FitchRatings

RATING ACTION COMMENTARY

Fitch Upgrades Pena Verde to 'BBB'; Outlook Stable

Fri 04 Jun, 2021 - 5:06 PM ET

Fitch Ratings - Mexico City - 04 Jun 2021: Fitch Ratings has upgraded Pena Verde, S.A.B.'s (PV) Long-Term Local Currency Issuer Default Rating (IDR) to 'BBB' from 'BBB-'. The Rating Outlook is Stable.

KEY RATING DRIVERS

PV's 'BBB' Local Currency IDR is derived by notching from subsidiary Patria's Insurer Financial Strength (IFS) rating, per Fitch criteria. The upgrade of PV's Local Currency IDR is based on a more favorable view by Fitch of Patria's IFS rating when considering only local currency risks. On such a basis, Fitch currently views Patria's international IFS rating as equivalent to an 'A-' level, and its implied Local Currency IDR at 'BBB+'. Under Fitch criteria, in ring-fenced regulatory environments, as designated by Fitch in Mexico, the IDR of a holding company is set one notch below that of the operating company.

Previously, Fitch's view of Patria's IFS rating on a local currency basis was one notch lower - see the current rating action commentary on Patria for additional details. It is important to note that after reflecting all applicable transfer and convertible risks, Patria's published international IFS rating is 'BBB+', and is treated by Fitch as a foreign currency rating given significant volumes of business sourced outside of Mexico. The implied Local Currency ratings of Patria discussed above are applicable only in the PV notching exercise.

Fitch views PV's business profile as favorable compared to the Latin American insurance market. Founded in 2012, PV is the direct holding company of five subsidiaries. At YE 2020, PV's total assets from its main (re)insurance operating entities made up 90%; 66% through Patria and 24% through General de Seguros S.A.B. and subsidiary. With a global position and focus in Latin America, PV's net written premiums (NWP) and equity totaled USD409 million and USD569 million, respectively. The company has a strong franchise in the region, which allows for a very highly diversified business, with 80% of premiums in Latam (43% in Mexico) and 20% overseas.

PV's capital quality is adequate for the rating category. Entity's gross and net leverage ratios (1.7x and 1.4x at YE 2020, respectively) remain favorable. Fitch's primary rating constraints include pressure on investments given the Mexican sovereign's related investments which represents 90% of equity at YE 2020. Fitch notes that premium growth given PV's strategic plan may affect net and gross leverage ratios relative to regulatory capital in the future. However, Fitch expects ratings subfactors to remain at current rating category. While the company currently has no debt outstanding, the current rating assumes debt capacity of up to 30% of total adjusted capital.

Fitch views PV's underwriting and overall profitability as adequate but pressured by volatility in financial results and operating expenses. Historically, PV's technical result has been positive, although consolidated five-year average combined ratio under international accounting standards reached 101%, in the lower bound of assigned rating. Return on equity ratio is influenced by the Mexican market financial system averaging 0.9% during the same period.

Fitch believes PV's financial profile could be boosted by premium growth expectation outside of Latam, which will potentially expand entity's underwriting and investment diversification and reduce below investment grade exposure as well as transfer and convertibility risks. However, such expansion comes with execution risks.

PV's reinsurance utilization ratio is adequate as a result of its business model, which relies on retaining 80% of the business written to its ample base of clients. Reinsurance recoverable to capital was 37% at YE 2020.

RATING SENSITIVITIES

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

-- Given the company's current business profile, the rating would also be sensitive to an upgrade of Mexico's sovereign rating and country ceiling.

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

-- A downgrade could be driven by a downgrade of Patria's rating or by a deterioration of PV's intrinsic financial performance, or by debt issuance that results in financial leverage ratio higher than 30%.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond 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.

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Pena Verde S.A.B.	LC LT IDR	BBB Rating Outlook Stable	Upgrade	BBB- Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Metodología de Calificación de Seguros (pub. 10 Sep 2020)

Metodología de Calificaciones en Escala Nacional (pub. 22 Dec 2020)

Insurance Rating Criteria (pub. 15 Apr 2021) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Pena Verde S.A.B.	EU Endorsed, UK Endorsed

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Non-Bank Financial Institutions Latin America Mexico

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