



AIRLINE INSURANCE MARKET OVERVIEW

Before long the combination of significant excess capacity and low loss levels had to see the level of premium increases being achieved by insurers start to fall. It took the increased number, size and diversity of the April renewals to reflect the change that has undoubtedly taken place in the airline insurance market.

April had more renewals and generated more premium than the whole of the first quarter combined. The level of premium increase for the month dropped to below 10%, less than half that of 2009 and less than two thirds that of the first quarter. This trend continued with the May renewals with premium increases slowing further to just over 7%.

The April and May renewals have therefore offered the clearest indication thus far of the market direction for the rest of the year. The market conditions are going to benefit the airline insurance buyer.

It is interesting to note the clear distinction between the largest Willis 50 carriers and the majority of the market programmes at this time. The eight Willis 50 programmes that have renewed thus far have demonstrated similar exposure changes to the market overall but have secured a premium increase that is 30% lower than the average experienced of the market as a whole. The market desire for these larger programmes and premium volumes continues to deliver economies of scale.

Good news for the airline industry is the undoubted signs of recovery after the economic downturn, with fleet value and passenger exposures starting to increase once more. It is therefore a question of how much of this increased exposure can be negotiated for no increase in premium.

The major renewal in April was the British Airways centred group programme which exhibited a reduced average fleet value. The programme however delivered a single digit percentage increase in passenger numbers.

Hainan Airlines was the second largest programme by average fleet value to renew during April. The Chinese carrier highlights the level of development still taking place in the Chinese airline industry with a 22% increase fleet value, 29% increase in passengers and a 34% increase in departures.

The parallel placement of the Virgin Group of Airlines including Atlantic, Blue and America is collectively the largest programme to renew during May. This group now excludes the former Virgin Nigeria operation renamed Nigerian Eagle which renews in August.

There have also been some broker and leader changes with Aerolineas Argentinas changing broker from Marsh to Willis, Porter Airlines changing broker from Marsh to JLT, Royal Brunei Airlines moving broker to Aon from Marsh and Transaero changing leader from Global Aerospace to Allianz.

With the recent renewals being negotiated in a benign loss environment, capacity levels remaining high and increasing signs of this capacity, being more regularly deployed and stretching vertical differentials, it remains to be seen to what extent the recent deterioration in loss experience influences the market direction.

HULL AND LIABILITY

Q4 2009 AND 2010 NET % PREMIUM AND EXPOSURE MOVEMENTS

2009	NO. OF RENEWALS	AFV % CHANGE	PAX % CHANGE	2008 NET PREMIUM US\$M	2009 NET PREMIUM US\$M	US\$M PREMIUM CHANGE	PREMIUM % CHANGE
OCTOBER	20	18.5%	3.4%	102.4	136.5	34.2	33.4%
NOVEMBER	23	-0.1%	-6.9%	276.6	316.4	39.8	14.4%
DECEMBER	65	3.3%	1.7%	775.9	932.3	156.4	20.2%
Q4 SUMMARY	108	2.5%	0.2%	1,154.9	1,385.2	230.3	19.9%

2010	NO. OF RENEWALS	AFV % CHANGE	PAX % CHANGE	2009 NET PREMIUM US\$M	2010 NET PREMIUM US\$M	US\$M PREMIUM CHANGE	PREMIUM % CHANGE
JANUARY	4	19.1%	-14.3%	8.6	10.5	1.9	22.7%
FEBRUARY	5	27.7%	7.9%	5.7	7.2	1.4	25.2%
MARCH	9	5.8%	-3.4%	32.2	35.9	3.8	11.7%
Q1 SUMMARY	18	11.0%	-3.9%	46.5	53.6	7.1	15.4%
APRIL	18	6.3%	12.9%	100.0	109.6	9.6	9.6%
MAY	16	11.2%	12.6%	60.2	64.5	4.3	7.1%
Q2 SUMMARY	34	8.0%	12.8%	160.2	174.2	13.9	8.7%
2010 TOTAL	52	8.2%	11.2%	206.7	227.8	21.1	10.2%
TOP 50 TO DATE	8	7.5%	12.9%	107.0	114.6	7.6	7.1%
OCTOBER 1, 2009 - 2010 TO DATE				1,361.6	1,613.0	237.5	18.5%

AVIATION REINSURANCE MARKET OVERVIEW

April was a significant renewal period in the aviation reinsurance market and delivered a greater degree of rating stability. More modest degree of pricing adjustment were applied to loss-affected layers on an account specific basis, dependent upon loss record, layer attachment and changes to underlying exposure profile.

MARKET NEWS

ALTERRA CAPITAL HOLDINGS

On May 12 Alterra Capital Holdings Limited announced the completion of a merger between Max Capital Group Ltd. and Harbor Point Limited to form Alterra.

ORTAC

Ortac Underwriting Agency recommenced underwriting in early May. Amlin, via their Lloyd's Syndicate, are the new underwriting partner. Amlin's Lloyd's Syndicate 2001 will provide 100% of Ortac's stamp capacity and will target a broad 'General Aviation' class. Ortac Underwriting Agency will continue to operate from its historical base in Guernsey.

TORUS

On May 4 Torus announced the acquisition of Glacier Insurance AG, a subsidiary of the Glacier Group. As part of the acquisition Glacier Insurance AG's underwriting and operational staff will join Torus and all its branch offices will be retained. Richard Etridge, Chief Executive of Glacier Insurance, will join the Torus management team, becoming Chief Operating Officer for Continental Europe as well as Global Head of Aviation.

MARKET MOVERS

It was announced on June 2 that Paul Maguire has been appointed as Head of Aviation at Faraday. Paul will take up his new position as soon as he has completed his contractual obligations at Aspen.

It has been announced that with effect from July 1, John Green is stepping down and being replaced by Malcolm Brett as Aviation Director and Product line head. John will remain at ACE, working 150 days a year for a period of time to assist the transition.

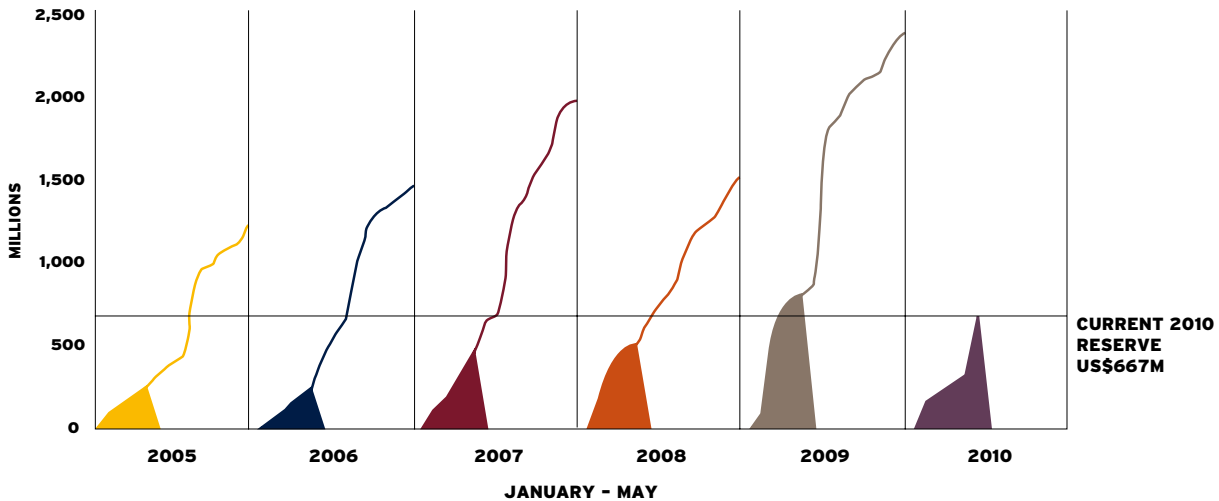
Ferdinando Martino joined Allianz Global Corporate and Specialty management Team as of May 1. Ferdinando will assume the role of Global Product Leader for Major Risks, i.e., Airlines, Manufacturers and large Airports. He will reside in Zurich but will travel extensively between Allianz offices in Munich, London, Paris and New York.

Gates and Partners, the specialist aerospace law firm, announced that Simon Balls, Rob Ireland and Alexandra Rodina will be joining the firm in the aerospace group as partners as soon as their contractual obligations to Clyde & Co have been completed.

LOSSES UPDATE

The past two months have seen a deterioration in the 2010 market loss picture. The recent losses, when including liability reserves, are anticipated to put the loss total at a similar level to the same point last year. After one of the best starts to the year it is clear that the market experience can change swiftly either through the loss of high valued hulls or fatalities. The hull loss total currently stands at US\$296 million and liabilities US\$183 million (excluding outstanding liability reserves). With the addition of the pro rata of our annual attritional estimate the loss total to date is US\$667 million.

CUMULATIVE MONTHLY INCURRED RESERVE DEVELOPMENT (US\$)



The table below compares the experience of the first five months of the year for the past five years. This snapshot of market experience highlights both the lack of connectivity between the frequency and severity of losses along with the comparatively poor passenger fatality experience of 2010.

YEAR	LOSSES EXCESS OF \$100M	LOSSES BETWEEN \$10M - \$99M	FATALITIES
2010	2	2	357
2009	2	7	59
2008	1	5	49
2007	2	5	237
2006	0	8	113

Significant losses that have occurred in the past two months are outlined below.

On April 13, a Merpati Nusantara Airlines B737-300, registration PK-MDE, sustained substantial damage and was declared a total loss when it overran the runway on landing in poor weather at Rendani Airport, Indonesia. The aircraft, which was operating a domestic flight from Sorong, came to rest 200 metres past the end of the runway. There were 10 serious injuries reported amongst the 103 passengers and seven crew.

Also on April 13, an Aerounion A300- B4-200F, registration XA-TUE, was destroyed when it reportedly undershot the runway on landing at General Mariano Escobedo International Airport, Monterrey, Mexico. The aircraft struck a car killing the driver just outside the airport boundary. The aircraft was operating a cargo flight from Mexico City.

On April 17, a Canadair CRJ of SA Express, registration ZS-NMM, sustained damage when the aircraft's nose undercarriage failed to extend on landing at Eros International Airport, Windhoek, Namibia following a flight from Cape Town. There were no serious injuries reported amongst the 33 passengers and four crew.

On May 5, a SATENA Embraer ERJ-145LR, registration HK-4536, sustained substantial damage and was declared a total loss when it overran the runway on landing in poor weather at Fabio A Leon Bentley Airport, Mitu, Colombia. The aircraft came to rest with its undercarriage collapsed on soft ground after crossing a road following a domestic flight from Villavicencio. There were no serious injuries reported amongst the 37 passengers and four crew.

On May 12, an Afriqiyah Airways A330-200, registration 5A-ONG, was destroyed when according to reports it undershot the runway on landing at Tripoli International Airport following a flight from South Africa. There was a single survivor among the 93 passengers and 11 crew.

On May 22, an Air India Express B737-800, registration VT-AXV, was destroyed when it overran the runway on landing at Bajpe Airport, Mangalore, India. The aircraft came to rest in the gully of a steep valley at the end of the runway after crossing the airports runway safety zone. The runway was reported to be 'wet' at the time of the accident. Reportedly there were eight survivors amongst the 160 passengers and six crew.

On May 23, a Canadair CRJ of SkyWest Airlines, registration N925SW, sustained damage when the aircraft's nose undercarriage failed to extend on landing at Ontario International Airport, Ontario, California following a flight from San Francisco. There were no serious injuries reported amongst the 24 passengers and three crew.

JUNE RENEWALS

AIRLINE	RENEWAL DATE	EXPIRING AFV US\$M
EVA AIR	01-JUN	4,112
JORDAN AVIATION	01-JUN	170
WIND JET	04-JUN	330
BULGARIA AIR	06-JUN	381
VIM AVIA	10-JUN	198
BELLE AIR	10-JUN	105
AUDELI	13-JUN	180
UZBEKISTAN AIRWAYS	15-JUN	512
EUROATLANTIC AIRWAYS	17-JUN	286
STRATEGIC AVIATION	18-JUN	119
ARMAVIA	21-JUN	188
KINGFISHER AIRLINES	24-JUN	3,012
CANJET	30-JUN	308

June sees only small number of significant renewals taking place with Eva Airways of Taiwan and Kingfisher Airlines of India being the largest two. One major renewal that will not be taking place is Aegean Airlines which cancelled and replaced its policy in May.

The market will therefore undoubtedly have an eye focused on the July renewals. Many of these programmes will be looking for some element of corrective action following the 'knee jerk' reaction of the market post the Air France loss in 2009. The extent to which any realignment can be provided against last year in addition to an accurate prediction of ongoing market sentiment will represent a challenge.

As we look even further ahead the picture of consolidation continues to take shape. The news of the merger between Continental Airlines and United Airlines in the U.S. to create the largest airline in the world will undoubtedly have significant ramifications on the airline insurance purchasing arrangements of these airlines. With renewal activity concentrated into the final quarter and particularly the last few weeks of the year there is considerable time for the Continental and United merger to take shape and transition through to their insurance arrangements.

The airline industry merger and consolidation ball is now well and truly rolling and there is no clear indication of what is going to stop it. The real effects of the economic downturn are now being felt by the airlines and there are, as evidenced by the Willis 50, economies of scale available in insurance purchasing. With insurers looking to deploy their capacity in an increasingly competitive market environment it is likely that without significant losses, the consolidation savings through insurance buying might be larger than first anticipated.

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