Best's Credit Rating Effective Date
July 10, 2019

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Best's Credit Rating Methodology

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Financial Data Presented

The financial data in this report reflects the most current data available to the Analytical Team at the time of the rating. Updates to the financial exhibits in this report are available here: Best's Financial Report.

Lloyd's

AMB #: 085202 | **AIIN#:** AA-1122000

Best's Credit Ratings – for the Rating Unit Members

Financial Strength Rating (FSR)	Issuer Credit Rating (ICR)
A	**a+**
Excellent	**Excellent**
Outlook: **Stable**	Outlook: **Stable**
Action: **Affirmed**	Action: **Affirmed**

Assessment Descriptors

Balance Sheet Strength	**Very Strong**
Operating Performance	**Strong**
Business Profile	**Favorable**
Enterprise Risk Management	**Appropriate**

Rating Unit - Members

Rating Unit: Lloyd's | AMB #: 085202

AMB #	Rating Unit Members	AMB #	Rating Unit Members
078649	Lloyd's Ins Co (China) Ltd	095926	Lloyd's Insurance Co. S.A.

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Rating Rationale

Balance Sheet Strength: Very Strong

- The market has the strongest level of risk-adjusted capitalisation, as measured by Best's Capital Adequacy Ratio (BCAR).
- A robust capital-setting regime, which incorporates a risk-based approach to setting member-level capital, helps protect risk-adjusted capitalisation from volatility.
- Member-level capital is subject to fungibility constraints as it is held on a several rather than joint basis.
- Balance sheet strength is underpinned by a strong Central Fund that is available, at the discretion of the Council of Lloyd's, to meet the policyholder obligations of all Lloyd's members.
- An offsetting factor is the market's significant exposure to catastrophe risk and its dependence on reinsurance to manage this risk.

Operating Performance: Strong

- Lloyd's long-term historical operating performance is strong, demonstrated by a ten-year (2009-2018) average combined ratio of 96.6% and a return on equity ratio of 7.1%.
- Technical performance is subject to volatility due to the nature of business underwritten. In 2018, major losses added 11.6 points to the combined ratio (2017: 18.5 points).
- Adjusted for average catastrophe experience, recent technical performance has been outside of AM Best's expectations for a strong assessment. However, robust remedial actions by the Corporation and individual managing agents are expected to support further incremental improvements in attritional accident-year performance over the next three years.
- The market's expense ratio is high compared to that of peers. Actions to reduce the cost of placing business at Lloyd's are subject to a high degree of execution risk due to initial investment and culture change required.

Business Profile: Favorable

- Lloyd's has a strong position in the global general insurance and reinsurance markets as a leading writer of specialty property and casualty risks.
- Although Lloyd's syndicates operate as individual businesses, the collective size of the market allows them to compete with international groups under the Lloyd's brand.
- The markets in which Lloyd's operates are highly competitive and have experienced soft market conditions for a number of years. Lloyd's reliance on brokers to underwrite specialty and reinsurance business makes it vulnerable to price-based competition.
- The portfolio is well diversified but with some geographical bias towards North America and product bias towards commercial specialty lines products.
- Product risk is moderate to high. Higher-risk lines include reinsurance, energy, aviation, some marine business and a high proportion of the casualty and property business written. The majority of small commercial and consumer business, as well as some of the business written through coverholders, is lower risk.

Enterprise Risk Management: Appropriate

- Lloyd's enterprise risk management framework is well developed and appropriate for the size and complexity of the Lloyd's market.
- Risk management capabilities are aligned with the market's risk profile.
- The Corporation's risk management function offers the market additional oversight. However, as managing agents of individual and competing syndicates have their own risk appetites and strategies there are some limitations on its ability to actively manage the market's risks.
- An internal capital model, in place since 2012, is used to calculate the solvency capital requirement under Solvency II as well as to stress test the market's risk-adjusted capitalisation. In AM Best's opinion, the internal capital model strongly supports the Corporation's ability to assess the capital adequacy of the market.

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Outlook

- The stable outlooks reflect AM Best's expectation that risk-adjusted capitalisation will remain at the strongest level, supported by Lloyd's capital management strategy and the requirement for members to replenish their funds at Lloyd's following losses. Long-term operating performance is expected to remain supportive of the strong assessment, albeit subject to volatility from catastrophe losses, subject to the success of remedial actions that are being taken. Lloyd's is expected to maintain its favourable business profile, underpinned by the strong Lloyd's brand and underwriting expertise. The business profile assessment takes into account the competitive conditions in Lloyd's core markets and pressure from changing market dynamics, including the regionalisation of insurance business.

Rating Drivers

- Upward rating movements are considered unlikely in the short term. Longer term, positive rating pressure could arise if Lloyd's business profile strengthens.
- Negative rating actions could arise if Lloyd's underlying performance does not improve in line with expectations over the next three years.
- Negative rating actions could arise following a material deterioration in the market's risk-adjusted capitalisation, for instance, due to a substantial loss to the Central Fund or a reduction in member-level capital requirements set by Lloyd's.

Key Financial Indicators

Best's Capital Adequacy Ratio (BCAR) Scores (%)

Confidence Level	95.0	99.0	99.5	99.6
BCAR Score	70.8	56.3	50.0	47.9

Source: Best's Capital Adequacy Ratio Model - Universal

Key Financial Indicators	2018 GBP (000)	2017 GBP (000)	2016 GBP (000,000)	2015 GBP (000,000)	2014 GBP (000)
Net Premiums Written:					
Non-Life	25,681,000	24,869,000	23,066	21,023	20,006,000
Composite	25,681,000	24,869,000	23,066	21,023	20,006,000
Net Income	-1,001,000	-2,001,000	2,107	2,122	3,016,000
Total Assets	118,008,000	108,396,000	101,602	83,629	79,713,000
Total Capital and Surplus	27,428,000	26,767,000	27,714	24,216	22,528,000

Source: BestLink® - Best's Financial Suite

Key Financial Indicators & Ratios	2018	2017	2016	2015	2014	Weighted 5-Year Average
Profitability:						
Balance on Non-Life Technical Account (GBP 000)	-1,130,000	-3,421,000	468	2,047	2,253,000	...
Net Income Return on Revenue (%)	-3.8	-7.7	8.9	10.0	14.8	3.6
Net Income Return on Capital and Surplus (%)	-3.7	-7.3	8.1	9.1	14.1	3.4
Non-Life Combined Ratio (%)	104.5	114.0	97.9	90.0	88.4	99.8
Net Investment Yield (%)	1.4	2.1	1.7	1.3	1.6	1.7
Leverage:						
Net Premiums Written to Capital and Surplus (%)	93.6	92.9	83.2	86.8	88.8	...

Source: BestLink® - Best's Financial Suite

Credit Analysis

Balance Sheet Strength

Lloyd's balance sheet strength assessment of very strong reflects risk-adjusted capitalisation at the strongest level, as measured by Best's Capital Adequacy Ratio (BCAR), as well as the market's good financial flexibility. The market has significant exposure to

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Balance Sheet Strength (Continued...)

catastrophe losses and is dependent on reinsurance to manage this risk. However, a robust market-wide capital-setting regime, which incorporates a risk-based approach to setting member-level capital and the requirement for members to replenish their funds at Lloyd's after a loss, helps protect risk-adjusted capitalisation against volatility.

Balance sheet strength is underpinned by a strong Central Fund that is available, at the discretion of the Council of Lloyd's, to meet the policyholder obligation of all Lloyd's members.It is the existence of this partially mutualising link that is the basis for a market-level rating.

The market's member-level capital is held on a several rather than joint basis and is only available to meet the liabilities of that particular member. The resulting fungibility constraints on available capital, the significant proportion of member-level capital provided through letters of credit (LOCs), the market's significant exposure to catastrophe risk, and dependence on reinsurance to manage this risk, are limiting factors for the balance sheet strength assessment.

Capitalisation

The BCAR scores shown in this report are based on the 2018 figures published in the Lloyd's annual report which contains the financial results of Lloyd's and its members in pro forma financial statements and includes the financial statements of the Society of Lloyd's (referred to in this report as the Society or the Corporation, which are used interchangeably). The pro forma financial statements include the aggregated accounts, which are based on the accounts of each Lloyd's syndicate, members' funds at Lloyd's (FAL) and the Society's financial statements.

The Society was formed in 1871, when the then existing association of underwriters at Lloyd's was incorporated by the Lloyd's Act. The Society produces consolidated financial statements that cover Lloyd's activities outside the underwriting market and Lloyd's central resources (the Central Fund).

Lloyd's benefits from risk-adjusted capitalisation at the strongest level, as measured by BCAR. This assessment takes into account capital resources available at member level, in the form of Members' FAL, and centrally in the form of the Central Fund and net assets of the Corporation. Capital credit is given in BCAR for subordinated debt issued by the Society, as well as for FAL provided through LOCs as if drawn these LOCs will turn into Tier 1 capital for Lloyd's. Nonetheless, the extensive use of LOCs as FAL reduces the quality of available capital. AM Best does not give explicit credit for contingent capital in the 'callable layer' which is the ability of the Corporation to supplement central assets by calling funds from members of up to 3% of their overall premium limits.

Any assessment of Lloyd's capital strength is complicated by the compartmentalisation of capital at member level. Member-level capital in the form of FAL and members' balances are held on a several rather than joint basis, meaning that any member need meet only its share of claims. However, Lloyd's central assets are available, at the discretion of the Council of Lloyd's, to meet policyholder liabilities that any member is unable to meet in full. This link in the chain of security comprises the Central Fund and other central assets, as well as subordinated debt. These central assets can be supplemented by funds called from members of up to 3% of their overall premium limits. It is the existence of this partially mutualising third link, and the liquid Central Fund in particular, that is the basis for a market-level rating.

Lloyd's Internal Model (LIM) captures Lloyd's unique capital structure and takes into account fungibility constraints on member-level capital and the mutual nature of central assets. If a severe market loss led to the exhaustion of some members' FAL, central assets would be exposed to any further losses faced by these members. The model captures this mutualised exposure, so that, at different return periods, the exposure of both member-level capital and central capital is demonstrated.

Lloyd's is subject to the Solvency II regulatory regime. As agreed with the UK regulator, the Prudential Regulation Authority (PRA), Lloyd's calculates two separate Solvency Capital Requirements (SCRs) and two separate SCR coverage ratios: a market-wide SCR (MWSCR) and a central SCR (CSCR). The MWSCR calculates the total capital consumed at a 99.5% value at risk (VaR) confidence level over a one-year period for the Lloyd's market as a whole (including the exposure of both member-level and central assets).

The CSCR is calculated at a 99.5% VaR confidence level over a one-year period in respect of risks facing the Society and its Central Fund. It captures exposure to losses that would not affect the majority of syndicates (and so would not erode capital at overall member level) but would have an impact on central assets. Calculating a CSCR addresses the fact that a 1-in-200 year loss to central assets could be bigger than the loss to central assets in a 1-in-200 year market loss event. By calculating both figures, Lloyd's has a better view of the likelihood that central and market level assets are sufficient.

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Balance Sheet Strength (Continued...)

Lloyd's has approval from the PRA to use existing LOCs, in the form that they are provided as FAL, as Tier 2 capital for Solvency II purposes. However, any new LOCs provided as FAL need to be individually approved. Under Solvency II at least 50% of the solvency capital requirement must be met by Tier 1 capital.

Lloyd's has introduced a phased reduction in the proportion of FAL that can be provided as LOCs. From December 2018 no more than 90% of member's capital requirement could be supported by LOCs, reducing to 70% from December 2019 and 50% from December 2020. This has reduced the amount of assets which are ineligible to meet the MWSCR and improve the quality of capital. Consequently, as at 31 December 2018 all Lloyd's Tier 2 assets were eligible to meet the MWSCR reducing from circa GBP 2 billion of ineligible Tier 2 assets as at 31 December 2017.

The MWSCR coverage ratio stood at 148% at year-end 2018 (2017: 144%) and the CSCR coverage ratio at 249% (2017: 215%). Lloyd's risk appetite for MWSCR coverage is a minimum of 125% and the CSCR coverage is a minimum of 200%. The MWSCR risk appetite is low relative to peers, but this should be seen in light of Lloyd's good financial flexibility and capital-setting process. The stability in the market's regulatory solvency levels, as a result of the capital-setting process, is considered to be a strength for the balance sheet strength assessment.

In 2018, the MWSCR and CSCR coverage ratios improved, despite the second year of above-average major losses affecting the market during the year. This is the result of an increase in the eligible funds following the reduction in ineligible Tier 2 capital relating to LOCs and updates in the central modelling risk profile. Lloyd's available capital was not directly affected by the year's operating loss, as member-level capital was replenished in line with expectations and no members subsequently became reliant on the Central Fund.

Lloyd's employs strict capital-setting criteria both at member level and centrally. Member-level capital is determined using syndicates' SCRs calibrated to correspond to a 99.5% VaR confidence level, provided on a one-year and -to-ultimate basis and calculated using syndicates' internal capital models. A 35% uplift is applied to the ultimate SCR to arrive at the FAL requirement.

Lloyd's members are required to replenish their FAL to meet their current underwriting liabilities as part of the "coming into line" process in June and November. However, Lloyd's can require a member to recapitalise in between these dates if deemed necessary. Most members underwrite with limited liability. However, if FAL are eroded due to underwriting losses, affected members will have to provide additional funds to support any outstanding underwriting obligations to continue to underwrite at Lloyd's. This requirement in effect provides the market with access to funds beyond those reflected in its capital structure.

Member contributions to the Central Fund reduced in 2016 to 0.35% of gross written premiums (from 0.50% of capacity) per annum, and remained at this level in 2018. The contribution rate can be increased to strengthen the Central Fund at any time.

Lloyd's good financial flexibility is enhanced by the diversity of its capital providers which include corporate and individual investors. Traditional Lloyd's businesses remain committed to the market. In addition, Lloyd's continues to attract new investors, although this has slowed in recent years, drawn by its capital efficient structure and global licences. As the capital to support underwriting at Lloyd's is supplied by members on an annual basis, an important factor in AM Best's analysis of the market is its ability to retain and attract the capital required for continued trading.

Liquidity Analysis (%)	2018	2017	2016	2015	2014
Liquid Assets to Total Liabilities	67.5	72.0	80.7	85.9	85.0
Total Investments to Total Liabilities	78.6	83.2	91.6	95.8	96.0

Source: BestLink® - Best's Financial Suite

Asset Liability Management - Investments

The majority of Lloyd's investments are managed independently by the individual syndicates' managing agents, while the assets in the Lloyd's Central Fund are managed centrally by the Corporation. Although syndicates are able to define their own investment strategy, asset risk is generally low, with more than three quarters of the market's total investments held in bonds and cash/deposits or represented by LOCs.

Assets held by individual members are general liquid, with the majority held in cash (which includes LOCs) and bonds. Equity and risk asset exposure accounted for 8.3% of invested assets in 2018. Lloyd's capital (FAL and the Central Fund) is largely matched in terms of currency to exposure.

Balance Sheet Strength (Continued...)

In AM Best's opinion, Lloyd's maintains good overall liquidity. Managing agents are responsible for the investment of syndicate premium trust funds, although Lloyd's monitors liquidity levels at individual syndicates as part of its capital adequacy review. Overall, these funds exhibit a high level of liquidity, as most syndicate investment portfolios tend to consist primarily of cash and high-quality, fixed-income securities of relatively short duration. Lloyd's also monitors projected liquidity for its central assets, which are tailored to meet the disbursement requirements of the Central Fund and the Corporation of Lloyd's (including its debt obligations).

Composition of Cash and Invested Assets	2018	2017	2016	2015	2014
Total Cash and Invested Assets (GBP 000)	71,240,000	67,902,000	67,646	56,900	54,889,000
Cash (%)	15.3	17.9	18.2	19.4	18.1
Bonds (%)	58.5	54.8	56.5	58.1	58.4
Equity Securities (%)	12.0	14.0	13.5	12.1	12.1
Real Estate, Mortgages and Loans (%)	10.9	10.1	8.9	8.0	8.6
Other Invested Assets (%)	3.3	3.3	2.9	2.3	2.8
Total Cash and Unaffiliated Invested Assets (%)	100.0	100.0	100.0	100.0	100.0
Total Cash and Invested Assets (%)	100.0	100.0	100.0	100.0	100.0

Source: BestLink® - Best's Financial Suite

Reserve Adequacy

In AM Best's opinion, reserving in the Lloyd's market tends to be prudent, with the majority of market participants incorporating an explicit margin in reserves above actuarial best estimates. Robust oversight of reserves is provided by the Corporation. However, reserve surpluses, which are not fungible across the market, vary significantly between syndicates.

Aggregate reserves have developed positively overall in every year since 2003. In 2018, the market reported reserve redundancies across all lines of business, with the exception of marine. The reinsurance and property classes made a material contributions to the overall reserve release in 2018, while the life and motor classes contributed significantly less. Prospectively, the explicit margin built into reserves by many syndicates should ensure a modest level of redundancies in reserves for most classes of business, as was seen in 2018.

Syndicates in run-off have historically been the principal source of reserve deterioration for Lloyd's. However, Lloyd's exposure to open run-off years has significantly reduced, principally due to better management of these years. In 2010, an ongoing focus on promoting efficiency and finding a means to close syndicates (largely through third-party reinsurance to close) supported a fall in the number of syndicate years of account in run-off to 10 from 22 in the previous year. Further reductions have been made in recent years. Five years of account were in run-off at the beginning of 2018. All of these run-off years had closed by the end of 2018. In aggregate, run-off years reported a surplus of GBP 7 million including investment return in 2018.

1992 and Prior Reserving: Equitas

Lloyd's exposure to uncertainty arising from adverse development of the 1992 and prior years' reserves was further reduced by the High Court order in June 2009 approving the statutory transfer of 1992 and prior non-life business of members and former members of Lloyd's to Equitas Insurance Ltd., a new company in the Equitas group.

This transfer was the final phase of a two-phase process, and with its completion policyholders benefit from a total of USD 7 billion of reinsurance cover from National Indemnity Co., a subsidiary of Berkshire Hathaway Inc., over and above Equitas' 31 March 2006 carried reserves of USD 8.7 billion. The transfer provided finality in respect of Lloyd's members and former members for their 1992 and prior years' non-life liabilities under English law and the law of every state within the European Economic Area. However, there continues to be uncertainty as to the recognition of the transfer in overseas jurisdictions, including the United States.

Operating Performance

Lloyd's cross-cycle operating performance is supportive of a strong assessment, demonstrated by ten-year (2009-2018) average combined ratio of 96.6% and return on equity (ROE) ratio of 7.1%. This assessment is based on analysis of the overall consolidated performance of Lloyd's, taking into account the stability, diversity, and sustainability of the market's sources of earnings. The

Operating Performance (Continued...)

assessment also incorporates analysis of the performance of individual syndicates, including the spread between the strongest and worst performers, with a particular focus on the potential exposure of central capital resources to losses from individual members.

Performance is subject to volatility, as illustrated by a standard deviation of 9.5% on the ten-year ROE ratio and on the ten-year combined ratio. The main source of volatility is the market's exposure to major losses including natural catastrophe losses. The market's performance in 2018 was impacted by a second consecutive year of higher than average major claims activity. Major losses added 11.6 points to the calendar-year combined ratio (2017: 18.5 points), compared to the five-year average of 8.2 points. However, this was partially offset by favourable reserve development and an improvement in the attritional loss ratio of 1.3 points, as modest rate increases and portfolio pruning started to earn through the portfolio. Prospective technical performance, assuming average catastrophe experience, is expected to improve, supported by the remedial actions being taken by the Corporation and taken by individual management agents. The long-term performance of the Lloyd's market is therefore expected to remain supportive of the strong assessment.

Underwriting Performance:

Underwriting performance is subject to volatility due to the market's exposure to catastrophe and other major losses. The market's net claims from major losses were GBP 2.9 billion in 2018, including losses from Hurricanes Florence and Michael, wildfires in California, and Typhoon Jebi. The level of major losses is in line with AM Best's expectations for Lloyd's given the catastrophe events during the year and the nature of business written.

The market's combined ratio once again benefited from favourable prior year reserve movements in 2018. Although releases were at a slightly higher level compared to 2017, they were below pre-2016 levels. Prior-year reserve movements improved the combined ratio by 4 percentage points in 2018 compared to 3 points in 2017, 5 points in 2016, and around 8 points each year in the period 2013-2015.

The market's operating expense ratio is high compared to peers at around 40%. The ratio has been relatively stable over the past five years, ranging between 39.2%-40.6%. Pre-2014 expense ratios were lower, ranging between 34.2%-37.1%, albeit still high relative to peers. An increase in acquisition costs due to a change in business mix, with more business written through coverholders, as well as costs associated with Solvency II implementation, partly explain the step change in the expense ratio.

The market's attritional accident-year combined ratio (excluding major claims and prior year movements) improved modestly from 98.4% in 2017 to 96.8% in 2018. However, accident-year combined ratios (excluding prior year movements) for most lines of business, excluding life, were above 100%, with only energy, motor, and life business achieving a calendar-year combined ratio below 100%. In AM Best's view, market participants are still impacted by soft market conditions, with continued pressure on pricing and terms and conditions.

For the 2018 business planning cycle, the Corporation's primary oversight activities included performance reviews and syndicate management. Actions were taken in response to weaker underlying performance as evidenced by the deterioration in the attritional loss ratio. The Corporation applied a risk-based approach to its oversight work, with a number of syndicates deemed to require additional oversight for various reasons. All syndicates over a certain size are included in this group due to their materiality to the market's performance overall.

In addition, the Corporation required all syndicates that had lost money for the past three years to agree with the oversight team a credible plan to return to profitability. The Corporation also announced that it would close down syndicates if they couldn't demonstrate a plan to sustainable profitability in the near term. Lloyd's is currently in the monitoring phase and expects syndicates to execute their action plans. The Corporation continues to expect syndicates to have credible plans to return to profitability and where plans cannot be agreed these syndicates will be closed. A similar approach was applied to underperforming portfolios, even within profitable syndicates, with the worst performing portfolios identified and remediation plans put in place.

Remedial activities continue in 2019 and a focus on growth in most profitable business classes, continued performance reviews, increased focus on expenses, and reinsurance optimisation strategies.

AM Best expects Lloyd's to report a combined ratio of below 100% for 2019, assuming a major loss loading in line with the long term average and a positive impact from reserve releases of 3 points. Attritional loss experience is expected to improve as a result of the actions taken by the Corporation, as well as by individual syndicate management teams. Overall underwriting performance will depend largely on the level of catastrophe experience.

Underwriting Performance by Line of Business:

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Operating Performance (Continued...)

The profitability of all lines of business over the past five-year period has been negatively affected by soft market conditions, with pressure on rates and terms and conditions.

The reinsurance book consists of property, casualty and specialty reinsurance. The performance of the overall book was affected by catastrophe losses in the property and marine segments in 2017 and 2018. Marine reinsurers were impacted by significant losses including the Lürssen shipyard loss, which had substantial reinsurance coverage as well as Hurricane Michael and Typhoon Jebi. Looking back over the past five years, 2014-2018, the reinsurance book has achieved strong overall underwriting profits.

The property book is a diversified worldwide book, although with some concentration to US excess and surplus lines business and to commercial risks. Performance in 2018 was affected by catastrophe losses and the segment suffered a significant loss for the year (GBP 700 million), albeit not as severe as the loss in 2017 (GBP 1.8 billion). Overall for the 2014-2018 period, the class returned a material underwriting loss driven primarily by the above-average major loss years of 2017 and 2018.

The casualty book is dominated by general liability and professional liability and also includes accident and health, cyber and warranty business. The combined ratio for this class has been just above 100% since 2015 and overall for the past five years, the class has made an underwriting loss on a calendar-year basis.

The marine book is well diversified and includes cargo, hull, marine liability, specie and fine art. The books performance in 2018 remained marginal as a series of large losses affected the cargo and hull classes, most notably the major Lürssen shipyard loss in September. The marine book has been historically profitable; however, losses since 2016 have led to an overall underwriting loss for the five-year period.

The energy book consists of onshore and offshore property and liability business. The book has made good profits over the past five years, including in 2018 on a calendar year basis. The accident year performance in energy was impacted by several substantial current year onshore property losses, balanced somewhat by benign loss activity for offshore property. With the inclusion of favourable prior year development the overall result was positive.

Motor business is focused on UK private car, commercial, and fleet business. International motor is also written; a large portion of which emanates from North America. Motor has made underwriting losses every year in the period 2014-2017, however the market saw robust price strengthening during 2018 following the Ogden discount rate change in February 2017, leading to a small underwriting profit in 2018.

The aviation segment includes airline, general aviation, space and war business. The segment has reported profits in two of the past five years. There were a few large losses in 2018, but overall major loss activity remained relatively benign. Airline and general aviation continued to be the main lines contributing to the negative result, alongside space, which experienced some large loss estimates.

Investment Performance:

Investment returns (including gains/losses) for the market were on average 1.6% in the period 2014-2018, ranging from 0.7% to 2.7%. The return of 0.7% in 2018 marks a low point in the period. In 2018, financial markets suffered from volatility in the last quarter of the year brought on by trade disputes, fears of a global slowdown, and geopolitical risk. The allocation, albeit conservative, to equity and risk assets generated losses for the year, but this was partially offset by positive returns in cash, government, and investment grade corporate bonds.

Performance on a Year of Account Basis:

On a traditional three-year accounting basis, the 2016 year of account closed at the end of 2018 with an overall loss of GBP 855 million (2015 year of account: profit of GBP 1,620 million). The 2016 year of account witnessed some above average risk losses, notably in the property sector, including Hurricane Matthew and the Fort McMurray wildfire.

The 2017 and 2018 years of account are both forecast to return overall losses, reflecting the major loss experience affecting both years.

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Operating Performance (Continued...)

Financial Performance Summary	2018 GBP (000)	2017 GBP (000)	2016 GBP (000,000)	2015 GBP (000,000)	2014 GBP (000)
Pre-Tax Income	-1,001,000	-2,001,000	2,107	2,122	3,016,000
Net Income after Non-Controlling Interests	-1,001,000	-2,001,000	2,107	2,122	3,016,000

Source: BestLink® - Best's Financial Suite

Operating and Performance Ratios (%)	2018	2017	2016	2015	2014
Overall Performance:					
Return on Assets	-0.9	-1.9	2.3	2.6	3.9
Return on Capital and Surplus	-3.7	-7.3	8.1	9.1	14.1
Non-Life Performance:					
Loss and LAE Ratio	65.3	74.5	57.3	49.9	49.2
Expense Ratio	39.2	39.5	40.6	40.1	39.3
Non-Life Combined Ratio	104.5	114.0	97.9	90.0	88.4

Source: BestLink® - Best's Financial Suite

Business Profile

Lloyd's favourable business profile reflects its strong position in the global general insurance and reinsurance markets as a leading writer of specialty property and casualty risks. Its network of global licences is a key competitive strength. The portfolio is well diversified but with some geographical bias towards North America and product bias towards commercial specialty lines products. Product risk is moderate to high. High product risk lines include reinsurance, energy, aviation, some marine business and a high proportion of the casualty and property business written. The majority of small commercial and consumer business, as well as some of the business written through coverholders is lower risk. The markets in which Lloyd's operates are highly competitive and have experienced soft market conditions for a number of years. A reliance on brokers makes Lloyd's particularly vulnerable to price-based competition.

Market Position:

Lloyd's occupies a strong position in the global general insurance and reinsurance markets as a leading writer of specialty property and casualty risks. The market's position is particularly strong in non-life reinsurance, where Lloyd's was ranked as the 4th largest global non-life reinsurer based on 2017 gross written premium (GWP).

Lloyd's is also a market leader in marine insurance, and has strong position in aviation, energy, and specialty property and casualty insurance. Although Lloyd's syndicates operate as individual businesses, the collective size of the market allows them to compete with major international groups under the Lloyd's brand. The competitive strength of Lloyd's comes from its strong brand and reputation for innovative and flexible underwriting, supported by the pool of underwriting expertise in London.

While Lloyd's position remains excellent in its core markets, it should be noted that the level of competition in these markets is very high.

Product Diversification and Product Risk:

Lloyd's is a significant writer of catastrophe and reinsurance business and is also a leading player in its core marine, aviation, energy and specialty property and casualty markets. Insurance business accounted for 69% of GWP in 2018 (2017: 69%), with reinsurance accounting for the balance. This split has been relatively stable in recent years.

Overall GWP increased by 5.8% in 2018, which is more modest than the circa 12.0% growth experienced in both 2017 and 2016. A significant driver of this growth in the prior years were movements in average rates of exchange, particularly for the US dollar against sterling. In 2016, there was only modest growth in premiums at constant exchange rates. In 2017, foreign exchange movements accounted for 6% growth in premiums.

The market is well diversified by line of business, although very little life business is written (0.2% of GWP in 2018) and there is a bias towards commercial lines business over personal lines. Product risk is moderate to high, as the business that comes to Lloyd's is predominantly specialty business that requires strong underwriting expertise. High product risk lines include reinsurance, energy, aviation, some marine business and a high proportion of the casualty and property business written.

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Business Profile (Continued...)

Reinsurance is the market's largest segment and accounted for 31% of GWP in 2018. Reinsurance business comprises property, casualty and specialty reinsurance (primarily marine, aviation and energy reinsurance). Lloyd's is a leading player in the global reinsurance market, ranking as the 6th largest risk carrier by reinsurance GWP based on 2017 premiums and the 4th largest when life premiums are excluded.

Property insurance business is Lloyd's second largest segment, which accounted for 27% of GWP in 2018. The property book is written on a global basis, but with some concentration towards US excess and surplus lines business. There is also a bias towards commercial risks with residential business written being mainly non-standard risks. The book also includes terrorism, power generation, engineering and nuclear risks.

Casualty business accounted for 26% of GWP in 2018. The book has a focus towards the US, but the UK, Canada and Australia are also significant markets. The main products written are general liability and professional indemnity. Accident and health business is also accounted for within this segment.

The remaining lines of marine (7%), energy (4%), motor (3%), aviation (2%) and life (0.2%) together accounted for 16% of GWP in 2018. Lloyd's is a leader in the global marine market, writing a diversified book, including cargo, hull, marine liability, specie and fine art. The energy book consists of onshore and offshore property and liability risks. The motor book is focused on the UK, covering commercial and personal motor business, with a focus on niche personal risks. An international book is also written, with a focus on North America. Aviation business includes airlines, general aviation, space and war risks.

Geographical Diversification:

Lloyd's writes a global portfolio, albeit with some bias towards North America, which accounted for 51% of GWP in 2018. The remainder was split 14% UK, 13% rest of Europe, 11% Central Asia and Asia Pacific, 4% other Americas and 4% rest of the world. The market's network of licences provides syndicates with access to a wide international client base, which is of benefit in particular to the syndicates that are not part of global insurance groups.

Lloyd's US domiciled business consists primarily of reinsurance and surplus lines insurance, which can be written in all 50 states. Participation in admitted US business (i.e. insurance business excluding surplus lines) is relatively modest. Lloyd's has admitted licences in Illinois, Kentucky and the US Virgin Islands and also writes insurance business in lines exempt from surplus lines laws (principally marine, aviation and transport risks).

In Canada, Lloyd's writes primarily insurance business, with reinsurance business accounting for a smaller share. In order to comply with local regulations, all Canadian business is written in Canada.

Over the past 20 years, Lloyd's has built out its licence network considerably, to be able to write insurance and/or reinsurance business in Brazil, Mexico, Colombia, Dubai, China, Singapore, and India, as well as a number of smaller markets. This work has been undertaken in response to the growth of local and regional (re)insurance hubs and the preference of clients to place business locally.

In order to maintain access to insurance business in the EU and wider European Economic Area (EEA) after a UK exit from the EU and its single market (referred to as "Brexit"), Lloyd's has established an insurance company domiciled in Belgium. Lloyd's Insurance Company S.A. (Lloyd's Brussels) is a wholly owned subsidiary of The Society of Lloyd's. The entity is incorporated, capitalised, and has received regulatory approval. It started writing business at 1.1.2019.

Membership of the single market allows UK-based insurance companies to conduct insurance business in all member states across borders. The establishment of an EU based insurance company enables the market to continue to write business in single market member states. However, the settlement of claims is also a regulated activity and Lloyd's may not be able to settle and pay claims on EEA business from London post-Brexit. In response to this, Lloyd's has initiated the process for a Part VII transfer, which would enable Lloyd's EEA insurance policies underwritten between 1993-2018 to be transferred to Lloyd's Brussels.

The unique Lloyd's structure subjects the market to heightened regulatory event risk, as the risk of it losing its licence in a jurisdiction following regulatory changes are higher than for an insurance company. The licencing of Lloyd's often relies on specific solutions and agreements that reflect its unique structure. A mitigating factor is the significant expertise and experience of Lloyd's in dealing with regulatory and licence issues.

Distribution:

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Business Profile (Continued...)

The distribution of Lloyd's business is dominated by insurance brokers, and in particular by the three largest global brokers. Lloyd's brokers play an active part in the placement of risks and in providing access to regional markets.

In addition, a significant part of Lloyd's business is distributed via coverholders (accounting for circa 30% of premiums), which write business on behalf of syndicates under the terms of a binding authority. Coverholders are important in bringing regional business to Lloyd's and providing the market with access to small and medium-sized risks. The growth in coverholder business in recent years has contributed to the higher expense ratio.

Lloyd's distribution model is expensive compared to that of its peers, with business often passing through several distribution links before arriving at Lloyd's. The reliance on brokers also makes the market vulnerable to price-based competition. Although the overall Lloyd's market is important to the large global brokers (as well as to the specialised London market brokers), individual syndicates are less important. Overall, the Lloyd's distribution model is considered to place the market at a competitive disadvantage compared to large global reinsurance groups, which have stronger individual positions with brokers as well as being able to distribute some of their business directly to cedants.

Modernisation Programme:

A comprehensive modernisation programme for the London market, the London Market Target Operating Model (TOM), was launched in 2015, the aim of which was to make operating in the London market, including at Lloyd's, more efficient and less expensive. Joint market initiatives underway include additional and improved functionality in respect of electronic back office and claim office transactions within the Central Services Refresh Programme, further implementation of e-trading via Placing Platform Limited (PPL) and on-going improvements to the Delegated Authority processes.

In 2018, the Corporation moved to mandate the use of e-trading via PPL. By the second quarter of 2018, Lloyd's syndicates were required to write no less than 10% of their risks on PPL, rising to 30% by the end of the fourth quarter. In addition, league tables of PPL usage are published to encourage use. Syndicates that met their target will received a rebate on their annual subscription, while those that didn't faced additional fees.

In AM Best's view, the modernisation programme is making important progress towards improving the efficiency of the market's operations. However, progress has been slow and the market is considered to be behind other global insurers in its adoption of technology. The fact that the Corporation has had to mandate use of the PPL to get usage past what is considered a critical mass is a sign of the market's resistance to change as well as dissatisfaction with the system among some of the underwriters and brokers that are asked to use it.

Off the back of the TOM project, on 1 May the new management team unveiled a modernisation plan called the Future at Lloyd's. The proposed reforms include plans to radically reduce the cost of doing business and creating new digital platforms for placing insurance risk and streaming claims services. If the plan is successfully implemented, meaningful cost reductions will support profitability. However, the plan is subject to a high degree of execution risk because it will likely require substantial investment and cultural change.

Lloyd's latest strategic plan is designed to increase access to the market while trimming costs. The plan focuses on such areas as complex risks, creating a risk exchange to handle less-complex business and making more flexible use of capital. It will also look at encouraging innovation, introducing a "next-generation claims service," and improving services to all market participants. Should Lloyd's be unsuccessful in its modernisation project and peers are able to widen the gap in both efficiency and the ease of doing business, the consequences could be considerable for the business profile.

Corporate Overview:

Lloyd's is the London-based market where approximately 90 individual syndicates underwrite all types of insurance and reinsurance business apart from long term life insurance. Each syndicate is formed by one or more members of Lloyd's, who join together to provide capital and accept insurance risks. Lloyd's members are mainly corporate members although a small proportion of Lloyd's underwriting capacity continues to be provided by private individuals.

In 1871, the then existing association of underwriters at Lloyd's was incorporated by the Lloyd's Act as the Society and Corporation of Lloyd's (referred to in this report as the Society or the Corporation which are used interchangeably in common usage), making the Society the legal entity which oversees the Lloyd's market. Its purpose is to facilitate the underwriting of insurance business by Lloyd's members, to protect members' interests in this context and to maintain Lloyd's Central Fund. The Society is also the holding company for Lloyd's Insurance Company S.A. and Lloyd's Insurance Company (China) Limited.

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Enterprise Risk Management

The enterprise risk management (ERM) of Lloyd's is considered supportive of an appropriate assessment. The market's enterprise risk framework is considered to be developed and risk management capabilities are aligned to the risk profile.

Lloyd's ERM is designed to manage risks arising from the market and the Society. It provides an extra layer of oversight over the market's risks which are also managed through the risk functions of individual managing agents. There are limitations on the ability of the Corporation to actively manage the market's risks, as it is supervising individual and competing syndicates each with their own risk appetites and commercial strategies. This limitation is reflected in AM Best's assessment of Lloyd's risk framework, which is viewed as developed rather than embedded.

Under the Lloyd's Act 1982, the Council of Lloyd's is responsible for the management and supervision of the market as the governing body of the Society. The Council delegates many of its functions to the board, the members of which are appointed by the Council and are drawn from both within and outside the Lloyd's market. The key committees of the board are the Audit Committee, the Market Supervision and Review Committee and the Risk Committee. The risk committee is responsible for the identification and management of Lloyd's key risks. From 1 January 2017, the risk committee became a non-executive committee, with members drawn from the Lloyd's Board and the Council. Lloyd's Chief Risk Officer, a position established in 2014, has a seat on the board.

The risk function has identified a number of key risk themes that are of particular concern for Lloyd's currently. Key risks include market performance, attractiveness of Lloyd's market, Brexit, operational resilience, cyber risk, financial crime, and failure to comply with relevant laws and regulations. Mitigating actions have also been identified.

The Board manages risks by setting and monitoring a risk appetite framework. A project to review and redefine all risk appetites (both market and central risk appetites) was completed at the end of 2017. The risk appetites are reviewed on a regular basis and may be updated as required. For example, staff behaviour is now to be included as separate risk. The framework includes 14 key risks and a number of underlying monitoring metrics. The risk appetites are structured under the three risk objective pillars of sustainability, solvency, and operational.

Over the past 2.5 years, there has been a much harsher tone and more active approach taken by the Corporation's oversight functions to managing under-performing syndicates as well as the under-performing lines of generally well performing syndicates. The executive team oversight has led to some syndicates being put into run-off as well as others having exited certain loss-making lines of business. Whether the Corporation's oversight functions are able to turn around the market's performance will be a key test of the effectiveness of the Board's activities.

The Society of Lloyd's and its managing agents are regulated by The Bank of England, acting through the PRA, as well as by the Financial Conduct Authority (FCA). In line with other insurers in the EU, Lloyd's is subject to the Solvency II regulatory and capital regime, which came into force on 1 January 2016. It applies to the "association of underwriters known as Lloyd's" as a collective entity. Although the UK's referendum vote to leave the EU has introduced uncertainty in respect of future regulation of the market, it is likely that the Solvency II form of regulation and capital regime will continue after a UK exit from the EU.

Lloyd's uses an internal capital model to calculate its SCR and SCR coverage ratio, with approval from the PRA. An internal model has been in use since 2012, although the current model has undergone radical change since then. In AM Best's opinion, the Corporation's ability to assess the capital adequacy of the market has been strongly improved by the modelling work undertaken for Solvency II.

Lloyd's recognises that one of the greatest risks to the Central Fund is the market's exposure to catastrophes. The Lloyd's catastrophe model (LCM) component of Lloyd's internal model allows the Corporation to assess catastrophe risk by syndicate, region-peril and class of business across return periods. It is fully embedded into Lloyd's Capital and Business Planning (CPG) process, assisting Exposure Management's recommendation for syndicate plan approval. The LCM is used to define the Tier 1 risk appetite for Exposure Management and through quarterly in-force tracking is an essential tool in managing catastrophe risk at both the syndicate and society level. In AM Best's opinion, this has improved its ability to monitor the market's aggregate catastrophe exposure against a defined risk appetite. Due to the nature of business written, Lloyd's has significant exposure to catastrophe losses, making this aspect of risk management particularly important.

Lloyd's Realistic Disaster Scenarios (RDSs) continue to play a critical role in exposure management at Lloyd's, both as benchmark stress tests validating the internal model output and as a source of data. The scenarios are defined in detail annually by Lloyd's and are used to evaluate aggregate market exposures as well as the exposure of each syndicate to certain major events. Syndicate-level scenarios are prepared by each managing agent, reflecting the particular characteristics of the business each syndicate writes. In addition, Lloyd's asks for syndicates' aggregate exceedance probability (AEP) loss at a 30-year return period for various regional perils. As the

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Enterprise Risk Management (Continued...)

Lloyd's RDSs represent different return periods for different syndicates, collecting this additional data helps to ensure a uniform treatment of syndicates' exposure to large losses.

Reinsurance Summary

Lloyd's use of reinsurance is relatively high when compared to large specialty insurers and reinsurers. This is due to the nature of the market, which consists of small-to-medium sized business that independently purchase reinsurance. The market as a whole ceded 27.7% of its GWP in 2018. This amount includes reinsurance from syndicates to their related groups as well as reinsurance between individual Lloyd's syndicates.

Lloyd's oversight function monitors individual syndicates' reinsurance placements to ensure the appropriateness and credit quality of the market's overall use of reinsurance.

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Financial Statements

Balance Sheet	12/31/2018 GBP (000)	%	12/31/2018 USD (000)
Cash and Short Term Investments	10,877,000	9.2	13,818,902
Bonds	41,679,000	35.3	52,951,919
Equity Securities	8,550,000	7.2	10,862,519
Other Invested Assets	10,134,000	8.6	12,874,943
Total Cash and Invested Assets	71,240,000	60.4	90,508,283
Reinsurers' Share of Reserves	23,394,000	19.8	29,721,375
Debtors / Amounts Receivable	18,167,000	15.4	23,080,628
Other Assets	5,207,000	4.4	6,615,337
Total Assets	118,008,000	100.0	149,925,624
Unearned Premiums	17,868,000	15.1	22,700,758
Non-Life - Outstanding Claims	60,450,000	51.2	76,799,912
Total Gross Technical Reserves	78,318,000	66.4	99,500,669
Debt / Borrowings	794,000	0.7	1,008,753
Other Liabilities	11,468,000	9.7	14,569,750
Total Liabilities	90,580,000	76.8	115,079,173
Other Capital and Surplus	27,428,000	23.2	34,846,451
Total Capital and Surplus	27,428,000	23.2	34,846,451
Total Liabilities and Surplus	118,008,000	100.0	149,925,624

Source: BestLink® - Best's Financial Suite
US $ per Local Currency Unit 1.27047 = 1 British Pound (GBP)

Income Statement	Non-Life GBP (000)	Life GBP (000)	Other GBP (000)	12/31/2018 Total GBP (000)	12/31/2018 Total USD (000)
Gross Premiums Written	35,527,000	...	...	35,527,000	45,135,988
	...	...	...	...	...
Net Premiums Earned	25,178,000	...	...	25,178,000	31,987,894
Net Investment Income	...	...	985,000	985,000	1,251,413
Realized capital gains / (losses)	...	...	-17,000	-17,000	-21,598
Unrealized capital gains / (losses)	...	...	-464,000	-464,000	-589,498
Total Revenue	25,178,000	...	504,000	25,682,000	32,628,211
Benefits and Claims	16,438,000	...	...	16,438,000	20,883,986
Net Operating and Other Expense	9,870,000	...	375,000	10,245,000	13,015,965
Total Benefits, Claims and Expenses	26,308,000	...	375,000	26,683,000	33,899,951
Pre-Tax Income	-1,130,000	...	129,000	-1,001,000	-1,271,740
Net Income before Non-Controlling Interests	...	...	...	-1,001,000	-1,271,740
Net Income/(loss)	...	...	...	-1,001,000	-1,271,740

Source: BestLink® - Best's Financial Suite
US $ per Local Currency Unit 1.27047 = 1 British Pound (GBP)

Related Methodology and Criteria

Best's Credit Rating Methodology, 12/20/2018

Catastrophe Analysis in A.M. Best Ratings, 10/13/2017

Available Capital & Holding Company Analysis, 10/13/2017

Rating Lloyd's Operations, 10/13/2017

Understanding Universal BCAR, 05/23/2019

A Best's Financial Strength Rating opinion addresses the relative ability of an insurer to meet its ongoing insurance obligations. The ratings are not assigned to specific insurance policies or contracts and do not address any other risk, including, but not limited to, an insurer's claims-payment policies or procedures; the ability of the insurer to dispute or deny claims payment on grounds of misrepresentation or fraud; or any specific liability contractually borne by the policy or contract holder. A Financial Strength Rating is not a recommendation to purchase, hold or terminate any insurance policy, contract or any other financial obligation issued by an insurer, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser.

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Credit risk is the risk that an entity may not meet its contractual, financial obligations as they come due. These credit ratings do not address any other risk, including but not limited to liquidity risk, market value risk or price volatility of rated securities. The rating is not a recommendation to buy, sell or hold any securities, insurance policies, contracts or any other financial obligations, nor does it address the suitability of any particular financial obligation for a specific purpose or purchaser.

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