



Marine P&I

P&I Newsletter – February 2018

P&I Confidential



Gallagher

Insurance | Risk Management | Consulting

P&I AT A CROSSROADS – IN MORE WAYS THAN ONE PERHAPS

Welcome to our first P&I Confidential of 2018, issued in the wake of the annual renewal at 20 February 2018. We have just completed renewals in a second successive environment where no general increases have been sought – this has proved challenging but we are confident that we have achieved the best deals for our clients.



As soon as 20 February 2018 has passed, we find ourselves looking forward to 2019. So where do we see the market going, and what factors do we see as influencing the market and the rates at the next renewal? As our headline would suggest, we see the market as being at a crossroads – indeed, if it were possible, at two crossroads! The first crossroad concerns the underwriting environment, and the second concerns the way Clubs operate – both individually and collectively.

The underwriting market definitely appears to be changing, and from an underwriter's perspective, for the worse. Claims, which have broadly speaking been declining for the past 3 years, appear to have bottomed out, if not potentially rising for some Clubs in 2017-18. We expect this flat / increasing trend to continue into 2018-19.

Fears of a surge in pooling claims, anticipated at the half year mark, seem to be unfounded: in fact the year is not dissimilar to 2014-15 at this early stage of development. Whilst claim numbers and values are higher than in the preceding year, the current value of the 2017 claims (so far reported to the pool) has not risen dramatically and, were it not for the probable limit loss in respect of the Kea Trader, the year would seem unremarkable.

On the underwriting income front, the true impact of two years of zero general increase is beginning to take its toll on rates. The erosion of the Clubs' premium base both by static general increases and the impact of churn may mean that rates per Gross Tonnage (GT) may have fallen by as much as 20% in the two years since the last reported figures at February 2017. Add to this the return of premium seen in many Clubs, and "something's got to give", as investment income cannot continue to subsidise negative underwriting balances: where have we heard this before?

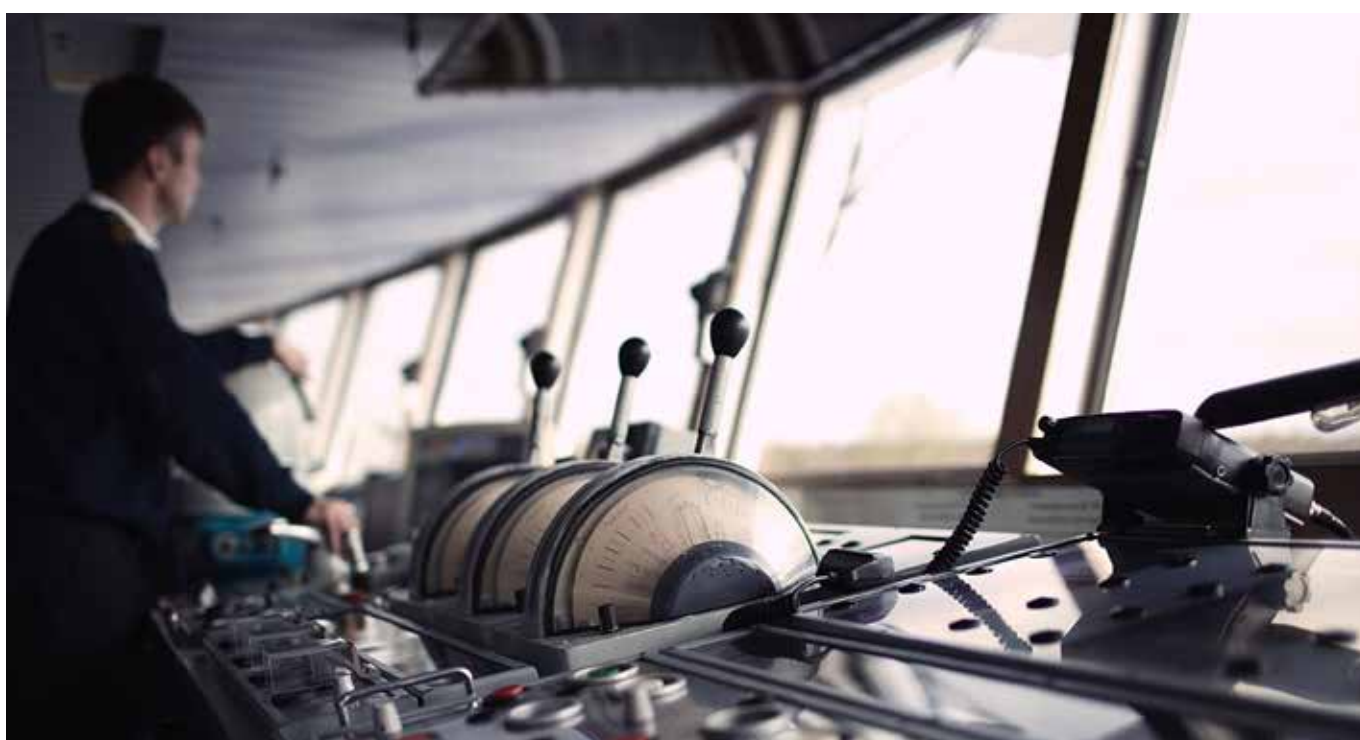
The mindset of the underwriters at the recent renewal very much seems to be "what we have, we hold", may not necessarily be in the best interest of the Fundamentals have perhaps been parked to one side and rating seems to be significantly driven by a need to retain members / vessels, potentially at the cost of price.

So here we see our first crossroad – declining rates and rising claims may have characterised the last 3 years: we expect both these trends to reverse over the next 12 months and inevitably this will pressurise the autumn general increase decisions. The Clubs need to act now in anticipation of these changes.

This may however emphasise the push towards a two tier market with the larger, more financially powerful Clubs being able to out-muscle their smaller cousins, looking to use their accumulated funds to continue to offer "rebates" (either return calls or capital distributions) to members. In effect this constitutes a discount, if consistently granted, and one has to wonder whether this potentially may be seen as a challenge to the financial inducement aspects of the IGA.

This takes us neatly on to the second crossroads that the Clubs will need to cross in 2018. Consideration of the agreements that bind them together. We understand that the Clubs are in the process of carrying out an overall review of their general governance at group level. The first visible sign of this is seen in the decision to put the International Group Reinsurance Programme out to tender.

The programme has been in the hand of Miller Insurance, under various names, since 1951, although others have been involved in Hydra's retrocessional programme and there are "private placement" lines in the lower layers of the programme. Whilst we encourage long term relationships (on the reinsurance contract)





between a client and his broker, sometimes change is good and can bring a different perspective.

The International Group Agreement itself has not been amended since 2013, and has been rarely significantly changed in the last 25 years – indeed recent changes have been down to the intervention of, and prompted by, the EU Competition Directorate. Given the changes seen in the market since then – particularly diversification and the more subtle implications thereof – a number of new dynamics will impact the quoting principles enshrined in the agreement.

As alluded to above, many in the market both “brokers” and “Clubs” suggest the annual reductions in ETC at Gard – attributed in part to a subsidy from and profits in diversified classes of business, may represent a financial inducement.

On a similar tack, are possible future capital distributions by Britannia, arising from past accumulations of funds, but payable to ongoing members, a challenge to the financial inducement principle? Capital distributions should not be so easily discredited though, as they are seen as a welcome relief to many Members, with the return of cash a necessary reprieve.

As far as Gallagher P&I are concerned, we see the Gard and Britannia positions resulting from past good technical underwriting performance, combined with member selection, and indeed investment revenue, as ‘fair’ in terms of the IGA (which of course we as Brokers are not party to). However, these Clubs currently lead the way in effectively creating a potential two tier market.

Another issue that could be usefully reviewed is the matter of voting on change. Significant changes require a 75% vote in

favour, with each club having one vote. This means that 4 clubs can resist change. This factor has had impact on decisions such as individual club retentions and pooling limits in the past, where the bigger clubs have pushed for higher retentions and limits only to be thwarted. All clubs no longer have the same commercial objectives and in many ways they are drifting apart, with at least one club arguably being big enough to “go it alone” should it want to.

So, is the one club, one vote principle sound? Should voting be along the lines of one vote per mutual owned entered GT? Or





perhaps voting based on owned mutual premium figures declared to pooling? Both would probably better reflect the commercial relationships between the individual clubs but might also lead to “minority persecution” of the smaller Clubs. Is there any evidence that the current one Club one vote system has held development of the group or its constituent members back?

These issues need careful consideration since a fine balance needs to be maintained between the interests of individual Clubs which are now far less homogenous than they were when the IGA was last revisited. It will be hard to balance the interests of a large diversified club such as the Gard with the smaller, monoline Clubs.

One final challenge for the Group this year will be the relocation implications of the Brexit decision. Different Clubs intend to adopt different locations – Ireland, Netherlands and Luxemburg amongst the plans. Having just changed their group structures and capital arrangements to allocate resources more efficiently for Solvency II, we may now expect to see a little more juggling to match the capital to the underwriting domicile to the regulatory solvency need.

All in all then, there are a lot of issues for the clubs to address, both individually and collectively, over the forthcoming months. We will of course keep you updated as things develop in future volumes of P&I Confidential.

We at Gallagher have had a good renewal and would like to thank our clients for their continued support. We have been able to expand into other areas such as Italy and Japan:-

After a twelve month exploratory period in the Italian market, we are pleased to report that Gallagher have been appointed

by a large Italian ferry fleet and a well-established supply vessel operator for the 2018 policy year, with both operators remaining with their existing P&I Clubs (i.e. no change in market). This now takes our Italian client base up to a modest five clients, which we hope to expand upon in 2018/19 accordingly. In Italy we work with our local retail partner Cincotti & Partners whom we wish to thank for their cooperation and support. We are pleased to see that Gallagher’s P&I entrance into the Italian market has been welcomed by many shipping companies we are in dialogue with. Whilst we are still “new comers” to the region, which has been dominated by very few P&I brokers, we hope to be given further opportunities as we enter into a hardening P&I market in 2019.

Gallagher first visited Japan in November 2015 and followed this up in the spring of 2016 to identify potential brokers to partner with. In October 2016, Gallagher announced agreements with Japan England Insurance Brokers (JEIB) and SC Global Brokers to explore new marine opportunities. We have now been active in Japan for the past fifteen months and have now secured clients across P&I/K&R/COFR covers, as part of a full range of marine broking services. We have quickly established our P&I credentials and now represent one of the top 10 Owners in the market. We appreciate that brokers in this market have a long road to prove their value, but this is a challenge we are willing to accept and hope that over the forthcoming years we are able to demonstrate our expertise to the Japanese market.



**NEW STAFF MEMBER,
Marilena Papachristodoulou**

We are pleased to report that Marilena joined the Gallagher Marine P&I division in January as an Associate Director. Marilena is a Greek national, trained as a lawyer, and her educational background includes a LLB

in Law from the National University of Athens and a Magister Juris degree from City University of London with two specialisations; in Maritime Law and in International Banking and Finance Law.

She has, previously, worked for a Greek Shipowner in London as well as for the UK P&I Club, before she moved to a Marine Insurance broker where she gained 7 years of experience as a P&I placing broker for shipowners and charterers.

Marilena is looking forward to working with us and we are sure you will join us in welcoming her to the team.

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