

Key Insurance Company Limited

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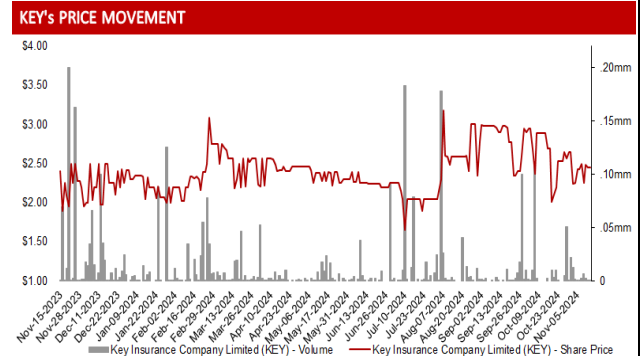
Executive Summary

Key Insurance Company Limited (KEY) is registered and domiciled in Jamaica, and its principal activity is the underwriting of motor, commercial and personal property and casualty insurance. On March 29, 2020, Grace Kennedy Financial Group Limited (GKFG) acquired 65% of the issued stock units of Key Insurance Company Limited (KEY). Subsequently, on April 9, 2020, KEY graduated from the Junior Market of the Jamaica Stock Exchange (JSE) to the Main Market. In January 2021, KEY raised \$668 million via a rights issue whereby an additional 190,862,238 ordinary stock units were issued to new and existing stockholders. GKFG exercised its rights and increased its shareholding to 72%.

For the 12-month period ending December 2023, KEY reported insurance revenue of \$2.50 billion, which represents a 16.4% increase from the previous financial year. However, net profit declined by 22.8% to \$41.94 million, down from \$54.35 million in the prior year.

In contrast, for the nine-month period ending September 2024, revenue increased by 14.8% to \$2.27 billion. During this same nine-month period, net profit rose by 24.2% to \$50.17 million, compared to \$40.40 million during the corresponding period in the previous year.

We assign an **UNDERWEIGHT** recommendation on KEY at this point, given the near to medium term challenges. Key Insurance continues to face significant challenges related to insurance service expenses. The growth in investment income has played a critical role in offsetting some of the financial pressures caused by rising claim expenses. The company's ability to sustain revenue growth and leverage investment income while addressing claims and operational expenses is crucial to its long-term success.



KEY's Statistics

Financial Year End	December	
Stock Price (14/11/2024)	\$	2.45
Trailing EPS	\$	0.09
Book Value per share	\$	2.48
Trailing P/E		26.50x
P/B		1.0x
Net Profit 9M FY2024 (millions)	\$	50.2
Price Target	\$	2.67
Dividend Yield		0.00%

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Key Insurance Company Limited

Company Overview

Key Insurance Company Limited (KEY) operates as a general insurance company in Jamaica. The company operates in Motor and Non-Motor segments. The company was incorporated in 1982 and is headquartered in Kingston, Jamaica. Key Insurance Company Limited operates as a subsidiary of GraceKennedy Financial Group Limited (GKFG). Grace Kennedy Financial Group Limited (GKFG) acquired 65% of the issued stock units of Key Insurance Company Limited which was completed on 29 March 2020. Subsequently, on April 9, 2020, KEY graduated from the Junior Market of the Jamaica Stock Exchange (JSE) to the Main Market.

In January 2022, the Company raised \$668,000,000 by way of a rights issue whereby an additional 190,862,238 ordinary stock units were issued to new and existing stockholders. GKFG exercised its rights and increased its shareholding to 72%.

The Company is licensed by the Financial Services Commission (FSC) to provide insurance protection for all classes of General Insurance and currently offers Motor and Non-Motor insurance coverage to the public. Motor offerings include Public and Private Comprehensive Insurance, Public and Private Third-Party Insurance and Public Passenger Vehicle Insurance. While non-motor offerings include Commercial and Personal Property Insurance; General Accident Insurance; Liability Insurance and Travel Insurance.

Key Insurance adopted International Financial Reporting Standard 17, “Insurance Contracts” (IFRS 17), effective for the annual reporting period beginning January 1, 2023. IFRS 17 supersedes IFRS 4 and introduces a current measurement model, requiring estimates to be re-evaluated each reporting period. This new standard has a significant impact on how insurance and reinsurance contracts are accounted for.

Financial Overview

Income Statement Review

Key Insurance reported total insurance revenue of \$2.50 billion for the fiscal year 2023, marking a 16.4% increase from \$2.15 billion in fiscal year 2022. This growth was driven by strong performances in both the motor and non-motor insurance segments. The non-motor segment saw an impressive 29% increase, while the motor segment grew by 12%, highlighting Key Insurance’s strategic efforts to diversify and strengthen its product offerings. For the nine months ending in September 2024, insurance revenue climbed 14.8% to \$2.27 billion. Key Insurance noted that this growth is primarily due to consistent premium increases in the motor portfolio, which accounted for 65% of the total insurance revenue.

The insurance service expense, which encompasses both claims paid and operating expenses related to providing insurance services, rose by 10% from \$1.68 billion in 2022 to \$1.84 billion in 2023. Although this increase in expenses is significant, it is lower than the revenue growth rate, suggesting that the

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company was able to partly manage its cost structure despite facing external challenges like rising claims costs and inflationary pressures. However, during the first nine months of the year, the insurance service expense grew faster than insurance revenue, climbing by 17.6% to \$1.59 billion. This rise in expenses is due to an increase in both the frequency and severity of motor vehicle accidents, resulting in higher claims costs. Specifically, claim expenses surged by \$177 million, or 22%, compared to the same period last year.

Net expenses from reinsurance contracts held saw a sharp increase of 41.2%, rising from \$503.51M in 2022 to \$710.89M in 2023. As a result of these higher costs, the insurance service result for FY2023 was a loss of \$51.43M, compared to a loss of \$30.02M in 2022. This outcome underscores the impact of rising claims and reinsurance expenses on the company's core insurance operations. For the 9M FY2024 period, KEY's insurance service continues to experience a loss, reported at \$24.09M, though an improvement from the loss of \$35.52M recorded in the same period in 2023.

On the investment side, interest revenue from financial assets rose by 39.1% from \$138.33M in 2022 to \$192.41M in 2023. This significant growth is attributed to higher returns from investment securities, as the company strategically invested in short-term, high-yield instruments to take advantage of rising interest rates. Investment income was essential in helping to partially offset the losses experienced in core insurance operations. Subsequently, interest revenue from financial assets increased significantly by 24.0%, to \$174.75M for the nine months FY2024. **The performance of KEY's investment portfolio continues to be the bright spot, offsetting some of the pressures from insurance service expenses.**

In FY2023, finance income derived from insurance contracts experienced a significant decline of 47.9%, totalling \$16.52 million. Concurrently, finance expenses related to reinsurance contracts decreased by 25.6%, amounting to \$11.61 million. As a result, the net insurance and investment income increased by 17.3% year-over-year, reaching \$145.90 million for the fiscal year 2023. This improvement underscores the effectiveness of Key Insurance's investment strategy and the beneficial impact of elevated interest income, notwithstanding the challenges present in the insurance segment.

In FY2023, other operating income experienced a marked decline of 32.0%, totalling \$45.94 million. In contrast, other operating expenses were reduced by 4.4%, amounting to \$114.58 million in 2023, reflecting diligent efforts to manage costs and enhance operational efficiency. However, during the nine months concluded in September 2024, operating expenses rose by 41.7% year-over-year, totalling \$108.71 million.

Consequently, the company reported a pre-tax profit of \$77.26 million in FY2023, representing a 7.2% increase from the \$72.10 million reported in 2022. This growth suggests that Key Insurance's strategic initiatives aimed at enhancing its investment portfolios and managing costs have proven partially effective in mitigating the effects of increased claims and reinsurance expenses.

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After accounting for taxation, which increased significantly by 99.0%, net profit fell by 22.8%, from \$54.35 million in FY2022 to \$41.94 million in FY2023. This decline in net profit reflects the combined effects of higher reinsurance and claims expenses, despite improvements in revenue and investment income. The net profit margin stood at approximately 1.68% down from 2.53% a year ago. Subsequently, for the nine months ended September 2024, Key Insurance recorded a profit before taxation of \$75.12M, an increase of 24.2% year over year. The company achieved a net profit of \$50.17 million, a 24.2% year-over-year growth and outpacing the 2023FY net profit by 19.2%.

The company's earnings per share (EPS) decreased from \$0.10 in 2022 to \$0.07 in 2023. The trailing twelve-month (TTM) EPS stands at \$0.09.

Balance Sheet Review

As of December 31, 2023, Key Insurance reported total assets of \$4.10B, reflecting an 8.9% increase from \$3.76B in 2022. This was mainly driven by the 18.7% year over year increase in investment securities reported at \$1.88B. This increase highlights the company's strategic investment in high-yielding, short-term securities, such as certificate of deposits, to optimize returns in a rising interest rate environment. Moreover, due from brokers experienced a substantial increase of 49.0%, rising to \$442.11M. This change indicates improved premium collection processes and possibly higher premiums processed through brokers. However, reinsurance contract assets decreased sharply by 92.5% year over year, reported at \$9.70M. This decline reflects lower recoverable amounts from reinsurance contracts, which could be due to changes in reinsurance arrangements. KEY highlighted that during the year, the Company signed a new Loss Portfolio Transfer (LPT) agreement and commuted its previous agreement. With this agreement, the reinsurers promise to cover/compensate Key Insurance for any motor loss suffered for cases reported or those that have insured and not yet reported prior to the inception date of the contract. Notably, the company's cash and cash equivalents remained relatively stable, increasing slightly by 0.2% to \$845.77M.

As of September 30, 2024, Key Insurance's total assets increased to \$4.34 billion from \$4.16 billion a year ago, reflecting a growth of 4.4%. This increase was mainly driven by a surge in investment securities, reported at \$1.71B, up 60.5% year over year. Notable, cash and cash equivalents was down 34.9% year over year, reported at \$1.03 billion.

Total liabilities increased by 11.9%, reported at \$2.76 billion as at the 2023FY. This was mainly attributable to the 7.5% year over year increase in insurance contract liabilities reported at \$2.55B, reflecting higher reserves set aside to cover potential future claims, consistent with prudent risk management practices. Furthermore, other payables more than doubled, rising by 163.6% from \$68.02M to \$179.29 million.

Total Liabilities was up 3.7% year over year, reported at \$2.96 billion as at September 30, 2024. This was mainly due to the increase in insurance contract liabilities up 9.7%, booked at \$2.82 billion.

Shareholder equity rose by 3.2%, reported at \$1.34 billion in 2023. Retained earnings were the primary driver of this growth, increasing by 15.0%, booked at \$321.04 million. Share capital and capital reserves remained unchanged, while fair value reserves saw a slight decrease of 0.6%, to \$55.06 million. As at September 2024, shareholders' equity rose by 5.9% booked at \$1.39 billion, driven by a 26.5% year over year improvement in retained earnings reported at \$371.21 million.

Cash Flow Statement Review

Key Insurance generated cash from operating activities (CFO) of \$182.38 million in 2023FY, a significant year over year increase of 89.3%. This increase in cash generation was driven by changes in working capital components, despite a decline in net profit. The company's changes in working capital improved to \$263.64 million from \$195.51 million a year ago, this was mainly driven by reinsurance contract assets and other liabilities, reporting cash inflows of \$119.46 million and \$111.26 million respectively.

The company cash from investing activities experienced a cash outflow of \$154.98 million in FY2023, relative to the cash outflow of \$720.91 million in FY2022. This is mainly due to the reduction in cash invested in investment securities, down 48.4% at \$787.09 million. Notably, interest received grew by 60.2%, from \$107.52million to \$172.09 million, further supporting the company's cash flow through strategic investments in interest-bearing assets.

Net cash used in financing activities decreased by 8.9%, from \$11.77M to \$11.68M in 2023, solely driven by its lease liabilities. As a result of these cash flow movements, KEY experienced a net increase of \$15.71 million in its cash balance by the end of FY2023.

Subsequently, for the nine months ended September 2024, KEY's net operating cash flow deteriorated to an outflow of \$50.23 million from an inflow of \$121.23 million a year ago. The main driver to this downturn, was the weakening of the changes in working capital. The company's change in working capital fell to an inflow of \$25.80M from an inflow of \$198.36 million a year ago. Moreover, cash flow from investing activities experienced a year over year downturn, moving from an inflow of \$612.92 million to an inflow of \$241.98 million, driven by a decrease in cash from investment securities, reported at \$104.21M down from \$445.63 million a year ago. Furthermore, cash from financing activities reported an outflow of \$9.30 million, driven solely by lease payments. Consequently, KEY experienced a net increase of \$182.46 million to its cash balance by the end of September 30, 2024.

Forecast and Valuation Key Insurance Company Limited

We employed the price-multiples approach to determine the fair price for KEY. We utilized our projections for the Company's book value per share and earnings per share for FY2025 and applied the harmonic mean price-to-book (P/B) and price-to-earnings (P/E) multiples of comparable firms. The

harmonic mean of the P/E of comparable listed companies gives a market multiple of 14.9x, which when applied to the forward EPS resulted in a target price of \$1.52, while the P/B for the peer group of 1.2x yields a price of \$3.07.

The 2-year historical mean for the P/B ratio is 1.2x, which when applied to the forward BVPS yields a price of \$3.27. The 2-year historical mean for the P/E ratio is 27.6x, which when applied to the forward EPS yields a price of \$2.81. **The average of our price forecasts, \$2.67 is 8.9% above the closing price of \$2.45 on November 14, 2024.**

KEY's P/E ratio exceeds its peers; this may suggest that the market has high expectations for the company's future earnings growth, despite current profitability challenges or this valuation may also imply that KEY is currently overvalued relative to its earnings. Furthermore, KEY's P/B ratio is below General Accident's (GENAC); its ROE which is considerably below its peers currently justifies this. The Company's low ROE relative to peers is primarily due to lower net profit margin. KEY has a ROA of 1.07%, which is significantly lower than GENAC's 5.80% and ROC's 5.98%. KEY's lower ROA indicates less efficiency in utilizing its assets to generate profit compared to its peers. This metric highlights the need for operational improvements and more efficient use of assets to boost profitability.

Key Insurance (KEY) demonstrates some financial weaknesses compared to its peers in the property and casualty insurance sector. The company's elevated P/E ratio suggests high market expectations, but its low ROA and ROE indicate inefficiencies and weaker profitability. The relatively low P/B ratio may appeal to value investors, but the low net profit margin and asset turnover highlight areas needing improvement. Comparatively, GENAC appears to be a stronger performer with higher profitability and efficiency metrics.

Property & Casualty Insurance								
Ticker	Market Cap(\$M)	P/E	P/B	ROA	ROE	Financial Leverage	Net Profit Margin	Total Asset Turnover
GENAC	6,188	14.2	1.90	5.80%	17.21%	2.97	6.37%	0.91
ROC	820	10.32	0.95	5.98%	11.78%	1.97	6.02%	0.99
KEY	1,370	29.74	0.98	1.07%	3.19%	2.98	1.68%	0.64
Mean	1,421	14.93	1.15	2.4%	6.6%	2.54	3.26%	0.82

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Outlook

KEY's performance for its most recent quarter ending September 2024 illustrates a cautiously optimistic outlook. The company managed to improve its earnings, primarily driven by higher revenue and strategic investment income growth. This was achieved in the face of rising motor vehicle crash payouts, which have significantly increased claim expenses. The ability to improve profitability, despite heightened claim costs, underscores the effectiveness of the company's strategy centered around product expansion and a

robust investment portfolio. However, the insurance service result, which measures the profitability of the core insurance operations after accounting for claims and related expenses, reported a loss for the 2023FY and for the most recent **nine-month period** of the 2024FY. This loss is primarily due to the increase in insurance service expenses outpacing the growth in insurance revenue. The higher claims costs, driven by a surge in motor vehicle accidents, have significantly eroded the profitability of Key Insurance's underwriting operations. Despite higher revenues from premiums, the financial impact of these rising claims expenses remains a major challenge for the company.

Furthermore, the macroeconomic conditions in Jamaica also present both risks and opportunities for Key Insurance. Elevated interest rates have benefited the company's investment portfolio, contributing significantly to net interest income. However, the anticipated decline in interest rates could negatively impact investment returns. Additionally, economic conditions such as inflation and slower economic growth may impact consumer spending, potentially limiting the demand for insurance products. The company's ability to remain agile and adjust its investment strategies in response to these shifts is crucial.

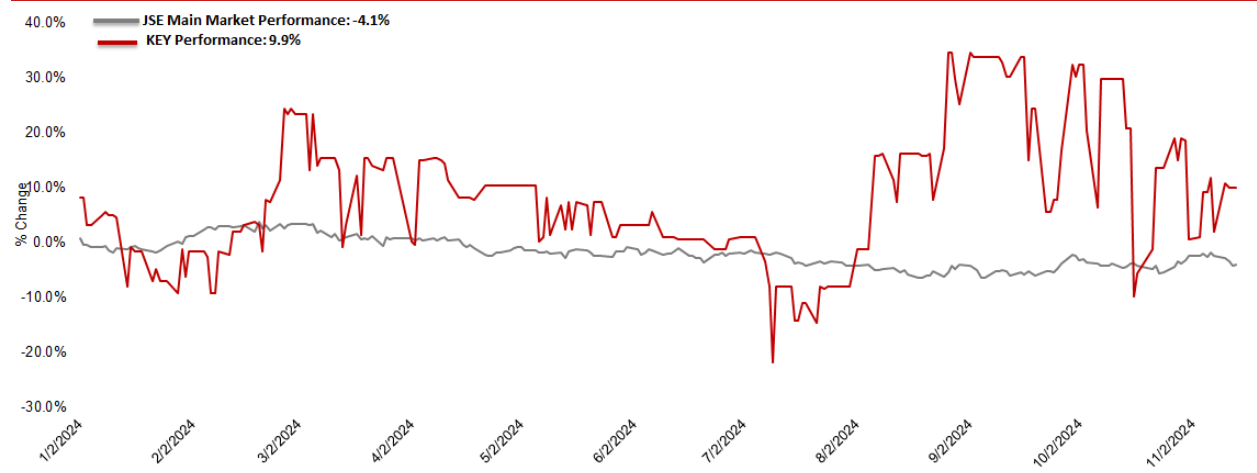
Recommendation

We assign an UNDERWEIGHT/ UNDERPERFORM recommendation on KEY at this point, given the near to medium term challenges. In addition, our recommendation considers the stability of KEY's earnings, operating cash flow and balance sheet strength. While Key Insurance faces several risks, particularly from rising claim expenses and macroeconomic uncertainties, the company's strategic initiatives, investment income growth, and revenue diversification provide a solid foundation for future performance. The company's ability to manage costs, leverage investment opportunities, and enhance customer engagement is essential to its sustained growth and profitability. The outlook is one of cautious optimism, with a focus on operational resilience and strategic execution to navigate a complex insurance landscape. Notably, our view is curtailed by KEY not making a dividend payment for several years and the vulnerability of earnings to a surge in claims expense.

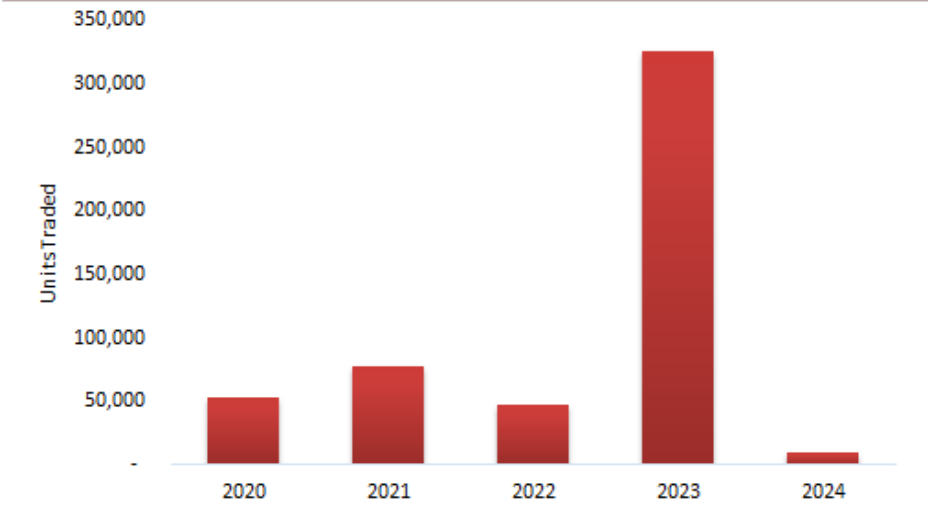
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KEY’s stock performance has improved 9.9% YTD, outperforming the JSE Main Market decline of 4.4% over the same period. Moreover, the liquidity of KEY’s shares surged to 325.89K units in calendar year 2023. As of present, the YTD average daily volume is 9.33K units.

JSE Main Market versus KEY Performance YTD



KEY Average Daily Volume



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Per Share Data	YE 2019	YE 2020	YE 2021	YE 2022	YE 2023	Change	Q3 2023	Q3 2024	Change
BVPS	1.79	0.70	1.92	2.32	2.39	3.2%	2.34	2.48	5.9%
EPS	0.73	0.81	0.29	0.10	0.07	-22.8%	0.07	0.09	24.2%
Price Per Share	3.2	6.0	4.0	3.3	2.2	-32.4%	2.5	3.0	20.4%
JSE Main Market	509,916	395,615	396,156	355,897	325,700	-8.5%	327,042	318,326	-2.7%
Dividend Per Share	0.00	0.00	0.00	0.00	0.00	N/A	0.00	0.00	N/A
Abridged Income Statement Data (in \$Millions)									
Gross Premium Written	1,403.7	1,432.1	1,915.0	0.0	0.0	N/A	N/A	N/A	N/A
Net Premium Net	-340.5	942.4	1,315.9	0.0	0.0	N/A	N/A	N/A	N/A
Insurance Revenue	0.0	0.0	0.0	2,149.6	2,503.1	16.4%	1,978.5	2,271.8	14.8%
Underwriting Profit/(Loss)	-793.5	-521.2	79.1	0.0	0.0	N/A	N/A	N/A	N/A
Insurance Service Result	0.0	0.0	0.0	-30.0	-51.4	71.3%	-35.5	-24.1	-32.2%
Investment income	32.9	27.5	59.7	138.3	192.4	39.1%	140.9	174.8	24.0%
Profit Before Taxation	-566.3	-449.5	237.6	72.0	77.3	7.2%	60.5	75.1	24.2%
Net Profit/(Loss)	-267.5	-299.7	160.4	54.3	41.9	-22.8%	40.4	50.2	24.2%
Abridged Balance Sheet Data (in \$Millions)									
Cash and deposits	937.0	745.2	1,474.2	844.3	845.8	0.2%	1,582.0	1,029.4	-34.9%
Due from reinsurers	2,037.1	363.9	1,059.6	0.0	0.0	N/A	0.0	0.0	N/A
Investment Securities	241.9	395.7	780.0	1,580.9	1,876.5	18.7%	1,068.4	1,714.9	60.5%
Total Assets	4,510.0	2,905.3	4,480.3	3,760.6	4,095.2	8.9%	4,161.0	4,344.3	4.4%
Due to reinsurers	1,604.8	151.9	800.4	0.0	0.0	N/A	0.0	0.0	N/A
Insurance contract liabilities				2,373.0	2,552.1	7.5%	2,572.5	2,821.4	9.7%
Insurance reserves	2,161.0	2,349.5	2,381.0	0.0	0.0	N/A		0.0	N/A
Total Liabilities	3,849.6	2,646.3	3,405.6	2,465.4	2,758.4	11.9%	2,851.5	2,957.1	3.7%
Fair value reserves	459.5	479.9	62.1	55.4	55.1	-0.6%	55.4	55.1	-0.6%
Total Equity	660.3	259.0	1,074.7	1,295.2	1,336.8	3.2%	1,309.6	1,386.9	5.9%
Abridged Cash Flow Statement Data (in \$Millions)									
CFO	-402.9	62.4	183.4	96.3	182.4	89.4%	121.2	-50.2	-141.4%
CFI	629.0	-238.5	-113.3	-720.9	-155.0	-78.5%	612.9	242.0	-60.5%
CFF	-11.6	-11.3	655.7	-10.8	-11.7	8.5%	-6.5	-9.3	42.9%
Key Ratios									
Dividend Payout Ratio	0.0%	0.0%	0.0%	0.0%	0.0%	N/A	0.0%	0.0%	N/A
Financial Leverage	4.6	8.1	5.5	3.5	3.0	-14.2%	3.1	3.2	2.3%
Net Profit Margin	-19.1%	-20.9%	8.4%	2.4%	1.7%	-31.6%	2.0%	2.2%	8.2%
ROE	-34.5%	-65.2%	24.1%	4.6%	3.2%	-30.4%	5.3%	6.1%	14.7%
ROA	-7.6%	-8.1%	4.3%	1.3%	1.1%	-19.0%	1.7%	1.9%	12.1%
P/E	-4.41	-7.33	14.02	33.99	29.74	-12.5%	20.4	20.9	2.7%
P/B	1.79	8.48	2.09	1.43	0.93	-34.5%	1.0	1.2	13.7%

Source: <http://www.jamstockex.com>, JMMB Investment & Research, Bloomberg, Various Company Financial Statements

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APPENDIX

IMPORTANT DISCLOSURES

ABSTRACT—As a part of our new Portfolio Strategy we are recommending strict adherence to the following Portfolio Allocation **DEFINITIONS/RECOMMENDATIONS**.

PLEASE NOTE THAT NO INDIVIDUAL ASSET IN YOUR PORTFOLIO SHOULD HAVE A WEIGHTING GREATER THAN 5% UNLESS OTHERWISE RECOMMENDED BY YOUR PORTFOLIO MANAGER OR A SPECIFIC JMMB RESEARCH REPORT. CONSEQUENTLY THE FOLLOWING **DEFINITIONS** ARE PROVIDED FOR CLARITY.

STRONGLY UNDERPERFORM—REDUCE EXPOSURE IN YOUR PORTFOLIO TO LESS THAN 2.5% FOR THIS PARTICULAR ASSET

UNDERPERFORM—REDUCE EXPOSURE IN YOUR PORTFOLIO TO 2.5% - 4.9% FOR THIS PARTICULAR ASSET

SELL—REDUCE EXPOSURE IN YOUR PORTFOLIO TO ZERO.

HOLD/MARKETPERFORM—EXPOSURE TO THE ASSET SHOULD BE EQUAL TO 5% OF YOUR TOTAL PORTFOLIO HELD AT JMMB.

OUTPERFORM/BUY—EXPOSURE TO THIS ASSET SHOULD BE BETWEEN 5% AND 10% OF YOUR TOTAL PORTFOLIO HELD AT JMMB

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