

# Peña Verde

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



## 4Q17 quarterly report and medium-term outlook

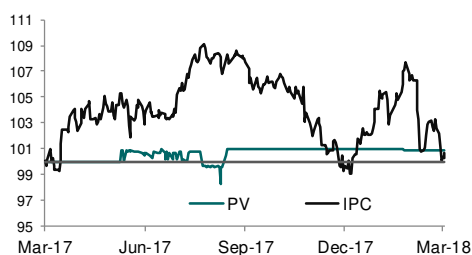
martes, 06 de marzo de 2018

### Solid net income in 2017, based on an excellent return on the investment portfolio, supports the first phase of a stronger corporate governance and the beginning of the digital technology improvement phase

#### 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*	0.9%
LTM Price Range	(10.18 - 9.91)
Outstanding Shares (Million)	476.68
Free Float	2.77%
Trading Volume	Low
Market Cap (USD Million)	USD 258.03
P/E (TTM)	8.31X
Price/Book Value	1.00X
Official Website	www.corporativopv.mx

#### 12M Return vs IPC



	2015	2016	2017	2018f
<b>Valuation</b>				
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

- 2017/2016 results.** Written premiums totaled 6,945 mp, a moderate increase of +1.2%. However, the technical profit totaled 362.0 mp, doubling the 2016 figure. The operating loss was 707.0 mp, but the comprehensive financing result was 1,368 mp, a strong increase of +50%. Thus, the profit reached 583 mp, an EPS of 1.2 pesos per share, more than a +100% growth against that of 2016 (0.54 pesos). The multiple P/E is 8.5X and the P/BV is 1.0X.
- 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 more cautious one in General de Seguros in the coming years.
- Low market cap. and trading volume.** The capitalization value of the issuer is approximately MXN 4,805 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 the premiums of PV\* will grow ~8%, driven by a growth of more than 20% in the Reaseguradora Patria business and a decrease of ~4% in the General de Seguros segment. We also anticipate an improvement in the combined ratio to 94% from the 104% in 2017. Capital gains of the portfolio could be slightly lower than those in 2017. Thus, we reached an estimated net profit of 818 mp, an EPS of 1.7 pesos.
- Target price.** We introduce our 12-month T.P. at 11.90 pesos, equivalent to 1.0X the estimated 2018 book value. This multiple is lower than the implicit or fair multiple that results from the Damodaran model, which is 1.05X. However, we do not incorporate a 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, higher a claims ratio, liquidity, ceded reinsurances (counterparty, strategic partners) and credit in their investments.
- 2018 relevant events.** During the current year, General de Seguros will be delisted from the BMV.

### 1. 2017 report

#### Income Statement

	Accumulated data		
	4Q17	4Q16	YoY Change
<b>Gross Written Premiums</b>	6,945	6,865	+1.2%
<b>Net Retained Premiums</b>	5,521	4,876	+13.2%
<b>Retention Premiums Accrued</b>	5,096	4,508	+13.0%
Acquisition Costs	1,550	1,317	+17.7%
Insurance Claims Incurred	3,184	3,065	+3.9%
<b>Underwriting (Technical) Income (Loss)</b>	362	126	+187.7%
Net Operating Expenses	720	605	+19.1%
<b>Operating Income (Loss)</b>	-707	-569	+24.2%
Comprehensive Financing Result	1,368	921	+48.6%
<b>Net Profit (Loss)</b>	583	257	+127.4%
<b>Acquisition Ratio</b>	28.1%	27.0%	+106 bp
<b>Claims Ratio</b>	62.5%	68.0%	-552 bp
<b>Operating Ratio</b>	13.0%	12.4%	+64 bp
<b>Combined Ratio</b>	<b>103.6%</b>	<b>107.4%</b>	<b>-381 bp</b>

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 6,945 million pesos (mp) in 2017, an increase of +1.2% y/y against the 6,865 mp in 2016. This variation is mainly explained by the dynamism of "Reaseguradora Patria", whose sales grew +25.7% y/y, reaching 3,459 mp. The branches with the highest growth were: fires (+454%), miscellaneous (+167%) and agricultural (+13.3%).

On the other hand, the subsidiary "**General de Seguros**" reached sales of 3,075 mp, which represented a decrease of -19.1%, due to some effects: the premiums in the fire, miscellaneous and civil segments decreased by 480 mp per business that were not renewed; in addition, the company suffered from a lower dynamism in the the CADENA program (Component of Natural Disaster Assistance).

The subsidiary **Patria Corporate Member Ltd**, which operates since January 2016 in the Lloyd's market in London, reported sales equivalent to 402.7 mp, +32.3%.

**The net consolidated acquisition cost** of PV \* amounted 1,550 mp in 2017, which compared to the 1,317 mp in 2016, showed an increase of +17.7%.

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**The net cost of consolidated claims** increased +3.9%, standing at 3,184 million pesos. Peña Verde's claims ratio was 62.5%, showing a decrease of 5.5 percentage points.

In line with the acquisition and claims costs, the **technical profit** increased + 188% YoY to 362 mp. added to this, net operating expenses totaled 720.5 mp. considering the net increase in technical reserves -affected by the regulatory change- PV registered an **operating loss** of 707 mp, up +24.2%.

The **integral result of financing** registered a gain of 1,368.4 million pesos, an important advance of +48.6%, generated mainly by shares liquidation and capital gains, despite a decrease in foreign exchange gains.

**PV reported a net profit** of 583.5 mdp, which compares favorably with respect to the 257 mdp of the previous year. This favorable result is based on (1) higher income from premiums, (2) decrease in the IBNR reserves, and (3) the good performance of the financial markets that benefited portfolio gains.

### Financial situation

**Assets amount to 20,679.9 mp** which, compared to the close of the previous year, show an increase of + 12.4%. Among the biggest changes in the year, there is an increase in investments in securities, reinsurers and reinsures, permanent investments, availability and other assets.

**Stockholder's equity.** As of December 2017, the majority stockholders' equity reached an amount of 4,842.2 mp (BV of 10.2 pesos per share), an increase of + 12.5%.

### 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.

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### Peña Verde's Annual Income Statement (MXN millions)

	2015	2016	2017	2018f
<b>Gross Written Premiums</b>	5,143	6,865	6,945	7,501
(-) Ceded Premiums	1,219	1,990	1,424	1,552
<b>Net Premiums Retained</b>	3,923	4,876	5,521	5,949
<b>Net Premiums Retained rate</b>	76%	71%	79%	79%
(-) Net Increase in Provision for Unaccrued Premiums	107	367	425	476
<b>Retention Premiums Accrued</b>	3,816	4,508	5,096	5,473
(-) <b>Acquisition Costs</b>	1,004	1,317	1,550	1,487
<b>Acquisition ratio</b>	26%	27%	28%	25%
(-) <b>Insurance claims incurred</b>	2,543	3,065	3,184	3,120
<b>Claims ratio</b>	67%	68%	62%	57%
Underwriting (technical) income (loss)	270	126	362	866
(-) <b>Net Increase in Other Technical Reserves</b>	331	90	349	270
Gross Income	-61	36	13	596
(-) <b>Net Operating Expenses</b>	451	605	720	714
<b>Operating ratio</b>	12%	12%	13%	12%
<b>Operating income (loss)</b>	-512	-569	-707	-117
<b>Comprehensive Financing Result</b>	1,370	921	1,368	1,310
Earnings before income tax	857	352	661	1,192
(-) Income tax payment provision	204	90	67	358
<b>Income tax rate</b>	24%	26%	10%	30%
<b>Net profit (loss)</b>	613	256.6	583	818
Minority interest	40	5.3	10	17
Majority Net Profit	613	256.6	583	818
<b>EPS (TTM)</b>	1.3	0.5	1.2	1.7
Number of shares (million)	476.7	476.7	476.7	476.7
<b>Gross Written Premiums growth</b>	N/A	34%	1%	8%
<b>Net Profit Growth</b>	N/A	-58%	127%	40%
<b>EPS growth</b>	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
<b>Assets</b>	15,224	18,397	20,677	22,913
Investments	11,733	13,407	14,756	16,709
<b>Liabilities</b>	10,939	14,092	15,835	17,253
Technical Reserves	8,897	11,043	12,610	14,665
<b>Total Equity</b>	4,285	4,305	4,842	5,660
<b>Shareholder's Equity (majority)</b>	3,954	4,263	4,794	5,604

Source: Prognosis and BMV

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