

Plane Talking

JLT AEROSPACE

SEPTEMBER 2009

Executive Summary

Slivers of Hope

- The crisis isn't over yet for the airline industry but there may be some positives to take away this month
- Mercifully we are not aware of any fatalities from airline losses
- Unusually there has been slight evidence of passenger growth amongst the few airline insurance renewals in September
- Several insurers have announced plans for expansion in Europe, changing access to capacity and product lines
- There have been no significant credit rating changes amongst the airline insurers

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Lead Lines

Angus Roberts, Aviation Underwriter, Travelers Syndicate 5000

“ It seems the Airline insurance market has finally been shocked into facing the reality of the effects of 4 or 5 years of reducing rates and reversed the trend. Why?

Clearly the recent catastrophic losses have been the catalyst for change but they are neither the reason nor the sole justification for this market movement.

Statistically, recent events should not have been unexpected and serve only to reaffirm most historically based assumptions of both frequency and severity on which rational pricing depends.

Overcapacity has often been proffered as the fuel of a soft market (or an excuse for capitulation). But capacity hasn't

significantly reduced recently and yet rates are increasing.

No, the real reason that rates are increasing is simply that they have been reduced, indeed by over 40% since 2004.

Of course rates reduced for everyone, but I fear that as ever, Assureds with recent adverse experience and those without the negotiating clout are easy targets will have the most challenging renewals ahead.

Surely though, if a less volatile pricing environment is a worthwhile goal for all parties, then the solution lies beyond those few accounts and in recognising the extent and randomness of risks and exposures faced by the whole Aviation Industry. ”



Airline News

Comment

Already battered airlines are projecting to lose US\$11 billion in 2009, US\$2 billion more than the International Air Transport Association's (IATA) original forecasts. The industry continues to suffer from weak yields driven by drastic drops in premium demand and rising fuel costs. IATA's revisions to its financial forecasts show a 12% and 15% drop in passenger and cargo yields for 2009 compared with projections released in June of a 7% decline in passenger yields and 11% in cargo.

Director General of IATA Giovanni Bisignani recently told reporters that the industry "is in intensive care" and that the crisis is not over.

Despite carrier capacity reductions to better match supply and demand, excess capacity still remains in the marketplace, which is contributing to the decline in yields.

It is estimated that European airlines might show the largest loss of US\$3.8 billion with Asia Pacific posting US\$3.3 billion.

A major investment bank is predicting that there will be a surplus of 1,400 airliners at the end of this year necessitating production cuts at both Airbus and Boeing.

One of the major leasing companies estimate that air traffic will begin to grow in 2011 at an annual rate of about 5%. This will reduce the airliner surplus to about 750 and then to 400 in 2012. These figures include all jet and regional airliners. With the prospect of parked aircraft coming back into activity, it is reckoned that passenger traffic would have to grow at the rate of an estimated 14% to avoid production cuts.

Start-Ups

- Cargoitalia, Italy, commenced operations from Milan to Hong Kong, on 9th September using a Boeing MD-11 freighter. The carrier will serve Hong Kong twice-weekly and intends to start services to North America with its second MD-11 shortly.
- Efly, Malta, is now operating flights from Malta to Catania using a BAe 146-300 aircraft configured in a single class.
- I Fly, Russia, plan to commence operations shortly using four Boeing 757-200s flying to holiday destinations in Europe, Latin America, the Middle and Far East.
- Peruvian Airlines, Peru, will commence operations from 29th October 2009. The carrier will operate domestic scheduled flights to Cusco, Arequipa, Tacna, Iquitos, and Piura using Boeing 737-200 aircraft.
- SolitAir, Mauritius, has now launched operations. The carrier is operating three daily flights between Mauritius and Rodrigues using a single leased BAe 146-200.
- Sol Linhas Aereas, Brazil, have been granted approval to begin operating domestic services. The carrier will operate initially to Curitiba, Foz do Iguacu and Maringa using Let L-410 turboprops.

Closures

- SkyEurope, the largest discount airline in Central and Eastern Europe filed for bankruptcy on 1st September because of a lack of liquidity to maintain operations. Fuel suppliers and airports had stopped their services due to outstanding

debts. The airline was a Slovakian company founded in 2001 and based in Bratislava, Vienna and Prague, and had been under Slovak creditor protection for some time.

- Confirmation was recently received that East Star Airlines, a private operator in China went bankrupt in March with substantial debts. Recent submissions for restructuring were rejected by the courts due to severe financial problems. The airline operated a fleet of A319s and A320s.
- Pace Airlines of Winston-Salem, North Carolina, suspended operations on 11th September due to ongoing financial difficulties. The company once operated as Hooters Air and performed operations for professional and collegiate sports teams, VIP charter and corporate shuttles. It is under investigation by the US Department of Labour for non-payment of employee wages. Their fleet consisted of six Boeing 737s.

Orders

Another quiet month for orders of airliners with only one confirmation of an order for 3 Boeing 737-700s being announced by Turkmenistan Airlines. Boeing's order book shows a recent order for 8 737s for the Indian Navy. It is assumed these are ASW (Anti Submarine Warfare) aircraft.

Despite the paucity of new orders, backlog for Airbus, towards the end of August, stood at 3,739 a reduction from 3,907 at the turn of the year with Boeing showing 3,497, a decline from 3,726.

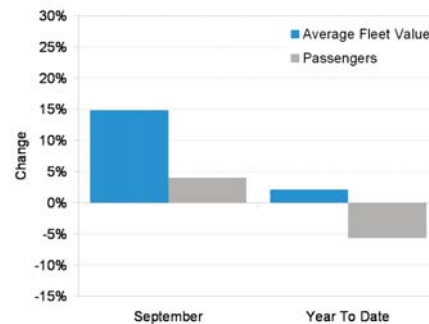
Renewal Analysis

Exposures

The accounts we have seen renew so far in September have presented an increase in passenger numbers which goes against the grain of recent trends. Interestingly, but perhaps just coincidentally, all of the accounts showing forecast passenger increases are domiciled in South America.

Year on Year % Exposure Change

September/Year to date. Based on latest Information at 25 September 2009



Source: JLT Database

Premiums*

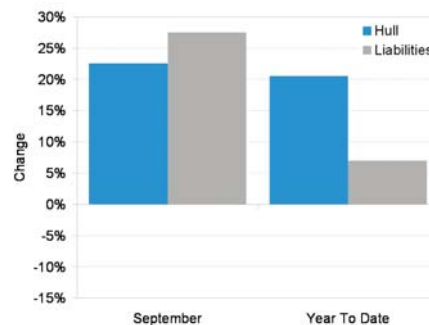
Underwriters are continuing their pressure to increase premiums on the accounts renewing in September with both hull and liability premiums receiving similar increases. This is slightly surprising given the increase in liability exposure described above.

| Year to Date (Like for Like) | Hull US\$M | Liability US\$M | Total US\$M |
|---------------------------------|---------------|--------------------|----------------|
| 2008 | 167 | 279 | 446 |
| 2009 | 201 | 298 | 499 |
| % Change | 21% | 7% | 12% |

* Net of brokerage and at lead terms

Year on Year % Premium Change

September/Year to date. Based on latest Information at 25 September 2009



Source: JLT Database

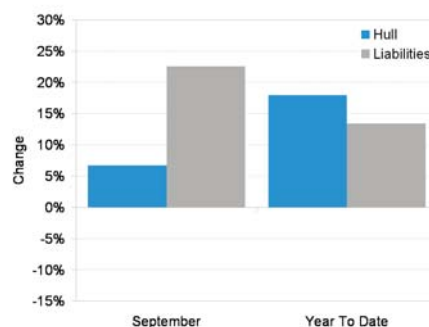
Rates

At first sight it seems the increase in passenger numbers for these renewals has taken the pressure off liability rating for this small group of renewals.

However this doesn't really explain the disparity between hull and liability rate changes for September. Instead it is possible that the growth in liability exposure is mitigating a potentially greater increase in passenger rates.

Year on Year % Rate Change

September/Year to date. Based on latest Information at 25 September 2009



Source: JLT Database

Insurance Market News

Kiln has announced the opening of a new office in Paris. The Lloyd's insurer said the Paris office would initially underwrite aviation business, including airline hull and liability lines.

Lloyd's has opened its first representative office in Sweden, which will act as the hub for all Nordic operations. The Nordic region as a whole (Norway, Sweden, Finland & Denmark) is Lloyd's third largest European market, and presents many niche opportunities for profitable diversification of the Lloyd's market, particularly in energy, aviation and property business.

Chartis, the unit recently formed by AIG, will decide before the end of next year on a possible stock market listing. "Chartis Europe continues to do very well. We're financially strong," said Julio Portalatin, Chief Executive Europe. Portalatin indicated Chartis wanted to hire people to develop new products for the aviation industry.

Arrivals and Departures

- Jean-Claude Gèze, previously at Allianz, has been appointed as Head of Aviation for QBE France
- Graham Spencer-Brown is moving from Allianz to CV Starr

Loss Analysis

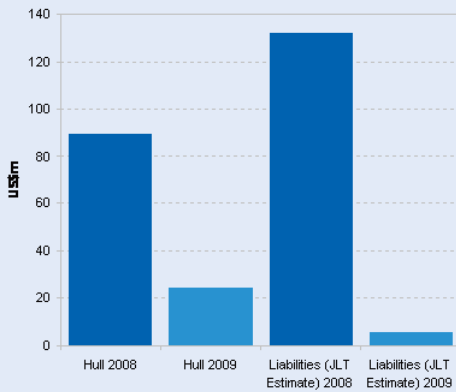
Losses Summary

August

- Hull losses exceeded US\$ 24.53M
- 35 fatalities
- US\$ 6.25M estimated liability loss

August Losses

All Known Losses Net of deductible

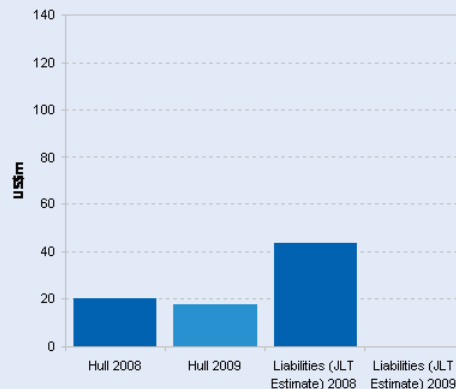


September

- US\$ 18.1M estimated hull losses
- No fatalities
- Liability loss estimate currently nil

September Losses

All Known Losses Net of deductible



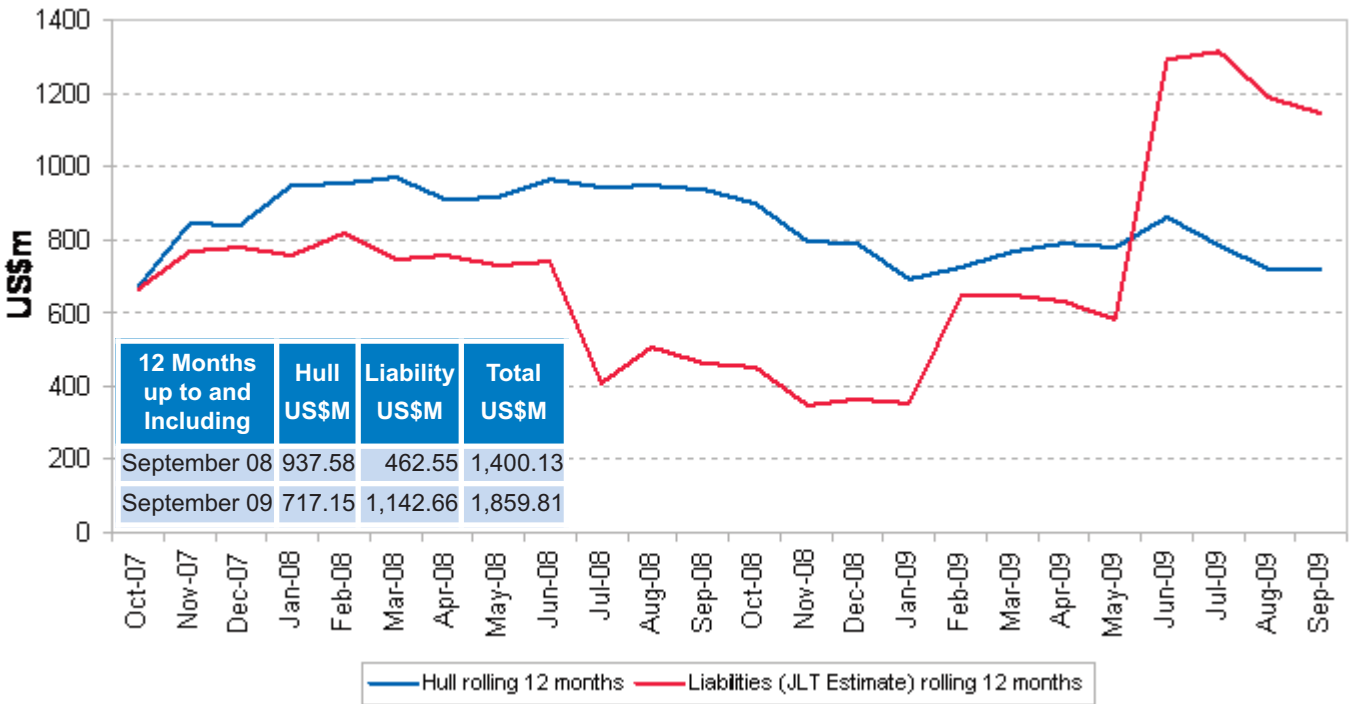
Known Losses in September

| | | | |
|---|-----------------------|------------------------------|--------------|
| 4th | Air India | Boeing 747-400 (VT-ESM) | India |
| Taxiing for take off at Mumbai for a flight to Saudi Arabia, the aircraft suffered an engine fire. The fire was quickly brought under control by the airport fire service. All passengers and crew evacuated the aircraft safely and completed their flight on another aircraft. | | | |
| 8th | Sita Air | Dornier 228-202 | Nepal |
| During a training flight, the aircraft's undercarriage collapsed on landing at Nepalgunj - Ranujha. No injuries were reported. | | | |
| 14th | Contact Air | Fokker F100 (D-AFKE) | Germany |
| On approach to Stuttgart following a domestic flight, the crew had difficulty in lowering the undercarriage. The aircraft was put into a hold for over one hour whilst the crew attempted to rectify the problem. Eventually, the aircraft was landed with the undercarriage retracted. | | | |
| 18th | Bering Air | CASA 212-200 (N349TA) | USA |
| The aircraft ran off the runway whilst landing at Savoonga Airport, AK following a domestic freight flight. The undercarriage collapsed in the soft ground. | | | |
| 24th | South African Airlink | BAe Jetstream 41 (ZS-NRM) | South Africa |
| Immediately following takeoff from Durban on a positioning flight, the aircraft suffered an engine fire/failure resulting in an attempted off-field landing. The aircraft came to rest with the fuselage broken in two. | | | |

* The JLT liability estimates are provided merely as a guide.

Cumulative Airline Loss Figures

Rolling 12 Months shown for 24 Months to September, 2009

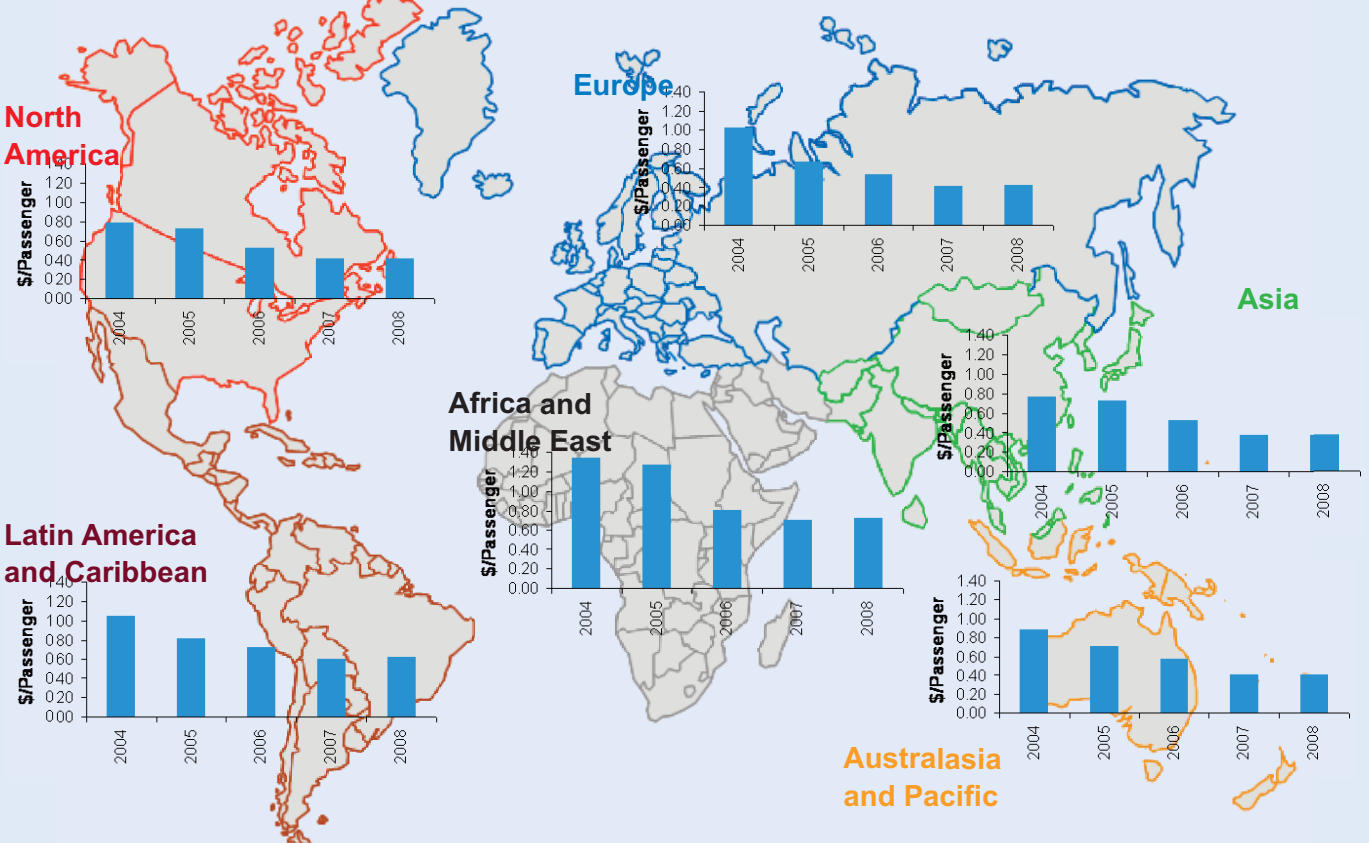


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Regional Chart

Passenger Rates, 2004 - 2008

By Domicile of Operator



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