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The United Kingdom Mutual Steamship Assurance Association (Bermuda) Ltd.

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The United Kingdom Mutual Steamship Assurance Association (Bermuda) Ltd.

SACP* Assessments				SACP*		Support		Ratings
Anchor	a	Modifiers	0	a		0		Financial Strength Rating
Business Risk	Strong	ERM and Management	0	Liquidity	0	Group Support	0	A/Stable/--
Financial Risk	Strong	Holistic Analysis	0	Sovereign Risk	0	Gov't Support	0	

*Stand-alone credit profile.
See Ratings Detail for a complete list of rated entities and ratings covered by this report.

Rationale

Business Risk Profile: Strong

- International Group of P&I Clubs (IG) membership provides market access.
- Second-largest IG member by owned tonnage and premium.
- Longstanding relationships with members.
- Improved operating performance.
- Exclusive focus on marine lines.

Financial Risk Profile: Strong

- Extremely strong capital adequacy, which is a key strength to the rating.
- A more stable technical profit since 2010.
- Exceptional loss record on the pool, and hence a low pool share compared to the club's market share by premiums.
- Conservative reserving.
- Low interest coverage, which limits our financial flexibility assessment.
- Underlying strong financial flexibility due to the United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd.'s ability to make supplementary calls on members.

Other Factors

- We have elected to assign the higher of the two anchor ratings implied by our assessments of the club's business and financial risk profiles to reflect the club's underlying financial flexibility.

Outlook: Stable

The stable outlook on United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd. (the U.K. Club) reflects our view that the club's capital adequacy will remain in the 'AAA' range. In addition, we expect the club's underwriting performance to remain on a par with a recent strengthening and stabilization through February 2017–February 2019. We anticipate that the club's conservative reserving, reinsurance program, and smaller share of the IG pool will serve to stabilize the results that enhanced underwriting standards have improved in recent years.

Downside scenario

We could take a negative rating action should the club revert to its former pattern of unstable results more than two years in a row or should capitalization, as measured using our model, fall below the 'AAA' range.

Upside scenario

We do not consider an upgrade to be likely over the two-year rating horizon. The competitive dynamics of the protection and indemnity (P&I) sector, and the fact that the club already enjoys the highest assessment for capital and earnings under our criteria, serves to limit rating upside.

Base-Case Scenario

Macroeconomic Assumptions

- Global shipping companies, and drybulk and containership operators in particular, will continue to face difficult operating conditions over the coming year, characterized by fragile demand and chronic structural oversupply in the industry.
- Shipping charter rates will remain at break-even or below operating costs in the drybulk and container industry segments.
- Neither the IG pool structure or the pool sharing methodology will change significantly.
- Increased capacity in the reinsurance markets will continue to have a positive impact on IG group reinsurance and retention protection premium and terms.
- Competition will continue to increase in the fixed premium business.

Company-Specific Assumptions

- Capital adequacy will remain within the 'AAA' range.
- The club will retain a leading position among the IG Clubs.
- Premiums will decrease slightly by up to 1% in February 2017. Thereafter, we expect growth to be modest, at around 1%-2% annually.
- The net combined ratio will be just below 105% for February 2017, and about 102%-105% in February 2018 and February 2019, assuming that there are no reserve releases and claims are not abnormally high. (Lower combined ratios indicate better profitability. A combined ratio above 100% signifies an underwriting loss.)
- Net income will be up to $5 million for the financial year ending February 2017, $5 million-$10 million for financial 2018, and around $5 million for financial 2019.
- Investment returns will be $20 million-$25 million in February 2017–February 2019.
- Interest coverage will stay at around 2x, before any mutual discount. We do not assume any reserve releases in our forecasts.

Key Metrics

	--Financial year ending 20 February--				
(Mil. $)	**2018f**	**2017f**	**2016**	**2015**	**2014**
Gross written premiums	396	390	394	408	396
Net income from ordinary activities	6.5	3.3	1.7	25.4	30.1
Combined ratio (%)	102-103	103-104	91.6	104.7	102.3
Capital adequacy	Extremely Strong	Extremely Strong	Extremely Strong	Extremely Strong	Extremely Strong
Free reserves (inc. Hybrid)	557	550	547	548	528
Free reserves (exc. Hybrid)	458	451	448	449	430
EBITDA fixed charge coverage (x)	1.8	1.1	2.3	(1.2)	1.87
EBITDA fixed-charge coverage including realized and unrealized gains/(losses) (x)	1.9	1.4	2.3	3.7	5.4

f--S&P Global Ratings base-case forecast. N.M.--Not meaningful. Forecasts including fixed charge coverage ratios do not assume reserve releases.

Company Description

The United Kingdom Mutual Steam Ship Association (Bermuda) Ltd. and the U.K.-based The United Kingdom Mutual Steam Ship Association (Europe) Ltd. comprise the U.K. Club, which has licensed branches in Japan, Singapore, and Hong Kong. We assess the club on a consolidated basis. The two underwriting entities have the same rating.

The U.K. Club is a member of the IG, an association of 13 mutual clubs, which between them write 90% of global P&I business. IG members benefit from a joint excess-of-loss reinsurance program and from the pooling of risks. If a member incurs large claims, it may access the pool for funds to settle those claims, but will then have to repay those amounts to the pool over time. The U.K. Club did not use this facility in either 2015 or 2014, and therefore its pool share will decrease further (see "Risk position" section below).

The U.K. Club is one of the largest IG members, insuring 135.3 million gross tonnage (gt) of shipping at February 2016. The club is owned by its participating mutual members, although it also writes fixed-premium business (15% of total premiums at February 2016) to members and non-members. The club is managed by Thomas Miller (Bermuda) Ltd., in which it owns a 15% stake.

Business Risk Profile: Strong

Insurance industry and country risk

We assess the industry and country risk for the U.K. Club as intermediate (3; on a scale of 1 to 6, where 6 is the highest risk), reflecting the ratings on the global marine P&I sector. The overall country risk assessment is low because the insurers operating in this sector typically write business in multiple countries around the world, resulting in high geographic diversification. Our industry risk score is moderate; although we see profitability and product risk as negative, these factors are offset by the sector's operational barriers to entry.

The mutual marine sector is less focused on profitability than other sectors and is more exposed to high-risk assets than other non-life insurers, increasing earnings volatility. The size and frequency of claims are also unpredictable, increasing product risk. We do not expect our assessment of country and industry risk to change over the next two years.

Table 2

The United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd. Insurance Industry And Country Risk (IICRA)

Sector	IICRA*	(%)
Global protection and indemnity	3	100

*On a scale of 1 to 6; 1 is the lowest risk.

Competitive position

The U.K. Club's membership of the IG is a key part of our assessment of its competitive position. Historically, non-IG players and fixed-premium providers have enjoyed limited success in the sector.

We consider the U.K. Club's competitive position to be strong, although entirely concentrated within the marine sector. As the second-largest P&I club by premium and owned tonnage in February 2016, its competitive strengths and weaknesses largely mirror those of the P&I sector, described above.

In line with the difficult market conditions that ship-owners are facing, the U.K. Club has reduced its growth target to maintain its market share at a minimum. At the February 2016 renewal date, the club's premium remained flat with a general increase of 2.5% announced October 2015. However, tonnage growth over the year was around 6%, which was ahead of market growth of 3.7% (source: Clarksons' forecast).

We consider that market confidence in the club has improved the quality of business in recent years. The club obtained what we consider to be good-quality entries at 2016 renewal, which demonstrates market support for the club's strategy of stable growth. In addition, commitments to the business pipeline at 2016 renewal were considerably greater than in previous years, despite market conditions. The pipeline consists of new entries that members have committed to the club, such as new builds or ship acquisitions.

Under our base-case scenario, we expect a decrease of about 1% in premiums in February 2017, reflecting fierce competition in the fixed-premium business and the churn effect--that is, that members scrapping older ships and replacing them with new ships, which are associated with lower risks and so attract lower premiums. We expect growth to be modest after February 2017, of 2% at most annually.

Table 3

Competitive Position					
	2016	**2015**	**2014**	**2013**	**2012**
Gross premiums written (GPW)	393.6	408.1	397.1	360.2	360.5
Change in GPW	(3.6)	2.8	10.2	(0.1)	(1.2)

Financial Risk Profile: Strong

Capital and earnings

We assess the U.K. Club's capital and earnings as very strong and a key strength of the rating. The club's current capitalization, as assessed using our capital model, is extremely strong (at the 'AAA' level), supported by a conservative reserving record. Our assessment is, however, limited to very strong due to the club's relatively small capital base in the context of our ratings on insurers.

Table 4

The United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd. Capital					
	2016	**2015**	**2014**	**2013**	**2012**
Free reserves (including hybrid)	547	548	528	494	486
Free reserves (excluding hybrid)	448	449	430	394	386

The club recorded net income of $1.7 million in financial 2016, mainly due to $26 million of underwriting income, on the back of a combined ratio of 91.6%. Income before hybrid capital interest and mutual premium discount was $17.5 million. The combined ratio benefited from $40 million of reserve releases, equating to a 13 percentage-point benefit.

Since 2010, the U.K. Club has been working to improve the quality of its book, and we view its efforts as positive. We believe that underlying profitability has improved due to the loss of members with poor claims records. Additionally, the club has refused to quote on a significant proportion of business (around 20%-25% of quotes by gt) over the past three years, owing to its stricter underwriting criteria. The club's average combined ratio for the previous six years was around 100%, and no individual year exceeded 105%. We consider this to be strong evidence that future returns will move within a narrower band than they have in the past.

On the other hand, similar to its peers, the club recorded a negative investment return of 1.4% in February 2016. This equates to a $16 million investment loss, of which $10 million was due to foreign exchange losses.

Our base-case scenario assumes a net combined ratio of just below 105% for February 2017 and about 102%-105% in February 2018 and February 2019, assuming that there are no reserve releases and claims are not abnormally high.

Factoring in the club's lower contributions to the IG pool in the future (see "Risk position" section below), our base-case scenario predicts that the U.K. Club will produce a post-tax surplus of up to $5 million for financial 2017, $5 million-$10 million for financial 2018, and around $5 million for financial 2019. These returns will likely be supported by a strong reserving record.

Table 5

The United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd. Earnings

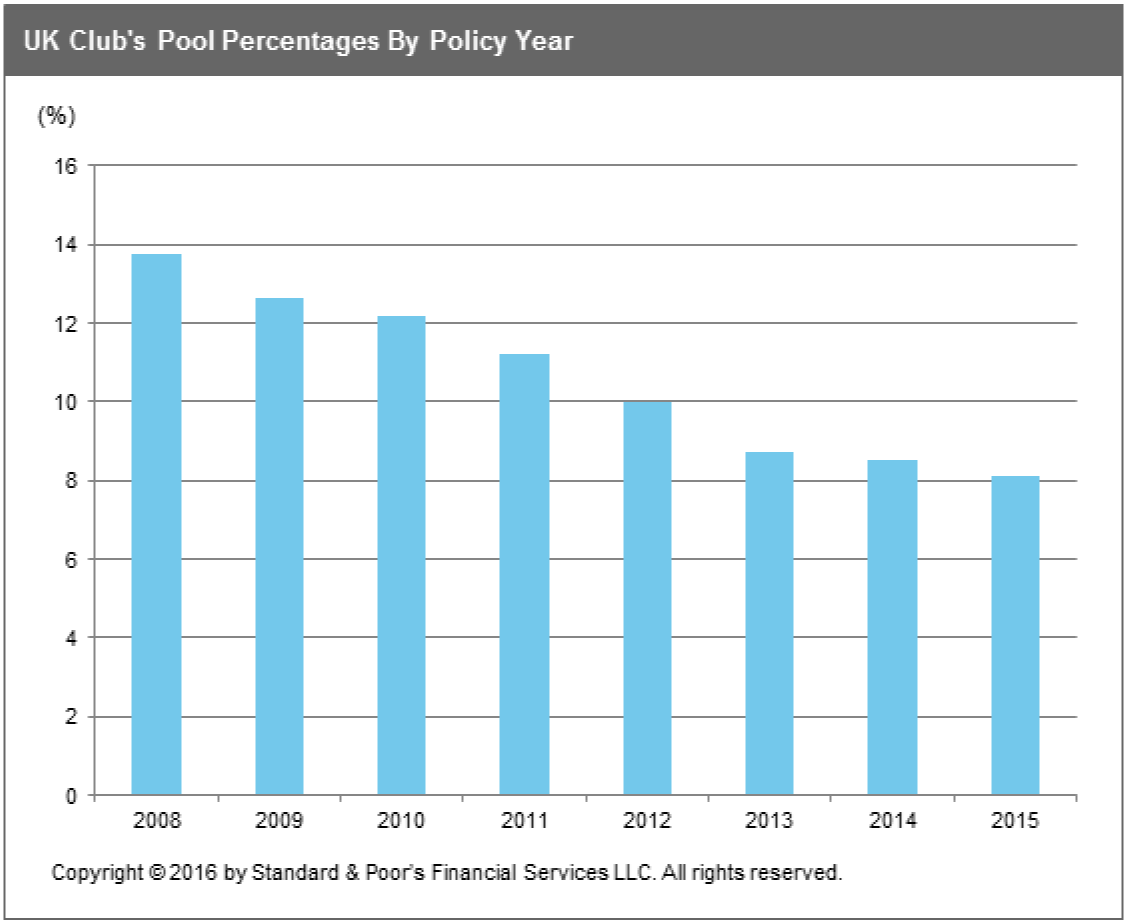
	2016*	2015	2014	2013	2012	Five-year std. dev. % (sample)
Net income (including other comprehensive income)	(1.2)	19.1	35.9	7.6	7.5	
Expense ratio	14.8	13.8	13.5	14.7	13.6	0.61
Loss ratio	79.4	90.9	88.8	92.5	83.9	5.38
Combined ratio	94.1	104.7	102.3	107.2	97.5	5.32

*Without including mutual premium discounts, the expense ratio would be 14.0%, loss ratio would be 77.6%, and the combined ratio would be 91.6%.

Risk position

We regard the club's risk position as intermediate, under our criteria. This primarily reflects the club's improved management of the volatility inherent in the marine P&I sector. The club's membership has been refined, reinsurance protection strengthened, and the expense base controlled. The Club's exceptional pool record--a projected $137 million credit balance and approximate savings of $12 million due to pool credit--and changes to the pool cost-sharing formula have reduced the pool percentage each year. The club's share of the IG pooling arrangement is now considerably lower at 8.1%, compared to 11.2% in 2011 and 13.7% in 2008 (see chart 1). Pool claims are large and unpredictable, so a smaller share of the pool reduces the club's claims volatility. This also aids the predictability of premium requirements.

Chart 1



In our view, the U.K. Club has some degree of market risk in its balance sheet from equities (around 20% of the February 2016 portfolio). However, investment risk is relatively low in the context of the club's available capital. Concentration risk is low and credit risk is fairly low, given that club invests in bonds with 'A' ratings or higher. In addition, the club has no remaining exposure to absolute return funds.

The club holds hedges to cover sterling management fee payments as its income is mainly in U.S. dollars. Hedges hold through to 2016 and most of 2017.

Financial flexibility

We believe that the club's financial flexibility is greatly enhanced by its ability to levy premium increases and make supplementary calls on its members. The club has a legally enforceable right to collect unlimited additional premiums on its mutual P&I business by making unbudgeted supplementary calls on open policy years--a right it last used in 2009 and which it has the ability to use again. Moreover, the club, unlike its peers, has a positive track record of raising debt capital. Therefore we view the underlying financial flexibility of the club to be at least as strong as other clubs within the International Group.

Nevertheless, we view financial flexibility as less than adequate. This assessment is triggered by the club's relatively low fixed-charge coverage. Our base-case EBITDA forecasts suggest coverage ratios of 1.5x-2.0x (before any mutual discount) over the financial years February 2017–February 2019. The club's debt comprises a $100 million hybrid issue (rated 'BBB+'), which accrues interest at 7.5% until August 2018.

Table 6

The United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd. Risk Position

	2015	2014	2013	2012	2011
Total assets	1,166	1,182	1,219	1,184	1,197
Bond investments (%)	64.88	72.78	66.7	61.8	66.0
Equity investments (%)	27.63	23.09	26.1	28.4	20.8
Cash investments (%)	7.48	4.13	7.2	13.4	13.2

Table 7

The United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd. Financial Flexibility

	2016	2015	2014	2013	2012
EBITDA fixed-charge coverage including realized and unrealized gains/(losses) (x)	1.4	4.6	5.4	1.9	1.9

Other Assessments

The combination of the club's enterprise risk management (ERM), and management and governance scores, leaves the 'a' anchor unchanged.

Enterprise risk management: Adequate

Our assessment of the club's ERM as adequate reflects our view that ERM is of low importance to the ratings, given the club's size, relatively simple structure, and focus on one line of business.

We consider that the club has adequate risk controls for its main risks--underwriting, reserving, and investment risk. We consider that the club's ERM framework is now well developed as it aligned with Solvency II (SII) requirements.

We assess the club's risk management culture as neutral. The club has developed a risk appetite framework and implemented a partial internal capital model that has been approved by the Prudential Regulation Authority for the U.K. entity. This has allowed for a more robust and transparent relationship between total capital and pricing adequacy, which forms a key part of the decision-making processes for risk and capital management.

The club has appropriate underwriting guidelines and the use of a pricing model is now common practice within the club. The reserves are regularly reviewed by integral and external actuaries. The club's size enables regular feedback and communication between the claims and underwriting teams.

The club has clear predetermined limits for asset allocations. The investment portfolio is actively managed within the broad parameters allowed by the investment policy that the board established.

The club manages its capital based on different capital measures (the Bermuda Monetary Authority's, SII, and S&P Global Ratings') and allows for an explicit buffer on top of the regulatory requirements as part of its risk tolerances.

Management and Governance: Strategy is clear and consistent with marketplace conditions

We view the club's management and governance as satisfactory.

The club's strategic plan focuses on maintaining underlying underwriting discipline. Growth targets are modest and in line with market growth.

The club's senior management team is stable and composed of individuals with vast experience in the sector. The club's management is capable of implementing its strategy, and the club's strong position in the P&I market should enable its strategic objectives. Since the supplementary call of 2008-2009, management has rebuilt the reputation and technical performance of the club.

Liquidity: Exceptional

We regard the U.K. Club's liquidity profile as exceptional; an assessment that is enhanced by the absence of confidence-sensitive liabilities, near-term refinancing concerns, or rating triggers. We do not regard liquidity as a restraining factor in the rating.

Accounting Considerations

We treat payments into the pool as ceded reinsurance premiums, as opposed to gross claims incurred. This treatment is based on the mutual reinsurance mechanism that this agreement provides for the IG.

Related Criteria And Research

- Group Rating Methodology, Nov. 19, 2013
- Insurers: Rating Methodology, May 7, 2013
- Enterprise Risk Management, May 7, 2013
- 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
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008

Ratings Detail (As Of May 26, 2016)	
Operating Company Covered By This Report	
The United Kingdom Mutual Steamship Assurance Association (Bermuda) Ltd.	
Financial Strength Rating	
Local Currency	A/Stable/--
Counterparty Credit Rating	
Local Currency	A/Stable/--
Junior Subordinated	BBB+
Domicile	Bermuda

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's 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.