MANAGING DIRECTOR'S SOAPBOX

A NEW IG CHAIRMAN COMING SOON...

Paul Jennings will takeover the helm as Chairman of the International Group this November. Paul has obviously seen and experienced a lot in his 30 years in the industry. His club, the North of England, has successfully grown from around just 4mil gt in 1990 to 142mil today... growing from one of the smallest in the Group to now the 2nd largest in tonnage terms.

It can only be hoped that Paul will engender greater confidence and vision for the Group, being inclusive to all its participants and not just pander to the self-interests of the few mega players. At Wilson we believe that a reduced number of IG participants will result in much reduced competition, with the mega clubs ultimately operating clone like; slow on their feet like equally matched heavyweight boxers just occasionally jabbing at each other... too big, too slow and ultimately too complacent to outmanoeuvre their opponents! Many of the industry players are nervous of Gard's size and financial strength, yet Gard still only has c.17% of Group market share, an amount the UK Club comfortably exceeded 20 years ago!

We wish Paul every success in his new and very important tenure as Chairman. We hope that his legacy will be an IG where all members respect the rights of the others to exist, all enjoying equal importance without discrimination, all pulling together to serve the needs of this most important and valued industry, and particularly the shipowner members (who the club managers are employed to serve) who 'chose' to join the clubs of which they are members!

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We should also not miss this opportunity to extend our congratulations to Mike Hall of Tindall Riley/Britannia who will replace Paul as Chairman of the Reinsurance Subcommittee. Mike is clearly the best and most qualified candidate for this role in the Group. Prior to joining Tindall Riley, Mike was a reinsurance broker for the Benfield Group. He also recently successfully chaired the review of the IG reinsurance broker 'beauty parade'.

WHEN DIVERSIFICATION IS NOT IN THE BEST INTERESTS OF SHIPOWNER CLUB MEMBERS...

Those (usually independent) club managers who have large appetites to find new income streams for their businesses, continue to 'peddle' the often dubious benefits that will be derived for their club shipowner members by diversification. However in recent times, and in most cases there is little or no evidence that such benefits are actually being delivered, with the possible and *current* exception of Gard, whose unique business model many seek to copy, but is now very difficult to replicate (and also relies heavily on investment income). Let's look at a few examples of diversification initiatives by club managers and the consequences:-

- Three years ago, the managers of The Standard Club created a Lloyd's syndicate - Standard Syndicate 1884. The club's underwriting capacity started at around 40% but has now grown to a massive 86%, notwithstanding, and perhaps as a result of the syndicate's heavy loss-making results. The syndicate is reported to be employing some 49 staff and has overhead costs of a substantial $7.9 mil for 2017! This syndicate has already lost its investors c. $92 mil. These reported results will have impacted negatively on Standard Club and their shipowner members to the tune of some $40 mil in lost reserves... and no doubt reduced the opportunities for more meaningful call returns to their mutual members. Charles Taylor on the other hand, continues to enhance its profits from the Syndicate and indeed other P&I 2nd and 3rd party related businesses acquired, such as Richards Hogg, who are currently loss adjusting the rather expensive 'Maersk Honam' casualty.

- Skuld also opened a syndicate at Lloyd's and over its four years of underwriting is reported to have lost circa £37m (or c.$50m), which again will have likely deprived its club mutual members of larger, more meaningful call returns.

- A couple of years ago, UK Club and Thomas Miller were seeking to takeover / merge with Britannia and Tindall Riley! Both management companies, and particularly some individuals stood to gain a lot from this union. However, once the 'merger' proposal was put to the Britannia shipowner Board, it was obvious to most that it was certainly not in the club's best financial interest. There were significant direct and indirect costs incurred in formulating the proposed takeover; undergoing due diligence, management time and costs, employee distraction, and uncertainty for their futures, all of which seemed to impact negatively on both businesses operations for more than a year! At least a positive consequence followed this failed exercise in that the Britannia Board, having finally focussed on their enormous uncommitted free reserves, are now releasing back to their members some of the very substantial club capital that had accrued and laid dormant for decades.

- The managers of the UK Club recently purchased Brookes Bell, a large international marine surveying company whose services are used by most / all clubs. Some clubs have suggested they will reduce their patronage of this company (as a result of its loss of independence and now owned by a competitor) to a 'necessity only' basis. How can club members be confident that resultant fees (paid through their loss records) are competitive, particularly if other clubs reduce their patronage of this company and income falls? Thomas Miller has also acquired two, arguably struggling P&I fixed premium facilities, and it has just been announced they have acquired a third - Hanseatic (a German fixed premium supplier). With the high limits provided by fixed premium facilities, and their capability to underwrite ships with large gross tonnages, it is perhaps difficult to argue, that in many cases, they are not directly competing, and perhaps even undermining the International Group clubs, who themselves underwrite comparable ships, which are often reinsured within the IG and operate under its non-compete rules.

"Why can't club managers be content with this extraordinary and financially rewarding position, rather than continually challenging the system?"

It appears that there are significant conflicts of interest for a number of club managers, ensuring the best interests of their members, operating businesses that are arguably in direct competition with, and detrimental to the IG. The 13 clubs of the Group insure circa 95% of the world's merchant fleet with currently no meaningful outside competition! Why can't club managers be content with this extraordinary and financially rewarding position? It is disappointing that they continually challenge the system by; seeking to reduce the number of IG clubs at the expense of IG competition, creating loss making Lloyd's Syndicates at the expense of their members, acquiring (often distressed fixed premium P&I suppliers in an effort to breathe new life into them, which then will compete with their IG partners), or by purchasing P&I related service suppliers at the likely expense of competition. The consequences of these diversification projects will likely result in greater ultimate cost to the shipowners that have to use (or are steered to use) these services. It is perhaps pretty clear that none of these diversification activities are done for the greater good of the shipowner members, but for greater club managers' reward!

CLUBS SHOULD INVEST MORE IN THEIR STAFF & LESS IN THE STOCKMARKET

The clubs' product is, on the face of it identical... it has to be as all share the same reinsurance protection. As a consequence, individual clubs often struggle to find their own USP. An analogy might be 'cola'… they are all selling it, but it's a question of brand choice for the consumer… taste v price! The clubs who thrive today are those who combine both financial strength and deliver to their members higher service levels and value for money.

The industry over the last decade or more has seen a large number of senior managers, claims handlers and specialists, who were intellectual and/or commercial heavyweights retiring from the industry. Through a lifelong career in the industry they were focused on delivering high quality service, with the long established goal of delighting the shipowner members they served, and only referring to the club rule book to pay difficult claims and not avoid them! It is essential in our view, that current club managements invest in a new generation of highly motivated and talented individuals to support this dying ethos… which has been at the core of clubs' success since their creation. Many owners have raised frustration of some club staff adopting too legalistic or inflexible approaches to claims handling or underwriting. One of the largest expenses for the clubs after claims is 'people'. During times of shipping and financial crisis and with reduced claims activity (as we have experienced for a decade), clubs have apparently felt the need to cut back on investing in staff, the very people who offer a real chance of reducing expensive claims settlements through skilful and knowledgeable claims handling. Now is the time for club managements to refocus their energies on fast tracking their talented staff, adopting intensive training, recognising the importance of maintaining staff continuity to ensure consistent high quality service delivery, and avoiding an environment where staff feel they have to move on to new job roles, either within the managers 'stable' of diversified businesses or leaving the industry entirely to progress their careers elsewhere.

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SHIPOWNERS WON'T KNOW WHAT THEY HAD UNTIL IT'S GONE

We read in TradeWinds that AP Moller... one of the world's mega merchant fleets is said to have applied pressure on the IG (through their clubs), and has been successful in pushing the IG to review its GXL reinsurance arrangements. There was a firm denial from the Group Chairman confirming that Moller's intervention had no impact on the Group's decision to put this contract out to a broker RFP (request for proposal). It is possible that Moller's goal was to achieve greater competition amongst both the reinsuring brokers and the reinsurance market, but no doubt this vision was primarily for their ultimate benefit and may have been counterproductive, particularly in the Lloyd's market! Whilst there has now been a broker 'beauty parade', in fact not much changed (and quite rightly!). The two brokers Miller and Aon, continue to place the contract with similar involvement as before, but perhaps now with a stronger mandate to work more cohesively together. In our view there is little more that can be done by way of pricing for this long-established contract, which continues to be very important to the interests of both the clubs and the Lloyd's reinsurance market. The commercial market underwriters are now likely to have arrived at a minimum premium situation for this contract, particularly in this period of low claims and resultant soft insurance environment.

Both parties heavily rely on mutual cooperation, and as a result they must be fair with each other, delivering a 'win-win' situation for both, to ensure that the contract is not 'rigged' in favour of one side or the other. If this were to happen it would bring disillusionment and resultant lack of support with damaging consequences to the club system!

The P&I clubs were created from small and medium sized independent shipowners who continue to be the bedrock of the system today, although understandably club managers regularly find the draw of very large fleets and resultant large premiums irresistible, often at the expense of smaller traditional shipowners. Less than a handful of overly bearing corporates sometimes seek to exercise undue leverage on the system and yet do not think twice themselves about 'record washing' by moving clubs following a substantial claim.

"Large and often opportunistic clubs say there are efficiencies to be achieved through there being fewer clubs. However these clubs do not themselves have the lowest expense ratios and their underwriting results are often mediocre."

Club managers often boast they are too large to be influenced by any one shipowner applying undue influence on their operation at the expense of their other members… these boasts perhaps look a bit shallow in some quarters! If as suggested, the clubs are in fear of losing such corporates to the commercial market, then we suggest 'let them try'. Often these mega companies do not need the clubs for service, but for unfettered access to the otherwise impossibly high limits the International Group 'excess loss contract' and the mutual system provides. This 'high limit' stance also assists the P&I clubs and their managers, as it makes competition from the commercial markets much more difficult to replicate. Fixed Premium commercial market players cannot provide the very high limits available from the IG. Generally speaking it is the mega corporates that bring the very large claims on the Group GXL contract e.g. the Costa Concordia.

It is quite likely that there has been some 'collusion', or support at least from a few club managers who want to see the demise or absorption of the smaller clubs, by encouraging the type of publicity recently generated, seeking dramatic structural changes to the P&I reinsurance structure. These large and often opportunistic clubs say there are efficiencies to be achieved through there being fewer clubs. However these clubs do not themselves have the lowest expense ratios and their underwriting results are often mediocre, perhaps hence their desire to see reduced competition as an easy fix for a more challenging issue!

The system may not be perfect but as with Brexit... if the likes of Moller or one or two clubs feel there are aspects that are fundamentally contradictory to their visions, then perhaps they should consider leaving the Group to follow their chosen paths, and let the enthusiastic 'remainers' work together to further improve this valuable system in a cohesive and supportive approach!

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