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Japan Ship Owners' Mutual Protection & Indemnity Assn. (The)

Primary Credit Analyst:
Kentaro Mukoyama, Tokyo 81 3 4550 8775; kentaro.mukoyama@spglobal.com

Secondary Contact:
Koshiro Emura, Tokyo (81) 3-4550-8307; koshiro.emura@spglobal.com

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Japan Ship Owners' Mutual Protection & Indemnity Assn. (The)

Anchor	bbb
Business Risk	**Satisfactory**
Competitive position	Satisfactory
IICRA	Intermediate
Financial Risk	**Fair**
Capital and earnings	Satisfactory
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/Stable/--
Financial strength rating

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

Credit Highlights

Overview

Key strengths	Key risks
Solid market position supported by strong relationships with Japan-related shipowners	Low diversification of its business because it specializes in marine P&I and concentrates on Japan-related shipowners
Generally higher profitability than the average of the 13 international protection and indemnity (P&I) clubs	Continued fierce competition in the P&I insurance market, making substantial expansion of its business unlikely
	Significant fluctuations in capital and profitability associated with the occurrence of large claims

We expect Japan P&I to maintain its competitive position through measures to improve earnings. In S&P Global Ratings' view, The Japan Ship Owners' Mutual Protection & Indemnity Association (Japan P&I) has a solid position in the P&I insurance market that endures. It is Japan's only shipowners' mutual P&I association and a member of the international P&I group. In addition, its position is 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. The association's concentration on P&I activity makes its earnings susceptible to large insurance claims. Japan P&I has taken measures to address profitability deterioration in recent years. It has, for example, hiked premium rates and selectively concluded contracts.

Japan P&I will likely restore its capital level gradually, in our view. Japan P&I has had to pay out many large insurance claims and suffered amid the COVID-19 pandemic in the past three years. Especially in fiscal 2021 (ended March 31, 2022), the association had to draw down significant free reserves (total of net assets and catastrophe loss reserves), mainly because it saw the biggest ever claim on a coastal ship. We expect Japan P&I to gradually accumulate free reserves by implementing profitability improvement measures.

Japan P&I is likely to maintain conservative asset management and risk management. To shore up investment profits, Japan P&I is slightly increasing its investment in foreign equity funds. 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. In particular, it has enhanced risk management in its insurance underwriting business, responding to a deterioration of its combined ratio (the total of its net loss ratio and net expense ratio) in recent years.

Outlook: Stable

The stable outlook reflects our view that Japan P&I will likely gradually improve its underwriting performance and capital and maintain them at an adequate level.

Downside scenario

We may downgrade Japan P&I within next two years under either of the following scenarios.

- Its capital level further deteriorates. This could result from an unexpectedly high frequency of claims or a significant increase in investment risk.
- Its profitability, measured by the combined ratio and return on equity, continues to significantly underperform the industry average.

Upside scenario

On the other hand, we may upgrade Japan P&I within the next two years if it significantly improves its capital adequacy through the accumulation of free reserves while maintaining its competitive position.

Key Assumptions

Macroeconomic assumptions

- Japan's real GDP will pick up in tandem with a recovery from the COVID-19 pandemic in 2022 and moderately grow from 2023.

The pandemic

- Insurance payouts related to the pandemic will decrease.

Loss ratio

- The frequency of claims will remain at the normal level. The loss ratio will gradually improve thanks to the effects of a premium rate hike and selective contract conclusions.

Financial market conditions

- Key variables, such as stock prices and exchange rates, will remain around the levels we assumed when making our forecasts about the association

Capital management policy

- The level of capital will improve through accumulation of free reserves. Japan P&I will not implement nonrecurring capital enhancement measures, such as unbudgeted supplementary calls and subordinated debt financing.

The Japan Ship Owners' Mutual Protection & Indemnity Association--Key Metrics

	--Fiscal year*--				
(Bil. ¥)	**2024f**	**2023f**	**2022f**	**2021a**	**2020a**
Gross premiums written	23-26	26-30	23-26	22	20
EBITDA adjusted§	0-1	2-3	0-1	(6)	1
Net income	0-1	1-2	0-1	(0)	3
S&P Global Ratings' capital adequacy	Strong	Strong	Strong	Strong	Excellent
Return on equity (adjusted) (%)§	2-4	9-11	2-4	(16.1)	6.3
Financial leverage (adjusted) (%)§	<40	<40	<40	0.7	0.6
Net combined ratio (%)	95-110	85-90	95-110	157.3	111.9
Net loss ratio (%)	75-85	65-70	75-85	132.3	88.3
Net expense ratio (%)	20-25	19-21	20-25	25.0	23.6
Return on revenue (%)§	4-8	15-17	4-8	(37.8)	7.2

*Fiscal years end March 31 of the following year. a--Actual. f--Forecast (S&P Global Ratings' base-case assumptions) . §Adjusted with S&P Global Ratings' views as equitylike reserves.

Business Risk Profile: Satisfactory

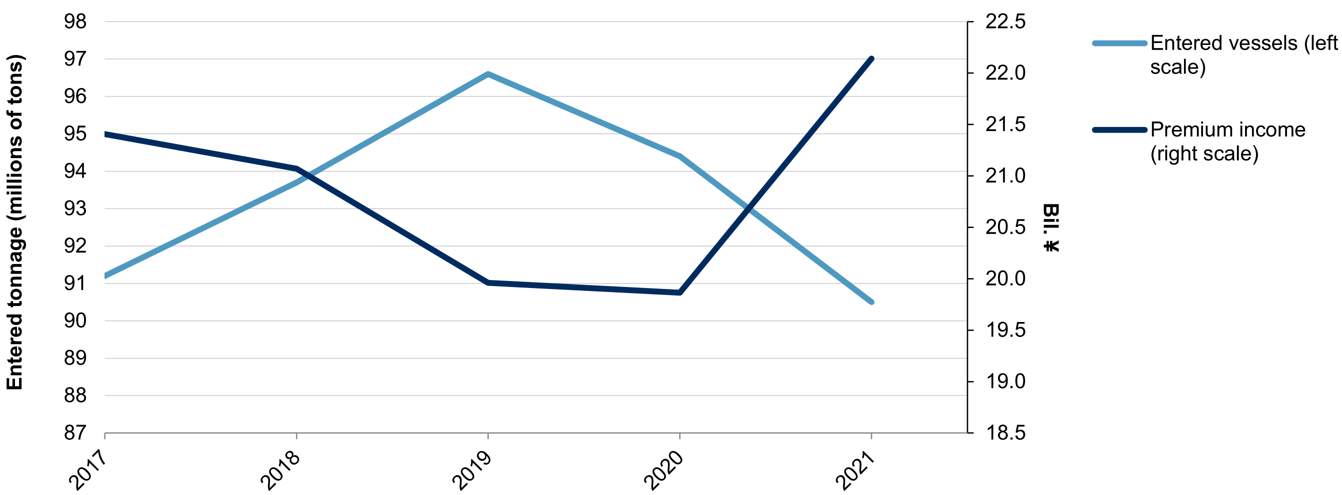
We expect Japan P&I to remain at the lower end of the average for the 13 international P&I clubs in terms of premiums and free reserves. It began operations in 1950 as a mutual insurance association. It engages in the non-life insurance business under a system of mutual insurance to cover the expenses and liabilities incidental to the operations of ships. In 1976, it became a member of the International Group 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. Most of its business is concentrated on global marine P&I, but it also engages in the domestic marine P&I business.

We believe Japan P&I maintains 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 an average competitive position in the global P&I market.

We expect Japan P&I's premium income to continue increasing thanks to continued rate revisions. Its premium income started to increase in fiscal 2021 thanks to the effects of a general increase on premiums that the association applied at renewal of contracts in the last three years. Previously, this income had been declining due to the aging ships with relatively high insurance premiums being sold or scrapped, as well as selective contract conclusions. We assume Japan P&I will continue to raise premium rates. In addition, Japan P&I has announced it would change the system to levy insurance premiums to the mutual premium system in fiscal 2023. Based on this, we calculate that premium income will increase in fiscal 2023 due to a one-time factor of a technical change of timing of premium payments.

Chart 1

Premium Income Is Increasing, Entered Vessel Tonnage Is Decreasing
Movements of premium income and entered vessels



Fiscal years end March 31 of the following year. Source: S&P Global Ratings, based on publicly disclosed financial materials.
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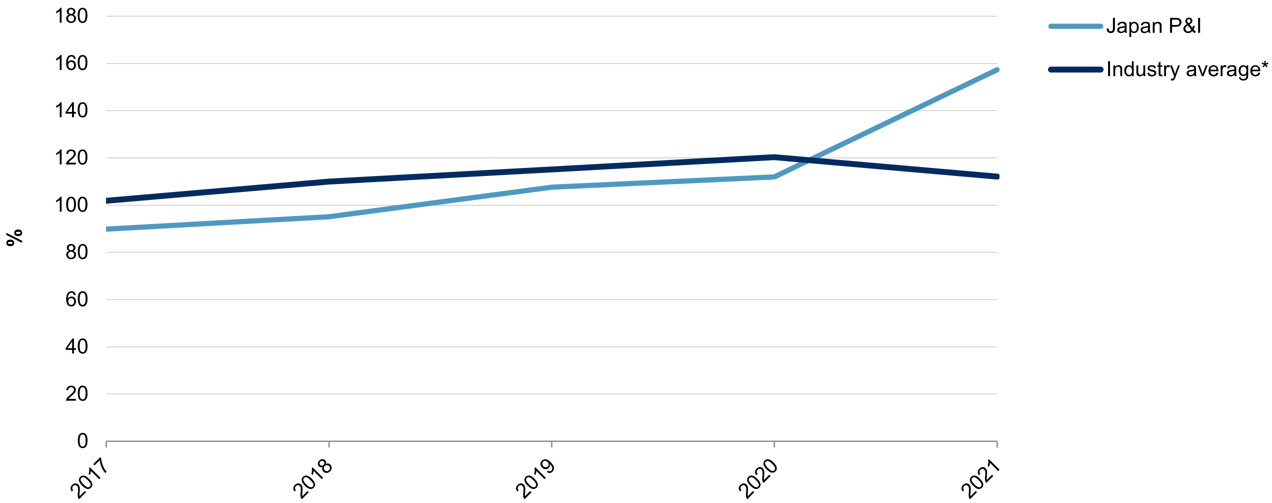
Japan P&I's profitability in terms of its combined ratio is likely to remain generally higher than the average for the 13 international P&I clubs, in our view. Its combined ratio exceeded 100% in the past three years. The ratio substantially deteriorated to 157.3% in fiscal 2021, mainly because the biggest ever claim on a coastal ship occurred. To address this, the association has carried out measures such as a premium rate hike and selective contract conclusions. Accordingly, we expect Japan P&I's profitability to improve from 2022. Furthermore, other P&I clubs have taken similar profitability improvement measures. Based on this, we think the frequency of occurrence of pool claims, in which all P&I clubs share losses, will likely taper off. We believe Japan P&I's premium income will likely increase in fiscal 2023 thanks to the aforementioned one-time measures, which should boost profitability temporarily.

Chart 2

Generally Higher Profitability Than The Industry Average Despite Volatility Due To Large Claims
Combined ratios



Fiscal years end March 31 of the following year for Japan P&I and Feb. 28 or Dec. 31 for other clubs. *Industry average combined ratio is a simple average of rated 13 clubs, which includes our estimates. Source: S&P Global Ratings, based on publicly disclosed financial materials of each club.
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Japan P&I will likely maintain an approach to maximize 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: Fair

We expect Japan P&I's capital to continue improving in the next two years. Its free reserves substantially declined in fiscal 2021 due to the occurrence of a large claim. Consequently, we figure its adjusted capital under our capital model also decreased considerably to the level required under our 'A' category from the level required under our 'AAA' category. We believe the association will likely gradually improve its capital through profitability improvement measures.

We expect Japan P&I to remain susceptible to large claims. The concentration of its business on P&I insurance with high frequency of midsize-to-large claims and its low absolute capital have increased the volatility of profitability and capital. The potential volatility of profitability is likely to remain high, although the profitability will likely improve.

Japan P&I has been enhancing asset management and internal risk management to ramp up investment profits. That said, we do not expect any significant changes in its conservative approach to investment. The association increased allocation for fixed-income and equity investments in the past few years. Nevertheless, we do not expect substantial growth in these investments; the pace of increase has been moderate. In addition, 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.

We believe Japan P&I is likely to continue to take adequate measures to control risks, such as a premium rate hikes and selective contract conclusions. Another supporting factor is that 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. As part of its effort to enhance risk management, the association has considered starting to monitor its overall risks on an economic value basis and prepare an own risk and solvency assessment (ORSA) report, taking into account changing regulations in Japan and overseas.

We assess Japan P&I's funding structure as neutral. It does not own debt. We assume that Japan P&I will refrain from financing any new debt.

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 across the organization been conducting generally conservative risk management. 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 occur.

Environmental, social, and governance

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

ESG factors have no material influence on our credit rating analysis of Japan P&I.

Related Criteria

- Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Insurers Rating Methodology, July 1, 2019
- Principles Of Credit Ratings, Feb. 16, 2011
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Related Research

- Ratings on Japan P&I Downgraded To 'BBB' As Major Claims Weaken Capital Adequacy; Outlook Stable, July 27, 2022
- ESG Credit Indicator Report Card: Asia-Pacific Insurance, Nov. 29, 2021
- ESG Credit Indicator Report Card: North And Latin America Insurance, Nov. 29, 2021
- ESG Credit Indicator Report Card: EMEA Insurance, Nov. 29, 2021

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 14, 2022)*

Operating Company Covered By This Report	
Japan Ship Owners' Mutual Protection & Indemnity Assn. (The)	
Financial Strength Rating	
Local Currency	BBB/Stable/--
Issuer Credit Rating	
Local Currency	BBB/Stable/--
Domicile	Japan

Ratings Detail (As Of September 14, 2022)*(cont.)

*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.

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