Underwriters can't remain static in an ever changing market

In the final roundtable for HMIS 2015 we ask leading members of the market for their views on the reduced oil pricing on transportation and the challenges of insuring large and complex projects from a cargo and marine liability standpoint.

ON THE PANEL

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(CV)

Q: What is the impact of the reduced oil price on marine transportation? Positives? Negatives? How are brokers and insurers responding?

BB: In the short term, lower fuel prices have positively impacted marine transportation i.e. fuel is probably the number one expense in marine transportation, so reduced pricing is saving marine transportation companies a significant amount of money making operations less costly and improving profits on what is being transported. As one can imagine, decreased shipping costs has increased the volume of shipping. If somebody wants to get cargo somewhere, the reduced cost has initiated movement. Furthermore, with increased shipping profits and activity, there is a drive by some to increase vessel fleet size by acquisition or new builds. Lastly, since crude prices have been sporadic at best, this has caused the market to be a bit more conservative with moving crude, resulting in a demand for storage tankers i.e. tankers with crude sitting on anchor waiting for a price spike. The long term picture is much harder to envision as some speculate that the oil and gas industry is on a bit of a ledge, with producers taking cautious steps forward to see how far the drop might be while living on hedging until the end of 2015. This will make 2016 a bit of an adventure for everyone tied to the industry.

In general, the market is very competitive on most lines of business, but, individual results will still depend on the specific line of business and an insured's underwriting details. Unfortunately, for insurers, budgets were set for 2015 when the market looked much more positive, but that doesn't mean they don't have to meet their presented goals in a market that has spiralled downward. This has resulted in Insureds being presented multiple competitive options at renewal, if desired. For brokers, it has been important to help Insureds manage the very fine balance between market competitiveness and long-term relationships. Insurance has always cycled and the key to success is to manage appropriate long-term relationships while achieving optimal market results.

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JP: Certainly in the Gulf of Mexico we are seeing reduced OSV and related craft utilisations, crew reductions in force and a slowing of new OSV orders in shipyards. This has been offset, in some part, by steady activity in other parts of the world. In areas that are not connected with E&P activity, such as the Upper Rivers and Great Lakes region, we are seeing a very active and expanding marine transportation sector.

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Negatives are the reduction in activity and income to the vessel owners that quite often translates to reduced vessel maintenance budgets and corresponding work. In addition, historically the industry has seen an increase in reported mystery accidents during periods of slowed activity. Brokers are responding, as they always do, with increased calls for rating relief and increased lay-up alternatives. Insurers are working with their clients to address and manage the exposures.

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MB: As I mentioned previously this is a whole topic in itself and whilst I think that there are some obvious issues like ship owner overhead reduction and increased tanker freight rates, at Marsh we are looking at things from a different perspective. We are just about to publish a white paper on the issue of "Contango" and how that is impacting the tanker world and in turn Insurers and I think this could be a focus. From an Insurance perspective the issues of long term storage that have been brought about due to the opportunistic buying of crude are numerous :

- Degradation of crude quality as it settles can lead to quality claims
- Shortage claims due to "un-pump able sludge"
- Possible damage to storage tanks due to the long term storage of crude
- Main engine damage due to long periods of idleness
- Increased collision risks during ship to ship transfer.

There are other risks and I'd be delighted to share our white paper once it's had its' final edit. (hopefully early next week). Hope that this whets the appetite though.

MB: There is no difference from our perspective concerning an LNG construction project for export say versus say a refinery construction project for import say. The operational risk may (or may not be) more hazardous but not pre-operational. There is very little approach difference therefore from a DSU perspective.
From a liability perspective the risk is also fundamentally the same – the product is either "coming in" or "going out" so no real exposure differences.

Q: The US LNG terminal business is 'flipping the switch' from import to export. What are challenges insurers and brokers face in insuring such large and complex projects both from project cargo perspective and marine liability perspective?

CV: Exporting LNG presents an exciting opportunity for the U.S. economy. There are currently 6 approved LNG export terminals either under construction or planned, to supplement 4 import terminals. These projects which have been made possible by significant discoveries of shale gas in the U.S. in recent years, will generate over 10 bcfd in export capacity. Much of the specialised equipment which is needed to bring these projects to fruition is being shipped into the United States either to be assembled on site or in a modular fashion prior to being shipped to site. The equipment needed for an export facility will need to be built to more robust standards, and thus overall unit and project values may be higher than is the case with import terminals. Shipping of assembled modules will require significant heavy lifts and many shipments will need to be moved by barge. Risk engineering will need to be paramount so as to ensure that these shipments are received at site, damage free. The Project Cargo market is well prepared for these challenges. Liberty as a strong lead and the rest of the global project cargo market are fully capable of handling the large capacity requirement and risk engineering challenges that these projects represent, thus protecting the LNG industry from the effects of potential physical damage and significant business interruption.

BB: Below are some of the key challenges that both insurers and brokers face:

- Contractual risk complexity – when you move from importer to exporter, you may be subject to different terms and conditions than you are originally accustomed to. This creates potential gaps is risk which may or may not be known. When will risk of loss begin and end? Is it clear?
- Business risk complexity – depending on the importer/location, you have to think about political risk, trade credit risk, terrorism risk, piracy risk, etc.
- Insurance placement risk – making sure you are properly meeting warranty / survey obligations in insurance policies. Making sure qualified surveyors are performing the required surveys. Addressing proper limits as the size of the shipments increase. Properly addressing international regulations for pollution risk and making sure the right processes are in place for handling incidents.
- Regulation risk – must address regulations that impact marine transportation such as the Nairobi Convention and the Maritime Labour Convention.

Below are some of the key challenges that the shipper faces which can have an impact on insurers and brokers:

- International shipping concerns / challenges – depending on the destinations, the shipments will be subject to unknown familiar export controls, duties, taxes and regulations. Improper handling can result in fines, payments of unnecessary taxes, or confiscation. All exporters need to think about:

o Licensing to ship
o Clearing customs
o Proper handling
o Logistics and transhipment if needed
o Proper documentation
o Proper insurance (including meeting local admitted requirements in some countries)
oTaxation (VAT, etc)

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SD: While some marine risk has always been static in nature, it is undeniable that in recent decades more and more static property risk has found its way into marine portfolios. Not only are warehouses being scheduled, but with larger cargo ships we expect more port accumulation of cargo which is nearly impossible for underwriters to track in real time. So, this is definitely a challenge and Tianjin has taught us that this challenge deserves a robust response. Technology can assist here. There are real time satellite services available as well as GPS for larger/higher valued cargos. There are also models traditionally designed for natural catastrophe analysis that can be used to understand nearby 'industrial risk.' Beyond that, it is incumbent on underwriters to understand which of the world's ports are exposed to industrial risk and to understand how robust safety requirements are for industrial operators in those areas. It should go without saying that heavy trading in susceptible areas should be addressed with appropriate rate and terms for the risk.

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MB: Marine underwriters no longer work in isolation and the vast majority of them now use RMS/AIR or equivalent modelling vehicles to maintain an accurate record of their catastrophe exposure in the same way that their Non-Marine Property colleagues do. Indeed it is often the case that a Chief Underwriting Officer for a company or Lloyd's syndicate has line of sight across both Marine and Non-Marine practices ensuring that there is consistency of approach to underwriting static risks, irrespective of which Underwriter actually accepts the risk within their portfolio. However accurately assessing exposure can be tough, Tianjin is a good example of this with perhaps a higher than expected auto risk present at the time of loss.

BB: Cargo by nature is "moving" coverage. Large static accumulation is typically pretty easy to identify. Getting a real-time picture of normal static accumulation, by location, is more difficult.

MN: This is definitely a serious challenge, most recently highlighted by the catastrophe in Tianjin, where the main concern for marine insurers is how much exposure they actually have in such heavy industrialised areas. 'Accumulation' risks will undoubtedly increase with the continued industrialisation of emerging markets, ports and terminal expansions to accommodate the world's new breed of very large cargo ships, and their enhanced global trade routes amalgamated by the expansion of the Panama and Suez Canals. Typically, marine cargo underwriters will look to underwrite exposure and manage aggregates for known or assumed 'static risks' in natural catastrophe prone regions whether in the ordinary course of transit or not, but may in fact overlook external risk factors/perils – namely fire – from neighbouring occupancies. On a macro level, a fresher view will need to be taken with portfolio management through technology with the use of portfolio modelling and data systems to capture key risk information such as key trade routes and shipment limit profiles touching identified heavy industrial ports. And on an individual risk level, underwriting through detailed front end risk engineering for high valued goods and/or shipments or critical project cargoes is paramount.

Q: Training and development - With continual advancements in technology and continually changing industry dynamics and challenges in the maritime world, are we providing the right technical training and continuing to attract talent to the insurance industry for the long-term?

MB: Great question. We are certainly trying to do our bit at Marsh. We run 4 training courses a year in the UK and dozens more throughout the Globe. The key though is Global technological advance and I think that the main concern should perhaps be about the changing risk landscape that our clients are facing. How do we help them to understand that? For example the issue of Drone or "ghost" ships is an interesting one.

MN: The maritime industry is indeed dynamic and resilient when faced with challenge. And, like its respective insurers, it is a global business that is impacted by its own various economic market cycles and pressures, regulatory, and geopolitical issues. As insurers, we must continually be engaged with the industry to understand its challenges, adaptations and technological advancements in order to continue to provide unique and responsive insurance products. A renewed focus on training and development, particularly in the current challenging market environment, should be at the forefront for all marine insurers and surrounding professional organisations. Most underwriters or claims professionals may not have any experience in the maritime field. The maritime industry is very tangible and we must create new opportunities to physically experience it in order to understand it better on paper. Therefore, the right balance between formal internal training programmes, on the job learning and opportunities in the field will be critical to success.

"Only during the last 2 to 3 years have both brokers and insurers began really focusing on bringing new talent up to help fill the gap."

BB: In general, we are doing better. However, there has been limited marine insurance talent in the 35 to 55 year old range for a while. Only during the last 2 to 3 years have both brokers and insurers began really focusing on bringing new talent up to help fill the gap. The reality is the sun is setting on some peoples' careers and if both insurers and brokers do not take advantage of the wealth of knowledge they provide, it may be lost forever. Like insurance, education is still a people business. People need to train people. The talent is there but we all need to help the marine insurance industry transition the knowledge to the next generation of professionals. m&er

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