Press Release

KBRA Assigns an "AA-" Insurance Financial Strength Rating to Lloyd's of London

DUBLIN (22 April 2021) – Kroll Bond Rating Agency Europe Limited (KBRA) assigns an AA- insurance financial strength rating (IFSR) to Lloyd's of London, the world's leading insurance and reinsurance marketplace. The Outlook for the rating is Stable.

Key Credit Considerations

The rating reflects Lloyd's sound risk-adjusted capitalisation, unique capital structure, conservative underwriting leverage, sound technical reserves, strong liquidity profile, diversified earnings sources, broad distribution channels and comprehensive risk management programme. Lloyd's capital has grown at a compound annual growth rate of 6.5% since end-2014 despite elevated catastrophe and attritional losses since 2016. At end-2020, Lloyd's market wide Solvency II ratio was 147%. Lloyd's unique capital structure incorporates multiple successive layers of claims paying resources. KBRA believes that the ability to request members to bring their capital in line after major loss events enhances Lloyd's overall financial strength. KBRA also believes that The Society of Lloyd's central Solvency II ratio of 209% at end-2020 indicates a strong backstop over and above the capital resources at the market level. Compared to the overall (re)insurance industry, Lloyd's maintains conservative premium and reserve leverage metrics. Net carried reserves exceed market and central actuarial best estimates. Lloyd's invests its assets conservatively and holds primarily cash and liquid, high credit quality fixed income securities. As one of the largest insurance underwriters in the world, Lloyd's writes business across all major sectors and covers over 60 lines of insurance and reinsurance in more than 200 countries and territories. Slightly more than 50% of gross premiums emanate from the U.S. and slightly more than one-third of Lloyd's business consists of reinsurance. KBRA believes that Lloyd's credit profile is enhanced by its constantly expanding, multi-jurisdiction distribution network that allows it to proactively select business that meets its risk/return benchmarks. Lloyd's has a robust, dynamic risk management framework and processes characterized by well-articulated risks and conservative risk tolerances which are regularly monitored and subject to various stress tests and scenario analysis.

Balancing these strengths are recent unfavourable underwriting performance, an elevated expense ratio, heavy reliance on reinsurance and exposure to event risk. While Lloyd's has reported a cumulative result before tax from 2015 – 2020 of £2.9 billion, the result has been driven solely by investment income as underwriting losses for the same period were £4.5 billion. While much of the underwriting loss is attributable to major and catastrophe events, including £3.4 billion in incurred losses in 2020 for COVID-19, more concerning to KBRA are the elevated attritional losses since 2017, somewhat offset by Lloyd's continued focus on performance management which has generated a trend of improving results by capitalising on the current price firming across the industry. Lloyd's focus on performance management includes increasing rates, reducing exposures in unprofitable classes, and growing the best performing syndicates and remediating, or removing, the worst ones. KBRA notes that attritional loss experience in 2020 moved in line with targets, although attritional loss experience that remains in line over the medium term will be a significant indicator of long-term underlying underwriting profitability. KBRA expects that the Future at Lloyd's programme may mitigate Lloyd's elevated expense ratio over the medium to longer term but believes that implementation presents material execution risk as the programme is large and complex and Lloyd's cannot mandate adoption of new digital processes and practices by managing agencies. Since each syndicate structures and purchases its own reinsurance programme, Lloyd's is more heavily dependent on reinsurance than peers who utilise reinsurance more strategically although this weakness is partially offset by central management's detailed monitoring of counterparty credit risk across the Lloyd's market. Due to the broad lines of business the market writes and its wide geographic footprint, Lloyd's incurs claims for most catastrophic events around the world. While exposure to catastrophes is partially mitigated by appropriate risk tolerances and high-credit quality reinsurance, KBRA expects Lloyd's to continue to provide material cover for large loss-generating events going forward.

Rating Sensitivities

Meaningful reduction in the number of syndicates subject to increased oversight, consistent attritional underwriting performance over the medium term and successful execution of the Future at Lloyd's programme could result in a positive rating action.

Continued unfavourable, or inconsistent, underlying underwriting performance over the medium term, meaningful reduction in capital or a drop in Solvency II ratios below Lloyd's minimum targets could result in a negative rating action.

ESG Considerations
In December 2020 Lloyd's published its first ESG Report, reflecting its commitment to address ESG factors that are important to various stakeholders. As Lloyd's makes progress in fulfilling its commitments to its ESG targets, the insurance financial strength rating may be influenced over the medium to longer term.

A full report will soon be available on www.kbra.com.

To access ratings and relevant documents, click here.

Related Publications

- Insurer & Insurance Holding Company Global Rating Methodology
- Credit Ratings Deserve ESG Risk Analysis, Not ESG Scores
- Carbon Pricing and its Potential Credit Impact

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Disclosures
A description of all substantially material sources that were used to prepare the credit rating and information on the methodology(ies) (inclusive of any material models and sensitivity analyses of the relevant key rating assumptions, as applicable) used in determining the credit rating is available in the Information Disclosure Form(s) located here.

Information on the meaning of each rating category can be located here.

This credit rating is endorsed by Kroll Bond Rating Agency UK Limited for use in the UK. Information on a credit rating's endorsement status is available on its rating page at KBRA.com.

Further disclosures relating to this rating action are available in the Information Disclosure Form(s) referenced above. Additional information regarding KBRA policies, methodologies, rating scales and disclosures are available at www.kbra.com.

About KBRA Europe
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