

Research Update:

Insurance Group Gothaer Upgraded To 'A' On Resilient Operating Performance And Robust Capitalization; Outlook Stable

September 16, 2021

Overview

- In 2020 and 2021, German insurance group Gothaer has demonstrated resilient operating performance that compares well with peers'.
- The group's competitive edge is underpinned by its prominent position within the German insurance market, well-established and diversified distribution channels, as well as broad product portfolio.
- Gothaer's capital position is robust as per our risk-based capital model and Solvency II, due to strict asset and liability management and low sensitivity to interest rates.
- We therefore raised our ratings on the group's core insurance operating entities to 'A' from 'A-'.
- The stable outlook reflects our expectations that the group will maintain its strong market position in the German small and midsized enterprise (SME) segment and robust capitalization levels backed by an attractive risk-return profile in property and casualty (P&C), life, and health.

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Rating Action

On Sept. 16, 2021, S&P Global Ratings raised its long-term issuer credit ratings to 'A' from 'A-' on the core companies of Germany-based multiline insurer Gothaer Insurance Group (Gothaer Group). This includes P/C insurer Gothaer Allgemeine Versicherung AG, life insurer Gothaer Lebensversicherung AG, and health insurer Gothaer Krankenversicherung AG. The outlook on all the entities is stable.

At the same time, we also raised the issue rating on the group's junior subordinated fixed-to-floating-rate notes to 'BBB+' from 'BBB'. The notes are issued by Gothaer Allgemeine Versicherung AG.

Rationale

Our ratings reflect Gothaer's established position within the German insurance sector's commercial and SME segment, coupled with robust operating performance and a resilient capital position.

The group's earnings have remained strong historically, supported mainly by Gothaer's underwriting discipline and a well-diversified business mix. The five-year (2020-2016) average return on equity is 8.4%, and the five-year average combined ratio (loss and expense ratio combined) is about 95%. We expect these ratios will remain between 6%-8% and 95%-97%, respectively.

In 2021, Gothaer will likely face net claims of €21 million (gross claims: >€410 million) for the damages incurred in Germany this July from the storm known as "Bernd". We do not expect a material negative impact on the group's capital and earnings, thanks to solid capital adequacy, effective reinsurance protection, and an ample equalization provision.

Gothaer's diversified distribution channels and business mix allows the group to offer insurance product solutions across all business segments, enabling it to become a leading insurance player for SME businesses in its domicile market of Germany. The group is the first insurer in the German market to offer a joint platform for a company's life and health insurance business administration, distribution, and services. Its platform is called "ePension".

Gothaer benefits from sound capital adequacy, and we expect it to remain comfortably above the 'A' level, according to our risk-based capital model, through 2021-2023. In our view, a capital adequacy level of at least strong will continue to support a strong financial risk profile. We therefore revised our respective outlook triggers.

Our assumption is mainly supported by Gothaer's ability to post strong bottom-line results, which will likely be in the €75 million-€85 million range, and the group's strategy to move toward unit-linked and biometric life businesses, which are less capital intensive and sensitive to interest rate movements. The shift to biometric products is further underscored by a solid and improving risk result within the gross surplus. Furthermore, Gothaer's health insurance business focuses on supplementary products with strong profitability. The gross surplus in health increased about 8% in 2020 compared with 2019.

Gothaer's strong regulatory solvency ratio, which stood at 269% (including transitionals) at year-end 2020, further backs our favorable view of its overall capitalization. The group's Solvency II ratio without transitionals is at 195% for half-year 2021, compared with 193% for year-end 2020, showing low volatility within 2021. The life Solvency II ratio increased to 210% for half-year 2021 from 187% for year-end 2020, mainly due to the increase in interest rates.

The group's investment portfolio is diverse, with no substantial segment or single obligor concentration. Gothaer accessed capital markets in 2015, when it issued subordinated debt that it used to refinance another maturing hybrid issuance. The group's leverage and coverage are within acceptable thresholds for the rating, and we do not foresee any material deviations.

Outlook

The stable outlook reflects our view that the group will defend its strong competitive position in the German life, health, and P&C insurance market, in particular in the SME and commercial segment, along with resilient capitalization levels and robust underwriting profitability over the next 12-24 months, despite ongoing low interest rates.

Downside scenario

We are unlikely to lower the ratings over the next 12-24 months. However, we could do so if:

- The group's earnings are consistently weaker than our base-case assumptions, or if we see higher earnings volatility and the group underperforms peers in the German market; or
- We thought Gothaer could no longer maintain capital adequacy at the 'A' level, which could happen as a result of aggressive growth, higher investment risk, or lower-than-expected retained earnings.

Upside scenario

A positive rating action is unlikely at this time. An upgrade would require an improvement in the group's competitive position, which could occur if it significantly diversifies earnings by business line or region, which we do not foresee over the next 12-24 months.

Ratings Score Snapshot

	To	From
Financial strength rating	A/Stable/--	A-/Positive/--
Anchor	a	a-
Business risk	Strong	Strong
IICRA	Intermediate Risk	Intermediate Risk
Competitive position	Strong	Strong
Financial risk	Strong	Strong
Capital and earnings	Strong	Strong
Risk exposure	Moderately low	Moderately low
Funding structure	Neutral	Neutral
Modifiers		
Governance	Neutral	Neutral
Liquidity	Exceptional	Exceptional
Comparable ratings analysis	0	0
Support	0	0
Group support	0	0
Government support	0	0

IICRA--Insurance Industry And Country Risk Assessment.

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
- Criteria | Insurance | Property/Casualty: Assessing Property/Casualty Insurers' Loss Reserves, Nov. 26, 2013
- 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

Ratings List

Upgraded

	To	From
Gothaer Allgemeine Versicherung AG		
Junior Subordinated	BBB+	BBB

Upgraded; Outlook Action

	To	From
Gothaer Allgemeine Versicherung AG		
Gothaer Lebensversicherung AG		
Gothaer Krankenversicherung AG		
Issuer Credit Rating		
Local Currency	A/Stable/--	A-/Positive/--
Financial Strength Rating		
Local Currency	A/Stable/--	A-/Positive/--

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