Research Update:

Norwegian Hull Club Affirmed At 'A' Under Revised Criteria; Outlook Stable

July 23, 2019

Overview

- Norwegian Hull Club (NHC) has an established position in marine hull and loss-of-hire insurance. Its strong profit record has enabled it to build up exceptionally strong capital adequacy.
- At the same time, NHC has a narrow product focus and a capital base that is small in absolute terms.
- We are affirming our 'A' financial strength and issuer credit ratings on NHC following a change in our criteria.
- The stable outlook reflects NHC's consistent profit record, which in our view means that it is likely to maintain its extremely strong capital position.

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Rating Action

On July 23, 2019, S&P Global Ratings affirmed its 'A' long-term insurer financial strength and issuer credit ratings on Norwegian Hull Club (NHC; see the ratings list below for further details). The outlook is stable.

The affirmation follows a review of NHC under our revised criteria "Insurers Rating Methodology," published July 1, 2019, including an assessment of the club's year-end 2018 results.

Outlook

The stable outlook signifies that NHC has differentiated its operating performance from that of its peers through the strength of its brand and its business mix. We anticipate that the club will maintain its capital adequacy above the confidence level we expect of a 'AAA' rated entity, according to our risk-based model. We also expect the club to maintain its premium reputation in the market and to expand its premium base conservatively over the next three years.

Downside scenario

We could lower the ratings on the club if its results were to be more volatile than we currently expect, or if its risk-based capital adequacy falls significantly and persistently below our 'AAA' level in our model. We could also lower the ratings if we consider NHC unlikely to sustain its peer-leading profitability, with an average combined ratio below 95% for 2018-2020. A combined ratio below 100% signifies an underwriting profit.

Upside scenario

A positive rating action is unlikely over the next two years. It would depend on the club substantially increasing its scale and diversity while not diluting its operating outperformance.

Rationale

The rating on NHC reflects its leading position as a provider of a wide array of marine insurance products and its competitive advantage in key marine markets, as demonstrated by its sector-leading underwriting results in hull insurance. NHC's robust capitalization and profitability are a key strength of the rating. Despite NHC's relatively high proportion of investment in high-risk assets, we see limited capital volatility arising from nonunderwriting activities. However, we view as a credit weakness the club's relatively small capital base, which makes it more vulnerable to single-event losses.

NHC holds a specialist position in the marine market, where it offers high-end loss-prevention solutions, and has the capacity to lead claims. These strengths have enabled the club to price at the top end of the market and have contributed to its strong average five-year combined ratio (loss and expense) of 94%. NHC's member retention rate has remained above 90% despite unfavorable market conditions in the shipping industry. The company also has a very geographically diverse client base, which we view as a positive, although its product and risk diversity are limited. That said, the club is well-diversified within marine and marine-related lines compared with its peers, and has ventured into new product areas such as cyber risk, special risk, and kidnap and ransom.

We forecast that NHC will maintain capital adequacy in excess of our 'AAA' level of confidence over the next two-to-three years. We expect the club's premiums to increase about 5% per year over 2019-2021, reflecting budgeted rate increases. On the back of positive claims developments and underwriting discipline, we forecast an average combined ratio of 95% over the next two-to-three years.

We estimate strong earnings of $14 million-$16 million over 2019-2021, due to strict control over underwriting. However, the club's capital position could fluctuate because of its narrower product portfolio, relatively small size of capital in absolute terms, and relatively high proportion of high-risk assets, even though a major proportion of its investments is in bonds and cash.

We anticipate that investment returns in 2019-2021 will remain constrained, with investment yields of about 2% due to low interest rates.

Ratings Score Snapshot

Business Risk Profile	**Strong**
Competitive position	Strong
IICRA	Intermediate risk
Financial Risk Profile	**Strong**
Capital and earnings	Very strong
Risk exposure	Moderately high
Funding structure	Neutral
Anchor*	A
Modifiers	
Governance	Neutral
Liquidity	Adequate
Comparable ratings analysis	0
Financial Strength Rating	A

*This is influenced by our view of the club's capital strength, niche specialism, and profit record.

Related Criteria

- Guidance | Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Norwegian Hull Club, Aug. 30, 2018

Ratings List

Ratings Affirmed	
Norwegian Hull Club	
Issuer Credit Rating	A/Stable/--
Financial Strength Rating	A/Stable/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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