

Research Update:

Santam Ltd. 'BB+' Ratings Affirmed; Outlook Stable; Group Status On Santam SI Revised To Highly Strategically Important

April 26, 2019

Overview

- Santam has demonstrated stable and improved operating results in 2018 benefiting from its leading position in the South African non-life insurance market. This will be further supported by its increasing presence in the rest of Africa and diversified revenue streams.
- We think management's actions should maintain operating earnings and strengthen the overall financial risk profile in line with our expectation over the medium term. However, we continue to view Santam's level of capital adequacy as an innate weakness to the rating.
- Santam continues to pass our stress test and, considering its board-approved risk mitigation plan, we rate Santam above the foreign currency sovereign rating on South Africa (BB/Stable), and at the level of our local currency sovereign rating on the country (BB+/Stable).
- We are therefore affirming our 'BB+' global scale rating and 'zaAAA' national scale rating on Santam.
- The stable outlook reflects our outlook on the sovereign rating, and our belief Santam will continue to post solid operating performance in South Africa and maintain capital adequacy and enterprise risk management practices at least in line with current levels.

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Rating Action

On April 26, 2019, S&P Global Ratings affirmed its 'BB+' global scale long-term issuer credit and financial strength ratings on insurer Santam Ltd. The outlook on the global scale ratings remains stable.

At the same time, we affirmed our 'zaAAA' South Africa national scale rating on Santam. We also affirmed our 'zaAA-' South Africa national scale rating on the subordinated deferrable hybrid instruments issued by Santam.

We affirmed our 'BB' ratings on Santam SI's core operating subsidiaries: Santam Structured Insurance Ltd., Santam Structured Reinsurance Ltd. PCC, and Santam Structured Reinsurance

dac. At the same time, we affirmed our 'zaAA+' South Africa national scale rating on Santam Structured Insurance Ltd.

Rationale

We continue to rate Santam above the level of our foreign currency sovereign rating on South Africa. We believe the insurer would be able to withstand the stress associated with a South African default on its foreign currency obligations, based on Santam's asset and regulatory capital base. We assume that group capital funds are fully fungible through the group and could be used in the event of capital stress. Our view is supported by Santam's execution of its credible and board-approved risk mitigation plan.

We also continue to limit the ratings on Santam at the level of our local currency sovereign credit rating on South Africa. We believe the insurer remains susceptible to the incremental adverse effect that a default of the sovereign's local currency securities would have on its liquidity and investment position, given its asset concentration to local investment assets.

We assess Santam's stand-alone credit profile (SACP), before the consideration of the sovereign risk (that is, the indicative SACP), at 'bbb', above the current ratings. The indicative SACP benefits from Santam's leading and profitable position in the South African insurance market and our view of its strong enterprise risk management. We consider its strategic investments within and beyond the South African border support its dominant position.

We continue to view Santam's risk-based capital levels as measured by our model as a weakness to the overall rating. Capital sufficiency remains at the lower end of the 'BBB' level due to balance sheet expansion through acquisition and investment activity.

We expect Santam to post premium growth of around 8% per year over the next 24 months and maintain its underwriting performance. We expect it will post a combined (loss and expense) ratio of below 95%, supported by its diversified portfolio. We anticipate that annual operating profits will be at least South African rand (ZAR) 1.2 billion over the same period. We do not expect acquisitions or dividend payments to further strain capital adequacy.

We now assess Santam SI Investments Group (Santam SI) as a highly strategically important subgroup for Santam, revised upward from a strategically important subgroup. This is due to Santam's senior management's strong support and involvement in operational and financial decision-making at Santam SI as it has been integrated into the wider group. This is further reinforced by the increasing role Santam SI plays within Santam's broader group strategy, its contribution toward the diversified revenue streams, and shared branding. We therefore affirmed our ratings on Santam SI's core operating subsidiaries, Santam Structured Insurance Ltd., Santam Structured Reinsurance Ltd. PCC, and Santam Structured Reinsurance dac. The rating on Santam SI is one notch below Santam's group credit profile of 'bb+'.

Outlook

The stable outlook on Santam reflects our outlook on South Africa because the ratings on Santam are constrained at the level of the long-term local currency rating on the sovereign. This also incorporates our view that its capital adequacy will remain in line with current levels as per our capital model, while its enterprise risk management practices will remain strong. We also take into account that Santam will continue to execute its risk mitigation plan.

Downside scenario

We could lower the ratings on Santam over the next 12 months if:

- We were to lower our local currency sovereign rating on South Africa;
- Santam stopped effectively implementing its risk mitigation plan and therefore failed our sovereign stress test; or
- Santam's capital adequacy and risk management practices were to weaken below current levels.

Upside scenario

We would only raise the ratings on Santam if we took a similar action on the local currency sovereign rating on South Africa.

Ratings Score Snapshot

Santam Ltd. Ratings Score Snapshot

	To	From
Financial Strength Rating	BB+	BB+
Anchor	bbb-	bbb-
Business Risk Profile	Satisfactory	Satisfactory
IICRA	Moderate	Moderate
Competitive Position	Strong	Strong
Financial Risk Profile	Less than adequate	Less than adequate
Capital and Earnings	Lower adequate	Lower adequate
Risk Position	Moderate	Moderate
Financial Flexibility	Adequate	Adequate
Modifiers	1	1
ERM and Management	1	1
Enterprise Risk Management	Strong	Strong
Management and Governance	Satisfactory	Satisfactory
Holistic Analysis	0	0
Liquidity	Strong	Strong
Group Support	0	0
Government Support	0	0

IICRA--Insurance Industry And Country Risk Assessment.

Santam Operating Subsidiaries Ratings Score Snapshot

	To	From
Financial Strength Rating	BB/Stable/--	BB/Stable/--
Anchor	bb+	bb+
Business Risk Profile	Fair	Fair
IICRA	Moderate	Moderate
Competitive Position	Adequate	Adequate
Financial Risk Profile	Less than adequate	Less than adequate
Capital and Earnings	Moderately Strong	Moderately Strong
Risk Position	Moderate	Moderate
Financial Flexibility	Adequate	Adequate
Modifiers	0	0
ERM and Management	0	0
Enterprise Risk Management	Adequate	Adequate
Management and Governance	Fair	Fair
Sovereign Risk	-1	-1
Liquidity	Exceptional	Exceptional
Group Support	0	0
Government Support	0	0

IICRA--Insurance Industry And Country Risk Assessment.

Related Criteria

- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, 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
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria | Insurance | General: Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

Ratings List

Ratings Affirmed

Santam Ltd.

Issuer Credit Rating	
Local Currency	BB+/Stable/--
South Africa National Scale	zaAAA/--/--
Financial Strength Rating	
Local Currency	BB+/Stable/--

Santam Ltd.

Subordinated	zaAA-
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Santam Structured Insurance Ltd.

Santam Structured Reinsurance Ltd. PCC

Santam Structured Reinsurance DAC

Issuer Credit Rating	
Local Currency	BB/Stable/--

Santam Structured Insurance Ltd.

Financial Strength Rating	
Local Currency	zaAA+/--/--

Santam Structured Insurance Ltd.

Santam Structured Reinsurance DAC

Santam Structured Reinsurance Ltd. PCC

Financial Strength Rating	
Local Currency	BB/Stable/--

Regulatory Disclosures(Santam Ltd.)

- Primary Credit Analyst: Trevor Barsdorf, Associate
- Rating Committee Chairperson: Marc-Philippe Juilliard
- Date initial rating assigned: Oct. 10, 2012
- Date of previous review: July 2, 2018

Regulatory Disclosures(Santam Structured Insurance Ltd., Santam Structured Reinsurance DAC, Santam Structured Reinsurance Ltd. PCC)

- Primary Credit Analyst: Trevor Barsdorf, Associate
- Rating Committee Chairperson: Marc-Philippe Juilliard
- Date initial rating assigned: May 24, 2017

- Date of previous review: July 2, 2018

Disclaimers

This rating has been determined by a rating committee based solely on the committee's independent evaluation of the credit risks and merits of the issuer or issue being rated in accordance with S&P Global Ratings published criteria and no part of this rating was influenced by any other business activities of S&P Global Ratings.

This credit rating is solicited. The rated entity did participate in the credit rating process. S&P Global Ratings did have access to the accounts, financial records and other relevant internal, non-public documents of the rated entity or a related third party. S&P Global Ratings has used information from sources believed to be reliable but does not guarantee the accuracy, adequacy, or completeness of any information used.

Glossary

- Anchor: The starting point for rating an insurer, based on S&P Global Ratings' assessments of the business and financial risk profiles.
- Business risk profile (BRP): Assesses the risk inherent in the insurer's operations and therefore the potential sustainable return to be derived from those operations.
- Capital and earnings: Measure of an insurer's ability to absorb losses.
- Combined ratio: The ratio of the sum of loss expense, loss adjustment expense, and operating expenses divided by premiums earned.
- Competitive position: An assessment based on an insurer's operating performance, branding, market position, diversification and control over its distribution channels.
- Date initial rating assigned: The date S&P Global Ratings assigned the long-term foreign currency issuer credit rating on the entity.
- Date of previous review: The date S&P Global Ratings last reviewed the credit rating on the entity.
- Enterprise risk management (ERM): Our assessment of ERM examines whether insurers execute risk management practices in a manner that effectively limits future losses.
- Financial flexibility: The balance between an insurer's sources and uses of external capital and liquidity over the current and next two years.
- Financial risk profile (FRP): The consequence of decisions that management makes in the context of its business risk profile and its risk tolerances.
- Financial strength rating (FSR): A forward-looking opinion about the financial security characteristics of an insurer with respect to its ability to pay under its insurance policies and contracts, in accordance with their terms.
- High-risk assets: Volatile or illiquid assets.
- Insurance Industry And Country Risk Assessment (IICRA): Addresses the risks typically faced by insurers operating in specific industries and countries, and is generally determined at a country or regional level.

- Issuer credit rating (ICR): A forward-looking opinion about an obligor's overall creditworthiness, focusing on its capacity and willingness to meet its financial obligations in full and as they come due.
- Risk position: Assesses material risks not incorporated in the capital and earnings analysis and specific risks that could affect the volatility of an insurer's TAC.
- Return on equity (ROE): Measures the return available to stockholders. Calculated as reported net income divided by the year-end average of reported stockholders' equity for the past two years.
- Stand-alone credit profile (SACP): S&P Global Ratings' opinion of an insurer's creditworthiness, in the absence of extraordinary intervention from its parent, affiliate, or related government.
- Total adjusted capital (TAC): S&P Global Ratings' measure of the capital an insurer has available to meet capital requirements.

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