

PEÑA VERDE

Quarterly Report 3Q17

Current Price: MXN 10.18

2018 Target Price: MXN 11.30 (no discount for illiquidity applied)

Monday, November 06, 2017

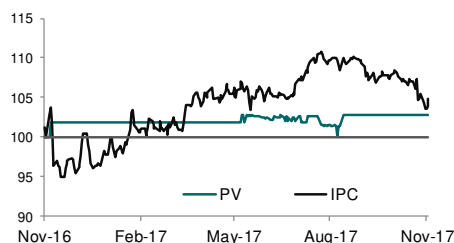
Quarterly results fell below expectations. The growth rate of written premiums slowed down, the operating loss rose, and financial gains fell, due to foreign exchange losses in the investment portfolio.

- Written Premiums of “General de Seguros” fell -9.2%, but those of “Reaseguradora Patria” jumped +21.4%.
- The comprehensive financing result of 830 mp fell vs the 930 mp of 2Q16.
- Net income of 477 mp slid -26.6% in the nine months to 3Q17.
- We maintain our y-e 2018 target price at 11.30 ps per share.

Key Data

Local Ticker	PV* MM
Exchange	BMV
12 Month T.P. (Estimated Fair Value)	MXN 11.30
Last Price	MXN 10.18
Expected Return	11.0%
12M Div. Yield	0.1%
Expected Dividend Yield	2.0%
Total Expected Return	13.0%
LTM Return PV*	2.8%
LTM Price Range	(10.18 - 9.90)
Outstanding Shares (Million)	476.68
Free Float	2.77%
Trading Volume	Low
Market Cap (USD Million)	USD 255.09
P/E (TTM)	57.90X
Price/Book Value	1.03X
Official Website	www.corporativopv.mx

12M Return vs IPC



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 55.3% in the 3Q17, partly supported by a change in methodology in the calculation of claims incurred but not reported (IBNR).

Target Price. We reiterate our y-e 2018 target price at 11.30 pesos per share. This price is equivalent to 1.3 times our forecasted 2018 book value. **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.

Low capitalization and marketability. The market capitalization of the issuer is USD 255 million, 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 increases its likelihood, potentially increasing the float and improving the visibility of the shares.

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.

	2015	2016	2017f
Valuation			
P/E	7.9x	18.7x	7.8x
P/BV	1.2x	1.1x	1.0x
Estimates (MXN million)			
Gross Written Premiums	5,143	6,865	7,218
YoY%		33.5%	5.1%
Net Retained Premiums	3,923	4,876	5,615
YoY%		24.3%	15.2%
Underwriting Income	270	126	648
YoY%		-53.4%	415.7%
Net income	613	257	623
YoY%		-58.1%	142.6%
EPS	1.3	0.5	1.3
YoY%		-58.1%	142.6%
Profitability			
Combined Ratio	103.7%	107.4%	96.7%
Acquisition Ratio	25.6%	27.0%	28.9%
Claims Ratio	66.6%	68.0%	56.7%
Operation Ratio	11.5%	12.4%	11.1%

Source: Peña Verde and Prognosis estimates
n.m.: not meaningful

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1. 3Q17 Report (accumulated data from January to September)

Peña Verde's written premiums totaled 4.997 billion pesos (bp) by the end of 3Q17, an increase of +4.2% y/y against the 4.794 bp in 3Q16. The recent figure was boosted by the good dynamism of "**Reaseguradora Patria**", which had sales of 2.399 bp, +21.4% y/y in 3Q17, resulting from increases in reinsurance premiums, considering refinancing operations and life.

On the other hand, the subsidiary "**General de Seguros**" reached premiums of 2.356 bp, which represented a drop of -9.2%, mainly due to the decrease in the insurance business of CADENA (component of attention to natural disasters) in the livestock branch, bringing the agricultural and livestock sector to plunge -42.5%. On the other hand, the "life" sector fell -11.2%. Such drops were compensated by the increase of +13.4% in the automobile sector.

Net increase in reserves. As of September 2017, the current and outstanding risk reserve of 246 million pesos (mp), showed a decrease of -36.7% compared to September 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.

Acquisition costs reached 1.141 bp in the three quarters of 2017, +23.2% (above the growth rate of written premiums) to 926 mp in the equivalent period of 2016, "influenced by the growth in reinsurance commissions paid to the ceding companies and the excess-loss coverage costs that protect the retention." The net cost of acquisition represented 28.9% of the retained premiums, whereas a year ago it was 25.4%.

Insurance claims incurred fell -1.4% y/y, totaling 2.050 bp. Peña Verde's claims ratio settled at 55.3%, which means a fall of 8.37 percentage points compared to the figure of 3Q16. This is explained by the change in the methodology of claims IBNR, that was introduced in 2016. The claims ratio remains at a very low historical level.

The technical profit increased to 513 mp in 3Q17 from 257 mp. This recovery is the result of: 1) a higher revenue, 2) lower increase in the risk reserve and 3) a lower net increase in the reserves for claims IBNR.

Operating income was -387 mp, which worsened vs the loss of -204 mp in 3Q16.

The comprehensive financing result posted a gain of 836 mp, falling -29.1%. Such change was the result of a forex loss in the portfolio and mark to market valuations.

Finally, PV* reported a **net income** of 477 mp, a decrease of -26.6% y/y.

Total assets amounted to 18.980 bp, an increase of +21.6% vs the first quarter of 2016. Among the major changes in the year, it must be noted that investments grew +17.9% also vs the 1Q16.

Stockholders' equity. As of September 2017, the stockholders' equity reached 4.663 bp, a book value per share of 9.8 pesos, +2.3% 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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Income Statement

	Accumulated data			Non accumulated data		
	3Q17	3Q16	YoY Change	3Q17	3Q16	YoY Change
Gross Written Premiums	4,997	4,794	+4.2%	1,806	1,852	-2.5%
Net Retained Premiums	3,950	3,650	+8.2%	1,351	1,396	-3.2%
Retention Premiums Accrued	3,704	3,262	+13.5%	1,296	1,277	+1.5%
Acquisition Costs	1,141	926	+23.2%	430	321	+34.0%
Insurance Claims Incurred	2,050	2,078	-1.4%	800	637	+25.5%
Underwriting (Technical) Income (Loss)	513	257	+99.3%	66	319	-79.3%
Net Operating Expenses	503	522	-3.6%	179	226	-21.1%
Operating Income (Loss)	-387	-204	+90.0%	-244	72	n.m.
Comprehensive Financing Result	836	1,178	-29.1%	-94	203	n.m.
Net Profit (Loss)	477	649	-26.6%	-201	234	n.m.
<i>Acquisition Ratio</i>	28.9%	25.4%	+351 bp	31.8%	23.0%	+883 bp
<i>Claims Ratio</i>	55.3%	63.7%	-837 bp	61.7%	49.9%	+1,183 bp
<i>Operating Ratio</i>	12.7%	14.3%	-156 bp	13.2%	16.2%	-299 bp
Combined Ratio	97.0%	103.4%	-642 bp	106.7%	89.1%	+1,767 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.

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Peña Verde's Annual Income Statement (MXN millions)

	2015	2016	2017f
Gross Written Premiums	5,143	6,865	7,218
(-) Ceded Premiums	1,219	1,990	1,603
Net Premiums Retained	3,923	4,876	5,615
<i>Net Premiums Retained rate</i>	<i>76%</i>	<i>71%</i>	<i>78%</i>
(-) Net Increase in Provision for Unaccrued Premiums	107	367	366
Retention Premiums Accrued	3,816	4,508	5,250
(-) Acquisition Costs	1,004	1,317	1,624
<i>Acquisition ratio</i>	<i>26%</i>	<i>27%</i>	<i>29%</i>
(-) Insurance claims incurred	2,543	3,065	2,977
<i>Claims ratio</i>	<i>67%</i>	<i>68%</i>	<i>57%</i>
Underwriting (technical) income (loss)	270	126	648
(-) Net Increase in Other Technical Reserves	331	90	534
Gross Income	-61	36	114
(-) Net Operating Expenses	451	605	623
<i>Operating ratio</i>	<i>12%</i>	<i>12%</i>	<i>11%</i>
Operating income (loss)	-512	-569	-509
Comprehensive Financing Result	1,370	921	1,170
Earnings before income tax	857	352	661
(-) Income tax payment provision	204	90	29
<i>Income tax rate</i>	<i>24%</i>	<i>26%</i>	<i>4%</i>
Net profit (loss)	613	257	623
Minority interest	40	5	10
Majority Net Profit	613	257	623
EPS (TTM)	1.3	0.5	1.3
Number of shares (million)	476.7	476.7	476.7
<i>Gross Written Premiums growth</i>	<i>N/A</i>	<i>34%</i>	<i>5%</i>
<i>Net Profit Growth</i>	<i>N/A</i>	<i>-58%</i>	<i>143%</i>
<i>EPS growth</i>	<i>N/A</i>	<i>-58%</i>	<i>143%</i>

Other Indicators

	2015	2016	2017f
ROE	16%	6%	13%
P/E	7.9	18.7	7.8
P/BV	1.2	1.1	1.0
Book Value Per Share	8.3	9.0	10.2

Balance Sheet Summary (MXN millions)

	2015	2016	2017f
Assets	15,224	18,397	19,701
Investments	11,733	13,407	14,562
Liabilities	10,939	14,092	14,842
Technical Reserves	8,897	11,043	12,022
Total Equity	4,285	4,305	4,860
Shareholder's Equity (majority)	3,954	4,263	4,809

Source: Prognosis and BMV

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