SOMPO INTERNATIONAL

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Navigating An Uncharted Aviation Market

The aviation sector was one of the first and hardest hit by the COVID-19 pandemic. During the three-month period of lockdown, air traffic dropped more than 90% compared to the same period in 2019, according to reports by S&P.

As the peak of the first wave of the virus appears to have passed in many countries, some governments have moved to open their borders slowly and selectively. But the path to air traffic recovery will not be short, even without the threat of a second wave of COVID-19 infections that could see lockdowns reintroduced. S&P now estimates that global passenger air traffic will decline by between 50% and 55% this year and that it will stay below pre-pandemic levels through to 2023.

Unmapped challenges

This is very much uncharted territory for the aviation sector. There has never been a situation where so many aircraft have been grounded for so long; many flights were suspended after 9/11 but that was for a matter of days rather than months. As a result, as lockdown eases and flights begin to resume, there is not an established playbook or past scenario to draw from as operations start up again. Meanwhile, the aviation sector faces a range of risks as it looks to get back towards something resembling business as usual.

As flights resume, pilots and support technicians who have not been active for a while could present risk issues particularly against a background of large job losses and low morale.

Airlines' risk profile changed from dynamic to static risk at the height of the lockdown while infrastructure risk for airports and air traffic control has obviously reduced during this period. However, it is important to note that this does not mean risk has gone away altogether. Parking aircraft is not simple. Considerable maintenance is required to keep the aircraft airworthy and safe. For example, the parking brake is hydraulic and needs to be reset regularly. In addition, a concentration of parked aircraft will inevitably lead to attritional losses, especially with third parties doing pushbacks who are not used to such a high concentration of aircraft. In one recent example, an investigation was launched after a collision between two planes on the tarmac at Aberdeen International Airport, where the nose of one of the aircraft ended up wedged under the engine of the other, lifting it off the ground.

At the height of the lockdown we had a situation where 60% of operational aircraft were stored, with 60% being wide-bodied exposure, according to Cirium data. Many of these were concentrated in natural catastrophe zones and quickly moving large numbers of aircraft in the event of a hurricane for example would be very difficult. It would be possible to move some to other locations but not all with availability of pilots being one issue.

As flights resume, pilots and support technicians who have not been active for a while could present risk issues particularly against a background of large job losses and low morale. The FAA estimates that around 75% of accidents are due to pilot error so it is vital that to get them ready to fly again. Some airlines may have been giving pilots time in simulators and rostering training flights so they can maintain their flying hours. However, this is very well regulated industry so maximum effort will be exerted to ensure safety standards are met before commercial flights resume.

A collaborative approach

Throughout the pandemic, insurers have been working with clients to provide interim relief on premium payments by reviewing their revenue profiles and trying to match their generation of income. But the new operating environment brings emerging risks such as insolvency. Although insurers are doing their best to reschedule premium payments against premium acceleration clauses in the event of an incident in order to protect both parties, policy holders need to remember that their insurers are not credit providers.

It is important to note that the airline insurance market relies on a certain income level for it to be sustainable.

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Catastrophic and large loss scenarios are priced on extended periods rather than annually. The fact that aircraft have not been operating anywhere near capacity for a relatively short period compared to the assumed extended periods applied to the pricing. But this will not significantly impact annual losses for airline insurance.

It is also clear that we need to move away from quasi financial metrics to measure risk as they are not aligned to large or Catastrophe level events. 'Fortuity' is what we insure, and it does not respect conveniently segmented time in the form of time defined in an insurance policy. Insurers need to work closely with their clients and brokers to help them to understand the issues. Together we will be able to redefine our methodologies and approach to risk in order to provide a more sustainable product that can be relied upon for the long term.

LEARN MORE

Our specialised underwriters, claims professionals and risk control specialists can help you address the exposures created by today's rapidly changing marketplace.

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A+
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