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XL Group

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Major Rating Factors

Strengths:

- Strong competitive position with a strong global market presence
- Strong property and casualty re/insurance operating performance
- Strong enterprise risk management
- Strong risk-adjusted capitalization

Weaknesses:

- Investments susceptible to mark-to-market volatility and realized losses relative to peers, attributed to sizable allocation in non-agency structured products
- Potential for losses from runoff businesses

Holding Company: XLIT Ltd.
Counterparty Credit Rating
Local Currency
BBB+/Stable/--
Operating Companies Covered By This Report
Financial Strength Rating
Local Currency
A/Stable/--

Rationale

Standard & Poor's Ratings Services' ratings on XLIT Ltd. (formally known as XL Group Ltd.) and its operating subsidiaries (collectively referred to as XL) are based on the group's strong competitive position with a strong global market presence, strong property and casualty re/insurance operating performance, strong enterprise risk management (ERM), and strong risk-adjusted capitalization. Partially offsetting these strengths are the group's investments susceptible to mark-to-market volatility and realized losses relative to peers, attributed to sizable allocation in non-agency structured products, and potential for losses from runoff businesses.

XL is strongly positioned in the U.S., European, and Bermudian P/C re/insurance markets, as demonstrated by its $6.3 billion in non-life gross premiums written (GPW) in 2010. The operations are well diversified geographically, by segment, and by line of business. The group's strong global market presence in the P/C re/insurance segments is a function of both its underwriting expertise in specialized industry segments and its global scale, which makes the group better than its less-diversified competitors at reaching and serving an array of global clients.

In the first nine months of 2011, XL's consolidated P/C GPW grew 14% to $5.6 billion. The insurance segment's premiums grew 14%, mainly because of general property and energy, excess casualty and programs, newly formed construction business, select new business initiatives, and favorable foreign exchange rates movement. The reinsurance segment's premiums also rose 13%, primarily from U.K. motor treaties, marine, recaptured business, and North American property catastrophe.

XL's underwriting performance from its core P/C re/insurance segments has been strong with an average combined ratio of 92.3% over the past five years (2006-2010). Similarly, the company's return on revenue (ROR) excluding realized capital losses and extraordinary charges from runoff operations averaged a strong 22.3% over the same timeframe. Despite XL's strong operating performance derived from its core operations, special charges and catastrophe losses have historically detracted materially from overall earnings.

In the first nine months of 2011, XL reported $438 million EBITDA adjusted compared with $904 million in the prior-year period. Similar to its peers, XL's operating performance deteriorated in the first nine months of 2011 because of catastrophe losses (Australia, New Zealand, Japan, and U.S.), with a combined ratio of 107.2% compared with 95.9% in the prior-year period. As of Sept. 30, 2011, the combined ratio included 19.7 percentage points of catastrophe losses, somewhat offset by 5.5 percentage points of favorable prior-year loss reserve development.

Since the financial crisis, XL has capitalized on the momentum for enhancing its ERM framework, which we view as strong. The group has cultivated a strong risk culture throughout the organization and has demonstrated improvements in capital modeling, strategic risk management, and controls. Given the complexity of the group and the earnings volatility inherent in the nature of its business, ERM is important to the rating on XL, and we expect the firm to maintain this momentum.

XL's risk adjusted capitalization is strong. Our evaluation is based on the balance between XL's quantitatively measured capital level, which was extremely strong as of Sept. 30, 2011, and the volatility of carrying a significant majority of fixed-maturity assets at fair value. We expect capitalization to remain strong and redundant through 2012.

We believe that XL remains more susceptible than many of its peers to mark-to-market volatility and to realized and unrealized losses. Its $3.8 billion exposure to non-agency structured products as of Sept. 30, 2011, though markedly reduced from a peak of $13.6 billion as of June 30, 2007, is sizable and, we think, could continue to generate realized losses. XL booked $138 million in realized investment losses for the nine months ended Sept. 30, 2011.

XL's discontinued businesses, which include life reinsurance (with $5 billion of future policy benefit reserves), financial lines, and certain segments of the P/C businesses, could generate adverse charges. However, such charges will be significantly lower than in prior years; charges exceeded $1.4 billion in 2008 and $1.0 billion in 2007, primarily in connection with the financial guarantee business. As of Sept. 30, 2011, XL's credit derivative exposures outside of the group's investment portfolio consisted of two contracts with an aggregate exposure of $159 million, for which XL recorded a $ 26 million liability. In January 2011, XL commuted 32 of the 37 of the financial guarantee transactions that were outstanding as of year-end 2010. As a result, the discontinued financial guarantee segment had five financial guarantee contracts outstanding as of Sept. 30, 2011, with $130 million in total insured contractual payments outstanding, with a $1.4 million liability. Finally, less than 5% of XL's net outstanding P/C reserves remain on discontinued P/C businesses as of Sept. 30, 2011, primarily in the surety business (discontinued in 2004), underwritten by Winterthur prior to XL's acquisition in 2001, and structured indemnity business from the financial solutions segment (discontinued in 2007). Although it's remote, there remains a chance that charges from these businesses will affect reported income.

The current rating incorporates our expectation that strong net earnings will result from the continuation of strong underwriting performance, further optimization of investments portfolio, and the materially reduced risk profile of the runoff businesses. More importantly, we expect the continued focus and recent enhancement of ERM to a strong level to materially reduce the frequency and severity of unanticipated losses.

Table 1

XL Group PLC/Financial Statistics							
	--Nine months ended Sept. 30--		--Year ended Dec.31--				
	2011	2010	2010	2009	2008	2007	2006
EBITDA Interest coverage* (x)	2.8	5.6	5.7	5.9	5.2	4.2	4.1
EBITDA fixed-charge coverage* (x)	2.8	4.6	4.3	4.4	4.3	3.8	3.8

Table 1

XL Group PLC/Financial Statistics (cont.)							
Debt leverage including pension deficit as debt (%)	16.0	16.3	16.7	17.7	27.0	18.9	20.7
Debt leverage excluding pension deficit as debt (%)	15.8	16.2	16.5	17.5	26.9	18.8	20.6
Financial leverage including pension deficit as debt (%)	22.5	26.5	27.2	29.5	49.8	29.7	30.9
Financial leverage excluding pension deficit as debt (%)	22.4	26.4	27.1	29.4	49.7	29.7	30.8

*Including operating leases

Factors Specific To Holding Company

Standard & Poor's applies standard notching between the core insurance and reinsurance operating companies and their holding company, XLIT Ltd. Similar to its Bermuda-based holdco peers, Cayman Island-based XLIT Ltd. is rated two notches below its operating subsidiaries. The two-notch difference reflects the holding company's dependence on dividends from its operating subsidiaries, which are less exposed to regulatory restrictions because of their geographic presence across different countries and jurisdictions. Accordingly, dividends from the operating company may be sourced from multiple jurisdictions.

XL's total financial leverage was 23% as of Sept. 30, 2011, which we consider moderate and is within our expectations. In September 2011, XL issued $400 million in 5.75% senior notes due in 2021. In October 2011, XL issued $350 million in Series D preferred shares as part of the Stoneheath Re contingent capital facility. The combined proceeds from these issuances will be used to fund the repayment of the $600 million guaranteed senior notes due in 2012 with the remaining proceeds to be used for general corporate purposes. Other upcoming debt obligations are $600 million due in 2014, $400 million due in 2021, $350 million in 2024, and $325 million due in 2027.

Unlike its peers, XL's fixed charge coverage remained positive in 2011. Because of the industry above-average catastrophe losses in the first nine months of 2011, fixed charge coverage deteriorated to 2.8x compared with 4.6x in the prior year period. In 2011, we expect XL's debt plus preferred-to-capital ratio to remain below 25% and fixed-charge coverage to be about 2.5x to 3.0x. In 2012, the financial leverage (debt plus hybrid securities) will likely be mid to low 20%. At the current rating level and assuming normalized earnings (i.e., including 5% catastrophe load), we would expect fixed-charged coverage of about 4x.

Outlook

Catastrophe losses so far in 2011 will create a drag on XL's full-year earnings. However, we expect these losses will be an earnings event rather than a capital event and should be contained within XL's 2011 operating results. Assuming normal catastrophe activity for the remainder of the year (i.e., 5% catastrophe load), we estimate that XL will likely report a combined ratio of 103%-105%. Based on our view of the near-term rate and loss cost trends, we expect the combined ratio in the mid 90s, assuming a catastrophe load of 5% in 2012 and a return on revenue (ROR) in the mid-teens.

GPW will likely grow 8% to 10% in 2011 and 6% to 8% in 2012, as a result of management strategic growth initiatives combined with somewhat favorable rate trends across various short-tails classes of business. XL will continue to focus on underwriting profitability over volume as its builds its underwriting expertise and reach as a way to successfully increase its business in the next favorable market cycle.

We could raise the ratings within the next 24 months if XL were to markedly enhance its competitive profile in the form of greater diversification within business segments and improved operating performance that is even more favorably differentiated from the P/C industry as a whole. At the same time, the group would have to further reduce the potential for adverse charges from the investment and runoff business. Conversely, we could lower the rating if the group does not meet our performance expectations, particularly if there were a significant shortfall in underwriting results (absent a significant catastrophe, in which event, we would expect XL's results to be consistent with the industry as a whole). We could also consider a downgrade if unexpected adverse events--such as additional realized investment losses, large underwriting losses, or other material charges--were to occur.

Competitive Position: Strong With Globally Diversified Insurance And Reinsurance Platforms

XL is strongly positioned in the U.S., European, and Bermudan P/C insurance and reinsurance markets, as shown by its $6.3 billion in nonlife GPW in 2010. The group's strong global market presence in the P/C insurance and reinsurance segments is a function of both its underwriting expertise in specialized industry segments and its global scale, which makes the group better than its less-diversified competitors at reaching and serving an array of global clients.

While the insurance operations accounted for 71% of the 2010 non-life GPW, its large multinational insurance accounts have a risk profile more consistent with that of its reinsurance operations. XL's premium production is geographically diverse, illustrated by its non-life net premium written being sourced 43% from the U.S., 11% from Bermuda, and 46% from Europe, including all other regions. XL's strong global market presence in the P/C insurance and reinsurance segments is a function of its underwriting expertise in specialized industries, risk engineering capabilities, ability to provide large coverage limits and its global market presence. XL's diversified competitive position is a significant strength to the rating; because of its strong diversification, XL is likely to have more earnings stability than its less-diversified competitors.

In 2009, XL successfully implemented disciplined underwriting decisions in response to soft market conditions. As such, a significant proportion of the 19% decline in GPW in 2009 was the result of exiting unprofitable programs and the markedly reduced practice of booking multiyear policies. Premium volume was flat in 2010, demonstrating XL's competitive resilience in a soft economy and an environment conducive to declining rates. In anticipation of the next favorable market cycle, XL has been hiring senior-level underwriting talent with the intent of broadening its specialty offerings. Also, XL has obtained a license for its insurance business to operate in China and has received prior approval from the Brazilian insurance and reinsurance regulator to establish an insurance operation in Brazil, which illustrates its intent to expand into developing markets. XL has demonstrated a competitive advantage in this segment based on its underwriting expertise and product design. Recent hires have been in the North America construction, property, surety, programs, inland marine, and excess and surplus lines of business, as well as political risk and international property lines. XL has also been focused on expanding the presence of its solid professional lines to other regions.

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Table 2

XL Group PLC/Business Statistics							
	Nine months ended Sept. 30		--Year ended Dec. 31--				
(Mil. $)	2011	2010	2010	2009	2008	2007	2006
Gross premiums written	5,936.2	5,264.6	6,673.3	6,687.5	8,260.3	8,998.0	9,786.2
Change in gross premiums written (%)	12.8	(2.6)	(0.2)	(19.0)	(8.2)	(8.1)	(17.4)
Net premiums written	4,585.7	4,164.4	5,381.7	5,276.6	6,388.1	7,126.9	7,617.4
Change in net premiums written (%)	10.1	(0.6)	2.0	(17.4)	(10.4)	(6.4)	(19.9)
Reinsurance utilization (%)	22.8	20.9	19.4	21.1	22.7	20.8	22.2
Gross premiums written by segment:							
P&C Insurance (%)	61.8	61.0	66.2	63.6	64.3	60.4	57.5
P&C Reinsurance (%)	33.2	33.2	27.6	27.8	27.4	29.6	31.3
Life Operations (%)	5.0	5.9	6.2	8.6	8.4	8.3	7.0
Other / Discontinued Operations (%)	0.0	0.0	0.0	0.0	0.0	1.7	4.1
Total (%)	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Historical

XL built its formidable P/C market presence through organic growth and a series of acquisitions that was capped with the Winterthur acquisition in 2001. However, the group was less successful in efforts to diversify its core P/C presence by expanding into life reinsurance and financial lines businesses in 1998. The group's goal was to leverage its investment expertise into lines of business more dependent on investment risk than its core P/C insurance and reinsurance businesses, which are driven by underwriting and for which the group continues to demonstrate a solid competitive advantage and presence.

XL successfully exited these businesses starting in 2007 and markedly reduced its exposure to them, but these businesses exposed the group to a string of material charges that distracted from its solidly positioned P/C insurance and reinsurance operations. XL rebounded by replenishing capital, strengthening the investment portfolio, and reducing runoff exposures--most notably by terminating certain reinsurance contracts and other agreements with monoline bond insurer Syncora Holdings Ltd. Because of these measures, employee retention and new and renewal business metrics had returned to historical levels by mid to late 2009. Nevertheless, the expansion weakened XL's competitive presence and we lowered our rating on the group in December 2008.

Insurance

XL's insurance operations are segmented into four business units, which consist of global professional liability, international P/C, North America P/C, and global specialty lines. The insurance operations market and distribute coverage through a wide variety of local, national, and international producers. XL's insurance operations are known for providing customized insurance policies for complex corporate risks that may require large limits. Large deductibles and self-insured retentions are incorporated into these policies to further manage risk along with its stringent underwriting guidelines. While XL is known for insuring large complex risk, certain of its products are targeted to small and midsize companies and organizations-- for example, professional liability and program business.

Premium volume for the insurance operation is segmented into six main lines of business, including professional liability, nonprofessional liability, property, marine/energy/aviation, other specialty lines (e.g. environmental, programs, and equine), and other lines (e.g. credit and surety). Premium growth in 2011 is attributed to new business initiatives that include expanding product lines (e.g. North American construction and surety, U.S. general aviation and international professional liability, construction and upper middle market) and entering emerging markets.

Reinsurance

XL's reinsurance operations are segmented into five geographic regions, which are North America, Europe, Bermuda, Latin America, and Asia Pacific. In this segment, the company focuses on providing non-catastrophe property, catastrophe property, casualty, marine, aviation, and other specialty coverage on both a proportional and excess of loss basis. Reinsurance is marketed primarily through the large reinsurance brokers as well as on a direct basis.

In 2011, XL's reinsurance operations have benefited from positive rate activity in the property catastrophe reinsurance market combined with success in recapturing lost business. In the past years, XL growth has been oriented towards short tail lines because of very challenging market conditions in long tail lines.

Prospective

While market conditions will largely determine premium production, we expect overall GPW to grow about 8% to 10% in 2011 and 6% to 8% in 2012. XL will likely report above-average premium growth from both the insurance and reinsurance segments relative to historical levels because of management strategic growth initiatives combined with somewhat favorable rate trends across various short-tails classes of business.

Management And Corporate Strategy: Renewed Focus On P/C Operations Through Strategic Growth Initiatives

Management has successfully defended XL's franchise, which was under significant pressure, following the financial market crisis in 2008. This was accomplished by divesting its ownership interest in Syncora Holdings Ltd., managing down the risk in its investment portfolio, and through expense reduction initiatives. Further, management has renewed XL's focus on P/C insurance and reinsurance operations and has placed the life reinsurance operations in run-off. Currently, management is focusing on enhancing XL's franchise through the execution of their value creation strategy.

Management's value creation strategy focuses on five core competencies, which include maintaining underwriting excellence, maintaining a strong risk management culture, executing upon strategic growth opportunities, achieving an optimum investment portfolio, and obtaining operating and capital efficiency. XL's adequate reserve position and the favorable reserve development illustrate its disciplined underwriting culture. A disciplined underwriting culture, strong risk management capabilities and recent acquisition of underwriting talent combine to place XL in a solid position to execute management's strategic growth initiatives.

Operational management

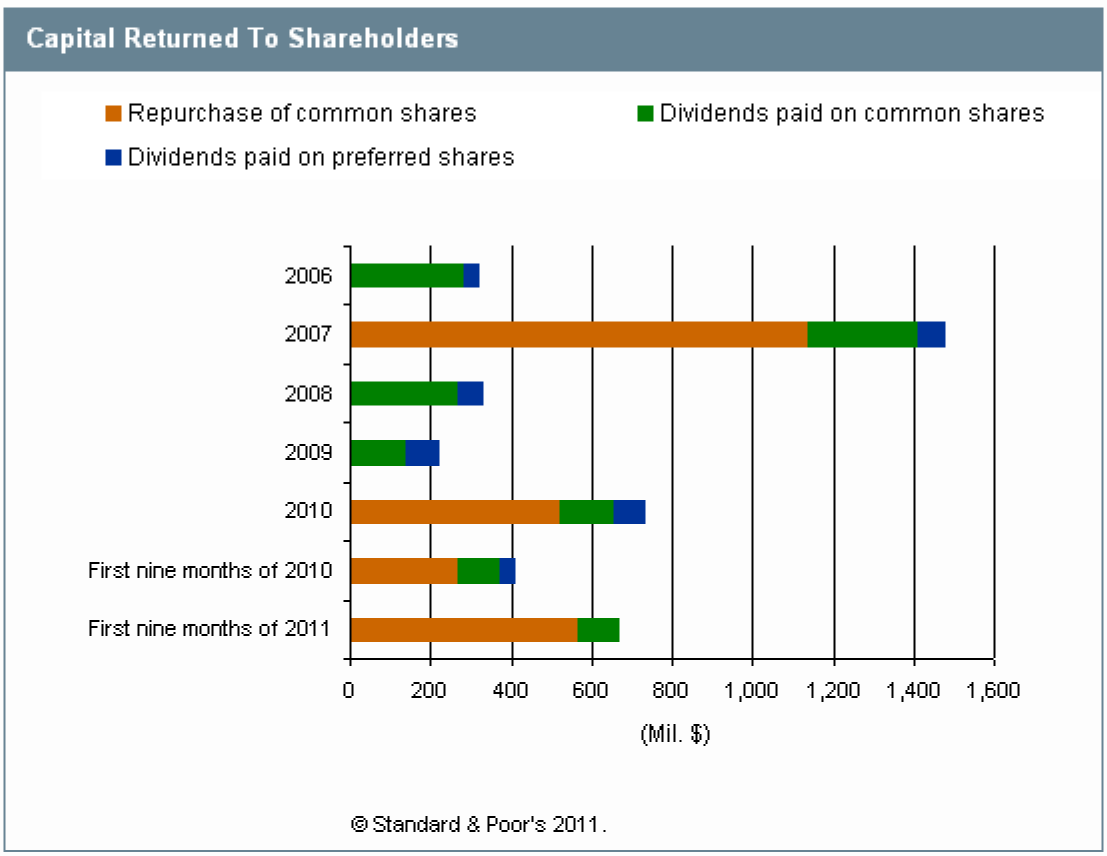
Commencing with Mike McGavick's joining XL in May 2008, there have been several high-level leadership changes at XL. In September 2008, Jacob Rosengarten joined XL as the chief enterprise risk officer. Since March of 2010, XL has benefited from the addition of underwriting talent—North America P/C chief underwriting officer, chief underwriting officer XL Re Ltd., and chief underwriting officers for North America construction and surety, North America and international property, North America programs, excess and surplus lines, inland marine, and political risk while at the same time enhancing its corporate ranks—chief financial officer, chief platform officer (the head of

I.T.), deputy chief enterprise risk officer, and SVP strategic analytics among others. We consider these changes to be in line with management's strategic plan of enhancing ERM, refocusing on core operations, and strategic growth. However, the extent of the changes does introduce heightened operational risk in the short term. Still, the continued strength of the insurance and reinsurance segment leadership structure and the recent enhancements to the ERM program offset some of these risks.

Financial management

XL targets a return on equity of 15% through the cycle. Under the new leadership, XL's financial management remains prudent and consistent with the rating level. XL's total financial leverage of 23% as of Sept. 30, 2011, is moderate and within expectations. Unlike that of similarly leveraged peers, XL's financial leverage (which includes debt and hybrid securities) is relatively conservative and consists primarily of senior notes and high-equity-like equity hybrid securities. XL repurchased $567 million of its ordinary shares in the first nine months of 2011. As of Sept. 30, 2011, about $290 million remained available under its existing program.

Chart 1



Enterprise Risk Management: Much Stronger Since The Financial Crisis

We continue to view XL's ERM framework as strong. This is primarily driven by consistently strong scores for all the components of our ERM evaluation (risk culture, risk controls, emerging risks management, risk models, and strategic risk management). XL's mix of business (insurance and reinsurance), exposure to various product lines, regions, and the severity prone nature of its reinsurance operations make risk management a key factor in the overall rating on XL.

XL's risk management culture is strong. Our view is supported by sound governance mechanisms including an independent ERM department, a developed and maturing risk appetite, and a strong reporting framework including robust risk disclosures relating to reserve ranges, loss triangles, catastrophe exposures, and outputs from the economic capital models. Strong ERM is one of the five key drivers identified by XL's management as a key driver of shareholder value as the organization made plans for a 'fresh start' earlier this year. While we recognize these positives, this is partially offset by the need to institutionalize the risk culture as several new senior level corporate and business line recruits have been hired and there has been expansion into new regions.

The overall risk controls at XL are regarded as strong. XL's investment risk controls are also considered strong. This is supported by a consistent set of risk limits informed by the organizational risk tolerance, risk policies with clearly defined escalation protocols, and a mature asset liability management process. This is partially offset by lack of seasoning in the recent enhancements to the credit risk monitoring processes. Underwriting risk controls are scored as strong, supported by historically strong underwriting performance, advanced analytical support to pricing and underwriting, peer reviews and underwriting audits. Underwriting and risk-transfer decisions are stress-tested via Realistic Disaster Scenario (RDS) analyses.

A strong score for catastrophe risk controls is influenced by articulated catastrophe risk tolerances, frequent monitoring of limits (real-time monitoring for the reinsurance business, and monthly for the insurance business) to ensure compliance, and a loss estimation process that has held up historically compared with peers. We affirm our opinion of XL's controls related to reserve risk as strong due to a demonstrated conservative attitude to reserve releases, and active monitoring of actual versus expected loss emergence.

The corroboration for a strong score for operational risk controls results from a well-developed internal audit program, and improvements in XL's business-continuity infrastructure. Support for a strong score for emerging-risk management is because of proactive/forward-looking management at each business unit and each function, coupled with the detailed risk-assessment process, and cross-functionally integrated via a risk-committee structure.

Risk models are viewed as strong. XL's internal Capital Management Program (CMP), which supports capital allocation, informs risk-adjusted performance targets, risk tolerances, and reinsurance evaluation. Multiple vendor models are used to analyze catastrophe risks, and these are integrated with the underwriting and pricing tools. On the investment front, models are used extensively for asset allocation purposes, monitoring credit risk, and to analyze the effect of stresses on the investment portfolio.

XL's strategic risk management is viewed as strong because of a positive risk/reward mentality exhibited in decision making, including, but not limited to, risk transfer decisions, strategic asset allocation in the investment portfolio and the use of risk-adjusted returns from capital models in incentive compensation programs. The capital model has been used in evaluating the risk/reward trade-offs in a potential strategic acquisitions and the output from the CMP aided in the decision making. The capital allocation process has been further stream-lined with the measurements that are aligned toward business strategies and there is a robust communication and reporting strategy developed around the CMP.

We expect XL to continue improving its risk models, and further enhance its strategic risk management and use risk-reward metrics for strategic decisions to maintain its strong ERM score.

Accounting

In our analysis, we adjusted our view of XL's operating cash flow for calendar-year 2008 to exclude the $1.8 billion cash payment to Syncora for the termination of certain reinsurance contracts. We determined this payment was not indicative of ongoing operations.

In July 2010, XL redomesticated to Ireland from the Cayman Islands whereby XL Group plc has replaced XLIT Ltd. (formerly XL Group Ltd.) as the ultimate parent company. However, we do not believe that this change in the corporate structure should have a material impact on the financials or in XL's ability to receive dividends from its operating companies.

In accordance with the requirement to closely monitor market risk and liquidity, the group has a well-developed risk management process to monitor securities that may be other-than-temporary impairments (OTTI).

Operating Performance: Strong Underlying Results, Despite Special Charges Detracting From Overall Earnings

Notwithstanding XL's strong operating performance derived from its core P/C insurance and reinsurance segments, special charges and catastrophe losses have historically detracted materially from overall earnings. The current rating incorporates our expectation that strong net earnings will result from the continuation of strong underwriting performance, reduction of risk in the investment portfolio (which generated $271 million and $921 million of realized capital losses in 2010 and 2009, respectively), and the materially reduced risk profile of the runoff businesses. Furthermore, the continued focus and recent enhancement of ERM to a strong level will materially reduce the frequency and severity of unanticipated losses.

Table 3

XL Group PLC/Operating Statistics

	Nine months ended Sept. 30		--Year ended Dec. 31--				
(Mil. $)	**2011**	**2010**	**2010**	**2009**	**2008**	**2007**	**2006**
Total revenue	5,110.4	4,973.4	6,652.1	7,069.9	8,461.2	9,468.4	9,579.4
EBIT	294.9	718.2	1,032.8	425.8	(1,964.8)	1,170.8	2,574.8
EBIT adjusted	438.2	904.0	1,256.8	1,298.4	1,864.3	2,693.7	2,297.6
EBITDA	331.4	747.2	1,073.2	481.9	(1,923.6)	1,172.5	2,577.2
EBITDA adjusted	474.8	933.1	1,297.2	1,354.5	1,905.5	2,695.3	2,300.0
Net income	110.2	448.1	643.4	74.9	(2,553.8)	299.8	1,787.8
Return on revenue (%)	8.6	18.2	18.9	18.4	22.0	28.4	24.0
Return on revenue (incl. realized capital gains/losses) (%)	5.3	14.8	14.9	5.5	11.6	22.3	23.2
Return on average equity (%) *	1.3	5.9	6.4	1.0	(31.8)	3.0	19.2
Return on average adjusted assets (%) *	0.3	1.4	1.6	0.2	(5.5)	0.6	3.4
Realized gains/EBITDA (%)	(52.1)	(26.0)	(28.4)	(198.2)	53.8	(56.2)	(0.6)
Administrative expense ratio (%)	18.4	17.6	17.9	18.5	17.5	15.9	15.6
Commissions expense ratio (%)	14.5	14.4	14.6	15.0	14.2	14.8	14.6
Expense ratio (%)	32.9	32.0	32.5	33.5	31.7	30.7	30.2
Non life loss ratio (%)	76.7	65.4	63.8	61.5	66.2	59.8	62.2

Table 3

XL Group PLC/Operating Statistics (cont.)							
Non life combined ratio (%)	107.2	95.9	94.8	93.6	94.9	88.7	89.5
Cash flows							
Net cash flow from operating activities	365.5	829.3	594.8	(42.8)	(427.3)	2,240.9	2,438.7
Net cash flow from investing activities	268.7	623.7	261.5	214.6	3,809.2	118.4	(2,972.3)
Net cash flow from financing activities	(500.0)	(1,129.7)	(1,473.3)	(962.6)	(2,829.3)	(754.9)	(968.2)

* Ratios for the nine months were annualized

Historical

XL's underwriting performance from its core P/C re/insurance segments has been strong, as measured by an average combined ratio of 92.3% over the past five years (2006-2010). Similarly, the company's ROR excluding realized capital losses and extraordinary charges from runoff operations averaged a strong 22.3% over the same timeframe.

However, this performance has been offset by significant adverse charges. While the capital base has absorbed these losses, they have had a material impact on earnings. XL reported a $1.1 billion charge in 2007 due to a write-down associated with Syncora Holdings Ltd. (formerly known as SCA) and Primus Guaranty Ltd. as well as losses associated with a prior reinsurance transaction with Syncora. In 2008, the group reported a charge of $1.4 billion resulting from an agreement with Syncora to terminate certain reinsurance and other obligations. The Syncora-related charge combined with the write-down of $990 million of goodwill and $963 million in net realized investment losses led to a net loss of $2.6 billion in 2008.

The investment portfolio generated further outsized net realized investment losses in 2009 of $921 million, which were comparable with the losses generated in 2008. We believe that the actions undertaken by management to reduce the risk embedded in the investment portfolio should result in net realized investment losses having a more moderate impact on earnings going forward.

Current performance

In 2010, XL reported strong results with $806 million in income before income taxes compared with $195 million in 2009. Markedly reduced realized investment losses ($271 million in 2010 versus $921 million in 2009) was modestly offset by reduced net investment income borne from a low interest environment and increased catastrophe losses ($349 million versus $83 million in 2009). Results from 2010 also benefited from prior-year reserve releases of $373 million with an overall P/C segment combined ratio of 94.8%.

Prospective

We believe that the expense ratio will remain in the low thirties over the next 12 to 24 months because of the startup costs and expense drag associated with forming new operations and hiring senior underwriters. Based on our view of the near-term rate and loss cost trends coupled with our expense ratio expectation, we would anticipate the combined ratio in the mid 90s, assuming a catastrophe load of 5% in 2012. After incorporating investment activities, we would expect the pretax ROR (excluding realized capital gains and losses) in the mid-teens in 2012.

Investments And Liquidity: Significant Progress In Reducing Risk, Though Some Exposure Remains

The current rating incorporates our belief that XL has successfully reduced the risk profile of the investment portfolio that generated $1.9 billion of realized investment losses in 2008 and 2009 combined. Although XL has a higher potential for investment losses relative to peers primarily due to nonagency structured assets, we believe this risk is markedly reduced, and more importantly, XL has implemented investment risk controls to sustain the reduced risk profile. Accordingly, we have a strong view of XL's investments and liquidity.

Table 4

XL Group PLC/Investment Statistics

	Nine months ended Sept. 30		--Year ended Dec. 31--				
(Mil. $)	**2011**	**2010**	**2010**	**2009**	**2008**	**2007**	**2006**
Total Invested assets	35,728.8	36,485.1	35,449.5	35,465.7	33,830.6	43,465.5	44,360.4
Change in invested assets (%)	(2.1)	1.5	(0.0)	4.8	(22.2)	(2.0)	6.0
Net investment income	866.9	907.6	1,198.0	1,319.8	1,769.0	2,248.8	1,978.2
Realized capital gains/(losses)	(172.6)	(194.2)	(304.6)	(955.1)	(1,035.4)	(658.7)	(15.3)
Unrealized gains/(losses)	357.2	1,341.6	1,092.5	2,469.9	(3,170.8)	(421.9)	165.2
Net investment yield (%) *	3.2	3.3	3.4	3.8	4.6	5.1	4.6
Net investment yield including realized gains/(losses) (%) *	2.6	2.6	2.5	1.1	1.9	3.6	4.6
Net investment yield including realized and unrealized gains/(losses) (%) *	3.9	7.5	5.6	8.2	(6.3)	2.7	4.9
Common Equity Investment/Capital (%)	3.2	0.2	0.6	0.1	3.6	6.9	6.7
Portfolio composition (% of invested assets)							
Bonds (%)	83.2	78.9	79.8	79.1	75.8	77.3	81.4
Equity investments (%)	1.1	0.1	0.2	0.1	1.1	2.0	2.0
Short term investments (%)	1.0	4.9	5.8	5.0	4.3	4.1	5.3
Other investments (%)	5.7	5.3	5.7	5.6	5.9	7.6	6.3
Cash and cash equivalents (%)	8.9	10.8	8.5	10.3	12.9	8.9	5.0

* Ratios for the nine months were annualized.

XL pursues a strategic asset allocation approach, which provides an optimal portfolio mix over the long term relative to liabilities. At the same time, this approach allows XL's experienced investment managers, whose decision-making authority is otherwise tightly defined, to modestly deviate from the long-term target portfolio in order to capitalize on changing market conditions. Consistent with the group's initiatives to strengthen risk management and control, XL's investment decisions are centered on tight measures of statistical risk analysis, supplemented by scenario stress testing, to provide guidance and transparency for exposure and risk tolerance, as demonstrated by its reduced exposure to the structured credit products and sector concentration (mainly financials) that led to undue mark-to-market volatility and losses from 2007 to 2009. Although efforts continue to reduce this risk, XL's investments remain susceptible to mark-to-market volatility and realized and unrealized losses, as the group still has sizable exposure in structured investments, which remains a weakness to the rating.

XL's strategic asset allocation involves continual monitoring of the portfolio's risk profile and periodic rebalancing to ensure that actual and intended risks are consistent under a controlled risk management framework. This risk management framework entails defining and controlling ranges of tolerance within which the portfolio can operate, including concentration and aggregation, credit quality, liquidity, rate and spread duration, value at risk, and tracking error. Furthermore, XL's portfolio structure is built to ensure the ability to hold assets to recovery with no forced sales to satisfy operating cash flow requirements at high confidence levels.

As of Sept. 30, 2011, XL's $32.7 billion fixed-maturity portfolio consisted of predominantly investment-grade bonds, constituting about 97% of total fixed-income assets with an average quality rating of 'AA'. At the end of third-quarter 2011, asset allocation within the fixed-income portfolio was 37% corporate bonds, 29% structured credit, 27% government and government related securities, and 7% cash and cash equivalents. XL's structured-credit allocation is split between 59% agency mortgage-backed securities and 41% non-agency, which is further segmented into various categories, including commercial mortgage-backed securities (CMBS), CDOs, subprime, and alt-A. XL has minimal exposure to the European periphery countries' securities (i.e., Greece, Ireland, Italy, Portugal, and Spain) of about $305 million as of Sept. 30, 2011.

Liquidity

XL's liquidity is strong with $3.2 billion in cash and cash equivalents and positive operating cash flow of $366 million for the nine months ended Sept. 30, 2011. As of Sept. 30, 2011, the group had a $5 billion letter-of-credit facility of which $2.0 billion has been drawn down. The largest facility for $3 billion expires in 2012, of which 49% has been drawn down. In addition, this facility includes a $750 million five-year revolver that is fully available. The next largest facility, $1 billion, expires in March 2014 and is fully available. The remaining three facilities are available on a continuous basis and have total commitments of $1 billion, of which $517 million has been drawn down. The bulk of this capacity is in a $3 billion facility expiring in 2012.

XL's letter of credit and certain derivatives are subject to collateral postings in the event of a downgrade. A downgrade to lower than 'A-' on the operating-company level would trigger cancellation provisions in a significant amount of XL's assumed reinsurance agreements and might require the group to return unearned premiums to cedants. Because of collateral posting requirements under the group's letter of credit and revolving credit facilities, such a downgrade would require posting of cash collateral in support of certain in-use portions of these facilities.

Prospective

Standard & Poor's expects management to continue optimizing the investment portfolio within the guidelines imposed by the strategic assets allocation. As they do so, they will also continue diminishing the remaining life reinsurance and financial lines exposures, which contributed to the higher duration and structured investment components of the portfolio. As such, over time, we expect less exposure to structured securities and financial institutions as well as an overall focus on shorter-duration investments.

Capitalization: Strong Supported By The Recovery Of The Investment Markets

XL's capitalization is strong supported by the recovery of the investment markets over the past two and half years. Our assessment is based on the balance between XL's quantitatively measured capital level, which was extremely strong as of Sept. 30, 2011, and the volatility of carrying a significant majority of fixed-maturity assets at fair value.

Prospective

Despite the 2011 share buybacks, Standard & Poor's expects XL's capital adequacy to remain strong and redundant for the rating level in 2011 and 2012.

Table 5

XL Group PLC/Capitalization Statistics							
	Nine months ended Sept. 30		--Year ended Dec. 31--				
(Mil. $)	2011	2010	2010	2009	2008	2007	2006
Total assets	46,625.2	46,296.0	45,023.4	45,663.9	45,682.0	57,762.3	59,308.9
Adjusted total assets	42,738.0	42,489.4	41,180.1	41,705.0	41,120.6	52,246.9	53,174.4
Common equity	9,942.0	9,869.6	9,613.1	8,432.4	5,115.2	8,948.1	9,131.2
Change in common equity (%)	0.7	20.8	14.0	64.8	(42.8)	(2.0)	22.2
Total capital	12,917.1	13,515.1	13,233.1	12,182.5	9,917.8	12,677.8	12,534.1
Change in total capital (%)	(4.4)	13.2	8.6	22.8	(21.8)	1.1	15.2
Reinsurance and reserves							
Reinsurance utilization (%)	22.8	20.9	19.4	21.1	22.7	20.8	22.2
Reinsurance recoverables to shareholders' equity (%)	35.5	35.0	36.2	42.0	74.6	55.4	60.6
Loss reserves to total shareholders' equity (%)	236.0	241.3	243.9	291.3	493.7	361.9	340.5
Loss reserves/net premiums written (%) *	384.7	429.9	435.7	465.5	395.3	454.4	408.2
Liquid assets/loss and unearned premium reserves (%)	143.6	145.1	142.6	136.4	126.0	124.0	133.7

* Ratios for the nine months were annualized

Reserves

We believe that XL's reserves are adequate, and we have noted improvements in the reserving process. We view reserving risk controls as strong. In addition to the customary use of multiple reserve development methodologies and the employment of a third-party review of its reserves beyond the normal audit process, XL employs stochastic techniques to analyze reserve adequacy and the risk of adverse reserve development. Further, a detailed internal review of reserves is completed for the second and fourth quarter financials.

In the past, XL, like some of its peers, exhibited adverse reserve development for excess casualty reinsurance business written during the previous soft market cycle (accident years 1997-2001). This exposure is highlighted by adverse loss reserve development on prior-year business of $1.1 billion in 2005 ($834 million related to a reinsurance write-off because of a lost arbitration case), $268 million in 2004, and $937 million in 2003. However, in more recent years, prior-year reserve development has been favorable (see table 6).

Table 6

XL Group PLC/Reserve Development And Combined Ratio							
	-- Nine months ended Sept. 30 --		--Year ended Dec. 31--				
	2011	2010	2010	2009	2008	2007	2006
(Favorable)/unfavorable reserve development (mil. $)	(217.1)	(251.4)	(372.9)	(284.7)	(610.7)	(425.4)	(110.6)
Initial accident-year combined ratio (%)	112.7	102.6	102.2	99.2	105.1	95.3	91.2
Calendar-year combined ratio (%)	107.2	95.9	94.8	93.6	94.9	88.7	89.5

XL does have exposure to claims on its directors and officers and errors-and-omissions book of business arising from the adverse economic conditions, particularly subprime issues. A significant proportion of this exposure resides in the professional insurance book of business, which generated nearly $1.5 billion in GPW, as compared with consolidated P/C segment production of $7.5 billion in 2008. Considering XL's robust reserving process, which included an additional 5% loss load on this business in 2008; it will be some time before these losses emerge.

Reinsurance XL has a centralized program that measures risk globally and then develops appropriate ways to manage these exposures on a group basis, including the purchase of reinsurance. We believe these measures appropriately address the group's reinsurance requirements. As of year-end 2010, XL's reinsurance utilization was about 19% (23% as of Sept. 30, 2011), which is consistent with the past five-year (2006-2010) average of about 21%. As of Sept. 30, 2011, the reinsurance recoverable on paid and unpaid losses was $3.9 billion or 36% of the group's shareholders' equity. Given XL's proactive approach to such risks, we consider XL's exposure to reinsurance recoverable risk as appropriate.

As of Dec. 31, 2010, the company's reinsurance counterparties were predominantly strong with approximately 90% of the recoverables rated 'A' or better. The company is also the beneficiary of LOCs, trust accounts, and funds withheld in the aggregate amount of $1.5 billion collateralizing reinsurance recoverables of certain reinsurers. It is worth noting that there is a concentration risk with two major reinsurers (i.e., Munich Re and Swiss Re).

Table 7

XL Group PLC/Reinsurance Recoverables Concentration

Reinsurer	Financial Strength Rating/Outlook As of Dec. 15, 2011	% of Total Reinsurance Recoverables as of Dec. 31, 2010
Munich Reinsurance Co.	AA-/Stable	21.5
Swiss Reinsurance Co.	AA-/Stable	13.8
Lloyd's Syndicates	A+/Stable	7.0
Swiss Re Europe S.A.	AA-/Stable	4.8
Transatlantic Reinsurance Co.	A+/Stable	3.8
Total		50.9

XL manages its catastrophe exposure globally at the corporate and segment levels and monitors exposures over multiple return periods. Corporate management provides the segment business leaders with their allocated catastrophe capacity, and each segment leader is then responsible for maximizing profitability while working within their allocated capacity.

Financial Flexibility: After Significant Improvements, Now Viewed As Strong

Standard & Poor's now views XL's financial flexibility as strong. XL has improved markedly since 2008, with improvements in equity valuation and credit spreads, as operating performance continues to be strong, and the group's risk profile is significantly reduced. Better conditions in the financial market, in combination with markedly reduced risk in the investment portfolio, have alleviated the potential for material investment write-downs and enhanced XL's financial flexibility.

Related Criteria And Research

- Re/Insurers Continue To Tally The Claims Stemming From The Japanese Earthquake And Tsunami, Sept. 7, 2011
- Crisis In Japan: First-Quarter Catastrophe Losses Are Creating A Significant Drag On Global Reinsurers' 2011 Full-Year Earnings, May 6, 2011

Ratings Detail (As Of December 15, 2011)
Holding Company: XLIT Ltd.

Ratings Detail (As Of December 15, 2011) **(cont.)**	
Issuer Credit Rating	
Local Currency	BBB+/Stable/--
Junior Subordinated (1 Issue)	BBB-
Preference Stock (1 Issue)	BBB-
Preferred Stock (4 Issues)	BBB-
Senior Unsecured (5 Issues)	BBB+
Operating Companies Covered By This Report	
XL Insurance (Bermuda) Ltd.	
Financial Strength Rating	
Local Currency	A/Stable/--
Counterparty Credit Rating	
Local Currency	A/Stable/--
Financial Enhancement Rating	
Local Currency	A/--/--
Greenwich Insurance Co.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
Indian Harbor Insurance Co.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Insurance America Inc.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Insurance Co. Ltd.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/NR
XL Insurance Co. of New York Inc.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Insurance Switzerland	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--

Ratings Detail (As Of December 15, 2011) (cont.)	
XL Re Europe Ltd.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Reinsurance America Inc.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Re Latin America Ltd.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Re Ltd.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Re Ltd. - U.K.	
Financial Strength Rating	
Local Currency	A/Stable/--
XL Select Insurance Co.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
XL Specialty Insurance Co.	
Financial Strength Rating	
Local Currency	A/Stable/--
Issuer Credit Rating	
Local Currency	A/Stable/--
Related Entities	
Nac Re Corp.	
Issuer Credit Rating	
Local Currency	BBB+/Stable/--
Domicile	Bermuda

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.