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R.V.I. Guaranty Co., Ltd.

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R.V.I. Guaranty Co., Ltd.

SACP* Assessments				SACP*		Support		Ratings
Anchor	bbb+	Modifiers	0	bbb+		0		Financial Strength Rating
Business Risk	Satisfactory	ERM and Management	0	Liquidity	0	Group Support	0	BBB+/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.

Major Rating Factors

Strengths	Weaknesses
• Leading player in the residual-value insurance market • Extremely strong capital adequacy • Strong balance sheet highlighted by limited financial leverage and exceptional liquidity	• Monoline nature of business creating potential volatility for earnings during times of stress • Client concentration risk

Rationale

S&P Global Ratings' ratings on Bermuda-based R.V.I. Guaranty Co., Ltd. and its U.S.-based subsidiary R.V.I. America Insurance Co. (collectively, RVI) reflect the group's satisfactory business risk profile and moderately strong financial risk profile (FRP). RVI enjoys strong brand recognition and benefits from a management team with many years of experience in the segment, with core members remaining stable for a number of years. We view RVI's capital and earnings profile as strong but offset by the absolute size of its capital. We also believe RVI is susceptible to adverse macroeconomic conditions. We view its liquidity as exceptional, consider its enterprise risk management (ERM) framework adequate with strong risk controls, and assess its management and governance as fair.

Outlook: Stable

We expect RVI to maintain its competitive position in the residual-value insurance market and continue to explore opportunities to grow its franchise. We also expect its FRP to remain moderately strong with the support of extremely strong capital adequacy.

Downside scenario

We may lower our ratings if RVI cannot sustain its already constrained competitive position, or if it significantly changes its capital-management strategy.

Upside scenario

We may raise the ratings in the next two years if the group's sources of premiums become more diverse, the absolute amount of premiums written rises meaningfully, and we view the level of premiums as sustainable.

Macroeconomic Assumptions

- Real U.S. GDP growth of about 3.0% in 2018 and 2.5% in 2019
- 10-year Treasury rate of about 3.2% in 2018 and 3.4% in 2019
- Core Consumer Price Index at 2.4% in 2018 and 2.1% in 2019
- Unemployment rate at 3.8% in 2018 and 3.6% in 2019

Key Metrics

	--Year ended Dec. 31--				
(Mil. $)	**2019***	**2018***	**2017**	**2016**	**2015**
Net premiums earned	34-37	33-36	34.1	37.2	33.5
Net income	13-14	12-14	(1.8)	11.0	13.0
Property/casualty net combined ratio (%)	<80	<80	108.1	71.1	61.9
S&P Global Ratings' capital adequacy/redundancy	AAA	AAA	AAA	AAA	AAA

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

Business Risk Profile: Satisfactory

RVI has a favorable brand name and extensive experience in the residual-value and leasing market, as seen in its strong and sustained operating performance. This is somewhat offset by its narrow business focus and concentration of premiums from its top five clients. Nevertheless, as the U.S economy continues to grow, combined with the company's efforts to expand in China, RVI may have more opportunities to grow and diversify its sources of premiums. Currently, as a source of revenue diversification, RVI offers consulting services in asset valuation to assist clients in managing their portfolios. This is a fee-based nonrisk assuming business, but it's unlikely to become a material part of revenue any time soon. Its five-year (2017-2013) average combined ratio was near 74% and return on revenue (ROR) was a robust 38%. We expect a combined ratio of 65%-75% and ROR of about 40%-50% for the next two years.

Financial Risk Profile: Moderately Strong

RVI's capital is redundant at the extremely strong level, and we expect it to remain so through 2019 in our base-case scenario. Our scenario assumes sizable dividends, which limits growth in capital. The absolute size of its total adjusted capital at less than $250 million limits the capital and earnings score. RVI has good operating performance, as measured by a combined ratio for the past five years. But there have been significant fluctuations in the combined ratio due to large claims relative to the company's earnings power, highlighting the vulnerability of its capital position. RVI's earnings are also susceptible to changes in economic conditions.

We view RVI's investment portfolio as conservative because it predominately consists of fixed-income instruments with an average credit quality of 'AA-'. The portfolio is well diversified in terms of sector and securities, and it does not create significant risk to the FRP.

Because we view residual-value insurance as a unique and specialized niche market, we believe RVI's access to capital markets is limited, so we view its financial flexibility as less than adequate. In 2018, the company established a revolving credit facility to meet working capital needs.

Other Assessments

We regard RVI's ERM as adequate with strong risk controls. This is supported by our positive view of its risk controls and neutral view of its risk-management culture, emerging risk management, risk models, and strategic risk management. A conservative approach to underwriting, investments, and risk culture has resulted in minimal losses for RVI. The chief risk officer updates the board on risk limits and the watch list quarterly and enforces underwriting guidelines and audits. The risk management group identifies emerging risks and mitigation strategies as part of its quarterly business review.

In our view, RVI's management and governance is fair. The team is highly experienced in the residual-value and leasing industries. In anticipation of the CEO stepping down from his day-to-day role (he will remain a board member and consultant), RVI has put in place a co-COO (the chief risk officer and the general counsel) structure to oversee operations.

RVI's strong liquidity reflects its adequate cash flow and high-quality liquid investment portfolio. There are no near-term liquidity concerns, and RVI has proven its ability to meet its claim payments from internal sources of cash.

Other Considerations

Accounting considerations

In our analysis, we have reviewed RVI's financial statements based on U.S. generally accepted accounting principles (GAAP) and on an insurance basis that eliminates the fair-value adjustment on many of the insurance contracts, which are accounted for as derivatives under U.S. GAAP. Under GAAP, RVI's contracts meet the derivative requirements pursuant to the Financial Accounting Standards Board's Accounting Standards Codification "Derivatives and Hedging" (ASC 815), which requires derivatives to be marked to market at each reporting date.

For residual-value insurance, we believe this accounting standard has introduced earnings volatility with little bearing on the likelihood of a potential claim or an insurer's intrinsic earnings power. Unlike other financial sectors for which ASC 815 might be more relevant, residual-value insurers' contracts are not traded and there is no business intention to trade to realize gains. Therefore, we believe recording a marked-to-market gain or loss due to changing spreads in the marketplace is unnecessary. Because almost all contracts expire without a claim, corresponding marked-to-market positions are usually zeroed out at maturity. We believe the insurer's loss reserves indicate potential claims and are a better representation of the economics of the residual-value policy. We also look to our own capital charge evaluations as good indicators of changes to the risk profile of any of RVI's insured exposures.

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: 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

Ratings Detail (As Of September 26, 2018)	
Operating Companies Covered By This Report	
R.V.I. Guaranty Co. Ltd.	
Financial Strength Rating	
Local Currency	BBB+/Stable/--
Issuer Credit Rating	
Local Currency	BBB+/Stable/--

Ratings Detail (As Of September 26, 2018) (cont.)	
R.V.I. America Insurance Co.	
Financial Strength Rating	
Local Currency	BBB+/Stable/--
Issuer Credit Rating	
Local Currency	BBB+/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.