

Sector View

Insurance

No Q4 Top Pick as there are too many risk factors

	1 M	3 M	6 M	31/12/15
Insurance	2.1%	13.1%	-6.0%	-18.8%
DJ Stoxx 600	-1.0%	10.2%	1.5%	-7.0%

*Stoxx Sector Indices

Companies covered

Company	Rating	Market Cap.	Price
AEGON	NEUTRAL	EUR6	
Last Price	EUR3.362	EUR7,254m	
ALLIANZ	BUY	EUR180	
Last Price	EUR130.2	EUR59,501m	
AXA	BUY	EUR29	
Last Price	EUR18.64	EUR45,188m	
CNP ASSURANCES	NEUTRAL	EUR15	
Last Price	EUR14.76	EUR10,134m	
COFACE	NEUTRAL	U.R.	
Last Price	EUR6.301	EUR991m	
EULER HERMES	BUY	EUR89	
Last Price	EUR75.73	EUR3,229m	
HANNOVER RE	SELL	EUR110	
Last Price	EUR94.76	EUR11,428m	
MUNICH RE	SELL	EUR185	
Last Price	EUR165.85	EUR26,711m	
SCOR	BUY	EUR35	
Last Price	EUR27.485	EUR5,277m	
SWISS RE	NEUTRAL	CHF100	
Last Price	CHF87.15	CHF31,380m	
ZURICH INSURANCE	NEUTRAL	CHF270	
Last Price	CHF248.8	CHF37,452m	



LOOKING BACK ON Q3 2016

The insurance sector slightly outperformed the market in Q3 after a terrible Q2. Yet only three companies we cover outperformed the sector in Q3: CNP (+4% vs. sector, partially driven by BRL), Munich Re (+2% vs. sector, as it partially recovered from a poor Q2 following a profit warning in May) and AXA (terrible performance post Brexit vote). Aegon was by far the worst performer (down 16% vs. sector).

Fears associated with Brexit did not materialise in Q3, because so far i/ there has been no Brexit!, and ii/ political management has been pretty satisfactory. Yet the hard work will come in due time...

H1 2016 insurance numbers were pretty much in line with expectations, down 6% on average for primary insurers (lower investment income, some pressure on underwriting results) and down 18% on average for reinsurers (lower investment income, higher natcats). FY guidance has been reaffirmed. As expected, and despite the negative impact of end-Q2 flight to quality, solvency margins remained very comfortable across the board. Investors should expect 2016 dividends (due spring 2017) to be stable in most cases.

The European bond market performed well in Q3, with rates and spreads going down (8bps for the 10Y Euro, 18bps for the iTraxx Main, 54bps for the iTraxx Xover, 25bps for the iTraxx Senior Financials, 26bps for the iTraxx Sub. Financials). The European equity market also rose slightly (3%). US rates have notched up (10bps) as most players expect the FED to raise interest rates in December. Bottom line, we can expect insurers' NAVs to be slightly higher at end-September vs. their June level.

WHAT WE SEE FOR Q4 2016

We expect a volatile market environment in Q4, as illustrated by the rise of volatility indexes in recent days. More specifically, we will deal with some critical events that may have major impacts on financial markets. For a start, Portugal on 21st October when rating agency DBRS will state whether Portugal is still Investment Grade, i.e. eligible for ECB refinancing, the US presidential elections on 8th November and the Italian referendum on 4th December. Current uncertainties in the banking sector (i.e. NPL issue in Italy + Deutsche Bank and Italian banks' weak capital positions) are also a concern as banking debt represents c. 12.5% of insurers' total investment portfolios.

Higher volatility and potential flight to quality due to these economic/political issues represent concrete risks for the insurance sector in the short term. Remember stress scenarios such as the Chinese crash at the beginning of the year and Brexit vote at end-June have had major negative impacts on the sector.

We do not expect Q3 results (due beginning of November) to provide any specific trigger for the sector, with ongoing pressure on investment income, lower commissions on asset management and unit-linked products (Stoxx50 down 12% yoy on average) as well as potential hedging losses.

CONCLUSIONS AND TOP PICKS

Considering that visibility remains poor in the short-term, we believe it is wise to again restrain from placing insurance companies in our quarterly Top Pick list.

For longer term investors, and provided the stress on financial markets remains under control, we believe current prices offer attractive entry points, especially for AXA. On the other hand, should markets be bumpy by year end, reinsurers, Zurich and Allianz offer more defensive profiles than average.

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