CHAIRMAN'S ANNUAL REVIEW

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2016 has been a very eventful year with major improvements in Club underwriting results, setbacks in investments, the successful introduction of Solvency II and the failure of the merger talks between UK & Britannia. The latter will likely deter future aspirants and reduce the likelihood of any further mergers, unless one party offers cash or shares to ensure there is an equitable balance of capital between the parties involved. P&I Clubs renounce mutuality at their own peril.

The Clubs have collectively had another very successful year, despite the fact that not a single Club had a positive return on investments after tax and currency losses. The IG collectively reported their 7th successive increase in free reserves to a new record high of over $4.7bn. We have been arguing for 3 consecutive renewals that the general increases demanded were not really necessary given the benign claims environment. Only now are the Clubs releasing monies from their over reserved claims to achieve record free reserves at a time when most Shipowner members have had to endure a sustained period of dire trading conditions.

Club finances saw a marked improvement in results despite weaker income levels, with only 14 IG Pool claims in the 2015 policy year, compared to 18 claims for the year earlier, although the estimated cost of those claims were slightly higher. The trend has been for minor improvements in the cost of attritional claims and a reduction in the frequency and severity of larger retained claims. The vast majority of Clubs also saw major improvements in their estimated cost of claims on earlier policy years. The continued rising cost of wreck removal claims is a real concern generally, but with the exception of "Alpine Eternity" there were no claims falling on the Group 'excess of loss' reinsurance programme.

Investment Managers had a torrid time resulting from historically low yields, a strong US dollar, falling equity values and a lack of "obvious" investment opportunities. The recent regulatory changes (Solvency II) has encouraged Club and Investment Managers to adopt more conservative investment policies and curb their enthusiasm for equities, as these performed particularly badly during 2015, delivering negative returns in excess of 10%. Some of the bonds produced positive returns, but overall the returns were also negative, leaving all Clubs with (modest) investment losses.

The Clubs with membership in the European Union single market, managed to pass a milestone by complying with the new Solvency II capital requirements, which finally came into effect in January 2016. This should reduce the Clubs' desire to continually build up their free reserves with no publicly stated upper limit / maximum. Once again we ask how large do the free reserves of a Mutual really need to be?

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The majority of Clubs in our view have sufficient funds to start delivering members discounts or other returns for earlier policy years, as well as halting, for the time being at least, the imposition of general increases. The likelihood of future investment income remains a concern, with no obvious solution other than perhaps for the Club Managers to focus on and maintain a low risk portfolio.

The next major obstacle for the UK based Clubs, many of whom have recently completed time-consuming corporate restructuring, will be continued membership of the EU single market as a consequence of the U.K. "Brexit" vote. The future status of Lloyd's will also be of concern to all Club Managers as a consequence of the IG reinsurance policies.

2016 policy year has thus far been favourable with no serious casualties and a steady stream of new buildings entering the market. These though remain extremely difficult times for Shipowners with reduced cargo volumes and low freight rates. We firmly believe whilst the current poor trading conditions persist and the trend of reduced claims continues, Owners expect and not unreasonably, these conditions to be reflected by their Clubs with no general increases, reduced rates and returns of premium.

Dudley Taylor
Chairman
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