

Beazley PLC

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Major Rating Factors

Strengths:

- Strong competitive position, benefiting from membership of the Lloyd's Market and the developing U.S. operations.
- Strong earnings from the participation in Beazley Furlonge - Syndicate 0623/2623/3622/3623.
- Strong enterprise risk management.

Weaknesses:

- Increased catastrophe and investment risk tolerance adds volatility to capitalization.
- Potential execution risk of long-term growth strategy.

Counterparty Credit Rating

Local Currency
BBB+/Stable/--

Rationale

The 'BBB+' long-term counterparty credit rating on Ireland-domiciled Beazley PLC reflects its position as the current holding company of the group (Beazley). The group's principal source of earnings is derived from its participation in Beazley Furlonge - Syndicate 0623/2623/3622/3623 (Lloyd's Syndicate Assessment '4/Stable'), which operates within the Lloyd's Insurance Market (Lloyd's or the Market; insurer financial strength rating, A+/Stable/--).

The rating primarily reflects key features of Beazley's operating profile, including strong competitive position, Syndicate 0623/2623/3622/3623's strong earnings, and strong enterprise risk management. These strengths are partially offset, however, by increased catastrophe and investment risk tolerance which adds volatility to capitalization, and potential execution risk of the long-term growth strategy.

Beazley's strong competitive position is derived from its long history of success within Lloyd's, notably its leading position in medium-tail specialty business, which accounted for 43% of premium income in 2010. Furthermore, the group has a strong reputation in property (22%), marine (15%), and treaty reinsurance (10%). Strategic acquisitions have supplemented the group's strong growth track record to some extent. In our view, the group will continue to look to acquire companies to enhance its offering, notably in the U.S., and we believe that this will bring with it execution risks, particularly given the complexity and tail of the risks Beazley typically writes. That said, Beazley's strong underwriting and effective cycle management controls have somewhat mitigated these factors in our view.

We view Beazley's operating performance as strong. Over the past decade, it has been consistently profitable and has demonstrated performance, on a risk-adjusted basis, at least in line with its Lloyd's peers. Despite the record catastrophe losses in the first half of 2011, the group posted a combined ratio of 108% which is better than most of its peers. Technical gains from noncatastrophe business and higher than usual reserve releases have largely offset the losses leading to a modest pretax loss of \$24.2 million. In our view, Beazley's diversified earnings profile should enable it to benefit from any improvement in pricing within the wholesale segment, notably in loss-affected property (re)insurance segments.

We view Beazley's capitalization as strong. We note that increased catastrophe risk and investment risk tolerance

adds volatility to Beazley's capitalization. We expect that Beazley will be able to appropriately manage its risk profile in such a way that its capitalization supports the ratings because of its strong enterprise risk management.

Our view of Beazley's capitalization is largely based on its risk-based capital adequacy, measured using our model. At year-end 2009, the group's risk-based capital deteriorated to the upper end of the 'BBB' level. This was due to a combination of increased exposure to catastrophe losses relative to capital base, increased market risk, special dividend payout, and share repurchases. We forecast that the group's risk-based capital is likely to improve to the lower end of the 'A' level at year-end 2011 through retained earnings. Beazley's investments in hedge funds, accounting for 10.6% of the group's total invested assets as of June 2011, has increased its market risk following the revised investment strategy in 2009. Under the new strategy, the proportion of this asset class could potentially increase to 14%. In our view, this could potentially place downward pressure on capitalization. The remainder of Beazley's assets are held in highly rated bonds and cash and cash equivalents (57.7% and 31.7% in June 2011, respectively).

Liquidity

Beazley continues to generate strong cash flows to support its highly liquid investment portfolio, with a low-duration bond portfolio, which has very strong credit quality. Although the hedge funds the company has invested in have relatively short redemption schedules, we believe that these investments will have limited liquidity in a stressed environment. In recognition of the potential growth in premiums--which could increase Beazley's funding requirement--the group has recently increased its letter of credit facility to \$225 million (from \$150 million previously) and extended it to the 2013 underwriting year. Currently this facility has not been drawn.

Outlook

The stable outlook reflects our expectation that the group's risk-based capital adequacy will be at least at the lower end of the 'A' range over the next 24 months, and that Beazley will maintain its strong competitive position. We anticipate that gross premiums for 2011 will remain flat when compared with 2010, partly reflecting the soft market conditions in specialty lines. In the absence of major merger and acquisition (M&A) activity we do not expect the syndicates' strong competitive position to change materially over the rating horizon.

In common with most of its peers, we expect Beazley's operating performance to deteriorate in 2011 because of the catastrophe losses in the first-half of 2011 and widespread low interest rates. We forecast a combined ratio of about 95%-100% and a return on revenue (ROR) of 5%-10%, which may put it ahead of its peers. In 2012, we expect Beazley to return to strong operating results, achieving a combined ratio of 90% or below, assuming average historical levels of catastrophe losses and challenging pricing conditions in specialty business. We expect this result to be supported by continued prior-year releases. We also anticipate that the accident-year combined ratio will be around a break-even level, reflecting the group's conservative reserving strategy. We also anticipate that any growth--notably in catastrophe-exposed segments--will translate into strong earnings, which will mostly be retained.

Any further material deterioration in the group's risk-based capital to a level that does not support the ratings could result in negative rating action. A positive rating action is unlikely over the rating horizon, given that the group's capitalization does not support a higher ratings level. In addition, the uncertainty surrounding the potential capital increase under Solvency II needs to be resolved satisfactorily. Furthermore, the challenging pricing conditions outside the loss-affected areas prevent the ratings from improving at this stage.

Financial Profile: Strong Financial Flexibility Demonstrated Regularly Since Formation

Beazley PLC's financial flexibility (defined as the ability to source capital relative to capital requirements) is viewed as strong. The group has increased its letter of credit facility (see liquidity section) in recognition of growth opportunities.

A strong level of financial flexibility was once again demonstrated when the group successfully completed a fully underwritten £150 million rights issue in April 2009, predominantly to support increased underwriting and to fund the acquisition of First State (subsequently named Beazley E&S). In October 2006, the group successfully issued £150 million of Tier II capital (rated 'BBB-') to replace its short-term borrowing facilities and secure a more permanent capital base to support the syndicate. Financial leverage at year-end 2010 was 21%, which is within the tolerance level for a rating at this level. Fixed-charge cover was a strong 19x for 2010.

The group potentially has access to other types of financial support through reinsurance, or arrangements for special-purpose reinsurers established to provide underwriting capacity to a specific reinsurer ("sidecar" arrangements).

Table 1

Beazley PLC Financial Flexibility		
	--Year-ended Dec. 31--	
(%)	2010	2009
EBITDA interest coverage (x)	18.6	12.5
EBITDA fixed-charge coverage (x)	18.6	12.5
Debt leverage, including additional pension deficit as debt	20.5	22.5
Financial leverage, including additional pension deficit as debt	20.5	22.5

Ratings Detail (As Of October 4, 2011)*

Beazley PLC

Counterparty Credit Rating

Local Currency

BBB+/Stable/--

Counterparty Credit Ratings History

09-Jun-2009

Local Currency

BBB+/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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