



Market Overview

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The soft market conditions the aerospace insurance market witnessed in the first quarter accelerated in the second with an average liability premium reduction of -6% in reporting currency. The early indications from the third quarter, based on the preliminary figures from July, are that the reductions have increased further.

In 2006, the second quarter was the second most active of the year, and the premium movement in reporting currency was very close to the +3% recorded for the full year. July, however, is the most active month in the industry both in terms of the number of renewals and the amount of premium renewed, and it may be that the reductions will hold in certain sectors for the rest of the year.

The aerospace market is comprised of a very diverse range of operations, and as a result, there will continue to be fluctuations for its individual sectors. While the average lead premium change is a useful gauge of market direction, it should always be approached with a certain amount of caution.

This is particularly true given that the aerospace insurance market increasingly renews programmes based on an individual operation's merit, location and claims history, rather than simply applying a blanket market average to a renewal.

The overall decline in lead premium is the result of two major factors, capacity and claims. Primarily, capacity still sits at around 190% according to Aon's calculations. What this means is that a risk with a good loss history and stable exposures could be filled nearly twice over, highlighting the relatively high level of competition in the market at this stage.

Equally, there has only been one major loss, the hangar fire in Abu Dhabi in April, that is likely to impact the aerospace market during 2007, and the loss rates have been low in the aviation industry as a whole for the last four years. This means that even given the complexity and time it can take for the impact of a claim to reach the aerospace insurance market, there are an increasing number of organisations with good loss histories which will drive competition further.

Generally, the benign market conditions continue to encourage organisations to try to look at longer-term policies of up to three years to ensure that they are making the most of the current soft market, although this development is generally being resisted by the market.

With nearly twice as much premium renewing than in April, July is the most active month in the aerospace insurance market renewal calendar. In 2006, nearly half of the annual aerospace activity took place during the month, and it is expected to have a similar impact in 2007.

As a result, July receives a great deal of focus because it is likely to set the tone for the rest of the year, particularly in the manufacturing sector where the majority of activity takes place.

It should be made clear at this point that the numbers we are reporting for July are preliminary. We expect there to be about another 15 renewals once the numbers for the full month are tracked. As a result, there may be some change in the averages once the full numbers are available.

	Renewals	Expiring Premium (US\$m)	Renewal Premium (US\$m)	US\$ Premium Movement (% change)	RC* Premium Movement (% change)
February	7	10.41	9.69	-7	-5
March	20	26.75	31.85	+19	-5
April	26	207.37	179.23	-14	-7
May	12	31.51	23.03	-27	-4
June	18	48.46	43.53	-10	-6
July	31	250.75	213.42	-15	-8
2007-to-date	141	620.15	549.22	-11	-5

Source: Aon Market Data
Numbers on a like-for-like basis

Sector Analysis

	Renewals	Expiring Premium (US\$m)	Renewal Premium (US\$m)	US\$ Premium Movement (% change)	RC* Premium Movement (% change)
Airport (YTD)	48	93.54	95.47	+2	-3
Manufacturer (YTD)	68	490.80	422.95	-14	-2
Service Provider (YTD)	25	35.81	30.80	-14	-11
2007-to-date	141	620.15	549.22	-11	-5

Airport (including ATC)

The airport sector's relative stability at the top level masks some fairly major changes at individual operations within the sector.

Stripping out the impact of the 15 air traffic control (ATC) operations that are included in the overall airport sector, two of the 33 airport renewals have seen their liability premium rise by over 50% for their 2007/8 policies, as a result of an increase in policy limit at one and a historic loss being added to the record of another. A third operation has seen its liability premium reduced by over a third as a result of selling a ground handling subsidiary.

Removing these airports from the overall numbers for the year-to-date, and the sector's average reduction would be more than -4% in reporting currency, as opposed to -2% as it currently stands.

Just over half of the expected airport programmes have renewed so far this year. Of these, just over a third of airports have received double-digit

reductions.

Focusing on the ATC sector, the reductions have been far more consistent, with only one of the 15 renewals seeing its liability premium increase so far this year. Six of the ATC operations recorded have seen their premium fall by between 0% and -5%, while eight have enjoyed a reduction of more than -5%.

This presumably reflects the more stable nature of the ATC sector which has enjoyed significant improvements in both cross border relationships and technology in recent years, while the major development work that is taking place at a number of airports globally is increasing the perception of exposure somewhat within the insurance markets.

Overall, the relatively low level of losses and high level of competition for good risks is creating a tension that is driving down the cost of liability insurance within both the airport and ATC sectors of the industry.

Manufacturer (Including MRO)

Discounting the impact of the maintenance, repair and overhaul (MRO) sector, which is included with the manufacturers sector because of its similar risk profile, around 60 manufacturers have renewed so far this year. Of these just under a quarter have seen their liability premium increase, ten of which were double digit increases.

The largest of the rises was the result of an increase to the organisation's policy limits, while the second largest saw its premium rise as a result of increases in its loss reserves. The third largest increase was the result of exposure increases and historical losses.

Factoring these three increases out of the total, and the year-to-date average liability premium change

would be around -9% for the manufacturing sector in reporting currency.

In terms MRO operations, there have only been eight renewals so far this year, making analysis difficult.

Overall, this sector of the market has reduced by around -4% on average in terms of liability premium, with the reductions relatively universal across regions and size of business.

In total, we expect there to be around 15 MRO renewals that meet our criteria during 2007. Last year saw average premiums fall by just over -1% overall.

Service Provider

There have been around 25 service provider renewals so far this year. We recorded just over 30 renewals for the whole of 2006, the majority of which had been placed by the end of August, so the -11% average liability premium reduction is likely to be fairly indicative of the market position by the end of 2007.

Despite having the most significant reduction, the service provider sector is the smallest in the aerospace market, and has a limited impact on the full year figures as a result.

Of the renewals recorded so far in 2007, 11 were

double-digit reductions, 12 were either the same as last year or single digit reductions, while the two increases that occurred have both been greater than 10%, the result of limit changes at both operations.

It appears that the refuelling sector has been benefiting from some strong reductions, with nearly a quarter of operators receiving reductions of around a fifth or more in reporting currency.

Another service provider received a reduction of nearly a quarter as a result of changing its leader, highlighting the level of competition that exists for programmes with good loss histories.

Premium Movement Shows Stark Market Shift

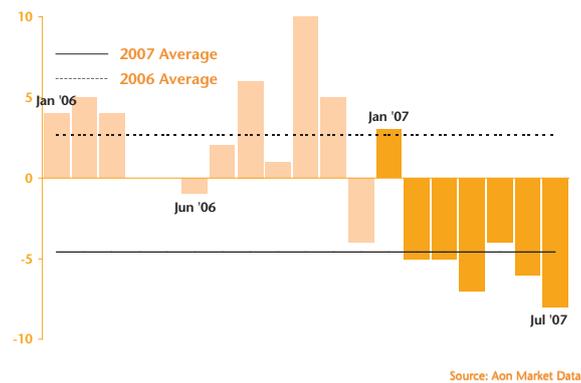
Just over mid-way through the year and a fairly clear pattern has developed for 2007/8 renewals when looking at the monthly average renewal rate in reporting currencies.

The average lead premium grew by around +2.7% for 2006/7 renewals placed last year, while the average for 2007/8 renewals, with over a third already placed, has been a reduction of more than -4.5%.

The change in the average liability premium trend in the aerospace insurance market between 2006/7 renewals and 2007/8 renewals is very clearly marked.

Now that the majority of expected programmes for the year have been placed, the question is how this perception of a softening market will impact activity next year.

Average Percentage Premium Movement (original reporting currency percentage change)



Cyber-Crime Risk Management

Good corporate governance demands that there are adequate controls on the vast amounts of electronic information aviation organisations hold, but cyber-crime presents increasing risks.

The 2006/7 Airline Risk Management Survey, conducted anonymously by Airline Business magazine in conjunction with Aon, found that computer crime insurance was the second most important future risk requirement among the world's top airlines. Last year it held the top spot, only slipping into second as a result of the current focus there is on environmental issues in many parts of the world.

Cyber-crime's prominence reflects the growing recognition that while IT brings massive efficiencies in terms of competitor, client and regulatory activity, it also creates a swathe of new risks.

While many picture a hacker as a lonely, disaffected young man or woman simply making mischief on the internet, the reality is of increasingly organised, professional criminals, carrying out targeted attacks to steal data for illicit profit from operations of all sizes around the world.

Most companies and their insurers prefer not to disclose incidents of cyber-crime. The British government, however, estimates that cyber-crime currently costs UK businesses over US\$5bn per year, a number which is rising quickly. Other governments around the world have made comparable estimates.

Modern cyber criminal activities include data theft to facilitate industrial espionage, credit card and passport fraud, human trafficking and straightforward theft.

Call centre hijacks, where hackers attack and gain control of centres through technology back-doors before demanding a ransom to restore the service, are becoming more common.

Similar denial of service (DoS) attacks have been launched on bookmakers prior to major sporting

events. The impact of a DoS attack on an airport car parking provider or the supply chain for a catering firm in the run-up to a holiday period, for example, would be very significant.

Bot software scams, where viruses are used to take over large numbers of computers that can then be programmed remotely to send spam to targeted victims or used for DoS attacks, are rampant. Criminal gangs are making a lucrative business from renting out these so-called zombie machines to each other to bolster the strength of their attacks.

Phishing, the use of bogus websites and emails to extract consumer data such as credit card details, increased significantly in 2006, while ready-made spamming programmes can be bought over the counter in some countries.

Given the type of data some aerospace organisations hold about their clients, and the bad press that any security lapse could cause, taking as many precautions as possible to ensure data security would make good business sense.

For an aviation organisation, every minute that an online system is unavailable, be it a result of criminal activity or otherwise, can cost a business large amounts of revenue.

Protecting and maintaining data from cyber-crime is a key issue facing the aerospace industry going forward, and the industry needs to be aware of the risks it faces.

Aon's cyber-crime specialists have worked with aviation operations globally to ensure that senior management is aware of the full plethora of cyber-crimes that they face. They can work to ensure that an organisation's actual risk position reflects their risk tolerance and help reduce the potential for sudden shocks if there is ever an issue.

If you would like further details about Aon's cyber-crime risk management capabilities, please email aviation@aon.com

Third Quarter Aerospace Renewals

Airports	Renewal Date
Airways Corporation of New Zealand	01 Jul
Australia Pacific Airports	01 Jul
Brisbane International Airport	01 Jul
Canadian Airport Council Tier 1	01 Jul
Incheon International Airport (Seoul)	01 Jul
Los Angeles World Airports Programme	01 Jul
NATS (UK)	01 Jul
New Tokyo International (Narita)	01 Jul
Northern Territory Airports Ltd.	01 Jul
The Government Of Hong Kong	01 Jul
UK Civil Aviation Authority	01 Jul
Auckland International Airport	31 Aug
Air Traffic Management Bureau of CAAC	01 Sep
City of Atlanta, Dept of Aviation	01 Sep
Kansai Int'l Airport (Airport Liabs)	01 Sep
Kansai Int'l Airport (Owners/Cont. Liabs)	01 Sep
Portuguese Airports	01 Sep
Singapore CAA	04 Sep
Government of Jordan	28 Sep

Service Providers	Renewal Date
Compania Logistica de Hidrocarburos	01 Jul
Penauille Servisair	01 Jul
Petrobas	01 Jul
Repsol	01 Jul
Royal Dutch Shell Group (Excess policy)	01 Jul
Saudi Aramco	01 Jul
Sonatrach	01 Jul
Asia Airfreight Terminal	03 Jul
Atlantic Aviation	03 Jul
Aviation Fuel Supply Co. (HK)	06 Jul
LSG Sky Chefs (SC Int'l)	01 Aug
Alpha Airports Group Plc	04 Aug

Manufacturers	Renewal Date
AMECO	01 Jul
ALCOA	01 Jul
Boeing (The Boeing Company)	01 Jul
CAE Inc.	01 Jul
Curtiss Wright Corporation	01 Jul
Dassault Aviation	01 Jul
Eaton Corporation	01 Jul
GKN Plc	01 Jul
Henkel of America	01 Jul
ITT Corporation	01 Jul
Kaman Corporation	01 Jul
Magellan Aerospace Corporation	01 Jul
New Piper Aircraft	01 Jul
Parker Hannifin Corporation	01 Jul
Rockwell Collins Corp.	01 Jul
SAAB Scania A.B.	01 Jul
SABCA	01 Jul
Senior PLC	01 Jul
SITA	01 Jul
Triumph Group	01 Jul
United Technologies Corporation (UTC)	01 Jul
Woodward Governor	01 Jul
Zodiac	01 Jul
Cirrus Industries Inc.	20 Jul
Embraer	31 Jul
Northrop Grumman	31 Jul
Vought Aircraft Industries	31 Jul
ATR	01 Aug
Columbia Aircraft Manufacturing	01 Aug
Finmeccanica	01 Aug
Goodrich Corporation	01 Aug
Marshall of Cambridge Aerospace Ltd	01 Aug
MTU Aero Engines	01 Aug
Smiths Industries	01 Aug
Superior Air Parts	01 Aug
General Motors	01 Sep
Landmark Aviation	01 Sep
MOOG	01 Sep
Qinetiq Holdings Ltd.	01 Sep
Teleflex (Sermatech)	01 Sep
Alliant Tech Systems	15 Sep
General Electric	16 Sep
Spirit Aerosystems	16 Sep

As can be seen from the table of renewals, quarter three, and July specifically, is the most active of the aerospace insurance market's year.

The second most active month is April, and as a result, by the end of July last year, nearly 75% of the total premium for 2006 had been renewed. There is little reason to expect the proportions will be significantly different when 2007 comes to a close.

Four of the industry's largest manufacturers, all US-based, dominate July. The largest of these is nearly 60% of the size of the other 73 organisations that renew in the quarter in terms of gross premium.

As a result, the numbers for the year will be significantly influenced by any premium movement in this programme, highlighting the need to look at programmes according to their sector and individual risk profiles, rather than applying a blanket industry average premium movement rate to their renewal.

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Our criteria for inclusion is accounts with any of the following: a combined single limit (liability limit) of over US\$650m; premium of over US\$2m; top 50 airport groups by revenue; top 100 manufacturers.

We welcome any comments or suggestions to add to or improve our product.

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