

It Is Coming and You Are In Its Path

By Thomas H. Chappell

Those of you who have read my articles over the years are fully aware the aviation insurance market is cyclical. When the market is overflowing with underwriters trying to increase or retain market share, rates and premiums decline. As underwriters see claims increasing and the losses begin to pile up, the underwriters' enthusiasm declines and premiums go up.

In the past, this has been the case for most market sectors except for the MU-2. Maligned by the flying community and avoided by much of the underwriting community, the MU-2 has rarely enjoyed the benefits of a typical soft insurance market. That is until the soft market of 2006. And, as with most less desirable general aviation market sectors, when we finally do get a bit of pricing relief from "soft market" pricing, it comes so close to the end of the cycle that many MU-2 owners never see the brief relief from their traditionally high rate structure.

Well, that is exactly the situation we are in now. The current general aviation soft market began in 2006 when a group of new aviation underwriters began to enter the market, buying market share and causing all sorts of discomfort for the legacy underwriters. The premiums started down. First the larger jet fleets and the corporate industrial aid risks benefited from the new market capacity and competition. Then the newer aircraft flown by the most experienced owner-operators realized improvements in rates and coverage. Then came the higher-end, single-engine turbines and the list goes on. It was not until mid-2008 that we began to see any real improvement in the premiums for the MU-2. And guess what? We are already seeing signs of a market that is cycling. Oh, you can tell. First the underwriters start to be less cooperative. Then they begin to object to older pilots and older aircraft. They become very selective in what they will write. Of course, those aircraft that have traditionally been considered to be less than desirable, such as the MU-2, become unacceptable again.

Here we are with less than a year of soft market performance for the MU-2 and we have just been told by one of the two primary markets for the MU-2 that they are moving rates up. Even if it costs market share, they plan to push for higher premiums on the MU-2. Is this justified? Yes it is but not for the reason you may be thinking. This time it is not the catastrophic losses that are the problem. It is the partial losses coupled with the relatively modest hull value of the MU-2 that may be pushing the premiums up.

All aircraft have partial losses. You know the seemingly insignificant hull loss that only costs \$60,000 to repair. When the total hull value is too small, the insurance rate per \$100 does not develop enough hull premium to begin to pay for these small partial losses. Forget the potential of the total loss.

Let's use the example of a 1 percent hull rate and an average hull value for the MU-2 of \$500,000. This aircraft would develop a \$5,000 annual hull premium. With an estimated U.S. fleet of 350 aircraft, a 1 percent average hull rate will generate a paltry \$1,750,000 in total fleet premium, or less than 30 partial losses, or three total losses. Well you get the message. It is not necessarily the catastrophic loss that is devastating to an underwriter; it could be the frequency of partial losses coupled with premium inadequacy that makes the MU-2 unprofitable. Obviously, higher average hull values will generate more total hull premium and enable lower hull rates. This is one reason that the King Air may receive a .5 percent hull rate while the MU-2 may be charged a 2.5 percent rate.

In recent years, the MU-2 has seen hull rates as high as 3.5 percent and as low as 1.5 percent. Obviously, there are exceptions to this sweeping statement. Exceptionally well-qualified operators, professionally flown aircraft, and large corporate fleets enjoy preferred rates. Again, they take advantage of generating larger premium dollars for the entire risk. Going forward, I cannot tell you what to expect other than to say you will see higher hull rates and more cautious underwriting on the liability side.

There is some good news, however, that may be a bit of a bright spot. Our agency has several underwriters that are not the traditional MU-2 underwriters that have selectively accepted some of our MU-2 clients. Why? I think that it is a combination of things. One is the improved loss experience that we believe to be the result of the SFAR training. A better trained stable of pilots will always pay off in better loss ratios and fewer losses –both partial and total. So the next time you feel a bit aggravated by having to comply with your SFAR training, remember your fleet of 350 fellow MU-2 owners are also becoming better pilots. Maybe someday, the MU-2 will achieve the reputation it deserves as a safe aircraft when flown correctly. ➔