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INTERNATIONAL RATING AGENCIES APPROACHES TO THE EVALUATION OF INSURANCE COMPANIES

Abstract: Growing need for an independent evaluation of the performance results of insurance companies is due to the need to meet the needs of stakeholders to reliable information about the evaluation results of insurers. It makes sense to study the approaches of international rating agencies to assess insurance companies. In the article the list of users (investors and management of insurance companies, insurance consumers and reinsurers) and purposes of rating insurance companies by international rating agencies, depending on the users of its results were determined. The article presents a description of methods of international rating agencies: A. M. Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings, which are used by insurance companies in Ukraine to determine the requirements for non-resident reinsurers. Analyzed methods of the international rating agencies: A. M Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings on the main directions of evaluation scales and criteria of international rating agencies of long-term financial reliability (stability) of insurers provided to determine the most informative method for users is methods of international rating agency Standard & Poor's.

Keywords: international rating agencies, users of evaluation results, objectives of rating, long-term financial reliability (stability), insurance company, directions of evaluation, scale of evaluation.

JEL Classification: G20, G22.

Formulas: 0; fig.: 0, tabl.: 4, bibl.: 10

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ПІДХОДИ МІЖНАРОДНИХ РЕЙТИНГОВИХ АГЕНТСТВ ДО ОЦІНКИ СТРАХОВИХ КОМПАНІЙ

Анотація. У статті обґрунтовано перелік користувачів та цілі рейтингової оцінки страхових компаній міжнародними рейтинговими агентствами, залежно від користувачів її результатів. Наведено характеристику методик міжнародних рейтингових агентств: А. М.

Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings, які використовуються страховими компаніями України для визначення виконання вимог до перестраховиків–нерезидентів. Проведений аналіз методик міжнародних рейтингових агентств: А. М. Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings за основними напрямки оцінки, шкалами та критеріями міжнародних рейтингових агентств довгострокової фінансової надійності (стійкості) страхових компаній надав змогу визначити, що найбільш інформативною методикою для користувачів є методика міжнародного рейтингового агентства Standard & Poor's.

Ключові слова: міжнародні рейтингові агентства, користувачі результатів рейтингової оцінки, цілі рейтингової оцінки, довгострокова фінансова надійність (стійкість), страхова компанія, напрямки оцінки, шкала оцінювання.

Формул.: 0; рис.: 0; табл.: 4; бібл.: 10;

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ПОДХОДЫ МЕЖДУНАРОДНЫХ РЕЙТИНГОВЫХ АГЕНТСТВО К ОЦЕНКЕ СТРАХОВЫХ КОМПАНИЙ

Аннотация. В статье обосновано перечень пользователей и цели рейтинговой оценки страховых компаний международными рейтинговыми агентствами, в зависимости от пользователей ее результатов. Приведено характеристику методик международных рейтинговых агентств: А. М. Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings, которые используются страховыми компаниями Украины для определения выполнения требований к перестраховщикам–нерезидентам. Проведенный анализ методик международных рейтинговых агентств: А. М. Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings по основным направлениям оценки, шкалами и критериям международных рейтинговых агентств долгосрочной финансовой надежности (устойчивости) страховых компаний предоставил возможность определить, что наиболее информативной методикой для пользователей является методика международного рейтингового агентства Standard & Poor's.

Ключевые слова: международные рейтинговые агентства, пользователи результатов рейтинговой оценки, цели рейтинговой оценки, долгосрочная финансовая надежность (устойчивость), страховая компания, направления оценки, шкала оценивания.

Формул.: 0; рис.: 0; табл.: 4; библи.: 10;

Introduction. Growing need for an independent evaluation of the performance results of insurance companies is due to the need to meet the needs of stakeholders to reliable information about the evaluation results of insurers, because only on the basis of such information it's possible to make the right and better decisions. One of the key factors influencing the needs of stakeholders are: transparency and information openness of insurers and results of evaluation of performance (for international and domestic methods of rating agencies). Relevance of the research approaches of international rating agencies to assess insurance companies is reflected in the need to protect insurance consumers, increase the investment attractiveness of insurance companies and the development of insurance market.

To meet the needs of users of rating is a question of selecting the most informative methods of international rating agencies.

The analysis of research and problem definition. Study of theoretical and methodological foundations of assessment proceedings of insurance companies by international rating agencies dedicated works by such scholars as: O. Zaletov [1], N. Opushko [2], O. Svitlichna [3], N. Tkachenko [4] and others. Not sufficiently developed issue of determining the most informative international methods of rating insurance companies for users of evaluation results. Therefore, the aim of the study is to analysis of international rating agencies approaches to evaluation of insurance companies.

The results of the research. Features of rating financial institutions given in The concept of the rating system of regions, sectors of national economy, entities which was approved by the Cabinet of Ministers of Ukraine of 01.04.2004 № 208–p. The document only mentions that during the rating of the financial institution analyzes the performance of its financial ratios and indicators set by law, the effectiveness of financial management and risk management, as well as programs of strategic development, investment policy [5]. In order to obtain objective rating estimates to the performance results of insurance companies is the need to obtain it estimates by international rating agencies.

Rating (ie assigning rating) of insurance companies is the process of independent evaluation, carried out by certain rules and techniques (international and domestic rating agencies). The characteristic of purposes of rating insurance companies by international rating agencies, depending on the users of its results are shown in Table 1.

Table 1

The characteristic of purposes of insurance companies rating by international rating agencies based on the results of its users

Users of evaluation results	Purposes of insurance companies rating
Investors of the insurance company	Decision making on the evaluation of the risk of losing the funds invested in the company
Management of the insurance company	Decision making on effective management of insurance company
Consumers of insurance services	Decision making on: selection of insurance company; early termination of the contract
Reinsurers	Decision making on the choice of reinsurer based on monitoring level (rating) financial reliability a non–resident reinsurer

Source: author's development

As shown in the Table 1, there are differences in the purposes of rating insurance companies by international rating agencies, depending on the users of its results. For investors receiving the rating is the basis for making decisions about whether investment as the expected performance of, the growth prospects of the insurance company is also largely due to its rating. For the management of insurance company the rating indicates financial soundness, ability to perform current and future obligations under the insurance contract, the outlook for the insurer. For the consumers of insurance services the rating indicates quality and reliability of insurance protection.

For reinsurers the rating is part of organizational guarantee of using reinsurance services as there are regulatory requirements for reinsurance, one of which is to monitor the level (rating) of reinsurer's financial reliability of a non–resident by international rating agencies ratings. All international rating agencies assess the company's ability to fulfill the obligations but differ in the assessment methodology, in particular they take into account: the financial condition of insurance companies, money management and financial reserves and others, the features of insurance performance or payments history.

To analyze methods of international rating agencies and determine which methods are most informative for users of assessment highlighted techniques used by insurance companies in Ukraine to determine the requirements for reinsurers, including non–residents. These techniques include: A. M. Best

(USA); Moody's Investors Service (USA); Standard & Poor's (USA); Fitch Ratings (UK). Each of the aforementioned agencies use to assess financial reliability (stability) of insurers closed its methodology, based on analysis of various aspects of the company and the company assigns certain rating (index) using the usual combination of numbers, uppercase and lowercase letters.

A Best's financial strength rating is an independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations. An FSR not assigned insurance policies or contracts and does not address any other risk, including, but not limited to, an insurers claims–payment policies or procedures; the ability of the insurer to dispute or deny claims payment on grounds of misrepresentation or fraud; or any specific liability contractually borne by the policy or contract holder [6].

Methods by Fitch Ratings with rating of insurance companies is designed to give an idea about the key rating factors that Fitch considers in companies rating of this sector, as well as their debt and obligations to policyholders. The global basic methods has general principles that belong to all ratings of insurance companies, assigned by Fitch, and is complemented by techniques on specific sectors. Within the analysis of insurance companies Fitch relies on the following main factors: industry–specific and business environment; and specificity of risk management; financial performance; strategy management and corporate governance; factors of property, and support groups. Generally, when one factor is significantly weaker than the other, a weaker element has a greater weight in the analysis [7].

Making decision on assigning the rating Moody's considers all relevant risk factors and takes into account all points of view, guided by a focus on the long term (the analysis focuses on the key factors that affect the ability to repay its debt in the long run) [8].

Standard & Poor's applies a methodology based on the processing a lot of different quantitative and qualitative data. By its nature, the process of assigning the rating largely objective, especially as regards the quantitative factors, but subjective evaluation is also present. That subjective approach enables Standard & Poor's to include in the final rating the entire set of factors and make a statistic ranking in a sense so that «looking ahead» [9].

The requirements of the international rating agencies have certain characteristics. The total comparative analysis of techniques, including A. M. Best, Moody's Investors Service, Standard & Poor's , Fitch Ratings given in Table 2.

Table 2

The requirements of international rating agencies

Methods of international rating agencies	Requirements
A. M. Best	Assessment of quality indicators such as the relationship with the parent (subsidiary) companies, dependent on participants in the financial–industrial groups, which include the insurer's membership in pools, associations, and the availability of reinsurance protection. More detailed company shares depending on the size of their assets.
Moody's Investors Service	Evaluation of indicators: quality of management, market position, the degree of business diversification, the degree of financial flexibility, transparency, regulation and the ability of the issuer to meet its financial obligations in the normal course of the country for the business cycle.
Standard & Poor's	Evaluation of indicators: industry risk; analysis of business potential; strategy development and management company; effectiveness of current activities; quality investment portfolio; capital adequacy; liquidity; flexible financing activities.
Fitch Ratings	Evaluation of indicators: sectoral risks, potential risks, opportunities in the operating environment, market position and performance of the quality management and ownership structure.

Source: author's developed on basis of [6; 7; 8; 9]

As shown in the Table 2, in most methods there are presented quality of the performance evaluation. Based on the comparative methods analysis of international rating agencies A. M. Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings shows the distribution of rating methods according to the areas being evaluated (Table 3).

Table 3

The distribution of rating methodologies according to the directions being evaluated

Directions of evaluation	Methods of international rating agencies			
	A. M. Best	Moody's Investors Service	Standard & Poor's	Fitch Ratings
Industry risks	+	–	+	+
Market position	+	+	+	+
The legal structure	–	–	–	–
Management quality and strategy	+	+	+	+
Reputation, development and stability of the customer base	–	+	–	–
Operational risks and activities	–	–	–	+
Analysis of the company's business potential	–	–	–	–
The effectiveness of current activities	+	–	+	–
Investment quality	–	–	+	–
Capital adequacy	–	–	+	–
Adequacy of insurance reserves	–	–	+	–
Liquidity	–	–	+	–
Elasticity of financial activities	–	+	+	–
Total number of estimates directions used in the methodology	4	4	9	4

Source: author's developed on basis of [6; 7; 8; 9]

As shown in the Table 3, the largest indicators structure, based on publicly available information, it is method of rating agency Standard & Poor's, because it allows for the greatest number of areas of evaluation.

However, an important factor is the use of methods of rating the quality of interpreting evaluation results. Given that the rating methodology based on a comprehensive qualitative and quantitative analysis of insurance company ratings can be long-term and short-term. For the purpose of selecting appropriate reinsurer is mentioned criteria and scales of international rating agencies is long-term rating (Table 4).

Data of Table 4 indicate that the rating is the most reliable source of information on the stability (reliability) of the insurance company. For techniques it's characterized rating outlook, which shows the possible direction of the rating over the next two to three years, "positive" – rating may rise, "negative" – the rating can go down, "stable" – change is unlikely that "evolving" – may increase or downgrade.

Long-term rating Standard & Poor's evaluates the issuer's ability to timely fulfill its debt obligations. Long-term ratings are aligned to the highest category – "AAA" to the lowest – "D". Ratings range from "AA" to "CCC" may be supplemented by the sign "plus" (+) or "minus" (–), which means the intermediate rating categories relative to the main categories. A. M. Best rating scale evaluation is from A ++ to F. In the case of the National rating scale [10], in contrast to assessments of international rating agencies use with the following additional notation: "ua" – ratings obtained according to the National rating scale; "–" or "+" – intermediate category rating regarding major categories; (pi) – ratings are based on using only public information; "withdrawn" – rating withdrawn due to the fact that not provided the necessary information to update the rating or other reasons; "suspended" – rating, which can be withdrawn.

Table 4

Scales and criteria of international rating agencies of long-term financial reliability (stability) of insurers

Methods of international rating agencies				Rating value
A.M. Best	Moody's Investors Service	Standard & Poor's	Fitch Ratings	
A++, A+	Aaa	AAA	AAA	Highest reliability
A, A –	Aa	AA	AA	High reliability
B++, B+	A	A	A	Reliability is higher than average
B, B –	Baa	BBB	BBB	Reliability is below average
C++, C+	Ba	BB	BB	Marginal reliability
C, C –	B	B	B	Weak reliability
D	Caa	CCC	CCC	Reliability is very low
E (Under control)	Ca	CC	CC	The potential of default
F (Under liquidation)	C	R	C	Close to default
S (Rating suspended)	–	SD	–	Selective default
–	–	D	–	In a state of default

Source: author's developed on basis of [6; 7; 8; 9]

Conclusions. Grounded list of rating users including: management, investors and insurance companies, consumers of insurance services and reinsurers. The purposes of rating insurance companies by international rating agencies, depending on the users of its results. The article presents a description of methods of international rating agencies: A. M. Best, Moody's Investors Service, Standard & Poor's, Fitch Ratings, which are used by insurance companies in Ukraine to determine the requirements for non-resident reinsurers. Proved that the most informative method of international rating agency estimates for its users is Standard & Poor's.

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Стаття надійшла до редакції 03.04.2017

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Received 03.04.2017

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