S&P Global Ratings

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Baloise Group

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Baloise Group

Anchor	a+
Business Risk	Strong
Competitive position	Strong
IICRA	Low
Financial Risk	Excellent
Capital and earnings	Excellent
Risk exposure	Moderately low
Funding structure	Neutral

+

Modifiers	0
Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0

=

SACP	a+

+

Support	0
Group support	0
Government support	0

=

A+/Stable/--	Financial strength rating
A-/Stable/--	Holding company ICR

IICRA--Insurance Industry And Country Risk Assessment.
SACP--Stand-alone credit profile.

Credit Highlights

Overview

Strengths	Risks
Well diversified multiline insurer with top market positions in almost all markets in which it operates.	Low interest rate environment weighs on the group's traditional life backbook with guarantees.
Sustainable and extremely strong capital adequacy, with high solvency ratios under the Swiss Solvency Regime.	Relatively high earnings volatility in the German property and casualty (P/C) business, although this is starting to stabilize.
Strong and stable technical performance, especially in its domestic market.	

S&P Global Ratings expects Baloise Group will retain its top market positions in the group's defined core markets. Switzerland-domiciled Baloise will maintain its top-five position in its domestic market, supported by its strong franchise. Also, we believe it will continue to retain strong market positions in other core markets defined by the group, such as Belgium and Luxembourg. This is also demonstrated by the group's recent acquisition of Belgian insurer Fidea NV in 2019, which further strengthened Baloise's position in Belgium. However, the group's earnings are less diverse compared with higher rated peers, dominated by its domestic market.

The group will maintain its underwriting profitability and stable income from the banking and asset management business. With a cautious and focused underwriting approach, we expect Baloise will continue to generate strong earnings from their nonlife business, with a combined ratio of 93%-95% over 2019-2021. In life insurance, the group faces challenges from the low- interest-rate environment, and to counter this Baloise is focusing on biometric and less-capital-intensive products. In addition to its insurance business, we expect Baloise's banking and asset management business will provide reliable income of over 12% of EBIT before consolidation.

Our ratings are underpinned by excellent capitalization, which we expect will remain in the 'AAA' range based on our risk-based capital model over the forecast period. Baloise also disclosed a very comfortable regulatory solvency ratio of 242% as of year-end 2018 in the Swiss Solvency Test (SST). Robust earnings stemming from their underwriting performance, and cautious dividends and investment policies will continue to support their capital adequacy.

Outlook

The outlook is stable because we expect that, over the next two years, Baloise will maintain capital adequacy comfortably at the 'AAA' level, according to our capital model. Sound earnings of at least Swiss franc (CHF) 500 million (about €458 million) per year in 2019–2021, an unchanged dividend policy, and a continued conservative investment and growth strategy support our view.

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 more aggressive risk appetite in terms of acquisitions, growths, and products.

Upside scenario

We see limited rating upside in the next 24 months. However, we could take a positive rating action if Baloise's competitiveness improved substantially through higher earnings contributions from countries other than Switzerland, or from non-insurance business. This is contingent on the group maintaining its current capitalization, risk profile, and earnings stability.

Key Assumptions

- Real GDP growth of 1.1%-1.4% over 2019-2021.
- Inflation remaining about 0.5%, coupled with continuously low unemployment rates of about 2.3% in Switzerland over 2019-2021.
- Negative 10-year average bond yields of -0.5% in 2019 and -0.6% in 2020, only gradually increasing to -0.2% in 2022 in Switzerland.

Key Metrics

(mil. CHF)	2020f	2019f	2018	2017	2016
Gross premiums written	>6800	>6800	6,766	6,741	6,712
Net income	>500	>500	523	532	534
Return on shareholders' equity	>8	>8	8.4	8.7	9.5
P/C net combined ratio (%)	93-95	93-95	91.9	92.1	93.2
Net investment yield (%)	1.8-2.0	1.8-2.0	2	2	2.2
S&P Global Ratings' capital adequacy (indicate rating level of redundancy)	Extremely strong	Extremely strong	Extremely strong	Extremely strong	Extremely strong
Fixed charge coverage	~20	~20	20.2	22.4	19.7

Key Metrics (cont.)					
(mil. CHF)	**2020f**	**2019f**	**2018**	**2017**	**2016**
Financial leverage (%)*	<30	<30	22.5	21.4	20.3

*Calculation changed as per 2018 following the criteria update of the insurance rating methodology as per July 1, 2019. f--S&P Global Ratings forecast. CHF—Swiss franc.

Business Risk Profile: Strong

Baloise group is a multiline insurer based in Switzerland, focusing on private businesses and small and midsize enterprises in wealthy economies. The group benefits mainly from its sound franchise and well-recognized brand in Switzerland (61% of gross written premiums [GWP]). In addition, the group has a solid foothold in other group defined core markets of Belgium (15% of GWP) and Luxembourg (10% of GWP) where it holds top market positions, and a less-prominent foothold in Germany (13% of GWP). We believe the group defines its competitive strength through its efficient customer and segment selection, with a clear focus on value creation.

In our opinion, the group has sound product and earnings diversity, offering various life (42% of operating profits in 2018) and P/C (46%) insurance products in its target markets. Additionally, Baloise Bank SoBa complements the product range mainly with mortgage products and wealth management solutions (12%).

The group's P/C earnings are fundamentally strong, driven by underwriting profitability, with five-year combined ratio of 93%. The trend continued in first-half 2019, with an improved underwriting performance of about 87.4% due to lower claims in the first half of the year, especially in Switzerland and Germany.

However, we believe that life earnings are under pressure from the challenges of low interest rates, especially in the domestic market. Baloise's continuous shift to biometric and less interest-rate sensitive life products (notably partially autonomous solutions in the Swiss group life business) will gradually mitigate the pressure, in our opinion. However, we believe Baloise benefits from earnings diversification in their banking and asset management business, which contributed about 12% to overall earnings before consolidation in 2018. We anticipate further increase in operating earnings from banking and asset management to the overall group earnings in the medium term, but that it will stay below 15% over the forecast period.

In first-half 2019, Baloise's profitability was in line with our expectations. However, the group reported a strong increase in net profit to CHF395 million, benefitting from a one-off tax effect in line with its domestic peers.

Financial Risk Profile: Excellent

We assess Baloise's capital adequacy firmly in the 'AAA' range based on the analysis of our risk-based capital model, which remains a key strength for Baloise over the forecast period. This is also supported by the group's reported SST ratio of 242% at year-end 2018, well above that of most peers.

The group's strong earnings fueled by sound and stable P/C technical profitability supports its overall capital position. The life insurance segment has also managed to maintain stable interest margins (investment performance above guaranteed obligations) over the last few years (2018: 130 basis points [bps], 2017: 114bps, 2016: 117bps, and 2015: 108bps) in a persistently very low interest rate environment. We expect Baloise will continue to deliver earnings of at least CHF500 million over 2019-2021, which combined with a dividend payout ratio of below 60% supports our view of 'AAA' range capital adequacy in the medium term and should lead to a return on equity of about 8%-10%, in line with the group's targets.

We believe the group has limited exposure to capital and earnings volatility. Baloise's solvency capital appears resilient based on company-defined stress scenarios. The group generally follows a risk-conscious investment strategy, with high asset quality with 'AAA' rated sovereign debt, and sound investment-risk control practices. Additionally, we have a favorable view on the group's stringent strategic risk management, risk-management culture, and risk controls, which we consider help Baloise reduce its major risks.

Baloise's leverage and coverage are within our acceptable thresholds and we do not foresee any material deviations. At year- end 2018, financial leverage was at 22% and we assume it will remain below 30% over the forecast period. Similarly we assume the fixed- charge coverage will stabilize at 20x over the forecast period, as it was in 2018.

Other Key Credit Considerations

Governance

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.

Liquidity

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.

Group support

We consider Basler Versicherung AG, Basler Leben AG, and Baloise Belgium NV as core operating entities to the group. We consider Basler Sachversicherungs-AG as highly strategic to the group.

Other considerations

The two-notch differential between the rating on Baloise Holding and those on the core operating companies reflects the structural subordination of the holding company's creditors to the group's policyholders. Baloise Holding has no operating characteristics in its own right.

Baloise Holding's liquidity profile is good, in our view. As a pure insurance holding company, it largely derives its liquidity from subsidiaries' dividends or profit transfers, which to date have been more than sufficient to meet interest payments. However, other sources of liquidity are very limited, in our opinion. The long-term nature of the holding company's debt maturity profile suggests that the group will not need additional liquidity to finance organic growth, at least over the next 12-18 months.

Accounting considerations

Baloise prepares its consolidated financial statements under International Financial Reporting Standards (IFRS). We view the group's financial communication and disclosure as sound and transparent.

Our assessment of Baloise's capital adequacy is based on reported IFRS shareholders' equity, which we have adjusted by:

- Crediting 50% of the life insurance value in force, but eliminating double counting by adjusting the on-balance-sheet values for the shareholders' portion in deferred policy acquisition cost;
- Including the statutory free and unallocated portion of the policyholder bonus reserve in life insurance; and
- Deducting goodwill and other intangible assets.

In adjusting risk-capital requirements, we have recognized hedging measures for equity exposures.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

Business risk profile	**Financial risk profile**							
	Excellent	Very Strong	Strong	Satisfactory	Fair	Marginal	Weak	Vulnerable
Excellent	aa+	aa	aa-	a+	a-	bbb	bb+	b+
Very Strong	aa	aa/aa-	aa-/a+	a+/a	a-/bbb+	bbb/bbb-	bb+/bb	b+
Strong	**aa-/a+**	a+/a	a/a-	a-/bbb+	bbb+/bbb	bbb-/bb+	bb/bb-	b+/b
Satisfactory	a	a/a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bb+/bb	bb-/b+	b/b-
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb/bb-	b+/b	b-
Weak	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b/b-	b-
Vulnerable	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b+/b	b/b-	b-	b-

Note: Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

Ratings Detail (As Of November 11, 2019)*

Holding Company: Baloise Holding AG

Ratings Detail (As Of November 11, 2019)*(cont.)	
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/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Basler Leben AG	
Issuer Credit Rating	
Local Currency	A+/Stable/--
Junior Subordinated*	
**Guarantor: Baloise Holding AG.*	A-
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.