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## Research Update:

# Amlin AG, Core Subsidiary Of U.K.-Based Amlin Group, Affirmed At 'A' After Insurance Criteria Change; Outlook Stable

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## Overview

- Following a review of U.K.-based Amlin Group under our revised insurance criteria, we are affirming our 'A' ratings on its core subsidiary, Amlin AG.
- The ratings predominantly reflect our view of the group's strong competitive position, based on its highly diverse franchise and sector-leading earnings. These are partly offset by Amlin's weaker capital position relative to peers and its high risk profile.
- The stable outlook reflects our expectation that Amlin's capital adequacy will improve to at least strong levels and that it will maintain its strong competitive position over the next two years as the benefits from the turnaround of Amlin Europe begin to emerge.

## Rating Action

On May 23, 2013, Standard & Poor's Ratings Services affirmed its 'A' counterparty credit and insurer financial strength ratings on Amlin AG, the core subsidiary of U.K.-based insurance and reinsurance group Amlin PLC. The counterparty credit rating on Amlin PLC was affirmed at 'BBB+'. The outlook on Amlin AG and Amlin PLC is stable.

## Rationale

The ratings reflect our view of the Amlin group's strong business profile and upper adequate financial risk profile. We derive these assessments from our view of the group's strong competitive position, based on its highly diverse franchise and sector-leading earnings, which are partly offset by a weaker capital position relative to peers'. Moreover, we consider Amlin's risk profile to be high, given its exposure to catastrophe risk. We derive our 'a-' anchor for Amlin from the combination of these factors. The counterparty credit rating is one notch higher than the anchor on the basis of our view of the group's strong enterprise risk management (ERM) and satisfactory management and governance.

Overall, we believe Amlin's risk exposures are well diversified across major global markets, which we consider to have largely intermediate insurance industry and country risk. We are unlikely to change this assessment over the rating horizon (2013-2015), given the group's globally diverse operations.

Amlin's insurance industry and country risk is well spread across the global reinsurance sector and several primary markets across Europe and the U.S. We believe Amlin has relatively low country risk across its major primary markets and we view its subscription business written through Lloyd's as reinsurance for this purpose because we believe the risk profiles are similar. In our opinion, Amlin's non-life reinsurance business is exposed to moderate industry risk, given our negative view of product risk associated with the non-life reinsurance industry and the associated property catastrophe volatility for reinsurers such as Amlin. Within this competitive sector, we believe there are moderate barriers to entry.

In our view, Amlin has a strong competitive position, supported by its outperformance of peers and its multiplatform distribution network, which provides geographic and product diversity. Amlin has a long-established, well-regarded franchise within the London market. Amlin's syndicate 2001 writes roughly 6% of the Lloyd's market, and is the second-largest syndicate at Lloyd's (capacity of £1.2 billion for 2013).

Amlin also has a strong presence in the U.S. and the U.K. through its reinsurance operations--40% of gross premium written (GPW) in 2012--and is expected to increase its presence in continental Europe through Amlin Europe and Amlin AG. The group writes more than 30 classes of business across the group, of which the largest are catastrophe reinsurance (20% of GPW in 2012), marine (14%), and property (16%). Our expectations are that Amlin will continue to grow across all its platforms, led predominantly by operations in London and Bermuda, supported by a turn in the performance of Amlin Europe and further acceptance of Amlin Re Europe to give top line growth of around 11%–13% in 2013.

Diversification of risks, particularly in its catastrophe business, has historically helped Amlin manage earnings volatility and demonstrates its strong cycle management. Amlin reported a five-year average combined ratio of 81.4% over 2008-2012, which includes results for 2011–-Amlin's worst-ever year on record. This clearly outperforms the peer average of 96.9% over the same period. We expect the group to report strong earnings over the rating horizon, exhibited by combined ratios under 90%, and at least 15% return on revenue and cross-cycle return on equity through to 2015 (assuming a normal level of catastrophe-related losses).

Our view of Amlin's competitive position is constrained by the impact on the group from its acquisition of Amlin Europe. Amlin Europe's operating performance compares unfavorably with the rest of the group's and has in recent years been a drag on the group's earnings and reputation. However, we believe that the results of management's restructuring of Amlin Europe's book and underwriting processes are emerging, and will result in combined ratios below 100% over the rating horizon.

We expect that Amlin's strong prospective earnings and ability to outperform peers will help rebuild its capital adequacy back to strong levels by 2015, if not sooner. Record losses in 2011 caused a material deterioration in the group's capital adequacy to below the A range, which it has yet to fully rebuild; thus we view Amlin's overall capitalization as weaker than we would expect for a company with its risk profile, as well as relative to peers.

In our view, Amlin demonstrates a high risk position because of its exposure to catastrophe risk and the potential volatility such risk could create in capital and earnings. In our opinion, a large proportion of the group's capital is required for its exposure to natural catastrophe losses, consistent with other large global reinsurers.

We view Amlin's financial flexibility as strong, given its demonstrated ability to access various significant sources of capital, including the hybrid and equity markets, and by issuing insurance-linked securitization in 2011. We believe the company has a good standing with equity investors, as evidenced by its 1.39x price-to-book ratio (compared with a market average of 1.0x) We also assume financial leverage will remain below 25%, despite a modest increase in 2012, and fixed-charge coverage will be around 7-8x.

We consider Amlin's ERM to be strong, and its management and governance as satisfactory. These assessments provide one notch of uplift to the group's credit profile. Our strong ERM assessment reflects our positive view of Amlin's risk-management culture, risk controls, and strategic and emerging risk management. We believe these capabilities will enable the group to continue to enhance its risk-return profile.

Amlin's management and governance is satisfactory, in our opinion. The group has a good track record of strategic planning, wide depth and breadth of expertise within the management ranks, and relatively conservative and sophisticated financial management.

We regard Amlin's liquidity as strong, owing to the strength of available liquidity sources, mainly premium income and an asset portfolio that contains more than £2 billion in liquid funds and fixed-income securities.

## Outlook

The stable outlook reflects our expectations that Amlin's capital adequacy will improve to at least strong levels over the next two years, which, combined with the resilience of Amlin's strong earnings, will strengthen the group's financial risk profile. We also anticipate that Amlin will maintain at least a strong competitive position as the benefits from the turnaround of Amlin Europe begin to emerge.

We might lower the ratings if, contrary to our expectations, Amlin fails to rebuild capital adequacy to above at least the 'A' range according to our model over the next 12–24 months.

We may raise the ratings on Amlin Group if:

- The recovery of Amlin Europe proves beneficial to Amlin's overall brand

and reputation, particularly in continental Europe, evidenced by profitable top-line growth and a greater proportion of group earnings coming from Amlin Europe;

- Amlin is able to sustain its strong outperformance of peers; and
- Capital adequacy is rebuilt much quicker than expected and sustained comfortably in the 'A' range according to our model.

## Rating Score Snapshot

| | |
|---|---|
| Financial Strength Rating | A/Stable |
| | |
| Anchor | a- |
| Business Risk Profile | Strong |
| IICRA* | Intermediate Risk |
| Competitive Position | Strong |
| | |
| Financial Risk Profile | Upper Adequate |
| Capital & Earnings | Strong |
| Risk Position | High Risk |
| Financial Flexibility | Strong |
| | |
| Modifiers | +1 |
| ERM and Management | +1 |
| Enterprise Risk Management | Strong |
| Management & Governance | Satisfactory |
| Holistic Analysis | 0 |
| | |
| Liquidity | Strong |
| | |
| Support | 0 |
| Group Support | 0 |
| Government Support | 0 |

*IICRA--Insurance Industry And Country Risk Assessment.

## Related Criteria And Research

### Related criteria

- Insurers: Rating Methodology, May 7, 2013
- Group Rating Methodology, May 7, 2013
- Enterprise Risk Management, May 7, 2013
- Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Principles Of Credit Ratings, Feb. 16, 2011
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

**Related research**

- List Of Issuers With Ratings Under Criteria Observation Due To S&P's New Insurers Rating Methodology, May 7, 2013
- Standard & Poor's Assigns Insurance Industry And Country Risk Assessments, May 7, 2013

## Ratings List

Ratings Affirmed

| | |
|---|---|
| Amlin PLC | |
| Counterparty Credit Rating | |
| Local Currency | BBB+/Stable/-- |
| Subordinated | BBB- |
| | |
| Amlin AG | |
| Counterparty Credit Rating | |
| Local Currency | A/Stable/-- |
| Financial Strength Rating | |
| Local Currency | A/Stable/-- |

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