

Research Update:

Spain-Based Mapfre Re Upgraded To 'A+' On Improved Underwriting Earnings Diversification; Outlook Stable

November 18, 2019

Overview

- Mapfre's effective implementation of restructuring measures in countries where it has been underperforming enhances the group's underlying earnings diversification and competitiveness.
- Despite a drop in reported earnings of 12.5% to €462.9 million in the third quarter of 2019, mainly driven by a write-down in the assistance business, underwriting earnings improved by 1.7 percentage points, leading to a combined (loss and expense) ratio of 96.4%.
- We are therefore raising our issuer credit and insurer financial strength ratings on Mapfre Re, a core operating entity of the group, to 'A+' from 'A'.
- We are also raising the ratings on the group's nonoperating holding company Mapfre S.A. and its senior unsecured bonds to 'A-' from 'BBB+', as well as its junior subordinated bonds to 'BBB' from 'BBB-'.
- The stable outlook reflects our expectation that Mapfre will remain focused on profitable growth, with solid technical performance and capitalization at least in the 'A' level, based on our capital model.

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Rating Action

On Nov. 18, 2019, S&P Global Ratings raised to 'A+' from 'A' the long-term issuer credit and insurer financial strength ratings on Spain-based Mapfre group's core operating entity Mapfre Re, Compania de Reaseguros, S.A. At the same time, we raised the long-term issuer credit rating on the group's holding company Mapfre S.A. to 'A-' from 'BBB+'. The outlook on both entities is stable.

Additionally, we also raised issue ratings on Mapfre's senior unsecured debt to 'A-' from 'BBB+' and the issue ratings on the group's subordinated debt to 'BBB' from 'BBB-'.

Rationale

We raised the ratings because we think Mapfre's implementation of its strategic plan has enhanced underlying profitability of its underperforming lines, mainly in Brazil and the United States, adding diversity to the group's overall earnings. Despite a decline in the group's net results by €65.9 million to €462.9 million so far in 2019, we believe that underlying profits improved because Mapfre has taken advantage of stronger diversification of earnings. We understand that the reported deterioration in net earnings is driven by one-off losses from the write-down of goodwill in its assistance operations, and we do not anticipate those losses will repeat in the coming years. We expect that the group will continue to enforce profitability in underperforming lines and countries, generating an annual net profit (after minorities) of about €700 million supported by a group combined ratio at around 97% and a return on equity of about 8% over the next two years.

Mapfre has been able to demonstrate its capacity to build global business outside of Spain mainly through its reinsurance business, as well as in Brazil and the U.S. The stringent implementation of profitability measures led to a reported combined ratio of 91.1% in Brazil and 99.7% in North America in the first nine months of 2019 compared with a five-year average of about 95% in Brazil and 104% in North America. As a consequence, so far in 2019, the group's reported combined ratio has improved to 96.4%, compared with 98.1% in the same period of 2018.

The group is the second-largest insurer in its domestic market in terms of premiums, holding leading positions in both property/casualty (P/C) and life insurance. It also ranks No.2 in Brazilian P/C through its joint venture with Banco do Brasil, one of Brazil's largest banks that serves more than 66 million clients. Mapfre Group generated €2.4 billion from external reinsurance in 2018 (65% of its gross inward reinsurance premiums), accounting for over 10% of the group's business and providing a significant source of profit diversification. However, compared with higher-rated peers, Mapfre is less diversified in life insurance. Additionally, a larger share of its business is generated in emerging markets, which are potentially more volatile than mature markets.

The group has a solid consolidated capital position with a Solvency II ratio (excluding transitional measures) of 183% based on June 2019 figures. Additionally, we expect capital adequacy to remain solid, at our 'A' confidence level according to S&P Global Ratings' risk-based capital model. In our opinion, Mapfre will continue to generate sufficient retained earnings to compensate for the rise in capital requirements deriving from both organic growth and small bolt-on acquisitions.

Mapfre Group's international diversification makes it resilient to a hypothetical domestic sovereign stress situation. As a result, under our criteria, we can rate the core operating entities of the Mapfre group above the Spanish sovereign long-term rating by a maximum of three notches, reflecting our view of Mapfre Group's moderate to high sensitivity to country risk.

Outlook

The stable outlook is based on our expectation that the group will remain focused on profitable growth in 2020-2022, maintaining a leading position in its main markets, without earnings being impacted by further material one-off losses. We also expect that the group will keep its capital position comfortably at the 'A' level, according to our capital model, backed by sound earnings of about €700 million and supporting Mapfre's growth and dividend targets.

Downside scenario

We could downgrade the group over the next 24 months if:

- Capitalization declined sustainably below our threshold for the 'A' level based on our capital model. This could result from severe combined global and domestic financial market stress;
- Performance consistently deteriorates below our expectations with combined ratios higher than 100%, cutting into the group's competitive strength; or
- We no longer believed Mapfre Group would pass our sovereign default test, which could result from an unexpected drop in regulatory capital or from an increase in Spanish assets relative to regulatory capital.

Upside scenario

We see limited rating upside in the next 24 months. We could take a positive rating action if we were to see a substantial enhancement in Mapfre's capital position through higher earnings contribution bringing capitalization at least in the 'AA' rating level.

Ratings Score Snapshot

	To	From
Financial strength rating	A+/Stable/--	A/Positive/--
Anchor	A+	A
Business risk	Very Strong	Strong
IICRA	Intermediate	Intermediate
Competitive position	Very 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: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 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

Ratings List

Upgraded

	To	From
Mapfre S.A.		
Issuer Credit Rating		
Local Currency	A-/Stable/--	BBB+/Positive/--
Senior Unsecured	A-	BBB+
Subordinated	BBB	BBB-
Mapfre Re, Compania de Reaseguros, S.A.		
Issuer Credit Rating		
Local Currency	A+/Stable/--	A/Positive/--
Financial Strength Rating		
Local Currency	A+/Stable/--	A/Positive/--

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.

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