EDISON Scale research report - Update

Nürnberger Beteiligungs

Insurance

27 March 2018

Solid 2017 results but still low rating

The turnaround in business levels in life insurance after the weak first half improves visibility, although the overall environment remains challenging. Strong 2017 profits mean the price to NAV ratio is barely changed at an undemanding 1.03x despite some gain in the share price. A highly tenable 4.2% dividend yield offers further attraction.

Return to growth in business volumes

The most welcome feature of the results was the healthy turnaround in life insurance business in the second half, when new premiums rebounded 30% y-o-y to €226m, making for an almost unchanged figure for the full year of €402m. This followed a weak first half when new premiums written fell 22.9% to €175.8m from €228.1m. Market pricing on single premium business appears to have recovered from prohibitively aggressive levels and Nürnberger Beteiligungs' business ended the year 4% up, after a 32% drop in the first half driven by a refusal to take business at uneconomic prices. The property and casualty and health segments saw solid gains continuing into the second half.

Dramatic swing in second-half investment income

The 68% surge in 2017 net profit was driven by a remarkable swing to a 67% rise in investment income in the second half after an 18% fall in H1. Few details were given of this improvement and it appears to have been unheralded, given the cautious guidance for the second half issued in September (upgraded in December), and a one-off as the interest rate environment remains low and company forecasts for 2018 appear to assume non-recurrence.

Cautious profit guidance for 2018

The company has given guidance for full-year net profit of €50m; approximately half of the level in 2017. This appears to assume non-recurrence of the investment income effect but, as the figure is even lower than the €59m achieved in 2016, there would seem to be an added layer of caution, although the only noteworthy negative feature of qualitative comments on the outlook for 2018 is the persistence of low interest rates. The cautious note appears especially strong in respect of the property and casualty segment.

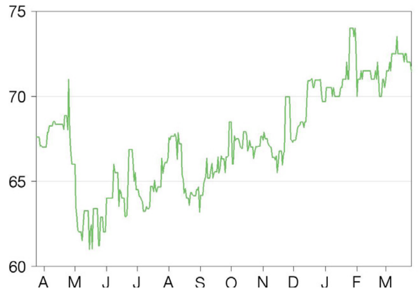
Historical financials

Year end	Revenue (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/14 IFRS	4,963	134.9	9.44	3.00	7.6	4.2
12/15 HGB	4,658	85.4	4.11	3.00	17.3	4.2
12/16 HGB	4,189	88.1	5.03	3.00	14.2	4.2
12/17 HGB	4,387	147.3	8.07	3.00	8.8	4.2

Source: Nürnberger Beteiligungs filings. Note: HGB, German GAAP; the company changed from IFRS to HGB in 2016.

Price	€71.5
Market cap	€824m

Share price graph



Share details

Code	NBG6
Listing	Deutsche Börse Scale
Shares in issue	11.52m
Liquid resources at 31 December 2017	€559.2m

Business description

Nürnberger Beteiligungs is the parent company of a group of insurers and financial service companies. It is one of Germany's oldest life insurers, and has 6.1m contracts, €3.4bn in gross premium income and €29.5bn in AUM.

Bull

- Very strong finances and conservative reporting
- Well-established brand name, solid historical performance; focus on top 10 strategy
- New organisational structure paves way for premium income growth and cost reductions

Bear

- Low-interest environment deters savers
- Regulatory uncertainty
- Early days for restructuring process

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Edison profile page

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Encouraging trends

Full-year 2017 results show encouraging trends pretty much across the board. Business resumed a positive trajectory in the dominant life insurance business after a first half marked by the tough market environment. The smaller insurance segments continued to perform well. There was a major boost to profitability from an unheralded and seemingly once-off fillip of 67% to investment income in the second half to €539m, more than reversing the 18% decline in the first. A cautious set of forecasts for the current year appears to go further than simply factoring in non-recurrence of these investment gains.

Exhibit 1: Financial data (€m)

	H116	H216	FY16	H117	H217	FY17
Gross Premiums						
Life	1,252.3	1,214.1	2,466.4	1,200.1	1,272.1	2,472.2
Change				-4.2%	4.8%	0.2%
Health	103.7	103.6	207.3	108.7	109	217.7
Change				4.8%	5.2%	5.0%
Property And Casualty	387.5	277.5	665	392.9	320.1	713
Change				1.4%	15.4%	7.2%
Total	1,741.6	1,593.0	3,334.6	1,701.4	1,701.2	3,402.6
Change				-2.3%	6.8%	2.0%
New Premiums						
Life	228.1	173.5	401.6	175.8	226.3	402.1
Change				-22.9%	30.4%	0.1%
Health	4.8	3.6	8.4	5.4	4.8	10.2
Change				12.5%	33.3%	21.4%
Property And Casualty	48.2	37.9	86.1	52.3	49.3	101.6
Change				8.5%	30.1%	18.0%
Total	281.1	215	496.1	233.5	280.3	513.8
Change				-16.9%	30.4%	3.6%
Investment Income	477	323	800	392	539	931
Change				-17.8%	66.9%	16.4%
Segmental Profit						
Life			33.4			64.3
Health			4			4
Property And Casualty			25.6			31.8
Consolidated net profit	25	34.3	59.3	42	57.5	99.5
Change				68.0%	67.6%	67.8%

Source: Nürnberger Beteiligungs

Turnaround in life insurance business after soft first half

The most notable feature of the results was the healthy turnaround in life insurance business after a weak first half, when new premiums written fell very sharply: 22.9% to €175.8m from €228.1m in H116 chiefly because of a 32.5% drop in single-premium business. In H2 new premiums rebounded 30% y-o-y to €226m, making for an almost unchanged figure for the full year of €402m, roughly in line with forecasts for the overall German market. The largest component in this improvement was a dramatic turnaround on single-premium business where the full year saw new premiums of €249m up 4% y-o-y. In the first half Nürnberger Beteiligungs was deterred from seeking new single-premium contracts by the uneconomically aggressive low pricing of competitors. Pricing would appear to have normalised. The decline in regular premium new business appears to have accelerated in the second half with an outturn of minus 7.5% for the full year compared to a decline of 3% in the first half. Low interest rates remain a drag on business in the market overall. The 4.2% drop in total gross premiums to €1.20bn from €1.25bn in the first half reversed to a 4.8% gain in the second, making for an almost unchanged full year outturn at €2,472m.

Non-life progresses gently

Nürnberger Beteiligungs' other insurance segments extended the good performance of the first half in far more benign market environments, making for solid growth in new premiums and gross premiums across the group in the full year compared to small declines in the first half.

Health insurance had an extremely commendable 30% rise in second-half new premiums, taking the full year improvement to €10.2m, up 21%. Gross premiums written progressed by 5% to €218m, fractionally faster than in the first half.

Property and casualty operations, too, saw an acceleration in new business levels with a 30% rise in the second half. In motor insurance, H2 saw a rebound after the decline of 1.0% in H1, which appears to have reflected the unwinding of guarantee-related business in 2016. Gross motor premiums ended the year practically unchanged at €266m.

Huge improvement in second-half investment income drives profits

The most notable effect on profitability in the second half was a dramatic and quite unheralded turnaround in the investment result, which saw a 67% increase to €539m. This completely reversed the poor performance of the first half when the tough investment environment made for a 17.8% drop. The report and accounts are rather silent on what lay behind this beyond a reference to increased distributions by Spezial-Investmentfonds, a class of non-consolidated investment vehicle. This move appears to have been driven by a change in tax law. Whatever lay behind this improvement presumably explains the upgrade in guidance for full year net profit to €90m from €60m made in December. This turnaround was sufficient for full-year net investment income to rise 16% to €931m.

The underwriting results in life and health insurance were buoyed by this improved investment income. By contrast, the full-year underwriting results at property and casualty, which does not include investment income, dropped 7% to €19.9m from € 21m despite an improvement of 150% to €18.0m at the halfway stage. The first half had been boosted by the non-recurrence of high levels of natural hazard and large claims in the comparable period of 2016, but in the second half there was a one-off transfer to employee pension provisions which was included in underwriting costs. The combined ratio weakened to 95.3% from 92.1% in the first half but still healthily ahead of the 96.2% recorded in 2016.

The small banking operation enjoyed a useful gain in its segmental profits, up 20% at €5.3m on the back of a surge in fee income.

The extraordinaries line saw a swing to a positive contribution of €4.3m as some of the provisions made in the €8.4m charge taken in 2016 were released. Some of the structural measures initiated in 2016 are starting to bear fruit. The total number of field staff dropped by 9.8% to 726, extending the trend of the first half.

We had already observed that the guidance for full-year net profit of €60m given at the interim stage appeared to be taking a prudent view of business outlook in light of the first half net profits of €42m. It manifestly did not factor in whatever drove the surge in investment income. Even the increased guidance (to €90m, given in December), was well overshot with a full-year outturn of €99.5m. The fact that the dividend was simply maintained at €3 reinforces our suspicion that a significant proportion of the investment income turnaround was one-off.

There was further improvement in the balance sheet in 2017. Cash generation remained strong with an inflow of €25.8m in the full year, taking the total to €559.2m. Group shareholders' funds were up 9.8% to €801m. Even allowing for a return to growth in the volume of business, we expect that the already healthy solvency ratio of 263% reported in the 2016 filings will have improved.

Cautious profit guidance

Persistently low interest rates make the underlying investment environment difficult. Coupled with the likely non-recurrence of the big boost from investment income in the second half, the company is guiding to a sharp fall in the segmental results from life insurance in 2018 to some €38m compared to €64.3m in 2017. This is still a healthy improvement on the €33.4m achieved in 2016. Management also expects progress in health insurance where it is guiding to €4.5m segmental profit in 2018 up from €4m in 2017. Non-recurrence of the investment income boost will hit segmental profits at property and casualty, which are expected to show a sharp fall to €22m from €31.8m, despite improved business volumes and a maiden contribution from a legal liability business. This would be lower than the €25.6m achieved in 2016. The company forecast of full-year net profit of €50m looks decidedly cautious even allowing for the investment income effect.

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