

Peña Verde

Current price: MXN 10.18
12-month target price: MXN 9.80
(No liquidity risk discount applied).



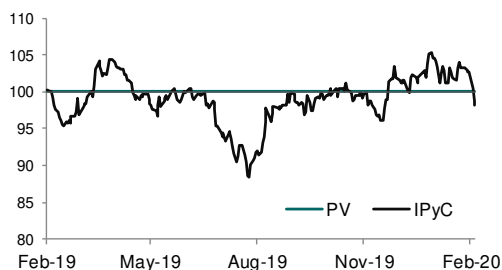
**4Q19 quarterly report and
medium-term outlook**
miércoles, 04 de marzo de 2020

4Q higher than expectations supports good earnings result in 2019. New plan 2020-2025 proposes digital, cultural and organizational transformation that could trigger strong growth in the medium term

Key Data

Ticker	PV* MM
Exchange	BMV
12 Month T.P. (Estimated Fair Value)	MXN 9.80
Last Price	MXN 10.18
Expected Return	-3.7%
12 M Dividend Yield	0.0%
Expected Dividend Yield	0.0%
Total Expected Return	-3.7%
LTM Return PV*	0.0%
LTM Price Range (MXN)	(10.18 - 10.18)
Outstanding Shares (Million)	476.7
Free Float	1.22%
Trading Volume	Low
Market Cap (USD Million)	USD 252.64
P/E (TTM)	10.9X
Price/Book Value	1.0X
Official Website	www.corporativopv.mx

12M Return vs IPyC



	2017	2018	2019	2020f
Valuation				
P/E	8.3x	-8.7x	10.9x	37.9x
P/BV	1.0x	1.1x	1.0x	1.0x
ROE	12.2%	-13.3%	9.4%	2.6%
Estimates (MXN million)				
Gross Written Premiums	6,965	7,259	8,163	9,224
YoY%	1.5%	4.2%	12.4%	13.0%
Net Retained Premiums	5,521	5,908	6,615	7,840
YoY%	13.2%	7.0%	12.0%	18.5%
Underwriting Income	357	680	796	958
YoY%	184.2%	90.3%	17.1%	20.3%
Net income	583	-561	446	128
YoY%	127.2%	n.m.	n.m.	-71.3%
EPS	1.2	-1.2	0.9	0.3
YoY%	127.2%	n.m.	n.m.	-71.3%
Profitability				
Adjusted Combined Ratio	100%	94%	101%	103%
Acquisition Ratio	28%	30%	30%	29%
Claims Ratio	62%	57%	57%	58%
Operation Ratio	10%	7%	14%	16%

Source: Peña Verde, Bloomberg and Prognosis estimates

Note: Adjusted combined ratio is calculate over net retained premiums

n.m.: not meaningful

- 2019/2018 results³.** Written premiums totaled 8,163 mp, an increase of +12.4%, driven by the rise in premiums issued by the reinsurance business that offset the fall in insurance premiums. Technical profit rose +17% to 796 mp; while, operating expenses increased +76% with an operating loss of -757 mp. On the other hand, the comprehensive financing result recorded gains of 1,431 mp, which contrast with losses of -304 mp in 2018. Thus, net profit was for 446 mp, recovering from the loss in 2018, and an EPS of 0.93.
- 2020 Estimates.** Guided by the company, we expect written premiums to grow approximately +13.0%. This rate would result from a growth consolidation in the reinsurance business and a gradual recovery of the insurance business after the organizational restructuring. We anticipate an adjusted combined index of around 103%, with increases in operating expenses related to the transformation of the company. For the comprehensive financial result, we expect it to report a normalized gain close to Cetes 28d, reaching 1,039 mp and a net profit of 128 mp at the end of 2020, equivalent to an EPS of 0.3 pesos.
- New 2020-2025 Plan.** The company has launched a new digital, cultural and organizational transformation plan that could be a catalyst for solid growth in the medium-term. This plan encompasses all Peña Verde's divisions with a horizon of 5 years, in which the company proposes; among other things, generate value, consolidate solid and sustainable growth and seek greater visibility in the stock market in order to access additional sources of financing that leverage future growth.
- Risk management.** The company visualizes itself as a specialist in risk management and plans to capitalize on this expertise, including a successful historical management of its investment portfolios.
- Low market cap. and trading volume.** The capitalization value of the issuer is approximately MXN 4,853 million, its trading volume is minimal, and its free float is only 1.2%, 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.
- Target price.** We introduce our 12-month T.P at 9.80 pesos, equivalent to 0.9X the estimated 2020 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, a higher claims ratio, liquidity, ceded reinsurances (counterparty, strategic partners) and credit risk in their investments.

³ Note: The figures presented in the report are preliminary. They do not include the fourth quarter of 2018 and 2019 of Patria Corporate Member LTD given the difference in reporting times of the operation in the United Kingdom.

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5-year Peña Verde Group business plan

Since the publication of the 4Q19 PV report in the BMV stock market, it has become clear that attention to the potential investor has increased, given the richer and clearer information reported. After the conference with the management – strengthened with new members with experience- it became clear that a transformation, not only organizational, but cultural and modernizer through investment commitments in digital technology, is underway.

Organizational. To begin with, the company announced the hiring of Andres Millan to Peña Verde Group, an executive with experience – among other places, in the World Bank – as Vice President of Asset Management and Financial Strategy, with the departure of María Cristina Rohde, who until November had served as General Director of Administrative Services of PV. In addition to that, the function of investor relations is formalized with the hiring of Miguel Angel Murcio (Corporate Finance Manager).

On the other hand, the role of the SAPV holding is transformed with two important functions to support the companies: 1) Business support and transformation and 2) asset management and financial strategy. It is worth mentioning that the Group is divided into two divisions, that of Insurance, which brings of Health and the Call Center and the Reinsurance division formed by Patria and Patria Corporate Member LTD in London.

Cultural. A greater professionalization of the subscription of risks and operation processes is sought, with measurements parameters that did not exist before.

Digital. The administration decided to promote a digital transformation of all its processes. To do this, it will invest 4% of its total revenues in cutting-edge technology to compete more strongly in the Mexican financial market. Of this total, between 15 and 25% of the resources will be classified as investment (CAPEX) and the remaining as operating expense.

The main objective of the transformation embodied in the 5-year Business Plan is to generate value for PV shareholders, customers and employees. Realistically, the plan sees that around 2023 the company could be growing at high and sustained rates, maintaining good profitability. A very important additional objective is to improve the visibility of the Group and its relationship with the stock market, in order to help leverage future growth. Over time, in our view, this will result in actions that gradually increase the stock market value of PV*.

2019 annual report, preliminary figures⁴

Income Statement			
	Accumulated data		
	4Q19	4Q18	YoY Change
Gross Written Premiums	8,163	7,259	+12.4%
Net Retained Premiums	6,615	5,908	+12.0%
Retention Premiums Accrued	6,184	5,683	+8.8%
Acquisition Costs	1,858	1,792	+3.7%
Insurance Claims Incurred	3,530	3,211	+9.9%
Underwriting (Technical) Income (Loss)	796	680	+17.1%
Net Operating Expenses	885	503	+75.8%
Operating Income (Loss)	-757	-512	+47.7%
Comprehensive Financing Result	1,343	-304	n.m.
Net Profit (Loss)	446	-561	n.m.
<i>Acquisition Ratio</i>	28.1%	30.3%	-225 bp
<i>Claims Ratio</i>	57.1%	56.5%	+58 bp
<i>Operating Ratio</i>	10.8%	6.9%	+391 bp
Adjusted Combined Ratio	96.0%	93.8%	+223 bp

Source: Prognosis and PV

n.m.: not meaningful

Note: Adjusted combined ratio is calculated over retention premiums accrued.

Peña Verde's written premiums totaled 8,163 million pesos (mp) in 2019, an increase of +12.4% y/y against the 7,259 mp in 2018. This variation is mainly explained by the great dynamism of "**Reaseguradora Patria**", that compensated for the low performance of "**General de Seguros**", which issued premiums for 2,555 mp, a decrease of -6.5% y/y, mainly due to "decreases in agriculture, fire and cars by 35.5%, 17.1% and 3.6%, respectively".

The subsidiary **Patria Corporate Member Ltd**, which operates since January 2016 in the Lloyd's market in London, reported sales equivalent to 538 mp, +19.1% y/y.

The net consolidated acquisition cost of PV * amounted 1,858 mp in 2019, which compared to the 1,792 mp in 2018, showed an increase of +3.7%. This resulted from an increase in reinsurance commissions paid to ceding companies and the costs associated with "excess losses" from hedges that protect retention.

The net cost of consolidated claims increased +9.9%, standing at 3,530 mp. Peña Verde's adjusted claims ratio was 57.1%, an increase of 6 percentage points.

In line with the acquisition costs and claims, the **technical profit** increased +17.1% y/y to 796 mp. In addition, net operating expenses totaled 885 mp and considering the net decrease in technical reserves, PV recorded an **operating loss** of -757 mp.

⁴ Note: The figures presented in the report are preliminary. They do not include the fourth quarter of 2018 and 2019 of Patria Corporate Member LTD given the difference in reporting times of the operation in the United Kingdom.

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The **comprehensive financial result** recorded gains of 1,343 mp, that compares favorably against the losses of 304 mp in 2018. This was the result of a "i) gains in the valuation of the equity portfolio, ii) profit from the sale of equity instruments and, iii) the yield of fixed income instruments".

As a result of all the above, **PV reported a net profit** of 446 mp, mainly due to the good performance of the portfolio and the growth in the written premiums which offset the rise in operating expenses.

Financial situation

Summary of the Balance Sheet (MXN millions)

	4Q19	%	4Q18	%	YoY Change
Investments	15,943	69.4%	14,586	72.6%	+9.3%
Receivables	2,494	10.9%	2,249	11.2%	+10.9%
Reinsurers	3,546	15.4%	2,342	11.7%	+51.4%
Other Assets	459	2.0%	384	1.9%	+19.7%
Total Assets	22,978	100.0%	20,086	100.0%	+14.4%
Technical Reserves	13,995	60.9%	12,458	78.8%	+12.3%
Reinsurers	2,018	8.8%	1,457	9.2%	+38.5%
Other Liabilities	1,139	5.0%	1,070	6.8%	+6.4%
Total Liabilities	18,186	79.1%	15,819	78.8%	+15.0%
Stockholder's Equity	4,792	20.9%	4,267	21.2%	+12.3%
Total Liabilities + Equity	22,978	100.0%	20,086	100.0%	+14.4%

Source: Prognosis based on GNP

n.m.: not meaningful

Assets amounted to 22,978 mp, +14% y/y. Among the major changes in the year, there was the increase of investments securities, reinsurers, and a jump of receivables.

Stockholder's equity. As of December 2019, the majority stockholders' equity reached an amount of 4,792 mp (BV of 10.05 pesos per share), a rose of +12.3% 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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2020 Forecasts

After discussing with the management, we expect that written premiums would grow around +13%. This rate would result from a consolidation of growth in the reinsurance business and some recovery of the insurance business after the organizational restructuring.

We have conservative assumptions for the cost structure that suppose a marginal increase from the level reached in 2019. Therefore, we estimate an adjusted combined index around 103%, higher than the one observed in 2019, with the cost composition skewed to a greater operating index resulting from technology expenses, relating to the digital transformation goal.

Finally, we assume that the comprehensive financial result reports a normalized gain close to Cetes 28d, reaching 1,039 mp and a net profit of 128 mp at the end of 2020, equivalent to an EPS of 0.3 pesos.

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Peña Verde's Annual Income Statement (MXN millions)

	2015	2016	2017	2018	2019	2020f
Gross Written Premiums	5,143	6,865	6,965	7,259	8,163	9,224
(-) Ceded Premiums	1,219	1,990	1,444	1,351	1,548	1,384
Net Retained Premiums	3,923	4,876	5,521	5,908	6,615	7,840
<i>Retention rate</i>	76%	71%	79%	81%	81%	85%
(-) Net Increase in Provision for Unaccrued Premiums	107	367	497	224	431	470
Retention Premiums Accrued	3,816	4,508	5,025	5,683	6,184	7,370
(-) Acquisition Costs	1,004	1,317	1,550	1,792	1,858	2,137
<i>Acquisition ratio</i>	26%	29%	31%	32%	30%	29%
(-) Insurance claims incurred	2,543	3,065	3,117	3,211	3,530	4,274
<i>Claims ratio</i>	67%	68%	62%	57%	57%	58%
Underwriting (technical) income (loss)	270	126	357	680	796	958
(-) Net Increase in Other Technical Reserves	331	90	349	689	668	643
Gross Income	-61	36	9	-9	128	315
(-) Net Operating Expenses	451	605	720	503	885	1,179
<i>Operating ratio</i>	12%	13%	14%	9%	14%	16%
Operating income (loss)	-512	-569	-712	-512	-757	-864
Comprehensive Financing Result	1,370	921	1,368	-304	1,343	1,039
Earnings before income tax	857	352	657	-816	586	176
(-) Income tax payment provision	204	90	63	-250	137	47
<i>Income tax rate</i>	24%	26%	10%	31%	23%	27%
Net profit (loss)	613	256.6	583	-561	446	128
Minority interest	40	5.3	10	-6	4	0
Majority Net Profit	613	256.6	583	-561	446	128
EPS (TTM)	1.3	0.5	1.2	-1.2	0.9	0.3
Number of shares (million)	476.7	476.7	476.7	476.7	476.7	476.7
<i>Gross written premiums growth</i>		+33.5%	+1.5%	+4.2%	+12.4%	+13.0%
<i>Net retained premiums growth</i>		+24.3%	+13.2%	+7.0%	+12.0%	+18.5%
<i>Retention premiums accrued growth</i>		+18.1%	+11.5%	+13.1%	+8.8%	+19.2%
<i>Net profit growth</i>		-58.1%	+127.2%	n.m.	n.m.	-71.3%
<i>EPS growth</i>		-58.1%	+127.2%	n.m.	n.m.	-71.3%

Other Indicators

	2015	2016	2017	2018	2019	2020f
ROE	15.5%	6.0%	12.2%	-13.3%	9.4%	2.6%
P/E	7.9	18.7	8.3	-8.7	10.9	37.9
P/BV	1.2	1.1	1.0	1.1	1.0	1.0
Book Value Per Share	8.3	9.0	10.2	9.0	10.1	10.3

Balance Sheet Summary (MXN millions)

	2015	2016	2017	2018	2019	2020f
Assets	15,224	18,397	20,681	20,086	22,978	24,521
Investments	11,733	13,407	14,756	14,586	15,943	17,248
Liabilities	10,939	14,092	15,841	15,819	18,186	19,600
Technical Reserves	8,897	11,043	12,610	12,458	13,995	15,680
Total Equity	4,285	4,305	4,840	4,267	4,792	4,920
Shareholder's Equity (majority)	3,954	4,263	4,792	4,228	4,748	4,875

Source: Prognosis and BMV

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Prognosis

Economía, Finanzas e Inversiones S.C.

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