

# Plane Talking

JLT AEROSPACE

JULY 2009

## Executive Summary

### Rating Changes

- Airline industry pressures continue to mount and are set to deepen further
- Renewals to date in 2009 witness average rate increases that generate net premium growth of 11%
- Hull exposures are still growing as a result of back order fulfillment, however, passenger numbers continue to fall partially mitigating the effect of rate increases
- Losses to date continue to grow with the last 12 months responsible for US\$2B of estimated hull and liability costs
- There are a number of impending personnel movements
- The business planning season is well underway, with capacity holding and growing anticipation of new opportunities

### Lead Lines

#### Emilio Di Silvio, Managing Director, QBE Aviation Syndicate 5555

Airlines need continuity of catastrophe insurance. Insurers need to ensure they can provide this security in the long-term – and make a profit. In reality these two axioms have proved difficult to reconcile.

Since their all time high in 2001, the airline industry has seen a steady reduction in rates. By the end of 2008 premium levels were similar to those seen ten years earlier, an unusual trend in a decade where the global airline fleet increased significantly in value. However, over a relatively long period with almost no major losses, the evidence seemed clear: new improved aircraft meant new improved safety. Or did it?

Following a series of high profile major losses in 2009 the airline insurance market has been left reeling and rates and premiums will now have to rise significantly in order for insurers to maintain their support in this class. However, this will be far from the “knee jerk” reaction which the market was accused of following 9/11.

This reaction will be based on profitability, following a broader realisation that airline insurers have made little or no underwriting profit in this class in recent years. The need to underwrite intelligently, differentiating between individual airline risks, must be much better developed. There can be no hiding from the basic fact that insurers need substantially more premium in the “pot” to pay for the frequency, and escalating cost, of claims.

Additionally, since the global recession took hold, the resulting loss in investment income and the increased cost of capital, together with indications that reinsurance costs will increase over time, has helped to refocus the airline market. Underwriting for a profit is key and the time has clearly come for premium income to move sharply upwards.

The final jolt to insurers followed the fourth large loss involving passenger fatalities this year. Rates simply must rise in order to prove, demonstrably, that insurers are able to cover the cost of claims and produce a satisfactory return for capital providers.

### In This Issue

Executive Summary	1
Airline News	2
Insurance Market News	3
Renewal Analysis	3
Loss Analysis	4



# Airline News

## Comment

One of the most important yardsticks defining the health of the world's airlines is how the North American carriers are performing. US stock markets and analysts rely on airlines' second quarter results in order to predict what state the airline industry will be in come the leaner winter months. Their predictions were pretty realistic with the majors performing unfavourably compared to the budget carriers.

Delta/Northwest, United, Continental and American all gave cause for alarm with reduced revenues and passenger numbers, resulting in negative returns which hit the US\$1 billion mark overall.

US airlines saw passenger revenues fall 26% in June, the eighth month of decline, the only sector proving resilient being the budget operators with JetBlue, Alaska, Airtran and Southwest being profitable albeit on a much reduced basis.

The same analysts who predicted the quarterly losses also suggest that for some, Chapter 11 is inevitable or alternatively some sort of forced marriage will have to be arranged.

The CEO of American Airlines quipped that he found it extraordinary that despite oil prices being half what they were in July 2008, the industry now finds itself in worse shape than a year ago.

The knock on effect is very detrimental for airports. One airport in particular on the east-west trade route is Hong Kong International which saw sharply lower passenger and cargo traffic. June passenger volume fell 18.9% to 3.3 million, and cargo traffic fell 13.45% to 270,000 tonnes.

Manufacturers are also reporting a glum picture for the first half of the year as the comment on orders describes.

## Start-ups

- Air Dominicana, Dominican Republic, is poised to launch one daily flight from Santo Domingo to New York JFK and Miami on 1 September using a single 737-400.
- Air Cargo Germany, Germany, has secured its air operator's certificate (AOC) to begin services using two Boeing 747-400SF aircraft.
- Cambodia Angkor Air, Cambodia, is shortly expected to receive its first aircraft, an ATR72-200 to begin operations with flights between the country's tourist destinations of Phnom Penh and Siem Reap.
- Fly Kumba, Zimbabwe, is a low cost airline scheduled to begin operations in September operating domestic and regional routes.
- I Fly, Russia, plan to launch as a new charter operator using Boeing 757 aircraft from Moscow Vnukovo Airport.
- Maya Island Air, Belize, launched regional services with three ATR72-200 turboprops, between Belize City, San Pedro Sula (Honduras), Guatemala City (Guatemala) and Cancun (Mexico).
- Medallion Air, Romania, expects to secure a further two Boeing MD-82/83 aircraft by the end of this year following the granting of its AOC. The airline intends to operate on European, Middle Eastern and African routes.
- Pet Airways, USA, has now launched services flying pet animals between five 'city regions' New York, Washington DC, Chicago, Denver and Los Angeles using a fleet of Beech 1900C, Beech 99, and Cessna.

## Closures

- JetAmerica, announced the cancellation of its entire proposed route network on the 17th July just over two weeks after announcing a delay of one month to its launch of services. The cancellation of services was blamed on continuing difficulties in obtaining slots at Newark Airport.
- The Italian civil aviation authority has suspended budget carrier MyAir's operating licence from 24th July. Following mounting disruption to MyAir flights, the authorities have decided that the airline could not ensure coverage of costs for essential services. It has been seeking recapitalisation for several months, but its failure has been reflected in deteriorating levels of service.
- Belgian cargo operator Cargo B Airlines stopped trading on July 1st after fresh investment failed to materialise.

## Orders

After a relatively busy month in June, the aircraft manufacturers' salesmen are again finding things tough.

Boeing have announced new airliner sales this month with a relatively large order from Copa Airlines of Panama for 13 737-800s plus options for an additional 8. SunExpress of Turkey ordered 6 further 737-800s to add to an existing all Boeing fleet. Ethiopian Airlines ordered 5 777-200LRs and 12 Airbus A350-900s being the first of these types in their fleet.

Both Boeing and Airbus have suffered cancellations and deferrals, though so far not in great numbers, and the record breaking backlog from last year is still, fortunately, fairly much intact thereby ensuring regular new deliveries for some time to come.

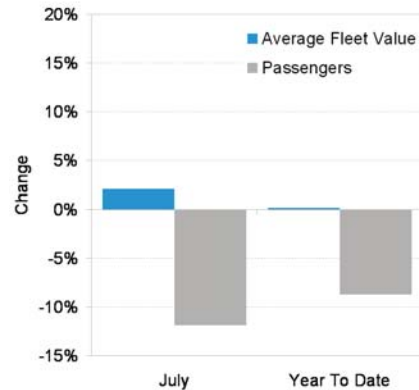
# Renewal Analysis

## Exposures

As expected, the trend seen so far this year continues with lower passenger numbers, due to market conditions, and a slight increase in overall fleet values supported by residual aircraft deliveries.

### Year on Year % Exposure Change

July/Year to date. Based on latest Information at 24 July 09



Source: JLT Database

## Premiums\*

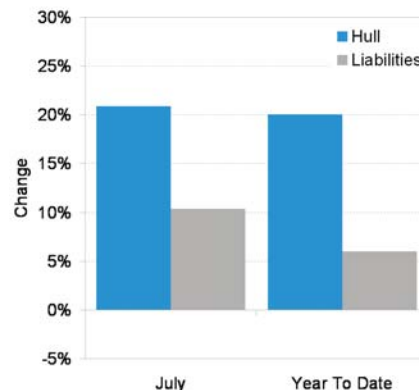
July has become one of the busiest months for airline renewals, generating substantial premium with about 30 airlines renewing overall. The largest by far is American Airlines who's fleet is valued at over US\$17.5 billion, and flying nearly 100 million passengers.

Year to Date (Like for Like)	Hull US\$M	Liability US\$M	Total US\$M
2008	142.49	257.40	399.89
2009	171.02	222.91	443.93
% Change	20%	6%	11%

\* Net of brokerage and at lead terms

### Year on Year % Premium Change

July/Year to date. Based on latest Information at 24 July 09



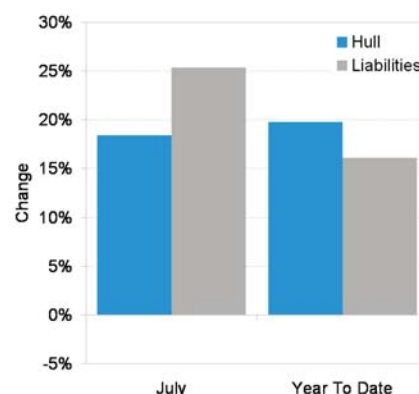
Source: JLT Database

## Rates

Following a spate of expensive losses during the first half of the year, and with the backdrop of an unprofitable 2008, underwriters have tabled their intentions to increase rating levels substantially and we are now seeing these demands implemented. Almost every airline seen in July received rate increases and, on an overall basis, this level came reasonably close to underwriters expectations of rate rises in the range 20% to 30%.

### Year on Year % Rate Change

July/Year to date. Based on latest Information at 24 July 09

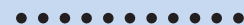


Source: JLT Database

## Insurance Market News

### Arrivals and Departures

- Former Aon Ltd deputy chairman Jonathan Palmer-Brown has been recruited to the executive board of JLT. He is currently chairman of the LIIBA aviation executive.
- Giles Wilkinson, previously Chairman of Willis Aviation, will be joining JLT Aerospace as a Partner.
- Additional hires at JLT include Bill Smith, Steve Turner, John Cruse, Sean Kelly, Paul Coombes, Roger Parrish, Andy Barham and Alan May from Aon.
- Peter Elson, formerly of Aon, will join JLT on 1st September.
- Martin Trumper has been appointed joint managing director of aviation for JLT Asia, based in Hong Kong.
- Richard Power will be joining the underwriting team at Catlin.



### A Revitalised Brand for JLT



On 6th July JLT unveiled its new logo. This is not about JLT changing but about focusing on the most effective way to communicate who we are and what we do more clearly, distinctively and in a more engaging style.

As with many successful international brand developments, our new look is a balance of old and new. By formalising the 'JLT' as our brand name, we capitalise on how we are already known amongst our clients, partners and colleagues.

# Loss Analysis

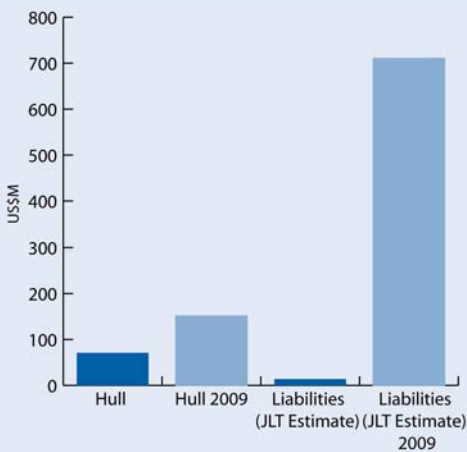
## Losses Summary

### June

- Hull losses exceeded US\$150.85M
- 382 fatalities
- US\$710M estimated liability loss

#### June Losses

All Known Losses Net of deductible

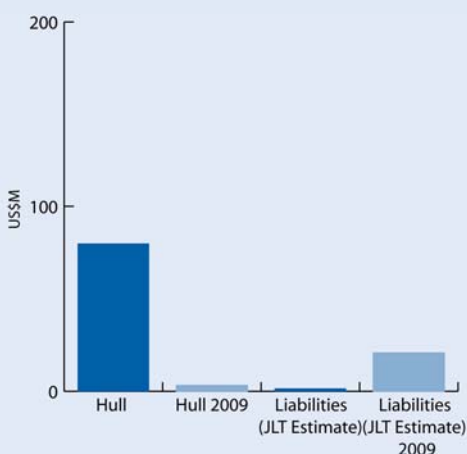


### July

- US\$3.09M estimated hull losses
- 186 fatalities
- Liability loss estimate US\$20.8M

#### July Losses

All Known Losses Net of deductible



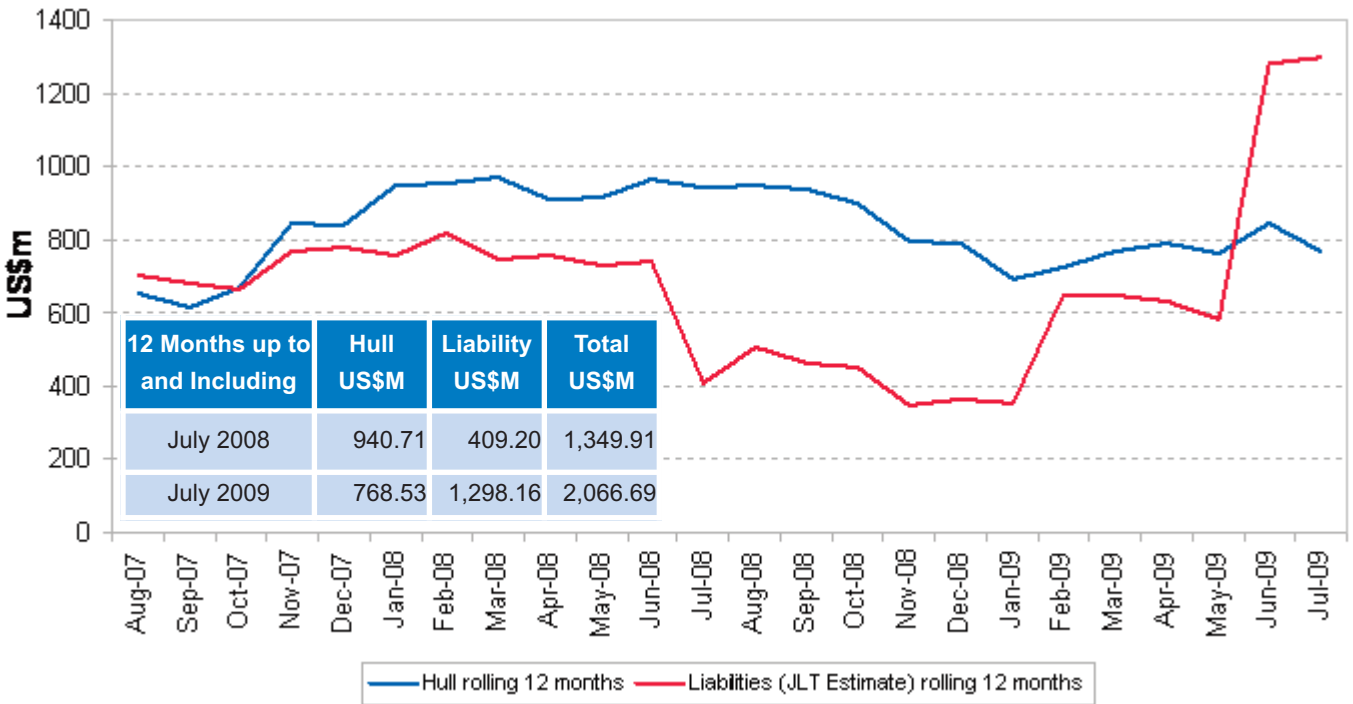
## Known Losses in July

13th	Southwest Airlines	Boeing 737-300 (N387SW)	USA
En-route near Charleston, West Virginia, a hole appeared in the cabin roof causing sudden decompression and resulting in an emergency landing.			
15th	Caspian Airlines	Tupolev Tu-154M (EP-CPG)	Iran
The aircraft came down in a field some 16 minutes after departure from Tehran on a flight to Armenia. Reports suggested a fire in the tail (engine) section and the aircraft circling as if looking for somewhere to land. There were no survivors from the 153 passengers and 15 crew.			
16th	American Airlines	Boeing 767-300EREM (N350AN)	USA
Whilst undergoing post maintenance testing Fort Worth, the undercarriage retract lever was pulled and, with the safety pin not being in place, the nose gear retracted causing significant damage to the fuselage.			
21st	Aeromexico	Boeing 737-700 (XA-NAM)	USA
The nose undercarriage failed during pushback from the gate at San Francisco.			
24th	Aria Air	Ilyushin IL-62M (UP-I6208)	Iran
Landing too fast at Mashad Airport at the end of a domestic scheduled passenger flight, the aircraft ran off the end of the runway and through a wall resulting in the demolition of the nose section and a number of fatalities.			

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

# Cumulative Airline Loss Figures

Rolling 12 Months shown for 24 Months to July, 2009

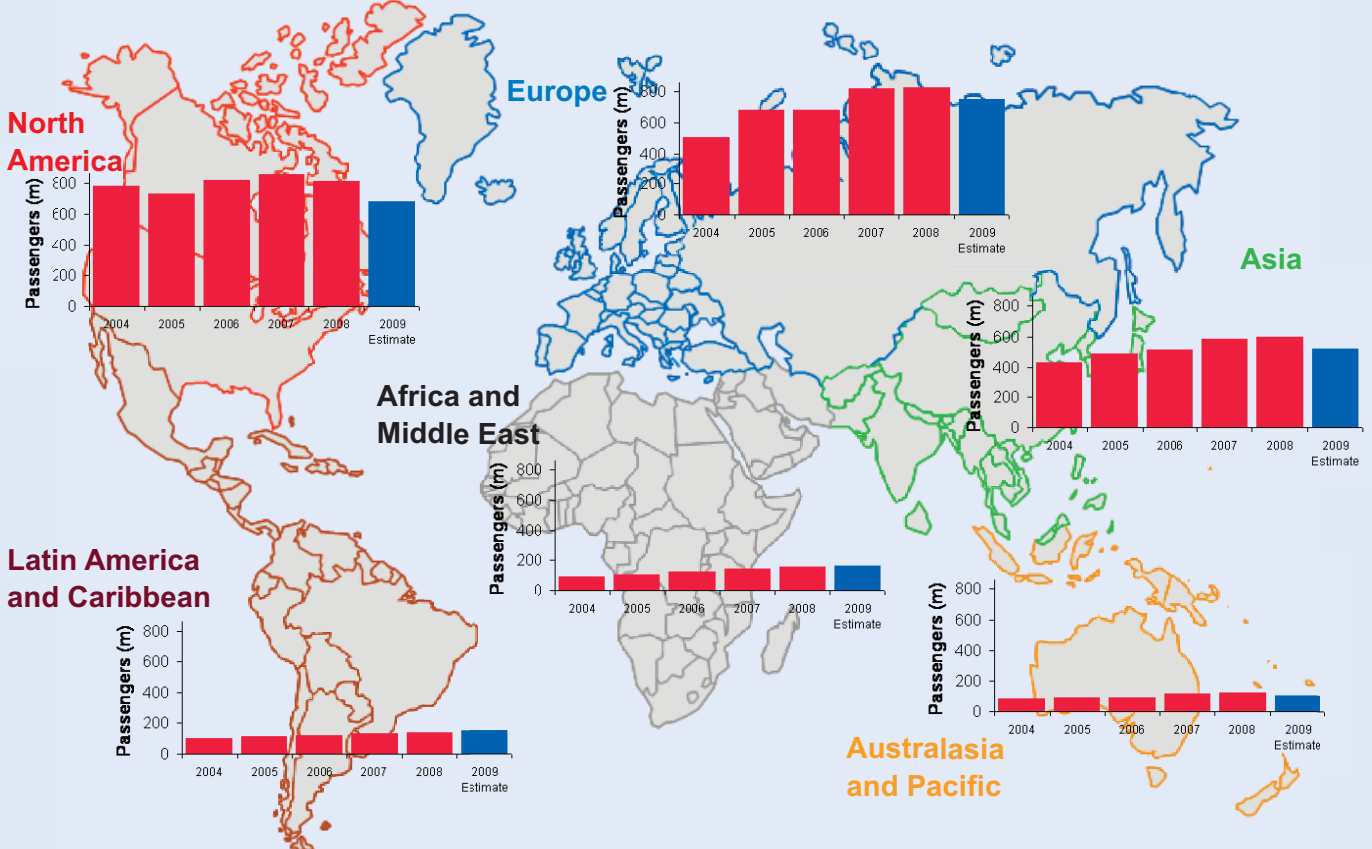


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# Regional Chart

Passenger Numbers 2004 - 2008 and Estimate for 2009

By Domicile of Operator



# PlaneTalking

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## Editorial

If you have any comments or suggestions or changes to your email address, or you know anyone who would like to be added to our mailing list, please advise by emailing details to [lucy.potter@jltre.com](mailto:lucy.potter@jltre.com)

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