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Powszechny Zaklad Ubezpieczen S.A.

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Powszechny Zaklad Ubezpieczen S.A.

Anchor	a-

+

Modifiers	0

=

SACP	a-

Business Risk	Strong
Competitive position	Very strong
IICRA	Moderately high
Financial Risk	**Strong**
Capital and earnings	Very strong
Risk exposure	Moderately high
Funding structure	Neutral

Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0

+

Support	0
Group support	0
Government support	0

=

A-/Stable/--
Financial strength rating

IICRA--Insurance Industry And Country Risk Assessment.
SACP--Stand-alone credit profile.

Credit Highlights

Overview

Key strengths	Key risks
Powszechny Zaklad Ubezpieczen (PZU, the group) is the largest financial conglomerate in Poland with a leading position in life and non-life insurance, as well as asset management, further enhanced by its investments in the Polish banking sector.	Bank payment holidays, weaker economic environment, and higher inflation in Poland could lead to further earnings volatility coming from its material investments in Bank Polska Kasa Opieki S.A. (Bank Pekao; BBB+/Stable/A-2) and Alior Bank S.A. (BB/Stable/B).
Well-diversified insurance portfolio with scale advantages, large own-agency network, and strong brand reputation in Poland.	Limited geographic diversification, with most business and earnings concentrated in Poland.
Sizable capital buffer at the 'AAA' level as per our risk-based capital model, supported by the group's underwriting discipline and sound reinsurance protection, which together allows robust ongoing business profitability.	

PZU's diversified operations enables it to source growth despite the Polish insurance market currently observing a period of higher competition in non-life obligatory motor line. PZU's undisputed leadership in the Polish life and non-life insurance market provides opportunities for profitable growth. PZU's leading position in retail property and commercial insurance continues to support its solid growth. As a result, the group's gross written premium (GWP) in 2022 grew by 6.5% to PLN26.7 billion (€5.7 billion). We believe PZU in 2023 and thereafter will continue benefiting from its significantly more diversified portfolio. In addition, its insurance operations in Baltic states and leading asset management business in Poland will provide further business and geographical diversification. Overall, we expect the company to continue displaying moderate growth levels at around 4%-10% in 2023-2024, safeguarding business stability and resilient operating performance.

PZU earnings in 2023-2024 to remain resilient due to continued disciplined underwriting. The group's 2022 earnings remained strong at the 2021 level of earnings. The investment contributions from its stakes in banks remained resilient despite implementation of cross-market bank payment holidays in Poland. In its insurance business, the group sustained strong non-life underwriting performance with a combined ratio of around 89.6%, while its life business margin gradually recovering to 17.4% in 2022. Even amid an expected weaker economic environment in Poland in 2023, we think PZU is well placed to sustain soundly performing insurance operations. This is to be complemented by income from its bank investments. Overall, we believe the group will sustainably source net income of at least PLN2.2 billion in 2023-2024, with 12%-15% return on equity.

In our view, PZU's very sound capital position continues to be a key ratings strength. Despite a more challenging economic environment we think PZU's balance sheet remained resilient and its capital position above the 'AAA' level in 2022, according to our risk-based capital model. In our view, PZU's excellent capital adequacy and good ongoing profitability has helped it counterbalance significant market volatility in Polish banking equity values during 2022. Going forward, we expect the group will maintain capitalization at least in the 'AA' range of our insurance capital model over the next two to three years, while the group continues to pursue solid organic growth opportunities.

Outlook: Stable

The stable outlook reflects our view that the group can sustain its leading business position in Poland, as well as the strength and stability of its capital position and insurance earnings, thereby enabling it to withstand potential further macroeconomic deterioration. In addition, we anticipate that PZU's banking and asset management businesses will continue to generate satisfactory earnings.

Downside scenario

We consider a negative rating action in the next 12-24 months remote. However, we could take a negative rating action if, contrary to our current expectations, the group:

- Materially and consistently underperformed its domestic and international insurance peers;
- Substantially increased business or investment risk exposures, leading to higher capital requirements and materially increased risk of earnings volatility; or
- Experienced a material balance-sheet loss that reduced capital below our 'AA' benchmark and brought into question the effectiveness of PZU's risk management.

Upside scenario

In the next 12-24 months, we could consider a positive rating action if the group's:

- Capital adequacy remained consistently at, or above, the 'AA' benchmark, while continuing to sustainably pass our hypothetical foreign currency sovereign stress test;
- Banking investments were successfully adapted to the changed business cycle to allow growth of profit contributions to PZU; and
- Insurance performance remained resilient, with the non-life combined ratio at or below 92% and the life business margin at about 20%. In this scenario, we would expect combined insurance and banking contributions leading to reported net income after tax exceeding PLN2.6 billion.

Key Assumptions

- The Polish economy is expected to grow by about 0.9% in 2023 and then recover to 3.2% in 2024.
- Unemployment rate to remain in the 3% range over 2023-2024.
- High inflation in 2022, estimated at 13.2%, to remain elevated in 2023 at around 13% and to reduce to around 6% in 2024.

Powszechny Zaklad Ubezpieczen S. A.--Key Metrics

(Mil. PLN)	2024f	2023f	2022	2021	2020	2019	2018	2017	2016
Gross premiums written (mil. PLN)	30,000 - 28,500	28,500 - 27,000	26,710.0	25,080.0	23,866.0	24,191.0	23,470.0	22,847.0	20,308.0
Change in gross premium written (%)	4 - 8	4 - 9	6.5	5.1	(1.3)	3.1	2.7	12.5	10.6
Net income (mil. PLN)	> 2200	> 2200	3,374.0	3,336.0	1,912.0	3,295.0	3,213.0	2,895.0	1,935.0
Return on shareholder equity (%)	12 - 15	12 - 15	19.5	18.6	10.9	21.2	22.1	21.4	14.9
P/C net combined ratio (%)*	< 93	< 93	89.6	89.2	88.2	88.5	87.1	89.6	95.7
Fixed-charge coverage	> 10	> 10	23.8	102.8	41.0	44.8	35.3	45.2	54.1
Financial leverage (%)§	~ 15	~ 15	15.2	16.0	12.7	14.2	28.7	28.7	22.8
S&P capital adequacy	At least very strong	At least very strong	Excellent**	Excellent	Excellent	Excellent	Excellent	Excellent	Excellent

*Reported by PZU Group. **Estimate. § Includes only debt issued by insurance operations. f--Forecast under Standard & Poor's base-case scenario. PLN--Polish zloty.

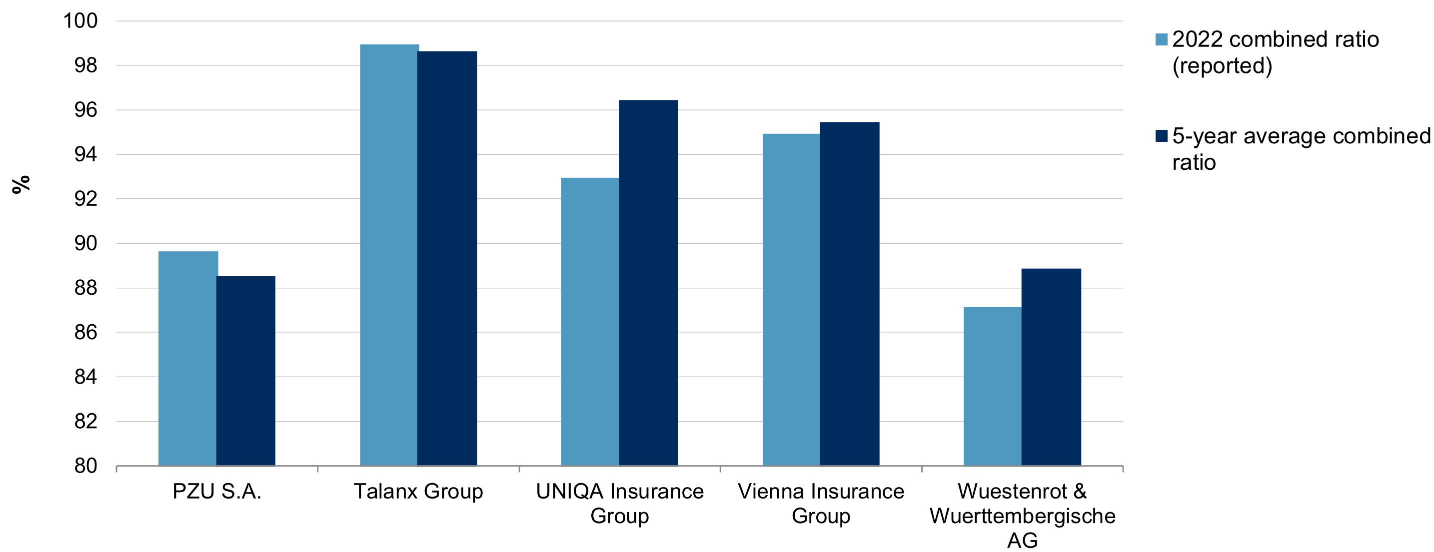
Business Risk Profile: Strong

PZU is the largest financial conglomerate in Poland. It is the largest insurer in Poland, and has insurance operations throughout all three Baltic states and small operations in Ukraine. At the end of 2022, the group's GPW totaled around PLN26.7 billion (€5.7 billion). Its asset manager is among the largest in Poland, complementing the group's overall business strength. In addition, PZU is a strategic investor in the Polish banking sector. In 2017, the group bought 20% of Bank Pekao, the second-largest bank in Poland. Furthermore, since 2016, it has owned a 32% stake in midsize Alior Bank in Poland.

In our view, the insurance sector in Poland is still coping well with lower economic growth, higher inflation, tighter monetary conditions, and increased geopolitical risks. Despite these challenges, in 2022 the sector remained relatively resilient, with some premium growth, solid-but-moderating underwriting profitability, and relatively stable investment results. We believe underwriting margins have slightly weakened in 2022 and will continue to weaken in 2023 due to higher competition in the obligatory motor line and an ongoing regulatory review of unit-linked products suitability. However, reduced underwriting margins may be offset by higher investment results due to higher interest rates in Poland. PZU's leading positions in Poland--in 2022 it had a market share of about 33% in non-life insurance and 43% in life--through its entities Powszechny Zaklad Ubezpieczen S.A. (A-/Stable/--), Towarzystwo Ubezpieczen Wzajemnych Polski Zaklad Ubezpieczen Wzajemnych (A-/Stable/--), Link4 Towarzystwo Ubezpieczen S.A. (not rated) and Powszechny Zaklad Ubezpieczen na Zycie S.A. (A-/Stable/--), enables the group to perform well through its insurance operations. Furthermore, its stakes in Polish banks provides investment income and provides longer-term opportunity to develop significant bancassurance operations in Poland. We believe PZU's large insurance market share allows some scale advantages against direct domestic competitors. In addition, its competitive edge is further driven by its established domestic reputation, with a strong brand, unrivalled tied-agent network across Poland, and a broad product range.

Chart 1

PZU's P/C Underwriting Performance To Likely Remain At Very Strong Levels In 2023



M--Months. P/C--Property/casualty. Source: S&P Global Ratings, respective companies 2022 reported combined ratio. Five-year average is for the period 2021-2017.

In our view, its diversified product offering and scale advantages gives the group considerable pricing power in Poland, enabling it to withstand softer market cycles in individual product lines. We believe that in the last few quarters PZU retained prudent underwriting despite higher inflation, cost increases, claims frequency normalization, and higher competition in the obligatory motor line. The group's selective risk taking focused on profitability resulted in slightly reduced market share in the last few quarters, particularly in the obligatory motor line. However, this has paid off, with PZU managing to maintain very robust underwriting performance.

PZU's flagship life operations again contribute around half of overall net income, while life represents around 35% of group premiums. The improvements in 2022 reflect reduced excess mortality, due to the receding pandemic, and several management actions to improve life portfolio pricing. On the other side, we think the ongoing regulatory cross-market review of unit-linked product suitability has a comparably smaller impact on PZU's performance, as the group offers proportionally fewer of these products than its domestic peers.

In our view, lower growth and elevated inflation in Poland along with still competitive motor lines could lead to some uptick in the group's combined ratio in 2023. That said, we consider PZU to still retain comparably favorable underwriting results supported by resilient property and commercial lines and the comparably strong performance of its group life portfolio. We expect PZU's unit linked performance and volumes to hold comparably better than other domestic peers. In addition, the 2021-2022 increase in interest rates in Poland will gradually improve its investment result for non-life and life, which will offset some underwriting margin reduction.

We believe commercial and property insurance rates in 2023 will continue to grow, but more slowly than in the past two years. Besides price increases, we also expect PZU will benefit from further scaling its insurance offerings, supporting the transition to a more sustainable economy and tapping the fast developing renewable energy sector in Poland. Continued inflation may lead to some market wide premium increases in motor prices in 2023-2024. In the meantime, we expect PZU will continue to leverage its strong digital capabilities--through its direct insurer Link 4--on its extensive pool of retail clients to protect motor premiums and margins. We expect that in life insurance and asset management the group will gradually extend its reach by advancing distribution cooperation with Bank Pekao and Alior Bank. In addition, the group continues developing new offers to unlock further growth in health and asset management.

Financial Risk Profile: Strong

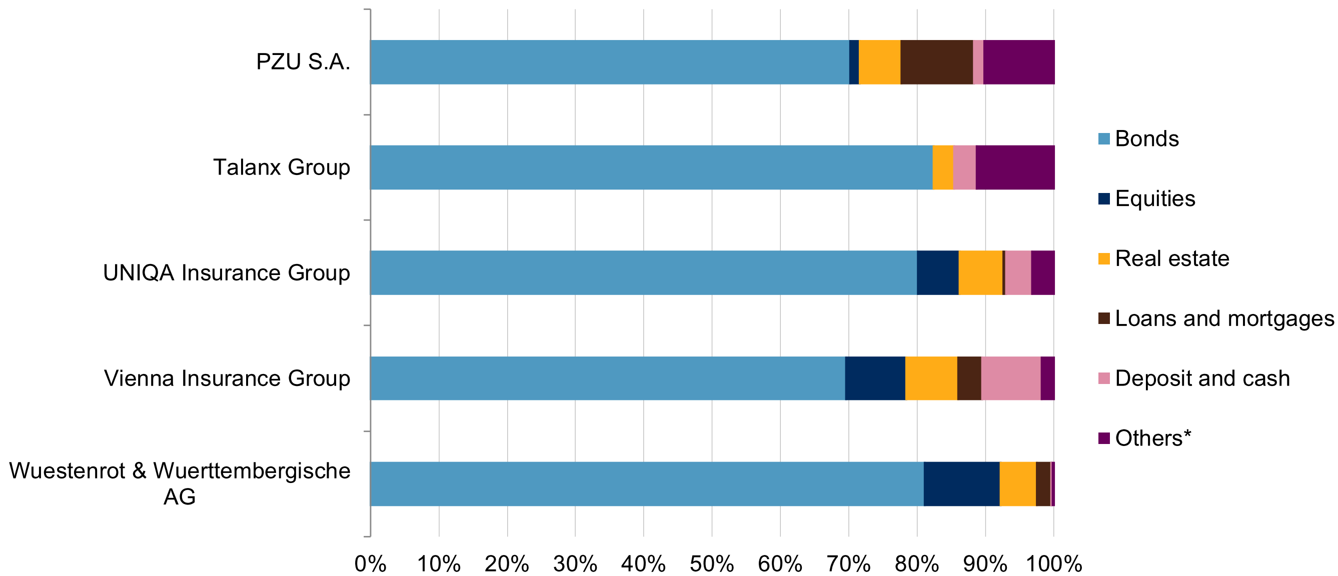
PZU's balance sheet remained resilient and its capital adequacy position is expected to have been at 'AAA' level at the end of 2022, as per our risk-based capital model. Based on a standard formula and no use of transitional adjustments, its regulatory Solvency II level remained resilient at the end of third-quarter 2022, at 230% despite capital market volatility in Poland. In fourth-quarter 2022 the group paid PLN1675 million (€350 million) in dividends in accordance with its strategy. We expect that PZU's continued solid earnings will provide ongoing capital generation, through which the group can finance expected moderate business growth while paying very solid dividends in accordance with its strategy for the next few years. In our view, we expect the group to maintain capitalization at least in the 'AA' range of our insurance capital model over the next two to three years, even if there is continued capital market volatility, a higher-than-expected increase in claims frequencies, a longer than currently expected period of elevated inflation with higher competition in motor lines on the domestic market.

PZU's equity investments into Bank Pekao and Alior Bank are around 10% of PZU's overall investments. Due to lower market value of bank equities in the first nine months of 2022, PZU's capital buffers reduced under our view of capital but remained above the 'AAA' level. Market prices materially recovered during fourth quarter 2022. That said, due to large banking equity investments, the group remains more susceptible to higher capital and earnings volatility. Outside PZU bank equity investments, other invested assets remained resilient, as a large amount of its fixed income assets are invested in Poland's sovereign bonds (local currency: A/Stable/A-1, foreign currency: A-/Stable/A-2) and are mainly accounted as hold to maturity. PZU asset exposure to Ukraine is limited and mainly related to its operations in Ukraine, which in 2022 showed GWP of PLN232 million (€50 million) and is unlikely to cause any material earnings erosion at the group.

In our view, PZU's stakes in banks make its risk framework more complex than pure insurance players. That said, the group's risk management capabilities are gradually maturing and lately leading to even further improvement in coherence and consistency of risk management across the group. We believe this helps keep in check risk accumulation and limits the impact of expected weaker economic environment in 2023.

Chart 2

PZU Investment In Affiliates (Bank Pekao And Alior Bank) Represents Comparably High Amount Of Invested Assets
2021 invested assets breakdown



*Includes affiliated companies and other investments. Source: S&P Global Ratings.

The group is materially less leveraged than its international peers. Following the 2019 senior bond repayment, the group materially reduced its leverage. Due to volatile capital markets and tightened monetary conditions, in mid-2022 PZU decided not to call the institutional hybrid debt it issued in 2017 at the bond's first call date on June 29, 2022 (see "Polish Insurer Powszechny Zaklad Ubezpieczen Doesn't Call Its 2017 Hybrid Bond But Keeps Strong Financial Position", published July 4, 2022). The fixed-charge coverage ratio for 2022 remains favorable at around 24x, but has materially reduced. This was due to a sharp increase in short-term interest rates in Poland, which increased to above 7% from 0.3% between September 2021 and June 2022. Consequently, interest payments on the PZU bond correspondingly increased. We expect that even at higher benchmark interest rates, PZU fixed charge coverage will remain above 10x in 2023-2024. We do not expect any material additional debt taking in the next two years, as such we expect financial leverage to remain rather stable at around 15%. At current levels, the group retains ample debt capacity, if needed.

Other Key Credit Considerations

Governance

PZU has credible strategic planning and conservative financial management. In the past we have seen fast and unexpected changes of CEOs and some board members. This development does not raise immediate concerns regarding the governance of the company. The changes had a relatively limited overall impact on the company's ongoing operational stability. Furthermore, new CEOs have not radically changed the company's business strategy, as evidenced by the evolution of its strategy from 2021-2024.

Liquidity

We regard PZU's liquidity as exceptional and don't expect liquidity constraints will keep it from meeting its obligations, given the substantial amount of liquid assets held by the group. In addition, expanding operations are providing constant cash inflows. Although most of the P/C business is short tail, larger risks are heavily reinsured, so larger claims are not a significant drag on the cash position. Furthermore, in our opinion, PZU's material stakes in banks gives it access to additional liquidity if needed.

Group support

PZU Banking remains one of the pillars of the group's business strategy for 2021-2024. The group is the largest investor in the Polish banking system, being the anchor investor in Bank Pekao and Alior Bank. We consider both banks moderately strategic for the group. We consider that the group has the means to support the banks if needed and will uphold its commitment to do so. Due to the already high stand-alone credit profile of Bank Pekao, we do not include any rating uplift derived from its group status to PZU. For Alior Bank, the issuer credit rating benefits from a one-notch uplift because of likely support from PZU.

Government

We consider PZU to be a government-related entity (GRE) with an important role for the Polish economy and a strong link with the Polish government, which is the group's largest and dominant shareholder, owning a 34.2% stake. Moreover, in our view, PZU, with its large and widespread agent network, plays a key role in providing insurance products to the non-urban areas of Poland. Overall, we consider that there is a moderately high likelihood that the government of Poland would provide timely and sufficient extraordinary support to PZU in the event of financial distress. Due to PZU's already high stand-alone credit profile, we do not include any rating uplift derived from the insurer's status as a GRE.

Environmental, social, and governance (ESG)

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

In our view, ESG credit factors have no material influence on our rating analysis for PZU.

Accounting considerations

PZU prepares its financial accounts in accordance with International Financial Reporting Standards.

To calculate PZU's total adjusted capital in our risk-based capital model, the largest adjustments we made to reported amounts are as follows:

- PZU provides supplementary embedded value disclosures for its life business that we use to analyze the life operating performance.
- With around 32% ownership of Alior Bank, PZU obtained control of the bank and consolidated it in its accounts as of year-end 2015. In our assessment of group capital adequacy, we reflect the market value of the group's shares in the bank.
- With 20% ownership of Bank Pekao, PZU obtained control of the bank and consolidated it in its accounts as of midyear 2017. In our assessment of group capital adequacy, we reflect the market value of the group's shares in the bank.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- 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: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Credit Conditions Europe Q2 2023: Costs Rising To Cure Inflation, March 28, 2023
- Polish Banks Remain In Choppy Waters Amid Economic Resilience And Continuing Legal Risks, Feb. 21, 2023
- Research Update: Poland 'A-/A-2' Foreign Currency Ratings Affirmed; Outlook Stable, Feb. 17, 2023
- Central and Eastern Europe Sovereign Rating Outlook 2023: The Top-Five Risks, Feb. 6, 2023
- EMEA Insurance Outlook 2023: In The Midst Of The Perfect Storm, Nov. 14, 2022
- Central And Eastern Europe: Growth Freezes, Risks Mount, Nov. 10, 2022
- Research Update: Poland 'A-/A-2' Foreign Currency Ratings Affirmed; Outlook Stable, Sept. 30, 2022

- Bulletin: Polish Insurer Powszechny Zaklad Ubezpieczen Doesn't Call Its 2017 Hybrid Bond But Keeps Strong Financial Position, July 4, 2022
- Poland Banking Industry Country Risk Assessment Unchanged On Evolving Industry Risks; No Ratings Affected, June 7, 2022

Appendix

PZU Group Credit Metrics History

Ratio/Metric	2022	2021	2020	2019	2018	2017
S&P Global Ratings capital adequacy	Excellent*	Excellent	Excellent	Excellent	Excellent	Excellent
Total shareholder equity (mil. PLN)	17,489	17,080	18,777	16,169	14,925	14,087
Gross premiums written (mil. PLN)	26,710	25,080	23,866	24,191	23,470	22,847
Net premiums written (mil. PLN)	25,043	23,780	22,850	23,179	22,715	22,235
Net premiums earned (mil. PLN)	24,334	23,232	23,024	23,090	22,350	21,354
Reinsurance utilization (%)	9.8	8.5	7.4	7.0	5.5	4.8
EBIT (mil. PLN)	4,384	4,284	2,833	4,260	4,120	3,707
Net income (attributable to all shareholders) (mil. PLN)	3,374	3,336	1,912	3,295	3,213	2,895
Return on revenue (%)	16.2	13.8	9.4	14.4	16.7	13.5
Return on shareholders' equity (reported) (%)	19.5	18.6	10.9	21.2	22.1	21.4
P/C: net combined ratio (%)	89.6	89.2	88.2	88.5	87.1	89.6
P/C: net expense ratio (%)	29.2	28.8	27.5	26.8	25.8	26.3
P/C: return on revenue (%)	N/A	N/A	N/A	N/A	N/A	N/A
Life: Net expense ratio (%)	18.0	16.1	15.3	15.0	14.4	13.6
EBITDA fixed-charge coverage (x)	23.8	102.8	41.0	44.8	35.3	45.2
EBIT fixed-charge coverage (x)	22.9	92.9	35.1	40.2	31.5	42.8
Financial obligations / EBITDA adjusted	0.7	0.6	0.8	0.6	1.3	1.5
Financial leverage (%)	15.2	13.7	12.7	14.2	28.7	28.7
Total invested assets (mil. PLN)	78,397	72,962	74,207	71,273	77,038	72,990
Net investment yield (%)	3.44	2.88	0.56	2.86	2.69	2.70
Net investment yield including realized capital gains/(losses) (%)	2.76	3.34	0.43	2.92	2.27	2.91
Net investment yield including all gains/(losses) (%)	3.06	3.82	1.36	3.59	2.47	3.40

*Estimated excellent capital adequacy at the end of 2022. PLN--Polish zloty. 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 April 24, 2023)*

Operating Companies Covered By This Report	
Powszechny Zaklad Ubezpieczen S.A.	
Financial Strength Rating	
Local Currency	A-/Stable/--
Issuer Credit Rating	A-/Stable/--
Powszechny Zaklad Ubezpieczen na Zycie S.A.	
Financial Strength Rating	
Local Currency	A-/Stable/--
Issuer Credit Rating	
Local Currency	A-/Stable/--
Towarzystwo Ubezpieczen Wzajemnych Polski Zaklad Ubezpieczen Wzajemnych	
Financial Strength Rating	
Local Currency	A-/Stable/--
Related Entities	
Alior Bank S.A.	
Issuer Credit Rating	BB/Stable/B
Bank Polska Kasa Opieki S.A.	
Issuer Credit Rating	BBB+/Stable/A-2
Resolution Counterparty Rating	A-/--/A-2
Domicile	Poland

*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.