FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms & Removes PartnerRe from Rtg Watch Positive; Outlook Negative on Coronavirus Pro Forma

Thu 14 May, 2020 - 10:04 AM ET

Fitch Ratings - Chicago - 14 May 2020: Fitch Ratings has affirmed and removed PartnerRe Ltd.'s (PRE) ratings from Rating Watch Positive, including its 'A-' Issuer Default Rating (IDR) and the 'A+' (Strong) Insurer Financial Strength (IFS) rating of Partner Reinsurance Company Ltd., the company's principal reinsurance operating subsidiary. The Rating Outlook is Negative.

KEY RATING DRIVERS

The removal of PRE's ratings from Positive Watch follows announcements by EXOR N.V. and Covea that the $9 billion cash deal for Covea to acquire PRE from EXOR under the terms of the memorandum of understanding announced on March 3, 2020 will not be completed. The Rating Watch Positive reflected the potential for ownership by Covea, a larger property/casualty (P/C), health and life insurance organization, to benefit PRE's ratings under a group credit approach. Fitch views EXOR's ownership as neutral to PRE's ratings.

Fitch last reviewed PRE's ratings on April 24, 2020, when Fitch maintained the ratings on Rating Watch Positive following its assessment of the impact of the coronavirus pandemic under a set of ratings assumptions described below. These assumptions were used by Fitch to develop pro forma financial metrics for PRE that Fitch compared to both ratings guidelines defined in its criteria, and relative to previously established Rating Sensitivities for PRE. Fitch had stated that absent the pending transaction with Covea, PRE's ratings would have been affirmed with a Negative Outlook under Fitch's pro forma financial analysis.

As such, the Negative Outlook reflects pro forma results that fall outside some rating sensitivities and guidelines. In particular, PRE's pro forma score on Fitch's Prism factor-based capital model declines to high in the 'Strong' category from an actual 2019 score of 'Very Strong' and breaches the rating sensitivity of failing to maintain at least a 'Very Strong' Prism score. The pro forma financial leverage ratio (FLR) of 21.0% is only modestly higher than the 19.9% actual at March 31, 2020 and remains below the 25.0% downgrade rating sensitivity and continues to be in line with an 'aa-' credit factor score.

These pro forma results reflect a 14% decline in shareholders' equity from YE 2019 that was primarily driven by Fitch's assumptions regarding a decline in stock indices and an increase in two-year cumulative high yield bond default rates. PRE maintains a manageable exposure in equities at 7% of the total investment portfolio and 18% of shareholders' equity at Dec. 31, 2019. Other invested assets comprise 18% of the total portfolio and 46% of shareholders' equity at Dec. 31, 2019, with the largest asset being corporate loans at 11% of the total portfolio and 26% of shareholders' equity. These loans are largely U.S. bank loans with a weighted average credit rating of 'BB-'/'B+'. The fixed maturity portfolio is high quality with an average rating of 'AA', 8% rated 'BBB' and 3% below investment grade/unrated at YE 2019.

The pro forma shareholders' equity decline also reflects Fitch's assumption of increased coronavirus-related reinsurance claims, although Fitch views the exposure as manageable. PRE reported a 1Q20 combined ratio of 103.8%, up from 97.7% in 1Q19, due primarily to $69 million (5.8pp) of adverse prior year reserve development compared to $11 million (1.0pp) favorable in 1Q19. The 1Q20 results also included a modest $18 million (1.5pp) of pre-tax losses from event cancellation claims associated with coronavirus that reflect estimates on claims incurred as of March 31, 2020, with potentially more sizable losses to be incurred in future quarters. Fitch's pro forma analysis also reflects exposure to somewhat higher potential mortality losses in its life reinsurance business due to the coronavirus.

PRE's operating results have been pressured recently with the non-life segment posting a three-year average (2017-2019) combined ratio and operating ratio of 101.5% and 93.5%, respectively, driven by increased catastrophe losses and a declining benefit from favorable reserve development. These results are inconsistent with both the company's historical performance and Fitch's expectations for the rating of combined ratios below 100% and operating ratios below 90%.

PRE's ratings continue to reflect the company's moderate and diverse non-life and life and health reinsurance business profile, very strong capitalization with reasonable financial leverage, strong long-term financial performance and strong reserve position.

KEY ASSUMPTIONS

Assumptions for Coronavirus Impact (Rating Case):

Fitch used the following key assumptions, which are designed to identify areas of vulnerability, in support of the pro forma rating analysis discussed above:

--Decline in key stock market indices by 35% relative to Jan. 1, 2020;

--Increase in two-year cumulative high-yield bond default rate to 16%, applied to current non-investment-grade assets, as well as 12% of 'BBB' assets;

--Both upward and downward pressure on interest rates, with spreads widening (including high-yield by 400bps), coupled with notable declines in government rates;

--Capital markets access is limited for issuers at senior debt levels of 'BBB' and below;

--A coronavirus infection rate of 5% and a mortality rate (as a percent of infected) of 1%;

--For non-life reinsurance, a negative impact on the industry-level accident year loss ratio from coronavirus-related claims at 3.5 percentage points.

RATING SENSITIVITIES

The ratings remain sensitive to any material change in Fitch's rating case assumptions with respect to the coronavirus pandemic. Periodic updates to our assumptions are possible given the rapid pace of changes in government actions in response to the pandemic, and the pace with which new information is available on the medical aspects of the outbreak. An indication of how ratings would be expected to be affected under a set of stress case assumptions is included at the end of this section to help frame sensitivities to a severe downside scenario.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A material adverse change in Fitch's ratings assumptions with respect to the coronavirus impact.

--Sustained reported combined ratios above 100%, operating ratios above 90% or net income ROE below 7%; fixed-charge coverage below 6.0x; consistent adverse loss reserve development; failure to maintain at least a 'Very Strong' Prism score; an FLR above 25%; deterioration in EXOR's credit profile.

--Hybrid securities ratings could also be lowered by one notch to reflect higher nonperformance risk should Fitch view Bermuda's regulatory environment as becoming more restrictive in its supervision of (re)insurers with respect to hybrid features.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--A positive rating action, including a return to a Stable Outlook, is prefaced by Fitch's ability to reliably forecast the impact of the coronavirus pandemic on the financial profile of both the global reinsurance sector and PRE.

--The Rating Outlook could return to Stable if PRE's actual Prism score is maintained at 'Very Strong', which Fitch believes could occur if asset market declines are materially less severe than suggested by Fitch's pro forma ratings assumptions, while posting combined ratios in line with or better than its 'A+' rated peers.

--Improvement to a favorable business profile as a result of an enhanced relative competitive market position; demonstrating favorable run-rate earnings and low volatility, with a combined ratio in the low 90% range; growth in risk-adjusted capital, while maintaining an 'Extremely Strong' Prism score; an FLR at or below 20%; fixed-charge coverage of at least 8.0x.

Stress Case Sensitivity Analysis

--Fitch's Stress Case assumes a 60% stock market decline, two-year cumulative high-yield bond default rate of 22%, high-yield bond spreads widening by 600bps, more prolonged declines in government rates, heightened pressure on capital markets access, a coronavirus infection rate of 15% and mortality rate of 0.75%, an adverse non-life industry-level loss ratio impact of 7 percentage points for coronavirus claims.

--The implied rating impact under the stress case would be a downgrade by one to two notches.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING		
PartnerRe Finance B LLC			
• senior unsecured	LT	BBB+	Affirmed
Partner Reinsurance Company Ltd.	Ins Fin Str	A+	Affirmed
PartnerRe Ltd.	LT IDR	A-	Affirmed
• preferred	LT	BBB	Affirmed
• junior	LT	BBB	Affirmed

VIEW ADDITIONAL RATING DETAILS

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The following issuer(s) did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure: PartnerRe Ltd., Partner Reinsurance Company Ltd., PartnerRe Ireland Finance DAC, PartnerRe Finance B LLC

APPLICABLE CRITERIA

Insurance Rating Criteria (pub. 02 Mar 2020) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Prism Factor-Based Capital Model, v1.7.1 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Partner Reinsurance Company Ltd.	EU Endorsed
PartnerRe Finance B LLC	EU Endorsed
PartnerRe Ireland Finance DAC	EU Endorsed
PartnerRe Ltd.	EU Endorsed

ADDITIONAL DISCLOSURES FOR UNSOLICITED CREDIT RATINGS

Partner Reinsurance Company Ltd. (Unsolicited)

With Rated Entity or Related Third Party Participation	No
With Access to Internal Documents	No
With Access to Management	No

PartnerRe Ireland Finance DAC (Unsolicited)

With Rated Entity or Related Third Party Participation	No
With Access to Internal Documents	No
With Access to Management	No

PartnerRe Ltd. (Unsolicited)

With Rated Entity or Related Third Party Participation	No
With Access to Internal Documents	No
With Access to Management	No

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SOLICITATION STATUS

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

UNSOLICITED ISSUERS

ENTITY/SECURITY	ISIN/CUSIP/COUPON RATE	RATING TYPE	SC ST
Partner Reinsurance Company Ltd.	-	Long Term Issuer Default Rating	Ur
Partner Reinsurance Company Ltd.	-	LT Financial Strength Rating	Ur
PartnerRe Ltd.	-	Long Term Issuer Default Rating	Ur
PartnerRe Ireland Finance DAC EUR notes	XS1489391109	Long Term Rating	Ur

ENTITY/SECURITY	ISIN/CUSIP/COUPON RATE	RATING TYPE	SC ST

ENDORSEMENT POLICY

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