

Research Update:

Finland-Based Pohjola Non-Life Insurance Co. Ltd. Affirmed At 'AA-' After Insurance Criteria Change; Outlook Negative

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Overview

- Following a review of Finland-based Pohjola Non-Life Insurance Co. Ltd. under our revised insurance criteria, we are affirming our 'AA-' ratings on the company.
- The ratings predominantly reflect our view of the company's core status to Pohjola Bank PLC and the wider OP-Pohjola group, owing to its successful bancassurance business model in Finland and the insurer's contributions to the group's earnings through insurance commission revenues.
- The negative outlook reflects that on Pohjola Bank, which is caused by rising economic risks in Finland. We expect the insurer to remain an intrinsic part of the OP-Pohjola group.

Rating Action

On July 5, 2013, Standard & Poor's Ratings Services affirmed its 'AA-' insurer financial strength and counterparty credit ratings on Finland-based Pohjola Non-Life Insurance Co. Ltd. (Pohjola). The outlook is negative.

Rationale

The ratings on Pohjola reflect our view of its core status as the non-life insurance subsidiary of the Finland-based OP-Pohjola financial services group.

In our view, Pohjola is an integral part of the parent group's strategy. It distributes insurance products to the corporate customers of its immediate parent, Pohjola Bank PLC, and to the retail and small and midsize enterprise (SME) customers of the cooperative banks of its ultimate parent, OP-Pohjola. In so doing, Pohjola contributes to a full financial services offering across all client sectors in Finland.

Pohjola has established a strong competitive position, in our view, based on its function within the group and its franchise and product diversity. The company is the largest non-life insurer in its domestic market and had a market share of around 30% in 2012, writing €1.1 billion in premium. Pohjola is also consistently ranked as a top-two Finnish insurer across all its main businesses. The company's competitive advantage is further enhanced by its proven ability to expand the distribution of its products through the bank

infrastructure and cross-selling and by generating high customer loyalty. In our base-case scenario, we assume that company will continue to grow above the market average, at about 7%, for the next two years.

Our view of Pohjola's core status to the group is also supported by its operating performance, which has been reasonably successful and is in line with group targets. Nevertheless, although we consider that Pohjola's strengthening earnings reflect its competitive position, we view Pohjola's capital and earnings as only upper adequate. This reflects our opinion that, in the long term, the company will maintain capital adequacy at about the 'BBB' level it has historically achieved, because of the group's centralized capital management policy. In addition, because the company has a high proportion of annuity-based workers' compensation business it pursues a high-risk investment strategy with associated increased asset-liability mismatch and duration risk. Although earnings have improved recently, the company's investment strategy could lead to some earnings volatility. In our base-case scenario, we expect that the combined (loss and expense) ratio will improve to below 95% in 2013-2014, unless the regulator unexpectedly imposes a requirement to increase reserves. Over the same period, we expect return on revenue to exceed 15%.

Outlook

The negative outlook on Pohjola reflects that on Pohjola Bank, which in turn reflects rising economic risks in Finland. We expect Pohjola to remain core to the OP-Pohjola group because of the contribution it makes to the banking division's business generation and profitability.

We could lower the ratings on Pohjola after a similar action on Pohjola Bank or in the unlikely event that Pohjola's credit profile deteriorated to such an extent that we revise our view of its role within the group.

We could raise the ratings on Pohjola following a similar action on Pohjola Bank, which we consider unlikely at this stage.

Related Criteria And Research

Related criteria

- Insurers: Rating Methodology, May 7, 2013
- Group Rating Methodology, May 7, 2013
- Enterprise Risk Management, May 7, 2013
- Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Principles Of Credit Ratings, Feb. 16, 2011
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Related research

- List Of Issuers With Ratings Under Criteria Observation Due To S&P's New Insurers Rating Methodology, May 7, 2013
- Standard & Poor's Assigns Insurance Industry And Country Risk Assessments, May 7, 2013

Ratings List

Ratings Affirmed

Pohjola Non-Life Insurance Co. Ltd.

Counterparty Credit Rating

Local Currency

AA-/Negative/--

Financial Strength Rating

Local Currency

AA-/Negative/--

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