

First Read

Porto Seguro

1Q16 beat on higher premiums and financial results

1Q16 adjusted net income R\$240.4mn, 13.7% above UBSe R\$211.4mn

Porto Seguro reported adjusted net income of R\$240.4mn, 5.7% above consensus R\$227.4mn. Adj. ROAE was 16.7% (20.6% in 4Q15 and 17.6% in 1Q15). The main positives: higher premium growth, good cost control, lower commission rate and strong financial results. The negatives: higher loss ratio (driven by auto and health) driving to a deterioration in the combined ratio, higher effective tax rate (higher CSSL) and asset quality deterioration in the credit card business. Although main results for Jan-Mar were already disclosed by Susep, we expect a positive market reaction.

Mixed results: higher combined but strong financial results

Auto premium growth accelerated to 4.7%yoy (from 1.8%yoy in 4Q15) despite the strong performance of Azul (14.8%yoy) and Itau brands (+15.5% yoy); Porto brand premiums contracted -4.3% yoy. Fleet was up 4.9%yoy while average premium per auto was slightly lower. The total loss ratio sharply deteriorated 129bps yoy to 57.1% driven by auto (+110bps qoq due to higher thefts and robberies, rains and price readjustments) and by health (+870bps yoy). Insurance G&A ratio was down to 14.7% (-30bps yoy), while tax expenses ratio was up to 4.7% (+70bps yoy). Acquisition cost ratio improved 10bps to 19.9%. The combined ratio deteriorated 187bps yoy to 98.9%. Financial result was up 15.3% qoq to R\$353mn (vs UBSe 280.2mn), yielding 119% of CDI, driven by real rates + inflation linked bonds and positive equity portfolio performance.

Looking forward: challenging outlook for 2016

Reflecting the exposure to the weak macro scenario and increase of competitive pressures, we observed deterioration in Porto margins driven by higher loss ratio. We expect this trend to continue during the year. For 2016, we currently expect auto premium growth at 1.4%yoy (vs 5.6% in 2015), while loss ratio should deteriorate 150bps to 56.0%. The still high Selic rate should continue to support financial income (+5.0% yoy). We expect 1.6% adj. EPS growth in 2016.

Valuation: Neutral; PT R\$32.0 (based on residual income model)

We think Porto Seguro is fairly priced, trading at 8.8x PE 16e vs 8.5xPE 16e for SulA.

Equities

Americas
Insurance, Full-Line

12-month rating **Neutral**

12m price target **R\$32.00**

Price **R\$27.65**

RIC: PSSA3.SA BBG: PSSA3 BZ

Trading data and key metrics

52-wk range	R\$42.35-22.71
Market cap.	R\$8.94bn/US\$2.24bn
Shares o/s	323m (COM)
Free float	29%
Avg. daily volume ('000)	681
Avg. daily value (m)	R\$18.2
Common s/h equity (12/16E)	R\$7.12bn
P/BV (12/16E)	1.3x

EPS (UBS, diluted) (R\$)

	UBS	Cons.
12/16E	3.15	3.06
12/17E	3.42	3.31
12/18E	3.93	3.76

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Figure 1: 1Q16 Earnings Review – Main Highlights

	1Q16a	1Q16e	4Q15a	1Q15a	Cons.	QoQ	YoY	A / E	A / Cons
Total written premium	3,541	3,441	3,707	3,363		-4.5%	5.3%	2.9%	
Total loss ratio	57.1%	55.1%	53.4%	55.8%		373 bps	129 bps	202 bps	
Total combined ratio	98.9%	97.8%	97.1%	97.4%		187 bps	158 bps	112 bps	
Adjusted earnings	240.4	211.4	294.0	230.9	227.4	-18.2%	4.1%	13.7%	5.7%

Source: Porto Seguro, UBS and Bloomberg data

Highlights (R\$m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	12,297	14,506	16,050	16,673	17,778	19,449	21,252	23,160
Operating earnings	703	876	1,002	1,018	1,107	1,269	1,485	1,646
EPS (UBS, R\$)	2.17	2.71	3.10	3.15	3.42	3.93	4.59	5.09
Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
ROE %	23.9	14.6	15.1	14.3	14.1	14.6	15.4	15.5
BVPS (UBS, R\$)	18.21	18.55	19.98	22.02	24.25	26.80	29.79	32.84
PE (UBS) x	12.1	11.5	11.0	8.8	8.1	7.0	6.0	5.4

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of R\$27.65 on 03 May 2016 08:41 EDT

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Forecast returns

Forecast price appreciation	+15.7%
Forecast dividend yield	4.0%
Forecast stock return	+19.7%
Market return assumption	15.6%
Forecast excess return	+4.1%

Valuation Method and Risk Statement

Our PT for Porto Seguro is derived from Residual Income model, with CoE of 14.3% and growth of 6.5%.

In addition to industry- and company-specific risk, such as increasing competition, there are potential risks inherent in investing in emerging market countries. Potential emerging market related risks include, but are not limited to, the volatile nature of the currency, regulatory and socio-political risk, and abrupt potential changes in the cost of capital and economic growth outlook. Valuations can also be affected by "contagion" from developments in other emerging and developed markets.

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Neutral	FSR is between -6% and 6% of the MRA.	38%	26%
Sell	FSR is > 6% below the MRA.	14%	19%
Short-Term Rating	Definition	Coverage ³	IB Services ⁴
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 March 2016.

1: Percentage of companies under coverage globally within the 12-month rating category.

2: Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Porto Seguro ²	PSSA3.SA	Neutral	N/A	R\$27.65	02 May 2016

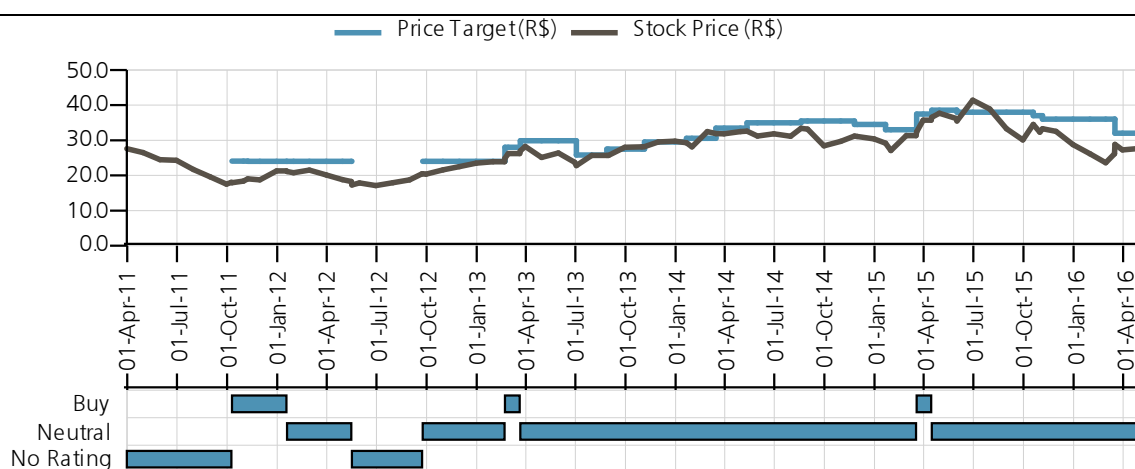
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Porto Seguro (R\$)



Source: UBS; as of 02 May 2016

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