P&I Bulletin

Financial update

June 2020

Empower Results®

Introduction: shipping's resilience tested

This year will long be remembered for the tragic events that have and continue to cause devastation in all walks of life, and shipping is no stranger to the effects of COVID-19. The resilience within the shipping world is well known, but some sectors have been powerless.

Practically every passenger-carrying vessel has been inoperable for some time with the future still far from clear. Add in the free fall oil prices causing freight rates to plummet, as well as offshore units still searching for work, and this has forced many units into lay- up. It is no wonder that even the most optimistic operators are struggling to find a glimmer of hope on the horizon.

With all this gloomy news, it would be nice to convey some positivity from the P&I world. Whilst some clubs have posted pleasing results, it is very much a mixed bag. The very best returning a combined net ratio (CNR) of 99.80% from Steamship Mutual with London Club posting high of 137%.

Renewal stance

Naturally, the CNR is not the governing factor for a club's well-being, but it is a significant indicator of the stance to be taken at the next renewal. For the better-reserved clubs, any shortfall can be absorbed, for now. However, remedial action will figure heavily on 20 February 2021.

For those clubs not so cash-rich, the situation will be more pressing. To address any further erosion of free reserves and premium base is not an easy task. However, as was demonstrated by the American Club, unbudgeted supplementary calls may yet figure. Understandably when others are bolstering free reserves and, in some cases, returning premiums, this will be a challenging time for a few clubs as the gap in financial strength increases.

We have no wish to see any contraction in the present number of clubs. We welcome choice but that this must be balanced with financial standing and, in many cases, the requirement to carry an A rating. No doubt, the talk of mergers will surface once again.

We have seen premium under pressure and claims escalating for the past few years, yet free reserves have, for most, increased. Will last year's results and this turmoil prove to be pivotal? The headline of 2019/20 was spectacular investment performance. At the low end was 5% reaching close to 10%. This return on capital, in many cases over USD 100 million, softened what was for all a 'wake up' call when looking at the loss ratio of net premium versus claims.

The financial sector post 20 February was a different landscape; whilst investments have shown a marked recovery, it is far too early to forecast with any confidence how this year will close out. At the time of writing, we are already hearing talk of general increases. We believe sending out such signals is premature. We have no crystal ball, but with shipping movements falling, this usually goes hand in hand with fewer claims. There will be the inevitable reduction in premium, but if ever there was time to extend a hand of support, this is it.

We appreciate that rates have fallen, and the likelihood that even older, better-paying vessels may leave the arena, puts the group in a difficult position. However, we believe that if free reserves remain static, this is a year to 'ride out the storm'.

Review from within

Not for one moment are we suggesting any club bury their heads in the sand, but a review from within may be the remedy. We have mentioned on numerous occasions the thirst for new tonnage continues to influence underwriting discipline. All too often, we see not just premium, but risk selection also faltering in the face of the opportunity of free business. How many offices have been opened at, one must assume, no little cost, for servicing or to stimulate growth?

We suspect consolidation will figure heavily this year and the coming renewal. Sadly, there will be some operators unable to weather this storm, so it is of paramount importance that existing members get all the support they need. We understand that individual loss records cannot be ignored, but a broad brush stroke to seek a hike in premiums should be resisted.

We are still waiting to hear of the underwriting results of the Japan Club. In due course, we will analyse each of the clubs' results in greater detail as their report and accounts are made available.

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Underwriting Results

As expected, underwriting results for most the International Group Clubs that have so far announced their figures are negative. With even Skuld announcing a USD 34 million underwriting loss, its first in 10 years. The only club to have an underwriting surplus is Steamship Mutual who scraped in just below 100%. As two of the worst of the Group currently, Standard and North, underwriting losses are too large to be offset by their investment returns.

The graph below demonstrates the proportion of each club's investments results that have been eaten up by the negative underwriting results, highlighting the clubs' reliance on investment returns to offset rising claims costs and reducing premiums.

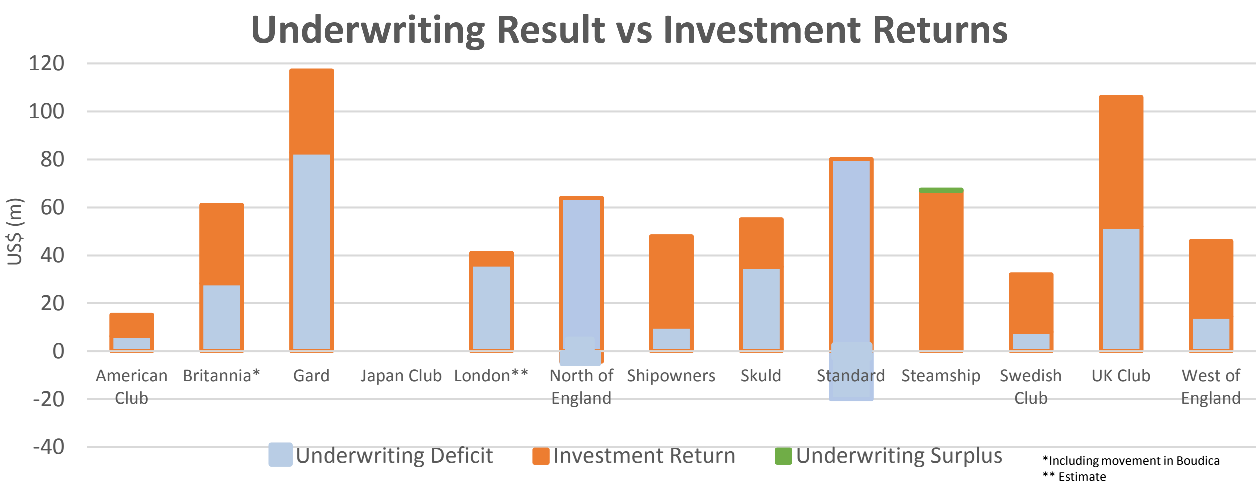
After a renewal of General Increases, have the clubs achieved the support from their membership to start to correct this imbalance?

Combined Net Ratio

	2019	2020
London	140%	137%
Standard	116%	131%
North	105%	125%
UK	114%	120%
Britannia**	104%	120%
Gard*	117%	114%
Skuld	97%	109%
Swedish	99%	107%
West	114%	107%
Shipowners	104%	105%
Steamship	116%	99.8%
American	117%	TBC
Japan	98%	

*Actual Call Basis

** Estimated to Include Boudica



Investment Returns

USD (m)	2019	2020
Gard	(7)	117
UK	6	106
Standard	12	80
Steamship	14	67
North	26	64
Britannia*	(3)	61
Skuld	3	55
Shipowners	(29)	48
West	29	46
London**	8	41
Swedish	(6)	32
American	(0.5)	15
Japan	20	

* Excluding Boudica
**Estimate

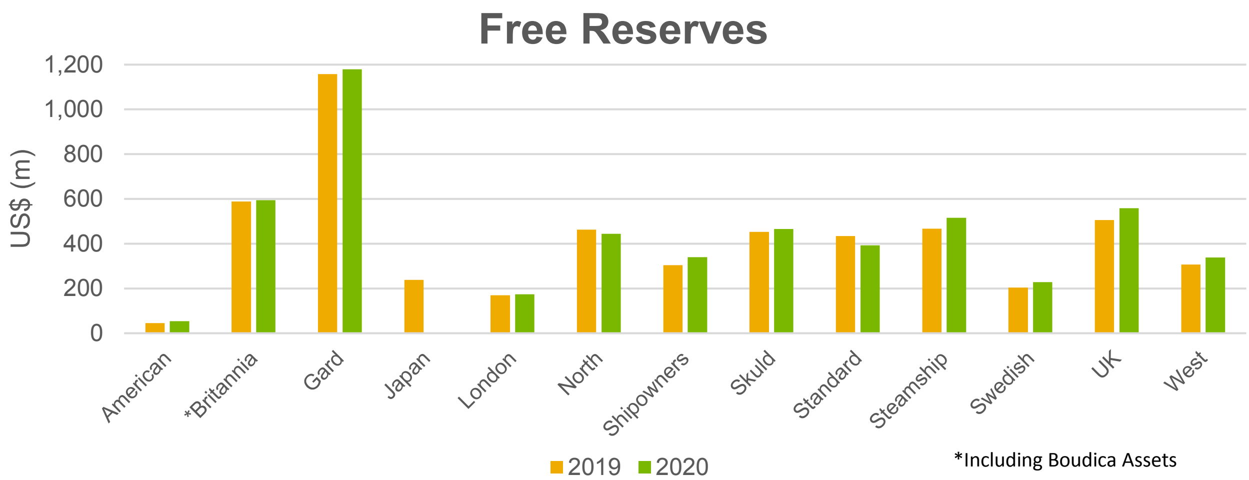
Investments

Across the board, investments had picked up from their position the previous accounting year, with Gard unsurprisingly, due to its size, bringing the highest returns. These figures however do not show the impact the pandemic has had on the investment market since the end of the accounting year for most clubs. Following the crash on the 12th March 2020 and its subsequent partial recovery, we expect the mid-year figures to be reduced especially for those clubs with a higher proportion of their investment in equities, such as the London and American clubs.

The impact will be seen first in the Japan Club annual report, whose year-end is 31st March, which will be released later this year.

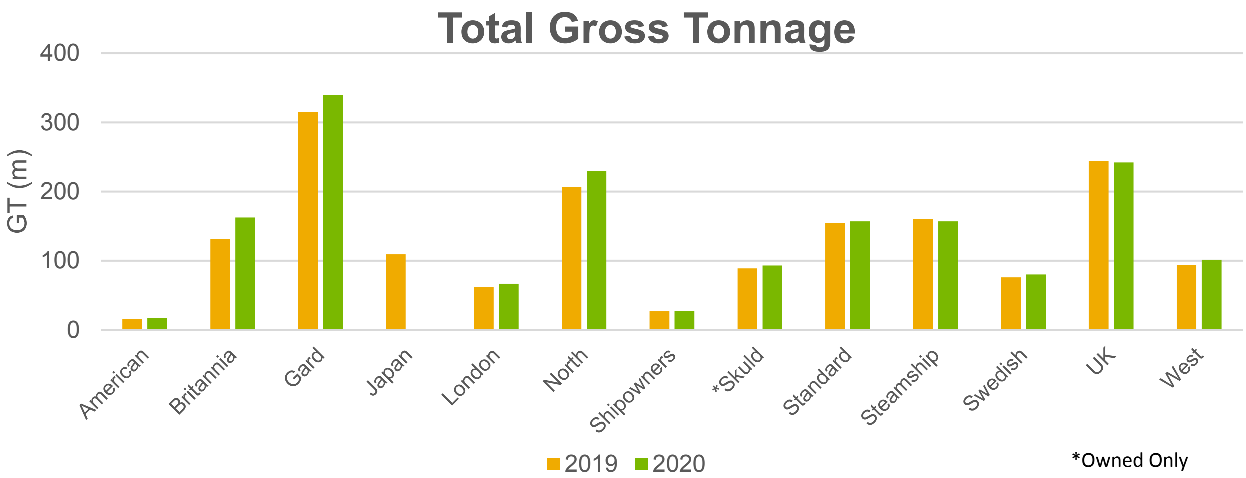
Free Reserves

Most of the clubs that have announced so far have seen a marginal increase in their free reserves due to investment returns. North and Standard have seen a small decrease in free reserves but are still both well within the requirements under the European Solvency II directive. Again, with the investments set to be impacted by the COVID-19 pandemic and, depending on current year claims activity, we are likely to see a reduction in free reserves mid-year ahead of the 2021 renewal.



Tonnage Movements

This year Britannia has proportionally seen the largest increase in tonnage, due to a major chartered account joining the club. Other clubs have also announced year-on-year increases in tonnage, both through new membership and expanding fleets.



Closing Comments

It is clear to see how influential investments have been to the benefit of each clubs' combined net ratio. A fact not lost on Standard and Poor who recently amended the Standard Club's outlook to A negative from A stable. This came straight after the club announced its split from Charles Taylor to form its own management unit, which we believe is a positive development.

It is clear that many members are enjoying rates that are likely to be unsustainable, never more obvious than with the so called 'churn'. However, we do not want to see a knee-jerk reaction with a hike in premiums to all. Whilst there is no longevity for underwriting with investment income to balance the books, it cannot be ignored. We will have a clearer picture of how the year is developing by AGM time and, if there are premium adjustments to be made, we hope these are done with an even hand, reflecting the loss performance of each member. If the financial sector does perform positively, then that should be used to ensure rates, where they need to be, are increased over a period of time.

The jury is still divided on diversification. In certain niche areas this may well prove beneficial, but operating in mainstream marine business hasn't shown the rewards expected and surely this is not a time to gamble with members' money.

Given the circumstances, there is little doubt the group is in great shape and, whilst clearly some clubs are performing better than others, they continue to meet all the maritime industry's needs.

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