# No. 9 2009/2010 - Class 1 (P&I) Policy Year Balances and Mid Year Financial Update

September 2009

Dear Sirs

**CLASS 1 (P&I) POLICY YEAR BALANCES AND MID YEAR FINANCIAL UPDATE**

At their meeting on 23 September 2009 the Board reviewed the latest policy year balances as at August 2009. The Board also considered the Club's overall financial position at mid-year in the light of investment performance for the year to date.

**CLOSED POLICY YEARS (2006 and prior)**

Closed years now include 2006 which to date remains the most expensive year in the Club's history and for the Pool. Claims from other Clubs involving the Pool continue to be notified but the movements which have made the year so difficult to project now appear to be moderating.

**OPEN POLICY YEARS**

**2007/2008**

As previously advised, 2007 is another very expensive claims year for the Club although not as expensive overall as 2006. For claims involving the Club's own Members, the net cost of incurred claims appears similar to the net cost of Members' claims for 2006 at the same stage of development, but, so far, Pool claims seem less high despite further Pool claim notifications since February.

The year had an investment income allocation of $20 million in May 2008, which together with the additional call set in December 2008 (paid in August 2009) results in a small surplus. No further call is anticipated and the year is due to be closed in May 2010.

In the meantime, because the year benefits from retention and stop loss reinsurance, and because the investment outlook now appears less volatile than was thought likely when the release was set in December 2008, the Board has decided that the further release call of 30% shall be reduced to 15% with immediate effect.

**2008/2009**

The 2008 policy year, as reported in May on the basis of the February 2009 figures, continues to develop more favourably than the 2006 and 2007 policy years.

In February, the Board noted that the number of claims was not materially different from the previous 2 years but the frequency of larger losses involving the Club's Members was lower, as was the incurred cost of Pool claims. This trend has been maintained in the six months since year end to August 2009. The frequency of larger losses continues to be lower as does the cost of Pool claims. This is clearly positive.

The Board will review in May next year the 45% additional call set in December 2008 which is currently due for payment in 2 instalments in January and August 2010. Any adjustment that is considered would apply to the August instalment.

Although no change has been made to the call or to the timetable for payment, because incurred claims for the year continue to look more benign than was thought likely last December and because the investment outlook now appears more stable, the Board has decided that the further release call of 40% set at that time shall be reduced to 20% with immediate effect.

**2009/2010**

Any comment about incurred claims for a policy year which has a further six months until year end can only be tentative; future claims patterns can change dramatically without warning within a very short time.

Nevertheless for claims involving the Club's Members early indications for 2009 are more encouraging than for any year since 1998. For reasons which may relate to the reduction in the level of world trade, the frequency of claims occurring in the first six months of the year is down by some 25% when compared with the previous 7 policy years at the same stage of development. At the same time incurred claims costs for the Club's Members for the year to date are, on average, at only half the level observed for the years since 2002. Furthermore, whilst it is too early to comment on claims from other Clubs involving the Pool, preliminary figures do not indicate a return yet to the levels experienced by the Pool in 2006 and 2007.

Although the Board is encouraged by a positive start to the year, no adjustment has so far been made to the claims forecast for the year as set at the outset so that a small underwriting loss is still anticipated before any allocation from investment income. This also takes account of the likelihood that premium for the year may reduce to reflect an increased volume of laid up returns and cancellations for vessels being scrapped.

The Board has made no change to the forecast 30% additional call (due in August 2010) or to the further 30% release.

**INVESTMENT INCOME AND FREE RESERVES**

As reported in detail in the Club's latest Report and Accounts at February 2009, the Club experienced an unprecedented investment and currency loss during 2008 on all assets including property.

During the last few months of 2008 the Board suspended elements of its long standing investment policy, particularly in relation to portfolio rebalancing, and reduced the Club's positions in absolute return funds. The decision not to abandon the Club's investment strategy altogether and sell all equity and absolute return funds has however had a positive impact on investment performance since 20 February 2009 as some of the unrealized losses made during 2008 have since been recovered. By the end of August 2009, an overall investment return in excess of $40 million has been achieved for the year to date.

The Board is satisfied that the Club's present asset allocation remains appropriate, at least for the short term, although the general position will remain under review.

Based on the updated claims figures for all open and closed policy years as at August 2009, and on the half year position for the current policy year, 2009, the Club's overall free reserve has increased to a mid year figure of approximately $180 million. Whether or not this position will be maintained to 20 February 2010 will however depend on two factors of particular relevance when making any mid-year assessment.

* Whether or not claims for the second half of the current year will be in line with or worse than the initial forecast or will continue to follow the positive pattern experienced for the year so far.
* Whether or not the level of investment income earned for the year to date will be sustained until year end. Investment markets, whilst perhaps less likely to repeat the extremes of a year ago, remain volatile with the potential for substantial downward corrections before February 2010.

**ENTERED TONNAGE**

During the six months to August 2009, entered mutual tonnage has increased by approximately 2.2 million GT after taking account of vessels cancelled over the same period. Mutual entered tonnage is up from about 51.0 million GT at 20 February 2009 to about 53.2 million GT. So far there has been limited impact on either premium or entered tonnage from vessels being scrapped or laid-up. Whether or not the trend continues for the remainder of the year remains to be seen. At present many Owners have decided to maintain vessels in a state of readiness for trading in “hot” lay-up even where there is no immediate prospect of employment.

As usual, all the figures will be kept under regular review as the year progresses. Should Members or their brokers have any questions, please do not hesitate to raise them with the Managers in the usual way.

Yours faithfully
For: **West of England Insurance Services (Luxembourg) S.A.**
(As Managers)

**P E Spendlove**
Managing Director