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Ratings

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The Japan Ship Owners' Mutual Protection & Indemnity Association

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The Japan Ship Owners' Mutual Protection & Indemnity Association

Anchor	bbb+
Business Risk	**Satisfactory**
Competitive position	Satisfactory
IICRA	Intermediate
Financial Risk	**Strong**
Capital and earnings	Very strong
Risk exposure	Moderately high
Funding structure	Neutral

+

Modifiers	0
Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0

=

SACP	bbb+

+

Support	0
Group support	0
Government support	0

=

BBB+/Positive/--
Financial strength rating

IICRA--Insurance Industry And Country Risk Assessment.
SACP--Stand-alone credit profile.

Credit Highlights

Overview

Strengths	Risks
Solid market position supported by strong relationships with Japan-related shipowners	Low diversification of its business because it specializes in marine protection and indemnity (P&I) and concentrates on Japan-related shipowners
Capital at the 'AAA' level and likely to strengthen further through accumulation of free reserves	Fierce competition in the P&I insurance market, making substantial expansion of its business unlikely

Japan P&I's credit quality is likely to improve moderately through enhanced capitalization. In S&P Global Ratings' view, The Japan Ship Owners' Mutual Protection & Indemnity Association's credit quality is likely to improve to near the average for the global P&I sector. It currently ranks at the lower end of the average for the sector. Japan P&I is Japan's only shipowners' mutual P&I association and is a member of the international P&I group. 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, its business is not particularly diversified and its customer base is geographically concentrated in Japan.

Japan P&I's capital is in the 'AAA' category for a second consecutive year and is likely to strengthen further. Japan P&I posted a net loss in fiscal 2019 (ended March 31, 2020), due to a number of large insurance claims and financial market turmoil stemming from the COVID-19 pandemic. However, its capital remained in excess of the 'AAA' level under our model, as it did in the previous year. In fiscal 2020, Japan P&I will need to pay large insurance claims related to the oil spill off the coast of Mauritius. Even so, its capital is likely to continue to improve stably at the 'AAA' level over our two-year rating horizon, in our view.

Japan P&I is likely to maintain a conservative asset management and risk management. To shore up investment profits, Japan P&I is diversifying its investment methods. Nevertheless, we do not expect any significant changes in its conservative approach to investment. Also, the association has made a continuous effort to improve its enterprise risk management. Given that discussions have begun regarding economic value-based capital regulations in Japan, Japan P&I has adopted a more flexible stance regarding its enterprise risk management policy, and is watching closely for further developments.

S&P Global Ratings acknowledges a high degree of uncertainty about the evolution of the coronavirus pandemic. The consensus among health experts is that the pandemic may now be at, or near, its peak in some regions but will remain a threat until a vaccine or effective treatment is widely available, which may not occur until the second half of 2021. We are using this assumption in assessing the economic and credit implications associated with the pandemic (see our research here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

Outlook: Positive

The positive outlook reflects our view of an at least a one-in-three chance that Japan P&I will continue to strengthen its capital through accumulation of free reserves, triggering an upgrade within the next two years. On the other hand, we expect Japan P&I to maintain its current business model, supported by the Japan-related shipping companies that constitute the majority of its membership.

Downside scenario

We may raise the ratings on Japan P&I within the next two years if:

- It stably strengthens its capital through accumulation of free reserves to a sustainable level commensurate with higher ratings, and
- The association maintains its competitive position.

Upside scenario

We may revise downward the outlook on Japan P&I to stable within the next two years 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 decline in premiums weakens its competitive position, and its operating performance consistently and materially falls short of its competitors'.

Key Assumptions

- Japan's real GDP will contract in 2020 due to the COVID-19 pandemic but recover substantially in 2021 and 2022.
- Interest rates in Japan will remain low over the next two years.

Key Metrics (Nonconsolidated)

	--Fiscal year*--							
(Bil. ¥)	**2022f**	**2021f**	**2020f**	**2019a**	**2018a**	**2017a**	**2016a**	**2015a**
S&P Global Ratings' capital adequacy§	Excellent	Excellent	Excellent	Excellent	Excellent	Very strong	Very strong	Very strong
Gross premiums written	19	19	19	20	21	21	23	25
Net income	0	0	1	(1)	2	1	2	(0)
Return on equity (%)	1-3	1-3	6-8	(12.1)	18.1	14.1	27.6	(2.1)
Return on equity (adjusted) (%)†	1-3	1-3	1-3	(4.2)	10.2	4.8	13.0	1.6
Net combined ratio (%)	100-102	100-102	98-100	107.5	95.0	89.8	83.7	87.8
Net investment yield (%)	1.3	1.3	0.6	0.2	1.2	2.3	1.8	1.3
Financial leverage (adjusted) (%)†	<1	<1	<1	0.5	0.6	0.4	0.5	0.5

*Fiscal years end March 31 of the following year. a--Actual. f--Forecast (S&P Global Ratings' base-case assumptions) N.A.--Not available. §Assessment for 2018 onward reflects an update to our framework; those from earlier were derived using our previous criteria. †Adjusted with what S&P Global Ratings' views as equitylike reserves.

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. It currently ranks at the lower end of the average for the 13 international P&I clubs in terms of premiums and free reserves.

We believe Japan P&I has a good niche position in the global marine P&I market and a stable business base for domestic shipowners, supported by strong long-standing relationships with its members in Japan. They are mostly direct business contacts without brokers. The association has low business diversification because it focuses on marine P&I insurance and concentrates on its Japanese members. These factors lead us to deem Japan P&I to have a satisfactory competitive position in the global P&I market.

Declining premium income at Japan P&I in recent years may not have started to bottom out, in our view. The association applied a general increase of 7.5% on premiums for the February 2020 renewal. This was in line with the trend of the global P&I market and the number of existing policies barely decreased after the hike. However, this may not lead to an increase in its premium income, while the impact of the sale and scrapping of aging ships with relatively high insurance premiums continues.

Furthermore, we think Japan P&I could struggle to further raise rates, given the weak business sentiment in the shipping industry--policyholders of Japan P&I--amid the pandemic-triggered economic downturn. Given persistently fierce competition in the market, a continued decline in its premium income could be a concern in terms of its competitive position, in our view.

When we compare Japan P&I's combined ratio (the total of its net loss ratio and net expense ratio) with those of its rated P&I club peers, we expect it to maintain better operating performance on a several-year average basis. Japan P&I's combined ratio had been favorable in recent years but worsened to 107.5% in fiscal 2019, due to a number of large claims, including the impact of exchange rates, from 95.0% in fiscal 2018. In fiscal 2020, the association will need to pay large insurance claims, including those related to the oil spill off the coast of Mauritius. However, we assume a return to normal levels of insurance claims over the medium term.

We also do not expect the pandemic to hurt Japan P&I's insurance underwriting profit substantially. This is because the association estimates the payment of pandemic-related insurance claims to be limited. In addition, the economic downturn will likely reduce marine distribution, meaning fewer accidents and a lower loss ratio. Reflecting a favorable combined ratio, Japan P&I's return on equity (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 declines to closer to those of global peers, in our view.

Japan P&I will likely maintain risk-adjusted returns commensurate with its business scale, in our view. It says it will focus on Japan-related business, a niche area in the global market, because it is an area of strength for the insurer. Accordingly, Japan P&I's assessment of risk and return and prioritization are relatively simple.

Financial Risk Profile: Strong

We expect Japan P&I's capital, which is extremely high, to improve further through accumulation of free reserves. In fiscal 2019, the association's free reserves declined as it posted a net loss due mainly to the occurrence of large claim payments and financial market turmoil. However, under on our capital model, the association maintained its capital at a level well into the 'AAA' category at the end of fiscal 2019, as it did at the end of the previous year, in our view. Under our base-case scenario, basically aligned with Japan P&I's conservative earnings forecast, we expect its prospective capital adequacy to continue to improve to a level consistently in excess of the 'AAA' category threshold over the next two years.

However, we lowered our assessment of its capital and earnings one notch to very strong, the second-highest of eight possible categories. This is based on our view that, considering its earnings volatility, its capital is not currently strong enough to exceed the 'AAA' level in a stable manner. In addition, Japan P&I's low absolute capital constrains our view of its capital and earnings, because we believe this makes it vulnerable to more frequent large losses.

In our view, Japan P&I has moderately high risk exposure, driven by potentially high volatility in its capital and earnings. We base our view mainly on the concentration of its business on P&I insurance with high frequency of midsize-to-large claims relative to its capital.

Japan P&I has been enhancing asset management and internal risk management to ramp up investment profits. However, we do not expect any significant changes in its conservative approach to investment. While the association has slightly increased its fixed-income and equity investments, their limits have been raised only at a moderate pace based on those initially set. Its investment portfolio continues to be made up of mostly fixed-income instruments, such as U.S. Treasury bonds and Japanese and foreign public and corporate bonds mostly rated 'A' or higher.

In addition, Japan P&I has taken adequate measures to control risk. For instance, it is a member of the Pooling Agreement of the International Group of P&I Clubs, which gives it access to the group's reinsurance program. Also, it can collect more additional premiums than scheduled by making supplementary calls from members and imposing premium increases at renewal when needed. As part of its effort to enhance risk management, it planned to start monitoring its overall risks in accordance with the Solvency II framework and writing an in-house risk and solvency assessment report in fiscal 2019. However, given that discussions regarding economic value-based capital regulations in Japan have begun in earnest, Japan P&I has adopted a more flexible stance regarding its enterprise risk management policy, watching further developments closely.

We assess Japan P&I's funding structure as neutral. It does not own debt and has no plan for debt financing, in our view.

Other Key Credit Considerations

Governance

We see no shortcomings in Japan P&I's management and governance. Its management team has a well-established favorable relationship with members and good expertise and experience in the P&I market. The management team clearly defines its management strategy and financial management policy, which are consistent with its scale and capabilities, in our view. We believe the association has been conducting generally conservative risk management as an entire organization. Its continued effort to strengthen capital and enhance internal risk management verifies this view.

Liquidity

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 major adverse claims should occur.

Related Criteria

- Insurers Rating Methodology, July 1, 2019
- 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

- Mauritius Oil Spill: Insurer Japan P&I Exposed, Aug. 12, 2020

Business And Financial Risk Matrix

Business risk profile	Financial risk profile							
	Excellent	Very Strong	**Strong**	Satisfactory	Fair	Marginal	Weak	Vulnerable
Excellent	aa+	aa	aa-	a+	a-	bbb	bb+	b+
Very Strong	aa	aa/aa-	aa-/a+	a+/a	a-/bbb+	bbb/bbb-	bb+/bb	b+
Strong	aa-/a+	a+/a	a/a-	a-/bbb+	bbb+/bbb	bbb-/bb+	bb/bb-	b+/b
Satisfactory	a	a/a-	**a-/bbb+**	bbb+/bbb	bbb/bbb-	bb+/bb	bb-/b+	b/b-
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb/bb-	b+/b	b-
Weak	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b/b-	b-
Vulnerable	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b+/b	b/b-	b-	b-

Note: Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

Ratings Detail (As Of September 8, 2020)*

Operating Company Covered By This Report	
The Japan Ship Owners' Mutual Protection & Indemnity Association	
Financial Strength Rating	
Local Currency	BBB+/Positive/--
Issuer Credit Rating	
Local Currency	BBB+/Positive/--
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.