Aircraft Leasing

Presentation by
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‘Airlines aren’t inherently profitable, but aircrafts are’

Tony Ryan, ex-CEO of GPA Group

1. The Players

- Airlines

✓ Flag Carriers
✓ Scheduled airlines
✓ Low-Cost airlines
✓ Charter airlines
✓ Freighter companies

1. The Players

- Manufacturers

✓ Large aircraft --- Boeing, Airbus
✓ Small aircraft --- Bombardier, ATR, British Aerospace, Embraer
✓ Corporate Jets --- Dassault, Learjet, Gulfstream
✓ Engines --- Pratt&Whitney, Rolls Royce, GE, SNECMA

1. The Players

- Providers of Finance

- ✓ Traditional bank debt
- ✓ Capital Markets
- ✓ Export Credit Agencies
- ✓ Manufacturers
- ✓ Hedge Funds/private equity
- ✓ Operating Lessors
- ✓ Insurance Companies and Arrangers

2. Common Financing Tools

- ✓ Secured Loan
- ✓ Operating Leases
- ✓ Finance Leases
- ✓ Tax Leases
- ✓ Sale and Leaseback
- ✓ Residual Value Guarantees
- ✓ Securitisation Products
- ✓ Export Credit
- ✓ Pre-Delivery Payment Facilities

3. Sources of Airline Finance

- Internal Finance

✓ these funds are generated from the cash retained in the business, or net profits (after paying interest, tax and dividends) but before providing for *depreciation.*

✓ deferred taxes and the profits from the sale of assets

✓ *the proportion of capital expenditure financed from internal sources is often called the self-financing ratio.*

3. Sources of Airline Finance

- External Finance

❖ <u>Short Term Loans</u>

✓ Bank Overdraft
✓ Short-term loans
✓ Trade Creditors

3. Sources of Airline Finance

❖ <u>Long Term Loans</u>

- ✓ Shareholder’s equity capital
- ✓ Preference share capital
- ✓ Convertible shares/bonds
- ✓ Bonds/debentures/unsecured loan stock
- ✓ Enhanced Equipment Trust Certificates (EETC’s)
- ✓ Term loans
- ✓ Manufacturer’s support

4. Aircraft Leasing

- *A lease is a contract whereby the owner of an asset (the lessor) grants to another party (the lessee) the exclusive rights to the use of the asset (the aircraft) for an agreed period of time, in return for the periodic payment of rent.*

4. Aircraft Leasing

- An aircraft lease is a contract between a lessor and a lessee such that the lessee:

- ✓ Selects the aircraft specification
- ✓ Makes specified payments to the lessor for an obligatory period
- ✓ Is granted exclusive use of the aircraft for that period
- ✓ Does not own the aircraft at any time during the lease term

4. Aircraft Leasing

- The *advantages* of leasing to airlines are:

- ✓ Volume discounts for aircraft purchase can be passed on to airline (better for smaller airlines)
- ✓ The conversion of an airline's working capital and credit capacity
- ✓ The provision of up to 100% of finance, with no deposits or pre-payments
- ✓ Shifting the obsolescence risk of aircraft to lessor (short term leases)
- ✓ No aircraft trading experience is needed
- ✓ The possibility of excluding lease finance from the balance sheet

4. Aircraft Leasing

- Possible disadvantages could be:

✓ A higher cost than, say, debt finance for purchase

✓ The profit from eventual sale of the aircraft going to the lessor (as title holder)

✓ Aircraft specification not tailor-made for lessee airline (short term leases)

4. Aircraft Leasing

- From a *lessor* point:

❖ Leasing is clearly advantageous to lenders, since it increases opportunities for business.

❖ The documentation for leasing is usually simpler than debt or equity financing

❖ The greatest disadvantage is the risk that insufficient care will be taken of the equipment

4. Aircraft Leasing

- **<u>Leasing types:</u>**

❖ Finance lease – *<u>form of acquisition finance/hire-purchase</u>*

✓ Often called as *full pay-out leases*
✓ Normal period of the lease is 10-12 years
✓ Right of use for limited period
✓ With (fixed price) purchase option
✓ Economic risks with lessee (repair, maintenance and insurance)
✓ Residual value of the aircraft not to be considered by Lessor

4. Aircraft Leasing

- Operating lease – ***<u>no desire to own the aircraft at any time</u>***

- ✓ Normal period of the lease can range from 1-7 years
- ✓ Right of use for limited period
- ✓ With or without purchase option
- ✓ Economic risk with lessor (risk of loss)
- ✓ Residual value of the aircraft is very important to lessor
- ✓ Dry lease -- lessee in full operational command
- ✓ Wet lease – wet lessor to provide crew and to arrange for flight operational matters (ACMI)

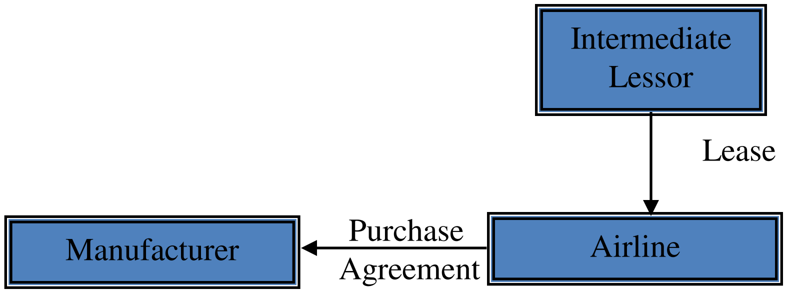
5. AVAILABLE STRUCTURES

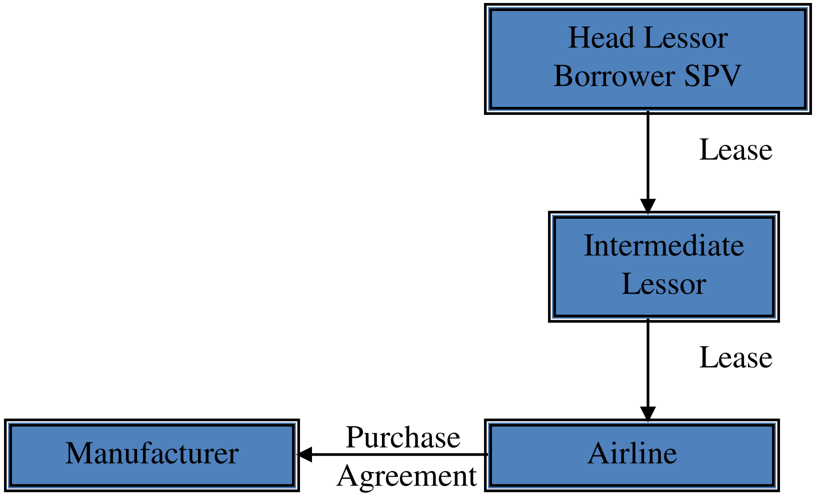
- ✓ “PLAIN VANILLA” ASSET BASED FINANCING
- ✓ GERMAN & FRENCH TAX LEASES
- ✓ ECA SUPPORTED FINANCE LEASE
- ✓ JAPANESE OPERATING LEASE
- ✓ SPANISH OPERATING LEASE
- ✓ ISLAMIC FINANCING
- ✓ THERE ARE OTHER STRUCTURES…..

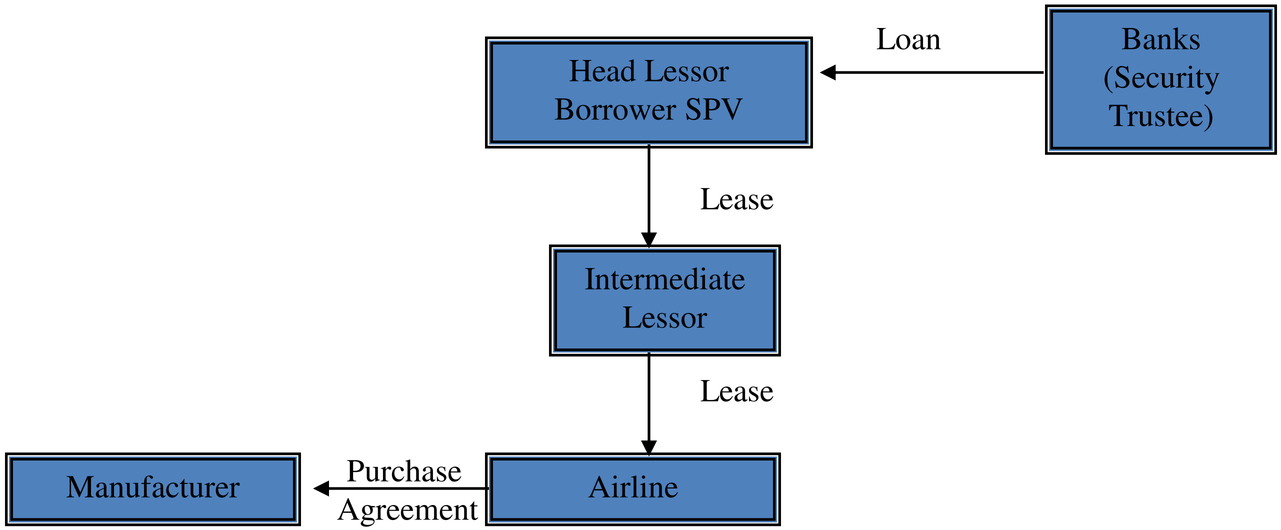
Bank Funding

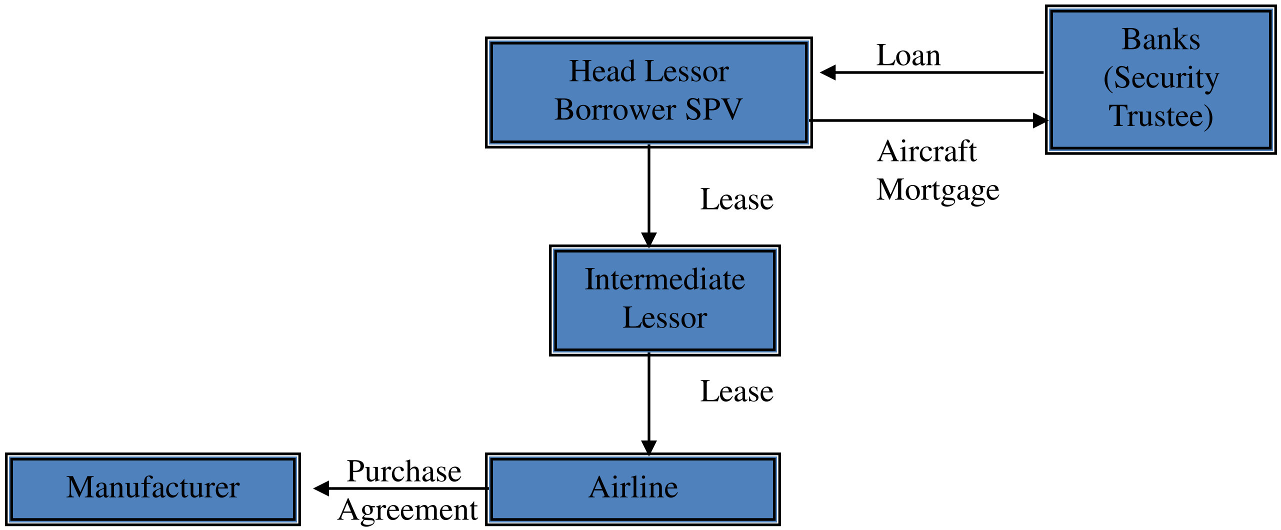
Airline

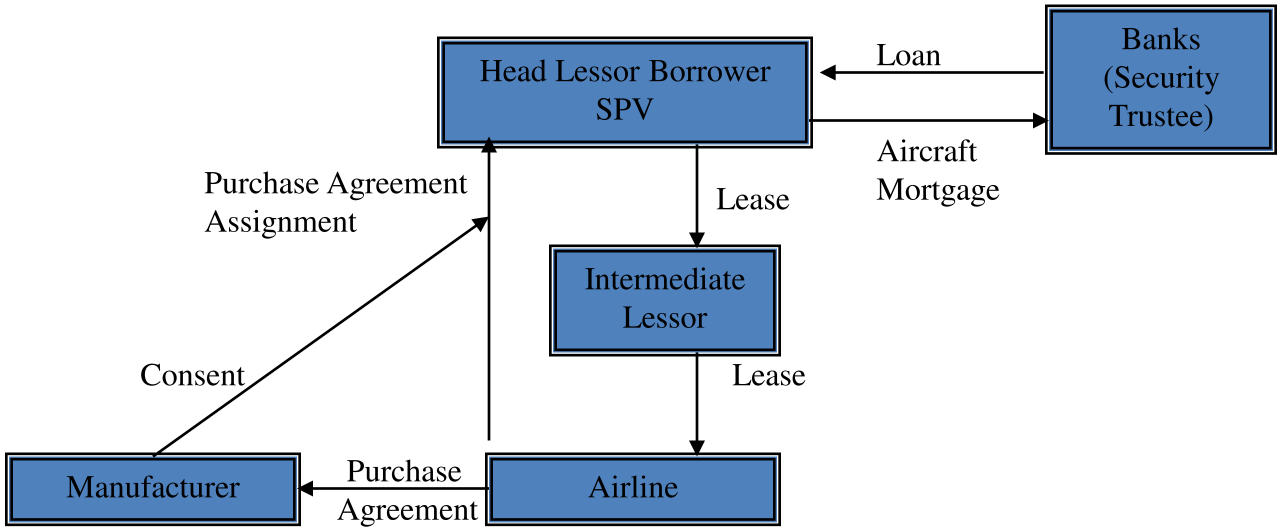

Manufacturer
Purchase
Agreement
Airline


Intermediate Lessor
Lease
Manufacturer
Purchase Agreement
Airline

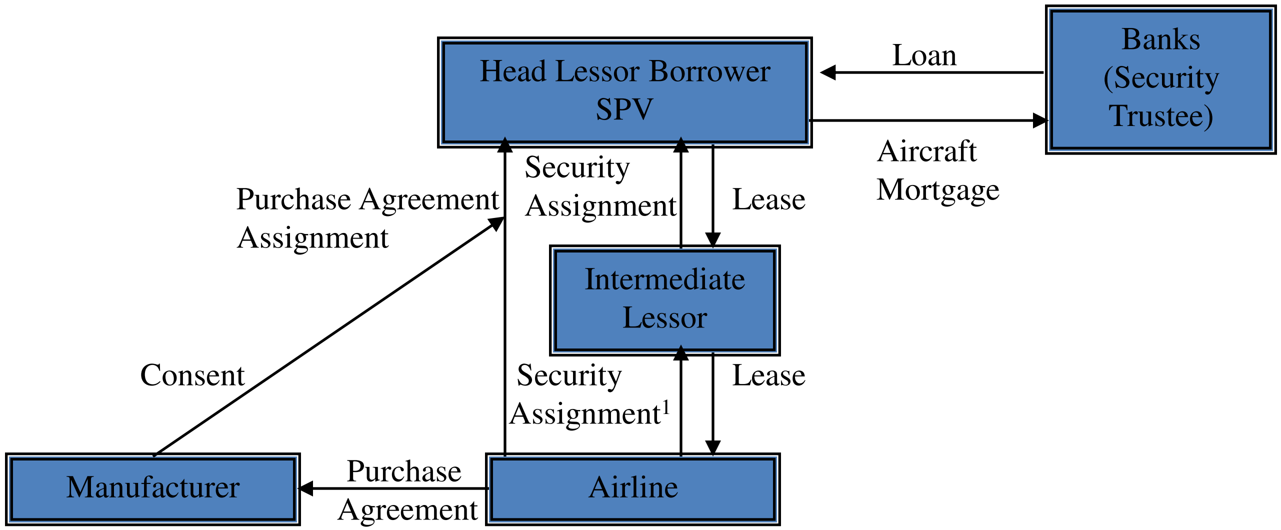

Head Lessor
Borrower SPV
Lease
Intermediate
Lessor
Lease
Manufacturer
Purchase
Agreement
Airline


Head Lessor
Borrower SPV
Loan
Banks
(Security
Trustee)
Lease
Intermediate
Lessor
Lease
Manufacturer
Purchase
Agreement
Airline

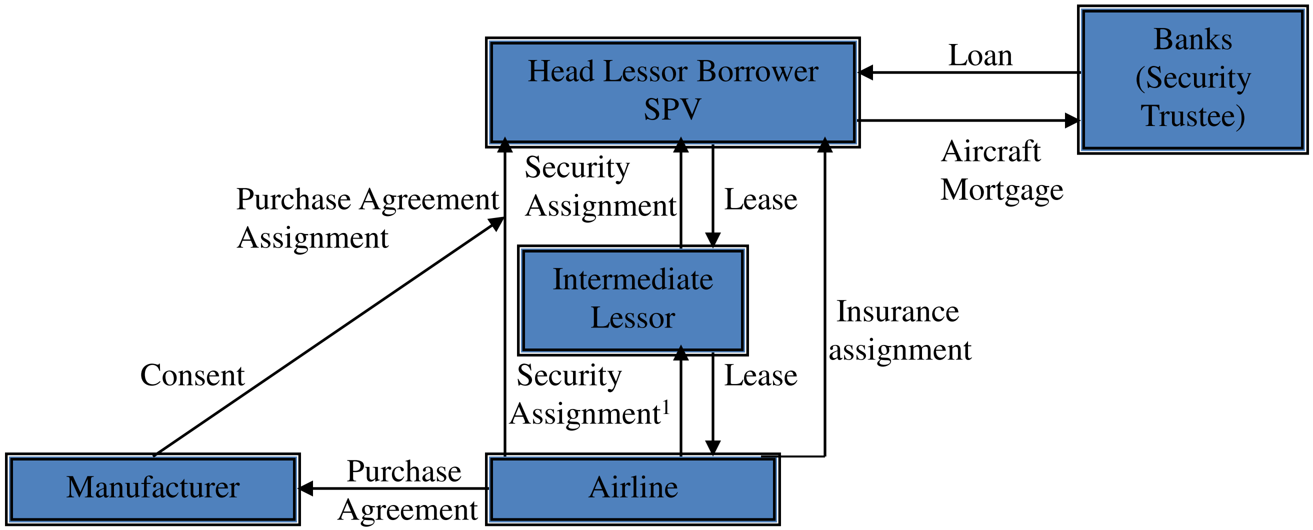

Head Lessor
Borrower SPV
Loan
Banks
(Security
Trustee)
Aircraft
Mortgage
Lease
Intermediate
Lessor
Lease
Manufacturer
Purchase
Agreement
Airline



Head Lessor Borrower SPV
Banks (Security Trustee)
Loan
Aircraft Mortgage
Lease
Purchase Agreement Assignment
Intermediate Lessor
Lease
Consent
Manufacturer
Purchase Agreement
Airline



[1](Insurances, Warranties, Requisition Proceeds, Subleases)



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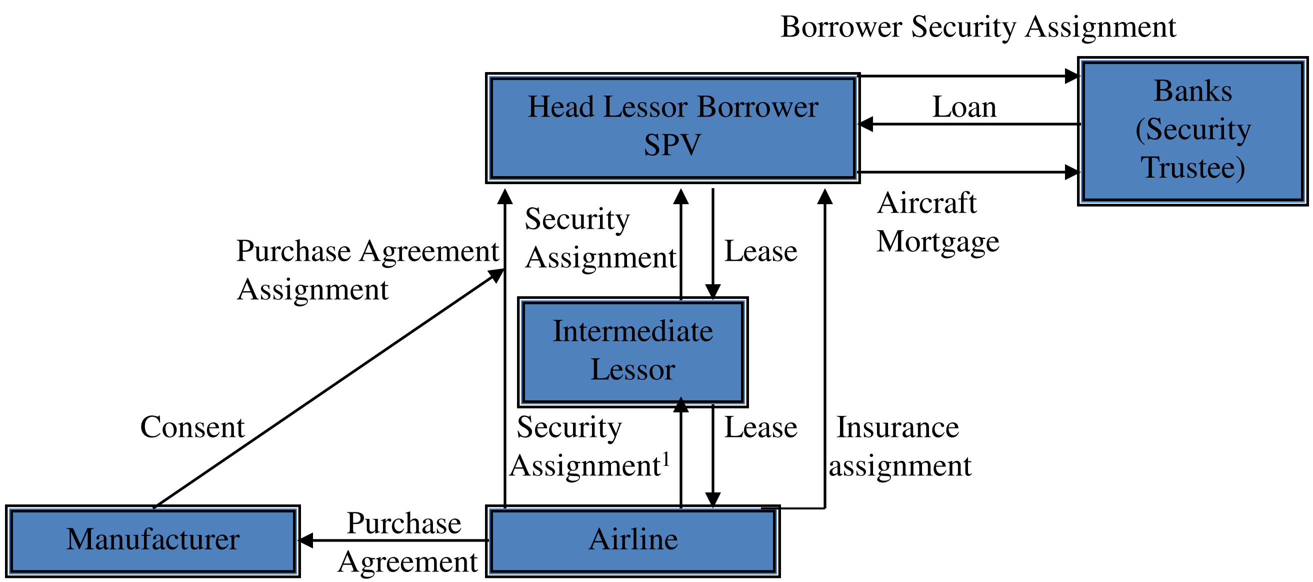

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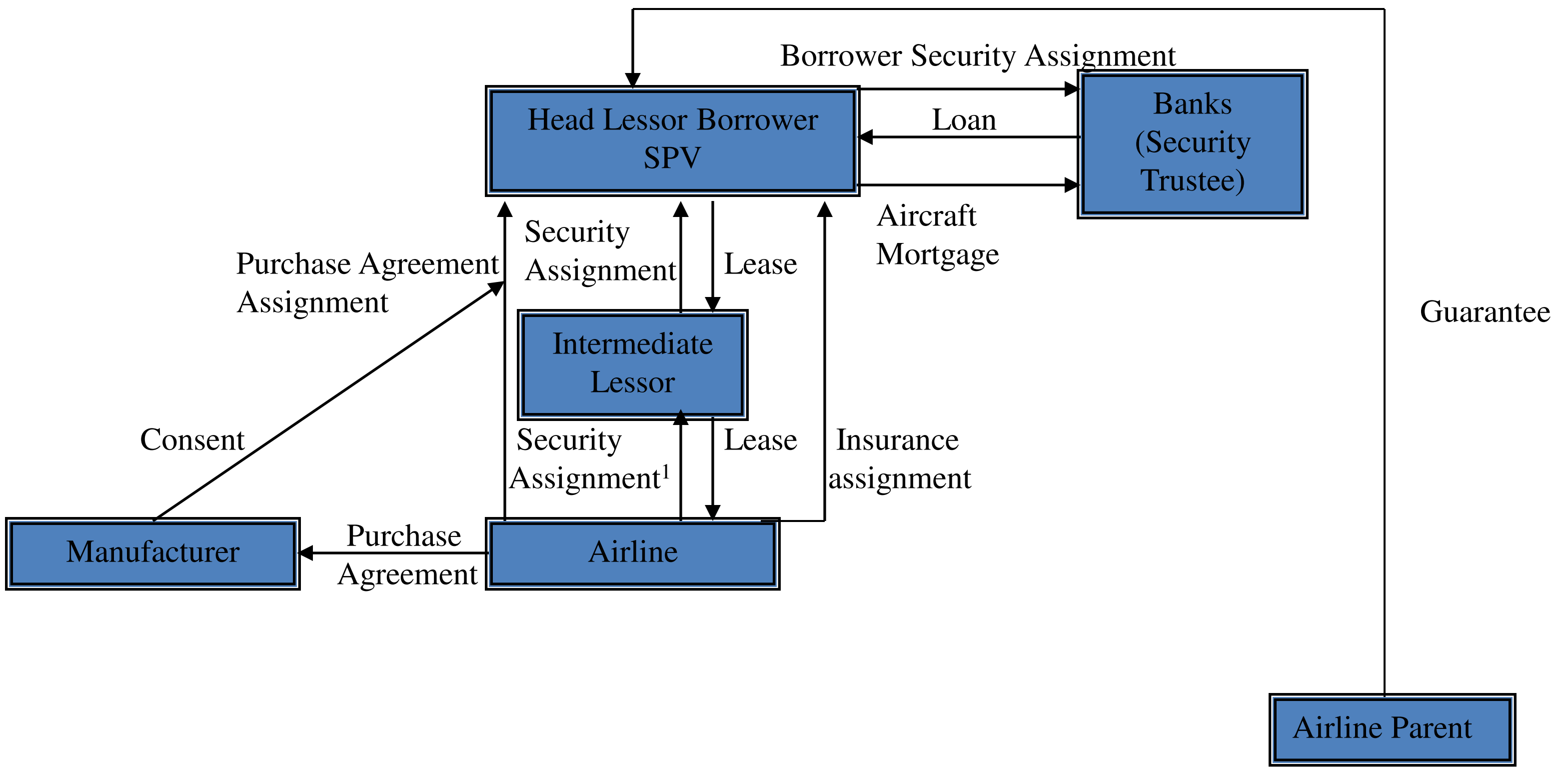

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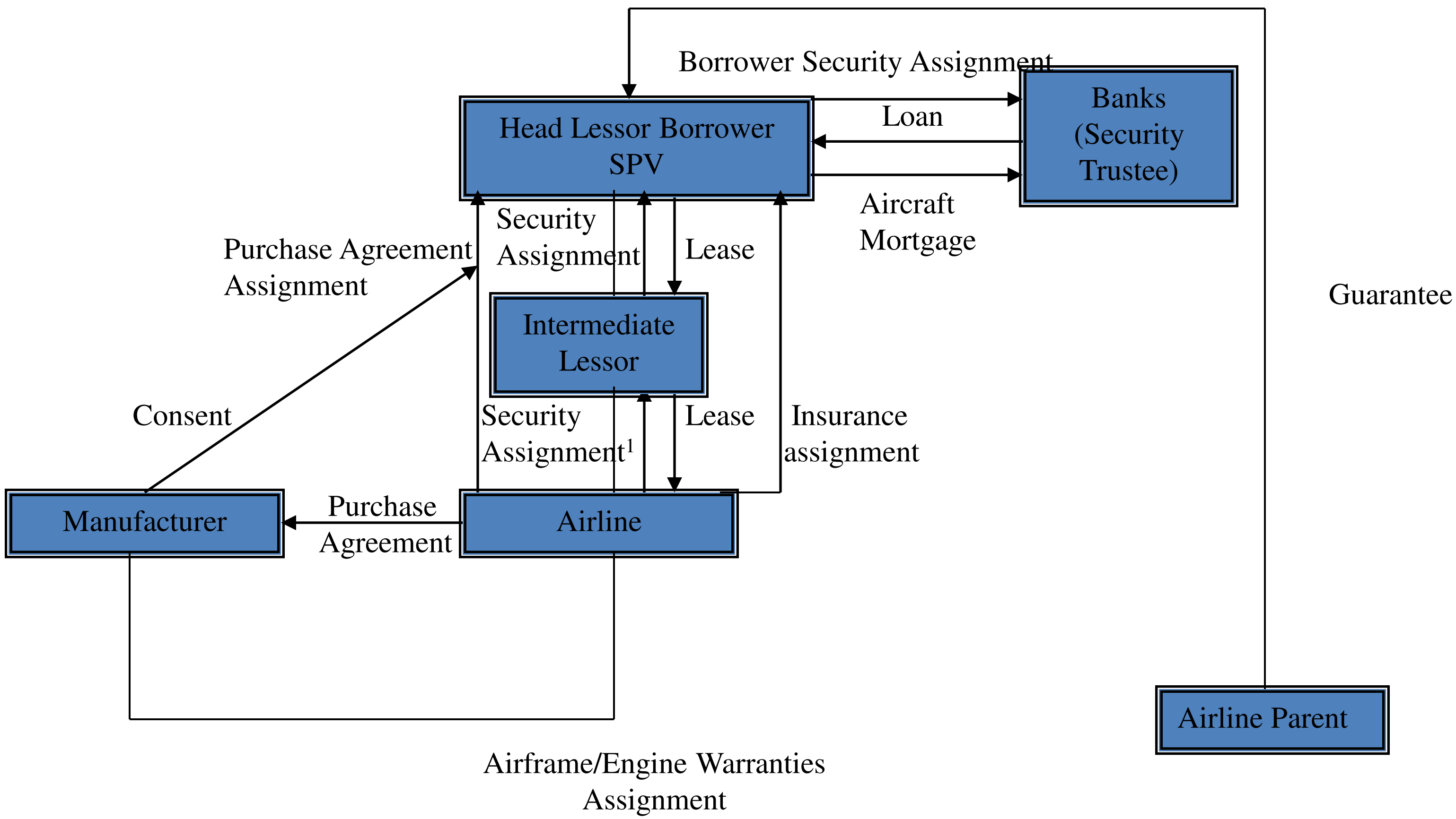

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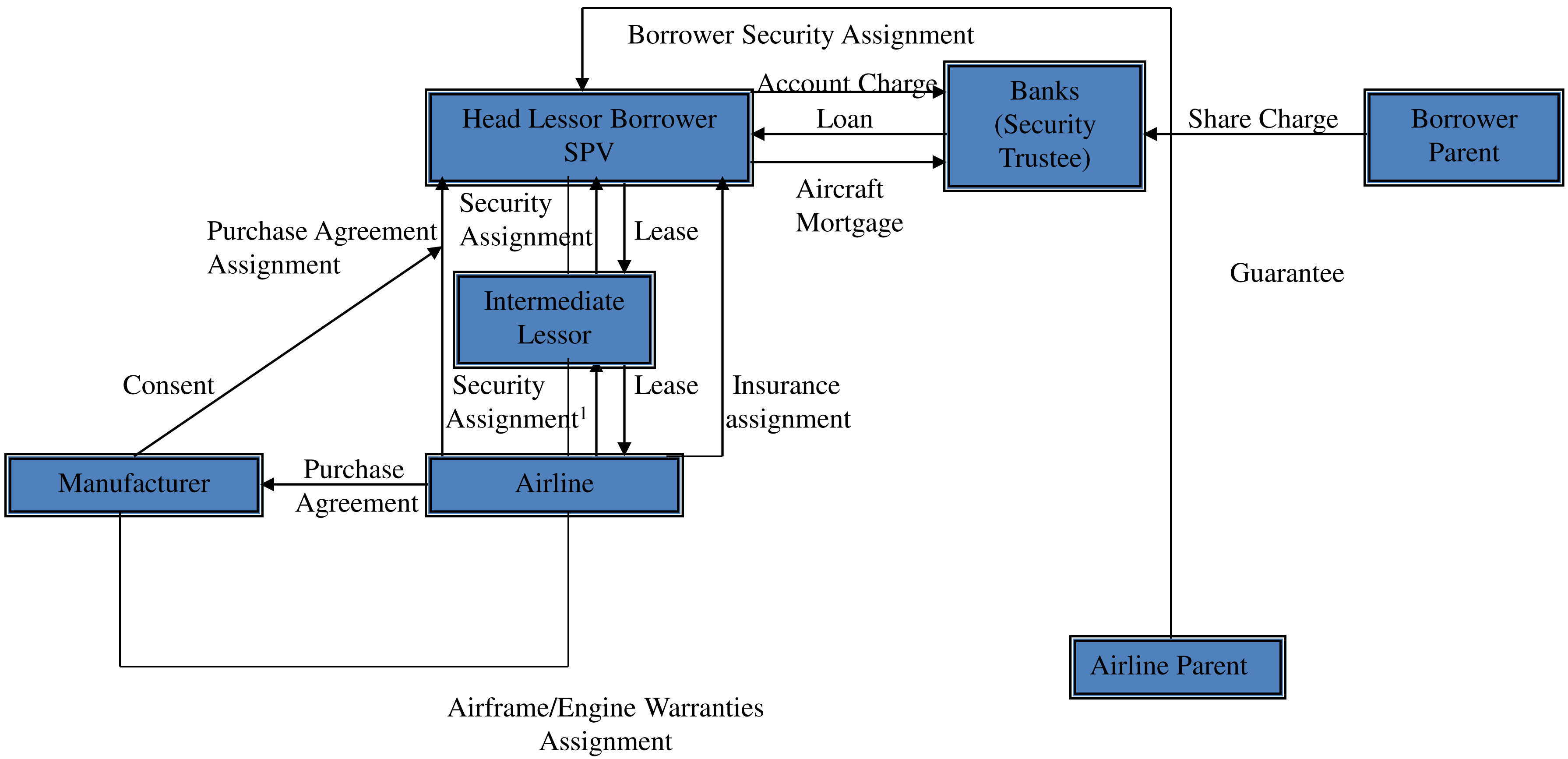

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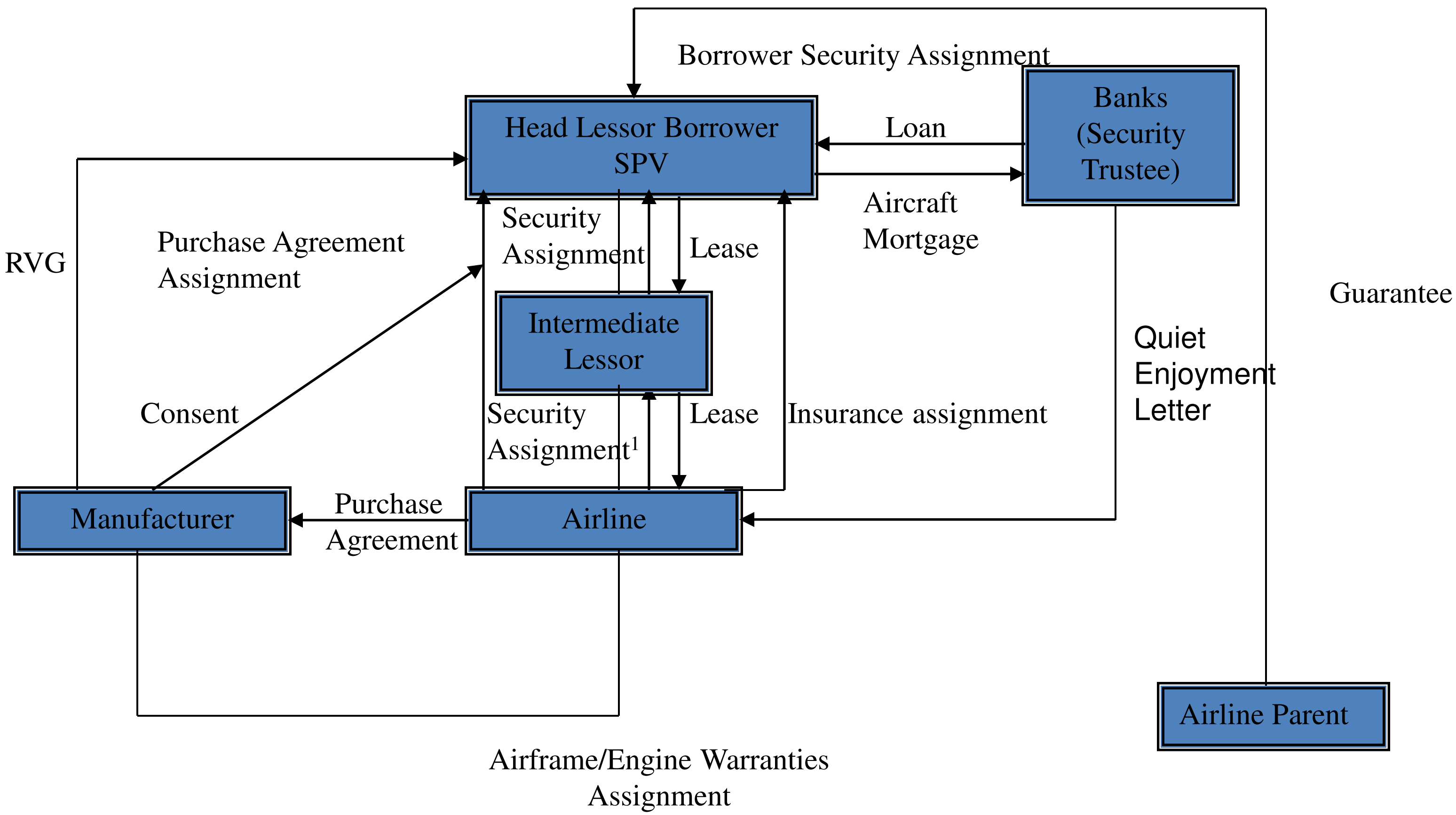

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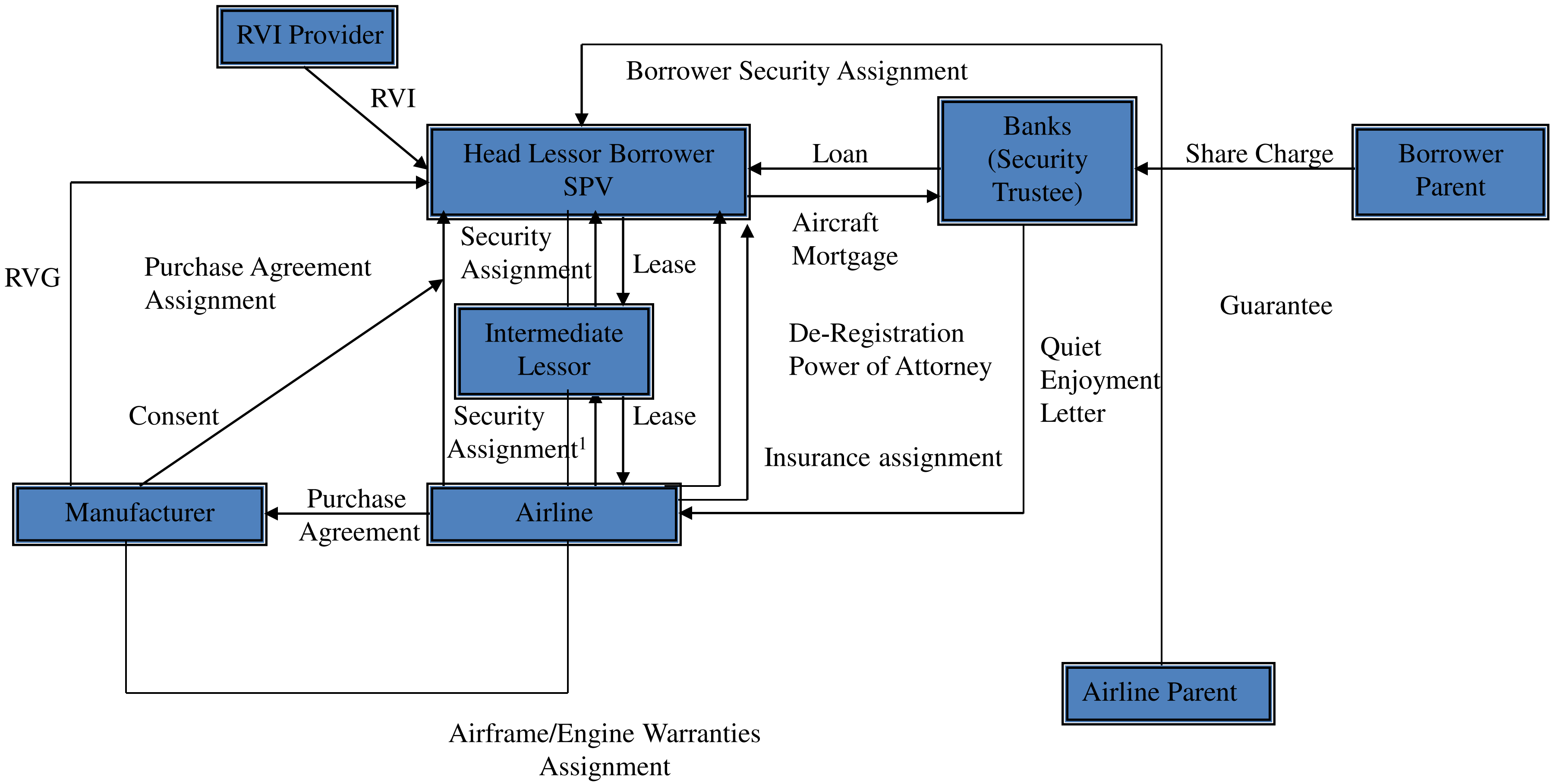

[1](Insurances, Warranties, Requisition Proceeds, Subleases)

6. Lease Agreement

- Important issues:

❖ Requirements at Lease Commencement and Termination
❖ Lessee Payment Obligations and Security
❖ Subleasing
❖ Repossession
❖ Governing Law and Jurisdiction

6. Lease Agreement

❖ Requirements at Lease Commencement and Termination

- ✓ Delivery Conditions
- ✓ Date of Delivery
- ✓ Acceptance and Inspection Flights
- ✓ Registration formalities
- ✓ Other registrations (loan or title)
- ✓ Conditions Precedent
- ✓ Return Conditions

6. Lease Agreement

❖ Lessee Payment Obligations and Security

✓ Lease Rent
✓ Security Deposit
✓ Maintenance Reserves

6. Lease Agreement

- Repossession

Prepare for termination of the lease and repossession of the aircraft

- ✓ Lessor should check, if all contractual formalities under the lease are observed
- ✓ Lessor should check the formalities connected to de-registration and re-registration of the aircraft

7. International Issues

- An airline based in India operates 1 aircraft;
- Aircraft is leased from a lessor based in Netherlands and SPC created in Ireland for tax purpose;
- The aircraft is financed by a bank based in UK and the mortgage is registered in UK;
- The engines are leased from a US company;
- 1 Engine failed in Netherlands and left at Schipol airport;
- Engine lessor wants to reposses the engine due to default in payment
- The Indian operator declared bankrupt when the aircraft is situated in Carribean Islands

7. International Issues

- Conflict of laws

❖ What is the applicable law?
❖ Common law Vs Civil law principles!!!
❖ Is there any international instrument to bring uniformity in asset-based financing?

7. International Issues

- Cape Town Convention – Objectives

✓ To provide for the creation of an international interest which will be recognized in all Contracting States

✓ to provide the creditor with a range of basic default remedies and, where there is evidence of default, a means of obtaining speedy interim relief pending final determination of its claim on the merits

7. International Issues

- ✓ To establish an electronic international register for the registration of international interests which will give notice of their existence to third parties and enable the creditor to preserve its priority against subsequently registered interests and against unregistered interests and debtor’s insolvency administrator
- ✓ To ensure through the relevant Protocol that the particular needs of the industry sector concerned are met

7. International Issues

- ✓ By these means to give intending creditors greater confidence in the decision to grant credit, enhance the credit rating of equipment receivables and reduce borrowing costs to the advantage of all interested parties.
- ✓ The Convention of Cape Town provides for legal certainty with regards to mobile equipment financing
- ✓ It brings uniformity concerning the property law and bankruptcy regimes of the contracting states

8. Conclusion

- The legal regime is uncertain
- Aircraft leasing is inherently very complex in nature
- Tax advisors, lawyers, financiers and many others in the aviation leasing field constantly strive to create new structures
- It is a multi billion dollar industry and every stone is unturned to save 0.0000001%, which in turn will help many airlines, lessors, financiers and manufacturer’s to run their business with out losses.

Thank you