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Research Update:

Länsförsäkringar Sak 'A' Ratings Affirmed On Improved Management And Governance; Outlook Stable

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Overview

- Länsförsäkringar Alliance (the Alliance) remains the leading non-life insurer in Sweden, with very sound capitalization despite potential volatility in earnings driven by a high proportion of high-risk assets.
- We believe the Alliance benefits from enhanced cooperation and integration, both between the 23 regional mutual companies that make up the Alliance and with the intermediate holding company Länsförsäkringar AB (LF AB), resulting in improved management and governance.
- We are consequently affirming our 'A' rating on Länsförsäkringar Sak Försäkrings AB (LF Sak), a core company within the Alliance, and the 'A-' counterparty credit rating on the intermediate holding company LF AB.
- The stable outlook reflects our view that the Alliance will maintain its strong business risk and financial risk profiles.

Rating Action

On Nov. 7, 2016, S&P Global Ratings affirmed its 'A' insurer financial strength and issuer credit ratings on LF Sak, a core company within the Alliance. At the same time, we affirmed the 'A-' counterparty credit rating on the intermediate holding company LF AB. The outlook on both entities is stable.

Rationale

The affirmation reflects the core status of LF Sak to the Alliance and our continued view of the Alliance's strong business risk and financial risk profiles, based on its strong competitive position and very strong capital and earnings.

The Alliance remains the leading non-life insurance provider in Sweden with a stable market share of 30% as of June 2016. In our view, the Alliance benefits from its ability to deliver high-quality services to its customers via a widespread network of local branches and a successful partnership with brokers. Furthermore, we regard the Alliance's powerful brand and strong pricing power as competitive advantages.

The Alliance's combined (loss and expense) ratio improved in recent years from about 100% in 2011 to 90% in 2015. As per September 2016, we noted a stable cost ratio but higher claims resulting in a combined ratio of 96%. The Alliance has a somewhat higher combined ratio than some of its peers in the Nordic region, which is to a large extent a consequence of its mutual status. In general, we believe the Alliance will continue to show beneficial combined ratios of about 96% in 2016 and around 95% over 2017-2018.

We believe the Alliance's investment income will remain volatile reflecting its rather high exposure to high-risk assets, for example its equity proportion as per Sept. 30, 2016 was about 39% of invested assets. Taking this into account, we expect return on shareholder's equity will exceed 7% in 2016 and 4% in 2017-2018, resulting in annual net income of more than Swedish krona (SEK) 3 billion in 2016 and SEK2 billion in 2017-2018. Based on the Alliance's strong earnings and solid capital base, we also assume that the Alliance's extremely strong capital adequacy will remain above our requirements for the 'AAA' level, according to our risk-based capital model.

From our perspective, the Alliance's management and governance has improved in recent years. We have noticed an increased integration and cooperation within the Alliance, in particular in preparation for the Solvency II regime. As the first insurers in Sweden, LF AB and its subsidiaries received the approval from the Swedish regulator to use partial internal models. Furthermore, we acknowledge the mutual companies' support for the growth in LF AB and its subsidiaries, in particular the capital injections to support the growth in Länsförsäkringar Bank. In addition, LF AB has successfully enabled an orderly run-off of Länsförsäkringar Liv (a subsidiary run on mutual principles that offers traditional life and pensions insurance). This underpins, in our view, the strengthened governance within the Alliance.

We believe the Alliance's strong business risk profile and very strong capital and earnings somewhat understate their contribution to the Alliance's overall creditworthiness and consequently we opt for an 'a' anchor, which is the higher of the two possible anchors indicated by our methodology.

Outlook

The stable outlook reflects our view that the Alliance will continue to maintain very strong capital and earnings and a strong competitive position over the next two years. We expect the Alliance's capital adequacy will provide a substantial buffer against potential investment losses, in particular from its high equity exposures.

UPSIDE SCENARIO

We could raise the ratings on LF Sak over the next two years if we saw a sustainable decrease of volatility risk in earnings and capital adequacy, stemming from the high-risk assets in the investment portfolio and a notable increase in earnings contributions from banking and life insurance.

DOWNSIDE SCENARIO

We could lower the ratings on LF Sak over the next two years if, contrary to our expectations:

- Capital and earnings deteriorated for a sustained period below very strong. This could result from large losses, possibly related to natural catastrophes in Sweden, or from investment losses, in particular from equity investments.

- Risks related to the investment portfolio materially increased volatility in capital adequacy.

Ratings Score Snapshot

	To	From
Holding Company Rating	A-	A-
Financial Strength Rating	A	A
Anchor	a	a
Business Risk Profile	strong	strong
IICRA	low	low
Competitive Position	strong	strong
Financial Risk Profile	strong	strong
Capital and Earnings	very strong	very 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	satisfactory	fair
Holistic Analysis	0	0
Liquidity	exceptional	exceptional
Support	0	0
Group Support	0	0
Government Support	0	0

IICRA--Insurance Industry And Country Risk Assessment

Related Criteria And Research

Related Criteria

- General Criteria: Group Rating Methodology - November 19, 2013
- Criteria - Insurance - General: Enterprise Risk Management - May 07, 2013
- Criteria - Insurance - General: Insurers: Rating Methodology - May 07, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13, 2012
- Criteria - Insurance - General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model - June 07, 2010
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

Related Research

- Sweden's Property/Casualty Insurance Sector Carries A Low Industry And Country Risk Assessment, August 11, 2016
- Sweden's Life Insurance Sector Carries An Intermediate Industry And Country Risk

Assessment, August 11, 2016

- Lansforsakringar Bank, August 30, 2016
- Lansforsakringar Sak Forsakrings AB, November 27, 2015

Ratings List

	Rating	
	To	From
Lansforsakringar AB		
Counterparty Credit Rating		
Foreign and Local Currency	A-/Stable/--	A-/Stable/--
Lansforsakringar Sak Forsakrings AB		
Counterparty Credit Rating		
Local Currency	A/Stable/--	A/Stable/--
Financial Strength Rating		
Local Currency	A/Stable/--	A/Stable/--

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