

Qatar Insurance

Upgrade to Buy on compelling valuations and earnings rebound

- We increase our GWP growth for FY 18e mainly due to the pending acquisition of Markerstudy's, which should add c.32% to group GWPs.
- CR has steadily deteriorated over the last few years, partly due to NatCat losses (GBP 174m, 7.4% of group NLR, 49.5% of Qatar Re last year) and expansion into global reinsurance market. However, for FY 18e we expect a strong improvement in CR from 106.4% to 96.4% FY 18e on lower NatCat and strengthening of global reinsurance rates.
- Investment income should gradually decline as QIC de-risks its investment books (increasing their exposure to fixed income products now making up 59% of total vs. 44.0% in FY 16), with gross investment yields dropping from 7.5% to 7.1%, as the company becomes more leveraged.
- We upgrade to BUY and remove the stock from our Core Sells following a sharp decline in the share price as the stock dropped out of the FTSE EM index and most of the overhang has been absorbed. Valuation looks compelling with P/tNAV 18e of 1.2x offering a 42.3% discount to historic average (Exhibit 4), and P/E 18e of 8.6x, and base case RoE 18e of 15.1%, on the back of rebounding underwriting margins.

GWP growth to be bolstered by Markerstudy's acquisition. QIC signed an SPA to buy Markerstudy's, which underwrites more than 5% of the UK motor insurance market, generating premiums of about GBP 750m, expected to be complete by H1 18e. We pencil in y/y GWP growth of +26.2% y/y, with the acquired insurer making up 32.6% of GWPs as of FY 17 on a fully consolidated basis.

Combined ratio peaking in FY 17. We attribute this to the insurers NatCat losses of USD 174m, with loss ratio at 79.2%, up +10.2ppt y/y. We pencil in loss ratio of 70.5% and a combined ratio of 96.4% in FY 18e from 79.2% and 106.4% respectively, in-line with FY 12-16A averages. Expense ratio declined to 27.2% vs. 29.5% at YE 16, on the back of SG&A declining by -5.3% y/y. CRs of global peers Swiss Re and Munich re sit at 91.9% and 129.1%, respectively.

Higher GPW/equity leaves less room for investment risk: We expect investment income to gradually decline as QIC de-risks its investment books (reducing equity exposure from 46.9% in FY 16A to 36.9% in FY 17A), with asset yields dropping from 7.5% to 7.1% (on a gross basis), a trend we expect to continue as capital is more utilized for underwriting insurance risk with GWP/equity now at 145.4%, vs. 98.4% a few years ago, although fully offset on our numbers by the increase in underwriting margin in FY 18e.

42 days of outflows from FTSE exclusion on 15 March. This was due to its turnover ratio, which met the minimum 0.04% turnover ratio only 7 out of 12 months. We forecasted USD 57m and 42 days in outflows, which led to a 10% decline in stock price over the past few days, bringing valuations closer to idea levels.

No capital generation as DPS is prioritized, with dividends paid at QAR 415m, 98.1% of net profits for the year, resulting in limited capital generation for the insurer. QIC also raised USD 450m subordinated T2 debt, which could be earmarked for this acquisition, in our view.

We upgrade to BUY. We pencil in a return to RoE of 15.1% in FY 18e and combined ratio of 96.4%, valuation multiples look attractive with P/tNAV18e of 1.2x, P/E 18e of 8.6x, and RoE 18e of 15.1%. Its global peers trade at similar P/tNAV of 1.2. We remove QIC from our Core Sells (10pct) and increase our Core Sell position in CBQ from 2.5pct to 12.5pct due to the ramifications on IFRS 9 and expected large loss on sale of its stake in UAB.

BUY

QAR 43.6

Insurance / Qatar

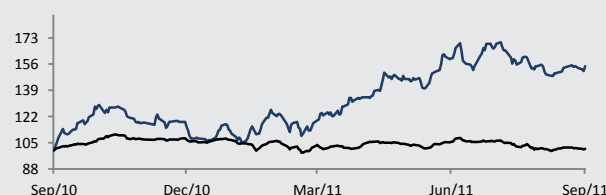
Bloomberg code	QATI QD
Market index	Qatar
Target Price	43.6
Upside (%)	24.5

Market data 19/03/2018

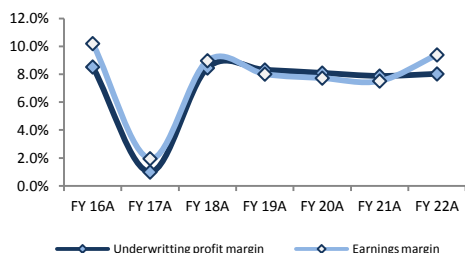
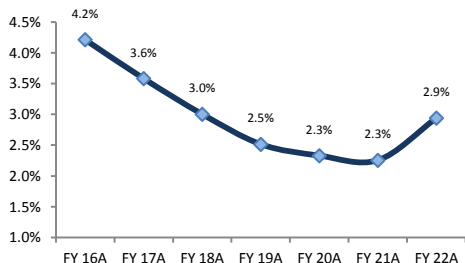
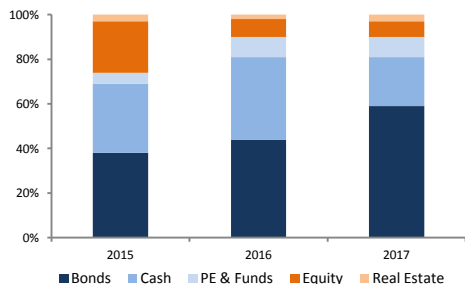
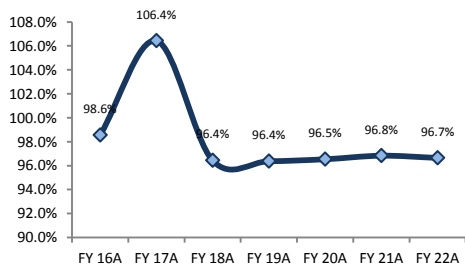
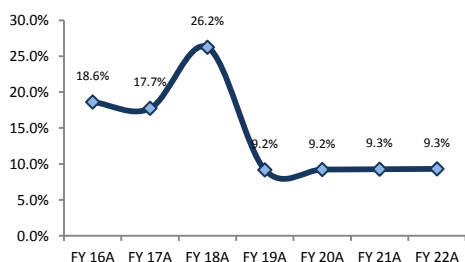
Last closing price	35.0
52 Week range	32.1-64.2
Market cap (QAR m)	11,162
Market cap (USD m)	3,043
Average Daily Traded Value (QAR m)	9.9
Average Daily Traded Value (USD m)	2.7
Free float (%)	100%

Year-end (local m)	2017	2018e	2019e	2020e
Gross Written Premiums	11,659	14,718	16,067	17,548
Underwriting Profit	115	1,245	1,336	1,421
EPS	1.31	4.07	3.96	4.16
P/E (x) (market price)	28.2	9.1	9.3	8.9
BVPS	26.02	28.89	31.67	34.64
Tangible BVPS	26.02	28.89	31.67	34.64
P/B (x) (market price)	1.4	1.3	1.2	1.1
P/TBVPS (x) (market price)	1.4	1.3	1.2	1.1
DPS	1.3	1.3	1.3	1.3
Div. yield (%)	3.5	3.5	3.5	3.6
RoAA (%)	0.7	3.5	3.1	2.9
RoAE (%)	2.7	15.1	13.4	12.9
Investments/Assets (%)	58.7	53.6	55.5	57.4
Investment Yield (%)	3.6	3.0	2.5	2.3
Net Loss Ratio	79.2	70.5	70.7	71.0
Combined Ratio	106.4	96.4	96.4	96.5
Underwriting Profit Margin	1.0	8.4	8.3	8.1
Net Profit Margin	1.9	9.0	8.0	7.7
Policy Reserves/Equity	221.0	213.5	225.9	238.0

Price Performance



Abacus Arqaam Capital Fundamental Data

Profitability

Investment Yield

Investment Exposure

Combined Ratio

Growth

Qatar Insurance Company

Year-end	2016	2017	2018e	2019e	2020e	2021e
Performance analysis						
Cession Ratio	13.4	18.1	17.6	17.5	16.9	16.4
Net Loss Ratio	69.0	79.2	70.5	70.7	71.0	71.2
Expense Ratio	29.5	27.2	26.0	25.7	25.6	25.6
Combined Ratio	98.6	106.4	96.4	96.4	96.5	96.8
Underwriting Profit Margin	8.5	1.0	8.4	8.3	8.1	7.9
Investment Yield	4.2	3.6	3.0	2.5	2.3	2.3
Net Margin	10.2	1.9	9.0	8.0	7.7	7.5
RoAE	12.4	2.7	15.1	13.4	12.9	12.5
RoAA	3.5	0.7	3.5	3.1	2.9	2.8
Net Premiums/Equity	1.0	1.1	1.3	1.3	1.3	1.3
Gross Premiums/Equity	1.2	1.5	1.7	1.6	1.6	1.6
Claims Reserve/NPE	0.9	1.0	0.9	0.9	1.0	1.0
Investment Income/Total Income	53.0	90.0	44.2	40.4	40.1	40.6

Year-end	2016	2017	2018e	2019e	2020e	2021e
Investment Exposure						
Investments/Assets	60.4	58.7	53.6	55.5	57.4	58.9
Equities/Investments	30.9	24.7	19.0	15.5	12.0	11.1
Equity/Assets (%)	29.5	23.8	24.4	24.0	23.6	23.1

Year-end	2016	2017	2018e	2019e	2020e	2021e
Liquidity/Leverage						
Policy Reserves/Gross Premiums	1.4	1.5	1.3	1.4	1.4	1.5
Policy Reserves/Net Earned Premiums	1.3	1.5	1.4	1.5	1.5	1.6
Policy Reserves/Equity	1.6	2.2	2.1	2.3	2.4	2.5
Debt/Capital	0.3	0.4	0.4	0.4	0.4	0.3
Debt/Equity (x)	0.5	0.7	0.7	0.6	0.5	0.5

Year-end	2016	2017	2018e	2019e	2020e	2021e
Growth						
Gross Premiums	18.6	17.7	26.2	9.2	9.2	9.3
Net Earned Premiums	44.5	6.8	27.4	9.9	10.0	10.0
Investments	7.9	19.4	3.9	6.2	6.3	6.4
Assets	21.3	21.0	8.4	11.4	11.2	11.9
Total Reserves	15.4	30.4	7.3	15.9	15.2	14.6
Equity	41.7	(2.7)	11.1	9.6	9.4	9.2

Year-end	2016	2017	2018e	2019e	2020e	2021e
Valuation						
P/B(x) (current price)	1.6	1.4	1.3	1.2	1.1	1.0
P/B(x) (target price)	1.6	1.7	1.5	1.4	1.3	1.2
P/E(x) (current price)	13.1	28.2	9.1	9.3	8.9	8.4
P/E(x) (target price)	13.7	61.1	10.5	10.8	10.2	9.6

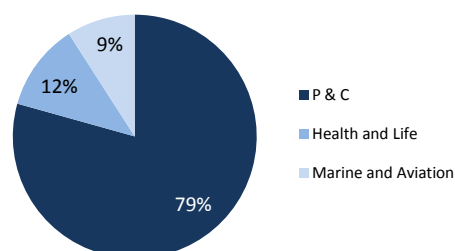
Abacus Arqaam Capital Fundamental Data

Investment thesis

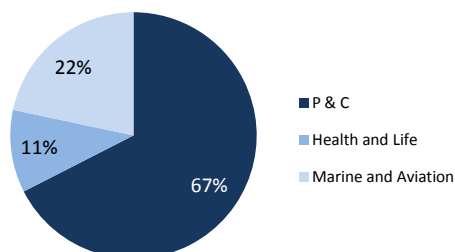
QIC invests (re)insurance premiums into its Asset Management business supporting overall RoE. However, as it grows, we expect it to start transforming into a diversified insurance company with a two-tier growth strategy across the insurance and reinsurance businesses.

We expect the growth of its Antares reinsurance business to continue to parallel Lloyds's growth profile. We expect its Qatar Re label to continue building on its strengths in Energy, Marine and Aviation.

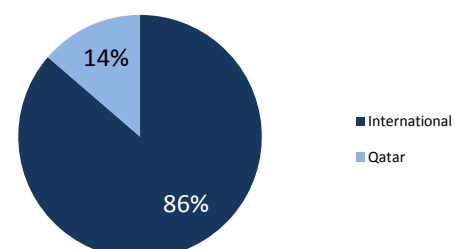
GWP Breakdown by business line:



Claims Breakdown:



GWP Breakdown by Region:



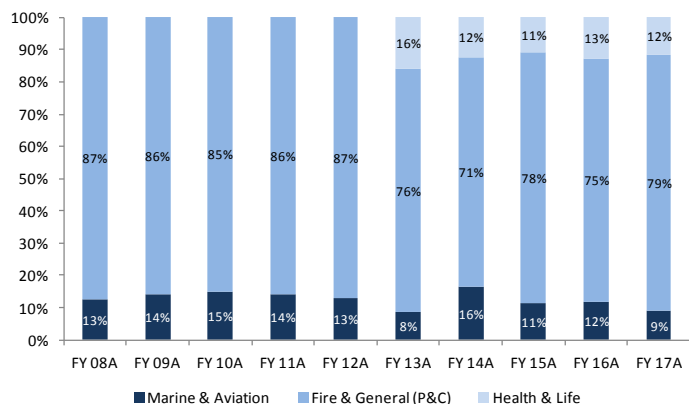
Qatar Insurance Company

Year-end	2016	2017	2018e	2019e	2020e	2021e
Income statement (mn)						
Gross Written Premiums	9,901.4	11,658.7	14,717.9	16,067.1	17,548.2	19,174.3
Ceded Premiums	1,323.3	2,108.8	2,583.6	2,805.2	2,968.9	3,140.1
Retained Premiums	8,578.1	9,549.9	12,134.3	13,261.9	14,579.3	16,034.2
Movement in Unearned Premiums	218.2	621.3	760.5	761.5	834.5	914.7
Net Premiums Earned	8,359.9	8,928.6	11,373.8	12,500.4	13,744.8	15,119.5
Commissions paid	-	-	-	-	-	-
Net commissions	(1,754.7)	(1,751.7)	(2,116.8)	(2,326.3)	(2,571.8)	(2,843.2)
Other underwriting expenses	(7.5)	(12.6)	(1.6)	(1.7)	(1.7)	(1.8)
Changes in technical reserves	(1,764.9)	(1,720.0)	(1,583.1)	(1,755.7)	(1,947.2)	(2,159.6)
Net Claims	5,769.0	7,074.6	8,013.8	8,839.5	9,754.0	10,766.9
Underwriting Profit	843.7	115.0	1,244.9	1,336.3	1,420.7	1,511.0
Investment Income	856.3	970.6	916.8	835.2	881.6	965.9
Other operating income	95.1	67.6	69.2	69.2	68.3	66.5
Investment & other income	-	-	-	-	-	-
Interest Expense	46.2	67.9	86.7	87.5	87.5	87.5
General & Administrative	715.5	677.4	838.7	881.6	943.5	1,031.2
Operating Profit	1,033.3	408.0	1,305.5	1,271.5	1,339.7	1,424.7
Distribution of surplus	-	-	-	-	-	-
Other income/(loss)	18.3	15.6	14.9	15.2	15.5	15.6
Tax	-	-	-	-	-	-
Minority Interest	(17.6)	(6.0)	25.6	28.2	31.0	34.1
Net Income	1,051.6	423.6	1,320.4	1,286.7	1,355.1	1,440.3
Reported EPS	2.82	1.31	4.07	3.96	4.16	4.42

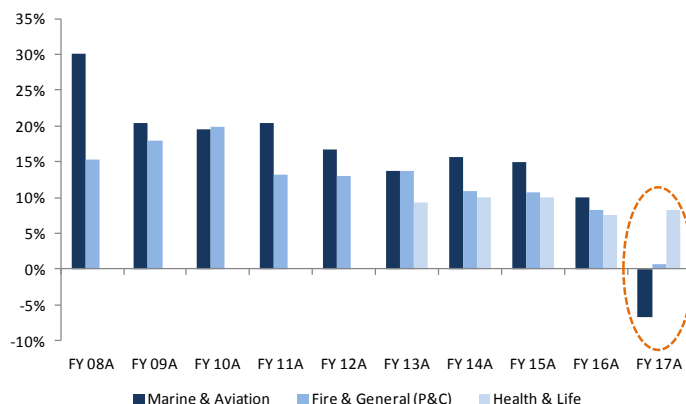
Year-end	2016	2017	2018e	2019e	2020e	2021e
Balance sheet (mn)						
Cash	6,962.3	7,914.1	7,308.1	9,877.3	12,760.9	16,105.8
Intangible Assets	1,038.9	1,316.9	1,194.1	1,203.5	1,244.1	1,292.2
Reinsurance Contract Assets	2,493.4	4,496.8	3,113.3	3,628.4	4,198.6	4,830.0
Investment Properties	575.8	585.8	578.9	572.2	545.7	517.1
Investments	11,435.1	13,654.5	14,192.3	15,071.2	16,025.6	17,056.2
Associates	138.8	142.5	153.0	163.6	174.5	185.4
Insurance Receivables	6,030.8	7,293.1	11,045.0	11,345.6	11,614.7	12,125.0
Fixed Assets	40.3	52.5	57.8	63.6	69.9	76.9
Other Assets	-	-	-	-	-	-
Total Assets	28,715.5	34,734.3	37,642.4	41,925.3	46,634.0	52,188.6
Short-term Insurance Contract Liabilities	13,583.3	17,718.0	19,015.2	22,047.5	25,399.4	29,105.0
Long-term Policyholder Liabilities	-	-	-	-	1.0	2.0
Debt	4,192.5	5,729.8	5,830.5	5,830.5	5,830.5	5,830.5
Insurance Payables	2,471.5	3,012.9	3,608.1	3,976.9	4,390.0	5,220.3
Other Liabilities	-	-	-	-	-	-
Total Liabilities	20,247.2	26,460.7	28,453.9	31,854.8	35,619.9	40,155.8
Shareholders Equity	8,236.1	8,017.3	8,906.5	9,760.3	10,673.0	11,657.5
Minority Interest	(17.6)	(6.0)	25.6	28.2	31.0	34.1
Total Equity	8,468.2	8,273.6	9,188.5	10,070.5	11,014.2	12,032.8
BVPS	23.09	26.02	28.89	31.67	34.64	37.84

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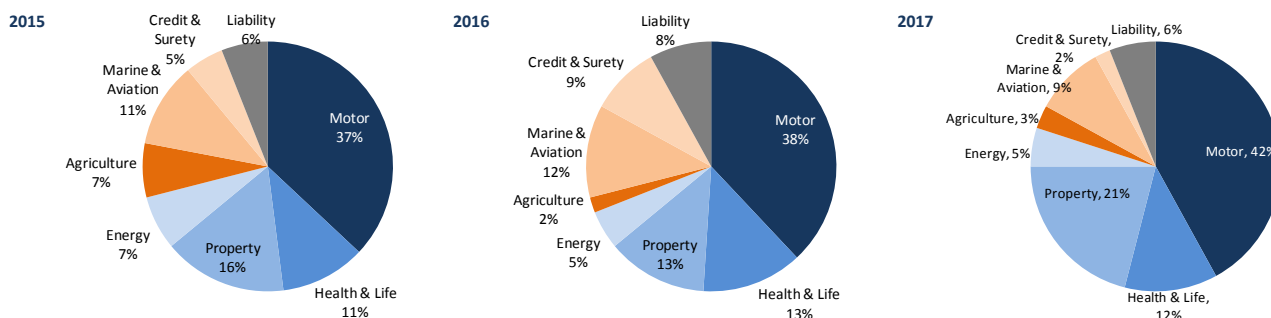
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Exhibit 1: GWP breakdown evolution (FY 08-17A)


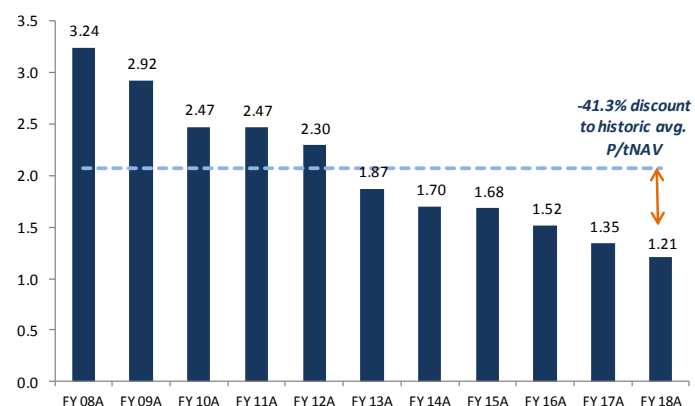
Source: Company Data, Arqaam Capital Research

Exhibit 2: Underwriting margin mainly worsening in Marine and Aviation and P&C


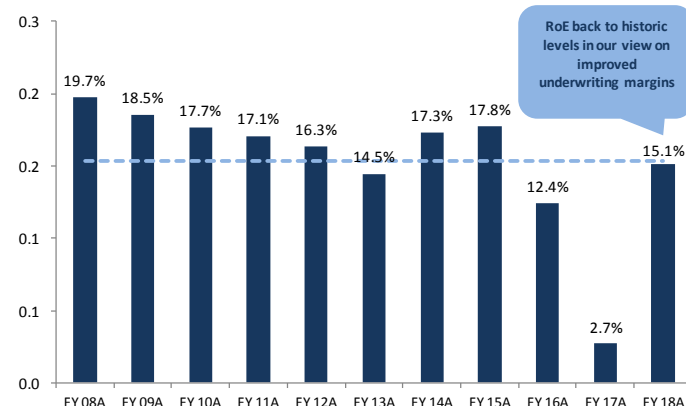
Source: Company Data, Arqaam Capital Research

Exhibit 3: Gross Written premium breakdown with motor underwriting expected to increase by another +43.6% in FY 18e, reaching QAR 8.6bn, due to Markerstudy's acquisition


Source: Company Data, Arqaam Capital Research

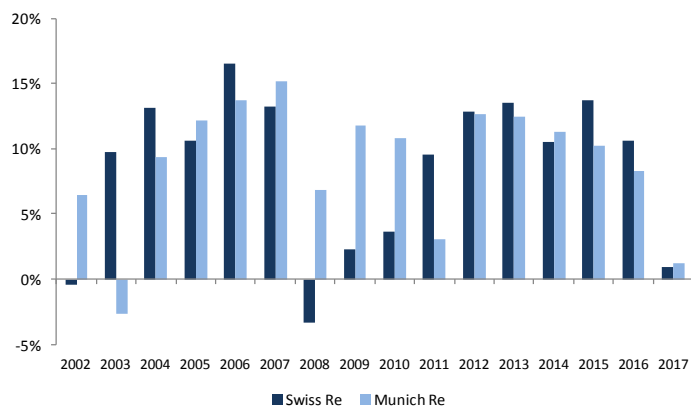
Exhibit 4: Trading at a -41.3% discount to historic avg. P/tNAV


Source: Company Data, Arqaam Capital Research

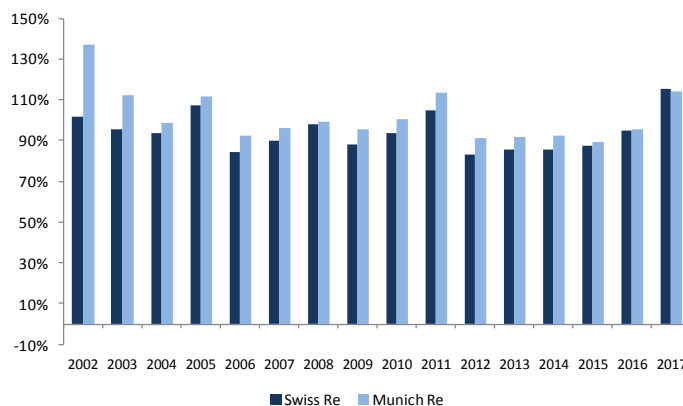
Exhibit 5: RoE expected to rebound in FY 18e on improving investment income and underwriting margins


Source: Company Data, Arqaam Capital Research

Valuations look attractive; with P/tNAV 18e offering a 41.3% discount to historic average (see Exhibit 4). We also expect a rebound in underwriting margins in FY 18e on the back of lower NatCat claims, with P&C underwriting margin dipping to 70bps in FY 17. We assume a rebound to similar levels as FY 16, where P&C underwriting margin stood at 8.4%, which should result in total underwriting margin of 8.4%, which on our numbers historically generated between 13-15% RoE, penciling in RoE 18e of 15.1%.

Exhibit 6: RoE evolution of Munich Re. and Swiss Re.


Source: Company Data, Arqaam Capital Research

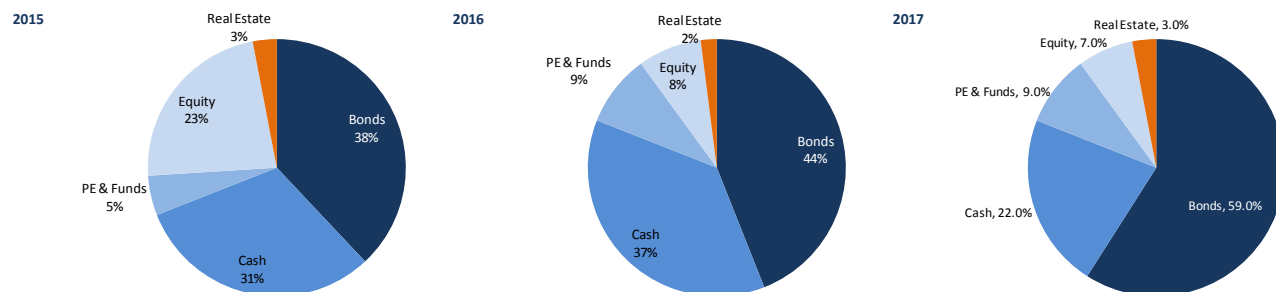
Exhibit 7: Combined Ratio evolution Munich Re. and Swiss Re.


Source: Company Data, Arqaam Capital Research

Exhibit 8: P/tNAV Munich Re and Swiss Re

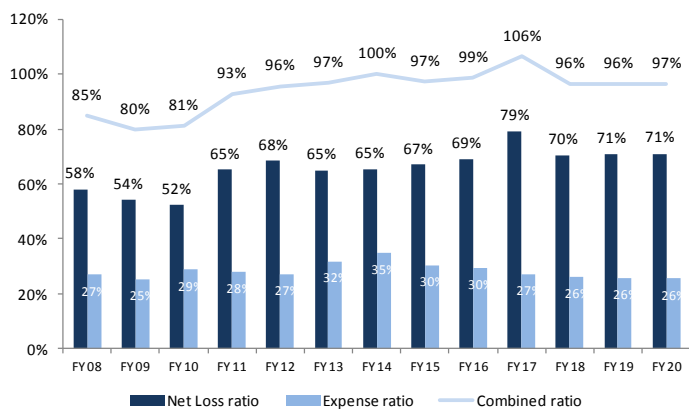

Source: Company Data, Arqaam Capital Research

Exhibit 9: Investment book leaning towards fixed income products now comprising 59.0% of total with equities at 7.0% vs. YE 15 at 23.0%



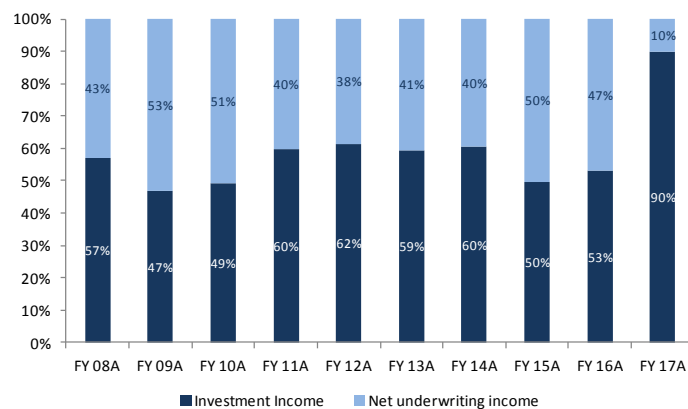
Source: Company Data, Arqaam Capital Research

Exhibit 10: Combined Ratio evolution



Source: Company Data, Arqaam Capital Research

Exhibit 11: Investment income vs. Underwriting income



Source: Company Data, Arqaam Capital Research

Exhibit 12: QIC EVA Valuation (QARm)

	2016A	2017A	2018e	2019e	2020e	2021e	2022e	2023e	2024e	2025e	perp	subtotal	% of total
1 DCF													
Net profit	1,010	227	1,320	1,287	1,355	1,440	1,968	2,122	2,289	2,680	2,788		
Other adjustments	--	--	--	--	--	--	--	--	--	--	--		
Minus: excess return excess capital	1	(36)	(22)	(17)	(10)	(16)	(14)	(15)	(16)	(19)	(19)		
Return on excess capital	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%		
Tax shelter	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%		
Adjusted net profit	1,009	263	1,343	1,304	1,365	1,456	1,982	2,136	2,305	2,699	2,807		
Capital requirements	7,403	7,999	8,635	9,347	10,065	11,191	12,464	13,871	15,425	17,238	17,927		
RoEcC	13.6%	3.3%	15.6%	13.9%	13.6%	13.0%	15.9%	15.4%	14.9%	15.7%	15.7%		
Cost of capital	11.8%	11.8%	11.8%	11.8%	11.8%	11.8%	11.8%	11.8%	11.8%	11.8%	11.8%		
Capital charge	876	947	1,022	1,107	1,192	1,325	1,476	1,642	1,826	2,041	2,122		
Economic profit	132	(684)	321	197	174	131	506	494	479	658	685		
Discount factor	0.00	0.00	1.00	0.89	0.80	0.71	0.64	0.57	0.51	0.46	0.41		
NPV of Economic Profit	--	--	321	176	139	94	324	283	245	301	685		
DCF EVA Forecast period												1,881	
Perpetual growth rate (GDP)												4.0%	
Terminal Value												8,732	
Terminal value discounted													3,568
Required Capital													8,635
Value of the insurance operations												14,084	101.6%
2 Capital surplus/deficit													
Available capital:													
Shareholders equity	8,468	8,274	9,189	10,070	11,014	12,033	13,415	14,907	16,517	18,399			
Less Goodwill & intangibles	1,039	1,317	1,194	1,203	1,244	1,292	1,358	1,452	1,560	1,692			
Less dividends	--	--	--	--	--	--	--	--	--	--			
Tangible equity	7,429	6,957	7,994	8,867	9,770	10,741	12,057	13,455	14,956	16,706			
Capital needs													
Net Written Premium (NWP)	8,578	9,550	12,134	13,262	14,579	16,034	17,641	19,416	21,376	23,797			
Claims reserves	6,851	8,571	10,154	11,910	13,857	16,017	18,412	21,068	24,015	27,283			
Equity investments	5,188	4,852	3,628	3,399	2,972	3,162	3,427	3,713	4,027	4,395			
Investment properties	576	586	579	572	546	517	489	462	436	411			
Associates	139	143	153	164	174	185	196	207	218	229			
Equity as % NWP	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%	32.0%			
Equity as % claims reserves	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%			
Equity as % of investments	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%			
Equity as % of investment properties	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%			
Equity as % of associates	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%			
Capital Requirements	7,403	7,999	8,635	9,347	10,065	11,191	12,464	13,871	15,425	17,238			
Surplus capital	26	(1,043)	(640)	(480)	(295)	(450)	(407)	(416)	(469)	(532)		(640)	-4.6%
3 Other adjustments													
Investment properties													
Capital increase													
Total adjustments	--	--	--	--	--	--	--	--	--	--		--	0.0%
4. Dividends													
												413	3.0%
Total Fair Value YE 2011												13,857	
Number of shares												318	
Fully diluted number of shares												318	
Fair value per share												43.6	
Current share price												35.0	
Upside												24.5%	

Source: Company Data, Arqaam Capital Research

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