

LPI Capital Berhad

(8621 | LPI MK) Financial services | Insurance

FY19 combined ratio deteriorated to above 70%

KEY INVESTMENT HIGHLIGHTS

- **FY19 normalised profit managed to grow marginally by +2.1%yoy to RM320.6m which is within our expectation**
- **Steady top-line growth with FY19 gross written premium (GWP) rose by +3.7%yoy to RM1.5bn but transitional challenges remain from industry liberalisation**
- **Higher FY19 net claims incurred which jumped by +16.7%yoy to -RM444.5m reduced earnings momentum**
- **Maintain NEUTRAL with a revised TP of RM15.50**

Within expectations. LPI Capital's (LPI) 4QFY19 normalised earnings grew marginally by +3.1%yoy to RM86.6m. Meanwhile, the full year FY19 normalised earnings increased by +2.1%yoy to RM320.6m which is within our expectation. This translated to about 97.2% and 99.3% of ours and consensus' full year FY19 estimates. The uptick in net profit was mainly attributable to higher net earned premiums (NEP) which rose by +8.7%yoy to RM1.0b. However, the higher NEP was mainly moderated by the +16.7%yoy jump in net claims incurred to -RM444.5m due to rising claim costs, resulting in a drag of earnings growth.

Steady top-line growth. For FY19, the group resiliently achieved a positive growth in GWP (+3.7%yoy) of RM1.5bn despite the continued declining trend in the general insurance industry. To put things in perspective, the industry posted a decline in GWP of -1.0%yoy for 9MCY19. We are of the view that the group's higher GWP was attributable to the continued infrastructure projects and the strengthening of its distribution channels. Nonetheless, we opine that that the ongoing motor and fire liberalisation exercise continues to add downward pressure on premium pricing.

Combined ratio worsens to above 70%. LPI's FY19 combined ratio rose to 70.4% through an increase of +2.5ppts(yoy). This was resulted primarily from the rise in claims ratio by +3.0ppts(yoy) to 43.9%. The higher claims ratio was mainly attributable to the jump in net claims incurred by +16.7%yoy to -RM444.5m. We opine that this was also partially due to the group continuing to retain more risks as reflected by the increase in retention ratio of +1.8ppts(yoy) to 67.6%. In addition, the motor, medical and miscellaneous accident insurance were the main areas of concern. This was evident from the rising FY19 net claims incurred for motor and miscellaneous by +12.0%yoy and +31.4%yoy to -RM235.9m and -RM151.1m respectively. Nonetheless, this led to a marginal increase of +0.3%yoy in the underwriting profit to RM299.2m due to higher NEP. Moving forward, we believe that the unfavourable claims environment and heightened competitive pricing pressure might continue to weigh on claims ratio as well.

Maintain NEUTRAL

Revised Target Price: RM15.50
(Previously: RM16.20)

RETURN STATISTICS

Price @ 3 rd February 2020 (RM)	14.80
Expected share price return (%)	+4.7
Expected dividend yield (%)	+4.7
Expected total return (%)	+9.4

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-3.0	2.7
3 months	-2.0	2.1
12 months	-10.3	-0.8

KEY STATISTICS


FBM KLCI	1,521.95
Syariah compliant	No
Issue shares (m)	398.38
Estimated free float (%)	48.47
Market Capitalisation (RM'm)	5,896.07
52-wk price range	RM 14.9 – RM16.9
Beta vs FBM KLCI (x)	0.44
Monthly velocity (%)	11.02
Monthly volatility (%)	6.64
3-mth average daily volume (m)	0.03
3-mth average daily value (RM'm)	0.40
Top Shareholders (%)	
Consolidated Teh Holdings	42.74
Sompo Holdings Inc	8.54
Retirement Benefits Fund	4.71

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Dividend. The group has declared a second interim single tier dividend of 43.0sen per share to be payable on 26th February 2020. As a result, this brought the total dividend for FY19 to 70.0sen per share which is on track with our forecast and represented a total dividend pay-out ratio of about 87.0%.

Earnings estimates. In view of the expected further fire liberalisation process and rising claims environment, we are revising downward our earnings forecasts by -3.9% and -4.2% for FY20 and FY21 to RM332.8m and RM348.2m respectively.

Target price (TP). We are revising our TP to **RM15.50** (*previously RM16.20*). We peg its FY20 Core EPS of 83.5sen to PER of 18.6x (2-year historical average).

Maintain NEUTRAL. While the group continues to remain firm in growing its top line and earnings momentum, we remain cautious of its growth prospects given the unfavourable claims environment and the escalating competition in the general insurance segment due to the motor and fire liberalisation. The further liberalisation of the fire insurance expected in CY20 could potentially be adding more pricing pressure on the group as fire alone accounts for about 68.0% of total group's underwriting surplus before management expenses. We have also observed that full year FY19 combined ratio rose to slightly above 70% for the first time in five years, illustrating the increasingly tough operating environment as evidenced by the rising claims ratio. Nonetheless, the announcement of the budget 2020 to allocate fundings for the rural and general infrastructure works where LPI is a major insurance provider will provide support to weather the structural change. All factors considered, we maintain our **NEUTRAL** stance on LPI Capital. 

INVESTMENT STATISTICS

FYE Dec	FY17A	FY18A	FY19A	FY20F	FY21F
Operating Revenue	1470.6	1513.7	1559.1	1629.9	1678.8
Net earned premiums (RM'm)	850.2	930.8	1014.6	1107.6	1145.6
Underwriting profit (RM'm)	305.8	303.5	318.7	321.8	340.4
Operating profit (RM'm)	401.3	402.0	414.0	422.8	442.4
Pre-tax profit	403.7	406.0	418.1	423.9	443.6
Net profit	313.8	314.0	329.8	332.8	348.2
Normalised net profit	310.8	314.0	329.8	332.8	348.2
Basic EPS	78.0	78.8	82.8	83.5	87.4
Core EPS (sen)	78.0	78.8	82.8	83.5	87.4
Recurring EPS growth (%)	7.5	1.0	5.0	3.2	4.6
PER (x)	19.8	19.6	18.7	17.7	16.9
Net Dividend (sen)	72.0	68.0	70.0	70.0	71.0
Net Dividend Yield (%)	4.7	4.4	4.5	4.7	4.8
BVPS (RM)	4.8	5.0	5.3	5.6	5.9
PBV (x)	3.2	3.1	2.9	2.6	2.5
ROE (%)	16.2	14.6	15.9	15.0	14.2

Source: Company, MIDFR

4QFY19 RESULTS SUMMARY

FYE Dec (RM'm)	Quarterly			Cumulative		
	4Q19	%YoY	%QoQ	FY19	FY18	%YoY
Operating revenue	399.3	2.6	-5.8	1,602.7	1,513.7	5.9
Gross earned premiums	379.6	2.4	-2.8	1,496.2	1,413.9	5.8
Net earned premiums	265.5	4.5	2.8	1,011.5	930.8	8.7
Investment income	19.6	6.3	-41.2	106.5	99.8	6.7
Commission income	24.0	2.7	-1.9	102.2	104.0	-1.8
Other income	47.3	8.6	-23.6	217.5	210.7	3.2
Gross claims paid	-158.0	-3.3	-3.3	596.3	-520.3	-214.6
Claims ceded to reinsurers	41.1	-29.0	-31.3	185.1	161.0	15.0
Net claims incurred	-107.0	7.6	3.1	-444.5	-381.0	16.7
Commission expenses	-42.7	0.0	-3.8	-170.9	-162.8	4.9
Management expenses	-45.9	2.8	-12.0	-199.1	-192.6	3.4
Other expenses	-90.1	2.2	-6.7	-370.1	-358.6	3.2
Operating profit	115.8	5.2	4.1	414.4	402.0	3.1
Share of associates and JV	0.5	-20.1	0.0	1.8	4.0	-55.8
Profit before tax	115.3	4.0	3.5	414.7	406.0	2.2
Taxation	-28.7	6.8	31.3	-92.4	-91.9	0.5
Net profit	86.6	3.1	-1.4	322.4	314.0	2.6
Normalised net profit	86.6	3.1	0.2	320.6	313.9	2.1
Underwriting profit/(loss)	94.1	3.6	13.9	299.2	298.4	0.3
Core EPS (sen)	21.7	3.1	0.2	80.5	78.8	2.1
	4Q19 (%)	+/- ppts	+/- ppts	FY19 (%)	FY18(%)	+/- ppts
Claims ratio	40.3	1.2	0.1	43.9	40.9	3.0
Management expense ratio	17.3	-0.3	-2.9	19.7	20.7	-1.0
Commission ratio	7.0	-0.6	-0.7	6.8	6.3	0.5
Combined ratio	64.6	0.3	-3.4	70.4	67.9	2.5
Retention ratio	70.0	1.4	3.8	67.6	65.8	1.8
Underwriting margin	35.4	-0.3	3.4	29.6	32.1	-2.5

Segmental breakdown						
	4Q19	%YoY	%QoQ	FY19	FY18	%YoY
Net earned premiums (RM'm)						
Fire	112.5	4.7	5.7	419.0	392.6	6.7
Motor	86.1	10.8	3.6	325.9	287.3	13.5
Marine, aviation & transit	5.2	2.8	30.8	19.4	19.0	2.2
Miscellaneous	61.7	-3.5	-4.8	247.2	232.0	6.5
Net claims incurred (RM'm)						
Fire	-11.2	-27.4	-16.4	-51.6	-52.3	-1.4
Motor	-63.4	17.9	6.7	-235.9	-210.7	12.0
Marine, aviation & transit	-1.7	260.3	22.2	-5.9	-2.9	102.3
Miscellaneous	-30.7	3.1	-19.9	-151.1	-115.0	31.4
Net claims incurred (%)						
Fire	10.0	-4.4	-2.6	-12.3	-13.3	1.0
Motor	73.6	4.4	2.1	-72.4	-73.4	1.0
Marine, aviation & transit	32.4	23.1	-2.3	-30.5	-15.4	-15.1
Miscellaneous	49.7	3.2	-9.4	-61.1	-49.6	-11.6
Net commission (RM'm)						
Fire	-18.5	1.2	153.8	-74.3	-70.6	5.3
Motor	-8.1	3.3	0.7	-32.9	-29.6	11.3
Marine, aviation & transit	-1.0	7.9	-326.5	2.9	1.2	146.5
Miscellaneous	-14.6	-6.1	198.4	-10.7	-7.1	50.6
Underwriting surplus* (RM'm)						
Fire	93.3	11.4	8.9	337.8	313.7	7.7
Motor	14.6	-12.2	-6.7	58.7	50.2	17.0
Marine, aviation & transit	3.9	-19.2	26.8	16.4	17.2	-4.8
Miscellaneous	28.2	-7.1	30.6	85.4	109.9	-22.3

Source: Company, MIDFR

*Before Management Expenses

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.