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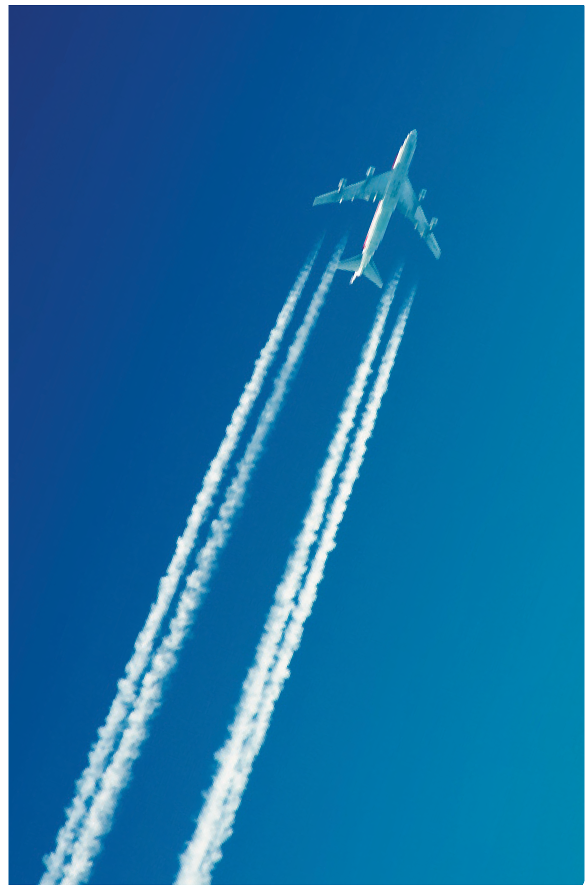
AFRICAN AVIATION TAKES OFF

REMARKS PREPARED FOR DELIVERY
AFRICAN AVIATION'S 20TH ANNIVERSARY
'AIR FINANCE FOR AFRICA' CONFERENCE
SEPTEMBER 13, 2011



Good afternoon. It is a great pleasure to be here at such an exciting time for African aviation. Africa is experiencing dramatic aviation growth, globalisation through alliance membership and perhaps, most significantly, the introduction of the newest generation of aircraft by numerous airlines across the continent.

When talking about risk and insurance we are focused on a service sector that exists to meet the insurance requirements of the current and future risks of the airline industry. The operational risks are potentially catastrophic but, thankfully, are increasingly safe. Our challenge is to keep pace with an industry which is developing fast and deliver solutions to your operations as you look to fly people further, faster and if possible burn no fuel!

As the leading broker to the global airline industry Willis Aerospace has great insight and proven experience in the development of solutions at the cutting edge of industry developments and I therefore will hopefully provide some useful insight for you to future proof your insurance buying.

9/11 CHANGED THE FACE OF AIRLINE INSURANCE

To look forward we need to briefly go back and remember the events that took place almost exactly 10 years ago on September 11 in the United States. That day changed the global airline industry and dramatically changed aviation insurance. It is interesting to note that despite more recent natural catastrophes, the World Trade Center losses remain the largest insurance market loss ever.

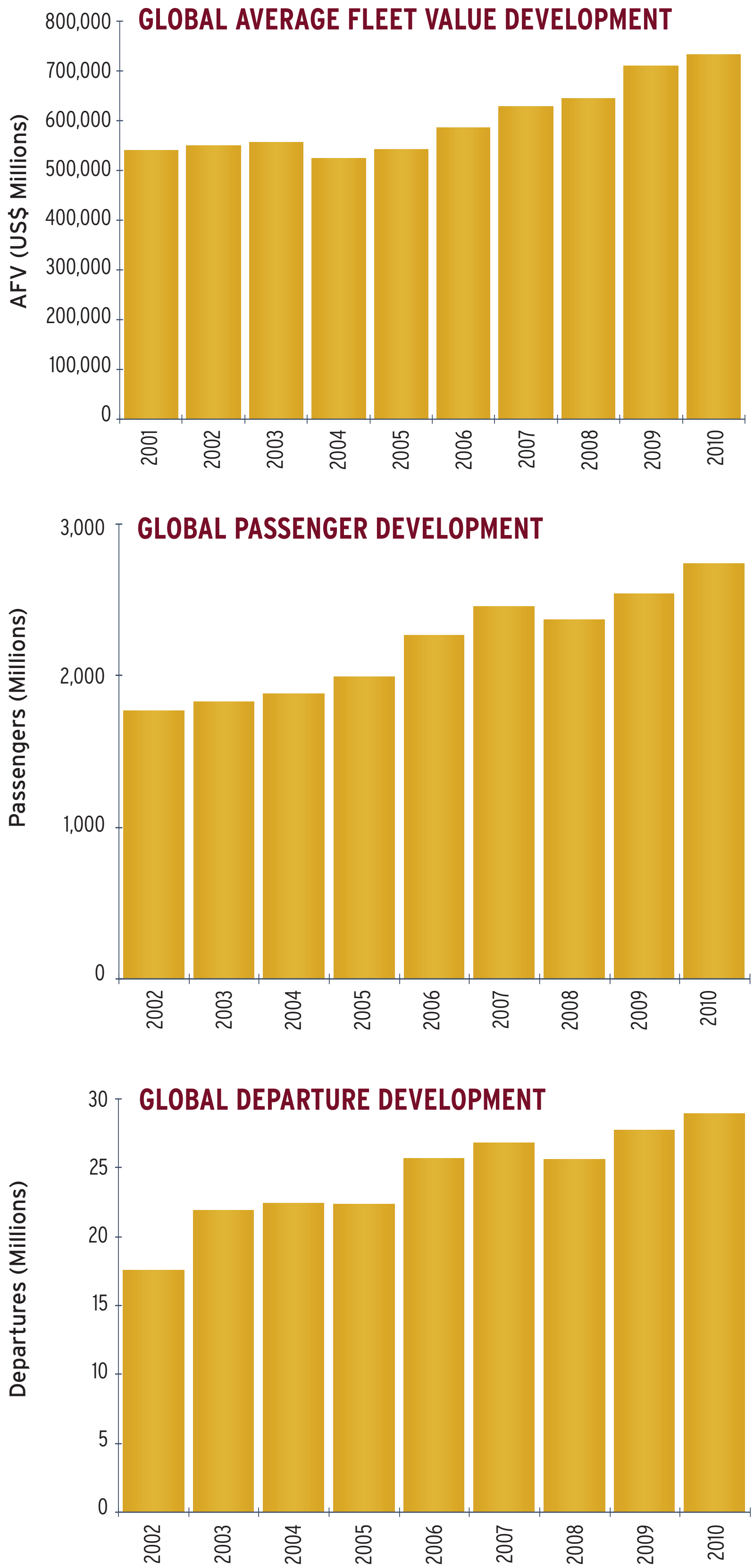
That day resulted in an accelerated re-equipping of the global fleet and the introduction of more technologically advanced aircraft, associated training and improvements in aviation infrastructure that collectively significantly improved the aviation safety record.

More recently, the global economic downturn has seen airlines go through a similar fleet "upgrade" with many of those airlines operating older less fuel efficient aircraft either modernising or ceasing operations. Traditionally many of the retired aircraft in more developed aviation environments would have been bound for Africa but this is becoming less the case.

The wave of industry consolidation that accompanied the downturn has resulted in further aircraft retirements and further improved the overall risk quality of the global fleet.

These two phases have seen the global airline risk profile improve with the current global fleet being the youngest and most technologically advanced ever.

FIGURE 1.



SO HOW HAS THIS AFFECTED INSURANCE?

When looking at these charts ***(Figure 1)*** that summarise the airline insurance market exposure over the last 10 years, we see a 36% growth in insured fleet value. This is a combination of the increase in the number of aircraft but more significantly an increase in the number of higher value aircraft now in operation.

We can also see the number of passengers and departures growing at in excess of 60%. It is noteworthy at this point that, from an insurance rating perspective, the old liability rating basis of RPKs is now largely obsolete due to it no longer being viewed as an accurate measure of airline liability exposure.

Looking at the same graphs for African airlines we see a similar scenario ***(Figure 2)***.

FIGURE 2.

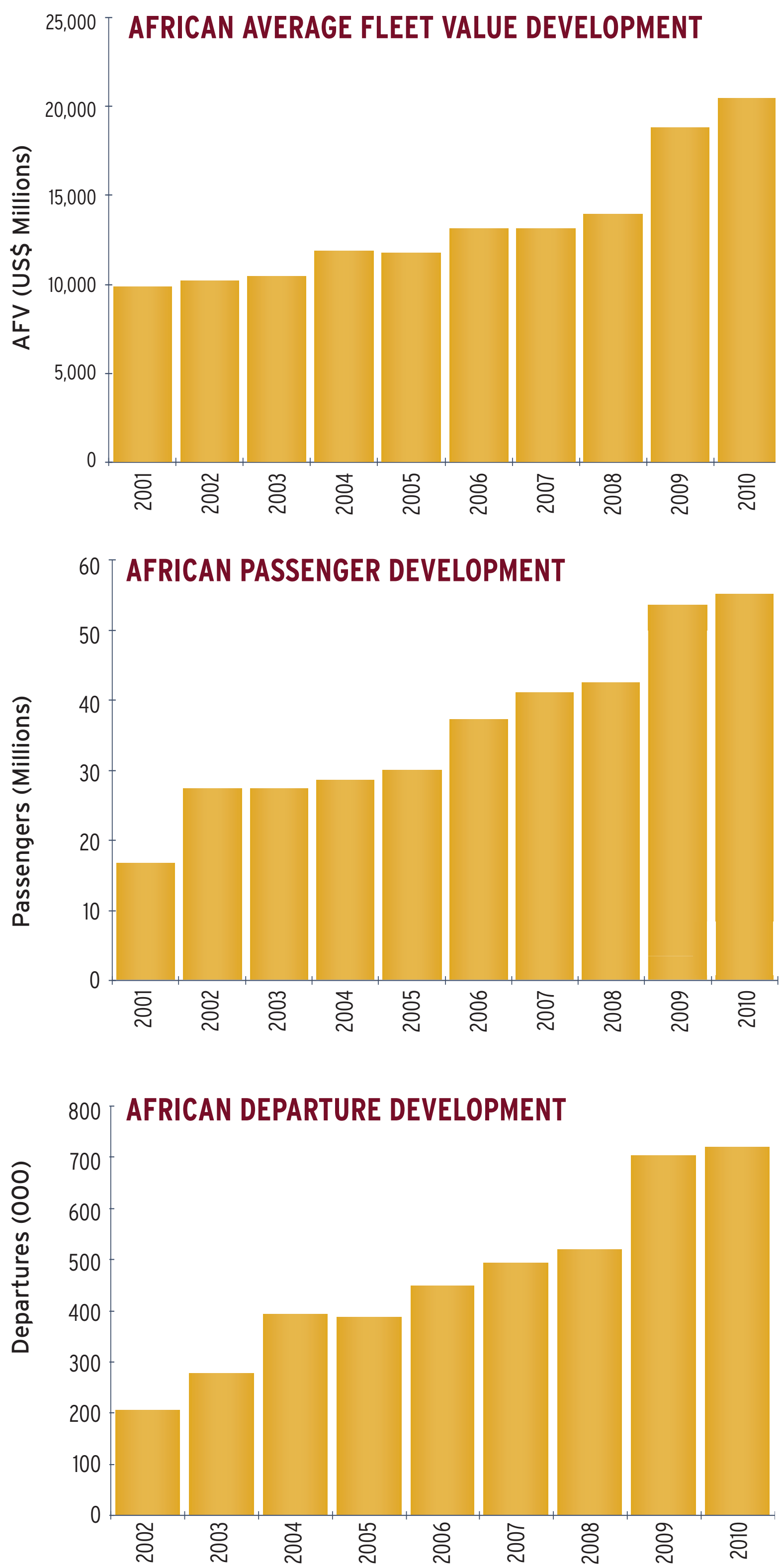
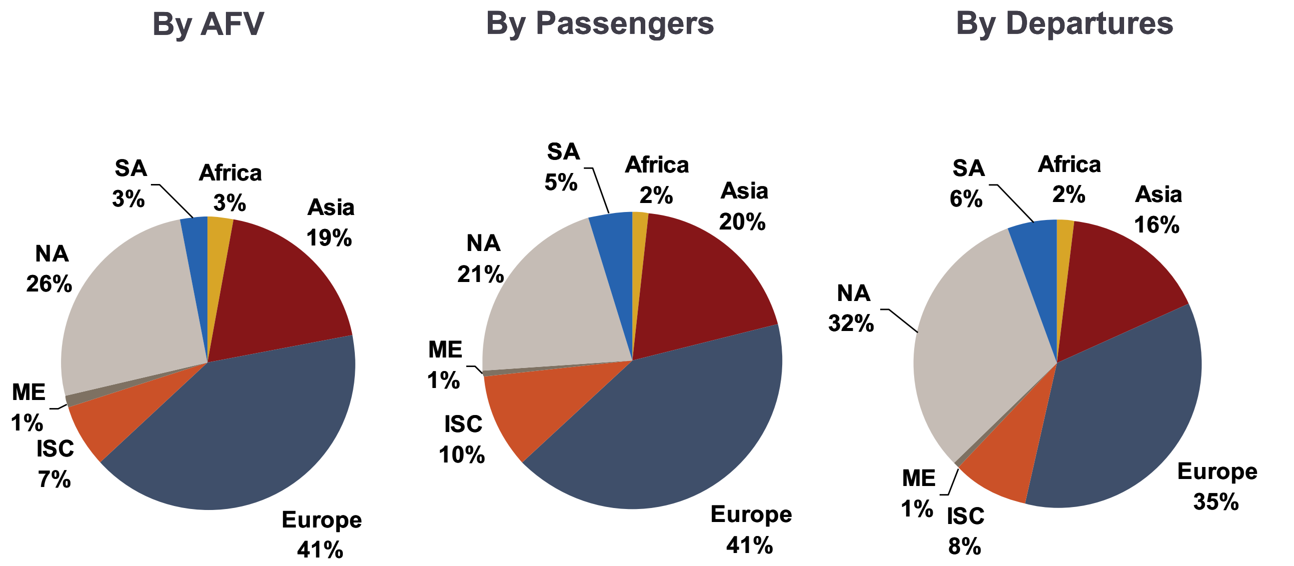
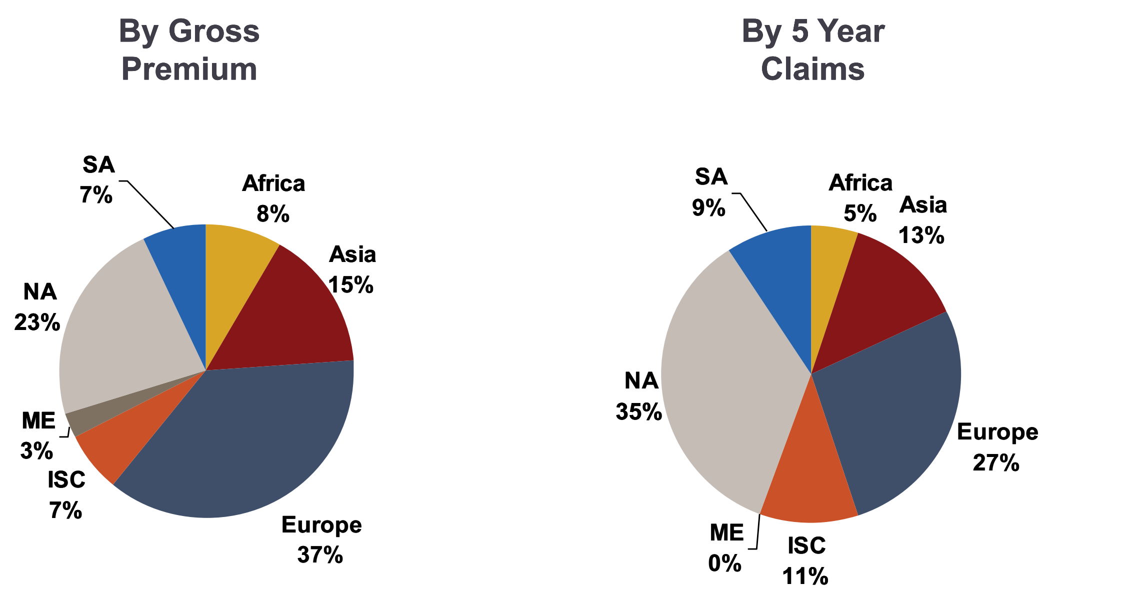


FIGURE 3. **GLOBAL AIRLINE REGION SHARE**



Despite these levels of growth, when looking at this next chart ***(Figure 3)***, the overall exposure contribution from the African continent remains small and significantly contributes a disproportionate amount of premium and claims. ***(Figure 4)***

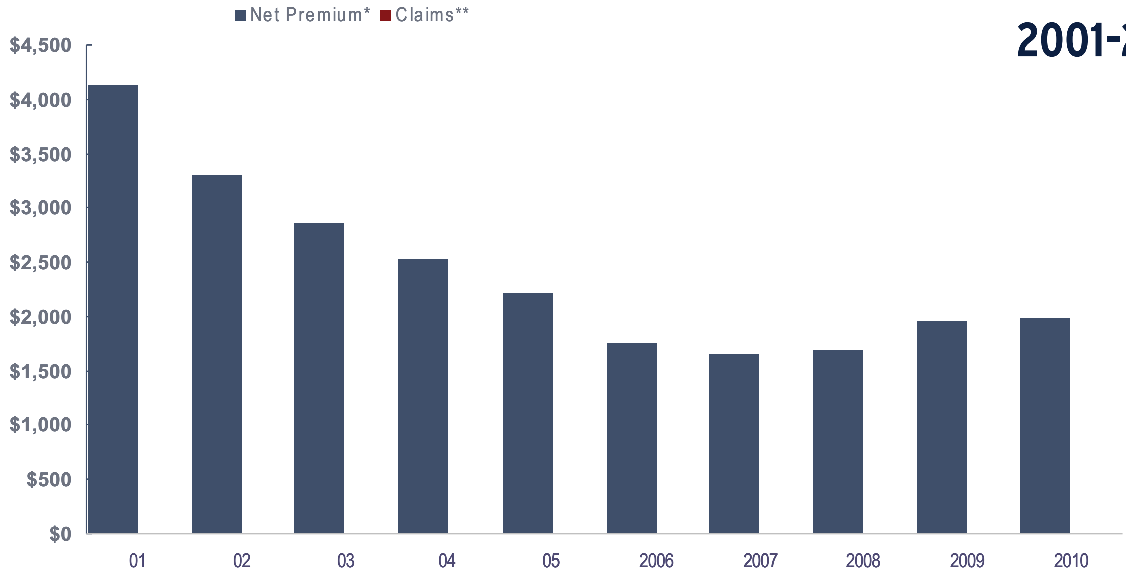
FIGURE 4. **GLOBAL AIRLINE REGION SHARE**



Our next view is of the market premium development over the same period ***(Figure 5)*** we can see that premiums have reduced dramatically since 2001 with the insurance rates applied being significantly reduced. The good news for you as buyers, therefore, is that all this new exposure is not translating into increased premium.

FIGURE 5. **WORLD WIDE AIRLINE HULL & LIABILITY PREMIUM**

2001-2010



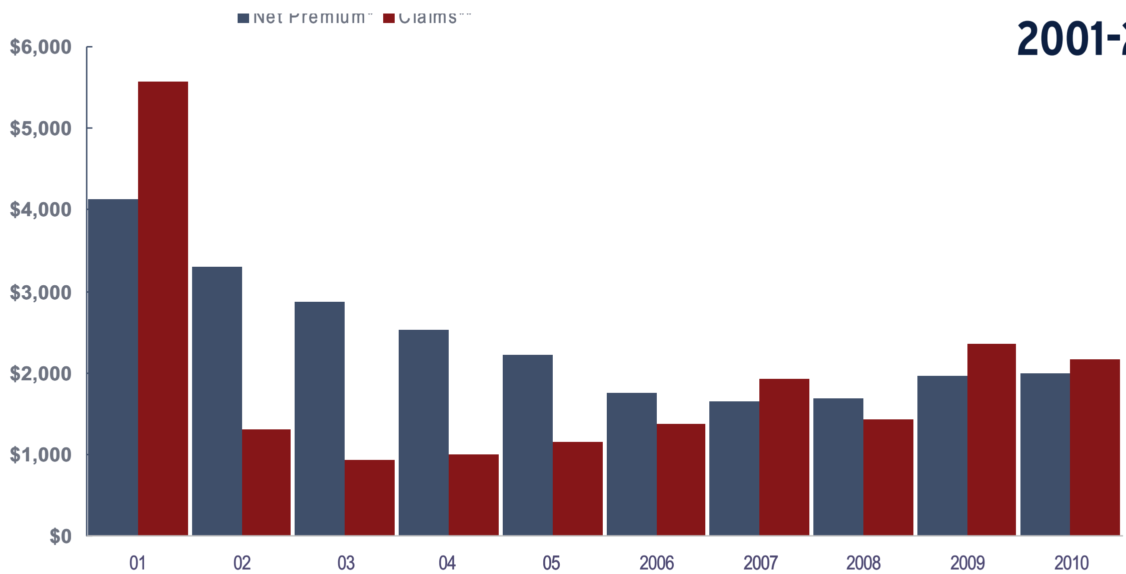
* Premium includes all known airlines with an AFV in excess of US$100m and is based on Net London Lead Terms; it is subject to change as more information becomes available.

** Claims shown include the estimated figure for attritional losses. Claims are updated as more information becomes available.

When we look at the claims situation ***(Figure 6)*** over the same period we can see that, fortunately for underwriters, all of this new exposure has not translated into claims either. We can clearly see the downward impact on the claims total from the fleet development previously mentioned.

FIGURE 6. **WORLD WIDE AIRLINE HULL & LIABILITY PREMIUM AND CLAIMS**

2001-2010



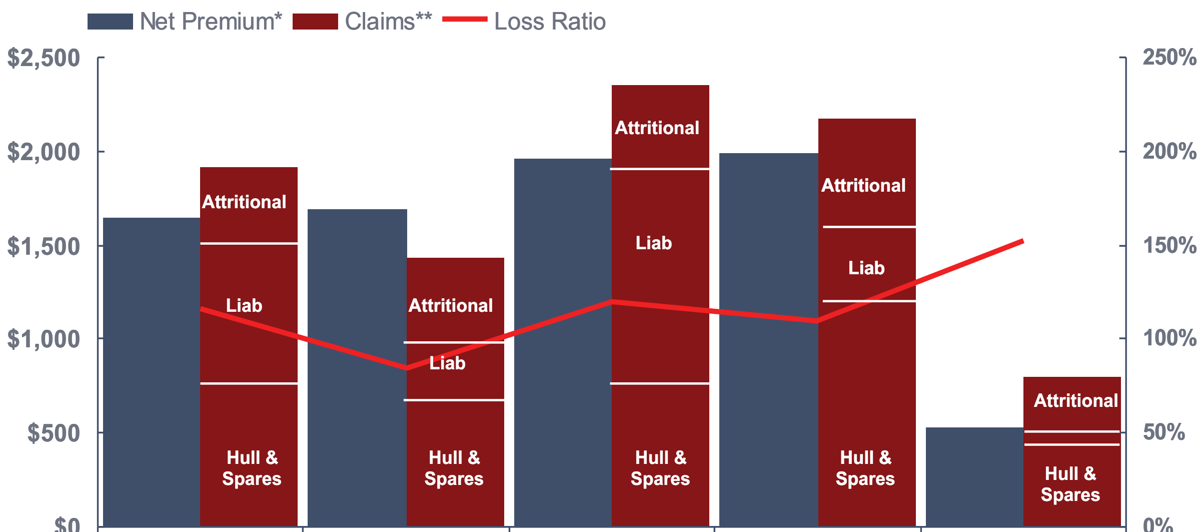
* Premium includes all known airlines with an AFV in excess of US$100m and is based on Net London Lead Terms; it is subject to change as more information becomes available.

** Claims shown include the estimated figure for attritional losses. Claims are updated as more information becomes available.

In recent years the level of claims has stabilised but we have seen a change in the nature of the claims taking place. The level of airline insurance losses during both the 2009 and 2010 exceeded US$2billion but the similarity of the loss total masks a significant change in the underlying make up of the losses. ***(Figure 7)***.

FIGURE 7. **WORLD WIDE AIRLINE HULL & LIABILITY PREMIUM AND CLAIMS**

2007-2011



	2007	2008	2009	2010	2011
Net Premium*	$1,645	$1,687	$1,961	$1,985	$526
Claims**	$1,918	$1,431	$2,352	$2,173	$801
Loss Ratio	116.6%	84.8%	119.9%	109.5%	152.3%
Est Att Losses	$425	$425	$450	$450	$450

* Premium includes all known airlines with an AFV in excess of US$100m and is based on Net London Lead Terms; it is subject to change as more information becomes available.

** Claims shown include the estimated figure for attritional losses. Claims are updated as more information becomes available.

LOW LOSS PATTERN

2010 did not see a catastrophe loss occur and there were just eight losses in excess of US$10M that included fatalities. The losses are now largely high valued hulls, numerous costly aircraft are slipping off runways or catching fire around the world. Added to this have been a few unusual but in insurance terms costly incidents, hangar fires or extreme weather related losses.

This loss pattern has continued into 2011 as the most recent three losses of an Asiana B747-400 Freighter, Egyptair B777 and Caribbean Airlines B737-800 bring a combined US$250 million loss value to market, without any passenger fatalities. The good news is that these losses are not of a sufficient value, either individually or in aggregate to change the overall direction of the market.

The major reason for the increased exposure and these claims not resulting in increased premiums is the level of capacity or number of insurers willing to accept the risks of airlines.

Aviation insurance represents a niche sector of a large insurance company's portfolio. Despite the catastrophe nature of the airline business there is predictability to the losses on an annual basis.

It has to be said that in insurance terms there is no direct correlation between frequency and severity and the catastrophe nature of the sector cannot be underestimated.

This level of predictability, along with a diversity of their portfolio keeps insurers in the sector. We can see from the graph that certainly recently it is not for overall underwriting profit!

The aviation insurance market is at this time potentially more likely to be influenced by some of the world's recent natural catastrophes than its own performance. There is currently little evidence that the losses experienced in the wider market as a result of these natural catastrophes have yet had an effect on the Aviation market.

It is currently a buyer's market, with new aircraft delivering proven safety improvements and growth. This is exactly what insurers want to see so don't miss your opportunity to capitalise from an insurance perspective.

INTRODUCTION OF THE A380

Moving on to the introduction of the new generation aircraft to Africa, it is important to note that with billions of dollars being spent across the continent the cost of insurance represents an extremely small percentage of the overall spend. The focus should, therefore, not be on how much do you pay but on whether you have the right cover.

I am going to touch only briefly out of interest on the A380. As the largest aircraft in the world it brought an inherent requirement for large hull and liability limits. The aircraft is primarily being operated by the largest airlines, which already operated the largest aircraft and as a result purchased the largest liability limits. The aircraft is operating between the world's major economic hubs that already had the infrastructure in place. The introduction of this aircraft in reality, therefore, didn't represent too much of an issue for airlines or their insurers.

At the smaller end of the scale the greater introduction of modern regional jets onto the continent again may create a requirement for slightly larger insurance limits or if introducing them into a larger fleet it may actually call for lower sub limits in your programme.

B787 – THE GAME CHANGER

The saying that "size doesn't matter but it is what you do with it that counts" therefore seems to ring true for aircraft and their insurance, which is why I would like to focus on the B787.

So often described as a game changer, this aircraft truly is when looking from insurance perspective. The new technology means that the B787 has completely different repair requirements and therefore the impact, should it be impacted by the trend for increasingly prevalent hull claims, is yet to be determined.

Of more importance from a risk profile perspective is that the aircraft, along with others such as the B777LR, is allowing airlines to change the nature of their operations, opening new routes and connecting more city pairs in different parts of the world than they do today. Unlike A380 operations, some of these routes may lack the supporting infrastructure.

It is a sad but true fact that in different parts of the world there is a different financial value placed on human life and it is therefore important to know you are buying appropriate levels of cover for these new destinations. The adequacy of your liability limits at the far reaches of a developing route structure is vital.

From a premium perspective the liability rating and exposure basis used is a key consideration in controlling future premium costs as your operations change.

It is therefore important that the programme you buy today in this buyer's market provides enough cover and is charged on an appropriate basis to fit future developments in your operation.

GROUP BUYING OF INSURANCE

Finally I would talk about the opportunity for group buying of insurance. There are proven economies of scale in Airline insurance purchasing. This is demonstrated by the analysis of the Willis 50, which is our study of the largest 50 programmes in the airline insurance market.

This group of 50 programmes represents just 18% of the programmes in the market but between 70% and 80% of the world's fleet and passengers. ***(Figure 8)*** The premium they contribute represents only 57% of the overall premium and 65% of the claims ***(Figure 9)***. You see the benefit.

FIGURE 8. 2010 WILLIS 50 VS OTHER MARKET PROGRAMMES

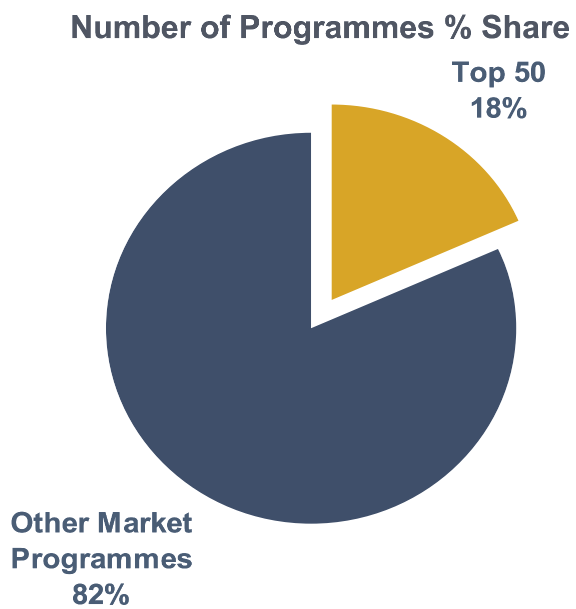
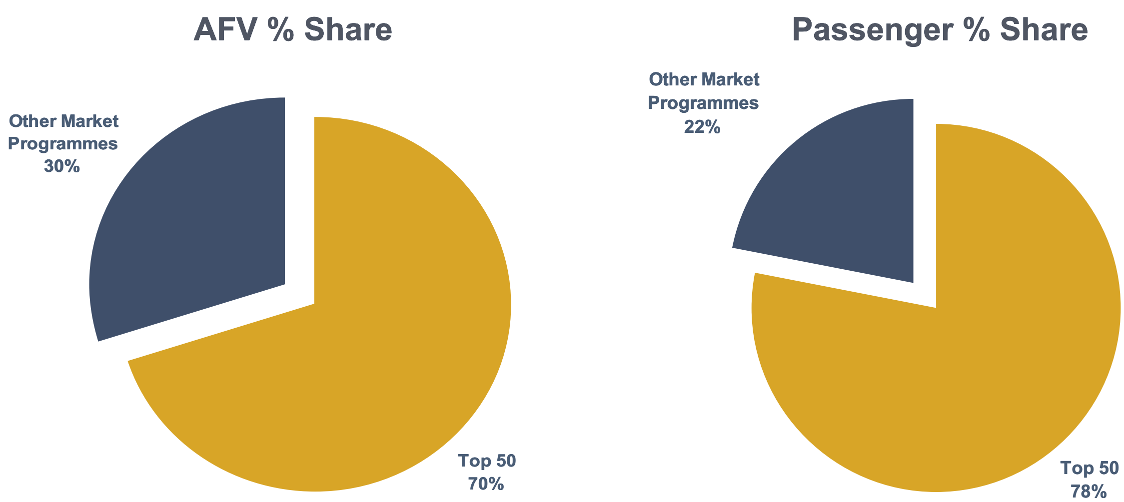


FIGURE 9. 2010 WILLIS 50 VS OTHER MARKET PROGRAMMES



These 50 programmes however represent the insurance buying of hundreds of individual airlines that have some form of economic connection to others in a group and therefore can access these discounts. At this time there are no African airline programmes in the Willis 50.

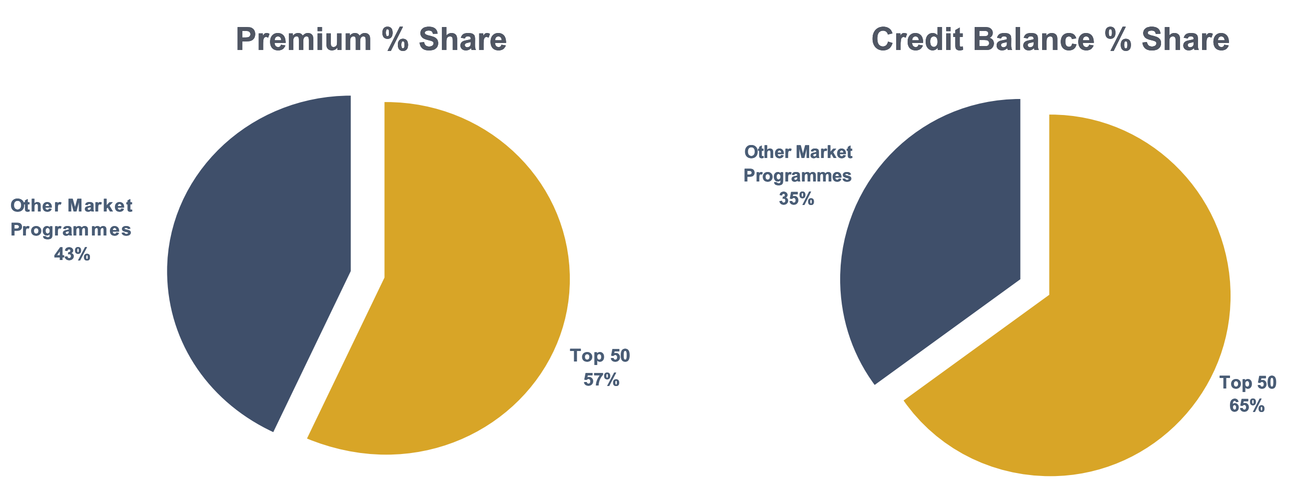
Group buying is not new to Africa. Historically a number of the North African carriers used to buy their aviation insurance on a combined basis but this appears unlikely to be resurrected in the very near future following the events of the “Arab Spring”.

We are going to hear tomorrow about global airline consolidation and the impact on the African airline industry. I can tell you this has already had a significant effect on insurance purchasing arrangements.

Star Alliance carriers Continental and United Airlines in the United States combined their insurance programmes on the completion of their merger in 2010 and earlier this year Oneworld carriers were included in the combined British Airways Iberia programme put together as a result of the formation of IAG.

As we look at the impact on the exposure of the three global alliances ***(Figure 10)*** and as alliance membership broadens across Africa it may represent an opportunity worth exploring when trying to further reduce insurance costs.

FIGURE 10. **2010 WILLIS 50 VS OTHER MARKET PROGRAMMES**



It is clearly an exciting time for African aviation and as the developments take place rest assured the expertise and insurance solutions exists to meet your needs.

In conclusion, let me emphasise the fact that it is important to understand both the insurance cover you will need and the methods available to allow you to buy it in the most cost-effective manner. Thank you. ***(Figure 11)***

FIGURE 11. **ALLIANCE SUMMARY STATS**

	Average Fleet Value (US$bn)	% Share	Passengers (millions)	%Share
oneworld	103.27	14%	385.07	15%
Sky Team	100.64	14%	379.45	15%
Star Alliance	169.03	24%	598.33	23%
Total Alliances	372.94	52%	1,362.85	53%
Airlines outside of Alliances (AFV over US$100m)	345.91	48%	1,231.85	47%
All Airlines (AFV over US$100m)	718.85	100%	2,594.70	100%