General increases not reflected in premiums

Every year, the protection-and-indemnity (P&I) clubs announce sizeable general increases. But one of the consequences of the business is that this is not reflected in the premiums ultimately collected.

The general increase announced for the forthcoming February re-entertainment average about 0.7%, lifting to about 1.4%, the increases cumulatively over the past decade.

The premiums collected by the clubs have fluctuated over the years but overall remain close to about $2.5bn per gross ton (gt) across the world fleet and certainly have not doubled in a decade. Although the clubs collect even more premiums each year, this is mostly from the expansion of the world fleet than as a result of the spate of general increases announced from October onwards.

The mutually insured, shipowner-controlled tonnage insured by the clubs has grown from around $650m gt to $900m gt over the past decade, with ships’ owners’ appetite, mainly written on a fixed-premium basis, lifting the total insured fleet from about $650m gt to $900m gt.

Premiums currently charged per gt are on average very similar to a decade ago, although there was a dip in P&I costs to an average of about $2.30 per gt about the turn of the millennium.

The riddle of how the general increase is disrupted is one that is attracting increasing scrutiny and a widening range of explanations.

A key answer is that overall the clubs fail to make the general increases stick and some may even announce inflated objectives on the basis that they expect to collect perhaps half the declared figure.

But a wide range of other explanations are also advanced including suggestions that the P&I members are not quite as mutual as they could be, with large powerful shipowners and maybe those who serve as directors of the clubs getting more favourable treatment than others.

Steamship Mutual underwriter turned Tyxor & Co broker Martin Hubbard goes as far as suggesting that if the 20 biggest members in each club paid the premium required by their records, general increases at the level of recent years would be consigned to history.

But the most common explanation for premium income falling to keep up with the general increases, however, is “churn.”

The argument is that competitive terminologies have to be offered to attract newbuildings and recently acquired second-hand ships and the premium these vessels generate fails to compensate for the amount paid by departing older ships—which have been the subject of successive general increases—and are sold or scrapped.

Some real-world examples of the difference between old and new tonnage was given by Jerry Winstone, another Steamship Mutual executive turned broker, at a Baltic P&I seminar in South Korea.

A European bulker owner paying about $2.50 per gt for P&I cover was quoted $4.25 per gt for new tonnage, although the claim record warranted a rate of about $4 per gt.

Another European owner of tankers currently paying $3.70 per gt for newbuilding was quoted $3.30 per gt for newbuildings.

A Far Eastern TELC (tankers) paying $8.975 per gt was quoted a rate of $8.62 per gt for newbuilding, although the International Group’s success of loss-reinsurance programs at the time peaked up $8.016 per gt of the premium of a crude tanker.

In another case, an Asian fleet paying $1.16 per gt was quoted $1.04 per gt for a 2002 built product tanker, although the club was already retaining only 28% of the gross premium.

Broker Mark Cockbain has suggested that churn could cost clubs as much as 7% a year in lost premium so the first 7.5% of general increase is needed to claw back the original position.

If churn is a key problem, growth of the world fleet and record newbuilding activity are making it a more central issue.