FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Rothesay Life at IFS 'A+'; Outlook Stable

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Fitch Ratings - London - 26 Sep 2024: Fitch Ratings has affirmed Rothesay Life Plc's Insurer Financial Strength (IFS) Rating at 'A+' (Strong) and Long-Term Issuer Default Rating (IDR) at 'A'. Fitch has also affirmed the group's ultimate holding company, Rothesay Limited's (Rothesay), IDR at 'A'. The Outlooks are Stable. A full list of rating actions is below.

The ratings reflect Fitch's assessment of Rothesay's 'Strong' company profile and 'Very Strong' capitalisation and leverage. We assess Rothesay's financial performance, investment risk and asset-liability management (ALM) as 'Very Strong'.

KEY RATING DRIVERS

Improved Company Profile: Our assessment of Rothesay's profile reflects improved operating scale and its position as a leader in the UK bulk purchase annuity market. Total assets under management (AUM) rose to GBP68.5 billion at end-1H24 (end-2023: GBP61 billion), supported by strong new business volumes that soared in 2023 to GBP12.7 billion from GBP3.3 billion in 2022; these remained resilient at GBP9.7 billion in 1H24, helped by improved market conditions. We expect strong medium-term volumes, supported by resilient demand from corporates to offload their pension liabilities.

Rothesay's agreement to acquire Scottish Widows Limited's (SWL; IFS Rating: A+/Stable) GBP6 billion in-force bulk annuity book in March 2024, is in line with the group's demonstrated record of acquiring large in-force annuity books from insurers and will add to Rothesay's operating scale within the UK bulk annuity market. The transaction was initially structured as a reinsurance deal, where the risks pertaining to the portfolio were transferred to Rothesay, until the portfolio is fully transferred under a Part VII insurance business transfer process in 2025.

Very Strong Capitalisation: Rothesay's Prism Global model was 'Extremely Strong' at end-2023, unchanged from end-2022. Rothesay's Solvency II (S2) coverage ratio at end-

1H24 was very strong at 244%, although reduced from 273% at end-2023 mainly due to increased business volumes. Strong surplus generation from the in-force book and higher long-term interest rates support the ratio, but this is offset by new business capital strain and some of the new business premiums being temporarily undeployed.

In September 2024, Rothesay also said that GIC, one of its main shareholders, has provided capital to support new business by reinvesting the interim dividend from the insurer in 2023 back into the business. Fitch expects Rothesay's S2 capital coverage ratio to remain strong and its capital buffer to comfortably absorb the initial capital strain from the in-force book acquisition from SWL.

Very Strong Leverage: Rothesay's Fitch-calculated financial leverage ratio (FLR) was strong at about 24% at end-1H24, and we expect the ratio to have improved to about 21% on a pro-forma basis following the GBP400 million Tier 2 redemption in September 2024. FLR has deteriorated slightly from 19% at end-2023, following its dual-tranche Tier 2 issuance (GBP500 million and USD325 million) in June 2024; however, we believe the ratio will remain strong and commensurate with the rating.

Very Strong Financial Performance: Rothesay reported operating profit of GBP725 million in 1H24, up from GBP403 million in 1H23, supported by the strong new business profit and improved in-force profitability helped by higher returns on surplus assets. Fitch expects Rothesay's operating profits to remain strong, supported by selective writing of profitable businesses and a steady release of earnings from its in-force book.

Volatile IFRS Results: Rothesay's IFRS net income is volatile due to economic variance due to market movements. In 1H24, Rothesay reported a negative economic variance of GBP240 million mainly due to higher long-term interest rates. As a result, IFRS pre-tax net income fell to GBP21 million in 1H24 from GBP260 million in 1H23. In addition, the timing of profit recognition is delayed under IFRS 17 and profits are recognised progressively over the duration of the insurance contracts. This profit deferral results in a significantly lower net income in comparison to the reported operating profitability.

Strong Asset Quality: Most of the group's investment portfolio is held in debt securities of a high credit quality, including privately placed investments, and this drives our assessment of investment risk. We view Rothesay's investments in illiquid assets, mainly in mortgages and secured lending, as being of good quality supported by the insurer's prudent risk selection process and strict controls over the lending criteria.

Rothesay continues to expand its international asset-origination capabilities mainly in the US, where about 21% of its end-1H24 AUM is invested. However, it continues to have high exposure to sovereign debt of the UK (AA-/Stable), in line with some of its similar-rated peers.

Very Strong ALM: The insurer has a sophisticated approach to ALM, in line with that required for the business it writes. It makes extensive use of longevity swaps to hedge longevity risk, and the duration of assets and liabilities are closely matched. As a result, the reduction in asset values owing to higher interest rates is broadly matched by a fall in Rothesay's insurance liabilities.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

-- A substantial weakening of the group's capitalisation as evidenced by a sustained fall in the Prism score to the 'Very Strong' category or a reduction in an S2 ratio to below 140%.

-- Deterioration in the FLR to above 28% on a sustained basis.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

-- A substantial improvement in Fitch's view of Rothesay's company profile, for instance demonstrated by a significant increase in product or geographical diversification.

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.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING	PRIOR
Rothesay Life Plc	LT IDR A Rating Outlook Stable Affirmed	A Rating Outlook Stable
	LT IFS A+ Rating Outlook Stable Affirmed	A+ Rating Outlook Stable
subordinated	LT BBB+ Affirmed	BBB+
subordinated	LT BBB Affirmed	BBB
subordinated	LT A- Affirmed	A-
Rothesay Limited	LT IDR A Rating Outlook Stable Affirmed	A Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Insurance Rating Criteria (pub. 04 Mar 2024) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Prism Global (ex-U.S.) Model, v1.8.1 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

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Rothesay Limited	UK Issued, EU Endorsed

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