S&P Global
Ratings

RatingsDirect®

Research Update:

Poland-Based PZU Group Outlook Revised To Positive On Ongoing Robust Performance And Capital Position; Affirmed At 'A-'

May 28, 2024

PRIMARY CREDIT ANALYST

Jure Kimovec, FRM, CAIA, ERP
Frankfurt
+ 49 693 399 9190
jure.kimovec
@spglobal.com

SECONDARY CONTACT

Johannes Bender
Frankfurt
+ 49 693 399 9196
johannes.bender
@spglobal.com

RESEARCH CONTRIBUTOR

Pratik C Giri
CRISIL Global Analytical Center, an S&P affiliate, Mumbai

ADDITIONAL CONTACT

Insurance Ratings EMEA
Insurance_Mailbox_EMEA
@spglobal.com

Overview

- Powszechny Zaklad Ubezpieczen S.A. (PZU) reported strong group operating performance for 2023 and first quarter 2024, supported by both its insurance and banking operations.
- Based on the year-end 2023 results, the group displays significant capital buffers in an extreme stress scenario (99.99% confidence level) under our risk-based capital model, which we assume will persist in our base-case scenario.
- PZU's robust capital position and ongoing operating performance allow it to pass our hypothetical foreign currency sovereign default stress test.
- We have therefore revised our outlook on PZU and its core subsidiaries to positive from stable and affirmed our 'A-' ratings.
- The positive outlook indicates that we could raise the ratings if the group continues to pass our hypothetical sovereign stress test while its earnings and capital position remain resilient.

Rating Action

On May 28, 2024, S&P Global Ratings revised its outlook on Poland-based insurer Powszechny Zaklad Ubezpieczen S.A. and its core operating subsidiaries Powszechny Zaklad Ubezpieczen na Zycie S.A. and Towarzystwo Ubezpieczen Wzajemnych Polski Zaklad Ubezpieczen Wzajemnych (together, PZU Group) to positive from stable.

We affirmed our 'A-' issuer credit and financial strength ratings on all three entities.

Rationale

The outlook revision reflects our view that PZU Group has demonstrated a track record of successful execution of its strategy, including its ambitious performance targets in its insurance and banking businesses. As a result, the group in the past year was able to generate record high net income of Polish zloty (PLN) 5.8 billion (approximately €1.3 billion). This translated into a strong return on equity of about 20.5% in the year ended Dec. 31, 2023, which was again materially better than that of domestic and international peers. Strong performance continued in the first quarter of 2024, with the group's net income further increasing by 9% year on year to PLN1.3 billion.

We believe the group's outperformance is likely to continue, since PZU in recent years has protected its leading position in the Polish non-life and life insurance markets. The non-life insurance segment continued to display very solid underwriting profitability in 2023 and first-quarter 2024 with combined (loss and expense) ratios of 85.9% and 90.1%. This was despite a more challenging underwriting environment in obligatory motor lines and generally high inflation in Poland. PZU managed to offset this through stronger performance in non-obligatory motor lines where cost and claims inflation was largely passed to policyholders through higher prices.

In life insurance, the group has implemented a number of underwriting measures following a decrease in underwriting profitability due to higher mortality in 2020-2022 amid the pandemic. These measures are now bearing fruit with life margins in 2023 recovered to more than 20%. Investments in banking operations in recent years were adapting to the changed business cycle. With currently very favorable interest rates, both banks were able to show steep growth of profit contributions to PZU in 2023 and in first-quarter 2024.

Although underwriting margins in non-life and life business may decline, we believe this will be largely offset by higher investment income, as well as by larger business scale due to expected continued solid business growth. We expect the banks' performance to slightly reduce due to prospectively lower interest rates. However, we still expect the banking segment's contributions to remain sizable at 20%-30% of total group net income. We expect that PZU group will continue to outperform its main peers, posting net income of between PLN3.6 billion and PLN5.5 billion in 2024-2026. This would translate into a return on equity of 13%-17% during that period.

PZU's financial profile underpins robust capital position based on our capital model and Solvency II. Robust earnings generation has helped PZU's capital to increase at the same pace as its rising capital requirements due to strong business growth in last few years, even as the group continued to pay relatively high dividends.

The group in recent years has maintained overall conservative financial management, including strong balance-sheet management and prudent reserve management. At the end of 2023, the group's capital adequacy remained at the 99.99% confidence level according to our risk-based capital model. Our view is supported by PZU's very solid solvency ratio of 229% (based on the standard formula, no transitional adjustment) at year-end 2023. We note that with the introduction of new accounting standard IFRS17, capital buffers in our capital model significantly increased. This was due to the group's now materially higher shareholder equity and full recognition of sizable life contractual service margin stemming from its strongly profitable life group business. We expect the group to maintain sizable capital buffers under our risk-based model in 2024-2026, despite capital market volatility affecting shareholder equity levels.

Retention of a robust capital position with upscaled and more sustainable earnings have now increased PZU's buffers in our hypothetical sovereign foreign currency default scenario. We believe this indicates that PZU Group is now unlikely to default on its foreign currency obligations under such a stress scenario. In our opinion, the likelihood that PZU will continue to pass the foreign currency sovereign stress test is now more likely.

Outlook

The positive outlook reflects our view that the group is likely to sustain favorable operating performance, as well as the strength and stability of its capital position. This would allow the group to withstand potentially tougher economic conditions or significant sovereign stress. In addition, we anticipate that PZU's banking and asset management businesses will continue to significantly support the group's earnings.

Upside scenario

In the next 12-24 months, we could consider raising the ratings in the following cases:

- The group continues to pass our hypothetical foreign currency sovereign stress test.
- Insurance performance remained resilient, with the non-life combined ratio at 95% or lower and the life business margin at 15%-20%. In this scenario, we would expect combined insurance and banking contributions leading to reported net income after tax exceeding PLN3.6 billion.
- Banking investments to remain resilient and provide stable and solid profit contribution to PZU, supporting sustainability of PZU's financial risk profile.

Downside scenario

We could consider revising the outlook to stable in the next 12-24 months if, contrary to our current expectations:

- Substantially increased business or investment risk exposures to the sovereign or Polish banking sector lead to PZU's failure to pass our hypothetical sovereign stress scenario; or
- The group's earnings display material and sustained volatility, resulting in a prolonged period of underperformance versus domestic and international insurance peers.

Environmental, Social, And Governance

In our view, environmental, social, and governance credit factors have no material influence on our rating analysis of PZU.

Ratings Score Snapshot

Financial strength rating	A-
Anchor	a-
Business risk	Strong
IICRA	Moderately High
Competitive position	Very strong
Financial risk	Strong
Capital and earnings	Very strong

Risk exposure	Moderately High
Funding structure	Neutral
Modifiers	0
Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0
Support	0
Group support	0
Government support	0

IICRA--Insurance Industry And Country Risk Assessment.

Related Criteria

- Criteria | Insurance | General: Insurer Risk-Based Capital Adequacy--Methodology And Assumptions, Nov. 15, 2023
- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, 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: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Bank Polska Kasa Opieki S.A., May 21, 2024
- Poland-Based Alior Bank Outlook Revised To Positive On Improving Risk Profile; 'BB+/B' Ratings Affirmed, May 17, 2024
- Poland 'A-/A-2' Foreign Currency Ratings Affirmed; Outlook Stable, May 10, 2024
- Insurance Industry And Country Risk Assessment: Poland Property And Casualty, Feb 26, 2024

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Powszechny Zaklad Ubezpieczen S.A.		
Issuer Credit Rating	A-/Positive/--	A-/Stable/--
Powszechny Zaklad Ubezpieczen na Zycie S.A.		
Issuer Credit Rating		
Local Currency	A-/Positive/--	A-/Stable/--
Powszechny Zaklad Ubezpieczen S.A.		
Towarzystwo Ubezpieczen Wzajemnych Polski Zaklad Ubezpieczen Wzajemnych		
Powszechny Zaklad Ubezpieczen na Zycie S.A.		
Financial Strength Rating		
Local Currency	A-/Positive/--	A-/Stable/--