

Insurance sector sees non-life segment more stable, life business still volatile in 2009

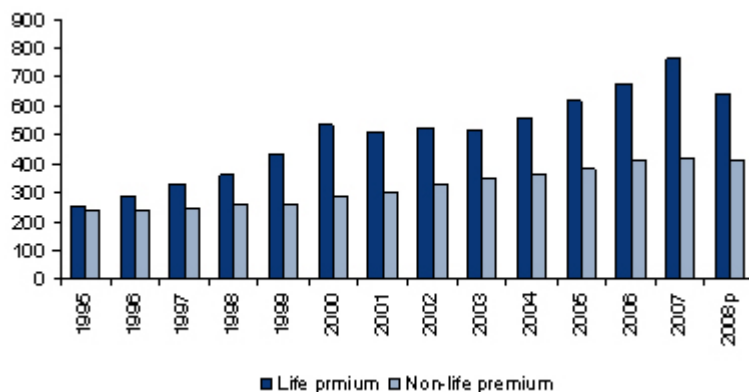
[Back](#)

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- Tough 2008 for the insurance sector: total premium income down by 7% in nominal terms
- Crisis impacted companies' investment portfolios, but insurers less affected than banks; more than a third of worldwide insurance sector losses attributable to US-based AIG
- 2009 to see non-life segment more stable, life business volatile; decline in total premiums expected in Western Europe, moderate premium increase in Central and Eastern Europe
- Insurance is cheapest of DJ Euro Stoxx sectors; Vienna Insurance Group as top pick

2008 was a tough year for the insurance sector. According to the estimates of the CEA (European insurance and reinsurance federation), in 2008, total premium income in Europe amounted to EUR 1,058bn, a decline of 7% in nominal terms and 11% in real terms. However, this has to be seen against the background of outstanding real growth rates in 2004-07, exceeding the 8% mark annually.

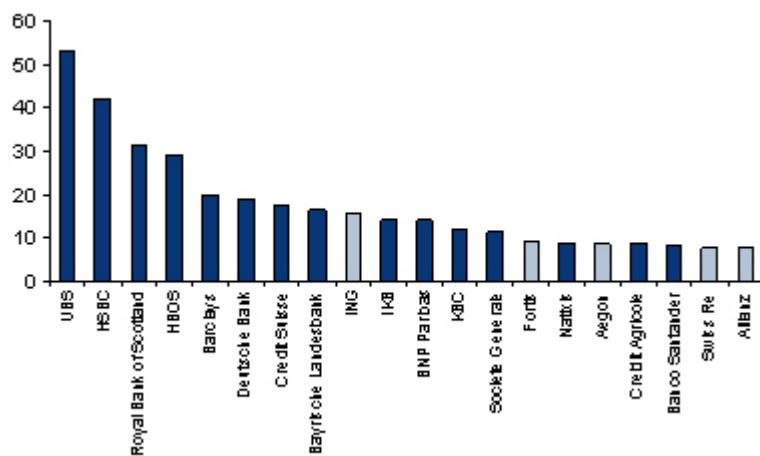
Life and non-life premium development (EUR bn)



Life and non-life premium development

Last year's decline was mainly due to the drop of the life insurance business, down to EUR 653bn or -11% in nominal terms. The sharp drop of the equity markets resulted in declining demand for unit- and index-linked products, where policy holders bear the investment risk. Furthermore, life products were competing against banking products offering higher returns, due to the inversion of the yield curve. The non-life insurance business has proven to be more stable. Premium income in this segment was estimated at EUR 415bn, slightly below the figure of the previous year.

Losses of European financial institutions (USD bn) until 1Q09



Impact of the financial crisis

Generally, most European insurers have largely weathered the financial storms, due to their robust business models as composite insurers.

However, most of them suffered from negative impacts on their investment portfolios. This was not the result of risky investment policies (only 1-2% of assets were invested in ABS), but rather because of falling equity markets and widening bond and liquidity spreads.

However, the insurance sector is less affected by the financial crisis compared to the banking sector. Until 1Q09, the worldwide banking sector (excl. Government-Sponsored Enterprises) had lost more than four times compared to the insurance sector. More than a third of the losses in the insurance sector are attributable to US-based AIG (USD 90bn).

“The financial crisis hit insurance companies with banking business and life insurers especially hard. This was quite obvious in the Netherlands, where this business model is rather common. Banks and life insurance companies have a much higher total amount of investments than non-life insurers. Depreciations of a certain percentage of the portfolio therefore have a bigger impact on companies with a huge investment portfolio. However, since the biggest part of the insurers’ portfolios is classified as available-for-sale, the bulk of the losses are only shown in the companies’ shareholders’ equity. Top decliners in this respect were again Dutch insurers such as AEGON (-60%) and ING (-53%). Only one insurance company was able to post increased equity - Vienna Insurance Group”, explains **Christoph Schultes**, Insurance Sector Analyst at Erste Group and author of the report.

Outlook on premium development for FY09

Looking at the first quarter results of sector companies, the Erste Group analysts do not see a homogenous picture. Non-life business should again be more stable in 2009, while life insurance will remain volatile. They expect a further slight decline in premium income in Western Europe.

In the CEE region, the first quarter showed a moderate premium increase. However, most of the growth was eaten up by the adverse effects of local currencies depreciation. In addition, while the Czech Republic and Poland recorded growth in non-life business, Slovakia and Romania reported shrinkage in this segment. The life insurance sector grew in the Czech Republic and Slovakia, but declined in Poland and Romania. Generally, Erste Group analysts do not expect major developments for FY09.

Valuation

The valuation of the insurance sector looks pretty attractive. The sector is currently traded at a PE ratio of 7.0x for 2010, which is the cheapest of the DJ Euro Stoxx sectors. The P/E ratio for 2011 amounts to 6.1x. A comparison based on ROE and P/B multiples confirms the positive picture.

For the CEE insurers, Erste Group analysts have the following recommendations

- Vienna Insurance Group remains our top pick. We maintain our Buy recommendation and our target price of EUR 44. The company is still traded below its embedded value (EUR 32.5 per share). VIG announced its solvency ratio at >180%, which is higher than those of its peer group. In addition, the company said that its current war chest exceeds EUR 1bn. All in all, the company’s balance sheet looks very healthy, with organically increasing equity and a ratio of investments to technical reserves of 114%.
- The stock of UNIQA – on the other hand – is still not attractive, in our eyes. We derive a new target price of EUR 14.0 (previously EUR 14.9). Due to the fact that UNIQA’s share price has significantly dropped since our last report, we upgrade our recommendation to Hold (from Reduce). A peer group comparison confirms our neutral stance on the share. While other insurance stocks look quite attractive at the moment, UNIQA’s stock (with the highest P/E ratios and relatively high P/B multiples) does not.

[Insurance Report \[pdf; 329.1 KB\]](#)

[Back](#)