January 9, 2012

Rating Outlooks Held at Stable for Personal Lines, Negative for Commercial Amid Catastrophes, Competition

Divergent trends are influencing rating outlooks for the various segments of the property/casualty industry, with personal lines continuing to benefit from solid performance in auto insurance, and commercial lines carrying on the struggle to turn pricing decisively upward. Balance sheets remain strong but susceptible to threats in both segments. Specific outlooks are discussed below.

Personal Lines: Stable

A.M. Best continues to maintain a stable outlook in 2012 for the personal lines segment. The stable outlook implies that the majority of 2012 rating actions for this segment are likely to be affirmations, with a fairly balanced distribution of negative and positive rating actions.

Similar to the past several years, results in the personal lines segment reflect two divergent trends among the segment's main lines of business – automobile and homeowners. On one hand, the auto line continues to perform well, with generally adequate and stable returns. This is in contrast to the extreme volatility associated with the property lines of business due to the effects of continued weather-related losses.

Given that the auto line represents more than 60% of the segment's net written premium, the outlook remains stable. While some geographically and property concentrated writers recently have come under rating pressure, A.M. Best believes that from an overall segment perspective, maintaining the stable outlook is appropriate at this time.

While the property line's volatility has not materially weakened the segment's overall capital position, it remains a drag on overall results. Accordingly, there is less room for additional deterioration in results than there was in previous years. A.M. Best believes the personal lines segment is adequately positioned to handle a "normalized" weather year without a corresponding change in the outlook. Conversely, a continuation of frequent, severe weather events in 2012 beyond expectations likely will lead A.M. Best to re-evaluate the segment's outlook.

Commercial Lines: Negative

Despite a mending economy and some encouraging signs of price firming, A.M. Best maintains its negative outlook for the commercial lines segment for 2012. This outlook implies that while the vast majority of rating actions will be affirmations, negative rating actions will outnumber positive rating actions during the year.

Although growing numbers of leading commercial lines insurers express publicly the need for rates to increase, premium growth in the segment is on the upswing for the first time in five years. While these recent pricing trends are both encouraging and noteworthy, A.M. Best remains skeptical that a long-term reversal in market pricing has arrived and believes insurance cycles are measured in years, not in quarters. That being said, any benefit will be incremental.

Given the fragility of the U.S. economy, the willingness and resolve of insurers to sustain further positive rate momentum in the small to midsize accounts will be tested by the purchasing power of Main Street American businesses – many of which are already strained by sluggish economic growth. As for large accounts, any increase in pricing will face pressure from insurance brokers and risk managers. Despite these headwinds, further pricing momentum through 2012 is expected for certain lines of business such as commercial property and workers' compensation.

Balance sheets of commercial lines insurers, while relatively strong, are expected to show continued erosion in loss-reserve adequacy. Workers' compensation and general liability already have turned from favorable to modestly adverse reserve development. A.M. Best believes reserve charges will become more common in 2012 than in the recent past, as more insurers have reported optimistic recent accident-year results.

While the commercial lines outlook remains negative, A.M. Best does not expect rating actions to move profoundly negative, as abundant capital and investment income continue to generate operating cash flows, positive earnings and continued growth in surplus. For some, however, marginal capital and low interest rates have forced greater emphasis on underwriting profitability to avoid negative rating actions.

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SR-2012-B-001