

PEÑA VERDE

Quarterly Report 2Q17

Current Price MXN 10.04

2017 Target Price MXN 11.30 (no discount for illiquidity applied)

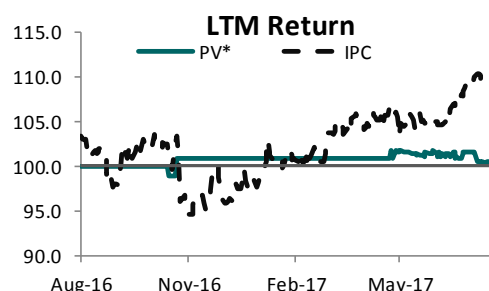
Friday, August 04, 2017

Solid financial products in 1H17 result in net income exceeding our forecast for the whole year; such figure was supported by a good performance of technical and operational profit

- Solid technical and operational results, while premiums advance + 8.5% vs. 1H16.
- RIF of 930 mp is substantially higher than our expectation of Cetes +300 bp.
- Net income of 678 mp surged +63% in 1H17, supported by higher premiums, a lower increase in reserves and a drop in the claims ratio.
- We increase our target price to 11.30 ps per share.

Key Data

Local Ticker	PV*
2017 Target Price	MXN 11.30
Last Price	MXN 10.04
Expected Return	12.5%
LTM Return PV*	0%
Outstanding Shares (million)	476.7
Free Float	3.0%
Marketability	Low
Market Capitalization (MXN million)	MXN 4,786
LTM Price Range	(9.90 - 10.38)



	2014	2015	2016	2017f
Valuation				
P/E	95.0x	7.9x	18.7x	6.5x
P/BV	1.32x	1.23x	1.13x	0.97x
Estimates (MXN)				
Gross Written Premiums	4,190	5,143	6,866	7,414
YoY%	26.2%	22.7%	33.5%	8.0%
Net Premiums Retained	3,204	3,923	4,876	5,561
YoY%	19.8%	22.5%	24.3%	14.1%
Underwriting income	287	270	126	737
YoY%	-37.7%	-6.0%	-53.4%	486.6%
Net income	46	613	257	748
EPS	0.10	1.29	0.54	1.60
YoY%	-22%	1228%	-58%	196%
Profitability				
Combined Ratio	97.0%	103.7%	107.4%	93.5%
Acquisition Ratio	28.3%	25.6%	27.0%	26.5%
Claims Ratio	58.7%	66.6%	68.0%	57.0%
Operation Ratio	10.0%	11.5%	12.4%	10.0%

Regulatory changes and cost structure. The regulatory changes in 2016 that increased the PV* cost structure will be reversed in 2017. An example can be observed in the declining the claims ratio which reached 51.9% in the semester, partly supported by a change in methodology in the calculation of claims incurred but not reported (IBNR).

Target Price. We increased our target price to 11.30 pesos per share, since our estimates have been exceeded. In addition to adjusting our model in the technical part, the main modification is that we now expect portfolio gains of 1,330 million pesos (mp) instead of 922 mp. This price is equivalent to 7 times the EPS expected for the same year and 1.06 times the book value. This T.P. is based on assumptions of premium increases of 8.5%, an improvement in the combined ratio vs 2016, to levels of 93.5%, and the performance of the investment portfolio mentioned. **We did not incorporate a discount due to the low liquidity of the shares.**

Balance between growth and quality of risks. The company's challenge continues to be to increase its market share and scale, while controlling costs and operating expenses.

The only Mexican company with registration to write risks in the well-known Lloyd's market. Patria Corporate Member, Ltd., with an investment of 8.78 million pounds, reported a +55% quarterly increase in revenue.

Low capitalization and marketability. The market capitalization of the issuer is 4,786 billion pesos (bp), its trading volume is minimal and its free float is only 3%, which limits the universe of potential investors of PV*. However, following the acquisition of the 12.2% of the total outstanding shares in 4Q16, the purpose of adding a strategic partner becomes effective, potentially increasing the float and improving the visibility of the shares.

Relevant events 2017. We anticipate: (1) the ambitious telephone medical orientation call center project will enter a commercial phase, although currently small, it could be a major revenue generator in the future and (2) the listing of the shares of *General de Seguros* will be withdrawn the Mexican Stock Exchange.

Risks. The main risks are: economic, competition, execution of new strategies and the behavior of the securities markets. Others may include: reinsurance costs, claims levels, liquidity, ceded reinsurance (counterparty, strategic partners) and credit risk in investments.

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1. 2Q17 Report

Peña Verde's written premiums totaled **3,191 billion pesos (bp)** in 1H17, an increase of +8.5% y/y against the 2.941 bp in 1H16. This figure was boosted by the good dynamism of "Reaseguradora Patria", which had sales of 1.553 bp, +37.3% y/y in 1H17, resulting from increases in reinsurance premiums for fire, cars, miscellaneous and refinancing operations and life.

On the other hand, the subsidiary "**General de Seguros**" reached sales of 1.483 bp, which represented a drop of -13.3%, mainly due to the decrease in the insurance business of CADENA (component of attention to natural disasters) in the subsector of livestock, bringing the agricultural sector to fell -55.6%. On the other hand, the "diverse", "health" and "civil liability" sectors recorded falls of -43.9%, -23.9% and -11.5%, respectively.

Net increase in reserves. "As of June 2017, the current and outstanding risk reserve of 190.4 million pesos (mp), showed a decrease of -29.3% compared to June 2016, mainly due to the impact that represented in 2016 the change in the methodology for the constitution of the risk reserve based on the Solvency II models." (Verbatim PV).

Acquisition costs reached 711.1 mp in the first half of 2017, which compared to 605.4 mp in 1H16 represents an increase of +17.5% (above the growth of written premiums), "influenced by the growth in reinsurance commissions paid to the ceding companies and the over-loss coverage costs that protect the retention." The net cost of acquisition represented 27.4% of the retained premiums, whereas a year ago it was 26.9%.

Insurance claims incurred fell -13.3% y/y, totaling 1.250 bp. Peña Verde's claims ratio settled at 51.9%, which means a fall of 20.7 percentage points compared to the figure of 1H16. This is explained by the change in the methodology of claims incurred but not reported, that was introduced in 2016. The claims ratio remains at a very low historical level.

The technical profit increased to 446.8 mp in 1H17 from a loss of 61.8 mp. This recovery is the result of: 1) a higher revenue, 2) lower increase in the risk reserve and 3) a decrease in claims.

Operating income was -142.9 mp, which improved vs the loss of -275.3 mp in 1H16.

The comprehensive financing result posted a gain of 930.0 mp, falling -4.6%. Such change was the result of a forex loss, but smoothed by gains in investments.

Finally, PV* reported a **net income** of 677.9 mp, an increase of 63% y/y.

Total assets amounted to 18.208 bp, an increase of +7.5% y/y. Among the major changes in the year, the increase in investments in securities of private companies must be highlighted, as it grew +110.3%.

Stockholders' equity. As of June 2017, the stockholders' equity reached 4.958 mp, +5.2% y/y.

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.

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Peña Verde's Annual Income Statement (million MXN)

	2014	2015	2016	2017e
Gross Written Premiums	4,190.0	5,142.6	6,865.5	7,414.7
Premiums Ceded	986.1	1,219.2	1,989.8	1,853.7
Net Premiums Retained	3,203.9	3,923.3	4,875.7	5,561.0
<i>Net Premiums Retained rate</i>	<i>76%</i>	<i>76%</i>	<i>71%</i>	<i>75%</i>
Net Increase in Provision for Unaccrued Premiums	314.7	107.0	367.3	419.0
Retention Premiums Accrued	2,889.2	3,816.3	4,508.3	5,142.1
Acquisition Costs	907.5	1,004.2	1,317.1	1,473.7
<i>Aquisition ratio</i>	<i>28%</i>	<i>26%</i>	<i>27%</i>	<i>27%</i>
Insurance claims incurred	1,694.9	2,542.5	3,065.5	2,931.0
<i>Claims ratio</i>	<i>59%</i>	<i>67%</i>	<i>68%</i>	<i>57%</i>
Underwriting (technical) income (loss)	286.9	269.6	125.7	737.4
Net Increase in Other Technical Reserves	282.9	330.8	90.1	475.7
Gross Income	4.3	-61.0	35.6	355.3
Net Operating Expenses	320.1	451.3	604.9	594.7
<i>Operating ratio</i>	<i>10%</i>	<i>12%</i>	<i>12%</i>	<i>11%</i>
Operating income (loss)	-315.8	-512.3	-569.2	-239.4
Comprehensive Financing Result	363.6	1,369.7	920.8	1,330.0
Earnings before income tax	47.8	857.4	351.6	1,090.6
Income tax payment provision	-9.9	204.2	89.7	327.2
Income tax rate	-20.8%	23.8%	25.5%	30.0%
Net profit (loss)	46.2	613.1	256.6	763.4
Minority interest	11.6	40.1	5.3	15.7
Majority Net Profit	46.2	613.1	256.6	747.8
EPS	0.10	1.29	0.54	1.60
Number of shares (million)	476.7	476.7	476.7	476.7
Gross Written Premiums growth	26.2%	22.7%	33.5%	8.0%
Net profit growth	-22.4%	1228.1%	-58.1%	191.4%
EPS growth	-22.4%	1228.1%	-58.1%	197.5%
Cost index				
Aquisition Ratio	28.3%	25.6%	27.0%	26.5%
Claims Ratio	58.7%	66.6%	68.0%	57.0%
Operation Ratio	10.0%	11.5%	12.4%	10.0%
Combined Ratio	97.0%	103.7%	107.4%	93.5%
Other Indicators				
P/E	95.00x	7.92x	18.72x	6.49x
P/BV	1.32x	1.23x	1.13x	0.97x
BV per share	7.0	8.3	8.9	10.7
PV's share price	9.2	10.2	10.1	10.4
Balance Sheet Summary (million MXN)				
Assets	12,569	15,224	18,397	18,979
Investments	9,741	11,735	13,407	13,675
Liabilities	8,949	10,939	14,092	13,810
Total Equity	3,619	4,285	4,305	5,169
Shareholder's Equity (majority)	3,327	3,940	4,263	5,118

Source: Prognosis and BMV

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