

## Quarterly Update

Rating

# HOLD

LATAM (Caribbean)

Sector: Finance

Industry: Banking, Insurance, Wealth Management



JSE Bloomberg  
SJ SJ JA

### 9M-2023: IFRS 17 lowers Sagicor's Shareholders' equity but Standard expected to improve transparency for investors.

(Reading time: 8-10 mins)

## Rationale

Sagicor Group Jamaica ("SJ" or "the Group"), is a leading financial conglomerate, commanding a large market share in many of the business lines in which it operates. Sagicor is as a premier provider of insurance solutions in the Caribbean. The Group's portfolio includes a diverse range of products, such as life and health insurance, annuities and pension investment and administration services. Additionally, they offer property and casualty insurance, complemented by other financial services including banking and investment management, further solidifying their position as a multifaceted financial group.

The Sagicor brand is very strong especially with regards to its insurance business line. Among the benefits it enjoys are economies of scale and better pricing possibility due to its customers being less price sensitive. Essentially, Sagicor has generally enjoyed higher margins and a strong bottom-line. However, the sustained success of the Sagicor Group also reflects its commitment to reliability, innovation, and good customer service.

Over the last few years, the Group performed commendably especially when considered within the context of the global pandemic and its negative impact on economic activity, high inflation and high funding cost which followed and currently exists. Further, in the first three months in 2023, the Group implemented the International Financial Reporting Standard (IFRS) 17. While the adoption does not change the fundamentals of its core operations and strengths, its implementation led to a noticeable reversal of previous years' profits and a decline in the Group's equity. While this may naturally cause investor apprehension about the Group, we are of the view that this is a necessary step towards better transparency and possibly stronger future earnings growth given the strength of the business.

While the fundamentals of the group remain strong, its current market price (J\$40.51) is marginally above our current price target of J\$34.31, suggesting that the stock is slightly above its fair value, and as a result, we recommend a HOLD at this time.

### 18-Dec-23

Current price	40.51
Forecasted Dividend	0.93
Target price	34.31
Previous recommended price	N/A
<b>TOTAL RETURN</b>	<b>-13.01%</b>

### Company Data

Outstanding shares	3,905,634,916
Market Cap	158,217,270,447
52-Week (Hi/Lo)	40.00/59.42
1Yr Daily Average Volume	90,309
5Yr Daily Average Volumes	249,902

### Major Shareholders

LOJ Holdings Limited	32.45%
PanJam Investment Limited	30.21%
Sagicor Life Inc.	16.66%

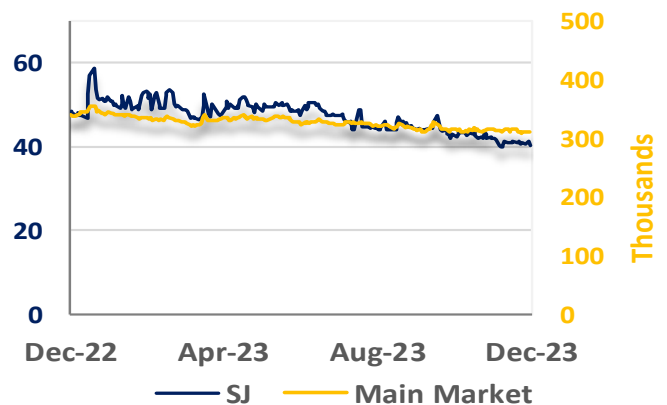
### Key Financials

J\$ Bn	FY21	FY22	FY23e	FY24e
Net Operating Income	102.56	97.10	74.64	79.27
Operating Profit	24.09	21.93	17.67	18.32
Net Profit	17.64	16.60	11.78	12.22
Net Profit Change (%)	293.4%	-5.9%	-29.0%	3.7%
EPS	4.46	4.19	2.98	3.09
Dividend Yield	1.91%	2.69%	1.56%	2.38%

### Price Performance

1MTH 3MTH 1YR

SJ	-3.9%	-9.3%	-26.5%
Main Index	-0.4%	-3.0%	-18.3%



Source: Bloomberg; JN Fund Managers Limited

Return on Equity 9M-2023	Return on Assets 9M-2023	Contractual Service Margin 9M-2023	Capital Adequacy Ratio (Bank Only) 9M-2023
16% +17%	1.96% +2.01%	\$4.08 B +29.52%	13.25% +0.15%
9M-2022: -1%	9M-2022: -0.05%	9M-2022: \$3.15 B	9M-2022: 13.1%

## Financial Overview

### Revenues & Profitability

For the nine-month period ending September 30, 2023, the Sagicor Group Jamaica continued to produce strong core operating results, with year-over-year growth recorded in its net insurance service results, net investment income and Fee income. The long-term and short-term insurance segments continue to show robust performance and have contributed substantially to the overall revenue growth of the group.

The long-term insurance segment includes products whose contracts exceed one year and are measured using the general measurement model and the variable fee approach under IFRS 17. The segment continues to report strong core insurance results; through the release of a Contractual Service Margin<sup>1</sup> (CSM) of J\$4.08 billion (FY 2022: J\$3.15 billion) and by generating a new business CSM of \$3.78 billion (FY 2022: J\$3.80 billion). The segment also saw improvements in investment income net of finance expenses. However, the Net profit for the segment was negatively impacted by exchange rate fluctuations. The short-term insurance segment, where contracts are less than a year old and measured under the Premium Allocation Approach under IFRS 17, also saw a marked improvement reporting a profit of J\$1.43 billion versus a loss of J\$1.26 billion a year earlier.

Despite improved market stability over the past year, current conditions continue to present challenges in the financial markets, particularly within the banking and investment sectors. As a result, the Commercial Banking segment produced net profits of J\$2.14 billion over the nine months, which was lower than the results (J\$2.34 billion) posted in the same period a year earlier. The segment recorded an 11.00% increase in revenues, linked to greater volumes on its card payments portfolios and growth in net interest income. Loan portfolios continue to exhibit growth, with new loans written and reported at J\$26.15 billion (versus J\$25.25 billion in the 9M-2022), contributing to a J\$2.06 billion increase in interest income. Importantly, loan quality improved year-over-year with the provision coverage ratio ending at 2.12% in September 2023 versus 2.29% September 2022. However, as deposit and other funding liabilities grew by J\$11.06 billion during the nine-month period, the increased cost of funding led to an approximate 66.00% increase in interest expense.

Overall, the group posted total revenues of J\$59.82 billion, 23.4% above the amount reported for the similar period in FY 2022 after the restatement of the original 2022 results as required by IFRS 17. Total benefits were J\$26.72 billion, reflecting modest 8.96% growth year over year. Other operating expenses were lower by 6.33%, however, coming in at J\$20.07 billion versus J\$21.43 billion in the same nine-month period in FY 2022.

<sup>1</sup> Contractual service margin - The contractual service margin (CSM) is a concept introduced by IFRS 17 for insurance contracts. It represents the unearned profit that an insurance entity expects to earn as it delivers services over the life of the contract.

**Strong Growth in Core Operating Revenues:** Despite the global headwinds, the Group continued to post net insurance service results, net investment Income and Fee income which were higher than the amounts reported last year, driven by expansion in its loan and card payment portfolios, strong insurance sales growth, particularly within the corporate segment, and despite unfavourable capital market conditions.

**Strong Regulatory Capital:** As of September 30, 2023, all operating entities continued to display key capital ratios that were still significantly better than the regulatory requirements, despite the negative impact of IFRS 17 on the group's capital and the impact of a high interest rate on fixed income prices.

**Strong growth in adjusted shareholders' equity** – SJ's shareholders' equity adjusted to include CSM, jumped by 26.00% over the nine-month period. The CSM is a metric used to measure the entity's future or unearned profits based on the long-term insurance contracts it has sold. Essentially, it is an indication of the SJ's future profitability.

### Risks to Monitor

**Low Economic Growth:** With the uplift ingrowth that followed the pandemic, now largely behind us, the countries in which SJ operates are expected to see slow growth in the short to medium term. A significant slowdown would likely mean that group could find it more difficult to grow its earnings within that context.

**High Interest Rate:** If high inflation remains "sticky," the relatively high interest rate environment that currently exists and is expected to remain throughout the short term could persist into the medium, which means that the group could face higher funding costs for a longer period. The high interest rate could also delay any significant rebound in asset prices.

**Basel III Implementation:** The Bank of Jamaica (BOJ) is currently implementing the Basel III capital requirements (Pillar I) and has updated the regulatory capital definitions. The new requirements come as the banking regulator is of the view that the current capital and liquidity requirements are no longer aligned with widely observed international regulations.

## Financial Overview cont'd.

### Revenues & Profitability

With the higher total revenues and lower operating expenses, the group's efficiency ratio improved to 33.55%, down from 44.21% when the current nine-month period is compared to the previous year's.

The share of profits from the joint venture was J\$82.27 million in the period, significantly less than the J\$329.73 million recorded in 9-Month 2022. These profits arose from the Group's shareholding in Sagicor Costa Rica, SA. Income before taxes for the nine-month period ended September 30, 2023 was J\$13.11 billion which was significantly better than the previous year's outturn of J\$2.86 billion and had an effective tax rate of 22.03%.

With the improved performance, several of the group's key metrics saw an improvement. Insurance service results of J\$5.11 billion were over 100% higher than what was reported for the restated 9-month period in FY 2022. The amount of Contractual Service Margin (CSM) released - the present value of the unearned profit that Sagicor expects to earn in the future as it provides the services grew by approximately 29.00% to reach J\$4.08 billion. These among other operational improvements helped to push net profits attributable to stockholders to J\$10.07 billion versus J\$-0.53 billion over the same nine-month period in FY 2022. Further, return on stockholders' equity was 16.00% following a 1.00% return recorded a year earlier.

### Balance Sheet

The group's total assets were J\$541.66 billion, marking a moderate 4.99% uptick on the amount (J\$515.94 billion) reported at the end of FY 2022. This movement came on the back of a 7.83% growth in Sagicor Bank's loan portfolio (up J\$8.82 billion) and the group's financial investments, which climbed by 4.34%, or J\$13.89 billion, over the nine-month period.

The growth seen in Sagicor's asset base was funded by increased deposits and securities liabilities, and its life insurance contract liabilities which grew by J\$12.84 billion and J\$4.41 billion respectively. It is likely that the growth in deposits was a result of the generally higher rates now being offered on deposits to consumers given that, over the last year, rates have increased substantially.

Shareholders equity grew by approximately 7.00% to J\$89.15 between December 2022 and September 2023. This improvement in the group's equity position was driven by an increase in profits over the nine-month period. This growth is also commendable considering the headwinds faced by the investment banking business due to high rates and the volatility in asset prices. Despite the challenges, the group's regulatory ratios not only continue to exceed the capital requirements across all its operating entities but also showed improvements in the respective ratios recorded when compared to September 30, 2022.

## Risks to Monitor Cont'd

### Basel III Implementation (Cont'd) -

After the (current) period of parallel reporting is complete, the rules will become mandatory for deposit taking institutions (DTIs). The new requirements will mean that DTIs must adhere to stricter capital rules, potentially prompting Sagicor Bank Jamaica to exercise greater caution in its lending practices, which may slow its loan growth and earning potential.

## Valuation Summary

### 1. Relative Valuation Method (Summary)

Industry Average P/B = 1.16x  
 SJ's Book Value = J\$22.83  
 P/B Valuation Est. = J\$26.59

### 2. Relative Valuation Method (Summary)

Historical P/E = 13.68x  
 SJ's Frwd. Earnings = J\$3.09  
 P/E Valuation Est. = J\$42.22

**SJ's Average Valuation Est. = \$34.31**

## Glossary of Terms

Asset Turnover .....	The asset turnover ratio measures how effectively a company uses its assets to generate revenue or sales.
Bank of Jamaica.....	The Bank of Jamaica is the central bank of Jamaica located in Kingston. It was established by the Bank of Jamaica Act 1960 and was opened on May 1, 1961.
Contractual Service Margin (CSM).....	The contractual service margin (CSM) is a fundamental concept introduced by IFRS 17. This represents the unearned profit that an entity expects to earn as it provides services.
Current Ratio .....	The current ratio (current assets/current liabilities) is a liquidity ratio that measures a company's ability to pay short-term obligations or those due within one year.
CY.....	Calendar Year (January to December)
Di.....	Next year's expected dividend
DTI – Deposit Taking Institutions .....	Financial institutions that are authorized to accept deposits from customers and provide various banking services.
Efficiency Ratio .....	The efficiency ratio shows expenses as a percentage of revenue (expenses/revenue). It essentially calculates how much a business spends to make a dollar.
FY.....	Financial Year or Fiscal Year
Gross Margin .....	A profitability measure that looks at a company's gross profit compared to its revenue or sales, expressed as a percentage.
Leverage Ratio (Assets/Equity) .....	The Asset to Equity ratio is derived by dividing a company's total assets by its shareholders' equity. This ratio is an indicator of the leverage (debt) used to finance the company.
NIR - Net International Reserve .....	Net reserves are defined as that portion of the gross reserves attributable to MOST's interests after deducting royalties and interests owned by others.
NOI - Net Operating Income.....	Earnings reported by a bank or bank holding company, after deducting normal operating expenses, but before taking gains or losses from sale of securities, other losses and charge-offs, and additions to the reserve account for possible loan losses.
Net Profit Margin .....	Measures how much net income or profit is generated as a percentage of revenue.
NPL - Non-performing Loans .....	Non-performing loans are loans as to which there have been no payments of principal or interest for 90 days or more.
Non-performing Loans (NPL) ratio .....	Non-performing loans as a percentage of gross loans and advances
QoQ - Quarter on Quarter .....	Used when comparing the financial performance between one quarter of one year to the same quarter of the previous year
Q1 .....	Quarter 1 or First quarter (usually of a company's financial year or country's fiscal year)
ROE - Return on Equity .....	Return on Equity is a measure of financial performance calculated by dividing net income by shareholders' equity.
YoY - Year over Year .....	Used to compare data or performance for a specific metric from one year to the same period in the previous year
YTD - Year to date .....	The period of time from the beginning of the current calendar year up to the present date.

**Disclaimer:** All information contained herein is obtained by JN Fund Managers Limited's Global Investment Research Unit from sources believed to be accurate and reliable. All opinions expressed are based on the Research Analyst's judgment as of the date of the report. As such, no warranty is made, expressed, or implied by JN Fund Managers Ltd. in any form whatsoever as to the accuracy, timeliness or completeness of the information contained in this report. JN Fund Managers Ltd. is therefore not liable for any actions taken in reliance on information contained herein.

JN Fund Managers Ltd.'s Global Investment Research Unit does not provide investment advice that considers the circumstances and objectives of the parties who receive this report. It is therefore recommended that before making any investment decision, investors seek the advice of a JN Fund Managers Limited's Investment Advisor.

This report does not represent an offer to buy or sell, or solicitation of an offer to buy or sell the securities mentioned. Past performance is not necessarily an indication of future performance. Estimates of future performance are based on assumptions that may not be realized. Additional information not available in this research report may be available upon request.

JN Fund Managers Ltd. is a multifaceted organization with, investment banking, investment management, fund administration, and brokerage business lines. JN Fund Managers Ltd. may, therefore, conduct investment banking or other business activities with some of the companies and countries covered by the Company's Global Investment Research Unit.

JN Fund Managers Ltd. may invest in and trade the securities covered in this report for its proprietary account and/or on behalf of its clients. JN Fund Manager Limited's trading activity in these securities may be contrary to the recommendation(s) indicated in this report.