

Research Update:

Six Insurers Operating in Mexico Downgraded After Similar Action On The Sovereign; Negative Outlook On Eight Insurers

March 27, 2020

Overview

- On March 26, 2020, we lowered our local and foreign currency ratings on Mexico to 'BBB+' from 'A-' and to 'BBB' from 'BBB+', respectively. We expect a pronounced hit to the Mexican economy following the combined shocks of the impact of COVID-19 in both Mexico and the U.S., and lower global oil prices.
- As a result, we lowered the global scale ratings on five Mexican insurers because the sovereign rating limits the ratings on these entities. Additionally, we downgraded PEMEX's Swiss-based captive reinsurer, Kot Insurance, in line with the parent rating in local currency, which also reflects that on the sovereign.
- We affirmed our ratings on TMX and AIGMX because in our view, the sovereign does not constrain these ratings. TMX's financial strength rating is supported by an irrevocable and unconditional guarantee provided by the Japanese parent, Tokio Marine Nichido and Fire Insurance Co. Ltd. (TMNF). AIGMX passes our stress test scenario for rating an entity above the sovereign given its robust cash position and low exposure to sovereign bonds.
- We affirmed our 'mxAAA' national scale ratings on AIGMX, AZMX, Axa Seguros, ChubbMX, GNP, and TMX.
- The downgraded entities have a negative global scale outlook and a stable national scale outlook. The outlooks are aligned with that on Mexico for both rating scales.

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Rating Action

On March 27, 2020, S&P Global Ratings lowered its ratings on the following entities by one notch, in line with our downgrade of Mexico:

- AXA Seguros S.A. de C.V. (AXA Seguros) and SOMPO Seguros Mexico, S.A. de C.V. (Sompo Mexico) to 'A-' from 'A';
- Chubb Seguros Mexico S.A. (ChubbMX) to 'BBB+' from 'A-'; and

- Allianz Mexico Compania de Seguros S.A. (AZMX), and Grupo Nacional Provincial S.A.B. (GNP) to 'BBB' from 'BBB+'.

We also downgraded Kot Insurance Co. A.G. (Kot) to 'BBB+' from 'A-' following our downgrade of Petroleos Mexicanos on local currency (PEMEX: local currency BBB+/Stable/--; foreign currency BBB/Negative/--). The outlook on these entities is negative, in line with that on Mexico.

We affirmed our ratings on Qualitas Controladora S.A.B. de C.V. (QualColown) and its U.S.-based subsidiary Qualitas Insurance Co. (QIC) at 'BB+' and 'BBB-', respectively, and revised their outlook to negative from positive following the sovereign downgrade.

We also affirmed our 'A+' rating on Tokio Marine Compania de Seguros S.A. de C.V. (TMX) and our 'A-' rating on AIG Seguros Mexico, S.A. de C.V. (AIGMX) to reflect that the sovereign rating does not immediately constrain their ratings. The outlook on TMX remains positive and the outlook on AIG stable.

Finally, we affirmed our 'mxAAA' national scale ratings on AIGMX, AZMX, Axa Seguros, ChubbMX, GNP, and TMX with stable outlooks.

Outlook

The negative outlook on the global scale ratings on AZMX, AXA Seguros, ChubbMX, GNP, Sampo Mexico, QualCo, and QIC reflects that on the local and foreign currency sovereign ratings. The negative outlook on Kot reflects that on its parent PEMEX, which at the same time reflects the sovereign's local currency rating outlook. Therefore, we could lower our ratings on these insurers following a similar action on the sovereign.

The negative outlook on Mexico indicates the risks of a downgrade over the coming 12-24 months as a result of uneven or ineffective policy execution; potential weakening in public finances, reflecting a difficult trade-off between sustaining GDP growth given Mexico's low non-oil tax base and spending rigidities; and rising pressure on PEMEX, a potential contingent liability for the sovereign.

The stable outlook on the global scale ratings on AIGMX reflects its two-notch buffer (out of a maximum four) between the rating and the foreign currency rating on Mexico. It also incorporates our expectation that its high capitalization levels and liquidity will allow it to withstand a sovereign default scenario in both foreign and local currency debt in the coming 12-18 months, according to our sovereign default stress test scenario.

The positive outlook on Tokio Marine Mexico reflects the same on its guarantor, TMNF, which in turn reflects the outlook on Japan. Therefore, a movement in the ratings on the latter would trigger the same action on the Mexican subsidiary.

The stable national scale outlook on AZMX and GNP reflects that we rate them at the same level as our 'mxAAA' national scale rating on Mexico, considering our current mapping tables for the country, because their stand-alone credit profiles (SACPs) are above the sovereign foreign currency rating.

The stable outlook on the AIGMX, AXA Mexico, TMX and ChubbMX national scale ratings reflects the at least one-notch buffer in our national scale rating mapping table.

Given that the risks are firmly on the downside given the spread of the coronavirus, we will keep close monitoring the potential impacts to insurers on a stand-alone basis.

Upside scenario:

We could revise the negative global scale outlooks to stable if we revise our outlook on the global scale ratings on Mexico to stable. However, we consider this unlikely given its negative outlook.

Rationale

On March 26, we downgraded Mexico following our expectation of a pronounced hit to the Mexican economy following the combined shocks of COVID-19 (both in Mexico and in the U.S., its main trading partner) and the lower global oil prices. Consequently, we lowered our ratings on AXA Seguros, Somo Mexico, ChubbMX, AZMX, and GNP, the ratings on which are constrained by the sovereign foreign currency rating. These insurers operate solely in Mexico and their investment portfolios have a significant portion of sovereign debt.

At the same time, we affirmed our ratings on TMX and AIGMX, both of which we rate above the sovereign. For the former, we base this on its group status as a highly strategic important subsidiary to its parent, Tokio Marine & Nichido Fire Insurance Co. Ltd. (TMNF; A+/Positive/A-1), while for the latter, we consider it able to withstand a sovereign foreign and local currency default scenario. We also affirmed our ratings on QualCo and QIC, because our foreign currency ratings on Mexico now constrain these ratings.

The ratings on Mexico reflect strengths and weaknesses in Mexico's democracy, which has brought political stability and regular changes of government over the last two decades. However, it has not created economic growth compared with other emerging markets, or improved public security. Amid the pronounced COVID-19 and oil price shocks, we expect Mexico's real per capita GDP growth to remain below that of peers with similar levels of economic development. We forecast a second year of economic contraction this year and the absence of a sharp recovery as the Lopez Obrador administration has failed to improve private sector confidence and investment dynamics.

According to our group rating methodology, we can rate highly strategically important insurance subsidiaries up to two notches above the foreign currency sovereign rating, while strategically important subsidiaries are limited to the foreign currency sovereign rating. Therefore, our 'BBB/A-2' foreign currency rating on Mexico is the reference point for the credit quality of subsidiaries of international insurance groups, such as AXA Seguros and Somo Mexico. In the case of AZMX, which we consider a strategically important subsidiary, we limit the ratings by the sovereign foreign currency rating. Although we consider AIGMX a strategically important subsidiary, the rating on it is above the sovereign foreign currency rating and at its SACP level, since we believe it would withstand a sovereign stress scenario in foreign and local currency. Similarly, ChubbMX is a strategically important subsidiary, but it passes our sovereign default scenario in foreign currency. However, it doesn't pass the local currency scenario, and so we limit the rating at the 'BBB+' local currency rating on Mexico.

Our financial strength ratings and outlook on Tokio Marine Mexico reflect the irrevocable and unconditional guarantee from TMNF. The explicit support agreement meets all of the conditions of our guarantee criteria. Therefore, we equalize our financial strength rating on the Mexican subsidiary to that on the guarantor.

The ratings and outlook on Kot, a Swiss-based captive reinsurer of PEMEX (a government-related entity), are directly linked to that of the state-owned company, which at the same time reflects the sovereign local currency rating.

In the case of GNP, which doesn't benefit from external support, we limit the global scale ratings at the sovereign foreign currency rating.

The ratings on QualCo and QIC reflect our view of the group's credit fundamentals, which are constrained by the sovereign. Therefore, the ratings are also constrained by those on Mexico. The ratings on Qualco and QIC are subordinated to our views of their group, so they're affected in tandem, although the ratings on them are below those on Mexico.

The 'mxAAA' national scale ratings on AZMX and GNP derive from us choosing the upper option (mxAAA or mxAA+) from our national scale mapping table. We consider AZMX will keep its strong capitalization level with well diversified earning sources, and GNP will remain the largest Mexican market player with sound profitability.

In the case of AIGMX, AXA Seguros, ChubbMX, and TMX, the affirmation of the 'mxAAA' national scale ratings reflects their strong credit quality and group support.

Although we don't expect the impact from COVID-19 to lead to a capital event for these insurers, the combination of adverse market conditions--such as lack of economic growth, market illiquidity, lower interest rates, and currency depreciation--could lead to tighter margins, business contraction, and hurts earnings, which could impair insurers' credit quality. We currently forecast that the effect of the measures to stop the spread of COVID-19 would lead to a global recession this year. As seen in China, restrictions could be lifted more slowly than originally thought, as public health concerns persist, which could affect insurers' credit quality.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Downgraded

	To	From
Allianz Mexico Compania de Seguros S.A.		
Issuer Credit Rating	BBB/Negative/--	BBB+/Negative/--
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--
Financial Strength Rating	BBB/Negative/--	BBB+/Negative/--
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--

AXA Seguros S.A. de C.V.

Issuer Credit Rating	A-/Negative/--	A-/Negative/--
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--
Financial Strength Rating	A-/Negative/--	A-/Negative/--
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--

Chubb Seguros Mexico, S.A.

Issuer Credit Rating		
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--
Financial Strength Rating	BBB+/Negative/--	A-/Negative/--
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--

Grupo Nacional Provincial S.A.B.

Issuer Credit Rating	BBB/Negative/--	BBB+/Negative/--
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--
Financial Strength Rating	BBB/Negative/--	BBB+/Negative/--
CaVal (Mexico) National Scale	mxAAA/Stable/--	mxAAA/Stable/--

Kot Insurance Co. A.G.

Issuer Credit Rating	BBB+/Negative/--	A-/Negative/--
Financial Strength Rating	BBB+/Negative/--	A-/Negative/--

SOMPO Seguros Mexico, S.A. de C.V.

Financial Strength Rating	A-/Negative/--	A-/Negative/--
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Ratings Affirmed; Outlook Action

Qualitas Controladora S.A.B. de C.V.

Issuer Credit Rating	BB+/Negative/--	BB+/Positive/--
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Qualitas Insurance Co.

Issuer Credit Rating	BBB-/Negative/--	BBB-/Positive/--
Financial Strength Rating	BBB-/Negative/--	BBB-/Positive/--

Ratings Affirmed

AIG Seguros Mexico, S.A. de C.V.

Financial Strength Rating	A-/Stable/--
CaVal (Mexico) National Scale	mxAAA/Stable/--

Tokio Marine Compania de Seguros S.A. de C.V.

Issuer Credit Rating	
CaVal (Mexico) National Scale	mxAAA/Stable/--
Financial Strength Rating	A+/Positive/--
CaVal (Mexico) National Scale	mxAAA/Stable/--

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