



NOVEMBER 21, 2016

CIRCULAR NO. 37/16

TO MEMBERS OF THE ASSOCIATION

Dear Member:

**RECENT CLUB PERFORMANCE.
DEVELOPMENT OF CLOSED AND OPEN POLICY YEARS.
RELEASE CALLS.
PREMIUM REQUIREMENTS FOR THE 2017 POLICY YEAR.**

At its recent meeting in Houston, your Board reviewed the American Club's present and prospective circumstances by reference to a variety of factors. These included the overall economic climate, the current state of the freight markets, the Club's recent operational performance, the nature of the present investment landscape and the implications of emerging trends within the P&I environment.

Against this background, your Board also analyzed the development of closed and open policy years. Having considered the Club's position in light of these several perspectives, a number of important decisions were made, including the determination of premium requirements for the 2017 policy year.

Recent Club performance

Over the last twelve months, the "churn effect" (the term applied to the reduction of premium volume as older, higher-rated vessels are replaced by newer, lower-rated ships) has continued to influence both the level of turnover and the risk profile of vessels entered in the Club, the more so as the freight market slump has endured.

Annualized premium income for 2016 has increased over the period since February 20. At the same time, the Club has experienced a comparatively larger rise in total tonnage and the average size of entered vessels, together with a reduction in their average age. These trends have combined to generate a reduction in the average net rate per ton. However, while pricing challenges persist, the Club's overall levels of rating continue to acquit themselves well by comparison with recent market norms.

As to claims, the Club's retained exposures have developed as expected over the first nine months of the current year. Claims for the Club's own account for 2016 are higher than they were for 2015 at the same point of emergence, but the frequency of underlying attritional exposures has been much the same in 2016 as it was during the previous year.

So far as the Pool is concerned, the 2013 through 2015 policy years continue to develop favorably, while claims for 2016, albeit at an early stage, are also emerging at a moderate pace. However, since large P&I losses tend to be volatile, it is impossible to say whether the current year will ultimately be less costly for pooling purposes than its predecessors. Nevertheless, present signs are encouraging.

On the investment front, the Club's portfolio, as of mid-November, 2016, had generated a year-to-date return of just over 2%. This compares with a yield of only 24 basis points at the same point twelve months earlier. Although market uncertainties persist, particularly in regard to continuingly sluggish global growth and concerns about the future direction of world trade following recent political developments on both sides of the Atlantic, it is hoped that investment earnings will continue to make a respectable contribution to global results over the months ahead.

Development of closed and open policy years

Closed policy years

There has been some degree of claims deterioration on closed policy years over the recent period. This, coupled with unrealized losses in the Club's investment portfolio as of September 30, 2016, has caused the Club's contingency fund to reduce by about \$1.5 million over the most recent quarter.

Accordingly, the excess of assets over liabilities for closed years, constituting the contingency fund, stood at \$64.5 million by comparison with \$66 million as of June 30, 2016.

Open policy years

2014

2014 is emerging in a manner similar to its predecessor year at the same stage of development. Retained claims are tracking at levels much in line with those of 2013 (which was closed in June, 2016), while Pool exposures to date are significantly lower.

Overall, the deficit for the year has improved from about \$9.7 million to \$7.9 million over the twelve months since September 30, 2015. There are grounds for optimism that this deficit will diminish as the year moves toward closure, scheduled to take place in June, 2017.

In the meantime, the release call margin for 2014 will be maintained at 12.5% of estimated total premium, having been reduced from the originally mandated figure of 20% twelve months ago.

2015

As foreshadowed in last year's pre-renewal commentary, both the Club's retained losses, and those to which it is exposed under the Pooling Agreement, remain significantly better than those of previous years. Accordingly, the year has moved into surplus as of September 30, 2016 (by about \$600,000), a trend which promises to gain further traction as the year moves toward closure, scheduled for the first half of 2018.

In the meantime, given an enduring potential for claims volatility, the release call margin for 2015 will remain at 15% of estimated total premium as amended downward – from the 20% originally mandated – in June, 2016.

2016

As mentioned above, attritional exposures for 2016 are broadly the same as they were for 2015 at the same stage of development. However, an increase in claims severity experienced at the

beginning of the year, and a continually conservative projection of ultimate losses, have combined to generate a deficit for the year at this early stage.

As has been the case in previous years, this deficit may be expected to reduce over time as investment earnings begin more significantly to contribute to overall results as the year moves toward closure. This is likely to take place in the first half of 2019.

In the meantime, the release call margin for 2016 will remain at 20% of estimated total premium as is presently the case.

Release calls

Following the European Commission's decision during 2012 to conclude its investigations into the International Group of P&I Clubs' claims sharing and reinsurance arrangements, all clubs have agreed to publish, at least annually, a statement of their release call percentages, including factors taken into account in calculating those percentages by reference to the actual assessment of enterprise and other risks.

The current release call margins for open years are set out above. As will be clear from the discussion of individual years' results, which represent the context for those margins, considerable thought has been devoted by your Board, in consultation with your Managers, in calibrating them.

Specifically, the following factors were taken into account in setting relevant release call percentages: premium risk, catastrophe risk, reserve risk, market risk and counterparty default risk, as well as the exposure of the Club generally to the wide variety of operational risks which, over time, it needs to consider in determining both its basic premium and, more particularly, release call needs in regard to all open policy years.

Premium requirements for the 2017 policy year

Many of the trends your Board identified last year are likely to influence the cost of P&I over the next twelve months. It has been hoped for several years that the outlook for shipping would get better as the global economy expands and, more particularly, international trade as a component of global GDP increases.

In the result, global economic development has remained mixed. Projections from several forecasting agencies have been revised downward over recent months. World GDP is currently projected to expand by just over 3% in 2016, a similar pace to 2015, with potential for a small uplift into 2017. This has informed a prediction that growth in global seaborne trade over the next year will emerge at a rate slightly higher than the 1.9% recorded in 2015, but below the 3.8% trend of 2011 through 2014.

However, recent political events on both sides of the Atlantic, particularly if greater protectionism begins to affect world trade, may disturb earlier projections. This makes the prospects for shipping rather uncertain.

As to the prospects for P&I, there has been significant pressure on premium rating over recent years. This is likely to continue. However, on the claims front, while the level of attritional losses continues to develop in comparatively benign manner, this trend cannot be expected to continue indefinitely. In any event, the size and volatility of large claims is always a matter of uncertainty.

Taking these, and other, considerations into account, the decisions set out below reflect a measured view of the business landscape which lies ahead, recognizing the difficulties bearing upon the shipping community at large while balancing the related perspectives of Members individually and of the Club as a whole.

Accordingly, your Board has adopted the following policy as to premium rating, and the application of deductibles, for the year commencing February 20, 2017.

Mutual Protection and Indemnity (P&I) Insurance

- All expiring estimated total premium to no (i.e. a zero) general increase.
- The component of premium represented by the Club's International Group reinsurance arrangements for 2017 to be adjusted separately.
- Premium to be defined as estimated total premium for 2017, subject to a zero (0) supplementary call forecast for the year.
- All estimated total premium to be debited in four equal installments due March 20, June 20, September 20 and December 20, 2017.
- Premium (call) to release to be charged as an additional margin of 20% of estimated total premium for the year.

Mutual Freight, Demurrage and Defense (FD&D) Insurance

- All expiring estimated total premium to have no (i.e. a zero) general increase.
- Such premium to be defined as estimated total premium for 2017, subject to a zero (0) supplementary call forecast for the year.
- All estimated total premium to be debited in two equal installments due March 20 and August 20, 2017.
- Premium (call) to release to be charged as an additional margin of 20% of estimated total premium for the year.

Fixed Premium Protection and Indemnity and Damage to Hull (DTH) Insurance

- All fixed premium P&I and DTH entries (e.g. those for charterers' risks) to have no (i.e. a zero) general increase.

Fixed Premium Freight, Demurrage and Defense Insurance

- All fixed premium FD&D entries (e.g. those for charterers' risks) to have no (i.e. a zero) general increase.

Having applied these guidelines as a first step in pricing the renewal of cover for 2017, Members' premium rates will be further reviewed against the background of their loss records, vessel-type

factors and other relevant matters, including the risk-based rating assessment of Members' individual circumstances, in consequence of which further adjustments may be made as appropriate.

In addition, expiring deductibles for all classes of business will be subject to the following changes for the forthcoming policy year, regardless of other factors as might inform the modification of deductible levels in the case of individual vessels or fleets:

- claims arising under the provisions of Class I, Rule 2, Section 14.4 will be subject to a minimum deductible of \$50,000 any one incident; and
- for vessels over fifteen (15) years of age, claims arising under the provisions of Class I, Rule 2, Section 13 will be subject to a minimum deductible of \$50,000 any one incident; and
- all expiring deductibles of less than \$10,000 will be increased by \$1,000 in every case, save that there will be a minimum deductible for all claims in respect of crew of \$7,500.

It will also be a condition for renewal that:

- all premiums and other sums due to the Club be fully paid up-to-date prior to February 20, 2017 as a condition of continuing cover; and
- all outstanding survey etc. requirements be completed prior to February 20, 2017 as a condition of continuing cover.

Summary

At a time of seemingly endless freight market recession, the need to reduce operating overhead remains at the top of the shipping industry's collective agenda. At the same time, it is not unreasonable to assume that claims costs, which have been subdued over recent years, will start to rise again as commodity prices continue their recent upward trend and the supply and demand for ships gains greater equilibrium over time, stimulating higher levels of utilization.

While giving as much price relief as possible in such difficult market conditions, your Board remains resolute in its commitment to consolidate the financial standing of the American Club, in light of the progress it has made in recent years and the new opportunities – including its recent investment in the hull sector through American Hellenic Hull Insurance Company Ltd. – which holds great promise for the future.

To recapitulate in brief the specific decisions reached, and described in greater detail above:

- 2014 exhibiting a deficit, but likely to improve toward closure expected in the first half of 2017. Release call to be maintained at 12.5% over and above current estimated total premium for the year.
- 2015 now emerging in surplus. Release call to be maintained, for the time being, at 15% over and above current estimated total premium for the year.
- 2016 exhibiting a deficit at this early stage of development, but circumstances likely to improve over time. Release call to be maintained at 20%.



- 2017 renewal to feature no (i.e. zero) general increase on expiring estimated total premium for mutual P&I entries. Group reinsurance cost component of premium to be adjusted separately. Premium to be characterized as estimated total premium for the year and to be debited in four equal installments. Release call 20% of estimated total premium.
- 2017 renewal to feature no (i.e. a zero) general increase in premium for both mutual and fixed FD&D covers. Release call 20% of estimated total premium for mutual entries.
- 2017 renewal also to feature no (i.e. zero) general increase in premium for fixed P&I and Damage to Hull (DTH) covers.
- 2017 renewal also to feature increases in, and minimum levels of, certain deductibles, as well as of deductibles for certain P&I risks, as specified above.

Your Managers will be in contact with individual Members with their proposals for renewal over the forthcoming weeks. If, in the meantime, any Members should require clarification in regard to the above, or generally, your Managers will be pleased to respond.

Yours faithfully,

Joseph E.M. Hughes, Chairman & CEO
Shipowners Claims Bureau, Inc., Managers for
THE AMERICAN CLUB