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# Rating Action: Moody's assigns an A1 insurance financial strength rating to CNP Assurances with a stable outlook

**06 Jun 2018**

London, 06 June 2018 -- Moody's Investors Service has today assigned an A1 insurance financial strength rating (IFSR) to CNP Assurances (CNP) with a stable outlook.

CNP is the leading French life insurer primarily selling life insurance savings and protection products through the networks of La Banque Postale (unrated) and BPCE (A2 positive, adjusted BCA baa2). The group also operates in Brazil where it has a joint venture with Caixa Economica Federal (CAIXA) (Ba3 stable, BCA b1), one of the largest banks in the country.

RATINGS RATIONALE

RATING DRIVERS

The A1 IFSR reflects CNP's very strong market position in the French life insurance market, a low liability risk profile, a very stable profitability as well as a very good financial flexibility. These strengths are partly mitigated by the distribution strategy, which relies on third-party channels and is concentrated on a small number of large partners, as well as a relatively high level of high risk assets.

CNP is the number one life insurer in France with a market share of around 13% and the number four life insurer in Brazil, benefitting from exclusive distribution agreements with some of the largest banks in these two countries. In addition, CNP's market share is more than 2x the average market share of French life insurers, reflecting CNP's significantly larger market share than most of its competitors. Moody's expects CNP's market share to decline gradually over the next three to five years as, since the end of 2016, the group has stopped distributing insurance savings products through BPCE networks, but Moody's expects CNP to maintain a high relative market share.

CNP's access to very large banking networks is positive for the group's market position but Moody's also considers the concentrated distribution strategy on a few third-party banking partners as the group's main credit challenge. In 2017, 54% of CNP's premiums were sourced from the networks of La Banque Postale and BPCE in France and 16% were sourced from Caixa Economica Federal's (CAIXA) networks in Brazil. A scenario of non-renewal of one of these agreements would materially weaken the group's market position and result in a gradual but long-lasting reduction in profits. However, Moody's considers this scenario as unlikely at this stage given that CNP has secured multi-year agreements with its banking distributors and the presence of La Banque Postale and BPCE amongst its major shareholders also mitigates the risks that CNP would be forced to renegotiate its distribution agreements with these two banks at materially unfavourable conditions. In addition, CNP is diversifying its distribution strategy by developing business through its salaried sales force, direct distribution and other partnerships.

Commenting on CNP's liability profile, Moody's mentions that CNP's balance sheet is dominated by guaranteed French insurance savings and pension products (78% of CNP's average net technical reserves in 2017) that Moody's considers as relatively low risk because the average guaranteed rate on CNP's French traditional saving products is only 0.34%, one of the lowest level within European life insurers. French pension products carry some longevity risk, but these products represent less than 10% of CNP's liabilities.

As concerns profitability, Moody's mentions that the participating nature of French life savings products together with their long duration contribute to CNP's very stable profitability, as evidenced by an excellent Sharpe ratio of return on capital of 1860% in 2017. Given the low level of guarantees granted to policyholders, CNP will be able to protect its profitability even in a persistently low interest rates by passing most of the decline in investment returns to policyholders. Most of CNP's profits in the savings business are generated by fees taken out from policyholders' reserves. Nonetheless, Moody's expects the profitability of traditional guaranteed products to erode gradually because of the net outflows on these products (negative €7.7 billion in 2017, equivalent to around 3% of reserves). CNP faces the challenge of reorienting its business mix to unit-linked products and protection products, but Moody's believes that CNP has well initiated this transition, as evidenced by the growth in unit-linked premiums and reserves. CNP reported a positive €2.3 billion of net flows on unit-linked policies in 2017. In addition, CNP continues to grow earnings generated by protection products. Protection represented 40% of the group's profits before interest and tax in 2017.

CNP's consolidated profitability metrics (return on capital of 6.1% in 2017, 6.3% on a five-year average) are good. These metrics include 100% of the profits generated by its operations in Brazil that it controls only at 51.75%. However, when only taking into account the stake of CNP in its Brazilian business and in other businesses, Moody's estimates CNP's return on capital to be closer to 5%. In addition, a new agreement with Caixa Economica Federal (CAIXA) will potentially be signed in 2018 which could ultimately result in reduced profits for CNP on a proforma basis, both because of a reduction of CNP's economic rights in the Brazilian business to be underwritten through the Brazilian bank and because the new distribution agreement would cover a reduced perimeter.

According to Moody's, one of the main financial risks that CNP faces is that of a sharp increase in interest rates, which would depress the value of CNP's fixed income assets and would likely also result in an increase in surrender rates on guaranteed savings products. Moody's notes positively that CNP has implemented hedges to partly protect its asset portfolio from this risk.

Commenting on asset risk, Moody's mentions that CNP's sharing of investment results with policyholders is a key mitigant to the risk arising from the high level of equities and real estate on the balance sheet. CNP's high risk assets (namely equities, real estate and below investment grade or non-rated bonds) represented 389% of CNP's shareholders' equity as of year-end 2017. Moody's says that this ratio is high relative to most similarly rated peers, but after taking into account the hedges on the equity portfolio and the group's ability to pass on a high level of asset losses to policyholders in stress scenarios, the risk appears to be more in line with CNP's rating level.

Moody's adds that CNP's Solvency II ratio is also in line with its expectations for A-rated insurers. CNP's ratio was 190% as of 31 December 2017, but Moody's mentions that this ratio remains volatile. This volatility partly reflects the significant level of future profits included in CNP's Tier 1 capital, which Moody's says is common for life insurance groups.

As regards to financial flexibility, Moody's mentions that CNP's leverage metrics (24.7% adjusted financial leverage and 30.3% total leverage as of year-end 2017) are consistent with a strong credit profile and earnings coverage (8.3x in 2017 but around 7x when adjusting for the 51.75% stake in the Brazilian business) is consistent with CNP's rating level. Nonetheless, Moody's believes that CNP's financial flexibility is also supported by the presence of Caisse des Dépôts et Consignations (Aa2 positive) within its reference shareholders.

WHAT COULD CHANGE THE RATING UP / DOWN

CNP's rating could be upgraded in case of material improvement in geographic, business and distribution diversification. A decrease in high risk assets and improvement in capitalisation, as evidenced by a Solvency II ratio sustainably above 200%, with low volatility risk, would also exert upwards pressure on the rating.

Conversely, negative pressure could be exerted on the rating in case of: (1) the loss of a significant distribution agreement, which would materially affect CNP's franchise and financial metrics, (2) a prolonged decline in profitability with a return on capital below 5% resulting, for example, from the group's unability to grow profitably protection and unit-linked business to offset the expected gradual decline in earnings generated by the traditional savings business, (3) a reduced capitalization resulting, for example, in a Solvency II ratio consistently below 160%, or (4) an increased adjusted financial leverage to above 30% and reduced earnings coverage to below 5x, or a material change in CNP's shareholders structure which would result in a reduced financial flexibility.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Life Insurers published in May 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

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