

## **FITCH AFFIRMS ADMIRAL'S IFS RATING AT 'A+'; OUTLOOK STABLE**

Fitch Ratings-London-06 July 2017: Fitch Ratings has affirmed Admiral Insurance (Gibraltar) Limited's and UK-based Admiral Insurance Company Limited's - the two main operating entities of Admiral Group plc (Admiral) - Insurer Financial Strength (IFS) Ratings at 'A+' (Strong). The agency has also affirmed Admiral's Long-Term Issuer Default Rating (IDR) at 'A' and subordinated notes at 'BBB'. The Outlook on the IFS Ratings and IDR is Stable.

### **KEY RATING DRIVERS**

The affirmation reflects Admiral's very strong financial performance and earnings, strong capitalisation, which benefits from significant use of co-insurance and reinsurance arrangements, continuing leading position in the UK motor insurance market, and prudent reserving practices. The ratings are constrained by Admiral's medium scale and a concentrated business profile.

Fitch views Admiral's track record of technical profitability as very strong and expects that Admiral will maintain its robust underwriting performance. In 2016, Admiral's underwriting results were impacted by a change in the Ogden discount rate used to calculate lump-sum payments in large bodily injury cases in the UK. The significant reduction in the Ogden discount rate to -0.75% from 2.5% meant that UK insurers had to substantially increase their reserves held for open and not yet notified claims on business earned prior to the change. As a result, Admiral's profit before tax for 2016 fell to GBP284 million, from GBP390 million on a pre-Ogden basis, and Admiral's reported combined ratio deteriorated to 94.4% (86.7% pre-Ogden and 85.6% in 2015). Earnings are expected to be reduced by a further GBP65 million over the next three to five years in total as a result of lower reserve releases and profit commissions.

Admiral implemented price increases on UK motor insurance ahead of the announcement on the new Ogden discount rate and further price increases following the change in the discount rate, helping it to mitigate some of the Ogden impact. Fitch views positively Admiral's ability to implement price changes within a short time, allowing the group to respond rapidly to changing market conditions.

Admiral's capital position is 'Extremely Strong' as measured by Fitch's Prism Factor-Based Model (FBM) capital score. The insurer's financial profile, including capitalisation, benefits from significant use of co-insurance and reinsurance arrangements, with Admiral sharing 30% of its UK motor insurance risks on a co-insurance basis and 10% on a quota share basis with Great Lakes, a subsidiary of Munich Re (IFS AA/Stable). The arrangements with Great Lakes are secured under multi-year contracts until 2020 and further quota share agreements are in place until at least 2018, providing substantial capital relief to Admiral. Fitch views the credit quality of Admiral's co-insurance and reinsurance counterparties as very strong.

Admiral's ratings are constrained by a concentrated business profile. UK car insurance is the main contributor to the group's profits and accounts for 83% of total net premiums earned. While Admiral's international operations are developing well, they are still small relative to the overall group.

Fitch takes a positive view of Admiral's prudent reserving strategy. Over the past 10 years, Admiral's prior-year reserve releases, excluding reserve releases on commuted reinsurance, averaged 14% of net premiums earned. The insurer's strategy is to maintain a buffer above

actuarial best estimate, allowing the group to support underwriting results with reserve releases every year.

## RATING SENSITIVITIES

A marked deterioration in technical or overall profitability, particularly compared with peers, could result in a downgrade. A downgrade could also be triggered by a substantial erosion of capital equivalent to a sustained increase in net underwriting leverage (net written premiums/equity) to 1.5x (2016: 1.0x).

A downgrade may also result from a loss of Admiral's co-insurance contract, resulting in an immediate and significant increase in capital requirements or significant falls in business volumes.

An upgrade is unlikely in the medium term given Admiral's concentrated business profile and limited geographical diversification.

Contact:

Primary Analyst

Ekaterina Ishchenko

Associate Director

+44 203 530 1532

Fitch Ratings Limited

30 North Colonnade

London E14 5GN

Secondary Analyst

Graham Coutts

Director

+44 203 530 1654

Committee Chairperson

Chris Waterman

Managing Director

+44 203 530 1168

Media Relations: Athos Larkou, London, Tel: +44 203 530 1549, Email: athos.larkou@fitchratings.com.

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

Applicable Criteria

Insurance Rating Methodology (pub. 26 Apr 2017)

<https://www.fitchratings.com/site/re/897260>

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