Research Update:

Austrian Insurer UNIQA 'A' Ratings Affirmed On Finalized Financing Structure For The AXA CEE Acquisition; Outlook Stable

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Overview

- UNIQA will finance the acquisition of AXA CEE entities with cash and senior and hybrid debt, which will alleviate the impact on the group's capital adequacy.
- In addition, we continue to view the parent holding company UNIQA Insurance Group as having operating insurance cash flows in the group's updated structure.
- We are therefore affirming our 'A' ratings on UNIQA's core subsidiaries--UNIQA Oesterreich Versicherungen AG and UNIQA Re AG--and removing them from CreditWatch negative, where we placed them on Feb. 12, 2020.
- The stable outlook reflects our view that, over the next two years, UNIQA would smoothly integrate AXA CEE entities, gradually recover profitability after COVID-19 impacts in 2020, and sustain a resilient capital position.

Rating Action

On June 29, 2020, S&P Global Ratings affirmed its 'A' long-term issuer credit and financial strength ratings on the core entities of Austria-based UNIQA Group, UNIQA Oesterreich Versicherungen AG and UNIQA Re AG. The outlook is stable.

We also affirmed our 'A-' ratings on the operating holding company UNIQA Insurance Group (UIG). The outlook is stable.

At the same time, we affirmed our issue ratings on UNIQA's existing debt. In addition, we assigned our 'A-' rating to the group's proposed senior unsubordinated unsecured notes and our 'BBB' rating to the proposed junior subordinated deferrable notes.

We removed all the ratings from CreditWatch, where we placed them with negative implications on Feb. 12, 2020.

Rationale

Under our base case, we expect the final financing structure for the AXA CEE acquisition will soften the reduction of UNIQA's capital buffers from the related goodwill and the acquired entity's capital requirements. The newly presented financing structure envisages that UNIQA will fund the transaction through a combination of cash, a €600 million senior bond, and a €200 million junior subordinated bond. We expect to classify the junior subordinated bond as having intermediate equity content. We believe the junior subordinated bond will support the group's capital position. As such, we expect that UNIQA's capital adequacy, according to S&P Global Ratings' model, will remain above the 'AAA' range in the medium term.

The acquisition increases UNIQA's debt on balance sheet, resulting in higher interest payments for a prolonged period. Conversely, UNIQA's 2020 operating performance will likely be relatively low due to COVID-19-related impacts and we assume only gradual improvements. This lead us to expect fixed charge coverage to drop materially in 2020 and to only gradually improve in 2021-2022, remaining on average below 4x over the period. At this level, funding structure metrics are somewhat weaker than peers' and will weigh on UNIQA's medium-term financial profile, in our opinion.

Positively, we think the AXA CEE acquisition will help UNIQA enhance its presence in Central and Eastern Europe (CEE), where the group already enjoys a solid footprint. Overall, we assume the acquisition will support the group's transition from predominant exposure to Austrian insurance market to a more diversified and balanced earnings contribution between Austria and the CEE region. In addition, the transaction offers material cost synergies and access to additional distribution channels. Furthermore, through the acquisition, UNIQA adds mostly capital light life insurance and non-life insurance, which should also help UNIQA to continue shifting the business mix away from capital-intensive insurance products, in line with the group's strategy. We consider integration risks to be limited, since UNIQA's management has similar experience in the CEE region.

Under the prospective organizational structure, UIG will continue to write reinsurance business and would as such remain an operating holding company of the group, generating cash to partly fulfil its financial obligations with own means. However, because we think that UIG's own cash flow is relatively limited, we continue to apply a one-notch differential between the ratings on the holding and the core operating entities of UNIQA Group.

The 'A-' issue rating on the senior notes is equalized with the rating on UIG, while the rating on the proposed junior subordinated bond is two notches below the long-term issuer credit rating on UIG. This reflects our standard approach for rating subordinated debt issues. We therefore consider the risk of mandatory deferral to be remote and don't believe it is necessary to deduct a further notch for additional nonpayment risk to derive the rating on the notes. The issue rating reflects the subordination and interest deferral features of the notes, and takes into account our understanding that:

- The notes are subordinated to UNIQA's policy holders and senior creditors.
- The issuer can choose to defer interest as long as the issuer has not declared or made a dividend or other payment (including payment in relation to redemption or repurchase) on a more junior security in the previous six months.
- Under the notes' terms and conditions, interest deferral is mandatory if a solvency event has occurred, which, under Solvency II, would be a breach of the solvency capital requirement.

The junior subordinated notes have a 15.25-year maturity, with UNIQA having the option to redeem the notes at the first call date, which is 5.25 years after issuance. UNIQA has the option to redeem remaining outstanding notes at any time following a tax event, a regulatory event, a capital event or a gross up event. Noteholders will receive the principal amount plus any accrued or deferred interest. Initially, UNIQA will pay a fixed coupon until the first call date, after which the coupon will be reset to five-year, euro mid-swap rate plus the initial margin. There is a 100 basis point step-up after 10 years.

Outlook

The stable outlook reflects our view that, over the next two years, UNIQA's capital position will remain resilient and its operating performance will gradually improve, while the integration of AXA CEE will proceed smoothly once the acquisition is completed.

We could lower the ratings over the next two years if adverse market developments materially weakened UNIQA's capital adequacy prospects and further depressed its profitability. A significant underperformance of AXA CEE's profit contribution could also create ratings pressure. We could widen the notching of UIG if the holding reported a material reduction in cash flow from operating activity.

A potential upgrade of UNIQA Group is unlikely, in our view. It would hinge on a material and sustainable improvement in the group's funding metrics, combined with a pronounced strengthening of operating performance. We'd also have to observe further improvements in earnings diversification through which the group enhanced the resilience of its business profile. We could upgrade UIG if the holding substantially and sustainably increased cash flows from operating activity.

Ratings Score Snapshot

Business Risk Profile	**Strong**
Competitive position	Strong
IICRA	Intermediate
Financial Risk Profile	**Strong**
Capital and earnings	Very Strong
Risk exposure	Moderately low
Funding structure	Moderately Negative
Anchor*	a
Modifiers	0
Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0
Financial Strength Rating	**A**

* Reflects that UNIQA following acquisition completion will materially strengthen geographic diversification of revenues and net income.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- 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

Related Research

- UNIQA Group Core Subsidiaries Ratings Remain On CreditWatch Negative After Profit Warning, April 15, 2020
- Research Update: UNIQA Insurance Group CreditWatch Placement Revised To Negative From Developing On New Merger Plans, Feb. 20, 2020
- Research Update: Ratings On UNIQA's Core Insurance Entities Put On Watch Negative On Planned Acquisition Of AXA's CEE Operations, Feb. 12, 2020

Ratings List

New Rating		
UNIQA Insurance Group AG		
Senior Unsecured	A-	
Junior Subordinated	BBB	
Ratings Affirmed; CreditWatch/Outlook Action		
	To	**From**
UNIQA Insurance Group AG		
Issuer Credit Rating	A-/Stable/--	A-/Watch Neg/--
Financial Strength Rating	A-/Stable/--	A-/Watch Neg/--
Junior Subordinated	BBB	BBB/Watch Neg
UNIQA Oesterreich Versicherungen AG		
UNIQA Re AG		
Issuer Credit Rating	A/Stable/--	A/Watch Neg/--
Financial Strength Rating	A/Stable/--	A/Watch Neg/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.