FitchRatings

FITCH AFFIRMS SELECTIVE INSURANCE'S RATINGS; OUTLOOK STABLE

Fitch Ratings-Chicago-13 December 2012: Fitch Ratings has affirmed Selective Insurance Group, Inc.'s (Selective) ratings as follows:

--Issuer Default Rating (IDR) at 'A-';
--Senior debt at 'BBB+';
--Junior subordinated debt at 'BBB-'.

Fitch has also affirmed the 'A+' Insurer Financial Strength (IFS) ratings of the members of the Selective intercompany pool. The Rating Outlook is Stable. A full rating list is shown below.

The affirmation of Selective's ratings reflects the company's conservative balance sheet with solid capitalization and reserve strength as well as underwriting performance in line with peers. The ratings continue to reflect Selective's strong independent agency relationships, strong loss reserve position, and improved diversification through continued efforts to reduce its concentration in New Jersey.

The company's underwriting results in 2012 were significantly impacted by Hurricane Sandy, a post-tropical storm that made landfall in New Jersey on Oct. 30th, representing the second consecutive year in which a storm with hurricane force winds appeared in the region within Selective's primary geographic footprint, following Hurricane Irene in 2011.

Selective reported that Sandy generated an estimated gross loss of $100 million-$120 million which more than doubled the company's previous record single event catastrophe loss, from Hurricane Irene. However, pre-tax net of reinsurance losses related to Sandy were limited to $52 million, reflecting the reinsurance program the company has in place to help mitigate its property catastrophe exposure. The impact of this loss was also somewhat offset by flood claim servicing revenue of $12 million from the National Flood Insurance Program (NFIP). Selective is the sixth largest writer for the NFIP.

Selective's combined ratio (GAAP) through nine-months 2012 improved to 102.3% versus 107.4% for full year 2011, due to a decline in non-catastrophe losses and premium growth that has outpaced growth in loss costs. As a result of Sandy, fourth quarter 2012 results are expected to modestly deteriorate and the company anticipates an additional 2.0 point impact on its full year 2012 combined ratio relative to previously stated projections. Fitch notes that the company's accident-year combined ratio, excluding the impact of catastrophe losses, improved by 2.0 points over the prior year period, reflecting a modest improvement in run-rate underwriting results. Selective's calendar year underwriting results also include a lesser impact from favorable loss reserve development than regional peers.

Fitch views Selective's historical profitability as better than peers but results have declined in recent years due to cyclical underwriting pressure, weaker investment performance and above average catastrophe losses.

Fitch continues to believe that Selective's balance sheet is conservative and that, as of Sept. 30, 2012, capitalization is good, with both stockholder's equity and statutory surplus maintaining strong positions of approximately $1.1 billion, respectively. Fitch believes that Selective maintains adequate capital and uses a moderate amount of operating leverage (annualized net premium written to equity). At Sept. 30, 2012, annualized operating leverage was 1.53 times (x), versus 1.34x at year-end 2011, with the increase driven primarily by the addition of excess and surplus lines premium as well as from price improvement experienced in the commercial and personal segments.

Fitch also believes that Selective employs a moderate amount of financial leverage, has ample financial flexibility, and limited near-term liquidity needs. The company's unadjusted debt-to-total capital ratio is roughly 21.4% at Sept. 30, 2012.

Historically, Selective's strong regional presence and small and middle market commercial lines focus has allowed for premium rate increases above industry experience. Selective conducts a sizable portion of its business in the state of New Jersey; however, the company has expanded into the Midwest to diversify its insurance exposure out of New Jersey and the Northeast U.S. In 2011, the top five states accounted for 59% of total net written premium, with New Jersey at 25%.

Key rating triggers that could lead to a downgrade include prolonged underwriting weakness, demonstrated by a failure to produce an underwriting profit given normal catastrophe losses, and a material deterioration in current balance sheet strengths. Fitch's rating rationale anticipates operating leverage as measured by net written premiums to equity to remain below 1.7x, financial leverage to remain below 25%, and operating earnings based interest coverage to reach 5x-7x or better.

Fitch considers a rating upgrade to be unlikely in the near term due to Selective's current company profile including its regional concentration, smaller capital base relative to larger peers, and pressured underwriting results. Key rating triggers that could lead to an upgrade over the long term include a material and sustained improvement on recent underwriting performance that causes Fitch to view Selective as meaningfully better than peers and the industry, and material capital growth with all else being equal.

Fitch has affirmed the following ratings with a Stable Outlook:

Selective Insurance Group, Inc.
--IDR at 'A-';
--$100 million senior notes 6.7% due Nov. 1, 2035 at 'BBB+';
--$50 million senior notes 7.25% due Nov. 15, 2034 at 'BBB+';
--$100 million junior subordinated notes 7.5% due Sept. 27, 2066 at 'BBB-'.

Selective Insurance Company of America
Selective Way Insurance Company
Selective Insurance Company of South Carolina
Selective Insurance Company of the Southeast
Selective Insurance Company of New York
Selective Insurance Company of New England
Selective Auto Insurance Company of New Jersey
Mesa Underwriters Specialty Insurance Company
--IFS at 'A+'.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

Applicable Criteria and Related Research:
--'Insurance Rating Methodology' (Oct. 18, 2012).

Applicable Criteria and Related Research:
Insurance Rating Methodology — Amended
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=692293