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A.M. Best Ratings on a National Scale

A Best's Issuer Credit Rating (ICR) is an opinion of an issuer/entity's ability to meet its ongoing senior financial obligations. The rating is based on a comprehensive quantitative and qualitative evaluation of a company's balance sheet strength, operating performance and business profile, as well as the company's risk management and the impact of country risk factors. Best's Issuer Credit Rating is a global rating that allows the comparison of companies from all countries on the same credit scale.

For an insurance company, a national scale rating provides a relative opinion of financial strength within a single country. Therefore, the national scale rating assigned to an insurer in one country would not be comparable to a national scale rating assigned to an insurer in another country.

The primary reason the national scale was created is to address two related issues: 1) using only a particular section of the rating scale and 2) ratings that are grouped tightly, creating less differentiation. These phenomena reflect country-specific limiting factors the industry faces, including economic, political and financial system risk and lack of maturity in the insurance industry. The national scale rating allows for maximum differentiation among insurers operating in a given country.

The process of assigning a national scale rating begins with the assignment of a Best's Issuer Credit Rating. All companies that enter the A.M. Best national scale rating process will be assigned an A.M. Best global rating first. This process involves the same comprehensive, quantitative and qualitative analysis of a company's balance sheet strength, operating performance and business profile, as well as the company's risk management and the impact of country risk factors that apply to all companies rated by A.M. Best. For an in-depth discussion of the financial analysis undertaken at the insurance entity level, please see *Best's Credit Rating Methodology (BCRM)*, which provides additional details on this process.

This criteria highlights the unique features and discusses the additional analysis that is undertaken in the assignment of a national scale rating.

As national scale ratings are only comparable within a certain country and not across countries, impairment statistics cannot be compared directly to a national rating. However, since the global rating is assigned as the base for the national rating, impairment rates can be inferred.

The national scale rating is a service that falls within A.M. Best's Interactive Credit Rating Service. At this time, national scale ratings will only be offered in Country Risk Tier (CRT) 3 through 5 countries for which there is adequate available market data to establish the national scale mapping, and the national scale ratings already are accepted as meeting a regulatory rating requirement or currently used within the country by market participants.

Country Risk and National Ratings

Country risk, along with country-specific, industry-related risks, can and does have an impact on the financial strength of the overall insurance industry in a specific country. However, since a national scale rating is a relative analysis of companies within a country, these macro-level, country-specific risks that impact all companies operating in the country are no longer rating differentiators, as all insurers in the country are subject to the same risks. Examples can include limited access to secure investable assets and limited industry maturity and/or regulation. Removal of these factors allows for the creation of a scale specific to that country.

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It would be incorrect to suggest that a national rating removes country risk from the analysis. As stated previously, the assignment of a national scale rating is derived from a global scale rating, which would have incorporated A.M. Best’s country risk criteria (*Evaluating Country Risk*). Therefore, the national scale rating captures the extent to which a particular company can mitigate and manage its country risk exposures. In other words, a company that manages its country risk exposure better than others would be relatively stronger than those that do not and therefore would have a higher national scale rating, all else being equal.

Constructing the National Scale Mapping

Each country’s scale is created individually. As the degree of country risk increases, the distribution of ratings on the global rating scale within that country moves farther away from the top end of the global scale. To assess the proper ratings mapping, an understanding of the “average” rating for a country, along with the distribution of companies around that “average,” must be achieved. Using country-specific information – including the Country Risk Tier, the Country Investment Class, the overall credit quality of the industry’s potential investment

portfolio and any current global ratings assigned within the country – the average national scale rating is estimated.

Exhibit 1 Relationship Between Ratings and CRTs

	Average Rating															
CRT-1	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-2	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-3	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-4	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-5	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-

To determine the distribution of ratings around the average national scale rating, a public data approach is used to analyze the active insurance companies within the market.

The evaluation of the distribution of financial strength in a country is done through analysis of nine individual factors:

- Amount of Capital and Surplus
- Ratio of Cash & Fixed Investments to Total Investments
- Gross Leverage Ratio: (Gross Premiums Written + Total Gross Provisions/Capital & Surplus)
- Amount of Gross Premiums Written
- Return on Equity
- Return on Assets
- Retention Ratio: (Net Premiums Written/Gross Premiums Written)
- Combined Ratio: (Incurred Loss & Loss-Adjustment Expense [LAE] Ratio + Underwriting Expense Ratio)
- Total Amount of Assets

The industry average for each factor listed above is calculated for the country being evaluated. Each company operating within this market is evaluated based on distance from the industry average for each measure. This process is based on a three-year average, and the result is a country-specific distribution of financial strength centered on the country’s industry average.

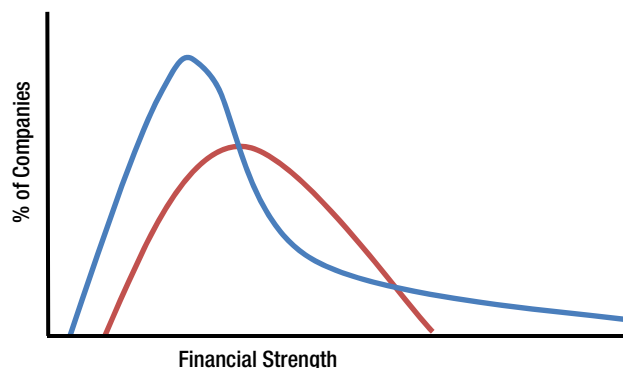
This generates an estimate of the distribution of financial strength in the insurance market. Different markets have different distributions. A common distribution is a small number of market leaders that are relatively stronger than the market as a whole. Another common distribution is a large group of companies clustered around a similar global rating level.

Exhibit 2 illustrates these two potential distributions of financial strength.

Understanding the shape of this distribution allows A.M. Best to efficiently spread out the global ratings curve within a country in a way that allows for maximum use of the rating scale within the country, thus creating the greatest degree of differentiation among national market participants.

This approach to the creation of a national rating scale is consistent with A.M. Best's belief that country factors, while clearly important and able to negatively impact an insurer's global rating, should not act as a ceiling to companies on the global scale.

Exhibit 2



The National Scale in the A.M. Best Rating Process

As stated previously, the analysis of an insurer begins with the assignment of a Best Issuer Credit rating.

This global rating then will be “mapped” to a national scale rating based on the country-specific national scale mapping that has been developed for the company's country of domicile. In cases where one global ICR level maps to more than one national scale rating, a rating committee will decide which level, in accordance with the mapping, is appropriate given the relative financial strength of the insurer. To denote the difference between an A.M. Best global rating and an A.M. Best national scale rating, the credit rating will have a “.XX” where XX represents a two-letter country code. In other words, for Mexico (full mapping illustrated in **Exhibit 3**), a national scale rating might appear as a+.MX.

Rating Definitions

The following are the rating definitions for A.M. Best's national scale rating where “.XX” represents a two-letter country code.

aaa.XX: Assigned to insurance companies that have, in A.M. Best's opinion, an exceptional ability to meet their ongoing senior financial obligations relative to other national entities.

aa.XX: Assigned to insurance companies that have, in A.M. Best's opinion, a superior ability to meet their ongoing senior financial obligations relative to other national entities.

a.XX: Assigned to insurance companies that have, in A.M. Best's opinion, an excellent ability to meet their ongoing senior financial obligations relative to other national entities.

bbb.XX: Assigned to insurance companies that have, in A.M. Best's opinion, a good ability to meet their ongoing senior financial obligations relative to other national entities.

bb.XX: Assigned to insurance companies that have, in A.M. Best's opinion, a fair ability to meet their ongoing senior financial obligations relative to other national entities.

b.XX: Assigned to insurance companies that have, in A.M. Best's opinion, a marginal ability to meet their ongoing senior financial obligations relative to other national entities.

ccc.XX: Assigned to insurance companies that have, in A.M. Best's opinion, a weak ability to meet their ongoing senior financial obligations relative to other national entities.

cc.XX: Assigned to insurance companies that have, in A.M. Best's opinion, a weak ability to meet their ongoing senior financial obligations relative to other national entities.

c.XX: Assigned to insurance companies that have, in A.M. Best's opinion, a poor ability to meet their ongoing senior financial obligations relative to other national entities.

An **Outlook** is assigned to a National Scale Issuer Credit Rating (aaa to c) to indicate its potential direction over an intermediate term, generally defined as 12 to 36 months. An outlook can be:

Outlook	Definition
Positive	Indicates possible rating upgrade due to favorable financial/market trends relative to the current rating level.
Negative	Indicates possible rating downgrade due to unfavorable financial/market trends relative to the current rating level.
Stable	Indicates low likelihood of a rating change due to stable financial/market trends.

In addition, a National Scale Rating can be put under review and assigned the following modifier.

Modifier	Descriptor	Definition
u	Under Review	Indicates the rating may change in the near term, typically within six months. Generally is event driven, with positive, negative or developing implications.

Exhibit 3 Best's Global ICR Scale vs. Mexico National Scale

Global ICR Scale	National Scale/Mexico
a	aaa.MX
a-	aa+.MX to aa.MX
bbb+	aa-.MX
bbb	a+.MX to a.MX
bbb-	a-.MX
bb+	bbb+.MX to bbb.MX
bb	bbb-.MX
bb-	bb+.MX
b+	bb.MX
b	bb-.MX to b+.MX
b-	b.MX
ccc+	b-.MX to ccc+.MX
ccc	ccc.MX
ccc-	ccc-.MX
cc	cc.MX
c	c.MX

Changes to the National Scale Rating

An insurer's national scale rating can change for two primary reasons:

- The analysis of the company's financial strength leads to a change in that company's rating.
- The country- (and industry-) specific characteristics lead to a change in the overall national scale mapping for the country of domicile.

The national scale mapping will be reviewed regularly for each country.

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METHODOLOGY

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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. An FSR is not assigned to specific insurance policies or contracts.

Best's Issuer Credit Rating (ICR): an independent opinion of an entity's ability to meet its ongoing financial obligations and can be issued on either a long- or short-term basis.

Best's Issue Rating (IR): an independent opinion of credit quality assigned to issues that gauges the ability to meet the terms of the obligation and can be issued on a long- or short-term basis (obligations with original maturities generally less than one year).

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.

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