

Research Update:

# Munich Reinsurance Co. Outlook Revised To Positive From Stable On Improving Diversification; Ratings Affirmed

August 16, 2023

## Overview

- Global reinsurer Munich Reinsurance Co. (Munich Re) continues to demonstrate a sound operating performance. Strong and improving underwriting performance in its various operations increase diversification, which compares well with peers.
- We believe Munich Re is well placed to continue to leverage favorable global reinsurance pricing and expect the group will post a net income of about €4.0 billion-€4.5 billion, with a return on equity (ROE) of above 14% and a consolidated combined ratio of about 89%-91% (based on IFRS 17) in 2023 and 2024.
- We therefore revised our outlook to positive from stable. At the same time, we affirmed our 'AA-' issuer credit and insurer financial strength ratings on Munich Re.
- The positive outlook reflects our view that the group will defend its excellent competitive position and conservative capital management via further earnings diversification by divisions.

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## Rating Action

On Aug. 16, 2023, S&P Global Ratings affirmed its 'AA-' issuer credit and insurer financial strength ratings on Munich Re (all affected entities are part of the ratings list at the end of this article). The outlook is positive.

## Rationale

**Munich Re's earnings diversification has improved significantly in the past couple of years.** In the first half of 2023, Munich Re generated strong and well diversified earnings, backed by a reported net income of €2.4 billion, an annualized ROE of 16.9%, and combined ratios of 83.5%, 84.7%, and 91.6% in the property and casualty (P&C) reinsurance unit, ERGO Germany, and ERGO International, respectively, based on IFRS 17 accounting standards. These combined ratios could

be higher if we excluded discounting and other adjustments consistent with IFRS 4. Munich Re's earnings diversification has benefited from sound technical performance in all major divisions, namely P&C reinsurance, Global Specialty, its retail primary insurance arm ERGO, and life reinsurance. ERGO's earnings contribution has stabilized in the past few years and is gradually improving. Life reinsurance has also improved significantly after a COVID-19-related drop in income in 2020 and 2021. The group therefore benefits from greater diversification and lower dependence on cyclical business, such as short-tail P&C reinsurance, compared with most reinsurance peers.

**Munich Re is well placed to continue to leverage the favorable market environment for P&C reinsurance, as demonstrated by high growth rates that exceed those of most peers.**

In addition, we believe Munich Re will benefit from a gradual rise in investment income, due to increasing interest rates. We think Munich Re is well placed to post a net income of about €4.0 billion-€4.5 billion in 2023 and 2024, with an ROE of above 14% and a consolidated combined ratio of about 89%-91% in 2023 and 2024. Under our base case scenario, we take into account that about 14 percentage points of the P&C reinsurance business's combined ratio stem from natural catastrophe and manmade large losses, while about 5 percentage points are positive run-off results from prior year loss reserves. This forecast is based on IFRS 17 accounting standards.

**In our view, capital management remains conservative.** In 2022, capital adequacy remained in line with our 'AA' base case assumptions, according to our risk-based capital model. This was despite the sharp increase in interest rates, related declines in asset value reserves of fixed income securities, and capital consumption due to strong growth rates of the underlying business. Munich Re's Solvency II ratio also remained high at 273%, as of June 30, 2023, comparing well with peers. We anticipate that the group will cope well with current challenges, such as high inflation and capital market volatility, based on its conservative balance sheet and strong reserving. We think this will enable the group to maintain capitalization at least at 'AA' confidence levels over the next two years, based on our risk-based capital model. We think Munich Re is exposed to large tail risks, such as natural catastrophes, which could lead to some capital and earnings volatility. However, the group's extremely diversified portfolio, strong risk controls, and cautious reserving practices offset these risks, in our view.

## **Outlook**

The positive outlook reflects our view that the group will defend its excellent competitive position and conservative capital management over the next two years via further earnings diversification by divisions and improvements, with an ROE of above 14% in 2023 and 2024.

## **Downside scenario**

We could revise the outlook to stable in the next two years if the group appeared likely to perform below our expectations or below higher-rated peers, or if its risk-based capital adequacy declined and stayed below the 'AA' level for a long period. This could occur following materially higher investment charges or significant unexpected losses from large natural catastrophes.

## **Upside scenario**

We could upgrade the ratings by one notch in the next two years if Munich Re continued to

demonstrate a strong operating performance that compares well with higher-rated peers and if it benefited from continued diversification from its various operations.

## Ratings Score Snapshot

### Munich Reinsurance Co.

	To	From
Financial strength rating	AA-/Positive/--	AA-/Stable/--
Anchor*	aa-	aa-
Business Risk	Very strong	Very strong
Competitive position	Excellent	Excellent
IICRA	Intermediate	Intermediate
Financial risk	Strong	Strong
Capital and earnings	Very strong	Very strong
Risk exposure	Moderately high	Moderately high
Funding structure	Neutral	Neutral
Modifiers	0	0
Governance	Neutral	Neutral
Liquidity	Exceptional	Exceptional
Comparable rating analysis	0	0
Support	0	0
Group support	0	0
Government support	0	0

IICRA--Insurance Industry And Country Risk Assessment. \*The anchor reflects the group's position as global market leader in global reinsurance and diverse business operations in the primary market, as well as very strong reserving.

## Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- 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: A New Level Of Enterprise Risk Management Analysis: Methodology For Assessing Insurers' Economic Capital Models, Jan. 24, 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

### Ratings Affirmed

#### Munich Reinsurance Co.

Junior Subordinated	A
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#### Munich Re America Corp.

Senior Unsecured	A-
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### Ratings Affirmed; Outlook Action

	To	From
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#### Munich Reinsurance Co.

#### New Reinsurance Co. Ltd

#### Munich Re of Malta PLC

#### Great Lakes Insurance SE

Issuer Credit Rating	AA-/Positive/--	AA-/Stable/--
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#### Munich Reinsurance Co.

#### Princeton Excess & Surplus Lines Insurance Co.

#### New Reinsurance Co. Ltd

#### Munich Reinsurance Co. of Canada

#### Munich Reinsurance Co. of Australasia Ltd.

#### Munich Reinsurance Co. of Africa Ltd.

#### Munich Reins America Inc.

#### Munich Re of Malta PLC

#### Munich Re of Bermuda, Ltd.

#### Munich American Reassurance Co.

#### Great Lakes Insurance UK Ltd.

#### Great Lakes Insurance SE (Australia Branch)

#### Great Lakes Insurance SE

#### ERGO Versicherung AG

#### American Alternative Insurance Corp.

Financial Strength Rating		
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Local Currency	AA-/Positive/--	AA-/Stable/--
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**American Alternative Insurance Corp.**

**Princeton Excess & Surplus Lines Insurance Co.**

**Munich Reinsurance Co. of Canada**

**Munich Reinsurance Co. of Australasia Ltd.**

**Munich Reins America Inc.**

**Munich American Reassurance Co.**

**Great Lakes Insurance UK Ltd.**

**Great Lakes Insurance SE (Australia Branch)**

**ERGO Versicherung AG**

Issuer Credit Rating

Local Currency AA-/Positive/-- AA-/Stable/--

**ERGO Group AG**

Issuer Credit Rating

Local Currency A/Positive/-- A/Stable/--

**Munich Re America Corp.**

Issuer Credit Rating

Local Currency A-/Positive/-- A-/Stable/--

**Munich Re Trading LLC**

**Temple Insurance Co.**

Issuer Credit Rating

Local Currency A+/Positive/-- A+/Stable/--

**Temple Insurance Co.**

Financial Strength Rating

Local Currency A+/Positive/-- A+/Stable/--

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