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XLIT Ltd. And Its Operating Subsidiaries

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Table Of Contents

XLIT Ltd. And Its Operating Subsidiaries

SACP* Assessments				SACP*		Support		Ratings
Anchor	a+	Modifiers	0	a+		0		Financial Strength Rating: A+/Stable/--
Business Risk: Very Strong		ERM and Management	0	Liquidity	0	Group Support	0	Holding Company Rating: A-/Stable/--
Financial Risk: Moderately Strong		Holistic Analysis	0	Sovereign Risk	0	Gov't Support	0	

*Stand-alone credit profile.

See Ratings Detail for a complete list of rated entities and ratings covered by this report.

Rationale

Business Risk Profile: Very Strong

- Very strong competitive position bolstered by the transformational acquisition of Catlin in 2015, which enhanced scale and product offerings
- Prospective underwriting results to improve as the company progresses through the final stages of integration, reflecting historical underwriting performance of individual entities, synergies, and improved market standing
- Intermediate insurance industry and country risk assessment (IICRA) reflects low country risk and moderate industry risk for the property/casualty (P/C) insurance and reinsurance sectors
- Reinsurance segment facing secular headwinds, though recent catastrophe events are likely to improve pricing in certain regions and business lines in the near term

Financial Risk Profile: Moderately Strong

- Very strong capital and earnings, supported by good operating results and redundant capital adequacy at the 'AA' stress level
- High risk position because of potential volatility of capital and earnings arising from exposure to property catastrophe, terrorism, and other severity risks
- Predominant insurance risks, with reserving risk using the bulk of economic capital, followed by market risk and natural catastrophe risk
- Adequate financial flexibility reflecting sufficient access to capital markets, partially offset by moderately high leverage and relatively low fixed-charge coverage despite prospective earnings improvement

Other Factors

- Strong enterprise risk management framework plays a significant role in value-creation strategy
- Satisfactory management and governance with a focus on realizing synergies from successfully integrating Catlin and benefitting from enhanced scale and market presence
- Very strong business risk profile and moderately strong financial risk profile leading to a possible anchor of either 'a+' or 'a'; we assigned the former, reflecting XL's broad diversification by product and geography, and its dual insurance and reinsurance platform, which partially mitigates volatility in XL's earnings profile

Factors Specific to the Holding Company

As we do with most of its Bermuda-based peers, we rate Cayman Islands-based XLIT Ltd. (XL) two notches below its operating subsidiaries, because of structural subordination reflecting the holding company's dependence on dividends from its operating subsidiaries. XL's operating companies are domiciled in different countries with the majority of capital held in Bermuda, which provides the group with significant regulatory flexibility in upstreaming dividends to the holding company.

Outlook: Stable

The stable outlook reflects our expectation that XL will maintain its very strong capital position and very strong competitive position. In our view, the company will continue to leverage a larger platform to realize business and cost synergies, and optimize its portfolio toward higher-margin businesses through underwriting actions, all of which would enhance its market position and underlie its ability to generate sustainable earnings that are in line with our expectations and those of its similarly rated peers. We also expect the company to continue its focus on enhancing its enterprise risk management (ERM) given the company's complex risk profile.

Downside scenario

We could lower the ratings over the next two years if XL does not meet our performance expectations, particularly if there is a significant shortfall in underwriting results (absent a significant catastrophe, in which case we would expect the company's results to be consistent with the industry's as a whole); if XL is challenged to fully leverage its platform post Catlin acquisition; or if the ERM program falls short relative to its risk profile. Further pressure could arise if XL's ability to access external markets is constrained and fixed-charge coverage falls below 4x.

Upside scenario

We could raise the ratings in the next two years if we assess capital and earnings volatility as better relative to the company's peer group, which can support a moderate risk position, or its capital position strengthens to extremely strong. Other contributing factors would include XL's ability to sustain a fixed-charge coverage ratio comfortably above 5x, and maintenance of financial leverage less than 30%.

Base-Case Scenario

Macroeconomic Assumptions

- Global credit conditions have brightened overall, but risks linger. Credit conditions are broadly favorable in North America, improving in Europe, turned favorable for Latin America, and are poised to improve further for Asia-Pacific.
- Real U.S. GDP growth of about 2.2% in 2017, 2.6% in 2018, and 1.9% in 2019.
- Long-term real-interest rates could stay relatively lower longer. We expect the 10-year U.S. treasury-note yield around 2.3% in 2017 and rising to 2.6%-2.9% in 2018-2019.
- U.S. core Consumer Price Index of 1.9% in 2017 and around 2.0% for 2018-2019.
- U.S. unemployment rate steadily dropping over the next few years to around 4.4% in 2017 and 4.0% for 2018-2019.

Company-Specific Assumptions

- Gross premiums written (GPW) to grow mid-to-high single digits in 2017-2019, benefitting from enhanced market presence and price increases in the catastrophe-exposed regions/business following recent catastrophe events.
- Growth in net premiums could be higher if reinsurance/retrocession utilization is optimized to capture the benefit of better-priced business and/or to manage retrocession costs.
- Combined ratio including corporate expenses to remain elevated in 2017 due to significant catastrophe losses in the third quarter. Underwriting performance to improve in 2018-2019 assuming normalized catastrophe losses of 6 points and some benefit from favorable reserve development, though lower in 2017. Earnings to benefit from rate increases in certain lines following recent catastrophe events, lower corporate expenses reflecting minimal additional integration costs, efficiency gains in operating costs, and shift in business mix leveraging synergies from a larger platform, pricing actions, and risk segmentation capabilities.
- Increase in interest rates should provide some benefit though considering the new money rate, investment yield will remain relatively low in the near term.
- Capital adequacy to be slightly redundant at the 'AA' level for 2017. Capital redundancy to strengthen at 'AA' over 2018-2019 through accrued earnings and a cautious stance on any further share repurchases to replenish the capital at or above XL's internal targets over the next year or so.
- Financial leverage to improve to below 30% helped by capital build-up with potential for some additional reduction in 2018 from maturing debt depending on capital position.
- Fixed-charge coverage will be negative for 2017. Assuming normalized earnings, coverage to be around 5x for 2018-2019, reflecting gains in underwriting results and lower service costs.

Key Metrics

	2019*	2018*	2017*	2016	2015
Gross premiums written growth (%)	4-7	5-9	5-7	26.5	35.6
P/C net combined ratio (%)	94-96	94-97	109-112	94.2	92.0
Return on revenue (%)	11-13	10-12	~(2)	7.1	12.1
S&P Global Ratings capital adequacy	AA	AA	AA	AAA	AAA
Financial leverage (%)	<=30	<=30	30-31	28.5	28.3
Fixed charge coverage (x)	4-6	4-6	<0	2.7	3.6

*Forecast data reflect S&P Global Ratings' base-case assumptions. Note--P/C net combined ratio inclusive of corporate expenses.

Company Description: Diversified Global Multiline Insurer

XL Group Ltd., through its subsidiaries, is a global insurance and reinsurance company providing property, casualty, and specialty products to industrial, commercial, and professional firms, insurance companies, and other enterprises on a worldwide basis. With the acquisition of Catlin in 2015, XL has created a stronger global franchise in both the insurance and reinsurance sectors, which has enhanced its scale and product offerings. In full-year 2016, the combined entity wrote about $13.9 billion in premiums and had a capital base of $15.6 billion and common shareholders' equity (excluding minority interests) of $11 billion. For 2016, the insurance segment contributed 71% of GPWs and reinsurance 29%.

Business Risk Profile: Very Strong

XL's very strong business risk profile reflects our assessment of its enhanced market position in both the insurance and reinsurance sectors and its diversification by regions and products.

Insurance industry and country risk: Globally diverse insurance and reinsurance operations in major stable economies

Our overall IICRA of XL is intermediate, reflecting low country risk and moderate industry risk for its P/C insurance and reinsurance. XL's global risk exposures are mainly in major markets such as the U.S., U.K., Germany, France, and Canada, providing it with relative stability vis–à–vis primary re/insurers that are more exposed to specific country risks. XL is mostly exposed to developed markets that are typically characterized by low risks, including political environment, financial system, payment culture, and rule of law. Our view of the global P/C reinsurance sector stems primarily from our negative assessment of the industry's exposure to property catastrophe volatility and the relatively moderate operational barriers to entry that materially expose P/C reinsurers to competition from existing players and new entrants.

Table 1

Industry And Country Risk

Insurance sector	IICRA	Business mix (%)
United States P&C	Intermediate Risk	41.6
Global P&C Reinsurance	Intermediate Risk	37.7

Table 1

Industry And Country Risk (cont.)		
Insurance sector	**IICRA**	**Business mix (%)**
Germany P&C	Low Risk	3.8
Other countries P/C		16.9
Weighted average IICRA	Intermediate Risk	100.0

IICRA--Insurance industry country risk assessment.

Competitive position: Very strong with globally diversified insurance and reinsurance platforms

XL has strengthened its competitive position with the acquisition of Catlin. We believe the combination of the two companies bolsters XL's specialty business through expansion at Lloyd's via Catlin's leadership role, and fosters growth in Catlin's network via XL's greater global footprint. The combined entity benefits from increased market presence, providing opportunities to increase its client penetration and tap into new opportunities as well as the ability to weather soft sector conditions.

Table 2

XL Group -- Competitive Position							
	--Nine months ended Sept. 30--		--Year ended Dec. 31--				
(Mil. $)	**2017**	**2016**	**2016**	**2015**	**2014**	**2013**	**2012**
Gross premiums written (GPW)	11,367	10,811	13,891	10,979	8,095	7,741	7,531
Change in GPW (%)	5.1	29.1	26.5	35.6	4.6	2.8	3.3
Net premiums written (NPW)	7,962	7,927	10,243	7,951	5,945	6,199	6,282
Change in net premiums written NPW (%)	0.4	30.8	28.8	33.7	(4.1)	(1.3)	8.4
Reinsurance utilization - premiums written (%)	30.0	26.7	26.3	27.6	26.6	19.9	16.6
Business segment (% of GPW)							
P/C insurance	67.7	67.6	70.8	78.7	77	71.3	68.6
P/C reinsurance	32.3	32.4	29.2	21.3	23	24.5	26.7
Life reinsurance	0	0	0	0	0	4.2	4.7

XL's very strong global market presence in P/C insurance and reinsurance reflects its underwriting expertise in specialized industry segments, its global scale, and its ability to provide large coverage limits, allowing the company to reach and serve its global clients better than its less-diversified competitors can.

Insurance XL Insurance (XLI) is a leading global provider of large corporate and specialty products. XLI transformed to a global commercial company from a niche excess player through acquisitions and organic growth. The Catlin acquisition has significantly enhanced the group's offerings, global commercial footprint, product breadth, and depth. It has also reduced its tail risk and reliance on the Americas region, with more than half of its GPW from non-U.S. operations. As of Sept. 30, 2017, XLI generated 34% GPW from casualty lines; 24% from specialty; 24% from energy, property, and construction; and 18% from professional lines.

XLI reorganized its business into three groups effective Jan. 1, 2017, aligning with distribution and client focus: Global Lines, International, and North America. The company is one of the top players in the Lloyd's market with about 9% market share and a leading market share in key specialty lines as a result. Furthermore, XLI's business generated outside the top-six brokers increased in 2016 after the Catlin acquisition and continuing growth. Currently, XLI is estimated to be among the top five largest insurance markets for Willis, Marsh, and Aon. In 2016, pricing was negative across most lines of business with the overall rate change for the segment down by about 2% for third-quarter 2017 year-to-date as competitive market conditions persisted. However, because of substantial industry catastrophe losses in third-quarter 2017, rates will increase in loss-affected regions/lines and possibly beyond those, which should provide some offset. Greater scale, a larger platform, and increased presence helped drive 4% growth in 2016 adjusting for acquisition, foreign exchange, and underwriting actions, with similar drivers at work for 2017 as well. We expect underwriting initiatives and portfolio optimization to result in gains in performance.

Reinsurance XL Reinsurance (XLR) is a leading specialist and a global reinsurer with a recognized brand. After the merger with Catlin, XLR strengthened its market position and became the 15th-largest reinsurer in the world based on 2016 net premiums written, according to S&P Global 2017 Global Reinsurance Highlights. Currently, XLR is organized by region, each of which has its own underwriting, actuarial, claims, and local operating responsibilities.

As of Sept. 30, 2017, XLR generated 27% GPW from property catastrophe lines of business, 33% from property, 16% from casualty, 6% from professional liability, 6% from specialty, and the remainder from other lines of business including whole account, credit and surety, accident and health, et cetera. In addition, the majority of its GPW is generated from outside the U.S. Year-to-date third-quarter 2017, GPW increased by 3.1% adjusting for foreign exchange and excluding reinstatement premiums. The growth reflected new business in property and casualty business and an increased share of lines partially offset by business cancellations and pricing declines of about 1%, albeit decelerating, reflecting sector headwinds.

With a diverse product suite and the benefit of a larger platform, XLR will continue to enhance its market presence through increasing line size with existing clients, cross-selling for large accounts, increasing its share in new lines, providing customized solutions, launching new products, harnessing alternate capital, and building strategic partnerships with its cedants. XLR should benefit from many cedants consolidating their reinsurance panel with a smaller group of major reinsurers. This trend will help it navigate the current challenging reinsurance environment, which is witnessing headwinds from secular trends that are expected to persist despite rate-strengthening in response to recent catastrophe events. The secular trends relate to the broader acceptance of alternative capital, centralizing reinsurance purchases by larger cedants, increasing sophistication and use of external models, and better understanding of risk in peak zones, which are putting pressure on traditional business models.

In 2017, with the Catlin acquisition and related integration efforts largely complete, XL will continue to focus on enhancing the benefit that the combination of two platforms provide, further strengthening its clients' relationships, and realizing synergies. With its newfound scale, XL is expected to become more resilient in the face of key market drivers such as globalization, changes in regulation, alternative capital, relevance and scale, and broker dynamics. We expect XL's top line to increase to about mid-to-high single digits and improve its underwriting performance though portfolio optimization, greater use of data analytics, better risk segmentation, and underwriting discipline, which will be further supported by a centralized reinsurance purchase approach to optimize gross-to-ceded strategy to optimize returns and manage tail risk.

Financial Risk Profile: Moderately Strong

XL's moderately strong financial risk profile reflects very strong capital adequacy, partially offset by its high-risk position.

Capital and earnings: Hit by third-quarter catastrophe losses

We assess XL's capital and earnings as very strong, which we view as reflective of the company's long-term capital management. Third-quarter catastrophe events and fourth-quarter California wildfires negatively affected the company's capitalization. The year-to-date second-quarter 2017 net income was more or less offset by common and preferred dividends and share repurchases of approximately $572 million; therefore, the net losses from recent catastrophe events primarily hit the existing capital buffer at the 'AAA' level, as assessed as of year-end 2016. Including the recently reported losses for California wildfires, there is sufficient reinsurance/retrocession coverage that the capitalization would likely be marginally redundant at the 'AA' level as of year-end 2017 absent any additional events. We also believe the company will suspend its share-repurchase plan to better assess the losses and prospective capital requirements. As a result, we expect annual normalized net earnings of $900 million-$1 billion and a cautious stance on any further share repurchases to replenish the capital at or above XL's internal targets and in line with our 'AA' assessment over the next year or two. Although the company has historically maintained 'AAA' capitalization and it may be the case during certain periods, our view of the company's long-term capital management strategy is better aligned with capital redundancy at the 'AA' level (as measured by S&P Global Ratings' capital model).

Table 3

XL Group -- Capitalization Statistics							
	--Nine months ended Sept. 30--		--Year ended Dec. 31--				
(Mil. $)	**2017**	**2016**	**2016**	**2015**	**2014**	**2013**	**2012**
Common shareholders' equity (including non-controlling interests)	10,053	11,686	11,054	11,748	10,091	10,005	10,510
Change in common shareholders' equity (%)	(14.0)	(2.6)	(5.9)	16.4	0.9	(4.8)	11.7
Total reported capital	14,739	16,240	15,608	16,299	13,098	13,613	13,529
Change in total reported capital (%)	(9.2)	(2.3)	(4.2)	24.4	(3.8)	0.6	3.8

Table 4

XL Group -- Earnings Statistics							
	--Nine months ended Sept. 30--		--Year ended Dec. 31--				
(Mil. $)	**2017**	**2016**	**2016**	**2015**	**2014**	**2013**	**2012**
Total revenue	8,308	7,980	10,641	9,132	6,857	7,307	7,155
EBIT adjusted	(665)	649	760	1,108	619	1,104	808
EBITDA adjusted	(611)	735	878	1,200	675	1,160	865
Net income (attributable to all shareholders)	(550)	261	570	1,313	269	1,137	730
Return on revenue (%)	(8.0)	8.1	7.1	12.1	9	15.1	11.3
Return on reported shareholders' equity (%)	(5.8)	2.5	4.3	10.5	2.4	9.8	6.5
P/C: net expense ratio (%)	34.2	32.3	37.0	33.6	31.2	30.5	30.9
P/C: net loss ratio (%)	80.8	61.6	62.2	58.4	57	62	65.3

Table 4

XL Group -- Earnings Statistics (cont.)							
	--Nine months ended Sept. 30--		--Year ended Dec. 31--				
(Mil. $)	**2017**	**2016**	**2016**	**2015**	**2014**	**2013**	**2012**
P/C: net combined ratio (%)	111.6	93.9	94.2	92	88.2	92.5	96.3
(Favorable)/unfavorable reserve development (%)	(1.2)	(2.7)	(3.1)	(3.8)	(4.5)	(4.8)	(5.5)
P/C: net accident year combined ratio (%)	116.2	101.6	102.3	95.8	92.6	97.3	101.7
P/C: net combined ratio (%) including corporate expenses*	115.0	98.9	99.2	97.7	91.9	95.8	99.6
Combined ratio by segment (As reported) (%):							
P/C insurance	108.3	96.4	96.6	96.9	94.4	97.1	100.6
P/C reinsurance	117.7	88.8	88.4	81	73.3	81.4	86.9
Catlin stand-alone	N/A	N/A	N/A	N/A	93.4	91.3	94.4

*Corporate expenses are allocated in proportion of gross premiums written. N/A--Not applicable.

XL's operating performance declined in 2016 as integration costs coupled with higher catastrophe losses, underwriting actions, and weaker market conditions pushed up both expense and loss ratios. With a heavy catastrophe season in 2017, the company will suffer net underwriting and operating losses. However, looking at period-over-period performance of segments, the accident year loss ratio excluding catastrophe losses, and expense ratios are trending in the right direction. The integration expenses were all taken in by second-quarter 2017 and the synergies should start to come through more clearly (some of which are already showing in segment operating expenses and those gains will also extend to corporate expenses). Furthermore, underwriting actions, pricing analytics, and underwriting discipline along with a centralized ceded approach to reduce volatility and gain efficiencies are likely to improve or maintain accident-year loss ratio over the near term. In addition, depending on the level of rate increases following recent catastrophe events, underwriting performance should benefit further. As a result, we expect an improved run-rate operating performance in 2018-2019.

Overall, we believe XL's reserves are adequate. The lower favorable development in the first nine months of 2017 as compared with the prior year period reflects unfavorable development from the impact of the Ogden rate change (which had a sectorwide impact) in the U.K. and deterioration in the London wholesale property book, partially offset by higher releases from professional and casualty insurance lines and property and other short-tail reinsurance lines. A prudent reserving process, conservative attitude toward reserve releases, and sophisticated risk metrics used in monitoring of actual versus expected loss emergence contribute to our view. We view favorably XL's detailed appraisal of the legacy books of both XL and Catlin prior to the merger, because it provides an in-depth understanding of the similarities and differences between the reserve liabilities and methodologies of both companies. Both legacy XL and legacy Catlin had a prudent reserving strategy, and the consolidated group has adopted best practices from each when establishing a combined entity framework . This is evident from their reserve redundancies and consistent net favorable reserve developments. Furthermore, XL is committed to improving data quality and has set up a data-governance structure including appointment of a chief data officer, which should add necessary oversight to the integration of the two companies.

Risk position

XL has a high risk position, stemming from the potential volatility in its capital and earnings because of its exposure to property catastrophe, terrorism, and other severity risks.

Table 5

XL Group -- Natural Property Catastrophe Losses Impact On The Combined Ratios							
	--Nine months ended Sept. 30--		--Year ended Dec. 31--				
	2017	2016	2016	2015	2014	2013	2012
P/C net premiums earned	7,651	7,312	9,766	8,164	5,717	6,014	5,766
Catastrophe net losses	1,760	408	220	220	118	370	550
Effect on combined ratio (%)	23.0	5.6	2.3	2.7	2.1	6.2	9.5

Table 6

XL Group -- Risk Position							
	--Nine months ended Sept. 30--		--Year ended Dec. 31--				
(Mil. $)	**2017**	**2016**	**2016**	**2015**	**2014**	**2013**	**2012**
Total invested assets (including life funds withheld assets)	41,335	42,181	40,468	41,603	35,893	36,192	36,599
Change in total invested assets (%)	(2.0)	(0.8)	(2.7)	15.9	(0.8)	(1.1)	3
Net investment income	612	631	827	872	919	958	1,012
Realized capital gains/(losses)	150	(493)	(204)	205	(255)	234	78
Net investment yield (%)	2.0	2.0	2.0	2.3	2.5	2.6	2.8
Portfolio composition (% of general account invested assets)							
Cash and short-term investments (%)	8.2	9.6	10.0	9.5	7.7	6.2	8
Bonds (%)	81.1	79.5	78.8	80.5	81.8	83.9	83.8
Equity investments (%)	7.5	7.6	8.0	7.3	8.0	7.8	6.2
Investments in affiliates (%)	0.9	1.2	1.2	0.8	1.2	0.9	0.8
Other investments (%)	2.2	2.0	2.0	1.9	1.3	1.2	1.2

Note: including life funds withheld assets.

The primary objectives of XL's investment strategy are to support the liabilities that arise from its operations, generate stable investment income, and build long-term book value. It has a consistent set of risk limits informed by the organizational risk tolerance, stress testing, and well-developed risk policies around investments, with escalation levels that are defined for deviations from risk limits and benchmarks.

XL's strategic asset allocation, which continues to form the foundation of the company's investment management activity post acquisition, involves continually monitoring the portfolio's risk profile and periodically rebalancing it to ensure that actual and intended risks are consistent under a controlled risk-management framework. This entails defining and controlling tolerance ranges within which the portfolio can operate, including concentration and aggregation, credit quality, liquidity, rate and spread duration, value at risk, and tracking error.

XL has successfully integrated Catlin's assets into the legacy XL investment framework, and has leveraged the best practices from each company. External managers primarily manage its investments, which provides better flexibility to allocate investments to various strategies and shift as needed for portfolio optimization. As of Sept. 30, 2017, XL had

$37 billion in invested assets (excluding $4.1 billion in Life Re's funds withheld assets) with 79.9% invested in fixed-income --mostly investment-grade bonds (average credit rating of 'AA' despite a slight shift in credit quality and 96.7% rated investment-grade), 11.4% in equity, investment in affiliates and other investments, and 8.3% in cash and cash equivalents. This portfolio had a duration of four years, which was slightly shorter than the company's P/C loss reserves' duration.

Financial flexibility: Adequate

XL's financial flexibility is assessed as adequate. In the past few years, fixed-charge coverage has been below 4x on average, though we expect a pick-up from earnings improvement, prospectively, and partially due to lower dividends following conversion to a floating-rate coupon on preferred shares. The projected coverage of around 5x, while an improvement, is expected to remain at the lower end of XL's peer group and reflects moderately high leverage (which is at the higher end of the peer group) that somewhat constrains headroom. However, the company has sufficient access to capital markets, reinsurance/retrocession, and alternative capital to enable its capital management strategies. We do not expect any additional debt/hybrid issuance in the near term. That, along with accrued earnings, should bring down the leverage ratio below 30%, which increased by a few points due to a combination of third-quarter losses, share-repurchases, and a slight increase in net debt. Depending on the pace of capital build-up, partial or full retirement of debt in 2018 can further reduce leverage.

Table 7

XL Group -- Financial Flexibility

	--Nine months ended Sept. 30--		--Year ended Dec. 31--				
	2017	2016	2016	2015	2014	2013	2012
EBITDA fixed-charge coverage (x)	(2.5)	2.6	2.7	3.6	2.6	5.6	4.2
Financial leverage (incl. NPV of operating leases and pension deficit as debt) (%)	30.4	28.6	28.5	28.3	21.7	23.6	22.3

In recent times XL has had an aggressive share buyback program. The total amount of share repurchases was $572 million year-to-date third-quarter 2017 and approximately $1 billion for full-year 2016 as the price-to-tangible book value was averaging between 1.0x-1.2x. In light of catastrophe events resulting in a hit to capital and potential for a better market environment from rate strengthening, we believe XL will refrain from additional share repurchases to replenish capital and better assess prospective capital needs.

Other Assessments

Enterprise risk management: Significant role in value-creation strategy

The ERM program is assessed as strong, based on positive scores for all the components of our ERM evaluation. The group's key risks are reserve and catastrophe exposure from its re/insurance operations and elevated, though receding, levels of operational risk related to integration following the Catlin acquisition. Because XL's global footprint, mix of business (insurance and reinsurance), exposure to long-tailed liabilities, and exposure to catastrophe risks could lead to significant earnings volatility, we view ERM to be of high importance to the rating.

We have a positive view of the group's risk-management culture given its sound governance framework including an independent ERM function with significant influence in strategic decision processes, and clearly defined risk-appetite and tolerance statements. XL has established a risk-focused culture and consistently creates incentives to improve underwriting quality.

XL is proactive in assessing emerging risks and in addition to having a formalized approach to identify and prioritize these emerging threats or opportunities, it performs detailed in-depth analyses to quantify the exposure to risk or value potential, which compares favorably with that of similarly ranked peers. Strategic risk management is also viewed positively, as the group has established a framework to apply risk-adjusted metrics when assessing key business decisions and capital allocation. Further supporting our opinion is the utilization of multiple metrics to create a holistic risk assessment and provide more granularity.

Risk controls are overall viewed as positive, recognizing the robust framework the group has established. XL actively uses risk-adjusted metrics in its cycle management process, enabling it to react quickly to changing market conditions and focus on growing lines of business with greater profitability potential. Its efforts at centralizing the actuarial database should improve data quality, and enhance pricing and risk metrics, which we view favorably.

Given the significant exposure to natural catastrophe risk, XL has pragmatically assessed its current risk appetite statements and maintained similar risk limits as it continues to apply a conservative approach to risk aggregations. The group emphasizes understanding modeled exposures and actively adjusts vendor models to more closely align with the risk profile XL has. That said, 2017 catastrophe events produced elevated losses but they were within group's tolerance levels. We will continue to monitor the development of losses from these events and the relative experience vis-à-vis XL's peer group.

While a majority of the integration has occurred, there is still an elevated level of risk as further elements are integrated and resource needs assessed. Although we recognize that the group has demonstrated a thorough and prudent approach toward integration, there would need to be seasoning of processes to determine the effectiveness of current operational risk controls.

Management and Governance: Focused on leveraging a broader platform

We view XL's management and governance as satisfactory.

The recent catastrophe losses from hurricanes Harvey, Irma, and Maria and the Mexico earthquake were substantial, although those were in line with the company's risk appetite and consistent with our assessment of high risk position considering substantial exposure to property-catastrophe risk.

In 2015, XL acquired Catlin, which significantly enhanced its franchise value and market presence. Given the size, complexity, and potential overlap between the two insurance and reinsurance portfolios, there are heightened execution and integration risks. Some of these were highlighted as the company changed its matrix organization structure that it put in place in its insurance group post acquisition. The company has now moved to reorganize its insurance business into three segments and brought both insurance and reinsurance segments under Gregory Hendrick (head of the reinsurance segment) to extract operating efficiencies and improve accountability, a positive development in our view. The company witnessed some turnover in the senior management team; however, we believe this to be less of a concern considering the depth and breadth of XL and Catlin's overall management team.

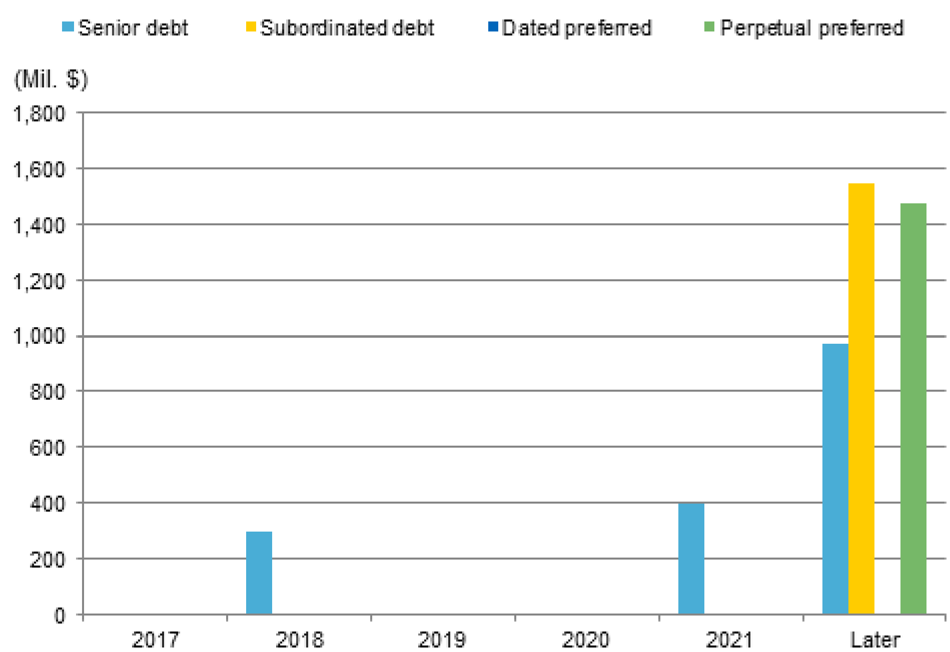
While the integration risks are higher due to the inherent nature of the transaction, we believe they are partially mitigated by a strong management team comprising members from both legacy XL and Catlin teams, each of which has a strong track record in running complex companies. As well, the integration efforts by and large have been progressing well and at the tail-end, with management now looking ahead at ways to enhance the value proposition of the combined platform. A disciplined underwriting culture, focus on service, and strong risk-management capabilities should enable XL to execute its strategy.

Management has successfully guided the company, which was under significant pressure following the 2008 financial crisis. It divested its ownership interest in Syncora (a financial guarantee reinsurance and insurance business), deleveraged its balance sheet, and reduced the risk in its investment portfolio. In addition, in 2009 XL announced the run-off of its life reinsurance business, of which it retroceded the majority through two transactions in second-quarter 2014 and fourth-quarter 2015 (see the Accounting section). We believe the sale reflects XL's management efforts to focus on its core P/C re/insurance business and reduce risks in its run-off operations.

Liquidity: Sufficient cash flows to meet business operations

XL's liquidity is exceptional, benefiting from liquid invested assets and a highly rated fixed-income portfolio. About 9% of its investments as of Sept. 30, 2017, excluding Life Re's funds withheld assets, were in short-term investments and cash and cash equivalents. We believe XL generates sufficient cash flow and access to liquid assets and credit lines to meet its short- and long-term cash requirements for its operations. XL has several credit facilities it uses to support its U.S. non-admitted re/insurance operations and capital requirements at Lloyd's. As of Sept. 30, 2017, the group had letter-of-credit facilities totaling $4.0 billion, of which $2.4 billion was utilized.

XL Group -- Debt Maturity Profile



Accounting Considerations

In second-quarter 2014, XL completed the sale of its subsidiary, XL Life Reinsurance (SAC) Ltd. (XLLR), to GreyCastle Holdings Ltd. XLLR reinsured the majority of XL's life reinsurance business via 100% quota share. This transaction covers a substantial portion of XL's life reinsurance reserves. As part of the retrocession, XL will no longer be exposed to the majority of its life reinsurance's invested assets volatility, given that the market volatility is passed on to XLLR through the funds withheld arrangement. As a result, XL is exposed to a large collateralized reinsurance recoverable from XLLR of approximately $4.2 billion. However, the counterparty credit risk is limited, as we expect the collateral to exceed the recoverable. In 2014, the transaction resulted in an overall after-tax U.S. generally accepted accounting principles net loss of $621 million. As a result of the transaction and associated accounting, the company's net income is subject to variability related to investment income and changes in valuation of funds withheld, which runs through XL's income statement (though reversed in comprehensive income). In our analysis of adjusted earnings before interest and taxes, return on revenue, and fixed-charge coverage, we exclude the impact of earnings and (un)realized gains related to life-funds withheld assets, and also exclude investments withheld from our capital model.

On Dec. 2, 2015, XL announced that its wholly owned subsidiary, XL Life Ltd., entered into a definitive agreement to reinsure a block of U.S. term life treaties to a subsidiary of Reinsurance Group of America Inc. This transaction includes all U.S. term life reinsurance policy reserves and cedes 80% of the remaining life reinsurance premiums that were not included in XL's 2014 sale of its life reinsurance subsidiary, SAC.

Related Criteria

- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Insurance - General: Enterprise Risk Management, May 7, 2013
- Criteria - Insurance - General: Insurers: Rating Methodology, May 7, 2013
- General Criteria: Methodology And Assumptions: Assigning Equity Content To Corporate Entity And North American Insurance Holding Company Hybrid Capital Instruments, April 1, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Criteria - Insurance - General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Insurance - General: Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

Related Research

- XLIT Ltd. And Subsidiaries Outlook Revised To Stable From Positive On Lower Capitalization; Ratings Affirmed, Oct. 12, 2017

Ratings Detail (As Of December 8, 2017)	
Holding Company: XLIT Ltd.	
Issuer Credit Rating	A-/Stable/--
Junior Subordinated	BBB
Preference Stock	BBB
Preferred Stock	BBB
Senior Unsecured	A-
Subordinated	BBB
Operating Companies Covered By This Report	
XL Bermuda Ltd.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Counterparty Credit Rating	
Local Currency	A+/Stable/--
Catlin Insurance Co. Inc.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
Catlin Insurance Co. Ltd.	
Financial Strength Rating	
Local Currency	A/Stable/--

Ratings Detail (As Of December 8, 2017) (cont.)	
Issuer Credit Rating	
Local Currency	A/Stable/--
Preferred Stock	BBB+
Catlin Insurance Co. (U.K.) Ltd.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Catlin Speciality Insurance Co.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
Greenwich Insurance Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Indian Harbor Insurance Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
XL Insurance America Inc.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
XL Insurance Company SE	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/NR
XL Insurance Co. of New York, Inc.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
XL Insurance Switzerland Ltd.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--

Ratings Detail (As Of December 8, 2017) (cont.)	
XL Re Europe SE	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
XL Reinsurance America Inc.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
XL Re Latin America Ltd.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
XL Re Ltd. - U.K.	
Financial Strength Rating	
Local Currency	A+/Stable/--
XL Select Insurance Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
XL Specialty Insurance Co.	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
Related Entities	
Catlin Re Switzerland Ltd	
Financial Strength Rating	
Local Currency	A+/Stable/--
Issuer Credit Rating	
Local Currency	A+/Stable/--
X.L. America, Inc.	
Issuer Credit Rating	
Local Currency	A-/Stable/--
Domicile	Bermuda

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.