# Munich Reinsurance Co.

**Primary Credit Analyst:**
Jean Paul Huby Klein, Frankfurt (49) 69-33-999-198; jeanpaul.hubyklein@spglobal.com

**Secondary Contact:**
Johannes Bender, Frankfurt (49) 69-33-999-196; johannes.bender@spglobal.com

**Research Contributor:**
Milan Kakkad, Mumbai + (022)33428336; milan.kakkad@spglobal.com

## Table Of Contents

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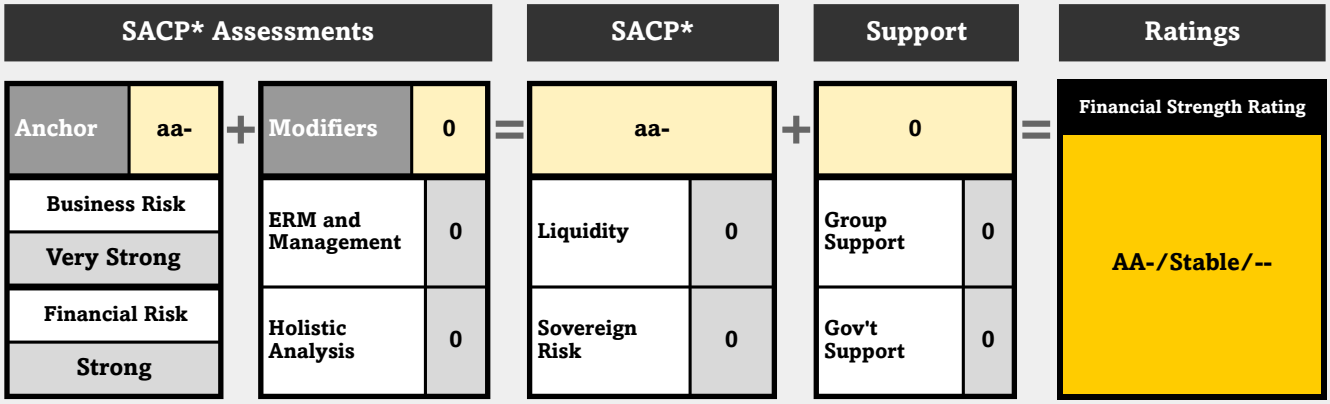


*Stand-alone credit profile.
See Ratings Detail for a complete list of rated entities and ratings covered by this report.

## Major Rating Factors

| Strengths | Weaknesses |
|---|---|
| • A global leading position in the property/casualty (P&C) and life reinsurance market, supported by a well-recognized brand name.<br>• Superior diversification across geographies and products compared with peers, including sizeable primary insurance operations under the ERGO brand.<br>• Strong track-record of maintaining healthy capital adequacy levels under regulatory requirements, and at 'AA' level based on S&P Global Ratings' capital model, backed by well-defined enterprise risk management (ERM) practices and strong reserve adequacy. | • Exposure to tail risk such as natural catastrophes, leading to potential earnings volatility, as experienced in recent years.<br>• Weaker market presence and earnings contribution from primary insurance operations under the ERGO brand compared with the reinsurance business, although improving. |

## Rationale

The ratings on Germany-based Munich Reinsurance Co. and its core operating companies (collectively Munich Re) reflect the group's extremely strong franchise as one of the global leading reinsurance companies, supported by solid and conservative financial capabilities. Munich Re is a global reinsurance group offering life and P&C reinsurance, with an extremely diverse regional and business line mix and leading account capabilities. Besides its market-leading position in reinsurance, it owns a sizable primary insurance operation, ERGO, with operations in Germany, Europe, and Asia across P&C, life, and health business.

The ratings also reflect our view of the group's healthy capitalization under its internal model and Solvency II, as well as under our capital model.

In our opinion, the global reinsurance sector is inherently more volatile than many other insurance sectors. Munich Re has built a strong capital buffer to safeguard its business against adverse market developments, including high catastrophe losses, as seen in 2017 and 2018, by diversifying its portfolio across various business lines and regions. The group actively manages volatility through stringent risk limits, group reinsurance optimization, and robust ERM capabilities.

**Outlook: Stable**

The stable outlook reflects our view that the group will defend its extremely strong competitive position during the next 12-24 months by:

- Continuing to leveraging moderate price increases in global P&C reinsurance business in 2019;
- Further optimizing growth opportunities in structured reinsurance;
- Capturing increasing earnings potential from primary insurance operations; and
- Maintaining capital adequacy securely in the 'AA' range in 2019-2021.

### Upside scenario

The global P&C reinsurance sector continues to face challenging business conditions, with only moderate price increases over the past two years. However, we might consider raising the rating if we saw a more favorable pricing environment on a sustainable basis in P&C reinsurance lines. An upgrade would also hinge on the group's ability to further diversify its earning streams, with a sustainable and sizable contribution from its primary insurance operations.

### Downside scenario

We regard a downgrade as remote over the next two years. However, we might consider a negative action if Munich Re's capital adequacy fell below the 'AA' level in our capital model over a prolonged period. This could occur, for example, as a result of materially higher investment charges, combined with unexpectedly large natural catastrophes or other large claims events, and prolonged weakened earnings well below our base-case assumptions.

## Base-Case Scenario

**Macroeconomic Assumptions**

- Moderate global economic growth and inflation.
- Long-term risk-free rates declining to 2.8% from 2.9% in the U.S. and increasing to 0.5% from 0.3% in Germany in 2019 compared with the previous year.

**Key Metrics**

| | --Year ended Dec. 31-- | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2021f | 2020f | 2019f | 2018 | 2017 | 2016 | 2015 | 2014 |
| Gross premiums written (mil. €) | >50,000 | >50,000 | >50,000 | 49064 | 49115 | 48851 | 50374 | 48848 |
| Net income | ~2600-2800 | ~2500-2700 | ~2400-2600 | 2310 | 375 | 2580 | 3122 | 3170 |
| Fixed-charge coverage (x) | >10 | >10 | >10 | 13.5 | 1.3 | 13.1 | 14.1 | 11.7 |
| Financial leverage (%) | <15 | <15 | <15 | 7.6 | 6.5 | 9.7 | 9.3 | 10.1 |
| S&P Global Ratings' capital adequacy | Very Strong | Very Strong | Very Strong | Very Strong | Very Strong | Extremely Strong | Extremely Strong | Extremely Strong |
| P/C: Net combined ratio (%)* | 96-98 | 96-98 | 96-98 | 98.7 | 109.2 | 96.4 | 92.4 | 93.7 |
| P/C: Net expense ratio (%) | N/A | N/A | N/A | 33.9 | 33.2 | 32.9 | 33.4 | 33.0 |
| P/C: Net loss ratio (%) | N/A | N/A | N/A | 64.8 | 76.0 | 63.5 | 59.1 | 60.5 |
| Return on shareholder's equity (%) | 8-9 | 8-9 | 8-9 | 8.4 | 1.3 | 8.2 | 10.2 | 11.2 |
| Common equity (mil. €) | N/A | N/A | N/A | 26,500 | 28,198 | 31,785 | 30965 | 30289 |
| Reinsurance utilization (%) | N/A | N/A | N/A | 4.8 | 4.0 | 3.5 | 3.7 | 3.3 |
| Return on revenue (%) | N/A | N/A | N/A | 4.7 | -2.7 | 3.8 | 5.2 | 3.0 |
| Net investment yield (%) | 2.7-2.9 | 2.7-2.9 | 2.7-2.9 | 3.1 | 3.5 | 3.5 | 3.6 | 3.3 |

*Includes reinsurance and primary insurance. F--forecast. N/A--Not applicable. Source: S&P Global Ratings.

## Business Risk Profile: Very Strong

Munich Re enjoys the benefit of a well-diversified portfolio across all geographies and segments, including global P&C reinsurance, life reinsurance, and global health insurance. It has a sound market position in the German Life and P&C primary markets, as well as a leading market position in the German health market and in some smaller primary insurance operations including in Poland and Austria. In our opinion, life reinsurance business is exposed to low industry risk, owing to a positive earnings trend and high barriers to potential new entrants. However, volatility is higher in P&C reinsurance business due to exposure to natural-catastrophe events. Moreover, the German primary life insurance industry remains exposed to high risk mainly due to asset-liability risks resulting from long life insurance contracts with guarantees, whereas the German health sector faces some political risks.

Munich Re has a market-leading position in the global P&C and life reinsurance markets, accompanied by a significant presence in all primary insurance lines. In our view, Munich Re's highly recognized brand, presence, and expertise in the global reinsurance market are key differentiating factors that are difficult to replicate. This is further supported by Munich Re's ability to leverage moderate price increases in global P&C reinsurance business over the last two years, as well as the group's access to large structured reinsurance deals. Such deals appear accessible to Munich Re and a few other larger peers, but not to the majority of peers in the reinsurance sector, underpinning Munich Re's competitive

advantages. Gross premiums remained nearly stable in 2018 at €49.1 billion, despite a strong increase in P&C reinsurance, fully offset by a premium decline in life reinsurance stemming from one-off restructuring of two major transactions. Group premiums increased by about 2% in first-quarter 2019.

The group's global presence in its various business lines, and the unique diversification by lines of business compared with reinsurance peers', makes it less vulnerable to adverse developments in individual markets. In recent years, we have observed that earnings among the group's P&C reinsurance, life reinsurance, and primary insurance businesses are well diversified. The contribution from primary business ERGO has been improving in recent years following a well-executed restructuring strategy, but remains lower than other segments.

## Financial Risk Profile: Strong

Munich Re's capital adequacy remained stable in 2018, despite heavy natural catastrophe losses for second consecutive year, unchanged dividends of about €1.3 billion, and share buybacks of €1 billion. The group's internal model and Solvency II ratio stood at 245% in 2018, securely above the group's 175%-220% target. The group's capital adequacy, based on our capital model, was securely in the 'AA' range at year-end 2018, and is expected to remain at a similar level for the next two to three years. Our assessment of Munich Re's financial risk profile is supported by the group's very strong and prudent reserves, which we partly incorporate in our assessment of the group's capital, as well as some benefit arising from the sound internal economic capital model.

The group's capital and earnings remain volatile because of their exposure to P&C reinsurance natural catastrophe risks, as demonstrated in 2018 and 2017, with catastrophe losses of € 1.3 billion and €3.7 billion respectively. The return on equity (ROE) for 2018 was 8.4% against 1.3% for 2017. Although we consider that the group's exposure to catastrophe risk could remain a source of material capital and earnings volatility, we think that Munich Re is less vulnerable to this than most reinsurers thanks to its diversified risk profile, strong modeling capabilities, and relatively low catastrophe risk exposure. We do not expect the overall risk profile will change materially in the next two years.

For the primary business, we forecast gradual earnings increases in 2019-2021 to €400 million-€600 million following further portfolio restructuring and cost-efficiency measures. These, combined with sound business performance in P/C and Life & Health reinsurance segments, will result in a gradual net income increase of about €2.4 billion to €2.8 billion in 2019-2021. Consequently, we expect ROE of 8%-9%, and a consolidated combined (loss and expense) ratio of 96%-98% including reinsurance and primary insurance operations. These estimates include assumed catastrophe losses of about 8% in P&C reinsurance and about 4% of run-off profits from prior-years' reserving in P&C reinsurance. We also assume the net investment yield will be 2.7%-2.9%.

The group's access to capital markets as a publicly listed company and its track-record of debt issuance continues to remain key strengths. In our assessment, the positive market indicators and low financial leverage will remain a potential opportunity to raise additional funding for the group, if required. The financial leverage for 2018 remained below 10% and it will remain under 10% for the next two to three years. We also assume fixed-charge coverage will remain over 10x in the near future because it recovered to 13.5x in 2018 from 1.3x in 2017. The low coverage in 2017 was highly influenced by the unusual high natural catastrophe events negatively affecting the group's results.

## Other Assessments

Munich Re's experienced management team displays a good track record of financial discipline and managing the group through difficult market environments, such as the 2008 financial crisis, the ongoing challenges for P&C reinsurance business, still-low interest rates, and large catastrophe losses in 2017.

Munich Re's well-established enterprise risk management framework has remained a key strength. The assessment in particular is supported by the risk culture, risk controls, risk models, emerging risk management, strategic risk management, and capital model. Munich Re is a complex group operating in many geographies and diverse lines of business and as a global and diversified group, the importance of enterprise risk management for Munich Re is high, in our view. The group faces catastrophe risks in the reinsurance division, significant exposure to financial losses in primary insurance, and exposure to global and regional economic cycles. We do not expect the group will experience losses beyond its risk tolerance over the rating horizon. The group's economic capital model is robust, fully integrated, and used to steer business decisions. The model governance structure is strong and supported by extensive documented analytics and process.

The group maintains exceptionally high liquidity to address any concerns. We do not expect any refinancing issues, and we believe the group is capable of managing unexpectedly large claims or a sudden rise in life insurance lapses.

## Other Considerations

### Factors specific to the holding company

The ratings on ERGO Group AG and Munich Re America Corp. reflect these companies' group status as intermediate, non-operating holding companies. The wider notching for Munich Re America Corp. reflects our view of greater structural subordination within insurance groups in the U.S. compared with those outside the U.S.

### Accounting considerations

Munich Re prepares its financial statements under International financial Reporting Standards. The group has a track record of rigorously impairing goodwill early, since operating performance no longer meets group standards. For Solvency II group reporting, the group does not use any matching adjustment, volatility adjustment, third-country equivalence, or transitional measures.

In our analysis of capital adequacy, we recognize partial credit for:

- Credit on deferred-tax liabilities relating to the claims equalization reserve;
- Equity credit for hybrid securities up to the level recognized in regulatory solvency capital;
- An adjustment to the standard duration mismatch on the back of a positive assessment of asset-liability management risk-controls;
- 50% of loss-reserve redundancy; and
- Some benefit from our review of Munich Re's ECM.

## Ratings Score Snapshot

| Munich Reinsurance Co.--Ratings Score Snapshot | |
|---|---|
| Financial Strength Rating | AA- |
| Anchor | aa- |
| Business Risk Profile | Very Strong |
| IICRA | Intermediate |
| Competitive Position | Extremely Strong |
| Financial Risk Profile | Strong |
| Capital and Earnings | Very Strong |
| Risk Position | Moderate Risk |
| Financial Flexibility | Strong |
| Modifiers | 0 |
| ERM and Management | 0 |
| Enterprise Risk Management | Very Strong |
| Management and Governance | Strong |
| Holistic Analysis | 0 |
| Liquidity | Exceptional |
| Support | 0 |
| Group Support | 0 |
| Government Support | 0 |

## Related Criteria

- General Criteria: Guarantee Criteria, Oct. 21, 2016
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- Criteria | Insurance | Property/Casualty: Assessing Property/Casualty Insurers' Loss Reserves, Nov. 26, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Insurance - General: Insurers: Rating Methodology, May 7, 2013
- Criteria | Insurance | General: Enterprise Risk Management, 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: 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
- 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 Detail (As Of June 28, 2019)* | |
|---|---|
| **Operating Companies Covered By This Report** | |
| **Munich Reinsurance Co.** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | AA-/Stable/-- |
| Junior Subordinated | A |
| **American Alternative Insurance Corp.** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **D.A.S. Legal Expenses Insurance Co. Ltd.** | |
| Financial Strength Rating | |
| *Local Currency* | A+/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | A+/Stable/-- |
| **DAS Rechtsschutz AG** | |
| Financial Strength Rating | |
| *Local Currency* | A/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | A/Stable/-- |
| **DKV Deutsche Krankenversicherung AG** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **ERGO Versicherung AG** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Great Lakes Insurance SE** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |

| Ratings Detail (As Of June 28, 2019)*(cont.) | |
|---|---|
| **Great Lakes Insurance SE (Australia Branch)** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Munich American Reassurance Co.** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Munich Reins America Inc.** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Munich Reinsurance Co. of Africa Ltd.** | |
| Financial Strength Rating | |
| *Local Currency* | A-/Stable/-- |
| **Munich Reinsurance Co. of Australasia Ltd.** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Munich Reinsurance Co. of Canada** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Munich Re of Bermuda, Ltd.** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Munich Re of Malta PLC** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Munich Re Trading LLC** | |
| Issuer Credit Rating | |
| *Local Currency* | A+/Stable/-- |
| **New Reinsurance Company Ltd** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |

| Ratings Detail (As Of June 28, 2019)*(cont.) | |
|---|---|
| **Princeton Excess & Surplus Lines Insurance Co.** | |
| Financial Strength Rating | |
| *Local Currency* | AA-/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | AA-/Stable/-- |
| **Temple Insurance Co.** | |
| Financial Strength Rating | |
| *Local Currency* | A+/Stable/-- |
| Issuer Credit Rating | |
| *Local Currency* | A+/Stable/-- |
| **Related Entities** | |
| **ERGO Group AG** | |
| Issuer Credit Rating | |
| *Local Currency* | A/Stable/-- |
| **Munich Re America Corp.** | |
| Issuer Credit Rating | |
| *Local Currency* | A-/Stable/-- |
| Senior Unsecured | A- |
| **Domicile** | Germany |

*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.