

Crying over the loss of cash-full coffers



Remember the honeyed epoch of zero annual rate changes, 10% investment returns, buoyant reserves, and low, low rates from rock-solid reinsurers? Shipowners and charterers are now weeping for that dreamtime of a mere three insurance seasons ago, writes

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Savaged by slumping stock markets and niggled by underwriting results stubbornly the wrong side of the line, P&I organisations are again turning to their members and clients to replenish the coffers.

Failure to do that would push reserves below a level acceptable to the respective P&I outfits, the credit rating agencies and an increasingly picky set of industry financial regulators and commentators.

Those free reserves, amounts uncommitted to outstanding claims which once seemed just like a handy cash-till float, are these days a cushion against insurance market movements and investment upsets.

Without a healthy back-up, clubs have to look to unbudgeted calls.

For that reason boards of directors at mutuals, which cover nine-tenths of world merchant shipping, and at rival facilities that are paid in fixed premiums are being heavy-handed again as they set rate increases for February 20, the key renewal date.

Already they have raised warning flags that they are determined to reverse the descent into loss-making.

Whacked by an average 40% underwriting deficit last time, members of the International Group of P&I clubs especially have cause to take remedial action.

In cold figures this will mean premium rises of anything up to 25%, with or without reinsurance element, and this is for many owners the second year they have taken a belting.

For starters, UK Club, Steamship Mutual and Swedish Club are each seeking 25%; Britannia and Gard 15%; and others are about to announce figures in that range, probably in the upper reaches.

Douglas Jacobsohn, president and chief executive of Skuld P&I, is making it clear that despite this year's increase by clubs premiums are failing to sustain the level of incoming claims.

"This, in addition to the lack of investment income and increased reinsurance costs, will make it necessary for all clubs to increase their premium income," he has said.

"We therefore believe that the industry as a whole will be facing challenges at the coming renewal."

Paul Jennings, underwriting director at North of England P&I, agrees that all clubs will need to consider significant general increases to maintain financial stability.

Cumulative underwriting loss for the International Group of P&I Clubs for the 2001 policy year was \$435m, which led clubs to reduce their free reserves per tonne by up to 45% or make those hated additional calls on members.

So, although premium income passing through the industry is soaring well above the \$2bn-a-year mark, getting the level of free reserves right is more critical than ever because of the risks of failure at reinsurance level, investment setbacks, catastrophe claims, unexpected claims trends and the need to maintain solvency margins.

As usual, Britannia P&I Club has been first out of the starting gate, and opted for a 15% rise in advance calls from February 20 next year.

For many of its members and clients — it covers 86m gt of shipping, of which 67m gt is owned tonnage — the total bill will be higher, especially for tanker operators, because a few extra percentage points will be stirred in to account for the rising cost of group reinsurance.

Question marks will remain over the latter element until the last minute because the contract is unlikely to be concluded until close to the February deadline.

Other clubs are expected to seek rises in the order of 20% or even more for few have as healthy a balance sheet as Britannia, which itself is working towards funding the \$70m it set aside on hopes that its investments would make that kind of contribution. Britannia chairman Sir David Thomson pointed the finger of blame at the international investment climate, and all his counterparts who have to explain shortfalls will concur.

At this stage the clubs and others are being reserved in their comments about reinsurance, but it is clearly worrying them. What happened at Oslo club Skuld P&I over the past year may be typical, and it amounted to an 11% increase.

Skuld, which has 29m gt in owned tonnage among 60m gt in all liability classes, endured a rise of almost \$2m in reinsurance premiums.

That was made up of a 28% increase in the group excess loss contract and an extended reinsurance programme below a pooled retention. Underlining the determined effort at club level to stem the tide, Skuld managed to reduce its half-year deficit to \$4.7m from \$20.4m at the corresponding stage of 2001.

P&I provides the world's largest reinsurance contract for Lloyd's and leading company reinsurers and, under the three-year deal negotiated during the soft market, it was a bargain. The contract is in its dying months and the quest for a continuing deal could produce surprises.

Although the various reinsurers appreciate the good record achieved by P&I, they will be seeking bigger premiums amid shrinking capacity.

The group and its brokers have been grappling with ways of easing the blow, one suggestion being to increase the retention and pool limit, although this would be unpopular with smaller clubs.

It might even contribute to reshaping the market by forcing some clubs to combine for strength.

If reinsurance is worrying for the clubs it will be a headache too for the fixed premium sector, where some operations may have to struggle to buy the right cover.

British Marine, Terra Nova, Intercoastal and a few others are in competition with Shipowners Club among the smaller vessels.

QBE has entered the field this time round for the larger tonnage where other big names, including Axa and Ingosstrakh, have been underwriting selectively.

It has to be said that, while many commercial insurers have tried their hand at P&I provision, their success record is low.

On the mutual front, last time Skuld, the American Club and Steamship had to ask their members for extra cash, the latter needing to initiate a three-year phased programme to repair the accounts to the tune of \$110m.

It looks as though all clubs will again take a tough line and owners with a poor loss ratio will be especially hurt by the new premiums. Charterers, who pay on a fixed premium basis, will face similar increases.

Should owners resist too strongly, that would simply cause chaos and give surviving clubs more power next time round. That was what happened in the early 1990s, when the clubs had to awaken their members to the need for big rises because of weak reserving and rising claims values.

Some 60,000 P&I claims are made every year, and the trouble is that they are getting more expensive.

Adding to the pain this time are dearer charges for hull and machinery policies and dearer war risk premium, which generally covers both hull and P&I but where the primary layers are placed in the general market.

Several thorny problems are irritating the sector beyond the cost of premiums.

As far as war and terror are concerned, club cover is at present remote because of group restrictions.

As market provision becomes more expensive, and the risk possibly more prolific, clubs will have to reconsider whether to re-enter the field, possibly with government support à la Pool Re. Bringing such cover back to the mutual system would need considerable support from the commercial reinsurance market, and perhaps political backing.

P&I providers are among those who have been watching with anxiety the work of the International Maritime Organisation on revising the Athens liability convention on passengers at sea.

While it may take time for a new convention to enter into force, it may lead to further calls for P&I clubs to treat cruiseships, with their already potentially onerous exposure to casualty, as a special case.

Operators might face having to pay a cruiseship premiums supplement, pay towards extra reinsurance or even say goodbye to the mutual system.

London Club, which is without cruiseship members itself, has been among those raising the question most vigorously, while the West of England, which has several interests in the passengership industry, is adamant that an accommodation could, and should, be found.

Can bulk carriers and tankers mutualise risk in a fair way with what in effect are floating hotels?

With a worst-case cruise disaster conceivably producing claims totalling \$5bn, there is a need for the question to be clarified soon.

Most clubs have fortified their own reinsurance arrangements in the past few years to hedge themselves against claims over-runs. It might be argued that this has been a substitute for making extra calls.

The UK Club, which pioneered an alternative risk-style programme backed by Swiss Re, and West of England with a more conventional programme, are among examples. More recently North of England took out a three-year retention insurance programme with Swiss Re.

In the near future the 13 group clubs will have to consider the ambitions of China Shipowners' Mutual Assurance Association to join their ranks.

Visiting London earlier this year, senior delegates from the mutual known for short as China P&I Club signalled their intention to align themselves more closely with the general market. Founded in 1984, the Chinese club has at least 7m gt in entries, including managed foreign flag ships.

More detailed attention is being paid all round to the needs of Far East owners. The clubs have appointed several Asian representatives to board positions and the fixed premium sector senses the region has been insufficiently served by the European-based mutuals.

If there are to be any significant shifts in membership next February from one provider to another this geographical area could turn out to be one of the main battlegrounds.

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