

AIRLINE RENEWALS

The airline insurance market continues to be finely balanced. There is much talk of a change of direction which is not yet really being reflected in our lead premium analysis. The vertical market is experiencing signs of firming and as a result the experience for each buyer is potentially significantly different. A divide is appearing between the opinion of the lead and following markets around where premiums should be and as a result there is an element of uncertainty around individual renewal treatment.

In terms of the number of renewals and premium income June is the quietest month in the second quarter of the year. Of the eleven renewals only two have an Average Fleet Value (AFV) in excess of US\$2 billion, being Eva Air of Taiwan and Kingfisher Airlines the fast growing Indian carrier. Kingfisher, which will renew in June for the first time, is a further sign of the consolidation taking place in the industry and insurance market programmes as it will also include Air Deccan, which was recently purchased by Kingfisher.

Thus far June has generated US\$33 million in premium, a reduction of 1%. This is the first month in 2008 that has seen a premium reduction. The low level of fleet growth at 6% and passenger numbers showing an increase of 3%, is likely to be a sign of things to come as the effect of the industry downturn and recently announced capacity reductions by many of the world's major carriers start to have an effect on exposures.

With underwriters relying on significant growth levels for premium uplift, this reduction in exposures will have an effect on premium levels as the year progresses. This could result in rate reductions lessening as, in the main, reductions have been achieved where airlines have been declaring growth. It is likely, by the time the 2007

year of account renewals are adjusted, that gross premium income will be much less than the US\$1,830 million we have previously estimated, which will only further increase the pressure on insurers to cease giving rate reductions.

The total premium generated in 2008 is US\$232 million, an increase of 8%, or just US\$17 million of additional premium which is more than offset on an annual basis by industry insolvencies and consolidation. This has continued in the past month with Silverjet ceasing operations and Edelweiss Air which is being acquired by Swiss, and included within the Lufthansa programme. These factors have removed over US\$31 million of premium from the market. The downturn in exposures, combined with consolidation and insolvency is the biggest challenge faced by the market. Underwriters already deem the premium base inadequate to meet annual loss totals, excluding a catastrophe. Should this be eroded further by the industry economics the losses of the few will be paid by a decreasing many.

Premium generated since October 2007, which marks the start of the '2007 renewal cycle', totals US\$1,333 million, a reduction of US\$99 million in premium or 7%.

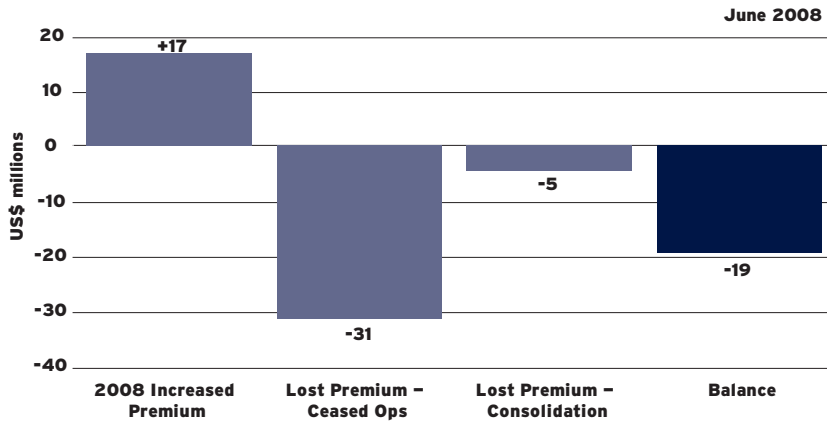


HULL & LIABILITY

GROSS 4TH QUARTER 2007 & 2008 % PREMIUM MOVEMENTS

2007	NO. OF RENEWALS	AFV % CHANGE	PAX % CHANGE	2006 PREMIUM US\$M	2007 PREMIUM US\$M	US\$M PREMIUM CHANGE	PREMIUM % CHANGE
OCTOBER	13	13.1%	13.2%	57.9	53.2	-4.8	-8.2%
NOVEMBER	21	14.0%	14.2%	331.4	303.5	-27.9	-8.4%
DECEMBER	50	5.4%	7.1%	827.4	744.7	82.7	-10.0%
Q4 SUMMARY		8.0%	9.1%	1,216.7	1,101.4	-115.3	-9.5%
2008	NO. OF RENEWALS	AFV % CHANGE	PAX % CHANGE	2007 PREMIUM US\$M	2008 PREMIUM US\$M	US\$M PREMIUM CHANGE	PREMIUM % CHANGE
JANUARY	3	41.6%	69.3%	3.7	4.8	1.1	29.5%
FEBRUARY	4	26.8%	25.8%	5.0	5.7	0.7	14.1%
MARCH	5	11.0%	1.4%	25.3	26.1	0.8	3.1%
Q1 SUMMARY		17.5%	3.0%	34.0	36.6	2.6	7.6%
APRIL	18	22.6%	16.8%	98.0	107.6	9.5	9.7%
MAY	13	12.4%	20.3%	48.9	54.0	5.1	10.5%
JUNE (TO DATE)	8	5.5%	3.3%	33.8	33.3	-0.5	-1.4%
Q2 SUMMARY		18.0%	16.1%	180.7	194.9	14.2	7.9%
2008 TO DATE	51			214.7	231.5	16.8	7.8%
OCT 07 - JUNE 2008 (TO DATE)	135			1,431.4	1,332.9	-98.5	-6.9%

GROSS 2008 HULL & LIABILITY PREMIUM BALANCE



LOSSES UPDATE

The current loss figure for 2008 is US\$692 million which is made up of US\$332 million hull, US\$147 million liabilities and a pro rata figure of US\$213 million in respect of attritional losses. This figure does not include reserves from some recent losses that are still to be confirmed and will therefore add to this total. This total is US\$28 million worse than at the same point in 2007, which then went on to become the worst year in terms of the monetary value of losses since 2001.

Recent incidents that may result in significant reserves are detailed below.

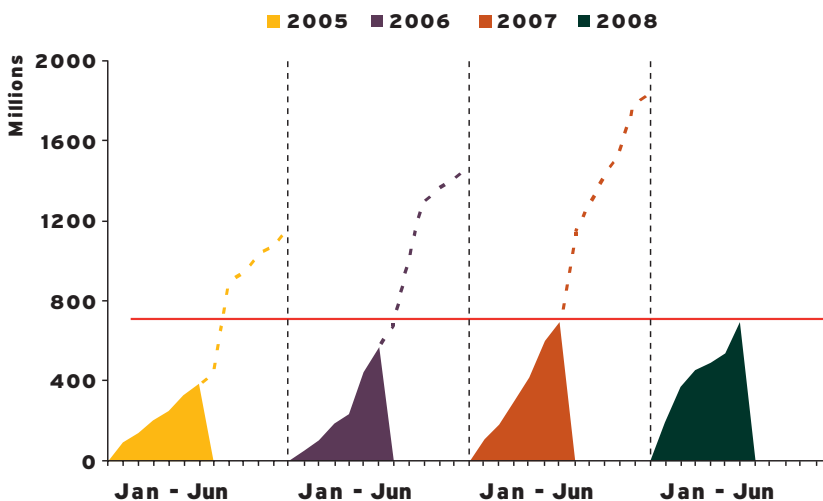
On May 30, a TACA Airbus A320, registration EI-TAF, overran on landing at Tegucigalpa-Toncontin Airport, Honduras before breaching the airport boundary and colliding with vehicles. Of the 124 passengers and 11 crew (including five off duty) onboard, two passengers and one crew member were killed. In addition there were also two third party fatalities following collisions caused by the aircraft crossing a busy highway.

On June 10, Sudan Airways Airbus A310-300, registration ST-ATN veered off the runway after landing at Khartoum International Airport, Sudan before bursting into flames. Of the 214 passengers and crew onboard there was 29 passenger fatalities and one crew fatality.

Also on June 10, an Air France Airbus A320, registration F-GKXF suffered a nose-gear collapse whilst under tow at Paris Charles de Gaulle International Airport, France. The nose-gear collapsed causing the aircraft's nose to impact the roof of the tug causing damage to the aircraft's underside.

On June 18, a Boeing 737-200Adv, registration ZS-OKD, operated by Comair (part of British Airways programme), skidded off the left side of the runway following a landing in rainy conditions at Durban International Airport, South Africa. The aircraft came to rest partially on the grass with its left main gear embedded in the earth and left engine contacting the ground. None of the 87 passengers and six crew onboard sustained serious injury.

CUMULATIVE MONTHLY INCURRED RESERVE DEVELOPMENT (USD)

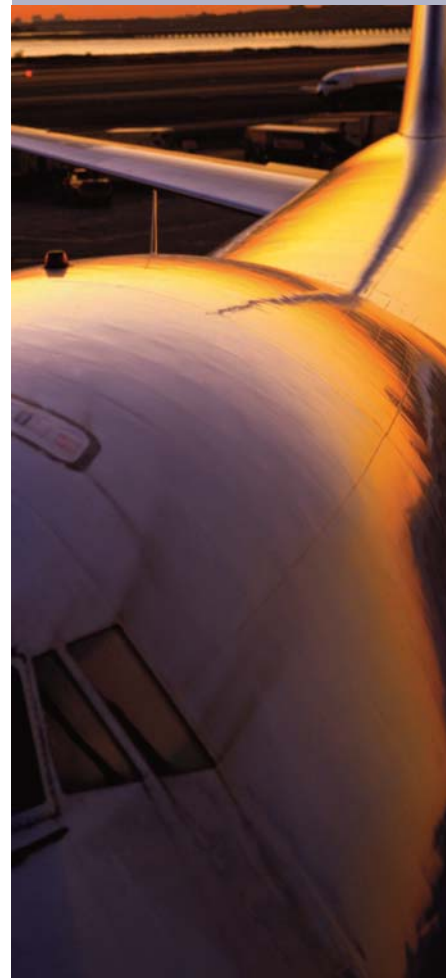


CRISIS AGAIN, DEEP LOSSES PROJECTED

This month the International Air Transport Association (IATA) held the Association's 64th Annual General Meeting and World Air Transport Summit in Istanbul, Turkey. The industry challenges were reflected in IATA revising its industry financial forecast for 2008 significantly downwards to a loss of US\$2.3 billion. The forecast uses a consensus oil price of US\$106.5 per barrel crude (Brent). This is a swing of US\$6.8 billion from the previously forecast industry profit of US\$4.5 billion that was announced in March and based on an average oil price of US\$86 per barrel (Brent).

Putting into context the cost of airline insurance and a market that in 2007 generated a premium adjusted for commission and verticalisation of less than US\$1.6 billion, it was highlighted by Giovanni Bisignani, IATA Director General and CEO that "For every dollar that the price of fuel increases, our costs go up by US\$1.6 billion." The industry's total fuel bill in 2008 is expected to be US\$176 billion (based on oil at US\$106.5 per barrel) accounting for 34% of operating costs. This is US\$40 billion more than the 2006 bill which was US\$136 billion (29% of operating costs).

A message from Mr. Bisignani that will be heard by the insurance industry among others is "Oil is changing everything. This is an extraordinary crisis with the potential to re-shape the industry with impacts throughout the global economy."



WILLIS RUSSIAN AVIATION INSURANCE CONFERENCE

During May Willis held their first Russian/CIS Regional Conference for more than 10 years. The conference, organised with the support and sponsorship of Airclaims, Atrium, Clyde and GAUM, was in response to the increasing traffic forecasts and numbers of Western built aircraft being delivered to meet the demands of the domestic market.

These factors, along with some regional specific challenges, are changing the face of both the aviation insurance market in Russia, and the airline and aircraft manufacturing industries in the region.

Attendance was excellent, with more than 100 delegates, representing the London and European Insurance markets, Russian and CIS Airlines, together with representatives from all of the major Russian aviation insurers.

The keynote speech from Mr Valery Okoluv, General Director of Aeroflot Russian Airlines, addressed issues ranging from Russia's impressive GDP growth and recovery of passenger traffic linked to the increasing disposable income of Russian citizens; to the challenges that Aeroflot itself was facing, together with the strategies for expansion and consolidation to increase Aeroflots share of the domestic market.

Mr. Okoluv was asked about the one issue that personally concerned him, over and above all others within the airline. His response was not that of the increasing fuel prices that most airlines highlight, but rather the risks associated to identity theft, fraud and credit risks, now that internet sales and e-ticketing have taken off within Russia. This is an area we have highlighted in this publication previously, and one upon which Willis can advise, and present options and ideas should any of our clients have similar concerns.

Other presentations took place which encompassed the following topics:

- An overview of the Aviation Insurance market by Willis, Global Aerospace and Ingosstrakh who presented on the current market climates both in Europe and in Russia. Rating trends in both regions were focused upon and in addition, the rising cost of claims rather than frequency, with concerns being expressed about jurisdiction issues, and the trend to bring cases to the US courts.
- KD Avia from Kaliningrad (the most western point of the Russian Federation) and Vladavia from Vladivostok (in the very far east of Russia) gave presentations on their operations, and highlighted the peculiarities that they were dealing with in their regions.
- Representatives from Clyde & Co, UT Air and Avicos discussed the topical issue of the new Russian Air Code. Whilst Clydes gave an

interpretation of its workings, and the problems they foresee in adopting its requirements, UT Air and Avicos gave presentations as to how each of them felt the code would have an effect on their operations. This was a highly anticipated debate and many underwriters and reinsurers learnt a lot from hearing first hand of the issues and outstanding concerns surrounding the Code that became effective on 6th June.

- There was an overview from the Financial Director of the new Sheremetyevo Terminal 3 project which is due to open in the last quarter of 2008 and how this would improve passenger throughput compared with the existing terminals at Sheremetyevo.
- Terry West of Willis presented a regional market forecast providing many facts and figures that gave evidence of the recovery of the passenger traffic in the region, and the challenges that the Russian aviation industry and the airlines were facing to cope with the increased demand.
- Day 2 opened with the theme of "Minimising and Managing Risks", with presentations from Willis Moscow on Enterprise Risk Management, from Bruce Carmen at Atrium regarding the professional use of data and information, and a very technical and impressive presentation from the Flight Safety Department of Volga Dnepr Cargo Airlines on Flight Safety Monitoring and how Volga are targeting a position of Zero Risk.
- The closing session focused on "Forum Non Conveniens" using the S7 Case as a practical example. Last, but not least, was a detailed presentation from Airclaims discussing the unique issues they encounter when handling claims in Russia, and managing clients expectations on the timing of loss settlements.

The forum provided an excellent opportunity for networking, and many European underwriters had their first experience of meeting their Russian counterparts on their homeground. Willis is proud to have arranged this regional event, which compliments the conferences already established in Asia, Latin America and the MiddleEast/Africa - demonstrating that we bring the market to our clients.

For any additional information on this event please contact Terry West, email: terry.west@willis.com.

FORTHCOMING RENEWALS

NAME	INCEPTION	EXPIRING AFV US\$M
AIGLE AZUR	1-JUL	352
AIR MACAU	1-JUL	627
AIR MEDITERANNEE	1-JUL	300
AIR NAMIBIA	1-JUL	125
ALASKA AIRLINES	1-JUL	4,685
AMERICAN AIRLINES	1-JUL	20,623
ARKIA AIRWAYS	1-JUL	158
ATLASJET INTERNATIONAL AIRWAYS	1-JUL	488
FEDERAL EXPRESS	1-JUL	12,816
KITTY HAWK	1-JUL	130
KTHY	1-JUL	210
MANDALA AIRLINES	1-JUL	185
MEA	1-JUL	566
NACIL - AIR INDIA/INDIAN AIRLINES	1-JUL	4,740
OMNI AIR EXPRESS	1-JUL	297
ONUR AIRWAYS	1-JUL	884
SAFAIR	1-JUL	160
TACA etal	1-JUL	1,478
TIGER AIRWAYS	1-JUL	405
VOLGA DNEPR	1-JUL	677
WIZZ AIR	1-JUL	505
AEROFLOT	2-JUL	1,945
SIBERIA AIRLINES	7-JUL	473
CHINA AIRLINES	15-JUL	7,312
TNT	15-JUL	962
BINTER CANARIAS	26-JUL	195
SPIRIT AIRLINES	29-JUL	1,710

With a number of large programmes migrating their renewal dates in recent years, July has become the third busiest month in the annual renewal calendar. The 27 major renewals now provide the market with a variety of experience, fortunes and future projections to deal with.

The size of the programmes and the premium volume increase sharply, when compared with June, as some of the world's largest programmes and two of the US Major carriers renew. The largest risks in terms of fleet value are American Airlines with an expiring Average Fleet Value of US\$20.6 billion and Federal Express with almost US\$13 billion. In addition China Airlines (Taiwan) and the NACIL group which now includes Air India and Indian Airlines will renew with expiring AFV in excess of US\$5 billion.

Alaska Airlines will also renew in July for the first time having cancelled its December 2007 policy. Atlasjet Airlines (Turkey) will also renew in July having extended its expiring policy by 20 days. In 2007 the month generated 12% of the years annual premium, a figure that is likely to show an increase in 2008.

Following recent press reports with regards to the specific economic challenges in the USA and the subsequent airline capacity reductions, we believe that some of these carriers will renew with reduced

fleet and passenger exposures. It will be of interest to see the effect that this will have on rate changes and whether this will temper the level of reduction negotiated as insurers continue to try and maintain premium levels.

China Airlines and the TACA Group have suffered total losses of high valued aircraft in their expiring periods. These will obviously significantly impact their previously good, single-digit 5 year loss ratios and there will therefore be considerable interest in the treatment they receive from insurers.

The comparatively low level of activity that takes place between now and October means that, without a change in the capacity and claims market drivers, it could be November before any insight into a meaningful change in market direction is seen.

Without any capacity change there does however appear to be an increasingly different stance taken by individual underwriting units. Some are looking to remain competitive to maintain their position whilst others are taking a much firmer stance in a bid to improve their position and send a stronger message. The market continues to be poised to change direction but the timing and extent are obviously yet to become apparent, and seemingly will need a combination of factors.

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