

Western & Southern Financial Group Inc.

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Western & Southern Financial Group Inc.

Anchor	aa-	+	Modifiers	0	=	SACP	aa-	
▲			▲			+		
Business Risk	Strong					Support	0	AA-/Stable/--
Competitive position	Strong		Governance	Neutral				Financial strength rating
IICRA	Low							
Financial Risk	Excellent		Liquidity	Exceptional		Group support	0	A/Stable/--
Capital and earnings	Excellent							Holding company ICR
Risk exposure	Moderately low		Comparable ratings analysis	0		Government support	0	
Funding structure	Neutral							

IICRA--Insurance Industry And Country Risk Assessment.
SACP--Stand-alone credit profile.

Credit Highlights

Overview	
Key strengths	Key risks
Excellent capital adequacy	Interest rate risk exposure
Stable operating performance	Higher-risk investment portfolio than similarly rated public peers
Sophisticated and robust enterprise risk management	

Western & Southern Financial Group Inc.'s capital redundancy declined year over year but will remain a key strength over the next two years. The group's capital redundancy at the 'AAA' level, per our risk-based capital (RBC) model, shrunk from its historically significant size (approximately 20%) to a more modest 4% as of year-end 2022. The decline arose primarily from an increase in required capital that stemmed from growth in the structured investment portfolio and opportunistic sales of fixed annuities amid the favorable interest rates in 2022. We expect the group's capital will remain redundant at the 'AAA' level through the next two years.

Like many mutual insurers, Western & Southern deliberately maintains a larger unhedged exposure to interest rate risk than similarly rated public life insurance peers. In general, Western & Southern allows wider asset-liability mismatches across the enterprise and hedges less of its interest rate risk exposure than its similarly rated public life insurance peers. Some of this is driven by its lower-risk product profile compared with those same peers. Despite this somewhat large unhedged exposure, we have faith in the company's ability to measure and manage this risk exposure within clearly defined limits and tolerances, given its extensive, granular, frequent risk reporting and the clearly evident ties between its actuarial, investment, and risk management teams.

Diverse product offerings, distribution channels, and brands enable Western & Southern to reach a wide market and maintain stable operating performance amid market turmoil. The multichannel distribution system of career agents, independent agents, and direct-to-consumer marketers offers a variety of insurance products (e.g., whole life, universal life, term life, deferred annuities, and payout annuities) and noninsurance products (e.g., mutual funds, individual retirement accounts, and 529 college savings plans) to Western & Southern's customers. This enables the group to reach consumers with incomes ranging from lower middle class to high net worth across its different channels and brands. Many of the group's policyholders buy insurance for protection as opposed to cash accumulation, which leads to inelastic demand and steady profits even during market turmoil.

Outlook: Stable

The stable outlook reflects S&P Global Ratings' expectation that the group will maintain its strong competitive position as well as its excellent capital and exceptional liquidity.

Downside scenario

We could lower the ratings over the next 12-24 months if Western & Southern's:

- Risk exposure worsens due to the introduction of products we view as higher risk or because of rising investment exposure to high-risk assets;
- Operating performance unexpectedly declines or volatility materially increases; or
- Capitalization declines and is expected to remain below the 'AAA' level per our RBC model.

We could also downgrade the nonoperating holding company if ordinary dividend capacity from the regulated subsidiaries declines significantly or if we believe the holding company will consistently hold less than about 3x its annual holding company debt service in cash and high-quality fixed income on its balance sheet.

Upside scenario

Although it is unlikely within the next two years, we could raise our ratings over the long term if the group:

- Successfully executes a transformative strategy so that we consider it to have broad business diversity, significantly improved market positions, or brand differentiation in line with higher-rated peers, while maintaining its consistent earnings and excellent financial risk profile; or
- Achieves returns (on both assets and capital) that we expect will be maintained at levels in line with those of peers rated 'AA'.

Key Assumptions

- U.S. GDP growth of 0.7% for 2023 and 1.2% for 2024
- Core U.S. Consumer Price Index inflation of 4.7% in 2023 and 3.0% in 2024
- Average 10-year Treasury yield of about 3.9% for 2023 and 3.9% for 2024
- Average unemployment rate of 4.1% in 2023 and 5.0% in 2024

Source: "Economic Outlook U.S. Q2 2023: Still Resilient, Downside Risks Rise," published March 27, 2023

Western & Southern key metrics

(Mil. \$)	--Year ended Dec. 31--				
	2024f	2023f	2022	2021	2020
S&P Global Ratings capital adequacy/redundancy	AAA	AAA	AAA	AAA	AAA
Net income	350-400	300-350	309	361	204
EBIT adjusted	450-500	400-450	407	487	228
Return on assets (%)	0.7-0.9	0.6-0.8	0.7	0.9	0.4
Return on capital and surplus (%)	4.5-5.5	4.0-5.0	4.3	5.5	3.5
EBITDA fixed-charge coverage (x) (GAAP)	> 4.0	>4.0	8.0	9.9	8.4
Financial leverage (%) (GAAP)	<20	<20	16.1	10.2	9.3

All data based on statutory accounting except where otherwise noted. f--Forecast; data reflects S&P Global Ratings' base-case assumptions.

Business Risk Profile: Strong

Diverse products, distribution channels, and brands all benefit Western & Southern's competitive position. Increasing sales of life insurance and asset management products are longer-term goals for the management team, but the group took full advantage of the favorable interest rates in 2022 to opportunistically sell a record amount of interest-sensitive annuities. As of year-end 2022, about 20% of insurance premiums came from life and accident & health products, whereas 80% came from annuity products. The proportion of Western & Southern's operating earnings derived from noninsurance sources (about 15% from asset management) bolsters its competitive strength.

Western & Southern sells products under multiple distinct brands. Its insurance brands include Columbus Life, Lafayette Life, Western & Southern Life, Integrity Life, National Integrity Life, and Gerber Life, and its asset management brands include Touchstone Investments and Fort Washington Investment Advisors. While the intentional "house of brands" approach allows the group to reach a variety of customers, it does not lead to a discernible competitive advantage that some competitors enjoy due to more cohesive brand recognition.

The group's diverse portfolio of low-risk products has led to stable operating performance and returns that are in line with similarly rated peers'. We favorably view the risk-sharing features in its participating whole life products (about 14% of general account liabilities) and expect the group could further stabilize its profits amid market turmoil by simply adjusting the dividend rate it pays to policyholders.

Financial Risk Profile: Excellent

Our view of Western & Southern's financial risk reflects the group's consistent investment yields and prudent management of higher-risk assets compared with publicly rated peers. We expect Western & Southern's organic capital growth will allow it to maintain capitalization above our 'AAA' threshold through the next two years.

Western & Southern's moderately low risk exposure is supported by the diversity of its investment portfolio. Overall, approximately 13% of the group's credit portfolio is below investment-grade, whereas only 1% of its structured

portfolio is below investment-grade. The group's overall portfolio remains high quality, with a weighted average credit rating of 'A-'.

Despite its mutual status, the group has shown that it can and will issue surplus notes if needed. It also has the ability to access other forms of short-term capital relief, including agreements with the Federal Home Loan Banks and reinsurers and a \$500 million credit facility. As of year-end 2022, financial leverage was 16% and EBITDA fixed-charge coverage was 8x. Financial leverage mostly consists of surplus notes (\$1 billion outstanding). We give these surplus notes intermediate equity credit until 10 years before the maturity date, since the notes were issued by Western & Southern Life Insurance Co., a legal entity prudentially regulated by the State of Ohio Department of Insurance. The first of these notes matures in 2049. We expect financial leverage will remain below 20% and fixed-charge coverage well above 4x over the next 12-24 months.

Other Key Credit Considerations

Governance

The management team is seasoned and has demonstrated its expertise in operating all of Western & Southern's major lines of business, as evidenced by the group's consistent growth and profitability. Its strategy includes boosting life insurance sales (via the direct-to-consumer, independent, and bank channels) and diversifying annuity products. We regard this strategy as realistic because it takes into account current market conditions, as well as the group's organizational capabilities.

The team continues to implement conservative operating practices, and the sufficiently independent board is clearly risk-aware and in close contact with the enterprise risk management team. We believe Western & Southern has a well-embedded risk management culture, in which employees from all levels of the organization interact with the independent risk management team for assistance in risk-aware decision-making. Risks are measured using a variety of granular metrics and models, and reporting is frequent.

Liquidity

In our view, the group's liquidity is exceptional, as reflected in its 270% liquidity ratio as of year-end 2022, per our calculations. The group has no exposure to confidence-sensitive liabilities, collateral posting risk, or problematic covenants or ratings triggers.

Factors specific to the holding company

Our issuer credit rating on Western & Southern Financial Group Inc., the nonoperating holding company, is two notches lower than our ratings on the group's operating companies, reflecting the group's high fixed-charge coverage and the holding company's unconsolidated liquidity position, as well as the strength of the operating companies' aggregate ordinary dividend capacity.

Annual dividend capacity for 2023 is about \$735 million from core operating subsidiaries. As of year-end 2022, the holding company held about \$396 million of assets to service long-term senior debt of \$500 million. We view more than \$200 million of the holding company's assets as those that are or can be easily converted to cash, which is more than sufficient to service its interest payments. Although the holding company has access to dividends from different

subsidiaries, we consider its regulatory diversification limited because all but two of its operating entities are domiciled in Ohio.

Environmental, social, and governance

ESG Credit Indicators

E-1	E-2	E-3	E-4	E-5	S-1	S-2	S-3	S-4	S-5	G-1	G-2	G-3	G-4	G-5
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ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumeric 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

Environmental, social, and governance factors have no material influence on our credit rating analysis of Western & Southern.

Accounting considerations

Western & Southern timely prepares its financial statements under generally accepted accounting principles (GAAP) and statutory accounting principles. In our analysis, we consider GAAP and statutory statements when examining capital, earnings, and other financial metrics compared with those of peers.

We exclude securities lending obligations from our financial leverage calculations because we view these as operational leverage. Nonrecourse trust and partnership obligations are also excluded from the financial leverage ratio.

In deriving our year-end 2022 capital model outcome, we applied an analytical look-through adjustment to Fort Washington private equity funds to charge them as unaffiliated equity. We also added approximately \$800 million in redundant reserves held at Western & Southern's operating companies to total available capital.

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Insurance | General: Methodology For Assessing Capital Charges For U.S. RMBS And CMBS Securities Held By Insurance Companies, Aug. 29, 2014
- Criteria | Insurance | General: Methodology For Assessing Capital Charges For Commercial Mortgage Loans Held By U.S. Insurance Companies, May 31, 2012
- Criteria | Insurance | General: Methodology For Calculating The Convexity Risk In U.S. Insurance Risk-Based Capital Model, April 27, 2011
- 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

Western & Southern Financial Group credit metrics history

Ratio/metric	2022	2021
S&P Global Ratings capital adequacy	AAA	AAA
Gross premiums written	10,565	6,096
Return on revenue	3.2	6.0
Return on assets (excluding realized gains/losses)	0.7	0.9
Capital and surplus	7,345	7,160
Return on capital and surplus (%)	4.3	5.5
Total invested assets	57,595	51,971
EBIT	407	487
Net income (attributable to all shareholders)	309	361
Net investment yield (%)	4.2	4.5
Financial leverage including pension deficit as debt (%) (GAAP)	16.1	10.2
Financial leverage including pension deficit as debt (ex. AOCI) (%) (GAAP)	13.0	11.3
EBITDA fixed-charge coverage (x) (GAAP)	8.0	9.9

All based on statutory accounting except where otherwise noted.

Business And Financial Risk Matrix

Business risk profile	Financial risk profile							
	Excellent	Very Strong	Strong	Satisfactory	Fair	Marginal	Weak	Vulnerable
Excellent	aa+	aa	aa-	a+	a-	bbb	bb+	b+
Very Strong	aa	aa/aa-	aa-/a+	a+/a	a-/bbb+	bbb/bbb-	bb+/bb	b+
Strong	aa-/a+	a+/a	a/a-	a-/bbb+	bbb+/bbb	bbb-/bb+	bb/bb-	b+/b
Satisfactory	a	a/a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bb+/bb	bb-/b+	b/b-
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb/bb-	b+/b	b-
Weak	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b/b-	b-
Vulnerable	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b+/b	b/b-	b-	b-

Note: Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

Ratings Detail (As Of June 13, 2023)*

Western & Southern Financial Group Inc.

Issuer Credit Rating

Local Currency

A/Stable/--

Senior Unsecured

A

Ratings Detail (As Of June 13, 2023)*(cont.)

Related Entities**Columbus Life Insurance Co.**

Financial Strength Rating

Local Currency AA-/Stable/--

Issuer Credit Rating

Local Currency AA-/Stable/--**Integrity Life Insurance Co.**

Financial Strength Rating

Local Currency AA-/Stable/--

Issuer Credit Rating

Local Currency AA-/Stable/NR**Lafayette Life Insurance Co.**

Financial Strength Rating

Local Currency AA-/Stable/--**National Integrity Life Insurance Co.**

Financial Strength Rating

Local Currency AA-/Stable/--

Issuer Credit Rating

Local Currency AA-/Stable/NR**Western and Southern Life Insurance Co.**

Financial Strength Rating

Local Currency AA-/Stable/--

Issuer Credit Rating

Local Currency AA-/Stable/--

Subordinated

A

Western-Southern Life Assurance Co.

Financial Strength Rating

Local Currency AA-/Stable/--

Issuer Credit Rating

Local Currency AA-/Stable/--**Domicile**

Ohio

*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.

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