



Understanding AM Best's Approach to Insurance Financial Strength Ratings and the Process

In association with the Federation of Afro-Asian Insurers and Reinsurers (FAIR)

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AM Best Analytical Briefing



Introduction to AM Best

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AM Best Overview

- Established in 1899 by Alfred M. Best with the mission to report on the financial stability of insurers and the insurance industry
- Oldest and most widely recognized provider of ratings, financial data and news with an exclusive insurance industry focus.
- Ratings are issued on approximately 4,000 companies in more than 100 countries.
- Cover 16,000 insurance companies globally through a wide range of analytical resources, references, directories and periodicals.
- Offices in the U.S., Amsterdam, London, Hong Kong, Dubai, Mexico City and Singapore.

AM Best Overview

- AM Best is the only global credit rating agency focused solely on insurance.
- We provide an independent, third-party assessment of business profile, operating performance, business profile and enterprise risk management.
- Our analysis offers valuable insight into an organization, its management and track record.
- The interactive rating process serves as a roadmap for practicing sound risk management and effective business strategy.
- Our rating process promotes credibility, transparency and acceptance for new market/business penetration.
- We rate new formations, startups and companies of all sizes.
- Best's Credit Rating Methodology (BCRM) is publicly shared and transparent.
- Best's Credit Ratings are registered by regulatory authorities around the world. [Click here](#) for the full list.
- We rate risk transfer, single-parent captives, group captives, risk retention groups (RRGs) and protected cells in a number of domiciles.
- Our unmatched access to global insurance data, industry intelligence and analytical resources helps us deliver an essential perspective to the marketplace.



What We Rate

- Insurance companies, health maintenance organizations, holding companies of these organizations, and debt and debt-like instruments issued by these organizations:
 - Financial Strength Ratings – an independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations. This rating is assigned to insurance companies.
 - Issuer Credit Ratings – an independent opinion of an issuer/entity's ability to meet its ongoing senior financial obligations. This rating is assigned to insurance companies and related holding companies and other legal entities authorized to issue financial obligations.
 - Debt Ratings – an independent opinion of an issuer's ability to meet its ongoing financial obligations to security holders when due. This rating is assigned to the debt securities and insurance-linked securities transactions of the entities rated by AM Best.

Insurance Specialisation Means:

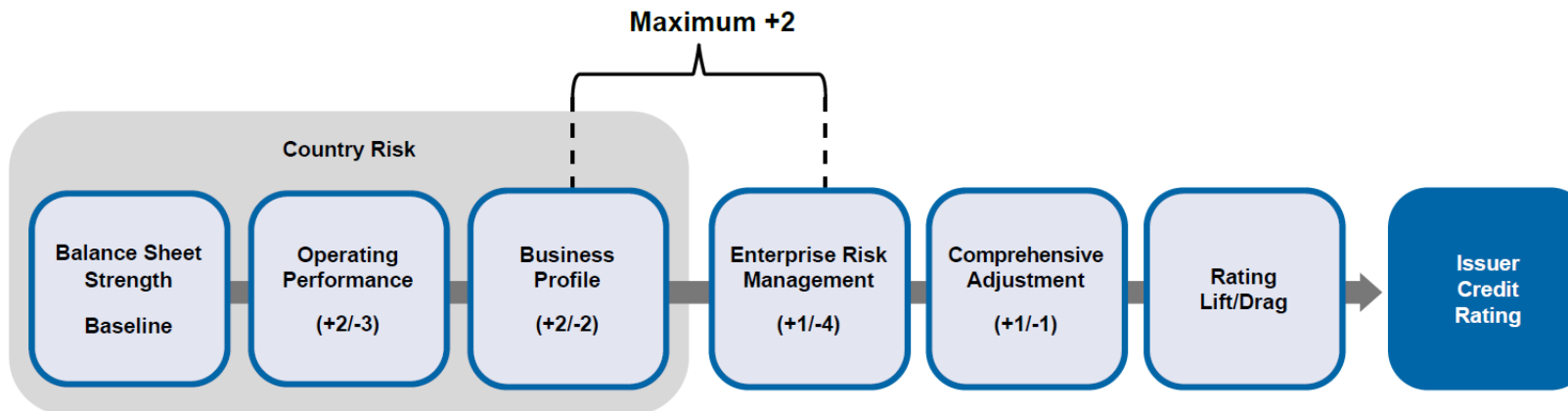
- Rating methodologies that are specific to the insurance industry.
- Analysts who are insurance specialists and only analyse insurance companies.
- Greater understanding of the insurance industry both globally and on a local level including growth markets.
- Ability to provide specific indications as to the main drivers of a rating grounded in industry knowledge.
- Focusing on the company and not the country's sovereign rating.
- Proven ability to rate start-ups, supporting industry development.

Why (Re)insurers Choose AM Best?

- Only international rating agency focused on the insurance industry.
- Specialist rating methodology incorporating criteria on all key insurance industry segments.
- Analytical teams with a thorough insurance industry understanding.
- Analytical focus on the company not the country.
- Interactive feedback and benchmarking.
- Quantitative assessment of capital adequacy including stress scenarios.
- World's leading provider of insurer Financial Strength Ratings (FSRs) by company coverage.
- Foremost rating coverage of the global reinsurance segment.
- Thorough understanding of emerging market dynamics.
- Leading rating agency for ART structures and captives.
- Key rating agency used by global broker security teams.

Fundamentals of AM Best Ratings

- Primary objective is to provide an opinion of the rated entity's ability to meet its senior financial obligations
 - Issuer credit ratings
 - Financial strength ratings
 - Issue credit ratings (debt)
- Fundamental rating drivers are
 - Balance sheet strength
 - Business profile
 - Operating performance
 - Enterprise risk management



AM Best's Rating Scales

Best's Issuer Credit Rating (ICR):

Opinion of an insurer's financial strength and ability to meet its ongoing **financial obligations**.

Can be issued on either a long-term or short-term basis.

Best's Financial Strength Rating (FSR):

Opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations.

Long-Term ICR	FSR
aaa, aa+	A++
aa, aa-	A+
a+, a	A
a-	A-
bbb+, bbb	B++
bbb-	B+
bb+, bb	B
bb-	B-
b+, b	C++
b-	C+
ccc+, ccc	C
ccc-, cc	C-



The rating process and its steps



← 2 weeks → ← 6-8 weeks → ← 1 day → ← 6-8 weeks → ← 1 day → ← 1-10 days →

← 3.5 – 4.0 months →

Step 1:	Issue contract and invoice Sign contract pay initial fee Assign analyst
Step 2:	Arrange Rating Meeting Compile public and proprietary information Complete Supplementary Rating Questionnaire
Step 3:	Analysts meet with the Senior Management and Technical team of the company The meeting may be virtual
Step 4:	Analysts prepare recommendation based on analysis and discussions with the company The Rating Committee reviews and determines the rating
Step 5:	The rating is communicated to the rated company
Step 6:	Once the company accepts the rating, it is published
Step 7:	The company is continuously monitored once the rating is accepted The rating is formally reviewed at least once a year but continuously monitored Open communication with the analysts is essential

Introduction to AM Best's Rating Methodology & Reinsurance Market Trends

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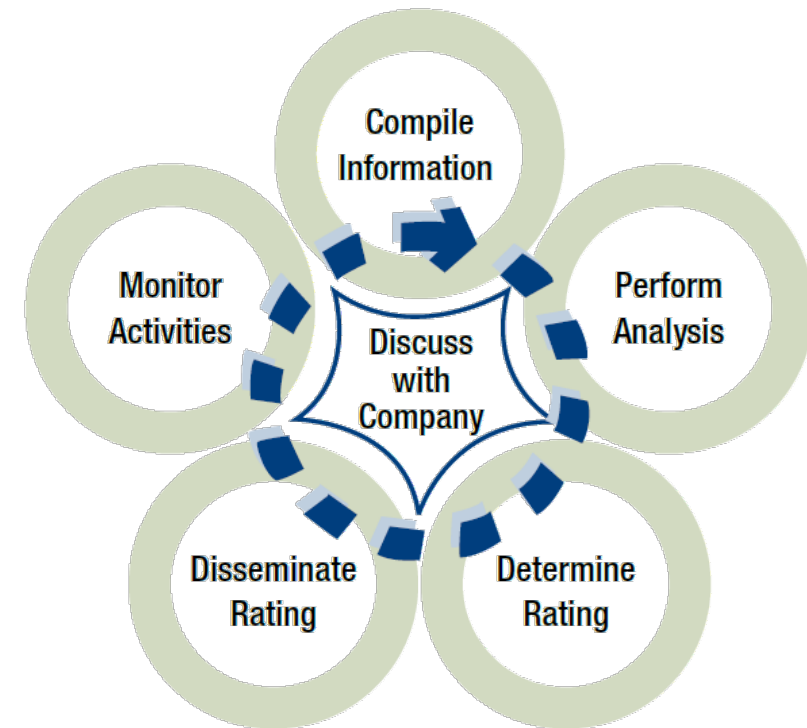


Introduction to AM Best's Rating Methodology



The Interactive Rating Process

- The foundation of the rating process is an ongoing dialogue with the rated company's management
- Ratings are determined by a rating committee, by simple majority vote
- Ratings process outlined in Best's Credit Rating Methodology (BCRM). Where applicable, specialty criteria procedures also apply.



Rating Translation Table

Best's Issuer Credit Rating (ICR):

Opinion of an insurer's financial strength and ability to meet its ongoing **financial obligations**

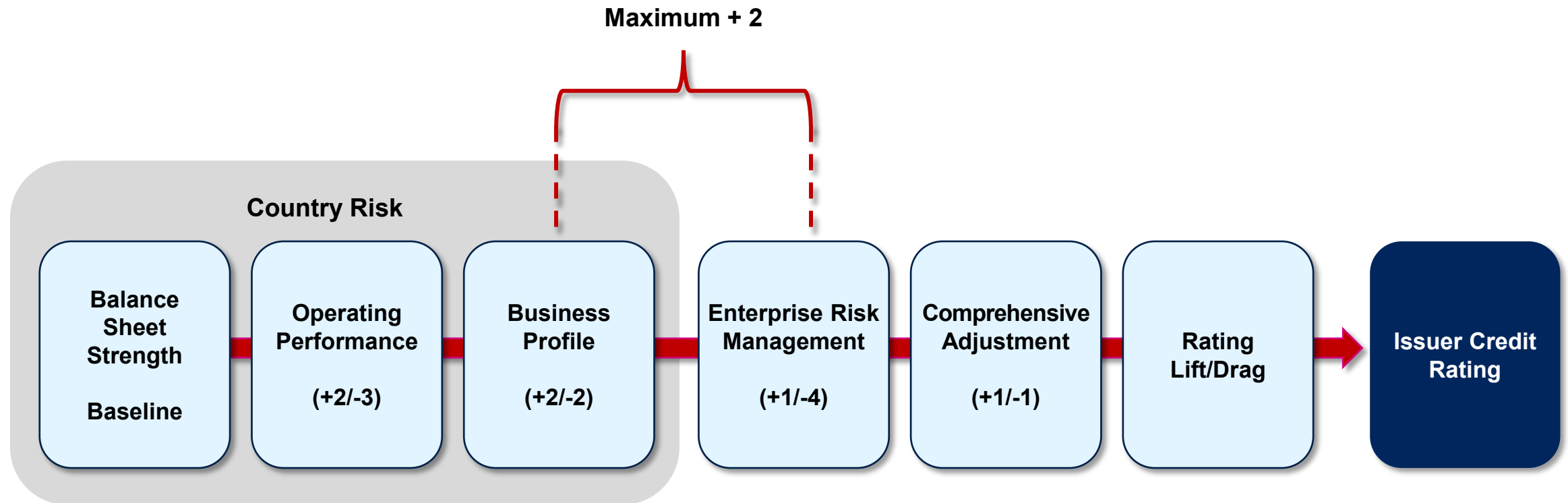
Can be issued on either a long-term or short-term basis

Best's Financial Strength Rating (FSR):

Opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations

Long-Term ICR	FSR
aaa, aa+	A++
aa, aa-	A+
a+, a	A
a-	A-
bbb+, bbb	B++
bbb-	B+
bb+, bb	B
bb-	B-
b+, b	C++
b-	C+
ccc+, ccc	C
ccc-, cc	C-

BCRM: Building Block Approach

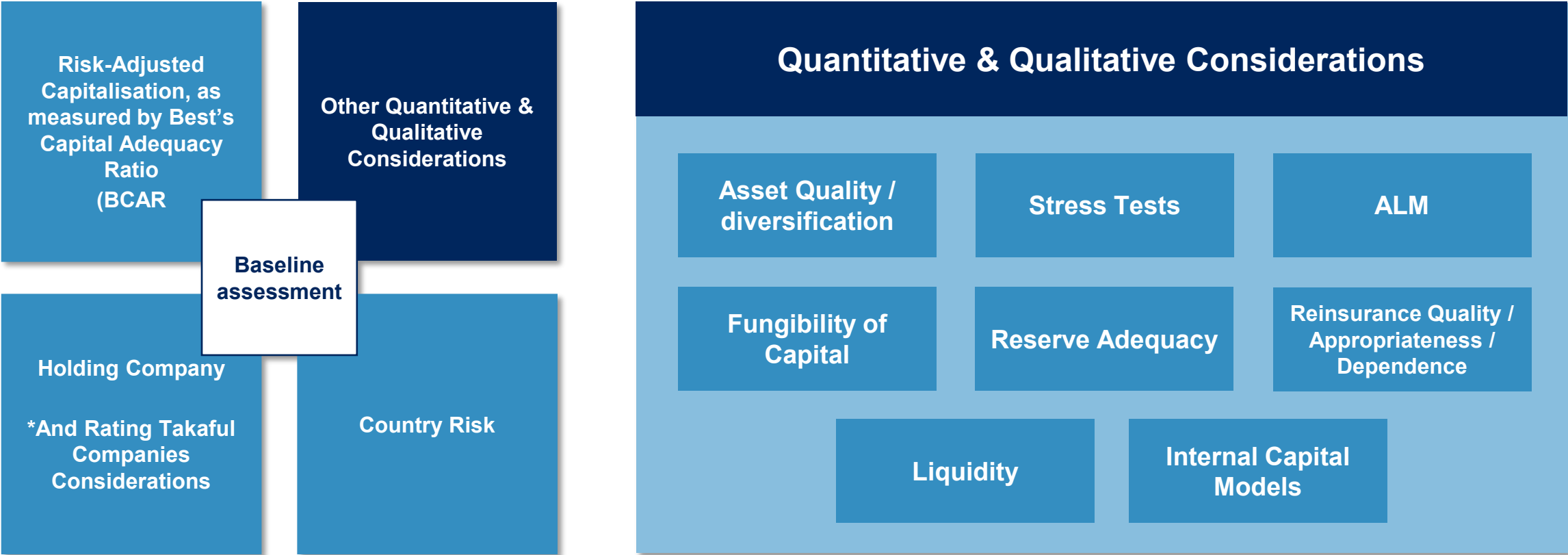


Balance Sheet Strength Assessment - BCAR

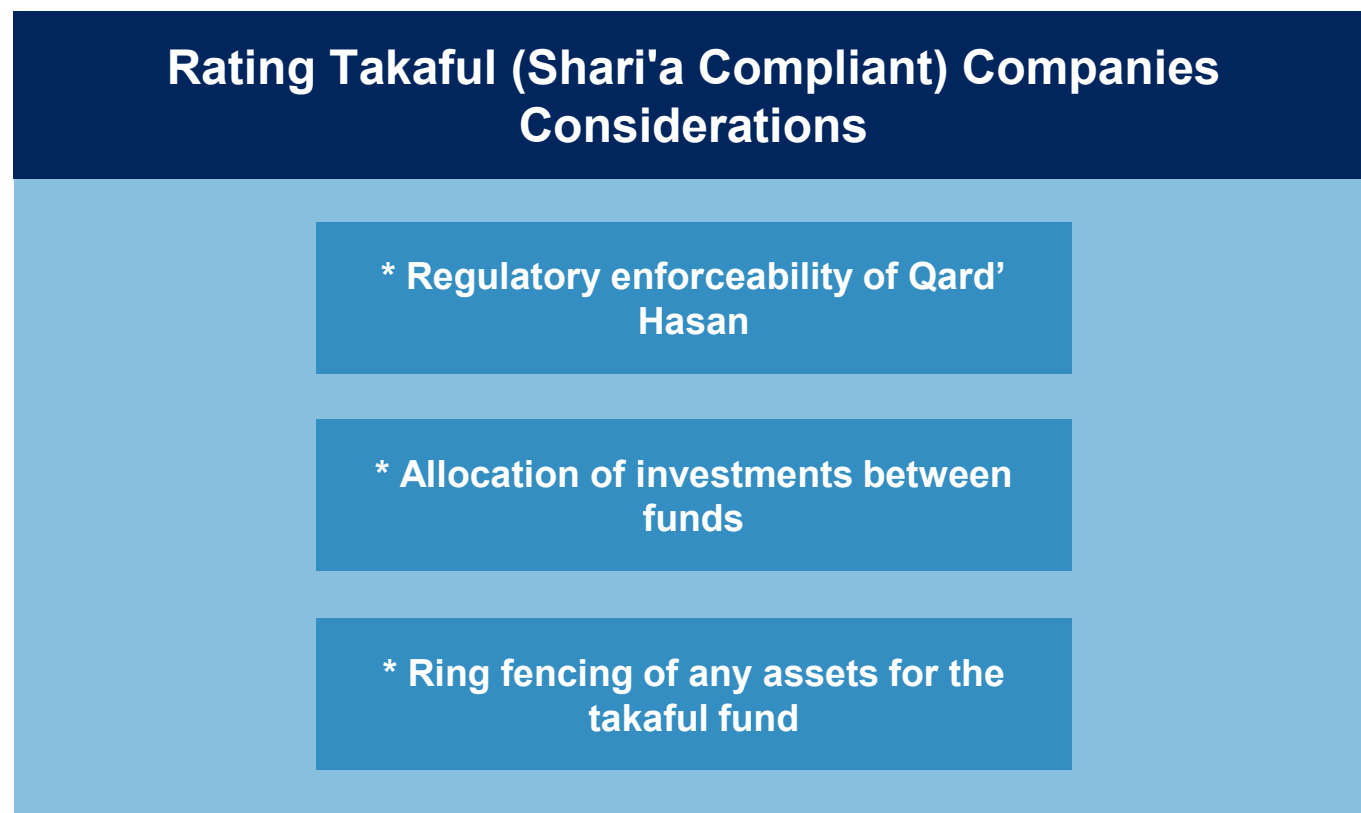


Risk-Adjusted Capitalisation as measured by Best's Capital Adequacy Ratio (BCAR)		
$\text{BCAR} = \frac{(\text{Available Capital} - \text{Net Required Capital})}{\text{Available Capital}} \times 100$		
Four scores corresponding to the 95%, 99%, 99.5% and 99.6% confidence level; translates to a BCAR assessment:		
VaR Confidence Level (%)	BCAR	BCAR Assessment
99.6	> 25 at 99.6	Strongest
99.6	> 10 at 99.6 & ≤ 25 at 99.6	Very Strong
99.5	> 0 at 99.5 & ≤ 10 at 99.6	Strong
99	> 0 at 99 & ≤ 0 at 99.5	Adequate
95	> 0 at 95 & ≤ 0 at 99	Weak
95	≤ 0 at 95	Very Weak
* Typically companies with < 20 million USD capital & surplus are not eligible for the strongest category		

Balance Sheet Strength Assessment - Quantitative & Qualitative



Balance Sheet Strength Assessment - Company Structure



Balance Sheet Strength Assessment - Country Risk & Baseline



Overall Balance Sheet Strength Assessment						
Combined Balance Sheet Assessment (Rating Unit / Holding Company)	Country Risk Tier					
		CRT-1	CRT-2	CRT-3	CRT-4	CRT-5
	Strongest	a+/a	a+/a	a/a-	a-/bbb+	bbb+/bbb
	Very Strong	a/a-	a/a-	a-/bbb+	bbb+/bbb	bbb/bbb-
	Strong	a-/bbb+	a-/bbb+	bbb+/bbb/bbb-	bbb/bbb-/bb+	bbb-/bb+/bb
	Adequate	bbb+/bbb/bbb-	bbb+/bbb/bbb-	bbb-/bb+/bb	bb+/bb/bb-	bb-/b+/b
	Weak	bb+/bb/bb-	bb+/bb/bb-	bb-/b+/b	b+/b/b-	b/b-/ccc+
	Very Weak	b+ and below	b+ and below	b- and below	ccc+ and below	ccc and below

Operating Performance Assessment



Rating Takaful (Shari'a Compliant) Companies Considerations

Balance of Earnings Between Shareholders and Policyholders

Wakala Fee Relative to Operating Expenses

Distribution of Surplus to Policyholders

Operating Performance Assessment

Very Strong +2

Strong +1

Adequate 0

Marginal -1

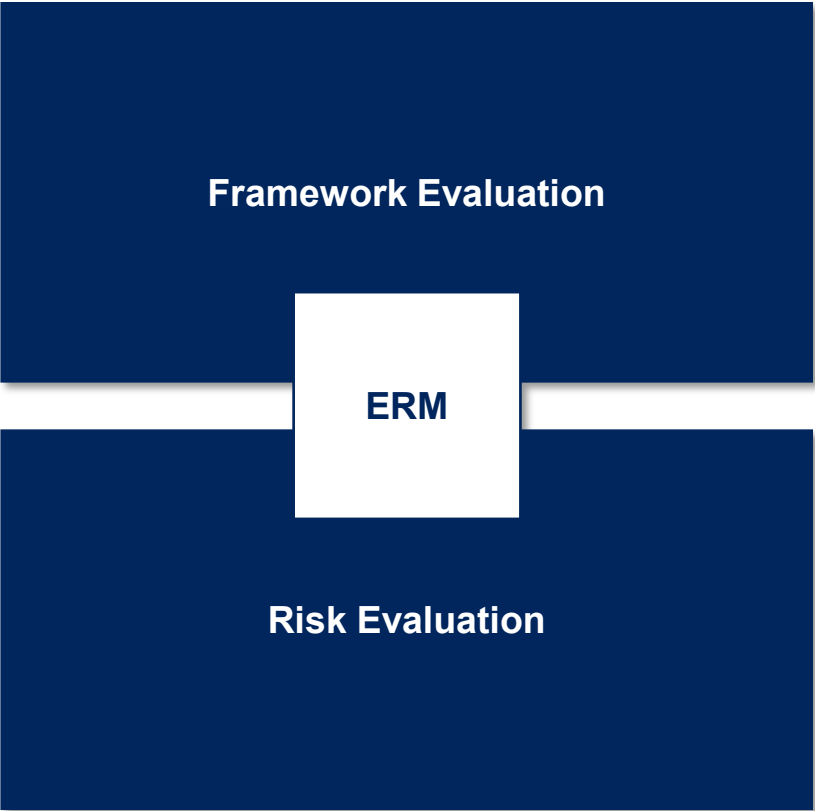
Weak -2

Very Weak -3

Business Profile Assessment



Enterprise Risk Management (ERM)



Risk Identification and Reporting	
Risk Appetite and Tolerances	
Stress Testing and Non-Modelled Risks	
Risk Management and Controls	
Governance and Risk Culture	
Product & Underwriting Risk	Operational Risk
Reinsurance Risk	Concentration Risk
Legislative/Regulatory/Judicial/Economic Risk	Investment Risk
Reserving Risk	Liquidity & Capital Management Risk

ERM Assessment
Very Strong +1
Appropriate 0
Marginal -1
Weak -2
Very Weak -3/-4

Reinsurance Market Trends

**Outlook – Stable
Past Peak, Fundamentally Strong**

Global Non-Life Re Outlook Remains Stable – Tailwinds



Despite softening property pricing, operating results remain solid



Property-catastrophe underwriting aided by favorable terms and higher attachment points



Robust nominal and risk-adjusted capital, prudent capital management plans



Elevated interest rates enhancing investment income and earnings

Global Non-Life Re Outlook Remains Stable – Headwinds



Accelerated softening in property reinsurance pricing, with modest loosening of terms and structure



Social inflation driving reserve and pricing concerns in certain US casualty lines



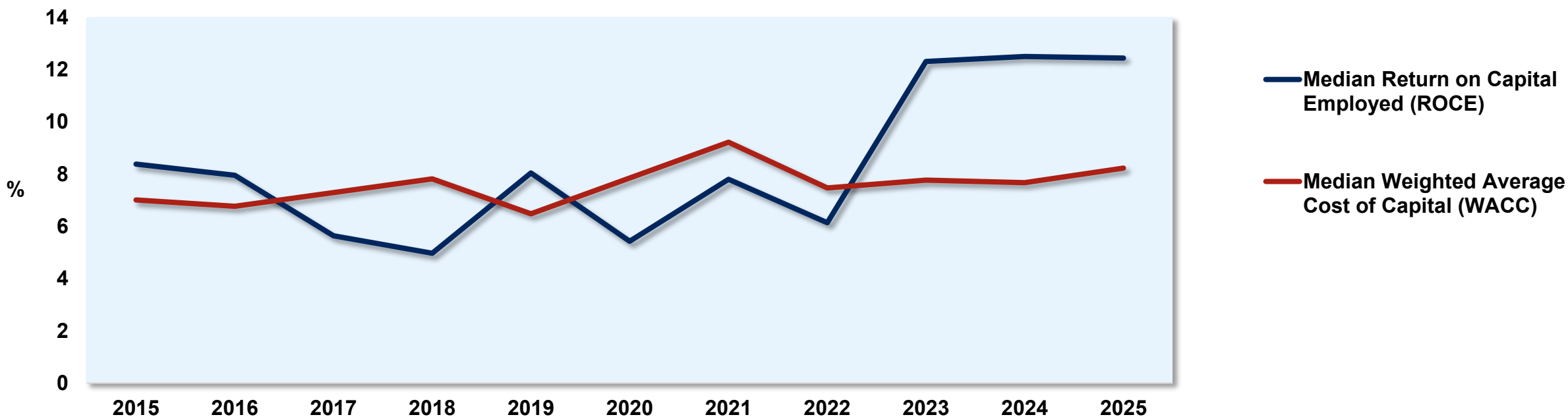
Elevated frequency and severity of weather-related events



Geopolitical and macroeconomic uncertainty – inflation, policy shifts, market volatility

**Robust Operating Results
Leads to
Robust Organic Capital Generation**

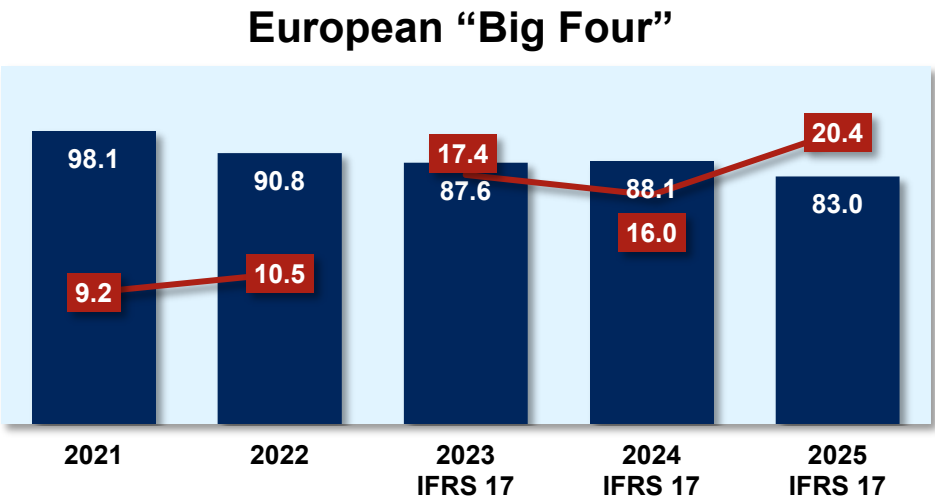
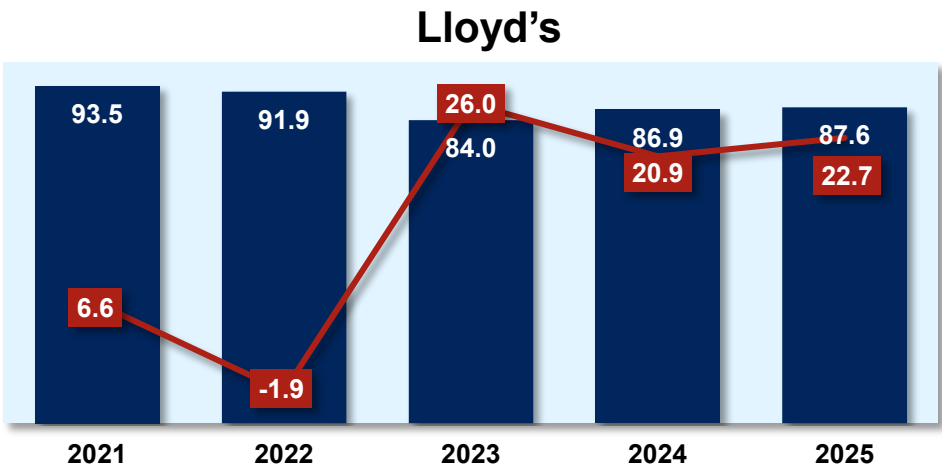
Returns Still Exceeding Cost Of Capital – Sustainable?



Reinsurers Meeting Cost of Capital

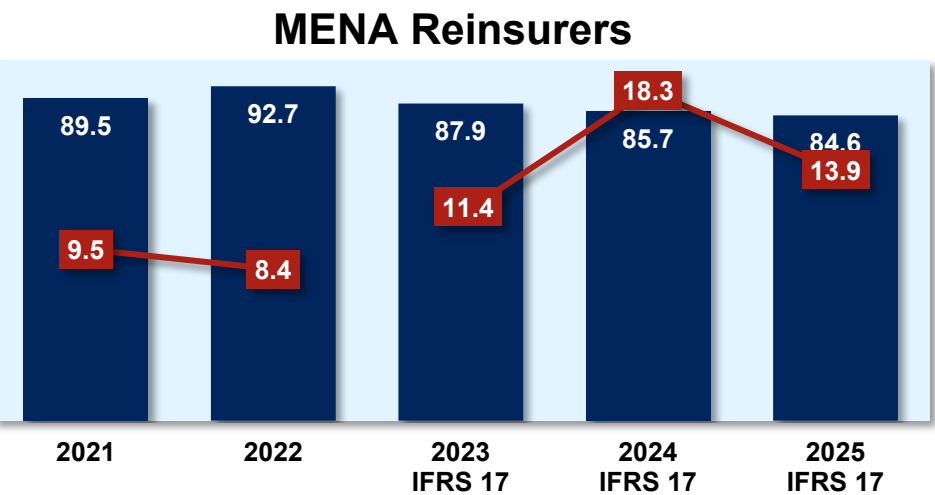
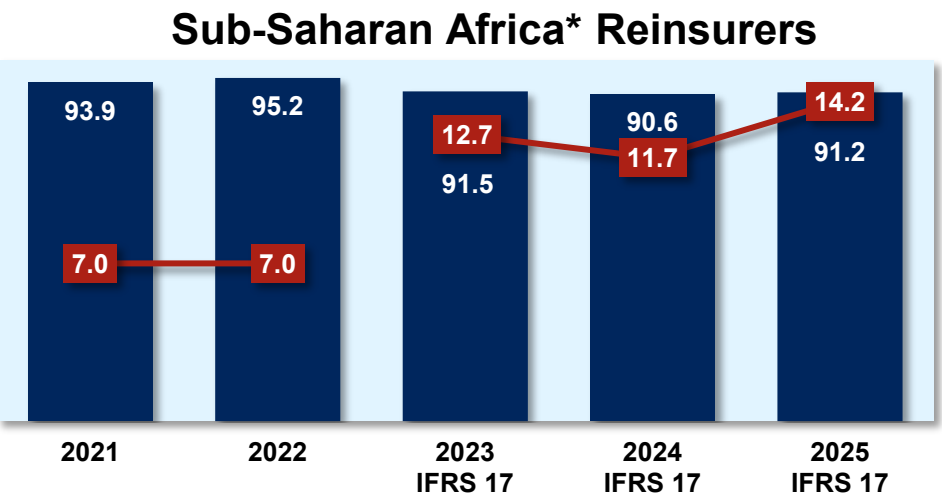


Robust Operating Performance Across Reinsurance Market Segments



Combined Ratio

Return on Equity

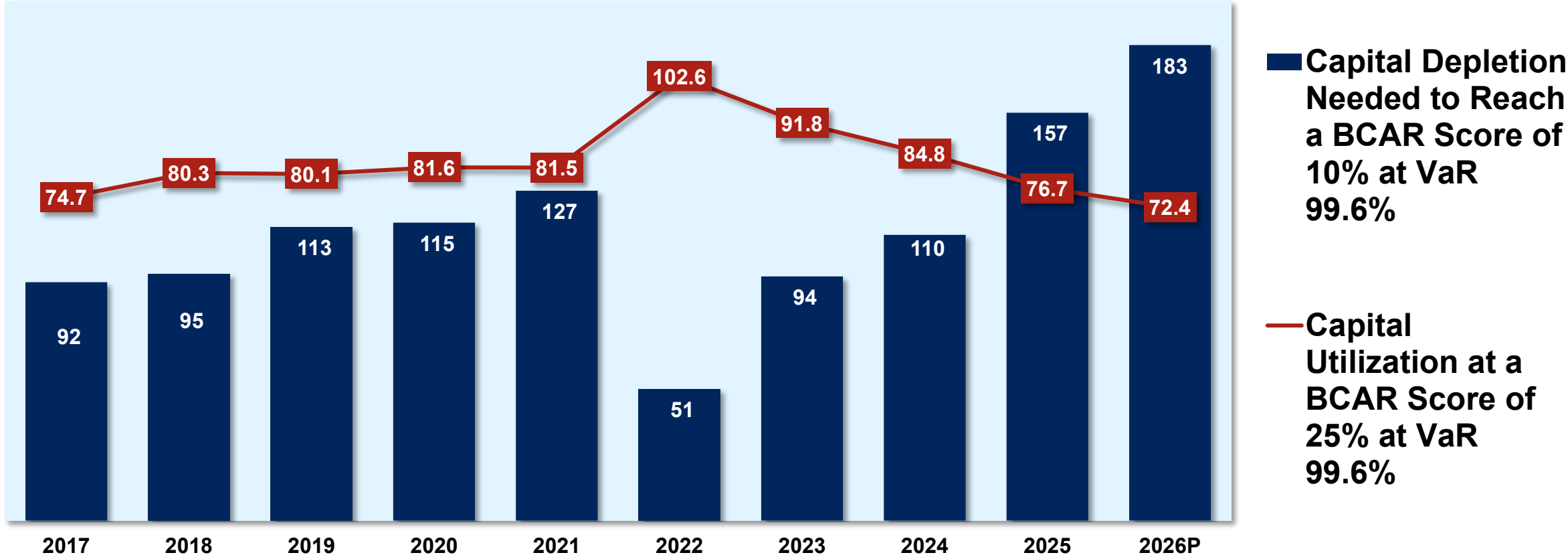


Source: AM Best data and research.
* Excludes South Africa



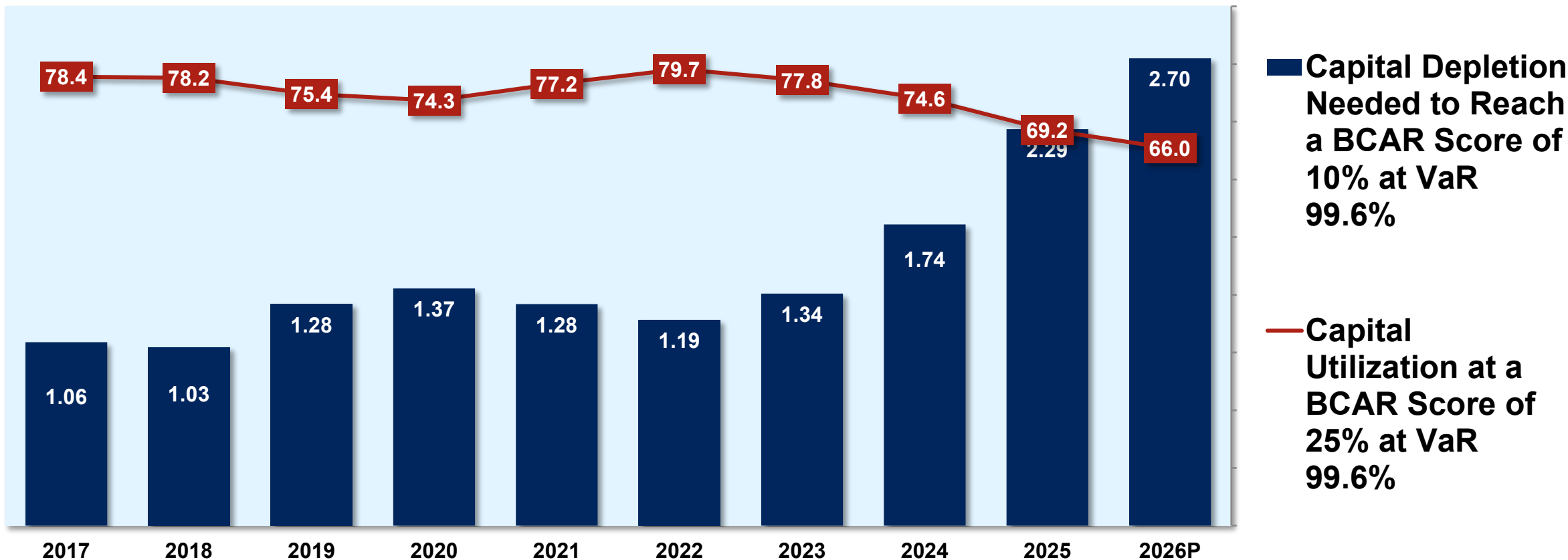
Risk-Adjusted Capitalization Remains Strong

Global Reinsurance – Capital Utilization (USD billions)



Risk-Adjusted Capitalization Remains Strong

MENA & SSA Reinsurance – Capital Utilization (USD billions)



Expectations – Solid but Moderating Pricing and Structures

What Could Cause a Negative Outlook?



Rate reductions that push pricing below adequacy



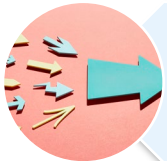
**Broad loosening of terms, lower attachments,
more aggregate capacity**



Adverse development that erodes capital



Weather loss(es) that reveal a structural weakness



Expected ROE at or below cost of capital

Q&A



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