



AM Best is a global credit rating agency, news publisher and data analytics provider specializing in the insurance industry. For more information, visit www.ambest.com.

AMERICAS

WORLD HEADQUARTERS

A.M. Best Company, Inc.
A.M. Best Rating Services, Inc.
1 Ambest Road, Oldwick, NJ 08858
Phone: +1 908 439 2200

MEXICO CITY

A.M. Best América Latina, S.A. de C.V.
Paseo de la Reforma 412, Piso 23, Mexico City, Mexico
Phone: +52 55 1102 2720

EUROPE, MIDDLE EAST & AFRICA (EMEA)

LONDON

A.M. Best Europe - Information Services Ltd.
A.M. Best Europe - Rating Services Ltd.
12 Arthur Street, 6th Floor, London, UK EC4R 9AB
Phone: +44 20 7626 6264

AMSTERDAM

A.M. Best (EU) Rating Services B.V.
NoMA House, Gustav Mahlerlaan 1212, 1081 LA Amsterdam, Netherlands
Phone: +31 20 308 5420

DUBAI*

A.M. Best - MENA, South & Central Asia*
Office 102, Tower 2, Currency House, DIFC
P.O. Box 506617, Dubai, UAE
Phone: +971 4375 2780

*Regulated by the DFSA as a Representative Office

ASIA-PACIFIC

HONG KONG

A.M. Best Asia-Pacific Ltd
Unit 4004 Central Plaza, 18 Harbour Road, Wanchai, Hong Kong
Phone: +852 2827 3400

SINGAPORE

A.M. Best Asia-Pacific (Singapore) Pte. Ltd
6 Battery Road, #39-04, Singapore
Phone: +65 6303 5000

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Best's Credit Rating Methodology (BCRM)

An Overview



This overview document provides a quick look at the components of Best's Credit Rating Methodology (BCRM) and rating process. For more information related to the complete BCRM, including various comprehensive criteria procedures applicable to aspects of the insurance and reinsurance industry globally, please visit the Best's Credit Rating Methodology section of our website at www3.ambest.com/ambv/ratingmethodology/.

All *key characteristics* described for each *assessment category* are ideal scenarios and are not intended to be prescriptive.

Rating Disclosure: Use and Limitations

A Best's Credit Rating (BCR) is a forward-looking independent and objective opinion regarding an insurer's, issuer's, or financial obligation's relative creditworthiness. The opinion represents a comprehensive analysis consisting of a quantitative and qualitative evaluation of balance sheet strength, operating performance and business profile or, where appropriate, the specific nature and details of a security. Because a BCR is a forward-looking opinion as of the date it is released, it cannot be considered as a fact or guarantee of future credit quality and therefore cannot be described as accurate or inaccurate. A BCR is a relative measure of risk that implies credit quality and is assigned using a scale with a defined population of categories and notches. Entities or obligations assigned the same BCR symbol developed using the same scale, should not be viewed as completely identical in terms of credit quality. Alternatively, they are alike in category (or notches within a category), but given there is a prescribed progression of categories (and notches) used in assigning the ratings of a much larger population of entities or obligations, the categories (notches) cannot mirror the precise subtleties of risk that are inherent within similarly rated entities or obligations. While a BCR reflects the opinion of A.M. Best Rating Services, Inc. (AMBRS) of relative creditworthiness, it is not an indicator or predictor of defined impairment or default probability with respect to any specific insurer, issuer, or financial obligation. A BCR is not investment advice, nor should it be construed as a consulting or advisory service, as such; it is not intended to be utilized as a recommendation to purchase, hold or terminate any insurance policy, contract, security, or any other financial obligation, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser. Users of a BCR should not rely on it in making any investment decision; however, if used, the BCR must be considered as only one factor. Users must make their own evaluation of each investment decision. A BCR opinion is provided on an "as is" basis without any expressed or implied warranty. In addition, a BCR may be changed, suspended, or withdrawn at any time for any reason at the sole discretion of AMBRS.

Best's Credit Rating Methodology – Rating Process Overview

Best's Credit Ratings (BCRs)

AM Best assigns various types of BCRs to a wide variety of insurance organisations, from single legal entity insurers to complex, multinational enterprises with diversified operations.

Best's Credit Rating Scale

Translation of Issuer Credit Ratings to Financial Strength Ratings

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-
c	D

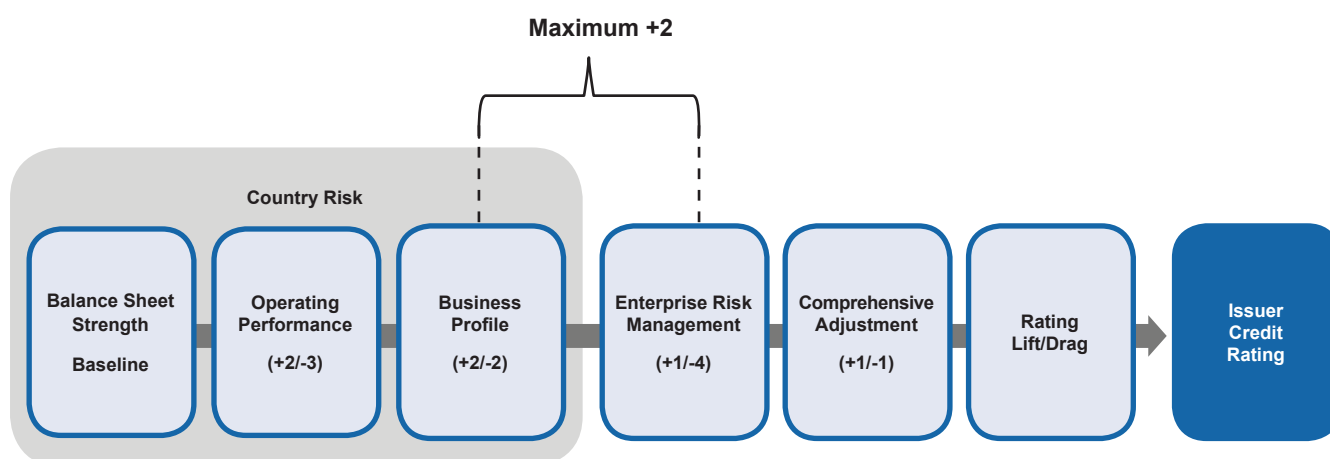
AM Best Credit Rating Definitions

- **Best's Issuer Credit Rating (ICR):** An independent opinion of an entity's ability to meet its ongoing financial obligations, issued on either a long- or short-term basis
- **Best's Financial Strength Rating (FSR):** An independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations
- **Best's Issue Credit Rating (IR):** An independent opinion of credit quality assigned to issues that gauges the ability to meet the terms of the obligation, issued on a long- or short-term basis
- **Best's National Scale Rating (NSR):** A relative measure of creditworthiness in a specific local jurisdiction that is issued on a long-term basis and derived exclusively by mapping the NSR from a corresponding global Issuer Credit Rating (ICR) using a transition chart

Best's Credit Rating Methodology (BCRM)

Best's Credit Rating Methodology (BCRM) provides a comprehensive explanation of AM Best's rating process. Key rating factors—including an insurer's balance sheet strength, operating performance, business profile and enterprise risk management (ERM)—are qualitatively and quantitatively evaluated during the rating process. The foundational building blocks of AM Best's rating approach are outlined below.

AM Best's Rating Process



Balance Sheet Strength

AM Best's rating analysis is an interactive process that begins with an evaluation of the company's balance sheet strength. This evaluation includes a three-part analysis focusing on the following areas:

1. The insurance rating unit (the insurer)
2. The financial flexibility and risks associated with the insurer's holding company and/or ownership structure
3. The impact of country risk on the insurer's balance sheet strength

Best's Credit Rating Methodology – Rating Process Overview

Baseline Balance Sheet Strength Assessment

Assessment Factors	
<ul style="list-style-type: none">Best's Capital Adequacy Ratio (BCAR)Quality and appropriateness of reinsurance programmesQuality and diversification of assetsFinancial and operating leverage	<ul style="list-style-type: none">Adequacy of reservesLiquidityQuality of capitalInternal economic capital models

Best's Capital Adequacy Ratio (BCAR)

The measurement of the insurer's capital adequacy is key to the balance sheet assessment. AM Best uses its Best's Capital Adequacy Ratio to differentiate an insurer's balance sheet strength and determine whether its capitalisation is appropriate for its risk profile. The BCAR evaluates many of the insurer's balance sheet risks simultaneously, generates an estimate of the capital needed to support those risks at different confidence intervals and compares it with the insurer's available capital.

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

Baseline Balance Sheet Strength Assessment

The assessments of the insurance company (Part 1) and its holding company (Part 2) result in the company's "Combined Balance Sheet Strength Assessment." AM Best arrives at a company's baseline balance sheet strength assessment by incorporating country risk (Part 3). The baseline is selected for the company from the various options in the Overall Balance Sheet Assessment chart and is determined through analytical judgment and rating committee review.

The Insurance Rating Unit:

Assessment	Key Characteristics
Strongest	The rating unit has the strongest BCAR score with a demonstrated pattern of stability. Its quality of capital and Asset Liability Management (ALM) are also the strongest. It has an appropriate and diverse reinsurance programme. Any additional analytical factors are in line with an assessment of strongest.
Very Strong	The rating unit has a very strong BCAR score with a demonstrated pattern of stability. Its quality of capital and ALM are also very strong. It has an appropriate and diverse reinsurance programme. Any additional analytical factors are in line with an assessment of very strong.
Strong	The rating unit has a strong BCAR score with a demonstrated pattern of stability. Its quality of capital and ALM are also strong. It has an appropriate and diverse reinsurance programme. Any additional analytical factors are in line with an assessment of strong.
Adequate	The rating unit has an adequate BCAR score that has been relatively stable. Its quality of capital and ALM are adequate. It has an appropriate reinsurance programme. Any additional analytical factors are in line with an assessment of adequate.
Weak	The rating unit has a weak BCAR score with a demonstrated pattern of volatility. Its quality of capital and ALM are weak. Its reinsurance programme is weak. Any additional analytical factors are in line with an assessment of weak.
Very Weak	The rating unit has a very weak BCAR score with a demonstrated pattern of volatility. Its quality of capital and ALM are very weak. Its reinsurance programme is very weak. Any additional analytical factors are in line with an assessment of very weak.

Best's Credit Rating Methodology – Rating Process Overview

Holding Company

This analysis involves a review of the impact of the holding company and/or affiliates on the rating unit (the insurer). AM Best considers financial flexibility (including the holding company's BCAR score), liquidity, financial leverage, interest coverage, dividend requirements and cash sources and uses (including unregulated non-insurance subsidiaries) to determine the effect on the lead rating unit.

Impact of Insurance Holding Company on Balance Sheet Strength Assessment

Assessment	Key Characteristics
Positive	The consolidated BCAR is supportive of or exceeds that of the rating unit BCAR. Financial flexibility, liquidity, and access to capital markets are high. Financial leverage is low on both an adjusted and unadjusted basis. Interest coverage is more than adequate.
Neutral	The consolidated BCAR is consistent with the rating unit BCAR. Financial flexibility, liquidity, and access to capital markets are adequate. Financial leverage is acceptable on both an adjusted and unadjusted basis. Interest coverage is adequate.
Negative	The consolidated BCAR score is inadequate relative to the rating unit BCAR. Financial flexibility, liquidity, and access to capital markets are low. Financial leverage is high on either an adjusted or unadjusted basis. Interest coverage is inadequate.
Very Negative	The consolidated BCAR indicates a poor financial position relative to the rating unit BCAR. Financial flexibility, liquidity, and access to capital markets are very low. Financial leverage is very high on either an adjusted or unadjusted basis. Interest coverage is inadequate.

Once the holding company analysis is completed, the result is integrated with the balance sheet strength assessment of the lead rating unit.

Combined Balance Sheet Strength Assessment

Lead Rating Unit	Holding Company				
		Positive	Neutral	Negative	Very Negative
	Strongest	Strongest	Strongest	Very Strong	Adequate
	Very Strong	Strongest	Very Strong	Strong	Weak
	Strong	Very Strong	Strong	Adequate	Very Weak
	Adequate	Strong	Adequate	Weak	Very Weak
	Weak	Adequate	Weak	Very Weak	Very Weak
	Very Weak	Weak	Very Weak	Very Weak	Very Weak

Country Risk

Country risk and its assessment are incorporated into the analysis of balance sheet strength, operating performance and business profile. AM Best defines country risk as country-specific risk factors that could adversely affect an insurer's ability to meet its financial obligations.

Overall Balance Sheet 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/bb-/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

Best's Credit Rating Methodology – Rating Process Overview

Operating Performance

The second building block of AM Best's rating process is operating performance. This analysis can result in an increase, decrease or no change to the baseline assessment. Possible adjustments range from +2 notches to -3 notches.

AM Best views operating performance as a leading indicator of future balance sheet strength and long-term financial stability. A company's profitability affects its ability to generate earnings, and profitable insurance operations are essential for a company to operate as a going concern. In general, more diversity in earnings streams leads to greater stability in operating performance. AM Best's analysis of operating performance focuses on the stability, diversity and sustainability of the company's earnings sources and the interplay between earnings and liabilities.

Operating Performance Assessment

Assessment	Notches	Key Characteristics
Very Strong	+2	Historical operating performance is exceptionally strong and consistent. Trends are positive and prospective operating performance is expected to be exceptionally strong. Volatility of key metrics is low.
Strong	+1	Historical operating performance is strong and consistent. Trends are neutral/slightly positive and prospective operating performance is expected to be strong. Volatility of key metrics is low to moderate.
Adequate	0	Historical operating performance and trends are neutral. Prospective operating performance is expected to be neutral. Volatility of key metrics is moderate.
Marginal	-1	Historical operating trends have been inconsistent. Trends are neutral/slightly negative with some uncertainty in prospective operating performance. Volatility of key metrics is moderate to high.
Weak	-2	Historical operating performance is poor. Trends are slightly negative and prospective operating performance is expected to be poor. Volatility of key metrics is high.
Very Weak	-3	Historical operating performance is very poor. Trends are negative and prospective operating performance is expected to be very poor. Volatility of key metrics is very high.

Business Profile

Business profile is the third building block in AM Best's rating process and is a highly qualitative component of AM Best's rating evaluation. Business profile may ultimately affect an insurer's current and future operating performance and, in turn, its long-term financial strength and ability to meet its obligations to policyholders. Possible adjustments for business profile range from +2 notches to -2 notches.

The business profile review includes evaluation of the following factors:

- Market position
- Degree of competition
- Distribution channels
- Pricing sophistication and data quality
- Management quality
- Product/Geographic concentration
- Product risk
- Regulatory, event, market, and country risks

Best's Credit Rating Methodology – Rating Process Overview

Business Profile Assessment

Assessment	Notches	Key Characteristics
Very Favourable	+2	The company's market leadership position is unquestionable, demonstrated and defensible with high brand recognition. Distribution is seen as a competitive advantage; business lines are non-correlated and generally lower risk. Its management capabilities and data management are very strong.
Favourable	+1	The company is a market leader with strong business trends and good control over distribution. It has diversified operations in key markets that have high to moderate barriers to entry with low competition. It has a strong management team that is able to meet projections and utilise data effectively.
Neutral	0	The company is not a market leader, but is viewed as competitive in chosen markets. It has some concentration and/or limited control of distribution. It has moderate product risk but limited severity and frequency loss. Its use of technology is evolving and its business spread of risk is adequate.
Limited	-1	The company has a lack of diversification in geographic and/or product lines; its control over distribution is limited and undifferentiated. It faces high/increasing competition with low barriers to entry and elevated product risk. Management is unable to utilise data effectively or consistently in business decisions.
Very Limited	-2	The company faces high competition and low barriers to entry. It has high concentration in commodity or higher-risk products with very limited geographic diversity. It has weak data management. Country risk may factor into its elevated business profile risks.

Enterprise Risk Management (ERM)

ERM is the fourth building block in the rating process. The impact of ERM on an insurer's rating is based on understanding the development and implementation of an insurer's risk management framework as well as the insurer's risk management capability relative to its risk profile. The framework and the risk evaluations include the following sub-assessments:

Framework Evaluation	Risk Evaluation
<ul style="list-style-type: none"> • Risk identification and reporting • Risk appetite and tolerance • Stress testing and non-modelled risks • Risk management and controls • Governance and risk culture 	<ul style="list-style-type: none"> • Product and underwriting • Reserving • Concentration • Reinsurance • Liquidity and capital management • Investments • Legislative, regulatory, judicial and economic • Operational

Enterprise Risk Management Assessment

Assessment	Notches	Key Characteristics
Very Strong	+1	The insurer's ERM framework is embedded. The insurer demonstrates market best practice techniques. The results are evident in a prudent and stable level of net required capital and successful performance over the long term. Risk management capabilities are very strong and are suitable for the risk profile of the company.
Appropriate	0	The insurer's ERM framework is developed. Risk management capabilities are well aligned with the risk profile of the company.
Marginal	-1	The insurer's ERM framework is evolving. Risk management capabilities show some weakness in key risk areas.
Weak	-2	The insurer's ERM framework contains some nascent elements. Risk management capabilities are largely not aligned with the risk profile of the company.
Very Weak	-3/4	The insurer's ERM framework is unrecognised. Risk management capabilities relative to the risk profile of the company are not aligned.

Best's Credit Rating Methodology – Rating Process Overview

If a rating unit is practicing sound risk management and executing its strategy effectively, the results will be evident in successful performance over the long term. Possible adjustments for ERM range from +1 notch to -4 notches.

Companies with complex global business profiles have a need for a robust and comprehensive ERM programme. In many cases, the complexities and demands of these companies' "Very Favourable" business profiles require an equally "Very Strong" ERM. Acknowledging this interaction, and the limited impact that these two highly qualitative building blocks may have on credit strength, the combined impact between business profile and ERM will be restricted to a maximum of +2 notches. This calculation would only affect those companies that have both a "Very Favourable" business profile assessment and a "Very Strong" ERM assessment.

Comprehensive Adjustment

A comprehensive adjustment may be applied in the rating process when the company being reviewed has an uncommon strength or weakness that exceeds (or is less than) what has been captured through the rating process up to this point. A comprehensive adjustment can increase or decrease the assessment by a maximum of 1 notch. The vast majority of ratings will not require a comprehensive adjustment.

Assessment	Notches	Key Characteristics
Positive	+1	The company has uncommon strengths that exceed what has been captured throughout the rating process.
None	0	The company's strengths and weaknesses have been accurately captured throughout the rating process.
Negative	-1	The company has uncommon weaknesses that exceed what has been captured throughout the rating process.

Rating Lift/Drag

In this step, the company may be afforded lift (or drag) based on factors such as integration, strategic importance and contribution to the overall enterprise. The amount of lift or drag assigned depends on the specific circumstances of the insurer. For further details please visit www3.ambest.com/ambv/ratingmethodology/.

The Credit Rating Process

The typical duration from signed contract to rating dissemination is generally about three to four months. Each interactively rated entity is assigned to a rating analyst, who manages the ongoing interaction with company management and conducts the fundamental credit analysis as described in AM Best's rating criteria.

BCRs are initially determined and periodically updated through a defined rating committee process. The rating committee itself consists of analytical staff and is chaired by senior rating officers. The committee approach ensures rating consistency across different business segments and maintains the integrity of the rating process (described briefly below).

1

Compile Information

The assigned analyst collects public and proprietary financial information and data to develop a tailored meeting agenda.

2

Perform Analysis

AM Best incorporates a host of qualitative and quantitative measures to evaluate the organisations' financial health.

3

Determine Best's Credit Rating

The AM Best Rating Committee ensures rating consistency and maintains the integrity of the rating process and methodology.

4

Disseminate Best's Credit Rating

Best's Credit Ratings are distributed via the AM Best website, press releases and a number of print and digital publications.

5

Monitor Best's Credit Rating

AM Best regularly monitors the rating by continually analysing the organisation's creditworthiness.

Best's Credit Rating Methodology – Rating Process Overview

Sample Information Inputs

Private		Public
<ul style="list-style-type: none"> • Capital structure • Investment and credit guidelines • Reinsurance guidelines • Exposure to catastrophes • Enterprise risk management (ERM) • Internal capital models 	<ul style="list-style-type: none"> • Meeting with key executives • Business plans and projections • Supplemental Rating Questionnaire (SRQ) • Actuarial memorandum • Loss provision reports • Cash flow stress testing 	<ul style="list-style-type: none"> • Financial statements • Reports to shareholders • Public records • Regulatory reports and disclosure notes • Audit reports • Compliance and ethical conduct reports

Characteristics of Highly Rated Insurers

- Superior and stable risk-adjusted capitalisation across the various confidence levels
- Strong, predictable and sustainable operating profitability developed from a favourable lower-risk liability profile, with results exhibiting limited volatility
- Competitive advantage in branding, customer experience, investments, and/or underwriting
- Competitive market position leading to pricing power in core business lines
- Strong and stable operating cash flows, with books of business demonstrating favourable retention trends
- Diversified earnings and revenue streams
- Effective use of technology/data analytics which positively impacts performance
- Product design with flexibility/risk-sharing features to effectively react to changing market environments
- Market-leading distribution system
- Comprehensive and proactive enterprise risk management
- Consistency of key metrics compared with peers
- Long-term, well-developed business strategy that has been tested over time
- Strong management team
- Key operations in stable regulatory environments

