S&P Global Ratings

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Talanx Primary Insurance Group

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Talanx Primary Insurance Group

Anchor	a+
Business Risk	**Strong**
Competitive position	Strong
IICRA	Intermediate
Financial Risk	**Very Strong**
Capital and earnings	Very strong
Risk exposure	Moderately low
Funding structure	Neutral

\+

Modifiers	0
Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0

=

SACP	a+

\+

Support	0
Group support	0
Government support	0

=

Financial strength rating
A+/Stable/--

IICRA--Insurance Industry And Country Risk Assessment.
SACP--Stand-alone credit profile.

Credit Highlights

Overview

Strengths	Risks
Sound geographic and business-line diversification of premiums, complementing the domestic market position as one of the largest insurance groups in Germany.	Our belief that lower-for-longer yields will continue to erode investment returns.
Excellent capital adequacy, based on our internal risk-based capital model, supported by sound earnings despite pandemic claims.	Our view that business operations, while diverse, don't contribute equally to bottom-line results as earnings depend on retail international business and dividends from Hannover Re.
Improving technical profitability in all segments benefiting from lower pandemic claims and effective restructuring measures in industrial lines and retail Germany.	

S&P Global Ratings expects Talanx Primary Insurance Group (TPG) to maintain its position as one of the largest insurance groups in Germany. The Talanx group operates mainly in industrial lines, German retail, international retail, and reinsurance. TPG operates in the first three segments. Gross premiums from its primary operations were €17.3 billion in 2020, down about 1% compared with 2019 levels following lockdown measures and a stricter underwriting focus in the German motor segment. The negative impact was partly offset by strong growth mainly in the commercial specialty business. For 2021, we expect premiums will increase 4%-7% driven by the global economic recovery.

Pandemic-induced losses and weaker economic conditions affected 2020 earnings; however, we expect a recovery in 2021. In 2020, the group generated net income of €698 million, affected by pandemic-related claims and reserving, especially in the industrial lines business. Furthermore, the group's investment returns were lower than that of the previous year due to the low interest rates. With improved economic conditions and stronger results in all lines of the business despite the large floods in Europe, we expect return on equity to improve to 6%-8% over the next two years.

Capital and earnings will remain very strong and protected by sound risk controls. We continue to assess TPG's capital adequacy at the 'AAA' level, based on our internal risk-based capital model. The group's regulatory solvency ratio was also solid at the end of June-2021, at 210% excluding transitional measures. The group's ample capital base and successful risk controls will likely mitigate capital volatility, enabling TPG to cope with further market volatility and possible large man-made losses or natural catastrophe events. We believe that capitalization will remain in 2021 and 2022 at least in the 'AA' range despite the group's growth ambitions and its exposure to tail risks like natural catastrophes or pandemics.

Outlook: Stable

The outlook is stable because we believe that the group will maintain its competitive strength, based on its strong business and regional diversification over our 2021-2023 forecast horizon. We expect earnings to improve in 2021 following lower pandemic-related losses and a still-favorable claims environment in the retail business, supporting our expectation that the company will maintain at least very strong capital and earnings.

Downside scenario

We would consider taking a negative rating action on TPG over the next 24 months if the company's capital and earnings sustainably weakened to lower than very strong. This could occur if significantly higher insurance losses led to markedly lower earnings than we anticipate in our base-case scenario, or capital needs increase higher than expected.

Upside scenario

We view a positive rating action as a remote possibility over the next 24 months. However, one could occur if TPG further and significantly diversifies its earnings base by geography in its industrial and retail insurance business. This would also require a continued improvement of its German retail and industrial lines operations.

Key Assumptions

- Germany GDP increase of 3.5% in 2021 with a further increase of 4.9% in 2022.
- Ten-year government bond yields in Germany to remain negative at about negative 0.14% in 2021, gradually improving to positive 0.12% in 2022.

Talanx Primary Insurance Group--Key Metrics

	2022f	2021f	2020	2019	2018	2017	2016
S&P Global Ratings capital adequacy	Excellent	Excellent	Excellent	Excellent	Excellent	Excellent	Excellent
Gross premium written* (mil. €)	>19,000	18,000-18,500	17,341	17,536	15,270	14,803	14,225
Net income (mil. €)	>800	>800	698	958	703	729	895
Return on shareholders' equity (%)	~6-8	~6-7	5.5	8.3	6.6	6.9	9.0
Financial leverage (%)	<30	<30	24.3	24.9	25.7	22.8	19.8
EBITDA fixed charge coverage (x)	~7-9	~7-9	5.2	7.8	7.0	6.6	7.6

Talanx Primary Insurance Group--Key Metrics (cont.)							
	2022f	**2021f**	**2020**	**2019**	**2018**	**2017**	**2016**
Financial obligation/EBITDA	~2-3	~3-6	3.4	2.4	2.6	2.3	1.5
Net investment yield (%)	~3.0-3.2	~3.1-3.3	3.3	3.8	3.5	4.1	3.5
P/C net combined ratio (%)	~95-98	~95-98	98.4	97.8	100.0	101.0	97.7
Return on revenue (%)	N.A.	N.A.	5.3	7.3	5.7	5.9	4.6

*Excluding saving parts. f--S&P Global Ratings forecast. N.A.--Not available.

Business Risk Profile: Strong

In our view, TPG benefits from its strong market position in Germany and its diverse set of international business portfolio offering life and property/casualty (P/C) insurance through its defined segments. Although the group benefits from strong premium diversification across segments and regions, this has not yet fully translated into broad earnings' diversity.

In 2020, gross premiums written (excluding saving parts) from primary operations declined to €17.3 billion from €17.5 billion due to pandemic-induced weaker economic conditions, negative currency effects in the international business and a decline in bancassurance operations following lockdowns. For 2021-2022, we expect premium growth to recover in light of improving economic conditions and mobility constraints, increasing 4%-7% with support from all segments. Half-year 2021 numbers support our estimation, as gross premiums in industrial lines increased by 9% mainly driven by its specialty, liability, and property operations. In retail Germany, half-year premiums increased by 3% in P/C and life. A strong increase in the P/C small and midsize operations of 11% was partly offset by a decline in motor premiums of 8%. Life premiums in Germany increased by 3%, especially in the bancassurance segment, because this distribution channel was heavily affected in 2020 via pandemic-related containment measures. Premiums in retail international increased by 11% supported by an increase of 8% in P/C and 17% in life. The strong life increase was influenced by high single premium contracts in Italy and strong growth in Poland, whereas P/C growth was mainly driven by nonmotor operations. We observe some growth challenges in the Latin America business, especially in Brazil, as foreign currency effects and an uncertain economic development weight on premiums. In the first six months of 2021, premium declined by 0.5%. However, the low premium volume in the Brazilian operations could partly be offset by positive developments in Chile and Mexico. In contrast, half-year figures showed strong growth in the European operation of 14.5% compared with the first six month in 2020.

In terms of earnings diversification, TPG still relies strongly on earnings from the retail international segment and dividends from Hannover Re, which together we expect to contribute more than 70% of 2021 net earnings. Nevertheless, restructuring measures in retail Germany and industrial lines are bearing fruits gaining weight of TPG's earnings and we expect that the trend will continue.

Financial Risk Profile: Very Strong

At year-end 2020, TPG holds a comfortable capital buffer above in 'AAA' range as per our analysis of our risk-based capital model, despite the group's exposure to large losses such as natural catastrophes and the pandemic.

Furthermore, the regulatory capital remained securely above the group target of 150%-200%. The regulatory solvency ratio was 206% in 2020 and 210% as of June 30, 2021, without including transitional measures which further supports our view of TPG's capital position. Over the forecast period, we expect the company to maintain capital adequacy at least above 'AA' range.

Our prospective capital view is based on our estimation of TPG's net profit of more than €800 million in 2021 and 2022 recovering from pandemic-affected earnings in 2020. We expect earnings in 2021 to be affected by high natural catastrophe and large manmade claims, mainly offset by lower pandemic-related losses. We believe that the claims frequency, especially in the international business, will normalize over the next 24 months, having some impact on technical results. However, improvements in underlying technical results reflecting the implementation of restructuring measures in industrial lines and retail Germany will further materialize leading to a combined ratio of 95%-98% for 2022.

We base our earnings expectation on normalized large loss and natural catastrophe claims not exceeding the group's budget. Losses from storm Bernd at the beginning of the second half of the year are material on a gross basis, but the strong reinsurance protection reduced the net exposure remaining within TPG's budget. Still, we believe that further large claims might add volatility on results, especially in the industrial lines segment.

We believe that lower-for-longer yields will continue to erode investment returns in the medium term. Therefore, we assume net investment yield to decrease to 3.1%-3.3% in 2021 and to 3.0%-3.2% in 2022.

We believe TPG follows a balance and conservative investment strategy. The asset allocation is heavily geared toward fixed-income investments, which account for more than 80% of the total. Moreover, the broad geographic business diversification and sound risk controls make the group relatively resilient against capital and earnings volatility. In our view, potential volatility might result from large losses, such as natural catastrophes. However, we believe that the risk is mitigated by a sound reinsurance protection and conservative natural catastrophe and other large loss budgeting.

TPG has demonstrated its access to ample sources of external funding, including equity, reinsurance, or debt markets, and we expect this to continue. At year-end 2020, the group's financial leverage ratio (debt plus hybrids to shareholders equity, and consolidating the Hannover Re subgroup) was 24.3%, while fixed-charge coverage stood at 5.2x despite a drop in earnings in 2020. Based on our capital and earnings forecast and assuming no major change in TPG's capital management approach, we expect financial leverage to remain below 30% and fixed-charge coverage ratio to be 7x-9x in 2021-2022.

Other Key Credit Considerations

Liquidity

We expect TPG's liquidity to remain exceptional over the next two years. The group has ample liquidity sources available, mainly premium income and a highly liquid asset portfolio. Moreover, there are no refinancing risks, in our view.

Factors specific to the holding company

The ratings on Talanx AG, the group's operating holding company, are equalized with those on TPG's core entities due to its role within the wider group as internal reinsurer, further enhancing the diversity of its cash flow and its ability to honor financial obligations. Furthermore, Talanx AG benefits from substantial levels of excess capital and a moderate level of financial leverage.

Group support

Our assessment of Hannover Re reflects the group's stand-alone characteristics. The group is 50.2%-owned by ultimate parent Talanx AG, while the remainder of its shares are widely held. We understand that Hannover Re's strategy, capital management, and cash flow are independent from Talanx AG. However, we believe there is a strategic alignment between the two groups, indicated by the joint venture in the industrial specialty business.

Environmental, social, and governance

We consider TPG's exposure to environmental and social risks as on par with that of the insurance sector globally, and of peers such as Mapfre and Allianz. Standards for corporate governance are typically high in Germany and in many of the other countries where TPG has material exposure. The group has three business segments in the primary insurance segment and a majority shareholding in Hannover Re. Much of TPG's exposure to environmental factors stems from its industrial lines sector. For example, climate change could increase the frequency and severity of claims from extreme weather events, including natural catastrophes. However, we believe TPG has contained the risk through sound reinsurance protection and conservative natural catastrophe and other large-loss budgeting--its budget for this was €370 million in 2021. TPG's life operations are exposed to social factors such as demographic trends relating to improved longevity or rising chronic diseases. These trends could increase liabilities, especially in Germany. Nevertheless, this is a common problem for life insurers. TPG's diversification by business line and the variety of life insurance products it offers mitigates the risks.

We do not foresee any material governance issues that could affect the ratings. We believe the group can implement its management succession plans with internal and external resources, as demonstrated in recent years. We think that the management team has a consistent track record of strategic planning, strong execution, and transparent, demanding, and sophisticated financial management.

Accounting considerations

We mainly base our assessment of TPG on its annual financial statements, including the mutual parent HDI Haftpflichtverband der Deutschen Industrie V.a.G., where we focus on the three primary insurance segments: German retail, international retail, and industrial lines, supplemented by nonpublic information on the life and P/C operations and a consolidated view on TPG including corporate operations. Our assessment of financial flexibility relies on the consolidated HDI Group figures rather than on TPG data only. In our ratings on domestic and nondomestic subsidiaries of HDI Group, we base our analysis on annual reports under local generally accepted accounting practices and International Financial Reporting Standards.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- Criteria | Insurance | Property/Casualty: Assessing Property/Casualty Insurers' Loss Reserves, Nov. 26, 2013
- 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

Appendix

Talanx Primary Insurance Group--Credit Metrics History

(Mil. €)	2020	2019	2018	2017
S&P Global Ratings capital adequacy*	Extremely strong	Extremely strong	Extremely strong	Extremely strong
Total invested assets	103,557	98,899	89,739	88,923
Total shareholder equity	13,015	12,459	10,650	10,532
Gross premiums written	17,341	17,536	15,270	14,803
Net premiums written	13,075	13,736	12,662	12,182
Net premiums earned	12,835	13,329	12,317	11,843
Reinsurance utilization (%)	24.6	21.7	17.1	17.7
EBIT	883.1	1,242.0	902.3	929.1
Net income (attributable to all shareholders)	698.4	957.7	702.6	728.8
Return on revenue (%)	5.3	7.3	5.7	5.9
Return on assets (excluding investment gains/losses) (%)	0.8	1.2	0.9	1.0
Return on shareholders' equity (reported) (%)	5.5	8.3	6.6	6.9
P/C: net combined ratio (%)	98.4	97.8	100.0	101.0
P/C: net expense ratio (%)	26.9	28.1	27.6	28.5
P/C: return on revenue (%)	4.4	5.8	3.9	4.8
Net investment yield (%), including all gains	3.3	3.8	3.5	4.1

Business And Financial Risk Matrix

Business risk profile	Financial risk profile							
	Excellent	**Very Strong**	Strong	Satisfactory	Fair	Marginal	Weak	Vulnerable
Excellent	aa+	aa	aa-	a+	a-	bbb	bb+	b+
Very Strong	aa	aa/aa-	aa-/a+	a+/a	a-/bbb+	bbb/bbb-	bb+/bb	b+
Strong	aa-/a+	**a+/a**	a/a-	a-/bbb+	bbb+/bbb	bbb-/bb+	bb/bb-	b+/b
Satisfactory	a	a/a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bb+/bb	bb-/b+	b/b-
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb/bb-	b+/b	b-
Weak	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b/b-	b-
Vulnerable	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b+/b	b/b-	b-	b-

Note: Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

Ratings Detail (As Of October 18, 2021)*

Holding Company: Talanx AG	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	A+/Stable/--
Senior Unsecured	A+
Operating Companies Covered By This Report	
HDI Haftpflichtverband der Deutschen Industrie V.a.G.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
HDI Global Insurance Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
HDI Global Network AG	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
HDI Global SE	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	A+/Stable/--
HDI Global Specialty SE	
Financial Strength Rating	
Local Currency	A+/Stable/--

Ratings Detail (As Of October 18, 2021)*(cont.)	
Issuer Credit Rating	
Local Currency	A+/Stable/--
HDI Lebensversicherung AG	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	A+/Stable/--
HDI Versicherung AG (Germany)	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
neue leben Lebensversicherung AG	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
PB Lebensversicherung AG	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
TARGO Lebensversicherung AG	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Towarzystwo Ubezpieczen i Reasekuracji WARTA S.A.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
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.