

Groundhog day as clubs seek to stash renewals cash

Dearer claims and fiercer external forces are leading underwriters to seek higher premiums, writes James Brewer - Friday 2 February 2007

IT might have been the melting of the ice age.

At this point in 2006, P&I providers were negotiating many rates and deductibles agreements with shipowners and charterers that looked to create the foundation to tilt the underwriting back to nice, robust breakeven.

Even the winter weather has been turning warmer.

The Baltic Sea largely flowed freely this season, with hardly a glimpse of white in the sights of icebreakers.

Shipowners ploughed through financially favourable seas to enjoy superb freight rates.

Having mended some leaks in their ancient but sturdy corporate vehicles, it looked as though 2007 could be the year when the P&I bodies could treat their members and clients more cosily.

Group clubs had made an overall net surplus of \$180m, with free reserves climbing to a record \$2.2bn, and only a tiny increase was conceded in the cost of group reinsurance.

Alas! It turns out to be Groundhog Day, the US holiday at the centre of a popular 1993 film. In the movie, a weatherman is sent to track a weather forecasting 'rat' and discovers that it is Groundhog Day again, and again, and again.

He is doomed to be stuck in the same place, seeing the same people do the same thing every day.

Groundhog Day is the US legend when the rodent peeps out of his burrow after his winter sleep to look for his shadow.

If he sees it, he regards it as an omen of more bad weather and scurries back to his burrow.

If the day is cloudy and shadowless, he takes it as a sign of spring and stays above ground.

Now Groundhog Day is February 2, while renewals day for most shipowners — those controlling around 635m gt — is February 20, a tradition dating back to the era when the Baltic Sea was the hub of world shipping, and that was the day ice was expected to give way to navigable conditions.

We can thank broker Gallagher Global Risks for the groundhog analogy.

Going into 2007 renewal, one might be forgiven for thinking that one had been trapped in the set of Groundhog Day, the Gallagher broking team mused recently.

“Once more, the clubs have failed to make a consistent technical surplus and it now seems that this objective is perhaps unrealistic, with an environment of typically low, single-digit general [premium] increases prevailing,” said its P&I Review.

Of course, the mutuals are duty bound to strive for modest surpluses, enough to keep their reserves healthy and reward the management sensibly.

Gone are the days when they could rely on investment income, and all have sworn never to do so again.

Or are those days gone? Any business wants to maximise its income, and naturally the clubs and others have overhauled their investment portfolios in recent years to buffer themselves against volatility.

In each of the last two years, some \$300m was available in total to the mutuals from this source, which were needed to offset underwriting deficits at all but profitable Britannia, Shipowners and Skuld. Hey presto! All but American Club, Japan Club, Swedish Club and West of England are now in the black.

While striving to improve their technical result, club leaders have had to monitor the larger picture.

No sooner do attritional claims come under control, through intensified focus on loss prevention and by the blunter instrument or higher deductibles, than major claims come knocking at the door.

These have put pressure on the pooling system, whereby individual claims figures above \$6m (from February 20, 2007 this will be adjusted to \$7m) are shared, up to a limit of \$50m.

But \$7m is still too low, say the larger clubs, and some want to increase the figure by \$1m a year until it is \$10m in 2010.

That might make the clubs tighten still further their animus against members that have intractable claims records, but it would lead to some of them buying more commercial reinsurance at the lower levels.

Nothing wrong with that, it might appear at first glance, but it erodes mutuality and could lead to over-reliance on reinsurance — something which the insurance market at large has been lectured against for the past decade.

For many, the beauty of the mutual system is that it provides insurance ‘at cost’ and avoids undue exposure to the for-profit sector.

This links with the debate on the degree to which insurers can help exorcise substandard shipping.

In practice this should be outside their remit, but they have a commercial interest in shunning ships with weak infrastructure or management.

One option that has many supporters is doubling the \$7m retention in the event that any club agrees to cover a ship rejected by another on grounds of poor condition.

Claims exposure is to some degree within insurer control, but external threats to stability loom ever larger. In its annual P&I report, HSBC Insurance Brokers was moved to say: “The European Union appears to be seeking to challenge the US as the legal environment that is most hostile to shipowners and their crew.”

This is in the field of criminalisation of shipowners and crews, and in the financial field there is nervousness too.

For liability insurers reporting to European Union jurisdictions, the evolving Solvency II rules which are meant to protect policyholders will bring in as yet unspecified, but certainly tighter capital adequacy requirements.

That means more reserves must be harvested beyond what seemed a reasonable club collective total of \$2bn.

West of England has been the one club unabashedly to ask its members to stump up more cash to ensure it was fortified against such regulatory demands — others claiming to be comfortably positioned already.

On another front, clubs have long been concerned over the introduction of the 2002 protocol to the Athens convention on passengership liability.

This is the year it could become a reality and rekindle the debate about whether to treat such ships as a class apart, given the potentially huge liabilities that could arise from a serious accident on a ship with 5,000 passengers and crew.

From the standpoint of the passengership operators, it can now be argued that other large ship types pose a weighty risk, chiefly LNG carriers and the emerging generation of containerships.

As far as the clubs themselves go, there is keen interest in the development of Gard, which has enjoyed much success through its spread of interest between liability, marine hull and energy insurance, and its officials exude confidence that further measured growth is possible and desirable.

At the other end of the scale, the American Club has a clear need to achieve its targets after a recent bumpy history of calls and a ratings downgrade.

Prospects of any merger deals seem remote again, after the Swedish Club and Skuld romance was scuppered by cautious Swedish Club board members.

Matchmakers have seen a Skuld link with North of England as a runner, but it would be foolish to bet heavily on such a such marriage in the near future.

Outside the International Group of P&I Clubs, the substantial China P&I Club continues to knock at the door, with those inside still debating whether the constitution and operations of the Beijing body are sufficiently similar to allow it to join the mutual party.

China Shipowners Mutual Assurance Association, to accord the full title, appears to meet all or most of the criteria for Group accession, with membership going beyond China to include shipowners in Hong Kong, Singapore and other Asian areas.

While in the small ships category many units have renewal dates other than February, owners will find themselves feted as much as ever in the next few days, with many strong organisations in the market, including Shipowners' Club, British Marine, Navigators, Gard and RaetsClub.

More such ships are being obliged statutorily to take P&I cover — and there are hundreds of newbuildings in prospect over the next few years.

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