MOODY'S
INVESTORS SERVICE

Rating Action: Moody's upgrades Coface's main operating company to A1 IFSR, stable outlook

28 September 2023

Paris, September 28, 2023 - Moody's Investors Service ("Moody's") has today upgraded the long-term insurance financial strength rating (IFSR) of Compagnie Francaise d'Assurance pour le Comm., the main operating company of Coface SA (Coface), to A1 from A2, Coface's long-term issuer rating, to A3 from Baa1, as well as Coface SA's backed subordinated/subordinated debt ratings, to A3(hyb)/Baa1(hyb) from Baa1(hyb)/Baa2(hyb) respectively. Moody's changed the outlooks on these entities to stable from positive. At the same time, Moody's also affirmed the P-1 short-term IFSR of Compagnie Francaise d'Assurance pour le Comm. and the P-2 Commercial Paper short-term rating of Coface.

RATINGS RATIONALE

The rating action reflects the increasing diversification of the group and the enhanced monitoring and improved management of credit risk exposures, which Moody's expects to result in lower volatility in profits and make the insurer better placed to weather an economic downturn. The upgrade also reflects the good capitalisation level maintained by the group since 2020 and the improvement in asset quality.

Since the launch of its Build To Lead strategic plan in 2020, Coface has actively grown its services activity. Fees and revenues related to services (including factoring) increased by 11.5% in 2022 and a further 11.5% in the first half of 2023, despite a still relatively subdued level of activity in the debt collection business. Moody's expects the revenues from services to grow at a quicker pace than insurance premiums in the next 12-18 months, and the weight of services in overall revenues will gradually increase. Moody's considers the diversification in services activity as credit positive, as it constitutes a source of recurring revenues and profits with low volatility, and some of these service activities are also negatively correlated with the credit insurance business.

Coface's continued focus on underwriting discipline and enhanced exposure management is also a key driver for the rating action. Hence, while total trade credit insurance exposures increased by 42% between year-end 2020 and mid-year 2023, the average quality of exposures (based on Coface's internal scoring methodology) improved over the same period. In addition, as the macroeconomic environment deteriorates, Coface is becoming more strict on risk acceptance, and has already increased its number of actions to reduce or restrict growth in exposures to the most risky sectors or exposures.

This focus on risk exposure also enabled the group to maintain a Solvency II ratio consistently above 190% since 2020, despite the rapid growth in insured exposure.

Recent improvements in the group's asset quality also supported the group's good economic capital level. The group's high risk assets (Moody's definition) as a percentage of shareholders' equity improved to 25.5% as at year-end 2022, down from 41.0% as at year-end 2019. The improvement was driven by the sale of low quality corporate bonds before the pandemic and continued reinvestment in high quality sovereign bonds since 2022.

In addition, Coface’s profitability has been very strong in the last five years, with an average combined ratio of 71% between 2018 and 2022. However, Moody’s expects a deterioration in combined ratios for the credit insurance industry, as the rating agency forecasts an increase in the level of credit defaults while credit insurance pricing deteriorates slightly. Nonetheless, even if earnings volatility will remain a feature of the credit insurance industry, Moody's expects volatility to remain moderate, as Coface improved its risk monitoring processes and has been more proactive to adjust its risk portfolio since a spike in its loss ratio in Asia in 2016.

The stable outlook reflects Moody's expectation that Coface will maintain a Solvency II ratio above 180%, a leverage ratio below 30% and that the group will not increase meaningfully its underwriting or asset risk appetite.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

While unlikely in the next 12-18 months, Coface's ratings could be upgraded if (1) the group's capital increased sustainably leading to Solvency II ratio above 220% and a financial leverage at 20% or below, (2) the group's profitability improves with a combined ratio below 75% through the cycle, with moderate volatility and limited spikes during credit crisis, and (3) the group's business diversification further improves with fee-based services representing more than 30% of its revenues.

Conversely, the following factors could exert downward pressure on the ratings: (1) a volatile underwriting profitability, with for example a spike in the combined ratio materially above 100%, (2) a decline in capital, as evidenced for example by a Solvency II capital coverage below 180%, (3) a financial leverage consistently exceeding 30% or a significant increase in the group's operational debt, (4) a significant erosion of the group's market position and franchise or (5) a meaningful change in asset or underwriting risk appetite.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Trade Credit Insurers Methodology published in January 2023 and available at https://ratings.moodys.com/rmc-documents/397709. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody’s key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody’s Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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