S&P Global Ratings:
Insurance Ratings History, Methodology and Process

NAIC/CIPR Webinar
October 14, 2016
Agenda

• S&P’s Ratings History in the Insurance Industry
• Global Insurance Ratings Coverage
• Ratings Process
• S&P Financial Strength Ratings Scale
• Insurance Ratings Framework
• Ratings Distribution

• Appendix
  • Capital Analysis
  • Ratings Performance
  • Assessment of Enterprise Risk Management
S&P Global Ratings’ Growing Insurance Presence

1860: Henry Varnum Poor’s “History of Railroads and Canals in the U.S.”

1916: Credit ratings on corporate bonds and sovereign debt

1941: Ratings on Municipal bonds

1971: Financial Strength Ratings on insurance companies

1993: Global Insurance Advanced Analytics team established
-- to assess complex risks such as insurance linked securitizations

2004: Global Enterprise Risk Management team formed
-- to assess risk management practices of complex issuers

2013: Insurance ratings criteria updated

Today: Strong global insurance analytics presence
-- in Asia, Europe, and South/Central/North America

Our insurance practice has grown globally in size and sophistication; our analytical team is further supported by specialists throughout S&P.
S&P Global Ratings’ Insurance Presence

FSR Ratings as of October 2016

- Canada
  - FSR: 36
- U.S. & Bermuda
  - FSR: 957
- LatAm & Caribbean
  - FSR: 87
- EMEA
  - FSR: 386
- Asia
  - FSR: 159
- Pacific
  - FSR: 72
1. Contract
The issuer requests a rating and signs an engagement letter.

2. Pre-evaluation
We assemble a team of analysts to review pertinent information.

3. Management Meeting
Analysts meet with management team to review and discuss information.

4. Analysis
Analysts evaluate information and propose the rating to a rating committee.

5. Rating Committee
The committee reviews the lead analyst’s rating recommendation and then votes on the credit rating.

6. Notification
We generally provide the issuer with a pre-publication rationale for its credit rating for fact-checking and accuracy purposes.

7. Publication
We typically publish a press release announcing the public rating and post the rating on www.standardandpoors.com.

8. Surveillance of Rated Issuers and Issues
# Our Insurer Financial Strength Rating Categories

<table>
<thead>
<tr>
<th>Rating</th>
<th>Description</th>
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<tbody>
<tr>
<td>AAA</td>
<td>Extremely strong financial security characteristics. Highest rating.</td>
</tr>
<tr>
<td>AA</td>
<td>Very strong financial security characteristics.</td>
</tr>
<tr>
<td>A</td>
<td>Strong financial security characteristics, but somewhat more likely to be affected by adverse business conditions than are insurers with higher ratings.</td>
</tr>
<tr>
<td>BBB</td>
<td>Good financial security characteristics, but more subject to adverse economic conditions.</td>
</tr>
<tr>
<td>BB; B; CCC; and CC</td>
<td>An insurer rated 'BB' or lower is regarded as having vulnerable characteristics that may outweigh its strengths. 'BB' indicates the least degree of vulnerability within the range, and 'CC' the highest.</td>
</tr>
<tr>
<td>BB</td>
<td>Marginal financial security characteristics. Positive attributes exist, but adverse business conditions could lead to insufficient ability to meet financial commitments.</td>
</tr>
<tr>
<td>B</td>
<td>Weak financial security characteristics. Adverse business conditions will likely impair its ability to meet financial commitments.</td>
</tr>
<tr>
<td>CCC</td>
<td>Very weak financial security characteristics; is dependent on favorable business conditions to meet financial commitments.</td>
</tr>
<tr>
<td>CC</td>
<td>Extremely weak financial security characteristics; is likely not to meet some of its financial commitments.</td>
</tr>
<tr>
<td>R</td>
<td>Under regulatory supervision owing to its financial condition.</td>
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<tr>
<td>D / SD</td>
<td>In default on one or more of its insurance policy obligations but is not under regulatory supervision that would involve a rating of 'R'.</td>
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An *S&P insurer financial strength rating (FSR)* is a forward-looking opinion about the financial security characteristics of an insurer with respect to its ability to pay under its insurance policies and contracts in accordance with their terms.

*Ratings from 'AA' to 'CCC' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.*

Insurance Ratings Framework

- **BUSINESS RISK PROFILE**
  - Industry And Country Risk
  - Competitive Position

- **FINANCIAL RISK PROFILE**
  - Capital And Earnings
  - Risk Position
  - Financial Flexibility

- **MODIFIERS**
  - Enterprise Risk Management
  - Management and Governance

- **Holistic Analysis**
  - Indicative Stand-Alone Credit Profile
  - or Indicative Group Credit Profile

- **SUPPORT FRAMEWORK**
  - Group or Government Support

- **ISSUER CREDIT RATING**
  - or Financial Strength Rating
S&P’s Financial Strength Rating Distributions

**Life Insurance**

**Property & Casualty Insurance**

**Health Insurance**

**Reinsurance**

FSR Ratings as of September 2016
Insurance Ratings Framework

- Business Risk Profile
  - Industry And Country Risk
  - Competitive Position

- Financial Risk Profile
  - Capital And Earnings
  - Risk Position
  - Financial Flexibility

- MODIFIERS
  - Enterprise Risk Management
  - Management and Governance

- Holistic Analysis
  - Indicative Stand-Alone Credit Profile
  - Indicative Group Credit Profile

- Support Framework
  - Group or Government Support
  - ISSUER CREDIT RATING
    - or Financial Strength Rating

- Liquidity
- Sovereign Risk
  - Stand-Alone Credit Profile
  - or Group Credit Profile
S&P’s Insurance Capital Analysis

- **Investment Risk – C-1 Analysis**
  - Corporate Bonds
    - Assumptions
      - 5 yr. cumulative average loss given default over 30 years
      - Different charges based on bond maturity
  - RMBS & Callable Bonds
    - Risk charges based on interest rate risk sensitivity
  - Input from S&P asset specialists across most sectors
    - Corp./Structured Finance/Private Equity/Public Finance

- **Capital and Earnings Forecast**
  - Our view of earnings & retention of capital
    - Over three years (current and next two years)
  - Forecast informed by
    - Knowledge of company
    - Sector level judgment
    - Macro-economic assumptions
Our Track Record Over Time

Ratings Performance:
Global Corporate Cumulative Default Rates Over 10 Years

Source: Default, Transition, and Recovery: 2015 Annual Global Corporate Default Study And Rating Transitions, May 2, 2016,
Global Default Risk By Ratings Categories

Global Corporate Average Cumulative Default Rates By Rating (1981-2015)

Insurance Ratings Framework
S&P’s ERM Evaluation Framework

- ERM reviews consist of five sub-factors
  - Provide prospective view of risk profiles and capital needs

Financial strength ratings can be influenced by our ERM opinion & its relative importance to rating
For more information on S&P Global Ratings, go to

www.UnderstandingRatings.com