MANAGING DIRECTOR'S SOAPBOX

TURBULENT TIMES AHEAD... IS IT THE CLUB MANAGERS THAT ONLY HAVE THEMSELVES TO BLAME?

As in previous years (usually 'coincidentally' following an RI Sub Committee meeting), we are again being told by the Clubs of their need for general increases. Yes, it is true most Clubs are reporting adverse combined ratios (poor underwriting results) and yes, investment income is down or flat this year, however the Clubs achieved bumper returns in 2019 of more than 9% in some cases. Clubs hardly mentioned their 'windfall' last year. Most are now bemoaning their results and their need, in some cases, for double digit percentage rate rises. Some Clubs, to their credit, have at least been allowing capital returns or discounting final call instalments. Although the latter is welcome, it is not always as helpful to the member as at first it seems! This practice deprives the member's record of previously anticipated premium with the likely consequence of destabilising the underwriting, with the subsequent consequence being a need for (perpetual) rate rises if the Member's record exceeds the acceptable loss ratio.

Many Clubs have been 'squandering' their members' free reserves on unfettered, unsustainable competition for new members/tonnage! In some cases, it is not even for bonafide new management business, as the IGA agreement requires. The more aggressive Clubs seem happy to support the weakest of excuses to quote on another Club's business, offering unrealistic and unsustainable quotations and yet insist that their existing, often long-term members, pay their general increase demands. Note the Standard Club's incredible (Lloyd's) losses as a consequence of Charles Taylor's alleged mishandling... the members of that Club of course continue to pay the cost of this entirely predictable and foolhardy venture.

We know of only one Club, the Steamship Mutual, who are openly prepared to volunteer the actual level of reserves that they deem necessary for the Club to hold.

No other Club seems willing to be transparent in communicating their target level. Wilson have asked for half a decade "how much (free reserve) is enough?". We see the Clubs' free reserves continue to rise exponentially and still do not get any clarity on this question!

The Clubs' underlying claims are largely predictable, but pool claims, we are told are generally far more volatile, and in fact are now "the worst ever"... perhaps over $400 million at the 6-month stage of 2020 and twice that in 2019. It should however be remembered that a substantial portion of these overall costs are recoverable from the GXL underwriters and other bespoke facultative reinsurances placed on members' behalf and for their protection.

Solvency II is the Directive of European Law that sets minimum solvency levels that the Clubs need to adhere to in order to ensure customer security/consumer confidence. We wonder for how long we are going to see the 'merry-go-round' of unabated, incredibly high and ever-increasing Club reserves, way beyond regulators' requirements, with Club managers demanding often unjustified general rate rises (to satisfy everyone other than their Shipowner members). These rises often help fuel unsustainable competition for new business. This, perhaps unintended consequence, undermines the IGA, and particularly at the expense of the many traditional members, satisfying the demands and opportunism of Corporates and overly ambitious Clubs and their Underwriters, always at the expense of the membership as a whole.
It is surely time for members to send a strong message of preferred direction to their Club boards and their Club managers, that particularly during these challenging trading times the members need real and meaningful (financial) support from their Clubs.

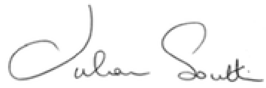
The leaders in the industry, particularly the IG Chairman Mr. Paul Jennings, should take action to provide direction, cohesion and influence on individual Club leaders to stop the damage that is being (self) inflicted on the industry due to poor, reckless and often ill-disciplined underwriting. The current, arguably necessary approach of Lloyd's and other commercial market underwriters' should not be the example stated and followed by (Mutual) Club managers. The H&M market particularly is hardening... and some Club managers see this as an opportunity for them to 'ride on an opportunistic wave'! Others are unduly influenced by S&P and the threats of rating downgrades.

Clubs with excessive reserves should distribute more capital back to their membership, particularly during these unprecedented times, be more accurate in their claims forecasting, by estimating claims costs on 'most likely outcomes' and not 'worst-case scenarios'. The latter practice inevitably leads to exaggerated claims estimates, only for the Club managers to be able to 'quietly' release claims reserves 2 or 3 years later, retaining members' money and further increasing the Clubs' free reserves and opportunities for aggressive growth.

If Club managers insist on applying general increases, a potentially more equitable solution might perhaps be; for Clubs to announce an initial general increase, apply it to all members' renewal premium rates and then take the (cash) equivalent from their Club's free reserves and credit the same to their members' loss records for the forthcoming renewal. From that point members / their brokers could negotiate the renewal in the usual way. This would have the benefit of instantly enhancing Clubs' underwriting results / combined ratios, redistributing a modest portion of Clubs' surplus capital, help ease the current financial challenges Shipowners are facing flowing from the trading disruptions caused by Covid and curb the underwriting abuses that are prevalent in the industry at present!

Some shipowners might even find it preferable for Clubs to apply the mechanism, unique to the industry, of making unbudgetted supplementary calls. Two potentially adverse claims years does not yet constitute "an adverse claims trend" necessitating general rate rises and if Club managers are unwilling to fund immediate deficits through free reserves (for which they are intended) then perhaps unbudgetted supplementary calls could be a short term answer to mitigate members' premium rates rising in perpetuity.

Monopolies can be the enemy of innovation... Clubs and the IG must be more innovative in finding better tools than general increases to address the Industry wide underwriting inadequacies and failings!



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