



As PG&E Intends to Seek Bankruptcy Protection, U.S. Insurer Exposure is Limited (01/16/2019)

On Monday, Jan. 14, 2019, Pacific Gas and Electric Corp. (PG&E) announced that it would seek bankruptcy protection in approximately two weeks after its shares experienced a significant decline of more than 60% and its bonds experienced a decline of about 19%, due to concerns that the company may be held liable for California's November wildfire, which was cited as the deadliest in the state's history. According to PG&E, liabilities from the wildfire, as well as others that occurred in 2017, could potentially exceed \$30 billion, which surpasses its annual revenue and market value. In addition, PG&E failed to make an interest payment on Jan. 15 on its 2040 senior notes; however, it has a 30-day grace-period to do so before an event of default is triggered.

In California (unlike other states), utility companies may be held liable for damages if their equipment contributes to a fire, even if the company itself was not negligent. Consequently, PG&E could end up owing billions for the recent fire damage; California state regulators and government officials are currently assessing PG&E's wildfire liability.

U.S. Insurer PG&E Bond Exposure

The U.S. insurance industry's exposure to PG&E bonds at year-end 2017 totaled approximately \$5.8 billion in book/adjusted carrying value (BACV). Life companies accounted for 88% of the exposure, followed by property/casualty (P/C) at 8%. (See Table 1) As of Jan. 15, PG&E unsecured bonds were trading between approximately 74 cents and 81 cents on the dollar according to MarketAxess, a fixed-income electronic trading platform, suggesting bondholders may not receive full recovery on their holdings.

Table 1: PG&E Bond Investments by Insurer Type as of Year-End 2017

Life	P/C	Fraternal	Health	Title	Total
\$ 5,140,014,291	\$ 465,800,707	\$ 167,784,695	\$ 61,329,829	\$ 1,045,123	\$ 5,835,974,645
88.1%	8.0%	2.9%	1.1%	0.0%	100.0%

The top five insurers (all of which were life companies) accounted for 23% of total U.S. insurance industry PG&E bond exposure, or \$1.3 billion BACV, and the top 10 (also all life companies) accounted for 37% of the total, or \$2.3 billion BACV. Almost all exposure carried NAIC 1 designations at year-end 2017; however, ratings were lowered by the three major nationally recognized statistical ratings organizations in 2018, and on Jan. 14, the rating on PG&E's senior unsecured bonds was lowered to CC by Standard and Poor's (S&P), from B; to Caa3 by Moody's Investors Service (Moody's), from Baa3; and to CC by FitchRatings, from BBB-. Note that the credit ratings from S&P are currently under review for further downgrade, and the credit ratings from Moody's have a negative outlook.

With regard to insurers' investment in PG&E bonds relative to their total company bond exposures, two insurers (one health company and one property/casualty (P/C) company) each had about 6% of their total bond investments in PG&E bonds as of year-end 2017.

U.S. Insurer PG&E Stock Exposure

For PG&E stocks, U.S. insurer exposure was minimal, at approximately \$69.8 million in common and preferred PG&E stock as of year-end 2017. The most concentrated exposure was with one insurer (a P/C company) in the amount of \$74,000, out of a total \$33,700 in the company's total stock exposure (22%).

On the contrary, PG&E was one of the hedge fund industry's most widely held stocks as of the third quarter of 2018, according to a *Wall Street Journal* article dated Jan. 14, 2019.

Risks to Insurers

For the insurers with relatively "large" exposure to PG&E bonds (that is, as measured within their own bond portfolios), these concentrations represent a credit risk if there is a default in principal and/or interest payment by PG&E. Moreover, any additional negative rating actions on these bonds; that is, any further downgrade to lower credit quality, or a possible downgrade to 'D' (i.e. if the missed interest payment is not cured), could negatively affect the bonds' liquidity and market value.

The NAIC Capital Markets Bureau will continue to monitor the developing events with PG&E and report as deemed appropriate.