Sjøassurandørernes Centralforening
The Central Union of Marine Underwriters
Oslo – Norway

CEFOR Annual Report 1999

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CHANGING ROLES TO MEET A NEW GLOBAL PERSPECTIVE

For decades the Norwegian insurance market has provided professional services to a global network of marine and energy clients. But like the global clients it serves, the Norwegian market is in a state of flux; adapting to new business demands, restructuring for effectiveness and consolidating for greater financial stability. Roles are changing. New business entities are appearing.

This year's CEFOR annual report once again presents a year-end summary of the insurance trends and statistics of the Norwegian insurance market. CEFOR's chairman (see page 2) is calling on marine and energy insurers to learn from their past mistakes and to redefine their roles, while brokers (see page 24) are saying its time to redefine the very nature of what they (insurance brokers) do. CEFOR's managing director (see page 4) sees change as an opportunity, an occasion to take a proactive approach and not to "follow the flock," but questions whether "the urge to merge" is always taking the client's best interest into account.

Consolidation and professionalism seem to be the keywords in shipping, marine insurance and every other major industry these days, says one shipowner (see page 10) while one energy client (see page 30) says that its insurance partners must create customised solutions and map out and maintain a comprehensive risk management strategy.

In the midst of change, the role of CEFOR remains the same: to help its insurance members to maintain a healthy equilibrium in an ever changing and challenging insurance environment.

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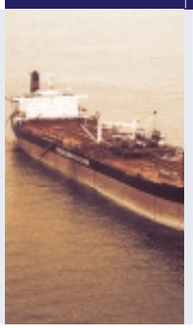

CLIENT:
"It is important that our insurance partners are reputable and concerned with improving our safety record."

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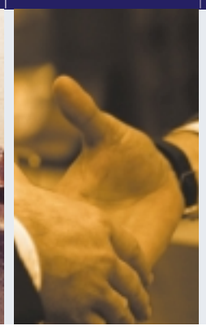
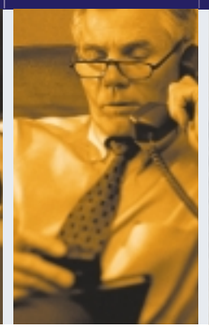


BROKER:
"Today's market demands cost-effective operational management and the ability to respond to business challenges."

Page 16



BROKER:
"There is a need to refine our work method... and to redefine the very nature of what we do."

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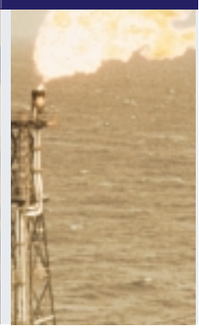

CLIENT:
"In a fast-moving industry, one fact is clear – the role of a quality insurance provider is expanding."

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RESTORING EQUILIBRIUM TO A TROUBLED MARKET

"In the energy market , the 10 – 15 largest players have sufficient capacity to absorb even the highest values"

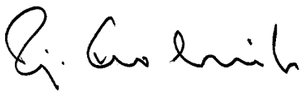
The marine and energy insurance market is currently suffering from heavy under-writing losses. This should not come as a surprise. Over recent years, warnings have sounded from all involved parties. Marine and energy underwriters continue to make the same mistakes. Due to the complexity and individual nature of risks, writing marine and energy insurance requires depth of experience. Why, then, does the market keep putting business on its books at rates and terms which they must know will produce deficit?

Previously, low accounting standards and lenient investors may have enabled marine underwriters to disguise poor results. However, managers and investors now measure return on capital quarterly, and they will only tolerate losses short-term if a timely return to profitability can be demonstrated. As the over-capacity situation endures, there will be no help from the market, or from disgruntled reinsurers who have either pulled out, or raised their prices and tightened terms. We are seeing signs of management losing its patience and deciding to withdraw from the market. However, a significant number will have to pull out before equilibrium is restored. In the energy market, the 10 – 15 largest players have sufficient capacity to absorb even the highest values, leaving room for few participants.

The wave of consolidations in the financial sector is aimed at managing capital and meeting competition in the global market more efficiently. We see initiatives to create synergies through client services between corporate companies and the mutual clubs. Products from the financial and insurance markets are beginning to converge. No doubt, by merging management operations, significant cost saving opportunities arise, as well as the opportunity to provide improved services to members and clients. Network technology will revolutionise distribution of goods and services.

Marine and energy insurers need to redefine their roles. Purely providing risk capacity in a subscription market has no future. Corporate enterprises are taking a new and broader approach to risk management, and are looking for new risk transfer solutions, normally tailor-made to the company's needs. We have to adapt ourselves correspondingly. Our industry has a tradition of offering individual risk solutions, and is prepared to meet the challenges of changing client needs.

In this process, CEFOR is looking to play an active role in further strengthening the marine insurance market in Norway, and to remaining a vital element in the Norwegian maritime cluster.



Bjarne Krokeide, Chairman, Cefor

"Change, undoubtedly, is inevitable in order to stay ahead in any business."

The end of a millennium represents in many ways a watershed: A time both for reflection and planning. In this year's annual report, we look back at a number of the recent changes in the industry and the possible future impact of these.

During the past year, the Norwegian marine insurance market has experienced significant changes. The joint initiative by Storebrand and Skandia to form a new Nordic property insurer gained further momentum by the establishment of if..., also including Finland's Pohjola. The marine and energy lines of if... have been accentuated by the creation of a separate management company together with P&I mutual Gard, thus pooling resources and capacity in an ambitious and exciting new venture. Zurich reorganised its Nordic activities and Zurich Protector is increasingly playing a key role on this scene. And finally, last autumn, Gjensidige Marine & Energy decided to withdraw from the energy insurance market and further changes have recently been announced whereby the marine activities will be restructured into the Gjensidige NOR Group. All these changes taking place at a time when marine insurance markets are witnessing the worst of times but also where the signs of hardening markets are showing.

Amid all these market changes, CEFOR's main challenge last year was to strengthen ties with all the marine insurance players on the Norwegian scene. Business as usual doesn't really prevail in a dynamic environment and the word "change" has been the order of the day also for CEFOR. Throughout 1999, we have been in close dialogue with Norway's mutual H&M and P&I clubs with a view to establish a more committing and productive structure for cooperation between the marine insurers. Four main areas for strengthening ties have been singled out, with activities defined from a cost/benefit point of view. The process has been further sparked by the above mentioned if.../Gard developments and the outcome may very well be a completely new and streamlined means of organising such joint activities.

In his 1953 novel "Fahrenheit 451", American novelist Ray Bradbury, penned the phrase "the sense of motion without moving". To me he could easily have been describing a feature of the present

THE SENSE OF MOTION WITHOUT MOVING?

global business environment. Change, undoubtedly, is inevitable in order to stay ahead in any business. Problems arise, however, when the only purpose for change is change itself. It seems that many of the mergers and acquisitions witnessed internationally have not mainly been driven by industrial arguments. Instead, they are results of sheer market adaptation and the constant push for increased, short term shareholder value. In my mind, it is a small paradox that a prerequisite for free market capitalism is free competition, yet capitalism's ultimate goal seems to be a state of oligopoly or even monopoly. How else to explain the megalomania witnessed during the last decade of the last millennium? The problem is that maintaining equilibrium between and within markets requires players of equal strength and bargaining power. Could it be that the driving force behind many of the changes we see is simply "microphobia"?

The roles are changing whether we like it or not. Norwegian marine insurers see this as an opportunity rather than a threat. The challenge now will be to take a pro-active approach to redefining our roles rather than a reactive, "follow the flock" mentality.

Tore Forsmo,
Managing Director, CEFOR

TRIMMING ACCOUNTS

"Over-capacity and strong market competition in international markets continue to cut into profits."

Gross premium income for direct marine insurance written in the Norwegian market in 1999 totalled USD 602.4 million (NOK 4,745 million), compared with USD 671 million (NOK 5,060.6 million) in 1998. In US dollars this represents a drop of 10 % (premiums for marine hull, energy and P&I insurance are paid in USD, which gained strength against the NOK throughout 1999).

Premium income has declined steadily for the past six years. The premium figures reflect the impact on the Norwegian market of the general fall in international marine insurance premium income in recent years. The Norwegian marine insurance market was, however, still able to exert its global position throughout 1999.

The most interesting development in 1999 was undoubtedly the decision to form if... through the amalgamation of the property and casualty insurance interests of Skandia (including Vesta Marine and Energy), Storebrand and Pohjola.

Ocean Hull

Premium income in the Norwegian market for 1999 amounted to USD 189.2 million (NOK 1,462.6 million), compared with USD 228.1 million (NOK 1,719.9 million) in 1998. The CEFOR companies accounted for 62.6 percent of premium income in 1999, and the mutual hull clubs accounted for 31.3 percent. Although the volume of the 1999 premiums represents a drop of 17 % compared with 1998, Norwegian hull insurers still maintain a high international profile. Around 80 percent of CEFOR companies' premium income is derived from foreign shipowners.

Over-capacity and strong competition in international markets continue to cut into profits. Competition between the Norwegian companies is still strong, and the battle for new domestic and international clients continues to exert pressure on premiums. However, several Norwegian companies have trimmed unprofitable accounts in order to position themselves to bid on more lucrative opportunities. The most significant example is Zurich Protector, which has halved its premium volume from 1998 to 1999.

CEFOR companies continue to place strong emphasis on compiling statistics for profitability and loss analyses through the Norwegian Marine Insurance Statistics (NoMIS) database. In 1999, electronic reporting was introduced, which enabled the CEFOR members to discontinue the facultative reinsurance facility.

Energy

The Norwegian energy insurance market experienced a minor decline in premium income from 1998 to 1999. Premium income totalled USD 63.2 million (NOK 545.8 m) in 1999, compared with USD 69.9 million (NOK 527 m) in 1998.

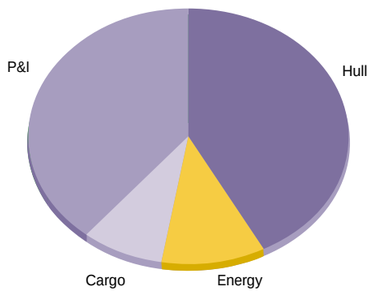
The global premium volume for energy insurance continues to decline, and with no reduction in the risk capital available for writing energy risks, the excess in capacity has put significant pressure on rating levels and operating margins. 1998 and 1999 have seen a surge in energy losses, and with less premium on their books, energy insurers face grim prospects if claims continue at these levels.

Excess of risk capital and lack of premium quality were leading factors in Gjensidige Marine & Energy's September 1999 decision to stop further acceptance of energy business in its present form. On the other hand, Storebrand and Vesta took a step to meet the demands of a dynamic future market by pooling their resources to create if...

P&I

The Norwegian P&I Clubs, Gard and Skuld, ended the 1999/2000 policy year by maintaining the status quo in

Gross written premiums, direct insurance 1999



USD 1 = NOK 7.73	NOKm	USDm	
Hull	1964.2	254.1	42.2 %
Energy	545.8	63.2	10.5 %
Cargo	387.0	50.1	8.3 %
P&I	1848.0	235.0	39.0 %
Total	**4745.0**	**602.4**	100.0 %

entered tonnage, and moderate reductions in premium levels, a reflection of competition in the international marine insurance market. On 20 February 2000, at the end of the policy year, the two clubs had owners' entries totalling 93 million gross tonnes. They also reported approximately 4 million gross tonnes of rigs and other mobile offshore units, and an average of over 55 million gross tonnes of charterers' entries for the year.

Due to the generally low premium level in marine insurance, the decline in overall premium income for own account was about USD 252 million as of 20 February 1999 and about USD 235 million at the end of the policy year.

The claims trend (excluding Pool), which rose by just under 10 % the previous year, levelled out during 1999 and the volume at year's end was about the same as for the previous year. Together with an improved financial outcome, this resulted in a moderate change in the clubs' total provisions for outstanding and unreported claims for own account.

Also this year, the reinsurance premiums showed a significant reduction.

Coastal and Fishing Vessels
Coastal and fishing vessel insurance basically applies to vessels trading along the Norwegian coast and in "limited North Sea trade", such as freighters, passenger vessels, ferries, supply vessels operating in the Norwegian sector of the North Sea and barges, as well as fishing vessels of all kinds and sizes, including industrial trawlers operating world wide.

Gross premium income amounted to USD 63.4 million (NOK 490 million) in 1999, compared with USD 66.4 million (NOK 500.5 million) in 1998. The CEFOR companies accounted for 56.2 % of premium income, while the Coastal Marine Clubs' Mutual Company (SGS) and the participating coastal marine clubs accounted for 41.5 percent. CEFOR members did not suffer any large total losses or many large particular average claims in 1999.

Competition still remained strong in 1999, particularly in the fishing vessel segment.

Loss ratios on many freighter accounts remained disastrously high and most of these risks were not renewed in the Norwegian market. By the end of 1999, there were signs of a hardening market.

Cargo
Premium income for cargo insurance totalled USD 49.8 million (NOK 385 million) in 1999, excluding war risks; a slight decline compared with 1998. Overall, losses were moderate in 1999. Vigorous competition in the Norwegian market still press premium levels. A couple of companies have increased their market share considerably at the expense of others. Mergers and acquisitions within Norwegian industry have influenced companies' choice of cargo underwriters. Shipment of fish and fish products continues to represent an important segment of the Norwegian cargo insurance market despite fierce competition among insurers, resulting in low rates and margins. Globally, Norwegian cargo insurers are seeing more claims resulting from floods and storms, presumably due to changing weather conditions.

Market shares, all sectors

	NOK mill.	USD mill.	
1. Ocean Hull			
Gjensidige	124.9	16.2	8.5 %
Industriforsikring	3.7	0.5	0.3 %
Storebrand	318.2	41.2	21.8 %
Vesta	340.9	44.1	23.3 %
Zurich Protector	127.2	16.5	8.7 %
Bergen Hull Club	307.1	39.7	21.0 %
Unitas	151.0	19.5	10.3 %
Fender	45.0	5.8	3.1 %
Gerling	44.6	5.8	3.0 %
Total	**1462.6**	**189.2**	100.0 %
War Risks	11.6	1.5	
2. Coastal and fishing			
Gjensidige	86.1	11.1	17.6 %
Storebrand	116.3	15.0	23.7 %
Vesta	69.4	9.0	14.2 %
Vår	3.3	0.4	0.7 %
Coastal Marine Clubs	203.3	26.3	41.5 %
Bergen Hull Club	11.6	1.5	2.4 %
Total	**490.0**	**63.4**	100.0 %
3. Energy			
Gjensidige	103.1	12.8	20.3 %
Storebrand	282.5	30.2	47.8 %
Vesta	102.8	12.8	20.3 %
Zurich Protector	57.4	7.4	11.7 %
Total	**545.8**	**63.2**	100.0 %
4. Cargo			
Total: All Insurers	385.0	49.8	
War Risks	2.0	0.3	
Total	**387.0**	**50.1**	
5. P&I			
Gard	1003.0	127.0	54.0 %
Skuld	845.0	108.0	46.0 %
Total	**1848.0**	**235.0**	100.0 %

INTERVIEW

THE DAYS WHEN SHIPOWNERS CUT DEALS WITH SUB-CONTRACTORS WITH A FRIENDLY CHAT ARE DRAWING TO A CLOSE. THE LAST TEN YEARS HAVE CREATED A MORE COMPETITIVE SHIPPING MARKET AND A MORE AGGRESSIVE REGULATORY ENVIRONMENT.

As a result, the loyalty and fellowship once felt at the negotiating table have been replaced by an emphasis on keywords such as financial responsibility, quality organisation, and risk management. Indeed, according to Norwegian shipowner Atle Bergshaven, "There are no alternatives to the most competitive bidder these days, in terms of price and quality."

Bergshaven and his family have been involved in global shipping for over half a century. Today the Bergshav Group's fleet consists of 16 wholly or partially-owned tankers, a car carrier, three container carriers and a number of new-buildings. Like many established family-oriented shipowners, Bergshav has felt the pinch of diminishing margins and noted the concomitant shift towards a strict, professional corporate culture.

"Today, business is transacted via a tender process much like that in the offshore and construction industries. Prospective sub-contractors must make – and customers demand – a coherent and professional presentation. The bottom line is important, but quality and coverage may often make the difference. People want to know not just the numbers, but what stands behind the numbers," says Bergshaven.

The current trend to closely examine figures and phrases that were once

"There are no alternatives to the most competitive bidder these days, in terms of price and quality."

Atle Bergshaven,
chairman – Bergshav Group.

Today the Bergshav Group's fleet consists of 16 wholly or partially-owned tankers, a car carrier, three container carriers and a number of new buildings.

taken for granted has had a domino effect on how the industry operates. As oil companies and other customers feel their profits squeezed by increased price competition, shipowners are forced to rationalise every expenditure and increase cost-effectiveness. Insurance brokers and underwriters, at the end of this chain, are thus under pressure to justify premiums and help shipowners reduce costs – in essence, help shipowners operate more safely and thereby reduce premiums.

"1990 marked a turning point in tanker operation. The Oil Pollution Act of 1990 forced the shipping industry to tighten its controls. In the late 80s and 90s some sub-par ships may have been operating internationally. Since 1990, insurance companies have had to ensure that their customers live up to the necessary standards; if they did not, port authorities, classification societies and charterers would do it for them," says Bergshaven.

Competitive premiums will always play a role when a shipowner looks to underwriters or marine insurance brokers, but new considerations are slowly filtering into the industry, such as name-recognition, clear financing and tight organisation. A shipowner's customers are showing more interest in how a shipowner runs his business. As a result, shipowners have to be more selective when choosing their sub-contractors and partners.

"When we begin to search for marine coverage, we are interested in both quality and capacity. It is important that our insurance partners are very reputable, competent and concerned with improving our safety record, thereby lowering our premiums. With respect to capacity, we expect our primary underwriters to have the resources and capital to cover a significant portion on their own books," says Bergshaven.

In the future, Bergshaven hopes that consolidation within the marine insurance industry will allow underwriters to provide complete marine coverage, including hull, off-hire, P&I and casualty in one neat package. He indicates that a shipowner like himself would be willing to pay more to obtain this service. And Bergshaven would also like to see the current trend towards long-term (two to three year) hull and machinery coverage extended to include P&I. Any change that reduces long-term risk and increases the shipowner's ability to forecast costs would be well received.

"Right now, Bergshav has 3-year hull and machinery coverage on many vessels. Altogether, insurance premiums account for seven to eight percent of vessel operation costs. This is quite good, but I expect to see premiums even out on a higher level over the next few years. The most important thing that a shipowner can ask from the industry regarding premiums is some stability; the last ten years have been too volatile," states Bergshaven.

Consolidation and professionalism seem to be the keywords in shipping, marine insurance and every other major industry these days. In the long-term, thin profit margins coupled with high risks are forcing the old-fashioned free-wheeling profiteers out of the market, and opening shipping to the savvy technicians and financiers of modern corporate culture.

Bergshaven sums up: "There will always be a bit of a mixed bag of players in shipping and marine insurance, but the trend is definitely towards larger, multinational organisations with highly professional attitudes and business relationships."

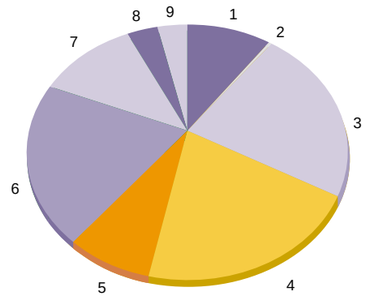
There are clear signs that we are getting closer to the end of the downcycle. The international ocean hull insurance market is a perfect market in the sense that there is free and full competition between a large number of individual players with no restrictive trade barriers or cartel agreements. The downcycle is created by an excess of risk capital in relation to demand, which drives prices down to a level that marginal suppliers cannot sustain. The purpose of market forces is to restore balance between supply and demand. Every week for the past six months we have read about companies that must pull out due to "overcapacity, a continuing soft market and a further deterioration in results". Another characteristic feature is the consolidation of capacity through mergers and acquisitions, creating fewer but stronger players. It is tempting to complain about the unremitting low rate level, but we should bear in mind that we cannot enjoy a better trading environment until excess capacity has been eliminated. A price level unsustainable to the marginal players is the most effective means to achieve equilibrium.

MARKET ACID TEST

The ability to handle this situation is the acid test for survivors. In most business operations, competent operators have a number of tools at their disposal. In a perfect market, no single supplier has any influence on the price, so we all have to adapt our actions to the price offered by the market. Fortunately, the market price for ocean hull insurance is not perfect. The main deficiency is that it makes too little distinction between good and inferior risks, simply because the majority of the players have so little knowledge of ship operation that they are unable to spot the difference. Herein lies the opportunity for the good underwriter to select a portfolio of quality operators that can better sustain a low premium level. Norwegian marine insurers have the great advantage of being part of a highly professional maritime environment that enables us to recruit people with profound knowledge of ship operation.

We say "better sustain" because the present rate level in ocean hull insurance is well below break-even also for the better half of the hull portfolio. The Norwegian ocean hull market incurred a considerable underwriting loss in 1999. Because the Norwegian market had braced itself for the downcycle, because Norwegian underwriters have the ability to select a better portfolio and thereby reduce losses, and because ocean hull insurance is a core activity in a national economy that boasts the third largest shipping fleet on the seven seas, Norway shall emerge from these market fluctuations among the winners. We have taken our share of consolidations to strengthen our financial position, prune operating costs and pool our resources. In the time to come we will continue to focus on cost-efficiency and the changing needs of our clients as their operating climate changes, and as enterprise risk management challenges traditional risk transfer solutions. But underneath the woes of a continuing soft market, Norwegian marine underwriters strive to enjoy the competitive climate because it offers the opportunity to show that we have the resilience and competence to beat the opposition. In the process we are aware that we have to produce an acceptable return to our capital providers over the cycle – a fundamental requirement of any commercial venture.

“A price level unsustainable to the marginal players is the most effective means to achieve equilibrium.”



CEFOR members

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War Risks	11.6	1.5	

The year 1999

In many ways, last year continued to reflect the gloomy state of international marine insurance, with few or no signs of an upswing in the market. However, activities in the Norwegian market were soaring and key marine underwriters are continuing to pool their resources and strengthen market co-operation.

Premium Transparency

One major market drive last year consisted of a joint effort between CEFOR companies, mutual clubs, marine insurance brokers and shipowners to establish an agreement for placing of marine risks through brokers. The push for greater transparency has internationally been lead by the Risk and Insurance Management Society (RIMS) in the USA and the Association of Insurance and Risk Managers in Industry and Commerce (AIRMIC) in the UK, with a focus on non-marine markets. The strong position of the maritime cluster in Norway has driven the industry to apply these principles in the field of marine insurance as well. Such a broker agreement partially embraces existing codes of conduct, issued by leading international brokers, and also reflects the well-established perception in the Norwegian market of “best practice”.

The joint process will continue into the new millennium and it is expected that all parties will accept the final document later this year. It will enter into force immediately thereafter and thus establishing itself globally as a unique market feature through its status as agreed document.

The Norwegian Maritime Law Commission – maritime enquiries or marine accident investigations ?

Norwegian marine underwriters were throughout 1999 actively engaged in the proceedings and outcome of the Norwegian Maritime Law Commission’s review of official maritime enquiries. The results of the Commission’s deliberations were issued in an official report towards the end of last year. Whenever a marine accident with a corresponding claim arises, it is in the interest of underwriters to establish the causal chain of events as early and as accurately as possible. The present Norwegian system of maritime enquiries has a reputation for inconsistent quality. There’s clearly a strong need for improvements.

The majority of the Commission proposes to abandon the institute of official maritime enquiries and instead establish a permanent independent marine accident investigation board. Although CEFOR members may question the wisdom of fragmenting the Norwegian maritime safety administration, it is nevertheless imperative that any restructuring does not imperil the functions and abilities of an efficient and well functioning Norwegian Maritime Directorate. It is expected that the official hearing will be completed in 2000 and specific proposals for amending the Norwegian Maritime Code will be proposed to the Norwegian parliament.

Classification Societies – machinery system damages and claims

For a number of years, machinery incidents have been the single most costly claims category for marine underwriters. In the period 1985 to 1997, Norwegian marine underwriters paid out a total of USD 650 million in machinery claims. There is little evi-

dence of improvements and last year CEFOR called on manufacturers as well as classification societies to face and deal with this challenge.

Last year, as part of a joint industry effort, CEFOR studied main engine claims in order to group these according to manufacturers and license builders. The study would determine if certain main engines have a higher degree of claims exposure than others.

Preliminary results indicate, not unexpectedly, that certain engines in the medium speed to high speed range are more prone to claims than the vast bulk of low speed installations. The study is expected to be completed by mid-2000 and its findings used to aid underwriters in their risk assessment. In addition, the industry hopes to use the study to confront machinery manufacturers and license builders with the objective to improve design and construction.

Classification societies and the day-to-day onboard operation of main engine installations must also shoulder some responsibility. From a marine insurance point of view it is extraordinary that classification societies are not putting more emphasis on operational aspects of machinery systems, which may be critical for managing the risk of such installations.

CEFOR expressed the opinion last year that class should verify that operational procedures have been established in the engine department and, thereafter, implemented and followed by those on board. In the process, relevant documentation, threshold parameters and recommendations from engine manufacturers and class should be available and known by those on board. This changes the focus to day-to-day activities and thus goes beyond formal competency requirements for crew and established planned maintenance systems with periodical interventions.

The three major classification societies and IACS have listened to these concerns and ideas with open minds, and new initiatives in this respect in the time to come are expected.

Quality Underwriting
In a bearish insurance market, underwriters' ability to select and manage risks may make the difference between failure and success. If the rates are "wrong", underwriters can at least ensure that the shipowners that they cover are "right". Last year the CEFOR Quality Committee started revising the CEFOR Quality Form. Preliminary results were presented to underwriters towards the end of the year. The CEFOR Quality Form has existed in the Norwegian market since the early 90's but has been left more or less to the discretion of each member company since 1996. The intention of ongoing revisions is to provide underwriters with a set of updated guidelines for better assessing technical and operational risks. Critical elements have been grouped in key categories such as "Vessels", "Institutional", "Organisation", "Commercial" and "Records". Each category possesses a set of criteria and guidance notes related to the various quality parameters. The final revised Quality Form will be released to market underwriters by the end of the year 2000.

Norwegian Marine Insurance Plan – Loss of Hire Conditions
The Norwegian Marine Insurance Plan (NMIP) has been actively followed up in order to keep insurance conditions competitive in an ever changing market. In 1999 CEFOR insurers focused on the loss of hire (LOH) conditions in Chapter 16 of the plan. A working group was formed to review clauses and its report has been presented to the Standing Revision Committee with a view to present a complete revised set of LOH-clauses in the next NMIP update (2001).

"From a marine insurance point of view it is extraordinary that classification societies are not putting more emphasis on operational aspects of machinery systems"

The Norwegian Insurance Academy – Training marine underwriters
Success in business is to a large extent dependent on a company's ability to manage its "human capital". Key elements are training and competence building.

The Norwegian marine insurance market depends on the services and quality of the Norwegian Insurance Academy (NIA).

NIA offers insurance-related training courses. It is financed by insurance company members and course fees. The marine insurance section of the courses offered by NIA was up for discussion and review within CEFOR last year. A two-year advanced study programme for marine claims handlers was completed last spring and generally regarded as hugely successful. The intention of CEFOR in the deliberations with NIA was to establish an equal emphasis on the remaining courses relevant to marine underwriting. CEFOR member companies have begun to address the need to provide teaching resources and allocate necessary time to training concerns. Furthermore, in order to communicate market training needs and requirements, CEFOR has established closer and more formal co-operation with NIA.

ISME
Information Solution Marine and Energy (ISME) has been a project in the Norwegian market since 1996. The project has produced a unique formatting standard for the electronic transaction of marine insurance risks between brokers and underwriters. Furthermore, ISME has developed a distribution channel using Internet technology together with a transaction database. Finally, the ISME application module has been a project output for those brokers or underwriters without production systems with basic data-import functions.

Like many "leading edge" IT-projects, ISME has run over budget and over time. Setting all blame and shame aside, the conclusion was made last year to lower ambitions in order to bring this marathon endeavour safely to completion by the year 2000.

R&D project: Next generation coastal ferries – Broad implications
The Norwegian Marine Technology Research Institute (MARINTEK) is currently running a programme with widespread support from the Norwegian maritime cluster. The programme will introduce tomorrow's technology in coastal ferry transport through aspects related to both design and operation. CEFOR has contributed to the project and served as a member of the reference group in 1999. Results related to simplification and streamlining of safety management systems under the ISM Code as well as a national maritime near-accident reporting system are of particular interest to underwriters. The programme will be completed in 2000 and the results have widespread application well beyond coastal ferry transport.

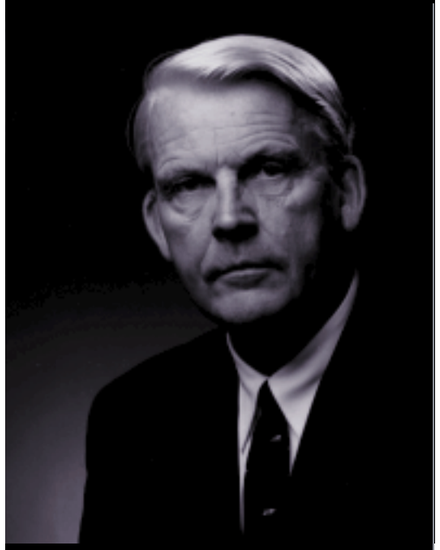
Premium collection – a common market approach
Last year, marine underwriters in the Norwegian market agreed to co-operate on a common position for collection of outstanding premiums. It is a well-known fact that marine insurers traditionally have offered "premium credits" totally unheard of in any other line of business. The purpose of this initiative is to agree on reasonable due dates for premium payment and procedures for how to handle outstanding payments and corresponding interests.

INTERVIEW

WITH UNSETTLING SPEED, TWO POWERFUL FORCES ARE CONVERGING IN THE MARINE INSURANCE INDUSTRY: A REDEFINING OF BUSINESS ROLES TO MEET A NEW GENERATION OF SHIPPING PROFESSIONALS AND THE URGE TO MERGE.

FREE TO MERGE



Aage Ditlev-Simonsen, chairman – Sev Dahl.

Established in 1867, Sev Dahl is the third largest insurance broking business in Norway with offices in Oslo, Stavanger, Trondheim and Bergen. The company, which has annual revenues of some £5 million, has been doing business with its new partner, Willis Group Limited, since 1914. Willis is one of the only three major risk management and insurance intermediary groups that operate on a worldwide basis.

"The biggest change likely to occur in brokering is a higher degree of accountability in all business practices and increased expertise."

Ten days before the dawn of the new millienium, Sev. Dahl Assurancekontor AS (Sev Dahl), one of Norway's longest standing and largest independent insurance brokers, announced the sale of its majority holding to the London-based international risk management consultant and insurance broker, Willis Group Limited.

"Today's shipping business is more about sound thinking than risks. Professional insurance, reinsurance and risk management advice are high on the shipowner agenda and Sev Dahl sensed a strong need to link up with an international organisation with strong professional resources and expertise," said Aage Ditlev-Simonsen, chairman, Sev Dahl.

According to Ditlev-Simonsen, shipping isn't getting riskier – it's just getting more demanding. Today's market demands cost-effective operational management and the ability to respond to business challenges in an increasingly global environment.

"Because of the tough business climate – risk management in all fields, including alternative risk transfer, captive management and financial risks, has become a vital part of our overall client service," said Ditlev–Simonsen.

Though most marine insurance brokers are talking about new goals and new products that go beyond the brokering norms of the 1990s, Ditlev-Simonsen is more concerned about designing outcomes.

"Like many of our competitors, we have developed new business products, but these new products must be a natural continuation of our business strategy. Before we introduce a new product, we must clarify our objectives, our means of achieving those objectives, and how to ensure that our customers and the organisation will benefit."

Is the role of the broker on the verge of being dramatically changed? "Demands for specialized services by our clients could result in a more diversified business portfolio, but a dramatic change in the broker's role is not likely," said Ditlev-Simonsen. "A first-class broker with a broad base of clients and a competent in-house consulting team – able to offer expert advice to owners about what they should do and obtain – will still be a wanted commodity by the shipowner," he says.

"Even the most clever risk manager cannot match a broker's expertise, especially in key areas such as insurance covers (comparing insurance conditions) legal expertise, long-term policies, clauses and review clauses," he says. Additionally, the broker will provide the underwriter with a volume of business that would cost significantly more to acquire independently, and shipowners will benefit from in house legal expertise and claims assistance.

Sev Dahl is taking a wait-and-see attitude prior to making final IT investments and introducing additional online broking applications. "Like other links in the insurance chain, brokers must communicate efficiently. And though IT is very necessary, it does not replace personal experience or relationships between underwriters, clients and brokers," maintains Ditlev-Simonsen.

The biggest change likely to occur in brokering is a higher degree of accountability in all business practices and increased expertise. Ditlev-Simonsen sees a future of expansion, both in human resources and corporate growth.

"Today's marine insurance broking company is not a commission-based business offering the cheapest rates. It's a professional service company built on clear lines of trust, respect and market expertise. Mergers and acquisitions aren't going to solve all problems. Our vision is to stay on top technically, utlilize the best people in the market, serve the best clients and to stay honest so we are respected by all sides."

ELECTRONIC REPORTING – A MAJOR STEP FORWARD

Since 1985, leading members of CEFOR have compiled and analysed statistical information relevant to their hull and machinery insurance portfolio. By the end of 1999, the Norwegian Marine Insurance Statistics (NoMIS) database had registered approximately 32,500 ship years and 14,200 claims. These figures encompass the underwriting years 1985 through 1998. In 1999 NoMIS membership comprised Gjensidige Marine & Energy, Storebrand, Vesta and Zurich Protector.

Electronic reporting – a major step forward

Until 1998, insurance data was compiled by appointing Norwegian Hull Statistics (NHS) as a compulsory facultative reinsurer; member companies ceded 0.1 percent of their lead hull and machinery insurance to NHS. In addition to customary information about premiums and claims, leading insurers also provided NHS with a detailed breakdown of claims.

In 1999, CEFOR introduced electronic reporting, which made the reinsurance facility superfluous. After the termination of NHS, all statistical information was transferred to a new Hull Statistics Committee within CEFOR. Insurance results from NoMIS are presented in the same way as in previous annual reports.

"In 1999, CEFOR introduced electronic reporting, which made the reinsurance facility superfluous"

Electronic reporting represents a major step forward in terms of data quality and integrity, amount of data reported, and the ability to continuously provide updated figures and analyses in a cost-efficient manner. With the new reporting system, all business is reported and all participants report their respective prices and shares. From 1997 to 1998, the number of coverages reported thus increased by 50 percent, primarily as a result of the inclusion of non-lead business.

Fleet Characteristics – 1998 cannot directly be compared with previous years

Due to the increased number of coverages in the reporting system in 1998, it is not possible to directly compare figures from 1998 and 1999 with previous years. The new fleet is not very different from the old fleet in terms of tonnage, class and age. Nevertheless, trends will have to be interpreted with caution as 50 percent of the 1998 fleet did not appear in previous statistics.

CEFOR companies underwrite a wide range of tonnage. Compared to world fleet averages, NoMIS includes a relatively low share of bulk carriers and a relatively high share of tankers (including chemical carriers and gas carriers). A variety of tonnage such as car carriers, passenger vessels and open-hatch carriers accounts for the remainder of tonnage in NoMIS. In 1998, tankers and bulk carriers comprised approximately 75% of the total deadweight tonnage in the NoMIS database.

The average age of vessels underwritten by CEFOR members in 1998 is 14.5 years, which is slightly lower than in 1997 **(Table 1)**. The average age of container carriers decreased, but for most other vessel types the average age has remained stable. CEFOR vessels are approximately one year younger than the world fleet average for comparable tonnage.

Det Norske Veritas, Lloyd's Register of Shipping and American Bureau of Shipping continue to be the leading classification societies for the CEFOR fleet. In terms of vessel numbers, Norway, Panama and Liberia flags of registration dominate.

Underwriting results are disappointing

For 1998, the marine hull portfolio monitored by NoMIS shows an actual loss ratio of 143% for reported claims. The final results are expected to be worse since a number of claims have incurred but not yet been reported (IBNR). With the inclusion of IBNR claims, based upon statistical estimate, the 1998 loss ratio is predicted to reach 170%.

The primary reason for the unfavourable development in results lies in the continued deterioration of premiums. The cash index in **Table 3** for renewed business shows that premiums are, on average, down 19 percent from 1997 to 1998. Premiums have dropped an additional 11 percent in 1999.

It is disconcerting that for 1998 we see both an increase in the number of claims and an increase in the average cost of claims per dwt. This runs contrary to the positive trend we experienced earlier in the 1990s. There is a frequency increase in almost all categories, and in particular for machinery claims. In addition, a number of large claims have negatively affected results in 1998 and 1999.

For most vessel types (such as tank, bulk, gas, and chemical), the average deductible remains relatively unchanged in 1998 and 1999. The figures for 1998

Table 1
A typical Vessel

Underwriting Year	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**		
Number of fleets	306	284	274	244	245	255	314	445	965		2)
Number of vessels	2 311	2 334	2 424	2 307	2 490	2 702	3 552	4 543	6 731		
(F)DWT (millions)	116	132	141	140	151	164	182	218	308		
Number of Claims	1 854	1 466	824	699	671	634	785	980	1 911		
Average	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	3)
Size (F)DWT	50 750	56757	58110	60 663	60 623	60 703	57 087	51 314	48 204	52 294	
Age (years)	13.4	13.1	13.5	13.5	13.1	12.6	14.5	15.0	14.5	14.5	
Value (USDm)	14.2	15.7	15.9	18.3	21.7	21.9	19.5	18.1	22.9	19.9	
Deductible (USD)	35 578	54 280	97 696	129 721	211 864	212 320	193 990	156 352	131 963	148 051	4)
Net Premium (USD)	81 935	99 513	123 032	154 120	145 723	123 646	87 792	61 468	53 741	45 665	
Claim (USD)	186 629	121 483	88 422	72 477	69 082	75 579	60 571	62 942	76 799		
Claim frequency	0.87	0.68	0.38	0.33	0.28	0.26	0.24	0.22	0.31		
Loss Ratio (%)	228 %	122 %	72 %	47 %	47 %	61 %	69 %	102 %	143 %		1)

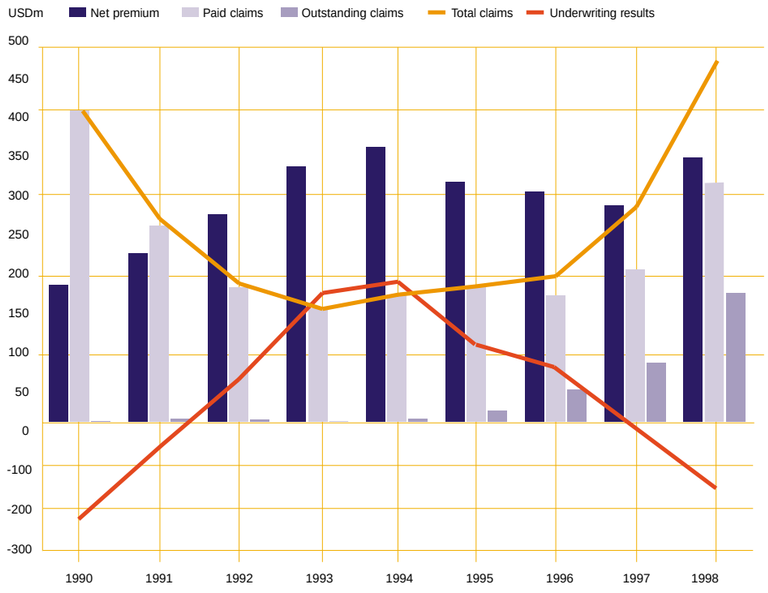
1) The figures in Table 1 are 100% figures per vessel underwritten by CEFOR companies. The same figures based on the actual shares placed in the CEFOR market show a loss ratio for 1998 of 130%.

2) The number of coverages reported increased by 50% from 1997 to 1998 primarily as a result of the inclusion of non-lead business.

3) For 1999, only the average vessel figures have been included as current data on premiums and claims are not yet representative for the underwriting year. The cash premium index for 1999 shows an 11% decrease in premium for renewed business. L/R for 1999 per 31.12.99 amounted to 67%. At this time, this figure includes a major share of total premiums and a minor share of total claims. Predicted L/R for 1999 (including IBNR) is 200%, see Table 4.

4) The decrease in average deductible per vessel from 1997 to 1998 is primarily due to changes in the fleet of "other" tonnage. The average deductible for tank and bulk and most other standard vessel types has remained stable from 1997 to 1998. Deductibles also appear stable in 1999.

Table 2
Underwriting results per 31-12-1999
Total results for all risks registered by NoMIS



compared to 1997 show for all vessels a decline in the average deductible per vessel. However, for vessels such as tankers and bulk carriers, deductibles remained relatively stable.

Worse results to come despite trend shift

Marine hull underwriters continued to suffer losses in 1998, and results are expected to be even worse in 1999. However, until recently, it was possible to purchase reinsurance at competitive rates. This is no longer the case as dramatic changes took place during 1999. The first change occurred in the retrocession market (reinsurer's reinsurance), where there premiums increased between 20 and 30 percent. Thereafter, reinsurers involved in the low-level market either disappeared completely or toughened their terms substantially. With no protective reinsurance programs available, underwriters will have to retain more risk and begin paying their own losses.

Table 2 shows the fall in premiums since 1994, and the loss ratio for 1998 is expected to end at 170 percent. This means a 70 percent premium rate increase is needed, before operating costs, in order to show profit. Nevertheless, 1999 gave a general 11 percent reduction in premiums.

Due to the high loss ratios and lack of competitive reinsurance, CEFOR forecasts that the year 2000 will show substantial rate increases for some of the accounts coming up for renewal in 2001. The overall increase will, however, be levelled out by the large amount of long-term contracts, and, on average, marine hull and machinery insurance will still be far from profitable in the immediate future.

The availability of capital has been the main concern of the marine insurance industry in the late 1990's, and future supply of marine insurance capacity is not likely to be a problem. On the other hand, professional capital will not stay long in a losing market, and investors' demand for return on equity will again have an effect on prices. The prognosis in **Table 4** is based on an average estimated premium increase of 10 percent in 2000 and 12 percent in 2001. With regard to claims, CEFOR forecasts a stable picture for 1999, 2000 and 2001. This results in average loss ratios as follows: 1997 – 110 percent; 1998 – 170 percent; 1999 – 200 percent; 2000 – 180 percent; 2001 – 160 percent. To sum up, fiscal signs point to a turnaround from the negative developments of recent years; unfortunately, this gradual upturn has not reached the point at which marine underwriting becomes profitable again for all insurers.

Increased claims frequency and claims cost

In 1998, CEFOR members experienced an overall increase in claims frequency compounded by a number of large claims. This increased the claims cost per dwt insured in 1998 compared to 1997. There is, however, one positive element: the average cost of most claims decreased. A limited number of large claims due to fire and explosion and grounding resulted in significant costs for these categories.

Table 5 shows the development in number and cost of claims adjusted for increase in number of vessels for the underwriting years 1994 through 1998, with an increased frequency in all claims types and with machinery claims

Table 3
Indexed key factors
1990 = 100 %

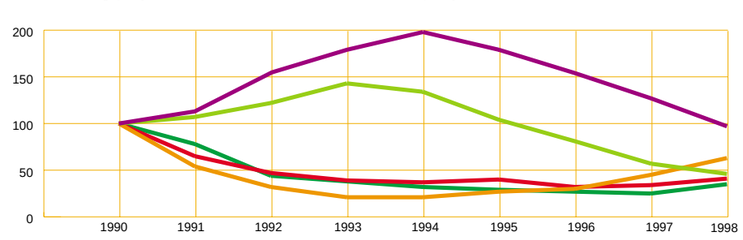
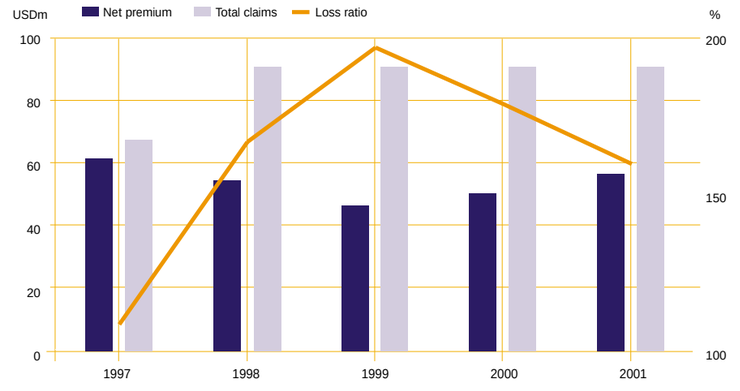


Table 4
Estimated Loss Ratio 1997 - 2001
Figures per 1000 vessels

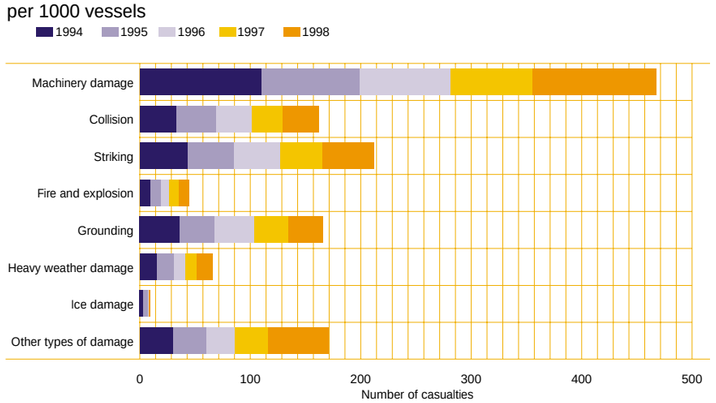


as the most frequent. The breakdown of the 1998 figures according to claims categories is shown in **Table 6.** Although high in frequency, the average cost of a machinery claim is relatively modest; machinery claims accounted for 19 percent of total claims costs.

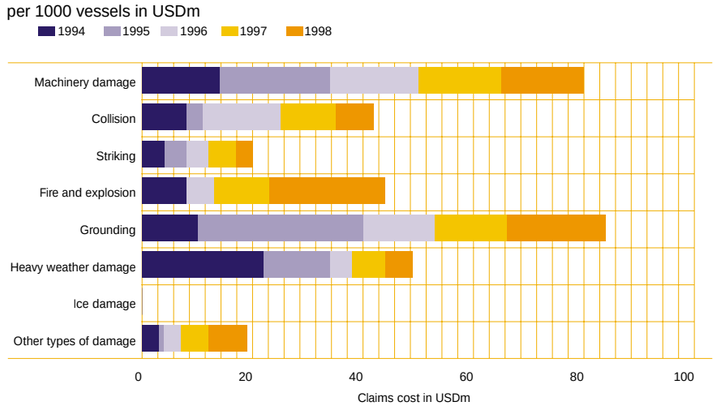
Fire and explosion, on the other hand, represents 27 percent of the claims cost, but only 3 percent of the number of claims; grounding accounts for 24 percent of the cost and 10 percent of the number of claims.

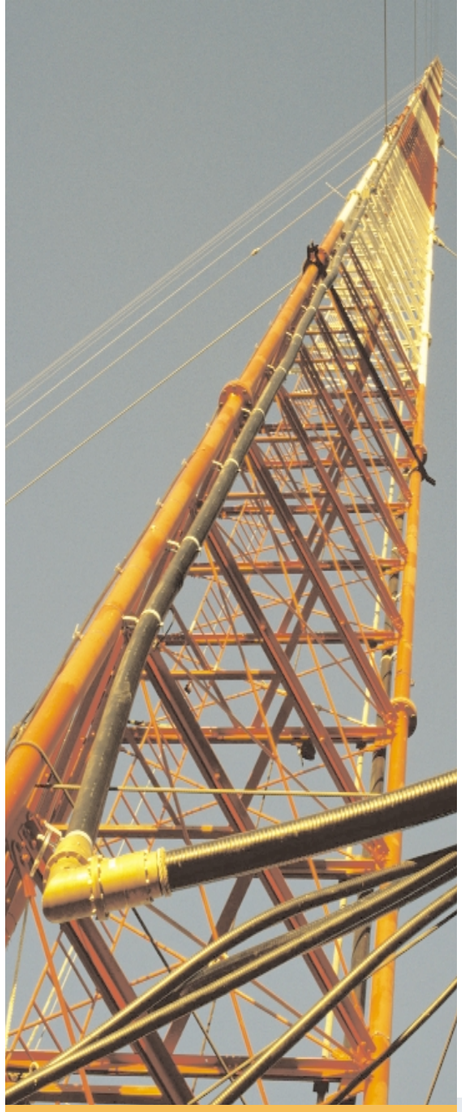
Can shipowners afford to maintain their vessels ?
In general, claims developments depend on the structure and the quality of the world fleet. The quality of the fleet depends on a number of factors, such as average age of vessels, operational competence and dedication, financial situation, freight markets, regulatory quality and safety initiatives, new technological developments, etc. Shipowners face a number of requirements affecting quality and have to comply with rules and regulations from different authorities, class societies, flag and port States, and cargo owners. It is, however, difficult to measure the immediate impacts of new requirements. The ISM Code became mandatory in 1998 without many of the feared difficulties, and it is believed that the Code will have

Table 5
Number of Claims per type of casualty
per 1000 vessels



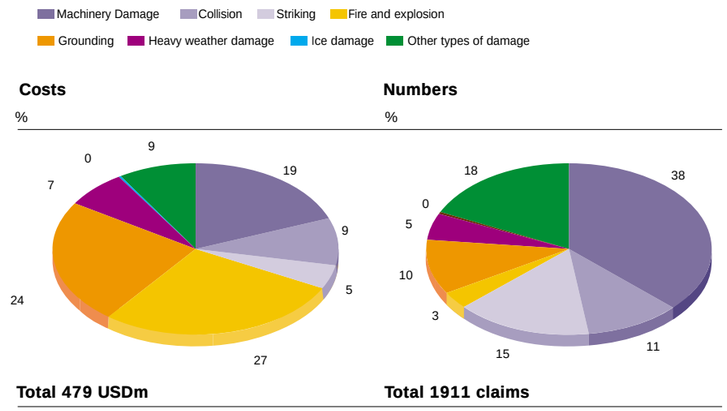
Claims Cost per type of casualty
per 1000 vessels in USDm





"There is an increasing difference between the quality conscious shipowner and the sub-standard operator. "

Table 6
Claims 1998



a long-term effect on safety and quality. A major concern is the quality of seafarers and the availability of trained personnel for the existing world fleet.

In addition, demand is expected to increase as a result of the number of newbuildings on order. The revised STCW Convention, STCW 95, will be a tool to improve personnel qualifications, and may also assist third parties in evaluating the standard of the crew.

1998 was a poor year for freight rates in most shipping segments, and 1999 did not bring the desired recovery. Freight volume increased, but freight rates remained low.

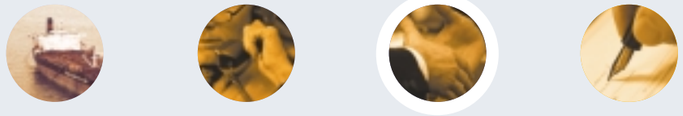
The rate of scrapping decreased, while market speculations led to a significant increase in new orders. Unfortunately (in terms of future quality of the fleet) an increasing number of investors have ordered vessels on speculation, with the intention to sell either the contract or the vessel within a short period.

Additionally, hardened competition and new international requirements have made it expensive and difficult to be small, and there have been a number of mergers in recent years. This consolidation has also been necessary from a market equilibrium point of view to counterbalance many of the acquisitions and mergers on the cargo owners' side. There is an increasing difference between the quality conscious shipowner and the sub-standard operator. During a period of low freight rates, owners may have difficulty keeping vessels properly maintained. Due to low prices for scrap, some choose to continue trading the old vessels for a few additional years without investing the necessary money to repair and maintain them. Premiums for marine insurance are currently very low, and there is little price differential between the favourable risks and the less favourable risks, but the difference in profitability will be significant depending on the ability to accurately select and underwrite the good risks.

INTERVIEW

IN THE EARLY YEARS, THE SHIPPING INDUSTRY WAS RUN BY AN INFORMAL NETWORK OF SHIPOWNERS, INSURERS AND BROKERS WHO ALL KNEW EACH OTHER BY NAME. THIS "OLD BOYS NETWORK" RELIED ON COSY ARRANGEMENTS BETWEEN EXECUTIVES WHO DISCUSSED CONTRACT TERMS OVER FRIENDLY DINNERS AND SEALED AGREEMENTS WITH HANDSHAKES.

OUR ROLE IN A CHANGING MARKET



Operating in the thick of this environment were insurance brokers, the middlemen who negotiated deals between ship owners and underwriters all over the world. Today, thanks in part to a gradual process of globalisation and the rise of new technology, the role of insurance brokers has changed dramatically.

According to Stig G. Andersen, managing director of Aon Grieg, insurance brokers can no longer survive on transaction fees and commissions alone; They must provide consulting services as well. "Our revenue is more and more based on fees providing consulting services," says Andersen. "Our role as brokers has changed from agent to advisor." Consulting is not simply a value-added service. For insurance brokers who want to survive, it is a key source of revenue.

Stig G. Andersen,
managing director – Aon Grieg,

With the market demanding increasingly sophisticated services, the broker company Aon Grieg has acted quickly to position itself as an industry leader.

"Consulting is not simply a value-added service. For insurance brokers who want to survive, it is a key source of revenue."

Andersen says that this trend is a result of gradual changes in the industry, characterised by fewer, bigger players competing for customers with increasingly specific demands. And since commission fees are "transparent," meaning the client always knows what commission the broker earns, the negotiation process for these fees has become standardised. This places additional pressure on both insurers and brokers to refine their expertise in risk assessment and claims management, and to constantly develop new products and refine services.

Andersen says: "The only thing we know for sure is that we will all experience a constant and all embracing change. There is a need in our business not only to refine our work methods to make it more efficient through technology, but to redefine the very nature of what we do."

Understanding their customers is the key to Aon Grieg's approach to gaining market share. Ten years ago, shipping companies would approach brokers for the sole purpose of negotiating insurance agreements with underwriters. Today, Marine & Energy clients are more likely to use brokers to provide insurance and business solutions to their total risk situation in order to make their clients more cost-efficient.

Indeed, before going to the market looking for the best insurance agreement, brokers at Aon Grieg first perform a comprehensive risk evaluation to determine the client's risk exposure, how they manage risk, and what insurance solutions fit a specific product. This evaluation not only defines risk accurately, it is the basis for recommending changes that are designed to improve a company's bottom line.

This holistic approach to client services has forced Aon Grieg to offer an increasingly broad range of services, and changed how the company looks at the relationship between risk and insurance. "Insurance is only one way to meet our clients' demands," says Andersen. "Our greatest asset is our ability to define and evaluate risk."

With the market demanding increasingly sophisticated services, Aon Grieg has acted quickly to position itself as an industry leader. Indeed, with Grieg's recent partnering with Aon, the brokerage has a greater international exposure. The company has also invested in IT, developing new products, and recruiting top personnel. While the company has made use of new technologies to process documentation and improve communications, recent software developments have helped streamline essential services, including quality control recommendations and risk modelling.

Years ago, risk evaluations were determined by broker experience and technical considerations. Today, computer technology allows for more comprehensive risk modelling, providing more accurate information. This information can then be applied to improve quality assurance, cost efficiency and management structure. Thanks in part to computer technology, the company can customise a business and insurance solution that best fits the customer's needs.

As quickly as many insurance brokers have adapted to the changing market, Andersen believes that the industry faces greater challenges in the future. Referring to a recently completed evaluation by McKinsey & Company, Andersen insists that the future of the insurance brokers is inexorably tied to the future of underwriters.

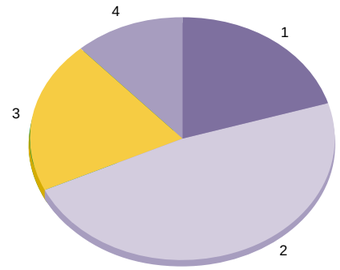
In the meantime, Aon Grieg will continue to meet the demands of a fast-changing market. "Once we establish ourselves, we are limited only by our own creativity," says Andersen.

SIGNS OF A HARDENING MARKET

It has been a tough year for the Norwegian energy insurance market, as with most other similar insurance markets abroad. In Norway, premium volume dropped from USD 69.9 million to USD 63.2 million in 1999, partly due to deflated rate levels and operating margins. Couple this reduced volume with a surge in market losses, and the result is a loss-incurring energy risk portfolio for all insurers who write an international book of business. The present rate levels simply cannot sustain the losses incurred.

Reflecting the prevailing market conditions during 1999, the four companies have reviewed their operations and market positions, and decided on some very tough measures.

Most drastic was the decision by Gjensidige to withdraw from the energy insurance market effective the last quarter of 1999. The move was triggered by the company's sober look at its market position, and the conclusion that expected future earnings would not meet the required rate of return on the substantial capital allocated to the energy sector. Earlier in the year, the two largest writers in the market, Storebrand and Vesta, agreed to pool their resources, consolidating their capacity and staff into a specialised marine and energy business area within the new Nordic property and casualty company, If P&C Insurance Ltd. The merger creates a powerful new partnership, well positioned to meet the demands of a dynamic future market. Meanwhile, Zurich Protector was assigned a new role within the Global Energy operations of the Zurich Group to focus primarily on developing business in the Nordic and Baltic area. The result of all these industry changes is a totally restructured Norwegian market for energy insurance.



USD 1 = NOK 7.73	NOKm	USDm	%
1 Gjensidige	103.1	12.8	20.3 %
2 Storebrand	282.5	30.2	47.8 %
3 Vesta	102.8	12.8	20.3 %
4 Zurich Protector	57.4	7.4	11.7 %
Total	**545.8**	**63.2**	100.0 %

The International Energy Insurance Market

Last year we predicted that the market would worsen before it improved. Unfortunately, our prediction was correct. The global premium volume for energy insurance continues to fall. And with no reduction in the risk capital available for writing energy risks, the excess in capacity produces further pressure on rating levels and operating margins. However, if we divide the total market into segments, wide variations in loss ratios between the individual segment areas become apparent. Variations in operating quality most likely exist between the segments as well. This leads us to suspect similar discrepancies in underwriting results between markets and between individual insurers in major markets. Over-capacity always leads to a decline in underwriting discipline, and any premium differentiation between good and inferior risks achieved in a hard market are levelled out. In this climate, an insurer can only hope to make a profit if he has selectively acquired the right portfolio mix, in respect to both market segments and client quality.

"Over-capacity always leads to a decline in underwriting discipline."

There are clear signs of a hardening market. Again, the direct insurers are not the ones instigating the market

change, but rather the reinsurance market. This should not come as a surprise to those who understand how the energy insurance market operates. In last year's report, we described the "two-tier market" phenomenon where direct insurers relieve themselves of the most unwanted part of the risk at a fraction of the original premium by accessing a facultative reinsurance market – the second tier. Inevitably, this sector was the first hit by unacceptable loss ratios, forcing them to pull out of the market during 1999. This in turn triggered a chain reaction. The direct insurers, who can no longer factor a cheap relief option into their quotes, must price risks more realistically. A simultaneous decline in the retrocession market is similarly affecting loss excess re-insurers who must also raise their prices, resulting in higher re-insurance costs for the direct insurers.

Premiums are rising, but very selectively. The fundamental problem is the excess risk capital in the market – a situation which will most likely be permanent. However, one thing has changed. Capital backing for some of the international market's key players, such as Lloyd's underwriters, is now corporate and demanding an acceptable return – whereas in the past it was private and more concerned with tax breaks. At present rate levels, with no access to cheap reinsurance, these underwriters cannot provide an acceptable return. And as a result, we are witnessing the first signs of corporate investors pulling out. They have had four years of profit, but are now most likely looking ahead to four years of losses – 1997 through 2000. Premiums must rise, but this can only be achieved through the loss-incurring segment of the portfolio. As long as there are too many insurers chasing too little premium, no insurer will attempt to raise rates on attractive risks for fear of losing the account to a competitor.

"…these "commodity" suppliers are bound for extinction."

We have witnessed 300 to 400 percent rate increases on construction risks. We can only refer to comments in last year's report to explain why this was bound to happen. Control of well rates have also risen as a result of poor performance in this segment of the portfolio. Some large losses due to fire and explosions in refineries and petrochemical plants have had a sobering effect on rate levels for this market segment. However, for the majority of the energy portfolio, rates will remain low as we enter a new millennium. A considerable number of accounts are still on long-term agreements with built-in renewal discounts. Here, rates will drop an additional five to 10 percent.

The global energy premium volume is insufficient to sustain the available risk capital. The critical survival factor will be the ability to write a significant portfolio of quality risks. Oil and gas companies, and their brokers, are sophisticated insurance buyers looking for the right mix of good and stable security, and competitive price. The 20 largest insurers in the market offer more than adequate capacity and security, competitive pricing and professional client service. These companies will be able to see a good cross-section of risks, and to select a quality portfolio. The other players will remain in the "commodity" section of the market. The only benefit they can offer is capacity, and they will largely be picking up risks which have been rejected by larger, professional insurers. However, as the operating margins in this category are insufficient, these "commodity" suppliers are bound for extinction. Therefore, we will continue to see a consolidation of the market until we have a better balance between supply and demand for risk capital.

A broader definition of risk management will require new solutions

Two factors will contribute to a great change in the energy insurance market as we enter a new millennium:

- Continued consolidation in the oil and gas industry creating companies with the financial strength to retain more risk, thereby requiring less traditional insurance.

- Greater focus from investors on a company's ability to manage risks and provide a stable return on shareholders' equity.

Enterprise risk management aims at identifying the broadest possible spectrum of risks which can affect the company's financial performance in respect to assets, liabilities and earnings volatility. Only a small – and diminishing – segment of an oil company's total risk exposure is insured, which is why the premium volume is declining. At the same time, financial instruments are being applied to offer risk protection. And as the barriers between insurance and other financial institutions are being eliminated, the term, ART – Alternative Risk Transfer – is being adopted into the insurance vocabulary. Energy insurers need to broaden their range of products and offer entirely new risk solutions in order to maintain a viable business relationship with their clients.

We see a trend where new risk financing solutions are tailor-made to the individual client's needs. This places the insurer in a position where he has less opportunity to spread his risk over a homogenous portfolio, and apply traditional models to calculate the risk price. However, to some extent, this can be compensated by spreading the risk along the time-axis by extending the contract period. Companies also face restrictions in ceding parts of such risk solutions to the reinsurance market on a contractual basis. Companies which offer this type of product must be financially fit in able to retain the risk on their own books.

Most new risk solutions are a combination of capital market and traditional risk products. To better serve this changing market, insurance companies need to broaden the skill base of their underwriters to understand, assess and underwrite these integrated products. Their ability to deal with non-tradable exposures puts insurers in a good position to meet clients demand for integrated risk solutions. Brokers and underwriters are accustomed to concluding contractual relations of great financial impact swiftly and efficiently without the involvement of lawyers. This gives the insurance market an important competitive advantage. There are a number of challenging opportunities facing the energy insurance market as we enter the new millennium. Our ability to grasp these opportunities will decide our position in the future integrated risk market.

The Millennium Bug Issue.

It must have been a relief to everyone to witness the dawn of a new millennium – without any of the major problems or disasters that had been predicted. Some people have suggested that the Y2K computer anxiety was all inflated hype generated by the software industry to boost income. Like most parties closely involved in Y2K preparation projects, we realise that the very reason for the smooth transition was most likely the tremendous effort made to identify potential system failures and make the necessary amendments. We maintained that the Y2K hazard was a risk management issue rather than a computer problem. We are pleased to see that the industry tackled this matter in a very professional manner.

One unexpected aspect of the Y2K issue alarming the insurance market is the attempt by some companies to secure coverage for their Y2K expenses under the "sue and labour" clause in their policies. The intention of this clause is to give coverage for expenses incurred to avoid or minimise a loss which would be recoverable under the policy. Most insurers will argue, and with considerable support from our legal advisors, that a failure in a computer system due to a Y2K-related incident does not constitute a physical loss recoverable under the policy. Consequently, we would not accept that expenses incurred to avoid a computer date recognition problem as recoverable "sue and labour" costs.

Y2K expenses are incurred for the sole purpose of ensuring that a computer system required for the efficient operation of the enterprise continues to operate past a certain date. In our view, it is well beyond the intention of the "sue and labour" clause to cover such expenses. We are tempted to consider such claims as yet another example of the creativity exerted by a few inventive plaintiff lawyers in the United States. It is sad to see that some energy companies have agreed to participate in these actions. Good faith between the parties is a fundamental principle in insurance. The mutual respect of this principle is the reason why insurance contracts can be drawn up with the present degree of flexibility and the absence of a hoard of lawyers which is typical of other contract negotiations in the financial sector. Those oil companies that look at their insurance policy as an asset to be exploited at all costs run the risk of undermining the confidence which is a prerequisite for the efficient operation of our industry. We hope they will realise that their actions do not serve their own long-term interests.

Energy Statistics
The offshore sector has seen further market deterioration in 1999. After very good results and a low frequency of claims in 1993 through 1995, the last four years have produced losses for underwriters on an overall basis.

The fact that the underwriting results in this period are negative should be a major concern to the market, bearing in mind the absence of catastrophic losses. However, when analysing the figures, it is quite clear that the worst loss ratios are found in the construction risk segment. With few construction projects last year, the activity was relatively low, and one could expect that the overall results for 1999 underwriting will improve as a result. It should however be noted that the largest single loss in the offshore market in 1999 was a construction loss.

Further, we have seen a general negative trend in the contractor business with unprofitable underwriting in some classes, such as control of well and mobile offshore drilling units.

Underwriting results
Table 1 shows the underwriting results for all offshore policies written by the CEFOR members. The offshore market had its best year ever in 1994, but since then we have seen a continuous fall in the profits. The main reason for this is the fall in rates, but it is also due to some of the oil Majors' withdrawal from the commercial market. The overall premium base in the offshore market has declined, forcing underwriters to look at other and less profitable business segments to keep up their premium volume. Despite these efforts, the overall premium to the CEFOR members for 1999 represents only one third of the premium volume for 1994.

The development in respect of the more recent underwriting years (i.e. 1996 and onward) should also be noted. These years are showing red figures. One would have to go back to the late 1980's to find poorer results than the underwriting year 1997. Further, there does not appear to be any reason to believe that underwriting in 1998 or 1999 will improve this situation.

The outlook does not look very optimistic. But changes will occur, the question is when. During 1999 we have seen relatively important market players withdraw from the energy market. It is quite obvious that a disproportion between

Table 1
Total underwriting results for all offshore policies 1990 – 1999

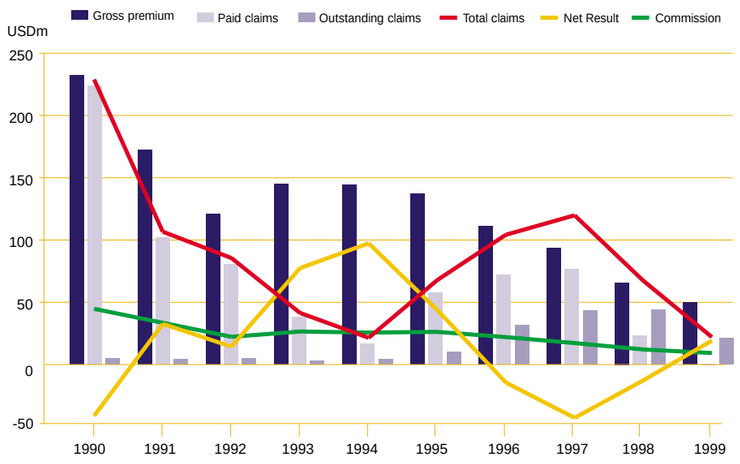
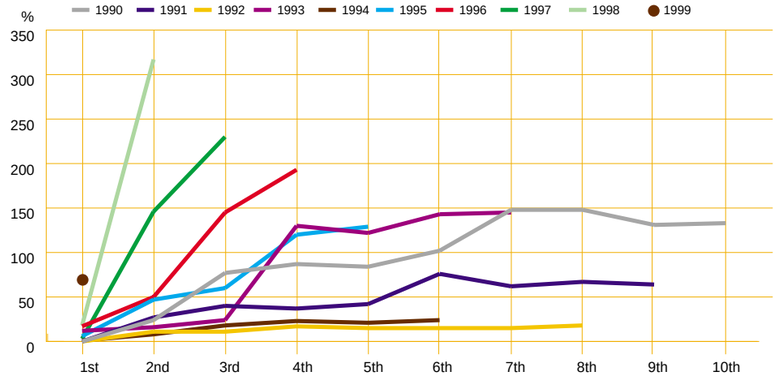


Table 2
Construction risks – loss ratio developments

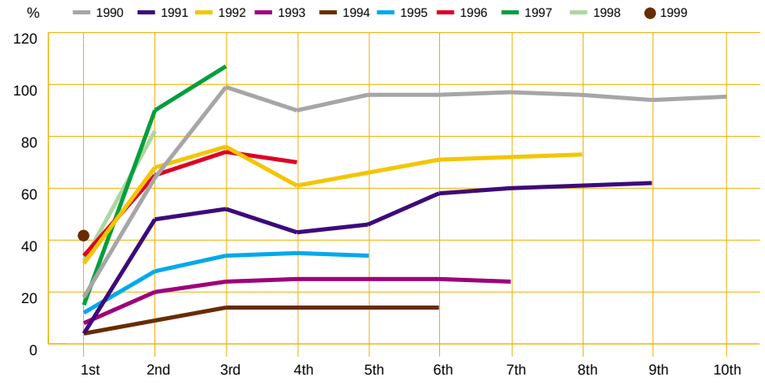


premium and claims exist in the market today. Further withdrawals are inevitable – which will eventually result in a hardening of the market.

Loss ratios – construction risks
Table 2 shows the development of loss ratios for construction policies. The graphs clearly indicate a market unable to price this class of business at the right level. There may be several reasons for this, but the Energy market needs to tidy up the rating of this business, despite the fierce competition between underwriters. Construction risks are currently avoided by many of the market leaders, and signs of a more normalised pricing is taking place, but there is a long way to go before the segment will be profitable to underwriters. Based on the previous year's experience, it is expected that the average loss ratio for the years from 1996 to 1999 may very well exceed 300 percent.

Loss ratios – operational risks
Table 3 shows the development of the various loss ratios for operational risks. The loss ratios for 1997 and 1998 have continued the negative trend and will most likely produce net losses to the market. This is alarming news, because this is the first time since 1989 that the market has suffered a loss from the operational risks it has written.
With the absence of catastrophic losses and the expected increase in activity as a result of the recent increase in the oil price, it will be a challenge for underwriters to charge enough premium to meet the resulting new claims.

Table 3
Operational risks – loss ratio developments



INTERVIEW

FOR MANY OF TODAY'S PROGRESSIVE COMPANIES THE MANAGEMENT OF RISK HAS TAKEN ON A MORE ENCOMPASSING MEANING.

Anil Jain,
insurance director – Petro-Canada

Petro-Canada, the second largest producer of petroleum products in Canada. Petro-Canada has three refineries that operate at capacity of 49,000 cubic meters per day, and is one of the largest manufacturers of lubricants in the world.

RECOGNIZING: INSURANCE CUSTOMERS WANT MORE




Petro-Canada has dedicated an entire department to implement its risk management strategy.

When Petro-Canada, the second largest producer of petroleum products in Canada, was looking to expand and enhance its panel of insurers, the company wanted more than a promise of financial compensation in the event of an accident. It wanted to add an insurer who understood its needs and business activities and who could respond to those needs with the right solutions. With a growing presence in offshore operations on the east coast of Canada and interests in the Norwegian North Sea, Petro-Canada looked to the Norwegian energy insurance market.

In a fast-moving industry, one fact is clear – the role of a quality insurance provider is expanding. And for many of today's energy companies, insurance providers must reach beyond their traditional area of expertise to help their clients create value.

"Petro-Canada is purchasing insurance coverage, services and products in the global market. As our business changes and faces new challenges, the professional skills, market expertise, value and customised solutions from our insurance providers are in greater focus," said Anil Jain, the director responsible for insurance at Petro-Canada.

Like many energy companies, Petro-Canada relies on its insurers to help map out and maintain a comprehensive risk management strategy. The purpose of this strategy is to reduce and contain risk, especially through loss management and reliability of it's operations. Here, the insurers' underwriting and loss prevention representatives play a vital role by sharing pertinent information and industry knowledge.

"Petro-Canada recognises the importance of loss control and the contribution of the insurance loss prevention engineers in reducing the potential for loss at our facilities. We employ a team approach. Our internal loss control experts work in collaboration with the insurers' specialists to identify opportunities to cost effectively mitigate losses. The insurers bring a unique perspective from around the industry which augments our own", says Ed Koshka, the oil company's senior engineer for risk management.

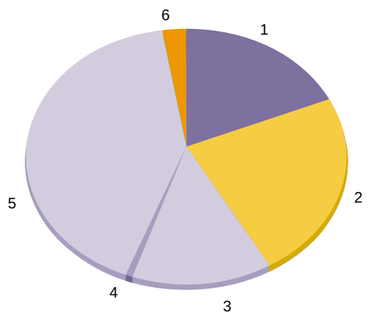
Petro-Canada has dedicated an entire department to implement its risk management strategy. The department provides financial risk management through insurance coverage and hedging programs, while supplying a broad range of in-house professional and technical risk management services aimed at helping the company manage its business risks.

"When selecting insurance providers, the company also looks for firms that are willing to commit to long-term, mutually benefiting relationships – firms that are committed to helping Petro-Canada create value", says Dr. Jain.

A strong focus on value creation has been key to the company's success. By selecting insurance companies that share the same core values, Petro-Canada's risk management department makes its contribution to how Petro-Canada meets the challenges of a very competitive market place.

Petro-Canada is one of the largest oil and gas companies in Canada with operations in mainly in Western Canada, but in the Hibernian oil field, Algeria, Norway and Eastern Canada as well.

Petro-Canada is the country's second largest marketer of refined petroleum products, with a 17 per cent market share. In 1999, Petro-Canada sold 18.7 billion litres of refined petroleum product.



CEFOR members

USD 1 = NOK 7.73	NOKm	USDm	%
1 Gjensidige	86.1	11.1	17.6 %
2 Storebrand	116.3	15.0	23.7 %
3 Vesta	69.4	9.0	14.2 %
4 Vår	3.3	0.4	0.7 %
5 Sjøtrygdgruppen*	203.3	26.3	41.5 %
6 Bergen Hull Club	11.6	1.5	2.4 %
Total	**490.0**	**63.4**	100.0 %

*Coastal Marine Club's Mutual Company and the coastal marine clubs

The market
Gross premium income amounted to USD 63.4 million (NOK 490 m) in 1999, compared with USD 66.4 million (NOK 500.5 m) in 1998. The CEFOR companies accounted for 56.2 percent of premium income, while the Coastal Marine Clubs' Mutual Company (SGS) and participating coastal marine clubs accounted for 41.5 percent.

CEFOR members did not suffer any large total losses or many particular average claims in 1999. Members were fairly satisfied with the year's results.

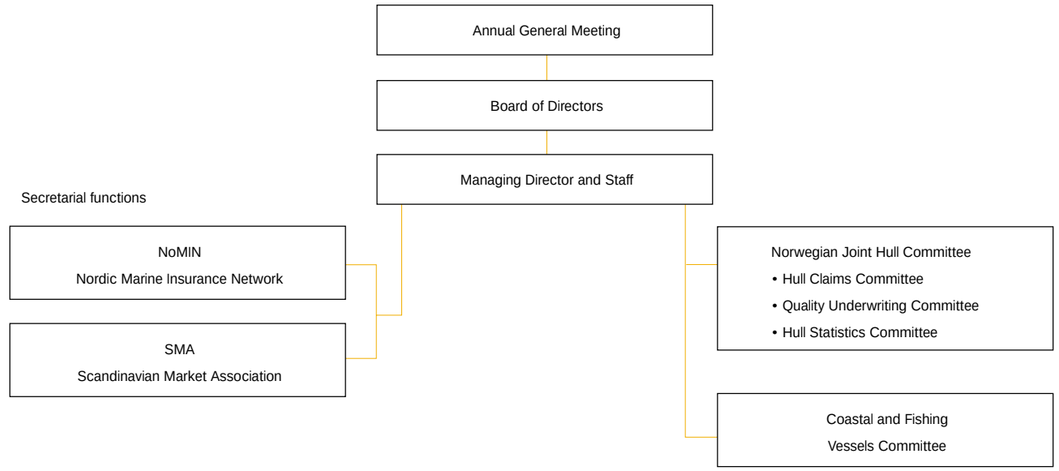
The Norwegian coastal and fishing vessel market includes fishing vessels of all kinds and sizes from small coastal fishing boats, large industrial trawlers operating world wide, freighters, tugs and other smaller ships trading in the coastal waters between Denmark and Sweden, ferries providing service in fjords and along the Norwegian coast, offshore supply vessels trading in the Norwegian sector of the North Sea, and lighters etc.

Market Conditions
Competition remained strong in 1999, particularly in the fishing vessel segment.

Premium levels are still too low, and only companies which did not suffer any large total losses or many particular average claims could report fairly satisfactory results. Loss ratios on many freighter accounts remained disastrously high and most of these risks were not renewed in the Norwegian market. By the end of 1999, there were signs of a hardening market.

Losses
The largest total loss in 1999 was the high-speed passenger craft Sleipner. The vessel ran aground between Haugesund and Stord in November with 80 passengers and a crew of nine aboard. 16 people perished in the rough seas. The second largest total loss was the purse seiner Havbas at NOK 37 m, which sank after colliding with a passenger ship.

"Competition remained strong in 1999, particularly in the fishing vessel segment."



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