AM Best's Insurance Market Briefing & Networking Reception – Cayman Islands

February 12, 2025

Building Block Approach & Use of the Best Capital Adequacy Ratio

Anthony Diodato – Managing Director AM Best

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AM Best at a Glance

- AM Best is the oldest and most widely recognized insurer-focused credit rating agency.
- It remains the only global rating agency with a specialist focus on the insurance and reinsurance sectors, publishing nearly 4,000 ratings on companies in more than 100 countries.
- The company was established in the US in 1899 and pioneered the concept of financial strength ratings in 1905.
- Today, in addition to our worldwide headquarters in the US, AM Best has regional offices in:

    - London
    - Amsterdam
    - Hong Kong
    - Singapore
    - Mexico City
    - Dubai*

*Regulated by the Dubai Financial Services Authority as a credit rating agency.

Why Best's Credit Ratings

- AM Best credit rating services assessing the creditworthiness of and/or reports on over 16,000 insurance companies worldwide.
- Our credit ratings provide an **independent**, third-party opinion of an insurer's ability to meet ongoing insurance and senior financial obligations.
- Our rating opinions are **indicative** of an insurance company's ability to pay claims, debts and other financial obligations in a timely manner.
- The **interactive** rating process serves as a roadmap for practicing sound risk management and effective business strategy.
- AM Best is the only global credit rating agency focused exclusively on insurance. Our analysts' diverse financial, operational, claims, underwriting and actuarial backgrounds equip them to deliver rating insights and research that help insurers, financial professionals and consumers make informed decisions.

Best's Credit Rating Process Overview

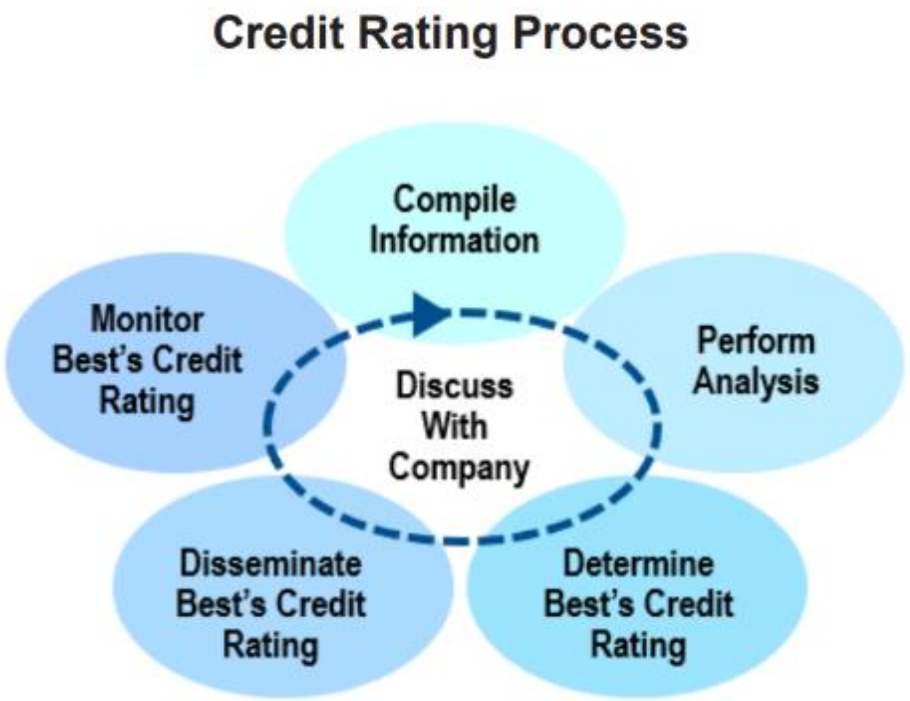
1 **Compile Information**
The assigned analyst collects public and proprietary financial information and data to develop a tailored meeting agenda.

2 **Perform Analysis**
AM Best incorporates a host of qualitative and quantitative measures to evaluate the organization's financial health.

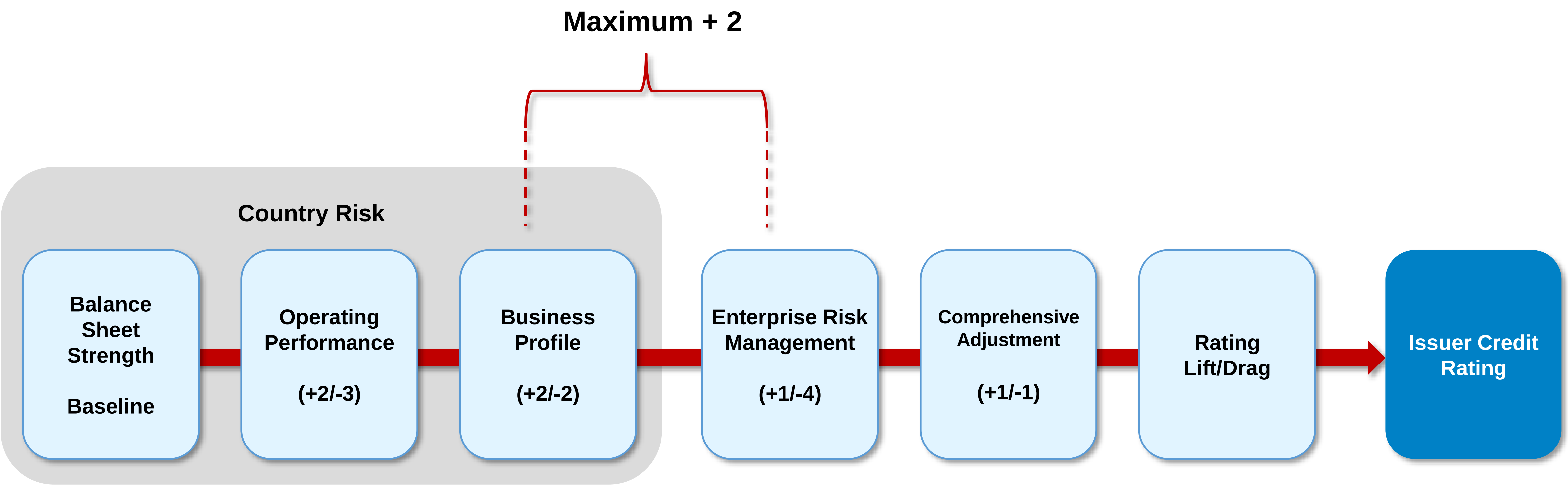
3 **Determine Best's Credit Rating**
The AM Best rating committee ensures rating consistency and maintains the integrity of the rating process and methodology.

4 **Disseminate Best's Credit Rating**
If the initial Best's Credit Rating is accepted, it is 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 analyzing the organization's creditworthiness.



AM Best’s Credit Rating Methodology: BCRM



Best Capital Adequacy Ratio (BCAR)

What is BCAR

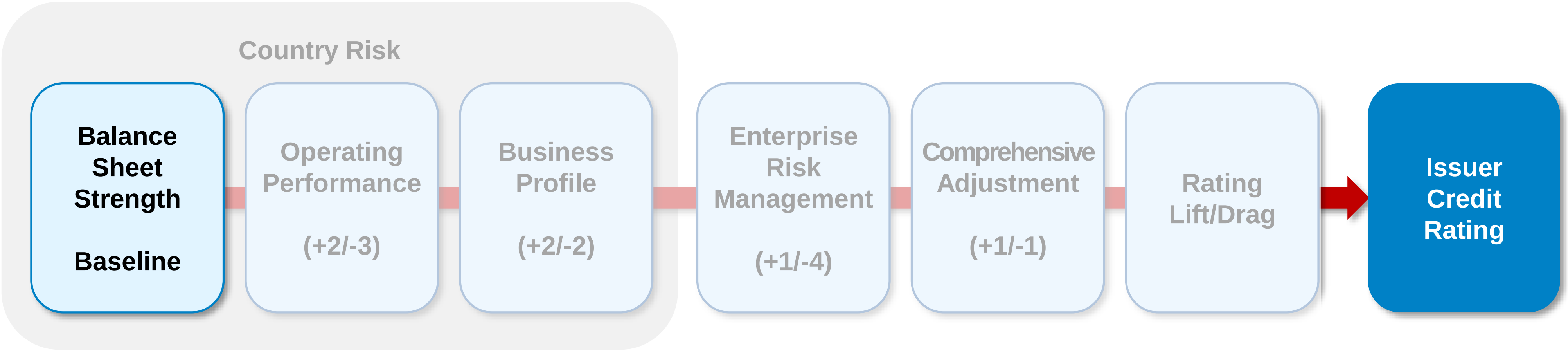
Comprehensive Quantitative Tool

- Evaluates many of the risks to the insurer's balance sheet simultaneously
- Generates an overall estimate of the required level of capital needed to support those risks
- Compares required capital with available capital

Assessment of Balance Sheet Strength

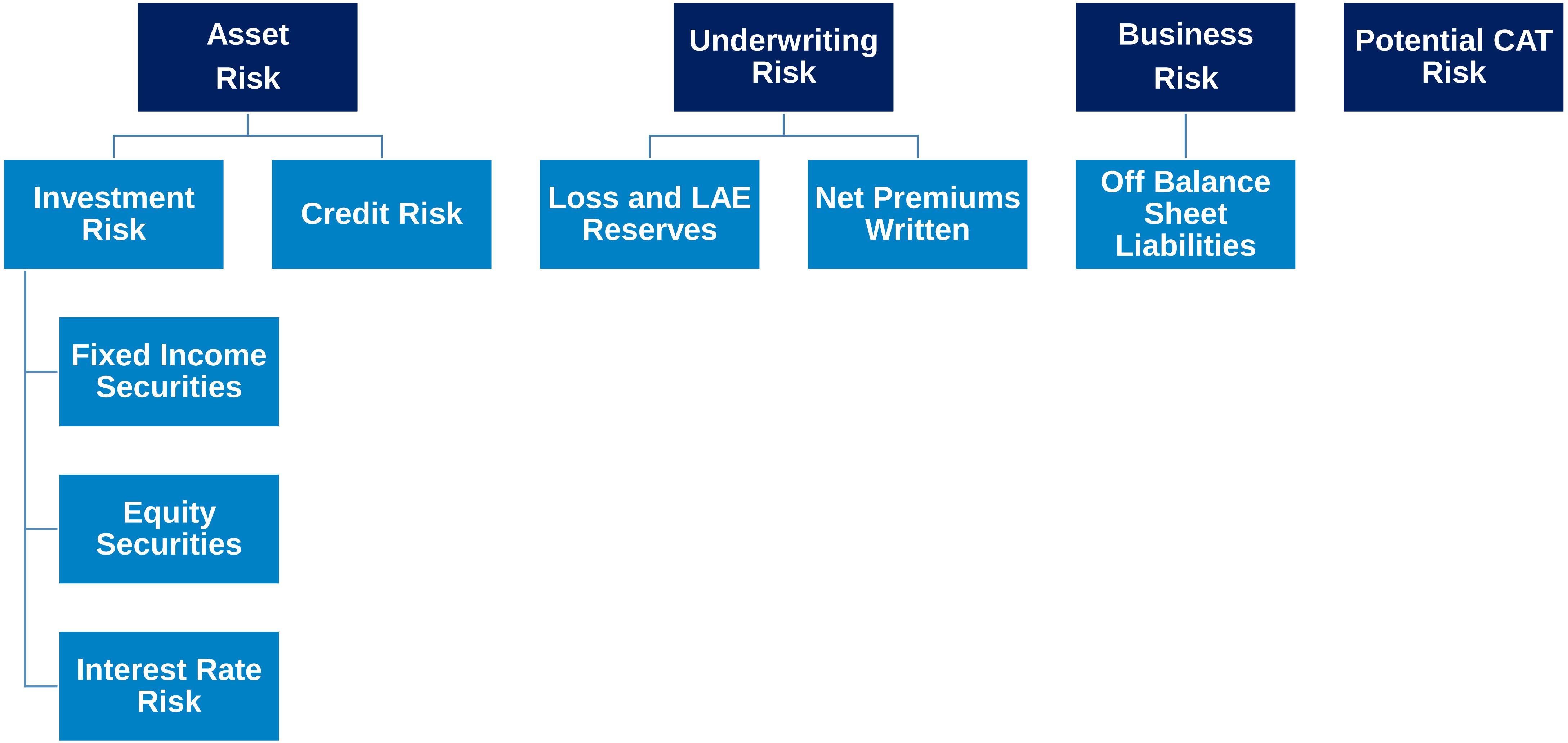
- Key tool in balance sheet strength assessment of insurer
- Not the sole determinant of balance sheet strength
- Not the sole determinant of the rating

BCRM: Building Blocks: Balance Sheet Strength



Balance Sheet Strength Components	
• BCAR	• Quality of Capital
• Stress Tests	• Quality of Reinsurance
• Liquidity	• Reinsurance Dependence
• Asset Liability Management	• Appropriateness of Reinsurance Program
• Internal Capital Models	• Financial Flexibility

What Risks Does BCAR Capture?



BCAR Formula

$$\text{BCAR} = \frac{(\text{Available Capital} - \text{Net Required Capital})}{\text{Available Capital}} \times 100$$

What is <u>Available</u> Capital?

The amount of assets in excess of liabilities that the insurer has <u>available</u> to absorb adverse financial outcomes. While subtle differences, also referred to as: Surplus, Book Value, or Equity

What is <u>Required</u> Capital?

A point in time estimate of the amount of capital <u>needed</u> to absorb adverse financial outcomes on the ultimate existing liabilities and the ultimate liabilities associated with writing one more year's worth of business.

US P/C BCAR

BCAR = (Available Capital – Net Required Capital) / Available Capital x 100

Available Capital (AC)	Net Required Capital
Reported Capital (PHS)	Gross Required Capital (GRC):
Equity Adjustments:	(B1) Fixed Income Securities
Unearned Premiums (DAC)	(B2) Equity Securities
Assets	(B3) Interest Rate
Loss Reserves	(B4) Credit
Reinsurance	(B5) Loss and LAE Reserves
Equalization/Contingency Reserves	(B6) Net Premiums Written
Debt Adjustments:	(B7) Business Risk
Surplus Notes	(B8) Potential Catastrophe Loss
Debt Service Requirements	
Other Adjustments:	Covariance Adjustment
Future Operating Losses	
Goodwill & Intangible Assets	Net Required Capital (NRC)*
Other	

$*NRC = SQRT\ [\ (B1)^2+(B2)^2+(B3)^2+(0.5*B4)^2\ +[(0.5*B4)+B5)]^2+(B6)^2\ +\ (B8)^2]\ \ +B7$

BCAR in AM Best's Rating Process

BCARs using VaR 95%, 99%, 99.5%, & 99.6%

BCAR using VaR 99.8%

- **Balance Sheet Strength** – Baseline
- **Operating Performance** – (+2/-3)
- **Business Profile** – (+2/-2)
- **Enterprise Risk Management** – (+1/-4)
- **Comprehensive Adjustment** – (+1/-1)
- **Rating Lift/Drag**
- **Issuer Credit Rating**

Balance Sheet Strength Components	
• BCAR	• Quality of Capital
• Stress Tests	• Quality of Reinsurance
• Liquidity	• Reinsurance Dependence
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Application of BCAR

Calculation	VaR 95	VaR 99	VaR 99.5	VaR 99.6	VaR 99.8
a. Available Capital =	3300	3300	3300	3300	3300
b. Net Required Capital (including Cat Losses) =	1529	2071	2481	2690	3667
BCAR = (a - b) / (a) =	53.7	37.2	24.8	18.5	-11.1
	For BCAR Assessment				For ERM

Notes: Available Capital is the same at each confidence level.

Net Required Capital increases as confidence level increases.

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**

2025 Market Outlooks

Anthony Diodato – Managing Director, AM Best
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Agenda

Overview and Definition of Outlooks

Global Reinsurance

Property & Casualty

Life/Annuity

AM Best Market Segment Outlooks

- Our market segment outlooks examine the impact of current trends on companies operating in particular segments of the insurance industry over the next 12 months.

- Outlooks consider:

  - Current and forecasted economic conditions

  - Regulatory environment

  - Lines of business developments: rates, terms & conditions, loss development

  - Competitive issues

- Outlooks can be Positive, Negative or Stable

- Market segment outlooks not directly connected to rating outlooks

AM Best’s Market Segment Outlooks – Definition

- A **Positive market segment outlook** indicates that AM Best expects market trends to have a positive influence on companies operating in the market over the next 12 months. However, a Positive outlook for a particular market segment does *not* mean that the outlook for all the companies operating in that market segment will be Positive.

- A **Negative market segment outlook** indicates that AM Best expects market trends to have a negative influence on companies operating in the market over the next 12 months. However, a Negative outlook for a particular market segment does *not* mean that the outlook for all the companies operating in that market segment will be Negative.

- A **Stable market segment outlook** indicates that AM Best expects market trends to have a neutral influence on companies operating in that market segment over the next 12 months.

Global Reinsurance

AM Best’s 2024 Market Segment Outlook – Global Non-Life Reinsurance

Outlook – Revised to Positive

- Not just re-pricing but de-risking
- Sustainable underwriting margins
- Capital protection instead of earnings stabilisers
- No capital depletion
- Claims activity driven by secondary perils, strong demand
- Investor pressure behind underwriting discipline for longer

AM BEST SINCE 1899 — BEST’S MARKET SEGMENT REPORT

Our Insight, Your Advantage™

June 12, 2024

Market Segment Outlook: Global Non-Life Reinsurance

The outlook is moving to Positive from Stable, as reinsurers continue to reap the benefits of higher interest rates

AM Best is revising its outlook for the global non-life reinsurance segment to Positive from Stable, driven primarily by the following factors:

- Improved property reinsurance margins, driven by increased rates and attachment points achieved in 2023. These conditions are unlikely to soften through the 2024 cycle.
- More robust investment income, driven primarily by higher new money yields on fixed-income instruments. A slower drop in rates than originally anticipated should support returns over the short term.
- The segment remains well capitalized, with no new players expected to disrupt current market discipline. Consolidation and a flight to quality are more likely.
- Demand for coverage remains high due to elevated loss frequency in property lines and general economic uncertainty.
- Adverse development reported on US casualty business has been mitigated by strong underwriting gains and redundant property reserves.
- Top performers have been able to raise capital to support growth initiatives.

Margins Continue To Improve; Property Cat Risk Realigns with Primary Carriers

In 2023, non-life reinsurers reported their most favorable year of the past five. The realignment of attachment points in the property reinsurance market allowed reinsurers to limit their losses throughout the year, despite active weather patterns. When combined with healthy increases to rate-on-line, the result was an underwriting margin that hasn’t been realized since 2014.

Recently improved and stabilized underwriting margins followed a string of disappointing results in the years after heavy weather-related losses in 2017 (due to Hurricanes Harvey, Irma, and Maria, among other events). Repricing efforts were compounded by actions aimed at tightening

Drivers

De-risking

- Realignment of interests
- Shift away from high-frequency layers
- Tighter terms and conditions

Robust Capitalisation

- Hard pricing to last longer
- More efficient capital management
- No capital depletion

No New Class of 2024

- No new company formations despite attractive pricing
- Capital used for opportunistic use or in ILS

Demand for Complex Risk

- Cedents looking to restore risk transfer
- Emerging risks, cyber and AI challenging risk transfer

Role of Interest Rates

- Impact on cost of capital and investment returns

AM Best's Expectations – The Next 12 months

Underwriting profits –
slight reductions, but still strong

Closely monitoring casualty lines Inflationary pressures (economic and social)

Rate movements –
modest declines in strong performing risks and higher levels of cover

Significant new (disruptive) capital unlikely

Retention levels –
minor movements into working layers

Increased use of Alternative Capital to flex capital needs

Property & Casualty

Property & Casualty Snapshot

- Industry reported significantly improved net underwriting results through first nine month of 2024
- Premium growth driven by aggressive push for more adequate rates
- Direct loss ratio was 5.4 percentage points better than 2023
- Improvement in results is primarily attributable to the personal lines segment
- Homeowners/farmowners improved by 13.3 points and private passenger auto by 9.7 points
- Homeowners/farmowners & private passenger auto lines account for ~50% of P&C industry direct premiums written

First Look: 9-Months of 2024 US Property & Casualty Financial Results

First Look: US P&C 9-Month Indicators and Combined Ratio Components

- $4.1B net underwriting gain
- UW gain primarily driven by the improvement in the personal lines segment
- Growth in net premiums primarily driven by rate increases
- 22.1% increase in net investment income drove pre-tax operating income – higher interest rate environment
- Realized gains of $76.7B
- Net income doubled from prior year to $130B
- Loss ratio & combined ratio improvement by 5-6 points

US Property/Casualty – 9-Month Financial Indicators and Combined Ratio Components

Financial Indicators	9-Months 2023	9-Months 2024	Year/Year Change (%)
Net Premiums Written	637.2	691.2	8.5
Net Premiums Earned	595.5	652.1	9.5
Losses & LAE	468.4	474.4	1.3
Underwriting Expenses	157.3	171.7	9.2
Policyholder Dividends	2.0	1.9	-4.3
Underwriting Income/(Loss)	-32.1	4.1	NM
Net Investment Income	49.5	60.5	22.1
Pretax Operating Income/(Loss)	18.2	65.9	261.7
Realized Capital Gains/(Losses)	51.7	76.7	48.4
Federal Income Taxes	5.5	12.7	130.0
Net Income	64.4	130.0	101.8
Combined Ratio Components			**Year/Year Change (Points)**
Pure Loss Ratio	68.8	63.3	-5.5
Loss Adjustment Expense (LAE) Ratio	9.8	9.4	-0.4
Loss & LAE Ratio	78.6	72.8	-5.9
Underwriting Expense Ratio	24.7	24.8	0.2
Policyholder Dividend Ratio	0.3	0.3	0.0
Combined Ratio (Reported)	103.7	97.9	-5.8
Less: Accident Year Catastrophe Losses (Points)1	10.0	8.8	-1.2
Less: A&E Losses (Points)	0.2	0.1	0.0
CORE Adverse/(Favorable) Development (Points)	-0.4	-1.5	-1.0
Combined Ratio (Normalized)	93.4	88.9	-4.5
Accident-Year Combined Ratio (Reported)	103.9	99.2	-4.7
Accident-Year Combined Ratio (Normalized)	93.8	90.4	-3.5

$ billions

Note: Figures may not add due to rounding. Data as of November 25, 2024.
NM = not meaningful..
* A Catastrophe loss is defined as an industry event that causes $25 million or more in insured losses. Source: AM Best data and research

First Look: US P&C 9-Month Policyholders’ Surplus

- Industry surplus increased to $1.1T
- Surplus growth driven by net income of $130B
- Stockholder dividends down 83.9% due to the distribution by one large reinsurer in the prior year period.

US Property/Casualty – Policyholders’ Surplus

	9-Months 2023	9-Months 2024	Year/Year Change (%)
Prior Year End Policyholders' Surplus	957.6	1,016.9	6.2
Net Income	64.4	130.0	101.8
Unrealized Capital Gains/(Losses)	23.8	-11.6	NM
Contributed Capital	1.4	1.4	5.6
Stockholder Dividends	-95.9	-15.4	-83.9
Other Changes	2.4	-1.4	NM
Ending Policyholders’ Surplus	953.6	1,120.0	17.4
Change in PHS from Prior Year End ($)	-3.9	103.0	
Change in PHS from Prior Year End (%)	-0.4	10.1	
After Tax Return on Surplus (ROE)	6.8	11.6	

$ billions

Note: Figures may not add due to rounding.
Data as of November 25, 2024.
Source: AM Best data and research

Personal Lines

US Personal Lines Segment Outlook

)ecember 2, 2024

Market Segment Outlook: US Personal Lines

'he outlook for he personal lines ;egment improves o Stable owing to mproved rate and ›ricing conditions, ›articularly in he auto space, ıs well as solid isk-adjusted :apitalization, ımong other actors

AM Best's outlook for the US personal lines segment has been revised to Stable from Negative, in line with a corresponding change in the personal auto outlook to Stable from Negative. In March 2024, the outlook for the homeowners line remained at Negative. The revised outlook reflects the following factors:

- An aggressive push for rate and improved pricing segmentation has led to improved underwriting performance, particularly for personal auto writers
- More accommodating regulatory treatment of rate requests
- Solid risk-adjusted capitalization with sufficient liquidity
- Rising investment yields as lower-yielding bonds mature and are reinvested at higher rates
- Accelerated technology adoption
- Improving catastrophe risk management practices

Factors counterbalancing these positives include the following;

- Ongoing volatility in reported results, particularly for the homeowners line of business
- Elevated loss cost severity owing to inflation and more expensive parts in newer vehicles
- Heightened severe weather activity
- Elevated reinsurance costs and tightened terms and conditions, including higher overall retentions and co-participation on property lines, driving higher net losses

Market Segment Outlook – Personal Lines

AM Best revised the outlook to Stable from Negative for the US Personal Lines segment based on the following factors:

- Improved personal auto underwriting performance driven by aggressive push for rate and more granular pricing segmentation
- More accommodating regulatory treatment of rate increases
- Solid risk-adjusted capitalization with sufficient liquidity
- Accelerated technology adoption
- Rising investment yields as lower-yielding bonds mature and are reinvested at higher rates
- Improving catastrophe risk management practices – refined risk appetites & underwriting guidelines

Market Segment Outlook – Personal Lines

Factors countering these positives include the following:

- Ongoing volatility in reported results, particularly for the homeowners line of business
- Continued heightened severe weather activity
- Higher loss cost severity owing to macro-economic inflation including labor and materials as well as more expensive parts in newer, more sophisticated vehicles
- Elevated reinsurance costs and tightened terms and conditions; higher overall retentions and co-participations on property lines; driving higher net losses for primary companies

Commercial Lines

US Commercial Lines Segment Outlook

December 2, 2024

Market Segment Outlook: US Commercial Lines

The segment's outlook remains at Stable, owing to strong underwriting performance, improved investment returns, countered by social inflation and rising climate risk

AM Best is maintaining its outlook for the US commercial lines segment at Stable, supported by the following key factors:

- Persistently strong underwriting performance for the US commercial lines segment, despite substantial economic and capital market volatility
- Sustained risk-adjusted pricing strength for most classes of business and moderating inflation
- Improved investment returns, which have bolstered operating profitability, especially in longer-tailed casualty lines
- Adequate and stable reserves, although certain lines of businesses continue to develop adversely
- Discipline about risk selection, terms and conditions, and capacity deployment, as evidenced in part by the continuation of strong submission flow and sustained growth in the non-admitted/excess and surplus lines (E&S) market

Near-term concerns include the following:

- Elevated casualty claims, reflecting the multi-year impact of social inflation, with adverse implications for underwriting and reserve margins
- Relatively high property claims costs, despite significant moderation in inflationary pressures
- Escalating geo-political risks and near-term policy uncertainty following the US elections

Market Segment Outlook – Commercial Lines

AM Best is maintaining its Stable outlook for the US Commercial Lines segment, based on the following factors:

- Persistently strong underwriting performance for the US commercial lines segment, despite substantial economic and capital market volatility
- Sustained risk-adjusted pricing strength for most classes of business and moderating inflation
- Improved investment returns which have bolstered operating profitability, especially in longer-tailed casualty lines
- Adequate and stable reserves, although certain lines of business continue to develop adversely
- Discipline around risk selection, terms and conditions, and capacity deployment, as evidenced in part by the continuation of strong submission flow and sustained growth in the non-admitted/excess and surplus lines (E&S) market
- Stable Outlooks for Workers Comp, Commercial Property / Positive Outlook for E&S

Market Segment Outlook – Commercial Lines

Factors countering these positive considerations include the following:

- Elevated casualty claims, reflecting the multi-year impact of social inflation, with adverse implications for underwriting and reserve margins
- Relatively high property claims costs, despite significant moderation in inflationary pressures
- Escalating geo-political risks & near-term policy uncertainty following the US elections
- Negative Outlooks for General Liability, Commercial Auto, D&O

Life & Annuity

Life Annuity Segment – Underpinning of Outlook

Maintain stable outlook

- Strong capital
- Strong top line
  - Fixed and RILA record sales
- Strong bottom line

December 3, 2024

Market Segment Outlook: US Life/Annuity Insurance

AM Best is maintaining its Stable outlook owing to strong capitalization industry-wide, top-line growth in most core lines, and consistent profitability

AM Best is maintaining its Stable outlook for the life/annuity segment, supported by the following key factors:

- Strong capitalization across the industry
- Top-line growth in most core lines of business
- Consistent profitability

Factors offsetting these tailwinds include the following:

- Increased allocations to higher risk assets
- Potential for further lowering of rates
- Ongoing drag of legacy liabilities

The Stable outlook for the US L/A segment is supported by strong capitalization across the industry robust top line growth in core lines of business, and consistent profitability. As in 2023, the overall L/A segment is strongly capitalized, with most companies maintaining more than adequate risk-adjusted capitalization. Top-line trends continue to be bolstered by favorable interest rates, resulting

Life Annuity Segment – Driver of strong Sales

Annuity sales drivers

- Aging population
- After low for long, higher rates improve margins
- Market volatility

Impacts

- Innovation of product
- Expense efficiency
- Increased allocation to high risk assets

Life Annuity Segment – Headwinds and Summary

Headwinds

- Legacy liabilities
- Expected decline in rates
- Risk management

Summary

- Medium term – expect profitability
- Expect individual annuity sales to continue
- Segment will maintain liquidity and capital

Life Annuity Segment – First 9-Months of 2024

- Capital and Surplus up 1% from Year End 2023
- Premiums / considerations up 13.7%
- Investment income up 9.6%
- Expenses up 8.8%, driven by surrender benefit increase

US Life/Annuity – 9-Month Financial Indicators, 2023/2024

$ billions

Financial Indicators	9-Months 2023	9-Months 2024	Year/Year % Change
Premiums and Annuity Considerations	559.6	636.0	13.7
Net Investment Income	163.0	178.7	9.6
Amortization of Interest Maintenance Reserve	0.5	-0.1	NM
Commissions and Expense Allowances - Ceded	29.1	24.3	-16.6
Other Income	49.7	5.1	-89.7
Total Income	802.0	844.1	5.3
Death Benefits	67.9	66.7	-1.7
Annuity Benefits	75.4	80.5	6.7
Surrender Benefits	301.4	364.4	20.9
Other Benefits	199.9	207.0	3.6
Total Incurred Benefits	644.6	718.6	11.5
Commissions and Expense Allowances - Direct & Assumed	56.8	59.2	4.1
General Insurance Expenses and Other	87.3	83.5	-4.4
Net Transfers to Separate Accounts	-58.7	-65.9	12.2
Dividends to Policyholders	16.5	17.0	3.5
Total Expenses	746.5	812.4	8.8
Pretax Net Operating Gain	55.5	31.6	-43.0
Federal and Foreign Taxes	10.2	7.2	-29.1
Net Operating Gain	45.3	24.4	-46.1
Net Realized Capital Gains/Losses	-14.2	-2.8	-80.5
Net Income	31.1	21.7	-30.5

Note: Percentages may not add up to 100 due to rounding.
Data as of December 4, 2024.
Source: AM Best data and research

Networking Break

AM Best's Insurance Market Briefing & Networking Reception – Cayman Islands
February 12, 2025

Proposed Changes to the Alternate Risk Transfer Criteria

Robert Raber – Senior Director, AM Best
Dan Teclaw – Director, AM Best

AM Best's Insurance Market Briefing & Networking Reception – Cayman Islands
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Agenda

Background for the proposed material revisions

Cell company focused revisions

General revisions

Public Comment process

Q&A

Background

Alternative Risk Transfer

- The Alternative Risk Transfer (ART) criteria is a specialty criteria used in conjunction with Best's Credit Rating Methodology (BCRM).
- Current version focuses on broad groupings of companies:
  - Single parent (and pure) captives
  - Group captives
  - Risk retention groups
  - Self-insurance funds
  - Protected cell companies
- The Criteria Team recognized the need for material revisions to the ART criteria
- Call for Comment period opened on December 2, 2024
- Allows industry participants and interested parties to provide comments on the proposed material revisions to the ART criteria

Alternative Risk Transfer

- Objectives of the proposed material revisions:
  - Broaden nomenclature to account for various cell entities
  - Establish a clear direct rating approach to assigning an ICR and an FSR to unincorporated cell companies and individual incorporated cell entities
  - Set operational and legal foundational requirements needed to assign ratings to unincorporated cell companies and individual incorporated cell entities
  - Current ART criteria established rating PCC’s only through the “weakest link” approach
  - Change criteria title: Rating Captives and Other Alternative Risk Transfer Entities
- Ratings Impact
  - Proposed revisions to ART are not expected to affect current rated entities

Cell Company Revisions

Alternative Risk Transfer

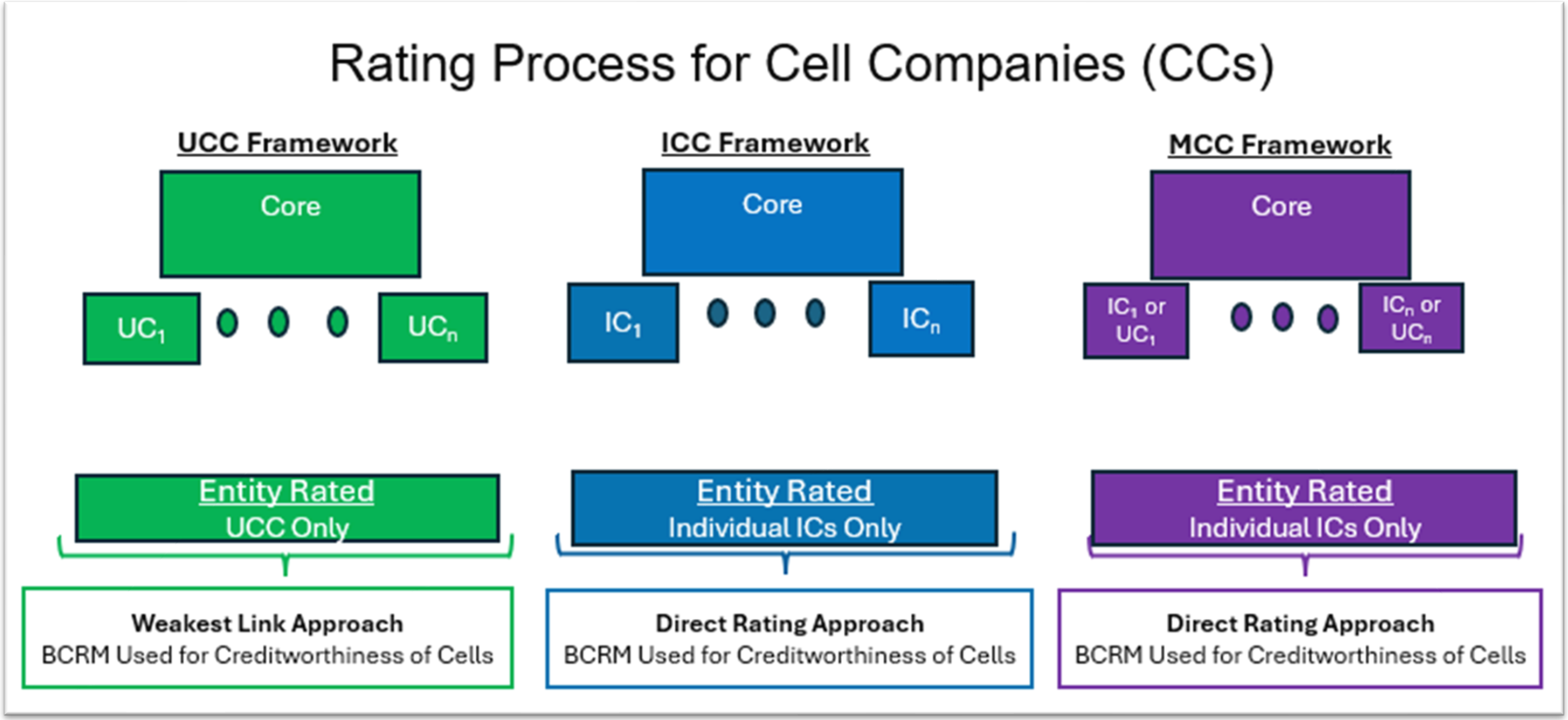
- Name and define cell companies and the various cell structures used in the market
  - Replace protected cell company (PCC) with a variety of terms to reflect market participants
    - Incorporated cell (IC)
    - Incorporated cell company (ICC)
    - Unincorporated cell (UC)
    - Unincorporated cell company (UCC)
    - Mixed cell company (MCC)

- An incorporated cell company (ICC) is a company composed of a number of individual cells, each of which is a separate incorporated legal entity. Each individual incorporated cell (IC) can hold its own insurance license, issue policies, and enter into transactions with third parties.

- An unincorporated cell company (UCC) is composed of a number of individual cells. In this case, only the UCC is an incorporated legal entity, and the individual unincorporated cells (UC) may not be considered separate legal entities. The individual UCs are unlikely to be independently licensed and therefore insurance policies are issued by the UCC on behalf of the individual UCs.

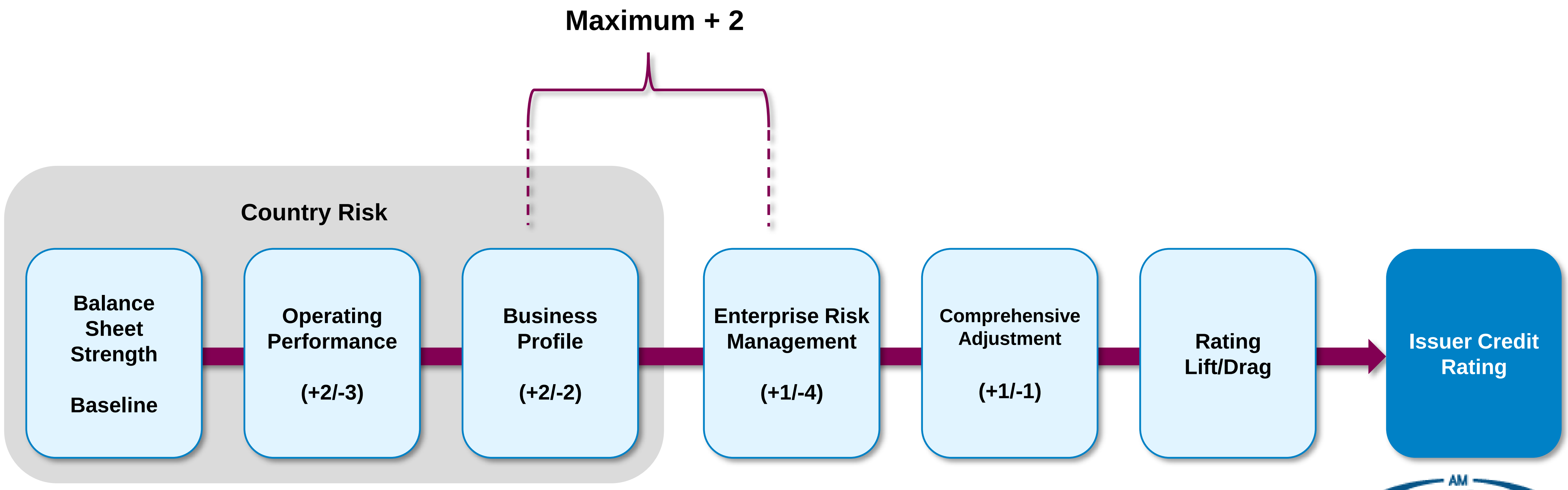
- A mixed cell company (MCC) is composed of both ICs and UCs.

Alternative Risk Transfer



Alternative Risk Transfer

- Map out specific factors for IC's which will support a path through BCRM to assign them ICRs and FSRs
  - Separation of assets and liabilities of an individual incorporated cell company from other cell entities and any core cell company



Alternative Risk Transfer

- Specific Building Block considerations:
- Balance Sheet Strength Assessment
  - Use combining financial statements to generate BCAR, or pseudo-BCARs for each individual cell
  - Distributions, capital quality, and capital management plans/history reviewed
  - Quarterly monitoring

- Operating Performance
  - Premium growth / utilization
  - Number and historical profitability of lines of business written
  - Feasibility studies

Alternative Risk Transfer

- Specific Building Block considerations:
- Business Profile
  - Product and geographic concentration across rated UCC or within rated IC
  - Management / sponsorship experience and quality overseeing CC platforms
  - TPA engagement and timeliness of reporting
  - Depth of domicile experience / activity supervising / overseeing these structures
- Enterprise Risk Management
  - Holistic view of risk appetite and tolerance across rated UCC or within rated IC
  - Risk management and controls of investments, capital distributions, collateral
  - Limits / retentions / PMLs / reinsurance arrangements reviews where appropriate
  - Ability / willingness of TPA to make capital calls prospectively or when necessary
  - Review domiciliary history legal cases testing separation of assets and liabilities

Alternative Risk Transfer

- Specific Building Block considerations:
- Lift / Drag
    - Ability and willingness of platform sponsor to infuse capital when appropriate to support claims
    - Consideration given to the notion that the platform sponsor may, in fact, be the policyholder
    - Similar to considerations for captives, materiality of size relative to overall corporate enterprise can have an impact in this assessment
    - CRA (credit rating agency) composite proxy used to inform quality of platform sponsor, when available

Alternative Risk Transfer

- Set a baseline operational level for individual incorporated cells to be considered for rating assignment
  - Authority granted to the IC by an insurance regulator to provide insurance contracts
- Establish that AM Best analytical teams will likely use external parties to aid in the confirmation of a cell entity’s baseline operational and legal capabilities
  - Outside counsel to ensure legal requirements are met
  - Third party actuarial firms to measure risk transfer mechanisms

Alternative Risk Transfer

- Affirm that the weakest link approach remains the path to an ICR and an FSR for unincorporated cell companies
  - Retain this approach as a pathway for UCC's to achieve a rating as only the UCC as a whole is an incorporated and licensed legal entity.

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

Alternative Risk Transfer

- Add an appendix supporting cell company data requests
  - Audited financial report for the CC and any ICs
  - Key documents and agreements
  - Business plan and formation documents
  - Licenses
  - (Re)insurance policies
  - Capital maintenance agreements and pooling agreements
  - Cell management agreements
  - Shareholder or subscription agreements
  - Any other agreements between the cells or between cells and the core
  - Gross and net PMLs for each cell

General Revisions

Alternative Risk Transfer

- Clarity in other areas affecting multiple entity structure types:
  - Letter of Credit
  - Parent / Holding Company Assessment
  - Operating Performance
  - Single Parent Captive - Business Profile and ERM
  - Exclude cells that issue structured finance instruments from obtaining an FSR
- Propose new criteria name “Rating Captives and Other Alternative Risk Transfer Entities”
  - Ensures focus of the criteria for its most frequent use – captive companies
  - Aligns with naming structure of other AM Best specialty criteria
- Proposed revisions to the criteria are not expected to affect current rated entities

Public Comment Process

Alternative Risk Transfer

- Public comment period is open until February 20, 2025

- Market participants in the insurance industry and other interested external parties may share their comments on the proposed material revisions with AM Best via an email function on the "Call for Comment" page on the AM Best website
  - AM Best Rating Services | Rating Methodology

- Commenters can select one of three options when submitting comments via email:
  - Allow comments to be made public and include contact information
  - Allow comments to be made public but to keep contact information anonymous
  - Do not publish my comments (confidential)

Q&A

At the Forefront: What AM Best is Currently Watching

Anthony Diodato – Managing Director, AM Best
Mike Porcelli – Senior Director, AM Best

AM Best's Insurance Market Briefing & Networking Reception – Cayman Islands
February 12, 2025

US Life & Annuity Outlook and Rating Trends

Market Segment Outlook – US Life & Annuity

AM Best is maintaining a Stable outlook for the US Life & Annuity segment, based on the following factors:

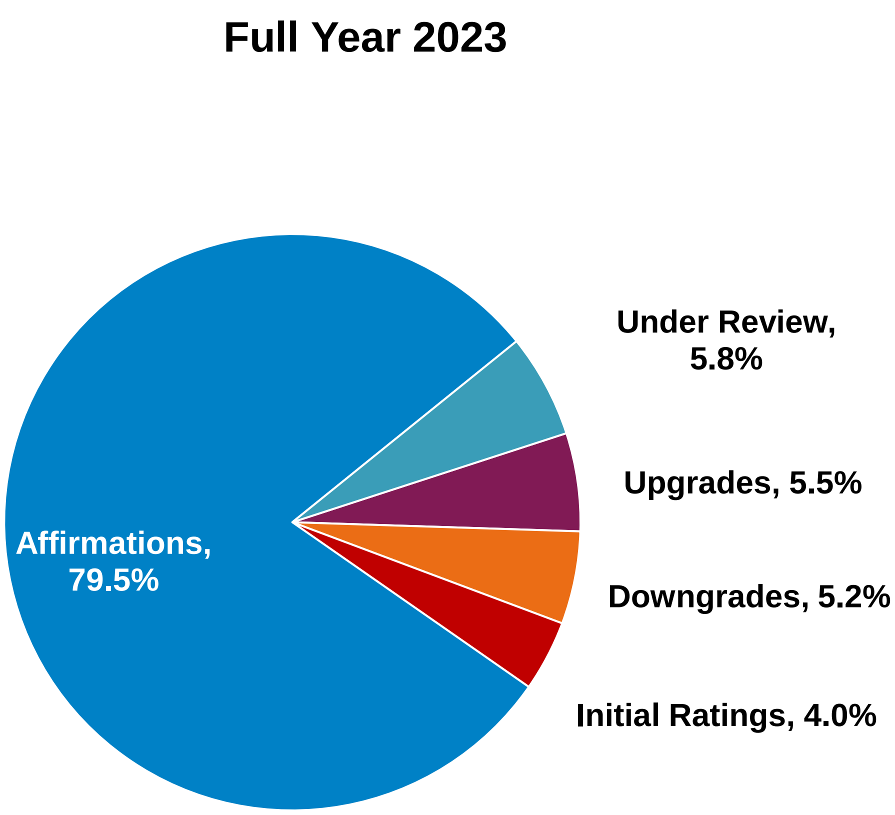
- Strong capitalization across the industry
- Top Line Growth in most core lines of business
- Consistent profitability

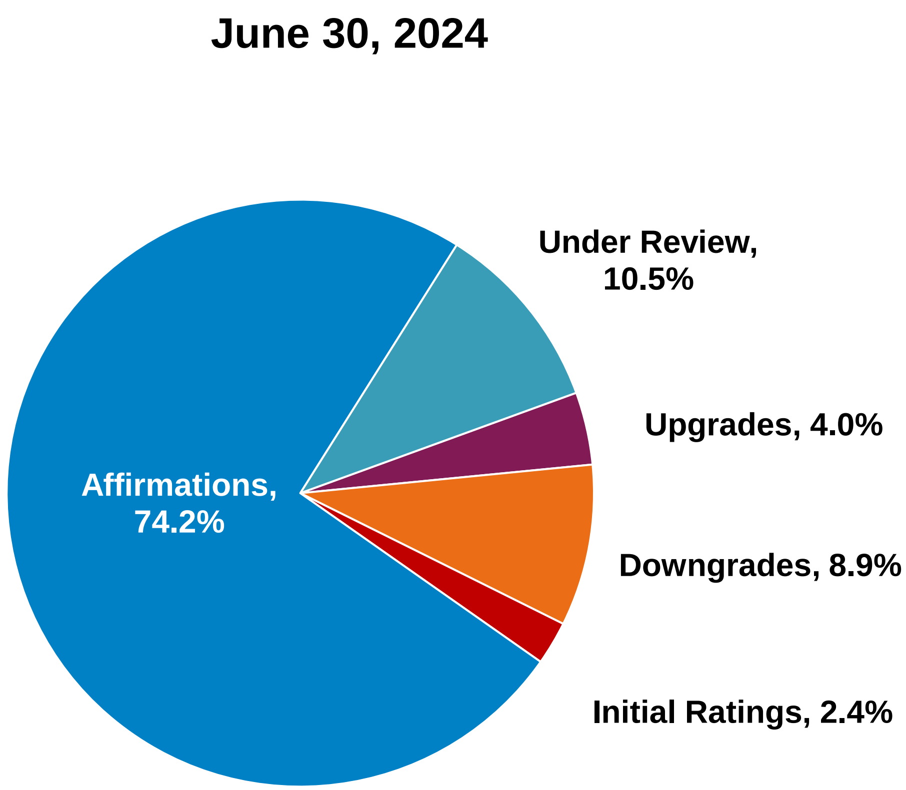
Market Segment Outlook – US Life & Annuity

Factors partially offsetting these positives include the following:

- Increased allocation to higher risk assets
- The potentially for further interest rate cuts
- Ongoing drag of legacy liabilities

Life/Health Issuer Credit Rating Activity





Observations on the Life & Annuity Business

Use of Reinsurance

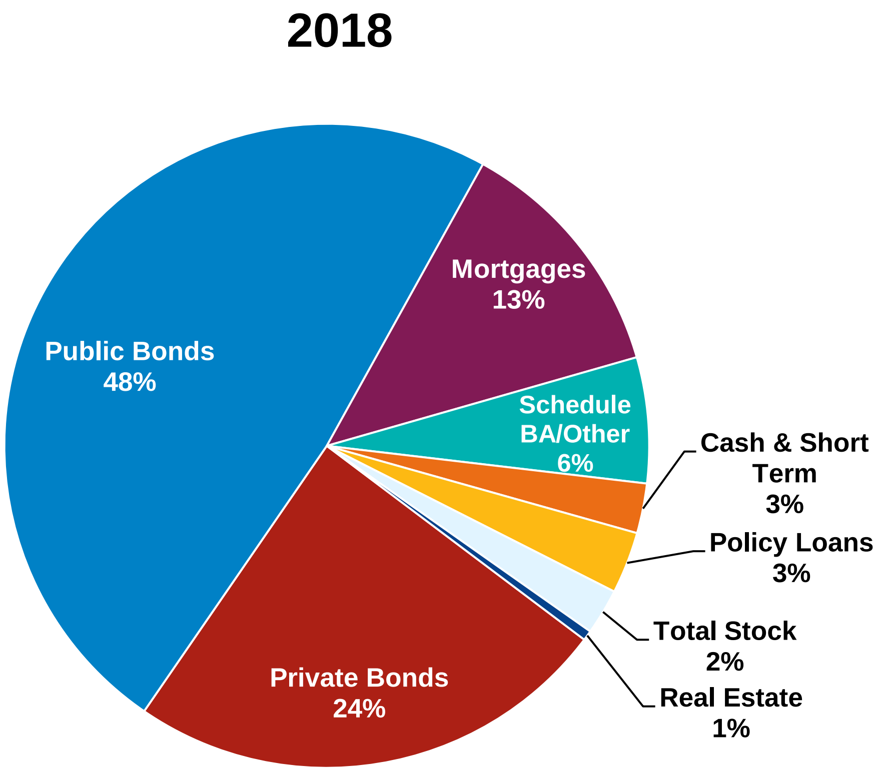
AM Best has seen an increase in the use of unrated or low-rated reinsurers to provide capital and capacity to some start up annuity writers

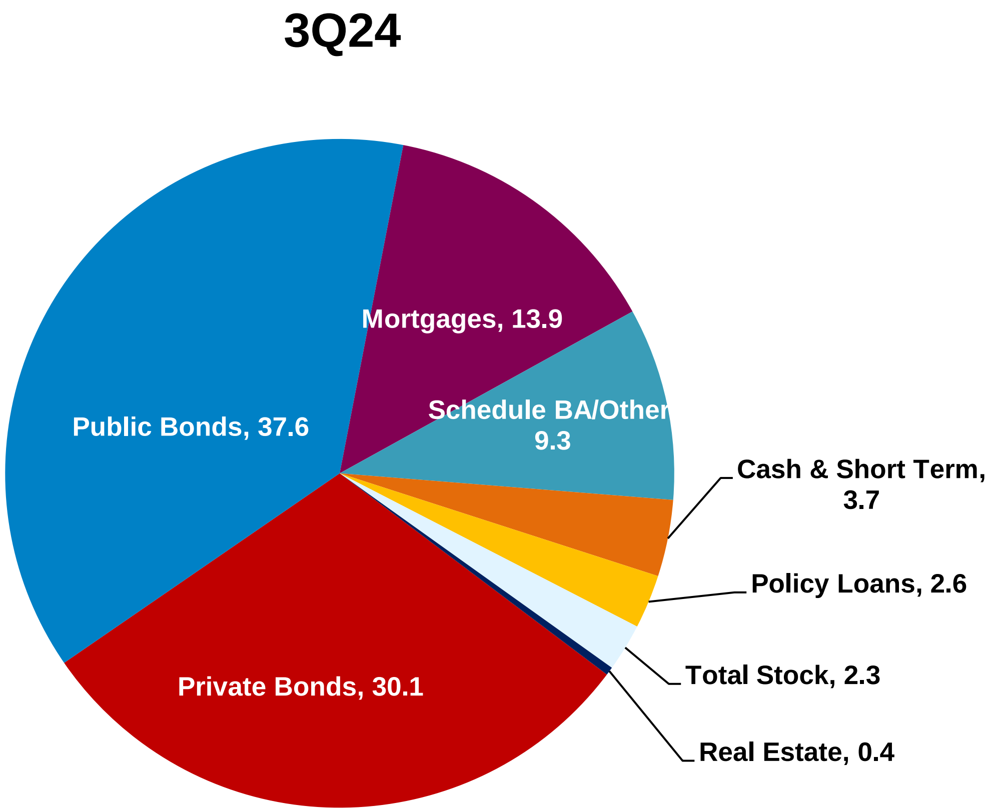
Lingering concerns about the source of capital and the understanding of the business

Affiliated investments have historically proven to be problematic

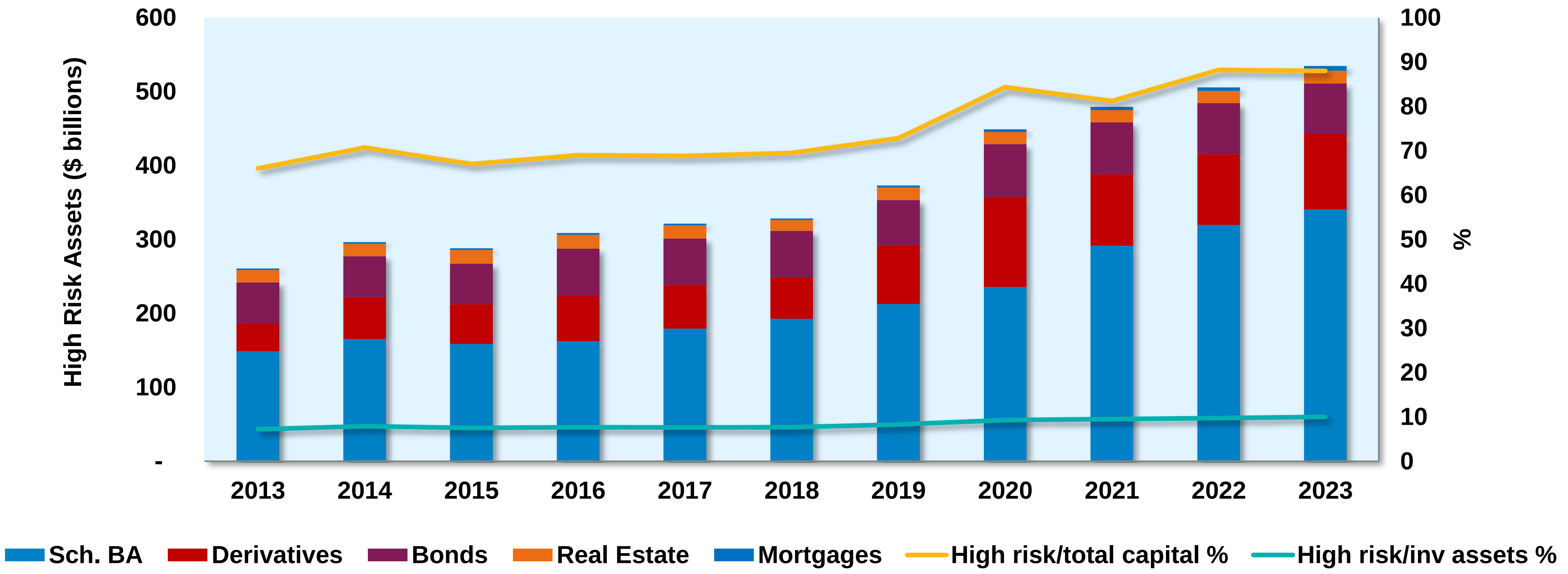
Increased focus on use of off-shore jurisdictions

Balance Sheet – Invested Assets

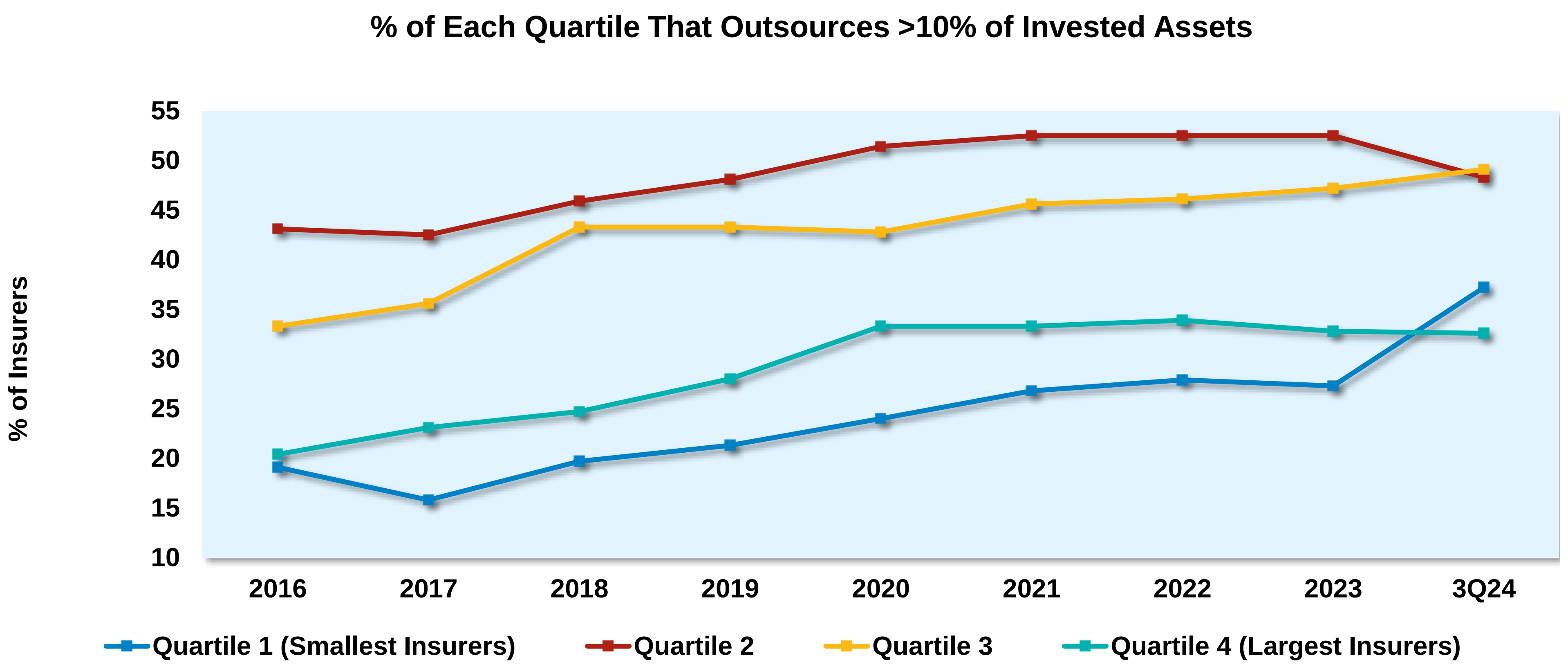




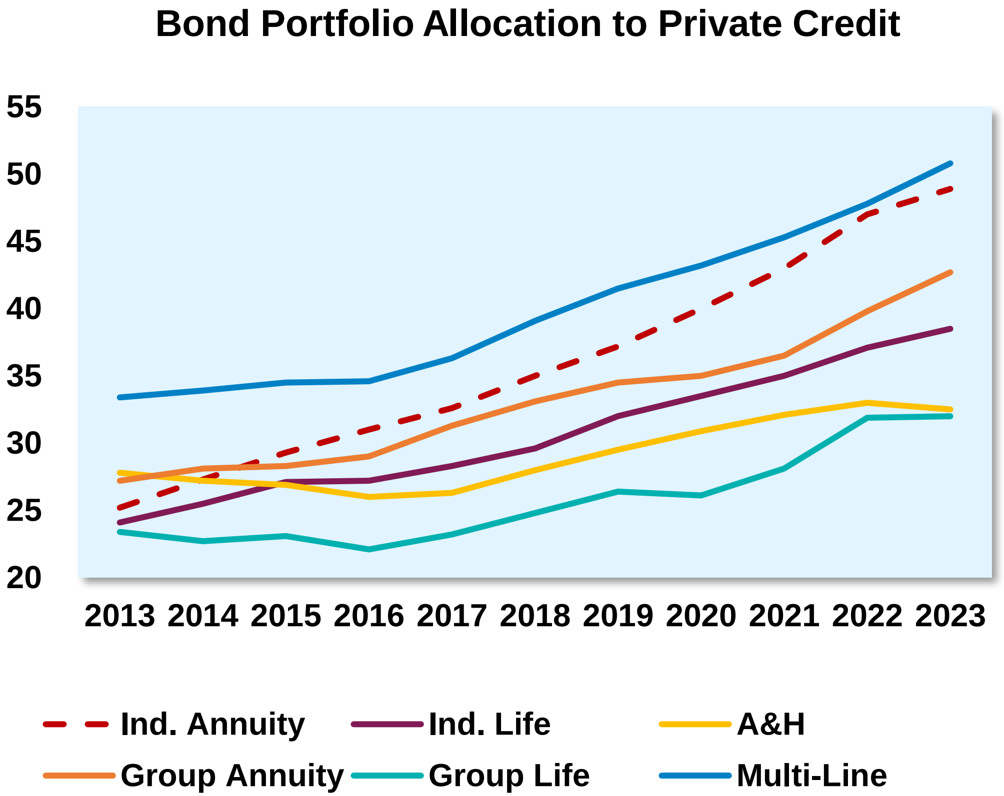
High-Risk Asset Exposure

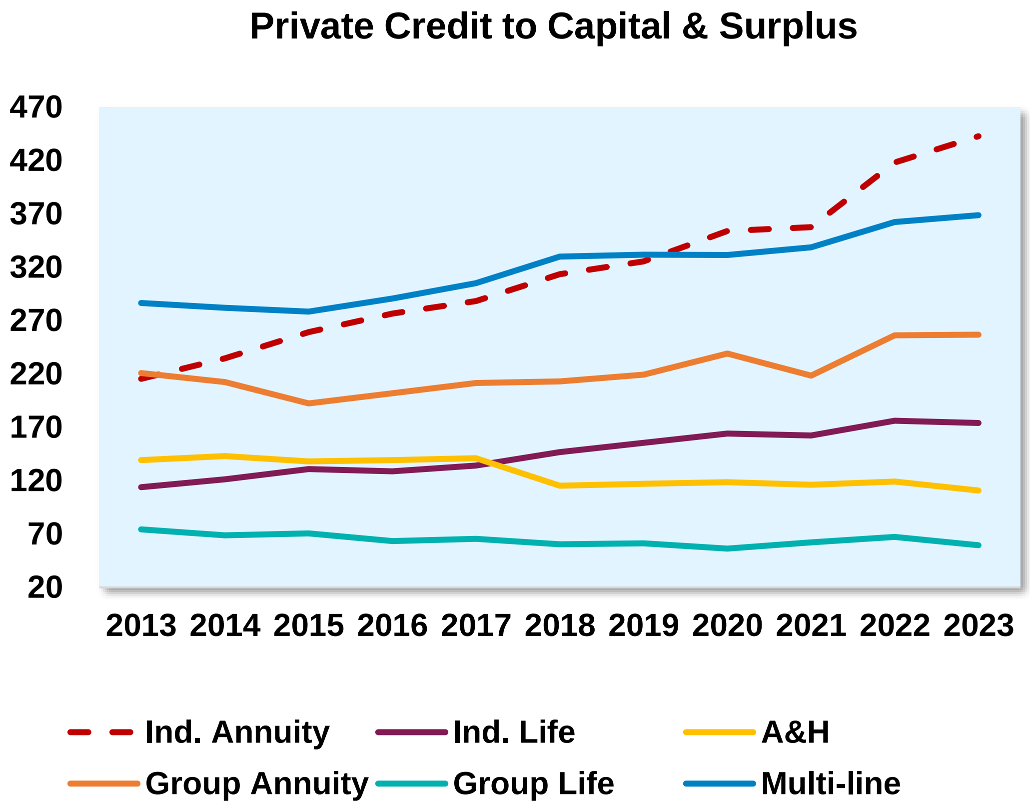


Companies of All Sizes Outsourcing More Assets to Third-Party Managers

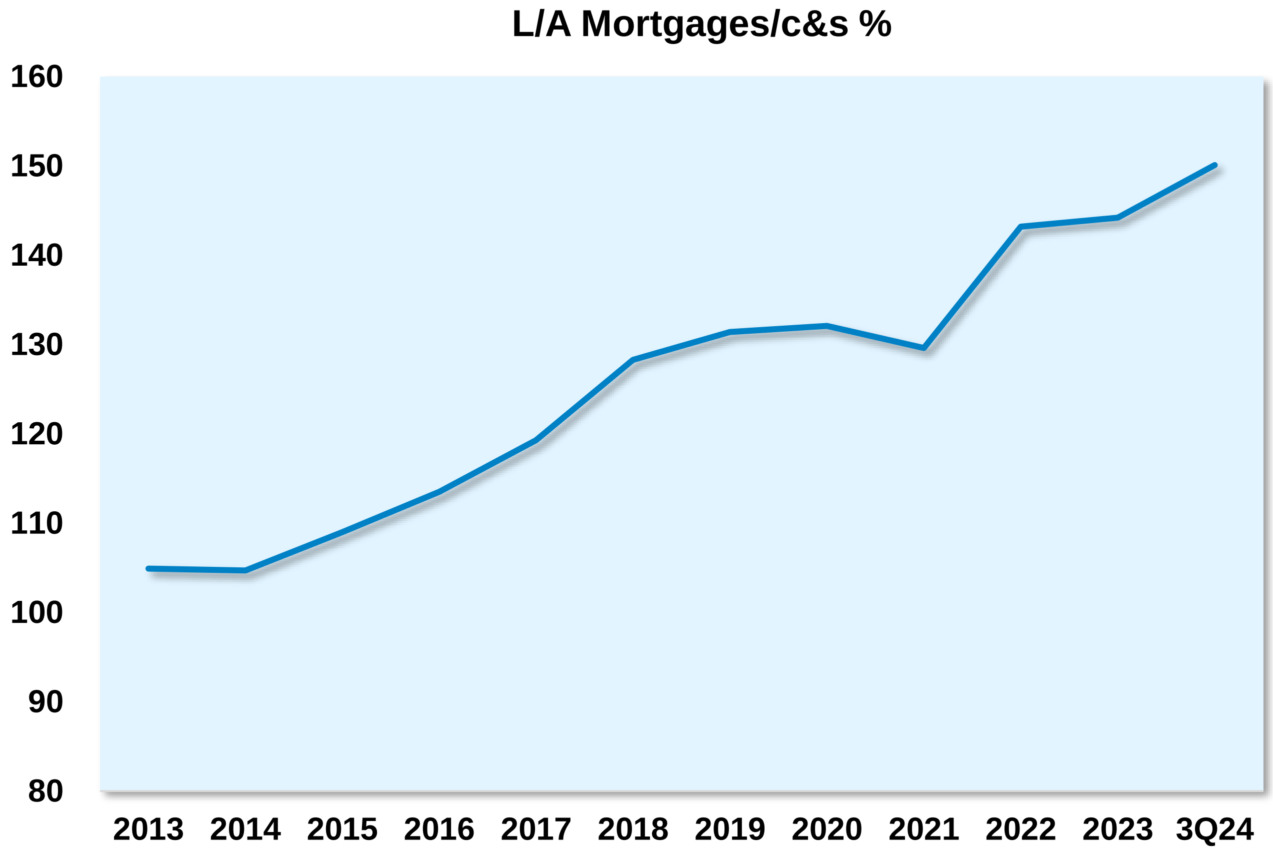


Private Credit becoming the Preferred Asset Class for Annuity Writers



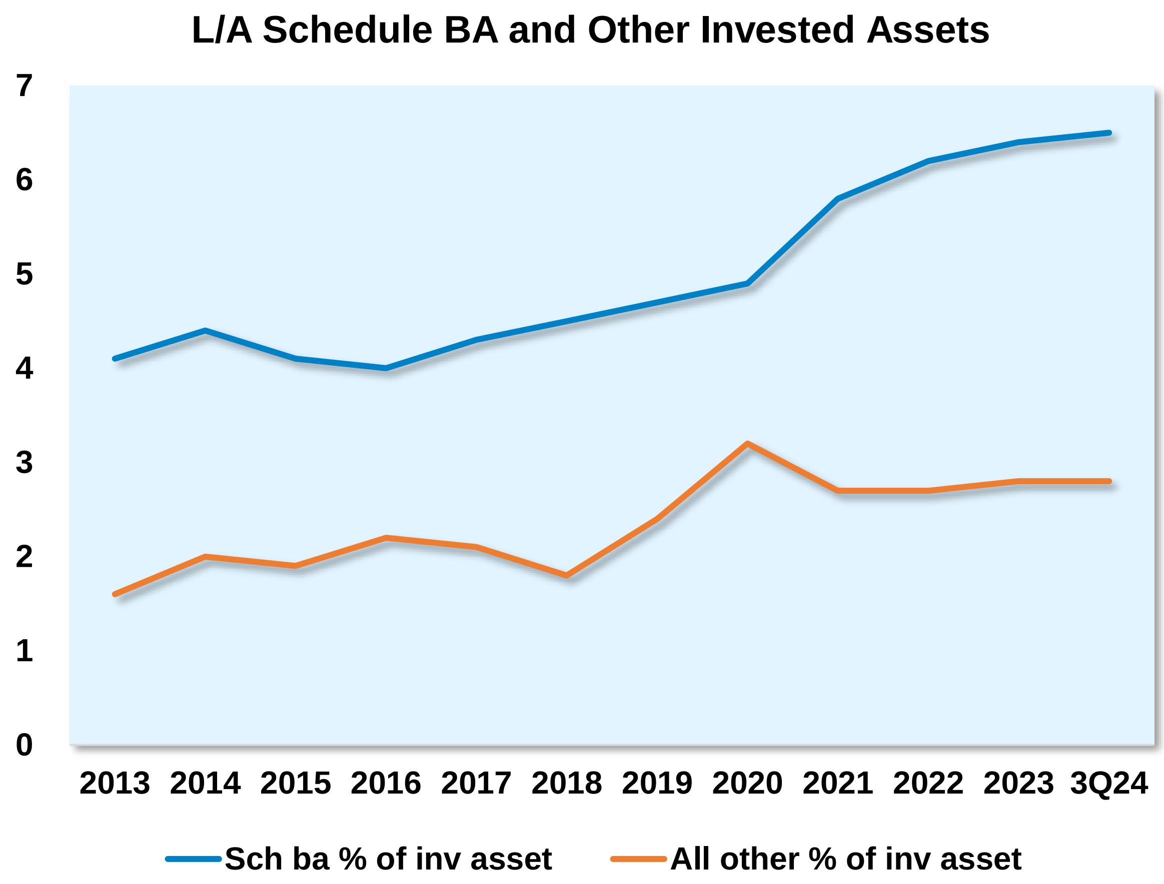


Mortgages



- L/A insurers increased investment in mortgage loans by more than 6% in 2023, with mortgages now representing 13.5% of invested assets

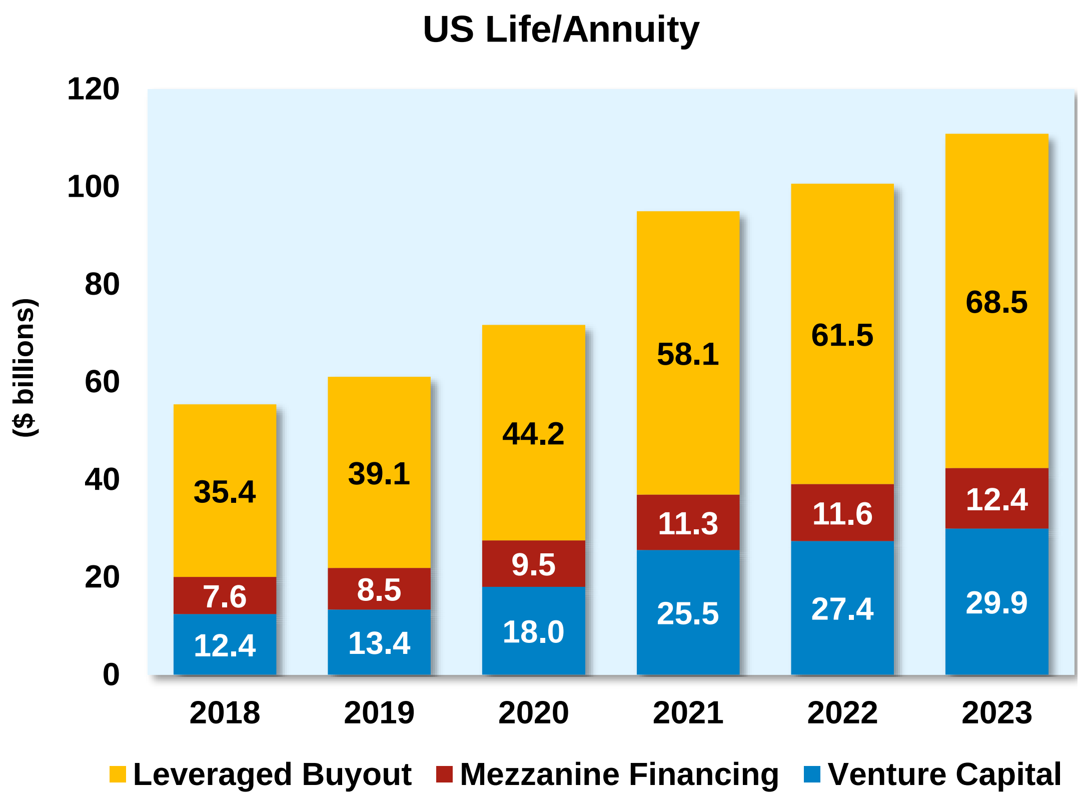
Schedule BA and Other Invested Assets



- Examples of Schedule BA assets include PE, hedge funds, real estate, equities, joint ventures, partnerships and LLCs
- Other invested assets are assets that generally do not fall into the categories of the other investment schedules (mostly Derivatives)
- These assets have increased from 6% of invested assets in 2013 to 9% in 2023

Schedule BA an Other Invested Assets

Private Equity Investments – Holdings by Type

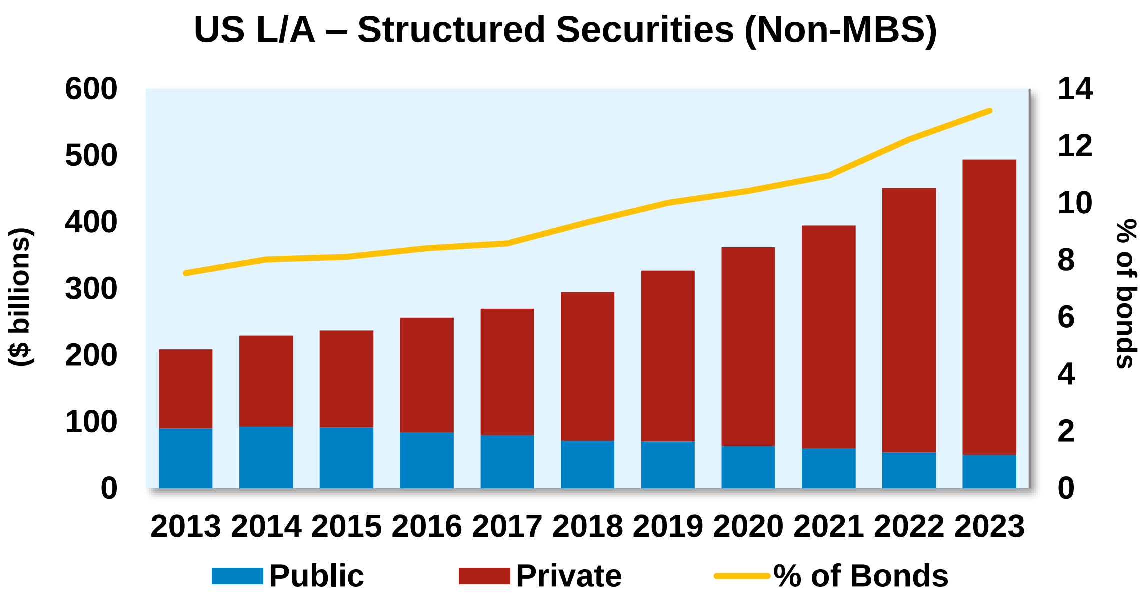


- Hedge funds have largely fallen out of favor with L/A insurers due to the unfavorable fee structures and capital charges

- Private equity continues to play a role within insurers' portfolios, with leveraged buyout funds representing the largest proportion of PE investments
  - LBO dealmaking has slowed in recent years and funds are facing pressure to return capital to investors

- These assets tend to provide yield enhancement and diversification

Structured Securities



Breakdown of Structured Securities (Non-MBS)

All Insurance Segments, %	2019	2023
CLOs	35.4	46.9
Other	28.9	28.3
Ind. Obligations	13.3	11.8
Lease Transactions	8.0	5.5
Corp. Obligations	4.9	4.8
Credit Tenant	5.8	2.4
Home Equity	3.5	0.2
Mobile Home Loans	0.1	0.1

- Securitized assets are becoming a larger portion of L/A insurers' bond portfolios, increasing from 7.5% in 2013 to 13.2% in 2023
  - This coincides with a decrease in government CMOs across the same period

- Increasing allocation CLOs, which are attractive in a rising rate environment due to their floating rates and attractive yields
  - May be less favorable with interest rates decreasing

Structured Securities

Credit Quality of Structured Securities (Non-MBS)

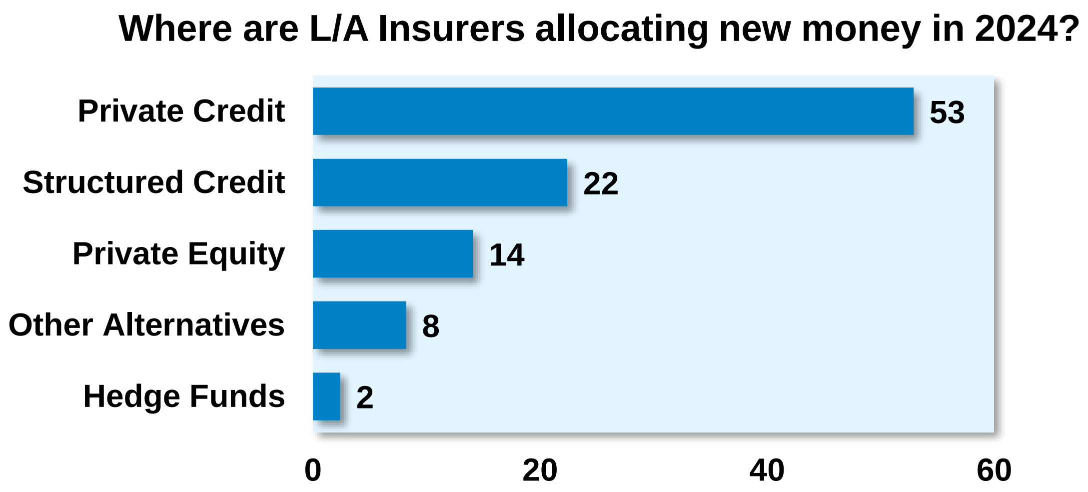
All Insurance Segments, %	CLOs	Other	Ind. Obligations
NAIC-1	83.6	72.9	92.2
NAIC-2	13.1	24.5	6.5
NAIC-3	2.8	1.7	0.9
NAIC-4	0.4	0.7	0.3
NAIC-5	0.0	0.2	0.0
NAIC-6	0.0	0.1	0.0

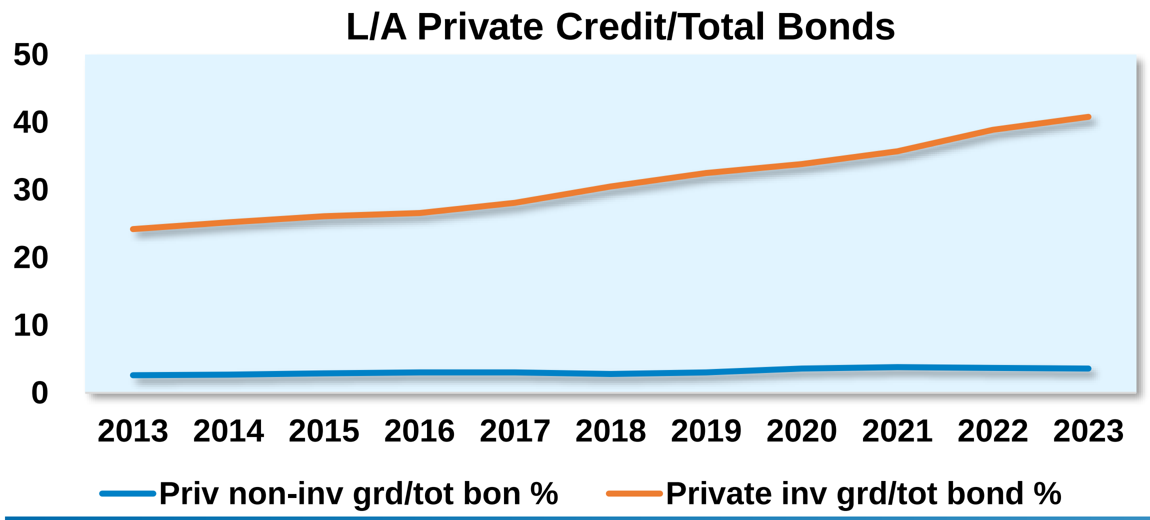
Credit Quality of Total Bonds

Life/Annuity 2023	Total Bonds
NAIC-1	59.1
NAIC-2	35.9
NAIC-3	3.1
NAIC-4	1.4
NAIC-5	0.5
NAIC-6	0.1

- Credit quality for these structured securities are higher than the credit quality of the average bond portfolio but tend to be lower than the agency MBS's that insurers invest in
- While credit quality for CLOs may be strong, prior AM Best research has shown that they may experience higher rates of OTTIs
- CLO holdings tend to be concentrated in larger insurers with greater capacity to analyze the underlying assets

Private Credit Overview





- Increasing interest among L/A insurers for private credit assets, citing desire to increase credit/illiquidity risk

- Private credit as a proportion of total bonds have steadily grown over past 10-year period

Median	Private Bonds	Public Bonds	All Bonds
Book/adjusted carrying value	5,306,021	2,000,000	2,173,022
Fair Value	4,992,852	1,896,351	2,036,461
Rate used to obtain fair value	94.40	95.08	95.00
Rate	3.63	3.30	3.38
Amount of interest received during year	199,864	69,988	78,522

Questions for Companies About Private Credit

- What goes into the underwriting process of your private credit portfolio?
- What is the collateral and type of private credit?
- How experienced is internal staff and external advisors in working with private credit and the type of private credit?
- Where do you see the risk in private credit vs public?
- How is fair value determined?
- What is your average fair value ranking? (i.e. level 1, 2, or 3 inputs)
- What goes into the monitoring process, the risk limit process and general risk management?

Questions for Companies About Private Credit

- What specific risk asset class do you focus on and why? Internal or external expertise? ALM?
- What does the monitoring process look like?
- How are you reaching or maintaining target allocations?
- How is illiquidity/credit/interest rate risk managed?
- How do capital market expectations impact allocations?

Where are the Assets?

- Where are the assets located?
- Are these assets on-shore? Off-shore? Is there use of captives?
- Who has discretion over the assets?
- How much third-party capital is involved or invested in pieces of the business? Is there use of side cars?

Thank You!

AM Best’s Insurance Market Briefing & Networking Reception – Cayman Islands

Closing Remarks

Brad Mazur– Managing Director, AM Best Rating Services

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