Research

Radian Group Inc. And Subsidiaries

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SACP* Assessments				SACP*		Support		Ratings
Anchor	bb+	+ Modifiers	0	= bb+		+ 0		= Financial Strength Rating: BB+/Positive/--
Business Risk: Satisfactory		ERM and Management	0	Liquidity	0	Group Support	0	Holding Company Rating: B+/Positive/--
Financial Risk: Less than Adequate		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.

Rationale

Business Risk Profile: Satisfactory

- Adequate competitive position reflects monoline business, improving operating performance, and diversified footprint in U.S.
- Macro environment supports continued recovery in the mortgage and housing sector

Financial Risk Profile: Less than Adequate

- Upper adequate capitalization and earnings reflect accumulation of retained earnings and reduction in legacy exposure partially offset by excess double leverage and expected growth in risk exposure
- Moderate risk position due to high susceptibility of monoline business to housing and macroeconomic cycles
- Less-than-adequate financial flexibility due to concentration in debt-maturity profile, elevated leverage, and challenging capital-market conditions.

Other Factors

Under Standard & Poor's Ratings Services' criteria, Radian's adequate business risk profile and less-than-adequate financial risk profile lead to a possible anchor of either 'bbb-' or 'bb+'. We have chosen the latter, giving greater weight to its financial risk profile as its capitalization is still recovering and we view its financial flexibility as constrained.

Factors Specific to the Holding Company

The ratings on the holding company reflect its structural subordination to its regulated insurance operating companies' obligations, its dependence on earnings from its subsidiaries, and adequate liquidity at the group level in the near term. We view the holding company as having sufficient resources to cover ongoing interest servicing and corporate expenses (which, for the most part, are covered by the operating companies) that could stretch to cover 2017 maturities. However, Radian would be hard-pressed to repay its 2019 maturities unless it could refinance them. The potential for contingent liability exists due to the company's ongoing dispute with the IRS.

Outlook: Positive

The positive outlook reflects the potential for strengthening of the company's capitalization and easing of concerns around financial flexibility, including reduction of its financial leverage. We expect Radian to maintain its competitive position, supported by ongoing compliance with Private Mortgage Insurers Eligibility Requirements (PMIERs), which should enable it to write new business and achieve operating performance in line with our expectations.

Upside scenario

We could raise the ratings during the next six-to-12 months if we get further comfort regarding the relative strength of the company's capitalization at the upper-adequate stress level from ongoing earnings accumulations and/or other management initiatives and if financial leverage declines in line with our expectations. This is in spite of an expected increase in exposure as a result of new business volumes and an anticipated increase in persistency, partially offset by a decline in legacy exposure, assuming the macroeconomic environment remains supportive and capital markets remain accessible.

Downside scenario

We can affirm the ratings if improvement in capitalization or financial leverage is lower than our expectations. We could lower the ratings during the next 12 months if we view capitalization as materially worse than upper-adequate. This could result from an earnings disruption that slows or impairs capital build-up--including deterioration in the economy--or increased capital requirements from higher-than-expected volumes of new business with an expanded risk profile, or from increased financial leverage. Further downside risk emanates from the potential for contingent liabilities that stretch Radian's resources materially or if the company faces challenges accessing capital markets.

Base-Case Scenario

Macroeconomic Assumptions

- Real U.S. GDP growth of about 2.5% in 2015 and 2.7% in 2016
- Payroll employment of $141.9 million for 2015, improving to $144.1 million for 2016
- 10-year Treasury rate for 2015 of 2.2% rising to 2.7% in 2016
- Core consumer price index of 1.8% in 2015 and 1.9% in 2016
- S&P Case-Shiller 20-City Home Price Index (December to December) change of 4.3% for 2015 and 4.3% for 2016

Company-Specific Assumptions

- New insurance written (NIW) of about $42 billion in 2015 and $38.5 billion-$39.5 billion for 2016
- Loss ratio of 23%-24% and 24%-27% for 2015 and 2016, respectively
- Capitalization of upper-adequate for 2015 and 2016
- Earnings accumulation to help reduce financial leverage to less than 35% for 2015 and 31%-33% for 2016

Key Metrics

	--Year ended Dec. 31--				
(Bil. $)	**2016***	**2015***	**2014**	**2013**	**2012**
New insurance written	38.5-39.5	~42	37.3	47.3	37.1
Loss ratio (%)	24-27	23-24	29.2	72.0	131.2
Standard & Poor's capital adequacy	Upper adequate	Upper adequate	Lower adequate	N.A.	N.A.

*Forecast data reflect Standard & Poor's base-case assumptions. N.A.-Not available.

Company Description

Radian Group Inc. provides mortgage insurance and mortgage and real estate services in the U.S. The company is one of the major players in the U.S. mortgage insurance sector, holding about 20% of the U.S. private mortgage insurance market. As of third-quarter 2015, total revenues were $918 million, including net written premiums of $689 million, primary insurance-in-force of $175 billion, and consolidated generally accepted accounting principles (GAAP) shareholders' equity of $2.4 billion.

Business Risk Profile: Satisfactory

Insurance industry and country risk: Intermediate

Our view of the company's very low country risk stems from the good economic growth prospects, relatively effective and stable political institutions, sophisticated financial systems, and strong payment culture in the U.S. We believe Radian's mortgage operations are exposed to moderate industry risks primarily because of the inherent product risk, given the company's underlying exposure to the mortgage market and consequent susceptibility to earnings volatility due to the sector's correlation with the performance of the economy and the housing sector. Since the financial crisis, Radian's portfolio quality has improved considerably, and the improving U.S. economy and recovery in the housing market are supporting the mortgage insurance (MI) sector's recovery. However, structural aspects of the mortgage market, such as mortgage interest deductibility for tax purposes, lack of full recourse, and potential for reversion to increased risk-taking over time as the risk appetite expands are offsetting factors. Although there is much more regulation surrounding mortgages and lending standards (e.g., Qualified Mortgages & Qualified Residential Mortgages) that should provide guardrails, we believe there is uncertainty about the efficacy of such initiatives in the long term. In addition, the fragmented nature of the regulatory jurisdiction and lack of a unified regulator for banking and insurance that can more effectively deal with systemic risks and failures of a few MI companies following the financial crisis further inform our view.

Table 1

Industry And Country Risk		
Insurance sector	**IICRA**	**Business mix (%)**
U.S. mortgage insurance	Intermediate risk	100.00

Competitive position: Adequate

Radian's competitive position reflects the company's strong presence within the MI sector, improving operating performance, and a diverse geographic presence across the U.S., offset by the monoline nature of its business.

We do not believe Radian has a significant and sustainable advantage over its competitors in the U.S. MI market. The commoditized nature of the products, the sector's dependence on government-supported entities such as Fannie Mae and Freddie Mac, and the regulated environment mean all market participants have similar capital requirements and product costs. Nevertheless, Radian has maintained the second-largest market share due to its well-established distribution relationships and technology platforms with geographically diversified national and regional banks. Its market share has also been helped by a high proportion of single-premium business (about one-third), which we view as discounted product. We believe single-premium business, especially lender-paid business, has lower earnings potential than equivalent monthly premium businesses, with higher premium revenue volatility and more susceptibility to mispricing due to uncertainties in refinancing activities and extension risk in light of anticipated increases in interest rates. Reflecting some of these concerns, Radian reduced its participation in certain discounted products, which had an impact on its market share. We believe the company would take a more measured approach to discounted business, which along with general reduction in origination activity due to lower anticipated refinance volumes will reduce new business in 2016. The competitive pressures in the market are increasing and the sector could see some pricing declines in 2016 for monthly premium business, though we expect the pricing to increase on lender-paid single business, reflecting higher capital requirements on this segment under updated PMIERs.

Table 2

Radian Group Inc. Competitive Position				
		--Year ended Dec. 31--		
(Mil. $)	**2015***	**2014**	**2013**	**2012**
Gross premiums written	767	982	1,032	804
Change in gross premiums written (%)	5.03	(4.87)	N.M.	7.98
MI: Net premiums written	735	925	951	806
Reinsurance utilization (%)	4.12	5.80	7.89	14.60

Table 2

Radian Group Inc. Competitive Position (cont.)				
MI: New insurance written	32,312	37,349	47,255	37,061

*Data as of Sept. 30. 2013 and later data reflect sale of Radian Asset (discontinued operations). N.M.-Not meaningful.

As a result of improving capitalization due to earnings accumulation and downstreaming of $375 million ($325 million of surplus notes and $50 million in capital contribution), we expect the MI operations to be in compliance with the PMIERs, which should help assuage market concerns and support the company's competitive position.

As of Sept. 30, 2015, Radian's NIW was $32.3 billion, higher than the prior year, with single-premium business constituting 32% (27% in third-quarter). The business being originated within the sector remains of high quality. Of the business written by Radian in the first nine months of 2015, 62.5% had FICO greater than or equal to 740, 93.5% had FICO greater than or equal to 680, and only 2.9% of business had loan-to-value ratios of more than 95%. Tightened post-crisis underwriting and strong credit quality are producing strong operating performance in more recent vintages, which along with declining losses from the legacy business is driving significant improvement in operating performance. As a result, the third-quarter 2015 year-to-date loss ratio was 20.5% as compared to 29% and 72% for full years 2014 and 2013, respectively.

In the base case, we expect the company to maintain a market share in the range of 19%-20% during the next two years, with NIW of about $42 billion for 2015 and about $38.5 billion-$39 billion for 2016, reflecting a lower level of refinance volumes and lower participation in single-premium business.

Financial Risk Profile: Less than Adequate

Capital and earnings: Improved earnings helping rebuild capital

We view Radian's capitalization as upper adequate prospectively during the next two years, an improvement from our lower-adequate assessment as of year-end 2014. A build-up of retained earnings through 2015 and monetization of Radian Asset Assurance, its bond insurer, has strengthened capitalization, though our view of capitalization is affected by the quality of capital due to high double leverage. We expect continued accumulation of earnings and reduction in leverage and/or additional management initiatives to strengthen capitalization further. However, in the short term, we believe Radian's capitalization can be sensitive to sector/company-specific assumptions.

Table 3

Radian Group Inc. Capitalization Statistics				
		--Year ended Dec. 31--		
(Mil. $)	**2015***	**2014**	**2013**	**2012**
Shareholders' equity reported	2,436	2,097	940	736
Change in shareholders' equity reported (%)	16.14	123.18	27.61	(37.72)
Total reported capital	3,674	3,382	1,870	1,509
Change in total capital (reported) (%)	8.63	80.87	23.92	(32.32)
MI: Statutory policyholders' surplus including contingency reserves¶	2,304	1,934	1,481	989
MI: Risk to capital (x)¶	17.90	20.30	24.00	29.90

*Data as of Sept. 30. ¶Government-sponsored entities reports. 2013 and later data reflect sale of Radian Asset (discontinued operations).

Table 4

Radian Group Inc. Earnings Statistics				
		--Year ended Dec. 31--		
(Mil. $)	**2015***	**2014**	**2013**	**2012**
Total revenue	869	993	856	859
Net premiums earned	689	845	781	739
MI: Net premiums earned	689	845	781	702
Net income (attributable to all shareholders)	212	960	(197)	(451)
Return on shareholders' equity (reported) (%)	14	63	(24)	(47)
MI: Net expense ratio (%)	24.3	29.6	36.6	26.6
MI: Net loss ratio (%)	20.5	29.2	72.0	131.2
MI: Net combined ratio (%)	44.8	58.8	108.6	157.8
MI: Primary insurance in force	174,866	171,810	161,240	140,363
MI: Primary risk in force	44,364	43,239	40,017	34,372
MI: Persistency (%)	79.2	83.4	81.1	81.8
MI: Primary default rate (%)	4.1	5.2	7.3	12.1

*Data as of Sept. 30. 2013 and later data reflect sale of Radian Asset (discontinued operations).

Under our base case forecast, we expect the loss ratio to be 23%-24% and 24%-27% for 2015 and 2016, respectively. We expect Radian's operating performance to benefit from a continuing decline in new notices of delinquencies, higher cure activity, and low losses from recent vintages, and for increased persistency to somewhat affect net premiums earned.

Risk position: Moderate

Radian is prone to capital and earnings volatility associated with insured mortgage losses that the macroeconomic cycle can exacerbate. The investment portfolio is well diversified with a low proportion of high-risk assets. As of Sept. 30, 2015, the consolidated investment portfolio comprised 64% fixed income, 34% cash and cash equivalents, and about 2% in equity and other investments. The fixed-income investments are of high quality with an average rating of 'AA' as of year-end 2014 and no noninvestment-grade holdings.

Table 5

Radian Group Inc. Risk Position				
		--Year ended Dec. 31--		
(Mil. $)	**2015***	**2014**	**2013**	**2012**
Total invested assets	4,456	3,674	3,407	5,208
Net investment income	59	66	68	114
Net investment yield (%)	1.65	1.85	1.58	2.07
Portfolio composition (% invested assets)				
Cash and short-term investments	34.56	36.62	28.80	16.00
Bonds	63.89	57.11	64.55	76.44
Equity investments	1.46	5.87	6.00	5.10
Other investments	0.08	0.40	0.66	2.45

*Data as of Sept. 30. 2013 and later data reflect sale of Radian Asset (discontinued operations).

Financial flexibility: Less than adequate

The company demonstrated access to the capital market as it tapped it for $350 million of senior notes in June 2015 to replace a significant proportion of convertibles due 2017 and raised new debt to partially fund its acquisition of Clayton Holdings LLC in 2014. Although the company has raised capital successfully, we continue to view financial flexibility as constrained due to concentration in its debt maturity profile, high (albeit improving) leverage, and potential challenges in accessing capital markets given market conditions. There is a significant amount of debt maturing in 2019 (and some in 2017) that can stress available resources if the company is unable to refinance it. The company's leverage dropped to about 40% for year-end 2014 from its improved equity position, in large part due to recognition of deferred tax assets related to prior operating losses as a result of its improving earnings profile. This is reflected in the increased intangibles/equity ratio of about 37% and 48% as of Sept 30, 2015, and Dec. 30, 2014, respectively, as compared to about 22% as of Sept. 30, 2014. This somewhat weakens our view of the improvement in leverage in the short term. However, we expect the leverage to continue to improve due to capital build-up from positive earnings. Under our base case, we expect the leverage to improve to around 36% as of year-end 2015 and 31%-33% as of year-end 2016. We also expect the fixed-charge ratio to be 5x-7x for the same period.

Other Assessments

Enterprise risk management: Adequate

Given the cyclicality of the mortgage insurance business and its high correlation with macroeconomic factors, we view enterprise risk management (ERM) as of high importance to our ratings on Radian. Much like its peers, Radian had outsize risk tolerances related to credit and underwriting during this past cycle and failed to exercise appropriate underwriting discipline and risk selection when mortgage origination credit quality declined. Post crisis, the company has made significant efforts to improve its ERM program as it looks to embed a corporate-wide risk culture from the top down that stresses the importance of balancing risk-reward trade-offs when making business decisions. To accomplish such a transition, significant oversight and involvement is needed from senior management and the board.

Radian's ERM council meets quarterly to discuss detailed reports highlighting key risks and mitigation strategies that are being considered, and this is presented to the ERM executive committee and ultimately to the board for approval. The company has expanded its analytical capabilities, processes, and systems to identify, assess, and manage risks proactively that came to bear during the financial crisis. Although there is limited room to differentiate from a pricing standpoint in the MI industry, Radian has been enhancing its risk model for the past few years to help the business obtain risk-adjusted metrics for greater insight into pricing and to develop risk thresholds. We expect continued enhancement of its risk models and further development of its risk tolerances.

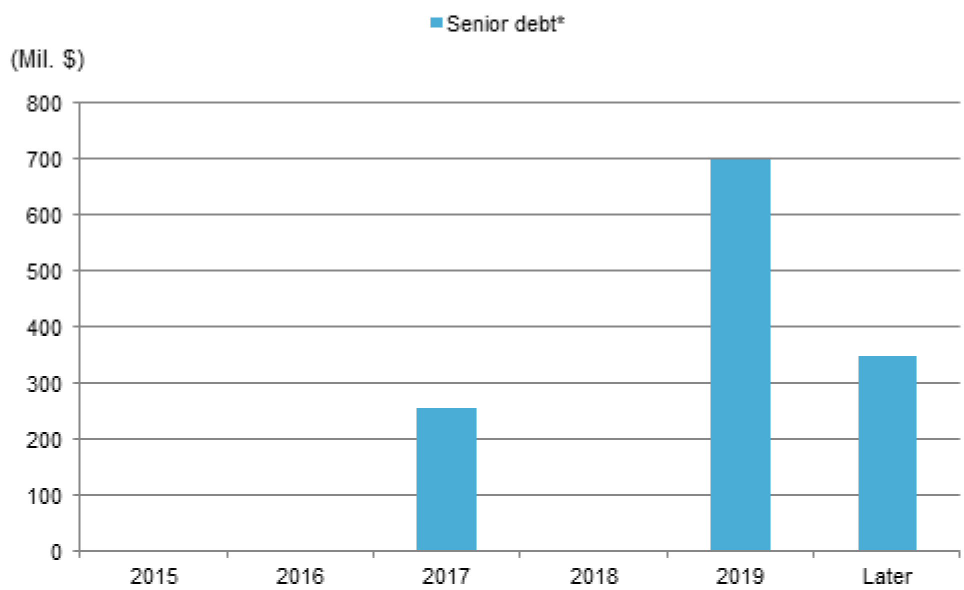
Management and governance: Satisfactory

Radian's management team has executed on various initiatives to strengthen its position in the sector and improve its financial strength. From a strategic perspective, the company is trying to diversify into ancillary operations, which is reflected in its acquisition of Clayton Holdings LLC in 2014. It has been building up its risk tolerances, updating its risk platform, and developing tools to better manage its risk-reward profile. However, the company has been more aggressive in pursuing single-premium business, which can have a bearing on its risk-adjusted margins if the loans stay longer on the books than expected.

Liquidity: Strong

Radian's liquidity reflects its high-quality investment portfolio, partially offset by elevated levels of outstanding claim reserves on the book from legacy vintages.

Debt Maturity Profile (as of Sept. 30, 2015)



*Includes convertible senior notes; reflects principal amount.

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Accounting Considerations

The company files both U.S. GAAP and statutory financials with its regulators. We utilize GAAP segment reporting, U.S. regulatory statutory filings, and other information provided by Radian to analyze the group.

Related Criteria And Research

- Key Credit Factors For The Mortgage Insurance Industry, March 2, 2015
- Methodology: Mortgage Insurer Capital Adequacy, March 2, 2015
- Group Rating Methodology, Nov. 19, 2013
- Insurers: Rating Methodology, May 7, 2013
- Enterprise Risk Management, May 7, 2013
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013

- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

Ratings Detail (As Of January 26, 2016)	
Holding Company: Radian Group Inc.	
Issuer Credit Rating	
Local Currency	B+/Positive/--
Senior Unsecured	B+
Operating Companies Covered By This Report	
Radian Guaranty Inc.	
Financial Strength Rating	
Local Currency	BB+/Positive/--
Counterparty Credit Rating	
Local Currency	BB+/Positive/--
Radian Mortgage Insurance Inc.	
Financial Strength Rating	
Local Currency	BB+/Positive/--
Issuer Credit Rating	
Local Currency	BB+/Positive/--
Domicile	Pennsylvania

*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. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.