

Aerospace Insurance market news

Q1/10

Despite the challenging global economic conditions and the very high level of losses in the airline sector in 2009, the aerospace insurance market looks set to continue its current direction in 2010.

CONTENTS

- Overview**
- Sector overview**
 - Airport
 - Manufacturer
 - Service provider
- Aerospace holds its pattern**
- ERM usage grows finds Aon survey**
- Elevated political risk levels continue into 2010, Aon says**



Aon Aviation & Aerospace website

Overview

The average price of lead aerospace insurance premium continued its remarkable consistency in the final quarter of 2009, concluding a year where average lead premium has barely fluctuated.

Overall, the average price of insurance in the aerospace sector declined by 2%. This continues the trend set in 2008, when average premium declined by 1%.

Trends continue

The trends in 2009 in the aerospace insurance market are likely to continue into 2010, following a pattern that has been in place for the last two years.

The average cost of aerospace lead premium has fallen by low single digits for six of the last seven quarters. The only exception was the final quarter of 2008 when average premium rose by 6%, mainly driven by loss related increases in the manufacturer sub-sector.

While market direction has been consistent, the reasons driving the slight reductions have changed.

In 2008, prices were being driven down by a robust level of capacity creating price competition.

In 2009 capacity began to fray at the edges, but at the same time, the global economic conditions meant that aerospace companies were looking to reduce their activity. Lower activity meant less risk, meaning reduced insurance requirements.

Positives

What does this mean for 2010? The short, if not very enlightening answer is that conditions continue to evolve.

Countries around the world are struggling out of recession. This should increase in economic activity, but confidence is unlikely to be high enough to raise demand for aviation services in the short term.

The International Air Transport Association says that passenger numbers were 4.5% higher in December 2009 than they were in 2008, but passenger numbers for the whole of 2009 were down by 3.5%.

This position was echoed by Anna.aero, a Europe-based airline network news and analysis service, which has said that only four European countries enjoyed increased passenger numbers during 2009.

What this means is that there will be more positive data emerging 2010, but it will be based on comparisons to a relatively low level of activity in 2009 and it will be some time before the aviation industry returns to a long term growth.

From an insurance point of view, the 2009 claims statistics for 2009 will make grim reading for the aerospace sector.

The high level of claims in 2009 were generated by a relatively low number of incidents, however, which

(continues overleaf)

	Renewals	Expiring Premium (US\$m)	Renewal Premium (US\$m)	US\$ premium movement (% change)	RC* premium movement (% change)
Quarter One	57	86.78	79.47	-8	-1
Quarter Two	58	163.52	158.22	-3	-2
Quarter Three	70	315.18	318.23	+1	-1
October	22	93.77	92.46	-1	-4
November	23	92.30	93.92	+2	0
December	15	38.10	39.47	+4	-4
2009	245	789.65	781.77	-1	-2

*RC: Reporting currency



Overview (continued)

should hold back the worst of the increases from the majority of operations in the aerospace sector.

While details are very limited at the moment, it appears that the roof collapse at a hangar at Washington Dulles International Airport on February 6 could lead to significant claims. It is unclear how many aircraft were damaged in the incident, which was caused by weight of snow on the roof.

Clairvoyance, Inc.

Despite some reticence in 2009, capacity in the aerospace insurance markets continues to be theoretically high. With other financial markets recovering from the economic turmoil, however, capacity providers will have an increasing choice over where to devote their resources.

That said, as the data shows, aerospace has provided a relatively consistent rate of return over the last couple of years. This is likely to be a positive factor for the sector.

What this means for 2010 is difficult to gauge, but it seems likely that the aerospace industry may see prices either continue with the current level of slight decline or potentially start to increase slightly.

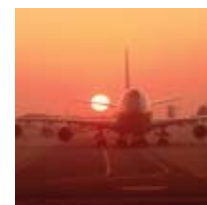
Certainly, no matter what the nuances are, there is little that points to significant increases in the cost of lead insurance premium at this stage, aside from the simple fact that prices fallen gradually for three consecutive years.

Prices seem set to continue their current direction in 2010, although a slight firming is possible.

SECTOR ANALYSIS

	Renewals	Expiring Premium (US\$m)	Renewal Premium (US\$m)	US\$ premium movement (% change)	RC* premium movement (% change)
Airport	81	129.52	118.14	-9	-3
Manufacturer	119	611.14	621.06	+2	0
Service provider	45	48.99	42.57	-13	-6
2009 to date	245	789.65	781.77	-1	-2

*RC: Reporting currency



Airport (including ATC)

The price of lead insurance premium has continued to decline in the airport sub-sector.

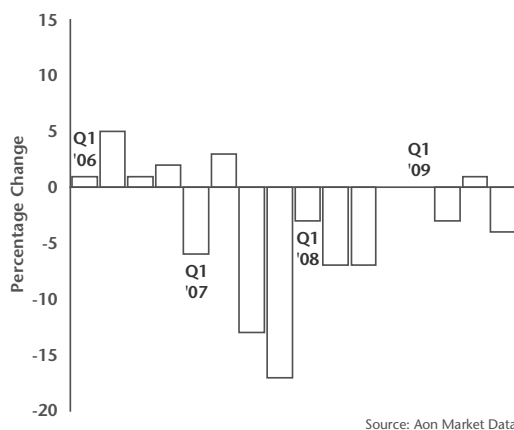
Stripping out the impact of air traffic control (ATC) operations, and the average price of insurance has fallen in 10 of the last 12 quarters, although, as discussed on page one, the driver for the reductions has shifted from plentiful insurance market competition to falling exposure in the airport sector.

Of the 55 airports that we have recorded, 18 saw their premium increase. In terms of exposure, passenger numbers are expected to fall by 11% while aircraft departure forecasts are expected to fall by 5% on 2009/10 insurance policies compared to the numbers given in 2008/09.

The position for ATC operations is similar. Of the 26 recorded, only six have seen premium increases, although aircraft departure numbers are expected to rise by just under 1% during the course of 2009/10 insurance policies. This compares to a 6% increase in aircraft departures forecast for 2008/09 policies.

As mentioned in the last edition of this newsletter (available from www.aon.com/aviationinsight), the falling exposure means that airports are actively seeking premium reductions to ensure that the level of insurance is closely aligned to actual risk.

Airports average quarterly percentage premium movement
(original reporting currency percentage change)



Airports and ATC operations forecast falling exposure throughout 2009. Robust insurance negotiations will be the consequence in 2010.

Manufacturer (including MRO)

Manufacturers still receive the toughest treatment from the insurance markets, but the increases have slowed.

The manufacturer sub-sector softened by 4% during the final quarter of 2009, a slight improvement on the second and third quarters when the average cost of premium rose by 2%.

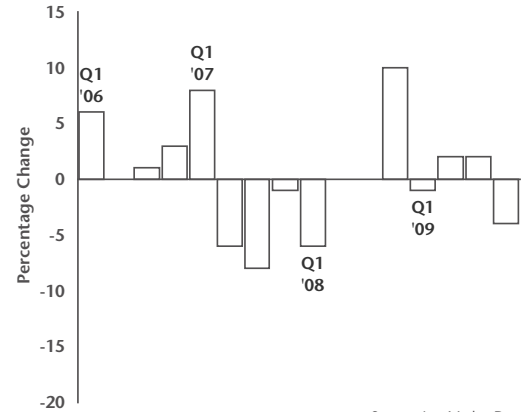
Of the 101 manufacturers currently in the list, just over a third saw lead premium increases, but only 14 of these were by more than 10%.

In terms of turnover forecasts, the position for manufacturers is fairly stable, with an overall decrease of less than 1% expected during the life of 2009/10 insurance policies. This compares to a forecast increase of 8% in 2008/09, suggesting that there is a healthy level of realism in the sub-sector.

Conditions for maintenance, repair and overhaul (MRO) operations have continued to fluctuate. A 10% average increase in the first quarter of 2009 was followed by 1% decreases in Q2 and Q3 followed by a 1% increases in the final quarter.

Manufacturer average quarterly percentage premium movement

(original reporting currency percentage change)



Source: Aon Market Data

Service provider

Service providers continue to see premium costs fall gradually. After three consecutive years, the question is how long can this continue?

Service providers have enjoyed 13 consecutive quarters of average reductions, reflecting the relative simplicity of claims in the sub-sector in comparison with, for example, manufacturers.

Overall, the average insurance price trend has been fairly constant for three years now, falling by 6% in 2007, 2008 and 2009.

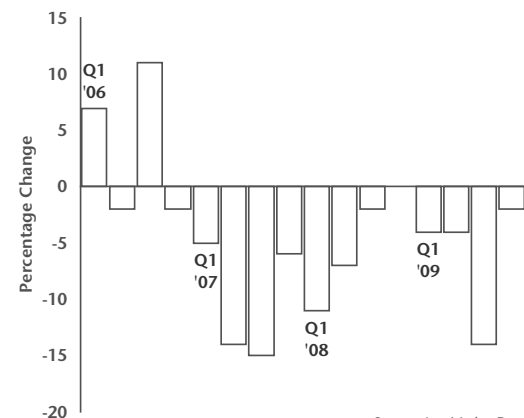
These gradual reductions are likely to mean that the current market direction may not continue in the long term as the sub-sector reaches the point where price effectively reflects claims history and risk.

That said, as the smallest of the sub-sectors, price changes at a single operation can potentially have a significant impact on the average.

Only six of the 45 service providers that we have recorded saw premium price increases in 2009.

Service provider average quarterly percentage premium movement

(original reporting currency percentage change)



Source: Aon Market Data

AEROSPACE HOLDS ITS PATTERN

The aerospace sector's recent consistency is highlighted by looking at the number of increases and decreases

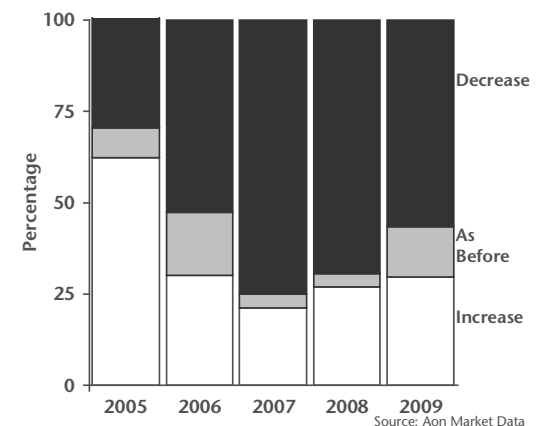
Using the average lead premium change as a guide for the direction of the aerospace insurance market runs the risk of missing the wide spread between the highest increase and decrease. This is particularly true given the diversity of the aerospace sector.

Looking at the number of increases and decreases the over the last few years backs up the suggestion of consistency in the sector, however. There has been a rise in the number of aerospace operations receiving an increase in their lead premium price, from a low of 21% in 2007 to the 30% recorded in 2009's preliminary data, but decreases have been the norm for more than half of operations each year since 2006.

While this is something of a blunt instrument, it does back up the suggestion that the sector is moving in a relatively consistent direction.

Proportion of increases and decreases

(Percentage of lead hull and liability premium changes)



Source: Aon Market Data



ERM USAGE GROWS FINDS AON SURVEY

More companies are employing mature enterprise risk management (ERM) practices to enhance organizational value and resilience, Aon's 2010 Global Enterprise Risk Management Survey finds.

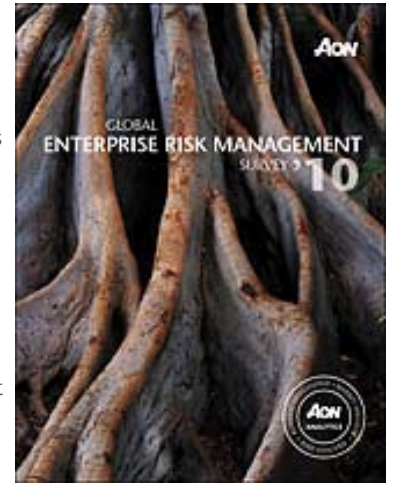
More than 60% of respondents say they have progressed beyond basic ERM practices compared with 38% of those surveyed in 2007. This suggests that companies are integrating risk management processes beyond senior management and developing more transparent relationships with shareholders, customers, vendors and employees. The number of respondents with advanced ERM programs has risen from 3% to 7% during the same period.

Organizations in the more mature stages of ERM report they can realize significant benefits in areas such as enhancing shareholder value, optimizing and reducing total cost of risk, strengthening business resiliency and increasing operational efficiency. This is encouraging news in light of the financial challenges many have faced since the 2007 report.

Scott Nicholl, senior consultant for Aon Global Risk Consulting (AGRC) in the UK, commented: "Companies can now use ERM to plan ahead and spend less time fire fighting. It is a vital part of an organization's armor."

"When risk managers truly understand risk and use information to enhance the organization's overall risk intelligence, they are able to make decisions more in line with strategic and operating plans and the external environment," adds Laura Taylor, global leader of enterprise risk management for AGRC. "Our report illustrates how these advanced organizations are able to move beyond focusing on risk avoidance and mitigation toward leveraging risk to drive sustainable growth, continuity and profitability."

A copy of the report can be downloaded from www.aon.com/ermssurvey2010.



ELEVATED POLITICAL RISK LEVELS TO CONTINUE INTO 2010, AON SAYS

Political and financial instability remain a feature of the business landscape as a result of the recession, according to Aon's annual Political Risk Map.

Miles Johnstone, director of Aon's Political Risk team, says: "Rising risk levels in 2009 have led to a significant volume of credit and political risk claims in international insurance markets which is driving many of this year's downgrades. For instance non-payment of sovereign and sub-sovereign debt obligations is a major issue for underwriters insuring risks in Ghana, and underwriters continue to experience a multitude of claims stemming from payment defaults by private sector banks in Ukraine."

Nine countries have been upgraded to a lower risk level: Albania, Myanmar/Burma, Hong Kong, Colombia, South Africa, Sri Lanka, East Timor, Vanuatu and Vietnam.

Conditions have deteriorated in 18 countries, leading to a downgrade: Algeria, Argentina, El Salvador, Equatorial Guinea, Ghana, Honduras, Kazakhstan, Latvia, Madagascar, Mauritania, Philippines, Puerto

Rico, Seychelles, Sudan, United Arab Emirates, Ukraine, Venezuela and Yemen.



Sudan, Venezuela and Yemen have been added to the Very High category, joining Afghanistan, Congo DRC, Iran, Iraq, North Korea, Somalia and Zimbabwe.

Johnstone concludes: "The elevated political risk levels will continue in 2010 before an overall tendency for improving global business conditions becomes established. Our interactive Political Risk Map gives clients up-to-date tools to assess the various contingencies and determine the impact on their ability to ensure continued survival, growth and profitability."

Aon's 17th annual Political Risk Map is available from your Aon account team.

Aon's 17th Political Risk Map reflects the challenging economic conditions endured in 2009.

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