

FITCH AFFIRMS NAVY MUTUAL AID ASSOCIATION'S IFS RATING AT 'A+'

Fitch Ratings-Chicago-25 July 2017: Fitch Ratings has affirmed Navy Mutual Aid Association's (Navy Mutual) Insurer Financial Strength (IFS) rating at 'A+'. The Rating Outlook is Stable.

KEY RATING DRIVERS

Navy Mutual's IFS rating and Stable Outlook reflect the association's very strong capitalization, good profitability and very strong investment profile. The ratings also consider the company's small market position and scale along with its interest-sensitive product profile.

Navy Mutual has a solid niche position as a low-cost provider of insurance protection products to United States Sea Service members and their families. However, Navy Mutual remains one of the smallest companies in Fitch's rating universe, and its relative size could heighten the impact of unexpected adverse scenarios.

Navy Mutual maintains very strong capitalization with an RBC ratio of 526% and a Prism capital model score of 'Extremely Strong' as of Dec. 31, 2016. The company's total adjusted capital (TAC) increased almost 2% to \$306 million during the first quarter of 2017, which was primarily driven by unrealized investment gains. The company has no financial leverage and very low operating leverage at 9.0x at year-end 2016.

Fitch views the company's profitability as adequate and in line with mutual peers, given its strategy of distributing excess earnings to its members through relatively high crediting rates and policyholder dividends. The company targets a level of profitability that maximizes value to its members while supporting new business growth and providing a cushion against unexpected losses. While prolonged low interest rates continue to pressure Navy Mutual's earnings, Fitch believes the company effectively manages this rate risk through product design, pricing, actively managed duration and liquidity management.

Navy Mutual has one of the most conservative investment portfolios in Fitch's universe with below-investment-grade bonds making up a modest 2% of fixed income assets, all comprising fallen angels. The company also has below-average exposure to 'BBB'-rated bonds, thus subjecting it to less credit risk than the industry. Total risky assets, which include below investment-grade bonds, lower quality real estate, unaffiliated common stock and Schedule BA assets, in relation to TAC remains exceptionally low at 40% compared with an industry average of 80%. Overall, Fitch views Navy Mutual's investment profile as very strong.

RATING SENSITIVITIES

Fitch does not anticipate an upgrade in the intermediate term, as Navy Mutual's small scale and narrow market focus limit the upside in its rating.

Key ratings triggers that could result in a downgrade include:

- A decline in estimated RBC to below 400% company action level or a Prism capital model score below 'Extremely Strong';
- A spike in investment-related losses or a trend of sustained net operating losses;
- A significant change in war risk exposure and experience;
- An unfavorable change in tax/regulatory status.

Fitch affirms the following rating with a Stable Outlook:

Navy Mutual Aid Association
--IFS at 'A+'.

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Applicable Criteria
Insurance Rating Methodology (pub. 26 Apr 2017)
<https://www.fitchratings.com/site/re/897260>

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