

QUÁLITAS: 1Q20 PREVIEW

BUY

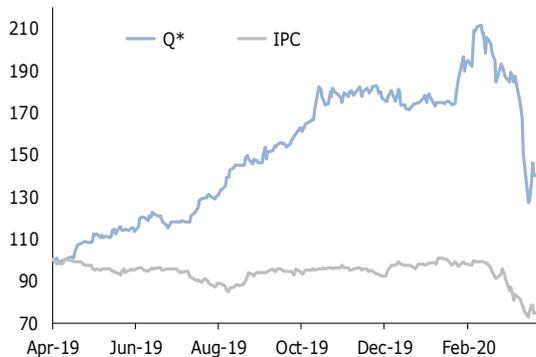
2020E Target Price (MXN\$)	\$ 100.00
Current Price (MXN\$)	\$ 69.88
Min / Max (L12M)	\$ 44.88 - 99.12
Expected Dividend (MXN\$)	\$ 1.70
Expected Return	45.5%
Market Cap (MXN\$ Mn)	29,699
Outstanding Shares (Mn)	425.0
Float	43.1%
6-month ADTV (MXN\$ Mn)	\$ 61.8

Opinion and Recommendation

Despite the fact that QUÁLITAS' written premiums will continue to increase, which is good news considering the current macroeconomic environment, the combined index will rise one percentage point to 88.1% due to a low base of comparison, while financial gains will decline due to the high volatility that prevailed in the Mexican stock market in March. We believe that these results have already been discounted by the markets.

We reiterate our BUY recommendation on QUÁLITAS mainly due to the sector's very favorable long-term prospects as result of a low insurance penetration as a percentage of GDP.

The valuation of QUÁLITAS' shares is very attractive with an estimated P/E of 5.5x, which we believe does not fully reflect the company's solid fundamentals, including its leading position in the Mexican car insurance market, its extensive distribution network, which the country's largest, its management team with a proven track record and the high profitability of its operations. We consider that QUÁLITAS is well positioned to face the current macroeconomic environment, with an investment portfolio of more than MXN\$32 billion, zero debt and an excess of regulatory capital of more than MXN\$8 billion.



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We expect QUÁLITAS's written premiums to rise 5% YoY in 1Q20, reaching MXN\$8.7 billion. We believe that the company is defensive against the current environment since around 60% of policies correspond to renewals. In addition, QUÁLITAS implemented a 10% discount on the renewals of existing policies and offers no interests periods on credit cards since two weeks ago. It also extended the period to recognize expired policies to 45 days, from 30 days. We believe that the reduction in new car sales (-25.5% in March and -10.9% in the quarter) will have an impact limited to 33% of the company's policies.

We expect a 62% loss ratio in 1Q20, in line with the company's annual guidance, driven by a lower automobile

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circulation. However, this index will be higher than the 60.9% in 1Q19 due to exchange rate pressure since 50% of costs are related to damages, of which 60% are denominated in foreign currency. Furthermore, last year's loss ratio was abnormally low during the government's fight against gasoline theft. It is worth mentioning that QUÁLITAS can transfer the incremental costs to its final clients since 80% of the policies are annual. We project a combined index of 88.1% in 1Q20, higher than the 87.1% in 1Q19. This will result in a 0.9% reduction in the operating profit.

As a consequence of the volatility in the Mexican stock market, we anticipate that QUÁLITAS financial gains will be MXN\$79 million in the current quarter, below last year's MXN\$681 million level.

The company's net profits will amount to MXN\$752 million in 1Q20, down 37.1% YoY.

High Dividends

QUÁLITAS will hold its Annual Ordinary and Extraordinary Shareholder's Meeting next April 20th through a novel remote-access scheme. The company will propose the payment of an MXN\$1.70 per share cash dividend, which is higher than last year's MXN\$0.85 per share dividend. The dividend yield will be 2.5% against the current share price. It will also propose the cancellation of 12 million treasury shares, which will bring down the number of shares outstanding to 413 million, as well as the creation of a MXN\$1.4 billion share buy-back reserve.

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