Research Update:

Oil Insurance Ltd. 'A' Ratings Affirmed; Outlook Remains Stable

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Overview

- Oil Insurance Ltd. (OIL) has a longstanding reputation in the energy industry as a provider of stable insurance capacity, with strong balance-sheet strength and a unique retrospective pricing plan, which offset underwriting losses.
- We are affirming our 'A' financial strength and issuer credit ratings on OIL.
- The stable outlook reflects our view that the company will sustain its competitive position in the energy industry and maintain significant capital redundancy at the 'AAA' confidence level.

Rating Action

On Sept. 24, 2019, S&P Global Ratings affirmed its 'A' financial strength and issuer credit ratings, as well as its 'BBB+' issue-level rating on Oil Insurance Ltd.'s preferred stock. The outlook remains stable.

Outlook

The stable outlook reflects S&P Global Ratings' view that OIL will sustain its competitive position in the energy industry with a relatively stable membership base while it continues to enhance its value to its members, and maintain substantial capital redundancy at the 'AAA' confidence level through 2021, supported by stable operating earnings.

Downside scenario

We could lower the ratings in the next 24 months if, contrary to our expectations:

- Capital adequacy deteriorates on a sustained basis such that the company is unable to maintain sufficient redundancy at the 'AAA' confidence level to absorb stressed underwriting and investment-related losses; or
- There are significant departures from OIL's membership base, which could undermine its

longstanding reputation in the energy industry as a provider of stable insurance capacity with an attractive value proposition.

Upside scenario

We are unlikely to raise the ratings in the next 24 months. While OIL enjoys an excellent financial risk profile supported by robust capitalization, its competitive position is somewhat limited and mostly focused on the energy sector.

Rationale

OIL's competitive position is anchored by its longstanding reputation in the energy industry as a provider of stable insurance capacity. OIL is a mutual insurance company and its competitive advantage lies in its comprehensive product offering, inclusiveness of assets covered, and its large line sizes. Members find OIL's product offering compelling and use it as a cornerstone capacity. OIL has 55 members; 78% of them have been with the company for more than 14 years. In 2018-2019, the company made further progress on its five-year strategic plan, including offering coverage for renewable energy, cyber wrap products, and increasing its visibility in targeted markets and sectors within the broader energy industry. We believe an effective execution of the strategic plan will enhance OIL's value proposition to its members. However, the company's sole exposure to the energy industry and its limited product profile partially offset our view of its competitive position.

OIL has robust risk-adjusted capital adequacy that is significantly redundant at the 'AAA' confidence level as of year-end 2018 and we expect it to remain so through 2021. The company's capital management plan is aligned with its underwriting portfolio, which is materially exposed to severity risk, as reflected in its volatile underwriting performance. Over the past three years, the combined ratio has averaged about 151%. Nevertheless, the company's retroactive premium plan allows OIL to recoup losses from its members through premiums over a five-year period, providing means to eliminate capital erosion due to underwriting losses. Furthermore, OIL pays large dividends to maintain its capitalization in line with its internal target levels. In 2018 and 2019, the company paid dividends of $450 million and $250 million, respectively. The dividend helps members to offset their increasing premium costs. In our view, OIL maintains a neutral funding structure with financial leverage of about 10% and fixed-charge coverage in excess of 4x.

We view OIL's risk exposure as moderately low, predicated on the company's robust capitalization, its ability to retroactively price its members for all of its underwriting losses, and its adequate risk management practices. OIL's business model is substantially exposed to investments and counterparty credit risks. The company has a relatively large appetite for investments in risky assets, with approximately 48% of its investments in common stocks and alternative investments. This, in our view, can lead to material volatility in its capital and earnings. However, we expect the company's robust capitalization to withstand any such potential volatility. The company's counterparty credit risk arises from its members and if members have any financial difficulties paying their premium dues to OIL. This risk is offset by capital charges for credit risk related to the theoretical withdrawal premiums (the amount members owe immediately if they leave OIL). In addition, the company has robust member eligibility criteria that include a minimum credit rating, track record of sound financial metrics, etc. As of Dec. 31, 2018, an overwhelming majority (80%) of the company's members are rated investment-grade ('BBB-' and higher) and about 20% are rated 'A-' or higher. Overall, we believe the company has adequate risk controls related to investments or counterparty credit risks, which allow it to limit its losses within its risk limits.

The rating on the preferred shares is two notches below the issuer credit rating, reflecting one notch each for subordination and other for deferral.

Ratings Score Snapshot

Business Risk Profile	Satisfactory
Competitive position	Satisfactory
IICRA*	Intermediate
Financial Risk Profile	**Excellent**
Capital and earnings	Excellent
Risk exposure	Moderately Low
Funding structure	Neutral
Anchor	A
Modifiers	
Governance	Neutral
Liquidity	Exceptional
Comparable ratings analysis	0
Financial Strength Rating	**A**

*Insurance Industry And Country Risk Assessment.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- 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

Ratings List

Ratings Affirmed	
Oil Insurance Ltd.	
Issuer Credit Rating	
Local Currency	A/Stable/--
Financial Strength Rating	
Local Currency	A/Stable/--

Ratings Affirmed	
Oil Insurance Ltd.	
Preferred Stock	BBB+

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.