

RATING ACTION COMMENTARY

Fitch Affirms Navy Mutual's Ratings; Outlook Stable

Wed 23 Nov, 2022 - 1:55 PM ET

Fitch Ratings - Chicago - 23 Nov 2022: Fitch Ratings has affirmed Navy Mutual Aid Association's 'A+' (Strong) Insurer Financial Strength (IFS) Rating. The Rating Outlook is Stable.

KEY RATING DRIVERS

Conservative Operating Profile: Navy Mutual is a low-cost provider of life insurance protection products to the U.S. uniformed servicemembers and their families. Navy Mutual's product liabilities are comprised primarily of interest-sensitive whole and term life policies that exhibit more predictable cash flow characteristics and lack the volatility of variable products. New sales consist primarily of term and participating permanent life products, which have a more favorable risk profile compared with the company's legacy products.

Small Scale and Narrow Focus: Navy Mutual serves a unique market niche with a narrow customer base and has a modest operating scale relative to the broader life insurance market. Rating considerations also include Navy Mutual's limited access to capital markets and the long-term challenge of membership growth due to its niche customer focus.

Very Strong Capitalization: Navy Mutual's rating reflects its very strong capitalization on both risk and nonrisk-adjusted measures, demonstrated by an RBC ratio of 465% at YE 2021 and a Prism capital model score of 'Extremely Strong' based on YE 2021 data. The company has no financial leverage and had very low operating leverage of 8x at YE 2021.

High-Quality Investment Portfolio: Navy Mutual continues to have one of the most conservative investment portfolios in Fitch's universe, as the company continues to maintain limited exposure to asset classes Fitch views as riskier. The company's risky assets ratio — defined as below-investment-grade bonds, lower quality real estate, unaffiliated common stock and Schedule BA assets — divided by total adjusted capital (TAC), was to 71% at YE 2021, which compares below the industry.

Adequate Earnings: Navy Mutual's profitability trails the industry, but is considered in line with mutual companies, and is viewed as adequate given its strategy of distributing excess earnings to 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.

Prudently Managed Reserves: Fitch believes that Navy Mutual's "war risk" is prudently managed and that mortality experience remains within expectations. The company has not currently experienced material adverse mortality with regards to the coronavirus pandemic, as overall mortality among policyholders is manageable and policies affected tend to be older and well reserved.

Macroeconomic Uncertainty: Growing macroeconomic volatility and the heightened probability of a recession could constrain earnings growth, although Fitch does not expect a material impact to Navy Mutual's earnings outside of a prolonged or severe recession.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--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.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A decline in estimated RBC to below 400% company action level or a Prism Capital Model Score below 'Extremely Strong';

--A trend of sustained net operating losses;

--A significant change in war risk exposure and experience;

--An unfavorable change in tax/regulatory status.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY / DEBT ↕	RATING ↕	PRIOR ↕
Navy Mutual Aid Association	Ins Fin Str A+ Rating Outlook Stable Affirmed	A+ Rating Outlook Stable

[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[Insurance Rating Criteria \(pub. 15 Jul 2022\) \(including rating assumption sensitivity\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Prism U.S. Life Insurance Capital Model, v1.3.1-2021 (1)

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Navy Mutual Aid Association

EU Endorsed, UK Endorsed

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