



Credit Rating Announcement

GCR upgrades Western National SA's national scale financial strength rating to A+(ZA) from A(ZA), Outlook Stable

Rating action

Johannesburg, 10 December 2021 - GCR Ratings ("GCR") has upgraded Western National Insurance Company Limited's ("Western National SA") national scale financial strength rating to A+(ZA) from A(ZA), with the Outlook accorded as Stable.

Rated entity / Issue	Rating class	Rating scale	Rating	Outlook/Watch
Western National Insurance Company Limited	Financial strength	National	A+(ZA)	Stable Outlook

Rating rationale

The rating upgrade reflects sustained strength in Western Group Holdings Limited's ("WGHL" or "the group") financial profile, largely driven by Western National SA, which is the core operating entity. Furthermore, the rating considers the overall risk profile of the majority shareholder, PSG Konsult Limited ("PSGK"), which was upgraded in July 2021 and the rating announcement can be found at <https://gcratings.com/announcements/gcr-upgrades-psg-konsult-limiteds-national-scale-long-term-issuer-credit-rating-to-aza-on-sustained-strength-of-credit-fundamentals-and-improved-view-of-competitiveness-of-the-wealth-busi/>.

WGHL's earnings strengthened over the past two years and the trend has been sustained in the interim period to 7M F22, supported by reducing claims and a well contained operating expense ratio. The two-year average underwriting margin registered at c. 14% versus 7% between FY17 and FY19 and remained strong at 15% in 7M FY22. Return on net earned premiums has broadly mirrored this trend, with the two-year average equating to 14% in FY20/FY21 (7M F22: 17%) versus 11% in the prior three years. We expect the group to continue reflecting very strong underwriting profitability relative to peers, given its selective underwriting and competitive operating expense ratio, while net earnings stability is likely to be supported by consistent realised investment income.

Strong internal capital generation has supported risk adjusted capitalisation within a high range, with the GCR capital adequacy ratio for the group ranging between 1.7x and 2x over the past three years. Similarly, Western National SA's Solvency Capital Requirement ("SCR") coverage ratio is strong and has followed an increasing trend, registering at 2.2x at 7M F22 (FY21: 2x; FY20: 1.8x). Looking ahead, solvency is likely to be maintained at similar levels, although it could moderate slightly in the near term as it is managed towards the dividend threshold.

Growing operational cash flow generation has supported a strengthening in liquidity coverage metrics, with stressed investment coverage of net technical liabilities exceeding 2x at FY20 and FY21 (FY19: c. 1.9x). Furthermore, coverage of operational cash flow requirements has been consistently maintained at around 11 months between FY19 and 7M F22. Conservative investment allocations and continued positive operational cash flow generation are likely to maintain liquidity levels within a rating appropriate range over the outlook horizon.

The above factors are partly offset by the group's limited competitive position, given low market shares in the South African and Namibian insurance sectors. Premium diversification is viewed to be moderate in terms of line of business spread, and the assessment also considers limited geographic diversification outside of South Africa. The group has

reflected a level of success in executing its strategic plans, as evidenced by the growth achieved over the review period, which has coincided with a strengthening in underwriting profitability. This may contribute towards a more positive assessment of the business profile if sustained going forward.

Outlook statement

GCR expects earnings strength to continue over the Outlook horizon, with the underwriting margin likely to be close to or above 15% and the net margin between 17% and 20%. Solvency and liquidity are also expected to remain within rating appropriate bands. The business profile is not expected to change materially over the near term, but we see potential for incremental increases in market share over the longer term as the group continues to execute its strategic plans.

Rating triggers

The rating could be upgraded on the back of sustained strength in liquidity and capitalisation, but this would need to be accompanied by a strengthening in PSGK's credit profile. Downward rating action could follow a material deviation in earnings relative to expectations if this impacts on the overall financial profile.

Analytical contacts

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Related criteria and research

Criteria for the GCR Ratings Framework, May 2019
 Criteria for Rating Insurance Companies, May 2019
 GCR Ratings Scales, Symbols & Definitions, May 2019
 GCR Country Risk Scores, October 2021
 GCR Insurance Sector Risk Scores, September 2021

Ratings history

Western National Insurance Company Limited					
Rating class	Review	Rating scale	Rating	Outlook/Watch	Date
Financial strength	Initial*	National	A _{-(ZA)}	Stable Outlook	April 2015
	Last	National	A _(ZA)	Stable Outlook	December 2020

*Formerly claims paying ability.

Risk score summary

Rating components & factors	Risk score
Operating environment	14.50
Country risk score	7.00
Sector risk score	7.50
Business profile	(2.75)
Competitive position	(2.00)
Premium diversification	(0.75)
Management and governance	0.00
Financial profile	2.75
Earnings	0.75
Capitalisation	1.25
Liquidity	0.75
Comparative profile	0.00
Group support	0.00
Government support	0.00
Peer analysis	0.00
Total score	14.50

Glossary

Capitalisation	The provision of capital for a company, or the conversion of income or assets into capital.
Capital Adequacy	A measure of the adequacy of an entity's capital resources in relation to its risks.
Cash	Funds that can be readily spent or used to meet current obligations.
Claim	A request for payment of a loss, which may come under the terms of an insurance contract.
Credit Rating	An opinion regarding the creditworthiness of an entity, a security or financial instrument, or an issuer of securities or financial instruments, using an established and defined ranking system of rating categories.
Investment Portfolio	A collection of investments held by an individual investor or financial institution.
Liquidity	The speed at which assets can be converted to cash. The ability of an insurer to convert its assets into cash to pay claims if necessary. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
National Scale Rating ("NSR")	National Scale credit ratings express risk in relative rank order, which is to say they are ordinal measures of credit risk and are not predictive of a specific frequency of default or loss.
Premium	The price of insurance protection for a specified risk for a specified period of time.
Rating Horizon	The rating outlook period
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Short Term	Current; ordinarily less than one year.
Solvency	With regard to insurers, having sufficient assets (capital, surplus, reserves) and being able to satisfy financial requirements (investments, annual reports, examinations) to be eligible to transact insurance business and meet liabilities.
Underwriting	The process of selecting risks and classifying them according to their degrees of insurability so that the appropriate rates may be assigned. The process also includes rejection of those risks that do not qualify.

SALIENT POINTS OF ACCORDED RATINGS

GCR affirms that a.) no part of the rating process was influenced by any other business activities of the credit rating agency; b.) the rating is based solely on the merits of the rated entity, security or financial instrument being rated; and c.) such rating is an independent evaluation of the risks and merits of the rated entity, security or financial instrument.

The credit rating has been disclosed to the rated entity. The rating was solicited by, or on behalf of, the rated entity, and therefore, GCR has been compensated for the provision of the rating. The rated entity participated in the rating process via virtual management meetings, and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible.

The information received from the rated entity and other reliable third parties to accord the credit rating included:

- Audited annual financial statements to 28 February 2021;
- Four years of comparative audited financial statements to February;
- Budgeted financial statements to 28 February 2022;
- Unaudited management accounts to 30 September 2021;
- Other relevant documents

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