FitchRatings

RATING ACTION COMMENTARY

Fitch Revises Legal & General's Outlook to Negative; Affirms IFS at 'AA-'

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Fitch Ratings - London - 29 Apr 2020: Fitch Ratings has revised the Rating Outlooks of Legal & General Group Plc's (L&G) and main operating entities to Negative from Stable. At the same time, we have affirmed the IFS Ratings of Legal and General Assurance Society Limited, Banner Life Insurance Company and William Penn Life Insurance Company of New York at 'AA-' and Legal & General Reinsurance Company Limited at 'A+.'

A full list of rating actions is detailed below.

KEY RATING DRIVERS

The rating actions are based on Fitch's current assessment of the impact of the coronavirus pandemic, including its economic impact, under a set of rating assumptions described below. These assumptions were used by Fitch to develop pro-forma financial metrics for L&G that are compared with both rating guidelines defined in its criteria and relative to previously established Rating Sensitivities for L&G.

The revision of the Outlooks to Negative reflects L&G's pro-forma financial leverage ratio (FLR) under our rating-case assumptions breaching our current negative rating sensitivity of 35%. This move is driven by weaker pro-forma shareholder equity. FLR improved to 31%

at end-2019 from 33% at end-2018, but weakens to 34% following the group's GBP500 million Tier 2 debt issue in April 2020, before application of Fitch's rating-case assumptions.

The affirmation of the group's ratings reflects our assessment of L&G's business profile, capitalisation and financial performance as very strong.

L&G's capital position remains resilient under our coronavirus assumptions in our rating case, with a Prism Factor-Based Capital Model (Prism FBM) score of 'Extremely Strong', unchanged from the actual score based on preliminary 2019 results. This is reinforced by a strong Solvency II capital coverage ratio of 174% at 28 February 2020, and 184% at end-2019.

The group's fixed-charge coverage (FCC) remained broadly stable at 13x in 2019 and is in line with the ratings. The pro-forma FCC under Fitch's rating case falls to 8x, but remains above our negative rating sensitivity of 5x.

L&G's earnings diversification is a strength, providing resilience against the impact of the pandemic on profitability. Strong profit and cash generation from its in-force annuity book helps to compensate for a potential decrease of fee income following a reduction in assets under management as a result of turbulent financial markets. L&G's profitability has been one of the highest among large UK-based peers' over recent years, with a net income return on equity (ROE) of 20% in 2019. Its pro-forma ROE under our rating case decreases to 16%, but remains well within the 'aa' category range.

We view L&G's investment and asset risk as low. We believe that L&G's significant exposure to credit risk is well-managed through a very low exposure to sub-investment grade assets and a credit default provision being held. These strengths are partly offset by the average credit quality of the group's fixed- interest portfolio and significant investment exposure to the UK infrastructure assets. Fitch-calculated risky asset ratio was 42% at end-2019. The group's pro-forma risky assets ratio under our rating case deteriorates to 71%.

We also believe that L&G's liquidity position is very strong, allowing the group to meet near-term liquidity requirements such as coupons, dividends payments and collateral requirements.

We view Banner Life and William Penn (together, Legal & General America (LGA)) as 'Core' to L&G as defined in our insurance criteria. As a result we align their IFS Ratings with that of Legal and General Assurance Society Limited, the other core rated operating entity in the group. L&G Re, the group's Bermuda-based reinsurance arm, is set up to enable the group to write international pension risk transfer business and shares branding with L&G's core entities. However, it remains a small part of the business with a limited track record. We therefore view L&G Re as 'very important' to the group and notch its IFS Rating off the core entities' at 'A+'.

Assumptions for Coronavirus Impact (Rating Case):

Fitch used the following key assumptions, which are designed to identify areas of vulnerability, in support of the pro-forma ratings analysis discussed above:

--Decline in key stock market indices by 35% relative to 1 January 2020.

--Increase in two-year cumulative high-yield bond default rate to 13%, applied to current non-investment grade assets, as well as 12% of 'BBB' assets.

--A decline in UK house prices by 5% and related decline in the valuation of equity release mortgages by 4.5%

--A coronavirus infection rate of 5% and a mortality rate (as a percent of infected) of 1%.

RATING SENSITIVITIES

The ratings remain sensitive to a material change in Fitch's rating-case assumptions with respect to the coronavirus pandemic. Periodic updates to our assumptions are possible given the rapid pace of changes in government actions in response to the pandemic, and the pace with which new information is made available on the medical aspects of the outbreak. An indication of how ratings would be expected to be impacted under a set of stress-case assumptions is included at the end of this section to help frame sensitivities to a severe downside scenario.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A material adverse change in Fitch's rating assumptions with respect to the coronavirus impact.

-- Prism FBM score falling to the low end of the 'Very Strong' range, FLR increasing to above 35% as indicated by our rating case or interest cover decreasing to below 5x, which could lead to a downgrade.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--A material positive change in Fitch's rating assumptions with respect to the coronavirus impact.

--A positive rating action is prefaced by Fitch's ability to reliably forecast the impact of the coronavirus pandemic on the financial profiles of both the UK life insurance industry and L&G.

--Sustained group FLR below 35% while maintaining a Prism FBM score at 'Extremely Strong', which would result in an Outlook revision to Stable.

--A substantial improvement in FLR , combined with a lower investment

exposure to the UK infrastructure assets, while maintaining a Prism FBM score at 'Extremely

Strong', which would lead to an upgrade. However, we view this as unlikely in the medium term.

Stress Case Sensitivity Analysis

--Fitch's stress case assumes a 60% stock market decline, a two-year cumulative high-yield bond default rate of 22%, more prolonged declines in government rates, heightened pressure on capital-market access, a coronavirus infection rate of 15% and mortality rate of 0.75, a notch-lower sovereign rating, and UK house prices declining by 10%, while equity release mortgages decline by 6.5%.

--The implied-rating impact under the stress case would be a downgrade of up to two notches.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Legal & General Finance PLC				
• senior unsecured	LT	A	Affirmed	A
Banner Life Insurance Company	Ins Fin Str	AA- Rating Outlook Negative	Affirmed	AA- Rating Outlook Stable
Legal & General Group Plc	LT IDR	A+ Rating Outlook Negative	Affirmed	A+ Rating Outlook Stable
• subordinated	LT	BBB+	Affirmed	BBB+

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Insurance Rating Criteria -- Effective March 2, 2020–Aug. 25, 2020 (pub. 02 Mar 2020) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Prism Factor-Based Capital Model, v1.7.1 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Banner Life Insurance Company	EU Issued
Legal & General Finance PLC	EU Issued
Legal & General Group Plc	EU Issued
Legal & General Reinsurance Company Limited	EU Issued
Legal and General Assurance Society Limited	EU Issued
William Penn Life Insurance Company Of New York	EU Issued

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