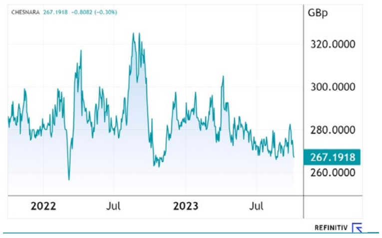
4 October 2023

HARDMAN&CO.

Life assurance



Source: Refinitiv

Market data

EPIC/TKR	**CSN**
Price (p)	**271.0**
12m high (p)	307.0
12m low (p)	259.0
Shares (m)	150.4
Mkt cap (£m)	407.5
Economic Value (£m)	523.2
Country of listing	UK
Market	London

Description

Chesnara primarily manages and acquires closed life assurance books in the UK, Sweden and the Netherlands.

Company information

CEO	Steve Murray
CFO	David Rimmington
Chairman	Luke Savage

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www.chesnara.co.uk

Key shareholders

Columbia Threadneedle	11.8%
Abrdn	10.9%
Hargreaves Lansdowne	7.5%
Interactive Investor	7.3%
M&G	6.5%
Canaccord Genuity	4.6%
Rotal London	3.7%
Janus Henderson	3.6%

Diary

10 Nov	Interim dividend paid
31 Dec	Financial year end

Analyst

Brian Moretta bm@hardmanandco.com

CHESNARA PLC

Good first half aided by markets and acquisitions

Chesnara has announced its 2023 interim results. Good returns in equity markets, most notably in Sweden, and the benefit from acquisitions meant earnings were well ahead of our normalised estimates. Economic Value profit was £61.0m, including £28.4m from acquisitions, compared with a loss of £75.7m in 1H'22. Despite paying the final dividend, Economic Value increased 2% over the half year to £523.2m. Cash generation was solid, with commercial cash generation of £21.8m, while base cash generation was lower after the symmetric adjustment at £11.1m. As expected, the interim dividend was increased by 3% to 8.36p per share.

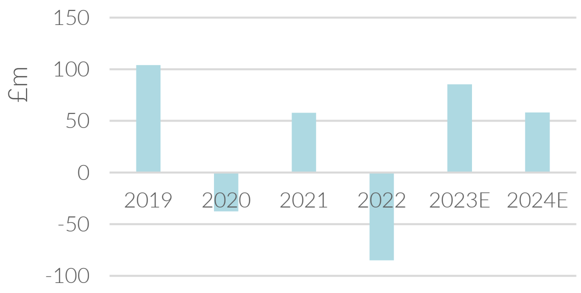
- **Acquisitions:** There was little incremental news on acquisitions, other than updates on completion. The gains on acquisition are slightly higher than expected, but base steady state cash generation is in line with expectations. With integration almost complete, Chesnara is ready for further M&A.
- **Estimates:** There were several operating lines that were better than expected and this has led to significant upgrades to our estimates. Our 2023E EPS is increased by 19% to 56.9p while our 2024E EPS increases 25% to 38.6p. Our 2024E Economic Value increases 2% to 375p per share.
- **Valuation:** With a price at approximately 75% of its forecast Economic Value, Chesnara seems undervalued. A prospective dividend yield of 8.9%, with good prospects of continued growth, also suggests an undervalued stock.
- **Risks:** Ultimately, the company remains tied to movements in financial markets and adverse developments in operational areas. Having just come through a testing period for the latter, in particular, we can see how well Chesnara can manage these challenges.
- **Investment summary:** Chesnara has three pillars for delivering value, under a responsible risk-based management. A close analysis reveals that there is substance underlying these aims. In our opinion, the discount to Economic Value looks wider than it should, and the yield appears high for a dividend that is both secure and growing.

Financial summary and valuation

Year-end Dec (£m)	2019	2020	2021	2022	2023E	2024E
Operating earnings	5.6	-66.1	-58.8	-26.8	14.1	13.7
Economic earnings	121.1	22.9	109.6	-109.1	43.4	44.7
Economic Value earnings	104.0	-37.6	57.8	-85.1	85.5	58.1
Economic Value/share (p)	446	424	416	340	360	375
Base cash generation	37	28	20	83	34	45
EPS (p)	69.3	-25.1	38.5	-56.6	56.9	38.6
Dividend (p)	21.30	21.94	22.60	23.28	23.98	24.70
Price/Economic Value (x)	0.60	0.63	0.64	0.79	0.74	0.71
Yield	7.9%	8.2%	8.4%	8.7%	8.9%	9.2%

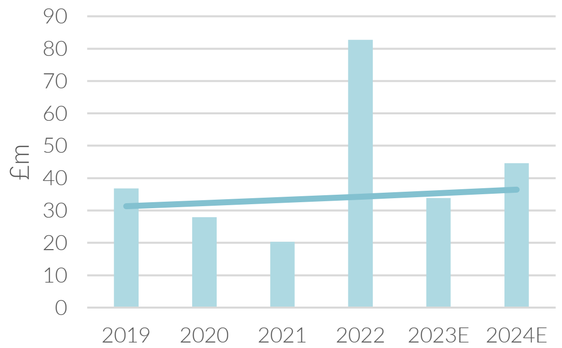
Source: Hardman & Co Research

Economic Value earnings



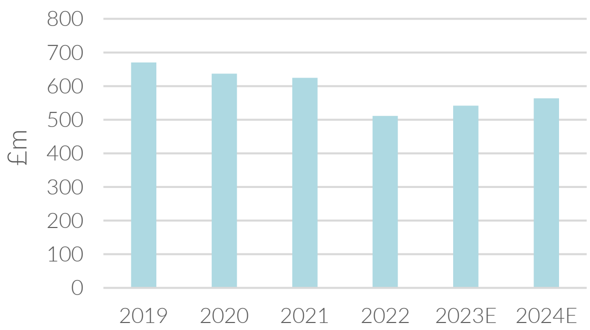
- Volatility for investment assets in 2020 and 2022
- Also affected by operational challenges
- Forecasts are based on normalised assumptions
- Gains from acquisitions in 2023 of £28m

Base cash generation and dividends paid (line)



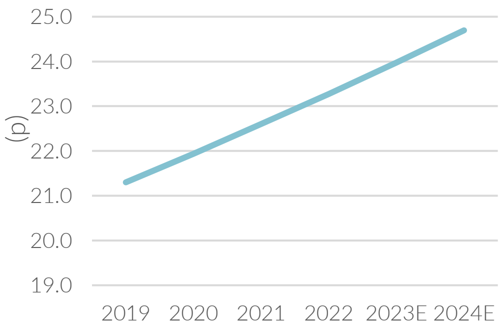
- 2020 affected by Scildon, 2021 by a challenging Swedish market
- Symmetric adjustment smooths effect of markets on cash
- 2022 cash boosted by currency hedge
- Removal of headwinds should restore cash generation to comfortable levels

Economic Value



- Volatility for investment assets in recent years
- Also affected by operational challenges
- Forecasts are based on normalised assumptions
- Gain from Sanlam, Robein Leven of £21m in 2022

Dividend per share



- Chesnara has been a consistent dividend payer for more than a decade and a half
- We forecast continued steady growth of 3% p.a.

Source: Company data, Hardman & Co Research

Results commentary

Headline results for 1H'23 showed much improvement over last year. They were doubly boosted by healthy market returns, especially from Swedish equities, and the benefits of acquisitions. Economic Value earnings of £61.0m were a strong turnaround from the loss of £75.7m in 1H'22. Economic Value increased 2% from £511.7m at 31 December 2022 to £523.2m. Within these figures, acquisitions provided a gain of £28.4m, offset by forex changes and, for the balance sheet, payment of the full year dividend.

Cash generation was decent, with base cash generation reducing from £21.9m to £11.1m (excluding impact of acquisitions). With positive markets, the symmetric adjustment weighed somewhat on base cash generation and commercial cash generation was higher at £21.8m, a turnaround from the £3.0m net consumption in 1H'22.

An interim dividend of 8.26p has been announced, exactly in line with our forecast and a 3% increase on the 2022 interim of 8.12p.

These results see the introduction of IFRS17. This changes the accounting for insurance contracts, but not investment contracts which constitute the majority of Chesnara's liabilities. This lack of completeness means we will continue to focus on Economic Value and cash generation as better indicators of what is going on in the business. While IFRS17 is perhaps a step forward from the previous accounting rules, and we will refer to a couple of items in it, to this analyst it feels like a wasted opportunity: despite the cost and significant efforts from finance teams, it isn't comprehensive enough to really help external analysts.

Earnings and operations

Economic Value earnings

Year-end Dec (£m)	2019	2020	2021	2022	1H'23
Expected movement	-0.4	0.3	-1.7	-1.3	7.7
New business	7.8	3.7	2.4	8	4.7
Operating experience variances	-6.8	-22.0	-19.2	-20.7	1.6
Operating assumption changes	3.8	-35.8	-13.9	-14.5	-5.4
Other operating variances	-0.3	3.9	-0.2	1.7	
Total u/l operating earnings	4.1	-49.9	-32.6	-26.8	
Material other operating items	1.5	-16.2	-26.2		
Total operating earnings	5.6	-66.1	-58.8	-26.8	8.6
Economic experience variances	143.1	45.7	79.5		
Economic assumption changes	-22.0	-22.8	30.1		
Total economic earnings	121.1	22.9	109.6	-109.1	31.6
Other non-operating variances	-5.2	-2.8	4.5	-2.6	-4.8
Risk margin movement	-7.0	4.7	10.8	20.4	0.9
Tax	-10.5	3.7	-8.2	12.0	-3.7
Gain on acquisition				21	28.4
Economic Value earnings	**104.0**	**-37.6**	**57.8**	**-85.1**	**61.0**
EPS (p)	69.3	-25.1	38.5	-70.6	40.6

Source: Hardman & Co Research

Although we don't have the breakdown of the economic earnings yet, improvement over 2022 is pretty clear across several lines of the P&L, not just the economic earnings.

Operating movements

As discussed in our previous notes, Chesnara has had some operating challenges over the past couple of years, much of which has been somewhat outwith their control. We have been optimistic that these will improve, and we are pleased to see that being realised in these results. While the positive operating result was underpinned by there now being a positive discount rate to unwind in the expected movement, the other lines showed the mixture of positive and negative experiences that we would expect to be more normal going forward.

Lapses

The largest challenge in the past couple of years has been the effect that legislative changes and some competitor pricing that defied rationality. We saw an improvement in 2H'22 and this has continued into 1H'23. Despite the strengthened assumptions, lapses were still slightly worse than expected but the experience was an order of magnitude better than what we saw a year ago.

Going forward, we note that Conservatrix policyholders have been locked-in due to the status of the company (recall, the parent was in bankruptcy). After being in place for a couple of years, this is being lifted on many policies. While Chesnara hope that there will be some uplifts from premium increases, there may be some additional lapses. We note that Waard saw higher-than-expected surrenders, which may be related its recent acquisitions. CASLP, another acquisition, also experienced higher-than-assumed lapses.

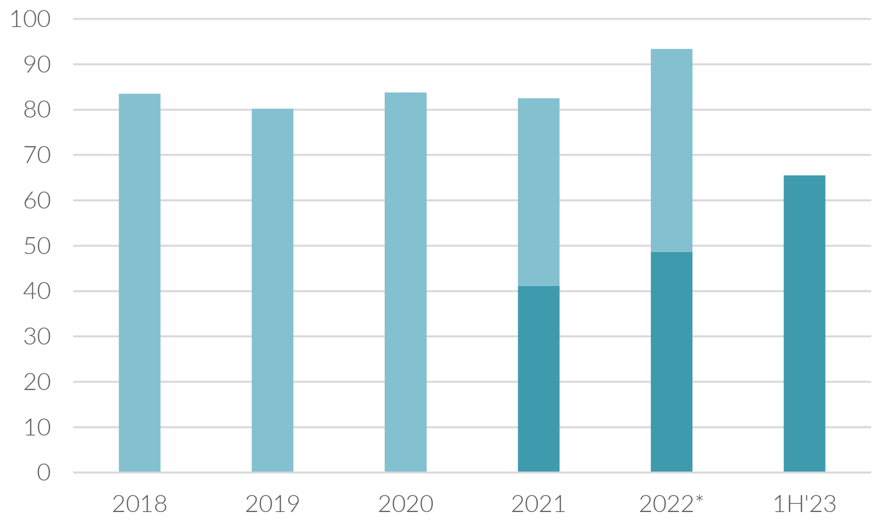
Mortality

With, hopefully, the worst of the pandemic behind us, we expect mortality to give less dramatic results going forward. In the first half, the only item noted is a positive experience within Waard. We have seen some strengthening in the past couple of years at the behest of the regulator, so hopefully the odds are we will see more of that going forward.

Expenses

Our expense analysis is somewhat complicated by the introduction of IFRS17. This affects the expense calculation shown in the accounts. While we have been supplied with restated 2022 figures, those for prior years remain on the old accounting basis.

IFRS expenses (£m) (1H'21 and 1H'22 highlighted)



Source: Chesnara, Hardman & Co Research
** 2022 figures are restated for IFRS17, prior years on the original accounting basis*

The first half saw a noticeable increase from £48.6m to £65.5m. The largest factor in this increase of 35% is acquisitions, with the addition of Sanlam in particular adding to the UK cost base. Other factors include the effect of inflation, as pay increases followed the surge that we have seen in the past year or so, and additions to central costs. The latter includes the growth in the M&A team and the (one-off) costs of implementing IFRS17[1].

Within Scildon, progress continues to be made on the IT system improvements. While this has had some cost overruns, completion is expected in early 2024 and this should lead to cost savings. Meanwhile, Waard saw some higher-than-expected surrenders, which had a positive effect on costs.

In the UK, a new outsourcing relationship with SS&C was announced. Chesnara expects that, in due course, it will realise unit cost savings and also be easier to integrate future acquisitions. Currently, SS&C is onboarding the former Sanlam business (now known as CASLP). However, in the short term there are some additional migration costs to be incurred.

While Chesnara previously strengthened its inflation assumptions, it followed the consensus view of a swift return to levels seen in the past few years. Although this is not materialising as expected, the short-term impact is limited. Chesnara assumes costs would rise ahead of inflation anyway (for example, the long-term assumption in the UK is 4.5%). There may be a muted impact from "higher for longer" in the next year or two.

Management changes

In September, Chesnara announced that Ken Hogg, the UK CEO, will be leaving. A new appointment has already joined the UK operation, suggesting a managed transition. With this, Countrywide Assured joins Scildon and Movestic in seeing CEO changes this year. The Scildon resignation took place in February and a new, experienced, CEO started in September. Movestic has appointed an interim CEO and a search is underway for a permanent replacement.

It is unfortunate that these have come so close together. All the departures had been in the role for several years and we see no reason to be concerned by the coincidental timing.

Economic movements

With positive market conditions, economic earnings in 1H'23 of £31.6m represented a great improvement over the loss of £91m in 1H'22. We forecast a full year result of £43.4m, so this is significantly ahead of our normalised expectations.

Of course, this result will always exhibit volatility, and we would hope, after a weak 2022, to get some balance with a better-than-expected result eventually. Chesnara notes that movements were in line with the published sensitivities.

Equities

Equity markets were positive in all three countries and the FTSE World Index rose 13% over the first half. In terms of influence on results, the 8% rise in the Swedish OMX All Share Index had the strongest effect, boosting Movestic's results to £15.0m. This was somewhat offset by fee pressure as the effects of strong competition continue.

Although the AEX Index's rise of 10% outperformed Sweden, the mix of business there is less exposed to equities, having a greater exposure to debt and credit. The

[1] That said, regulatory change seems to be an ongoing feature of the landscape. At least the expected changes to the risk margin calculations should have no cost implications.

FTSE All Share Index was a laggard, only rising 0.5% and behind what we would expect for a long-term return.

Interest rates

Interest rates have generally risen in 2023, although the rate of change in bond yields slowed relative to 2022. In the UK, the 10-year gilt yield rose to 4.43% from 3.78%. Although the Netherland bond yield has been on a rising trend since the end of 2021, this has been volatile. From 31 December to 30 June, the 10-year yield actually decreased from 2.9% to 2.7%, although it has since risen to over 3.3%.

Credit spreads also continued to widen, although there was a notable difference between the UK and Europe. In the former, AA corporate spreads increased only 2bps from 1.04% to 1.06%. Meanwhile, European AA credit spreads increased to 0.43% from 0.29%.

Interest rate changes affect both the assets and liabilities (although not equally), but credit spreads only affect the value of assets (albeit, if credit losses don't rise, there is an earnings benefit in due course).

With such variation, the effect on the individual divisions varied significantly. Although bond returns exceeded expectations in the Netherlands, this was offset by the mortgage portfolio reducing in value and, overall, the country saw an economic loss of £0.6m. In the UK, rising yields had a positive effect on Economic Value which exceeded the smaller benefit of equities.

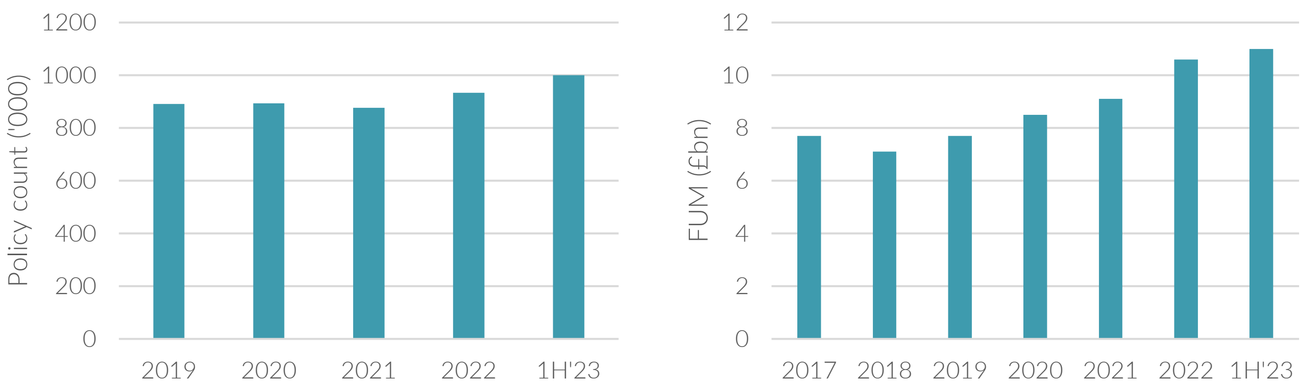
Fund returns

After several years of mostly positive performance relative to benchmarks, key UK fund returns underperformed over the past 12 months by 2.5%-3.0%. Despite this, the longer-term relative performance remains positive. Swedish policyholders saw an average return of 10.8%.

Operational KPIs

The alternative KPIs show the general improvement in Chesnara's operations. Although new business and market movements contribute to changes, recently acquisitions have been the biggest drivers. In 1H'23, the completion of Conservatrix and Canada Life were positive contributors, as were the positive equity market movements.

Policy count and funds under management



Source: Hardman & Co Research

CSM

IFRS17 has introduced a contractual service margin (CSM) figure. While it is incomplete (as noted above, it only applies to the 42% of Chesnara's liabilities that are classified as insurance) and the calculation basis is much less prescribed than for Solvency II (which may make comparisons with other companies a challenge), it does have some value to investors.

In short, the CSM is the present value of the future profits that insurance contracts are expected to deliver. Prudence means that these cannot be recognised immediately (although losses will be) but will be taken to the Income statement over time. Hence, it can be seen as an intangible asset for insurance companies.

As of 1 January 2023, the value of Chesnara's CSM was £103m. By 30 June, it had grown £54m to £157m. The largest factor in this by far was the acquisitions which added £56m. New business added £6m, with £10m release of profit.

Acquisitions

There has been one new deal announced so far in 2023: the protection book from Canada Life's onshore UK business. The results announcement was largely about how this and some of the earlier deals are progressing.

Recent acquisitions

	Sanlam (CASLP)	Conservatrix	Canada Life
Discount	19%	34%	44%
Day 1 Economic Value gain	£15m	£22m	£7m
Steady state annual cash	£5m	£4m	£3m
Integration status	On track	Complete	On track

Source: Hardman & Co Research

These transactions are progressing as follows:

- **CASLP**: as indicated earlier, SS&C are currently onboarding the policies onto their systems. As indicated at the time of the full year results, the Part VII transfer, which is full legal transfer of policies and assets to Chesnara and requires court approval, is expected to complete at the end of the year.
- **Conservatrix**: has now been fully integrated in Waard. Where customers wish to restart premiums, this is now possible again.
- **Canada Life**: as indicated at the time of the announcement, this is initially being enacted through a reassurance arrangement that took effect from 31 December 2022. Integration through SS&C is on track and the Part VII transfer is expected in early 2024. The consideration is £9m and the expected cash flow over the next five years is £16m.

The effect of Conservatrix in addition to the previous acquisitions is to bring better scale to Waard, which is now a meaningful contributor of cash for the group. The expected steady state cash flow is £8m p.a..

We note that market movements after the announcement led to a small increase in the day 1 Economic Value gain for Conservatrix to £22m.

Prospects

In our review of the annual results, we observed that market volatility had made the environment for transactions a little more uncertain. Given the first half was more stable, we should not be surprised that there has been an increase in transaction activity in UK and Europe. Most of these were portfolio transfers, which would fit Chesnara's desired profile.

With a positive first half, internal resources have increased, with £128m of cash now available on the balance sheet. The revolving credit facility takes resources to over £200m, before any further capital raising. We note that IFRS17 has had the effect of reducing leverage ratios, which may make capital raising easier. The M&A team has also been strengthened. With the recent Netherland acquisitions integrated and the UK ones on course for completion by early 2024, there are no operational barriers to further deals.

In terms of targets, the overall perspective is unchanged. The desire for value creation brings an implicit preference for deals in the three territories in which Chesnara operates. The synergies from existing operations and comfort with regulators are distinct advantages over entering new countries, although the latter is not ruled out.

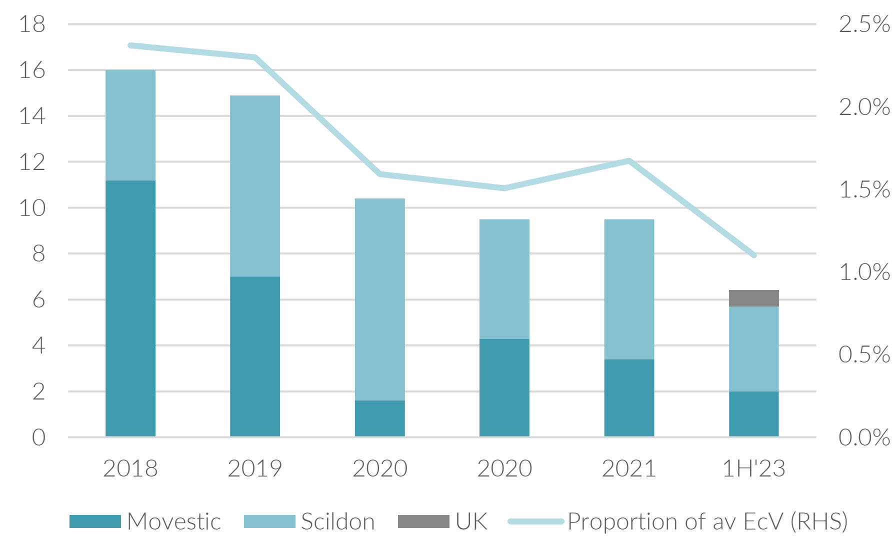
From management comments, Sweden is getting a little more attention as a location where it hasn't done a deal since buying Movestic over a decade ago. As always, the timing, scale and location of future transactions remains beyond our ability to predict, although we remain confident that there will be more deals in the near future.

New business

Although Sanlam was bought primarily as a closed book of business, it was selling some new business. Chesnara has decided to keep one of those lines going, an onshore bond offering. This is sold through a third party. With a realistic value of sales of £0.7m in 1H'23, this is a small, but helpful addition, to the existing sales through Movestic and Scildon.

After a tough couple of years, 1H'23 saw some improvement in the value of new business. The existing businesses produced business worth £5.7m, a 24% improvement over 1H'22. Adding the UK brings the total to £6.3m, or 1.1% of average Economic Value. This suggests new business is heading for its best year since before the pandemic.

Chesnara's value of new business (£m)



Source: Chesnara, Hardman & Co Research

We have discussed at length the challenges that the Swedish market has presented in our notes over the past couple of years. Unlike previous changes, the recent legislation to open up books to transfers affects areas in which Movestic has little existing business, and so presents more of an opportunity than a threat. Nevertheless, pricing remains competitive, so margins on new business remain tighter than previously.

Movestic's new business volumes increased 19% in 1H'23. This reflects an improvement in transfer in volumes, although custodial business, which had previously been a strength, fell 14%. In terms of market shares, the occupation pension market share rose to 4.2% from 4.1% six months ago, while the custodial market share declined from 9.5% to 7.7%. A risk product has been added to the offering.

The housing market in the Netherlands, which is a major influence on the term assurance market, remains subdued. Nevertheless, Scildon managed to grow volumes and market share as new business value increased from £3.1m in 1H'22 to £3.7m in 1H'23. The market share calculation has changed methodology, with a share of 12.1% as of June 2023, compared with 11.6% a year ago and 10.6% as of December 2022.

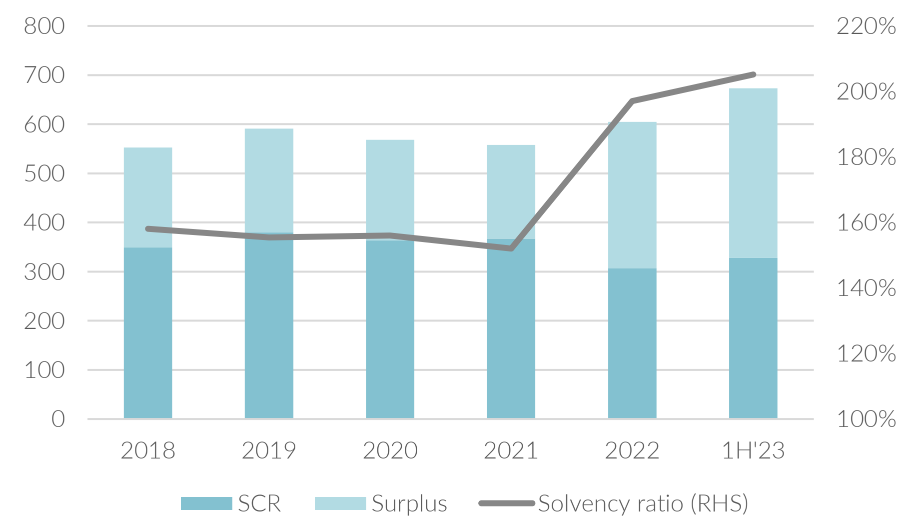
Capital and cash generation

Risk assets can have a complex effect on solvency ratios. While price rises or declines affect assets, the corresponding value changes of liabilities means the risks to be covered are also impacted. Within Solvency II, the Symmetric Adjustment is a countercyclical measure to smooth out changes: in times of good returns, some of the return is effectively set aside, to be released when returns are weaker. The positive returns on risk assets in 1H'23 meant that some return was set aside.

While IFRS17 does not affect solvency or Economic Value, it does affect the accounting balance sheet. It increased IFRS equity by £51.5m as of December 2022 to £385m. This decreased to £362m at the half year. This has an effect on the leverage ratio, which reduced from 37.6% under the old basis at the year end to 29.5% at the half year, although it is not clear yet how rating agencies will treat these changes.

Solvency

Group Solvency II metrics



Source: Chesnara, Hardman & Co Research

Over the half year, the Solvency Capital Requirement (SCR) and the surplus both increased: the former by 7% to £328m and the latter by 16% to £345m. The net effect was for the solvency ratio to increase to 205%. This is comfortably above the target range of 140%-160% and reflects the additional resources from last year's bond issue. This further illustrates the scope that Chesnara has to do further acquisitions.

The growth in the SCR was due to the increase in equity markets, increasing the risk capital required to back the company, and the acquisitions, which brought additional market and life underwriting requirements.

The largest contributor to the growth in surplus was from a reduction in the restrictions on the tier 2 debt which added £39.9m to the surplus. Although Chesnara has had to inject capital into some recent acquisitions, this still counts towards solvency and these added £8.8m to the surplus. Exchange rates were a negative contributor (£11.9m) as were dividends (£12.6m).

Operationally, all the divisions contributed positively to the surplus. The UK, with Countrywide and CASLP, was by far the largest contributor (£10.4m in total) with the Swedish and Netherland operations contributing £6.1m in aggregate. The Swedish and Netherland results were both depressed by exchange rate movements, although these were smaller than previous years, supported by the hedge that was introduced last year.

Cash generation

Cash generation in Chesnara is the net change in available surplus. Cash, and the dividend, at the group level, is funded from dividends from the individual divisions. These are generally paid annually and, in 1H, the dividend paid is only the final dividend, so coverage ratios would not be appropriate. The internal dividend figure is the UK contribution, with £10m being paid by Movestic in September and Waard paying £5m before the year-end.

Group cash generation breakdown

£m	2018	2019	2020	2021	2022	1H'23
Base cash generation						
UK	55.8	33.6	29.5	27.4	40.8	10
Sweden	18.1	-6.2	12.4	-14.4	16.1	-6.4
Waard	7.8	0.8	4.1	2.9	8.4	-0.4
Scildon	-17.7	22.6	-22.3	15.2	-3.4	-0.9
Group	-16.2	-14	4.1	-10.8	20.8	8.8
Total cash generation	**47.8**	**36.8**	**27.8**	**20.3**	**82.7**	**11.1**
Internal dividends						
UK	32.0	32.0	33.5	27.5	56.0	
Sweden	2.9	6.2	10.2	0.0	12.0	
Waard	12.9	4.9	4.0	6.1	5.3	
Scildon	21.7	7.0	0.0	5.0	0.0	
Total dividends from subsidiaries	**69.5**	**50.1**	**47.7**	**38.6**	**73.3**	
Dividends paid to shareholders	**30.4**	**31.3**	**32.3**	**33.3**	**34.3**	**22.8**
Cash cover (x)	1.6	1.2	0.9	0.6	2.4	
Internal dividend cover (x)	2.3	1.6	1.5	1.2	2.1	

Source: Chesnara, Hardman & Co Research

The first half produced a solid result for base cash generation, with the UK and central group activities being positive contributors, while Movestic and the Netherland operations were net consumers. The UK result was through growth in its Own Funds, with positive market movements supported by fee income and improved assumptions on future expenses. Compared with 1H'23, it also saw a full period contribution from CASLP.

Movestic's result was largely a function of the equity market movements, as the positive equity returns increased its capital requirement, including a contribution to the symmetric adjustment. Waard had solid operating results, but had increased market risk requirements. Scildon also had a good operating result, but capital requirements rose due to rising equity and credit risk.

Commercial cash generation was almost double the base generation a £21.8m, almost entirely due to the symmetric adjustment. This drew £10.6m, with the majority being required by Sweden. The with-profits adjustment was only £0.1m. The overall figure is slightly under half the full year 2022 figure, so is a healthy result.

Looking forward, although acquisitions have significantly increased our base expectations, their additional effect on future cash will be muted. Conservatrix has been included since January and the Canada Life deal was structured to be effective from the start of 2023. Thus the first half will have seen almost the full effect of them.

Dividend cover

As indicated above, dividends from the divisions will total £72m in 2023. This would be more than 2x the cost of dividend to shareholders, which we estimate at £35.3m. This should give shareholders comfort that the dividend is, at least, sustainable going forward.

Prospects

Operations

Since 30 June, equity markets have not been hugely supportive. At the time of writing, the UK All-Share Index was marginally up while the OMX had declined a handful of percentage points. Looking at bonds, UK gilt yields are flat-to-up, while the 10-year Netherland bond yield has increased to over 3.3%. The aggregate is likely to be a small negative effect on Economic Value, although with 4Q still to go, the full-year result is far from determined.

Operationally, we can look forward to the UK's ongoing transition to the SS&C platform, while Scildon's IT upgrade should complete in early 2024. While the costs of each of these can be seen as one-offs, our view is that there is usually a steady stream of such projects: Chesnara is continually looking to keep its systems competitive and that involves ongoing costs.

Hopefully, we will soon see the results of the Risk Margin consultation in the UK and a finalising of the reduction, although the actual rule changes may take a little longer to be enacted. Nevertheless, that should have a positive effect by increasing own funds, and hence, the surplus will improve the solvency ratio. It should also increase resources for acquisitions. Even better, it is a regulatory change with no cost implications. All this is, as yet, unquantifiable and we do not take account of it in our forecasts.

Acquisitions

As we discussed above, we can't say when we will see any further announcements on acquisitions, although management continues to talk positively about prospects. We note that completion typically takes several months. An announcement now would not affect the 2023 results and, realistically, the 2024 results may only see a partial benefit.

Forecasts

We had already forecast a more benign operating environment, albeit the mix in 1H'23 was slightly different from our forecast. However, we hadn't properly allowed for rising risk-free rates in the expected movement, so we have upgraded those figures. We have also upgraded our new business estimates in light of the improved first half. While the economic earnings came in at 73% of our full-year forecast, market movements since then have given us pause and we have left the full-year estimates unadjusted.

Our forecasts are on a normalised basis. The positive first-half results, most notably the adjustment to the expected movement, has led to significant upgrades to our forecasts. Our 2023E EPS has increased by 19% to 56.9p and our 2024E has increased 25% to 38.6p.

We have kept our dividend forecast unchanged, with 3% growth in 2023 and 2024. We note that Chesnara management are aware that many investors hold the shares primarily for income and recent inflation has been higher than the dividend growth rate. Should inflation stay higher for longer, we may see a temporary increase in the growth rate. We note that doubling it to 6% for one year would initially cost £1m. Given the benefits of recent acquisitions, this is affordable, albeit it would come out of the resources for future growth.

Economic Value earnings

Year-end Dec (£m)	2019	2020	2021	2022	2023E	2024E
Expected movement	-0.4	0.3	-1.7	-1.3	11.6	11.6
New business	7.8	3.7	2.4	8.0	9.4	10.3
Operating experience variances	-6.8	-22.0	-19.2	-20.7	1.6	-8.2
Operating assumption changes	3.8	-35.8	-13.9	-14.5	-8.1	0.3
Other operating variances	-0.3	3.9	-0.2	1.7	-0.3	-0.3
Total u/l operating earnings	4.1	-49.9	-32.6	-26.8	14.1	13.7
Material other operating items	1.5	-16.2	-26.2	0.0	0.0	0.0
Total operating earnings	5.6	-66.1	-58.8	-26.8	14.1	13.7
Economic experience variances	143.1	45.7	79.5	0.0	41.1	42.3
Economic assumption changes	-22.0	-22.8	30.1	0.0	2.3	2.3
Total economic earnings	121.1	22.9	109.6	-109.1	43.4	44.7
Other non-operating variances	-5.2	-2.8	4.5	-2.6	3.6	3.7
Risk margin movement	-7.0	4.7	10.8	20.4	2.4	2.4
Tax	-10.5	3.7	-8.2	12.0	-6.3	-6.5
Gain on acquisition	0.0	0.0	0.0	21.0	28.4	0.0
Economic Value earnings	**104.0**	**-37.6**	**57.8**	**-106.1**	**85.5**	**58.1**
EPS (p)	69.3	-25.1	38.5	-70.6	56.9	38.6
DPS (p)	21.30	21.94	22.60	23.28	23.98	24.70

Source: Hardman & Co Research

While the normalised basis is our core expectation, in practice, results will rarely match the average. To give some idea of sensitivity, the following table gives estimates with two adjustments:

- annual equity returns of 3.5% instead of 7%; and
- no returns from credit spreads, i.e. credit losses match the gain from the spread.

Investors can easily imply the effect of different assumptions from these.

Sensitivity to economic assumptions

£m	2021	2022E	2023E	2024E
Normalised Economic Value earnings	57.8	-106.1	85.5	58.1
Half equity returns			60.1	33.1
Reduction			-30%	-43%
No credit spreads			65.0	38.2
Reduction			-24%	-34%

Source: Hardman & Co Research

Although there has been much movement in different lines, our forecast for the 2023 year-end Economic Value is unchanged at £542.1m. Our 2024E is increased by 2% to £563.8m. In per share figures, these are 360p and 375p respectively.

For cashflow, we had downgraded our 2023 estimates for the European operations in the light of the weak first half but upgraded our group figures. Although this reduces our dividend cover a little, it still remains comfortable.

Key balance sheet and cash generation

Year-end Dec (£m)	2019	2020	2021	2022	2023E	2024E
Borrowings	88.2	67.0	47.2	212.0	209.3	209.3
Economic Value	670.0	636.8	624.2	511.7	542.1	563.8
Economic Value/share (p)	446.0	424.0	416.0	340.0	360	375
Base cash generation						
UK	33.6	29.5	27.4	40.8	24.7	27.1
Movestic	-6.2	12.4	-14.4	16.1	0.1	13.7
Waard	0.8	4.1	2.9	8.4	3.6	8.8
Scildon	22.6	-22.3	15.2	-3.4	1.8	5.6
Group	-14.0	4.1	-10.8	20.8	3.7	-10.6
Total	36.8	27.8	20.3	82.7	33.9	44.6
Dividends paid	-31.3	-32.3	-33.3	-34.3	-35.4	-36.4
Dividend cash cover (x)	1.2	0.9	0.6	2.4	1.0x	1.2x

Source: Hardman & Co Research

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The full detail is on page 26 of the full directive, which can be accessed here: https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2031-EN-F1-1.PDF

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