

Plane Talking

JLT AEROSPACE

MAY 2011

Executive Summary

Gone with the wind?

Despite the recent history of insurance losses seemingly exceeding premium volumes, premium rates continue to fall in many of the recent airline renewals. The general increase in exposures, both fleet values and forecasted passenger numbers, offer some relief in maintaining premium levels up.

Risk selectivity by underwriters is clearly an embedded feature of today's market, and this seems to be a key component of the rationale supporting 2011 business models. Additional comfort is brought by the relatively benign cost of recent losses however this situation could change instantly.

Cross-subsidisation of the airline insurance business by premiums from other classes of aviation continues, however the effectiveness of this strategy is under increasing pressure due to the softening of premium rates in the other sub-classes.

Capacity is largely unchanged and the appetite for aviation business holds firm.

Loss frequency continues and whilst fortunately the market has avoided suffering any new very large losses, the smaller (attritional) losses now are consuming a very significant proportion of the available premium.

Aviation reinsurers are being pulled into the same direction as their aviation insurer clients, supportable only by the favourable (reinsurance) loss experience but they are acutely aware of the need to balance exposure against potential underwriting returns.

The spectre of non-aviation "market event" catastrophe losses continue to loom with the US hurricane season now underway and ultimately, in the absence of a number of major aviation losses, may actually be the catalyst that forces capacity to withdraw from aviation.

The fine balance just gets finer.

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Lead Lines

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Many years ago a London aviation insurance conference was awoken from its usual torpid state by an amusing and thought provoking speech from a leading underwriter of the day (who has long since moved to the dark side). His discourse was more a cry of frustration than complaint, the central point being that in aviation insurance you can only compete by lowering your standards to those of the worst protagonists. He contrasted this with general industry, where to exist in the same sphere as BMW, Sony, Marks and Spencer et al you have to aspire to excellence, being at least as good and preferably better than the market leaders.

I have often reflected on this clever line of reasoning and conclude that all is not what it seems. In many respects the companies and syndicates that make up the market are the Mercedes or Waitrose of their chosen field. Although slightly less appealing than a Porsche 911, the product, being the promise to pay valid insurance claims and defend the assured against claims made by others, is excellent. These days most carry high grade ratings and have a proven record of responding to losses. The market in general has performed well in times of crisis and periodically adapts to the changing legal and regulatory environment. However what our mid-nineties speaker was essentially referring to was pricing, that in order to obtain a share of the business in the depths of a soft market, it was necessary to reduce rates to a level he clearly considered uneconomic.

This taboo matter is highly subjective – what is uneconomic to one entity may be perfectly acceptable to another. While we often discuss airline financial data down to a level of minutiae in client meetings, the topic of insurers' expenses, the cost the client must pay to simply have the market exist, is rarely if ever covered. My assumption, although I have no proof, is that these must vary greatly across the industry. A lean operation with few staff should in theory be cheaper to run than another that tries to access business across all the sector sub classes.

In a soft market a prolific buyer of reinsurance may fare better than a net retainer, and vice versa in better times. Leaders have greater costs than followers but are arguably compensated by preferential terms and, increasingly, leader's fees. Differing levels of capital allocation will drive different return targets and internal charges for both direct and indirect expenses will vary across the spectrum. Some organisations are even outsourcing quoting to the brokers, which must save cost albeit have a dubious effect on the loss ratio. Overall, short of being party to competitor business plans, we don't know. Everybody thinks they are the only good guy in the game but the reality is much more opaque and complicated.

The only certainly is that if the market as a whole is trading at a loss, something will eventually have to change – this is capitalism after all. Past experience shows that casualties fall when such change takes place and only the good, the lucky and the subsidized survive. The lucky are rarely perpetually fortunate while for the subsidized we should return to the wider comparison with other industries.

The Mini was launched in 1959 and soon acquired cult status, sold over five million units and is still the template for BMW's successful model today – a truly great product. However because of an accounting error or deeper structural malaise, each model sold delivered a £35 loss to the manufacturer and contributed to the eventual demise of Austin, Morris, BMC and British Leyland etc.

In summary for the aviation insurer of 2011, if they wish to remain in business, providing future support to one of the world's most dynamic and cutting edge industries, the message is clear. Be good, and if you can't be good be very, very careful.

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David Whiter,

Head of Aviation & Executive Committee Member - Aspen Insurance

Biography

Aviation Experience: 30 years

David previously led international aviation operations at CIGNA and XL Insurance.

David possesses over 30 years experience in the London Aviation Market and is currently Chairman of the International Underwriting Association's (IUA) Aviation Technical Committee.

If you want to feature in Lead Lines, or know someone who does, email a brief description of yourself and your job role to: publications@jltre.com

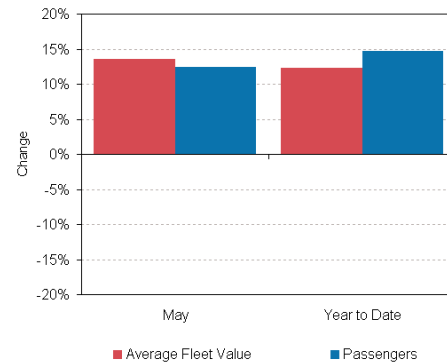
Renewal Analysis

Exposures

Exposure growth continues in May with nearly all the renewals showing noticeable growth in passengers and AFV.

Year on Year % Exposure Change

May / Year to date. Based on latest Information at 26 May 2011



Source: JLT Database

Premiums*

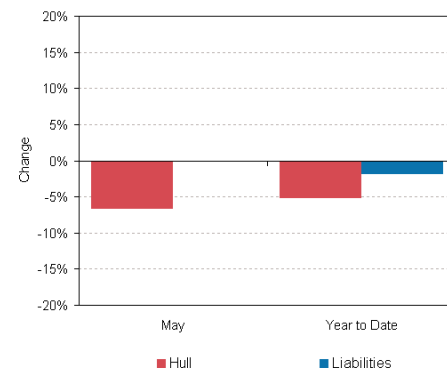
Despite the exposure increases premium overall is down slightly. A few of the larger accounts renewing in May received rate reductions better than would be expected from the influence of exposure growth alone.

Year to Date (Like for Like)	Hull USDm	Liability USDm	Total USDm
2010	65	125	190
2011	62	123	185
% Change	-5%	-2%	-3%

* Net of brokerage and at lead terms

Year on Year % Premium Change

May / Year to date. Based on latest Information at 26 May 2011



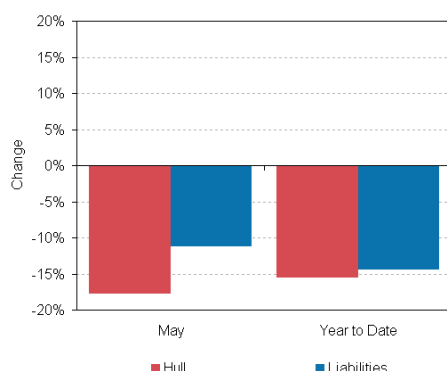
Source: JLT Database

Rates

Following the pattern seen so far in 2011 airlines with significant exposure growth have been able to achieve good rate reductions.

Year on Year % Rate Change

May / Year to date. Based on latest Information at 26 May 2011



Source: JLT Database

Comment

May continues the momentum of airline renewals and provides the market with an interestingly varied cross-section of operators from around the world.

The largest is the UK based budget airline easyJet which has shown continued fleet and passenger growth over the years, and for 2011 has moved broker from Marsh to JLT. The easyJet fleet value now stands in excess of USD7 billion, flying over 57 million passengers annually.

The Virgin Group is another major player consisting of Virgin Atlantic, Virgin Blue in Australia and Virgin America with a combined fleet valued in excess of USD11 billion.

Other notable operators renewing are AirAsia from Malaysia, Air Transat from Canada, Transaero of Russia, Freebird Airlines of Turkey, Ryan International of the USA, and flag carriers such as Royal Brunei Airlines, and Tarom of Romania.

Forthcoming Airline Renewals

Of the June renewals there are only two airlines which have substantial fleet values.

The largest of the two, by far, is Eva Air of Taiwan followed by Aegean Airlines of Greece.

In the table below we list a selection of the larger renewals due to take place next month.

One airline that is missing from this years June renewals is Kingfisher Airlines of India, with a fleet valued in excess of USD2.8 billion. Kingfisher had originally been a June renewal but owing to a thirteen month policy now comes up in July.

Airline	Renewal Date	Expiring AFV USDm
Eva Air	1st June	4,800
Jordan Aviation	1st June	219
Wind Jet	4th June	362
Bulgarian Aviation Group	6th June	342
STC Russia	6th June	761
Belle Air	9th June	142
Vim Airlines	10th June	221
Uzbekistan Airways	14th June	663
Amsterdam Airways	16th June	107
Olympic Air	17th June	937
Aegean Airlines	17th June	1,178
Nile Air	19th June	122
Armavia	21st June	215
Canjet	30th June	182

Source: JLT Database, based on current risks with AFV in excess of USD100m

Loss Analysis

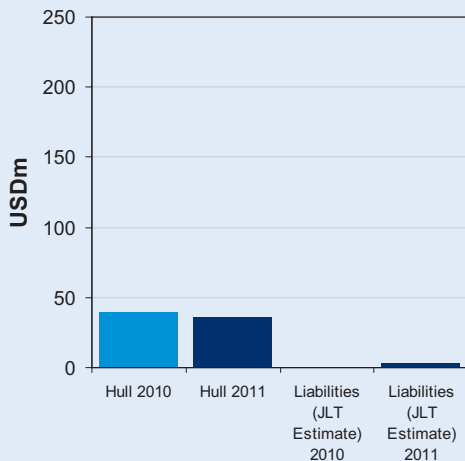
Airline Loss Summary

April

- Hull and spares losses of USD35.80m
- 32 airline fatalities
- Liability loss estimate of USD3.25m

April Losses

All Known Airline Losses Net of deductible

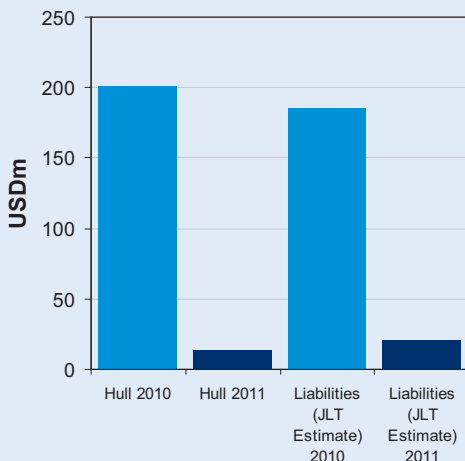


May

- Hull losses USD14.36m
- 47 airline fatalities
- Liability loss estimate of USD20.70m

May Losses

All Known Airline Losses Net of deductible



Airline Loss Summary

7th	Merpati Nusantara	Xian MA-60 (PK-MZK)	Indonesia
<p>On approach to Kaimana from Sorong in rain and thick fog, the aircraft impacted water around 800 meters before the runway threshold. The aircraft was on a scheduled passenger flight with 19 passengers and 6 crew, 2 of whom were airline technicians travelling as passengers. There were no survivors. Reports suggest the aircraft was in a hold due to visibility at the aerodrome being below acceptable levels.</p>			
9th	Continental Airlines	Boeing 737-800 (N12221)	USA
<p>Taxying for takeoff at Greenville - Mid Delta Regional Airport on a ferry flight following repainting, the aircraft taxied into a hole which had appeared in the taxiway causing a main undercarriage to collapse and the vertical wingtip to break.</p>			
10th	VLM Airlines	Fokker F50 (OO-VLE)	Netherlands
<p>The aircraft was undergoing pre-departure maintenance at Rotterdam Airport when the main undercarriage collapsed. The aircraft suffered some skin and structural damage. No persons were injured.</p>			
17th	Great Lakes Airlines	Beech 1900D (N218YV)	USA
<p>Landing at Denver International, the aircraft encountered windshear in the final stages of the approach causing control to be lost and the aircraft running off the runway. The port main undercarriage failed as the aircraft left the runway.</p>			
18th	Sol Lineas Aereas	Saab 340 (LV-CEJ)	Argentina
<p>The aircraft crashed near Los Menucos en-route Neuquen to Comodoro after declaring an emergency and requesting descent out of icing conditions. There were no survivors of the 19 passengers and 3 crew.</p>			
18th	Omega Aerial Refueling Services	Boeing 707-300C Tanker (N707AR)	USA
<p>The aerial refuelling tanker under contract to the US Navy was departing from Point Mugu, CA, when, reportedly, two of the aircraft's engines suffered a compressor stall. The crew decided to abandon takeoff but in so doing, the aircraft suffered an undercarriage collapse and departure of an engine. The ensuing fire engulfed the aircraft but the three crew escaped with minor injuries. No insurance details are known currently but it is believed to be covered in the the London market.</p>			

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

Market News

Insurance

- AM Best has removed the ratings of Tunis Re from under review with negative implications.
They have now affirmed the financial strength rating of B+ and issuer credit rating of bbb-. The outlook assigned to both ratings is stable.
- AM Best has affirmed the financial strength ratings of A+ (Superior) and issuer credit ratings of "aa" for Travelers Companies Inc. The outlook for these ratings is stable.
- AM Best has removed Brit Insurance from review with negative implications and affirmed the financial strength rating of A (Excellent). The outlook assigned to the rating is stable.
- Standard & Poor's has downgraded the financial strength rating of French Insurer Groupama S.A. to BBB+ from A- because of its "material exposure to Greek government bonds". Standard & Poor's awarded the BBB+ rating a negative outlook.

Airline

- Icelandic volcano activity threatened the airline industry, again.
The Grímsvötn volcano, Iceland's most active volcano at the heart of its biggest glacier, began erupting late on 21 May 2011, spewing forth a high density cloud of ash 12 miles high.
Scientists declared the end of the eruptions on 28 May 2011.
It is estimated that as a result of this event around 1,200 flights were cancelled across British and European airspace.
The case for Business Interruption...
Non-damage BI cover has always been a low priority aspect of an

airlines/airports risk management programme.

However the recent events such as the Icelandic volcanic ash clouds and the Japanese earthquake and tsunami have highlighted the economic risk to airlines/airports worldwide.

To help limit these risks there have recently been a number of innovative Business Interruption products unveiled in the aviation sector. These products have been designed to pay out for the business interruption costs in precisely these circumstances.

For further information on this topic please contact your local JLT representative or email us at publications@jltre.com

- Japan's Sendai airport, currently under reconstruction from March's earthquake and tsunami, is due to resume international flights in late June, said Japan's Ministry of Land, Infrastructure, Transport and Tourism (MLIT).

The airport in the disaster-hit Miyagi Prefecture will begin handling international charter flights in late June and aims to resume regular scheduled international flights from 25 July.

The number of arriving domestic flights, now at one per hour, will be doubled from 25 July and the terminal building and its facilities will be fully operational at the end of September, the ministry said.

Arrivals and Departures

- Brit Insurance has announced the appointment of Nick Prettejohn as Chairman after the company's annual general meeting.
In addition Hans-Peter Gerhardt was voted onto the board.
- Barlow Lyde & Gilbert LLP (BLG) announced the appointment of nine new partners across its offices in the UK and Asia.
The new partners include Ian Plumley (commercial risk and reinsurance) in London, Antony Sassi (insurance and reinsurance) in Hong Kong and Mark Errington (insurance and reinsurance) in Singapore.
- Tim Liddiard, Phil Stafford, Matthew Farrar and Geoff Deal have resigned from their roles at Colemont Insurance Brokers.

PlaneTalking

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