

Delta Lloyd Operating Companies 'A-' Ratings Affirmed; Outlook Negative

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- We are affirming our 'A-' ratings on the core operating entities of Netherlands-based multiline insurance group Delta Lloyd, because it has sustained its strong competitive position in the Dutch market, although the rating is somewhat constrained by the relative weakness of the financial risk profile.
- We continue to assess Delta Lloyd on a stand-alone basis. Netherland-based insurer NN Group announced its intention to buy Delta Lloyd in October 2016, but there are multiple uncertainties surrounding the potential transaction (see "Delta Lloyd Operating Companies 'A-' Ratings Affirmed After Cash Offer From NN Group; Outlook Negative," published on Oct. 7, 2016). That said, we consider that this transaction would be unlikely to weaken Delta Lloyd's creditworthiness in the short term.
- We are revising our liquidity assessment to exceptional from strong, primarily reflecting the insurer's more liquid asset mix.
- The negative outlook reflects the execution risk linked to Delta Lloyd's ongoing efforts to reduce risk on its balance sheet, strengthen its financial flexibility, and sustain the turnaround of its operating performance.

LONDON (S&P Global Ratings) Dec. 15, 2016--S&P Global Ratings today affirmed its 'A-' long-term counterparty credit and insurer financial strength ratings on Delta Lloyd Levensverzekering N.V. and Delta Lloyd Schadeverzekering N.V., the core operating companies of the Delta Lloyd N.V. group. We also affirmed our 'BBB' counterparty credit rating on the holding company, Delta Lloyd N.V.,

and financing company Delta Lloyd Treasury B.V., and affirmed all related debt ratings. The outlook is negative.

The affirmation reflects our view of Delta Lloyd's strong and sustainable competitive position in the highly competitive Dutch insurance market. Delta Lloyd occupies one of the top five positions in various lines in the non-life sector in the Netherlands (motor, property, and liability) and in the life sector (e.g., pensions).

Delta Lloyd's capital adequacy was reinforced by a successful rights issue in April 2016. However, we have seen persistent earnings volatility over the past 12-18 months demonstrating the insurer's high sensitivity to market fluctuations; this caps our risk position assessment to moderate. Earnings volatility arises from both the life and non-life operating business units, despite various management actions aimed at reducing risk on the balance sheet, such as investment portfolio reallocations.

The adoption of a new International Financial Reporting Standards discount curve gives a one-off boost of €326 million and therefore we forecast net income after tax of over €450 million in 2016. Net income is expected to be more normalized in 2017, at more than €250 million, followed by €300 million in 2018. We also forecast average return on equity (ROE) of 10%, average return on revenue including unrealized gains/losses of 8%, return on assets excluding realized gains/losses of 0.3%, and a net combined loss and expense ratio of 97% for 2016-2018. We also expect Delta Lloyd's fixed-charge coverage ratio to exceed 4x in 2016-2018.

As of June 30, 2016, Delta Lloyd had increased the proportion of cash within its liquid assets to 5% from almost 0%. As a result of Delta Lloyd's more liquid asset mix, we are revising our assessment of its liquidity to exceptional from strong. In addition, Delta Lloyd's increased access to revolving credit facilities would ease its liquidity position should the need arise. We do not expect Delta Lloyd's collateral posting risk to threaten its liquidity.

We are closely monitoring announcements from Delta Lloyd's peer, Netherlands-based insurer NN Group, which has said it intends to buy Delta Lloyd. Although Delta Lloyd's creditworthiness could benefit from its acquisition by a larger and higher-rated insurer, we consider that the uncertainties surrounding the capital and earnings and financial flexibility of the combined group after the transaction offset the positives. That said, in our view, the potential transaction is unlikely to have a short-term negative impact on Delta Lloyd's balance sheet or business profile.

The negative outlook reflects the execution risk linked to Delta Lloyd's ongoing efforts to reduce risk on its balance sheet, strengthen financial flexibility, and sustain the turnaround of its operating performance. We consider that Delta Lloyd's balance sheet derisking is almost complete, but it

has yet to make tangible progress on improving its financial flexibility and operating performance.

We could lower the rating over the next six to 24 months if Delta Lloyd's financial risk profile deteriorates, as demonstrated by capital adequacy falling below the 'BBB' benchmark, its fixed-charge coverage declining below 4x, or its operating performance metrics continuing to compare unfavorably with Dutch peers.

We could revise the outlook to stable over the next 12-18 months if Delta Lloyd's financial risk profile stabilizes, as indicated by a sustainable improvement in earnings, fixed-charge coverage remaining above 4x, and its capital adequacy settles sustainably at the upper end of the 'BBB' range or above.

RELATED CRITERIA

- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Insurance - General: Enterprise Risk Management, May 07, 2013
- Criteria - Insurance - General: Insurers: Rating Methodology, May 07, 2013
- General Criteria: Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 07, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 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, Sept. 14, 2009
- Criteria - Insurance - General: Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

RELATED RESEARCH

- Delta Lloyd Operating Companies 'A-' Ratings Affirmed After Cash Offer From NN Group; Outlook Negative, Oct. 7, 2016

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