

Peña Verde

Current price: MXN 10.17
12-month target price: MXN 11.90
(No liquidity risk discount applied).



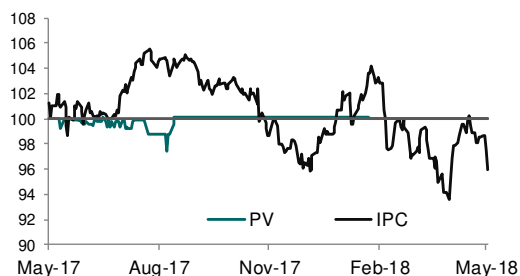
1Q18 quarterly report
lunes, 07 de mayo de 2018

A loss in the investment portfolio triggers a quarterly net loss of 181 million pesos. Operating results also lower than our forecast

Key Data

Ticker	PV* MM
Exchange	BMV
12 Month T.P. (Estimated Fair Value)	MXN 11.90
Last Price	MXN 10.17
Expected Return	17.0%
12 M Dividend Yield	0.1%
Expected Dividend Yield	2.0%
Total Expected Return	19.0%
LTM Return PV*	0.0%
LTM Price Range	(10.18 - 9.91)
Outstanding Shares (Million)	476.68
Free Float	2.77%
Trading Volume	Low
Market Cap (USD Million)	USD 251.56
Official Website	www.corporativopv.mx

12M Return vs IPC



	2015	2016	2017	2018f
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Valuation

P/E	7.9x	18.7x	8.3x	5.9x
P/BV	1.2x	1.1x	1.0x	0.9x
ROE	15.5%	6.0%	12.2%	14.6%

Estimates (MXN million)

Gross Written Premiums	5,143	6,865	6,945	7,501
YoY%		33.5%	1.2%	8.0%
Net Retained Premiums	3,923	4,876	5,521	5,949
YoY%		24.3%	13.2%	7.7%
Underwriting Income	270	126	362	866
YoY%		-53.4%	187.7%	139.5%
Net income	613	257	583	818
YoY%		-58.1%	127.4%	40.2%
EPS	1.3	0.5	1.2	1.7
YoY%		-58.1%	127.4%	40.2%

Profitability

Combined Ratio	103.7%	107.4%	103.6%	94.0%
Acquisition Ratio	25.6%	27.0%	28.1%	25.0%
Claims Ratio	66.6%	68.0%	62.5%	57.0%
Operation Ratio	11.5%	12.4%	13.0%	12.0%

Source: Peña Verde, Bloomberg and Prognosis estimates

n.m.: not meaningful

- 1Q18/1Q17 results.** Written premiums totaled 1,391 million pesos (mp), a drop of -17.0%. The operating loss was -47.0 mp and the comprehensive financing result reached -172 mp. Thus, the loss totaled -181 mp, an EPS of -0.38 pesos per share.
- After concluding the governance chapter, the company will focus on strengthening its digital platform.** After the creation of the Peña Verde SAB holding company in 2013, the implementation of better corporate governance practices and a strengthening of the management team, the company plans to focus on improving its digital platform in 2018, which could imply significant investments.
- Profitable growth.** The company's challenge continues to be to increase its market share and scale, while controlling its cost structure, particularly the claims ratio. We anticipate an accelerated growth in Reaseguradora Patria and a stability in General de Seguros in the coming years.
- Low market cap. and trading volume.** The capitalization value of the issuer is approximately MXN 4,847 million, its trading volume is minimal, and its free float is only 3%, which limits the universe of potential PV* investors.
- Commitment to the stock market.** The company is open to possibilities to increase its stock's float. According to Prognosis, a private transaction would make sense if a strategic partner adds value to the PV business.
- 2018 forecasts.** We anticipate that premiums of PV* will grow ~8%, driven by a growth of more than 20% in the Reaseguradora Patria business and a fall of ~4% in the General de Seguros segment. We also anticipate an improvement in the combined ratio to 94% from 104% in 2017. Capital gains of the portfolio will be lower than those in 2017. Thus, we reached an estimated net profit of 818 mp, an EPS of 1.7 pesos.
- Target price.** We reiterate our 12-month T.P at 11.90 pesos, equivalent to 1.0X the estimated 2018 book value. However, we do not incorporate a liquidity discount, due to the low trading volume of the shares.
- Risks.** The main risks are: slow economic growth, competition, the execution of new strategies and the behavior of financial markets. Others may include the cost of reinsurance, a higher claims ratio, shares liquidity, ceded reinsurances (counterparty, strategic partners) and credit risk in their investments.

1. 1Q18 report

Income Statement			
Accumulated data			
	1Q18	1Q17	YoY Change
Gross Written Premiums	1,391	1,675	-17.0%
Net Retained Premiums	1,104	1,347	-18.0%
Retention Premiums Accrued	1,287	1,254	+2.6%
Acquisition Costs	361	374	-3.5%
Insurance Claims Incurred	735	579	+27.0%
Underwriting (Technical) Income (Loss)	190	301	-36.8%
Net Operating Expenses	73	125	-41.4%
Operating Income (Loss)	-47	47	n.m.
Comprehensive Financing Result	-172	515	n.m.
Net Profit (Loss)	-181	500	n.m.
<i>Acquisition Ratio</i>	32.7%	27.8%	+490 bp
<i>Claims Ratio</i>	57.2%	46.2%	+1,098 bp
<i>Operating Ratio</i>	6.6%	9.3%	-264 bp
Combined Ratio	96.4%	83.2%	+1,324 bp

Source: Prognosis and PV

n.m. = not meaningful

Note: The acquisition and operating ratios consider the net retained premiums, while the claims ratio considers the retention premiums accrued.

Peña Verde's written premiums totaled 1,391 million pesos (mp) in 1Q18, a fall of -17.0% y/y, against the 1,675 mp in 1Q17. This variation is mainly explained by the expected low activity in "General de Seguros", "which as of March 2018, reached sales of 697.7 mp, a drop of -22.7% vs the same period of the previous year, originated mainly due to the non-renewal of a life operation business for an approximate amount of 238 mp".

On the other hand, the subsidiary "**Reaseguradora Patria**" reached sales of 689.8 mp, which represented a decrease of -1.1%, due to "the withdrawal of a portfolio involved with business from the branch of accidents and illnesses for an amount of 81 mp; however, it was offset by the increases in reinsurance premiums from life operations, but also from others, like catastrophe risks, autos and fire".

The net consolidated acquisition cost of PV * amounted 361 mp in 1Q18, which compared to the 374 mp in 1Q17, a fall of -3.5%.

The net cost of consolidated claims increased +27.0%, standing at 735 mp. Peña Verde's claims ratio was 57.2%, an annual increase of 11 percentage points.

The **technical profit** fell -36.8% YoY to 190 mp. On top of that, net operating expenses totaled 73 mp and the **operating loss** amounted -47 mp.

The **integral result of financing** recorded a loss of -172 mp, which compares unfavorably against the profit of 515 mp a year ago. That is the result of a loss in investments, mainly in the stock market.

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PV reported a **net loss** of -181 mp, which also compares unfavorably against the 500 mp profit in the previous year. The 1Q18 result is explained by the following: "(1) an increase in the IBNR reserves and (2) the poor performance of the financial markets that caused the decline in the valuation of investments".

Financial situation

According to the company's information, **total assets** amounted 19,340 mp in 1Q18, growing +6.1% y/y. "Among the most significant changes is the increase in investments, amounting 391 mp, a 698.2 mp increase in reinsurers, and the other items of the asset show little relevant behavior."

Stockholder's equity. As of March 2018, the majority stockholders' equity reached 4,660 mp, an annual decrease of -3.4%.

2. Target Price

We recalculated the implicit or fair value multiple using the Damodaran formula, $P/BV^* = (ROE-g)/(K_e-g)$. We used cost of capital of 10.2%, a sustainable ROE of 10.5% and a nominal perpetuity growth of 4%, resulting in a "fair" multiple of 1.0488X. The product of this multiple with the BV estimated for 2017 (11.9 ps.), is 12.50 pesos; "fair" value according to this method.

If we gave the reason to the market that today values the issuer at 1.0X its known book value, the target price would be 11.9 pesos per share, which we decided to use for the next 12 months.

This price does not assume a discount for the stock low visibility in the market. However, PV * qualifies as a stock with high risk and low profit predictability.

Company's description:

PV* is a holding company. Its main business consists in managing its subsidiary companies General de Seguros and Reaseguradora Patria through a third subsidiary, "Servicios Administrativos Peña Verde", with the purpose of improving management, regulatory compliance and generating economies of scale. General de Seguros operates all insurance segments except for pensions in all states of the Mexican Republic. The company's health segment is managed by its subsidiary "General de Salud". Reaseguradora Patria provides reinsurance services in all its forms in Mexico, Latin America and the rest of the world.

Peña Verde's Annual Income Statement (MXN millions)

	2015	2016	2017	2018f
Gross Written Premiums	5,143	6,865	6,945	7,501
(-) Ceded Premiums	1,219	1,990	1,424	1,552
Net Premiums Retained	3,923	4,876	5,521	5,949
<i>Net Premiums Retained rate</i>	76%	71%	79%	79%
(-) Net Increase in Provision for Unaccrued Premiums	107	367	425	476
Retention Premiums Accrued	3,816	4,508	5,096	5,473
(-) Acquisition Costs	1,004	1,317	1,550	1,487
<i>Acquisition ratio</i>	26%	27%	28%	25%
(-) Insurance claims incurred	2,543	3,065	3,184	3,120
<i>Claims ratio</i>	67%	68%	62%	57%
Underwriting (technical) income (loss)	270	126	362	866
(-) Net Increase in Other Technical Reserves	331	90	349	270
Gross Income	-61	36	13	596
(-) Net Operating Expenses	451	605	720	714
<i>Operating ratio</i>	12%	12%	13%	12%
Operating income (loss)	-512	-569	-707	-117
Comprehensive Financing Result	1,370	921	1,368	1,310
Earnings before income tax	857	352	661	1,192
(-) Income tax payment provision	204	90	67	358
<i>Income tax rate</i>	24%	26%	10%	30%
Net profit (loss)	613	256.6	583	818
Minority interest	40	5.3	10	17
Majority Net Profit	613	256.6	583	818
EPS (TTM)	1.3	0.5	1.2	1.7
Number of shares (million)	476.7	476.7	476.7	476.7
<i>Gross Written Premiums growth</i>	N/A	34%	1%	8%
<i>Net Profit Growth</i>	N/A	-58%	127%	40%
<i>EPS growth</i>	N/A	-58%	127%	40%

Other Indicators

	2015	2016	2017	2018f
ROE	16%	6%	12%	15%
P/E	7.9	18.7	8.3	5.9
P/BV	1.2	1.1	1.0	0.9
Book Value Per Share	8.3	9.0	10.2	11.9

Balance Sheet Summary (MXN millions)

	2015	2016	2017	2018f
Assets	15,224	18,397	20,677	22,913
Investments	11,733	13,407	14,756	16,709
Liabilities	10,939	14,092	15,835	17,253
Technical Reserves	8,897	11,043	12,610	14,665
Total Equity	4,285	4,305	4,842	5,660
Shareholder's Equity (majority)	3,954	4,263	4,794	5,604

Source: Prognosis and BMV



Prognosis

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