Marine Hull & Machinery and War Risks Market Report

DECEMBER 2021

Gallagher

Insurance | Risk Management | Consulting

ABOUT GALLAGHER

Founded by Arthur J. Gallagher in Chicago in 1927, Gallagher has grown to be one of the leading insurance brokerage, risk management, and human capital consultant companies in the world. With significant reach internationally, our organisation employs over 32,000 people and our global network provides services in more than 150 countries.

Our people partner with businesses across countries and international territories to provide relevant and impactful professional advice. Regardless of what risk and human capital challenges our clients have, we work hard and utilise industry specific expertise to find the best solution and to deliver it with world-class service. We continue to build on 90 plus years of expertise that spans global industries. No matter the size of the organisation we partner with and the challenges presented by the industry, we work tirelessly to provide solutions that maximise value for our clients.

Our values are core to our culture. Passionate service, strategic innovation, and ethical behaviour form the basis of how we do business. All with one purpose:

TO HELP YOU FACE YOUR FUTURE WITH CONFIDENCE.

CONTENTS

01. MARINE HULL & MACHINERY AND WAR RISKS INTRODUCTION: DECEMBER 2021

Welcome to the final edition of the Gallagher Marine Hull & Machinery and War Risks Market Report for 2021.

A More Sustainable Future

At the time of writing, political and business leaders from around the globe are meeting in Glasgow for the COP26 Summit. It is a fitting time for the final edition of the year where our focus has been on sustainability in shipping and, more specifically, the role that the insurance industry plays in helping to drive the necessary changes for a greener and more sustainable future. In this edition we welcome back Iain Henstridge of Apollo who has written a piece entitled 'Sustainability: How marine insurers will be driving the change'.

Achieving the emissions targets required to stop irreversible global warming will be a monumental challenge, but equally presents great opportunity, no more so than for shipping and insurance. The role of the broker, in terms of risk management advice, has never been more critical as we continue to help our clients navigate the challenges ahead. It is a matter of certainty that insurers will reduce their appetite and capacity for those businesses deemed to be unsustainable as economies move to a greener future. It is our duty to advise our clients where access to insurance products may become more limited, and on any changes needed to ensure access to as much insurance capacity as possible.

It is not easy to predict exactly where these changes are likely to be but it is evident that two key areas are set to be in the spotlight. The first, and perhaps most obvious, is how companies look to improve the direct environmental impact of their activities. Will insurers give additional credit for vessels using new technologies with greener, cleaner fuels? And how will they balance this with underwriting vessels often using new equipment and technology, largely untested in the real world environment? A perfect example of this would be the recently launched CMA CGM Jaques Saade, the world's first ultra large container vessel powered solely by LNG.

Perhaps of equal importance is how revenues are derived. Will underwriters look to diversify away from fleets where large proportions of the revenue are generated from the transportation, or extraction of fossil fuels? In some cases we are already seeing this with coal transportation, but will there be differentiation between different types of coal, for example? What will be an acceptable percentage of total revenue to derive from a certain activity? Will that percentage vary from one insurer to another?

Gallagher is the only insurance broker to feature in the list of the world's most ethical companies as recognised by the Ethisphere Institute. We have driven dialogue on these complicated issues in our recent market reports and we are now prepared to advise our clients as real changes have the potential to take effect.

Market Losses

The insurance market has generally been hit by losses from an active US windstorm season. The marine market was certainly affected by this with a number of large claims on vessels and infrastructure. There have been a number of other significant losses, most notably in respect of the 'X Press Pearl' and more recently the 'Zim Kingston', both of which are containerships. However, there has been some easing in the marine hull market over recent months. Whilst the market cannot be described as soft, with increases still being sought on clean business, it is undoubtedly less difficult than 2020, with limited pockets of new capacity in addition to some carriers looking to selectively grow their books again. Any easing will be welcome for owners in 2022 where well reported likely increases on P&I will perhaps be more of a financial concern.

Market Moves

In terms of market moves, Mike MacColl, previously head of hull at Axa XL has recently started a new role at Atrium Syndicate writing the hull portfolio. Paul Russell has left Lancashire and will join privately owned Bermuda domiciled insurer Fidelis. Charlie Jenkins has joined Travelers as an underwriter having previously been a broker at Willis.

Weathering The Storm

It is most encouraging to see a strong shipping market in many sectors after a long period of difficulties. A perfect storm of contributory factors means that the fundamentals are likely in place for a sustained strong market for containers and bulk carriers throughout 2022. Typically speaking this should be good news for insurers as well, as they are hopefully able to share in some of this success having supported long term clients through a very difficult market. There will be extra premium going into the market due to increasing asset values but with that comes the possible increase in severity of large claims as total loss exposures increase and loss of hire daily amounts reach levels not seen for some considerable time.

It is great to report that the market is returning to some normality after many months of lockdown due to the COVID–19 pandemic. We are cautiously optimistic that the most restrictive lockdowns are behind us although wary of the challenges which may arise during the winter months. The office is operating as normal, Lloyd's of London is open, and some travel has resumed. We are very much looking forward to seeing all of our clients and partners over the coming months, either here in London or on our travels.

02. SUSTAINABILITY: HOW MARINE INSURERS WILL BE DRIVING THE CHANGE

Author: *Iain Henstridge*, Apollo

COP26 is finally upon us and I am writing this article as the climate conference, of which so much is expected, gets under way. Hype is a word that is often associated with climate change and ESG (Environmental, Social and Governance) matters, but global warming and making the changes necessary to usher in a low carbon economy are the biggest challenges facing, not only our customers, but we as insurers too.

Today, the measure of a company's success is just as likely to be their green credentials, as their profitability. You only have to look at Tesla to see the attraction of green businesses to investors. A motor company no one had heard of 15 years ago, that now has a market capitalisation of around USD1trn and is more valuable than the world's nine largest car makers combined. There are many reasons for this, but surely the most compelling are that, as a corporation, it is quite literally driving change and is an enterprise with no perceived dirty legacy.

Companies that do not adapt to change risk extinction. Just ask a teenager if they have ever heard of Kodak, and that blank look you receive in return will make you realise just how quickly a company's relevance can plummet. At one time the undisputed king of imaging, but a company that arguably failed to react in time to change.

It's Only Insurance, or Is It?

Underwriters are in a strong position to drive change.

Marine underwriters have been the bedrock of world trade for over 300 years. We have been there on the journey with our clients, as they moved from sail via steam, to the modern diesel engines that provide efficient propulsion to today's ever larger ships. And we will be there for the next generation of ships.

Marine insurers potentially have real leverage to help move shipping into a low carbon future. Banks do not lend and ships do not sail, without insurance. The downside risk to a company's balance sheet and its people of sailing without cover is incredibly high.

Banks can adopt a strong ESG stance with their lending, but what about those loans already on their books? What can they do—call the loan in for lack of progress on sustainability? Of course not. A marine mortgage is a long-term loan and the banks may not want to risk their own balance sheets by making waves.

But a vessel's insurances are generally short-term arrangements, typically 12 months. If an insurer has concerns about its client's sustainability credentials, it is in a much stronger position than a banker to exit that client relationship early. Marine insurers do not generally turn their backs on what may be an otherwise healthy long-term relationship, but times change and the underwriter may simply not be allowed by their management's ESG committee or board to continue writing that business.

Measuring Sustainability

Insurers will want to do the right thing, but with sustainability being such an amorphous concept and its public perception so subjective, there will be a wealth of challenges ahead. This issue raises so many questions within the marine insurance community. To name but a few:

- Responsible ship recycling is a noble aim, reducing pollution in South Asia, but at the same time denying an income for workers and their families there. Who are we to take the moral high ground?
- How far do we go in measuring and quantifying sustainability? Refusing to insure vessels that carry coal for thermal power generation is a relatively easy decision for an underwriter, but what about soy beans or palm oil from areas that were previously rainforest?
- Where does it end? We are not policymakers, but we are enablers. Existing insurers and bankers can steer responsible behaviour, but does this judgemental approach then allow questionable challenger players to enter the market to cater for the needs of those legacy assureds struggling to find cover?

Insurers model risk, and the big challenge will be how to derive an effective ESG score for each of our clients, enabling us to establish a benchmark. The big data companies and modellers will need to step up here to provide granularity of detail, allowing insurers to assess this previously unassessed element of the risk. I predict that within a couple of years underwriters will routinely be using these ESG scores in their pricing models, with those assureds who are making progress in the green transition certain to benefit from a rating differential and advantage.

So what kind of things will make up an ESG score that insurers can use to assess a risk? The list below is just the tip of the iceberg:

- The forthcoming EU Monitoring Reporting and Verification regulations will mandate the transparent reporting of a ship's environmental performance. Insurers will potentially be able to benchmark using this data.
- The use of shoreside electrical feeds to allow vessels to power down in port. This would lead to tangible health benefits to those living near ports.
- What type of fuel does the vessel use?
- Shipping companies that reduce their potential environmental impact by not navigating the Northern Sea Route and other unspoilt waters.
- Shipowners who adhere to strong crew welfare practices, such as those set out in the Neptune Declaration.
- External data sources, such as Glassdoor, give an insight into corporate behaviours. They help insurers build a picture of their client's quality of governance.
- Counterparty quality. Banks, for example, will have an insight into a shipping company's credentials. Highly subjective, but the quality of the lender can often mirror that of their client.
- Engagement. Shipowners who actively engage with their insurers rarely have much to hide, and that transparency can be an indicator of good governance.

Reputational Risk

As environmental issues come to the fore, shipping is being seen by the general public as a dirty industry. Insurers, and their capital providers, want to support sustainable companies and those who publicly declare that they are on a defined path to be more sustainable, as it is the right thing to do. And doing the right thing is an increasingly crucial element of the insurance industry today.

Pressure groups, with vociferous social media campaigns, are playing their part, driving insurer behaviour. There has been online pressure, naming and shaming companies that offer insurance to new coal mines, for example. That has led to a withdrawal of insurer capacity for these massive facilities. In our world of marine insurance, the NGO Shipbreaking Platform has been successful in highlighting the illegal scrapping of ships, and the dangerous pollution arising from their disposal on the beaches of South Asia. This has caused many underwriters to review their underwriting of such risks, with a consequent reduction in capacity.

Extinction Rebellion is a direct action pressure group that has staged highly visible, imaginative and disruptive protests against insurers for their perceived lack of environmental concern.

Increasingly, a company's ESG credentials are the focus of insurers and such scrutiny will only intensify as time goes on. It is only a matter of time before shipping companies themselves really come into the sights of environmental pressure groups. Only those companies that can prove they are making the change will be able to fend off these pressures.

Social media has proven to be a hugely valuable tool in putting pressure on insurers and their clients alike. It has given a megaphone to anyone with an opinion, without the filters that mainstream media often use to verify the facts.

Lloyd's with its 333 years of always paying valid claims is rapidly adapting to this changing world. Such a tremendous reputation could be savaged if the market did not adapt, so CEO John Neal has put sustainability and ESG front and centre of his strategy for the future Lloyd's market.

A Global Push For Change

The United Nations Environment Programme has also been working with the insurance industry to produce their Principles for Sustainable Insurance. They have produced four guiding principles for insurers:

1. We will embed in our decision-making environmental, social and governance issues relevant to our insurance business.
2. We will work together with our clients and business partners to raise awareness of environmental, social and governance issues, manage risk and develop solutions.
3. We will work together with governments, regulators and other key stakeholders to promote widespread action across society on environmental, social and governance issues.
4. We will demonstrate accountability and transparency in regularly disclosing publicly our progress in implementing the Principles.

These overarching principles are not mere "greenwashing", but keep the pressure on the insurance community to push for change.

Innovation

Insurance is an economic and social utility. As such, our industry has an important role to play in pushing for/advocating and supporting real and tangible change. The development of new R&D and opportunities can be supported by insurance. And whilst there are 'new' risks, this is a challenge our industry has always risen to address. The opportunities are mutually beneficial both commercially and seen through an ESG lens of their impact on society.

Conclusion

Shipping has become one of those things the world takes for granted. Even more so since the growth of globalisation in the late 20th century, where so much of what we consume has been conveyed by ship. Out of sight and out of mind, that is, until things go wrong. The unfortunate blockage of the Suez Canal by the "Ever Given" earlier this year, and the subsequent chaos that ensued, showed us all just how dependent we are on shipping.

Nearly three years ago my chairman asked me what our hull account would look like without fossil fuels being a part of it. I was really taken aback by such a line of questioning. Dark thoughts went through my mind, wondering how we might manage such a change, but as insurers adapt to this new order, that question proved to be more prophetic than I realised at the time. We will need accelerated action by 2030, if we are to meet the 2050 net zero target. A defined timeline is important to businesses and populations, but we must always remember that nature itself does not work to a calendar. The green revolution in shipping, and the drive towards net zero, offer not only the greatest opportunity in our lifetimes, but could be that vital part of the jigsaw that pulls humanity back from the edge of the ecological abyss.

Iain Henstridge, Apollo

ABOUT APOLLO

Apollo Group Holdings Limited, including Apollo Syndicate Management Ltd, is an independent specialist insurer and reinsurer with a team of talented and experienced professionals across a number of specialty lines. Apollo offers adaptable and flexible underwriting services at Lloyd's and leads a number of London market consortia. Apollo's market-leading underwriting talent has allowed the business to spearhead sharing economy initiatives such as ibott ("Insuring Businesses of Tomorrow, Today"). For more information, please see: http://www.apollounderwriting.com/

03. MARINE CASUALTY REPORTS

Tanto Mitra: Collision

Containership 'Tanto Mitra' has been in collision with a coal barge in the Java Sea on the 13th September 2021 sustaining substantial damage to the bow. The vessel was escorted by tug toward the container terminal at Banjarmasin on the 14 September.

Click here for more information.

Zephyr Lumos

Bulk carrier Galapagos collided with large container vessel Zephyr Lumos on 10 July 2021. Both vessels sustained damage with the bulk carrier reported to be punctured badly, resulting in signs of oil spillages. Both vessels proceeded to anchorage for further assessments as well as being detained.

Click here for more information.

Jin Wan Nv Wang

Two ships, heavy load carrier Jin Wan Nv Wang (IMO 9513452) and Service Ship Qi Ye 6 were impacted by approaching typhoon Kompasu in Chinese waters on 11 October 2021. The Jin Wan Nv dragged anchor and started to drift at anchorage off Changle Airport, Fuzhou. Sixteen crew were reported to have been evacuated. Qi Ye 6 was understood to be disabled off Xiamen, with 42 personnel airlifted to safety.

Click here for more information.

Zim Kingston

Container ship Zim Kingston (IMO 9389693), capacity 4,253 teu, lost 109 containers overboard on 22 October 2021 in heavy weather when it was some 40 miles west of the Juan de Fuca Strait, south of Vancouver Island. The vessel was reportedly waiting in heavy weather due to port congestion. After reaching anchorage on 23 October, a number of containers caught fire resulting in 16 crew members being evacuated. Two of the burning containers held potassium amylxanthate, a "reactive flammable material".

CONTACT US

MIKE INGHAM
DIVISIONAL DIRECTOR

T: +44 (0)20 7204 1864
E: Mike_Ingham@ajg.com

ajg.com/uk | gallagher-uk | @GallagherUK

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