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Research Update:

South African Life Insurer Liberty Group Ltd. Assigned 'zaAAA' South Africa National Scale Rating

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Overview

- Liberty Group Ltd. is one of South Africa's largest life insurers. We assess its competitive position as strong and its capital and earnings as moderately strong, although the latter reflects its reliance on soft forms of capital.
- Partly offsetting these strengths is our assessment of the moderate industry and country risk in the South African life insurance market.
- We are assigning our 'zaAAA' South Africa national scale issuer credit rating to Liberty, and 'zaAA+' South Africa national scale issue ratings to its subordinated notes.

Rating Action

On Feb. 18, 2016, Standard & Poor's Ratings Services assigned its long-term 'zaAAA' and short-term 'zaA-1' South Africa national scale issuer credit ratings to Liberty Group Ltd. (LGL). We also assigned long-term 'zaAA+' South Africa national scale issue ratings to its subordinated notes (see list below).

Rationale

The ratings on LGL reflect our assessment of the group's satisfactory business risk profile, built on a strong competitive position, and moderately strong financial risk profile, supported by its strong risk-based capital and stable earnings. We assess LGL as core to its parent Liberty Holdings Ltd. (LHL or the group), as LGL makes up majority of the group's revenue, earnings and capital.

The group faces moderate industry and country risk, in our view, based on its exposure to the South African life insurance market. This assessment is unlikely to change as we believe that the company's business will continue to primarily come from South Africa.

Liberty's competitive strengths in the South African life insurance market are complemented by its asset management platform STANLIB, owned by LHL, which contributes about 15% of the group's earnings. One of the largest players in the market, Liberty benefits from a well-established position in the middle affluent market, which it services with sophisticated wealth management solutions. We believe that Liberty has developed a competitive edge in this field, backed by its internal risk management platforms that enable the company to propose attractive product structures and guarantees and dynamically manage the ensuing risks. Liberty has begun to place a greater focus on the institutional sector, where it lags behind its major peers. Liberty does not actively focus on the entry-level market, which it perceives as highly competitive.

We believe that the growth rate in the group's premium income is likely to drop to about 5% annually over 2016-2017, primarily because of the population's lower disposable income due to reduced forecast GDP growth. Liberty's new business margins have been fairly stable at near 2% (based on present value of net new business), which is broadly in line with peers. Liberty has a strong track record of generating return on equity (ROE), with a five-year average of 19%. While the level of ROE is broadly in line with local peers, it is above those in developed markets, mostly reflecting high interest rates and high inflation. We expect the group to achieve similar ROE levels over 2016-2017.

Our view of Liberty's moderately strong capital and earnings is supported by our forecast of strong risk-based capital over 2016-2017, taking into account the group's reliance on a weaker capital component, value of in-force, which makes up a substantial level of total adjusted capital, as well as its appetite for acquisitions. Liberty's capital strengths stem from its prudent policy of managing its capital buffers above a minimum level. Capital management is a central consideration in Liberty's strategic planning, which explicitly identifies capital expenditures and capital sources, allowing Liberty to manage its capital within preset tolerances. The group is well capitalized under both the current regulatory regime and the next one--Solvency Assessment and Management--which is expected to be implemented from January 2017, having been delayed by one year. Our overall financial risk profile assessment of Liberty is moderately strong.

Our assessment of Liberty's intermediate risk position reflects its low-risk, fee-based business with annuity and linked business with guarantee offerings. About 30% of its income from continuing operations come from fee revenues generated by its asset management arm, STANLIB, and from fee-generating insurance products. Liberty's significant exposure to high-risk assets is mitigated by its material amount of products with profit-sharing features. For its shareholder investments portfolio, the group's strategy is to hold 29% in equities, 13% in property, 7.5% in other risky assets (5% in alternative and 2.5% in preference shares), and the remainder in fixed income.

Due to Liberty's access to the local debt market by issuing short-term nondeferrable debt, we assess its financial flexibility as adequate. Its financial leverage ratio is about 15% (based on IFRS equity) and we expect it to remain at similar levels over 2016-2017. Based on our earnings forecasts, we expect Liberty's fixed-charge coverage to remain well above 8x.

We recognize that Liberty's financial risk profile is sensitive to the average credit quality of its investment portfolio. If average credit quality falls below the current 'BBB' range, it could have a negative impact on its creditworthiness leading us to potentially lower its financial risk profile materially (to less than adequate).

We regard Liberty's enterprise risk management (ERM) and management and governance practices as neutral factors to the ratings. We think Liberty's management has a strong track record of executing its strategy and positioning the group to reach its 2020 vision. The group has a very clear strategic plan over both the short term (three years) and long term (six years), containing financial and operational goals geared toward maximizing shareholder value. The goals are tailored to business units and have been applied to customer-facing units (CFU): individual life, group life, and asset management. In common with its peers, the group has a clear acquisition strategy which so far has been in line with its goals.

We assess the group's ERM as adequate with strong risk controls. We consider ERM to be of relatively low importance because of the group's strong capital position and its primary focus on its local market. In our opinion, the group's risk management culture and risk controls are positive factors, while emerging risk management, risk models, and strategic risk management are neutral factors. The risk management culture is strong, with a sound governance structure and good levels of awareness of the importance of risk management. Although the group provides guarantees, it has an extensive hedging programme in place. More importantly, Liberty has a well-embedded risk management platform, LibFin, which is fully dedicated to dynamic hedging and day-to-day portfolio rebalancing in order to monitor risks stemming from asset/liability mismatches. Lapse risk is the most significant risk as a proportion of economical capital requirements. Generally, Liberty's risk tolerance limits are based on the approved strategic initiatives of each business unit.

Owing to the strength of Liberty's available liquidity sources relative to requirements, we assess its liquidity as exceptional.

We consider LHL to be strategically important to its parent Standard Bank SA (SBSA), primarily reflecting Liberty's contribution to the broad wealth management offer of the bank and its meaningful contribution to SBSA's earnings. At the same time, we insulate the ratings on LHL from that on its parent. This reflects our views of LHL financial independence from its majority owner and our expectation that the oversight of the South African regulator will safeguard Liberty's balance-sheet's independence should SBSA's experience financial distress. Our view is also based on LHL's independent board of directors and its sizable minority shareholders who maintain an active economic interest. The ratings on Liberty are therefore not capped by the rating on SBSA at the current level, although a downgrade of SBSA could potentially have a rating impact on Liberty. Our view of Liberty as insulated from its parent could changes if we reconsider the extent of the influence SBSA has on Liberty's management of capital buffers, strategy, or risk-taking.

Under our hypothetical sovereign foreign currency default scenario, we believe that LHL would likely retain positive regulatory capital and a liquidity ratio in excess of 100%. Liberty's excess level of available capital over the regulatory minimum and its discretionary buffers allow it to withstand our foreign currency default scenario. It doesn't pass the more severe local currency default scenario, however. Liberty's liquid investment portfolio also allows it to pass a liquidity stress for assigning ratings above the sovereign.

If we were to lower the local or foreign currency ratings on South Africa, we could lower the ratings on Liberty.

Related Criteria And Research

Related Criteria

- Standard & Poor's National And Regional Scale Mapping Tables, Jan. 19, 2016
- National And Regional Scale Credit Ratings, Sept. 22, 2014
- Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Enterprise Risk Management, May 7, 2013
- Insurers: Rating Methodology, May 7, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Criteria Clarification On Hybrid Capital Step-Ups, Call Options, And Replacement Provisions, Oct. 22, 2012
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- Methodology: Hybrid Capital Issue Features: Update On Dividend Stoppers, Look-Backs, And Pushers, Feb. 10, 2010
- Banks: Assumptions: Clarification Of The Equity Content Categories Used For Bank And Insurance Hybrid Instruments With Restricted Ability To Defer Payments, Feb. 9, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

Ratings List

New Rating

Liberty Group Ltd.	
Counterparty Credit Rating	
South Africa National Scale	zaAAA/--/zaA-1
Liberty Group Ltd.	
Subordinated	zaAA+
Fixed, 5-Year, Issued 13/08/2012	zaAA+

Fixed, 5.5-Year, Issued 03/10/2012	zaAA+
Fixed, 7-Year, Issued 14/08/2013	zaAA+
Floating, 7-Year, Issed 12/12/2014	zaAA+

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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.