

Factory Mutual Insurance Co.

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Factory Mutual Insurance Co.

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

*Stand-alone credit profile.
See Ratings Detail for a complete list of rated entities and ratings covered by this report.

Major Rating Factors

Strengths	Weaknesses
<ul style="list-style-type: none"> Industry leader in engineering-based property underwriting and research Highly valued customized loss prevention services complementing large commercial property products Strong long-term underwriting performance with recent outsized losses due to natural catastrophes 	<ul style="list-style-type: none"> Susceptibility to significant capital and earnings volatility arising from high exposure to catastrophic events Large equity portfolio exposing capital to financial-market volatility Growth prospects limited by relatively narrow focus on commercial property coverage

Rationale

S&P Global Ratings' ratings on Factory Mutual Insurance Co. and its core operating subsidiaries (collectively, FM Global) reflect the group's very strong business risk profile (BRP) and strong financial risk profile that lead us to a split anchor of 'aa-/a+'. We assigned the latter, reflecting our view of the BRP as being on the lower end of the very strong assessment due to the company's narrow focus on commercial property.

Our ratings also reflect FM Global's adequate enterprise risk management (ERM) with sufficient processes to control the large risks assumed by the group. It has strong liquidity arising from its liquid investment portfolio and strong operating cash flows. Further supporting our ratings is FM Global's adequate financial flexibility. As a mutual insurer it lacks access to the public equities markets, but the group holds no debt, consistently maintains sufficient levels of cash and short-term investments, and has access to large, highly rated reinsurers.

Outlook: Stable

The stable outlook reflects our view that the group has a very strong competitive position supported by its highly regarded reputation for assessing risk to prevent and mitigate loss and leading market presence in the large commercial property market. FM Global's extremely strong capital adequacy and generally strong operating results also allow it to absorb catastrophe losses and financial market volatility. Given FM Global's monoline focus on large commercial property, the potential for elevated catastrophe losses is always present, and such losses have resulted in material underperformance in the past two years--an unusual occurrence for the group. But we expect a combined ratio of 92%-95% in the next two years, assuming a more-normal level of catastrophe losses.

Downside scenario

We could lower the ratings in the next 12-24 months if FM Global's operating performance comes in substantially below our expectations, and we believe that a systemic change has occurred that's weakened its competitive position. We may also lower our ratings if, during the next two years, FM Global's capital redundancy per our proprietary risk-adjusted capital model falls and persists below the 'AAA' confidence level due to significant underwriting losses and/or equity markets volatility.

Upside scenario

It is unlikely that we will raise the ratings in the next two years because of FM Global's exposure to capital and earnings volatility stemming from its high equity concentration and narrow focus on the commercial property business.

Macroeconomic Assumptions

- Real U.S. GDP growth of about 2.3% in 2019 and 1.8% in 2020
- 10-year Treasury rate of about 3.4% in 2019 and 3.6% in 2020
- Consumer Price Index (CPI) at about 2.2% in 2019 and 2.4% in 2020
- Somewhat inelastic demand for property/casualty (P/C) insurance products
- Neutral industry economic outlook for P/C insurers

Key Metrics

(Mil. \$)	--Year ended Dec. 31--						
	2020*	2019*	2018	2017	2016	2015	2014
Net premiums earned	4,000	3,950	3,892	3,910	3,601	3,579	3,617
Net income	400-500	400-500	161	254	797	738	956
Property/casualty net combined ratio (%)	92-95	92-95	128.6	129.9	83.2	85.3	79.4
Return on revenue (%)	11-13	11-13	(17.4)	(19.3)	23.6	21.5	27.1
Return on shareholders' equity -- reported (%)	3-4	3-4	1.4	2.0	6.9	6.8	9.4
S&P Global Ratings' capital adequacy/redundancy	Extremely strong	Extremely strong	Extremely strong	Extremely strong	Extremely strong	Extremely strong	Extremely strong

*Forecast data reflect S&P Global Ratings' base-case assumptions.

Business Risk Profile: Very Strong

FM Global is a global commercial property insurer and risk management services provider focused on the large commercial property market. Its operations are globally diversified and mostly in developed markets that we typically view as low risk. We believe FM Global's P/C operations are exposed to intermediate industry risk due to the sector's inherent product risk in these markets.

We base our very strong assessment of FM Global's competitive position on its strong reputation and major presence in the large commercial property market. Its highly regarded reputation for engineering expertise in assessing client risks to prevent and mitigate losses gives it a significant commercial advantage over competitors, as shown by its high client retention and generally favorable underwriting performance. FM Global reported strong 10-year (2009-2018) operating results based on an average combined ratio of 94.6%. But more-recent performance has been significantly affected by catastrophe events in 2017 and 2018, which pushed its five year (2014-2018) average combined ratio above 100%, highlighting the volatility inherent in its business concentration. Despite 2017-2018's lagging underwriting performance, we expect a return to a more-normal level of catastrophe losses that will lead the group to report a combined ratio of 92%-95% (assuming about 20 percentage points in annual catastrophe losses) in the next two years.

Financial Risk Profile: Strong

We view FM Global's capital adequacy as extremely strong, supported by strong earnings generation and its mutual structure. We assess its capital redundancy as well within the 'AAA' range per our proprietary capital adequacy model. This mitigates the risk of substantial losses due to catastrophe events or a sharp decline in equity markets causing a significant decline in capital. While 2017 and 2018 underwriting and investment losses did not modify our capital assessment, we view the group's earnings volatility as partially offsetting its generally strong underwriting performance.

We regard FM Global's risk position as high, specifically due to its large proportion of equity investments (44% of its investment portfolio, including private equity and hedge funds), exposure to catastrophic events, and some legacy asbestos and environmental exposure. Its high catastrophe exposure is a direct result of its large commercial property business concentration. While the group does have a high risk tolerance toward equities, the risk is partially offset by its adequate diversification by issuer and sector.

Other Assessments

ERM is of high importance to our ratings because of the group's exposure to large complex risks that could quickly cause a significant loss of capital and earnings. We regard FM Global's ERM framework as adequate because it can identify, measure, and manage most key risk exposures and losses. The cornerstone of its ERM program is the group's positive risk management culture. FM Global employees are predominantly engineers with substantial technical expertise who work as underwriters and claims adjusters, fostering a deep-rooted risk-reward culture. FM Global believes the majority of losses are preventable, and it works diligently with its insureds to help foster best-in-class loss-prevention plans. FM Global's senior management has sustained its strategy of providing extensive competitive property insurance capacity. Management has significant depth and breadth in the business, reflective of its tendency to make promotions within the company.

We do not expect FM Global to face any liquidity constraints from meeting its obligations in the next two years due to its strong operating cash flows.

Other Considerations

Group ratings methodology

FM Global includes insurance operating companies Factory Mutual Insurance Co. (FMIC), Affiliated FM Insurance Co. (AFM), F.M. Insurance Co. Ltd. (FMI), and FM Insurance Europe S.A. (FMIE). FMIC is the flagship insurance company and parent company of AFM, FMI, and FMIE, which, under our group methodology criteria, we view as core to FMIC. FMIC and AFM are U.S.-based and participate in an intercompany reinsurance pooling agreement. U.K.-based FMI and Luxembourg-based FMIE each benefit from explicit support provided by FMIC in the form of a reinsurance agreement and performance guarantee. Under the reinsurance agreement, FMIC provides excess-of-loss protection and stop-loss protection to each subsidiary. Under the performance guarantee, FMIC assures the full performance of the lawful obligations with respect to contracts of insurance and reinsurance issued by each subsidiary.

Accounting considerations

As an alternative to dividends, FM Global routinely provides a membership credit to policyholders. When afforded, the credit is contingent upon renewal or anniversary of an existing policy and is recorded as a reduction of net premium earned. FMIC and AFM each file U.S. statutory financial statements. FMIE's and FMI's annual financial statements are prepared using local accounting standards in Luxembourg and the U.K., respectively. The group also prepares consolidated annual financial statements under U.S. generally accepted accounting principles (GAAP). We believe all of the group's accounting is consistent with industry standards.

Related Criteria

- General Criteria: Guarantee Criteria, Oct. 21, 2016
- 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: 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

Ratings Detail (As Of February 20, 2019)

Operating Companies Covered By This Report

Ratings Detail (As Of February 20, 2019) (cont.)

Factory Mutual Insurance Co.

Financial Strength Rating

Local Currency

A+/Stable/--

Issuer Credit Rating

Local Currency

A+/Stable/--

Affiliated FM Insurance Co.

Financial Strength Rating

Local Currency

A+/Stable/--

Issuer Credit Rating

Local Currency

A+/Stable/--

F.M. Insurance Co. Ltd.

Financial Strength Rating

Local Currency

A+/Stable/--

Issuer Credit Rating

Local Currency

A+/Stable/--

FM Insurance Europe S A

Financial Strength Rating

Local Currency

A+/Stable/--

Issuer Credit Rating

Local Currency

A+/Stable/--

Domicile

Rhode Island

*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.

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