Barita
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Fixed Income Analysis

# SAGICOR FINANCIAL COMPANY LIMITED

Barita Investments Limited
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## Company Overview

Sagicor Financial Company Limited ("Sagicor" or "SFC") is a multinational provider of various financial services. Their operation is dominated by insurance services (life, health, property, and casualty insurance), but also commercial banking, investment banking, pension management, and real estate investment services. Sagicor has three reporting operating segments. The first segment is Sagicor Life, which provides services such as insurance and asset management to countries including Barbados, Trinidad and Tobago, the Bahamas, and other countries in the Eastern and Dutch Caribbean, as well as across Central America. The second segment is Sagicor Jamaica, which provides insurance, commercial and investment banking, and other services to Jamaica, The Cayman Islands, and Costa Rica. The last final operating segment is Sagicor USA, which provides life insurance and annuity products to middle-market America in 45 states in the US and the District of Columbia.

| | |
|---|---|
| Industry: | Diversified Financials |
| Bond Name | SFCCN 5.30% 2028 |
| Credit Rating (Fitch) | BB- |
| Credit Rating (S&P) | BB+ |
| Maturity | May 13, 2028 |
| Issue Size | US$550 Mn |
| Rank | Senior Unsecured |
| Price (Source: Bloomberg) | 95.37 |
| Yield to Worst | 6.442% |
| Recommendation | **Overweight** |

| Financial Summary (US$ in Thousands) | | | |
|---|---|---|---|
| **Metrics** | **FY2020** | **FY2021** | **FY2022** |
| Revenue, net | 1,878,367 | 2,359,094 | 2,540,252 |
| EBITDA | 112,046 | 342,488 | 333,480 |
| EBIT | 72,487 | 309,787 | 302,530 |
| Total Assets | 9,266,313 | 10,377,932 | 10,621,376 |
| Total Equity | 1,658,210 | 1,666,213 | 1,449,924 |
| Financial Ratios | | | |
| EBIT margin | 3.9% | 13.1% | 11.9% |
| Debt/ EBIT | 6.5X | 2.2X | 2.1X |
| EBIT/Interest | 1.6X | 6.9X | 7.6X |

## Investment Rationale

While the credit has seen some spread compression we believe that there might be more to come. This comes as it trades slightly cheap relative to peers with the major concern as it relates to macroeconomic exposure to Caribbean government debt is likely to be improved with the Ivari transaction. In this regard, the successful closure of the acquisition means that there is potential for more spread compression. In addition to this, approaching closer to the end of the Fed hiking cycle might also limit the potential downside tailwinds on price from even more restrictive monetary policy. In this regard we opt to maintain our **OVERWEIGHT** rating on the credit and believe investors can continue to find comfort in SFC's growing operations in an investment-grade country, having a strong brand and presence in a growing industry, strong capital adequacy ratios that stood the test of the downturn in FY2020 caused by the pandemic, as well as their credit rating and access to the capital markets.

## Credit Rating Assessment

Fitch maintained SFCL's credit rating at BB with a positive rating watch in November 2022. Based on Fitch's credit rating scale, BB is the rank just below the minimum rank needed to be considered investment grade, with that minimum rank being BBB. Therefore, according to Fitch, SFCL has a speculative grade rating. Fitch initially placed SFCL on a positive rating watch in August 2022 following the announcement of its intended acquisition of Ivari, a leading middle-market insurer in Canada, and reflects prospective improvement in the credit quality of SFCL's insurance operating company group. In this regard, Fitch highlighted several key rating drivers for their latest assessment which includes:

- Ivari Acquisition Completion: Fitch expects to resolve the "Rating Watch Positive" (RWP) following SFCL's acquisition of Ivari with either an affirm or upgrade if the acquisition proceeds under their assumptions.
- Improved Company Profile: The RWP is supported by an improved company profile at the group operating company level as a result of the acquisition.

- Strong Capitalization with Some Pressures and strong recent financial performance for 2021 and the First 9-months of 2022: Fitch views the capitalization of SFCL's insurance operations to be strong and supportive of the ratings.
- Higher Financial Leverage Ratios: SFCL's financial leverage has historically been high and is expected to increase modestly due to the Ivari acquisition. Fitch has stated they will balance the credit positives (improved operating company credit quality) with the credit negatives, (higher financial leverage) while accounting for regulatory restrictions on the acquired cash flows.
- Investment Risk Above Average with Manageable Exposure: SFCL's investment portfolio has considerably above average investment risk relative to the industry. SFCL's investment portfolio has substantial concentrations in Jamaica and Barbados sovereigns.

In addition to the above, Fitch included several rating sensitives/scenarios that may lead to an upgrade/downgrade or a return to a stable instead of a positive outlook watch of SCFC's credit rating. These rating sensitivity factors are illustrated in table 1.1 " Sensitivity factors" below:

**Table 1.1:** Fitch Rating Sensitivity Factors

| Upgrade | Stable | Downgrade |
|---|---|---|
| **1)** Significant improvement in SFC's consolidated industry profile, operating environment, and company profile achieved by the closing of the Ivari acquisition, and the view that it materially enhances the operating group's overall credit quality;<br><br>**2)** FLR ratios maintained at or below current levels and not higher than 35%; and Fixed charge coverage ratio of at least 3x.<br><br>**3)** Economic uncertainties do not result in a decline in Ivari's stand-alone credit quality implied at the current 'A-' Insurer Financial Strength (IFS) rating.<br><br>**4)** No material deterioration in economic and operating environments and sovereigns of Jamaica, Trinidad, and Barbados.<br><br>**5)** Below investment grade assets to capital ratio close to 130% and risky asset ratio below 250%, along with minimal exposure to sovereigns to capital especially Barbados, Jamaica, and Trinidad. | **1)** The transaction is not completed;<br><br>**2)** There is a decline in Ivari's IFS rating on a standalone basis to below 'A-', and/or available cash flows available to the holding company would appear to be lower than expected; | **1)** Significant deterioration in the economic and operating environments and sovereigns of Jamaica, Trinidad, and Barbados, which would lead to a material decline in operating performance and/or credit profile of SFCL's investment portfolio.<br><br>**2)** Deterioration in key financial metrics, including consolidated MCCSR falling below 180% and financial leverage exceeding 35%, and ROE below 5% on a sustained basis; |

## Industry Outlook

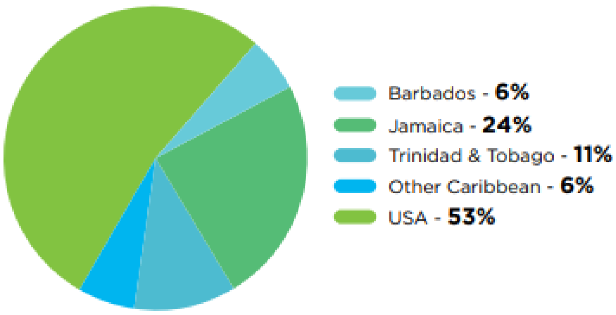
In the 2022 Global Insurance Market Report (GIMAR) report, the outlook for the profitability of the global insurance industry was noted. Specifically, the expectation of continuing geo-political tension, a worsening macroeconomic backdrop, as well as the ongoing tight global monetary policy, coupled with increased credit risk and cost associated with the implementation of IFRS17 is expected to weigh on future performance. Namely rising inflation and an overall slowdown in economic activity are expected to harm profitability. In the case of rising interest rates, this typically positively impacts the profitability of life insurers, for example as they reinvest at higher rates, however, there remains nuance based on specific asset liability management frameworks and the expected losses from fair value declines due to rate hikes.

In the life segment, insurance premiums saw a boost globally, in 2021 which in some jurisdictions was attributed to reopening and an improvement in economic conditions. In 2023, while the expectation is for a slowdown in growth, which is a net negative for insurance demand and spending, this is somewhat alleviated by the expectation for lower inflation which will therefore ease the burden on consumer balance sheets and claims inflation. Thus far, it is unclear which factor will dominate the near-term trajectory of the industry. Notwithstanding, it is notable that indicators such as the MIB Group's (a membership corporation of insurance companies in the United States and Canada) life index which measures life insurance application activity on a year-to-date basis, activity is up 5.9% in 2023 compared to the same period 2022. Hence, despite the expectation of slowing growth, insurance activity currently still appears fairly robust.

## Financial Performance (2022 Financial Year)

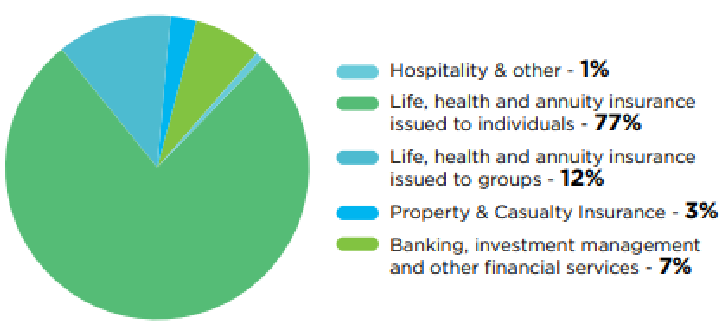
Total revenues grew by 7.7% to US$ 2.5 billion for the 2022 financial year, compared to 2021.  Note the largest contributor to this growth was Net premium income which contributed 14.2% followed by Interest Income net of credit impairment which contributed 3.6%. These revenue streams largely outweighed the negative contribution of other investment income which primarily reflects fair value losses on investment securities of 8.8%. Historically, revenue has grown at a compounded annual growth rate (CAGR) of 16.3% from the US$1.4 billion in revenues generated in 2018 with Net premium growth being the largest historical driver of revenue growth.

**REVENUE BY GEOGRAPHICAL SEGMENTS**
For the year ended December 31, 2022




DECEMBER 2022 REVENUE: **US $2,540.3M**

**REVENUE BY LINE OF BUSINESS**
For the year ended December 31, 2022

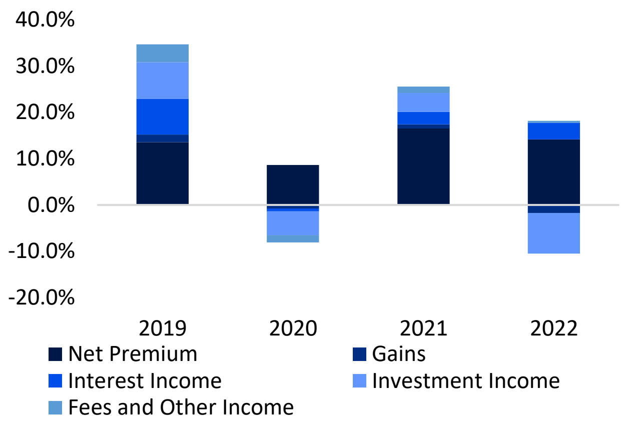



DECEMBER 2022 REVENUE: **US $2,540.3M**

**Core Insurance the Driver**

Net premium income amounted to US$2.05 billion, representing an increase of 19.6% year-over-year (YoY) or US$334.9 million for 2022. The strong performance was mainly reflected in the robust net premium growth in the group's USA operations which saw an over US$258.5 million increase in net premiums written. **This strong net premium growth overall occurred within the context of strong gross premium growth of 18.8% (higher than the US industry-wide growth of 9.8%) while the group maintained a relatively constant reinsurance rate YoY.** As such, historically, the strong rate of growth in Net premiums has been due to this strong gross premium revenue growth and a fairly stable reinsurance rate, particularly as their US operations grew.

**Fig 1.1**: Revenue Contribution




## Higher Rates, stronger Interest Income

The second largest contributor to overall revenue growth was the Group's interest income net of impairment, which contributed 3.6 percentage points of overall revenue growth, amounting to US$432.7 million, compared to US$337.4 million in 2021, representing an increase of 24.8%. The driver of this improved interest income was the increase in the Group's investment portfolio due to strong sales performance as well as the impact of the rising rate environment. For reference, the Group's holding of financial investments increased by approximately 5.6% YoY at the end of 2022 (totalling US$9.0 billion including pledged assets), increasing the base of interest-earning assets. In addition to this the bulk of this is comprised of debt securities which in 2022 had an average yield of 5.8% up from an average of 4.8% in 2021. Notably, while this segment isn't the largest driver of revenue growth, it is the second most consistent next to premium income, and the 2022 outturn reflected the best performance for this segment throughout the last five years.

## Investment Income: Outweighed but Laggard non-the-less

Higher net premium income and interest income largely outweighed the negative contribution of 8.8% from net investment income, which amounted to a loss of US$114.7 million, compared to a gain of US$92.4 million in 2021. This loss came against the backdrop of the contractionary shift in global monetary policy in the face of rising inflation, which acted as a headwind to financial markets. This is evidenced by the Fed raising the federal funds rate from a target range of 0.00%-0.25% to 5.25-5.50% as of July 2023, which has facilitated a decline in asset prices. Notably, only around 29.6% of the group's investment assets carried through profit and loss are debt instruments. *Therefore, apart from the general decline in bond prices equity prices have a large impact on profitability, which is represented by the over US$31.2 million loss on the equity investment in Playas Hotel and Resorts compared to a gain of US$21.6 million in 2021, further explaining the weakened investment performance for 2022.*

*(for completeness fees and other income contributed 0.4% to the overall growth of 7.7% seen in 2022. Historically fees have been a fairly small portion of the group's overall revenue and has been growing even smaller. Fees now comprise 6.9% of total revenues compared to 9.0% in 2019)*

### Lowest Loss Ratio in 4 years: Strong underwriting profits

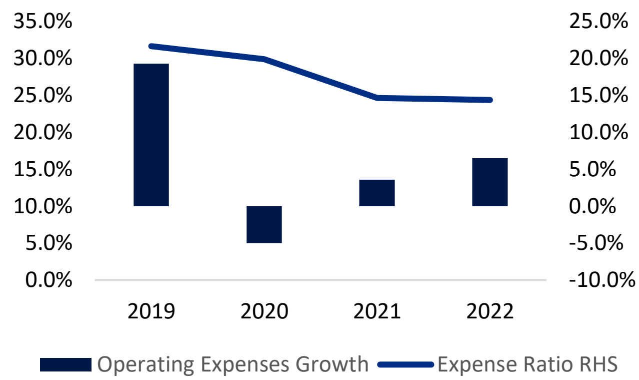
Total benefits expense grew by 8.8% in 2022 to US$1.7 billion. This was notably lower than the gross premium growth of 18.8%. Hence the group registered an improved loss ratio (combined net benefits expenses as a portion of gross premiums) to 77.2% compared to 84.3% in 2021. A portion of this increase in benefits payout was related to increased policy benefits due to higher mortality rates in the Sagicor life operating segment. The group also benefited from fairly large changes in actuarial reserves which amounted to US$312.3 million compared to US$3.7 million in 2021. As such, this effectively reduced total benefits and facilitated the aforementioned improved loss ratio. Importantly, releases in actuarial reserves might be due to operating efficiencies and/or higher interest rates, which effectively lowers the net present value of reserves required to meet benefit claims of future policyholders and hence might explain the positive reserve release.

Historically, over the last five years, benefits have grown at a CAGR of 21.5%. This is higher than the CAGR of gross premiums suggesting that the loss ratio has generally trended higher despite the 2022 outlier results. This can be seen by the loss ratio of 67.0% in 2018 which then climbed as high as 84.3% in 2021 before the fall to 77.2% in 2022.

### Continued Improvement in Operating Efficiency

Total operating expenses for 2022 came in at US$618.6 million representing a growth of 6.5%. This growth was lower than the growth in revenues and therefore, the Group saw an improvement in its operating expense ratio which declined to 24.4% from 224.6% in 2021. The Group's operating expense over the 2018-2022 period has noticeably grown at a slow pace relative to revenue with a CAGR of 5.7% over the period. Against this backdrop, the Group has seen its expense ratio fall from over 35.7% in 2018. The Group's largest operating expense is its administrative expense which includes wages and salaries and constitutes approximately 63.5% of total operating expenses. In addition to this, it is also the fastest-growing expense line item, growing at a CAGR of 6.7% over the last five years from US$303.1 million to US$392.9 million.

Fig 1.2: Operating expense ratio and growth




The impact of the global financial market downturn on investment income outweighed the majority of the benefits of the Group's surge in premium income in 2022 (with an improved loss ratio) and the improved operating expense ratio, leading to a marginal decline in profit before tax of 0.7% to US$262.9 million. Ultimately, profit after tax from continued operations declined by 13.7% in 2022.

### Outsized Other Comprehensive Income Loss..relatively

The Group generated other comprehensive losses of US$153.0 million. These losses primarily reflected losses on fair value securities carried through other comprehensive income of US$490.8 million. Based on the Group's classification of investment securities at the end of 2022, the majority of this represented debt securities and as such reflected the direct impact of the rising interest rate environment. Notably, the outturn compares to a much smaller loss of US$40.5 million in 2021. These marked-to-market losses in other comprehensive income outweighed positive changes in net actuarial liabilities to the tune of US$312.3 million leading to the ultimate loss seen in other comprehensive income. Historically, as expected, other comprehensive income has been relatively volatile for the Group, however, the loss made in 2022 was the largest loss made over the last five years given the unprecedented monetary policy tightening. Other comprehensive income has been as high as a gain of US$43.7 million in 2019 just before the pandemic.

## Recent Developments (Q1 2022)

**Lower Insurance Revenue..but higher investment income**

The Group generated insurance revenues of US$166.2 million for the first quarter ended March 31, 2023 (Q1 2023), compared to US$148.8 million for the comparable period in 2022. This represents an increase of approximately 11.7%, or US$17.4 million, of which US$9.9 million was attributed to the Group's operations in Jamaica, while US$5.6 million was attributed to the United States. This growth in revenues outpaced the growth in total insurance service expenses, which rose to US$136.7 million from US$131.7 million for an increase of 3.8%. This comes as the claims expenses were relatively subdued, rising by approximately 1% for the quarter, which management attributed to lower claims in the USA business segment. However, net expenses from reinsurance contracts increased by over 400% to US$27.2 million, compared to US$5.0 million in Q1 2022 leading to an overall 80.9% decline in net insurance service results.

This decline in insurance segment performance was however outweighed by an over US$341.2 million improvement in net investment income (from a loss of US121.5 million in 2022 to a gain of US$219.6 million in 2022). The large bulk of this improvement was a result of other investment income which includes the marked-to-market gains of investments carried through profit and loss which amounted to a gain of approximately US$171.2 million. This income line item likely benefited from the some marked-to-market gains in the group's holding of Playa Resorts which saw some recovery in its stock price. Playa's stock appreciated from US$6.53 at year-end 2022 to US$ 9.60 by the end of March 2023 for a gain of approximately 47.0%.

**Higher Net Insurance Finance cost..but still higher profits**

Finance costs from insurance contracts amounted to US$145.8 million compared to a gain of US$84.3 million in finance income from 2022. These finance costs were associated with the measurement of insurance contracts at present value and represent changes in these net present values due to changes in discount rates and the general passage of time. Most of these increased finance costs were associated with the Sagicor USA segment, however, higher interest rates drove finance costs of US$96.6 million compared to a financial gain of US$68.3 million for the comparable period in 2022.

Despite the higher net insurance finance cost and the reduction in net insurance result, the impact of much improved net investment income bolstered by other investment income drove a net insurance and investment result at a gain of US$88.2 million. This compares to a loss of US$36.3 million in 2022. In keeping with the trend of maintaining operating efficiency total operating expenses only increased marginally YoY, rising by 3.5%, facilitating a profitable first quarter with profit before tax of US$17.0 million, compared to a loss of US$ 90.8 million last year. In addition to this, the Group made net profits of US$9.2 million compared to US$82.3 million in losses last year.

The Group also generated other comprehensive income of US$9.9 million compared to a loss of US$26.2 million in 2022. This primarily represented the Group's holding of debt securities carried through OCI.

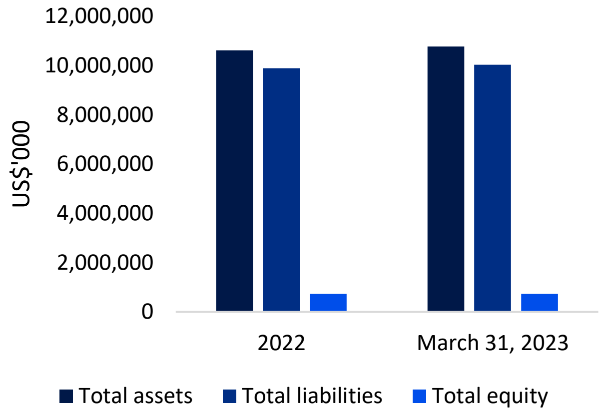
## Balance Sheet and Solvency

*Note that with the advent of IFR 17, the latest balance sheet information provided is not directly comparable to the 2018-2021 balance sheet. Hence in this segment, we focus on the change in asset composition between December 2022 (restated balance sheet) and March 2023 while taking a historical look at the 2018-2021 balance sheet separately.*

### Assets and Liabilities

As of March 2023, the Group had total assets of US$10.8 billion, growing 1.4% since December 2022. Over the 2018-2021 period total assets increased at a CAGR of 12.3%. In terms of the composition of the group's asset base, 77.8% of assets were in the form of financial investments, while the total of financial investment and pledged investment assets was approximately 83.7% of total assets. For these financial assets, a large portion represented debt securities, (72.9%) of which approximately (78%) are of the BBB credit rating and below (the group generally has a large exposure to Trinidad, Jamaica, and Barbados government bonds) and the majority are carried at fair value through profit and loss (64.1%)). The second largest asset line item was reinsurance contract assets at 4.4% of total assets and then the combination of cash and restricted cash at 4.4%. Historically investment securities have been the largest component of the group's balance sheet, though its share has increased marginally over the years from 65.5% to 76.0% in 2021.

**Fig 1.3**: Balance Sheet Extract




The Group's total assets were 6.9% funded by equity and 93.1% by liabilities. Looking firstly at liabilities, which amounted to US$ 10.0 billion as of March 2023, representing an increase of 1.5% year-to-date (YTD). In terms of its composition, insurance reserves/ insurance contract liabilities unsurprisingly comprise 63.2% of total liabilities, followed by deposits and other security liabilities at 21.7% and then notes and loans payable at 6.5%. Historically, between 2018-2021, total liabilities increased at a CAGR of 12.1%, rising from US$6.2 billion to US$8.7 billion. This came on the back of growth in total policy liabilities, which increased at a CAGR of 15.2%, from US$3.7 billion to US$5.6 billion. This was driven by the expansion of the business as the Group continues to issue policies. Notes and loans payable grew at a CAGR of 11.7% over the review period, from US$490.3 million to US$683.4 million. Of this US$ 683.4 million, US$532.2 million was derived from the 5.30% 2028 senior notes.

### Equity and Solvency

Total equity as of March 2023 stood at US$738.1 million, representing marginal growth of 0.2% YTD. Total equity attributable to shareholders amounted to US$428.3 million down slightly from US$429.7 million at the end of December 2022. This decline occurred despite the return to profitability for the quarter, with total comprehensive income to shareholders of US$6.6 million, the Group opted to pay dividends of approximately US$8.0 million, hence the marginal increase in shareholder's equity. As of March 2023, debt to equity stood at 53.0% (Debt to equity in this case includes notes payable, and lease liabilities in debt while also including the contractual service margin which is a part of insurance liabilities in equity). This compares to the ratio of 51.0% in 2022.

## Important Update

### Ivari Transaction

In 2022 Sagicor agreed to purchase Ivari, a leading middle-market individual life insurer in Canada with an expected purchase price of C$325 million. This purchase price included a capital injection to meet IFRS17 and LICAT 2023 standards (final Life Insurance Capital Adequacy test for Canada). The acquisition serves the strategic purpose of expanding SFC's protection and wealth management services to Canada with the expectation that post-acquisition Ivari and its Canadian operations will constitute over 50% of Assets and the 3rd largest revenue-generating geographic segment behind the US and Jamaica. Ivari's investment portfolio is almost entirely concentrated in investment-grade assets, namely US Treasury and Canadian government securities, invariably increasing the credit quality of SFC's overall portfolio.

The transaction is expected in the short term to be accretive to earnings. In 2022 Ivari generated approximately C$10.5 million in profits, down from the C$73.8 million made the year prior, primarily due to marked-to-market losses on investment holdings. The acquisition is also expected to be accretive to book value per share as it is expected that the transaction should close at a discount to Net book value. In their proforma guidance for 2023, SFC noted that combined with Ivari shareholder's equity would be approximately $725 million, up from $650 million due to this bargain purchase. While the original transaction was agreed upon in 2022, it is expected that the transaction will eventually close in 2023. The latest guidance from Sagicor's management from their first quarter 2023 earnings release is that they expect the Ivari transaction to close successfully by Q3 2023.

## Credit Metrics and Relative Valuation

### Sagicor Credit Metrics

**In this segment, we focus on the relevant credit metrics for Sagicor while simultaneously comparing this to the metrics of close competitors. These competitors include Unum Group, SBL Holdings, American Equity, FG annuities and CNO financials. While the peer group is comprised entirely of life insurers, we note that SAGICOR's competitors all currently have a higher credit rating. Sagicors's S&P rating is currently BB while the majority of its peers are currently rated BBB.**

| | 2018 | 2019 | 2020 | 2021 | 2022 | Mar-23 |
|---|---|---|---|---|---|---|
| EBIT | 183,034 | 206,917 | 72,487 | 309,787 | 302,530 | 47,082 |
| Finance | 36,511 | 43,633 | 44,885 | 45,054 | 39,626 | 30,071 |
| | | | | | | |
| Total Debt | 490,275 | 517,732 | 471,622 | 683,388 | 632,535 | 648,196 |
| Net Debt | 393,487 | 429,336 | 391,984 | 605,253 | 264,398 | 263,562 |
| | | | | | | |
| EBIT/Interest | 5.01 | 4.74 | 1.61 | 6.88 | 7.63 | 1.57 |
| Debt/Total Assets | 6.7% | 5.9% | 5.1% | 6.6% | 6.0% | 6.0% |
| Debt/Equity | 43.2% | 29.6% | 28.4% | 41.0% | 43.6% | 45.4% |
| Debt to Capital | 30.2% | 22.8% | 22.1% | 29.1% | 30.4% | 31.2% |

On average, the Group generated approximately $215.0 million in earnings before interest and taxes (EBIT) between the 2018-2022 period. During this same period, finance costs averaged $41.9 million, with the interest coverage ratio remaining above 1.5x over the entire period. As of December 31, 2022, the interest coverage ratio stood at 7.6x, representing a recovery from the pandemic lows of 1.6x. Notably, the Group's leverage ratio as of March 31, 2023, stood at 31.2% (note, we measured this as total debt divided by the sum of debt, shareholders equity and the contractual service margin) **and has been rising from 22.8% in 2019 (Recall a level below 35% was one of Fitch's criteria for a possible upgrade).** Likewise, the debt to equity ratio had increased to 43.6% in 2022 compared to 41.0% in 2021. The worsening of these ratios was also partially due to other comprehensive losses that the Group had been making in the prior year due to the higher rate environment which has deteriorated equity (through accumulated losses due to lower asset prices).

Hence, as we approach the peak of the hiking cycle, we expect that the volatility seen in equity due to volatile bond prices will begin to subside. This will therefore allow the Group to rebuild their equity reserves. However, it is expected that in the short-term, the leverage ratio will increase particularly as the closure of the Ivari transaction will result in the group taking on additional debt. **In their Q3 2022 report, management noted that it is expected that they would take on approximately $320 million in new debt to fund the transaction and expects total equity in 2024 after a full year of ownership with rise to approximately $2.0 billion (inclusive of CSM). This translates to a debt-to-capital ratio of approximately 32.6% assuming no further debt is taken on, which places the ratio below 35%.**

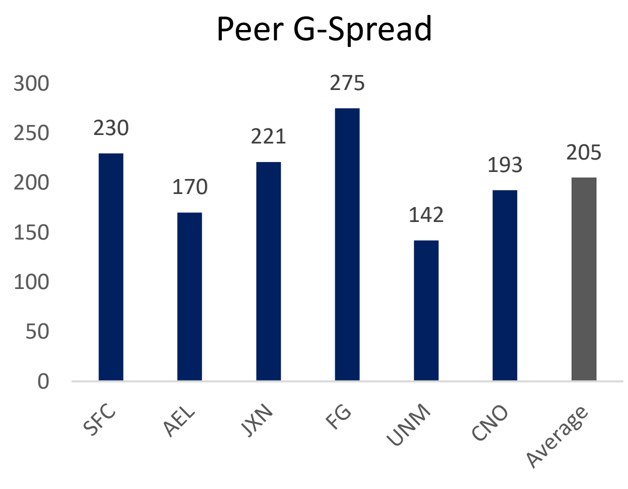
## Relative Valuation and Spread Analysis

### Sagicor Financial Company Peer Comparison

| | SFC | Unum | American Equity | FG | CNO | Jackson |
|---|---|---|---|---|---|---|
| EBIT | 302,530 | 1,819,900 | 1,584,000 | 627,000 | 654300 | 7,224,000 |
| Interest Expense | 39,626 | 188,500 | 37,000 | 29,000 | 137,000 | 113,000 |
| Interest coverage | 7.6 | 9.7 | 42.8 | 21.6 | 4.8 | 63.9 |
| Total Equity | 1,449,924 | 9,197,500 | 3,190,456 | 1,816,000 | 1,400,800 | 9,155,000 |
| Total Debt | 632,535 | 3,431,800 | 792,073 | 1,114,000 | 3,882,900 | 4,367,000 |
| Leverage | 30.4% | 27.2% | 19.9% | 38.0% | 73.5% | 32.3% |

When we compare SFC to their peers, we see that the Group had a lower interest coverage than all but one, CNO. The average interest coverage ratio of the comparables group was 25.1x. Despite this lower coverage, the Group did however have a generally lower leverage ratio than its peers with a ratio of 30.4% at the end of 2022 compared to the peer average of 36.9%. Currently, the SFC 2028 bonds trade at a G-spread that is currently wider than that of their peers at 230 basis points. This compares to the peer group average (peer companies with maturity dates between +/- 1 year of the 2028 SFC bond) of approximately 205 basis points. This spread is likely because SFC is of a lower credit rating, particularly due to exposure to lower credit-rated operating environments such as the Caribbean. However, the bond has seen notable spread compression since our last analysis. This is likely due to the improving fundamentals of the company as well as the pending transaction to acquire Ivari, which should improve credit portfolio quality and equity and hence the market is likely pricing a successful close.

In this regards the spread on the SFC 2028s has averaged approximately 276 basis points over the last 6 months and has come down from a high of over 400 basis points under a year ago (December 2022) pointing to the favorable performance of the bond since our last recommendation. In that regard, the latest price of approximately $95.10 compares to highs of over 106.0 dollars in October 2021 before the current hiking cycle. Hence when taken in line with the spread compression this price decline is likely more related to the general economic environment.




## Recommendation

While the credit has seen some spread compression, we believe that there might be more to come. This comes as it trades slightly cheap relative to peers with the major concern as it relates to macroeconomic exposure to Caribbean government debt likely to be offset with the Ivari transaction. In this regard, the successful closure of the acquisition means that there may be slightly more spread compression ahead. In addition to this, approaching closer to the tail-end of the Fed hiking cycle might also limit the potential downside tailwinds on price from an even more restrictive monetary policy. In this regard, we opt to maintain our **OVERWEIGHT** rating on the credit and believe investors can continue to find comfort in SFC's growing operations in an investment-grade country, having a strong brand and presence in a growing industry, strong capital adequacy ratios that stood the test of the downturn in FY2020 caused by the pandemic, as well as their credit rating and access to the capital markets.