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Ratings

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NOVIS Insurance Company

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Table Of Contents

Credit Highlights

Outlook

Key Assumptions

Business Risk Profile

Financial Risk Profile

Other Key Credit Considerations

Rating Score Snapshot

Related Criteria

Appendix

NOVIS Insurance Company

Credit Highlights

Overview	
Key strengths	**Key risks**
Strong growth and access to multiple key distributors.	Relatively small capital size dominated by value in force, creating significant sensitivity to lapses and expense assumptions.
Already some regional diversification, even though recently established in 2012.	Dependence on reinsurance and external funding for financing acquisition costs, with an expected financial leverage of 60%-80%.

NOVIS Insurance Company (NOVIS Pojistovna a.s. [NOVIS])'s competitive position remains in a buildup phase. Since its foundation in 2012, we believe that NOVIS has grown fast, and has attracted distribution partners across regional markets in Europe. In 2020 and first-half 2021, business growth was affected by the pandemic and, to a lesser extent, interim regulatory measures, including fines. Although an interim measure was withdrawn in April 2021, we will closely monitor regulatory actions on NOVIS and their implications for its competitive position.

NOVIS' financial risk profile is marginal. We believe that NOVIS' financial risk profile reflects its sufficient solvency position, with a 137% solvency ratio as of year-end 2020 and capital adequacy above the 'A' range, according to S&P Global Ratings' capital model. The company's capital adequacy under our capital model and regulatory solvency consists predominantly of value in force, which in our view creates a high sensitivity toward lapses and assumption changes, such as administrative expenses on portfolio profitability. This makes NOVIS' capital base more sensitive to assumption changes compared with higher-rated peers. Moreover, the company's absolute size of capital makes it more vulnerable to adverse economic developments than larger, more diverse peers.

Outlook: Stable

The stable outlook reflects our view that NOVIS will continue to expand its franchise, maintain regulatory solvency capital well above 100%, and maintain capital adequacy according to S&P Global Ratings' capital model above the 'A' range over 2021-2023.

Upside scenario

A positive rating action within 12 months would largely depend on the insurer's ability to:

- Continue generating profitable growth, gain scale, and develop the franchise in line with the business plan in target markets; and
- Reduce sensitivities toward lapses and its dependencies to reinsurers and capital market debtors.

Downside scenario

A negative rating action in the next 12 months could follow if:

- Regulatory measures on its product portfolio or sales activities affect the company's competitive position;
- Solvency under the Solvency II ratio drops to 100% or below;
- Capital adequacy according to our capital model sustainably deteriorates below the 'A' range;
- NOVIS fails to fund acquisition costs via capital markets or reinsurance financing, which could affect its competitive position; or
- The company loses access to key distribution partners, in particular in Italy and Iceland.

Key Assumptions

- We expect the economy in Slovakia and Italy to grow by 3%-5% over 2021-2022.
- Unemployment rate in Slovakia to remain at about 6%-7%, and in Italy at about 10% through 2021-2022.
- Inflation to remain at about 2% over 2021-2022.
- Ongoing low interest rate environment in the eurozone.

NOVIS Insurance Company--Key Metrics

	2022f	2021f	2020	2019	2018	2017	2016
Gross premium written (Mil. €)	~52.7	~50.2	47.8	51.2	39.0	24.9	12.8
Net income (Mil. €)	5-10	5-10	3.8	3.7	6.2	2.8	7.4
Return on shareholders' equity (%)	>10	>10	10.8	12.0	24.7	14.0	48.6
S&P Global Ratings capital adequacy	Strong	Strong	Strong	N.A.	N.A.	N.A.	N.A.
Net investment yield (%)	0 - 2	0 - 2	4.2	1.4	(0.7)	(0.1)	1.2
Financial leverage (%)	60 - 80	60 - 80	16.8	8.4	12.7	20.0	3.4

NOVIS Insurance Company--Key Metrics (cont.)	2022f	2021f	2020	2019	2018	2017	2016
EBITDA fixed charge coverage (X)	2 - 4	2 - 4	13.8	45.6	48.2	53.9	397.0

f--S&P Global Ratings forecast. N.A.--Not available.

Business Risk Profile: Fair

NOVIS is a small life insurance company based in Slovakia. The company underwrites life insurance in Slovakia, and in several European countries on a freedom of services basis and through three branches. NOVIS has grown fast since its foundation in 2012 and has attracted distribution partners in different European regional markets. Although the company has very low market shares in these markets, it manages to generate solid underwriting margins. We understand that the company's modern IT infrastructure, which allows NOVIS to offer its clients a flexible life insurance product with various protection options, is key to this successful development.

The insurer writes a narrow product range of unit-linked business with additional protection coverage on mortality, morbidity, accidents, and disability. Geographically, about 40% of NOVIS' 2020 gross written premiums came from Italy, 23% from Iceland, 20% from Hungary, and the remaining 17% from Slovakia, the Czech Republic, and Germany.

The company distributes via third parties, so we believe its competitive position will significantly depend on reinsurance support or capital market financing to cover acquisition costs for new business. In 2020, reinsurance utilization was above 50% based on premiums, and liabilities toward reinsurers were about 32% of its total balance sheet.

In 2020 and first-half 2021, business growth was affected by the pandemic and, to a lesser extent, interim regulatory measures. Consequently, gross written premiums declined by 7% in 2020, but grew in the first half 2021 by 15% in comparison with the first half 2020. The portfolio count increased by 10% in 2020, and by 8% in the first half 2021 versus the same period of 2020. Under our base-case scenario, we assume the company will maintain full license to continue to write business in the target markets. While an interim measure was withdrawn in April 2021, we will closely monitor regulatory actions on NOVIS and their implications for its competitive position.

We expect that the company will continue to tap into growth opportunities in its key markets--Italy and Iceland. To further scale up, the company looks for profitable growth opportunities in the existing, as well as new, markets in Europe. We note that the company stopped underwriting new business in Hungary. However, NOVIS continues to receive premium inflows from existing clients in Hungary, which in 2020 accounted for €9.8 million. We expect that premiums from Hungary will gradually reduce in 2021-2023. Overall, under our base-case scenario, we anticipate that NOVIS' gross premiums will increase by 5%-10% in 2021-2022.

Financial Risk Profile: Marginal

We believe that NOVIS' financial risk profile reflects the company's sufficient solvency position, with a 137% solvency ratio as of year-end 2020 and capital adequacy above the 'A' range, according to our capital model. The company's capital adequacy under our capital model and regulatory solvency consists predominantly of value in force, which in our view creates a high sensitivity toward lapses and assumption changes, such as administrative expenses on portfolio profitability. This makes NOVIS' capital base more sensitive to assumption changes compared with that of higher-rated peers. Moreover, the company's absolute size of capital makes it more vulnerable to adverse economic developments than larger, more diverse peers. We assume the company's capital adequacy will remain in the 'A' range and the Solvency II ratio at 140%-160% in 2021-2023, although sensitivity toward lapses and assumption changes will persist. We believe that additional open items with the regulator on lapse assumptions could further stress the Solvency II ratio, but this is partly offset via a subordinated convertible bond issuance of €20 million, which we believe will be fully paid in 2021 and accepted under regulatory solvency.

In our view, investment risk and foreign exchange risk remains relatively limited to NOVIS. The insurer maintains a conservative investment portfolio, with the majority of investments in government bonds that have an average rating of 'A' on them. The company accounts its fixed income investments at fair value, and as a result it has intermediate exposure to market volatility. At the end of 2020, the company did not have material investment exposure to high-risk assets like real estates or equities. Overall, we believe that NOVIS is less sensitive to market volatility. We do not expect any material increase in investment risk in 2021-2023.

NOVIS reported a return on equity of 10%-12% in 2019-2020, and a net income of about €4 million. With expected further premium growth, relatively stable underwriting margins and good cost controls, we expect that the company's net income will be in the range of €5 million-€10 million in 2021-2023. However, the company's gross revenue consists of more than 50% of changes in insurance contracts' value and reinsurance commissions, highlighting the company's dependance on up-front financing and assumption changes, in particular on costs and lapse development. Under our base-case scenario, we believe that NOVIS will continue to write profitable new business, helping to increase the value of its insurance portfolio that flows through the company's profit and loss account.

We expect that NOVIS' funding structure will change fundamentally in 2021-2023. The company issued a subordinated convertible bond in 2021 with €20 million volume, and we expect NOVIS will issue senior debt to finance acquisition costs from 2021-2025. At the same time, we believe the insurer will reduce its reinsurance financing, which capital market financing will gradually replace. In addition, we also expect further business growth to be financed through the capital markets. We therefore expect that financial leverage will strongly increase to 60%-80% in 2021-2023, creating a significant dependance on this source of financing and high fixed charges. We assume the fixed charge coverage will remain at 2x-4x in 2021-2023.

Other Key Credit Considerations

Governance

NOVIS, as a joint stock company, has approximately 20 shareholders. Board members hold shares, but no shareholder holds more than 10%. We believe the company's management team is sufficiently experienced in the insurance sector, and the corporate governance structure and risk management capabilities are in line with industry standards. We note that in the last 24 months, the company had some regulatory measures on its products, however, we understand that the company has now resolved all product related issues. We do not see governance issues, except a few regulatory measures on solvency ratio calculations that are currently left outstanding, which we will continue to monitor closely.

Liquidity

We believe that liquidity is sufficient in view to the company's highly liquid asset portfolio and an additional credit line from banks is available if the need arises.

Accounting considerations

NOVIS prepares its financial accounts in accordance with International Financial Reporting Standards.

The company activates values of insurance contracts on its balance sheet. To calculate NOVIS's total adjusted capital in our risk-based capital model, we use its embedded value disclosures for its life business and give credit for its value in force of the portfolio, but deduct any liabilities related to the finance acquisition costs of these contracts.

Rating Score Snapshot

Rating Score Snapshot	
Business Risk Profile	**Fair**
Competitive position	Fair
IICRA	Intermediate risk
Financial Risk Profile	**Marginal**
Capital and earnings	Satisfactory
Risk exposure	Moderately low
Funding structure	Negative
Anchor*	bb-
Modifiers	0
Governance	Neutral
Liquidity	Adequate
Comparable ratings analysis	0
Issuer Credit Rating	BB-/Stable

*This reflects NOVIS' sensitivity toward lapses and assumption changes in its financial risk profile.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Appendix

NOVIS Insurance Company--Credit Metrics History

Ratio/Metric	2020	2019
S&P Global Ratings capital adequacy	Strong	N/A
Total invested assets (Mil. €)	65.8	61.8
Total shareholder equity (Mil. €)	36.4	33.3
Gross premiums written (Mil. €)	47.8	51.2
Net premiums written (Mil. €)	23.6	33.3
Net premiums earned (Mil. €)	23.7	33.6
Reinsurance utilization (%)	50.64	34.92
EBIT (Mil. €)	12.3	10.5
Net income (attributable to all shareholders) (Mil. €)	3.8	3.7
Return on shareholders' equity (reported) (%)	10.76%	12.02%
Return on assets (including investment gains/losses) (%)	16.63%	17.21%
EBITDA fixed-charge coverage (including realized and unrealized gains/losses) (x)	13.8	45.6
EBIT fixed-charge coverage (including realized and unrealized gains/losses) (x)	13.1	44.1
Financial obligations/EBITDA adjusted	0.6	0.3
Financial leverage including pension deficit as debt (%)	16.84%	8.43%
Net investment yield (%)	4.24%	1.44%
Net investment yield including investment gains/losses (%)	-4.33%	25.46%

N/A--Not applicable.

Ratings Detail (As Of October 27, 2021)*

Operating Company Covered By This Report	
NOVIS Insurance Company	
Issuer Credit Rating	
Local Currency	BB-/Stable/--
Domicile	Slovak Republic

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.