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A WORLD OF CHANGE?

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Graham Watts of Bunker Insure surveys the marine credit insurance market and finds that good coverage is still available for bunker companies, but through a far more limited number of providers

The last 10 years for marine credit insurance have been challenging, to say the least. Aside from the Hanjin bankruptcy in 2016, there have been a whole raft of major defaults and bankruptcies amongst the bunker community, kicked off by OW in 2014 and then followed by Bunkers International in 2015, Wiljo in 2016, Macoil in 2018, Praxis in Dubai in 2019, and Hin Leong and GP Global in 2020.

The cumulative losses to insurers are difficult to calculate. But suffice to say they easily outstrip premiums to this sector to the extent that a large number of credit insurers have completely withdrawn from this market. Today it remains a segment which is still unpopular with insurers.

In tandem with this position – whilst in the past the only marine credit insurance buyers were the bunker companies – when vessels started fitting scrubbers a number of banks also realised the security potential that marine credit insurance could provide so began buying individual debtor limit coverage at market rates. As a rough guide, single debtor market pricing is currently running at a minimum of 1.25% to as much as 5% on limit, making the price for a $5 million limit anything between $62,500 up to as much as $250,000.

Now a quick mention about how credit insurers make available debtor limit capacity. All insurance companies are heavily reinsured. Reinsurance negotiations generally occur at the beginning of each year. Aside from pricing, which will be calculated on key factors such as claims experience, this will also dictate the way that policies can be underwritten, the structure that can be applied but, most importantly, in establishing the total amount of capacity available for each individual debtor. Then the race is on. Reinsurance coverage is very expensive, but once acquired it then has to be made use of to try and generate sufficient premium to cover this cost. But this also means in effect that some insurers can quote lower prices than others simply because their reinsurance costs are lower. Then clearly some debtors represent a safer risk than others, so balance and care is needed. But debtor limit capacity has to be carefully allotted. For example, if one insured is provided with $5 million of coverage for XYZ Shipping then that is $5 million less available to provide to any other insured. It therefore makes sense to try and sell that capacity at the highest price.

Then there is limit usage. Banks would generally buy a limit coverage that would be in use for a whole year. On the other hand, given the nature of the business, a bunker company might request a debtor limit coverage, but if they then struggle to make a deal or if that ownership's vessels do not call, then they may rarely use any given limit at all. So, as policy pricing is usually based on sales, insurers could easily find themselves providing a limit for which they receive little or even no premium.

By contrast, the banks use limits for 12 months so they can justify the higher prices. This, in and of itself, has had the effect of reducing the availability of debtor credit lines for bunker companies.

But the good news is that the shipping market itself is in a stronger state than it has been for some time whilst the fitting of scrubbers has slowed. Good coverage is still available for bunker companies, but through a far more limited number of insurers.

> ‘Reinsurance coverage is very expensive, but once acquired it then has to be made use of to try and generate sufficient premium to cover this cost’

If there is any misunderstanding that I could correct in this article it would be to point out that credit insurance possesses two unique characteristics that make it different from other types of insurance. First of all, it is not technically an insurance. By definition, Insurance can only cover ‘accidental risk’ and companies do not generally go bankrupt because of an accident. So, credit insurance really is more akin to a bank guarantee. By this I mean that it is the security provided which has a value in and of itself in that it secures an unsecured debt. There are, thankfully, a few people that have the attitude that if they have not made a claim then insurance has been valueless. But the coverage itself elevates its buyer’s creditworthiness, which in the current climate is crucial. People generally do not complain about the price if a bank guarantee is not triggered and neither should they do so if they have not suffered a claim.

There are differences of course. Unlike a bank guarantee, credit insurance generally carries an aggregate deductible. But without this, the pricing would be far too high or, alternatively it would not allow insurers sufficient confidence to provide the low-priced debtor limits that bunker companies can afford. Additionally, credit insurance is conditional. The seller has to comply with a set of rules designed to enhance the recoverability of debts – such as the setting of payment terms or ensuring that sellers act quickly to manage overdue debts. But by and large it is a provision of security.

But the other key difference regards the actual coverage wording. Nowadays few people take the time to read their insurance wordings. After all, we all know roughly what is covered by house insurance, car insurance etc. Even marine insurances have standard wordings that all insurers use worldwide.

But credit insurance differs, in that every insurer uses their own unique wording and they differ enormously, and to an extent that means in effect that they are difficult to compare, one with another.

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For example, many credit insurers allow themselves to amend debtor limits or even cancel them whenever they wish with a few days’ notice. There have even been extreme cases where all debtor limits have been cancelled without warning and even with no return of premium while others do not allow limits to be amended or cancelled at all, so clients can be sure their debtor limit coverage is in place.

Other major differences are that, while some insurers allow companies to retain part of their recoveries first, others will demand that it is all repaid to them first before anything can be considered to be applied to the insured. Some do not even cover political risks which in effect means that in the event of an embargo or general political act preventing payment, there is no cover.

Of late, several other factors have changed to affect marine credit insurance. Arguably, the key change has been the manner by which courts in certain jurisdictions will no longer sway in favour of a creditor lacking a direct relationship with the ownership or charterer. So, for example, as with OW, suppliers supplying via a trader which fails to pass on a payment, will find it harder to arrest a vessel.

The good news is that the financial performance of credit insurers generally has been strong. Going forwards, with fuel prices having risen significantly, we are seeing more demand for either syndication on risk, especially where the primary insurer has capacity constraints, or top up lines. These additional ‘top up’ lines are more expensive but structurally the syndication of a programme creates benefits for both insurers and bunker companies – accessing more capacity and spreading the risk.

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