FitchRatings

Does Your Company's Credit Rating Need You?

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Agenda

Rating Process Overview

Application of Criteria

Case Studies

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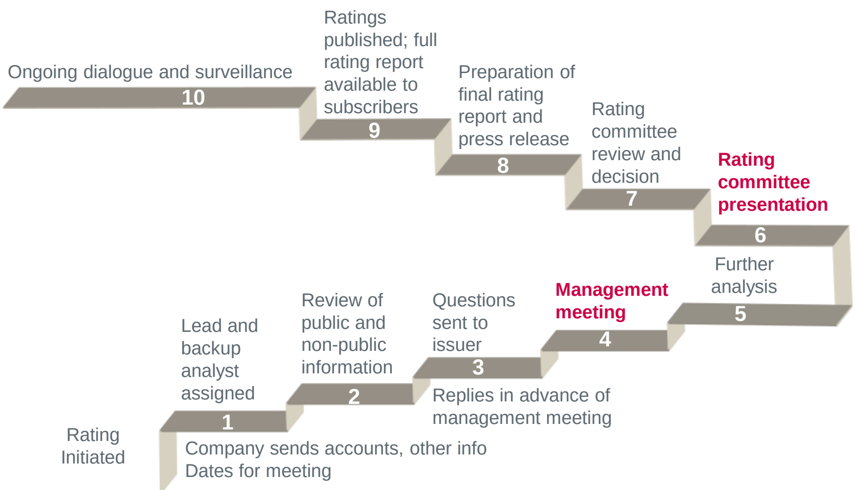
Insurer Financial Strength Rating (IFS)

- An assessment of the financial strength of an insurance organisation
- Is assigned to the insurance company's policyholder obligations
- Reflects an insurer’s ability to meet these obligations on a timely basis, and
- Expected recoveries in the event that payments are ceased or interrupted

Steps in the Rating Process



Management Meeting

- Information request
  - Public information
  - Non-public information

- Rating meeting agenda
  - Corporate overview
  - Operating and Underwriting Review
  - Financial review
  - Investment and Liquidity Review
  - Reserve review
  - Reinsurance

Committee Process

- Rating pack and rating recommendation by lead analyst
- Committee considers relevant quantitative and qualitative issues
- Committee challenge and discussion; votes on the recommendation
- Rating decision/rating triggers/right to appeal

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12 Key Credit Factors for Insurance Ratings

Quantitative

1. Capitalisation and Leverage
2. Debt Service Capabilities and Financial Flexibility
3. Financial Performance and Earnings
4. Investment and Asset Risk
5. Asset/Liability and Liquidity Management
6. Reserve Adequacy
7. Reinsurance, Risk Mitigation and Catastrophe Risk

Qualitative

8. Sovereign and Country-Related Constraints
9. Industry Profile and Operating Environment
10. Market Position and Size/Scale
11. Ownership
12. Corporate Governance and Management

Median Ratio Guidelines

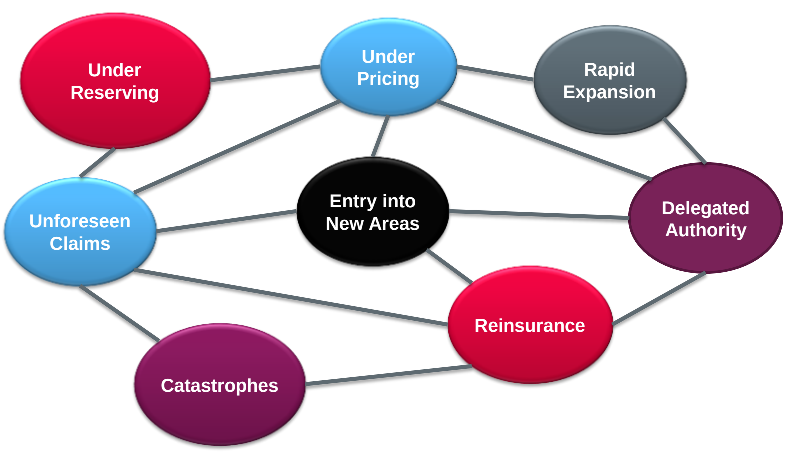
Capital & Leverage	AAA	AA	A	BBB
Net premiums written/equity (x)	0.5	1.1	1.8	2.5
EU solvency I ratio (%)	220	175	150	125
Financial leverage (%)	7	20	28	35
Debt Service Capabilities				
Fixed Charge Coverage Ratio (x)	18	12	7	3
Financial performance & earnings				
Combined Ratio (%)	85	95	103	110
Return on Equity (%)	16	12	8	4
Investments & liquidity				
Risky Assets/equity (%)	25	50	75	100
Reserve adequacy				
Loss reserve development/equity (%)	-5	-2	0	5
Loss reserve development/premiums (%)	-4	-1.5	0	3

Peer Group Comparison

(EURm)	IFS Rating / Outlook	Shareholders Equity	RoE	GWP	Total assets	RoA	Net income	Solvency I ratio (%)	Reported combined ratio (%)	Financial leverage (%)
AXA	AA–/Stable	55,314	8%	85,509	757,143	0.6%	4,482	221	96.6	24
Allianz	AA–/Stable	52,849	12%	72,051	711,530	0.9%	6,344	182	94.3	20
Generali	A–/Neg	21,405	10%	62,726	449,656	0.5%	2,142	141	95.6	35
ZFS	AA–/Stable	25,170	12%	39,367	300,763	1.0%	3,227	258	95.5	26
Mapfre	**BBB+/Stable**	**9,894**	**8%**	**21,836**	**56,826**	**1.4%**	**790.5**	**246**	**96.1**	**21**
RSA	A/RWN e	3,617	-10%	11,590	26,316	-1.5%	-399.0	110	99.6	36

What Could Cause A Failure?

The Atomium of Insurance Company Failure



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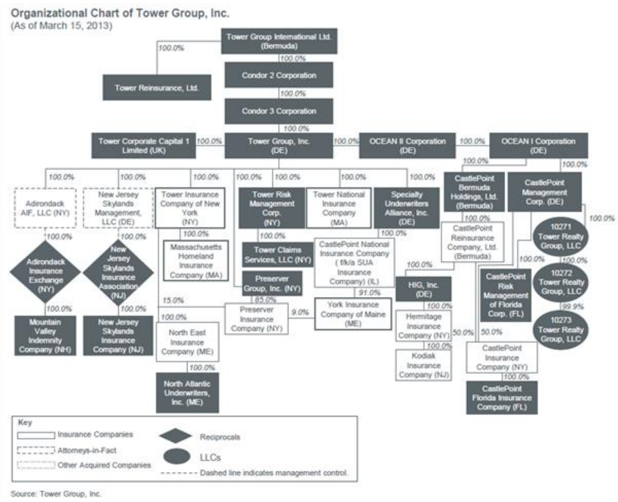
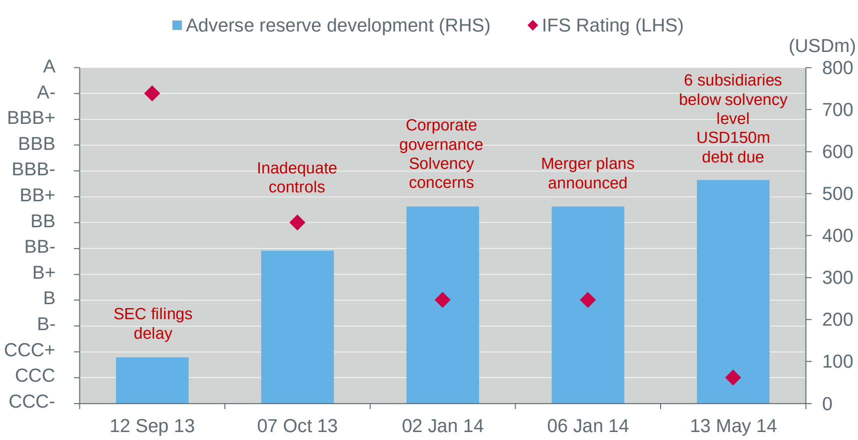
Case Study 1:
Tower Group International

Tower Group International



Tower Group International – IFS Development



Tower Group International: Credit Rating History

- 13 March 2013: **Affirm A-/stable outlook**
- 12 September 2013: Delayed Q2 SEC filings and earnings. Possible USD60-110 adverse reserve development. **Affirm A-/revise outlook to negative**
- 7 October 2013: USD364m adverse reserve development and write down USD214m in goodwill. **Downgrade to BB/rating watch negative**
- 2 January 2014: Additional USD75-105m adverse reserve development, concerns on the effectiveness of corporate governance and solvency of some of its subsidiaries. **Downgrade to B/rating watch negative**
- 6 January 2014: Announcement of a planned merger with a subsidiary of ACP Re. **B/revise rating watch to evolving**
- 13 May 2014: 2013 GAAP filing disclosed further reserve deterioration. USD150m debt matures on Sept. 15, 2014; unable to meet this obligation using its own financial resources. **Downgrade to CCC/rating watch evolving / withdraw the ratings**

Tower Group International: Key Ratios

	December 2012	December 2013
Capital & Leverage		
Net premiums written/equity (x)	1.7	12.2
Financial leverage (%)	44.3	99.5
Debt Service Capabilities		
Fixed Charge Coverage Ratio (x)	(1.4)	(28.1)
Financial performance & earnings		
Combined Ratio (%)	109.2	141.5
Return on Equity (%)	(8.1)	(196.3)
Investments & liquidity		
Risky Assets/equity (%)	24.3	118.4
Reserve adequacy		
Loss reserve development/equity (%)	6.9	58.8
Loss reserve development/premiums (%)	4.0	35.6

Case Study 1: Key Takeaways

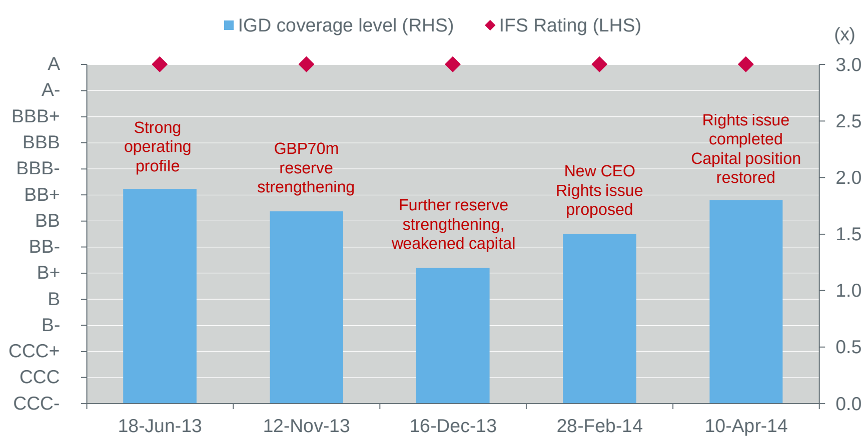
- Rapid growth through acquisitions resulted in a complex structure and ineffective oversight
- Inadequate reserving for the long-tail business acquired earlier
- Adverse reserve development led to erosion of solvency position

Case Study 2: RSA

RSA: Credit Rating History – Why Different?

- Reserving issues – a starting point similar to the previous case
- Internal control framework undermined by 'inappropriate collaboration' among a few senior executives
- Weakened capitalisation

RSA’s Credit Rating History



Key Takeaways

- Deficient reserving leads to solvency erosion
- News creep raises governance and management oversight concerns
- New management steadies confidence / increases probability of solvency restoration
- Level of earnings drag due to restructuring costs remains unclear

Summary

- Actuarial work feeds into a number of important areas of rating criteria
- Inaccurate reserve setting can have significant financial consequences
- Company financial health can be affected in a number of ways
- Actuarial skills are important for an insurer's credit rating!

People in pursuit of answers

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