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GLOBAL CREDIT RATING CO.

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GLOSSARY OF TERMS, ACRONYMS AND RATIOS USED IN THE INSURANCE SECTOR

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Introduction

This list of terms, acronyms and ratios is compiled from those that are commonly used in Global Credit Ratings' published reports and occasional research papers. The content of this glossary is not intended to be comprehensive and/or complete, remains a work in progress and will be updated periodically as needed.

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Terms, Acronyms and Ratios (A-Z Selector)

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A

Accident	An unplanned event, unexpected and undesigned, which occurs suddenly and at a definite place.
Accommodation Line	Business accepted from an agent or broker, which would normally be rejected according to strict underwriting standards but which is accepted because of the overall profitability of the agent's or customer's other business.
Accounting	A process of recording, summarising, and allocating all items of income and expense of the company and analysing, verifying and reporting the results.
Acquisition Cost	The expenses incurred by an insurance company that are directly related to putting the business on the books of the company. The largest portion of this cost is usually the agent's or sales representative's commission or bonus.
Actuary	A person proficient in the study of mathematics, statistics and finance who applies this knowledge to problems in the corporate arena to solve problems involving variable circumstances and outcomes with related probability distributions, whilst taking practical financial considerations into account.
Adjuster	A representative of the insurer who seeks to determine the extent of the firm's liability for loss when a claim is submitted.
Administrative Services	An arrangement under which an insurer or independent organisation will, for a fee, handle the administration of claims, benefits and other administrative duties for a group.
Admissible	Values that are permitted by law to be included for regulatory purposes.
Agency	An insurance sales office which is directed by an agent, manager, independent agent, or company manager.
Agent	One who solicits, negotiates or effects contracts of insurance on behalf of an insurer. An agent can be independent, being one that represents several companies, or a captive (tied) agent that sells insurance for only one company.
Aggregate Limit	Indicates the amount of coverage that the insured has under the contract for a specific period of time, usually the contract period, no matter how many separate accidents may occur.
All-Risks Insurance	Insurance against loss of or damage to property arising from any fortuitous cause except those that are specifically excluded.
Amortisation	From a liability perspective, the paying off of debt in a series of instalments over a period of time. From an asset perspective, the spreading of capital expenses for intangible assets over a specific

period of time (usually over the asset's useful life).

Annual Financial Report	The annual report of an insurer to a governmental regulatory body, showing its assets and liabilities, receipts and disbursements, and other financial data. Often the information has to be contained in a prescribed format.
Annual Report	A status report on the current financial condition of a company. It usually includes the chairman's report, the auditor's report and detailed financial statements. It is issued once a year for shareholders to examine before the annual general meeting (AGM). In many markets, comprehensive Integrated Reports covering a wide spectrum of information have replaced traditional annual reports.
Annuity	A contract that provides a series of payments for a specified period of time which may or may not be contingent on the survival of the annuitant.
Assets	A resource with economic value that a company owns or controls with the expectation that it will provide future benefit.
Assurance	Terminology used to describe life insurance. This is common practice in Great Britain, Canada and South Africa. Insurance is usually used for the description of short-term insurance. However, the term insurance is used indiscriminately to describe both life and short-term insurance in practice.
Automatic Cover	Coverage given automatically by a policy, usually for a specified period and limited amount, to cover increasing values and newly acquired and changing interests.
Audited Financial Statements (AFS)	Financial statements that bear the report of independent auditors (attesting to the financial statements' fairness and compliance with generally accepted accounting principles).
Average Premium Debtors Days	Measures the number of days it takes on average to collect outstanding premiums, relative to the gross premiums written for the period.

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Bad Debt	Amounts in arrears, i.e. overdue, and often classified as defaulted or written-off.
Balance Sheet	Also known as a Statement of Financial Position. A statement of a company's assets and liabilities provided for the benefit of shareholders and regulators. It gives a snapshot at a specific point in time of the assets the company holds and how they have been financed.
Bankruptcy	Court proceedings at which an individual or a company is declared unable to pay its creditors. The liabilities of a bankrupt company typically exceed its assets.
Basis Point	A basis point is 1/100th of a percentage point.
Beneficiary	Nominated person or institution in the policy document that is entitled to receive the proceeds stated in the policy.
Benefits	Financial reimbursement and other services provided to insureds by insurers under the terms of an insurance contract.
Binder	An agreement by which an insurer mandates a third party (or binder holder) to perform certain functions for and on its behalf. These functions relate to the administration of insurance policies and subsequent claims.
Bond	A long term debt instrument issued by either: a company, institution or the government to raise funds.
Book of Business	A total of all insurance policies written by an insurer.
Book Value	The value at which an asset is carried on a company's balance sheet.
Bourse	French term for stock exchange.
Branch Offices	Offices established in various areas for product distribution.
Broker	One who represents an insured in the solicitation, negotiation or procurement of contracts of insurance, and who may render services incidental to those functions. By law the broker may also be an agent of the insurer for certain purposes such as delivery of the policy or collection of the premium.
Budget	Financial plan that serves as an estimate of future cost, revenues or both.
Business Cycle	Regular fluctuations in overall activity in an economy over time. The cycle has four distinct elements: recession, recovery, peak and

slowdown.

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C

Capacity	The largest amount of insurance available from a company. In a broader sense, it can refer to the largest amount of insurance available in the marketplace.
Capital	The sum of money that is invested to generate proceeds.
Capitalisation	The provision of capital for a company, or the conversion of income or assets into capital.
Capital Adequacy	A measure of the adequacy of an entity's capital resources in relation to its risks.
Capital Base	The issued capital of a company, plus reserves and retained profits.
Capital Gain	Profit realised on the sale of securities. An unrealised capital gain is an increase in the value of securities that have not been sold.
Captive Insurance Company	A company owned solely or in large part by one or more non-insurance entities for the primary purpose of providing insurance coverage to the owner or owners.
Cash	Funds that can be readily spent or used to meet current obligations.
Cash Equivalent	An asset that is easily and quickly convertible to cash such that holding it is equivalent to holding cash.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Cash Flow Statement	The cash flow statement shows the cash flows associated with the operating, investing and financing activities of a company, combining to explain the net movement in cash holdings.
Catastrophe (CAT)	An event, which causes a loss of extraordinary magnitude.
Catastrophe Reinsurance	A form of reinsurance that indemnifies the ceding company for the accumulation of losses in excess of a stipulated sum arising from a catastrophic event such as conflagration, earthquake or windstorm.
Cede	To transfer all or part of a risk written by an insurer (the cedant or primary company) to a reinsurer.
Cession	Amount of the insurance ceded to a reinsurer by the original insuring

company (cedant) in a reinsurance transaction.

Claim	A request for payment of a loss, which may come under the terms of an insurance contract.
Claims Cash Months Cover	Indicates the number of months that an insurer would be able to pay out claims incurred using current cash and equivalent balances.
Claims Incurred	Claims that have occurred, irrespective of whether or not they have been reported to the insurer.
Coinsurance	A policy provision by which the multiple insurers share the covered losses under a policy in a specified ratio.
Combined Ratio	Measures the ability to conserve profits through the expense line.
Commercial Lines	Insurance for businesses, professionals, and commercial establishments.
Commercial Paper (CP)	A negotiable instrument with a maturity of less than one year.
Commission (Comm)	A certain percentage of premiums produced that is received or paid out as compensation by an insurer.
Compulsory Insurance	Any form of insurance, which is required by law.
Conditions	Provisions inserted in an insurance contract that qualify or place limitations on the insurer's promise to perform.
Consumer Price Index (CPI)	CPI is an index of inflation. It is calculated by collecting and comparing the prices of a set basket of goods and services bought by a typical consumer at regular intervals over time.
Contract	An agreement by which an insurer agrees, for a consideration, to provide benefits, reimburse losses or provide services for an insured. A "policy" is the written statement of the terms of the contract.
Convertible Bond	A bond that is convertible into shares at a pre-set conversion price. Conversion may be automatic or at the option of the holder.
Cooperative Insurance	Insurance issued by a mutual association such as a fraternal society, an employee association, an industrial association, or a trade union.
Country Risk	The range of risks emerging from the political, legal, economic and social conditions of a country that have adverse consequences affecting investors and creditors with exposure to the country, and may also include negative effects on financial institutions and borrowers in the country.
Coverage	The scope of protection provided under a contract of insurance.

Credit Rating	An opinion regarding the creditworthiness of an entity, a security or financial instrument, or an issuer of securities or financial instruments, using an established and defined ranking system of rating categories.
Credit Rating Agency	An entity that provides credit rating services.
Creditworthiness	An assessment of a debtor's ability to meet debt obligations.
Currency Risk	The potential for losses arising from adverse movements in exchange rates.
Current Assets	Assets that can be expected to turn into cash within a year or less.

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Death Benefit	A payment made to a designated beneficiary upon the death of the policy holder.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Debt Equity Ratio	Measures the proportion of debt and equity used to finance assets.
Debt Servicing Capabilities	A measure of a company's ability to service its interest and principal redemption costs, expressed as the ratio of earnings or cash flows over a period to the sum of interest and principal payments over the same timeframe.
Debt Service Coverage	Measures the ratio of cash available for debt servicing to interest, principal and lease payments.
Deductible	The portion of an insured loss to be borne by the insured before he is entitled to recovery from the insurer.
Default	Failure to meet the payment obligation of either interest or principal on a debt or bond. Technically, a borrower does not default, the initiative comes from the lender who declares that the borrower is in default.
Deposit Administration	A type of group annuity providing for the accumulation of contributions in an undivided fund out of which annuities are purchased as the individual members of the group retire.
Disability Benefit	A feature added to some life insurance policies providing for waiver of premium, and sometimes payment of monthly income, if the policy holder becomes totally and permanently disabled.

Distribution Channel	The method utilised by the insurance company to sell its products to policyholders.
Diversification	Spreading risk by constructing a portfolio that contains different investments, whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Dividend	The portion of a company's after-tax earnings that is distributed to shareholders.
Dividend Cover	The extent to which a company's dividend is matched or exceeded by the earnings available for distribution to shareholders.
Dread Disease Insurance	Insurance providing an unallocated benefit, subject to a maximum amount, for expenses incurred in connection with specified diseases, such as cancer, poliomyelitis, encephalitis and spinal meningitis.
Downgrade	The assignment of a lower credit rating to an insurer by a credit rating agency. Opposite of upgrade.
Drawdown	When a company utilises facilities availed by a financial institution or an international lender there is said to be a drawdown of funds.
Dual Listing	A company that is listed on more than one stock exchange.

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Earned Premium	That part of the premium applicable to the expired part of the policy period, including the short-rate premium on cancellation, the entire premium on the amount of loss paid under some contracts, and the entire premium on the contract on the expiration of the policy. When a premium is paid in advance for a certain time, the company is said to “earn” the premium as the time advances.
Earned Loss Ratio	Measures the proportion of claims to the net premiums earned.
Earnings Before Interest, Taxes, Depreciation, and Amortisation (EBITDA)	EBITDA is useful for comparing the income of companies with different asset structures. EBITDA is usually closely aligned to cash generated by operations.
Economies of Scale	Economies of scale are the cost advantages of an increase in output if the fixed costs of doing so remain the same. The marginal cost, or the cost of the last unit of production, falls as output is raised.
Effective Tax Rate	Measures the average rate at which earned income is taxed.
Equity (or Shareholder’s Funds)	Equity is the holding or stake that shareholders have in a company. Equity capital is raised by the issue of new shares or by retaining profit.
Equity Investment (Equities)	An instrument that signifies an ownership position of shares of stock in a company that is either listed or traded on a stock exchange (also

	known as a counter) or are unlisted.
Enterprise Risk Management (ERM)	ERM refers to an integrated or holistic approach to managing risk across an organisation, using clearly articulated frameworks and processes controlled from board level.
Ex Gratia Payment	A payment by an insurer to an insured for which there is no liability under the contract. In some cases an insurer may feel there has been a mistake or a misunderstanding, and he may pay a claim even though he does not appear to be liable.
Excess of Loss (XoL)	A type of reinsurance that covers specified losses incurred by the cedant in excess of a stated amount (the excess) up to a higher amount. An excess of loss reinsurance is a form of non-proportional reinsurance.
Exchange Rate	The value of one country's currency expressed in terms of another.
Execution Risk	The risk that a company's business plans will not be successful when they are put into action.
Experience	A term used to describe the relationship, usually expressed as a percent or ratio, of premiums to claims for a plan, coverage, or benefits for a stated time period.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For an insurer, its exposure may also relate to the risk related to policies issued.

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Facultative	Facultative reinsurance means reinsurance of individual risks by offer and acceptance wherein the reinsurer retains the “faculty” to accept or reject each risk offered.
Fair Value	The fair value of a security, an asset or a company is the rational view of its worth. It may be different from cost or market value.
Financial Flexibility	The company’s ability to access additional sources of capital funding.
Financial Leverage	The degree to which a company uses debt relative to equity in its capital structure.
Financial Services Board (FSB)	A regulatory agency responsible for the non-banking financial services industry in South Africa. It is an independent body that supervises and regulates the financial services industry in the public interest.
Financial Statements	Presentation of financial data including balance sheets, income statements and statements of cash flow, or any supporting statement that is intended to communicate an entity’s financial position at a point in time.

Financial Year (FYE)	The year used for accounting purposes by a company. It can be a calendar year or it can cover a different period. It can also be referred to as the fiscal year.
Fixed Assets	Assets of a company that will be used or held for longer than a year. They include tangible assets, such as land and equipment, stake in subsidiaries and other investments, as well as intangible assets such as goodwill, information technology or a company's logo and brand.
Fixed Deposit	Where funds are deposited in a savings account for a pre-determined period of time.
Forecast	A calculation or estimate of future financial events.
Fronting	The act of providing claims or administrative services by a primary insurer to a secondary insurer or reinsurer, with no risk retention.

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Gearing	Gearing (or leverage) refers to the extent to which a company is funded by debt and can be calculated by dividing its debt by shareholders' funds or by EBITDA.
Generally Accepted Accounting Principles (GAAP)	A term that refers to the standards and conventions that underpin accounting rules and the preparation of financial statements in a particular country.
Going Concern	An accounting convention that assumes a company will continue to exist and trade normally for the foreseeable future. In practice this is likely to mean at least for the next 12 months.
Goodwill	Arises upon the sale/acquisition of a business and is defined as an established entity's reputation, which may be regarded as a quantifiable asset and calculated as the price paid for a company over and above the net value of its assets. Negative goodwill refers to a situation when the price paid for a company is lower than the value of its assets.
Gross Incurred Loss	The total gross amount of paid claims and loss reserves associated with a particular time period, usually a policy year.
Gross Written Premium Growth	Measures the growth in total premiums written and assumed by an insurer before deductions for reinsurance and ceding commissions.
Group Annuity	A pension plan providing annuities at retirement to a group of people under a master policy. It is usually issued to an employer for the benefit of employees. The individual members of the group hold certificates as evidence of their annuities.
Group Life Insurance	Group insurance plan providing life insurance for employees under a master policy.

H

Haircut	The percentage by which the market value of an asset is reduced. The size of the haircut reflects the expected ease of selling the asset and the likely reduction necessary to realised value relative to the fair value.
Hard Market	That part of the insurance sales cycle in which competitive pricing is at a minimum as companies charge the premiums necessary to meet their underwriting losses in order to avoid insolvency and boost capacity. Usually associated with a sharp decline in capacity.
Hazard	A specific situation that increases the probability of the occurrence of loss arising from a peril, or that may influence the extent of the loss.

I

Illiquid	Markets or financial instruments are described as being illiquid if there are few buyers and sellers. Assets may also be considered illiquid. It may be difficult, or even impossible, to find a reliable price for an illiquid security.
Impairment	Reduction in the value of an asset because the asset is no longer expected to generate the same benefits, as determined by the company through periodic assessments.
Income Statement	A summary of all the expenditure and income of a company over a set period.
Incurred But Not Reported (IBNR)	Losses which have occurred during a stated period, usually a calendar year, but have not yet been reported to the insurer as of the date under consideration.
Incurred Claims	The total amount of paid claims and loss reserves associated with a particular time period, usually a policy year.
Incurred Loss	The total amount of paid claims and loss reserves associated with a particular time period, usually a policy year.
Industry Risk	The risk that defaults will arise in an industry because of factors specifically affecting that industry.
Insolvent Insurer	An insurer which is unable to meet its financial obligations.
Intangible Assets	The non-physical assets of a company such as trademarks, patents, copyright, information systems and goodwill.

International Financial Reporting Standards (IFRS)	IFRS is designed as a common global language for business affairs so that company accounts are understandable and comparable across international boundaries.
International Scale Rating (ISR)	ISRs relate to either foreign currency or local currency commitments, assessing the capacity of an issuer to meet these commitments using a globally applicable (and therefore internationally comparable) scale.
International Solvency Margin	Measures the ability to cover current year's written premiums using shareholder's funds.
Intermediary	A third party in the sale and administration of insurance products.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Interest Rate	The charge or the return on an asset or debt expressed as a percentage of the price or size of the asset or debt. It is usually expressed on an annual basis.
Interest Rate Risk	The potential for losses or reduced income arising from adverse movements in interest rates.
Investment Income	The income generated by a company's portfolio of investments.
Investment Portfolio	A collection of investments held by an individual investor or financial institution.
Investment Risk	The risk of a decline in the net realisable value of investment assets arising from adverse movements in market prices or factors specific to the investment itself (e.g. reputation and the quality of management).
Investment Yield (excluding unrealised gains/losses)	Measures the investment return achieved relative to funds invested in financial instruments, excluding unrealised gains/losses.
Investment Yield (including unrealised gains/losses)	Measures the investment return achieved relative to funds invested in financial instruments, including unrealised gains/losses.

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Lapsed Policy	A policy which has been allowed to expire because of non-payment of premiums.
Layer	A horizontal segment of the liability insured, e.g., the second R100,000 of a R500,000 liability is the first layer if the cedant retains R100,000 but a higher layer if it retains a lesser amount.
Lead Reinsurer	The reinsurer who negotiates the terms, conditions, and premium rates and first signs on to the slip. Reinsurers who subsequently sign on to the slip under those terms and conditions are considered following reinsurers.
Liabilities	All financial claims, debts or potential losses incurred by an individual or an organisation.
Life Annuity	A series of payments under which payments, once begun, continue throughout the remaining lifetime of the annuitant but not beyond.
Life Expectancy	The average number of years of life remaining for a group of persons of a given age according to a particular mortality table.
Line of Business	The classification of business as utilised in the insurance industry.
Liquidity	The speed at which assets can be converted to cash. The ability of an insurer to convert its assets into cash to pay claims if necessary. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Liquid Assets	Assets, generally of a short term, that can be converted into cash.
Liquidity Risk	The risk that a company may not be able to meet its financial obligations or other operational cash requirements due to an inability to timeously realise cash from its assets. Regarding securities, the risk that a financial instrument cannot be traded at its market price due to the size, structure or efficiency of the market.
Long Term	Not current; ordinarily more than one year.
Loss	The amount paid on a claim when the insurer is liable.
Loss Control	Any combination of actions taken to reduce the frequency or severity of losses.
Loss Development	The difference between the amount of losses initially estimated by the insurer and the amount reported in an evaluation on a later date.
Loss Frequency	The number of times a loss occurs over a specific period of time.
Loss Severity	The amount of a loss expressed in financial terms.

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Management Expenses	Expenses linked to management's efforts to run the day to day business. This includes amongst other things marketing & administrative expenses.
Market Risk	Volatility in the value of a security/asset due to movements in share prices, interest rates, currencies, commodities or wider economic factors.
Monoline Policy	Any insurance coverage written as a single line policy.
Moral Hazard	A condition of morals or habits that increases the probability of loss from a peril. An extreme example would be an individual who previously burned his own property to collect the insurance.
Morbidity	The incidence and severity of sicknesses and accidents in a well-defined class or classes or persons.
Mortality	A table showing how many members of a group, starting at a certain age, will be alive at each succeeding age. It is used to calculate the probability of dying in, or surviving through, any period, and for the valuation of an annuity.

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National Scale Rating (NSR)	The national scale provides a relative measure of creditworthiness for rated entities only within the country concerned. Under this rating scale, a 'AAA' long term national scale rating will typically be assigned to the lowest relative risk within that country, which in most cases will be the sovereign state.
Net Asset Value (NAV)	The value of an entity's assets less its liabilities. It is a reflection of the company's underlying value and is usually quoted on a per share basis.
Net Commission Expense Ratio	Measures the proportion of commission expense to net premiums.
Net Incurred Loss	The total amount of paid claims and loss reserves associated with a particular time period, less the reinsurance portion.
Net Loss	The amount of loss sustained by an insurer after giving effect to all applicable reinsurance, salvage, and subrogation recoveries.
Net OCR/NWP	Measures the proportion of outstanding claims reserve to net written premiums.
Net Profit	Trading/operating profits after deducting the expenses detailed in the profit and loss account such as interest, tax, depreciation, auditors' fees and directors' fees.

Net Premiums Earned (NPE)	That portion of a policy's premium that applies to the expired portion of the policy, net of reinsurance premiums and net movements in the unearned premium reserve.
Net Retention	The percentage of insurance that a ceding company keeps for its own account and does not reinsure.
Non-Admitted Assets	Assets that do not qualify under law for insurance statement purposes.
Net Written Premium (NWP)	Written premium less deductions for commissions and ceded reinsurance.
Net UPR/NWP	Measures the proportion of unearned premiums to net written premiums.

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O

Off Balance Sheet	Off balance sheet items are assets or liabilities that are not shown on a company's balance sheet. They are usually referred to in the notes to a company's accounts.
Operating Expense Ratio	Measures the proportion of operating expenses to net premiums earned.
Operating Margin	Measures the efficiency of profit generation from investments and underwriting.
Operating Profit	Profits from a company's ordinary revenue-producing activities, calculated before taxes and interest costs.
Operational Risk	The risk of loss resulting from inadequate or failed internal processes, people or systems or from external events. This includes legal risk, but excludes strategic risk and reputational risk.
Operating Result	The sum of underwriting result and investment income.
Ordinary Life	A policy which continues during the whole of the insured's life and provides for the payment of the amount insured at the insured's death.
Outstanding Claims Reserve (OCR)	A technical reserve of an insurance company established to provide for the future liability for claims which have occurred and have been reported but which have not yet been settled.
Outstanding Premiums	Premiums due but not yet collected. Also referred to as premium debtors or premium receivables.
Overriding Commission	(1) A commission which an agent or broker may receive on any business sold in his exclusive territory by subagents. Also sometimes called "overwriting" or "overriding." (2) An allowance paid to a ceding company over and above the acquisition cost to allow for overhead expenses, often including a margin for profit.

P

Parent Company	A company that controls other companies by owning an influential amount of voting stock or control in a group or fleet of insurers.
Pension Benefits	A series of payments to be provided in accordance with the plan of benefits.
Pension Plan	A plan established and maintained by an employer, group of employers, union or any combination, primarily to provide for the payment of definitely determinable benefits to participants after retirement.
Personal Lines	Types of insurance, such as auto or home insurance, for individuals or families rather than for businesses or organisations.
Policy	The legal document issued by the company to the policyholder, which outlines the conditions and terms of the insurance.
Policyholder	The person in actual possession of an insurance policy.
Political Risk	The risk associated with investing and operating in a country where political changes may have a negative impact on earnings or returns.
Pool	An organisation of insurers or reinsurers through which particular types of risk are underwritten and premiums, losses and expenses are shared in agreed-upon amounts.
Portfolio	All of the insurer's in-force policies and outstanding losses, with respect to described segments of its business.
Prime Rate	The benchmark interest rate that banks charge their customers.
Preference Share	Preference or preferred shares entitle a holder to a first claim on any dividend paid by the company before payment is made on ordinary shares. Such dividends are normally linked to an interest rate and not determined by company profits.
Premium	The price of insurance protection for a specified risk for a specified period of time.
Pro Rata	(1) Distribution of the amount of insurance under one policy among several objects or places covered in proportion to their value or the amounts shown. (2) Distribution of liability among several insurers having policies on a risk, usually in the proportion that the amount of coverage in each policy bears to the total amount of coverage in all policies.
Probability	The likelihood or relative frequency of an event expressed in a number between zero and one. The throw of a die is an example. The probability of throwing five is found by dividing the number of faces that have a five (1) by the total number of faces (6). That is a probability of one-sixth or one divided by six, which is 0.17. See also

Degree of Risk, Law of Large Numbers, and Odds.

Profit Commission

A provision found in some insurance agreements, which provides for profit sharing. A commission that is payable according to a pre-determined formula as an incentive and reward for profitable underwriting.

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Quota Share

The basic form of participating treaty whereby the reinsurer accepts a stated percentage of each and every risk within a defined category of business on a pro rata basis. Participation in each risk is fixed and certain.

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Rating Horizon

The rating outlook period

Rating Outlook

A rating outlook indicates the potential direction of a rated entity's rating over the medium term, typically one to two years. An outlook may be defined as: "Stable" (nothing to suggest that the rating will change), "Positive" (the rating symbol may be raised), "Negative" (the rating symbol may be lowered) or "Evolving" (the rating symbol may be raised or lowered).

Rating Watch

Indicates that a rating is under review for possible change in the short term and the movement may be either positive or negative.

Real Interest Rate

An interest rate adjusted for the effect of inflation by deducting the inflation rate from the nominal interest rate.

Receivables

Any outstanding debts, current or not, due to be paid to a company in cash.

Reinstatement

The resumption of coverage under a policy, which has lapsed.

Reinstatement Clause

When the amount of reinsurance coverage provided under a treaty is reduced by the payment of a reinsurance loss as a result of one catastrophe, the reinsurance cover is automatically reinstated usually by the payment of a reinstatement premium.

Reinsurance

The practice whereby one party, called the Reinsurer, in consideration of a premium paid to him agrees to indemnify another party, called the Reinsured, for part or all of the liability assumed by the latter party under a policy or policies of insurance, which it has issued. The reinsured may be referred to as the Original or Primary Insurer, or Direct Writing Company, or the Ceding Company.

Renewal	The re-establishment of the in-force status of a policy, the term of which has expired or will expire unless it is renewed.
Reserve	(1) An amount representing actual or potential liabilities kept by an insurer to cover debts to policyholders. (2) An amount allocated for a special purpose. Note that a reserve is usually a liability and not an extra fund. On occasion a reserve may be an asset, such as a reserve for taxes not yet due.
Retained Earnings	Earnings not paid out as dividends by a company. Retained earnings are typically reinvested back into the business and are an important component of shareholders' equity.
Retention	The net amount of risk the ceding company keeps for its own account.
Retention Rate	The net amount of risk the ceding company keeps for its own account as a percentage of GWP.
Retrocession	The transaction whereby a reinsurer cedes to another reinsurer all or part of the reinsurance it has previously assumed.
Return on Assets (ROA)	A ratio of the attributable profits for the last 12 months to total assets (fixed and current) for the same period, expressed as a percentage. It measures how effectively a company generates earnings from its assets.
Return on Equity (ROE)	ROE is the ratio of a company's profit to its shareholders' equity, expressed as a percentage. It is the most widely used measure of how well management uses shareholders' funds. Its main advantage is that it is a benchmark that allows investors to compare the profitability of companies in different industries.
Revaluation	Formal upward or downward adjustment to assets such as property or plant and equipment.
Rights Issue	One of the ways that a company can raise additional funds is to issue new shares. These must be first offered to current shareholders and a rights issue allows a shareholder to buy shares in proportion to the number already held.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Risk Rating	The statistical process by which insurers determine risks and pricing for the basic classes of insurance.
Risk Management	Process of identifying and monitoring business risks in a manner that offers a risk/return relationship that is acceptable to an entity's operating philosophy.
Risk Management Process	The systematic application of management policies, procedures and practices to the tasks of risk identification, assessment and measurement, response and action, monitoring and review, and risk reporting.

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Securities	Various instruments used in the capital market to raise funds.
Shareholder	An individual, entity or financial institution that holds shares or stock in an organisation or company.
Shareholders' Funds	Shareholders' funds (or equity) are the holding or stake that shareholders have in a company. Equity capital is raised by the issue of new shares or by retaining profit.
Short Term	Current; ordinarily less than one year.
Short Term Rating	A short term rating is an opinion of an issuer's ability to meet all financial obligations over the upcoming 12 month period, including interest payments and debt redemptions.
Soft Market	When the availability of some or all classes of insurance or reinsurances is high relative to demand for such insurance or reinsurance. Competition amongst insurers and reinsurers leads to downward pressure on premiums and to the availability of more extensive coverage terms. Opposite of hard market.
Solvency	With regard to insurers, having sufficient assets (capital, surplus, reserves) and being able to satisfy financial requirements (investments, annual reports, examinations) to be eligible to transact insurance business and meet liabilities.
Statutory	Required by or having to do with law or statute.
Statutory Solvency Margin	Gives an indication as to whether the minimum regulatory solvency margin is being met, based on the net statutory assets to statutory net premiums ratio.
Statutory Reserve	A reserve, either specific or general, required by law.
Stock Exchange	A market with a trading-floor or a screen-based system where members buy and sell securities.
Stop Loss	Any provision in a policy designed to cut off an insurer's losses at a given point. In effect, a stop loss agreement guarantees the loss ratio of the insurer.
Subordinated Debt	Debt that in the event of a default is repaid only after senior obligations have been repaid. It is higher risk than senior debt.
Sum Insured	The maximum amount that an insurer will pay under a contract of insurance.
Surplus Treaty	A type of reinsurance under which bands of cover known as lines are granted above a given retention which is referred to as the cedant's line. Each line is of equivalent size and the capacity of the treaty is expressed as a multiple of the cedant's line. The reinsurer receives an equivalent proportion of the full risk premium. A surplus treaty is a form of proportional reinsurance.
Surrender	The termination of a life insurance policy while the life assured is still

alive in return for a cash sum.

Systemic Risk

The risk inherent to the entire market or an entire market segment.

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Technical Expense Ratio	Measures the percentage of net earned premium used to cover claims and expenses incurred.
Technical Liabilities/Reserves	The sum of Net UPR and Net OCR & IBNR.
Technical Margin	Measures the percentage of net earned premiums remaining after accounting for claims and expenses incurred.
Technical Reserve Cash Coverage	Indicates the number of times that cash and equivalents would be able to meet total net technical reserves.
Technical Result	Net premiums earned less net claims incurred and net commission expenses.
Tier 1/Tier I (Primary) Capital	Primary capital consists of issued ordinary share capital, hybrid debt capital, perpetual preference share capital, retained earnings and reserves. This amount is then reduced by the portion of capital that is allocated to trading activities and other regulatory deductions.
Tier 2/Tier II (Secondary) Capital	Secondary capital is mainly made up of subordinate debt, portfolio impairment and 50% of any revaluation reserves and other specified regulatory deductions.
Total Capital	The sum of owner's equity and admissible supplementary capital.
Total Expenses	The sum of operating expenses and net commission expenses.
Total Expense Ratio	Measures the ability of the insurer to manage expenses associated with core operating activities.
Tranche	A portion of a total, especially of a block of assets such as cash or securities.
Treasury Bill	Short-term obligation backed by the government that bears no interest and is sold at a discount.

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U

Undercapitalised	Term used when a business is not supplied with enough funds by its owners to support its activities and provide for any needed expansion.
Under Review	Failure to carry out a full review of a rated entity within the designated timeframe, either through lack of information or delays in finalisation, i.e. review is ongoing.
Underwriting	The process of selecting risks and classifying them according to their degrees of insurability so that the appropriate rates may be assigned. The process also includes rejection of those risks that do not qualify.
Underwriting Margin	Measures efficiency of underwriting and expense management processes.
Underwriting Result	The profit or loss that an insurer derives from providing insurance or reinsurance coverage, exclusive of investment income and other income.
Unearned Premium Reserve (UPR)	The amount shown in the insurance company's balance sheet which represents the approximate total of the premiums which have not yet been earned as of a specific point in time. Also known as insurance funds.
Upgrade	The assignment of a higher credit rating to an insurer by a credit rating agency. Opposite of downgrade.
Unrealised Gain/Loss	The profit or loss that would be made if a position were to be liquidated.

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Waiver	The act of giving up or surrendering a right or privilege that is known to exist.
Working Capital	Working capital usually refers to the resources that a company uses to finance day-to-day operations. Changes in working capital are assessed to explain movements in debt and cash balances.
Working Layer	The first layer above the cedant's retention wherein moderate to heavy loss activity is expected by the cedant and reinsurer. Working layer reinsurance agreements often include adjustable features to reflect actual underwriting results.
Write-down	The partial reduction in the value of an asset.
Write-off	The total reduction in the value of an asset.

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Yield

Percentage return on an investment or security, usually calculated at an annual rate.

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Ratios

Term	Measure	Calculation	Explanation
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Solvency/Liquidity

International Solvency Margin	(%)	$\frac{\text{Shareholders Interest}}{\text{Net Written Premiums (NWP)}} \times 100$	Measures the ability to cover current year's written premiums using shareholders' funds.
Statutory Solvency Margin	(%)	$\frac{\text{Statutory Net Assets}}{\text{Statutory NWP}} \times 100$	Indicates whether the minimum regulatory solvency margin is being met, based on the net statutory assets to statutory net premiums ratio.
Claims Cash Coverage	months	$\left(\frac{\text{Cash and Cash Equivalents}}{ \text{Claims Incurred} } \right) \times 12$	Indicates the number of months that an insurer would be able to pay out claims incurred using current cash and equivalent balances.
Technical Reserve Cash Coverage	x	$\left(\frac{\text{Cash and Cash Equivalents}}{ \text{Net OCR} + \text{Net UPR} } \right)$	Indicates the number of times that cash and equivalents would be able to meet total net technical reserves.
Average Premium Debtors Days	days	$\left[\frac{\left(\frac{\text{Premiums Receivable}_t + \text{Premiums Receivable}_{t-1}}{2} \right)}{\frac{\text{Gross Written Premiums}}{365}} \right]$	Measures the number of days it takes on average to collect outstanding premiums, relative to the gross premiums written for the period.

Efficiency/ Growth

Gross Written Premium Growth	(%)	$\left(\frac{\text{Gross Written Premiums}_t}{\text{Gross Written Premiums}_{t-1}} - 1 \right) \times 100$	Measures the increase in gross premiums between times t-1 and t as a percentage of the t-1 gross premiums.
Retention Rate	(%)	$\frac{\text{Net Written Premiums}}{\text{Gross Written Premiums}} \times 100$	Measures the net amount of risk the ceding company keeps for its own account as a percentage of the GWP.
Earned Loss Ratio	(%)	$\frac{ \text{Claims Incurred} }{\text{Net Premiums Earned}} \times 100$	Measures the proportion of claims incurred to net premiums earned.

Net Commissions Expense Ratio	(%)	$\frac{ Commission\ expenses }{Net\ Premiums\ Earned} \times 100$	Measures the proportion of commission expenses to net premiums
Operating Expenses Ratio	(%)	$\frac{ Operating\ expenses }{Net\ Premiums\ Earned} \times 100$	Measures the proportion of operating expenses to net premiums earned.
Total Expense Ratio	(%)	$Operating\ Expense\ Ratio + Commission\ Expense\ Ratio$	Measures the ability of the insurer to manage expenses associated with core operating activities.
Underwriting Margin	(%)	$\frac{Underwriting\ result}{Net\ Premiums\ Earned} \times 100$	Measures efficiency of underwriting and expense management processes.
Combined Ratio	(%)	$Earned\ Loss\ Ratio + Operating\ Expense\ Ratio + Commissions\ Expense\ Ratio = 100 - Underwriting\ Margin$	Measures the ability to conserve profits through the expense line.
Operating Margin	(%)	$\left(\frac{Investment\ Income}{Net\ Premiums\ Earned} \times 100 + Underwriting\ Margin \right)$	Measures efficiency of profit generation from investments and underwriting.

Profitability

Investment Yield (excluding unrealised gains/losses)	(%)	$\left[\frac{Investment\ Income}{\left(\frac{(Cash_t + Investments_t) + (Cash_{t-1} + Investments_{t-1})}{2} \right)} \right]$	Measures the investment return achieved relative to funds invested in financial instruments, excluding unrealized gains/losses.
Investment Yield (including unrealised gains/losses)	(%)	$\left[\frac{Investment\ Income \pm Unrealised\ Movements}{\left(\frac{(Cash_t + Investments_t) + (Cash_{t-1} + Investments_{t-1})}{2} \right)} \right]$	Measures the investment return achieved relative to funds invested in financial instruments, including unrealized gains/losses.
Technical Expense Ratio	(%)	$\frac{Net\ Claims\ Incurred + Net\ Commission\ Expense}{Net\ premiums\ earned} \times 100$	Measures the percentage of net earned premium used to cover claims and expenses incurred.
Technical Margin	(%)	$100 - (Earned\ loss\ ratio + Net\ commission\ expense\ ratio)$	Measures the percentage of net earned premiums remaining after accounting for

claims and expenses incurred.

ROE (excluding unrealised gains/losses)	(%)	$\frac{\text{Net Profit After Tax}}{\text{Shareholders Interest}} \times 100$	Measures the realised return after tax on shareholder's investment.
ROE (including unrealised gains/losses)	(%)	$\left[\frac{\text{Net Profit After Tax} \pm \text{Unrealised movements}}{\text{Shareholders Interest}} \right] \times 100$	Measures the return after tax, including unrealised gains, on shareholder's investment.

Reserving

Net UPR/NWP	(%)	$\frac{\text{Net Unearned Premium Reserves}}{\text{Net Written Premiums (NWP)}} \times 100$	Measures the proportion of unearned premiums to net written premiums.
Net OCR/NWP	(%)	$\frac{\text{Net OCR}}{\text{Net Written Premiums (NWP)}} \times 100$	Measures the proportion of outstanding claims reserve to net written premiums.

Operating

Effective Tax Rate	(%)	$\frac{\text{Taxation}}{\text{Underwriting result} + \text{Investment Income} + \text{Other Income}} \times 100$	Measures the average rate at which earned income is taxed.
Dividend Cover	x	$\frac{\text{Net Profit After Tax}}{\text{Dividends for the year}}$	The extent to which a company's dividend is matched or exceeded by the earnings available for distribution to shareholders.

Financial leverage

Debt/Equity Ratio	(%)	$\frac{Debt}{Total\ Capital} \times 100$	Measures the proportion of debt and equity used to finance assets.
Debt Service Coverage	(x)	$\frac{EBIT}{Debt\ Interest\ Expense}$	Measures the ratio of cash available for debt servicing to interest, principal and lease payments.

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