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Nacional de Reaseguros S.A.

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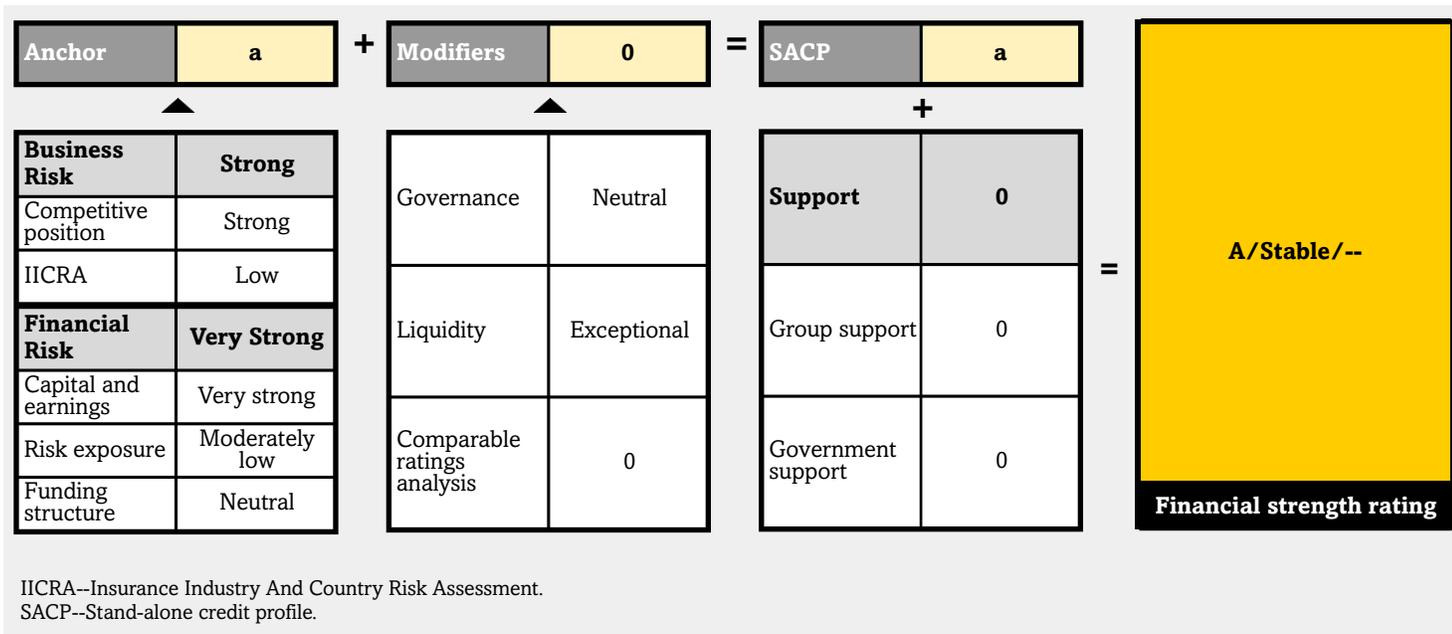
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Nacional de Reaseguros S.A.



Credit Highlights

Overview	
Key strengths	Key risks
Leading position in the Spanish reinsurance market with some diversification via foreign business.	Small absolute size and position in the global reinsurance market.
Limited historical earnings volatility from natural catastrophe events.	Relatively short track record of improved earnings from international business.
Resilient earnings generation and excellent risk-adjusted capital adequacy.	Limited depth of workforce creates a key-man risk.
Very low expense ratio is a competitive edge.	

We believe that Nacional de Reaseguros (NRe) will maintain excellent capitalization, supported by sound earnings retention despite unusually high claims. The company's earnings declined in 2020 with a combined ratio of 97.5% and return on equity of 7.3% compared with 92.9% and 10.9% in 2019. The decline was driven by pandemic-related claims and capital market volatility. Nevertheless, capitalization remained a strength with a regulatory solvency ratio of 226% and an excellent capital adequacy based on our internal risk-based capital model at year-end 2020. We expect 2021 to be another year of elevated claims, mainly driven by Storm Bernd in Western Europe and Storm Filomena in Spain, leading to a combined ratio of 98%-100%. However, we expect earnings to continue to support NRe's growth ambition and maintain capital adequacy at the excellent level over the next two years.

We expect NRe to maintain its leading position in Spain's reinsurance market. Thanks to long-lasting relationships with insurers and brokers, NRe is a well-recognized brand in Spain, where we expect it will keep its competitive advantage and strong market position. Outside Spain, NRe has progressively expanded its activities over the past decade thanks to a selective distribution approach. Notwithstanding the diversification from this foreign business, the company's scale and geographic footprint remains small in a global context. This influences our view of NRe's competitive position compared with that of most 'A+' rated peers.

We consider that risk exposure will remain moderately low. Despite some elevated natural catastrophe claims in 2021, we believe that some tail property/casualty (P/C) risks underwritten in Spain are mainly mitigated by the Consorcio de Compensacion de Seguros (CCS; a national scheme that will notably cover specific large catastrophe events). Outside Spain, we think that NRe has adopted a prudent approach to its expansion strategy, underwriting a low amount of catastrophe risk, as well as continually improving risk management to accompany its expanding international presence. The insurer's international investment diversification allows us to rate it up to four notches above the long-term rating on Spain (A/Negative/A-1).

Outlook: Stable

The stable outlook indicates that we do not expect to change our ratings on NRe over the next two years. NRe demonstrates resilience while facing the current COVID-19 crisis. We expect that NRe will maintain its leading, profitable position in Spain while prudently and profitably expanding its business outside Spain. We also expect earnings to recover in 2022 and capital to remain solid and stable with no material rise in volatility from increased exposure to catastrophes or other lesser-known risks. Furthermore, we expect Nacional will increasingly align its enterprise risk management to that of larger peers, with capital adequacy further consolidating at an excellent level.

Downside scenario

We could lower the ratings on NRe if foreign business growth and related risks were to increase volatility, weaken the company's strong operating performance, or decrease its capital adequacy below the excellent level.

Upside scenario

We consider a positive rating action to be remote at this stage given the company's lack of geographical diversification compared with that of higher-rated peers.

Key Assumptions

- Spanish real GDP growth to recover to 4.5% in 2021 and 7.0% in 2022, rebounding from a contraction of 10.8% in 2020. Real GDP growth in the eurozone to enhance to 5.1% in 2021 and 4.4% in 2022, following a decline of 6.5% in 2020.
- Long-term Spanish interest rates to remain at historical lows of 0.5%-0.9% for 2021 and 2022. Same trend in the eurozone, with rates that we estimate at 0.1%-0.6% for the coming two years.
- Unemployment rate to remain high in Spain at 15.1% in 2021 and 14.4% in 2020, compared with 7.9% and 7.5% in the eurozone over the same period.

Nacional de Reaseguros S.A.--Key Metrics

	2022f	2021f	2020	2019	2018	2017	2016
S&P Global Ratings capital adequacy	Excellent						
Gross premium written (Mil. €)	~635	~620	608.5	590.8	567.5	556.0	532.0

Nacional de Reaseguros S.A.--Key Metrics (cont.)

	2022f	2021f	2020	2019	2018	2017	2016
Net income (Mil. €)	34-36	25-27	28.9	40.2	37.0	32.1	37.7
Return on shareholders' equity (%)	8-10	6-7	7.3	10.9	10.8	9.7	12.4
Property/casualty: Net combined ratio (%)	94-96	98-100	97.5	92.9	92.9	96.1	90.5

f--Forecast.

Business Risk Profile: Strong

NRe is the leading reinsurer in terms of premiums in Spain, with an estimated market share of about 15%, excluding intercompany operations in the Spanish reinsurance market. It reported €609 million of gross premium at year-end 2020. Thanks to solid relationships with both insurers and brokers in Spain, which have been built over the decades, NRe has a leading position on most contracts in its domestic operations.

NRe's expansion across Europe, started in 2010, has borne fruit. The international portfolio now contributes about one third of the company's total gross written premium, providing volumes and diversification. However, we believe that its market position internationally is less prominent than in its domestic market. NRe demonstrates disciplined execution of its geographic expansion strategy outside Spain, which helps to preserve its strong operating performance.

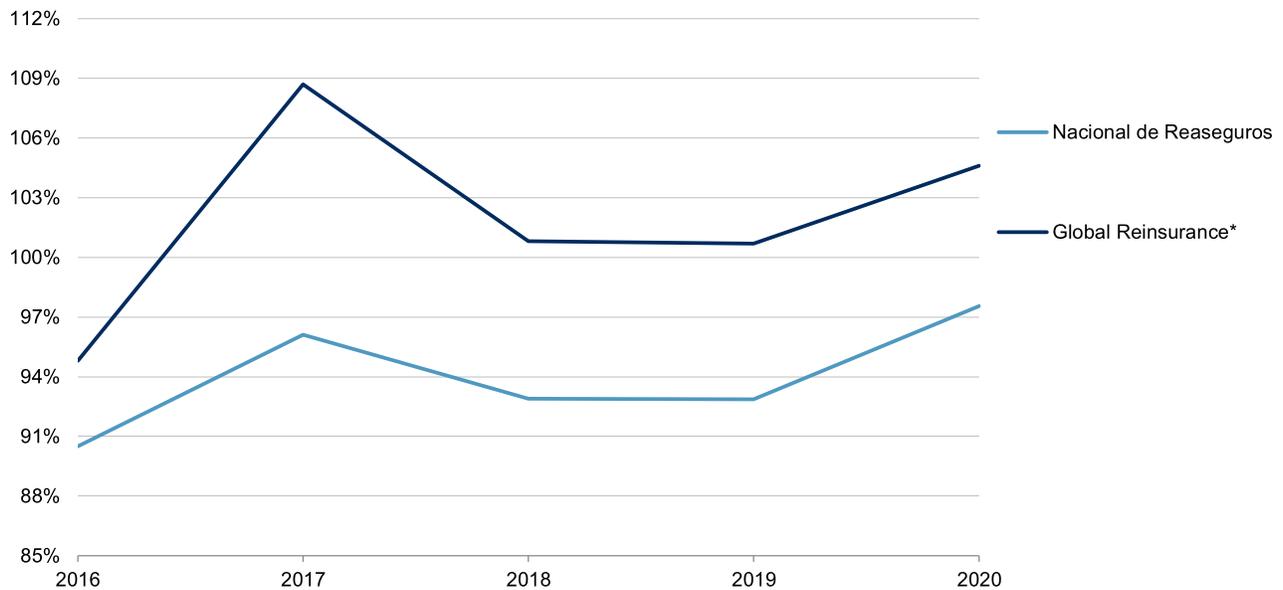
NRe has a diversified insurance business mix, which at year-end 2020 included: fire and multi-risk (42% of gross premiums), life (19%), motor and third-party liability (18%), marine (9%), personal accident and health (6%), and other lines (7%).

We project that NRe's overall premium will increase by about 2% in 2021 and 2.5% in 2022, benefiting from some rate increases in continental Europe after high natural catastrophe claims in the market, demonstrating its cautious international expansion.

NRe's performance declined in 2020 compared with 2019, disclosing a combined ratio of 97.5% and a return on equity of 7.3% compared with 92.9% and 10.9%. The decline was mainly caused by pandemic-related business interruption claims, as well as lower investment returns in a volatile capital market environment. Nonetheless, the performance was again beneficial compared with global reinsurance peers (see chart 1). For 2021, we expect unusually high claims related to natural catastrophe events, mainly from Storms Filomena and Bernd. We forecast the combined ratio to remain high at 98%-100% compared with the five-year average of 94% and the return on equity to be at 6%-7%. For 2022, we believe that the company will return to average performance, benefiting from higher reinsurance rates, especially in the natural catastrophe business, and low administrative costs.

Chart 1

Nacional de Reaseguros' Combined Ratio Versus Global Reinsurance Market
 Nacional de Reaseguros' stable P/C technical results



Source: S&P Global Ratings & company financials. *Top 21 global reinsurers - Alleghany, Arch, Ascot, Aspen, AXIS, China Re, Everest Re, Fairfax, Fidelis, Hannover Re, Hiscox, Lancashire, Lloyd's, Markel, Munich Re, PartnerRe, Qatar Ins., RenaissanceRe, SCOR, Sirius, and Swiss Re. P/C--Property/casualty. Copyright © 2021 by Standard & Poor's Financial Services LLC. All rights reserved.

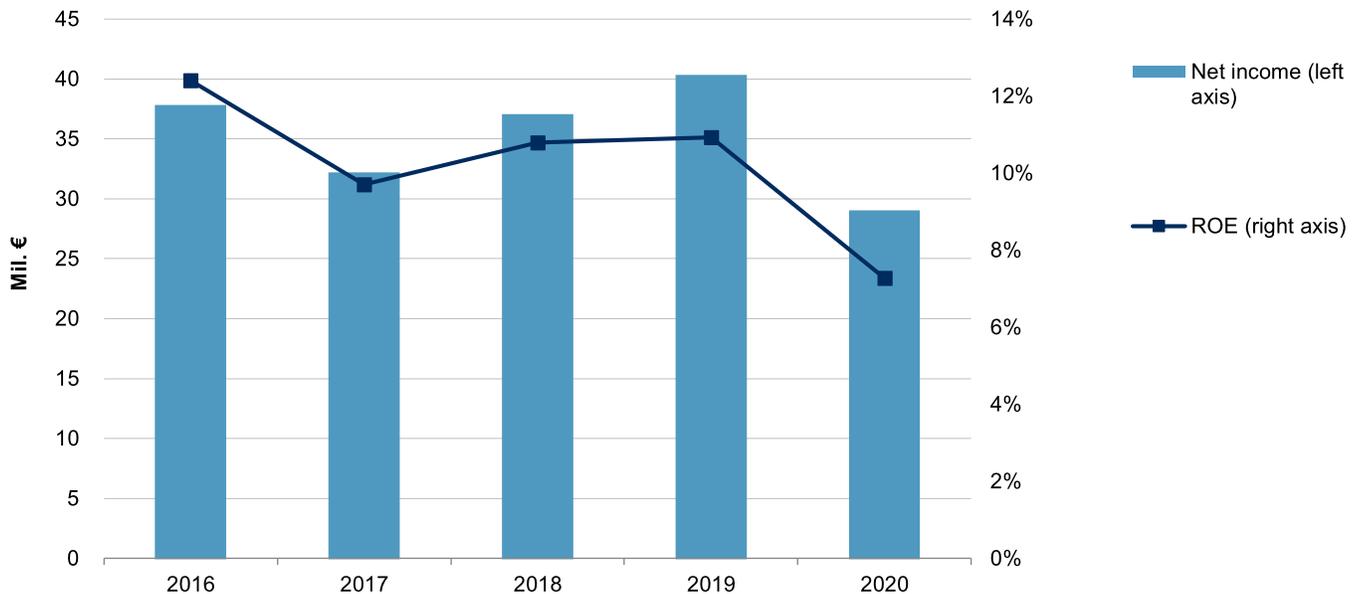
Financial Risk Profile: Very Strong

NRe's operations are backed by a solid and protected balance sheet, which is resilient against the current crisis environment. We expect NRe to maintain excellent risk-adjusted capital adequacy according to our model in the years to come. It comfortably covers its solvency capital requirements with a regulatory solvency ratio of 226% at year-end 2020. However, we believe that the small absolute size of its capital remains a risk compared with larger reinsurers, making the company somewhat susceptible to movements in capital and earnings in the event of potential large losses.

NRe's shareholders have a long-term commitment to its development. We therefore forecast that the company's retained earnings will support NRe's growth ambitions. Despite the pandemic, we forecast that NRe will generate annual net earnings of €25 million-€27 million in 2021, recovering to €34 million-€36 million in 2022, retaining about 65% of this to finance capital requirements from the expanding business and continually increase its capital base. NRe has no debt, and we consider its need for extraordinary additional funds to be modest because of its long-established strategy of self-financing organic growth.

Chart 2

Nacional de Reaseguros--Consistent Profitability



Source: S&P Global Ratings and company financials.
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We expect earnings volatility to remain modest, especially thanks to the stability of the domestic operations. Spain's system for assessing damages in personal injury claims (Baremo) provides a solid and effective framework to anticipate claims amounts. Meanwhile, the CCS scheme to cover natural catastrophes absorbs most losses on claims arising from such events like recently experienced in the volcano outbreak in La Palma, which lessens the volatility of technical results.

We expect conservative underwriting and comprehensive reinsurance cover will limit peak risks outside Spain. The majority of NRe's new portfolio comes from proportional treaties in line with existing ones. In addition, NRe's focus on the EU reduces volatility, as well as regulatory and political risk, because of its physical and cultural proximity.

NRe's investment strategy focuses on short-duration and liquid assets, consistent with a strict asset-liability management policy. NRe's average credit quality in its fixed-income portfolio is at the 'BBB+' level compared with 'A' in 2019, cautiously increasing credit risk to partly offset the consequences of continuing low interest rates. Exposure to equities is relatively high, representing about 15% of total invested assets at market values, although around 9% refers to NRe's long-term investment in Grupo Compañía Española de Crédito y Caución S.L. Net investment yields were 1.1% (1.7% including realized and unrealized gains) in 2020.

NRe's catastrophe and overall risk management is improving to support its increasing international profile. It mitigates

the exposure to potentially more volatile earnings. We believe NRe's overall risk profile remains largely unchanged since we do not anticipate that it will take material catastrophe risk in its international business, and that catastrophe risk will generally remain controlled in its Spanish business.

Other Key Credit Considerations

Governance

NRe has an effective governance framework in place, with management and shareholders seamlessly committed to gradually and prudently building its market position outside Spain, taking advantage of the company's established expertise as a service-led coverage provider for small and midsize companies. Risk management is ingrained in NRe's culture, with continual efforts to embed risk-based decisions at all levels of the organization.

Liquidity

Liquidity is exceptional. NRe maintains a sufficient level of cash or cash equivalents, as well as a high portion of readily realizable assets to face its obligations in the short term.

Ratings above the sovereign

Our ratings are based on NRe's stand-alone credit profile. NRe could be rated above Spain because it passes our capital and liquidity sovereign stress tests thanks to a well-diversified asset portfolio; more than two thirds is allocated outside Spain in various geographies. NRe could be rated up to four notches above Spain, reflecting our view of moderate sensitivity to country risk.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Insurance | Property/Casualty: Assessing Property/Casualty Insurers' Loss Reserves, Nov. 26, 2013
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Appendix

Nacional de Reaseguros S.A.--Credit Metrics History				
Ratio/Metric	2020	2019	2018	2017
S&P Global Ratings capital adequacy	Excellent	Excellent	Excellent	Excellent

Nacional de Reasegueros S.A.--Credit Metrics History (cont.)

Ratio/Metric	2020	2019	2018	2017
Total shareholder equity	404.5	390.9	345.2	340.0
Gross premiums written	608.5	590.8	567.5	556.0
Net premiums written	480.5	472.2	450.4	444.0
Net premiums earned	479.3	467.3	449.0	482.0
Reinsurance utilization (%)	21.0	20.1	20.6	20.0
EBIT	36.3	52.0	47.7	41.0
Net income (attributable to all shareholders)	28.9	40.2	37.0	32.1
Return on revenue (%)	5.9	9.1	9.6	5.8
Return on shareholders' equity (reported) (%)	7.3	10.9	10.8	9.7
P/C: net combined ratio (%)	97.5	92.9	92.9	96.1
P/C: net expense ratio (%)	30.7	29.7	30.5	28.3
Net investment yield (%)	1.1	1.1	1.1	0.7
Net investment yield including investment gains/(losses) (%)	1.7	2.0	1.4	2.1

P/C--Property/casualty.

Business And Financial Risk Matrix

Business risk profile	Financial risk profile							
	Excellent	Very Strong	Strong	Satisfactory	Fair	Marginal	Weak	Vulnerable
Excellent	aa+	aa	aa-	a+	a-	bbb	bb+	b+
Very Strong	aa	aa/aa-	aa-/a+	a+/a	a-/bbb+	bbb/bbb-	bb+/bb	b+
Strong	aa-/a+	a+/a	a/a-	a-/bbb+	bbb+/bbb	bbb-/bb+	bb/bb-	b+/b
Satisfactory	a	a/a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bb+/bb	bb-/b+	b/b-
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb/bb-	b+/b	b-
Weak	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b/b-	b-
Vulnerable	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b+/b	b/b-	b-	b-

Note: Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

Ratings Detail (As Of December 17, 2021)*

Operating Company Covered By This Report

Nacional de Reasegueros S.A.

Financial Strength Rating

Local Currency

A/Stable/--

Issuer Credit Rating

Local Currency

A/Stable/--

Domicile

Spain

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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