

INVESTORS TITLE CO. (ITIC)

\$44.00

Please see important disclosures and analyst certification on page 6 of this report.

**Equity Research
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Statistics

52-Wk Range:	\$53.25-\$35.50
Market Value:	\$105.6 mil.
Dividend:	\$0.28
Yield:	0.60%
Shares Out.:	2.4 mil.
Float/Avg. Trading Volume:	2.0 mil./3,706
L-T Debt/Total Capital:	Nil
Est. 3-5 yr. EPS Growth:	10%
Book Value/Share (12/31/07):	\$41.18

Diluted Earnings per Share

	2006A	2007A	Prior Est.	2008E	Prior Est.	2009E
Mar. 1Q	\$1.11	\$0.92		\$0.71	\$0.93	NE
Jun. 2Q	\$1.68	\$0.46		\$0.93	\$1.21	NE
Sep. 3Q	\$1.44	\$1.40		\$1.27	\$1.46	NE
Dec. 4Q	\$0.91	\$0.43	\$0.80	\$0.84	\$0.89	NE
FY	\$5.14	\$3.35	\$3.49	\$3.75	\$4.50	\$4.25
P/E	8.6x	13.1x		11.7x		10.4x

Rating: **NEUTRAL**
Target Price: **NA**

**Solid Results in a Difficult Real Estate Market;
Reducing Estimates**

Action

Reiterate Neutral Rating

Key Points

- **4Q07 results:** Investors Title Company reported diluted 4Q07 EPS of \$0.43 a share vs. \$0.91 last year, missing our \$0.80 assumption. A tax rate adjustment (roughly \$0.20 a share) to reclassify taxable muni bonds that had been previously reported as tax exempt along with slightly higher salaries and commissions explains the variance to our estimate.
- **In-line premiums:** Net written premiums decreased 3.9% to \$15.57 million vs. \$16.19 million last year, reasonably consistent with our projection. Investors Title's premiums continue to hold up well compared to peers, most of which reported premium declines in excess of 20% during 4Q07. While premium growth was down modestly in its top-three states, the company posted positive growth in four of its smaller states.
- **Book Value/Investments:** Book value ended the year at \$41.18 a share, a 1.2% sequential increase (+8.4% for the year). Investment income grew approximately 12% to \$1.41 million vs. \$1.26 million last year, outpacing our \$1.09 million expectation.
- **Revising estimates:** We are lowering our 2008 EPS estimate to \$3.75 (from \$4.50), reflecting an uptick in our salaries and operating expense assumptions. We are introducing a 2009 EPS estimate of \$4.25.
- **Investment opinion:** While we expect the market environment to stay challenging for title insurers during at least the first half of the year, we think that Investors Title's results should hold up well in the near term compared to its peers. With that in mind, the shares are currently trading at 1.1x book value, a premium multiple to all peers in the space. With no clear catalyst to improve results near term, all else being equal we would be a buyer of ITIC shares below book value, but patient otherwise. Accordingly, at the current share price, our rating on ITIC shares remains Neutral.

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Recent Results, Outlook, Valuation

Investors Title Company reported diluted 4Q07 EPS of \$0.43 a share, down 53% vs. \$0.91 last year and well below our \$0.80 assumption. A tax rate adjustment (roughly \$0.20 a share) to reclassify taxable muni bonds that had been previously reported as tax exempt (2006 and YTD 2007) along with slightly higher salaries and commissions explained the variance to our estimate. As a result of the tax reclassification, the 4Q07 tax rate approximated 59% vs. 21% during last year's fourth quarter.

Agency commissions on a dollar basis were essentially flat with the prior-year period. Salaries, employee benefits, and payroll taxes (in dollar terms) increased approximately 3% vs. last year's December quarter. The title loss claims provision amounted to 10.3% vs. 9.4%, a solid number that demonstrates claims activity (while slightly elevated from historical levels) remains under control. The company's loss ratios have risen modestly above historical levels, but remain considerably below its peers.

Net written premiums decreased 3.9% to \$15.57 million vs. \$16.19 million last year, reasonably consistent with our projection. Premiums have held up better than peers in the group for virtually all of this current housing slowdown with most peers reporting title premium declines in excess of 20% during the final quarter of the year. Agency-generated premiums constituted 57% of the mix, level with last year and reflecting the company's emphasis on agency business during these difficult times. The Exchange Service business generated fourth quarter revenues of \$1.18 million vs. \$1.44 million, beating our \$1.09 million assumption.

From a geographic standpoint, the results were reasonably solid with few states reporting significant decreases during the final months of the year. Premiums within the core state of North Carolina (49% of premiums) decreased 2%, as we believe that certain areas of this state continue to hold up considerably better than the national average. Net written premiums in South Carolina (12% of premiums) and Virginia (8% of premium) decreased 14% and 23%, respectively, reflecting deteriorating conditions in these states in the current environment. Premium growth was positive within its non-core states of Illinois, Kentucky, Tennessee, and West Virginia, likely reflecting respectable agency premium generation within these states.

Direct premiums written by state (\$ thousands)			
	4Q07	4Q06	% Chg.
North Carolina	\$7,679	\$7,801	-2%
South Carolina	1,886	2,193	-14%
Virginia	1,275	1,647	-23%
Michigan	723	904	-20%
Kentucky	683	516	32%
Tennessee	566	499	13%
New York	606	621	-3%
West Virginia	484	459	6%
All other	<u>1,689</u>	<u>1,667</u>	<u>1%</u>
Total	\$15,591	\$16,308	-4%

Source: FBW estimates

We are lowering our 2008 EPS estimate to \$3.75 (from \$4.50), reflecting an uptick in our salaries and operating expense assumptions. We are modeling in essentially another flat year of premiums for Investors Title in 2008, representing another year of outperforming its peers from a top-line standpoint. We are introducing a 2009 EPS estimate of \$4.25.

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Despite the sharp downturn in residential housing this year, Investors Title has managed to navigate through the housing recession with flying colors (while staying profitable throughout the cycle). The company's exposure to comparatively more stable housing regions (as opposed to bubble markets) explains the smoother all-around performance both in the up and down cycles of the housing market. We believe that modest premium declines and solid expense management should enable the company to report margins well above its peers in the near term. With no clear catalyst to improve results near term, all else being equal we would be a buyer of ITIC shares below book value, but patient otherwise. Accordingly, at the current share price, our rating on ITIC shares remains Neutral.

Balance Sheet/Investments

Book value ended the year at \$41.18 a share, a 1.2% sequential increase (+8.4% for the year). Investment income grew approximately 12% to \$1.41 million vs. \$1.26 million last year, outpacing our \$1.09 million expectation. Fixed-income securities equated to 71% of total invested assets, down from 85% at the end of 2006. The main difference is increased allocation toward short-term investments (likely cash, Treasuries, etc.). Claim reserves totaled nearly \$37 million at the end of December, level with the end of 2006. The board of directors recently hiked the annual dividend earlier this week by 17% to \$0.28 a share from \$0.24. Moreover, the company repurchased 72,009 shares in the fourth quarter and 111,437 shares in full-year 2007 (235,336 shares remain authorized under the current share buyback program). The company finished the year again with no balance sheet debt.

2008 Mortgage Outlook: Bracing for Another Challenging Year in Housing

Mortgage origination activity ended 2007 on a soft note, extending the slump in residential housing that began many months ago. A wide variety of factors continue to weigh on the housing market, including (1) near record-high inventory levels, (2) rising foreclosure rates, (3) increasingly stringent lending standards, and (4) a period of decelerating economic activity. The good news is that the Fed's recent interest rate easing actions along with the stimulus plan (which enables a number of qualified jumbo mortgage holders to refinance at lower rates) has spawned a considerable uptick in refinancing activity in recent weeks. With 30-year mortgage rates comfortably below 6% and considering that a large number of ARMs have yet to reset, we think it is reasonable to assume the refis have the potential to surprise to the upside this year.

Even though refinancings have staged a comeback since the start of 2008, the residential housing industry continues to navigate through a recessionary period. Total housing starts plummeted 25% in 2007 and have now tumbled an extraordinary 56% from peak levels established in January 2006. Publicly traded homebuilders remain in survival mode while grappling with surging cancellation rates, falling home prices, and waning consumer confidence. Consequently, title insurers are feeling the pinch of softer mortgage originations and continue to struggle to keep cost structures consistent with falling demand trends. Although 2008 is off to a rough beginning and a full-fledged recovery could be years away, the vast majority believe that this is the year the industry reaches a bottoming point.

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Mortgage Rates and Loan Volume, 1999 to 2009E

<u>Year</u>	<u>Total Loan</u>		<u>Refinance</u>			<u>30-Year</u>
	<u>Volume</u> <u>(billions)</u>	<u>Purchase</u> <u>Activity</u>	<u>Loan</u> <u>Volume</u>	<u>Refinance</u> <u>Percent</u>	<u>Purchase</u> <u>Percent</u>	<u>Fixed</u> <u>Interest</u> <u>Rates</u>
1999	\$1,318	\$797	\$521	39.5%	60.5%	7.43%
2000	\$1,046	\$821	\$225	21.5%	78.5%	8.06%
2001	\$2,027	\$880	\$1,144	56.5%	43.5%	6.97%
2002	\$2,613	\$1,043	\$1,440	61.5%	38.5%	6.54%
2003	\$3,832	\$1,184	\$2,648	69.1%	31.9%	5.82%
2004	\$2,792	\$1,335	\$1,457	52.2%	47.8%	5.84%
2005	\$3,034	\$1,512	\$1,522	50.2%	49.8%	5.87%
2006	\$2,761	\$1,447	\$1,314	47.6%	52.4%	6.41%
2007	\$2,485	\$1,250	\$1,235	49.7%	50.3%	6.34%
2008E	\$2,259	\$992	\$1,266	56.1%	43.9%	6.01%
2009E	\$2,042	\$1,030	\$1,012	49.5%	50.5%	6.15%

Source: Fannie Mae

Fannie Mae is projecting a difficult year for residential housing, as evidenced by a 9% expected decline in mortgage originations for 2008. Refi transactions are forecasted to comprise a larger piece of the share (again) and are expected to reach 56.1% in 2008 vs. 49.7% in 2007. Although Fannie Mae projects a modest increase in refi volume for the year, purchase activity is expected to weigh on overall mortgage originations and remain in the doldrums for the year.

The MBA forecast is predicting that total mortgage originations will come in at \$1.96 trillion in 2008, a touch below its previous forecasts just north of \$2 trillion. Purchase transactions are expected to deteriorate 21% in 2008 followed by a 3% rebound in 2009. Refinancings are projected to post declines of 11% and 21% in 2008 and 2009, respectively, a sharp contrast compared to Fannie Mae's assumptions. The MBA composite index closed at 684.9 for the week ended 3/5/08, approximately 2% above the same period a year earlier. Refinancings have led the recovery since the beginning of the year, albeit activity has deteriorated somewhat over the past few weeks. Purchase transactions have been fairly weak so far this year and the index was approximately 10% below the year-ago period for the most recent week.

Company Description

Based in Chapel Hill, North Carolina, Investors Title is a holding company whose principal business is underwriting and issuing land title insurance policies to lenders and borrowers. Formed in 1972, the company has 30 branch offices and a network of agents in 23 states and the District of Columbia. Agent channels generate approximately 58% of premiums with direct channels producing the balance. More than 40% of premiums originate in North Carolina, where the company has approximately a 26% market share. The company is led by J. Allen Fine, the founder and chairman.

INVESTORS TITLE COMPANY and Subsidiaries
Income Model & Selected Financial Data

(\$ thousands, except per share)

	2006A	1Q07	2Q07	3Q07	4Q07	2007A	1Q08E	2Q08E	3Q08E	4Q08E	2008E	2009E
REVENUES												
Premiums	\$ 70,197	16,793	18,626	18,994	15,571	\$ 69,983	16,205	18,160	18,614	15,571	\$ 68,550	\$ 70,263
Investment Income	4,326	1,210	1,272	1,302	1,414	5,197	1,307	1,322	1,367	1,443	5,439	5,660
Net Cap. Gains (Losses)	551	166	200	521	35	922	-	-	-	-	-	-
Exchange Service revenue	5,980	1,245	870	1,042	1,182	4,340	1,071	896	1,063	1,182	4,213	4,423
Other	3,607	920	1,139	1,199	1,240	4,499	1,050	1,100	1,100	1,200	4,450	4,800
Total Revenues	84,661	20,334	22,107	23,059	19,442	84,941	19,633	21,478	22,144	19,396	82,652	85,146
EXPENSES												
Salaries/Benefits	19,981	5,274	5,091	5,136	5,317	20,819	5,400	5,300	5,300	5,300	21,300	21,800
Commissions	26,715	6,845	7,733	7,461	6,386	28,425	6,650	7,453	7,533	6,302	27,938	28,435
Claims Provision	7,405	1,809	4,352	2,364	1,609	10,135	1,783	2,034	1,973	1,635	7,425	6,499
Operating Expenses	13,231	3,434	3,636	3,155	3,514	13,739	3,550	3,750	3,300	3,500	14,100	14,700
Total Expenses	67,332	17,363	20,812	18,116	16,827	73,118	17,383	18,537	18,106	16,736	70,763	71,434
Pretax Income	17,329	2,971	1,295	4,942	2,615	11,824	2,250	2,941	4,038	2,659	11,889	13,712
Provision for Taxes	4,144	649	141	1,085	1,547	3,422	495	647	888	585	2,616	3,291
Net Income from Ops.	13,185	2,322	1,154	3,857	1,068	8,402	1,755	2,294	3,150	2,074	9,273	10,421
Dil. Shares Outstanding	2,564	2,536	2,518	2,507	2,473	2,509	2,475	2,475	2,475	2,475	2,475	2,450
Dil. EPS	\$5.14	\$0.92	\$0.46	\$1.54	\$0.43	\$3.35	\$0.71	\$0.93	\$1.27	\$0.84	\$3.75	\$4.25
Operating Dil. EPS	\$5.00	\$0.87	\$0.41	\$1.40	\$0.42	\$3.11	\$0.71	\$0.93	\$1.27	\$0.84	\$3.75	\$4.25
Growth Rates												
Premiums	-8.2%	1.0%	-2.6%	4.1%	-3.9%	-0.3%	-3.5%	-2.5%	-2.0%	0.0%	-2.0%	2.5%
Investment Income	29.7%	21.7%	22.9%	25.7%	12.1%	20.1%	8.1%	3.9%	5.0%	2.0%	4.6%	4.1%
Exchange Services Revenue	31.6%	21.2%	-54.4%	-35.1%	-17.8%	-27.4%	-14.0%	3.0%	2.0%	0.0%	-2.9%	5.0%
Ratios												
Expense Ratio*	85.4%	92.6%	88.4%	82.9%	97.7%	90.0%	96.3%	90.9%	86.7%	97.0%	92.4%	92.4%
Loss Ratio	10.5%	10.8%	23.4%	12.4%	10.3%	14.5%	11.0%	11.2%	10.6%	10.5%	10.8%	9.2%
Combined Ratio	95.9%	103.4%	111.7%	95.4%	108.1%	104.5%	107.3%	102.1%	97.3%	107.5%	103.2%	101.7%
Operating Ratio	89.8%	96.2%	104.9%	88.5%	99.0%	97.1%	99.2%	94.8%	89.9%	98.2%	95.3%	93.6%
Net Investment Yield	4.0%	4.0%	4.2%	4.2%	4.4%	4.2%	4.4%	4.4%	4.3%	4.3%	4.4%	4.4%
Tax Rate	23.6%	21.8%	10.9%	22.0%	59.2%	28.5%	22.0%	22.0%	22.0%	22.0%	22.0%	24.0%
Net After-Tax Margin	15.6%	11.4%	5.2%	16.7%	5.5%	9.9%	8.9%	10.7%	14.2%	10.7%	11.2%	12.2%
Year-End Book Value	\$38.00					\$41.18					\$44.77	\$48.86
ROE (Beginning)	15.6%					8.8%					9.1%	9.5%

*This includes branch expenses not related to acquisition costs.

Source: company documents and FBW estimates

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Prices herein are intraday March 7, 2008.

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Ratings Distribution & Investment Banking Disclosure

Rating	Ratings Distribution ^	Investment Banking*
Buy-rated	63%	19%
Hold (Neutral)-rated	34%	10%
Sell-rated	1%	0%

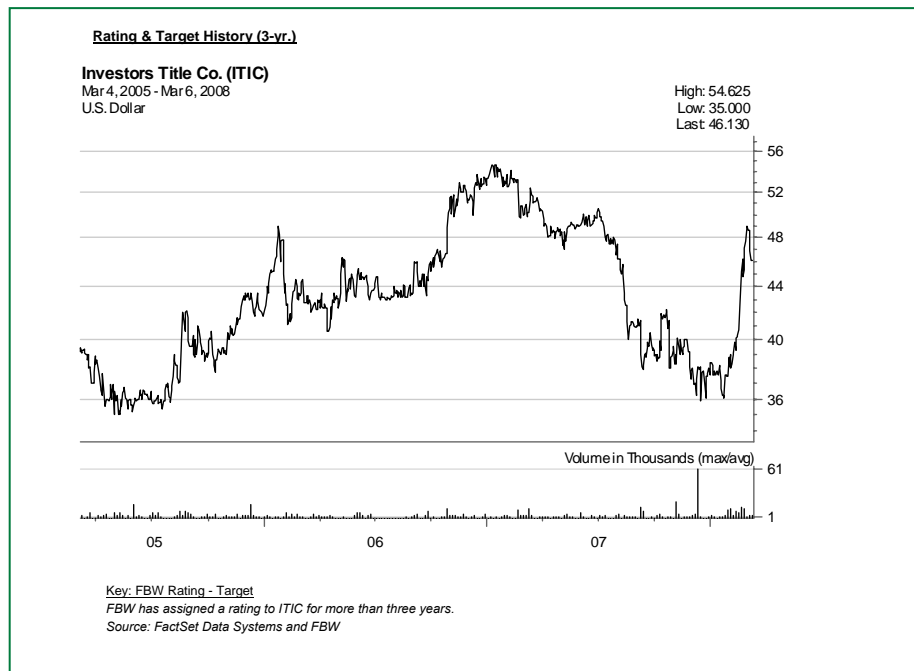
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Data as of 12/31/07

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