



AIRLINE INSURANCE MARKET OVERVIEW

Fragile appears to be the best way to describe the current state of the airline insurance market. There is undoubtedly increasing resistance from the market against the size of actual or 'as if' premium reductions being targeted by broker and buyers.

At this stage this can only be considered a firming rather than a hardening of the stance of underwriters and is therefore just continuing to halt a slide in overall premium volumes. The industry rebound and therefore the level of growth in exposures is doing much to fuel the single digit premium increase as rates reductions are currently just below 5% for both hull and liabilities on a lead basis.

This period of market uncertainty is providing some airlines with the ability to provide a considered argument to underwriters regarding growth, improved loss performance or programme consolidation or separation and is allowing true differentiation to be achieved.

There are, however, examples of the lead price being less and less reflective of the overall price being paid by airlines. An aggressive target, combined with late entry to the market or perceived lack of credibility to a broking argument are being increasingly met with firm resistance from underwriters.

According to market sources the distortion in pricing for some programmes is considerable, which obviously creates challenges when looking to analyse the overall market trend. This potential for distortion in the level of verticalisation available, if there is any at all, will be having a varied impact on the level of premium change actually being incurred by airlines.

The buying strategy and market concern regarding specific additional premiums in respect of specific losses, loss AP's, is now starting to play out. Increasingly these are being eroded or removed as a part of the negotiation with some having a seismic impact on the renewal picture.

The GCC break up was the biggest news during November, the Saudia spares loss, currently the largest loss of the year, acting as a catalyst for the member airlines to go against the market trend for consolidation and seek alternatives outside a group arrangement. The majority have capitalised on the market conditions, while others have been significantly impacted and received many of the largest premium increases of the month.

The United Parcel Service (UPS) programme, which had a significant loss during its expiring policy, received nearly a doubling of the premium. This loss highlighted the challenges faced in the cargo sector, and as the industry re-equips the losses could become increasingly significant if the sector accident record doesn't improve.

Other changes on major renewals include two airlines, Air Atlanta Icelandic and Aires, both changing broker from Aon to Marsh.

If the market trend continues unchanged and is applied to the forthcoming renewals we predict a premium volume of approximately US\$1.95 billion for 2010 versus an estimated loss total of just over US\$2 billion.

2011 WILLIS AEROSPACE INTERNATIONAL AVIATION INSURANCE COURSES

The dates for the 2011 Willis Aerospace Aviation Insurance Courses have now been established. As in recent years there will be two identical courses which cover the operation of the Aerospace Insurance market and will take place in the Willis Building in London. The first will take place between April 4 and 8 and the second will take place between June 6 and 10.

Please contact your account executive regarding securing a place on either course.

HULL AND LIABILITY

2010 NET % PREMIUM AND EXPOSURE MOVEMENTS

	NO. OF RENEWALS	AFV % CHANGE	PAX % CHANGE	2009 NET PREMIUM US\$ M	2010 NET PREMIUM US\$ M	US\$ M PREMIUM CHANGE	PREMIUM % CHANGE
JANUARY	5	16.1%	-14.3%	9.4	11.2	1.9	19.9%
FEBRUARY	5	27.3%	7.9%	5.7	7.1	1.4	24.7%
MARCH	9	5.8%	-3.4%	32.2	35.9	3.8	11.7%
Q1 SUMMARY	19	10.6%	-3.9%	47.3	54.3	7.0	14.9%
APRIL	19	6.7%	13.2%	101.9	110.5	8.6	8.4%
MAY	20	11.2%	10.8%	72.9	73.2	0.3	0.4%
JUNE	15	2.0%	4.1%	40.4	49.3	8.9	22.0%
Q2 SUMMARY	54	7.5%	11.4%	215.2	232.9	17.8	8.3%
JULY	42	12.8%	14.1%	246.9	258.0	11.0	4.5%
AUGUST	5	18.4%	21.5%	20.9	21.2	0.3	1.7%
SEPTEMBER	8	38.8%	67.3%	18.9	24.0	5.1	27.2%
Q3 SUMMARY	55	14.0%	16.0%	286.7	303.2	16.5	5.8%
OCTOBER	15	7.1%	10.7%	109.4	118.1	8.6	7.9%
NOVEMBER	29	9.0%	9.7%	181.3	214.9	33.6	18.5%
Q4 SUMMARY	44	8.6%	10.1%	290.8	333.0	42.2	14.5%
2010 TOTAL	172	9.6%	11.9%	839.9	923.4	83.5	9.9%
TOP 50 TO DATE	17	7.2%	11.4%	290.5	296.7	6.2	2.1%
OCT 2009 - SEP 2010				1,707.5	1,980.7	238.8	16.0%

EXCESS THIRD PARTY WAR LIABILITY

The Excess Third Party War Liability market (AVN52) is also starting to demonstrate a firmer stance toward the level of premium reduction sought. This market has seen the overall premium volume eroded from in excess of US\$750 million to less than US\$200 million over the last nine years. It is now felt that this market has reached the minimum premium requirement for the coverage provided.

INDUSTRY NEWS

The International Air Transport Association (IATA) announced international traffic results for October showing a 10.1% year on year increase in passenger demand and a 14.4% year-on-year increase for international freight.

‘As we approach the end of 2010, growth is returning to a more normal pattern. Passenger demand is 5% above pre-crisis levels of early 2008, while freight is 1% above. Where we go from here is dependant on developments in the global economy. The U.S. is spending more to boost its economy.

Asia outside of Japan is barrelling forward with high-speed growth. And Europe is tightening its belt as its currency crisis continues. The picture going forward is anything but clear, but for the time being, the recovery seems to be strengthening.’

THE WILLIS 50

There have now been 17 renewals within the Willis 50 programmes. These programmes have received premium increases of 2% against fleet growth of 7% and passenger growth of 11%. It is worth noting that at this stage as the industry recovers at varying pace across the world that the level of percentage exposure change within Willis 50 programmes is not dissimilar to that of the rest of the industry.

The reason for the creation of the Willis 50 is to show that, as previously highlighted, the largest programmes have consistently outperformed the rest of the market. This has been the case throughout 2010 and we see no reason that this will change between now and the end of the year. The premium increase level is currently approximately a fifth of that being experienced by carriers outside the 50.

The economies of scale available to these programmes combined will likely increase the performance gap between the Willis 50 programmes and the other programmes in the market. The level of consolidation taking place among these largest programmes will further exacerbate this situation.

As we come towards the end of the year and start to think of 2011 the Willis 50 will be significantly influenced by the industry and also the insurance purchasing arrangements. There has been one member of the 50 that has ceased operations during 2010, a number that have consolidated and with the changes in the GCC programme and there will be some airline programmes entering the Willis 50 in their own right in 2011.

A summary of 2010 impact and influence and the Willis 50 for 2011 will be published in early January. Contact airline.insight@willis.com for a copy of the 2010 overview publication.

MARKET NEWS

MUNICH RE AVIATION TO TRANSFER FURTHER UNDERWRITING AUTHORITY FOR CERTAIN SMALLER AIRLINES TO BEAUFORT UNDERWRITING AGENCY WITH EFFECT FROM JANUARY 1, 2011.

With effect from January 1, 2011 Munich Re Aviation will transfer underwriting authority for freighter operations, military, governmental and presidential aircraft risks to Beaufort Underwriting Agency. For these risks the geographical scope is worldwide excluding only risks from the USA, Canada and Brazil. The threshold of a fleet value of up to US\$150 million applies.

Furthermore, all excess liability line slips emanating from the Russian Federation and Ukraine will be underwritten by Beaufort Underwriting Agency, also with effect from January 1, 2011.

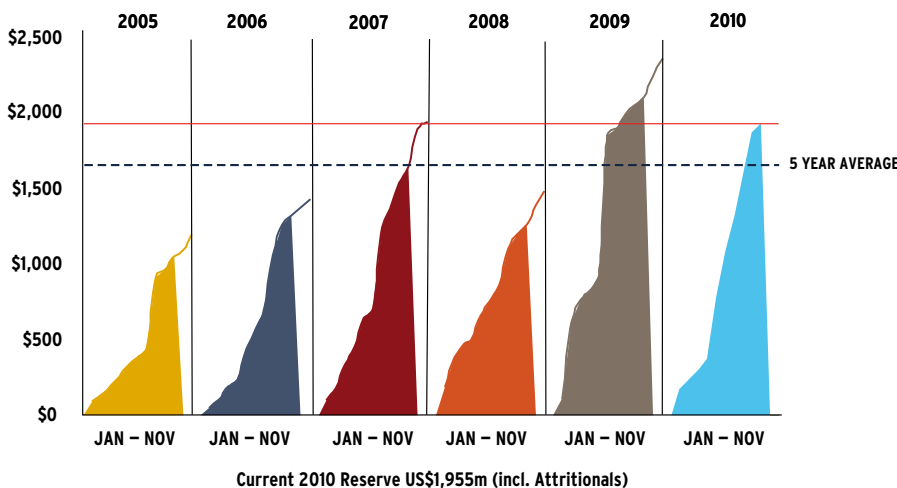
Beaufort will have complete and sole underwriting authority, and Munich Re Aviation's underwriters will no longer be involved in the underwriting of this business. Brokers are thus requested to direct relevant business to Beaufort, without including Munich Re Aviation in the placing process.

For the full press release please contact airline.insight@willis.com.

LOSSES UPDATE

The market has fortunately witnessed a rather benign few months in terms of losses and has continued to avoid a catastrophe loss. Since our last publication there have been seven further losses taking the loss total to US\$1,187 million for hull and spares and US\$353 million for liabilities, the addition of our pro rata estimate for attritional losses generates an overall loss total of US\$1,955 million. The impact on the overall loss total of the ongoing, seemingly minor incidents, such as heavily landings or engine related damage is becoming increasingly significant.

CUMULATIVE MONTHLY INCURRED RESERVE DEVELOPMENT (US\$M)



Significant losses that have occurred since our last publication are outlined below.

On October 12, a Lockheed L-100 Hercules Cargo plane operated by National Air Cargo, registration 5X-TUC, was damaged beyond repair in an accident near Kabul Airport, Afghanistan. There were eight fatalities as a result of the accident. The hull reserve for this loss is US\$6 million.

On October 30, one of the winglets of an Air France A330 aircraft, registration F-GZCH, struck the aircraft fuselage of an Air France A380 aircraft, registration F-HPJD at Paris-Charles de Gaulle International Airport. Both aircraft received damage, with the A380 apparently having substantial skin damage. The A380 was grounded for replacement of its damaged tail cone. The hull reserve for this loss is US\$3 million.

On November 2, a B737-400 operated by Lion Air, registration PK-LIQ, overshot the runway while landing at Pontianak in West Kalimantan province after a flight from Jakarta. There were 169 passengers and six crew members on board the aircraft. The hull reserve for this loss is US\$7 million.

On November 4, an A380-800 plane operated by Qantas Airways, registration VH-OQA, sustained damage after it suffered an uncontained failure of its No.2 engine shortly after take off from Singapore Changi International Airport. Fragments punctured

the underside of the left wing creating a hole in the leading edge area near the No.2 engine pylon. The aircraft returned and landed at Singapore Airport. The hull reserve for this loss is estimated to be US\$68.5 million.

On November 4, two Aklak Air aircraft, registration numbers C-GZVH and C-FKBK, were destroyed due to a hanger fire. The fire was caused by an emergency generator after a power outage. The hull reserve for this loss is US\$4.4 million.

On November 4, an ATR72 operated by Aerocaribbean, registration CU-T1549, crashed in a mountainous area near Guasimal, in the Sancti Spiritus region of Cuba, killing all 68 passengers and crew. According to reports, a distress call was made before contact with the aircraft was lost. The aircraft was operating an internal Cuban flight from Santiago Antonio Maceo Airport, to Havana. The hull reserve for this loss is US\$7 million.

On November 5, a Beech 1900 operated by JS Air, registration AP-BJD, crashed shortly after taking off from Karachi International Airport, coming down in a residential area killing all four crew and 17 passengers. According to reports the pilot had requested to return to the airport after the aircraft had suffered an engine failure. The hull reserve for this loss is US\$1.9 million.

FORTHCOMING RENEWALS

December is, without question, the most influential month of the year in terms of the number of renewals and the volume of premium generated. This impact and influence increased during 2009 and with prediction of in excess of 50 major renewals generating approaching 50% of the annual premium, this situation is expected to continue.

Even with all the renewal activity taking place, there is still one market sector that exerts significant influence on the overall result, the U.S. Majors. The North American carriers represented approaching 50% of the premium for December in 2009. The wave on consolidation that continues to sweep this sector of the industry will be of considerable interest when these carriers negotiate their renewals towards the end of the month.

MAJOR RENEWALS IN DECEMBER

AIRLINE	RENEWAL DATE	EXPIRING AFV (US\$)
CAAC	01-DEC-10	55,664,418,706
AIR FRANCE/KLM GROUP	01-DEC-10	35,470,501,098
JAPAN AIRLINES (JAL)	01-DEC-10	14,542,741,186
ALL NIPPON AIRWAYS	01-DEC-10	10,267,208,350
KOREAN AIRLINES	01-DEC-10	9,440,145,560
RYANAIR	01-DEC-10	8,987,150,981
IBERIA GROUP	01-DEC-10	8,674,928,919
THAI AIRWAYS INTERNATIONAL	01-DEC-10	7,950,120,599
JETBLUE AIRWAYS	01-DEC-10	5,300,000,000
WESTJET AIRLINES	01-DEC-10	5,034,583,803
MALAYSIA AIRLINES	01-DEC-10	4,987,271,505
ASIANA AIRLINES	01-DEC-10	4,668,312,961
AEROMEXICO	01-DEC-10	2,569,403,416
GARUDA INDONESIA	01-DEC-10	2,406,662,890
AIR TAHITI NUI	01-DEC-10	2,035,608,444
ROYAL AIR MAROC	01-DEC-10	1,469,875,094
AIR ALGERIE	01-DEC-10	1,343,660,000
TUNISIAN AIRLINE TEAM	01-DEC-10	1,299,755,923
NIPPON CARGO AIRLINES	01-DEC-10	1,125,014,067
UNITED CONTINENTAL HOLDINGS	15-DEC-10	21,726,900,000
QANTAS AIRWAYS	15-DEC-10	13,801,479,726
AIR CANADA	15-DEC-10	11,165,775,053
SOUTHWEST AIRLINES	15-DEC-10	10,969,000,000
SKYWEST	15-DEC-10	6,368,363,340
AIR NEW ZEALAND	15-DEC-10	3,388,154,106

AIRLINE	RENEWAL DATE	EXPIRING AFV (US\$)
VIETNAM AIRLINES	15-DEC-10	2,866,697,391
GLOBAL AERO LOGISTICS	15-DEC-10	1,952,219,111
PHILIPPINE AIRLINES	15-DEC-10	1,915,560,543
MESA AIRLINES	15-DEC-10	1,828,905,789
PAKISTAN INTERNATIONAL	15-DEC-10	1,576,380,447
EGYPTAIR	16-DEC-10	2,493,900,000
TAM	19-DEC-10	6,336,194,638
HAWAIIAN AIR	20-DEC-10	1,433,345,000
DELTA AIR LINES	21-DEC-10	21,204,162,820
US AIRWAYS GROUP	22-DEC-10	10,708,450,000
ROYAL JORDANIAN	22-DEC-10	1,706,681,470
EL AL	30-DEC-10	1,315,637,052
REPUBLIC AIRWAYS	31-DEC-10	7,001,496,000

The Chinese CAAC programme renews in December and is the largest programme in terms of both fleet and passenger exposure. The programme continues to demonstrate significant year on year growth, highlighting the different industry experiences taking place across the globe.

The airlines renewing this month offer a wide variety of circumstances, both significant growth and contraction, consolidation, recent losses and improvement in historical loss records.

The migration to renewal dates later and later in the year has created an unprecedented concentration of activity and premium volume. The subsequent 'no worse than average' mentality delivers the market a challenge when it comes to delivering any form of differentiation.

The concentration is now so great that it could now be perceived as providing buyers and the market with a level of activity and a pace of change that is increasingly unmanageable. As airlines, brokers and insurers go through the process of assessing each airline in its peer group, 'run it through their model' and deliver or respond to the argument of why each airline is better than average the challenge is to do each programme justice.

With few currently looking to break free from this market created situation it is likely to be approaching another year before any change in market conditions can be brought to bear in terms of significant premium changes.

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This newsletter offers a general overview of its subject matter. It does not necessarily address every aspect of its subject or every product available in the market. It is not intended to be, and should not be, used to replace specific advice relating to individual situations and we do not offer, and this should not be seen as, legal, accounting or tax advice. If you intend to take any action or make any decision on the basis of the content of this publication you should first seek specific advice from an appropriate professional. Some of the information in this publication may be compiled from third party sources we consider to be reliable, however we do not guarantee and are not responsible for the accuracy of such. The views expressed are not necessarily those of the Willis Group. Copyright Willis Limited 2010. All rights reserved.

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