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Ratings

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Research Update:

German Insurance Group Gothaer Affirmed At 'A-' On Less Risk Exposure And Steady Earnings Retention; Outlook Stable

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Overview

- In our view, Gothaer has actively reduced credit risk and interest risk exposure over the past years, bringing its risk levels in line with that of its domestic peers.
- We forecast that stable earnings retention and reduced appetite for credit and market risk exposure will support Gothaer's capital adequacy sustainably in our 'A' range over the next two to three years.
- We are therefore affirming our 'A-' long-term ratings on the core entities of the Gothaer insurance group.
- The stable outlook reflects our expectation that Gothaer will continue to prioritize earnings generation over growth, and that the group's capital and earnings will not weaken from the current strong level in 2018–2020.

Rating Action

On Oct. 1, 2018, S&P Global Ratings affirmed its 'A-' issuer credit and financial strength ratings on Gothaer Lebensversicherung AG, Gothaer Allgemeine Versicherung AG, and Gothaer Krankenversicherung AG, the core operating entities of Germany-based Gothaer Insurance Group. The outlook is stable.

Rationale

The affirmation reflects our view that Gothaer has actively decreased its credit risk and interest risk exposure over the past years, aligning its risk levels with that of its peers in the German insurance market. We anticipate that the group will maintain a reduced appetite for credit and market risk exposure, allowing Gothaer's capital adequacy to remain firmly in the 'A' range of our model.

Gothaer's prospective capital adequacy is strong thanks to favorable earnings contribution from the property and casualty (P/C) segment and sound capital buffers. We estimate that Gothaer's capital requirements may increase gradually on the back of modest business growth and a greater focus on capital efficient products. This follows the group's strategic decisions regarding business mix and investment policies. However, the life backbook, in particular, is still affected by traditional products with guarantees that weigh on interest rate risk, similar to most peers in the German market. Various management measures--such as the introduction of new capital light products and an increase in asset duration in order to reduce the asset liability mismatch--have helped to contain risks arising from the prolonged low interest rates. Moreover, the group has gradually improved the average credit quality of its portfolio over the past three years, which has reached the upper 'A' range in 2017 and 2018 year to date, with its fixed income portfolio accounting for about 82% of its total investment portfolio. We believe that, following these sustained measures, the group's interest rate and credit risk exposure is in line with peers in the German market and that the group remains committed to maintain that prudence in its investment policy.

That said, we project that the group's capital requirements will slightly outweigh the available capital, leading us to project that capital adequacy will remain in the 'A' range.

Our view of Gothaer's strong competitiveness continues to reflect its diverse earnings from its P/C, life, and health segments, supported by the group's well-diversified product portfolio and distribution channels. However, the business profile is somewhat narrower than that of higher-rated peers, because of the focus on domestic markets. We continue to note that the prevailing low-yield environment and additional reserving requirements (Zinszusatzreserve; €1.1 billion at year-end 2017) constrain Gothaer's life subsidiary's earnings and its capacity to strengthen policyholder capital funds. Nevertheless, we expect the group to generate net income of about €130 million-€140 million annually over 2018–2020, mainly driven by the group's P/C business.

Outlook

The stable outlook reflects our expectation that the Gothaer group will continue to prioritize earnings generation over growth, and that the group's capital and earnings will not weaken from the current strong level over 2018-2020.

Upside scenario

We could raise the rating over the next two years if Gothaer strengthens its capital adequacy to at least very strong levels, while investment portfolio risks consolidate at current levels.

Downside scenario

We consider a downgrade as a remote possibility. But, we could lower the rating over the next two years if the group underperforms relative to our capital and earnings benchmarks, or if heightened concerns from its investment exposures emerge.

Ratings Score Snapshot

	To	From
Financial Strength Rating	A-/Stable/--	A-/Stable/--
Anchor	a-	a-
Business Risk Profile	Strong	Strong
IICRA	Intermediate	Intermediate
Competitive Position	Strong	Strong
Financial Risk Profile	Strong	Moderately Strong
Capital and Earnings	Strong	Strong
Risk Position	Intermediate	Moderate
Financial Flexibility	Adequate	Adequate
Modifiers	0	0
ERM and Management	Strong	Strong
Enterprise Risk Management	Adequate with Strong Risk Controls	Adequate with Strong Risk Controls
Management & Governance	Satisfactory	Satisfactory
Holistic Analysis	0	0
Liquidity	Exceptional	Exceptional
Support	0	0
Group Support	0	0
Government Support	0	0

Related Criteria

- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 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

Ratings List

Ratings Affirmed

Gothaer Lebensversicherung AG	
Gothaer Krankenversicherung AG	
Gothaer Allgemeine Versicherung AG	
Issuer Credit Rating	A-/Stable/--
Financial Strength Rating	A-/Stable/--
Gothaer Allgemeine Versicherung AG	
Junior Subordinated	BBB

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.