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Vienna Insurance Group

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Vienna Insurance Group

SACP* Assessments				SACP*		Support		Ratings
Anchor	aa-	+ Modifiers	-1	= a+		+ 0		= Financial Strength Rating
Business Risk		ERM and Management	0	Liquidity	0	Group Support	0	A+/Stable/--
Very Strong								
Financial Risk		Holistic Analysis	-1	Sovereign Risk	0	Gov't Support	0	
Very Strong								

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

Rationale

Business Risk Profile: Very Strong

- We view the group's competitive position as very strong, based on leading market positions in Austria and Central and Eastern Europe.
- The group has sound diversification by business line and a well-established multichannel distribution strategy including exclusive distribution with Austrian bank Erste Group.
- We think earnings will recover to strong levels in 2014-2016 after a drop in 2013 owing to the Romanian and Italian businesses.

Financial Risk Profile: Very Strong

- Capital adequacy is excellent, exceeding our benchmark for the 'AAA' level in 2013.
- We anticipate that capital will remain at least very strong in 2014-2016, based on strong earnings that will be sufficient to finance growth and dividend expectations.
- We assess risk position as intermediate based on the group's conservative investment portfolio and comprehensive reinsurance coverage.

Other Factors

- Our views of Vienna Insurance Group's business risk and financial risk profiles lead us to apply an anchor of 'aa-' to the group. The ratings are one notch lower than the anchor, however, because we factor in a one-notch negative adjustment for our holistic analysis. This reflects our view of the group's lower geographic earnings diversification than its higher rated European peers and the need to rebuild a sustainable track record of strong operating performance after the fall in 2013 earnings.

Factors Specific to the Holding Company

- Vienna Insurance Group AG Wiener Versicherung Gruppe is the ultimate holding company for the Vienna Insurance Group's operating entities, and itself writes internal reinsurance and international corporate and large customer business. Based on our assessment of the company as an operating holding company with sizable excess capital at holding level, sound revenues from own activities like internal reinsurance and corporate business, and comparatively low financial leverage, we apply a non-standard zero-notch differential to the ratings relative to those on the group's rated core operating subsidiary.

Outlook: Stable

The stable outlook on Austrian multiline insurer Vienna Insurance Group AG (VIG) reflects our view that the group will sustain its very strong competitive position in its home market and its leading market position in Central and Eastern Europe (CEE). We think VIG will achieve the strong earnings we foresee in our base case for 2014-2016, recovering from the drop in 2013 earnings. We also consider that it will likely maintain very strong capital adequacy despite needs arising from business growth and dividend payments.

Downside scenario

We could take a negative rating action if:

- VIG's competitive position deteriorated in its domestic market or in CEE; or
- Its operating performance did not meet our base-case earnings assumptions in 2014-2016; or
- Its capital adequacy fell significantly below very strong levels for a prolonged period, possibly as a result of deteriorating credit conditions in CEE.

Upside scenario

We see limited rating upside in the next 18-24 months. However, we could take a positive rating action if:

- VIG further diversified its geographic earnings base, significantly and sustainably;
- Operating performance consistently remained at the higher end of our expectations, with no unexpected one-off large losses; and
- Capital adequacy sustainably exceeded the level for an 'AA' rating.

Base-Case Scenario

Macroeconomic Assumptions

- Credit market conditions in Europe will likely improve slightly on the back of stabilizing economic growth.
- The Austrian 10-year government yield will likely remain low over the next two years.
- We think economic growth in the CEE region will remain moderate, leading to good but not excessive organic growth opportunities.

Company-Specific Assumptions

- Capital adequacy should remain at least in the 'AA' range.
- Net income will likely exceed €400 million in 2014-2016, with return on equity of 7%-9%.
- We think VIG will maintain its leading market positions in Austria and its key CEE markets.
- We anticipate a net combined ratio, the industry's main measure of profitability, in the 95%-98% range in 2014-2016.
- A life/health new business margin of 3.5%-4.0%.
- Fixed-charge coverage of 7%-9% and financial leverage at less than 20%.

Key Metrics

	2015f	2014f	2013	2012	2011
Gross premiums written (mil. €)	about 9,400	about 9,300	9,219	9,646	8,884
Net income (mil. €)	>400	>400	256.4	444.9	441.9
Return on shareholders' equity (%)	7-9	7-9	4.8	8.3	8.8
Property/casualty: Net combined ratio (%)	95-98	95-98	99.3	93.9	93.9
Life: New business margin (%)	3.5-4.0	3.5-4.0	4.1	4.3	5.5
Net investment yield (%)	3.5-3.8	3.5-3.8	3.8	4.0	4.4
S&P capital adequacy	Very strong	Very strong	Extremely strong	Very strong	Very strong
Fixed-charge coverage	7-9	7-9	7.0	8.4	8.6
Financial leverage	<20	<20	17.3	15.5	16.0

f--Standard & Poor's forecast.

Company Description

VIG is the leader in insurance markets in Austria and holds leading positions in CEE, notably in the Czech Republic, Slovakia, Poland, and Romania, writing life, non-life, and health business through various recognized brands. Overall, the group reported gross premiums written of €9.2 billion in 2013, split between property/casualty, 50%; life, 46%; and health, 4%. Austria contributed 44% to total premium income in 2013, with the remaining 56% generated outside Austria, including 20% from the Czech Republic, 12% from Poland, and 9% from Slovakia.

VIG's ultimate majority owner is mutual insurer WIENER STÄDTISCHE WECHSELSEITIGER VERSICHERUNGSVEREIN – VERMÖGENSVERWALTUNG – Vienna Insurance Group (Wiener SWVV; not rated), which currently owns about 70% of VIG. The remaining shares are free float.

Business Risk Profile: Very Strong

Insurance industry and country risk: Intermediate based on diversified geographic presence

VIG faces intermediate industry and country risk, in our view. It has built up a diverse business portfolio, including a leading market position in its domestic Austrian market (property/casualty [P/C] including health, 24% of VIG's total premiums in 2013; life 20%) and leading positions in its main CEE markets, notably the Czech Republic (P/C 10%; life 10%), Poland (P/C 6%, life 6%), Slovakia (P/C 4%; life 5%), and Romania (P/C 3%; life 1%).

We believe that VIG's Austrian P/C and life business is exposed to low risk, reflecting our view of high barriers to entry, a neutral view of product risk in P/C, and high product risk in life. The latter is predominantly because of long-term policyholder guarantees in insurers' traditional products, which create a duration mismatch risk relative to shorter-duration assets, particularly in a low interest rate environment. In the Czech Republic, VIG faces intermediate risk in P/C and life, and in Poland, this risk is moderate. We believe our overall industry and country risk assessment will remain unchanged in 2014-2016, although we anticipate greater growth potential and selectively higher risk in the CEE region compared with the domestic market.

Table 1

Vienna Insurance Group Industry And Country Risk

Insurance sector	IICRA	Business mix (%)
Austria Life	Low	20
Austria P/C	Low	24
Czech Republic Life	Intermediate	10
Czech Republic P/C	Intermediate	10
Poland Life	Moderate	6
Poland P/C	Moderate	6
Turkey P/C	Moderate	1
Germany P/C	Low	1
Germany Life	Intermediate	1
Other markets	Moderate	21
Weighted average IICRA	Intermediate	100

IICRA--Insurance Industry And Country Risk Assessment. P/C--Property/casualty.

Competitive position: Very strong based on leading positions in Austria and CEE

In our view, VIG has a very strong competitive position, mainly reflecting the group's leading positions in life and non-life insurance in Austria and CEE. We believe the group's multibrand policy, multiple distribution capabilities, and broad geographic and business line (P/C 50% of total premiums in 2013, life 46%, health 4%) diversity are strong market credentials. We also believe that its exclusive bancassurance cooperative agreement with Erste Group Bank AG (Erste Group; A/Watch Neg/A-1) is a competitive advantage in Austria and particularly in CEE.

The decline in total earnings to about €355 million pretax in 2013, owing to the Romanian and Italian P/C businesses, is a setback, in our view, to the group's strong track record. Any further unexpected material one-off losses in the group's main markets could weigh unfavorably in our assessment of its very strong competitive position. We believe that the restructuring measures including tariff increases, claims handling initiatives, and portfolio rebalancing will need full management attention in 2014 and beyond. We think VIG has taken most of the one-time losses and restructuring measures related to its Romanian and Italian businesses in 2013. Under our base-case assumptions in 2014-2016, we believe VIG will recover strong operating performance in line with levels in 2009-2012. This is against the continued low interest rate environment and our assumption of declining net investment yields for VIG in the 3.5%-3.8% range in 2014-2016.

We expect VIG to defend its leading position in Austria and CEE in 2014-2016 by leveraging its existing operations and through potential mergers and acquisitions in CEE if opportunities arise.

Despite the diversification in VIG's operations, the Austrian and Czech markets mainly fuel group earnings, in our view. We think the group still has progress to make in diversification of earnings streams from other CEE operations.

Table 2

Vienna Insurance Group Competitive Position					
	--Year ended Dec. 31--				
(Mil. €)	**2013**	**2012**	**2011**	**2010**	**2009**
Gross premiums written	9,219	9,646	8,884	8,593	8,019
Change in gross premiums written (%)	(4.4)	8.6	3.4	7.2	1.5
Net premiums written	8,445	8,935	8,145	7,871	7,288
Change in net premiums written (%)	(5.5)	9.7	3.5	8.0	3.5
Total assets under management*	36,511	36,571	34,047	33,915	30,883
Growth in assets under management (%)	(0.2)	7.4	0.4	9.8	7.8
Reinsurance utilization (%)	8.4	7.4	8.3	8.4	9.1
Business segment (% of gross premiums written)					
Life	45.6	47.5	44.4	45.4	43.5
Property/casualty	50.1	48.4	51.5	50.6	52.5
Health	4.3	4.1	4.1	3.9	4.0

*Excluding third-party assets under management.

Financial Risk Profile: Very Strong

Capital and earnings: Very strong

We assess VIG's capital and earnings as very strong. Capital adequacy in 2013 exceeded our benchmark for the 'AAA' rating, benefitting from a successful €500 million hybrid issue, a moderate decline in premiums, a continued conservative investment strategy, and earnings retention after dividends of about €100 million. We assume under our base case that VIG will at least maintain capital adequacy in excess of our benchmark for the 'AA' rating in 2014-2016. We assume that VIG's earnings of more than €400 million in 2014-2016 will continue to support this very strong position, while the group finances its growth and expected dividend outflows.

Table 3

Vienna Insurance Group Capital					
	--Year ended Dec. 31--				
(Mil. €)	**2013**	**2012**	**2011**	**2010**	**2009**
Common equity	5,020	5,689	5,050	5,030	4,629
Change in common equity (%)	(11.8)	12.7	0.4	8.7	11.8
Total capital (reported)	7,259	7,952	8,282	7,963	7,012
Change in total capital (reported) (%)	(8.7)	(4.0)	4.0	13.6	11.2

Table 4

Vienna Insurance Group Earnings					
	--Year ended Dec. 31--				
(Mil. €)	**2013**	**2012**	**2011**	**2010**	**2009**
Total revenues*	9,797	10,319	9,542	9,208	8,539
EBIT adjusted§	300	525	902	617	703
Net income	256	445	442	413	364
Return on shareholders' Equity (reported) (%)	4.8	8.3	8.8	8.6	8.3
P/C: Net expense ratio (%)	29.9	28.0	28.1	28.7	28.2
P/C: Net loss ratio (%)	69.0	65.3	65.5	66.1	64.5
P/C: Net combined ratio (%)	99.3	93.9	93.9	95.6	93.4
P/C: Return on revenue (%)	1.0	7.6	10.3	8.6	5.2
Life: Net expense ratio (%)	15.6	14.1	16.1	17.4	18.5
Life: Value of new business	159	204	195	193.9	133.1
Life: New business margin (%)	4.1	4.3	5.5	5.3	4.3
Operating earnings by segment					
Life & health	297.9	232.8	287.5	285.1	202.4
Non-life	57.3	330.9	271.5	222.7	238.9
Other	0	0	0	0	0

*Reported, including unit-linked products. §Excluding (un)-realized capital gains/losses. P/C--Property/casualty.

Risk position: Intermediate

In our view, VIG's risk position reflects intermediate risks, based on its conservative investment strategy and sufficient reinsurance cover against the group's natural catastrophe exposure in Austria and CEE. About 75% of its investments comprise fixed-income securities with an average rating of 'A' in the bond portfolio. Moreover, VIG's equity and alternative investment exposure, about 4% at year-end 2013, is relatively low compared with peers, in our view. Although VIG is exposed to natural catastrophes in Austria and CEE, we believe its comprehensive reinsurance cover significantly reduces the group's net exposure.

Table 5

Vienna Insurance Group Risk Position					
	--Year ended Dec. 31--				
(Mil. €)	**2013**	**2012**	**2011**	**2010**	**2009**
Total invested assets	36,511	36,571	34,047	33,915	30,883
Net investment income	1,130	1,186	1,258	1,207	1,189
Net investment yield (%)	3.8	4.0	4.4	4.4	4.6
Net investment yield including realized capital gains/(losses) (%)	4.5	4.7	4.7	4.9	5.2
Net investment yield including all gains/(losses) (%)	4.1	4.4	3.6	4.3	3.9
Investment portfolio composition (%)					
Cash and short-term investments	6.1	6.6	5.4	4.8	4.9
Bonds	69.0	66.9	58.4	56.8	55.5
Equity investments including investment funds	6.6	5.7	5.8	9.1	9.7
Real estate	9.0	10.7	15.5	14.3	12.6

Table 5

Vienna Insurance Group Risk Position (cont.)					
Mortgages	1.4	1.3	1.3	1.3	1.1
Loans	4.4	5.0	10.6	10.6	12.4
Investments in affiliates	3.3	3.7	3.0	3.1	3.8
Other investments	0.1	0.1	0.0	0.1	0.1

Financial flexibility: Strong

VIG has strong financial flexibility, in our view, thanks to the group's proven access to capital markets and comparably low financial leverage. This is backed by the successful issue of the €500 million hybrid debt in 2013. We expect the majority shareholder WIENER STÄDTISCHE WECHSELSEITIGER VERSICHERUNGSVEREIN – VERMÖGENSVERWALTUNG – Vienna Insurance Group to maintain an at least 51% stake in VIG and to secure the group's financial independence. We expect the financial leverage ratio (debt plus hybrids to economic capital) to remain comparably low, at less than 20% in 2014-2016 and the fixed-charge coverage to be at about 7x-9x in the same period.

Table 6

Vienna Insurance Group Financial Flexibility					
	--Year ended Dec. 31--				
(x)	**2013**	**2012**	**2011**	**2010**	**2009**
Fixed-charge coverage	7.0	8.4	8.6	8.2	6.2
Financial leverage (%)	17	16	16	15	17

Other Assessments

Enterprise risk management: Adequate with strong risk controls

VIG's enterprise risk management (ERM) is adequate with strong risk controls, in our opinion. We do not expect the group to experience losses from traditional risk areas outside of the normal range. We base our assessment on what we view as VIG's positive risk-management culture and positive risk controls for the group's major risks. We believe that VIG's strategic risk management is still neutral because a holistic approach, including economic capital and risk-and-return considerations in operational and strategic decision-making and performance assessment, is not yet in place.

Management and governance: Strong

VIG's management and governance is strong, in our view. This reflects the group's clear and credible strategic planning and defense of its leading position in the domestic market and its conservative financial management, with strong balance sheet management. However, we believe restructuring the Romanian and Italian business will require intense management attention in 2014 and beyond, to demonstrate the group's continued successful execution of its strategy.

Holistic analysis: Lower geographic earnings diversification compared with some higher rated peers

The combination of our views of the business risk and financial risk profiles leads us to apply an anchor of 'aa-' to VIG. The ratings on the group are one notch lower than the anchor, however, based on our negative holistic analysis. This reflects our view of VIG's lower geographic earnings diversification than its higher rated European peers and the need to rebuild a sustainable track record of strong operating performance after the earnings drop in 2013. Within the group, Austria and the Czech Republic remain the main earnings contributors, with a combined share of about 121% of pretax profits in 2013, against a pretax loss of about 28% from Romanian operations.

Liquidity: Exceptional

We regard VIG's liquidity as exceptional, owing to the strength of available liquidity sources--mainly premium income--and its liquid asset portfolio. There are no refinancing concerns, in our opinion. We think the group is capable of managing any unexpected large claims or any unexpected increase in life insurance policy lapses.

Accounting Considerations

VIG prepares its consolidated financial statements according to International Financial Reporting Standards (IFRS). We base our analysis of the group's life profitability and risk exposures mainly on market consistent embedded value disclosure. The group bases its calculation on year-end swap rates and includes liquidity premiums. A particular feature of VIG's IFRS accounting is the limited recognition of deferred acquisition costs in its balance sheet. This is because VIG channels most of its commissions directly through its profit and loss statement.

We base our assessment of VIG's capital adequacy on its reported shareholders' equity, which we adjust mainly to account for 50% of the life insurance value in force not included in the balance sheet, hybrid debt classified as equity according to our criteria, parts of the policyholder capital available to absorb losses, and off-balance-sheet asset-value reserves. We deduct the on-balance-sheet goodwill from capital.

Related Criteria And Research

- Insurers: Rating Methodology, May 7, 2013
- Group Rating Methodology, Nov 19 2013
- Enterprise Risk Management, May 7, 2013
- Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Principles Of Credit Ratings, Feb. 16, 2011
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Ratings Detail (As Of July 31, 2014)	
Operating Company Covered By This Report	
Vienna Insurance Group AG Wiener Versicherung Gruppe	
Financial Strength Rating	
Local Currency	A+/Stable/--
Counterparty Credit Rating	
Local Currency	A+/Stable/--
Junior Subordinated	A-
Domicile	Austria

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable

Ratings Detail (As Of July 31, 2014) (cont.)

across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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