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The Japan Ship Owners' Mutual Protection & Indemnity Association

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The Japan Ship Owners' Mutual Protection & Indemnity Association

SACP* Assessments					SACP*			Support			Ratings
Anchor	bbb+	+	Modifiers	0	= bbb+		+	0		=	Financial Strength Rating
Business Risk			ERM and Management	0	Liquidity	0		Group Support	0		BBB+/Stable/--
Satisfactory											
Financial Risk			Holistic Analysis	0	Sovereign Risk	0		Gov't Support	0		
Upper Adequate											

*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
• Solid market position supported by strong relationships with Japan-related shipowners • Conservative investment policy with low financial leverage	• Low diversification because it specializes in marine protection and indemnity (P&I) and concentrates on Japan-related shipowners • Moderately strong capital and earnings constrained by low capital in terms of absolute value

Rationale

The 'BBB+' ratings on The Japan Ship Owners' Mutual Protection & Indemnity Association (Japan P&I) reflect S&P Global Ratings' assessment that the company's creditworthiness is at the lower end of the average of the global P&I sector in terms of business and financial positions.

Japan P&I is Japan's only shipowners' mutual P&I association and a member of the international P&I group. It ranks at the lower end of the average among 13 international P&I clubs in terms of premiums and free reserves. It specializes in marine P&I and has a solid market position supported by strong and long-standing relationships with Japan-related shipowners. On the other hand, Japan P&I's business line is less diversified and its customer base is geographically concentrated in Japan.

Japan P&I focuses more on underwriting profit rather than investment profit. While it is now enhancing its investment capabilities and making its internal risk management more sophisticated, we believe its conservative investment approach would remain unchanged. Also, Japan P&I is improving its ERM to start monitoring its overall risks in accordance with the Solvency II framework in a few years.

Under Japan P&I's last mid-term plan for fiscal 2015 (ended March 31, 2016) to fiscal 2017, it accumulated capital in the form of free reserves stably. Also, Japan P&I has no outstanding debt and issuance plans. Therefore, it has improved its capital to the 'AA' level at end-March 2018. In our base-case scenario, we expect Japan P&I to continue improving its capital, bringing it close to the 'AAA' level over the rating horizon. However, the absolute value of its capital would remain small, constraining our assessment of its capital. We base our stable outlook on this view.

Outlook: Stable

S&P Global Ratings' stable outlook on Japan P&I reflects its view that Japan P&I is likely to maintain its current business model, supported by the Japan-related shipping companies that make up most of its members. On the other hand, we expect Japan P&I to continue strengthening its capital through free reserve accumulation; however, the absolute value of its capital would remain small.

Downside scenario

We may lower the ratings on Japan P&I within the next 24 months under either of the following scenarios.

- Its prospective capital adequacy deteriorates significantly. This could result from an unexpectedly high frequency of claims or a significant increase in risk exposure.
- A significant premium decline weakens its competitive position, and its operating performance consistently and materially falls short of its competitors'.

Upside scenario

We may raise the ratings on Japan P&I within the next 24 months if it grows its free reserves to a sustainable level that leads us to revise upward our assessment of its capital.

Macroeconomic Assumptions

- Interest rates in Japan will stay low over the next two years.
- Japan's real GDP growth will grow at a steady pace and remain moderate.

Key Metrics (The Japan Ship Owners' Manual Protection & Indemnity Association On A Stand-Alone Basis)						
	Year ended March 31 of the next year					
(Bil. ¥)	**2015A**	**2016A**	**2017A**	**2018F***	**2019F***	**2020F***
Gross premiums written	25	23	21	21	20	21
Net income (attributable to all shareholders)	0	2	1	0-1	0-1	0-1
EBITDA fixed-charge coverage (X)	N.M.	N.M.	N.M.	N.M.	N.M.	N.M.
Financial leverage (%)	N.A.	N.A.	N.A.	<20%	<20%	<20%
Return on equity (%)	(2.1)	27.6	14.1	4-5	1-2	1-2
S&P Global capital adequacy	Very strong	Very strong	Very strong	Very strong	Very strong	Very strong
Net investment yield (%)	1.3	1.8	2.3	1.6	1.6	1.6
Net combined ratio (%)	87.8	83.7	89.8	92-94	97-99	97-99
Return on revenue (%)	9.7	15.8	17.2	3-4	1-2	1-2

*Forecast data represent S&P Global Ratings' base-case assumptions. F--Forecast. A--Actual. N.M.--Not Meaningful. N.A.--Not Available.

Business Risk Profile: Satisfactory

Japan P&I began operations in 1950 as a mutual insurance association. It engages in the non-life insurance business under a system of mutual insurance to cover the expenses and liabilities incidental to the operations of ships. In 1976, it became a member of the International Group (IG) of P&I Clubs. In 1989, it became a member of the Pooling Agreement of the International Group of P&I Clubs, giving it access to the group's reinsurance program. The majority of its business is concentrated on global marine P&I, but it also engages in the domestic marine P&I business.

Japan P&I has an adequate competitive position, in our view. It has a good niche position in the global marine P&I market and strong long-standing relationships with its members in Japan. They are mostly direct business contacts without brokers. Japan P&I has low business diversification because it focuses on marine P&I insurance and concentrates on its Japanese members.

When we compare Japan P&I's combined ratio with those of its rated P&I club peers, we consider its operating performance as slightly better than average. The combined ratio of Japan P&I could have been affected by fluctuations of the yen against the U.S. dollar. Japan P&I's combined ratio deteriorated slightly in fiscal 2017. Excluding the impact of the yen's appreciation, its combined ratio worsened to 100.5% in fiscal 2017 from 84.4% in fiscal 2016. The deterioration reflects a slight increase in claims, including one pool claim in fiscal 2017, although the absolute level remains comfortable, in Japan P&I's view. Meanwhile, the combined ratio's deterioration also reflects the moderate reduction of a supplementary call from a planned 40% to 30%, supported by the aforementioned favorable loss results. The reduction is also meant to reward the shipowners, which is the same as in fiscal 2016. We need to monitor the pricing from fiscal 2018, given the highly competitive market in recent years. A continued decline in its premium income could be a concern, in our view. Japan P&I's ROE seems a lot higher than its peers, but after adjusting for Japan's special accounting of catastrophe reserves and its high volatility, the ratio becomes closer to its global peers, in our view.

In our opinion, Japan P&I will likely keep its adequate competitive position over the medium term, especially in

Japan's shipowner market. However, we think its profitability could still fluctuate depending on the size and frequency of claims, even though Japan P&I could raise premium rates.

Financial Risk Profile: Upper Adequate

Japan P&I exhibits moderately strong capital and earnings, in our view. Capital adequacy--measured by our risk-based capital model--improved but stood in the 'AA' category as of end-March 2018, due to an increase in accumulation of free reserves as well as a decrease in premium income, which reduces insurance risk. Japan P&I's low absolute capital, however, constrains our view of its capital and earnings, because we believe it makes it more vulnerable to more frequent large losses. Under our base-case scenario, which is basically aligned with the company's mid-term plan, we expect Japan P&I's prospective capital adequacy to continue to improve close to the 'AAA' category over the rating horizon through the accumulation of free reserves.

Specifically, we assume Japan P&I's annual accumulation of free reserves (net income + catastrophe reserves accumulation) will be ¥0.2 billion-¥0.8 billion from fiscal 2018 to fiscal 2020. We assume its premium income will decrease until fiscal 2019 and gradually bottom out thereafter, and its combined ratio will slightly deteriorate because of the falling unit price.

In our view, Japan P&I's risk position reflects moderate risk, driven by potential volatility in its capital and earnings. We base our view on the club's exposure to midsize-to-large claims, relative to its capital. This assessment also reflects our positive view of its investment strategy, which we view as conservative compared with those of its peers. Most of the assets in its investment portfolio are fixed-income instruments such as Japanese government bonds and corporate and foreign bonds that are mostly rated 'A' or higher. While Japan P&I's investments in equity funds have increased slightly, it has also set a risk limit for its investments. We think its investment policy is likely to remain conservative.

We view Japan P&I's financial flexibility as adequate, because it can collect additional premiums by making supplementary calls from members in open policy years and impose premium increases at renewal when needed. The association has a track record of using this facility in the past, and we believe its strong relationships with its members would enable it to do so again, if necessary. Our adequate assessment of financial flexibility is reinforced by our view that it does not need to take on financial debt and it is not the mulling possibility.

Other Assessments

We assess Japan P&I's ERM as adequate and its management and governance as fair. We view both assessments as consistent with our ratings on Japan P&I.

We regard Japan P&I's ERM as consistent with our ratings on the entity. We see ERM as having low importance to the ratings given Japan P&I's size and virtually monoline status as a P&I insurer. It has conservative risk controls over its major risks and we believe its risk management culture is strengthening. In fiscal 2017, Japan P&I conducted a stress test so that it can take precautionary measures for potential emerging risks. In addition, it aims to start measuring its risk, based on the solvency ratio requirements under the Solvency II framework. This also supports our adequate assessment of its ERM.

We assess Japan P&I's management and governance as fair, reflecting our view that there are no shortcomings in this area. Its management team has a long history with the association, and we think they have good expertise and experience in the P&I market. We think that Japan P&I's strategic positioning and financial management are generally consistent with its capabilities. Japan P&I established its new mid-term plan in fiscal 2018 with specific financial and operational goals. We intend to monitor its implementation of this new plan.

We regard Japan P&I's liquidity as exceptional because of the strength of its available liquidity sources, which are mainly premium income, and an asset portfolio with ample liquid assets. We think Japan P&I is well positioned to meet its liquidity needs even if any major adverse claims should occur.

Rating Score Snapshot	
Financial Strength Rating	BBB+/Stable
Anchor	bbb+
Business Risk Profile	Satisfactory
IICRA*	Intermediate Risk
Competitive Position	Adequate
Financial Risk Profile	Upper Adequate
Capital & Earnings	Moderately Strong
Risk Position	Moderate Risk
Financial Flexibility	Adequate
Modifiers	0
ERM and Management	0
Enterprise Risk Management	Adequate
Management & Governance	Fair
Holistic Analysis	0
Liquidity	Exceptional
Soverign Risk	0
Support	0
Group Support	0
Government Support	0

Note: Support does not consider Ratings Above Sovereign criteria. *Insurance Industry And Country Risk Assessment.

Related Criteria

- Insurers: Rating Methodology, May 7, 2013
- Enterprise Risk Management, 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

Related Research

- P&I Sector Remains Strong Despite Market Pressure, Feb. 20, 2018
- The Global Marine Protection And Indemnity Industry, Jan. 31, 2018

Ratings Detail (As Of August 23, 2018)	
Operating Company Covered By This Report	
The Japan Ship Owners' Mutual Protection & Indemnity Association	
Financial Strength Rating	
Local Currency	BBB+/Stable/--
Issuer Credit Rating	
Local Currency	BBB+/Stable/--
Domicile	Japan

*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.