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Mapfre Group

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Mapfre Group

Please note that the ratings covered by this full analysis apply only to core entities of the group, which are listed below. These ratings do not apply to any noncore or unrated entities of the group. Ratings assigned to noncore entities of the group are published individually.

Major Rating Factors

Holding Company: Mapfre S.A.
Counterparty Credit Rating
Local Currency
BBB/Negative/--
Operating Companies Covered By This Report
Financial Strength Rating
Local Currency
A-/Negative/--

Strengths:

- Increasing geographic diversification, enhanced by leading positions in the Spanish and Latin American insurance markets.
- Strong operating performance, despite challenging operating and financial environments.
- Management's good track record and focus on underwriting discipline.

Weaknesses:

- Relatively high credit risk exposure, resulting from a significant exposure to Spanish sovereign fixed-income securities and Spanish banks.
- Increased and significant country risk exposure, resulting from the difficult economic and financial climate in Spain, Mapfre's core market.
- Weakened, albeit still strong, capital adequacy and weakened quality of capital, mostly resulting from acquisitions and organic business growth.

Rationale

Mapfre S.A. is the holding company of Spain-based Mapfre insurance group (Mapfre). We regard Mapfre Global Risks, Compania Internacional de Seguros y Reaseguros S.A. and Mapfre Re, Compania de Reaseguros, S.A. as core operating entities of Mapfre. The ratings on these entities reflect Mapfre's increasing geographic diversification, enhanced by leading positions in Spain (foreign currency BBB+/Negative/A-2) and Latin America, and its strong operating performance together with a track record of good management, which Standard & Poor's Ratings Services considers to be marginally positive for the ratings. These factors are partially offset by relatively high credit risk exposure, increasing country risk exposure, and weakening levels of capital adequacy and quality. Under our criteria (see "Nonsovereign Ratings That Exceed EMU Sovereign Ratings: Methodology And Assumptions", published on June 14, 2011), we maintain a one notch rating differential between the ratings on Mapfre and the Spanish sovereign ratings. This is based Mapfre's geographic diversification in countries rated higher than Spain, and the sensitivity of the insurance sector to country risk, which we regard as high.

The Mapfre group has a strong competitive position. The group business and risk profiles benefit from increasing geographic diversification, enhanced by leading and profitable positions in its core markets. In our base case scenario, despite the constrained organic growth prospects in its domestic market, we expect the South American (particularly Brazilian) and global businesses to drive consolidated annual business growth of 10% in 2012 and 2013.

Mapfre's operating performance remains stable and strong, benefiting from the group's successful geographic diversification, a mix of organic growth and acquisitions, and strict underwriting discipline. In our base-case scenario we expect Mapfre will report a post-tax and minorities result of approximately €750 million in 2012, a contraction from €963 million in 2011, mostly driven by higher impairments and unrealized losses on investments, and lower positive exceptional items. The expected return on equity (ROE) is 10%, which we still regard as strong in the current difficult environment. On a consolidated basis, we expect the non-life combined ratio to remain below 98% in 2012 and 2013. We also expect new life insurance business margins in Spain to remain strong above 5% based on PVNBI.

We consider management to be a marginally positive factor for the ratings. It has demonstrated its ability to grow, both organically and by acquisition, without losing its focus on profitability, underwriting discipline, and customer service. However, management has pursued growth that has consumed capital at a time when asset risk has increased markedly. Furthermore, in our opinion the group's ERM does not yet benefit from the more-sophisticated approaches (including well embedded internal models) used by some peers.

We regard Mapfre's investments as a relative weakness for the ratings. Our opinion mostly reflects the credit risks associated with Mapfre's dominant fixed-income portfolio of €30 billion, 67% of which is rated in the 'BBB' category or lower. Spanish government and financial institutions debt comprises 44% of its fixed-income portfolio or 1.3x its shareholders' funds. Although consistent with a close ALM strategy, this concentration is exposing Mapfre to the risks associated with the deterioration of Spanish government and financial institution credit quality.

Although we regard Mapfre's capitalization as strong, we believe the level and quality of capital adequacy have weakened since 2010. Capitalization no longer represents a relative ratings strength. Over the past two years, strong business growth and deteriorating credit quality of Spanish and other European bonds have not been matched by growth in shareholders' capital.

Outlook

The negative outlook reflects that on Spain and our view of the potential weakening in Mapfre's business and financial risk profiles if the operating, economic, and financial environment in Spain were to deteriorate further.

We could lower the ratings on Mapfre's core operating subsidiaries if we were to lower the ratings on Spain. We could also lower the ratings on Mapfre if the country risk exposure were to significantly increase as a result of increased exposure to Spain and/or increasing difficult operating conditions in Spain; or if the level or quality of capital and the investment portfolio were to deteriorate further. Conversely, we could revise the outlook to stable following a similar rating action on Spain and if pressure on Mapfre's capital and investment quality were to ease.

Corporate Profile: An Increasingly Diversified Multinational Group

Established in 1933 in Spain as Mapfre Mutualidad, as a mutual providing coverage for work-related accidents, Mapfre is a multinational insurance group. In 2011, its premiums totaled €19.6 billion and shareholders' funds totaled €9.7 billion. The group writes most lines of insurance business and operates in 46 countries. Mapfre groups its operations into three main business divisions:

- Spanish direct insurance business. This division accounted for €7.9 billion in gross premiums written (GWP) in 2011 and operates in its local market via three unrated entities: Mapfre Familiar (not rated) for individual non-life insurance, Mapfre Vida (not rated) for life insurance, and Mapfre Empresas (not rated) for commercial insurance.
- International direct business. This division, which accounted for €8.8 billion GPW in 2011, embraces two main entities. Mapfre America (not rated) is the holding company for the subsidiaries operating in 17 countries in Latin America, while the remaining international direct operations are grouped under Mapfre Internacional (not rated). These include U.S.-based Commerce Insurance Co. and Citation Insurance Co. (both rated A-/Negative/--, and collectively referred to as Commerce).
- Global insurance business. This area includes Mapfre's operations providing global solutions, mostly via local representative offices: Mapfre Re, Compania de Reaseguros, S.A. (Mapfre Re; A-/Negative/--), Mapfre Global Risks (A-/Negative/--), and Mapfre Asistencia (not rated). This area accounted for €4.2 billion GPW in 2011.

Mapfre S.A. (BBB/Negative/--) has been the holding company controlling all the group's operating entities since 2006. Mapfre S.A. is itself ultimately 64.6%-owned by Cartera Mapfre, S.L., which is fully owned by Fundación Mapfre, a charitable foundation. Banco Financiero y de Ahorros S.A. (BFA; B+/Watch Neg/B), parent company of Bankia S.A. (Bankia; BB+/Watch Neg/B) owns 14.9% of Mapfre S.A., and the remaining 20.4% is widely held as the entity is listed on the Madrid and Barcelona stock exchanges.

Competitive Position: Strong, With Robust International Growth Increasingly Offsetting A Challenging Domestic Market

Table 1

Mapfre S.A. -- Competitive Position					
	-- year-end Dec. 31 --				
Mil. €	**2011**	**2010**	**2009**	**2008**	**2007**
Gross premium written	19,600	16,973	15,607	14,305	12,310
Annual change in gross premium written (%)	15.48	8.75	9.10	16.20	12.60
PC: Gross premium written	14,842	13,053	12,076	10,983	9,384
PC: Annual change in gross premium written (%)	13.71	8.09	9.96	17.03	9.99
Life: Gross premium written	4,758	3,920	3,531	3,322	2,926
Life: Annual change in gross premium written (%)	21.37	11.04	6.27	13.53	21.88
Net premium earned	17,093	14,823	13,714	12,473	10,606
Annual change in net premium earned (%)	15.31	8.08	9.95	17.60	13.52
Separate accounts/unit linked assets	1,879	1,717	799	472	362
Life: Growth in separate accounts/unit linked assets (%)	9.43	114.95	69.06	30.37	41.67
Total invested assets	37,610	34,957	31,488	31,000	29,019
Growth in invested assets (%)	7.59	11.02	1.57	6.82	9.42

The group's overall competitive position is regarded as strong. The group business and risk profiles benefit from increasing geographic diversification, enhanced by leading and profitable positions in its core markets of Spain and Latin America, a balanced exposure between mature and fast growing countries, and reducing reliance on Spain, its core market. Underpinning these leading positions are diversified and sizable distribution networks, a client-service focus, and successful sharing of best practices. In 2011 and first-half 2012 gross premiums grew by 15% year-on-year, mostly driven by strong organic growth and acquisitions and JVs in Latin America.

Because some 39% of Mapfre's business is still written in its domestic market and a further estimated 24% in markets that have same or lower sovereign ratings than Spain, our view of Mapfre's overall competitive position is constrained by its relatively significant exposure to country risk. We believe this risk is high relative to peer Europe-based global insurance groups and has increased following the recent downgrade of Spain. The group's overall business risk profile is also constrained by an increasing exposure to large corporate risks, as well as natural catastrophe risks.

Direct Spanish operations

With a 13.7% market share, Mapfre is the largest Spanish insurer, benefiting from its leading position in the non-life sector. Mapfre Familiar is the largest underwriter of Spanish motor business with a market share of 21%. Mapfre Vida ranked as the third-largest life insurer in Spain in 2011. It had a market share of about 11% and is also the largest asset manager among Spanish insurers. This leadership in personal and small commercial lines is reinforced by market-leading positions in large corporate/industrial business through Mapfre Global Risks (see below) and Mapfre Empresas.

The insurer benefits from the power of the Mapfre brand, which has seen the group expanding its activities into add-on services, such as domestic and roadside assistance, which have also boosted its technical performance. The group's major strength is its wide geographic coverage, reinforced by an extensive network of 3,155 offices. This is complemented by a distribution capacity of 4,336 bank branches provided by joint ventures and agreements with an increasing number of Spanish savings banks, most notably Bankia (formerly Caja Madrid) since 2000 and Catalunya Caixa (not rated) since 2010. These factors, together with the 2010 launch of Verti (a direct sales company operating via the Internet and telephone), and an increased focused on exploiting cross-selling opportunities, has seen the group post 6.1% growth in Spain versus 4.1% for the market generally. This has partly offset the negative impact of the difficult economic and financial climate.

International business: direct and global

Mapfre's business risk profile increasingly benefits from its geographic diversification, in particular in Brazil and the U.S. These are Mapfre's second- and third-largest markets, representing €3.6 billion and €1.4 billion GWP, respectively, in 2011. The Mapfre group is the third-largest insurance player in Latin America, an expanding market. It has signed distribution agreements with financial and nonfinancial entities. The full consolidation of the joint ventures with Banco Do Brasil S.A. (BBB/Stable/A-2) and strong organic growth increased Mapfre's Latin American premium volumes by 46% in first-half 2012 and 33% in 2011 (20% in 2010). This has strengthened its position in the life sector in South America and consolidated its position as the largest non-life insurer in the region with an estimated market share of 10.5%. In the U.S., Commerce is a significant and entrenched player in Massachusetts and has privileged access to various American automobile associations.

Further geographical and business diversification is provided by Mapfre Re (€2.6 billion GWP in 2011), the group's reinsurance arm, and Mapfre Global Risks (€1.0 billion GWP in 2011), a specialized unit focused on the coverage of large and global commercial risks. The most international of the Mapfre group companies is Mapfre Asistencia (€0.6 billion premiums in 2011), which has a direct presence in 40 countries.

Prospective

We anticipate that Mapfre group will maintain its strong competitive position by consolidating its market-leading positions in Spain and Latin America, and further increasing its geographical diversification.

Domestically, protracted economic and financial uncertainty in Spain is likely to continue to hinder volume growth prospects, in particular in the motor business and life business sold via its major bancassurance agreements. Although Mapfre will continue to build on its main competitive advantages, increasing its focus on cross-selling, we expect domestic business to contract by 5% in 2012. In our opinion, Mapfre is also well placed to become the exclusive insurance partner of Bankia, should the bank eventually opt for just one partner. This would give Mapfre access to some 1,100 further bank branches, although it would likely reduce the benefits to its business risk profile deriving from its international diversification.

Despite the constrained organic growth prospects in its domestic market, in our base-case scenario we expect the South American business, in particular Brazil, and the global business to drive 10% consolidated annual growth in both 2012 and 2013.

Management And Corporate Strategy: Proven Track Record

We view Mapfre's management as marginally positive for the rating. It has demonstrated its ability to grow, both organically and by acquisition, without losing its focus on profitability, underwriting discipline, and customer service. However, management has pursued growth that has consumed capital at a time when asset risk has increased markedly. Furthermore, in our opinion financial management does not appear to have kept pace with some peers with more sophisticated and embedded full internal models.

Strategy

Mapfre's long-term strategy is centered on strengthening the group via profitable organic and external growth, focusing on its core insurance business and maintaining strict underwriting discipline. The 2008 acquisitions in the U.S. and Turkey provide ready evidence of a widening of Mapfre's geographic focus beyond its traditional core regions of the Iberian Peninsula and Latin America, although more recent acquisitions demonstrate the continuing importance of these regions. The creation of Mapfre Global Risks reflects the group's intention to compete in the international large corporate insurance market.

Standard & Poor's sees little strategic risk in further small-scale acquisitions, JVs, and other acquisitions in Latin America. However, the more recent buy-outs of minority interests and JVs have consumed capital at a time when asset risk has increased markedly. We consider that Mapfre is successfully managing the integration of Commerce, the acquisition of which introduced the associated risks of operating in a highly regulated, unfamiliar market.

Operational management

Mapfre's corporate structure has been rationalized over the past few years, improving both operational efficiency and market transparency. The group has generally adapted strategies to organizational capabilities and vice versa, as demonstrated most recently by the latest group reorganization into three major divisions (see "Corporate Profile").

The reorganization should enable Mapfre to further build on its existing operating strengths in tight cost-control policies: centralized reporting of underwriting, investment, and planning. Mapfre's acquisitions in the U.S. and Turkey put its operating strengths and its other group strengths--e.g., training, transfer of expertise, and pricing--to the test. Mapfre has a disciplined approach to sharing best practices and dealing with underperforming units, as demonstrated by the disposal of Quavitae and its 49% share in Banco de Servicios Financieros, its former banking JV with Caja Madrid, in 2011.

Financial management

We understand that capital is being managed more actively than in the past. The increased level of debt needed to finance the acquisitions pushed the financial leverage ratio (including hybrid as well as short-term debt) as high as 36.7% at year-end 2008, placing it slightly outside the rating category tolerance range. Mapfre has since made conscious efforts to reduce its outstanding debt and thus this ratio fell to 20.8% by the end of 2011. The group maintains a good level of capitalization for all subsidiaries, although its approach to assessing capital requirements and allocating capital, which in theory we would expect to see evolve in tandem with group financial and business risk profiles, does not yet benefit in our view from the more-sophisticated approaches (including well embedded internal models) used by some peers. Although Mapfre's strength in Latin America exposes it to sovereign risk, the concentration risk is mitigated by its exposure to 17 countries. Capital adequacy at the subsidiary level and overall balance-sheet currency risk are both well managed.

Enterprise Risk Management: Adequate With Strong Risk Controls

We consider enterprise risk management (ERM) in the Mapfre group as adequate overall, with strong risk controls for most of its major risks. Historically of moderate significance to the group's overall rating, ERM's importance continues to increase in line with the group's more active capital management strategy, increasingly complex and diversified business risk profile, and increasing asset-risk exposure.

Insurance risks remain the most important risk exposure for the group and these are generally controlled using strong or well-developed risk controls. Investment risk is the second most important exposure for the group and we believe it is increasing as a result of the deteriorating credit quality of its investment portfolio. The group's risk culture is robust, but our assessment continues to remain at adequate as Mapfre has not yet fully articulated its risk appetite in a comprehensive framework.

We see ERM as increasingly embedded in the strategic decision-making process. The group is acquisitive and risk concerns are a key part of these considerations. The group currently uses an economic capital framework to model insurance risks in its domestic market, and it has planned a gradual implementation of a wider economic capital framework at other subsidiaries and at group level. The group already uses return on risk-adjusted capital (RORAC) approaches in its pricing and planning processes; however, these are currently still broadly based on Standard & Poor's risk-based capital (RBC) model, rather than on its internal assessment of risk. This holds back its strategic risk management (SRM) score to adequate.

The controls over the group's underwriting processes are generally regarded as strong and are based on a clear articulation of limits, authorizations, etc. against the group's minimum standards. Underwriters can write most business locally; however, more complex and large cases are assessed centrally. A similar process operates for life assurance underwriting.

Reserving is carried out using traditional tools. Reserves for complex and large cases are managed centrally. The group uses regular external actuarial reviews to ensure that reserves (at both group and subsidiaries levels) are appropriate and make substantial use of Mapfre Re for all reinsurance needs. We consider Mapfre Re's process for assessing its outward programs to be strong as it uses its internal capital model to decide which program will bring the best return for the group.

Accounting: Adjustments Made To IFRS Numbers For European Embedded Value, Goodwill, And Discounting In Capital Analysis

Mapfre reports under International Financial Reporting Standards (IFRS), although for regulatory purposes the Mapfre group still reports under Spanish generally accepted accounting practices (GAAP), which now closely resemble IFRS. Our data is derived from the IFRS annual accounts, which merge figures for direct non-life, indirect non-life, and indirect life insurance.

While we regard the level of disclosure adequate for a publicly-listed entity, continuous changes in the consolidation scope, and related nonrecurring items in the accounts, make it difficult to compare performance year-on-year.

Our non-life net expense and combined ratios of 28.1% and 97.5%, respectively, in 2011, differ from those reported by the company (27.7% and 96.9%). In determining the total expenses base, we have included €24 million net other nontechnical charges, disregarding €44 million other underwriting income.

Our non-life GPW include the non-life direct insurance and accepted reinsurance gross written premiums, minus all the consolidations adjustments.

In adjusting the 2011 reported shareholders funds to TAC in our capital model, the most material changes were:

- Partial equity credit given to the off-balance-sheet value of Spain and international business in-force before minorities;
- Credit for off-balance-sheet unrealized gains and losses on real estate investments, net of corporate taxes;
- Partial credit for discounted non-life claims and unearned premiums reserves; and
- Deduction of intangible assets included in the balance sheet net of corporate tax.

Operating Performance: Strong; Resilient To The Difficult Operating and Financial Environment

Table 2

Mapfre S.A. -- Operating Performance					
	-- year-end Dec. 31 --				
Mil. €	**2011**	**2010**	**2009**	**2008**	**2007**
Net income after minorities	963	934	927	901	731
Return on revenue (%)	8.89	7.78	9.10	10.35	11.14
Return on revenue (including realized & unrealized gains/losses) (%)	8.93	9.08	10.01	10.71	12.50

Table 2

Mapfre S.A. -- Operating Performance (cont.)					
Return on assets excluding all investment gains (%)	3.50	2.97	3.48	3.93	3.92
Return on equity (%)	13.92	14.29	16.18	17.58	18.22
Total net expense ratio (%)	24.55	23.23	22.40	22.15	22.14
PC: Return on revenue including realized & unrealized gains/ (losses) (%)	8.48	10.36	10.63	12.11	13.21
PC: Gross loss ratio (%)	69.34	76.90	68.09	69.74	68.66
PC: Net loss ratio (%)	69.28	70.54	70.73	68.80	68.09
PC: Total net expense ratio (%)	28.14	25.92	24.88	25.26	25.24
PC: Net combined ratio (%)	97.47	96.49	95.65	94.08	93.40
PC: Net investment income / Net premium earned (%)	6.14	7.30	6.72	6.74	7.22
Life: Return on revenue including realized & unrealized gains/ (losses) (%)	10.40	7.91	7.42	6.26	5.65
Life: Net acquisition expense ratio (%)	11.44	12.20	10.62	9.36	9.56
Life: Net administrative expense ratio (%)	3.15	3.40	4.21	3.81	3.59
Life: General expense ratio (%)	15.24	16.12	15.23	13.79	13.45
Life: Pre-tax earnings (pre-bonus result) / Assets (%)	1.49	1.08	0.90	0.94	0.70
Net investment income / Net premium earned (%)	10.23	10.74	10.78	13.32	11.60
Net investment yield (%)	5.07	4.98	4.83	5.61	4.48
Net investment yield including realized capital gains/ (losses) (%)	5.49	5.61	5.41	5.93	5.25
Net investment yield including all capital gains/ (losses) (%)	5.08	5.59	5.35	5.57	5.20

Mapfre's operating performance continues to be strong, benefiting from the group's increasing and successful geographic diversification, very strong underwriting, and mix of organic and external growth. Our opinion is based on the insurer's notable track record of strong and stable underwriting and reported results. Despite the difficult global economic and financial environment, Mapfre has consistently reported a net income and ROE above €900 million and 14% since 2008. The group reported a €434.2 million net result at end-first-half 2012. Although implying a contraction of 20.1% versus the same period in 2011, given the current difficult operating and financial environments we believe these levels remain evidence of the continuity of Mapfre's strong performance. Higher realized and unrealized investment losses are expected to be offset by continuing strong underwriting results, in particular non-life, and strong business growth. We expect the 2012 non-life combined ratio to remain in line with 2011 at 97.5% (96.5% in 2010), while we expect life new business margins to remain high at 5%.

Historic performance

We believe that the group's earnings reflected another strong performance in first-half 2012, and, in particular, in 2011. Organic growth, a conservative approach to market risk, and underwriting discipline continue to sustain Mapfre's income. The first-half 2012 non-life combined ratio as reported by Mapfre slightly improved by 90 basis points year-on-year to 95.6%, versus our calculation of 97.5% in 2011 and 96.5% in 2010 (see Accounting section). The deteriorating expense ratio, mostly driven by business growth, is being offset by a strong and improving loss ratio. The results are remarkable given the softening market conditions in both motor and commercial insurance in Spanish non-life. The market continues to benefit, however, from improving frequency and the historic low severity of motor claims versus other markets. Dependence on the Spanish non-life business to total earnings continues to reduce, and it represented about 39% of the total at end-June 2012, versus 43% at year-end 2011. All major operating units recorded an underwriting profit at end-first-half 2012. In particular, Mapfre USA Corp. and Mapfre Re are showing a stronger improvement compared with the first six months of 2011. Mapfre Re saw a substantial increase in the loss ratio at year-end 2011, which weakened by 6% to 72%, as a result of major catastrophic events, namely in Japan, New Zealand, and Thailand, which together cost the Mapfre Group some €140 million net, including reinstatements, versus some €106 million costs related to the Chilean earthquake in 2010. Mapfre's PC return on revenue (ROR) weakened to a still very good 8.5% (10.4% in 2010).

The group reported very stable investment yields of just above 5% in 2011, which we consider more than respectable considering the current financial environment and the group's prudent investment strategy.

Mapfre's operating performance continues to benefit from a very profitable life insurance book. We view positively the strong organic and external growth in the life insurance business in South America, which is reducing concentration in Spain. In 2011, Mapfre's new business margins in Spain further improved to 6.1% (5.4% in 2010), driven by the persistency of strong mortality experiences and a more profitable business mix, which have more than offset a 23% contraction in the present value of the new business income generated by the banking channel (in particular Bankia and Catalunya Caixa). The increasing incidence of protection products versus saving products sold via the banking channel, and the impressive performance of the agency channel, have seen 7.7% growth in the value added by new business, to €237.5 million. The return on European embedded value (EEV) improved to 7.8% from 4.9% in 2010. The aggregate EEV itself increased to €2,729 million from €2,490 million in 2010, benefiting also from a higher net asset value.

Quality of earnings is strong, reinforced by the increasing geographic and business diversification resulting from strong organic and external growth outside Spain. At first-half 2012, over 45% of Mapfre's profits were generated by direct foreign and global operations, representing a substantial increase in non-Spanish earnings compared with less than 30% just three years before.

Prospective

Standard & Poor's expects Mapfre's operating performance to remain strong. In our base-case scenario we expect Mapfre will report a post-tax result of approximately €750 million in 2012, implying a 22% deterioration year-on-year, and an ROE of 10%.

On a consolidated basis, we expect the non-life combined ratio to remain below 98% in 2012 and 2013. We forecast the technical performance of the Spanish operations will remain very strong, with all lines of business--other than the motor personal line--driving a small improvement in the combined ratio, domestically.

The difficult Spanish economic and financial climate is likely to hinder premium growth, in particular the life business sold via the bancassurance channels. We expect, however, new business margins to remain strong above 5%, while the incidence of the foreign business continues to increase.

In our base-case scenario we also assume a contraction in the investment yield of 0.5%, from a very stable 5% in 2011, owing to expected higher impairments and unrealized losses compared with 2011. First-half-2012 results were negatively affected by a €131.9 million assets impairment related to Greek bonds and the strategic participations in Bankia and Cattolica, in part offset by a €21.5 million net release in the provision for financial instability.

The major threat to our base-case scenario is the potential negative impact on both the domestic and global business, and on the investment performance, of a significant deterioration of yields on and credit quality of both Spanish financial institution and government bonds.

Investments: Credit Quality Of The Investment Portfolio Has Deteriorated

Table 3

Mapfre S.A. -- Liquidity and Investments					
	-- year-end Dec. 31 --				
Mil. €	**2011**	**2010**	**2009**	**2008**	**2007**
Total invested assets adjusted	35,731	33,241	30,689	30,528	28,657
Illiquid invested assets / Total invested assets (%)	8.75	10.59	9.60	11.27	9.79
High risk assets / Total invested assets (%)	14.59	15.19	13.22	16.07	18.33
Common equity investments / Capital (%)	48.36	40.88	26.72	71.44	55.83
Real estate investments / Capital (%)	58.07	66.05	46.10	90.03	40.16
Investment Portfolio Composition					
Cash & cash equivalents (%)	3.51	4.50	2.81	4.64	5.72
Total bonds (%)	81.90	80.31	83.98	79.29	75.95
Common stock (%)	5.84	4.60	3.61	4.81	8.54
Real estate (%)	7.01	7.43	6.24	6.06	6.14
Investments in affiliates (%)	0.37	1.20	1.40	1.07	1.17
Other investments (%)	1.38	1.96	1.97	4.14	2.48
Total portfolio composition (%)	100	100	100	100	100
LIQUIDITY					
Liquidity ratio (x)	4.92	5.35	5.95	4.94	6.90
Invested assets / Total assets (%)	69.31	72.93	75.55	78.03	80.77
Invested assets / Loss & unearned premium reserve (%)	312.14	342.50	330.53	349.19	389.30
Liquid assets / Short-term debt (%)	2,826.81	2,755.62	2,736.16	1,458.12	5,227.23
P/C: Liquid assets to technical reserves	269.63	282.65	282.36	292.31	327.43

Strategy

Standard & Poor's regards Mapfre's investments as good (see table 3). Our opinion mostly reflects the credit risks associated with Mapfre's fixed income portfolio of €30 billion, 67% of which is rated in the 'BBB' category or lower. Mapfre has historically focused on high quality and liquid fixed income assets, maintaining its market risk exposure at relatively low levels. The group's geographic business mix has driven Mapfre to build a significant exposure to Spanish bonds. Although consistent with a close ALM strategy, this concentration is exposing Mapfre to the risks associated with the deterioration of Spanish government and financial institution credit quality, which are negatively affecting the insurer's investment and wider financial risk profile.

Credit risk

In our opinion, Mapfre's credit risk exposure has increased over the past 12 months to levels no longer in line with its ratings. At June 2012, we estimate the group had some €8.1 billion invested in Spanish sovereign debt (27% of its fixed-income portfolio or 0.8x its shareholders' funds). Mapfre also invests €4.9 billion in Spanish financial institutions (16% of its fixed income portfolio or 0.5x of shareholders' funds), and holds an estimated 70% of its €1.3 billion bank deposits in Spanish financial institutions.

Exposure to Italy, Ireland, and Portugal amounts to €1.8 billion, while in first–half 2012 the group had impaired Greek bonds of €41.5 million.

Although 30% of Mapfre's fixed-income investments are matched with life reserves, it maintains the credit risk associated with these investments.

Market risk

Overall exposure to equity investments (including mutual funds) is limited, having decreased to 6% at year-end 2011, following a gradual divestment over the past five years. Real estate investments represent 7% of the total invested portfolio, and a significant proportion of these investments backs technical reserves. This figure is not likely to increase as the group focuses on the management, rather than the expansion, of the existing portfolio. Properties are reported in the accounts at their acquisition cost, at more than 30% lower than market value.

In the first six months of 2012, Mapfre has been negatively impacted by global financial market developments, impairing its participations in Bankia and Cattolica by €90.4 million. Mapfre's relative concentration in these participations is understandable when looking at their strategic rationales. In our base case, we do not expect potential further significant impairments on the equity/real estate portfolios.

Asset-liability management

Given the strong regulatory control in this area, we do not consider ALM to be a major concern, as the average duration of assets matches liabilities in almost all the classes.

There is a theoretical exposure to interest rate risk arising from life insurance contracts carrying guaranteed rates of return above 4%, and these liabilities represent almost a third of the total Spanish life liabilities. Exposure to interest rate risk is mitigated, however, by the close ALM, and the fact that about 80% of these reserves do not have a guaranteed surrender value, while only 8% of these reserves would have brought about the realization of some losses for Mapfre at year-end 2011 in the event of lapses by all policyholders. Liabilities deriving from the pensions externalization process are matched through swaps.

Liquidity: Liquid Investment Portfolio And Strong Operating Cash Flows

Liquidity is strong, given the high percentage of readily realizable assets and strong operating cash flows. The ratio of liquid assets to total technical reserves remained substantially unchanged year-on-year at 98% in 2011. Volatile yields on Spanish bonds could impede the ability and willingness of Mapfre to freely dispose of bonds in order to raise cash. Furthermore, we expect life net inflows to be negative in 2012, as a result of the expected strong contraction of the Spanish life business sold by the bancassurance channel. This risk is in part offset by the expected strong consolidated operating cash flows, current levels of cash holdings, and the fact that part of its fixed-income portfolio is made up of readily realizable bonds, which do not carry any unrealized loss.

At year-end 2011 and first-half 2012, holdings in cash and cash equivalents stood at €1.2 billion (€1.5 billion in 2010), against €1.2 billion of non-hybrid debt. We understand the decrease in 2011 has been a conscious management decision, although we note weaker investment cash flows and reducing levels of leverage. Mapfre has ready access to bank facilities, as evidenced by the syndicated loan facility provided for the acquisition of Commerce, as well as committed credit lines.

Capitalization: Strong; Weakened Due To Strong Business Growth And Higher Credit Risk Charges

In our opinion, Mapfre's capitalization has deteriorated to just strong, from previously very strong levels. Acquisitions, joint ventures, buy-outs of minorities, and deteriorating credit quality of its investment portfolio have caused both the level and quality of capital adequacy to weaken. Our opinion on capitalization also reflects adequate reserving, and effective reinsurance protection.

Table 4

Mapfre S.A. -- Capitalization					
	-- year-end Dec. 31 --				
Mil. €	**2011**	**2010**	**2009**	**2008**	**2007**
Total shareholder equity (%)	9,726.60	7,795.80	7,093.80	5,716.40	5,614.40
High risk assets / Total adjusted capital (%)	120.92	135.05	97.70	238.88	119.86
Shareholders funds to reported general account reserves	0.50	0.43	0.42	0.34	0.34
Reinsurance utilization (%)	10.92	10.58	10.50	10.58	10.60
PC: Reinsurance utilization (%)	12.64	12.29	12.43	12.84	12.99
PC: Loss reserves / Net premium written (%)	47.67	49.07	47.77	51.04	52.11
PC: Loss & unearned premium reserve / Net premium written (%)	93.26	91.85	92.91	96.81	96.69

Capital adequacy

According to Standard & Poor's risk-based model, Mapfre's capital adequacy has deteriorated since 2009, and in our base-case scenario we forecast little redundancy at the 'A' level at year-end 2012. Shareholders funds, if adjusted by the level of intangible assets (including goodwill), have remained almost flat since 2009. Liability and asset risks have increased, driven by strong business growth (10% annual compound rate), while the deterioration of the credit risk of its portfolio causes higher related charges in our capital model. We expect pressure on capital adequacy to remain during 2012, owing to strong business growth, an acquisitive strategy, dividend payments, and weaker earnings.

Quality of capital

We believe Mapfre's quality of capital has weakened to just good. Intangible assets at first-half 2012 accounted for 48% of total shareholders' funds. Minority interests now account for 28% of total shareholders' funds versus 13% at year-end 2009, negatively affecting the fungibility of the overall capital. Quality of capital continues to benefit from the low exposure to equity market volatility and to catastrophe risks in Spain, its largest market. However, the increasing geographical expansion of Mapfre is raising the previously relatively low exposure to catastrophe risks elsewhere. We note positively, though, that Mapfre has significantly reduced its outstanding debt levels, which had increased when it acquired Commerce. Mapfre's financial leverage (including short-term debt) decreased to 20.8% as of year-end 2011 from 36.7% in 2008.

Reserves

Favorable reserves development and regular external actuarial reviews (at both the group and subsidiaries level) show an appropriate level of reserving, particularly for Mapfre's Spanish and indirect businesses. The ratio of non-life technical reserves to net premium written decreased to about 85% at year-end 2011 (92% in 2010). This figure may not appear to be particularly high, but Mapfre's book of business is predominantly short-tail and its claims are settled speedily.

Reinsurance

The Mapfre group uses reinsurance to effectively smooth peak risks. Mapfre Re acts as the group's reinsurer. The reinsurance utilization ratio remained extremely stable at 10.9% in 2011. The ultimate net retention level is conservative, and the retrocessionaires used by Mapfre Re are of excellent quality.

Financial Flexibility: Strong; Under Pressure In Difficult Market Conditions

We consider Mapfre's financial flexibility (defined as the ability to source capital relative to capital requirements) as good, having weakened from very strong levels given current state of the capital markets, as well as the pressure of capital adequacy and earnings.

Table 5

Mapfre S.A. -- Financial Flexibility					
	-- year-end Dec. 31 --				
Mil. €	**2011**	**2010**	**2009**	**2008**	**2007**
EBIT interest coverage (x)	23.58	14.88	14.66	10.43	9.41
EBIT fixed charge cover (x)	23.58	14.88	14.66	10.43	9.41
Dividend cover (x)	3.32	2.46	2.66	2.76	2.86
Debt leverage (%)	14.22	16.76	16.61	27.97	10.35
Financial leverage (%)	20.83	23.53	23.77	36.69	20.13
Debt / EBITDA (including capital gains/losses) deficit as debt (x)	0.73	0.97	0.92	1.48	0.52
Financial obligations / EBITDA (including capital gains/losses) (x)	1.07	1.36	1.32	1.94	1.01
Hybrids treated as equity	608	610	621	724	738

Mapfre's capital needs over the next two years are expected to derive mostly from strong organic growth in South America, increasing exposure to large commercial and catastrophic risks as well as to severe weather-related claims, acquisitive strategy, and dividends payments to its shareholders.

The group's main sources of financial flexibility remain its sound track record of strong operating performance, and flexible, although less than before, capital allocation strategy. Effective reinsurance covers also play a key role in absorbing major losses.

In recent years, Mapfre S.A. has also demonstrated its ability to raise capital more effectively than under its previous mutual-based structure. Fundación Mapfre, the ultimate shareholder, remains an important potential source of capital.

The acquisition of Commerce in 2008 was initially financed via a bridging loan, repaid in 2010. In 2008, Mapfre successfully raised a further €700 million via a hybrid debt issuance. Since then Mapfre has repeatedly increased its capital via annual dividend reinvestment plans, which have always attracted widespread shareholder participation. We believe, however, that current difficult financial markets conditions and the loss of 32% in Mapfre's share price since the beginning of the year 2012, would make more difficult, although not impossible, to tap the markets, should Mapfre need to do so.

Related Criteria And Research

- Principles Of Credit Ratings, Feb. 16, 2011
- Interactive Ratings Methodology, April 22, 2009
- Holding Company Analysis, June 11, 2009
- Group Methodology, April 22, 2009
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008
- Criteria Update: Factoring Country Risk Into Insurer Financial Strength Ratings, Feb. 11, 2003
- Nonsovereign Ratings That Exceed EMU Sovereign Ratings: Methodology And Assumptions, June 14, 2011
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Ratings Detail (As Of August 10, 2012)	
Holding Company: Mapfre S.A.	
Issuer Credit Rating	
Local Currency	BBB/Negative/--
Subordinated	BB+
Operating Companies Covered By This Report	
Mapfre Global Risks, Compania Internacional de Seguros y Reaseguros S.A.	
Financial Strength Rating	
Local Currency	A-/Negative/--
Counterparty Credit Rating	
Local Currency	A-/Negative/--
Mapfre Re, Compania de Reaseguros, S.A.	
Financial Strength Rating	
Local Currency	A-/Negative/--
Issuer Credit Rating	
Local Currency	A-/Negative/--
Related Entities	
Citation Insurance Co. (MA)	
Financial Strength Rating	
Local Currency	A-/Negative/--
Issuer Credit Rating	
Local Currency	A-/Negative/--

Ratings Detail (As Of August 10, 2012) (cont.)	
Commerce Insurance Co.	
Financial Strength Rating	
Local Currency	A-/Negative/--
Issuer Credit Rating	
Local Currency	A-/Negative/--
Mapfre U.S.A. Corp.	
Issuer Credit Rating	
Local Currency	BBB-/Negative/--
Senior Unsecured	BBB-
Domicile	Spain

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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