

Rating Agency Presentation
International Congress of Actuaries
March 2002

Karen Davies
VP/Senior Analyst
Moody's Investors Service



Moody's Investors Service

Topics

- ◆ **About Moody's Investors Service**
- ◆ Moody's General Insurance Ratings
- ◆ Credit Risk in General Insurance
- ◆ Update on Impact of Terrorist Attacks
- ◆ Outlook for Ratings of General Insurers

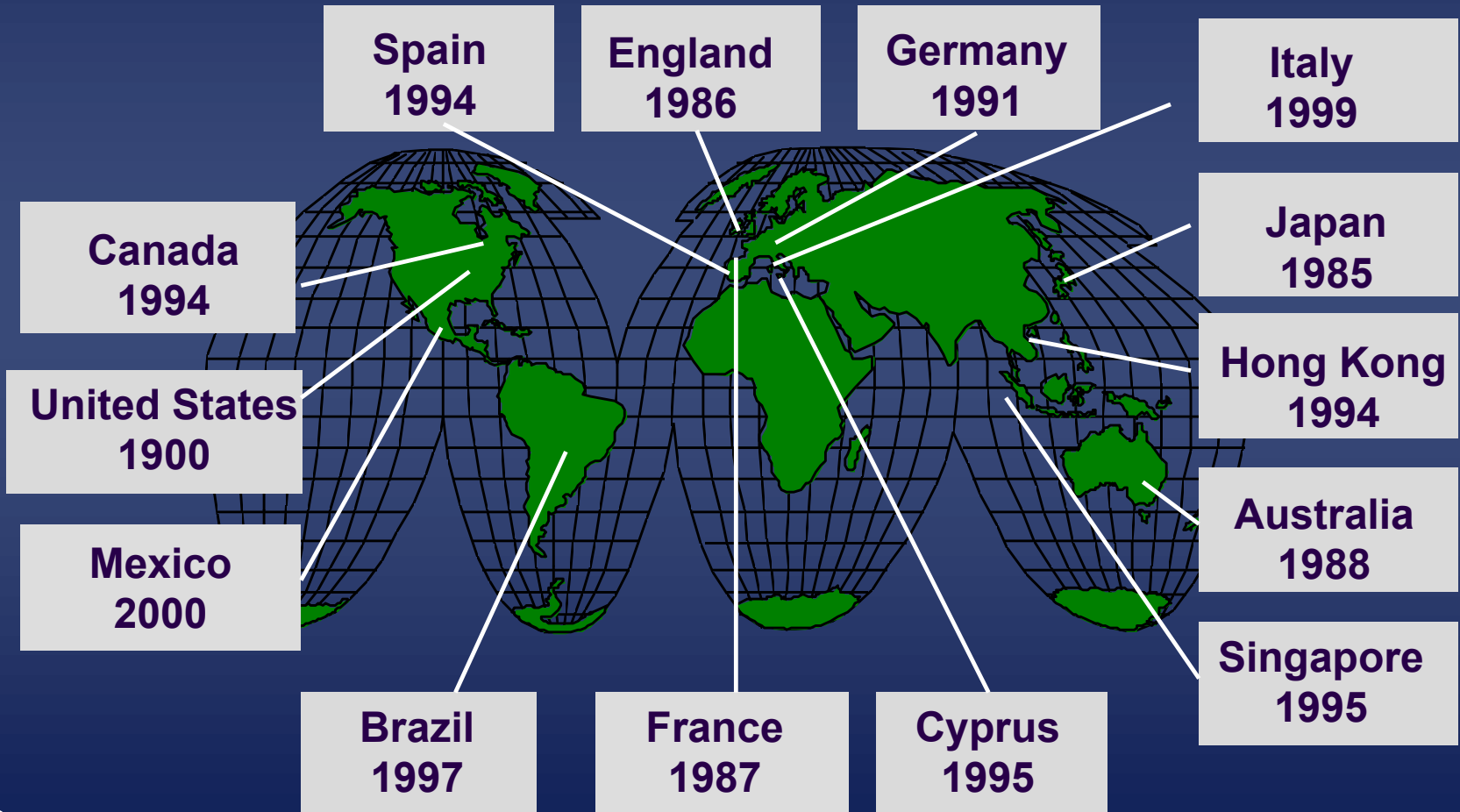


Moody's Investors Service

- ◆ Leading global provider of credits ratings, research, and analysis for debt instruments and other securities
- ◆ Coverage in key segments of the world's capital markets: credit analysis and ratings on over \$30 trillion in debt
- ◆ Rates more that 85,000 securities issued by corporation and governments in more the 100 nations
- ◆ Leading publisher of investor-oriented credit research for over 15,600 subscribers globally

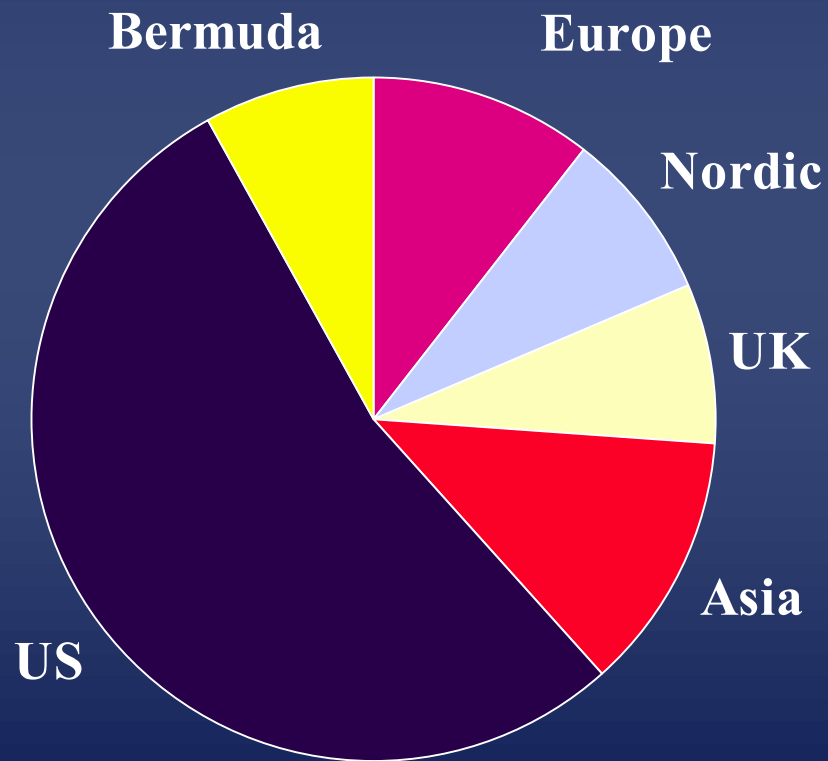


Moody's has over 1400 employees located in 14 strategic locations



Moody's General Insurance Ratings

Group Basis



Topics

- ◆ Introduction
- ◆ **Moody's General Insurance Ratings**
- ◆ Credit Risk in General Insurance
- ◆ Update on Impact of Terrorist Attacks
- ◆ Outlook for Ratings of General Insurers



Moody's General Insurance Ratings

Nature of Ratings Coverage

- ◆ Ratings coverage and active relationships with virtually all major market participants
- ◆ No limits on types of insurers we will rate
- ◆ Often have a dialogue with firms without public ratings
- ◆ Indicative ratings / right of refusal



Moody's General Insurance Ratings

Meaning of the Ratings

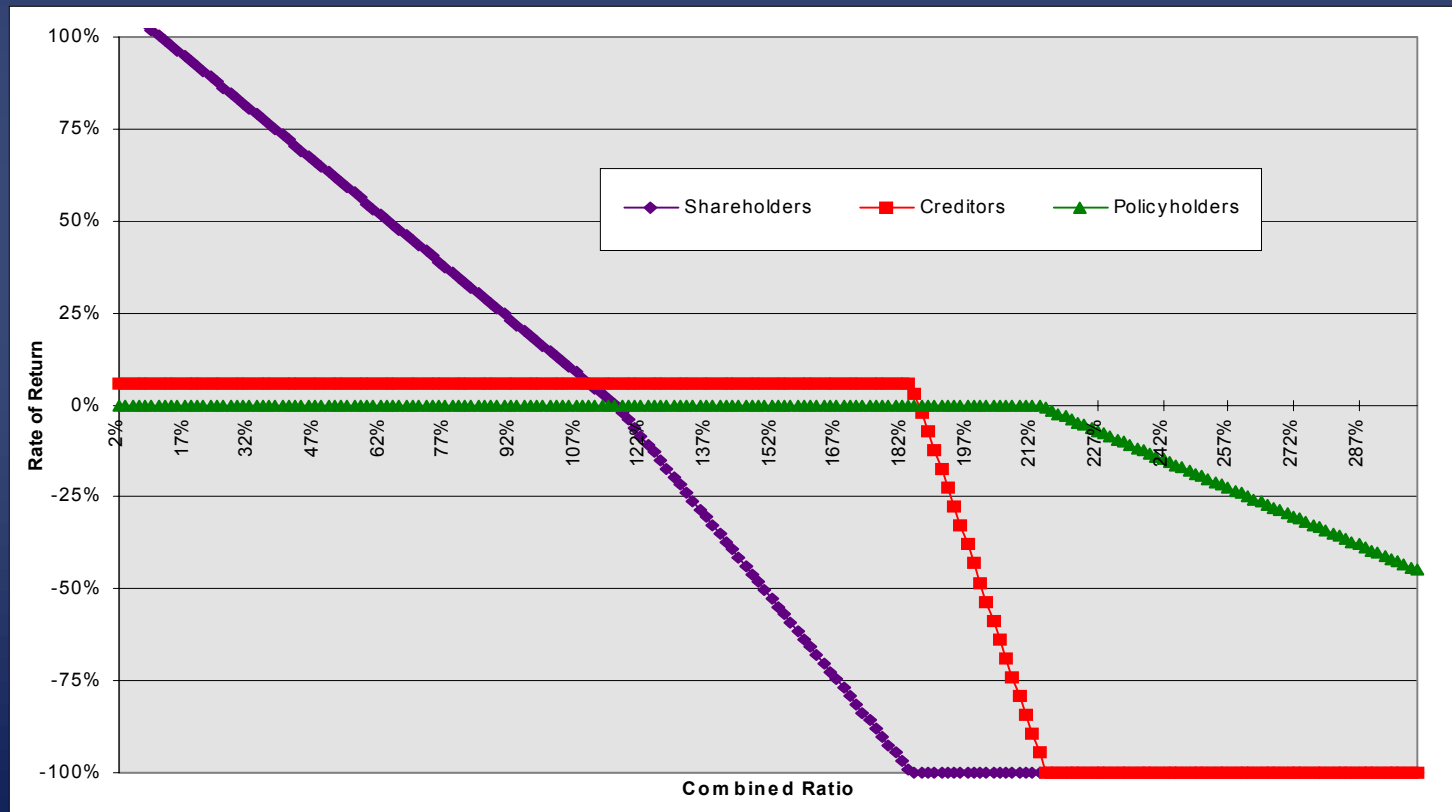
- ◆ Debt and preferred: investor orientation - speak to both default frequency and loss-given-default
- ◆ Financial strength: policyholder orientation - speak to ability to pay, considering recovery value
- ◆ Rating horizon, long-term (3-5 years)
- ◆ Financial strength ratings do not speak directly to likelihood or timing of claim payments

■ *Ability Vs. Willingness*



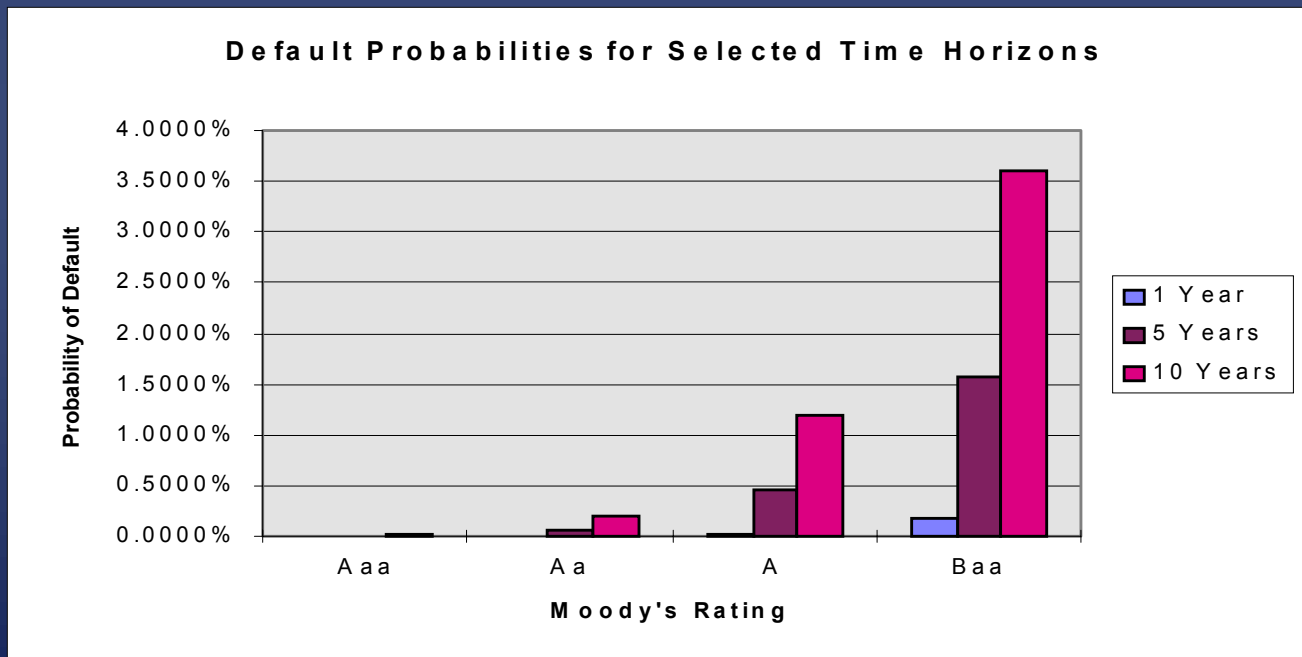
Moody's General Insurance Ratings

Evaluate company's ability to withstand stress:



Moody's General Insurance Ratings

Globally consistent ratings - benchmark:



Moody's General Insurance Ratings Analytical Approach

Industry Fundamentals	
Competitive Dynamics Barriers to Entry Regulation Market/Product Trends	
Company Fundamentals	
<i>Business Fundamentals</i>	<i>Financial Fundamentals</i>
Strategic Focus	Investment Risk
Distribution Channels	Liquidity
Franchise Value	Reserve Adequacy
Management	Use of Reinsurance
Governance	Profitability
Legal Structure	Capitalization & Funding



Topics

- ◆ Introduction
- ◆ Moody's General Insurance Ratings
- ◆ **Credit Risk in General Insurance**
- ◆ Update on Impact of Terrorist Attacks
- ◆ Outlook for Ratings of General Insurers



Credit Risk in General Insurance

State of the Market Pre 9-11

- ◆ Years of intense competition, soft pricing broadening coverages eroded financial health
- ◆ Earnings weak, propped up by finite risk covers
- ◆ Balance sheets weakening, reserve deficiencies, more aggressive investments
- ◆ Legitimate turnaround in pricing had begun in commercial lines, reinsurance



Credit Risk in General Insurance

Key Credit Risks - Primary Insurers

- ◆ Financial statements are unreliable indicators of financial health and economic performance
- ◆ “Hidden” leverage: e.g., reserves and reinsurance exposure, as well as high excess business
- ◆ Incentives exist for weak firms to expand instead of contract, inviting spectacular reversals of fortune
- ◆ Because a firm’s position is clear only in retrospect, market perception can sustain or cripple



Credit Risk in General Insurance

Key Credit Risks - Reinsurers

- ◆ All comments about primary insurers apply, but to a greater degree
- ◆ As a derivative market, reinsurers face less stable demand function, more capital market competition



Topics

- ◆ Introduction
- ◆ Moody's General Insurance Ratings
- ◆ Credit Risk in General Insurance
- ◆ **Update on Impact of Terrorist Attacks**
- ◆ Outlook for Ratings of General Insurers



Update: Impact of Terrorist Attacks Rating Revisions

- ◆ 25 insurance groups placed on review; outlooks changed for 6 others
- ◆ Year end 2001, reviews completed with 17 companies receiving downgrades.
- ◆ Going forward, need to consider altered risk profile of industry



Update: Impact of Terrorist Attacks Rating Revisions

- ◆ Ground-up estimates of ultimate loss appear sound, but uncertainties exist
- ◆ Heavy burden of loss on reinsurers increase scrutiny of counter-party credit risk
- ◆ Event tests investor and customer confidence
- ◆ Strong cyclical rebound in pricing and terms offset concerns, to a degree



Update: Impact of Terrorist Attacks

Industry Response

- ◆ Re-examination of risk models, aggregations
- ◆ Terrorism coverage excluded where possible
- ◆ Acceleration of rate increases and stricter underwriting
- ◆ Federal solution appears increasingly unlikely



Topics

- ◆ Introduction
- ◆ Moody's General Insurance Ratings
- ◆ Credit Risk in General Insurance
- ◆ Update on Impact of Terrorist Attacks
- ◆ **Outlook for Ratings of General Insurers**



Ratings Outlook for General Insurers and Reinsurers

- ◆ Most insurers and reinsurers should maintain their ratings in the near term
- ◆ Where changes occur, downgrade more likely
- ◆ Key issues: earnings quality, reserve adequacy, asbestos litigation, loss cost trends, low reinvestment rates, fallacy of excess capital

