

## CREDIT RATING ANNOUNCEMENT

GCR upgrades Centriq's national scale financial strength rating to AA<sub>(ZA)</sub> on sound competitive positioning and liquidity; Outlook Stable

### Rating action

Johannesburg, 31 August 2023 – GCR Ratings (GCR) has upgraded Centriq Insurance Company Limited's (Centriq) national scale financial strength rating to AA<sub>(ZA)</sub> from AA<sub>-(ZA)</sub> with a Stable Outlook.

Rated entity	Rating class	Rating scale	Rating	Outlook/Watch
Centriq Insurance Company Limited	Financial strength	National	AA <sub>(ZA)</sub>	Stable Outlook

### Rating rationale

The rating has been upgraded on the back of Centriq's strengthened market position, reflecting its strong branding and market status as well as high levels of premium diversification. Furthermore, the rating is supported by consistently positive earnings and sound liquidity, while capitalisation remains adequate. The rating derives uplift from implied support from Santam Limited, given Centriq's strategic relevance, earnings history and operational integration.

Centriq has reflected very strong premium growth over the past three years, supporting a compound annual growth rate of 20% over the period. This has seen the insurer's share of overall industry gross premiums increase to about 3.6% from 2.5% in 2019, after normalising for a large risk finance premium in 2022. Furthermore, the insurer has reinforced its position as the second largest player in the cell captive sub-segment, with a market share of above 20%, from around 16% in 2020. The underlying premium base is well diversified by lines of business, consisting of four material classes and lower exposure to catastrophe prone classes / segments affecting the broader industry. Centriq also has a good balance between risk finance and underwriting management agency (UMA) business and a fairly material contribution from affinity channels.

Centriq's earnings quality is credit positive, with its fee-centric business model and diversified earnings base supporting a sound and stable earnings track record. Net after tax profits increased by 14% to ZAR138m in 2022, although normalised return on promoter net premiums moderated slightly to about 8% in 2022 (2021: 11%). This was nevertheless within the expected range given growth in lower margin business types and was reasonably aligned with the industry average. We expect return on revenue to be maintained within an 8% to 10% band over the outlook horizon, while reflecting low volatility given very limited participation on underwriting risk at the promoter level.

The insurer reflects sound solvency on a consolidated basis, with the unadjusted GCR capital adequacy ratio (CAR) registering at 1.8x at 31 December 2022 (31 December 2021: 1.9x). However, our assessment considers a fungibility adjustment for surplus funds in the cells, which brings the ratio to an average of about 1.1x after factoring in various levels of stresses. Solvency Capital Requirement (SCR) coverage was stable at 1.04x at 31

December 2022 and we expect this to continue to be managed at similar levels, as consistent earnings generation supports targeted shareholder returns. The majority of cells had surplus capital levels, and Centriq's exposure to undercapitalised cells remained very low, equating to only 2% of shareholders' funds at fiscal year-end 2022 (2021: 2%; 2020: 15%).

Liquidity is sound, supported by conservative investment allocation and strong operational cash flow generation. After applying a conservative stress for potential withdrawal of surplus funds, GCR's liquidity coverage ratio registered at a stable 1.1x at 31 December 2022 and is expected to be maintained at a similar level going forward, given consistency in the investment mix.

## Outlook statement

GCR expects solid earnings generation and profit retention to support adequate risk adjusted capitalisation, and strong operational cash flow generation to maintain the liquidity coverage ratio above 1x. We do not expect a material change in the business profile over the outlook horizon, although a further strengthening in competitive position could follow over the longer term if the insurer continues its strong growth momentum.

## Rating triggers

The rating could be upgraded if earnings strengthen and compare well with peers, supporting a strengthening in liquidity. Furthermore, continued growth in market share could positively impact the rating over the medium term. Negative rating action could follow a material weakening in earnings that adversely impacts the overall financial profile.

## Analytical contacts

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## Related criteria and research

Criteria for the GCR Ratings Framework, January 2022  
Criteria for Rating Insurance Companies, July 2022  
GCR Ratings Scales, Symbols & Definitions, May 2023  
GCR Country Risk Scores, August 2023  
GCR Insurance Sector Risk Scores, February 2023

## Rating history

### Centriq Insurance Company Limited

Rating class	Review	Rating scale	Rating	Outlook/Watch	Date
Claims paying ability	Initial	National	A <sub>(ZA)</sub>	Stable Outlook	March 2006
Financial strength	Last	National	AA <sub>-(ZA)</sub>	Stable Outlook	August 2022

## Risk score summary

Rating Components & Factors	Score
<b>Operating environment</b>	<b>14.50</b>
Country risk score	7.00
Sector risk score	7.50
<b>Business profile</b>	<b>0.25</b>
Competitive position	0.25
Management and governance	0.00
<b>Financial profile</b>	<b>(0.25)</b>
Earnings	0.50
Capitalisation	(0.75)
Liquidity	0.00
<b>Comparative profile</b>	<b>2.00</b>
Group support	2.00
Peer comparison	0.00
<b>Total risk score</b>	<b>16.50</b>

## Glossary

Agency	An insurance sales office which is directed by an agent, manager, independent agent, or company manager.
Capital Adequacy	A measure of the adequacy of an entity's capital resources in relation to its risks.
Capital	The sum of money that is invested to generate proceeds.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Cash	Funds that can be readily spent or used to meet current obligations.
Catastrophe	An event, which causes a loss of extraordinary magnitude.
Compound Annual Growth Rate	The year on year percentage growth rate of an investment over a given period of time. It is found by calculating:
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. 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.
Premium	The price of insurance protection for a specified risk for a specified period of time.
Retention	The net amount of risk the ceding company keeps for its own account.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Shareholder	An individual, entity or financial institution that holds shares or stock in an organisation or company.

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.
Undercapitalised	Term used when a business is not supplied with enough funds by its owners to support its activities and provide for any needed expansion.
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.
Upgrade	The rating has been raised on its specific scale.

### Salient points of accorded rating

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 was based solely on the merits of the rated entity, security or financial instrument being rated; and c.) such rating was 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 above 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 face to face management meetings, as well as 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 financial statements to 31 December 2022;
- Four years of comparative audited financial statements to 31 December;
- Full year budgeted financial statements to 31 December 2023;
- Unaudited management accounts to 30 June 2023;
- Other relevant documents.

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