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Ratings

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Baloise Group

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Baloise Group

SACP* Assessments				SACP*		Support		Ratings
Anchor	a+	+ Modifiers	0	= a+		+ 0		= Financial Strength Rating
Business Risk		ERM and Management	0	Liquidity	0	Group Support	0	A+/Stable/--
Strong								
Financial Risk		Holistic Analysis	0	Sovereign Risk	0	Gov't Support	0	Holding Company Rating
Extremely Strong								A-/Stable/--

*Stand-alone credit profile.
See Ratings Detail for a complete list of rated entities and ratings covered by this report.

Strengths:

- Baloise is a Switzerland-domiciled multiline insurer with a sizable market share in almost all markets it operates, except in Germany where its competitive strength is less prominent.
- Sustainable and extremely strong capital adequacy and high solvency ratios under the Swiss solvency regime.
- Strong and stable technical performance, especially in its domestic market.
- High quality investment portfolio with 71% of bonds rated 'AA' or higher.

Weaknesses:

- Relatively high earnings volatility in the German property and casualty (P&C) business.
- Pressure on life earnings due to still very low interest rates, although margins have stabilized compared with last year.
- Some product risk from traditional life business with guarantees.

Rationale

S&P Global Ratings' issuer credit and insurer financial strength ratings on Baloise Group's core and highly strategic operating subsidiaries (together Baloise or the group), reflect our view on the group's sizable market share and very profitable technical results in nearly all markets it operates, with the exception of Germany. Furthermore, the group has extremely robust capitalization under the S&P Global Ratings risk-based capital model and the Swiss regulatory solvency ratio (SST).

Baloise is a multiline insurer focusing on private, small, and midsize enterprises. Based on half-year 2018 figures, about

54% of its business is generated in Switzerland, complemented by about 15% in Germany, 17% in Belgium, and 14% in Luxembourg. The group's parent company Baloise Holding AG, is listed on the Swiss stock exchange with a widely distributed 100% free float.

Outlook: Stable

The stable outlook reflects our expectation that Baloise will maintain its capital adequacy comfortably at 'AAA' level, according to our capital model. Sound earnings of at least Swiss franc (CHF) 500 million per year in 2018-2020, an unchanged dividend policy, and a continued conservative investment and growth strategy, support this.

Downside scenario

We could lower the ratings over the next 24 months if the group's capital weakened because of significantly lower-than-expected retained earnings, or a shift towards a more aggressive risk appetite in terms of acquisition, growth, or product offering.

Upside scenario

We see limited rating upside in the next 24 months. We could take a positive rating action if Baloise's business risk profile improved substantially through higher earnings contributions from countries other than Switzerland, or from non-insurance business. This also assumes the group will maintain its current capitalization, risk position, and earnings stability.

Base-Case Scenario

Macroeconomic Assumptions

- Moderate economic growth and inflation and continued low unemployment rates in Switzerland over 2018-2020.
- Rising trend in 10-year Swiss government bond yields at 0.1% in 2018, increasing to 0.3% in 2019 and 0.7% in 2020.
- No major financial market dislocations.

Key Metrics

Baloise Group						
(mil. CHF)	**2019f**	**2018f**	**2017**	**2016**	**2015**	**2014**
Gross premiums written	> 6.700	> 6.700	6,741.3	6,711.6	6,833.4	7,175.6
Net premiums written	> 6.500	> 6.500	6,556.2	6,543.2	6,683.2	7,010.4
Net income	> 500	> 500	531.9	533.9	511.1	711.9
Return on shareholders equity (%)	> 8,0	> 8,0	8.7	9.5	9.1	13.3
P/C Net combined ratio (%)	93 - 95	93 - 95	92.1	93.2	93.1	94.0
Net investment yield (%)	1,8 - 2,0	1,8 - 2,0	2.0	2.2	2.3	2.6
S&P Global Ratings' capital adequacy	Extremely Strong	Extremely Strong	Extremely Strong	Extremely Strong	Extremely Strong	Extremely Strong
Fixed-charge coverage (x)	~20	~20	22.4	19.7	19.7	24.5
Financial leverage (%)	~20	~20	21.7	17.6	21.4	20.1

CHF--Swiss franc. f--forecast.

Business Risk Profile: Strong

Baloise is a multiline insurance group, focusing on its target markets in Switzerland, Belgium, Luxembourg, and Germany, where is has mainly a strong presence. The group is, however, somewhat less prominent in Germany. Baloise has exposure in life insurance, which accounts for 59% of group gross premiums written and 54% of operating profits based on half-year 2018 figures. P&C contributes about 41% of premiums and 40% of earnings. Other business segments include asset management, and banking, which provide a reliable income of about 12% of pre-tax earnings before consolidation.

Baloise benefits from wealthy and diversified economies in the countries it operates, with strong and predictable institutions. Demand remains robust on the back of relatively low unemployment rates. However, the group is facing the challenge of low interest rates, especially in Switzerland and Germany. To counter this, Baloise is focusing on biometric and less interest-rate sensitive life products. In the Swiss group life business, where the group is a leading player, Baloise continues to shift its business mix towards partially autonomous solutions and risk insurance. As a consequence of a more cautious and focused underwriting approach, we observed an 8.7% premium decline in life business in the first-half of 2018, and we expect premiums will continue on that trend until year-end 2018. We expect stable life premiums at best over the following two years, reflecting stringent underwriting in the current very low interest rate environment.

In P&C, Baloise is offering a wide range of products with motor (33.7% of premiums at half-year 2018), property (29.6%) and accident (12.5%) the main lines of business. Gross premiums increased in the first six months by 5.2%, mainly thanks to property operations. We expect P&C premiums will increase annually by about 2%-4% without compromising the group's profitability. Overall, we expect that P&C growth will partly offset the premium decline in life, with annual gross premium growth of about 1%-4% expected in 2018-2020.

The group has a sound business diversity by premiums across its target markets. However, we believe the group's main strengths stem from its domestic insurance business. While the contribution of the international business to overall earnings is increasing, it remains limited compared with higher-rated insurers.

In addition to insurance operations, Baloise receives increasing operating earnings contributions from banking and asset management. The group's subsidiary, Baloise Bank SoBa, supports the overall earnings with CHF82 million in 2017, or 11%, complementing the product range mainly with mortgage products. In 2017, Baloise reported a mortgage portfolio of CHF6.2 billion, and loan and clients assets from insurance solutions of CHF3 billion.

In the first half of 2018, Baloise's performance was in line with our key assumptions. The group reported a net profit of CHF270 million, a group combined ratio of 94.1%, and its interest rate margin increased further to 129 basis points (bps). We believe Baloise will achieve at least CHF500 million for the full year result.

Financial Risk Profile: Extremely Strong

Based on the analysis of our risk-based capital model, we assess Baloise's capital adequacy firmly in the 'AAA' range, which we expect it will maintain over 2018-2020. Our assessment is supported by the group's reported SST ratio of 262% at year-end 2017, well above that of most peers.

The group's capital position also benefits from strong earnings, which we estimate will be at least CHF500 million over 2018–2020. This should lead to a return on equity of about 8%-10%, supported by a sound and stable P&C technical profitability, with a combined ratio of 93%-95% over the same period. In life insurance, various actions by management have helped preserve the profitability, with a stable interest margin (investment performance above guaranteed obligations) over the last few years (2017: 113bps, 2016: 117bps and 2015: 108bps) in a still very low interest rate environment. We believe the group will be able to maintain this profitability at similar levels over 2018-2020. We also assume that net investment yield will decline to about 1.8%-2.0% over the forecast period, reflecting the current interest rate environment. In the first half of 2018, Baloise's performance was in line with our key assumptions.

We believe that the group has limited exposure to capital and earnings volatility. Baloise's solvency capital appears to be resilient, based on company defined stress scenarios. If in a stress scenario interest rates reduced by 100 bps, and the stock market fell 50% at the same time, solvency ratios would remain above 140%, based on January 2018 assumptions. The group's stringent focus on its inforce business has significantly reduced its sensitivity to interest rates movements, for example in its life portfolio, with guarantees below 1% in 2017. The group has an overall conservative investment strategy with a high amount of 'AAA' rated sovereign debt. Nevertheless, we see relatively high exposure to employee benefits obligation risk, in line with other Switzerland-based insurance companies.

Baloise has demonstrated access to different sources of capital, and we expect it will continue to be able to access different sources of capital via hybrid securities, reinsurance coverage, or shares if necessary. At year-end 2017, financial leverage was at 22%, which is higher than in 2016, based on the issuance of two hybrid instruments in 2017 totaling CHF500 million. We assume leverage will decline to about 20% in 2018-2020 following a potential repayment of CHF175 million of senior debt in 2019, and CHF300 million in 2020. We also assume that this repayment will affect fixed-charge coverage, expected at about 20x over the forecast period.

Other Assessments

The group has, in our view, a stringent strategic risk management, risk-management culture, and risk controls for its major risks. Therefore, we think it is unlikely that the group will experience losses exceeding its risk tolerance.

Our assessment of Baloise's management and governance practices are based on our generally positive opinion of its strategic positioning, financial management, and organizational effectiveness. Management demonstrated a smooth transitioning of the CFO in 2017, as well as of the CEO in the previous year, and has adhered to a consistent overall strategy in 2018.

In our view, Baloise's enterprise risk management and management and governance practices reduce downside risks.

Baloise's has, in our opinion, ample access to liquidity sources and a liquid asset portfolio. The group has strong cash flow generation from premium income and investment returns. Moreover, there are no refinancing concerns, in our view.

Ratings Score Snapshot

Baloise Group Ratings Score Snapshot	
Financial Strength Rating	**A+/Stable**
Anchor	a+
Business risk profile	Strong
IICRA	Low Risk
Competitive position	Strong
Financial risk profile	Extremely Strong
Capital and earnings	Extremely Strong
Risk position	Intermediate
Financial flexibility	Adequate
Modifiers	
ERM und management	0
Enterprise risk management	Strong
Managment and governance	Satisfactory
Holistic analysis	0
Liquidity	Exceptional
Support	0
Group support	0
Government support	0
Holding company rating	A-/Stable/--

IICRA--Insurance Industry and Country Risk Assessment.

Related Criteria

- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- Criteria - Insurance - General: Methodology For The Classification And Treatment Of Insurance Companies' Operational Leverage, Oct. 31, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Insurance - General: Enterprise Risk Management, May 7, 2013
- Criteria - Insurance - General: Insurers: Rating Methodology, May 7, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Criteria Clarification On Hybrid Capital Step-Ups, Call Options, And Replacement Provisions, Oct. 22, 2012
- Criteria - Insurance - General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- Criteria - Financial Institutions - General: Methodology: Hybrid Capital Issue Features: Update On Dividend Stoppers, Look-Backs, And Pushers, Feb. 10, 2010
- Criteria - Financial Institutions - Banks: Assumptions: Clarification Of The Equity Content Categories Used For Bank And Insurance Hybrid Instruments With Restricted Ability To Defer Payments, Feb. 9, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Insurance - General: Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

Related Research

- Swiss Insurer Baloise Upgraded To 'A+' On Strengthening Capital Position; Outlook Stable, June 27, 2018

Ratings Detail (As Of February 1, 2019)	
Holding Company: Baloise Holding AG	
Issuer Credit Rating	
Local Currency	A-/Stable/--
Operating Companies Covered By This Report	
Basler Versicherung AG	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Baloise Belgium N.V.	
Financial Strength Rating	
Local Currency	A+/Stable/--

Ratings Detail (As Of February 1, 2019) (cont.)	
Issuer Credit Rating	
Local Currency	A+/Stable/--
Basler Leben AG	
Issuer Credit Rating	
Local Currency	A+/Stable/--
Basler Sachversicherungs AG	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
Domicile	Switzerland

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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