MANAGING DIRECTOR'S SOAPBOX

CLUBS ARE NOW PREDICTABLY REPORTING DIRE UNDERWRITING RESULTS... IS THE POOL REALLY TO BLAME?

Industry players instinctively know when P&I Club results are bad and perhaps even 'finessed'. I cannot recall a year when Clubs' R&As have been so delayed in their issuance! Two Clubs had not released their full audited accounts until well into September, whereas others with better results were released in the Spring as usual.

All Clubs are reporting various degrees of poor underwriting results which are said to be largely attributable to other Clubs' Pool claims (claims in excess of $10mil). Interestingly, the IG has required all Clubs to sign a NDA, to stop Clubs from publicising current and historical results and yet the Clubs' main focus this year is to persuade their membership and indeed the world at large that they need General Increases to address the Pool claims expenditure. There clearly needs to be much greater transparency in this area if members are to embrace their Club(s') issues! Unfortunately Pool claims have increased in value if not necessarily in number. We believe rising Pool claims was entirely predictable, however the total value of Pool claims estimates are arguably only some 25% more than what some Clubs were estimating back in 2004-2006. This is notwithstanding a doubling of the International Group's GT during that time. Ship sizes and their cargo carrying capacities are so much larger today. In addition to Pool claims, claims within the Club's retention, particularly within the abatement layer, are also causing enormous financial stress on Club's underwriting.

UNDERWRITING DISCIPLINE

All Clubs have been competing ferociously with each other for market share (largely funded by their 'AAA' capital 'war chests' of members' free reserves). The ultimate intention being to increase their market share, but not all have been successful in achieving their goals. This has resulted in a 'race to the bottom' in underwriting discipline... unsustainable premium rates and often acceptance of new members with lesser operating standards. Inevitably there have been winners and losers in this race - one leading Club, whose management has arguably been overly focused and distracted by seeking to merge or acquire, has actually seen its market share drop by nearly 50% in a little over a decade and yet has delivered its worst underwriting results over the same period!

In my view, most Clubs have not been sufficiently focused on their responsibility to properly reserve for Pool contributions, largely in their haste to attract new business at unsustainable prices. We regularly witness and hear stories of Clubs underwriting new business at rates that barely cover the General Excess of Loss Reinsurance (claims in excess of $100m). It clearly must therefore follow that premium to cover Pool claims up to $100m must also be totally inadequate. Past IG managers recognised this danger

for tankers and required Clubs to allocate a 'minimum Pool contribution', which perhaps needs to be considered for all ship types. The lower the premium rates charged the more the Pool is deprived of adequate funding.

At Wilson, we have been calling for greater underwriting discipline for a number of years, but greed and short-term gratification of Clubs has often taken priority over sensible commercial prudence. We have witnessed over the last five years shocking underwriting in some Clubs' haste to swap surplus capital for subsidised tonnage growth. This is inevitably at the expense of long-standing traditional Shipowner members. The Shipowners who benefit the most from this approach are the asset players or venture capitalists who have little regard for the P&I system and the loyal members it serves.

By way of recent examples, there have been situations where so-called 'new' fleets (but are actually long-established Shipowners with new investors) are presented to receptive Club underwriters who embrace the "new commercial management" argument. This triggers the 'free business' rule under the IGA, thus providing an opportunity for those willing Clubs to re-rate the fleet with a disregard for previous loss record performance (this of course only happens when the owner's loss record results are poor). Why a Club regards this new financial management influence (whose focus is primarily to cut operating costs and increase profitability) as a valid reason to cut existing premiums by up to 50%, is beyond professional comprehension!

It is surely time that Clubs and their managers are held accountable for such reckless behaviour and its consequences. The leaders of the IG need to properly police this issue before it inflicts further self-harm!

Entirely predictably the unfettered desire for growth at (virtually) any cost has now 'come home to roost', and Clubs are again using the blunt mechanism of GIs (contrary to the commercial markets approach) to address their underwriting inadequacies. This disproportionately impacts on good, long-standing members who already pay appropriate levels of premium, reflecting their loss record, who do not asset play and maintain a consistent well run fleet.

An ex CEO of a major P&I Club manager who is a vocal proponent of mergers and acquisitions, and the shrinking of the IG to 7 large Clubs, has again been in the press lamenting past failures of finding potential partners. It is interesting to note that those Clubs at the top of the P&I 'premier league' do not crave mergers, nor the need for their Club to significantly increase in GT in order to compete. It is only those Clubs who are struggling to meet the key measures that rating agencies and others demand of them to maintain their 'A' ratings, who push this argument!

Mergers and acquisitions of P&I Clubs are just a lazy path for managers to impress their Shipowner boards, none of which have thus far been convinced of the value or argument... hence there has never been any "non distressed" merger or acquisition in the IG. This is in spite of all the hype, particularly from some 3rd party managers... who primarily want to enhance their own rewards and cover for their own shortcomings!

As we said last year, we believe some of the Clubs have only themselves to blame for their premium deficiencies. It is now long overdue for Clubs to stop unrealistic underwriting (which always comes at the expense of long-standing members). The Clubs need to adopt a strategy more appropriate to their role as custodians of this unique and enormously valued mutual system and stop being distracted by some Club's obsession with M&As or diversification, which other than the unique and somewhat fortunate business model of Gard, will likely never be replicated. In fact, it is the approach of the rating agencies in requiring balanced underwriting, with an apparent disregard of free reserves held (which in most cases far exceed the industry approved Solvency II requirements) and pressurising the Clubs to embrace multi-line diversification, which has caused significant financial stresses for a number of Clubs!