THE NEWSLETTER FOR THE AIRLINE INSURANCE INDUSTRY Q1 2013

AIRLINE INSURANCE MARKET

2012 was a great year for the airline insurance market. Buyers, generally, received premium reductions, the global fleet grew generating increased exposure levels, the industry accident experience was excellent making it the safest year ever in terms of fatalities and as a result the insurers experienced the lowest level of airlines insurance losses for over 25 years.

The low loss levels combined with the excess capacity levels meant that by the end of the year in excess of US$200 million of premium had been removed from the airline market as a whole. More than half of this was removed in December. The escalation of premium erosion in the final month of the year demonstrates the level of competition that exists in the market due to excess capacity levels.

Despite this erosion of premium insurers, as a whole, made a profit on their closing 2011 underwriting year. If loss levels remain similar to the last two years, they will also have enough premium income to generate a profit on their 2012 year of account.

If the industry performance continues to be excellent and this does turn out to be the case it will build on two profitable years in the last three and three in the last five. It will also continue to raise the question of what premium volume is enough for market sustainability over the medium term?

The December renewals generated over 40% of the annual premium total from 30% of the renewals. The month generated the largest level of premium reduction at over 14%. The double digit reductions achieved in November and December were the only months to have such a level of reduction, other than April.

The major renewals that took place during the month were the US Majors United Continental, Delta, US Airways and Southwest. The largest programme in the market, CAAC, also renewed with significantly increased exposures highlighting the level of air travel growth that continues to take place in China.

The renewals were spread across all regions and sectors and provided a mix of risk profile, loss performance and exposure growth. The concentration of activity in the final few weeks of the year must however limit the opportunity for differentiation. If the level of reduction is greatest when "hunting in a pack" is the requirement for differentiation diminished?

CONTENTS

AIRLINE INSURANCE MARKET OVERVIEW………1

MARKET NEWS…………….3

WILLIS 50……...……………3

INDUSTRY NEWS…….……4

LOSSES OVERVIEW………6

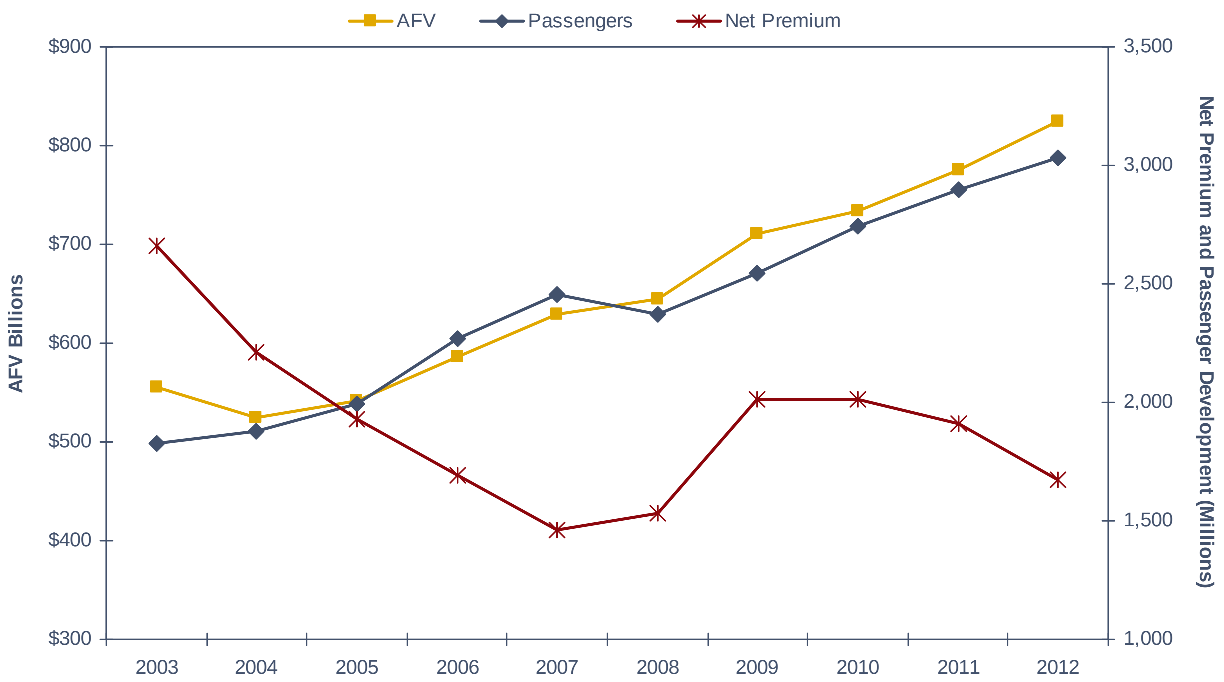
FORTHCOMING RENEWALS……………......8

AVIATION REINSURANCE…………....9

2012 NET % PREMIUM AND EXPOSURE MOVEMENTS (HULL & LIABILITY)

	No. of Renewals	AFV % Change	PAX % Change	2011 Net Premium US$ m	2012 Net Premium US$ m	US$ m Premium Change	Premium % Change
January	4	14%	25%	$ 3.85	$ 4.42	$ 0.57	14.7%
February	4	12%	7%	$ 7.13	$ 6.70	$ -0.43	-6.1%
March	11	21%	30%	$ 35.59	$ 38.16	$ 2.57	7.2%
Q1	**19**	**20%**	**27%**	**$ 46.57**	**$ 49.28**	**$ 2.71**	**5.8%**
April	13	8%	8%	$ 123.36	$ 106.73	$ -16.62	-13.5%
May	17	1%	7%	$ 71.74	$ 69.13	$ -2.62	-3.6%
June	17	1%	7%	$ 34.77	$ 33.31	$ -1.46	-4.2%
Q2	**47**	**5%**	**8%**	**$ 229.87**	**$ 209.17**	**$ -20.70**	**-9.0%**
July	35	3%	0%	$ 227.71	$ 209.79	$ -17.92	-7.9%
August	9	3%	4%	$ 36.65	$ 34.75	$ -1.90	-5.2%
September	10	18%	13%	$ 29.34	$ 27.97	$ -1.38	-4.7%
Q3	**54**	**4%**	**1%**	**$ 293.70**	**$ 272.50**	**$ -21.20**	**-7.2%**
October	11	7%	-2%	$ 123.05	$ 118.77	$ -4.28	-3.5%
November	40	4%	2%	$ 366.71	$ 318.12	$ -48.59	-13.2%
December	73	5%	4%	$ 820.62	$ 704.66	$ -115.96	-14.1%
Q4	**124**	**5%**	**3%**	**$ 1,310.38**	**$ 1,141.55**	**$ -168.83**	**-12.9%**
2012 Total	**244**	**5%**	**4%**	**$ 1,880.52**	**$ 1,672.51**	**$ -208.01**	**-11.1%**

10 YEAR PREMIUM AND EXPOSURE MOVEMENTS (HULL & LIABILITY)



HULL WAR AND EXCESS 52

The Hull War and Excess AVN52 markets also remain soft with rate reductions in the region of 15% to 20%. The premium volume has been eroded to such an extent that these markets have limited ability to create leverage on the core hull and liability programme but can still be the source of premium savings. These markets would likely react swiftly and dramatically to any significant market loss

MARKET NEWS

MARKEL TO ACQUIRE ALTERRA

Alterra announced on December 19, 2012 that it signed a definitive merger agreement with Markel Corporation. Under the terms of the agreement, Markel will acquire Alterra for an aggregate consideration of approximately $3.13 billion.

Markel Corporation is a diverse US financial holding company serving a variety of niche markets. Its principal business markets and underwrites specialty insurance products. Markel is viewed as a high quality insurance enterprise with a winning investment strategy. The integration of Alterra's people and franchises is expected to fulfil a key business need in Markel's strategy to gain scale and diversification in the global market.

MARTIN JACKSON OF ASPEN PROMOTED TO DEPUTY ACTIVE UNDERWRITER

Martin Jackson has been appointed to the position of Deputy Active Underwriter for the Aspen Lloyd's Syndicate, with Kate Vacher remaining as Active Underwriter. Martin will undertake this role alongside his existing responsibilities as Manager of Underwriting in the Aviation Insurance team.

AIRCLAIMS NEW APPOINTMENTS

Airclaims have announced that John Morgan and Sally Sutherland have joined their Risk & Asset Management team recently. They also announced that Phil Spurr, who was a Surveyor/Project Manager within the Risk & Asset Management team, has been promoted to the role of Continuing Airworthiness Manager.

There have also been changes to the claims team, with Stephen Hill being promoted to Senior Surveyor and Gary Clift joining the Claims team from his previous employer, Qantas Airways.

WILLIS 50

The airline industry consolidation that has taken place in recent years has had a significant knock on effect to the airline insurance purchasing arena. The general increase in insurance programme size and in particular the rise of group programmes along economic, regional or alliance lines has developed what Willis believe to be very much a two tier and perhaps even three tier market for airline insurance purchasing.

It is with an understanding of this change in market dynamics that we choose to split our market trending and analysis between the largest 50 programmes, by passenger volume, and the other market placements. We call this the Willis 50.

This is in no way designed to diminish the importance of the airlines and or the programmes outside the 50 but is reflective of the fact that there is an increasingly distinct market treatment and influence between the largest programmes and the overall market result. It is therefore designed to be of greater relevance to airline insurance buyers in either segment.

This difference in treatment is highlighted in the 2012 renewal summary table below.

	AFV % Change	PAX % Change	2011 Net Premium USD M	2012 Net Premium USD M	USD M Premium Change	% Premium Change
Market Risks Excluding Willis 50 Programmes	6%	1%	$716.42	$659.19	-$57.23	-8.0%
Willis 50	5%	4%	$1,164.10	$1,013.32	-$150.78	-13.0%
All Programmes Excess of $100 million AFV	**5%**	**4%**	**$1,880.52**	**$1,672.51**	**-$208.01**	**-11.1%**

INDUSTRY NEWS

AMERICAN AIRLINES & US AIRWAYS TO MERGE

American Airlines and US Airways have announced plans to merge in an $11 billion deal that will create the largest airline in the world.

The combined carrier will carry more than 170 million passengers and generate revenues of more than $170 billion annually, based on 2012 numbers. It will retain the American name, be based in Fort Worth, Texas, and be a member of the Oneworld alliance.

"The combination of American and US Airways brings together two highly complementary networks with access to the best destinations around the globe and gives us a strong platform to provide our customers the most connected, comfortable travel experience available," says Tom Horton, chairman, president and chief executive of American.

"The operational and financial strength of the combined airline is expected to enable continued investment in new products and technologies and will create exciting new opportunities for our people, even as we deliver strong cash flow and sustainable profitability."

Doug Parker, chairman and chief executive of US Airways, says: "Today marks an exciting new chapter for American Airlines and US Airways. The combined airline will have the scale, breadth and capabilities to compete more effectively and profitably in the global marketplace."

Parker is to become chief executive and Horton chairman of the new company. Horton will step down and Parker will become chairman after the new carrier's first annual meeting of shareholders.

American creditors will receive a 72% stake and US Airways shareholders a 28% stake in the new company.

The airlines hope to close the deal during the third quarter, however it requires approval of the bankruptcy court, US Airways shareholders, as well as US antitrust regulators.

The combined fleets will have 948 mainline aircraft, ranging from the 99-seat Embraer 190 to the 310-seat Boeing 777-300ER, and 568 regional aircraft, as of the end of 2012. It will have hubs at Charlotte, Chicago O'Hare, Dallas-Fort Worth, Los Angeles, Miami, New York John F. Kennedy (JFK), Philadelphia, Phoenix and Washington National.

Source: Flight Pro

AIRLINE ACCIDENT RATE HITS NEW LOW IN 2012

World airline safety in 2012 was exceptionally good whichever way the statistics are cut, particularly in terms of accident rates, but also in simple accident numbers.

Paul Hayes, senior safety analyst at Flightglobal consultancy Ascend, has warned, however, that the rate is probably "a bit of a fluke", and that the figures for 2013 may be less good without actually indicating a reversal in real airline safety.

A single year's world airline safety statistics, particularly when there are so few fatal or serious airline accidents, is not statistically significant except as part of a longer-term trend, Hayes notes. Nevertheless, he adds, 2012 has reinforced a favourable trend in an emphatic manner.

Flightglobal figures show there were 21 fatal airline accidents in 2012, resulting in a total of 425 deaths. This compares with respective figures in 2011 of 32 and 514. Flight International's statistical sample produces figures that vary slightly from those from other sources even if they tell much the same story. They take account of all fatal airline accidents whether they involve Western- or Eastern-built aircraft, and include aircraft of all weights, sizes and engine types, in passenger and non-passenger airline operations.

Ascend's Special Bulletin analysing airline safety performance last year says: "2012 was another good year for safety, with the fatal accident rate falling from about one per 1.4 million flights overall in 2011 to one per 2.3 million flights in 2012. On this basis, 2012 was certainly the safest year ever and, on the face of it, 65% safer than 2011, which itself had been labelled 'the safest year ever'. However, unfortunately, we do not believe that the world's airlines have suddenly become this much safer and 2012's accident rate, perhaps, should be considered more of a fluke than the new norm."

Source: Flight

WORLD'S SAFEST AIRLINES REVEALED

The Jet Airliner Crash Data Evaluation Centre, based in Germany, analysed all serious incidents suffered by airlines since 1983 in its study, as well as the number of miles flown by each carrier, to produce its annual Safety Index.

Air New Zealand, Cathay Pacific, Emirates and Etihad were also named among the five safest carriers, while BA came 10th, Virgin 15th, easyJet 17th and Ryanair 32nd.

No US airlines made the top 20 - Southwest Airlines was the highest ranked at number 21.

Other British carriers ranked in the study included Thomas Cook Airlines, which was placed in 18th, and Thomsonfly, which came 26th.

There were 496 fatalities on commercial passenger flights last year, according to the report, two fewer than in 2011. The most significant involved a Dana Air flight which crashed in Nigeria, killing 169 people, and a Bhoja Air flight which crashed in Pakistan, killing 127.

A total of 30 planes were destroyed and there were 44 “hull losses”, or aircraft write-offs, one less than the previous year.

The world’s safest airlines:

1. Finnair

2. Air New Zealand

3. Cathay Pacific

4. Emirates

5. Etihad

6. EVA Air

7. TAP Portugal

8. Hainan Airlines

9. Virgin Australia

10. British Airways

Source: Daily Telegraph

ASCEND VOTED AIRCRAFT APPRAISER OF THE YEAR

Flightglobal's Ascend Online advisory and data service has been voted aircraft appraiser of the year in the Airline Economics Aviation 100 Awards.

The award is in recognition of Ascend Online's "consistent and professional approach, combined with thorough, measured and impartial appraisals".

In recognition of the award, Les Weal, head of valuations at Ascend Online, will be hosting a free webinar entitled "2013 - The Year of Snakes (and Ladders)?" on 7 February at 16:00 GMT.

The webinar will interpret traffic data from 2012 and early indicators from 2013 in order to assess whether lease rates and values are emerging from the global financial crisis.

"If we do see an earnest recovery in values, by the end of 2015 market values may return to above the base value line for in-production types," Weal notes.

Source: Flight Pro

AIRBUS DELIVERIES IN 'BALLPARK' OF 2012 TARGET

Airbus will far exceed its gross order forecast for 2012 and expects deliveries to be in the region of its target of 580.

The airframer has yet to disclose its final backlog and delivery figures for the year, and will reveal the totals during an event on 17 January.

But an analyst familiar with the matter says the order for 75 Airbus A320neo jets from Turkey's Pegasus Airlines will be booked into 2012.

The airframer had predicted sales of 600-650 aircraft for the year, and by the end of November 2012 its gross total had reached 646. Pegasus's order takes the total past 720. The analyst also indicates that the airframer will unveil more "Christmas presents" during the January event.

Airbus had originally set a delivery target of 570 aircraft and raised this figure to 580 by mid-year. The analyst says the delivery total for 2012 is "in the ballpark" of the target. Airbus declines to comment. But the airframer, which had delivered 516 aircraft by the end of November, has lately been handing over some 50-60 aircraft in the final month of the year.

Airbus met its target of 30 A380 deliveries for 2012 and the airframer last year nudged monthly production rates upwards for the A320 family.

Rival Boeing had delivered 537 aircraft by the end of November 2012, and had forecast 585-600 for the full year.

Source: Flight Pro

BOEING POSTS 1,203 ORDERS IN 2012, LARGEST GAIN SINCE 2007

Boeing posted 1,203 net orders for commercial aircraft in 2012, the second-highest tally over the past decade.

The first full year of sales of the re-engined and updated 737 Max drove the growth in net orders. The 737 Max alone accounted for 1,029 of the 1,124 orders for the single-aisle aircraft, with the balance of 95 orders going for the 737NG.

The 737 total includes orders for 40 aircraft that were added to the order backlog between 18 and 31 December, along with cancellations of 25 orders. The customers who made the orders and the cancellations have not been identified.

Boeing's four other aircraft models accounted for only 79 aircraft combined in the net orders column for 2012.

The 787 programme finished the year with 12 net orders fewer than it began, as 62 cancellations or conversions wiped out 50 new aircraft orders. In three of the last four years, Boeing has lost more 787 orders than it gained.

The 777 programme booked 75 new orders and seven cancellations, yielding a positive net of 68 aircraft. The 767 net orders increased by 22, while the 747-8 added one.

Source: Flight Pro

US AIRLINES POISED FOR POSITIVE 2013

Investment bank Dahlman Rose is "bullish" about the prospects of the US airline industry in 2013.

The firm anticipates that a 1% to 2% increase in traffic and a 2% to 4% increase in unit revenues will benefit the entire industry, according to a report today.

"We are upgrading our view of the airline industry to a bullish one from a cautious one," says Helane Becker, airline analyst and a director at Dahlman Rose, in the report. "We believe the year is ending on a fairly strong note, with November the worst month of the current quarter."

Delta Air Lines is the bank's top pick for 2013. It cites the Atlanta-based carrier's focus on paying down debt, various strategic investments including those in Virgin Atlantic Airways and the Trainer oil refinery, and build up in New York as rationale for the selection.

"Delta is well positioned to benefit from higher passenger revenue, higher ancillary revenue, and lower fuel costs in 2013," writes Becker.

Dahlman Rose also cites improving forecasts for Alaska Airlines, Allegiant Air, JetBlue Airways, Southwest Airlines, United Airlines and US Airways.

Becker noted that United, which has had a difficult year from an operational perspective, is set to perform better in 2013. "When United merged its operations with Continental, the wings fell off the aircraft and the company sunk, delivering a disappointing product to its consumers (especially to those in San Francisco and in New York/Newark). We believe the airline turned the corner sometime during the past four months, and this should make for easier year-on-year comparisons in 2013."

Dahlman Rose does not include any impact from the fiscal budget cliff that the USA faces at the end of 2012 in its estimates. It anticipates that the US government will "get its house in order" with little long-term impact on the airline industry, in the report.

Source: Flight Pro

LOSSES OVERVIEW

The airline insurance market has experienced another fantastic year in terms of loss performance. The industry recorded the safest year ever and this has fortunately translated into the lowest level of loss for over 25 years. If inflationary increases were applied to the historical losses 2012 is undoubtedly the best year ever in terms of loss performance.

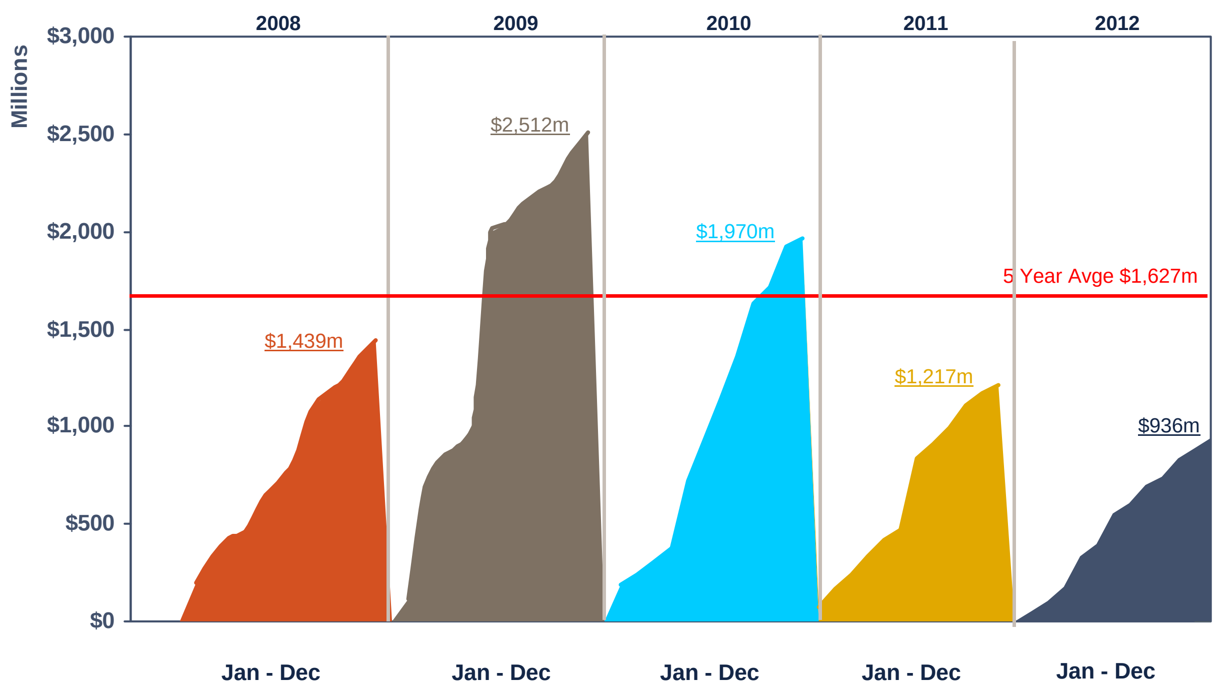
There were 13 losses in 2012 with Hull & Liability reserves over US$10 million. The largest loss of the year was the Dana Air loss which occurred on 3rd June 2012. The MD-83, registration 5N-RAM was destroyed when it crashed into a residential area of Lagos, Nigeria. The aircraft was reported to have lost power in both engines. All 147 passengers and 6 crew members were killed. There were also 10 fatalities on the ground. The hull reserve for this loss was a relatively small amount, but the liability reserve set means that this loss will be the largest in 2012, although this is still below US$50 million.

The hull losses totalled US$386 million, with US$100 million for liabilities and US$450 million for attritionals. The attritional total has not increased significantly in recent years but its importance in the overall total has grown due to the low level of losses overall.

2012 HULL & LIABILITY LOSSES WITH A RESERVE OVER $10 MILLION

Date of Loss	Operator	Aircraft Type	Location of Loss	Fatalities
April 2	Utair	ATR72-200	Tyumen Airport, Russia	31
April 3	American Airlines	Various	Fort Worth International Airport, Dallas, USA	0
April 20	Bhoja Air	B737	Islamabad, Pakistan	127
April 28	UPS Airlines	Various	Louisville Airport, USA	0
June 3	Dana Air	MD-83	Lagos, Nigeria	193
June 9	CSA Czech Airlines	ATR42	Ruzyne International Airport, Prague, Czech Republic	0
June 10	LIAT	Dash 8 & Spares	V C Bird International Airport, Antigua	0
June 20	All Nippon Airways	B767	Narita Airport, Tokyo, Japan	0
August 5	Thai Airways International	B777	Suvarnabhumi International Airport, Bangkok, Thailand	0
August 17	Mandarin Airlines	E-190	Makung International Airport, Taiwan	0
October 13	Centurion Air Cargo	MD-11	Viracopos Airport, Sao Paulo, Brazil	0
October 14	Corendon Airlines	B737	Antalya Airport, Turkey	0
October 29	Atlas Air	Spares	Inwood, New York, USA	0

FIVE YEAR CLAIMS STATISTICS



The erosion of premium means that the level of attritional losses is a focus for underwriters as the premium available for the catastrophe risk is diminished.

The industry is undoubtedly safer and the global fleet is the most technologically advanced it has ever been. The higher values of individual aircraft are being more than offset by the low level of liability losses. We can only hope that the industry experience continues to be excellent and that frequency continues to match severity.

Significant losses that have occurred in December are outlined below.

On December 25, an Air Bagan Fokker 100, registration XY-AGC, crashed into some trees after the aircraft missed the runway and overflew Heho Airport, Myanmar. One passenger on board was killed along with a motorist on the ground. The hull reserve for this loss is US$3.5 million.

On December 25, an Asiana A330, registration HL-7792, suffered damage after a bird strike. The hull reserve for this loss is US$1 million.

On December 6, a VRG Linhas Aereas B737, registration PR-VBY, suffered damage after the engine ingested a bird shortly after take-off. The hull reserve for this loss is US$2.5 million.

FORTHCOMING RENEWALS

With less than 20 renewals the first quarter of the year is the quietest in terms of renewal activity. It generates the lowest level of premium volume of any quarter and represents just 2% of the fleet and 1% of the passenger exposures. It is not fair to say that a quarter is insignificant but with less than $50 million of premium the impact on the market is minimal in terms of influence.

With such low levels of activity we already turn attention to what the 2013 year as a whole may bring.

Whether 2012 marks the bottom of the airline market remains the unanswered question. It is a question that has been posed and answered with a resounding no for the past three years! How much of this will be influenced by the loss position either through improvement or deterioration? How much deterioration would be required to change the direction bearing in mind the abundant capacity that exists? What is going to cause any withdrawal of capacity from a class that is profitable and has an improving safety performance?

Will 2013 be the year that all these questions are answered? Unlikely. The continued downward trend against continued exposure growth is recognised as being unsustainable. However, as we look ahead the early renewals will, in all likelihood, be looking to complete the cycle of significant premium reductions for the first nine months of the year. Unless there is a significant change in either of the market drivers of capacity and claims there will be little change until we approach the 2013 renewal season.

Q1 RENEWALS

Airline/Group Name	Renewal Date	Expiring AFV US$
Federal Govt of Nigeria	01-Jan-13	269,053,000
Airlinair	07-Jan-13	137,800,000
Tailwind Havayollari	07-Jan-13	120,041,667
Hi Fly	05-Feb-13	273,254,000
Corendon Airlines	06-Feb-13	267,679,452
Skynet Asia Airways	20-Feb-13	326,350,576
Almasria Universal Airlines	01-Mar-13	108,588,178
Evergreen International	01-Mar-13	199,850,000
Montenegro Airlines	10-Mar-13	132,272,225
Pullmantur Air	20-Mar-13	159,000,000
Berkut	23-Mar-13	252,147,655
New Livingston	25-Mar-13	220,964,384
Bangkok Airways	28-Mar-13	455,955,565
Cameroon Airlines	28-Mar-13	108,615,000
Sriwijaya Air	29-Mar-13	345,703,809
Passaredo Transportes Aereos	29-Mar-13	224,626,026
Qatar Airways	31-Mar-13	13,565,036,695

AVIATION REINSURANCE

Willis Re have published their 1st View January 2013 newsletter, in which the following information was reported:

- Within the reinsurance market, Aviation excess of loss reinsurers have been responsive to the needs of their direct writing clients; non-proportional reinsurer results have remained favourable and this continues to influence pricing with rate reductions, after risk adjustment, in the region of 5% to 10% being evident depending on base starting price and record

- Despite the on-going softening within the direct Aviation market, commission levels on a number of proportional treaty contracts have been subject to increases due to favourable performance

- Aviation retrocession pricing has remained relatively stable although again favourable experience and continuity has been rewarded, with rate improvement circa -2.5% to -5.0% being evident

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