

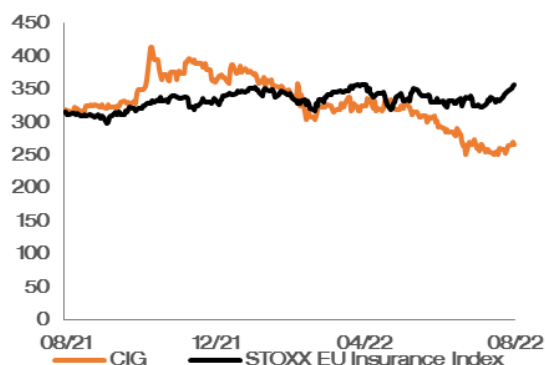
CIG Pannonia

Recommendation: BUY (unch.)

Target price (e-o-y): HUF 410 (unch.)

Share price: HUF 258

Share price as of 26/08/2022	HUF 258
Number of diluted shares [million]	94.4
Market capitalization [HUF mn/EUR mn]	24 363/59.4
Daily turnover 12M [HUF million]	0.02
Bloomberg	PANNONIA HB
Reuters	CIGP.BU
Free float	42.65%
52 week range	HUF 228 – 398



Healthy underlying profit growth subdued by extra taxes

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- CIG Pannonia (Pannonia) posted consolidated after-tax profit of HUF 183 mln for Q3/2022. Adjusted for net net impact of extra insurance tax of HUF 275, after-tax profit was HUF 406 mln on our estimate (+40% YoY). GWP came in at HUF 7.7 bln (+53% YoY). Life insurance segment had after-tax losses of HUF 49 mln compared to losses of HUF 195 mln in Q3/21, while non-life business also generated losses of HUF 378 mln as against losses of HUF 213 mln in the same period a year earlier due to the cost of aggressive expansion. Other activities also went into the red, with after tax losses of HUF 67 mln compared to after-tax losses of HUF 70 mln in Q3/21. Elimination amounted to HUF 677 mln vs. HUF 767 mln in the base period.
- Total reported comprehensive loss amounted to HUF 1.4 bln in Q3/22 versus gains of HUF 242 mln in the same period of last year amid a rising yield environment having a harmful impact of HUF 1.33 bln on mark-to-market valuation of the government securities portfolio, while there also were unrealized losses to the tune of HUF 249 mln on OPUS shares held by Pannonia.
- In the first nine month of the year Pannonia reached after-tax profit of HUF 828 mln (+4% YoY), while after adjusting for the net impact of extra taxes, after-tax profit was HUF 1.05 bln (+32% YoY) driven by rapid GWP growth (+42% YoY) primarily in UL, CASCO, industrial property insurances and other non-life products. Meanwhile, the positive effect of guaranty and loan collateral products was also visible a result of which the strategic cooperation with Magyar Bankholding. UL products and single life premium products profitability was weaker as yields and insurance taxes increased, while the considerable increase (+64% YoY) in commission led by new business sales growth and cost inflation also put temporarily a drag on results, which however were partly compensated for by a decrease in reserves mainly for single-fee UL products, and accounting reserves for traditional products, and higher interest income (the latter increased by HUF 371 mln YoY).

- Despite rapid cost inflation and rising yields, Pannonia's businesses remained financially stable and fundamentally solid: the consolidated solvency II capital adequacy ratio stood at as high as 200% at the end of September, compared with 237% at the end of June, 249% at the end of March, 2022 and 273% at the end of 2021. EMABIT's (non-life segment) standalone solvency II capital adequacy ratio should have remained above National Bank of Hungary's minimum requirement of 150%.
- At the Group level, premium arising from new group life insurance product contracts in Q1-3/22 (+107% YoY) was driven by the sales contracts with larger companies, while unit-linked products saw a moderate 5% increase YoY (mainly on the back of surging top-up and single life premiums). New traditional life insurance products sales remained broadly flat (+1% YoY), while non-life segment saw a stunning increase in GWP, albeit from a very low base (from HUF 155 mln to HUF 2.4 bln), mainly owing to fleet CASCO and corporate property insurances (both were virtually non-existing activity a year ago). We note that a significant increase in non-life insurance sales is not yet reflected in the net premiums written, as they appear time proportionally over the period covered by the insurance in accordance with the reporting standards in force.
- As a whole, life insurance GWP rose by 32% YoY in Q3//22 from HUF 4.9 bln to HUF 6.4 bln. Total unit-linked life insurance amounted to HUF 4.6 bln (thereof 37%, ie. HUF 1.6 bln was pension insurance policies), HUF 1.6 bln were traditional life products (thereof HUF 0.3 bln came from pension insurance policies), and HUF 0.2 bln were health insurance policies.

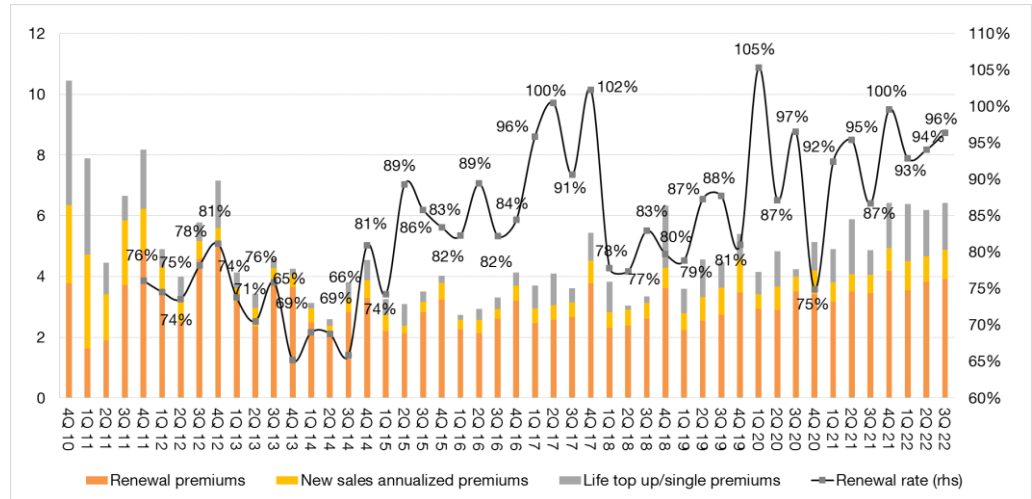
Breakdown of the Group's GWP and after tax profit (HUF mln)

	Life			Non-life			Other			Cons.			Total		
	Q3	Q2	Q1	Q3	Q2	Q1	Q3	Q2	Q1	Q3	Q2	Q1	Q3	Q2	Q1
	2022														
GWP	6 415	6 271	6 310	1 268	1 203	1 195	0	0	0	0	0	0	7 683	7 474	7 505
Reported after-tax profit	-49	1 282	-232	-378	77	-273	-67	-508	-157	677	-272	728	183	579	66
After-tax adjustments	0	0	0	0	0	0	0	0	0	0	0	0	-223	0	0
Adjusted after-tax profit	-49	1 282	-232	-378	77	-273	-67	-508	-157	677	-272	728	406	579	66
Reported total comprehensive income	-1 482	-525	-1 372	-524	6	-456	-67	-508	-157	677	-272	728	-1 396	-1 299	-1 257
Change in adj. after-tax profit (YoY)	-75%	68%	n.a.	77%	n.a.	239%	-4%	370%	104%	-12%	n.a.	n.a.	40%	17%	685%
Change in GWP (YoY)	32%	7%	29%	683%	1367%	1537%	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	53%	25%	51%
	2021														
GWP	4 859	5 887	4 906	162	82	73	0	0	0	0	0	0	5 021	5 969	4 979
Reported after-tax profit	-195	764	339	-213	-266	-52	-70	-108	-77	767	79	-173	289	469	37
After-tax adjustments	0	0	0	0	-26	29	0	0	0	0	0	0	0	-26	29
Adjusted after-tax profit	-195	764	339	-213	-240	-81	-70	-108	-77	767	79	-173	289	495	8
Reported total comprehensive income	-202	547	-84	-246	-284	-79	26	-108	-77	-664	79	-173	242	234	-413
	2020														
GWP	4 234	5 083	4 149	71	46	22	0	0	0	0	0	0	4 305	5 129	4 171
Reported after-tax profit	-231	844	271	-269	413	0	263	141	-116	191	468	-89	-428	930	244
After-tax adjustments	0	0	0	0	-315	315	0	0	0	0	0	0	0	-315	315
Adjusted after-tax profit	-231	844	271	-269	-240	-315	263	141	-116	191	468	-89	-428	277	-71
Reported total comprehensive income	-448	1 520	-1 038	-328	486	-122	263	141	-116	191	468	-89	-704	1 679	-1 187

Source: CIG Pannonia, Concorde's estimate

- Life segment benefited mostly from the increase in top-up and single premium income as well as growing income from renewals. GWP from renewals amounted to HUF 3.9 bln in Q3/22 (+13% YoY). GWP from the first annual premiums of policies sold was HUF 0.95 bln (+59% YoY), and top-up and single premiums came in at HUF 1.5 bln (+90% YoY), accounting for 28% of total life insurance GWP in H1/22 compared to 56% YoY. Renewal ratio remained inched up from 94% to 96% QoQ and from 87% YoY.

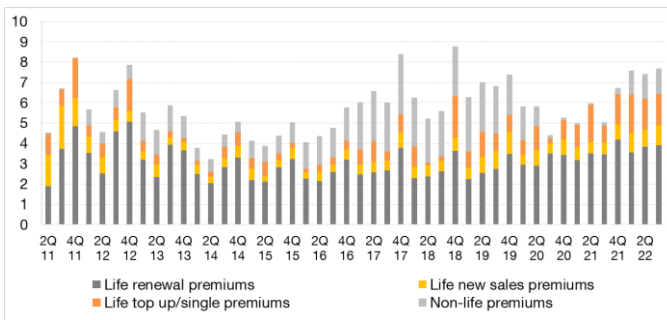
GWP breakdown in the life insurance segment (HUF bln)



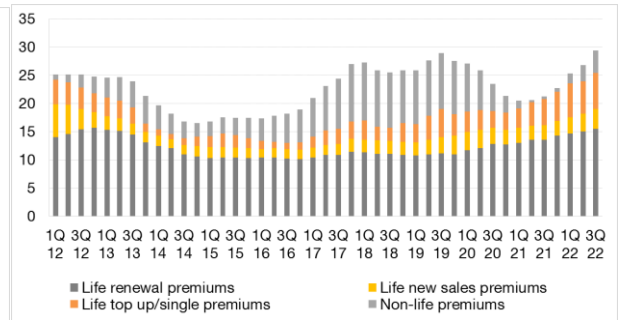
Source: Pannonia, Concorde estimate.

- 12-month rolling GWP appeared to have kept on increasing thanks to the improved renewal ratio, higher top-up income and fast-growing non-life business sales.

Quarterly consolidated GWP breakdown (HUF bln)



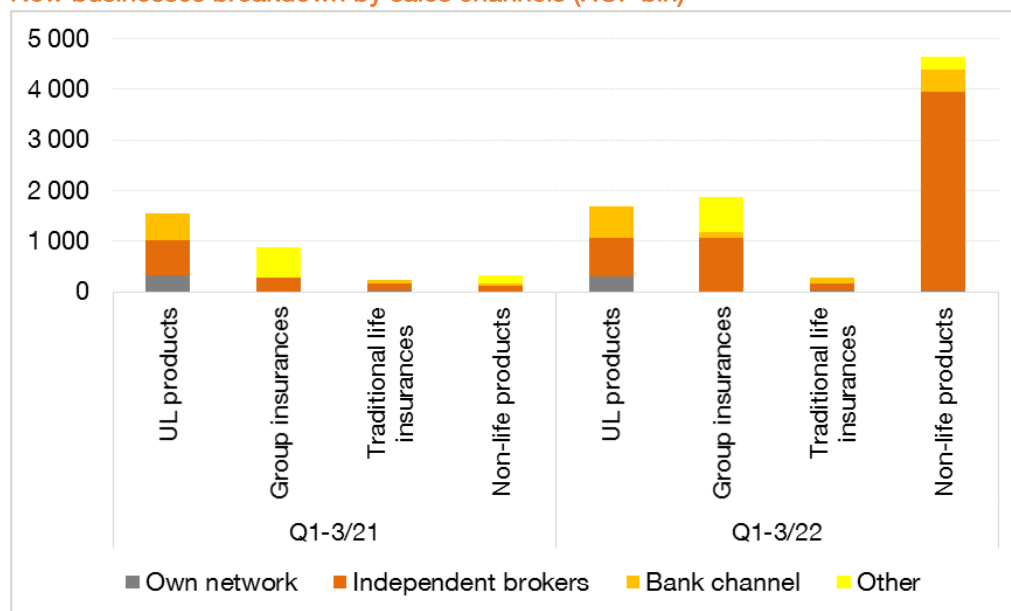
12-m rolling GWP breakdown (HUF bln)



Source: Pannonia, Concorde estimate

- All sales channels increased their sales volume, with the banking channel (Bankholding) generating an outstanding 285% YoY growth in Q3/22 followed by independent brokers which delivered 175% YoY growth, supported by newly launched products in line with the new growth-driven business strategy. Pannonia concluded a framework agreement with the Hungarian Bankholding Group (Bankholding) for a period of 20 years, according to which Bankholding Group member banks, ie. MKB Bank, Budapest Bank and Takarékbank, will sell exclusively the life and non-life insurance products of the CIG Pannonia Group.

New businesses breakdown by sales channels (HUF bln)



Source: Pannonia, Concorde estimate

- Investment results were negative at HUF 2.8 bln in Q3/22 (vs. a gain of HUF 2.2 bln in Q3/21) as a result of rising bond yields and higher volatility in the global stock markets.
- The total operating cost of the Issuer was HUF 2.8 bln in Q3/22, of which HUF 1.8 bln was related to the fees, commissions and other acquisition costs (+22% YoY), and HUF 0.5 bln was related to other operating costs (-13% YoY) and another HUF 0.5 bln was other expenses (+361% YoY). Acquisition costs show a significantly increasing trend overall, while gross earned premiums increased only by 8% YoY. This is primarily due to an increase in other acquisition costs than commissions, following the development and recruitment of new business lines, organizations and employees, and the related implementation of Pannonia’s medium-term growth strategy. Life acquisition costs rose by 14% YoY, accounting for 100% of new businesses (incl. 10% of single life premiums) in Q3/22 vs. 72% YoY, while in the non-life segment acquisition costs jumped by 460% YoY.
- Consolidated net claims and related settlement expenses rose by 5% YoY in Q3/22 due to the combined impact of lower life segment claims expenditures in the wake of the lower number of surrenders of unit-linked products, while traditional and group claims increased, but less than the decrease in unit-linked repurchases, and higher claims in non-life business in line with inflation and business expansion.
- The net decrease in insurance reserves was mainly attributed to decrease in reserves for single-fee UL products and accounting reserves for traditional products.

Outlook

- We reiterate CIG Pannonia (Pannonia) as BUY, as well as our 12-m target price at HUF 410 (implying a 59% upside potential from the current share price).
- We leave our 2022E/2023E net income forecasts for 2022 and 2023 unchanged at HUF 1.56 bln and HUF 2.04 bln, respectively, which reflect the harmful impact of 1) a substantial increase (<+40%) in insurance (“windfall”) tax imposed on Hungarian insurers for the period between 1 July 2022 and 31 December, 2023, and 2) a potential recession, which we see approaching as a consequence of the severe energy crisis in Europe, and rising yields.

- Consequently, EPS may come in at HUF 17 in 2022 and then to grow again by 27% to HUF 22 in 2023. Dividend will also inevitably drop, albeit from an unsustainably high level, to ca. HUF 11 a share for 2022, implying a DIVY of 4.3% based on the current share price.
- We remain confident that Pannonia's resilient and flexible organization can weather the impending economic slowdown, rather than being overwhelmed by it, while remaining committed to market expansion and product innovation.

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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.

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Valuations and risks:

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