

# Aerospace Insurance market news

## Q2/10

The aerospace sector continues its long period of consistent slight declines, with little evidence of a catalyst that will change the market direction significantly in the near term.

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### Overview

With around a quarter of the year's aerospace insurance policies placed, it appears that the trends of the last three years have continued. Lead premium in the sector has continued its slight decline, falling by 4% on average so far in 2010 in reporting currency.

The average reduction for the whole of 2009 was 2%, and 1% in 2008, so the current 4% reduction could be suggested to be a slight acceleration of the soft market conditions.

In reality it is more likely to reflect the fact that only just over 10% of the total expected premium for 2010 has renewed so far.

The long period of consistency would suggest that the market is due to turn, but at this stage, while individual underwriters are trying to make the case of increases, they are generally isolated and capacity can generally be found that will take up any shortage.

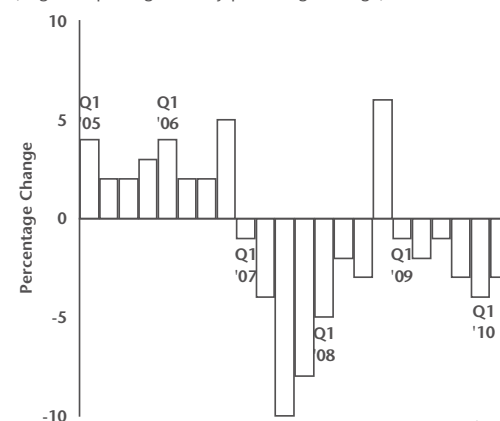
The soft markets are also being exacerbated by the fact that exposures have declined over the last eighteen months as a result of the global downturn's impact on the aviation sector.

### A break in the clouds

There is a chance that this will become less of an issue as the year progresses however, with more positive economic signals emanating from some regions of the world.

### Average quarterly percentage premium movement

(original reporting currency percentage change)



Source: Aon Market Data

The International Air Transport Association (IATA), one of the key indicators of the health of the aviation sector, says that air travel continued to grow in March, with passenger demand up by 10.3% and cargo demand up by 28.1% compared to March 2009.

It should be pointed out that these increases reflect the very low conditions in market in 2009, but the data does suggest that the position is improving.

IATA warns that the numbers are likely to have been less positive in April as a result of the disruption caused by the volcanic eruption in Iceland.

	Renewals	Expiring Premium (US\$m)	Renewal Premium (US\$m)	US\$ premium movement (% change)	RC* premium movement (% change)
Q3 '09	71	316.55	319.66	+1	-1
Q4 '09	61	226.83	228.43	+1	-3
January	30	43.97	42.85	-3	-5
February	6	11.04	10.99	-1	-3
March	18	21.33	21.00	-2	-3
April	10	25.27	23.28	-8	-3
2010	64	101.61	98.12	-2	-4

\*RC: Reporting currency



## SECTOR ANALYSIS

	Renewals	Expiring Premium (US\$m)	Renewal Premium (US\$m)	US\$ premium movement (% change)	RC* premium movement (% change)
Airport	27	47.91	47.09	-2	-3
Manufacturer	22	43.60	41.31	-5	-4
Service provider	15	10.10	9.72	-4	-6
<b>2009 to date</b>	<b>64</b>	<b>101.61</b>	<b>98.12</b>	<b>-3</b>	<b>-4</b>

\*RC: Reporting currency

### Airport (including ATC)

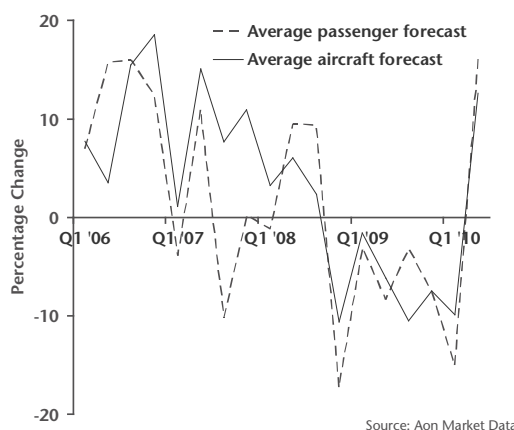
A third of the total expected number of airports and air traffic control (ATC) operations have renewed their insurance policies so far in 2010. This translates to nearly half of the total expected annual premium.

The price of lead premium has continued to fall, extending a trend for 0-5% reductions that has been in place since the fourth quarter of 2008 (prior to which the reductions were more pronounced).

Looking at the passenger and aircraft departure forecasts made by airports so far this year suggests that confidence is growing in the sub-sector, backing up the data produced by the International Air Transport Association (discussed on the front page).

It should be stressed that this is forecast data and as a result, the picture could change as the year progresses, but it at least suggests a more positive outlook for the sector compared to 2009.

#### Average quarterly percentage aircraft and passenger number movement



Source: Aon Market Data

Airports are beginning to be more positive in their passenger and aircraft forecasts. Could the sector be a bellwether for an aerospace recovery?

### Manufacturer (including MRO)

Nearly 20% of the year's total number of aerospace manufacturers or maintenance, repair and overhaul (MRO) operations have now renewed. This translates to around 5% of the total expected annual lead premium, making meaningful observations difficult at this stage.

One interesting point that we can make is that in contrast to the improving optimism in the airport sub-sector, manufacturers that have placed so far in 2010

are still expecting turnover to decline on average by 1% during the course of 2010/11 insurance policies. This is a slight decline on the position in 2009, when the sub-sector forecast a very slight increase in turnover of less than 1%.

Only two MROs have renewed so far this year, making analysis impossible at this stage.

Relatively little manufacturer premium has renewed so far in 2010, making analysis difficult.

### Service provider

The service provider sub-sector has seen nearly a quarter of 2010's expected lead premium renew, with an average decrease of 4% so far this year. This broadly continues the trend witnessed in 2009, when average lead premium fell by 6%.

This does beg the question: when will the bottom of the market be reached? The cost of lead premium in the service provider sub-sector has now declined for 15 consecutive quarters. At this stage, however, there is little evidence from underwriters that prices will begin to climb in the near term.

All 15 of the service provider renewals have enjoyed

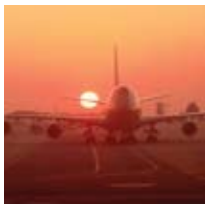
premium reductions or as before pricing so far this year. This suggests that underwriters are confident about pricing in a sub-sector where claims tend to be relatively predictable and exposures evolving at a manageable rate. The robust level of competition for sub-sector's programs is also likely to be a factor.

All of the renewals so far except one are refuellers. Despite the improving forecasts from the airport sub-sector, the amount of fuel expected to be supplied continues to decline, by slightly more than 11% on average year to date. It should be pointed out that this is based on 14 placements, with more than 35 expected for the whole year.

The trend that began in 2007 continues

# INDUSTRY REELS FROM VOLCANO IMPACT

The recent eruption of the Eyjafjallajokull volcano in Iceland has turned attention on business interruption practices at organisations around the world.



Just as the aviation industry appeared to be getting back on its feet, the eruption of the Eyjafjallajokull volcano in Iceland has wreaked further havoc. An estimated 100,000 flights were cancelled towards the end of April when the majority of governments in Europe closed their airspace, costing the industry between €1.5 billion and €2.5 billion.

The volcano is located in the north of Europe, but the disruption that followed the closure of most of the region's airspace was pretty much global, with passengers, crews and aircraft stranded in the wrong place. For many of the airlines, it will have been weeks before their schedules returned to normal.

Further, albeit limited, cancellations occurred throughout May, and there is a chance that the disruptions could continue sporadically for some time. There are also those that point out that an eruption of Eyjafjallajokull tends to be a prelude to an eruption of Katla, a far bigger neighbouring volcano.

The current issues could have a number of ramifications for the aviation industry. From the perspective of the insurance markets the position is relatively clear. Successful claims against standard airline liability insurance policies due to delays as a result of the volcanic eruption in Iceland are unlikely.

The main reason for this is that this is a natural event and there has not been any actual damage to aircraft or property at this stage.

Under European regulations, EC261/2004, the obligations on airlines should be limited or excluded in cases where an event is caused by extraordinary circumstances that could not have been avoided even if all reasonable measures had been taken.

## Business, interrupted

The picture is similar from a business interruption (BI) point of view, suggests Stephen Cross, CEO of Aon Global Risk Consulting (AGRC). "Typically, BI policies will most likely not be responding to the disruption to airspace caused by the volcanic ash," he says. "BI policies usually only kick in when there is physical damage. If ash falls to Earth and lands on a business' premises and causes damage, blocking air pipes that could lead to an explosion for example, then that could trigger a resulting BI policy.

"It is important to note, however, that insurance policies vary," Cross points out. "A firm should always study their policy to determine whether they are able to claim on their insurance cover."

Cross suggests that ensuring that BI policies are as responsive as possible is a key part of AGRC's work in the sector. "Aon has been working for some time now with insurers and industry bodies in the London insurance market on bringing BI cover into the 21st century, developing this product to make it more relevant to today's world and today's risks," he explains. "The recent crisis underlines the importance of this ongoing work."



Stephen Cross, CEO,  
Aon Global  
Risk Consulting

## Supply chain management

Cross points out that while it is difficult to foresee every possible event, it is the companies that have an effective plan for disruption that are likely to get back on their feet most quickly.

"Supply chain management becomes a critical area of business in situations such as Europe has been experiencing," he observes. "While you can't plan for every eventuality, especially such rare occurrences as a volcanic eruption affecting large swathes of a region's airspace, the fundamental principles of sound supply chain management still apply: you should always be aware of what business continuity measures your suppliers of critical inputs have in place and be thinking about alternative suppliers.

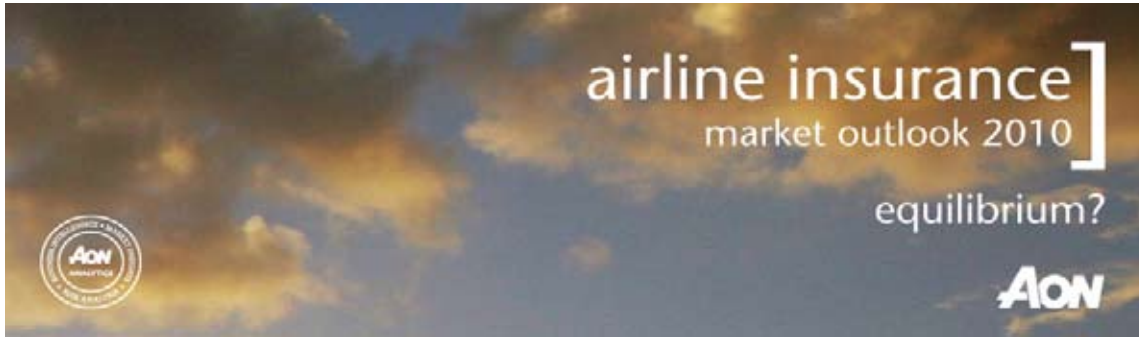
"Unfortunately, as economies contract or competition increases, lean manufacturing becomes the name of the game, either through Just-in-Time inventory management or moving to single suppliers in order to generate economies of scale. Such an approach might be highly efficient when things are running smoothly, but in the case of a major disruption event such as this, it can lead to significant delays in key materials and inputs being delivered, or in a worst case scenario to a systemic failure in your supply chain."

Cross points out that this is as true for the aviation as any sector, with airlines reliant on fuel suppliers, as well as food and refreshments providers in order to ensure that they can look after their passengers.

## The silver lining

While the last few weeks have proved difficult for many and the position looks like it may continue to be challenging for some time, there are positives that can be taken. "There is an upside for firms that invested in rigorous business continuity planning," concludes Cross. "They will have examined alternative ways of providing their product or service and will come out the other side of a lengthy disruption in a better position than those who haven't."





## SLOWER ASCENT FOR AIRLINE INSURANCE IN 2010

Average lead hull and liability premium in the airline insurance market rose by 20% in 2009, taking total lead hull and liability to US\$1.9 billion, according to Aon's Airline Insurance Market Outlook 2010. Total estimated claims for the year however, were US\$2.3 billion, meaning that airline underwriters potentially suffered a third consecutive year of losses.

As a result, hull and liability premium prices are likely to continue to rise in 2010, although the rate of increase could slow because of the high level of capacity that is currently available.

According to the report, airlines forecast passenger numbers to fall by 2% on average as a result of the global economic difficulties, and while average fleet values are forecast to grow by 3% during the course of 2009/10 insurance policies, this is well down on the 9% growth forecast in 2007.

Among the report's key findings are:

- 2009 was one of the most expensive years in the

recent history of the aviation industry, with US\$2.3 billion of claims (including an estimate for minor losses). This compares to an average of US\$1.8 billion between 1998 and 2008 (including 9/11);

- There were 58 major losses globally, compared to the long term average of 68. Total fatalities for the year were 423, compared to an average of 635;
- Lead hull and liability premium grew by the highest rate in the Middle East, which also forecast the highest levels of passenger and fleet growth, both 12%;
- Operations in North America forecast reductions in both fleet value, 3%, and passenger numbers, 5%. European operations forecast fleet increases of 2% and passenger reductions of 1%.

Aon's Airline Insurance Market Outlook 2010 document can be obtained from [www.aon.com/aviationinsight](http://www.aon.com/aviationinsight). Back issues of all of our publications are available from this site.

The Aon Aviation Insurance Market Outlook 2010 document is now available.

## ABC 2010 ANNUAL CONFERENCE

The Aircraft Builders Council (ABC) holds a conference each year that looks at recent developments in the aviation and aerospace industry and products liability. The conference brings together insureds, potential insureds, lead underwriters, brokers and legal experts. The 2010 conference is scheduled for September 19-21 at the Renaissance Vinoy Resort in St Petersburg, Florida.

The 2010 pre-conference brochure, speaker details and registration information will be available from June at [www.aircraftbuilders.com](http://www.aircraftbuilders.com).



**Aircraft Builders Council, Inc.**

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