

## Research

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# West of England Ship Owners Mutual Insurance Association (Luxembourg)

**Primary Credit Analyst:**

Robert J Greensted, London + 44 20 7176 7095; robert.greensted@spglobal.com

**Secondary Contact:**

Mark D Nicholson, London + 44 20 7176 7991; mark.nicholson@spglobal.com

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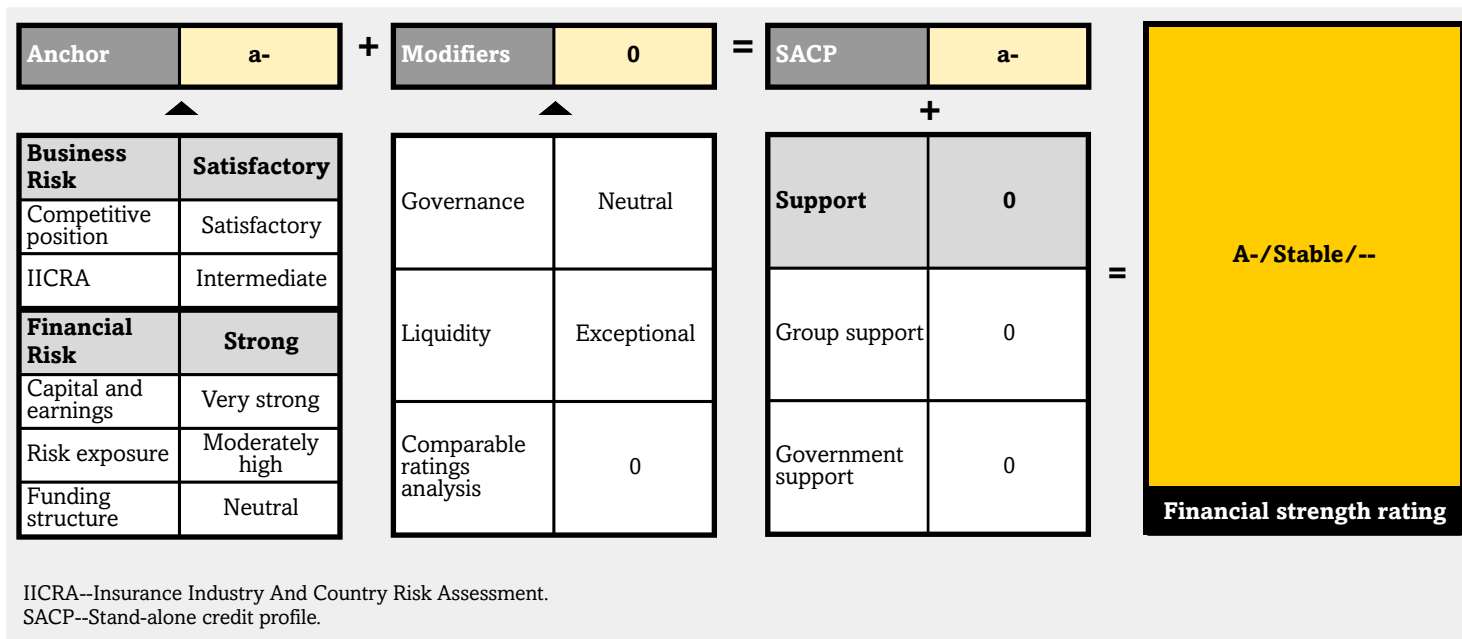
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# West of England Ship Owners Mutual Insurance Association (Luxembourg)



## Credit Highlights

### Overview

Strengths	Risks
Well capitalized, in excess of our benchmark for the 'AAA' level under our risk-based capital model.	An undiversified product range outside of marine and marine-related insurance.
Much improved brand and reputation in the protection and indemnity (P&I) sector.	Exposure to the volatility of other IG clubs' claims through a pooling system.
Market access through membership in the International Group of P&I Clubs (IG).	Challenging market conditions weighing on underwriting performance.

**The club will likely remain well capitalized at the 'AAA' level under S&P Global Ratings risk-based capital model.** The P&I insurer The West of England Ship Owners Mutual Insurance Association (Luxembourg) (West) has consistently maintained solid capitalization, despite pressure on profitability from tough underwriting conditions over the past few years. We expect its capital adequacy will remain resilient over the next two years, despite likely underwriting losses.

**We expect conditions in the P&I market to remain tough over the next two years.** West recorded another year of underwriting losses in the fiscal year ending Feb. 20, 2020 (FY2020), with a net combined (loss and expense) ratio of 107% due to a significant amount of pool claims. We expect that West will record a larger underwriting loss in FY2021, since the number of pool claims at half-year FY2021 was at a record high. We expect its underwriting results will improve in FY2022 and FY2023 policy years as rates improve across the sector.

**West's limited business diversification will continue.** West's core business remains the marine insurance sector and within that sector, West is relatively undiversified compared with some peers. We believe that West remains committed to the mutuality concept, and is unlikely to significantly diversify by offering hull or energy products.

**Outlook: Stable**

The stable outlook reflects our view that West will sustain excellent capitalization over the next two years, despite underwriting losses.

**Downside scenario**

We could lower the ratings, if West's underwriting performance deteriorated such it was materially below the IG average or its risk-based capital adequacy fell significantly and persistently below the 'AAA' level in our model.

**Upside scenario**

A positive rating action is unlikely over the next two years, and would depend on West substantially increasing its scale while significantly improving its operating performance

**Key Assumptions**

- The COVID-19 pandemic will lead to a global recession in 2020. In 2020, we forecast GDP will fall by 4% in the U.S., 7.4% in the eurozone, and 9.7% in the U.K.
- We expect central bank monetary policy responses will cement interest rates at a lower level for a longer period, putting pressure on insurers' investment yields. We expect U.S. ten-year bond yields will fall to 0.8% in 2020, slightly increasing to 1.46% in 2021.
- We believe business conditions in the P&I sector will remain weak in 2021-2022, but expect rate increases at the upcoming renewal. The pandemic will continue to test marine insurers both through investment losses and their underwriting portfolios. Investment losses will be generated through equity market falls and credit spreads widening whereas underwriting losses will flow from COVID-19-related claims and premium returns due to lower trading activity (with those writing cruise and passenger vessels most impacted).

**Key Metrics**

	2022f	2021f	2020	2019	2018
S&P Global Ratings' capital adequacy	Excellent	Excellent	Excellent	Excellent	Excellent
Gross premium written (mil. \$)	~250	~240	228.2	219.7	213.8
Net income (mil. \$)	~(10)	~(20)	31.5	(0.7)	(8.2)
Return on shareholders' equity (%)	~(2)	~(5)	9.8	(0.2)	(2.7)
P/C: net combined ratio (%)	~110	~115	107.0	113.8	115.6

f--S&P Global Ratings forecast.

## **Business Risk Profile: Satisfactory**

West, being a member of the IG group of clubs, benefits from significant market access, a substantial excess-of-loss reinsurance program, and the pooling of risks. It has a geographically diverse client base with members from across the globe. Members in Asia and Europe contribute over 70% of its premiums.

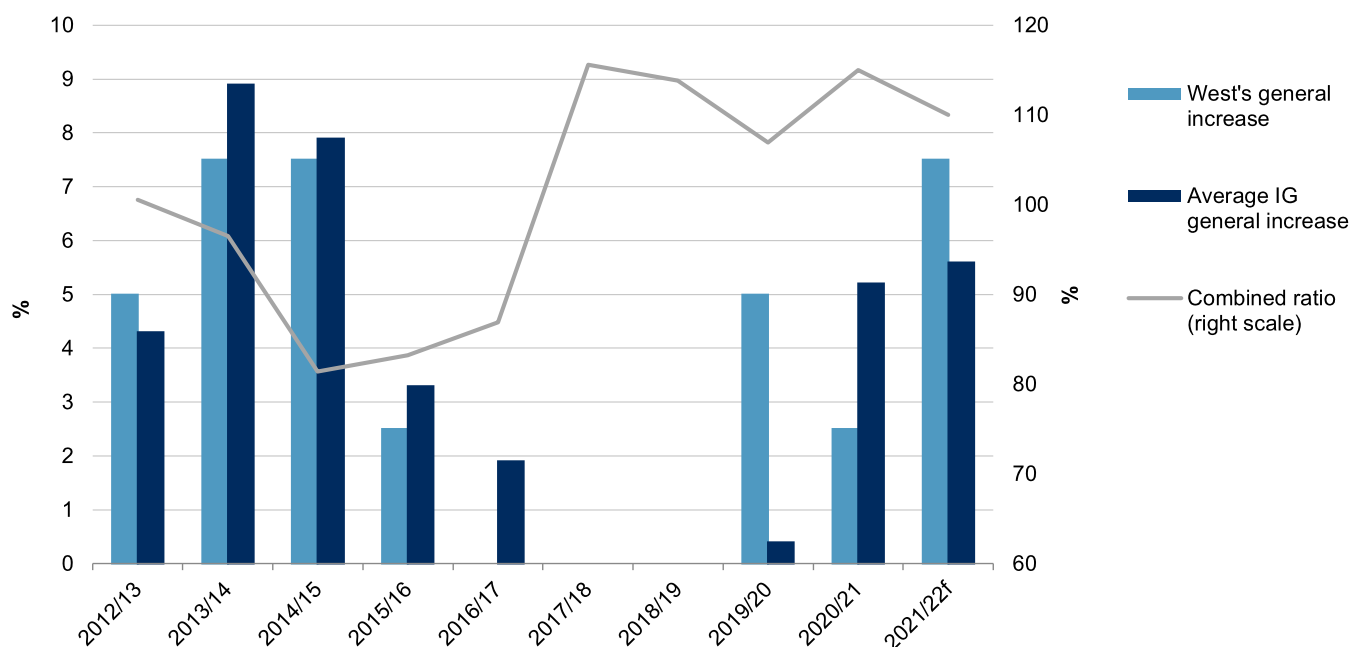
West is relatively undiversified by product, with all its business being P&I or marine related. West does offer some non-mutual P&I cover on a fixed premium basis, however, we do not expect the share of fixed premium to increase significantly in the medium term. West has expanded its product offering through small acquisitions in the past year, taking stakes in a marine cyber consultancy, a delay insurance specialist, and a marine services company--all of which will offer ancillary products to the main P&I offering. We do not expect West to move into hull or energy lines.

We believe that the club's brand and reputation has significantly improved over recent years. Previously the club was associated with unbudgeted calls and poor relative performance to peers, but a new senior management team, new logo, and a change of offices have improved its image. Recently West was rated the fourth-best P&I club in the sector by broking firm Tysers, ahead of some of its 'A'-rated peers such as Standard, UK Club, and North of England.

Like many of its IG peers, West's has recorded underwriting losses in recent years, with a combined ratio of 107% for FY2020, and 114% for FY2019. The underwriting losses reflected both an increase in large claims and significant pool claims the club has seen in the last couple of years. We expect West's underwriting performance will deteriorate in FY2021, given that pool claims at half-year were at a record high. We expect West will record a combined ratio close to 115% in FY2021, improving to 110% year-end FY2022.

Chart 1

West 's Underwriting Portfolio Should Improve After A Series General Increases



Source: S&P Global Ratings. f--S&P Global Ratings' forecast.  
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**Financial Risk Profile: Strong**

Under our capital model, we expect that West will maintain capitalization in excess of our 'AAA' confidence level over the next two-to-three years. However, we expect the amount of surplus to reduce, since the club is likely to record losses in the next years due to underwriting losses and reduced investment returns due to low interest rates. We expect West's underwriting result will be in line with, if not better than, the IG average.

The structure of West's investment portfolio is similar to its IG peers': over 80% comprises cash or bonds. The sale of West's premises (Tower Bridge Court) in 2018 helped to derisk the portfolio while reducing currency exposure.

West has no debt and strong liquidity. Like its IG marine mutual peers, it has a legally enforceable right to collect unlimited additional premiums on its mutual P&I business. While West, like other clubs, receives credit for this ability in its Solvency 2 capital calculation, we do not give explicit credit for this in our capital model. Nevertheless, West's ability to make unbudgeted calls is a significant factor in our choice of the 'a-' anchor.

As a member of the IG, West is also exposed to potential volatility in its results through other clubs' pool claims, which can have a significant impact on its earnings. However, West's pool loss ratio has been consistently below 100% over past few years, so that it is now one of just one of five clubs in a net credit position. This will help reduce volatility in

its earnings. We do note, however, that West provided two large claims to the pool in 2020, which may weaken its position in future years.

We view West's risk management capabilities as appropriate, given its size, relatively simple structure, and focus on marine insurance.

## Other Key Credit Considerations

### Governance

West benefits from well-articulated risk tolerances, the expertise of an experienced management team, and good knowledge transfer across the organization.

### Liquidity

We regard West's liquidity profile as exceptional, reflecting the absence of confidence-sensitive liabilities, near-term refinancing concerns, or rating triggers.

## Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- Criteria | Insurance | Property/Casualty: Assessing Property/Casualty Insurers' Loss Reserves, Nov. 26, 2013

## Related Research

- Difficult Decisions Lie Ahead For Protection And Indemnity Mutuals At The 2021 Renewal, Oct. 21, 2020

## Appendix

### West of England Ship Owners Mutual Insurance Association (Luxembourg)--Credit Metrics History

	--Fiscal year end Feb. 20--	
	2019	2018
S&P Global Ratings' capital adequacy	Excellent	Excellent
Total invested assets	718,623.0	704,320.0
Total shareholder equity	338,147.0	306,373.0
Gross premium written	228,186.0	219,726.0
Net premium written	187,388.0	181,080.0
Net premium earned	181,755.0	181,080.0

Reinsurance utilization (%)	17.9	17.6
EBIT	32,667.0	2,575.0
Net income (attributable to all shareholders)	31,481.0	(676.0)
Return on revenue (%)	1.7	(5.5)
Return on assets (excluding investment gains/losses) (%)	0.4	N/A
Return on shareholders' equity (%)	9.8	(0.2)
Property/casualty: Net combined ratio (%)	106.9	113.8
Property/casualty: Net expense ratio (%)	20.7	20.1
Property/casualty: Return on revenue (%)	1.7	(5.5)
Net investment yield (%)	2.3	2.2
Net investment yield including investment gains/(losses) (%)	6.4	4.1

N/A--Not available.

### 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-/bbb	bb-/bb+	b+/b
<b>Satisfactory</b>	a	a/a-	<b>a-/bbb+</b>	bbb+/bbb	bbb/bbb-	bbb-/bbb	bb+/bb	bb-/bb+
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bbb	bbb-/bbb	bb+/bb	b+/b
Weak	bbb+/bbb	bbb/bbb-	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb
Vulnerable	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb	bbb-/bbb

**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 November 30, 2020)\*

#### Operating Company Covered By This Report

#### West of England Ship Owners Mutual Insurance Association (Luxembourg)

#### Financial Strength Rating

Local Currency

A-/Stable/--

#### Issuer Credit Rating

Local Currency

A-/Stable/--

#### Domicile

Luxembourg

\*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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