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Airlines face rise in insurance costs

By Alistair Gray in London

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Airlines are facing a possible rise in insurance premiums after the industry’s latest disaster struck little more than four months following the disappearance of another passenger jet. Yet several insurance analysts and brokers said they expected the fallout to be contained.

While aviation premium levels may tick up from their lowest levels in a generation following the downing of the Malaysia Airlines jet over eastern Ukraine this week, the analysts and brokers said insurance costs were unlikely to rebound strongly.

Insurance companies are facing two categories of payouts after the latest crash: relatives seeking compensation, and physical damage to the aircraft.

A group, led by Allianz, will be on the hook for the passenger liability claims as part of an “all-risk” aviation policy.

It was unlikely the airline would be deemed negligent assuming the aircraft was shot down, said Sean Gates, chairman of risk management consultancy Gates Aviation. Several other airlines had been flying over the same area, he added.

Under multinational agreements that govern compensation payments to air disaster victims, the lack of negligence would limit the airline’s liability bill to about £100,000 a passenger – less than £30m overall – Mr Gates said.

If the airline were deemed negligent, however, the uncapped liability insurance costs could run into the low hundreds of millions of pounds. But the final sum will not be known for several months or years.

Losses arising from the physical damage are much more certain – about $100m. But which insurance companies will pay out for the destruction will depend on what caused the disaster.

If the airliner was shot down, even by mistake, insurers led by Lloyd’s of London underwriter Atrium would be on the hook under an aviation “war” policy.

If it emerged that the aircraft was not shot down, the same insurers due to pick up the passenger liability bill would also be liable for the physical damage under the “all-risk” policy.

If the cause is disputed, the two groups of insurers may agree to share the payouts – as was the case with the Malaysia Airlines flight MH370, which went missing in March.

Each multinational airline typically spends several million pounds a year on insurance. Brokers said the global aviation insurance industry will remain well capitalised in spite of the latest losses.

Premiums are likely to remain low, they said, partly because underwriters benefit from less onerous capital requirements writing aviation insurance as the risks are uncorrelated with their other policies.

However, premium rises could be more pronounced in the niche aviation “war” corner of the market, analysts said.

As well as possible losses from the latest crash, recent fighting at Tripoli Airport in Libya is expected to trigger at least $200m worth of damages under these policies, according to a note from Barclays. It expected the losses should support aviation insurance pricing “on the margin”.

“Rates should start to harden,” said Mark Williamson at the stockbroker Peel Hunt in London. “They have been heading downwards for as long as I can remember.”

On Friday he downgraded his recommendation on the Lloyd's of London insurer Catlin because of its exposure to recent losses.

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