

Baloise Holding AG

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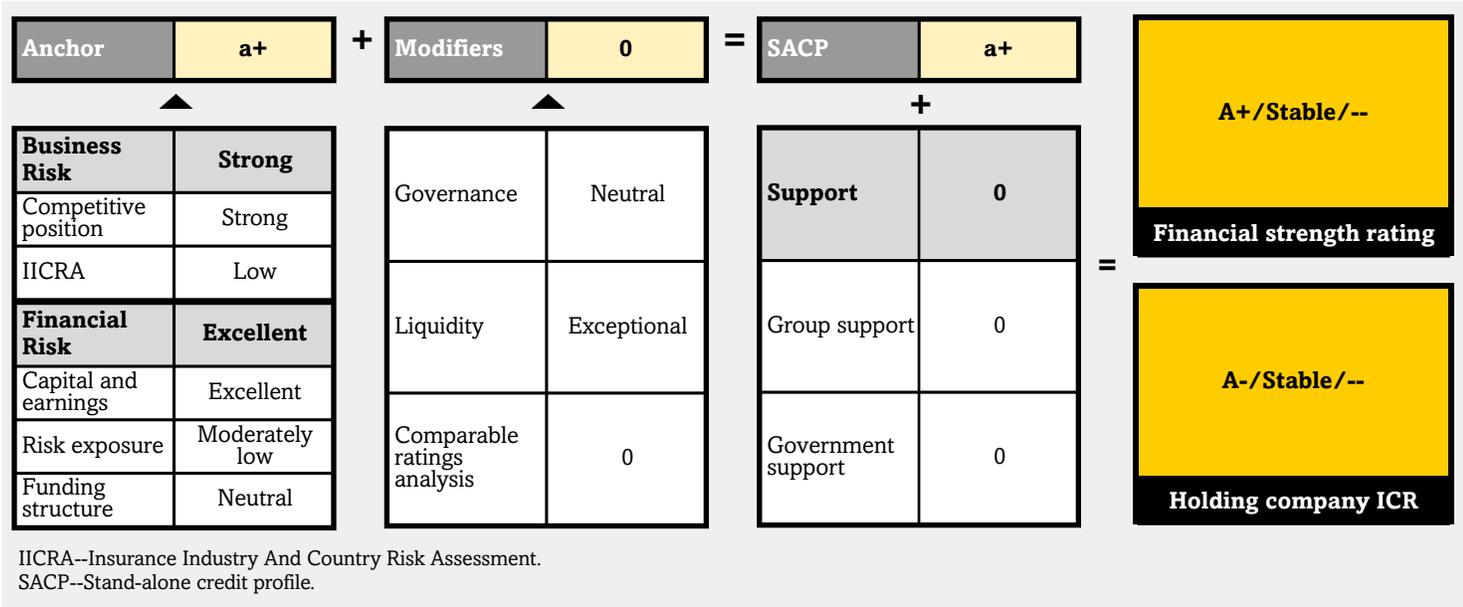
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Baloise Holding AG



Credit Highlights

Overview

Key strengths

Top market positions coupled with strong and stable technical performance in most markets of operations, with diversified business.

Sustainable and extremely strong capital adequacy, with high solvency ratios under the Swiss Solvency Regime.

Key risks

Low interest rates weighing on the group's traditional life back book with guarantees.

Baloise Holding AG will retain its top market positions in the group's defined core markets, in S&P Global Ratings' opinion. Switzerland-domiciled Baloise will maintain its top 5 position in its domestic market, supported by its strong franchise. Also, we believe it will retain a strong market position in Belgium, where the group strengthened its position through a recent acquisition. However, its earnings, dominated by its domestic market, are less diverse compared with those of higher-rated peers.

The group will maintain its strong underwriting profitability and stable income from the banking and asset management businesses. With a cautious and focused underwriting approach, we expect Baloise will continue generating strong earnings from its property and casualty (P/C) business, with a combined ratio of 90%-95% over 2021-2023. Although business volume and net income contracted in 2020, they remained in line with our expectations and we expect they will likely increase amid our overall forecast of an improved economy in 2021 and 2022. We expect net income of more than Swiss franc (CHF) 500 million annually during this period, which is in line with the average net income over the past five years.

Our ratings are underpinned by Baloise's excellent capitalization, which we expect will remain in the 'AAA' range based on our risk-based capital model over the forecast period. The company also disclosed a very comfortable regulatory solvency ratio of 186% as of year-end 2020 in the Swiss Solvency Test (SST) despite COVID-19's implications on capital markets. We expect that capital will remain solidly above the 'AAA' benchmark over 2021–2023 despite the pandemic. Robust earnings stemming from underwriting performance, and cautious investment policies, will continue

supporting capital adequacy.

Outlook: Stable

The stable outlook reflects our expectation that Baloise will maintain its capital adequacy comfortably at the 'AAA' level, according to our capital model. Sound earnings, which will recover to at least CHF500 million per year in 2021-2023, an unchanged dividend policy, and a consistent 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 weakens over a prolonged period because of significantly lower-than-expected retained earnings or a shift toward a more aggressive risk appetite in terms of acquisitions, growth, and product offering.

Upside scenario

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

Key Assumptions

- Real GDP growth recovery to 3.6% in 2021, then bouncing back to around 3.0% in 2022 and 1.8% in 2023.
- Inflation rising by 0.3%, coupled with increased unemployment rates of about 5.2% in Switzerland for 2021.
- Negative 10-year average bond yields of 0.30% in 2021 and 0.16% in 2022, only gradually increasing to negative 0.11% in 2023 in Switzerland.

Baloise Holding AG--Key Metrics

(Mil. CHF)	2022f	2021f	2020	2019	2018	2017
Gross premiums written	>7,000	>7,000	7,093.8	7,602.4	6,766.2	6,741.3
Net income	>500	>500	428.3	689.5	522.9	531.9
Return on shareholders equity	>8	>8	6.3	10.8	8.4	8.7
P/C net combined ratio (%)	<95	<95	91.8	90.4	91.9	92.1
Net investment yield (%)	1-2	1-2	1.5	1.7	2.0	2.0
S&P capital adequacy (indicate rating level of redundancy)	Excellent	Excellent	Excellent	Excellent	Extremely strong	Extremely strong
Fixed charge coverage	>15	>15	20.4	21.6	20.2	22.4
Financial leverage (%)*	<30	<30	25.3	26.1	22.5	21.4

*Calculation changed as per 2018 following the criteria update of the insurance rating methodology as per July 1, 2019. CHF--Swiss franc.
f--Forecast.

Business Risk Profile: Strong

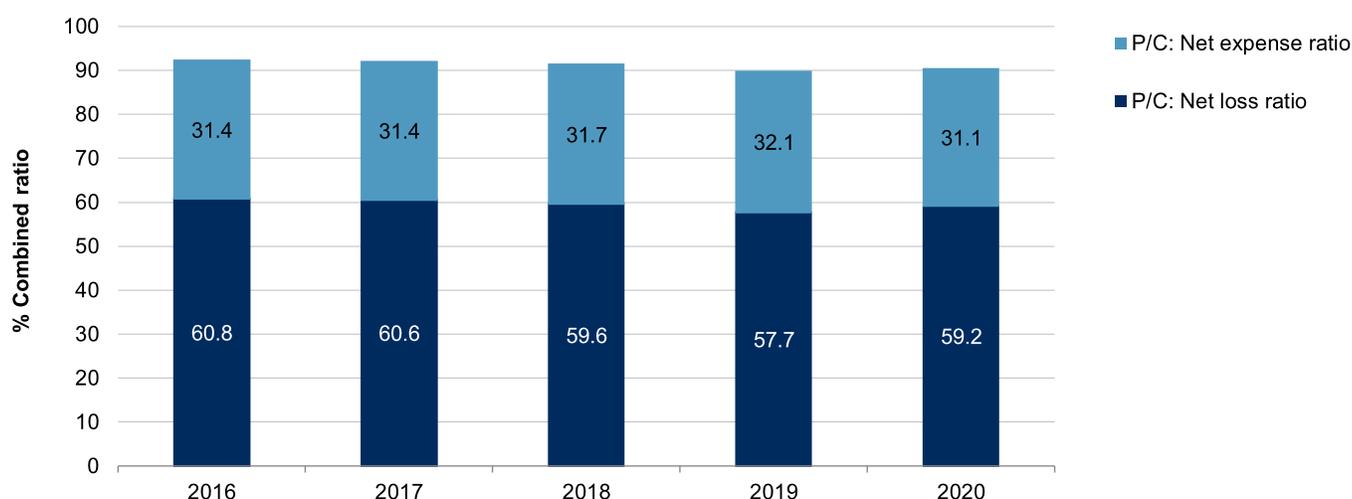
Baloise group is a multiline insurer based in Switzerland, focusing on private businesses and small and midsize enterprises in wealthy economies. The group benefits mainly from its sound franchise and well-recognized brand in Switzerland (46% of total business volume in 2020). In addition, the group has a solid foothold in other group-defined core markets of Belgium (25% of total business volume) and Luxembourg (14% of total business volume) where it holds top market positions, and a less-prominent foothold in Germany (15% of total business volume). 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 (46% of operating profits in 2020) and P/C (43%) insurance products in its target markets. Also, 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 a five-year combined ratio of 91%. In our view, the group's combined ratio (loss and expense) has remained relatively strong compared with peers'. The impact of COVID-19 claims on underwriting in 2020, with a combined ratio of 91.2%, was only 2% and partly offset by better claims performance in the motor business.

Chart 1

Underwriting Performance



Source: S&P Global Ratings.

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The now-core Germany-based entity Basler Sachversicherung AG has previously seen some hit to earnings from reserve strengthening, but followed consistent performance improvements in the past three years. After changes in the

business mix, restructuring, and exiting loss-making hospitality insurance, the German subsidiary's combined ratio has improved since 2018 to less than 100%. Despite the pandemic and some exposure to the affected business lines, such as business interruption, the German subsidiary continued to report positive underwriting income with a combined ratio of 94.9% in 2020 (after 90.9% in 2019). We expect the combined ratio will stay in line with the group's target of 90%-95% for 2021-2023 and now see the entity as highly integrated and a more stable earnings provider, with Germany a core market in Baloise's group strategy.

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 (such as semiautonomous solutions in the Swiss group life business) will gradually mitigate the pressure, in our opinion. We believe the group benefits from earnings diversification in its banking and asset management business, which contributed about 15% of EBIT in 2020. We also think Baloise's foray into noninsurance business will support earnings diversification, but we don't expect a meaningful contribution in the medium term.

Financial Risk Profile: Excellent

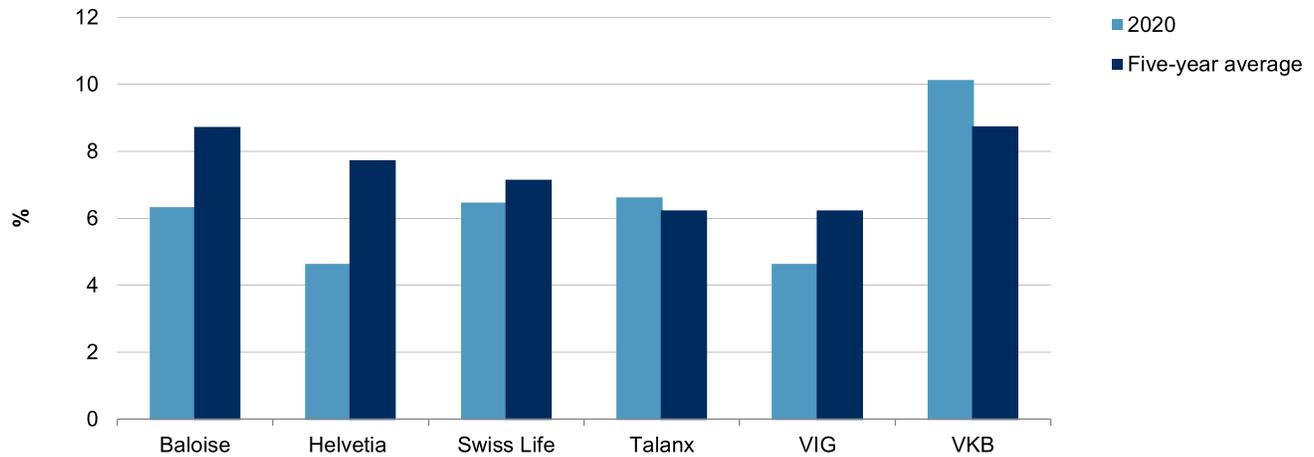
We assess Baloise's capital adequacy firmly in the 'AAA' range based on the analysis of our risk-based capital model, which remains a key strength for the group over the forecast period. This is also supported by the group's reported SST ratio of 186% at year-end 2020, which compares well with peers'.

The group's strong earnings, fueled by sound and stable P/C technical profitability, support its overall capital position. The life insurance segment has also maintained stable interest margins (investment performance above guaranteed obligations) over the past few years (2020: 102 basis points [bps]; 2019: 109 bps; 2018: 130 bps; and 2017: 114 bps) in a persistently very low interest rate environment.

Although business volume and net income contracted in 2020, they remained in line with our expectations and we expect they will likely increase amid our overall forecast of an improved macroeconomic environment in 2021 and 2022. We expect net income of more than Swiss franc (CHF) 500 million annually during this period, which is in line with the average net income over the past five years. We further expect a 'AAA' range capital adequacy in the medium term and a return on equity of greater than 8% after 2021, when economic markets somewhat recover from the pandemic.

Chart 2

Return On Equity In Line With Peers'



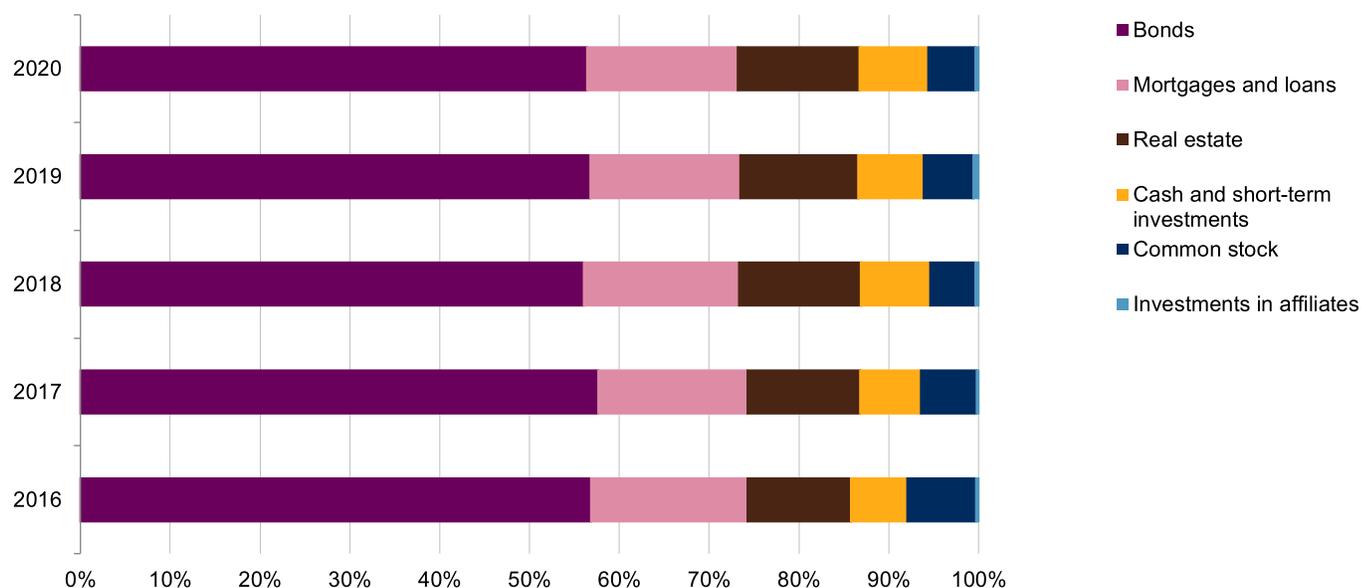
Source: S&P Global Ratings.

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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 namely 'AAA' rated sovereign debt, and sound investment-risk control practices. Also, we have a favorable view of the group's stringent strategic risk management, risk-management culture, and risk controls, which we believe help Baloise reduce its major risks.

Chart 3

Investment Portfolio



Source: S&P Global Ratings.

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Baloise's leverage and coverage are within our accepted thresholds and we do not foresee any material deviations. At year-end 2020, financial leverage was at 25.3% 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 2020.

Other Key Credit Considerations

Governance

Our assessment of Baloise's management and governance practices are based on our generally positive opinion of the group's strategic positioning, financial management, and organizational effectiveness.

Liquidity

Baloise 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 risks, in our view.

Factors specific to the holding company

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.

Government/other support/group support

We consider Basler Versicherung AG, Basler Leben AG (both Switzerland), Baloise Belgium N.V., and Basler Sachversicherungs AG (Germany) core operating entities of the group. We revised the group status for Basler Sachversicherung AG to core based on improving and sustainable profitability.

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

- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Appendix

Baloise Holding AG--Credit Metrics History				
Ratio/Metric (Mil. CHF)	2020	2019	2018	2017
S&P Global Ratings capital adequacy*	Excellent	Excellent	Excellent	Excellent
Total invested assets	83,648.4	82,520.5	76,714.3	79,248.6
Total shareholder equity	6,985.8	6,715.6	6,008.2	6,409.2

Baloise Holding AG--Credit Metrics History (cont.)

Ratio/Metric (Mil. CHF)	2020	2019	2018	2017
Gross premiums written	7,093.8	7,602.4	6,766.2	6,741.3
Net premiums written	6,830.9	7,363.0	6,555.8	6,556.2
Net premiums earned	6,766.8	7,329.8	6,528.0	6,542.9
Reinsurance utilization (%)	3.7	3.1	3.1	2.7
EBIT	602.9	723.9	737.5	684.1
Net income (attributable to all shareholders)	428.3	689.5	522.9	531.9
Return on revenue (%)	7.3	8.2	9.0	8.3
Return on assets (excluding investment gains/losses) (%)	0.4	0.5	0.8	0.3
Return on shareholders' equity (reported) (%)	6.3	10.8	8.4	8.7
P/C: net combined ratio (%)	91.8	90.4	91.9	92.1
P/C: net expense ratio (%)	31.1	32.1	31.7	31.4
EBITDA fixed-charge coverage (x)	20.4	21.6	20.2	22.4
EBIT fixed-charge coverage (x)	17.6	19.2	18.5	19.9
EBIT fixed-charge coverage including realized and unrealized gains/losses (x)	17.6	19.2	18.5	19.9
Financial obligations/ EBITDA adjusted	3.4	2.9	2.2	2.3
Financial leverage including pension deficit as debt (%)	25.3	26.1	22.5	21.4
Net investment yield (%)	1.5	1.7	2.0	2.0
Net investment yield including investment gains (losses) (%)	2.0	2.3	2.1	2.7

P/C--Property/casualty. CHF--Swiss franc.

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 June 29, 2021)***Baloise Holding AG**

Issuer Credit Rating

Local Currency

A-/Stable/--

Ratings Detail (As Of June 29, 2021)*(cont.)

Related Entities**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/--

Basler Sachversicherungs AG

Financial Strength Rating

Local Currency

A+/Stable/--

Issuer Credit Rating

Local Currency

A+/Stable/--

Basler Versicherung 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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