



INVESTORS SERVICE

Rating Action: Moody's affirms Rothesay Life Plc's A3 IFSR and changes the outlook to positive

21 June 2021

London, June 21, 2021 – Moody's Investors Service ("Moody's") has affirmed the A3 insurance financial strength rating ("IFSR") and the Baa1 long-term issuer rating of Rothesay Life Plc, the main operating company of Rothesay Limited ("Rothesay" or "Group"). In the same rating action, the Baa2 long-term issuer rating of Rothesay has also been affirmed. The rating outlook has been changed to positive from stable.

A list of affected ratings can be found at the end of this press release.

RATINGS RATIONALE

The affirmation of Rothesay's ratings reflects the Group's good market position in the growing UK bulk annuity market, together with good return on capital (ROC) performance, asset quality and financial flexibility. These strengths are mitigated somewhat by the Group's limited business and geographic diversification and relatively high asset leverage. The positive outlook reflects the likelihood that Rothesay will undertake meaningful bulk annuity volumes over the medium term, further establishing its market position and leading to a consistently good level of earnings.

Rothesay has a good market position in the growing and relatively concentrated UK bulk annuity market, writing significant amounts of new business of around £7 billion and £16 billion in 2020 and 2019 respectively, and is one of the few companies with the ability to write very large transactions.

Rothesay's overall business profile will remain somewhat constrained by its sole focus on UK annuities which dominate the Group's liabilities. As such the Group has significant exposure to longevity risk although in 2020 it ceded 87% of this to reinsurers. Such reliance on reinsurance is a potential long-term risk, but at least in the short to medium term, we see a continued appetite amongst reinsurers to take on longevity exposure.

Rothesay's financial profile is good with profitability, asset quality and financial flexibility as relative strengths. The Group's ROC performance has been strong averaging around 13% over the last five years although volatility of results has been a feature with the high ROC of around 21% at YE20 contrasting with the 12% and 3% at YE19 and YE18 respectively. Inherent volatility of results stems from the focus on lumpy annuity business together with the fact that assets are often not sourced until after the execution of bulk annuity deals which is particularly noticeable under current IFRS accounting standards.

Rothesay's asset quality benefits from its lack of intangible assets and a relatively conservative investment portfolio although Rothesay's asset leverage is relatively high. Notwithstanding the good match they provide for the Group's illiquid annuity liabilities, Rothesay also has a meaningful proportion of its asset portfolio in more complex and illiquid investments, some of which are not externally rated and are subject to legislative risk such as loans secured on ground rent.

Rothesay's financial flexibility benefits from the support of its two main shareholders, GIC and Massachusetts Mutual Life Insurance Company (MassMutual), which, together with former shareholder Blackstone, injected £380 million of capital in 2018 (to partly fund the Prudential Public

Limited Company transaction) and £700 million in 2019 to fund new business. Furthermore, the Group's adjusted financial leverage reduced to a relatively low level of 24.5% at YE20 (YE19: 29.1%).

With regard to capitalization, Rothesay has a relatively moderate regulatory solvency ratio target range of 130-150%, and notwithstanding the overall close matching of the Group's assets and liabilities and use of interest rate hedging, the ratio is relatively sensitive to interest rate movements. However, solvency has been consistently and significantly above the target range in recent years and was stable and relatively high during 2020 at 201% (YE19: 202%).

POSITIVE OUTLOOK

The positive outlook for Rothesay reflects the likelihood that the insurer will undertake meaningful bulk annuity volumes over the medium term further establishing its market position. Should Rothesay deliver this, Moody's expects it would lead to more consistent results and with the company continuing to invest assets successfully, return on capital should be sustained at a good level putting upwards pressure on the rating.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Moody's said that the following factors could lead to an upgrade of the Group's ratings: (i) maintenance of good position in the UK bulk annuity market; (ii) sustaining return on capital (Moody's definition) consistently above 6%; (iii) maintaining solvency ratio comfortably above 150%; (iv) sustaining earnings coverage consistently above 6x.

Conversely, the outlook could be revised back to stable if the Group is unable to achieve these rating upgrade factors.

LIST OF AFFECTED RATINGS

Rothesay Life Plc:

- Insurance Financial Strength Rating, affirmed at A3
- Long-term Issuer rating, affirmed at Baa1

The outlook has been changed to Positive from Stable

Rothesay Limited:

- Long-term Issuer rating, affirmed at Baa2

The outlook has been changed to Positive from Stable

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Life Insurers Methodology published in November 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1187348. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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