

MOODY'S

INVESTORS SERVICE

Rating Action: Moody's affirms Covea's Aa3 IFS rating following announcement of agreement to purchase PartnerRe; outlook stable

29 October 2021

Paris, October 29, 2021 – Moody's Investors Service ("Moody's") has today affirmed the Aa3 insurance financial strength (IFS) rating of Covea Cooperations (Covea). The outlook for Covea is stable.

The rating action follows Covea's announcement that it reached an agreement with EXOR N.V. (EXOR) to acquire PartnerRe Ltd. (PartnerRe), a global reinsurer, for a cash consideration of \$9.0 billion (€7.7 billion).

RATING RATIONALE

The affirmation of Covea's rating reflects the benefits of increasing diversification in terms of product, geographic reach and earnings counterbalanced by a weakening in Covea's financial profile as a result of the significant reduction in capitalisation and moderate increase in leverage. Earnings will become more volatile over time as a result of the natural catastrophe and long-tail liability exposure that is inherent to reinsurers. Despite these negatives, Covea will maintain a conservative balance sheet following the transaction. In particular the group will maintain very strong capitalisation and very good financial flexibility following the acquisition despite the purchase consideration being paid entirely in cash.

The acquisition will cause a significant reduction in Covea's Solvency II ratio, which was 394% at year-end, albeit Moody's expects Covea's capitalization and Solvency II ratio to remain strong, and above that of some Aa3 rated peers. In addition, because Covea is a mutualist group, all future earnings can be retained to strengthen the group's solvency ratio. Moody's expects the group to generate profits representing more than 10 percentage points of Solvency II ratio every year on a normalized basis, based on Covea's annual net income which averaged approximately €0.8 billion over the past five years and additional net income from PartnerRe which averaged €0.3 billion over the same period. PartnerRe's net income has been significantly more volatile than that of Covea, particularly in heavy catastrophe years. That said, Moody's expects PartnerRe's profitability to improve in coming years as a result of rising prices for reinsurance and underwriting actions taken by PartnerRe to reduce volatility.

The group's adjusted financial leverage will also deteriorate on a pro-forma basis given PartnerRe's outstanding debt (estimated as €1.9 billion as at H1 2021) will be added to Covea's debt (€0.5 billion as at year-end 2020) on a consolidated basis. Nonetheless, Covea will maintain conservative financial leverage metrics, below many other highly rated insurers, keeping some capacity to issue subordinated debt and strengthen its solvency.

Moody's adds that the acquisition of PartnerRe will give rise to significant goodwill on Covea's balance sheet. Nonetheless, the ratio of goodwill and intangibles assets over shareholders' equity will remain consistent with Moody's expectations for Aa-rated insurers. Reserving risk will also increase given the long tail nature of PartnerRe's casualty reserves. The significant excess in Covea's retail business reserves will also help ensure a strong level of reserve adequacy overall.

Commenting on the impact of the acquisition on Covea's business profile, Moody's says that the group's geographic and business diversification will be significantly enhanced. The weight of French business will reduce and group will also gain exposure to life and property and casualty (P&C) reinsurance businesses (31% of premiums on a consolidated basis post acquisition). At the same time, the group's risk profile will increase and profits' volatility will rise, as PartnerRe is significantly exposed to natural catastrophes and man-made risks and covers US liability and casualty risks which continue to be subject to social inflation.

Moody's expects that Covea will largely rely on PartnerRe's expertise to manage these risks. Therefore, Moody's will closely monitor the ability of Covea to retain key personnel. More positively, the limited overlap between existing Covea and PartnerRe's businesses will limit integration risks. In addition, Moody's understands that it is Covea's intention to let PartnerRe continue to develop its current strategy, which should limit disruption risk at PartnerRe level.

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

Moody's says that an upgrade of Covea's rating is unlikely at this stage. Nonetheless, positive pressure could be exerted in case of continued profitable diversification of the business outside of France and in life reinsurance, while strengthening capital levels significantly and maintaining very low financial leverage.

Conversely, negative pressure on the rating could arise in case of (i) a material reduction in the group's capital, as evidenced by a Solvency II ratio remaining below 230% on a sustained basis, (ii) an increase in financial leverage above 30% and a decrease in earnings coverage below 7x, (iii) a reduction in profitability, as evidenced for example by a combined ratio sustainably above 100%, combined with a sustained increase in the volatility, (iv) a significant deterioration in its asset quality, or (v) failure to develop PartnerRe's business, for example in case of inability to retain key personnel.

Covea is the leading French P&C insurance group and ranks number four in the overall French insurance market. It reported gross written premiums of €16.6 billion in 2020 and shareholders' equity of €16.5 billion as at year-end 2020.

PartnerRe, based in Bermuda, is the 12th largest global reinsurer. It reported gross written premiums of \$6.9 billion (€5.9 billion) in 2020 and shareholders' equity of \$7.3 billion (€6.3 billion) as at year-end 2020.

PRINCIPAL METHODOLOGIES

The methodologies used in this rating were Life Insurers Methodology published in September 2021 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1254133, and Property and Casualty Insurers Methodology published in September 2021 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1254163. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

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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 at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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