



JLT RISK SOLUTIONS Limited



PLANE TALKING

JANUARY FEBRUARY 2006

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2006 - No Surprises So Far

Despite apparent attempts by market pundits to talk up a hard market over the last six months, conditions look set to remain static in the aviation sector in the current loss-free environment. It will be some months before we have the opportunity to make any firm comments as to how we feel the year will pan out. At this juncture however, we would envisage an overall continued gentle decline in rates. This, of course, is largely dependent on a continued favourable loss scenario; a factor that could easily be reversed.

The more predictable aspect is the level of expansion and growth of the airline

passenger and freight markets, both of which are forecast to be significant in the majority of regions, except the USA. This should result in overall insurance rate reductions, albeit accounts will be assessed very much on an individual basis. Therefore, all being well, the overall impact should result in a similar level of premium income being generated as last year.

Capacity at one point seemed to be a factor which could influence premium rating. With significant new players coming to the market, these have essentially replaced those insurers who have, for the time being, opted to lie dormant. The situation is relatively stable and therefore the danger of a shortage of capacity driving up rates has for the moment receded.

Editorial

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January Renewals

In January there are five airlines of varying size renewing overall. This is down on last year due to the bankruptcy and subsequent liquidation of Independence Air, which was one of the largest airlines in the month by way of fleet value. Our own compilation only includes one airline of significant size and, although fleet value and passenger growth continues the trend set throughout last year, one airline's renewal statistics must be regarded as inconclusive with regard to prospective market trends. Suffice to say, overall premiums for January remained very close to that of last year.

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February Renewals

Just two airlines feature this month, continuing the scarcity of airline underwriting activity in the market. Mytravel, the inclusive tour charter operator based in Manchester is the largest with a fleet of 14 jets valued at over US\$1.5 billion. The only other airline of note is Tarom the national flag carrier of Romania. This has moved its renewal date from October and changed broker from Marsh to Alexander Forbes.

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Loss Analysis

January Losses

The market enjoyed a benign start to the year with the usual assortment of incidents that in most cases failed to breach the appropriate level of insured retention. There were 2 losses in the Congo to small Russian cargo equipment that seemed to be a feature so many times last year.

Although our estimation for hull claims comes to US\$7.35 million plus liability reserves of approximately US\$4 million, one other incident that does not feature in our figures is worth mentioning. On the 9th January an F16 fighter belonging to the manufacturer Lockheed Martin crashed while practising for an air show in Oman. The aircraft was insured under the manufacturers policy in London and valued at US\$35 million. This substantial loss will not feature in the usual categories that we produce but will nonetheless contribute rather insidiously to the overall loss figures.

Airline accidents that do contribute to our statistics include:

On the 2nd an AN26 belonging to Ruwenzori Airways crashed into a swamp prior to landing at Bunia in the Congo with a cargo of cigarettes. The crew managed to escape from the remains of the aircraft which was valued at approx US\$250,000.

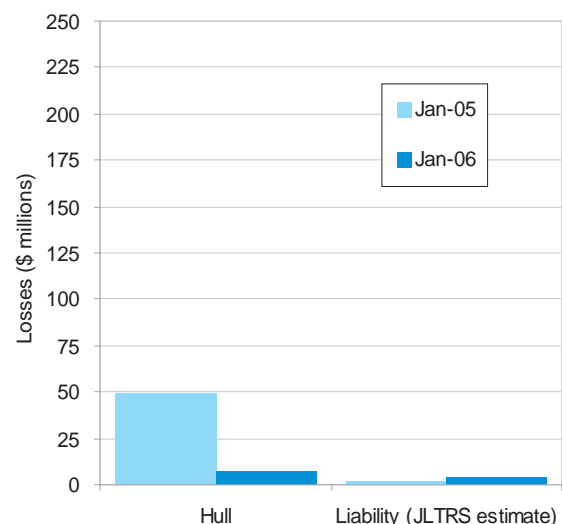
A Nature Air Twin Otter was severely damaged on the 10th when it suffered an aborted take off from Puerto Jimenez in Costa Rica. Cost of repairs are estimated at US\$850,000.

One crewmember and two passengers were killed and five passengers injured on the 22nd when a Sonic Blue Airways Cessna Caravan reg CGRXZ suffered engine failure and crashed near Port Albernie, British Columbia. The aircraft was insured for US\$1 million.

Another accident took place in the Congo on the 24th when an AN12 reg 9QCER belonging to Aerolift Airlines made a hard touchdown at Mbuji Maya causing both wings to collapse. A fire developed rendering the aircraft a Total Loss. The estimated value of the aircraft was US\$250,000.

A Boeing 747-400 freighter reg LX-TCV belonging to Cargolux had nose landing gear collapse while being moved at Shanghai on the 25th. There was additional damage to the fuselage resulting in an estimated cost of repairs of US\$5 million.

January Major Airline Losses



Source:
JLTRS
database

Insurance Industry News

Capacity Update

While we have commented that some prominent insurers have opted to withdraw their support from the aviation market we have also witnessed a number of new entrants.

The "loss of capacity" for airlines was due to certain underwriters refusing to write reductions in rates with a resultant drop in renewal premium. The most notable market is Axis (post Katrina) but other Lloyd's syndicates took the same view at times during the year. The capacity is not lost, as such, but is dependent on market conditions.

One of the largest new entrants is Berkley Aviation in Santa Barbara, California. To expand on their intentions they have announced their scope which will be offered on a worldwide basis, focussing on general and specialty aviation risks in the following classes of business:

- Airline Carriers - Aircraft Hull and Liability
- Non-owned Aircraft Liability
- Fixed Base Operations
- Aircraft Leasing - Contingent and Possessed coverage
- Airports - major international airports and small private operations
- Helicopters - Aircraft Hull and Liability

At present the new operation has indicated that it will be offering a line of between 5 and 15% but it is unclear where this capacity will be allocated. They are currently writing US Domestic business and not yet writing worldwide although this should be forthcoming.

Berkley Aviation offers both admitted and non-admitted paper through StarNet Insurance Company and Gemini Insurance Company. Both companies are rated "A XIV" by AM Best and "A+" by Standard & Poor's.

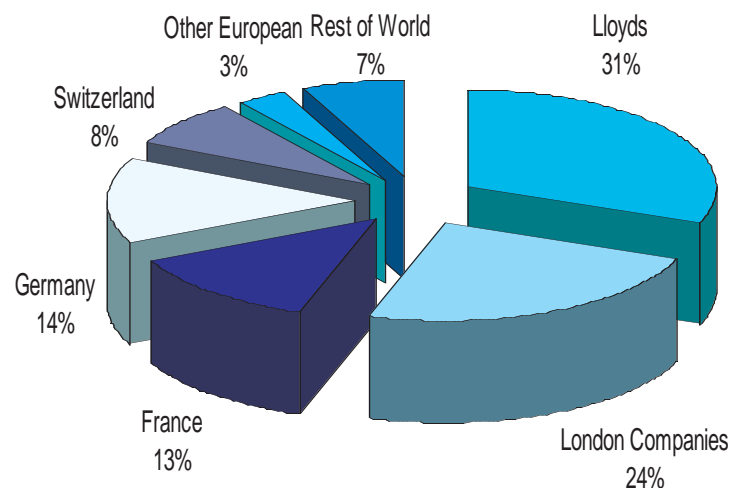
Inter Aero is another new operation that will be writing from the USA using Arch (USA) paper. They have indicated that they can write up to US\$150m but we are awaiting a date for commencement of the new operation and the scope of their offering. Again it is unclear as to where this level of capacity will be applied.

Standard & Poor's ratings for Arch Excess & Surplus Insurance Company in the USA, Arch Insurance Company in the USA, Arch Reinsurance Company in the USA, Arch Reinsurance Ltd in Bermuda and Arch Specialty Insurance Company in the USA are "A -".

Samsung and Qatar are two new operations to enter the aviation market. Qatar has indicated that it will offer a line of 1.3% on airline all risks (on the basis of a combined single limit of US\$1.5bn) and Samsung have not yet confirmed their line.

In addition a number of the larger insurers have indicated their intentions to offer increased capacity, although in reality we will have to see how the year unfolds as to the level of rates and how much the individual insurers will be prepared to offer. This brings maximum worldwide airline capacity to some 175% on the basis of a combined single limit of US\$1.5bn. However it must be noted that insurers will not necessarily offer their maximum line on every piece of business, with a substantial level of discrepancy being applied to each and every individual case. This overall maximum represents an increase of some 20% over last year's capacity and this figure does not include the latest entrants.

The breakdown equates to Lloyd's line of 54%, London Companies 42% and World Companies, 79%.



A new operation by the name of Lancashire in Bermuda, headed up by Richard Brindle, ex. Lloyd's underwriter, is offering a significant line for Excess AVN52 Risks. The line of around US\$150m will add to the already ample capacity for this market and gives greater options to clients when it comes to negotiating rates.

Lloyd's 2006 Capacity

Lloyd's capacity for 2006 has increased to £14.8bn up from £13.7bn in 2005. It was previously projected to reduce by 7% but following one of the worst hurricane seasons in history this has been reversed as the market outlook has changed from a soft market to a slightly hardening market (although not in all sectors).

Lloyd's rating had been placed on Credit Watch Negative by Standard & Poor's (S&P) in the aftermath of the hurricanes, however this status has been reviewed and ratings from S&P are affirmed and A / Stable and remain at A / stable from AM Best and Fitch.

The top 15 Lloyd's Syndicates for 2006 are as follows:

Syndicate	Managing Agent	Capacity (£)
2001	Amlin	1,000,000,000
4472	Liberty	912,000,000
33	Hiscox	832,968,324
2020	Wellington	799,966,529
2999	Limit	660,000,000
2623	Beazley	646,882,003
510	Kiln	625,187,134
1414	Ascot	550,000,000
2987	Brit	500,000,000
1084	Chaucer	450,000,000
2003	Catlin	450,000,000
218	Equity	400,732,035
2791	Managing Agency Partners	399,961,711
2488	Ace	350,000,000
386	Limit	339,877,479

Space Capacity on the Rise

Liberty Syndicates at Lloyd's, part of Liberty Mutual have announced their increased participation in the space insurance sector, offering a line of US\$250m as reported by Airclaims. Previously Liberty offered a much smaller share of capacity and this could have a significant impact on space insurance rates. This new line dwarfs its competitors lines by about 10 times which illustrates the limited size of the market previously. This marks a response to four years of favourable loss ratios in the space insurance sector and Liberty have indicated that they feel a need to accommodate those 'good' insureds that have had to suffer severe restrictions and reductions in coverage over the last five years which could have been considered as a 'knee jerk reaction' to the huge adverse

financial impact of satellite anomalies that surfaced during the boom years of the late 1990's and resulted in a surge in rates. These factors have led to a number of clients opting for self insurance in the last couple of years and this move could be construed as Liberty Syndicates inviting these 'good' operators back into the market.

Sirius Celebrates First Year

Sirius International Aviation & Space Zurich Branch office has celebrated its first annual anniversary. The operation started up on the first of February 2005 and the team has since increased in number from the initial two members to seven. Sirius is now an established Aviation player writing a comprehensive book of business.

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Arrivals and Departures

As reported overleaf Richard Brindle, ex. Lloyd's underwriter has set up a new operation in Bermuda by the name of Lancashire to underwrite Excess AVN52 Risks.

In a surprise move, Derek Webb is leaving Willis after many years with the company. He is to commence a new role, co-ordinating the US portfolio at XL London Markets.

Chris O'Gwen has announced his resignation from USAIG to head up the new XL operation in New York.

Eddie Dawson has left Marsh to join Aon to work on the Aerospace account.

Stuart Pearce has moved from HSBC to Liberty Mutual to assume the position of General Aviation Underwriter.

Trevor Light has joined GAB Robins Aviation in London as a Director.

Bill Isakson has also been appointed Manager for GAB Robins Aviation in their Fort Lauderdale Office.

New CEO at AIG

American International Group, Inc. (AIG) has announced that David M. Hupp has been named President and Chief Executive Officer of AIG Aviation, Inc. (AIG Aviation), a wholly owned subsidiary of AIG.

Mr. Hupp will be responsible for day-to-day operations of AIG Aviation, headquartered in Atlanta, with operations in five additional U.S. cities and an international operation based in London. He will report to AIG Executive Vice President Kristian P. Moor. Mr Hupp who has been with AIG in a number of different capacities since 1970 succeeds Steven G. Blakey, who has left the company.

In addition, Martin C. Stevens has been named AIG Aviation's Chief Underwriting Officer. Mr. Stevens who has been with AIG since 1979 and has managed AIG's international airline, aerospace and general aviation business in London since 1987, will continue to be based in London.

Mr. Moor said, "The appointments of David Hupp and Martin Stevens underscore AIG's unsurpassed aviation underwriting strength and our unwavering commitment to the global aviation market."

AIAA Developments

Following his departure from AIG, Steve Blakey has assumed the position of President and CEO of AIAA which handles the aviation business within CV Starr & Co. Inc. We will report further when we have more details of this operation as to their intentions and the scope of coverage they will be offering.

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Airline Industry News

The seemingly endless demand for aircraft in 2005 finally left the combined order books at Airbus and Boeing at 2057 units, the highest since 1989 when 1631 orders were placed. In a display that will benefit Boeing by US\$11 billion, Air India put their name to an ultimate order for 68 aircraft at the end of December that include 50 777's and 787's plus 18 737's.

It now seems apparent that the versatility and economics of Boeing's two large twins is not only proving more attractive to many than the current offerings from Airbus, but also usurping the monopoly for large long distance transports once held by its own 747. Because of the sustainable reliability of modern jet engines both airlines and their passengers now seem quite confident in flying huge distances, often over water, on just two engines.

Could it be that Boeing have made a smart move by sewing up the market with the 787 in the 200 to 300 seat sector and up to 375 seats and beyond (440 in some cases) with the 777? Air India's chairman said it is a question of "positive economics" where fuel prices play a much larger part of airline budgets today than ever before. As a 747 replacement, the longer range 777-300ER is ideal providing similar capacity but with twin-engine economics. As an example, Singapore Airlines says it will gradually decommission its 747-400 passenger fleet and convert many into freighters as it takes delivery of new B777-300ER's and A380's. "to progressively replace the 747-400 as the high capacity long-range aircraft in our fleet". We shall have to wait and see if anyone orders the passenger version of the new 747-8. With the exception of the A380, which will show its true economical potential by year-end, the four engine archetypal large passenger commercial aircraft might soon be showing signs of possible extinction.

Boeing reached a milestone recently with the delivery of the 5,000th 737, thus becoming the best selling commercial jet in the history of aviation. Total orders now exceed 6,100 that span a production period of over five

decades. It is estimated that more than 12 billion passengers have flown on the various marks since it entered service in 1968 and thus accumulated over 120 billion kilometres. The latest derivative - the 900ER - is the 12th major passenger variant since the programme kicked off in 1965 with an order from Lufthansa for 22 of the 100 seat 100 series. Today Boeing are offering the longest range aircraft in the series, a 700ER which All Nippon Airways will operate on a 5,500 mile sector making it the longest range 737 ever offered.

Although IATA are forecasting traffic growth of about 4.5% for 2006 much depends on not only continued global stability but the cost of oil. Their estimation is that the price per barrel will stabilise at around US\$53. Analysts suggest a boom in traffic last year helped revenues grow by almost 10% as the industry reached the peak of the cycle. As the downward trend begins revenues will slide back to grow at about 4% this year and that could translate into an overall loss for the airline market of US\$4 billion. IATA anticipates a return to profitability for the industry in 2007 but considers that this will be short lived and profits may well peak in 2008 before heading down again.

End to United's 3 Year Limbo

After sheltering under the protection of Chapter 11 for over three years, United Airlines emerged on the 1st February after the longest stay in bankruptcy protection the industry has ever known. Compared with December 2002 the company has 20,000 fewer employees, 100 fewer full sized jets, US\$8 billion less in debt, and its annual costs have fallen by US\$7 billion. On top of this and perhaps its biggest burden, the pension plan has gone. In exchange for the government's Pension Benefit Guarantee Corp taking on the liability, it acquired a 20% stake in the new company, an asset it is now trying to sell.

Hawaii's Aloha Airlines has also exited Chapter 11 this month after 14 months, with exit financing of US\$63m in equity and US\$35m in debt financing from new investors.

Jet Airways Acquires Air Sahara

India's Jet Airways is to buy Air Sahara in a deal worth US\$500m which will see the combined entity holding a 35% share of the (currently booming) Indian domestic airline market. These two more established players are however up against some stiff competition as we are witnessing new low cost carriers (LCC's) entering the arena by the day.

All considered these LCC's are very much creating a whole new market of airline passengers that are being wrested from the rail travel sector with prices that compare extremely favourably. The domestic airline passenger market is said to have expanded in a year to 2006 from 18m to 24m and the overall aviation sector, both cargo and passenger is considered to be expanding at an annual rate of 25%. Only this month SpiceJet, which commenced operations in May last year, has ordered 10 Boeing 737s with options for 10 more. The legacy carrier Air India has gained government approval to purchase 68 Boeing aircraft for some US\$7.88bn and Indian Airlines is finalising an Airbus deal for 43 aircraft worth US\$2.25bn. Both are particularly motivated by the need to keep up with the latest competition.

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Space News

As we go to press we have received news that the Russian Proton launcher failed at launch on 28th February. It appears that the Breeze M upper stage shut down early during firing and the Arabsat 4A satellite it was carrying, was therefore released somewhere well short of its intended orbit. At this point it is unclear where the satellite is and it is considered unlikely that it will have enough on board propellant to reposition itself to a useful orbit. The satellite was insured in the market for a reported figure of US\$179m.

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And finally...

Everybody in the world of aviation was saddened to record the passing of the legendary Sir Freddie Laker who so single-mindedly changed the face of air travel over his long career in the industry.

Of the many obituaries to him, one would surely have brought a smile to his face:

'Sir Freddie Laker may be at peace with his maker, but he is *persona non grata* with IATA.'

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Launch Log

JANUARY LAUNCHES

19th January

Site: Cape Canaveral
Launcher: Atlas 5/551
Payload: Pluto New Horizons

24th January

Site: Tanegashima
Launcher: H-2A/2022
Payload: Daichi (ALOS-1)

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