Garantia Insurance Company Ltd.

General

Garantia Insurance Company Ltd. published its Solvency and Financial Condition Report for 2019 on Monday 23 March 2020. The report is in its entirety available on the company's website at www.garantia.fi.

The purpose of this amendment is to supplement the information given in the report by assessing the impact of the COVID-19 pandemic and the subsequent market changes on the solvency and financial condition of the company, as required by Paragraph 6 of Section 8a of the Insurance Companies' Act.

Garantia has on 13 August 2020 published a financial summary concerning the period 1 January – 30 June 2020. the summary is available on the company's website. The following table presents the key financial figures for the period.

Profit and loss account and key ratios

EUR thousands	1-6/2020	1-6/2019	Change	2019
Gross premiums written	**7,864**	**7,753**	**1.4 %**	**19,627**
Other items *	-771	-1,161	-33.6 %	-6,384
Earned premiums	**7,093**	**6,593**	**7.6 %**	**13,242**
Claims incurred	-314	-1,427	-78.0 %	-1,618
Operating expenses	-1,798	-2,879	-37.6 %	-5,752
Balance on technical account before changes in equalisation provision	**4,981**	**2,287**	**117.8 %**	**5,873**
Change in equalisation provision	314	1,427	-	1,618
Balance on technical account	**5,296**	**3,713**	**42.6 %**	**7,491**
Investment income and expenses, net	-2,428	3,988	-160.9 %	6,266
Other income and expenses	24	4	-	14
Earnings before tax	**2,892**	**7,706**	**-62.5 %**	**13,771**
Claims ratio, %	4.4 %	21.6 %	-17.2 %-p.	43.4 %
Expense ratio, %	25.3 %	43.7 %	-18.3 %-p.	55.7 %
Combined ratio, %	29.8 %	65.3 %	-35.5 %-p.	12.2 %
Return on investments at fair value, %	-4.5 %	5.3 %	-9.8 %-p.	8.1 %
Solvency ratio, % **	232.4 %	224.5 %	0.6 %-p.	231.8 %
Total insurance exposure, EUR bn.	1.85	1.65	0.5 %	1.84
Average number of personnel	22	27	-5	25
Credit rating (S&P)	A-	A-	-	A-

Profit & loss items are compared against figures of the corresponding period in 2019. Balance sheet and other cross-section items are compared against the end of 2019 unless otherwise indicated. Figures for the half-year periods 1-6/2020 and 1-6/2019 have not been audited.

* Reinsurers' share of premiums written, change in provision for unearned premiums and reinsurers' share of change in provision for unearned premiums.

** Solvency II regulations do not fall within the sphere of statutory auditing. Solvency II figures have not been audited.

Operating environment

The COVID-19 epidemic, having evolved into a global pandemic during the first half of 2020, quickly led to steep deterioration of the outlook for both the global and the Finnish economies. The S&P500 index, a stock index describing the US stock market, reached its lowest point during the first half of the year in March, when the value of the index had fallen 31% from the beginning of the year. Bond spreads widened and liquidity in the capital markets weakened. However, stock market performance soon reverted to positive, and at the end of June, the S&P500 index was only about 4% below the levels seen in the beginning of the year.

In order to curb the spreading of the epidemic, the Emergency Powers Act was taken into use on 13 March 2020, on the basis of which the Government restricted public gatherings and the freedom of movement, closed down schools and other educational institutions, and ordered restaurants to mostly cease their operations. Movement across the Uusimaa region border was restricted in Mach and April. The global effects of the pandemic and the related control measures led in to diminishing economic activity in the country, despite the withdrawal of the Emergency Powers Act and relaxation of several control measures as of 1 June 2020.

According to economic forecasts published in April and May, the Finnish economy will contract 5-6% this year. In forecasts predating the crisis, economic growth in 2020 was estimated to be around 1%. The estimates concerning the contraction of the economy, however, are subject to significant uncertainty.

As a concequence of the rapid contraction of the economy, coporate revenues and profitability will decline and the financial position of companies will weaken. Direct consequences will be primarily suffered by small and medium-sized enterprises and companies operating in the services sector. The deterioriation of the financial standing of enterprises will lead to workforce layoffs and, if sustained for a longer time, to rising unemployment. Consumer purchasing power will diminish, and this will have negative effects on private consumption and the willingness of households to invest.

During spring, the Finnish Government has published economic support measures in order to back up business enterprises financially, and to avoid unnecessary bankruptcies. The support efforts are especially aimed at providing direct support and securing financing for companies suffering the most. Also, the social security of private individuals has been temporarily improved.

Development and risk position of insurance operations

Garantia's business operations consist of guaranty insurance operations and investment operations. The principal risks associated with the operations are credit risk arising from insurance operations, and market risks incurred in investment operations.

The company's total guaranty insurance exposure grew 0.5% in January-June, and stood at EUR 1.85 (1.84) billion at the end of June. During the period, insurance exposure growth was mainly attributable to the well-diversified residential mortgage guaranty portfolio.

Of the total guaranty insurance expoure, consumer exposures made up 47% (45) and corporate exposures made up 53% (55). The consumer exposures include a diversified and low-risk residential mortgage portfolio and a rental guaranty portfolio. The corporate exposures include corporate loan guaranties, commercial guaranties and other guaranties. 72.4% (72.4) of the corporate exposures were rated BB- or above. The proportion of weak ratings of C+ or lower was 1.5% (1.7).

So far, the market changes seen in the first half of the year have not resulted in increased claims. Claims incurred in the period of January-June amounted to EUR 0.3 (1.4) and claims ratio was 4.4% (21.6).

Development and risk position of investment operations

Garantia's investments are used for covering the technical provisions and equity capital, and their primary purpose is to secure the liquidity of insurance operations also in years with exceptionally high claims.

Garantia's investment return, at fair value, was -4.5% (5.3) in January-June 2020. Net investment return recorded in profit and loss was EUR -2.4 (4.0) million.

The fair value of Garantia's investment portfolio (incl. cash and bank balances) was EUR 142.8 (150,8) million at the end of June. At the end of June, fixed income investments made up 88.5% (84.4), equity & private equity investments 10.2% (14.4) and real estate investments 1.3% (1.2) of the investment portfolio (incl. cash and bank balances).

Investment return has a significant effect on Garantia's financial results. However, the risk profile of investment operations is low, restricting the amount of losses.

Solvency

Garantia's basic own funds amounted to EUR 107.8 (112.7) million at the end of June 2020. The reduction of basic own funds during the first half of the year was mainly due to the decrease in the fair value of investment assets. The company's solvency capital requirement was EUR 46.4 (48.6) million at the end of June. Solvency ratio was 232% (232).

Solvency, EUR thousands	30.6.2020	31.12.2019	30.6.2019
Basic own funds	**107,840**	**112,681**	**105,615**
Solvency capital requirement			
Market risk	19,438	23,704	20,622
Non -life underwriting risk	28,560	21,019	21,760
Counterparty default risk	257	278	105
Operational risk	441	420	433
Diversification effect and adjustment for loss-absorbing capacity	-17,557	-16,665	-15,723
Total	**31,140**	**28,756**	**27,197**
Capital add-on	15,265	19,848	19,848
Total	**46,405**	**48,604**	**47,045**
Amount of own funds in excess of the solvency capital requirement	61,435	64,077	58,570
Solcency ratio, %	232.4 %	231.8 %	224.5 %

Solvency remained unchanged in January-June. Basic own funds decreased, but also the solvency capital requirement was slightly reduced. The decrease in the solvency capital requirement resulted from a decrease in the capital requirement for market risk and a decrease of the capital add-on. The capital requirement for market risk was reduced due to the decrease in the fair value of investment assets. The growth in the capital requirement for insurance risk was mainly attributable to the changes in the Solvency 2 calculation principles, that became effective as of 1 January 2020.

The Financial Supervisory Authority, through a decision made on 29 May 2020, reset the capital add-on imposed on Garantia Insurance Company Ltd. at EUR 15.3 (19.8) million. The new capital add-on has been applied from 30 June 2020 onwards. The main reason behind the reduction of the capital add-on was a change in calculation principles. The Financial Supervisory Authority for the first time utilised Garantia's own economic capital model while determining the amount of the capital add-on. Garantia's solvency capital requirement has included a capital add-on since 30 June 2018. The Financial Supervisory Authority reassesses the capital add-on at least annually.

The company's solvency continues to be strong, and the company has basic own funds twice the amount of the solvency capital requirement. The basic own funds carry a EUR 61.4 (64.1) million risk buffer in relation to the solvency capital requirement.

Contingency planning and precautionary measures in exceptional circumstances

As decreed by Paragraph 8 of Section 6 of the Insurance Companies' act, Garantia has a business continuity plan that is used in the preparation for exceptional circumstances in the operating environment. Business continuity is also secured through stand-in arrangements within company staff. Despite the exceptional circumstances, business operations of the company have continued as normal.

As part of its risk management framework, Garantia prepares an Own Risk and Solcency Assesment as required by the Solvency 2 Directive (EU 2009/138). The assessment is prepared at least annually and in also whenever necessary. The purpose of the Own Risk and Solvency Assessment is to evaluate the the company's general solvency requirements and the continuous adherence to capital requirements and requirements concerning technical provisions.

The Own Risk and Solvency Assesment includes a Capital Plan with predifined solvency levels and required precautionary measures for each level for exceptional circumstances. The purpose of the Capital Plan and the defined precautionary measures is to anticipate and ensure capital adequacy in such circumstances.

The company's solvency position remains strong despite the coronavirus epidemic and the subsequent market turbulence, and it has not been necessary to execute any of the precautionary measures. The company, however, has enhanced the monitoring of its solvency position and prepares for the excecution of any precautionary measures, should this become necessary,

Outlook

So far, Garantia's business operations have remained in a normal state, and the demand for guaranty insurance has been good. However, the level of credit risk, a defining feature of guaranty insurance, increases when the general economy shifts into recession. During recessionary periods, the creditworthiness of corporates and households deteriorates. Increasing payment difficulties of corporates and households, should such development occur, will lead to increasing claims in guaranty insurance operations. However, Garantia's solvency is strong and the company has sufficient risk buffers to cover the risks inherent in its operations.