior year.

First American has not traditionally provided guidance to investors. However, in this uncertain environment, we wanted to provide our internal expectations for 2020. Our forecast can be volatile and key assumptions are likely to change as the year progresses. The forecast is not a goal or financial objective but rather our most recent projection for 2020. We are projecting a 45% year-over-year decline in open purchase orders in the second quarter with a gradual improvement in the second half of the year.

We also expect refinance orders to remain elevated throughout 2020. This implies a mortgage origination market of $2.8 trillion in 2020, comprised of $2 trillion refinance and $800 billion purchase. Our investment income will decline sharply in the second quarter given the 150 basis point decline in the federal funds rate in March. We expect investment income in our title segment to be in the range of $40 million to $45 million per quarter. For our commercial business, we expect a 50% decline in revenue in the second quarter, with a gradual improvement for the remainder of the year.

Using these assumptions, we expect title pretax margin to be between 9% to 11% in 2020, excluding net realized investment gains and losses.

Next, I’ll comment on our liquidity and capital position. We have $420 million available on our $700 million line of credit. Borrowing on our line of credit increased $120 million in the first quarter to partially fund the Docutech acquisition. Today, we have $153 million of cash at the holding company, with an additional $506 million of dividend capacity available from our regulated subsidiaries for the remainder of 2020.

Our debt-to-capital ratio was 23% as of March 31. This provides us with nearly $1.5 billion of potential debt capacity with $420 million readily available on our line. None of our long-term debt is due until 2023. So we have ample financial flexibility at our holding company. If debt market conditions are favorable, we will consider terming out the outstanding amount on our line of credit to take advantage of the low rate environment.
The investment portfolio at our insurance companies totaled $3 billion as of March 31. Of this amount, 87% are debt securities and 13% are equities. Of the debt securities, 46% are government-backed treasuries, agency mortgages and agency bonds. The average credit rating of the portfolio was AA-. We have just 4% of the debt securities portfolio rated below investment grade, and we have no CLOs or non-agency mortgage-backed securities.

The investment portfolio at our bank totaled $3.4 billion as of March 31. Of this amount, 100% are debt securities with 78% of the securities being government backed. The average credit rating of the portfolio is AA+. On a consolidated basis, the value of our investment securities has rallied since the beginning of the year. And we were in an unrealized gain position of $95 million as of March 31. Given the forecast I described earlier, we expect to add to this already strong financial position. But if we're wrong and the market takes a turn for the worse, we have ample liquidity and a strong capital position to lean on.

Given the price of our stock, our long-term optimism of the business and our strong capital position, we elected to repurchase shares in the first quarter.

We repurchased 1.7 million shares at an average price of $38.64, representing 1.5% of our shares outstanding. Our strong balance sheet gives us the ability to play offense in this market. We'll continue to be opportunistic with acquisitions and make organic investments that accelerate our digital transformation.

I would now like to turn the call back over to the operator to take your questions.

**QUESTIONS AND ANSWERS**

**Operator**

(Operator Instructions) Our first question comes from the line of Jack Micenko of SIM (sic) [SIG].

**John Gregory Micenko - Susquehanna Financial Group, LLLP, Research Division - Deputy Director of Research**

Jack Micenko, SIG. First question on the loss ratio increase. You make sense historically.

I'm curious how much thought was given to the forbearance plans that have been rolled out in at least 6 months of relief before we start seeing defaults? And maybe a little bit of context around where title-only claim rates were in the ’08, ’09 window, I know it’ll be a combined loss ratio, but I was curious that I couldn’t seem to find the title only loss ratio out of a financial crisis sense.

**Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director**

Okay. This is Dennis, and I'll start, and Mark will come back on the second part of that question. You're right. With the current forbearance plans, we don't expect to see any material change in default rates for a minimum of 6 months, potentially even a year. So we think the market will be pretty stable right now from a default rate perspective. If we see any deterioration, it will probably be in the second or third quarter of 2021, actually. And so we're just taking a cautious approach on this right now. And I should also point out to you, we're entering this process as strong as we've ever been. Our quality of our books' very high, high equity.

So I think it's the right move going forward, but it's a cautious move right now.
And in terms of the title loss ratios back in '05 to '08 in terms of our title segment, they were generally between 10% and 13% but the worst year we had was '07, it was about 13%. And '05 through '08 were somewhere around 10%, 11%. And there's obviously a lot of reasons why we don't think it's going to approach those levels.

And then a side question, how much of the $208 million of revenue was provided by Docutech for the stub month of the quarter?

Yes. I'll start with Docutech. So we closed Docutech like the first couple of days in March. And so in the quarter, we had $6.4 million of revenue related to Docutech, really just 1 full month in that. All that revenue was in our information and other line item. So you really got 1 month of Docutech revenue in the quarter.

And just in terms of the acceleration of digital title and closing, yes, that's something that we've been really investing in heavily, both on title automation as well as making our closing process, our escrow process more digital. And the interesting thing is we've invested heavily in those 2 things, and we think these events that have happened in the last several weeks are really going to accelerate that adoption. So we just see it increasing over time, and we're well positioned to capitalize on that trend.

I wanted to start with the agent channel. I recognized the investments you've made in being able to handle the current operational environment. I was wondering if any smaller agents are -- how they're dealing with the current stay-at-home orders, disruptions, who might not have nearly the investment capacity as you?

I think what we're going to see on that, it's going to be really a mix all over the board, depending on how people go into the crisis. So it will just depend, and we'll partner very closely with our agents. I mean, overall, for our perspective, we're going into this situation stronger than we've ever been. So we're fairly confident with how we're going to come through this process.

Yes. I was wondering if maybe you would see more shift to direct if there are disruptions in the agent channel.
**Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director**

Probably not, but I think it will probably create some interesting opportunities for acquisitions going forward. From a capital deployment standpoint, I think there’s a lot of really interesting opportunities probably that will present themselves over the next 12 or 15 months.

**Edward Christopher Gamaitoni - Compass Point Research & Trading, LLC, Research Division - MD & Head of Research**

And on that acquisition, is it -- I mean, besides the normal tuck-in, is it most or mostly on the data side?

**Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director**

Both data and tuck-in on the title side, yes. So again, I mean, assets have been pretty pricey coming into the situation. So it’s a really good situation we have coming into this with such strong liquidity. I just think, again, I think there are going to be great opportunities coming forward over the next 12 to 15 months.

**Edward Christopher Gamaitoni - Compass Point Research & Trading, LLC, Research Division - MD & Head of Research**

Okay. And I fully acknowledge the commentary you gave about maintaining personnel for the second quarter. I was wondering how this situation impacts planned investments, other spend that will be in the other operating line item and how you’re managing more fixed cost or investment spend rather than personnel?

**Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO**

Generally speaking, I would say the other operating expenses are just coming down. Obviously, we’re traveling a lot less these days. In the second quarter, we did have some, I would say, unusual items and just in terms of -- right when the pandemic broke, I mean we rushed to buy as many laptops as we could for employees to enable them to work from home. So we had about $6 million of IT-related expenses, mostly laptops. And we also had about $4 million of professional services related to the Docutech acquisition that hit this quarter.

But generally speaking, we do have some flex in OpEx.

Our next questions come from the line of Bose George of KBW.

**Bose Thomas George - Keefe, Bruyette, & Woods, Inc., Research Division - MD**

Okay. Great. Sorry, messed my headphones. So thanks a lot for the margin guidance. I think it was very helpful given all the volatility out there. So a couple of questions related to that. First, the $2.8 trillion, that’s like the NBA, I think, is around $2.4 trillion. So is that based on your sort of your internal forecast for the market? And then secondly, the 9% to 11% margin you guided to, is a variance there on what happens on the revenue side or on the expense side? Or just curious as to what’s driving that range?

**Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director**

Well, this is Dennis. Let me start on the forecast. I think we’re going to continue to see a lot of volatility on that number from a lot of angles to it. So right now, that’s our best estimate. But let me kind of tell you what’s happening in the market. I think it’s important. Right when the original stay-at-home orders were put in place, we saw a remarkable decline in volumes on the purchase side, for example. In some markets, 60-plus percent and in some markets, more in the 30% range. What we’ve seen probably more importantly right now is over the last 3 weeks, it’s our call right now.
We've not only hit a bottom or a floor, if you will. We're actually starting to see trend back upwards. So no question, purchase will be difficult in the second and third quarter. We're forecasting right now the purchase will be down 45%. But I think, again, and optimistically, potentially could even do better than that.

And then the other part of that forecast is our refinance volumes. And we ended the quarter really hot on refinance volumes. We had a few days over 4,000 orders per day. Right now, we're averaging 3,000 orders per day. To put that in perspective, we're up well over 120% from a year ago.

And so again, I think on the refinance, probably the most volatile part of the forecast, what we're seeing right now is the mortgage market settling down. They're getting more clarity. We'll probably see additional capacity coming into the market. So what I expect to see is refinance will stay at around that 3,000 or accelerate going forward. And I'll tell you, we're well suited to handle that right now. So long answer, I think the forecasts are going to be volatile, but we're pretty optimistic with what's happened, looking forward right now.

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Okay. And Bose, just a follow-up on the mortgage origination. So the NBA is at $2.4 trillion, and we're at $2.8 trillion, but the mix is very different. So I mean we're seeing our refinance volumes more than double, which is way higher than what the NBA is. And also on the purchase side, the NBA had purchased down 2% this year, and we're obviously seeing a much bigger drop in that.

So we basically -- we kind of look at our order forecast, and we project out what we think is going to happen for the year, and then we kind of translate that into a mortgage origination environment. So that's how we come up to $2.8 trillion.

Bose Thomas George - Keefe, Bruyette, & Woods, Inc., Research Division - MD

Okay. That makes sense. And then just on the margin. I mean, obviously, there's a lot of volatility, so I'm not asking anything more precise, but just curious what's kind of driving the that range?

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Well, the range -- we -- again, as Dennis said, the forecast is so volatile, especially in this market. But given everything we know today, given all the assumptions that we outlined, we're coming in at somewhere between a 9% to 11% margin. Now last year, we were at 15%, but obviously, the environment has changed. Investment income is following but the Fed fund is 0 and between the decline in commercial and purchase that we expect and the strength in refinance. And that also includes a loss ratio of 5% for the rest of the year now. We don't know if that's going to happen or not. But given all those assumptions, we're coming in somewhere in the range of 9% to 11% for the title segment.

Bose Thomas George - Keefe, Bruyette, & Woods, Inc., Research Division - MD

And just on the cost side, if you just -- in terms of the resi versus commercial, do you have more flexibility on the residential side? Just curious where you have sort of more ability to cut your costs.

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Yes. I mean I think there's costs that are obviously that we can reduce, as Dennis talked about, we're really holding the line on the personnel cost right now because we think we can do it. And we don't think we're going to be in this long-drawn-out period. So there's definitely flex on the personnel side, although Dennis said, we're going to hold the line for at least at the end of the second quarter and wait to see what happens with the market.
Our next questions come from the line of John Campbell of Stephens.

John Robert Campbell - Stephens Inc., Research Division - MD

Mark, I really appreciate the kind of informal guidance. I think that was super helpful in kind of framing stuff up. I wanted to check on one thing, though. On the $2.8 trillion origination market, can you talk about the home price appreciation, kind of what you guys are assuming maybe over the near-term and for the balance of the year?

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Yes. When we look at our average fee per file, and it really, really -- it mostly applies on the purchase side. We've seen a 4% increase in the average fee per file in the first quarter. And we think that's going to be somewhere in the 2% to 3% range for the rest of the year. It's not like an exact science. And so obviously, if we have some sharp decline in home prices, that's going to affect our model. But we're basically assuming flat to slightly up HPA for the year.

Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director

And I'll only add on that is why we're taking that assumption right now is we've got such inventory shortages across almost all of the markets right now. We really don't see a lot of pressure on prices. Now that could obviously change in '21, if we see a spike in default rates. But right now, we're thinking that because of the inventory situations that purchase price appreciation will be in those kind of ranges.

John Robert Campbell - Stephens Inc., Research Division - MD

That makes sense. I think we're in lockstep with you guys for the market outlook for sure. On the Docutech, Gil, I want to touch on the accretion. I know you guys had said maybe 10% or maybe $0.10 of EPS accretion. Could you talk to maybe -- I guess, if you remember if you said a percent to the EPS accretion or if you said an actual dollar amount. So could you touch back on the accretion. And then, Mark, on the $6.4 million of revenue contribution, how seasonal is that in transactional? Is that a good kind of run rate for the rest of the year?

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

I'll start with this. So when we initially closed the Docutech acquisition, our internal expectation was that it would be $0.10 accretive to 2020 earnings, about 2.1%. However, since we closed the deal, the volumes have really just exploded. So it's going to be higher than that now. And yes, we haven't gone back and reforecasted that, but the volumes at Docutech, the revenue has doubled where it was last year, and we're getting margin expansion now just because of the -- a lot of it's automated. So we're feeling really good about that deal right now.

Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director

Yes, I'll just add that margins, I think we'll continue to expand there. It's a high leverage business. Our timing is very good here. And so as we quickly move down, really accelerated by the pandemic drive to an e-solution across our enterprise and the closing of the mortgages, Docutech will play a key role there.

John Robert Campbell - Stephens Inc., Research Division - MD

Is it a timely acquisition?
Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

John, I'll start. Just to it. So in March, we had about $6.4 million of revenue. And it's hard to say what the -- what's going to happen for the year. But we think refi volumes are going to be elevated for the rest of the year. So I think that's a pretty good run rate.

Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director

John, let me also add, it's not direct to part of your question, but just to put it out there right now. Just post pandemic, moving everybody working from home, we're now working over 80% at home, we instituted the plan very early, probably 2 weeks earlier than anybody else. As Mark mentioned, we front-loaded laptops into the quarter and other things. It's been incredible how well our people have adapted. Our productivity lines are very good. Our title production is highly efficient right now, highly automated, actually. And our closing, while we had some issues in those with some early issues early on, all of those issues have dissipated.

So when people have the -- the concerns are, are we running smoothly. We're running very smoothly. We really don't have any material issues going on in the production lines right now in closing the deals.

Operator

Our next questions come from the line of Mark Hughes of SunTrust.

Mark Douglas Hughes - SunTrust Robinson Humphrey, Inc., Research Division - MD

On the commercial, I think you gave guidance on the revenue down 50%. What are you seeing in terms of open order trends here recently?

Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director

Let me start and give it a little bit of high level, and then Mark will come back on the order trends. We're guiding at 50%. We're actually running low 40s right now. So we're running a little bit better than our guidance. Commercial dropped off very, very quickly in some of the key markets led by New York, Chicago, when the stay-at-home orders were put in place. I will tell you right now, we're starting to see some optimism that some transactions are starting to move again. So no question it's going to be a difficult second quarter, but I think it will probably bottom in second and start to clearly improve as we get through the second and go into third. And specifically on the trends and orders.

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Yes. So so far in April, for the first 3 weeks in April, our commercial open orders are down 37% from the same period of the prior year.

Mark Douglas Hughes - SunTrust Robinson Humphrey, Inc., Research Division - MD

And then is there any nuance on purchase versus refi on commercial?

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

There's subtle differences in price, but I would say it's negligible. It's not nearly to the degree it is on the residential side. So I would say it's not material.
And then just in terms of mix, are you getting more refi?

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO
No. I would say the mix is the same as it’s been. We’re not seeing any real differences between purchase and refi. I’d mentioned that open orders were down 37%. The thing that we really track is revenue because orders can be lumpy, you get some big deals, there are some smaller deals and at least so far, in the month, our revenue in commercial is down about 44% from prior year. And that’s the metric that we track more than the order counts in commercial.

Mark Douglas Hughes - SunTrust Robinson Humphrey, Inc., Research Division - MD
On the residential refi, I’m curious in your budget, kind of how you see those orders tapering if we’re running 3,000 per day. I think you -- Dennis suggest you might see that actually accelerate a bit. But as we progress through the year, how should that look as we go into Q3, Q4 -- early thinking?

Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director
Again, being a little optimistic on this right now. We’re running and we’re forecasting 3,000 a day through the rest of the year. But our call on the market may be a little different in that sense is the market itself with the purchase -- excuse me, the mortgage market, a lot of disruption over the last 3 or 4 weeks. Spreads really widened out. Capacity came in, those kind of issues. But what we’re seeing right now is some stability starting to enter back into the market, some better clarity for the lenders. And so I think it’s not out of the realm of possibility that we see the 3,000 accelerate as we move in, probably into the third quarter and beyond. But we’ll see where interest rates are. Regardless of how it turns out, we’re really well positioned to handle the volumes we’ve got or any increasing volumes we have in the future with the stats we got.

Mark Douglas Hughes - SunTrust Robinson Humphrey, Inc., Research Division - MD
And then final question. The no layoff agreed, that sounds like a great policy. Did you measure how much of an impact that could be in terms of margin in Q2 specifically?

Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director
Well, I won’t answer you on the margin question, but what I’ll tell you is what it really means financially short term. It’s probably an impact to our short-term performance of $15 million to $20 million. But I got to say it’s clearly the right thing to do right now. We are facing such a different situation than we’ve ever faced before. We’ve never dealt with a global pandemic. Our people across all organization and others are highly stressed right now. So we thought it’s absolutely the right thing to do. It’s actually the smart thing to do. Our people are highly focused, highly committed right now, delivering an incredible level of service. So I actually think when we’ll look back on this in 5 years it will be one of the pivotal decisions we’ve made.
First question. And can you just maybe explain a little bit how closings are largely being done? Are you primarily seeing more drive through closings in the hardest areas? Are you primarily seeing remote closings? Because it looks like a lot of states have at least temporarily adopted e-notarization and e-signatures. What is the predominant means of closing all this activity in the harder markets? So I do acknowledge that obviously, there's parts of the country that are not as hit as heavily as maybe the coast.

Dennis Joseph Gilmore - First American Financial Corporation - CEO & Director

Yes, Geoff, let me start on that one. It's a little of all of the above. We've done the drive through. We did that early on. We've done by appointment only. When we bring anybody into the office, it's always with the appropriate social distancing and all the appropriate precautions. And so what we saw earlier, Geoff, on the closing issue with some issues with the notaries, but they really quickly worked themselves out. So specifically to the future aspect of the ROMs and remotes, I think that's probably going to play itself out and accelerate quicker over the next few quarters than what it has typically been adopted.

So not a big issue right now, but I think it will be quicker for an adoption curve going into the second, third and fourth quarters. So we're really optimistic about that, and we've made some investments there. So again, just one more time on that. The way we're doing it right now has been traditionally the way it's been done with all of the appropriate caution involved. I think how we're going to see going forward, there is a quicker adoption of ROM.

Geoffrey Murray Dunn - Dowling & Partners Securities, LLC - Partner

Okay. And then from a capital management standpoint, I think you indicated before that you remain watchful of opportunities in the market. I'm just curious with the stock down here and you buying back stock in Q1 below $40, on average, do you think your acquisition opportunities and the potential returns there remain more attractive than buying your stock in the low 40s?

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Geoff, I'd say it's going to be a balance, and it's going to be a mixed approach. I mean, on the one hand, we think the value of our stock is really attractive at the current price. And we've got a strong balance sheet, and we're in this really good position where we want to put it to work in this market. So I think it's going to be kind of a mix of acquisitions. And depending on where our shares trade, it could be buybacks as well. But it will be a blended approach.

Geoffrey Murray Dunn - Dowling & Partners Securities, LLC - Partner

Okay. But I mean you guys have tended to be very opportunistic on the stock. So these are levels where we could see activity from you?

Mark Edward Seaton - First American Financial Corporation - Executive VP & CFO

Yes. I mean we bought it at $38-and-change in the first quarter. And so you know what levels we're definitely interested in, and we're not too far from that right now. It's a lot of time we check. So we do think it's attractive here.
Yes. Just a follow-up on capital deployment here. Can you just give a sense of how much more capacity you think you have to do either buybacks or acquisitions at your current debt to cap?

Yes, Mark. So one of the things that we look at is we track our excess capital. And we look at how much cash we have at the holding company, and we always want to have 1 year of cash at the holding company. We track how much excess capital we have at FATICO, which is our primary insurance company. And we track our -- obviously, our debt, we've got excess debt capacity today. So when we look at all those 3 things. As of the end of March, we had about $400 million of what we would consider excess capital. But I would say that's a conservative number. Just because in that, we assume a stressed environment, and we're already in a stress environment. And so I would say at a minimum, at a very minimum, it's $400 million. We've obviously got a lot more flexibility than that.

Got it. Another follow-up question on the margin guidance. Does the 9% range kind of assume -- is that based more on like what you're assuming today for the development in the market? And 11% might be if it the economy opens up faster and maybe the market evolves in a way that I think Dennis is optimistic that maybe we could see. Is that a fair way to think about it? Or is it not quite that simple?

I would just say, we have this point estimate, which is resales opened, down 45% in Q2 with a gradual improvement. We've got commercial revenue down 50% with a gradual improvement, and we've got refinance orders, which currently we're at 3,000 a day, and we assume that's going on for the whole year. So that's our point estimate. And if you use that, you get to 10% margins. And then we do some sensitivities about slightly higher and slightly lower, and that's how we get to the level 9% to 11%.

Okay. Got it. That's helpful. And then just one last one on expenses. Understanding that near term, there won't be any layoffs. If revenue remains challenged over the course of the year, how do you -- how should we think about the success ratio? And how you'll look to manage expenses relative to revenues?

Well, I would just say on the success ratio that we have been, for years now, we've been targeting 50% success ratio with -- and we've had success with that. And that's one of the reasons why last year we had the highest margin we've ever had because we've really been focused on hitting that. And I think especially in the last 6 weeks or so, we have not really been focused on success ratio. We -- that's not a metric that we're really focused on, at least in the current market environment. So there's no question that our success ratio is going to be sacrificed because of that.

There are no additional questions at this time. That does conclude this morning's call.

We'd like to remind listeners that today's call will be available for replay on the company's website or by dialing (877) 660-6853 and enter the conference ID 13701584.
The company would like to thank you for your participation. This concludes today’s conference call. You may disconnect.