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Fitch Downgrades Insurance Hybrids on Revised Criteria Ratings

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Fitch Ratings-London/Chicago/Frankfurt-29 January 2010: Fitch Ratings has taken rating actions on over two hundred preferred and hybrid capital instruments of issuers in the insurance sector to implement revised guidelines for rating preferred stock and hybrid securities that Fitch published recently ('Rating Hybrid Securities', 29 December 2009). A full list of affected securities is shown in a spreadsheet entitled 'Insurance Hybrid Rating Actions' available at www.fitchratings.com. http://www.fitchratings.com/creditdesk/reports/report_frame?rpt_id=498128

The new guidelines apply to instruments issued by companies in all sectors, including banks, insurers, non-bank financial institutions, and non-financial corporate entities. The new guidelines typically resulted in downgrades of one notch for many deferrable instruments that are currently performing, while those performing hybrids with more material loss absorption provisions or with triggers for loss absorption that are easily triggered were subject to a two notch (or greater) downgrade. The new criteria also provided guidance on how Fitch will rate and notch hybrids and preferred securities at different stages in the "life cycle" of an instrument.

As noted on 29 December 2009 in its comment 'Fitch Announces Forthcoming Changes in Insurance Hybrid Securities Ratings', Fitch's previous notching methodology for hybrid securities did not explicitly consider the risk of going-concern loss absorption, such as deferral risk, as a factor in rating a hybrid unless deferral appeared likely (or had occurred). Under its revised methodology, Fitch now considers the presence of a going concern loss absorption feature as a risk to be reflected in ratings even in periods when the likelihood of deferral appears remote.

Under the new hybrid rating methodology, insurance hybrids with going-concern loss absorption (e.g. deferral) that are issued or guaranteed by operating companies are typically rated two to three notches below the insurer's Issuer Default Rating (IDR). Although more detail is provided in the criteria, the wider notching is most commonly used either where the trigger is viewed as easily activated (e.g. an annual profits test) or where the form of going concern loss absorption is considered to be particularly aggressive and therefore, meriting further notching. Examples of more aggressive forms of loss absorption typically include features such as contingent conversion to equity or a permanent write-down to a hybrid issue.

For those hybrids that are either issued or guaranteed by insurance holding companies, hybrid securities are typically notched three to four notches from the relevant holding company IDR. The wider notching from the holding company IDR is consistent with Fitch's prior treatment of hybrid security notching as most hybrids have historically been rated two notches below the holding company IDR compared to one notch for most hybrids at the operating company level. This wider notching continues to reflect Fitch's assumption that these issues are likely to have weaker recoveries in the event of default compared to insurance operating companies as a result of deeper legal subordination.

Certain preferred and hybrid securities are not subject to any rating change as a result of the new criteria. Straight subordinated debt without any deferral or going-concern loss absorption features is not subject to any change in notching. Hybrid instruments that have deferred or are deemed close to deferral have generally not been affected by the new criteria. In most of these cases, ratings have already moved beyond the standardized notching. In addition, the new criteria have already been implemented in a few instances where Fitch took a rating action on an issuer subsequent to the criteria change announcement on 29 December 2009. Hybrid securities with ratings that have been deemed unaffected by the implementation of the new criteria are not listed on the spreadsheet shown on Fitch's website.

Applicable criteria, 'Insurance Rating Methodology', 'Rating Hybrid Securities' and 'Insurance Industry: Global Notching Methodology and Recovery Analysis', all dated 29 December 2009, are available on www.fitchratings.com.

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