FitchRatings

RATING ACTION COMMENTARY

# Fitch Affirms Coface at IFS 'AA-'; Outlook Stable

Wed 23 Nov, 2022 - 11:32 ET

Fitch Ratings - Paris - 23 Nov 2022: Fitch Ratings has affirmed Coface SA's operating entities' (together Coface) Insurer Financial Strength (IFS) Ratings at 'AA-'. Fitch has also affirmed Coface SA's Long-Term Issuer Default Rating (IDR) at 'A+'. The Outlooks are Stable. A full list of rating actions is below.

The affirmations reflect Coface's very strong company profile and capitalisation, as well as strong profitability through the cycle. The Stable Outlooks reflect our view that Coface continues to maintain sufficient rating headroom to weather rising corporate default risk in the current recessionary economic environment.

## KEY RATING DRIVERS

**Very Strong Company Profile:** Fitch ranks Coface's business profile as 'Favourable' compared with other global trade credit insurers due to its very strong, well established and diversified franchise in the global trade-credit insurance sector, where the group is the third-largest insurer, with an estimated 15% market share. We expect global economic slowdown to pressure revenue growth in the next 12-24 months. However, inflation is supportive of the company's growth in revenues, which are based on client turnover and therefore largely linked to inflation.

**Very Strong Capitalisation:** Fitch views Coface's capitalisation as 'Very Strong'. The Solvency II (S2) ratio was very strong at 192% at end-June 2022, (196% at end-2021), above the group's target of 155%-175%. We expect the S2 ratio to have increased at end-2022, partly driven by eligible debt issuance in September 2022.Net leverage (net premiums written + net insurance liability/ equity), an important capital adequacy ratio for trade-credit insurers, was 1.1x at end-2021 (1.0 at end-2020), which is consistent with both its five-year average and 'aa' rating guidelines. We forecast an increase of net leverage to around 1.4x at end-2022, driven by increased sales activity and slight erosion of the capital base.

Gross credit insurance risk exposure rose to an historical high of EUR642 billion at end-June 2022 (a 25% increase from the end-2020 trough). This is broadly consistent with earned premium, but the increase led to the highest Fitch-calculated net exposure to capital ratio of the last 10 years. Fitch believes that Coface maintained underwriting discipline, as reflected in the overall stable credit quality of the insured portfolio. We expect nominal gross exposure to diminish in 2023, given Coface's increasingly prudent stance in the current macro-economic context.

**Low Financial Leverage:** The financial leverage ratio (FLR), from which we exclude factoring assets, was broadly stable at 16% at end-2021 (end-2020: 17%). We estimate the FLR will have increased to around 20% at end-3Q22 as a result of the September issuance. This level remains consistent with Fitch's 'aa' category rating guidelines.

**Strong Financial Performance:** Fitch views Coface's financial performance as 'Strong' across the economic cycle, underpinned by underwriting profitability, effective risk management and reinsurance. Coface demonstrated resilient financial performance, particularly during the pandemic. The Fitch-calculated return on equity and reported combined ratio (CR) averaged 6.9% and 77.7%, respectively, over the past five years.

Coface reported very strong earnings at end-2021 and end-9M22, driven by strong revenue growth and subdued loss activity. The net CR slightly improved to 63.8% at end-September 2022 from 64.6% at end-2021 (79.8% at end-2020), which was better than peers. We expect the CR to normalise to the cycle's average of around 80% in the next 12 to 24 months, reflecting our expectation for rising claims activity in 2023 as the credit cycle turns, amid a soft pricing environment. Coface's exposure to Russia is limited, falling to EUR0.9 billion at end-September 2022 from EUR4.8 billion in February 2022.

## RATING SENSITIVITIES

**Factors that could, individually or collectively, lead to positive rating action/upgrade:**

-- An upgrade is unlikely in the medium term, given Coface's smaller size and lower product diversification than higher-rated insurers

**Factors that could, individually or collectively, lead to negative rating action/downgrade:**

-- A CR above 90% on a sustained basis

-- S2 ratio falling below 160% or net leverage increasing above 1.6x, both on a sustained basis

-- Deterioration in business profile, as reflected in a substantially weaker competitive position or higher business risks

### BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579

### REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

### ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

## RATING ACTIONS

| ENTITY / DEBT ⬍ | RATING ⬍ | PRIOR ⬍ |
| --- | --- | --- |

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|---|---|---|---|
| Coface Finanz GmbH | LT IDR | A+ Rating Outlook Stable Affirmed | A+ Rating Outlook Stable |
| COFACE SA | LT IDR | A+ Rating Outlook Stable Affirmed | A+ Rating Outlook Stable |
| | ST IDR | F1 Affirmed | F1 |
| subordinated | LT | A- Affirmed | A- |
| subordinated | LT | BBB+ Affirmed | BBB+ |
| senior unsecured | ST | F1 Affirmed | F1 |
| Coface North America Insurance Company (CNAIC) | Ins Fin Str | AA- Rating Outlook Stable Affirmed | AA- Rating Outlook Stable |
| Compagnie Francaise d'Assurance pour le Commerce Exterieur SA | LT IDR | A+ Rating Outlook Stable Affirmed | A+ Rating Outlook Stable |
| | Ins Fin Str | AA- Rating Outlook Stable Affirmed | AA- Rating Outlook Stable |
| | Ins Fin Str ST | F1+ Affirmed | F1+ |

**VIEW ADDITIONAL RATING DETAILS**

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## APPLICABLE CRITERIA

Insurance Rating Criteria (pub. 15 Jul 2022) (including rating assumption sensitivity)

## APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Prism Factor-Based Capital Model, v1.8.0 (1)

## ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

## ENDORSEMENT STATUS

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|---|---|
| Coface Finanz GmbH | EU Issued, UK Endorsed |
| Coface North America Insurance Company (CNAIC) | EU Issued, UK Endorsed |
| COFACE SA | EU Issued, UK Endorsed |
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