

CIG Pannonia

Recommendation: Neutral (unch.)

Target price (e-o-y): HUF 315 (unch.)

Share price: HUF 335

Share price as of 18/11/2020	HUF 335	Bloomberg	PANNONIA HB
Number of diluted shares [million]	94.4	Reuters	CIGP.BU
Market capitalization [HUF bn/EUR mn]	31 633/87.7	Free float	75%
Daily turnover 12M [HUF million]	0.08	52 week range	HUF 100 – 388

Surprisingly weak Q3 results

Equity Analyst

Attila Vágó

+361 489 2265

a.vago@con.hu

Alkotas Point

55-61 Alkotás utca,

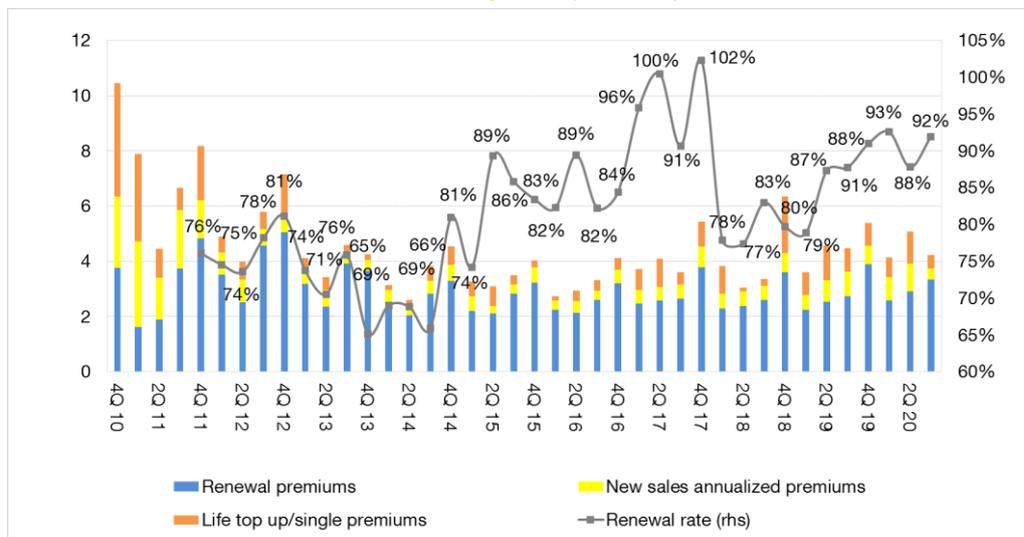
H-1123 Budapest

www.con.hu

- CIG Pannonia Life Insurance (Pannonia) reported an unexpectedly low profit after tax of HUF 9mn for Q3/20 compared to HUF 489mn in the same period a year earlier and HUF 520mn in Q2/20. The precipitous fall in after-tax profit on a QoQ basis was primarily due to significantly lower GWP and higher OpEx. The increase in OpEx was driven by the expected loss on policies sold by CIG Pannónia Pénzügyi Közvetítő Zrt, a wholly-owned agent subsidiary.
- In Q1-3/20, the insurer's consolidated profit before tax amounted to HUF 1bn (in 2019 the profit before taxation was HUF 282mn), that was reduced by HUF 162mn tax liability. EMABIT as discontinued non-life operation generated HUF 100mn loss. The overall profit after tax was HUF 746mn, which is HUF 1.06bn higher than the profit after tax of first three quarter in 2019. The other comprehensive income contains the decrease in the fair value of available-for-sale financial assets amounting to HUF 958mn, of which HUF 667mn is the unrealized loss on OPUS shares owned by the Group, while the remaining loss (HUF 291mn) arose from the unrealized loss on government bonds. The total comprehensive income represents a gain of HUF 212mn in 2020.
- CIG Pannónia Life Insurer is financially stable, its fundamentals are certain, the Solvency II capital adequacy is outstandingly high 348%. The consolidated capital adequacy is 326%.
- Life insurance GWP rose by 11% YoY from HUF 4.6bn to HUF 5.1bn in Q2/19. In the life segment, the new acquisition amounted to HUF 0.7bn which was 36% lower compared to the new acquisition in the same period a year earlier. In the traditional segment the decrease was attributed to a significant group insurance policy, which increased the acquisition in the base period of 2019. While in case of the unit-linked products, the decrease is mainly due to the COVID-19.
- GWP of unit-linked life insurance dropped by 5% to HUF 4.2bn YoY (thereof 29%, ie. HUF 1.22bn was pension insurance policies), HUF 0.9bn were traditional life products (thereof HUF 0.3bn came from pension insurance policies), and HUF 0.1bn were health insurance policies. In the life segment GWP from the first annual premiums of policies sold came to HUF 0.4bn (-55% YoY). GWP from renewals was HUF 3.34bn in Q3/20 (+22YoY), while top-up and single premiums amounted to HUF 0.5bn (-41% YoY), the latter was mainly due to a decrease in unit-linked life insurance policies. Within the total life insurance premium income top-up and single premiums

represented 12% in Q3/20 compared to 19% in Q3/19. Non-life GWP dropped by 93% YoY from HUF 2.35bn to HUF 1bn mainly because of the divestment of some major activities.

GWP breakdown in the life insurance segment (HUF bln)

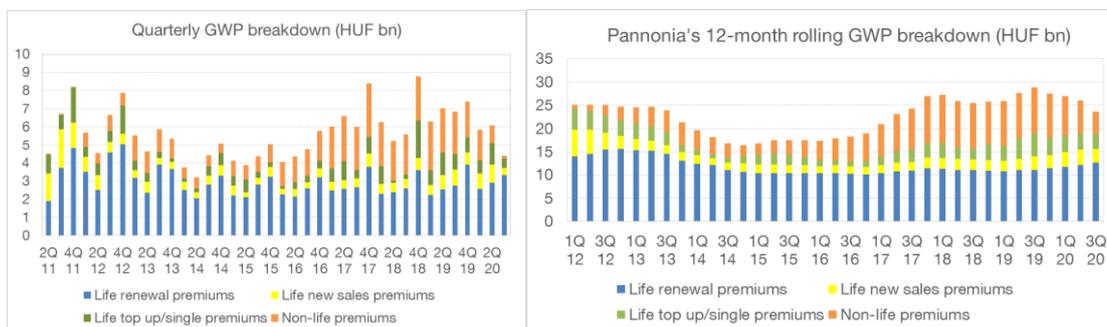


Source: Pannonia, Concorde estimate

- 12-month rolling GWP continued sliding for the fourth consecutive quarter due to deteriorating non-life premium income as a consequence of divestments.

Quarterly consolidated GWP breakdown (HUF bn)

12-m rolling GWP breakdown (HUF bn)



Source: Pannonia, Concorde estimate

- Pannonia earlier had decided to dispose of its Hungarian property, liability, goods in transit, cargo and vehicles insurance activities of its non-life company EMABIT (including more than 100 thousand pieces insurance with nearly HUF 6bn annualized premium), which is still subject to the approval of the Hungarian National Bank. Pannonia deems that the going concern is unsustainable in case of the EMABIT, therefore the whole activity of the non-life subsidiary has been defined as discontinued activity according to IFRS.
- As a result of recovery measures made earlier, EMABIT's solvency capital adequacy has been restored by increasing from 57% at 31 March, 2020 to 147% by 30 June 2020, including the additional capital requirement, but it fell again to 135% by the end of September, 2020 due to non-reinsured Italian surety insurance portfolio (of which the size was EUR 256mn at the end of 2019). For the most exposed and problematic product types (such as gaming which accounts for ca. 20% of total Italian exposure and 59% of non-reinsured portfolio) duration is less than six months. However, some of the contracts allow claims to be made even after the expiration date, for up to 1 year.

- Investment results were positive at HUF 2.7bn in Q3/20 as a result of an unprecedented recovery in the stock and bond market valuation after a collapse globally triggered by the outbreak of the coronavirus pandemic early this year.
- Operating costs rose by 23% YoY in Q3/20 and accounted for 38% of GWP in Q2/20 (vs. 30% in Q3/19), of which fees, commissions and other acquisition costs represented 54% (vs. 69% in Q3/19), while admin costs and other expenses (mainly provisions) accounted for the rest.
- Other expenses (HUF 333mn) is higher with HUF 275mn compared to the 2019 same period (HUF 51mn), the most significant part of the rise (HUF 185mn) is the expected loss on policies sold by CIG Pannónia Pénzügyi Közvetítő Zrt. Acquisition costs fell 4% YoY mainly due to traditional insurance products, and accounted for 128% of annualized premium of new sales compared to 98% in Q3/19. Net claims and related settlement expenses dropped by 26% YoY.
- As for life insurance policies sold so far in 2020 the share of the tied agent network is 12%, independent brokers bring in 36% and the bank channel accounts for 18%. The financial intermediary subsidiary delivers 6% of new sales, while other business developments represents 28 percent of new sales.
- We hold our view that only when it becomes clear that synergy can be achieved by realizing economies of scale and extracting cross-selling opportunities offered by new banking partners will we really be able to estimate how much profits can additionally be generated on a sustainable basis under the new leadership and through a close partnership with friendly domestic banks (Budapest Bank, MKB and Takarékbank, etc.). It is conceivable in our view, that CIG Pannonia could benefit from synergies from the partnership with these domestic banks in such scale that can be enough to explain a further improvement in stock valuation, and that our current estimate for CIG Pannonia's appraisal value proves to be too conservative.
- We still see an opportunity for CIG Pannonia to be more tactical with capital management (acquisitions, dividend payments) given its currently strong capital base, including a renewed shift in business mix towards the non-life segment and asset management while also focusing increasingly on selling healthcare insurance products. Evidently, in order for investors to ascribe higher multiples to CIG Pannonia's business, the insurer has to provide greater disclosure about how to develop growth of its businesses on a sustainable basis.
- We believe that CIG Pannonia has plenty of room to grow (in terms of premium income) more rapidly in the medium than larger insurance carriers in Hungary and at a quicker clip than the overall domestic insurance market once partnership with the friendly banks starts working. We are also confident that CIG Pannonia remains on track to achieve efficiency gains through diversification of its distribution channels. We reiterate both our TP at HUF 315 a share and our Neutral rating on the insurer.

Disclaimer

Concorde Securities Ltd. does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interests that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. For analysts' certification and other important disclosures, please refer to the "Disclaimer" section at the end of this report.

DISCLAIMER I.

This research report has been prepared by Concorde Securities Ltd., a full-service Hungarian investment banking, investment management and brokerage firm. Concorde Securities Ltd. is under the supervision of the National Bank of Hungary in its capacity as financial supervisory authority.

Concorde Securities Ltd. is registered in Hungary and does not have any subsidiaries, branches or offices outside of Hungary. Therefore we are not allowed to provide direct investment banking services to US investors and restrictions may apply to our potential investment banking services according to your country's jurisdiction.

Our salespeople, traders and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are their own and may be contrary to the opinions expressed in our research products, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed by our analysts or traders.

Our research, sales and trading professionals are paid based on the profitability of the respective divisions of Concorde Securities Ltd., which from time-to-time may include revenues from the firm's capital market activity. Concorde Securities Ltd. does not prohibit analysts, salespeople and traders from maintaining a financial interest in the securities or futures of any companies that they cover or trade on their clients' behalf in strict compliance with the Hungarian Capital Markets Act.

ANALYSTS CERTIFICATION

The research analysts undersigned and responsible for the preparation of this report hereby certify that (i) the views expressed in this research report accurately reflect their personal views about any and all of the securities or issuers referred to in this research report; (ii) no part of the analysts' compensation was, is or will be directly or indirectly related to the specific recommendation or views expressed in this report and (iii) no part of their compensation is tied to any specific investment transactions performed by Concorde Securities Ltd.

Name and job title of individuals involved in the production of this report are disclosed at the end of this report.

Concorde Securities Ltd. is a leading manager and underwriter of Hungarian equity offerings. We have investment banking and other business relations with a substantial percentage of the companies traded on the Budapest Stock Exchange and covered by our research department. Concorde Securities Ltd, its directors and employees may have a position in these securities, which may change at any time.

Concorde Securities Ltd. acted as Lead Manager of the private and public share placement of the shares of FHB in 2003, Masterplast in 2012 and Duna House in 2016. Concorde Securities Ltd. acted as the Co-lead Manager of Gedeon Richter's exchangeable bond issue in September 2004. Concorde Securities Ltd. has provided financial advice to Magyar Telekom.

EXPLANATION OF RATINGS AND METHODOLOGY

Rating	Trigger
Buy	Total return is expected to exceed 20% in the next 12 months
Accumulate	Total return is expected to be in the range of 10-20%
Neutral	Total return is expected to be in the range of 10%-(-10%)
Reduce	Total return is expected to be in the range of -10-(-20%)
Sell	Total return is expected to be lower than -20%
Under Revision	The stock is put Under Revision if the covering analyst considers new information may change the valuation materially and if this may take more time.

Coverage in transition

Coverage in transition rating is assigned to a stock if there is a change in analyst.

Securities prices:

Prices are taken as of the previous day's close on the home market unless otherwise stated.

Valuations and risks:

Analysis of specific risks to set stock target prices highlighted in our investment case(s) are outlined throughout the report. For details of methodologies used to determine our price targets and risks related to the achievement of the targets referred to in the main body of the report or at [Rating Methodology](https://www.con.hu/wp-content/uploads/2016/04/Methodology_concorde_research.pdf?tstamp=201710021038) on our website, visit (https://www.con.hu/wp-content/uploads/2016/04/Methodology_concorde_research.pdf?tstamp=201710021038)

Research disclosures:

Concorde Securities Ltd. may have published other investment recommendations in respect of the same securities/instruments recommended in this report during the preceding 12 months. Disclosure of previous investment recommendations produced by Concorde Securities Ltd. in the previous 12 months can be found at [Rating history](https://www.con.hu/wp-content/uploads/2016/04/Rating-history.pdf?tstamp=201710021038). (<https://www.con.hu/wp-content/uploads/2016/04/Rating-history.pdf?tstamp=201710021038>)

GENERAL

This report is provided for information purposes only and does not represent an offer for sale, or the solicitation of any offer to buy or sell any securities.

The information, and any opinions, estimates and forecast have been obtained from sources believed by us to be reliable, but no representation or warranty, express or implied is made by us as to their accuracy or completeness. The information, opinions, estimates and forecasts may well be affected by subsequent changes in market conditions. This document may not be reproduced in whole or in part, or published for any purpose.

REPRODUCTION OR REBROADCAST OF ANY PORTION OF THIS RESEARCH REPORT IS STRICTLY PROHIBITED WITHOUT THE WRITTEN PERMISSION OF CONCORDE SECURITIES LTD.

DISCLAIMER II.

This research/commentary was prepared by the assignment of Budapest Stock Exchange Ltd. (registered seat: 1054 Budapest, Szabadság tér 7. Platina torony I. ép. IV. emelet; company registration number: 01-10-044764, hereinafter: BSE) under the agreement which was concluded by and between BSE and Concorde Securities Ltd. (registered seat: H-1123 Budapest Alkotás utca 50., company registration number: 01-10-043521, hereinafter: Investment Service Provider)

BSE shall not be liable for the content of this research/commentary, especially for the accuracy and completeness of the information therein and for the forecasts and conclusions; the Service Provider shall be solely liable for these. The Service Provider is entitled to all copyrights regarding this research/commentary however BSE is entitled to use and advertise/spread it but BSE shall not modify its content.

This research/commentary shall not be qualified as investment advice specified in Point 9 Section 4 (2) of Act No. CXXXVIII of 2007 on Investment Firms and Commodity Dealers and on the Regulations Governing their Activities. Furthermore, this document shall not be qualified as an offer or call to tenders for the purchase, sale or hold of the financial instrument(s) concerned by the research/commentary.