# Citing long-term care exposures, A.M. Best lowers Genworth’s strength ratings

By Editorial Staff    *Thu, Feb 19, 2015*

*Genworth’s LTC business “is likely to exhibit volatility going forward due to the limited credibility of claims data, the profile of its in-force block and the challenge of achieving regulatory approval for actuarially justified rate increases,” the ratings agency reported.*

The ratings agency A.M. Best has downgraded the financial strength ratings of three key life/health subsidiaries of Genworth Financial Inc. to A- (Excellent) from A (Excellent) and the issuer credit ratings (ICR) to “a-” from “a”.

The three subsidiaries are Genworth Life Insurance Co. (GLIC), Genworth Life Insurance Co. of New York, and Genworth Life and Annuity Insurance Co.

A.M. Best also downgraded the ICR to “bbb-” from “bbb” of Genworth and its existing debt ratings by one notch. The ratings had been under review with negative implications since Dec. 18, 2014. The outlook assigned to all ratings is stable.

Driving the downgrade, A.M. Best said in a release, was the opinion that Genworth’s long-term care insurance (LTC) business “is likely to exhibit volatility going forward due to the limited credibility of claims data (particularly with later-stage claim duration data), the profile of its in-force block and the challenge of achieving regulatory approval for actuarially justified rate increases.”

A.M. Best noted the continued poor performance of the acquired block (i.e., business acquired before 1996). Additionally, roughly one-third of Genworth’s older vintage organically written LTC contracts, amounting to $1.1 billion, have lifetime benefits. (Genworth has slightly more than $2.5 billion of total in-force LTC premium.) A.M. Best believes that it is important for Genworth to take actions to reduce this tail risk, such as policyholders accepting reduced benefits in lieu of higher premiums.

On the plus side, A.M. Best said it “believes future positive rating actions could occur if LTC profitability substantially improves, GLIC’s risk-adjusted capital is maintained at or above current levels and operating performance of the mortgage insurance operations continues to trend favorably.”

But further negative ratings could occur “if a material weakness in internal controls is identified, if GLIC’s risk-adjusted capital falls below A.M. Best’s expectations, or if another significant reserve charge on the in-force LTC block is taken."

According to the A.M. Best release:

"In the near to medium term, the company is unlikely to experience growth in sales of life insurance, annuities or long-term care, which may pressure operating results in this segment. Genworth may also face additional challenges within the U.S. mortgage insurance (USMI) segment regarding its ability to execute one or more reinsurance transactions to comply with the yet-to-be finalized Private Mortgage Insurance Eligibility Requirements (PMIERs) capital standards.

"While the performance of USMI recently has been trending favorably, it will likely take a few years for the business to contribute significant dividends. Genworth's Canadian and Australian mortgage insurance operations continue to generate solid cash flows that the holding company will rely on primarily to service its debt obligations.

"As management has committed to refraining from taking dividends from the domestic life/health companies in the near to medium term, A.M. Best will monitor Genworth's ability to source healthy dividends from the mortgage insurance operations if a sell-down of either Australian and/or Canadian operation is undertaken.

"A.M. Best notes that Genworth plans to allocate new money to slightly lower credit quality assets over the long term. This concern is mitigated by the organization's seasoned investment management team, its sound risk-adjusted capital position at the life/health entities and good financial flexibility at the holding company, with more than $1.1 billion of cash and liquid assets.

"Additionally, A.M. Best views favorably Genworth's plans to repatriate the LTC business currently at its Bermuda affiliate, Brookfield Life and Annuity Insurance Company Limited. Moreover, A.M. Best recognizes Genworth's favorable history of achieving premium rate increases on its in-force blocks.

"The ability of the company to successfully obtain state regulatory approvals for rate actions, achieve expense savings from the corporate consolidation and divest non-core operations and unprofitable blocks of business are key factors driving the firm's future profitability.

The ratings downgrade followed Genworth's reporting of fourth-quarter 2014 results, which reflected the substantial completion of its long-term care insurance (LTC) active life margin review. Additionally, management confirmed its intention to conduct a thorough review of Genworth’s businesses, encompassing holding company debt reduction and a multistep restructuring plan to streamline operations.