GENERAL INSURANCE RATING METHODOLOGY

INTRODUCTION

Insurer Financial Strength (IFS) rating of a General insurance company assesses the financial strength of an insurance company and its capacity to meet obligations to policyholders on a timely basis. The financial strength rating is assigned to the company itself, and no liabilities or obligations of the insurer are specifically rated unless otherwise stated. The financial strength rating does not address the willingness of management to honor company obligations, nor does the rating address the quality of a company's claims handling services. In the context of the financial strength rating, the timeliness of payments is considered relative to both contracts and/or policy terms and also recognizes the possibility of acceptable delays caused by circumstances unique to the insurance industry, including claims reviews, fraud investigations and coverage disputes.

METHODOLOGY

NCR's analyses incorporate an evaluation of the rated company's current financial position as well as an assessment of how the financial position may change in the future. Our ratings methodology includes an assessment of both quantitative and qualitative factors based on in-depth discussions with senior management. The evaluation of financial strength and credit quality focuses on the ability of the company to meet all of its obligations.

NCR's rating methodology focuses on the following five areas of analysis:

- Industry Review
- Operational Review
- Organizational Review
- Management Review
- Financial Review

INDUSTRY REVIEW

The starting point for NCR's ratings is a thorough understanding of the industry in which the insurer operates. One of NCR's goals is to judge the extent industry dynamics can impact the ratings levels that individual insurers operating in a given industry segment can achieve. NCR also uses its industry analysis to allow it to make better judgments' on the unique attributes of individual insurers by being able to understand them on a relative as well as absolute basis. NCR's specific evaluation of the general insurance industry focuses on:

i. Level of competition in specific sectors, and how variable competition has been over time.
ii. The basis for competitive advantage in the sector.
iii. Barriers to entry and threats of new products
iv. The potential "tail" of losses and ability to make accurate pricing decisions, as well as exposure to large unexpected losses
v. Regulatory, legal and accounting environment and framework.

OPERATIONAL REVIEW

NCR's operational review focuses on a given company's unique competitive strengths and weaknesses, operating strategies, and business mix. NCR's analysis focuses on both the

historical and current business position and how it is expected to change over time.

NCR believes that its operational analysis is among the most critical parts of its ratings review. Companies that have strong balance sheets and acceptable risk exposures can provide near-term financial strength.

However, for high levels of credit quality and financial strength to be maintained over the long-term, the company must exhibit favorable operating characteristics. NCR's operational review includes an evaluation of:

- Underwriting expertise and market knowledge
- Distribution capabilities and mix
- Classes of business and changes in mix
- Market share and growth
- Brand name recognition and franchise value
- Expense efficiencies and operational scale
- Product and geographical mix
- Administrative and technological capabilities

The operational review includes a significant degree of qualitative judgment. There is a delicate balance that needs to be maintained between attaining growth and market share, and maintaining underwriting discipline. NCR places underwriting expertise and market knowledge as the most important operational attributes of a highly rated general insurance company.

ORGANIZATIONAL REVIEW

NCR places importance on the influence of the owners on the company and the extent of financial support they would extend in case of any emergency. Moreover, NCR also assesses the credibility, market reputation and experience of the owners in the relevant field.

MANAGEMENT REVIEW

One of the most difficult, yet critical aspects of NCR's rating process is the level of confidence we develop in the management team and its stated strategies. NCR has found that the ability of management to establish a "performance-based" culture, and have in place an appropriate risk/reward system, is a key determinant to overall success. Our specific evaluation of management focuses on the following:

- Strategic vision
- Appetite for risk
- Credibility and track record for meeting expectations
- Controls and risk management capabilities
- Depth, breadth, and succession plans
- Accomplishments of key executives

FINANCIAL REVIEW

NCR's financial review includes the calculation of numerous financial ratios and other quantitative measurements. These are evaluated based on industry norms, specific rating benchmarks, prior time periods and expectations developed by NCR specific to the rated entity. Though the financial review is largely a quantitative exercise, the interpretation of the results and weighing them into the final rating includes significant elements of

subjectivity and qualitative judgment.

In addition to the published financial statements NCR examines the management reports, evaluations and company projections. The financial review is broken into seven main segments:

- Underwriting quality
- Profitability
- Investments
- Reinsurance utilization
- Reserves and Capital adequacy
- Liquidity

UNDERWRITING QUALITY

The evaluation of underwriting quality, especially for insurers in higher risk classes of business, is the first part of the financial review and in many ways the most important. NCR's goal is to judge the overall health of the book of business, and management's understanding of its risks and ability to control them. Key areas considered include:

- Underwriting expertise in each class of business
- Pricing credibility
- Pricing flexibility given competitive and regulatory environment
- Exposure to large losses
- Balance of premium growth and underwriting discipline
- Controls over any third party underwriters, such as managing general agents
- Claims management and expertise
- Expense efficiencies, and impact of ceding commissions on expense ratios

NCR measures underwriting performance using two common ratios – the loss ratio and the expense ratio. To properly interpret these ratios, NCR considers the company's business mix, pricing strategy, accounting practices, distribution approach and reserving approach. NCR examines these ratios for the company as a whole, and by each category. NCR also looks at underwriting results both before and after the impact of ceded reinsurance. The combination of the loss and expense ratios is referred to as the combined ratio. A combined ratio below 100% translates into an underwriting profit, and above 100% represents an underwriting loss. NCR also evaluates underwriting quality in the context of growth in premiums and revenues. NCR tries to understand how premium growth is influenced by changes in pricing versus growth in exposures. NCR generally prefers to see reasonably steady and even growth trends, and is concerned by both excessive growth and negative growth. Growth is evaluated in the context of market conditions and strategic initiatives of the insurer.

PROFITABILITY

The focus of NCR's analysis of profitability is to understand the sources of profits, the level of profits on both and absolute and relative basis, and potential variability in profitability. Profits for general insurers are sourced from two primary functional areas --underwriting and investment income. As indicated above, profits from underwriting are generated when correlates with the level of risk that is being assumed.

Profits derived from investments can take the form of interest, dividends and capital gains and can vary as to their taxable nature. The level of investment earnings is dictated by the

investment allocation strategy and the quality of management. Like underwriting income, investment returns and their volatility are also correlated with the level of risk assumed. NCR measures overall profitability (underwriting and investing) by calculating the company's operating ratio. To further understand the quality of earnings, NCR evaluates the diversification of earnings, as earnings that are well diversified tend to be less volatile. NCR also calculates the following standard profitability ratios: return on assets (ROA) and return on equity (ROE).

NCR is very careful in interpreting the ROE and ROA ratios, since they are influenced by not only overall profitability levels, but also the degree of operating and financial leverage. NCR also emphasizes on the stability and growth pattern, on Year on Year basis, of the underwriting profits and other supporting sources of income.

INVESTMENTS/LIQUIDITY

NCR's analysis of the investment portfolio focuses on credit risk, market risk, liquidity and historical performance. As part of NCR's analysis, the company's investment guidelines and management controls are also evaluated to understand how the investment portfolio may change over time. NCR examines credit risk by looking at the company's exposure to higher risk investments relative to the total investment portfolio and capital base. Overall diversification of the investment portfolio by major asset class and industry sector is also evaluated to identify any concentration issues.

Market risk is evaluated to identify potential changes in asset valuation due to a change in market conditions and the interest rate environment. Historical investment performance is evaluated to determine how well the company's investment strategies are executed. NCR examines the company's investment yield, total return, duration and maturity structure, and historical default experience. Volatility of investment valuations is considered in the context of both book value and underlying market (liquidation) values.

REINSURANCE UTILIZATION

In assessing an insurer's use of reinsurance, NCR's goal is to determine if capital is adequately protected from large loss exposures, and to judge if the ceding company's overall operating risks have been reduced or heightened. In the traditional sense, reinsurance is used as a defensive tool to lay off risks that the ceding company does not want to expose to its earnings or capital. When reinsurance is used defensively, NCR's goal is to gain comfort that:

- Sufficient amounts and types of reinsurance are being purchased to limit net loss exposures given the unique characteristics of the book
- Reinsurance is available when needed
- The cost of purchasing reinsurance does not excessively drive down the ceding company's profitability to inadequate levels, and weaken its competitive pricing posture
- The financial strength of reinsurers is strong, limiting the risk of uncollectible balances due to insolvency of the reinsurer.
- Exposure to possible collection disputes with troubled or healthy reinsurers is not excessive

Reinsurance can also be used aggressively an potentially add to risk. In such cases, NCR examines why the reinsurance approach is being used, and stresses what would happen if the programmed developed adversely. Examples of aggressive use of reinsurance include excessive cessions under quota share treaties simply to earn ceding commissions, and use

of finite or other financial reinsurance that "smooth results" rather than transfer risk as the core part of the reinsurance programme.

RESERVES AND CAPITAL ADEQUACY

Reserve adequacy is a critical part of the financial review, and a demonstrated ability to maintain an adequate reserve position is a crucial characteristic for a highly rated insurer. While the analysis of reserve adequacy includes a robust quantitative element, much of NCR's reserve review is qualitative in nature. Accordingly, our review focuses on the following:

- Historical track record in establishing adequate reserves
- Management's reserving targets
- Key reserving assumptions
- General market and competitive pricing environment, and propensity of management to carry weaker reserves during down cycles
- Use of discounting, financial reinsurance or accounting techniques that reduce carried reserves
- Comparison of company loss development trends relative to industry and peers

There is significant overlap in NCR's qualitative analysis of underwriting quality and reserve adequacy, as NCR believes the two generally go hand in hand. Most insurers with lax underwriting standards will also have ineffective reserving standards, and vice versa. Inadequate reserving can thus result in poor pricing decisions on current and future business. NCR's evaluation of capital adequacy and profitability are also closely linked with its assessment of reserve adequacy.

NCR assesses the level of Capital in relation to underwriting business and reinsurance by calculating the premium solvency ratio and adequacy of the loss reserve is measured through reserve solvency ratio. Moreover, solvency ratio (calculated according to statutory standards) is also evaluated. These analyses help in establishing the extent of the company's capacity to meet its obligations both in absolute and relative terms.

Future capital needs based on business growth and other factors are also considered in NCR's analysis. Financial flexibility, or the company's ability to access internal and external capital sources, is an important ratings factor. In good times, the ability to access capital to support growth while maintaining capital adequacy is critical to maximizing the franchise value. In bad times, maintaining the confidence of the capital markets and lenders can prove critical in allowing accompany to avoid problems such as an inability to refinance maturing debt. Financial flexibility is derived first from the overall quality and reputation of the financial leverage, debt service coverage and liquidity

LIQUIDITY

In short-tail insurance sectors, liquidity is particularly important. NCR judges liquidity based on the marketability of the investments. The manner in which the company values its assets on the balance sheet is also closely examined.

NCR evaluates trends in operating and underwriting cash flows to judge liquidity at the operating company level. NCR also considers cash flows in the context of future levels of investment income generated by a shrinking or growing portfolio. Off balance sheet sources of liquidity, including committed and uncommitted lines of credit, asset securitization and other funding arrangements, are also considered.