FitchRatings

Insurance
Composite Insurers
United States

HCC Insurance Holdings, Inc.

And Insurance Subsidiaries

Key Rating Drivers

Ownership Limits Ratings: HCC Insurance Holdings, Inc. (TMHCC) was acquired by Tokio Marine Holdings, Inc. (TMHD) in October 2015 for $7.3 billion. The core operating subsidiaries of TMHD were recently affirmed with a 'AA–' Insurer Financial Strength (IFS) rating with a Stable Outlook, and are two notches above the Japan local-currency sovereign rating of 'A' with a Negative Outlook. The standalone assessment of TMHCC is a 'AA' IFS rating.

Manageable Coronavirus Losses: Losses from the coronavirus pandemic added approximately 6 percentage points on the combined ratio in 2020. Losses weve primarily in the North American property/casualty (P/C) segment and related to U.S. event cancellation, though the company also incurred a loss from the postponement of 2020 Tokoyo Olympics. The elevated pandemic losses also drove the large increase in reinsurance recoverables. Favorably, the company uses high-rated reinsurers and had over half of the gross recoverable collaterized at YE 2020.

Consistently Favorable Underwriting Results: TMHCC is a diversified specialty underwriter that maintains a strong market position in a number of narrowly defined, less correlated insurance lines. The company targets a long-term average combined ratio of 88% with its current mix of business. From fiscal 2016 to 2020, the combined ratio averaged 90%. Despite the elevated losses from the pandemic in 2020, the company still reported a combined ratio of 93%.

Very Strong Underwriting Culture: TMHCC compensates both underwriters and executive officers to encourage a focus on both short-term and long-term profitability. The compensation strategy and underwriter accountability facilitates the company's generation of consistently solid underwriting results throughout market cycles.

Leader in Specialty Markets: TMHCC operates in lines of business where underwriting skill and analytics can create superior returns long term, and limits activity in segments that compete solely on price. Above-average, long-term performance is also a function of underwriting discipline and a willingness to shrink the premium base as market forces dictate. Additionally, TMHCC is a leader in several niche markets, which gives the company a competitive advantage over peers.

Very Strong Capitalization: Fitch Ratings views TMHCC's P/C insurance subsidiaries' capitalization as very strong based on operating leverage of 0.8x, a preliminary 'Extremely Strong' Prism score, 17% financial leverage ratio and has very high fixed-charge coverage due to low interest rates on debt as of YE 2020.

Rating Sensitivities

Downgrade Sensitivities: A downgrade of TMHD's operating company Issuer Default Rating (IDR), or a two-notch or more downgrade in TMHCC's standalone assessment, could lead to a downgrade. Fitch believes it is unlikely that any potential future downgrade of the TMHCC ratings would be to levels lower than those of the parent.

Upgrade Sensitivities: Fitch views a rating upgrade as unlikely, but an upgrade of TMHD's ratings could result in an upgrade to TMHCC's ratings.

Ratings

HCC Insurance Holdings, Inc.

IDR	A–

Operating Companies

Insurer Financial Strength	AA–

Outlook

Stable

Financial Data

HCC Insurance Holdings, Inc.

($ Mil.)	2019	2020
Net Income	376	215
Total Capital	5,903	6,319
ROE (%)	8	4
Combined Ratio (%)	90	93

Note: GAAP and excludes Privilege Underwriters, Inc. and subsidiaries.
Source: Fitch Ratings; HCC Insurance Holdings, Inc.

Applicable Criteria

Insurance Rating Criteria (April 2021)

Related Research

HCC Insurance Holdings, Inc. – Ratings Navigator (Augustl 2021)

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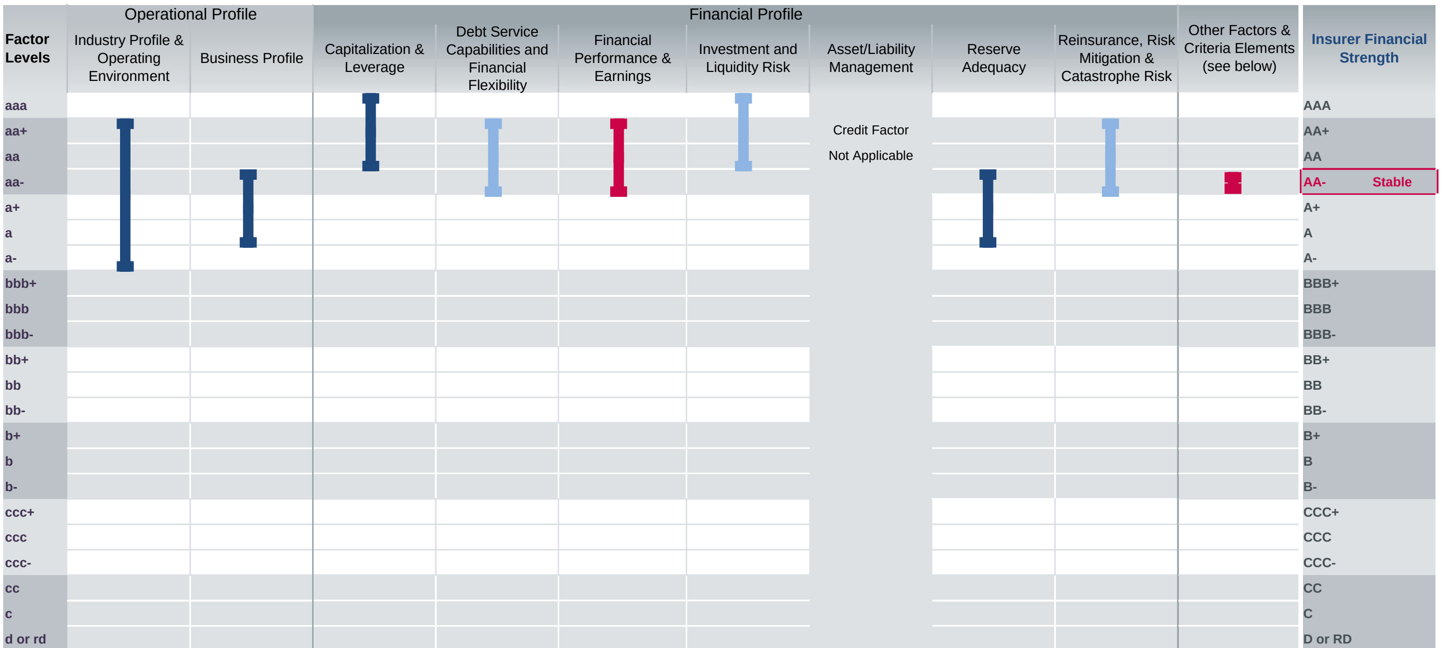
Key Credit Factors — Scoring Summary



Other Factors & Criteria Elements				
Provisional Insurer Financial Strength				**AA**
Non-Insurance Attributes	Positive	**Neutral**	Negative	+0
Corporate Governance & Management	**Effective**	Some Weakness	Ineffective	+0
Ownership / Group Support	Positive	Neutral	**Negative**	-1
Transfer & Convertibility / Country Ceiling	Yes	**No**	AAA	+0
Insurer Financial Strength (IFS)			Final:	**AA-**
IFS Recovery Assumption	**Good**			-1
Issuer Default Rating (IDR)			Final:	**n.a.**

Bar Chart Legend

Vertical Bars = Range of Rating Factor
Bar Colors = Relative Importance
Higher Influence
Moderate Influence
Lower Influence
Bar Arrows = Rating Factor Outlook
⇧ Positive ⇩ Negative
⇳ Evolving ◽ Stable

Latest Developments

- Fitch made no changes to TMHCC's rating and subfactors scores from prior-year analaysis.

Peer Comparison

Click here for a report that shows a comparative peer analysis of key credit factor scoring.

Industry Profile and Operating Environment (IPOE)

Click here for a link to a report that summarizes the main factors driving the above IPOE score.

Business Profile

Favorable Profile

TMHCC is a stock company that is 100% owned by TMHD, which is based in Japan and has a business profile score of ‘aa+’ by Fitch. TMHD has actively acquired several other U.S.-based insurers over time, including: Delphi Financial Group (2012) and Philadelphia Insurance Companies (2008). Approximately 36% of TMHD’s operations at YE 2020 were from outside of Japan. TMHCC’s operations are managed separately from other TMHD U.S. operations, but there are various levels of collaboration and shared services among subsidiaries.

TMHCC’s primary product offerings include agriculture, aviation, property, energy, marine, directors and officers liability, professional liability, surety, credit and other specialty risks that are lowly correlated. Additionally, the company is a market leader in medical stop-loss coverage. The company divides its operations into three key segments: North America Property & Casualty, Accident & Health and International.

Favorable Competitive Positioning

Competitive positioning is comprised of two subfactors: general and operating scale. Together these factors aggregate into a favorable position. TMHCC has a leading business franchise within the sector and strong competitive advantages that are partly derived from its franchise. As of YE 2020, the company reported net written premiums of $4.0 billion and shareholders’ equity of $5.2 billion.

Favorable Risk Profile

TMHCC’s risk appetite is lower than the sector as a whole and focuses on stable and established lines of business. In particular, the company’s expertise as a specialty writer is to obtain adequate rate for the risk that is underwritten. By direct premiums, the largest P/C line of business underwritten is crop insurance.

Ownership Is Negative to the Rating

TMHCC is a specialty insurance group formed in 1974, based in Houston and acquired by TMHD in October 2015 for $7.3 billion. Fitch’s standalone rating of TMHCC is one notch higher than current ratings as ownership reduces the ratings by one notch.

Capitalization and Leverage

Very Strong Capitalization

Fitch views TMHCC's capital to be very strong and supportive of the current rating category. Overall capital adequacy has a moderate influence in determining the company's ratings.

Fitch evaluates capital on both a nonrisk-adjusted basis, such as operating and net leverage, and a risk-adjusted basis, such as RBC and Fitch's Prism capital model, to gain a more comprehensive view of capital. From a nonrisk-adjusted perspective, TMHCC's metrics are slightly favorable relative to the rating category and peer-rated companies.

Life RBC continues to grow from the decline in 2017 due to the acquisition of American International Group, Inc.'s (AIG) medical stop-loss operations. Since the P/C company owns the life company, the P/C company's decline in RBC was related to ownership of the life subsidiary. Fitch expects RBC growth to be more modest going forward.

Fitch believes TMHCC's financial leverage will approximate the 20% range over the near to intermediate term. TMHCC retired all existing public debt in 2015. The company's current debt structure comprises two debt facilities: a bank term loan and borrowings under a revolving credit facility.

Fitch Expectations

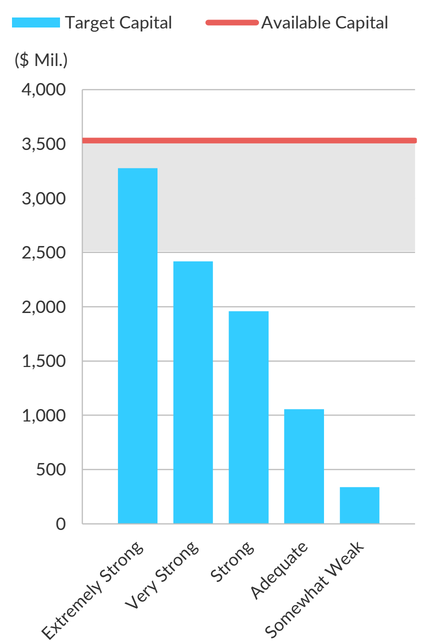
- Capitalization is expected to remain solid, with operating and net leverage near current levels. Financial leverage is expected to remain at or below 20%.

Financial Highlights

	2019	2020
Total Capital ($ Mil.)	5,903	6,319
Financial Leverage Ratio (%)	16	17
Net Premiums Written/ Equity (x)	0.7	0.8
Net Leverage (x)	1.8	2.1
P/C RBC Ratio (%)	239	195
Life RBC Ratio (%)	212	220

P/C – Property/casualty. Note: RBC ratio is calculated at company action level for lead operating subsidiary and is based on statutory accounting. Financial leverage ratio excludes FAS 115. GAAP accounting principles.
Source: Fitch Ratings; HCC Insurance Holdings, Inc.

2020 Preliminary Prism Score — HCC Insurance Holdings Group



($ Mil.)	2018	2019	2020[a]
Prism Score	Very Strong	Extremely Strong	Extremely Strong
AC/TC at Prism Score (%)	130	120	108
AC/TC at Higher Prism Score (%)	97	N.A.	N.A.
Statutory Surplus	3,624	3,454	3,624
Affiliated Investments	—	—	—
Unrealized Bond Gains/ (Losses)	29	—	—
Other Adjustments	239	(92)	(94)
Available Capital (AC Base)	2,585	3,483	3,530
Target Capital Contributors (%)			
Underwriting	26	25	25
Reserves	15	13	18
Investments	25	22	16
Catastrophe	15	19	17
Other	19	21	23

[a]2020 results are prelinary. AC – Available capital. TC – Target capital. Note: Red line is AC base; shaded area represents the high and low of AC due primarily to unrealized bond gains and the affiliated capital.
Source: Fitch Ratings, S&P Global Market Intelligence.

Debt Service Capabilities and Financial Flexibility

Very Strong Financial Flexibility and Debt-Servicing Capabilities

Fitch views TMHCC's financial flexibility and debt service capabilities to be very strong and supportive of the current rating category. Overall, this factor has a lower influence in determining the company's ratings.

Due to the company's strong profitability, moderate financial leverage and low interest expense, fixed-charge coverage is anticipated to remain near current levels over the near to intermediate term. The interest rate on the company's term loan is now fixed instead of floating. This was changed when the company refinanced in 2020, extending the duration to March 2027.

For purposes of the statutory fixed-charge coverage ratio, Fitch used the maximum dividend the U.S. subsidiaries could send to the holding company without regulatory approval, which was $226 million in 2020. Fitch notes that the company has additional liquidity sources outside of the U.S., but the bulk of revenues and profits are derived within the U.S.

Fitch Expectations

- Coverage ratios will fluctuate between the high-single-digit to low-double-digit range over the near term depending on the floating interest rate on the debt.

Financial Highlights

	2019	2020
Interest Expense ($ Mil.)	29	20
GAAP Fixed-Charge Coverage (x)	17	16

Note: GAAP.
Source: Fitch Ratings; HCC Insurance Holdings, Inc.

TMHCC Debt Outstanding

($ Mil., as of Dec 31, 2020)	
Bank Term Loan	475
Revolving Credit Facility	600

Source: Fitch Ratings; HCC Insurance Holdings, Inc.

Financial Performance and Earnings

Very Strong Profitability

Fitch views TMHCC's financial performance and earnings to be very strong and supportive of the current rating category. Overall profitability has a high influence in determining the company's ratings.

TMHCC's underwriting performance is a hallmark of the rating. Unique expertise in specialty lines has led to consistently strong operating results, evidenced by very strong yoy combined ratios with minimal deviations.

The company's management and underwriters are compensated with an emphasis on delivering very strong bottom-line results over top-line growth. In fact, the company actively reduces writings in lines of business that are too competitive to sustain a strong underwriting margin at the expense of maintaining market share or top-line growth.

Approximately, 14% of TMHCC's net written premiums are related to crop insurance. Due to adverse commodity prices, lost business and reduction in renewal premium, 2020 was a difficult year for crop insurance, but TMHCC, through a tangible demonstration of its risk analysis, was still able to produce profitable results on a consolidated basis.

Fitch Expectations

- Calendar-year combined ratio will approximate 90% over the near term.
- Premiums will continue to increase over the rating horizon.

Financial Highlights

($ Mil.)	2019	2020
Premiums Earned	3,518	3,809
Pretax Operating Income	456	456
Net Income	376	296
ROE (%)	8.0	1.0
Combined Ratio (%)	89.8	93.3
Operating Ratio (%)	82.6	87.1

Note: GAAP accounting principles. Operating income excludes investment gains/(losses).
Source: Fitch Ratings; HCC Insurance Holdings, Inc.

Investment and Liquidity

High-Quality Investment Portfolio

Fitch views TMHCC's investment and liquidity to be very strong and supportive of the current rating category. Overall investments and liquidity have a lower influence in determining the company's current ratings.

TMHCC maintains high-quality, fixed-income securities with a 'AA–' average credit rating and a modest 3% allocation to below-investment-grade bonds. The duration of its fixed-income portfolio is 4.9 years. Fitch believes that TMHCC's liquidity remains adequate to pay claims.

TMHD purchased Delphi Financial Group, Inc. in 2012 for approximately $2.7 billion. Delphi has unique investment management expertise, particularly in longer duration assets. Delphi's investment management organization oversees a portion of TMHCC's risk asset portfolios. TMHCC's investment strategy of allocating approximately 15% of assets into risk assets is unlikely to change from this shift in management, but the composition of these assets will differ over time.

Financial Highlights

	2019	2020
Total Invested Assets ($ Mil.)	8,087	9,025
Invested Assets/ Common Equity (x)	1.6	1.7
Risky Assets/Equity (%)	5	6
Investment Yield (%)	3	3

Note: GAAP.
Source: Fitch Ratings; HCC Insurance Holdings, Inc.

Fitch Expectations

- The risky asset ratio to approximate current levels.
- Investment leverage to remain relatively consistent yoy.

Reserve Adequacy

Reserve Position Is Strong

TMHCC's reserve adequacy is strong and supportive of the current rating category. Overall reserve adequacy has a moderate influence in determining the company's ratings.

In 2020, the company reported a modest amount of adverse reserve development primarily related to casualty lines in North America P/C, partially offset by favorable development in medical stop-loss. In the past 10 calendar years, reserves developed favorably eight times. The company also has low reserve leverage, which leads to limited capital exposure. The company demonstrates conservatism when estimating reserves, and continues to take prompt and sufficient measures when claims diverge from initial estimates.

TMHCC historically reported modest reserve volatility, as longer tail professional liability and casualty lines were offset by shorter tail accident and health and surety lines. The company's weighted-average duration of all claims was approximately 2.5 years in 2020 and approximated this level for several years.

TMHCC consistently reports consolidated net reserves above its actuarial point estimate, but within the actuarial range.

Financial Highlights

($ Mil.)	2019	2020
Loss and LAE Reserves	2,978	3,509
PAY Reserve Development	(9)	36
PAY Reserve Development/ NPE (x)	(0.3)	0.9
PAY Reserve Development/ BOY Common Equity (x)	(0.2)	0.7
Net Reserves/ Common Equity	0.6	0.7

LAE – Loss adjustment expense. PAY – Prior accident year. NPE – Net premiums earned. BOY – Beginning of year. Note: GAAP accounting principles.
Source: Fitch Ratings; HCC Insurance Holdings, Inc.

Fitch Expectations

- Reserving philosophy will remain conservative.
- Calendar-year reserve development is expected to be neutral to favorable over the near term.
- No material changes in reserve leverage.

Reinsurance, Risk Mitigation and Catastrophe Management

Reasonable Reinsurance Protection Limits Large Losses

Fitch views TMHCC's reinsurance, risk mitigation and catastrophe risk to be very strong and supportive of the current rating category. Overall, this category has a lower influence in determining the company's ratings.

TMHCC continues to purchase significant reinsurance to protect against catastrophe losses. The company also uses a fair amount of proportional reinsurance to more effectively manage risk in new lines of business. Reinsurance recoverables at YE 2020 increased considerably from the prior year, primarily due to the use of reinsurance for pandemic-related claims. Favorably, the company had over half of the outstanding recoverable balance collatoralized as of YE 2020. The company uses a panel of highly rated reinsurers to help offset any financial strength concerns. Also, the reinsurance recoverable balance declined $300 million thus far in 2021.

Fitch views TMHCC's risk management process as effective and notes the company has a history of favorable long-term underwriting performance. The company also built an economic capital model, which allows it to better assess risks associated with capital management decisions.

Fitch Expectations

- No major changes to TMHCC's reinsurance and risk mitigation over the ratings horizon.
- The retention ratio is expected to stay in the 70% range over the near term.
- Reinsurance recoverables will drift down towards longer term average over the rating horizon.

Financial Highlights

	2019	2020
Reinsurance Recoverables (RR, $ Bil.)	1.8	3.3
RR/Shareholders' Equity (%)	36	63
Retention Ratio (%)	74	73

Note: GAAP
Source: Fitch Ratings; HCC Insurance Holdings, Inc. fillings.

Appendix A: Other Ratings Considerations

Below is a summary of additional ratings considerations that are part of Fitch's ratings criteria.

Group IFS Rating Approach

Fitch considers TMHCC's insurance subsidiaries (listed in the table to the right) as Core operations. HCC Life Insurance Co. is owned by Houston Casualty Co. and writes predominately medical stop-loss business. These entities share common management, resources and branding. Only normal regulatory barriers exist to dividend movement between entities and the parent.

Notching

For notching purposes, the regulatory environment of the U.S. is assessed by Fitch as being Effective and classified as following a Ring-Fencing approach.

Notching Summary

IFS Ratings
A baseline recovery assumption of Good applies to the IFS rating, and standard notching was used from the IFS "anchor" rating to the implied operating company IDR.
Holding Company IDR
Standard notching was applied between the implied operating company and holding company IDRs, with no adjustments made for unusual leverage, coverage or diversification of cash flow.

IFS – Insurer Financial Strength. IDR – Issuer Default Rating.

Short-Term Ratings

Not applicable.

Hybrid — Equity/Debt Treatment

No hybrid debt exists at TMHCC currently.

Corporate Governance and Management

Corporate governance and management are adequate and neutral to the rating. No material issues to the rating are noted. The board appears to have an appropriate amount of independence from management and seems reasonably involved in establishing the company's strategic direction. There appear to be no major audit-related issues or related-party transactions.

Transfer and Convertibility Risk (Country Ceiling)

None.

Criteria Variations

None.

Complete Ratings List for Core Subsidiaries

Houston Casualty Co.	
Avemco Insurance Co.	
U.S. Specialty Insurance Co.	
American Contractors Indemnity Co.	
United States Surety Co.	
HCC Life Insurance Co.	
Insurer Financial Strength	AA–

Appendix B: Environmental, Social and Governance Considerations

FitchRatings **HCC Insurance Holdings, Inc.** Insurance Ratings Navigator US Non-Life

Credit-Relevant ESG Derivation

HCC Insurance Holdings, Inc. has 7 ESG potential rating drivers

- HCC Insurance Holdings, Inc. has exposure to underwriting/reserving exposed to environmental and natural catastrophe risks; impact of catastrophes on own operations or asset quality; credit concentrations but this has very low impact on the rating.
- HCC Insurance Holdings, Inc. has exposure to compliance risk; treating customers fairly; pricing transparency; privacy/data security; legal/regulatory fines; exposure to insured and own cyber risk but this has very low impact on the rating.
- HCC Insurance Holdings, Inc. has exposure to social responsibility and its effect on brand strength; increased vulnerability due to credit concentrations but this has very low impact on the rating.
- Governance is minimally relevant to the rating and is not currently a driver.

			Overall ESG Scale
key driver	0	issues	5
driver	0	issues	4
potential driver	7	issues	3
not a rating driver	2	issues	2
	5	issues	1

Environmental (E)

General Issues	E Score	Sector-Specific Issues	Reference	E Scale
GHG Emissions & Air Quality	1	n.a.	n.a.	5
Energy Management	1	n.a.	n.a.	4
Water & Wastewater Management	1	n.a.	n.a.	3
Waste & Hazardous Materials Management; Ecological Impacts	2	Underwriting/reserving exposed to asbestos/hazardous materials risks	Capitalization & Leverage; Financial Performance & Earnings; Reserve Adequacy; Reinsurance, Risk Mitigation & Catastrophe Risk	2
Exposure to Environmental Impacts	3	Underwriting/reserving exposed to environmental and natural catastrophe risks; impact of catastrophes on own operations or asset quality; credit concentrations	Capitalization & Leverage; Financial Performance & Earnings; Reserve Adequacy; Reinsurance, Risk Mitigation & Catastrophe Risk; Investment & Asset Risk	1

Social (S)

General Issues	S Score	Sector-Specific Issues	Reference	S Scale
Human Rights, Community Relations, Access & Affordability	1	n.a.	n.a.	5
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risk; treating customers fairly; pricing transparency; privacy/data security; legal/regulatory fines; exposure to insured and own cyber risk	Industry Profile & Operating Environment; Business Profile; Reserve Adequacy	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Corporate Governance & Management	3
Employee Wellbeing	1	n.a.	n.a.	2
Exposure to Social Impacts	3	Social responsibility and its effect on brand strength; increased vulnerability due to credit concentrations	Business Profile; Investment & Asset Risk; Financial Performance & Earnings; Reinsurance, Risk Mitigation & Catastrophe Risk	1

Governance (G)

General Issues	G Score	Sector-Specific Issues	Reference	G Scale
Management Strategy	3	Operational implementation of strategy	Corporate Governance & Management; Business Profile	5
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Corporate Governance & Management	4
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Corporate Governance & Management; Ownership	3
Financial Transparency	3	Quality and timing of financial reporting and auditing processes	Corporate Governance & Management	2
				1

How to Read This Page
ESG scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the individual components of the scale. The right-hand box shows the aggregate E, S, or G score. General Issues are relevant across all markets with Sector-Specific Issues unique to a particular industry group. Scores are assigned to each sector-specific issue. These scores signify the credit-relevance of the sector-specific issues to the issuing entity's overall credit rating. The Reference box highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis.

The Credit-Relevant ESG Derivation table shows the overall ESG score. This score signifies the credit relevance of combined E, S and G issues to the entity's credit rating. The three columns to the left of the overall ESG score summarize the issuing entity's sub-component ESG scores. The box on the far left identifies some of the main ESG issues that are drivers or potential drivers of the issuing entity's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI) and the Sustainability Accounting Standards Board (SASB).

Sector references in the scale definitions below refer to Sector as displayed in the Sector Details box on page 1 of the navigator.

CREDIT-RELEVANT ESG SCALE
How relevant are E, S and G issues to the overall credit rating?

5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.