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Sava Insurance Group

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Credit Highlights

**Operating Company Covered
By This Report**

Financial Strength Rating

Local Currency

A/Stable/--

Overview

Strengths

Strong competitive position backed by the market position in Slovenia and reinforced by stable international reinsurance business

Risks

Limited geographic diversification outside Slovenia in terms of premiums and earnings

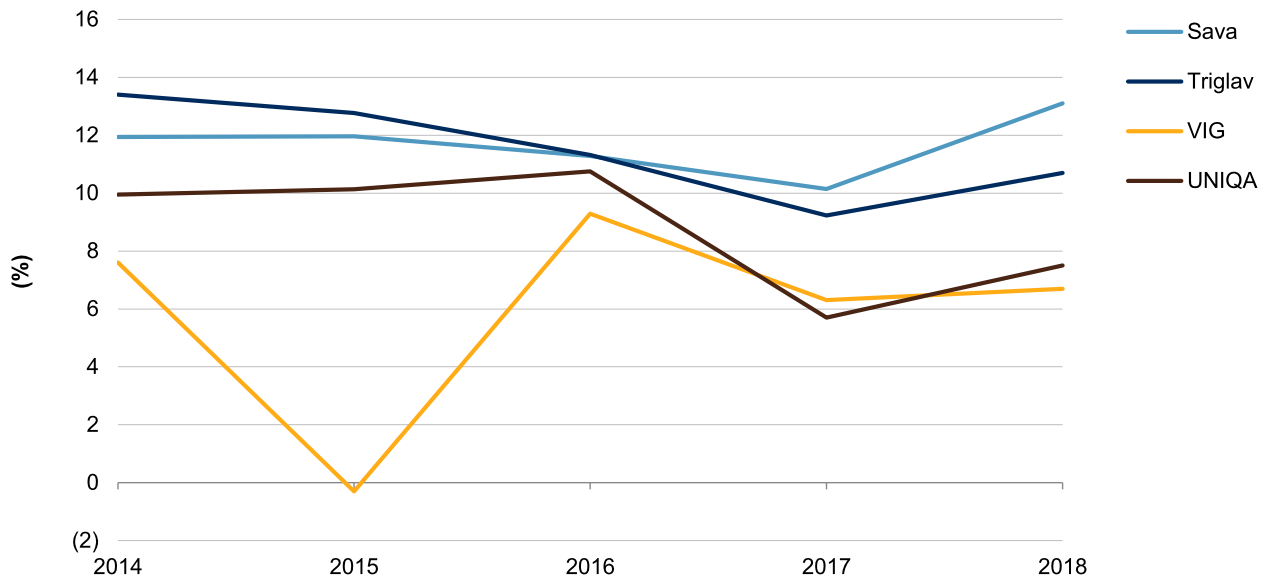
Extremely strong capital adequacy levels with very conservative investment portfolio and limited underwriting risk

S&P Global Ratings expects that Sava Insurance Group to retain its no. 2 position in an attractive Slovenian insurance market while focusing on profitable opportunities. We expect Sava's market share in the Slovenian insurance market will remain stable at about 17%, and benefit from its wide distribution network and solid brand reputation in Slovenia and in some of the Adria countries. The group's international reinsurance operations is stable and soundly profitable, further enhancing its earnings diversity. Still, Sava continues to have lower geographic diversification in terms of revenues and net income than higher-rated competitors.

Sava's group earnings are likely to remain sound, thanks to its sustainably strong underwriting results at its largest subsidiary, Zavarovalnica Sava, and stable performance of its reinsurance entity, Sava Re. The group's combined (loss and expenses) ratio gradually improved and is now comparably strong at 93.0% in 2018 compared with its five-year average of 95.1%. Stable and attractive margins underline a better operating performance than most of its international peers. We expect the company to continue with prudent underwriting through which to keep operating performance resilient with a nonlife combined ratio of below 95% and group return on equity (ROE) of above 10% in 2019-2021.

Chart 1

Return On Equity At Sava And Selected Peers



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Capitalization is likely to remain one of the key strength for Sava, despite further organic and inorganic business expansion. Our risk-based capital (RBC) model, with which we measure capitalization, is robust and above the 'AAA' level, further supported by expected strong earnings. We believe the company might use some of the extremely strong capital for faster business expansion. However, we expect the group will maintain capitalization at least in the 'AA' range of our insurance capital model over the next two-to-three years.

Outlook

The stable outlook on Sava's core operating entities reflects our expectation that the group's management will continue to implement its strategy of profitable growth while further diversifying premiums and income streams. Despite growth, we expect Sava will sustain at least very strong capitalization, while posting solid and stable earnings over the next two years.

Downside scenario

We could lower the ratings in the next two years if Sava's competitive position were to weaken because of significantly eroded volumes or profitability triggered, for example, by external conditions that would also derail sound macroeconomic development in Slovenia.

Upside scenario

We consider a positive rating action as remote in the next two years. An upgrade would require the group improving its competitive position, which could occur, for example, if sustainable economic growth propels Slovenia's income in GDP per capita terms further toward the eurozone average and strengthens prospects for profitable domestic growth, which we do not foresee over the next 12-24 months.

Key Assumptions

- The Slovenian economy will expand by 3.4% in real terms this year and slightly below 3.0% per year from 2020-2022
- Inflation to average 2% over 2019-2020, the slight increase reflecting sound domestic demand and wage growth
- Continuation of accommodative monetary policy from the European Central Bank will lead to interest rates and investment yields staying low for longer.

Table 1

Sava Insurance Group--Key Metrics						
(Mil. €)	2021F	2020F	2019 E	2018	2017	2016
Gross premiums written (Mil. €)	>600	~590	~570	546.3	517.2	490.2
Net premiums earned (Mil. €)	>550	~550	~530	504.7	470.9	458.1
Net income (Mil. €)	>39	>37	>34	43.0	31.1	32.9
Total reported capital	>380	>360	>340	340.4	316.4	321.0
Return on shareholder equity (reported, %)	>10	>10	>10	13.1	10.1	11.3
P/C net combined ratio (%)	<95	<95	<95	93.0	94.8	95.5
Net investment yield (%)	>1.5	>1.5	>1.5	1.7	1.8	1.9
Fixed charge coverage	-	-	-	-	66.9	58.3
Financial leverage (%)	-	-	-	-	0.0	4.9

Table 1

Sava Insurance Group--Key Metrics (cont.)						
(Mil. €)	2021F	2020F	2019 E	2018	2017	2016
S&P Global Ratings-calculated capital adequacy	At least Very Strong	At least Very Strong	At least Very Strong	Extremely Strong	Extremely Strong	Extremely Strong

P/C--Property and casualty. F--Forecast under S&P Global Ratings base-case scenario. E-- Expected.

Business Risk Profile

Sava is the second-largest insurer in Slovenia, with further operations through the Adria region. The group is expanding its operations and has sustainably strong earnings in its domestic insurance business, while its stable and soundly profitable international reinsurance business offers the group additional income diversification.

In our view, a key strength of Sava's solid competitive position is its strong and stable operating performance. This is mainly from its domestic market in Slovenia, which contributes about 70% of group earnings. The sector benefits from a growing economy, strong operating performance, and good diversification of insurance assets. Demand for property and casualty (P&C) insurance remains robust on the back of relatively low unemployment. Life insurance sector performance remains fair with relatively stable margins. However, business growth remains relatively limited due to low interest rate environment. Overall, we view the risk to which Sava is exposed in the domestic market as intermediate.

Sava benefits from attractive technical results in P&C and life segments, in particular in Slovenia. The group has a wide network of controlled distribution in particularly across the country, and a relatively well-recognized brand among large parts of Slovenia and in some of the Adria countries. A well-diversified insurance portfolio allows the group balanced and resilient operating performance. In the past six years, a favorable macroeconomic environment, operational changes, and enhanced risk management capabilities with tighter underwriting controls enabled the group to gradually improve its combined ratio to 93.0% at the end of 2018. The trend continued in first half 2019, when underwriting performance was about 95.0%, benefiting from fewer domestic natural catastrophes and the group's higher operational efficiency. In life insurance, the group is mostly underwriting risk products and capital light savings, which let Sava sustain very good and stable margins even with low interest rates.

In its international reinsurance business, the group is leveraging its established and proven expertise as a service-driven coverage provider, through which it built strong and stable relationships with its cedents. We believe its reinsurance operations are an important contributor to the overall group performance, as well as group risk know-how and access to international primary and reinsurance markets. Therefore, we believe reinsurance operations are enhancing the group's overall competitive position.

In our view, Sava is constantly working on developing its Slovenian operations; and gradually and cautiously expanding its foreign operations, either in primary or reinsurance space. In the past two years, the group expanded its scope of operations into asset management, assistance business and health operations in Slovenia and pension and primary business in Adria countries. We see these additions positive for Sava since they are enabling the company to offer competitive products in line with domestic and international peers. Moreover, newly added operations are fairly

profitable and are adding to some extent to higher earnings stability. However, Sava continues to have lower geographic diversification of revenues and net income than those of higher-rated peers.

We expect the group will continue with profitable growth of its core operations and that it will gradually scale up its foreign operations, along with its recently acquired pension and asset management operations. We expect Sava's overall premiums to grow 3%-5% in 2019-2021, with the group to continue with prudent underwriting in life and nonlife, even in slightly less favorable macroeconomic times. This will allow the group to keep operating performance resilient, with nonlife combined ratio of below 95% and good life insurance performance in 2019-2021. These attractive and stable margins should sustainably support better operating performance than that of most international peers.

Table 2

Sava Insurance Group--Competitive Position					
(Mil. €)	2018	2017	2016	2015	2014
Gross premiums written	546.3	517.2	490.2	486.3	468.2
% change	5.6	5.5	0.8	3.9	21.1
Net premiums written	519.4	483.0	459.0	455.9	440.8
% change	7.5	5.2	0.7	3.4	21.1
Net premiums earned	504.7	470.9	458.1	447.6	437.6
Total assets under management	1,464.6	1,482.0	1,455.4	1,388.6	1,223.9
Growth in assets under management (%)	(1.2)	1.8	4.8	13.5	6.7
PC: Reinsurance usage (%)	5.8	7.9	7.6	7.5	7.1

Financial Risk Profile

We believe that the group's capitalization is robust--above the 'AAA' level according to our risk-based capital model--and is in our view one of the key rating strengths. Reaffirming our solvency view is a Solvency II ratio of 218% on Dec. 31, 2018, based on a standard formula and no use of transitional adjustments. In our view, the company's capital position benefits from significant core capital, which is supported by prudent margins on its P/C loss reserves. Strong income and dividend payments enable the company to generate enough capital to cover capital requirement from moderate organic growth and providing some budget for acquisitions. We believe Sava may use some of the currently extremely strong capital for further business expansion. However, we expect that the group will maintain capitalization at least in the 'AA' range of our insurance capital model over the next two-to-three years.

Sava's risk profile is very solid, benefiting from its very conservative investment portfolio and conservative reinsurance protection. This, in our view, makes the group's balance sheet less sensitive to interest rates, credit spreads, and equity market volatility than most of the European peers at similar levels. We believe that tighter underwriting risk controls that Sava gradually implemented in the past decade, combined with enhanced reinsurance protection, will safeguard the group against losses that would be outside its risk tolerances. Investment assets, mainly fixed income instruments, have creditworthiness in the high 'A' range and are broadly diversified across the eurozone. Exposure to Slovenian country risk is relatively low, making up only 18% of its investments at the end of first-half 2019. In our view, continued sound macroeconomic development in Slovenia strengthened creditworthiness of Slovenian assets (for

more information, see "Slovenia Ratings Raised To 'AA-/A-1+' On Sound Macroeconomic Fundamentals; Outlook Stable," published June 14, 2019, on RatingsDirect) and is solidifying the group's very conservative investment risk profile.

In 2018, Sava used the good operating environment and managed to deliver material growth in net income, which jumped by almost 40% year-over-year to €43 million. Very strong results enabled the group to post attractive ROE of 13.1% in 2018. The five-year average ROE is 11.7%, and is in our view strong compared with that of European peers. Also in the first half of 2019, Sava continued to deliver strong results, with net income of €22.6 million and reported annualized ROE of 12.5%. The company is on pace to deliver its planned net income of at least €43 million. We expect that in 2019-2021 earnings will remain resilient, with the group to deliver ROE of at least 10%. We expect that dividend distributions to remain moderate and to continue to support execution of Sava's business expansion strategy.

Table 3

Sava Insurance Group--Capitalization And Earnings					
(Mil. €)	2018	2017	2016	2015	2014
Common equity	340.2	316.1	297.0	286.4	271.5
Net income	43.0	31.1	32.9	33.4	30.5
Return on shareholder equity (reported, %)	13.1	10.1	11.3	12.0	11.9
P/C net expense ratio (%)	36.2	36.0	36.5	35.3	36.6
P/C net loss ratio (%)	56.9	58.9	58.6	60.5	59.5
P/C net combined ratio (%)	93.0	94.8	95.5	96.0	96.2
Life: Net expense ratio (%)	30.2	27.1	26.2	23.6	27.3

P/C--Property and casualty.

Sava has a debt-free balance sheet. We believe the group retains adequate financial flexibility to issue subordinated debt to cover any capital needs.

Other Key Credit Considerations

We see favorably Sava's clear and credible strategic planning and its conservative financial management. We consider the board experienced and capable of executing the group's business strategy, as shown in business development and group performance in recent years.

We believe Sava has access to ample liquidity mainly due to its very conservative highly liquid investment portfolio. In addition, growing operations are providing constant cash inflows. Moreover, most of the business is short tail, of which larger risks are heavily reinsured. Therefore, larger claims are not a significant drag on its cash position.

We continue to regard Sava as a government-related entity, chiefly because the Slovenian government is its largest shareholder. Moreover, the group plays a key role in protecting Slovenians in a structured way from the impact of catastrophe events, to which the country is exposed. We believe there is a moderately high likelihood that the government of Slovenia (AA-/Stable/A-1+) would provide timely and sufficient extraordinary support to Sava in the event of financial distress. Although we do not include any uplift for support in the ratings, a change in shareholding would have a negative impact on the ratings if a financially weaker group were to take over Sava.

Rating Score Snapshot

Ratings Score Snapshot	
Business Risk Profile	Strong
Competitive position	Strong
IICRA	Intermediate Risk
Financial Risk Profile	Very Strong
Capital and earnings	Very Strong
Risk exposure	Moderately Low
Funding structure	Neutral
Anchor*	a
Modifiers	0
Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0
Financial Strength Rating	A

*Reflects that Sava continues to have lower geographic diversification of revenues and net income than its higher-rated peers.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Insurance | Property/Casualty: Assessing Property/Casualty Insurers' Loss Reserves, Nov. 26, 2013
- 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

Related Research

- Insurance Industry And Country Risk Assessment: Slovenia Property/Casualty, Sept. 9, 2019
- Research Update: Slovenia-Based Sava Insurance Group 'A' Ratings Affirmed; Outlook Stable, July 30, 2019
- Slovenia Ratings Raised To 'AA-/A-1+' On Sound Macroeconomic Fundamentals; Outlook Stable, June 14, 2019
- Solvency II Gives European Insurers Room To Issue More Hybrid Debt, But Not Without Risk To The Ratings, May 29, 2019

Ratings Detail (As Of September 10, 2019)*

Operating Company Covered By This Report

Ratings Detail (As Of September 10, 2019)*(cont.)

Sava Re

Financial Strength Rating

Local Currency

A/Stable/--

Issuer Credit Rating

Local Currency

A/Stable/--

Related Entities**Zavarovalnica Sava d.d.**

Financial Strength Rating

Local Currency

A/Stable/--

Domicile

Slovenia

*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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