MOODY'S
INVESTORS SERVICE

CREDIT OPINION
26 March 2019

Update

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RATINGS

AG Insurance

Domicile	BRUSSELS, Belgium
Long Term Rating	A2
Type	Insurance Financial Strength - Fgn Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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AG Insurance

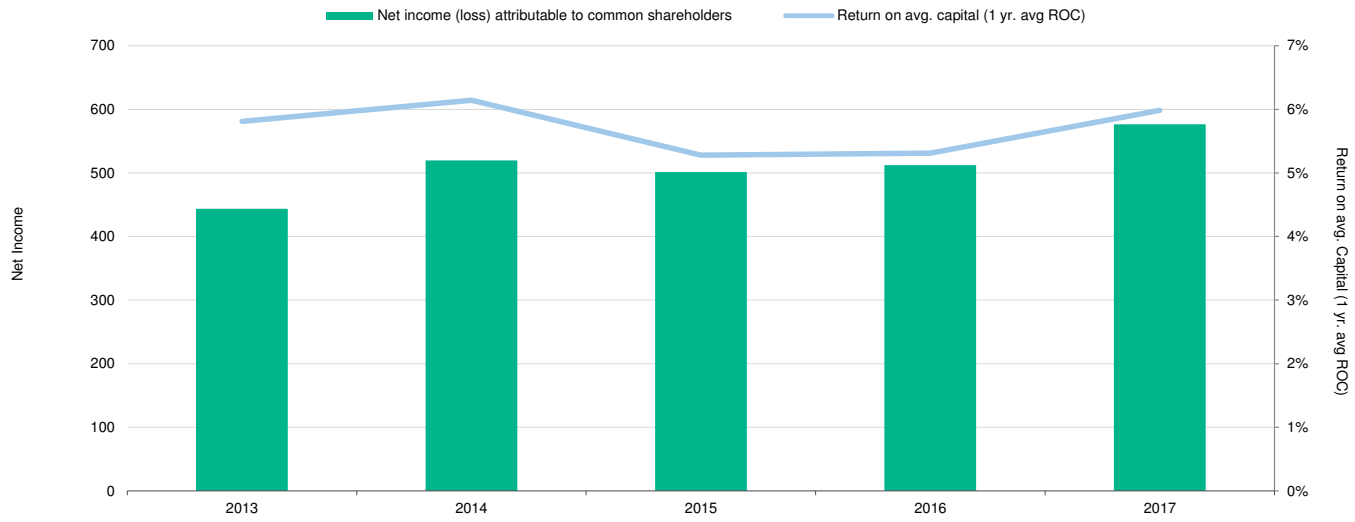
Update to credit analysis

Summary

The credit profile of AG Insurance (rated A2 for insurance financial strength) is supported by the company's (1) leading market position in Belgium, (2) diversified business profile, and (3) solid capitalisation. These strengths are partly offset by the company's reliance on third-party distribution channels and potential constraints on premiums given the Belgian market is mature and offers limited opportunity to grow. Positively, AG Insurance has shown a consistent profitability over a number of years as a result of disciplined underwriting in both life and non-life. In its life segment, AG Insurance has been proactive in reducing guarantees on new business so as to mitigate the strain on its financial margins. We expect AG Insurance to be able to cope with the low interest rate environment, given its good asset-liability management (ALM) with a low duration gap limiting the reinvestment risk. In non-life, the issuer has reported good underwriting profitability since 2015, with combined ratios ranging between 91-96%, in spite of a competitive domestic market.

Exhibit 1

Net income and return on capital (1-year average ROC)



Sources: Company reports, Moody's Investors Service

Credit strengths

» Strong market positions in Belgium in both the life (largest market share by premiums) and non-life segments (second largest)

» Good diversification of its business profile across individual life, group life and non-life activities

» Strong capitalisation and ALM

Credit challenges

» Control of distribution channels

» Reporting premiums growth in a mature and competitive domestic market

» Managing reinvestment risk in the current low interest rate environment while maintaining good asset quality

Rating outlook

AG Insurance's IFSR carries a stable outlook, primarily driven by our expectation that the company will maintain a leading market position, as well as solid capitalisation and consistent operating performances over the next 12-18 months.

What could change the rating - Up

Positive rating pressure for AG Insurance could arise from a combination of:

» An improvement in profitability with a 5-Year Return on Capital consistently above 7%

» An improvement in asset quality with a lower amount of holdings invested in relatively volatile assets such as Equities and Real Estate, resulting in a high risk asset ratio (as a proportion of Shareholders Equity) below 80%

What could change the rating - Down

The following factors could exert downward pressure on the rating:

» A material deterioration in capital adequacy and/or

» A material deterioration in net income with Return on Capital decreasing to below 4% and/or

» Adjusted financial leverage at Ageas Group, AG Insurance's majority shareholder, consistently above 40% with earnings coverage below 4x

Key indicators

Exhibit 2

AG Insurance [1][2]	2017	2016	2015	2014	2013
As Reported (Euro Millions)					
Total Assets	75,625	76,607	74,006	74,260	67,432
Total Shareholders' Equity	7,060	6,501	6,810	6,488	5,025
Net income (loss) attributable to common shareholders	583	521	512	522	447
Gross Premiums Written	4,993	5,659	5,187	5,444	5,394
Life Insurance Gross Premiums Written	3,077	3,777	3,306	3,551	3,539
Property & Casualty Insurance Gross Premiums Written	1,427	1,404	1,389	1,380	1,339
Net Premiums Written	4,932	5,603	5,126	5,367	5,323
Moody's Adjusted Ratios					
High Risk Assets % Shareholders' Equity	102.0%	107.3%	96.2%	95.6%	108.7%
Reinsurance Recoverable % Shareholders' Equity	3.5%	4.2%	3.2%	4.1%	3.9%
Goodwill & Intangibles % Shareholders' Equity[3]	13.8%	15.1%	18.7%	19.5%	22.6%
Shareholders' Equity % Total Assets	8.5%	7.7%	8.5%	8.0%	6.9%
Return on avg. capital (1 yr. avg ROC)	6.0%	5.3%	5.3%	6.1%	5.8%
Sharpe Ratio of ROC (5 yr. avg)	1450.3%	1297.4%	58.5%	58.5%	NA
Adv./(Fav.) Loss Dev. % Beg. Reserves (1 yr. avg)	2.7%	1.4%	-4.6%	-1.9%	-3.5%
Financial Leverage[3]	25.4%	27.3%	23.8%	25.2%	25.0%
Total Leverage[3]	39.0%	41.4%	36.6%	38.0%	39.9%
Earnings Coverage (1 yr.)[3]	10.4x	4.2x	9.9x	7.6x	6.6x

[1] Information based on IFRS financial statements as of Fiscal YE December 31
[2] Certain items may have been relabeled and/or reclassified for global consistency
[3] Information based on IFRS financial statements of Ageas SA/NV as of Fiscal YE December 31
Sources: Company reports, Moody's Investors Service

Profile

AG Insurance is the leading insurance company in Belgium, with around 25% market share (based on gross inflows) in the life segment (largest in the domestic market) and around 16% market share in the non-life segment (second largest) in 2017. The company's business mix consists of non-life (33%), and life and savings (67%), based on 2018 gross inflows. The company's products are mostly sold through brokers and the BNP Paribas Fortis SA/NV's network. BNP Paribas Fortis (BNPPF; A1 stable; A2 stable; baa1)[1], a subsidiary of BNP Paribas Group (Aa3 stable; baa1)[2], holds a 25% share in AG Insurance. AG Insurance's parent, Ageas SA/NV (Ageas; Long Term Issuer rating A3 stable) holds a 75% controlling stake in AG Insurance via Ageas Insurance International N.V., which is the intermediate holding company for Ageas' insurance operations.

As of year-end 2018, Ageas SA/NV reported for its Belgium operations a net result of €415 million and shareholders' equity of €5.1 billion.

Detailed credit considerations

We rate AG Insurance A2 for insurance financial strength, in line with the rating indicated by Moody's Insurance Financial Strength Rating Scorecard.

Insurance financial strength rating

The key factors currently influencing the rating and outlook are:

Market position and brand: Sustained leadership and stable franchise

AG Insurance is the leading insurance franchise in Belgium, ranking number one in life and number two in non-life. Despite the challenges experienced by the company's parent during the break-up of the Fortis group in 2008 and 2009, AG Insurance has maintained a leading market position, which demonstrates the stability of its franchise within the domestic market. Furthermore, the exclusive distribution agreement between AG Insurance and BNPPF, the largest bank in Belgium, enables the company to maintain access to a very large client base, especially in the retail life segment. However, as in many mature European markets, competition between banking and insurance savings products is high in Belgium, which may affect premium growth for AG Insurance.

Distribution: Predominantly through independent channels

Bancassurance is the largest source of sales for AG Insurance. However, the company also maintains significant alternative distribution capacity, including independent brokers and direct sales, especially in the employee benefits segment.

The existing agreement with BNP Paribas Group provides AG Insurance with an exclusive distribution relationship with BNPPF. The agreement is open-ended but subject to termination with a three-year notice period. Regardless of the strategic partnership between their respective majority shareholders (Ageas and BNP Paribas Group), AG Insurance and BNPPF do not belong to the same group, hence we consider AG Insurance's control of this distribution channel to be relatively low, in comparison to the overall rating level. The high proportion of sales through brokers also contributes to AG Insurance's relatively low control of the distribution strategy, notwithstanding the preferred position with brokers the company holds. Therefore, we consider AG Insurance's distribution strategy consistent with a Baa rating.

Product risk and diversification: Good business diversification, relatively high but decreasing product risk in the life segment

AG Insurance's business portfolio is well diversified, with a 67%/33% split between the life and non-life businesses respectively, based on 2018 gross inflows. In addition, the company's non-life book has a relatively low risk profile with approx. 63% of non-life gross inflows concerning short-tail lines such as motor and home, with the remainder primarily coming from the health and third-party liability lines. Nonetheless, AG Insurance is also exposed to workers' compensation insurance, a long-tail line of business, and the company has no geographical diversification beyond its domestic market.

Furthermore, AG Insurance's life book has a relatively high risk profile, given the high proportion of guaranteed products, which have historically included high guaranteed rates in the Belgian market. Although guarantees on new business have been reduced significantly in the past few years to 0.25%, some products sold through banks have seen an increase to 0.5% since the first quarter of 2018. Moody's notes that as of year-end 2018 the average guaranteed rate on the company's inforce book is at 2.17%, which is high relative to the yield on the 10-year Government bond (c. 0.77% as of December 2018). More positively, the yield on AG Insurance's fixed

income portfolio at year-end 2018 at around 3.3% remains well above the average guaranteed rate and the company's parent Ageas maintains good matching between consolidated assets and liabilities. We expect AG Insurance to manage its portfolio with a duration gap close to zero.

The company has been trying to reduce product risk in its life segment by increasing the proportion of unit-linked (UL) products. However, the demand for UL products has historically been limited in Belgium. Also, the size of UL products on AG Insurance's balance sheet is still relatively modest at about 13.7% of gross technical liabilities in the life segment (year-end 2017). As of year-end 2018 guaranteed products represented about 79% of total life inflows, partly reflecting a limited appetite for market rate products on the domestic market.

Asset quality: Good asset quality with modest re-risking

The quality of the company's assets is good, supported by a low level of reinsurance recoverables and relatively low level of goodwill and intangibles on the balance sheet, both at AG Insurance and at Ageas consolidated level. Exposure to high-risk assets as a percentage of shareholders' equity was at 102% as of year-end 2017 and we do not expect significant changes given the company's conservative investment approach.

Positively, the average quality of the €47.4 billion bond portfolio, which represented around 75% of the year-end 2017 investment portfolio, remains strong (around 78% of debt securities rated A3 or above). Some concentration risk exists, though it is to highly rated sovereign debt (Belgium, Aa3 stable and France, Aa2 positive).

Capital adequacy: Robust regulatory capitalisation

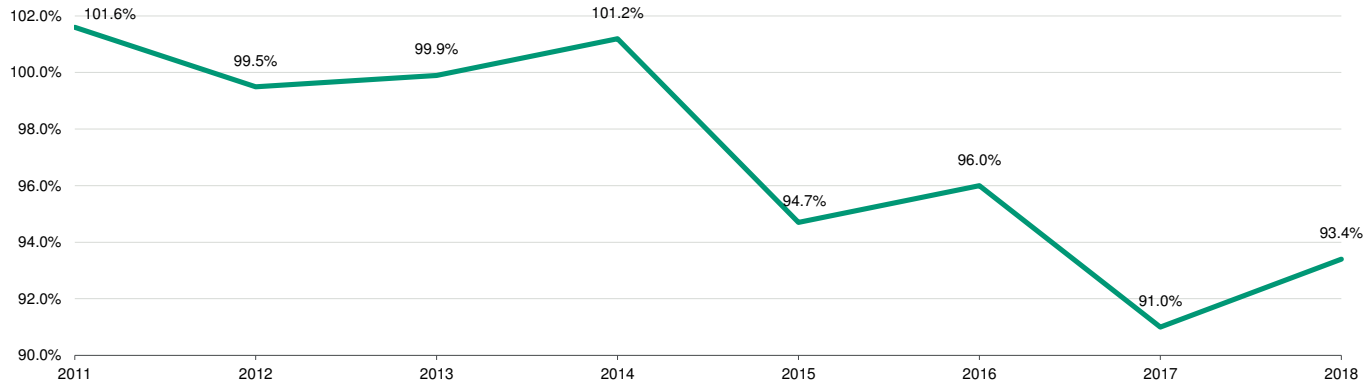
We continue to view AG Insurance's capitalisation as robust and consistent with its risk profile. In 2018, Ageas' business segment "Belgium" - whose vast majority is consisting of AG Insurance's balance sheet - reported a Solvency II (SII) coverage ratio of 222% based on its partial internal model adjusted for non-life insurance risks.

The SII ratio does not include transitional or temporary measures other than those applied to the grandfathering of AG Insurance's subordinated debt. Given the high proportion of government bonds on the issuer's balance sheet, the SII coverage ratio would decreased by 60 percentage points (pp) if the credit spreads on these investment were to increases by 50 bps, or decrease 35pp and 10pp if the value of properties were to decrease by 20% and equities by 25%, respectively (sensitivities as of year-end 2017).

Profitability: Relatively stable profitability in both non-life and life business segments

In the non-life segment, at year-end 2018, the operating results declined to €223 million (2017: €265 million), mainly due to adverse weather events which accounted for 2.8pp increase in claims ratio and thus drove the increase in the combined ratio to 93.4% (2017: 91.0%). Prior year loss reserve releases continue to positively influence reported claims ratios, by 8.3pp in 2018 (7.7% points in 2017). Also, in line with previous years, the company's expense ratio continues to be consistently above 35% (2018: 37.4%; 2017: 37.9%), which is higher than that of European peers.

Exhibit 3
AG Insurance's Combined ratio for 2011-2018



Sources: Ageas SA/NV reports, Moody's Investors Service

The operating results for the life segment have been very stable in recent years. In 2018, operating result remained solid at €438 million (2017: €435 million), supported by an improved underwriting result that offset the decrease in investment result stemming from lower investment income. We expect the investment component of the operating result to remain constrained in the current low interest rate environment.

Operating margins in the life segment remained fairly stable too. Guaranteed life reported margin for 2018 was 85 basis points (bps) in line with the previous year, which was adequate given the low interest rate environment and within the issuer's 85bps-90bps target range (now increased to 85bps-95bps with Ageas' new 2021 business plan). UL products reported strong inflow increases by 11% in 2018 with an improved 40bps margin (2017: 34bps), in line with the issuer's updated target range of 30bps-40bps.

We expect AG Insurance's profitability to withstand the low interest rate environment and to manage its exposure to the high guarantees in its life backbook on the basis of (1) the company's proactivity in decreasing guarantees on new business when facing increasing strain from lower interest rates; (2) the reduced returns to policyholders on policies including profit-sharing mechanisms; and (3) the company's disciplined ALM, with a duration gap close to zero, which limits reinvestment risk.

Liquidity and ALM: Adequate ALM discipline

We believe the company is intrinsically exposed to a decrease in interest rates reflecting the high guarantees granted to policyholders in the past, which resulted in an average guaranteed rate of 2.17% as of end-2018. Positively, AG Insurance has managed this risk by building a low interest rate reserve for past guarantees and by closely matching its assets to its technical liabilities. The above are likely to limit the negative impact of prolonged low rates.

The company is also exposed to the risk that an increase in interest rates could at the same time hurt the market value of the fixed-income portfolio and create a liquidity shock for the company via potential lapses, although some high guarantees and surrender penalty mechanisms currently limit this risk.

Reserve adequacy: Some exposure to long-tail risk, significant reserve releases in recent years

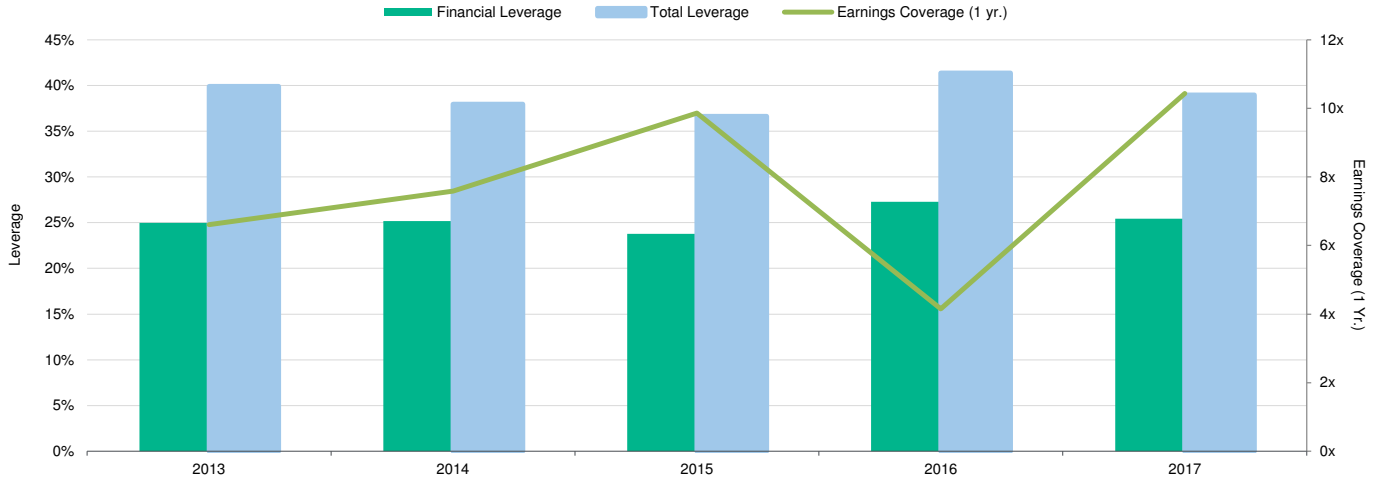
AG insurance's non-life business is concentrated on short-tail business lines with limited reserving risk, however the company's workers' compensation business is longer tail. In view of this, we consider AG insurance's reserving approach prudent. AG Insurance's loss reserve development has been favorable with positive run-off results since 2015.

Financial flexibility: Improving financial flexibility at Ageas

Consistent with our methodology, we assess financial flexibility at the group level. For more information please see Ageas SA/NV.

Exhibit 4

Financial flexibility



Sources: Company reports, Moody's Investors Service

Rating methodology and scorecard factors

Exhibit 5

Financial Strength Rating Scorecard [1][2]	Aaa	Aa	A	Baa	Ba	B	Caa	Score	Adj Score
Business Profile								Aa	A
Market Position and Brand (20%)								Aaa	A
- Relative Market Share Ratio	X								
Distribution (5%)								Baa	Baa
- Distribution Control				X					
- Diversity of Distribution			X						
Product Focus and Diversification (10%)								Baa	A
- Product Risk - P&C			X						
- Product Risk - Life					X				
- Product Diversification	X								
- Geographic Diversification					X				
Financial Profile								Aa	A
Asset Quality (10%)								A	A
- High Risk Assets % Shareholders' Equity				102.0%					
- Reinsurance Recoverable % Shareholders' Equity	3.5%								
- Goodwill & Intangibles % Shareholders' Equity[3]	13.8%								
Capital Adequacy (15%)								Aa	A
- Shareholders' Equity % Total Assets		8.5%							
Profitability (15%)								Aa	A
- Return on Capital (5 yr. avg)			X						
- Sharpe Ratio of ROC (5 yr. avg)	X								
Liquidity and Asset/Liability Management (5%)								A	A
- Liquid Assets % Liquid Liabilities			X						
Reserve Adequacy (5%)								A	A
- Adv./(Fav.) Loss Dev. % Beg. Reserves (5 yr. wtd avg)			X						
Financial Flexibility (15%)								A	A
- Financial Leverage[3]		25.4%							
- Total Leverage[3]			39.0%						
- Earnings Coverage (5 yr. avg)[3]			7.7x						
Operating Environment								Aaa - A	Aaa - A
Aggregate Profile								Aa3	A2

[1] Information based on IFRS financial statements as of Fiscal YE December 31
[2] The Scorecard rating is an important component of the company's published rating, reflecting the stand-alone financial strength before other considerations (discussed above) are incorporated into the analysis
[3] Information based on IFRS financial statements of Ageas SA/NV as of Fiscal YE December 31
Source: Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
AG INSURANCE	
Rating Outlook	STA
Insurance Financial Strength	A2

Source: Moody's Investors Service

Endnotes

1 The ratings shown are the Long-term deposit rating, Senior unsecured rating and Baseline Credit Assessment (BCA)

2 The ratings shown are the Long-term deposit rating and Senior unsecured rating, and Baseline Credit Assessment (BCA)

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