

QUALITAS: 2Q20 RESULTS

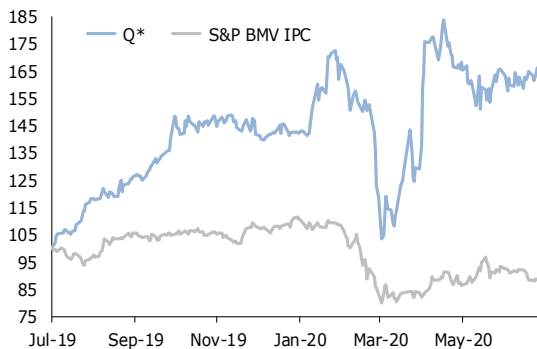
Low Claims Ratio and High Financial Gains Boost Net Profits in a Significant Way

BUY

2020E Target Price (MXN\$)	\$ 110.00
Current Price (MXN\$)	\$ 92.18
Min / Max (L12M)	\$ 54.01 - 102.22
Expected Dividend (MXN\$)	\$ 1.70
Expected Return	21.2%
Market Cap (MXN\$ Mn)	38,070
Outstanding Shares (Mn)	413.0
Float	43.1%
6-month ADTV (MXN\$ Mn)	\$ 79.9

Opinion and Recommendation:

- We consider that QUÁLITAS' 2Q20 results were positive, as they far exceeded our expectations in terms of loss ratio, financial gains and net profits. This took place despite the fact that written premiums declined due to the Covid-19 impact, as we broadly expected.
- We anticipate a favorable short-term reaction on QUÁLITAS share price. We reiterate our BUY recommendation and we are revising upwards our target price to MXN\$110.0 per share, from MXN\$100.0 per share.



Premiums Written / Earned

Premiums written fell 14.1% YoY to MXN\$7,094 million, practically in line with our expectations, which was mainly due to the impact of the pandemic. Financial institutions was the most affected segment with a 26.1% reduction, followed by the fleets with a 23.2% fall and the individual segment with a 3.8% decrease. Foreign subsidiaries posted a 46.5% growth. The company applied 10% price discounts, granted payment periods of up to 12 months without interests, and extended the fleet's grace period.

Despite the sharp 54.5% drop in new car sales, the number of insured units rose 2.5% annually, reaching 4.2 million. However, it decreased 2.5% compared to 1Q20. Mexico presented a quarterly 2.6% decline as a result of a 2.9% reduction in the number of insured cars.

Premiums earned remained practically unchanged in 2Q20 in the annual comparison. They were higher than premiums written due to multi-year policies issued in previous years. In addition, they benefited from the fact that the release of technical reserves, related to the low loss ratio, exceeded the creation of new reserves. Among total policies, 81% were annual and 19% were multi-annual, compared to a 71/29 mix from the same period three years ago. Annual policies allow the company to adjust its prices 3 to 4 times a year, which we believe is excellent news, taking into account the prevailing environment.

Profitability

Quarantine and the macroeconomic slowdown reduced car

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circulation, dragging down claims by 43.3%. In addition, there were fewer robberies and the recovery rate continued to rise. These factors had a positive effect on the loss ratio, which stood at 43.4% in 2Q20 (well below the 52.0% we expected), with an annual improvement of 15.9 percentage points. However, the acquisition ratio rose to 23.1%, from 21.6%, as a consequence of higher bonuses paid to agents and commercial areas which were generated in 1Q20. In addition, the operating index stood at 10.5%, from 7.1% the previous year, due to a higher profit sharing and some measures that the company took to face the pandemic. As a result, the combined ratio was 77.0% (vs. 79.2%), the lowest level in the company's history. It compared favorably against 88.1% in the same period of the previous year.

Financial Gains

Financial gains were up 6.3% to MXN\$659 million in the current quarter, by far exceeding our projections.

Net Profits

Net income registered a much higher-than-expected 72.1% increase, reaching MXN\$2,237 million (vs. our MXN\$1,235 million estimate), which translated into a 46.7% L12M ROE, higher than the 38.6% in 2Q19.

Investments

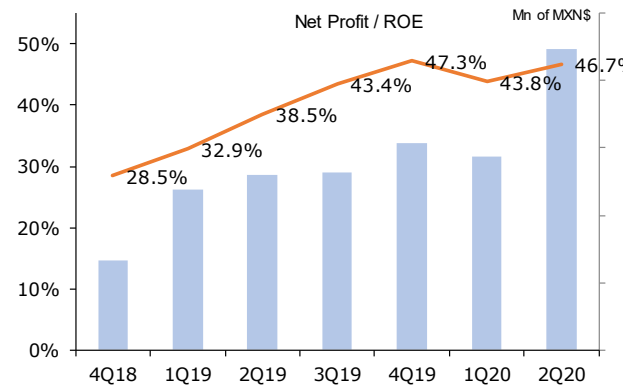
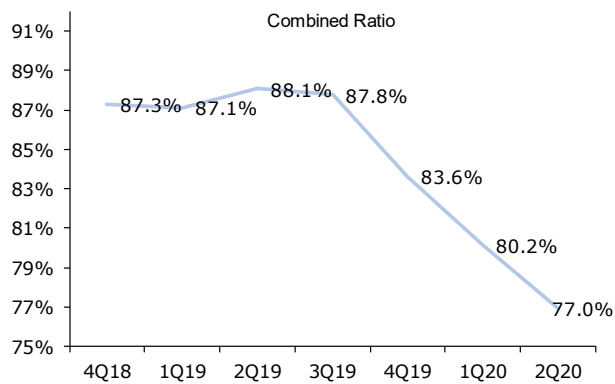
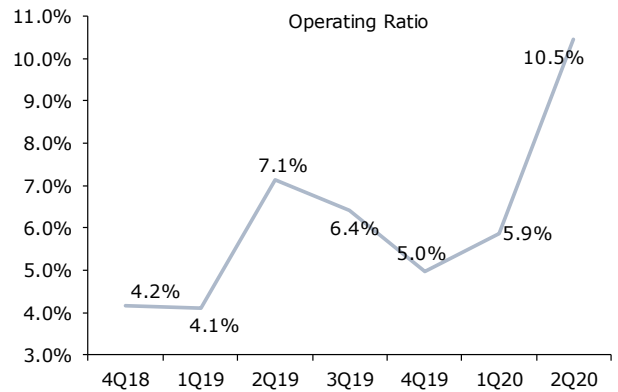
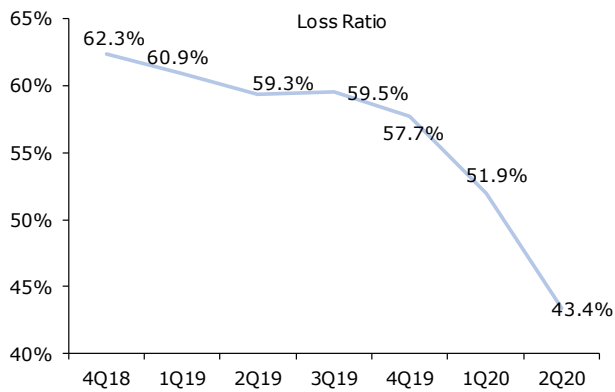
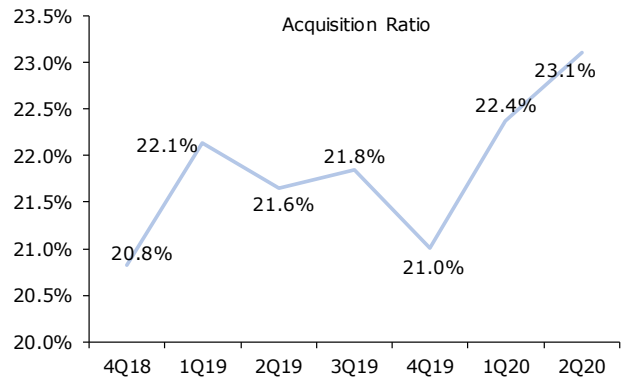
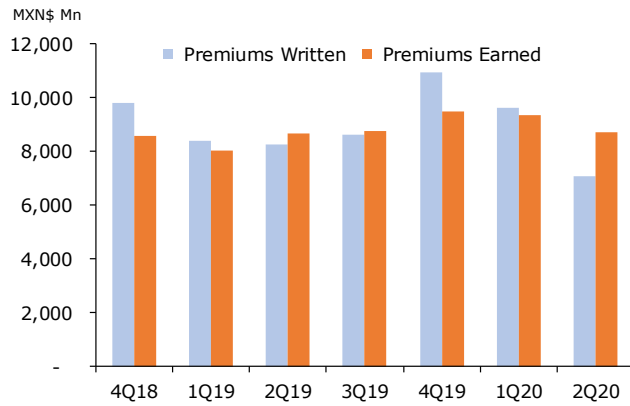
The investment portfolio rose 14.1% annually, closing the quarter at MXN\$31,568 million. 81% of the investments were in fixed income and the remaining 19% in equities.

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(Figures in MXN\$ Mn)	2Q20	2Q19	Change	Acum 20	Acum19	Change
Premiums Written	7,094	8,256	-14.1%	16,700	16,642	0.3%
Net Premiums Written	7,029	8,195	-14.2%	16,465	16,545	-0.5%
Premiums Earned	8,707	8,642	0.7%	18,053	16,685	8.2%
Acquisition Cost	-1,624	-1,774	-8.4%	-3,735	-3,622	3.1%
Loss Cost	-3,779	-5,125	-26.3%	-8,633	-10,023	-13.9%
Technical Result	3,304	1,743	89.5%	5,685	3,040	87.0%
Net Operating Expenses	-742	-589	26.0%	-1,306	-932	40.1%
Underwriting Result	2,565	1,158	121.5%	4,382	2,113	107.4%
Comprehensive Financing Result	659	620	6.3%	718	1,301	-44.8%
Pre-Tax Profit	3,224	1,778	81.3%	5,100	3,414	49.4%
Tax Reserve	-988	-475	108.1%	-1,423	-914	55.7%
Net Profit Before Minorities	2,237	1,304	71.6%	3,677	2,500	47.1%
Minority Interest	-1	-1	-40.4%	-2	-2	-8.1%
Net Profit After Minorities	2,236	1,302	71.7%	3,675	2,498	47.1%
EPS	\$ 5.41	\$ 3.06	76.7%	\$ 8.85	\$ 2.78	218.2%
FINANCIAL RATIOS	2Q20	2Q19		Acum 20	Acum19	
Acquisition Index	23.1%	21.6%		23.1%	21.6%	
Loss Index	43.4%	59.3%		43.4%	59.3%	
Operating Index	10.5%	7.1%		10.5%	7.1%	
Combined Index	77.0%	88.1%		77.0%	88.1%	
Adjusted Combined Ratio	70.6%	86.6%		70.6%	86.6%	
Underwriting Result	29.5%	13.4%		29.5%	13.4%	
Tax Rate	30.6%	26.7%		30.6%	26.7%	
ROE	46.7%	38.5%		46.7%	38.5%	
ROA	10.8%	6.7%		10.8%	6.7%	

Source: Quálitas, BMV

QUÁLITAS: 2Q20 Results



Source: Quálitas

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