

Sava RE (POSR SV)

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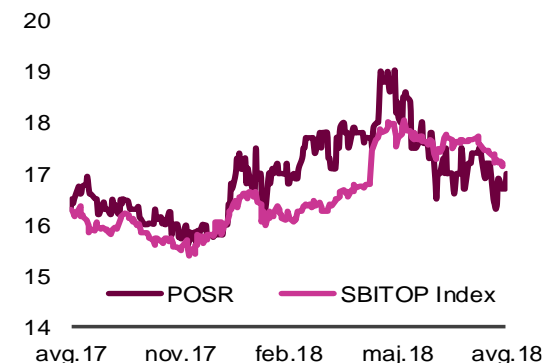
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12M Target price: 23.5 EUR Recommendation: BUY

Previous target price: 23.9 EUR, BUY (25.5.2018)

KEY MARKET DATA:

Stock data as of 31.08.2018 :		Price performance:		3M	12M
Market price (EUR)	17.0	Price change in %	-7.6%	1.8%	
52 week range (EUR)	15.6 - 19.0	SBI 20 index change in %	-2.3%	6.0%	
Market Cap (EUR)	292.7	Relative to SBI 20 index in %	-5.5%	-4.0%	
		Valuation multiples:		TTM	Forward
Avg. daily trade vol., EUR(k)	39	P/GWP	0.49	0.49	
Average daily % of stock traded	0.013%	P/E	9.2	7.2	
No. of Shares in millions	17.2	P/B	0.82	0.76	
Dividend yield	4.8%	S&P Global Ratings rating A/positive outlook A.M. Best rating A-/stable outlook			

SHARE PRICE DYNAMIC:



KEY COMPANY DATA & ESTIMATES:

million €	FY2016	FY2017	TTM	2018F	2019F
GPW	490.2	517.2	528.1	533.2	549.1
NPE	458.1	470.9	480.7	487.9	502.3
Claims paid	268.4	296.1	319.8	304.6	314.9
Net income	32.8	31.1	28.1	35.9	35.9
ROE	11.1%	9.8%	8.9%	10.6%	9.9%
EPS	2.10	1.96	1.77	2.31	2.31
DPS	0.80	0.80		0.80	0.93
Equity Inv	17.0	17.5	17.9		
Fin. Assets	1,038.2	1,038.1	1,013.9	1,080.1	1,116.6
Tech. Prov.	1,138.2	1,157.9	1,202.9	1,181.7	1,211.6
Equity	296.3	315.8	314.8	339.2	360.8
Assets	1,671.2	1,708.3	1,755.7	1,757.9	1,812.0
Equity/Assets	18%	18%	18%	19%	20%
P/E	8.2	8.7	9.2	7.2	7.2
P/B	0.91	0.86	0.82	0.76	0.72

KEY CURRENT DEVELOPMENT:

- Sava Re reported losses amounting to EUR 5.9m from hail storm that hit Slovenia in June. According to the management, Sava Re did forecast a one loss event amounting to EUR 5m in 2018 and if no more catastrophic events happen during the year it can still achieve its 2018 plan.
- S&P upgraded Sava Re's rating from A- to A with a medium-term stable outlook. Improved rating was one of main priorities of the management, with higher dividends being on the opposite side of the trade-off. However despite some demands for higher dividend, management proposal prevailed. Higher rating is a prerequisite for faster expansion on international reinsurance market.
- Slovenian Insurance Supervision Agency (AZN) refused for the third consecutive time to issue approval to Croatia Osiguranje and Adris to increase its stake in Sava Re to 33%. Adris, which holds a 19% stake in Sava Re, currently has a license to increase its stake by up to 20%. In June, Adris filled a lawsuit on Administrative Court, which judged in favor of Adris when AZN for the second time rejected to issue approval to Adris for increase of ownership in Sava Re.
- **Despite trailing our mid year estimates we are for now sticking with our estimates (but risks elevated). Target price only slightly lowered.**

1H18 Results

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- Please note 2Q18 results (income statement) already includes 3 acquired companies. So YoY comparability is slightly tougher.
- GPW went up by 3.7% YoY to EUR 308.6m, signaling that GWP guidance will be overreached.
- Segment wise, mixed results were delivered:
 - Life: -4.9% (EUR 42.7m / 12.2%)
 - Non-life: +8.7% (EUR 211.9m / 60.7%)
 - Pension: +13.9% (EUR 1.4m / 0.4%)
 - Reinsurance: -2.3% (EUR 93.2m / 26.7%)
- As usual, Non-life Slovenia was the growth driver. Non-life International also delivered strong growth, which was driven by high growth on Serbian market, though other markets showed solid growth figures as well.
- Overall Life segment reported a fall in GWP due to 6.3% YoY drop in Life Slovenia, which is a consequence of numerous maturing policies. In Life International, which grew by 11.8% YoY to EUR 3.9m, Serbia again delivered the highest growth.
- Reinsurance showed 2.3% YoY drop resulting from decline in both proportional and non-proportional reinsurance premiums in addition to contracting business in Russia and Turkey.
- Net earned premiums have risen by 4.3% YoY to EUR 240.1m in part due to lower reinsured premiums (-17.4% YoY).
- Net claims amounted to EUR 165.6m, up by 16.7% YoY mainly resulting from damages from hail storms that hit Slovenia in June (EUR 5.9m). Consequently, net incurred loss ratio (FX adjusted) increased by 2.3 p.p. to 61.1% in reinsurance and non-life.

Unconsolidated GPW by markets (in € mio)	1H17	1H18	YoY
Reinsurance (global)	95.4	93.2	-2.3%
Slovenia	207.1	216.7	4.6%
Slovenia Insurance	205.9	215.3	4.6%
Slovenia Pension	1.2	1.4	13.9%
Croatia	7.8	8.3	6.8%
Serbia	8.6	12.1	40.8%
Montenegro	6.5	6.6	2.2%
Kosovo	4.7	5.7	21.2%
Macedonia	6.4	6.5	1.6%

Unconsolidated GPW by segments (in € mio)	1H17	1H18	YoY
Reinsurance	95.4	93.2	-2.3%
Non-life Slovenia	164.5	176.5	7.3%
Non-life International	30.5	35.3	16.0%
Life Slovenia	41.4	38.8	-6.3%
Life International	3.5	3.9	11.8%
Pension Slovenia	1.2	1.4	13.9%

Income statement	1H17	1H18	YoY
Gross premiums written	297.8	308.6	3.7%
Reinsured premiums	-23.3	-19.2	-17.4%
Net earned premiums	230.3	240.1	4.3%
Net claims	-142.0	-165.6	16.7%
Net operating expenses	-75.8	-81.0	6.8%
Net inv. Income	7.8	10.1	29.1%
EBT	22.4	18.4	-17.7%
Net profit	17.1	14.1	-17.6%
Balance sheet	2017	1H18	YoY
Total Assets	1,708.3	1,755.8	2.8%
Shareholders' equity	315.8	314.8	-0.3%

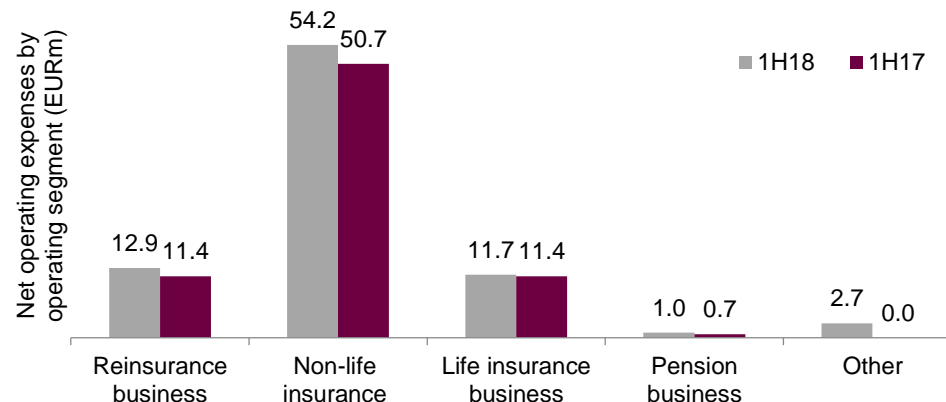
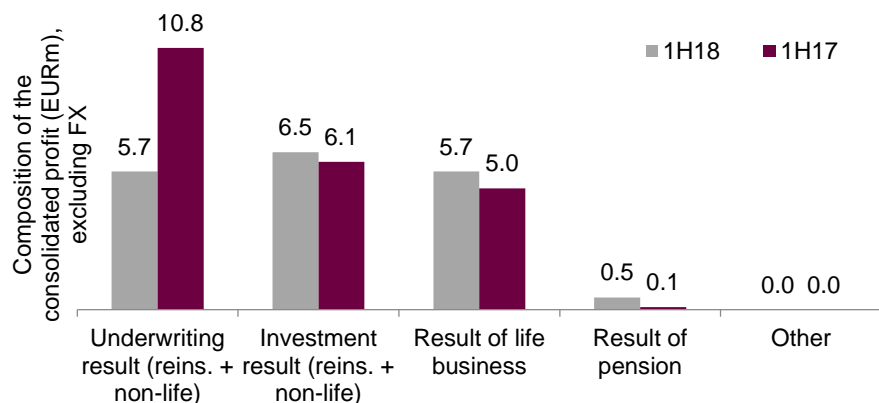
- Net operating expenses jumped by 6.8% YoY to EUR 81.0m, resulting from higher acquisition costs incurred by Serbian insurer due to high premium growth on Serbian market as well as due to higher marketing and IT expenses in Slovenia.
- Net expense ratio at 33.0% vs 32.1% in 1H17.
- Reported net combined ratio is at 97.1%, higher by 4.8 p.p. vs a year ago (FX adjusted 97.1% vs. 94.3%). Sudden upsurge in combined ratio mostly reflects a sharp increase in loss ratio resulting from hail storms in Slovenia.
- Net inv. income surged by 29.1% YoY to EUR 10.1m. However, excluding FX differences, net inv. income actually plummeted by 10.7% YoY to EUR 10.3m. Low interest rates environment continues to put pressure on investment results.
- Return on investments, excluding FX, stood at 1.9% in 1H18 vs. 2.2% in 1H17.
- Net profit amounted to EUR 14.1m, which is below our expectation. However, guidance regarding profit (EUR 37 to 39m) is still valid by management, although net profit currently stands at 36% - 38% of guided range.
- Shareholders' equity slightly declined from year-end due to lower fair value of reserves.
- Book value per share now stands at EUR 20.34 with annualized ROE at 9.9%.
- Total assets amounted to EUR 1,755.8m, up by 2.8% from year-end mainly due to higher receivables, which is chiefly due to the dynamics of annual renewal of insurance contracts.

1H18 Results - Supplemental

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Non-consolidated in EURm%	1H17 GWP	1H18 GWP	YoY	1H17 Claims	1H18 Claims	YoY
Reinsurance	95.4	93.2	-2.3%	37.9	37.0	-2.4%
Zavarovalnica Sava (SLO non-life)	164.5	176.5	7.3%	74.9	85.0	13.5%
Sava Montenegro	6.5	6.6	2.2%	2.0	2.1	8.8%
Sava osiguranje, Belgrade	7.9	10.6	35.1%	2.9	3.9	32.3%
Sava osiguruvanje, Skopje	6.4	6.5	1.6%	3.1	2.7	-12.4%
Zavarovalnica Sava (CRO non-life)	5.9	6.5	9.5%	2.1	2.7	31.4%
Illyria	3.8	4.7	21.7%	1.8	2.6	44.1%
Energoprojekt Garant	0.0	0.5	n.a.	0.0	0.1	n.a.
Zavarovalnica Sava (SLO life)	41.4	38.8	-6.3%	38.0	44.1	16.0%
Zavarovalnica Sava (CRO life)	1.9	1.8	-1.8%	0.4	1.1	213.7%
Illyria Life	0.9	1.0	19.3%	0.3	0.3	1.4%
Sava životno osiguranje	0.7	1.0	37.6%	0.2	0.2	13.8%
Sava pokojninska	1.2	1.4	13.9%	0.2	0.3	61.7%
Consolidated in EUR	1H17 GWP	1H18 GWP	YoY	1H17 Claims	1H18 Claims	YoY
Reinsurance	56.8	52.8	-7.1%	24.1	22.3	-7.7%
Non-life insurance	194.8	211.8	8.7%	86.2	98.1	13.8%
Life insurance	44.9	42.7	-4.9%	38.8	45.7	17.7%
Pension	1.2	1.4	13.9%	0.2	0.3	61.7%
Total	297.8	308.6	3.7%	149.4	166.4	11.4%

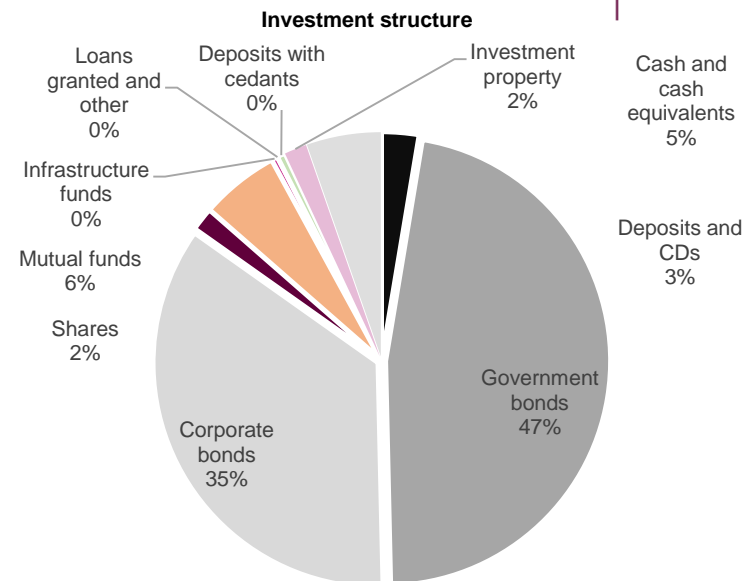


1H18 Group Financial Asset Allocation

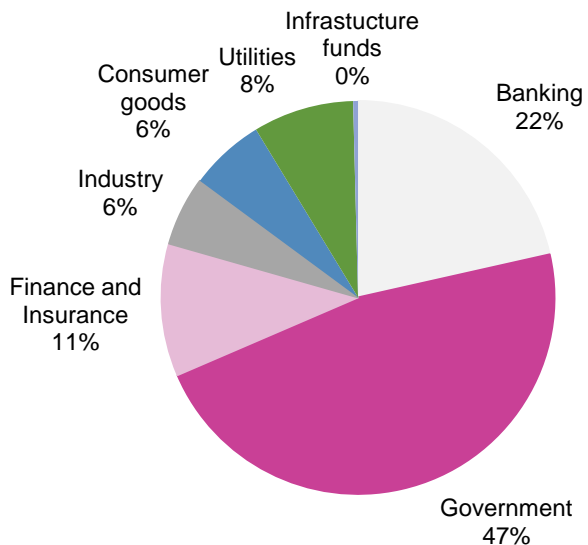
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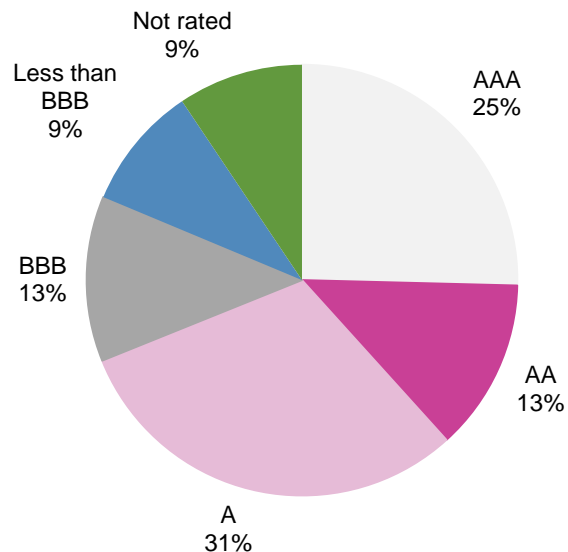
Investment portfolio	Index		Structure		
	1H18	1H17	1H18	1H17	
Deposits and CDs	28.6	22.6	126.6	2.6%	2.1%
Government bonds	512.3	544.1	94.2	47.0%	51.6%
Corporate bonds	383.1	380.0	100.8	35.2%	36.0%
Shares	17.9	17.0	105.2	1.6%	1.6%
Mutual funds	61.2	48.8	125.4	5.6%	4.6%
bond and money market	57.3	46.1	124.3	5.3%	4.4%
equity and mixed funds	3.9	2.6	145.7	0.4%	0.3%
Infrastructure funds	4.3	0.0	n.a	0.4%	0.0%
Loans granted and other	0.6	0.7	87.4	0.1%	0.1%
Deposits with cedants	5.9	6.8	86.9	0.5%	0.6%
Total financial investments	1,013.9	1,019.9	99.4	93.0%	96.7%
Investment property	17.6	7.9	221.8	1.6%	0.8%
Cash and cash equivalents	58.3	26.4	220.4	5.3%	2.5%
Total investment portfolio	1,089.7	1,054.3	103.4	100.0%	100.0%



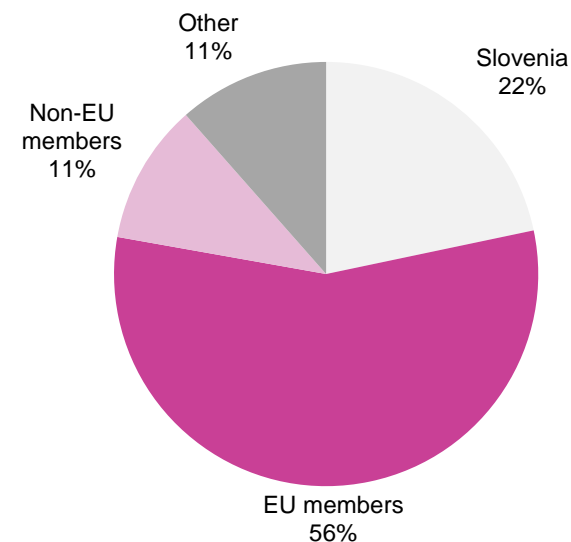
Group Exposure by Industry in 1H 2018



Group Exposure by Rating in 1H 2018



Group Exposure by Region in 1H 2018



SFCR of the Sava Re Group for 2017

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IFRS Balance Sheet		Solvency II market consistent Balance sheet	
Assets	Equity	Assets	AFR
1,733	341	1,464	491
	Liabilities		Liabilities
	1,392		973

Source: Sava Re Group

Sava Re Group	Gross capital req. (in EUR million)
Total market risk	51.7
Total counterparty default risk	14.4
Total capital requirement for life underwriting risk	40.2
Total health underwriting risk	23.9
Total non-life underwriting risk	142.4
Diversification	-88.1
Basic SCR	184.5
Total capital requirement for operational risk	15.4
Loss-absorbing capacity of technical provisions	-0.2
Loss-absorbing capacity of deferred taxes	
SCR	199.7
Other SCR	5.3
Total SCR	205.0

Basic own funds	
Share capital	114.892
Reconciliation reserve	336.393
Reconciliation reserve before deduction	491.2
Expected dividend payment	-12.4
Other	-142.4
Subordinated liabilities	0.0
Other adjustments	0.1
Eligible own funds (EOF)	451.4
Solvency ratio of Sava Re Group (EOF/SCR)	220%

Market risk	
Spread risk	38%
Property risk	21%
Currency risk	20%
Equity risk	16%
Interest rate risk	3%
Concentration risk	3%

Risk profile for non-life insurance	
Premium and reserve risk	57%
Catastrophe risk	38%
Lapse risk	5%

Risk profile for life insurance	
Lapse risk	65%
Expense risk	13%
Mortality risk	12%
Catastrophe risk	4%
Disability-morbidity risk	3%
Longevity risk	2%
Revision risk	1%

Health underwriting risk	
NSLT health underwriting risk	80%
Catastrophe risk	17%
SLT health underwriting risk	3%

- Spread risk** is the risk of the sensitivity of the values of assets and financial instruments to changes in the level or in the volatility of credit spreads over the risk-free interest rate term structure.
- Lapse risk** is the risk of changes in the value or volatility of probabilities taken into account for policy lapse, termination, renewal and surrender.

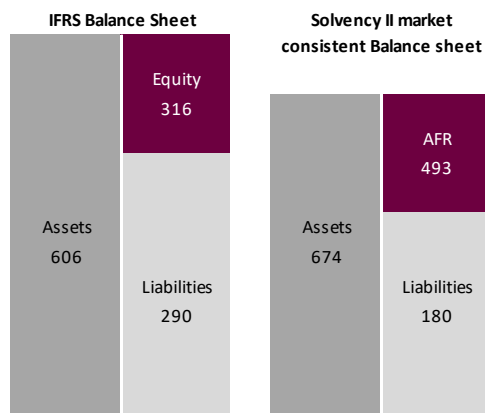
Solvency 2 ratio	Dividend policy	
> 230%	Overcapitalization	Additional engagement of capital
200 – 230%	Appropriate capitalization	Potential reallocation of capital
170 - 200%	Optimal capitalization	Optimization of the investment strategy and underwriting strategy
140 – 170%	Still appropriate capitalization	Potential reallocation of capital
< 140%	Undercapitalization	Measures to safeguard the company's solvency

- Solvency and Financial Condition Report of the Sava Re Group for 2017 indicated strong capital position with **Solvency II ratio of 220%**.
- Optimal level of capitalization starts at 170%, therefore signaling that Sava Re is appropriately capitalized.
- Solvency II ratio stood at 204% in 2016 indicating a significant improvement in 2017 mostly due to increase in EOF.
- Rating is indicating continuation of **higher level of net profit distribution**, however, the sensitivity/volatility of future rating is still unknown.
- Note that solvency rating of both insurers are not fully comparable since Triglav is using also loss-absorbing capacity of deferred taxes.

SFCR of the Sava Re d.d. for 2017

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Source: Sava Re Group

Sava Re Group	Gross capital req. (in EUR million)
Total market risk	98.5
Total counterparty default risk	5.5
Total capital requirement for life underwriting risk	0.0
Total health underwriting risk	3.6
Total non-life underwriting risk	94.1
Diversification	-46.1
Basic SCR	155.6
Total capital requirement for operational risk	4.5
Loss-absorbing capacity of technical provisions	0.0
Loss-absorbing capacity of deferred taxes	
SCR	160.1
Other SCR	0.0
Total SCR	160.1

Basic own funds	
Share capital	126.1
Reconciliation reserve	327.5
Reconciliation reserve before deduction	493.2
Expected dividend payment	-12.4
Other	-153.3
Subordinated liabilities	0.0
Other adjustments	0.0
Eligible own funds (EOF)	453.6
Solvency ratio of Sava Re Group (EOF/SCR)	283%

Market risk	
Equity risk	55%
Concentration risk	26%
Currency risk	10%
Spread risk	4%
Interest rate risk	3%
Property risk	2%

Risk profile for non-life insurance	
Catastrophe risk	52%
Premium and reserve risk	45%
Lapse risk	3%

Risk profile for life insurance	
Disability-morbidity risk	0%
Revision risk	0%
Catastrophe risk	0%
Mortality risk	0%
Longevity risk	0%
Lapse risk	0%
Expense risk	0%

Health underwriting risk	
NSLT health underwriting risk	100%
SLT health underwriting risk	0%
Catastrophe risk	0%

- **Spread risk** is the risk of the sensitivity of the values of assets and financial instruments to changes in the level or in the volatility of credit spreads over the risk-free interest rate term structure.
- **Lapse risk** is the risk of changes in the value or volatility of probabilities taken into account for policy lapse, termination, renewal and surrender.

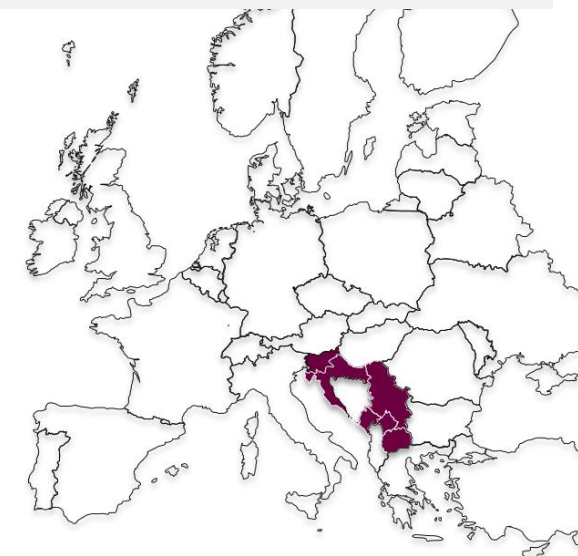
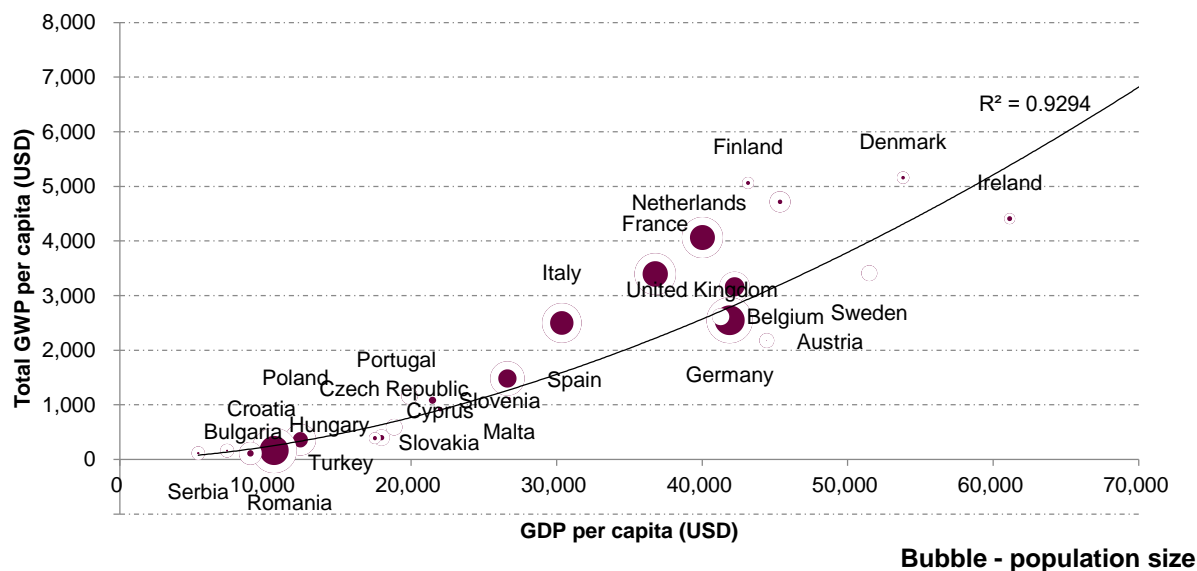
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- Solvency and Financial Condition Report of the Sava Re d.d. for 2017 indicated strong capital position with **Solvency II ratio of 283%**.
- Optimal level of capitalization starts at 220%, thus indicating that Sava Re is overcapitalized.
- Excessive capitalization is partly due to change in valuation methodology that had a material effect on EOF.
- Rating is indicating continuation of **higher level of net profit distribution**, however, the sensitivity/volatility of future rating is still unknown.
- Note that solvency rating of both insurers are not fully comparable since Triglav is using also loss-absorbing capacity of deferred taxes.

Market overview

		Insurance penetration 2017 (NL / Life)	Insurance density in EUR per capita 2017	Sava RE GWP 1H 2018 in EURm	Market Share In 1H 2018	Market Position	Market GWP growth in 1H 2018
Slovenia		4.9% (3.5%/1.5%)	1,055	216.7 (+4.6%)	18.0%	2	+6.4%
Croatia		2.5% (1.7%/0.8%)	295	8.3 (+6.8%)	1.1%	14	+9.2%
Serbia		2.1% (1.6%/0.5%)	109	12.1 (+40.8%)	2.8%*	9*	+2.4%*
Montenegro		1.9% (1.5%/0.3%)	131	6.6 (+2.2%)	18.2%**	2	+3.2%
Macedonia		1.4% (1.2%/0.2%)	71	6.5 (+1.6%)	8.8%*&***	5*&***	+5.2%*
Kosovo		1.4%	47	5.7 (+21.2%)	12.9%	n.a.	+5.0%

*1Q18, **only non-life



Investment Thesis

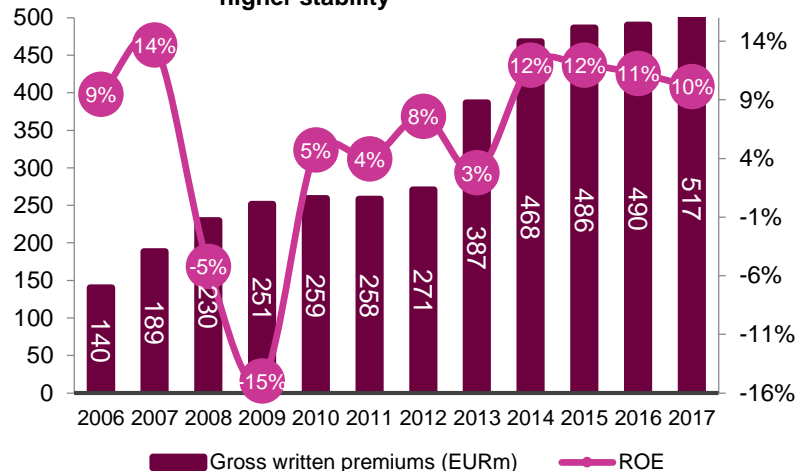
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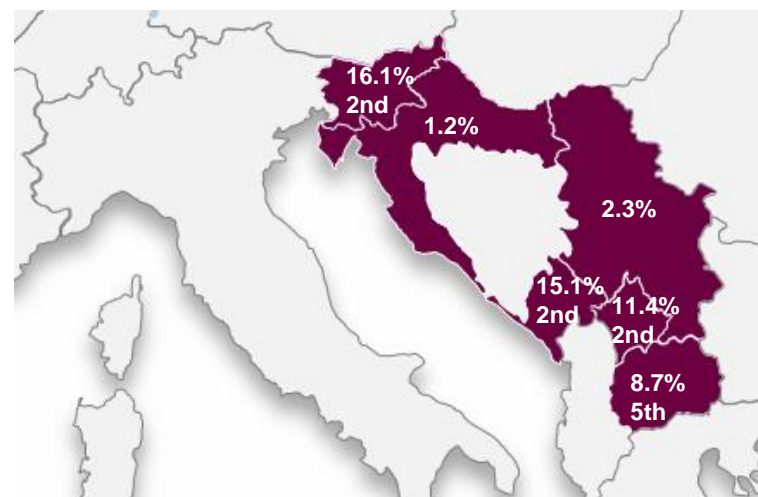
POSITIVE:

- In recent years Sava RE transformed itself from reinsurance player to **2nd largest insurance group in Adria region** with insurance presence in 6 countries. In the same time, Group strategy is seeking further growth through acquisitions, digitalization and technological modernization.
- Sava Re Group is 2nd largest insurer in Slovenia where it generates majority of its GWP and **held 16.1% market share in 2017**, trailing only Triglav.
- With acquisition of **Zavarovalnica Maribor** the Group took an opportunity to consolidate Slovenian insurance industry and to **benefit from synergies**. While takeover was concluded already in 2013, in 2016 Sava Re started with further centralization of insurance segment, connecting its Slovenian and Croatian operations. Operations have become more streamlined. While previously announced synergies were delivered, Sava RE expects there will be a further add-on in 2018.
- Sava Re Group stable profitability and positive effects following the ZM acquisition activities led to high capital adequacy ratio which enabled Group to pay out **above average dividend payout** and also initiate share buybacks which ended in 2016. For this year management proposed a repetition of dividend in the amount of EUR 0.8, **yielding a hefty 4.7%**. Given the fact management is sticking with current guidance of EUR 37 to 39m profit, we can expect this hefty dividend level to continue in 2019 as well.
- Majority of Sava Re premiums are generated on the domestic market, however the Group also has an **exposure to other SEE markets** where future GDP growth will be faster and Sava Re could benefit from development of insurance market. Here Sava RE embarked more ambitiously in the last period with several M&A transactions.
- Sava Re generates a part of premiums also on global reinsurance market.** Although pricing trends are remain though (good global 2018 price expectations were short lived), this segment provides positive diversification effects.
- While Triglav Group will be very likely the preferred **takeover target** for large insurance groups, the acquisition of Sava Re is likely to be much easier since its smaller than Triglav. However there are no signs of privatization process which would be necessary for clearance to increase its ownership above 33% - denial was overturned on Slovenian courts - so battle rages on.

Acquisition of ZM led to improved profitability and higher stability



Market share in 2017



Investment Thesis

NEGATIVE:

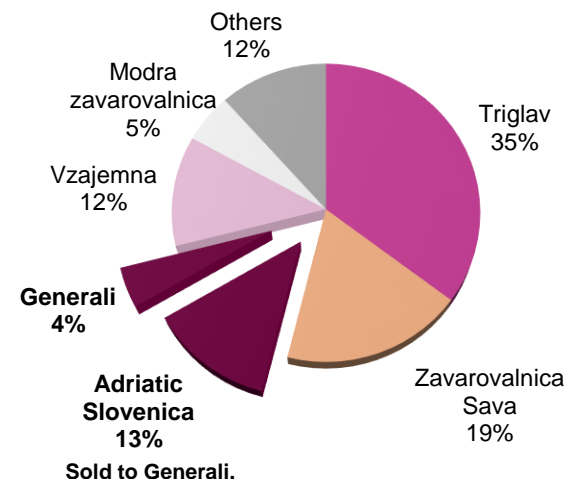
- Although Sava Re Group is the second largest insurance group in Adria region, that is mainly due to domestic Slovenian premiums which is also the most developed country in the region. The **importance of GWP outside Slovenia still very low**.
- Although the region presents an opportunity for above average growth of Sava Re Group, the **SEE region is also a highly macroeconomically and politically unstable** region with the legal systems and controlling mechanisms still in earlier stages of development (the lag in development varies from country to country).
- During the Slovenian banking crisis insures had an opportunity to benefit from higher interest rates on domestic market. However, currently also Slovenian insurance companies can feel the effects of zero interest rate central bank policy. **Low interest environment (reinvestment and interest rate risk) will weigh on investment returns** and consequently on profit level versus past few (excellent) years.
- In 2016 Sava Re ended the share buyback program with reaching maximum of 10% minus 1 of all issued shares. Since there is **no plan of retiring own shares** and could even be used for M&A, this could eventually negatively weigh in on EPS and the valuations.
- We believe reinsurance business is positive for diversification of operational risk, however current environment remains adverse. Due to low interest rates capital inflows on **global reinsurance market** pressured prices. Also high 2017 CAT events did not significantly improve pricing to recoup for higher claims.
- Although we consider Sava Re Group as most likely takeover target, we cannot get pass the fact that around 40% of shares are directly or indirectly **owned by the government influenced entities**. Since privatization is not supported by the public it is unlikely that politicians will support any takeover attempts. Additionally, there is also a risk of politically motivated influence on strategic focus and management stability.
- Adriatic Slovenica (3rd on Slovene market) was sold to Generali which also held a footing in Slovenia (4.7% market share). Together they will surpass Sava RE market share and possibly Generali could be better competitor in the future (time will tell how this will disrupt the market).

Interest rate sensitivity analysis for life and non-life (2017)

	+100bp		-100bp	
	Value	Change in value	Value	Change in value
Government bonds	460.4	-16.1	460.4	17.4
Corporate bonds	394.0	-12.5	394.0	13.5
Bond mutual funds	28.4	-1.0	28.4	1.0
Total	882.8	-29.7	882.8	31.9

	+100bp		-100bp	
	Value	Change in value	Value	Change in value
Value of mathematical provision	263.8	-10.5	277.3	13.5

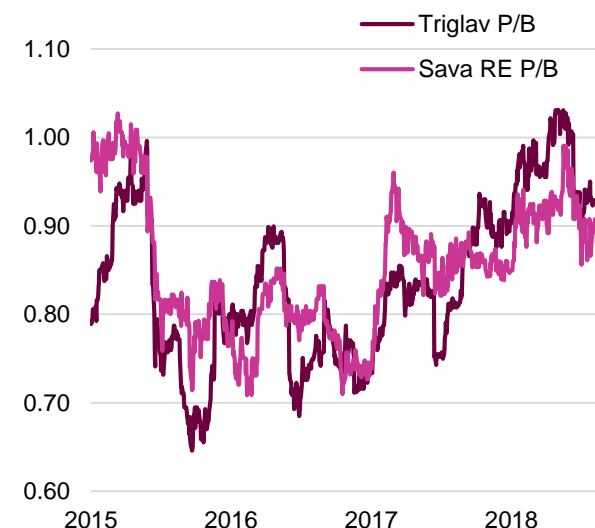
Slovenia insurance market by GWP



Relative valuation

Company name	P/E			P/B			ROE TTM		
	TTM	2018F	2019F	TTM	2018F	2019F	TTM	2018F	2019F
Zavarovalnica Triglav	10.6	9.4	9.1	0.95	0.88	0.87	8.9%	9.8%	9.6%
PZU SA	13.2	11.5	10.9	2.86	2.32	2.18	21.7%	22.2%	20.7%
Aksigorta	7.9	4.5	4.2	2.05	1.19	1.10	25.9%	33.1%	27.4%
Generali	10.2	8.9	8.7	0.96	0.85	0.82	9.4%	10.1%	9.7%
VIG	6.8	10.1	9.0	0.67	0.61	0.58	9.9%	6.3%	6.6%
Uniqua	10.7	11.4	10.4	0.88	0.87	0.87	8.3%	7.7%	8.3%
Allianz	11.8	10.0	9.5	1.32	1.14	1.08	11.2%	12.2%	11.6%
Hannover Re	14.5	12.0	11.5	1.71	1.54	1.46	11.8%	13.5%	13.0%
MunichRe	41.9	10.1	9.2	1.04	0.97	0.93	2.5%	9.9%	10.3%
Sava Re	9.2	7.2	7.2	0.82	0.76	0.72	8.7%	11.0%	10.2%
Median	10.7	10.1	9.2	1.04	0.97	0.93	9.9%	10.1%	10.3%

Company name	Div. yield (%)			Assets/ Equity (%)	Price to GWP	Price to Net Prem. Earned
	TTM	2018F	2019F			
Zavarovalnica Triglav	8.4	8.4	8.7	5.2	0.66	0.74
PZU SA	5.7	5.9	6.2	24.2	1.64	1.72
Aksigorta	0.0	16.3	17.3	4.9	0.60	0.80
Generali	5.9	6.6	6.9	22.2	0.35	0.35
VIG	3.8	4.2	4.6	11.5	0.32	0.35
Uniqua	6.0	6.7	6.9	9.6	0.47	0.56
Allianz	4.3	5.0	5.3	14.9	1.21	1.11
Hannover Re	4.2	4.5	4.7	7.7	0.76	0.86
MunichRe	4.6	5.2	5.5	10.1	0.57	0.61
Sava Re	4.8	4.8	5.5	5.6	0.49	0.54
Median	4.6	5.9	6.2	10.1	0.60	0.74

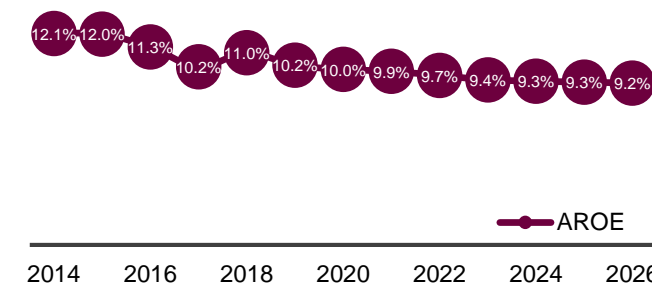
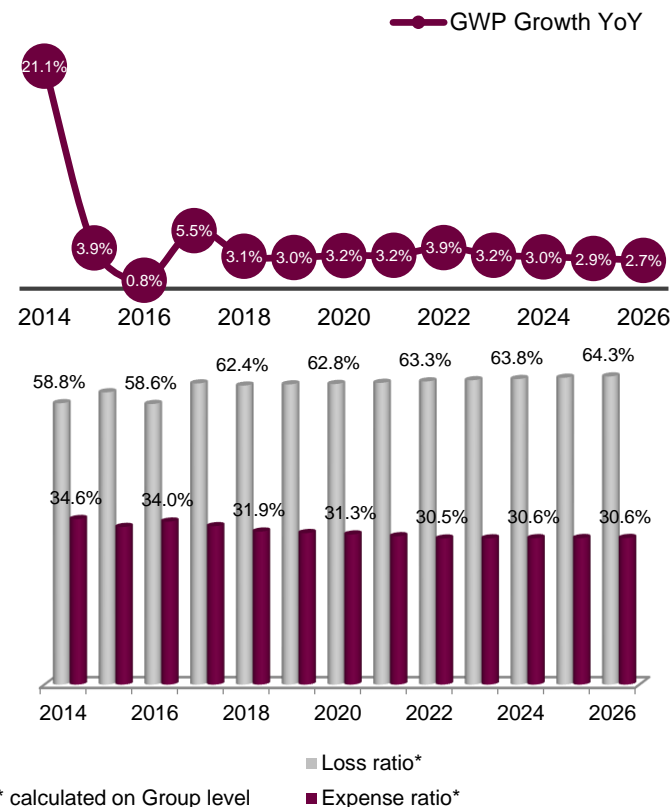


- Given the relative multiples analysis, Sava RE has a significant upside. Also given the Slovenian peer Triglav, Sava RE has more upside as its share price dynamic lagged the performance from Triglav in the last year. Discounts move around 20%.
- In May 2018 KD Group (Adriatic Slovenica, being 3rd largest on Slovene market) was sold to Generali for EUR 245m. This would roughly translate into 2.51x P/B, 23.0x P/E and 0.81x P/GWP (this entails Adriatic Slovenica insurance business and mutual fund business; ROE 10.9%). Versus these multiples Triglav trades at a significant discount as it would on average warrant a 60 per share price target despite similar profitability and despite higher risk profile of AS.
- Our target price for remained unchanged after weak 1Q18 and despite the fact 2Q18 was significantly better, target price lowered from EUR 23.4 per share to EUR 21.3. Nevertheless this still points to a hefty upside.

FCF valuation - Assumptions

MAIN ASSUMPTIONS:

- Sava RE guided for GWP in excess of EUR 520 in 2018, net combined ratio of 94.5%-94.5%, a gain mostly due to lower expense ratio, and a 1.7% return on investment portfolio. This should together add to a profit of EUR 37m to EUR 39m in 2018.
- 2018 estimates include acquisition of Energoprojekt garant and NLB Nov penziski fond AD, which by our estimates should increase their GWP by additional EUR 3.5m. On the other hand we also included expectation of continuation of organic growth in all segments except in Life Slovenia, where we predicted stagnation.
- In reinsurance we see further growth as Sava Re has a good credit rating.
- We expect a lower loss ratio in 2018 vs difficult 2017, albeit in the long term, loss ratio should increase (and with it combined ratio), partially as long term weather trends are worsening and partially as we believe competition will improve, especially once investment results will show improvement. Note this improvement in investment result can be hoped for only gradually through reinvestment (which takes time).
- Expense ratio should further improve in 2018 and also onwards (albeit at a slower pace), in 2018 due to already announced synergies in combining Slovene and Croatian operations, and afterwards due to economies of scale.
- Combined ratio is targeted between 94.0% and 94.5% in the next 5 years.
- For now we have calculated in effective tax rate achieved in last two years, which can provide some upside risk through lowering it.
- Our forecasted net income for 2018 has increased and is set at EUR 35.9m below management guidance. As we believe management guidance was ambitious in terms of bottom line, demanding optimal environment, this gave our estimates some room for disappointments like 1Q18.
- Solvency ratio should remain strong ... as we have appropriately set the dividend payout ratio as Sava RE strategy implies. However as we used 40% dividend policy and given the profit level, we see pressure on ROE. Higher dividend would improve ROE and hence valuation.
- Note Sava Re ended 2016 with the Solvency ratio of 200%. Since Sava Re's calculations do not include „Loss-absorbing capacity of deferred taxes“, adequacy ratio is in line with Triglav Group which ended 2016 with ratio of 246%.



FCF valuation - Forecasts



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ESTIMATES:

Year	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F
Total Assets	1,757.9	1,812.0	1,872.0	1,938.6	2,023.2	2,094.7	2,165.2	2,234.1	2,301.1
Total investment assets	1,080.1	1,116.6	1,157.2	1,210.8	1,241.6	1,289.0	1,335.8	1,381.3	1,425.5
Financial investments in assoc.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cash and cash equivalents	27.0	22.3	23.1	24.2	24.8	25.8	26.7	27.6	28.5
Technical reserves	1,181.7	1,211.6	1,245.7	1,285.0	1,340.3	1,386.6	1,433.0	1,479.1	1,524.9
Equity	339.2	360.8	383.7	407.9	432.9	454.3	474.7	493.6	510.8

Year	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F
Gross written premiums	533.2	549.1	566.4	584.3	607.2	626.6	645.5	664.0	681.9
Growth (%)	3.1%	3.0%	3.2%	3.2%	3.9%	3.2%	3.0%	2.9%	2.7%
Net earned premiums	487.9	502.3	518.1	536.2	557.4	575.5	593.3	610.6	627.5
Growth (%)	3.6%	3.0%	3.1%	3.2%	4.0%	3.2%	3.0%	2.9%	2.7%
Net claims	304.6	314.9	325.2	337.9	352.9	365.7	378.5	391.2	403.7
Loss ratio*	62.4%	62.7%	62.8%	63.0%	63.3%	63.6%	63.8%	64.1%	64.3%
Expense ratio*	31.9%	31.6%	31.3%	31.0%	30.5%	30.5%	30.6%	30.6%	30.6%
Combined ratio*	94.4%	94.3%	94.1%	94.0%	93.8%	94.1%	94.4%	94.7%	94.9%
Net investment result	22.0	23.1	24.9	27.0	29.6	31.9	34.8	37.8	40.9
Profit/(loss) before tax	45.2	45.1	46.9	49.3	51.1	52.6	54.6	56.6	58.4
Net income	35.9	35.9	37.3	39.2	40.6	41.7	43.4	44.9	46.4
Growth (%)	15.5%	0.0%	3.9%	5.1%	3.7%	2.8%	3.9%	3.6%	3.2%

* calculated on Group level

Year	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F
EPS	2.31	2.31	2.40	2.53	2.62	2.69	2.80	2.90	2.99
EPS growth	15.5%	0.0%	3.9%	5.1%	3.7%	2.8%	3.9%	3.6%	3.2%
ROE	11.0%	10.2%	10.0%	9.9%	9.7%	9.4%	9.3%	9.3%	9.2%
ROA	2.1%	2.0%	2.0%	2.1%	2.1%	2.0%	2.0%	2.0%	2.0%
BVPS	21.9	23.3	24.8	26.3	27.9	29.3	30.6	31.9	33.0
Dividend	0.80	0.93	0.93	0.96	1.01	1.31	1.48	1.68	1.88

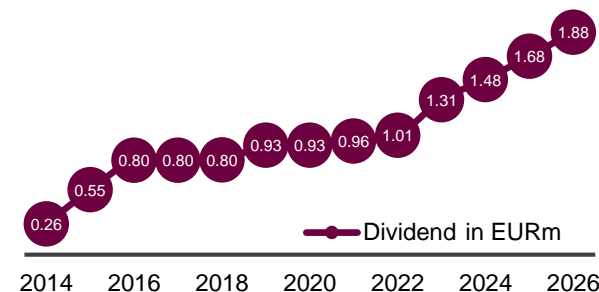
Excess return - Commentary

VALUATION TABLE:

Year	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F	2027F
Net profit	35.9	35.9	37.3	39.2	40.6	41.7	43.4	44.9	46.4	45.7
Cost of Equity	-25.2	-28.3	-30.1	-32.0	-34.1	-36.2	-37.9	-39.6	-41.2	-42.7
Excess return	10.7	7.5	7.1	7.1	6.5	5.6	5.4	5.3	5.1	3.0

Long-term cost of capital	
Equity Invested	301.3
Period PV of Equity Excess Return	48.3
Terminal PV of Equity Excess Return	23.0
Value of Equity	372.6
Equity value per share	24.0

Cost of equity	2018	TV
Leveraged beta	1.0	1.0
Risk free rate	1.25%	1.25%
Premiums	6.92%	6.92%
Cost of equity	8.4%	8.4%
Perpetuity growth rate	2.0%	

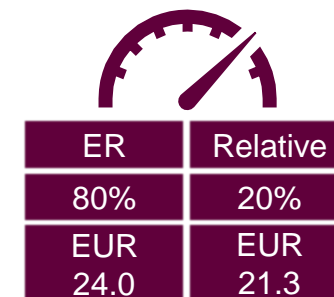


- Given the stability of capital adequacy ratio dividend payout policy is now more linked to estimated future capital needs and return of the excess capital. Dividend payout ratio could be around 40% in the next few years.
- Despite weaker 1H18, which is mostly due to weak 1Q18 burdened by CAT events, we have for now stuck with our estimates from 2017 report. This means target price is also unchanged. True, this on one hand means downside risk is elevated. However its also true, we were more cautious regarding estimates vs management guidance. In addition, management did not change its 2018 guidance but reiterate it.

Solvency 2 ratio	Capital
> 230%	Overcapitalization Additional engagement
200% – 230%	Appropriate capitalization Potential reallocation
170% - 200%	Optimal capitalization Optimization of operations
140% – 170%	Still appropriate capitalization Potential reallocation
< 140%	Undercapitalization Safeguarding the solvency

WEIGHTING SCHEME & END COMMENTARY:

- Our baseline target price consists of peer (20% weight) and excess return valuation (80% weight) method. Combination of both valuation methods derives to a target price of EUR 23.5 and hence only slightly lower vs our previous research report.
- We still believe Sava RE has more upside versus the closest peer, that is Zavarovalnica Triglav (however Triglav is delivering a better dividend yield) on relative and excess return basis. True Zavarovalnica Triglav price corrected as well, so we rate both insurance companies with a buy.
- Note that investor sentiment could be under the influence of possible shareholder structure change news and/or rumors (that is Adris M&A story). On this front however, there was little news in the last few months and little can be hoped for.



Historic Financial Data

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in EURm	2010	2011	2012	2013	2014	2015	2016	2017
Assets	578.4	582.0	640.6	1,378.3	1,454.4	1,607.3	1,671.2	1,708.3
Intangibles	23.3	18.3	17.8	40.2	34.9	30.5	25.5	22.7
Property, plant and equipment	26.7	24.5	24.6	46.0	44.5	47.2	51.9	45.4
Investment property	4.9	6.1	5.1	5.6	5.1	8.0	7.9	15.4
Investments in associates	42.3	49.1	55.3	2.9	3.1	0.0		
Financial investments	324.2	325.2	350.2	931.1	974.7	1,015.1	1,030.2	1,038.1
Unit-linked insurance assets	23.7	24.1	27.6	175.8	202.9	214.2	224.2	227.2
Cash and cash equivalents	4.0	4.7	4.1	3.4	5.6	4.7	33.9	38.0
Equity	154.7	148.1	171.4	240.1	271.5	286.4	297.0	316.1
Equity of non-controlling interests	4.4	2.5	2.0	2.0	1.9	1.0	0.8	0.3
Subordinated liabilities	31.2	31.2	31.2	30.5	28.7	23.5	23.6	0.0
Insurance technical provisions	303.3	320.9	360.1	846.2	870.0	887.1	911.2	931.4
Insurance technical provisions for unit-linked insurance contracts	23.6	23.7	27.0	170.8	195.7	207.6	227.0	226.5
Book Value per share	8.7	8.5	9.8	13.8	15.7	16.6	17.2	18.3

in EURm	2010	2011	2012	2013	2014	2015	2016	2017
GWP	259.1	258.4	270.8	386.7	468.2	486.3	490.2	517.2
ceded written premium	-25.3	-24.4	-20.6	-22.6	-27.4	-30.3	-31.2	-34.2
change in unearned premiums	-1.9	1.1	-3.9	15.6	-4.2	-8.0	-1.8	-13.8
change in unearned premiums for the reinsurance and co-insurance part				-0.5	0.9	-0.4	1.0	1.6
NPE	231.9	235.1	246.2	379.1	437.6	447.6	458.1	470.9
Net claims incurred	-140.0	-136.2	-149.9	-229.0	-257.1	-273.1	-268.4	-296.1
gross claims settled	-131.3	-128.4	-136.3	-221.2	-255.3	-271.5	-269.4	-309.7
reinsurers' and co-insurers' share	13.3	8.6	5.4	9.1	10.6	17.7	14.8	15.8
changes in claims provisions	-22.0	-16.4	-19.0	-11.6	-16.9	-5.4	-15.8	-2.9
change in the provision for outstanding claims for the reinsurance and co-insurance part				-5.3	4.6	-14.0	2.1	0.7
Operating expenses	-85.3	-87.9	-87.7	-129.4	-146.6	-148.9	-159.6	-157.0
Acquisition cost	-44.3	-53.5	-54.8	-46.9	-47.5	-49.9	-51.9	-51.9
Investment Income	19.9	17.8	21.7	36.4	36.1	39.6	33.1	27.4
Net unrealised gains on investments of life insurance policyholders who bear the investment risk		2.5	3.5	9.2	19.1	26.6	18.0	16.8
Expenses for financial assets and liabilities	-10.2	-14.2	-10.7	-42.0	-6.9	-13.0	-8.6	-11.9
Net unrealised losses on investments of life insurance policyholders who bear the investment risk		-5.5	-2.3	-9.5	-7.9	-25.9	-11.3	-8.3
EBT	8.8	7.7	14.3	15.8	39.0	40.1	40.7	39.9
Total taxes	-3.3	-3.7	-2.5	-0.2	-8.4	-6.7	-7.8	-8.8
Net profit / loss	5.5	4.1	11.8	15.6	30.5	33.4	32.9	31.1
Attributable to equity holders of the parent	7.5	6.0	12.1	15.7	30.6	33.4	32.8	31.1

in EURm	2010	2011	2012	2013	2014	2015	2016	2017
Loss ratio	60.4%	57.9%	60.9%	60.4%	58.8%	61.0%	58.6%	62.9%
Expense ratio	36.8%	37.4%	35.6%	34.1%	33.5%	33.3%	34.8%	33.3%
Combined ratio	97.2%	95.3%	96.5%	94.5%	92.3%	94.3%	93.4%	96.2%
Net margin	2.9%	2.3%	4.5%	4.0%	6.5%	6.9%	6.7%	6.0%
Assets Turnover	0.45	0.44	0.42	0.28	0.32	0.30	0.29	0.30
ROA	1.3%	1.0%	1.9%	1.1%	2.1%	2.1%	2.0%	1.8%
Assets to Equity	3.85	4.00	3.78	5.79	5.39	5.63	5.64	5.41
ROE	5.0%	4.1%	7.2%	6.6%	11.3%	11.7%	11.1%	9.8%

Source: Annual and Interim reports

Company & ALTA Description

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COMPANY DESCRIPTION:

- A leading Slovenian reinsurer with a 31% domestic market share while it is also the largest locally-based non-captive reinsurer in the CEE region.
- Through consolidation of Zavarovalnica Maribor and Tilia which ended with forming Zavarovalnica Sava the Group became second largest insurance company in Slovenia.
- It also operates on foreign markets in the Western Balkans (Croatia, Kosovo, Macedonia, Montenegro, and Serbia).
- 64% of total GWP tied to non-life, 17% to life, 19% to reinsurance (2017).

OWNERSHIP STRUCTURE:

SDH d.d.	17.7%
Zagrebačka Banka (Fiduciary)	14.2%
Republic of Slovenia	10.1%
Sava RE d.d.	10.0%
EBRD	6.2%

Source: KDD

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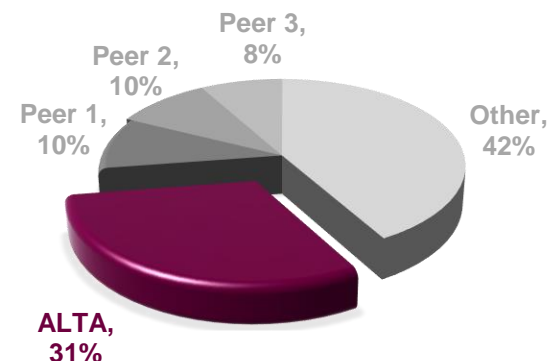
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- ✓ 38,300 brokerage clients with EUR 3.3 bn of assets.
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