

S&P Aviation Outlook: ISTAT EMEA

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Airlines

Global Airlines

Key Assumptions

1	<p>Global air traffic remains strong but growth is moderating</p> <p>Global air traffic (revenue passenger kilometers) expanding at around long-term trend of around 5%, fueled by generally satisfactory economic conditions, stable fuel prices, and the spread of low-cost (and low-fare) airlines. We expect growth to cool somewhat as airlines raise fares.</p>
2	<p>Oil prices ease from 2018 highs</p> <p>Fuel hedging cushions fluctuations some, mostly for non-U.S. airlines. U.S. airlines mostly raise fares to respond, but this occurs with a lag and relies on sufficiently healthy economic conditions. For airlines whose currencies fluctuate significantly against the dollar, oil and fuel prices may exhibit additional volatility.</p>
3	<p>Interest rates less of a risk but trade and FX more concerning</p> <p>The U.S. Fed decision to lower interest rate hikes pushes out upside risk, though most aircraft-backed debt is fixed rate anyway. Trade and geopolitical risks (e.g. U.S.-Iran) are rising. Worries about such threats generally pushes up the value of the U.S. \$, which increases pressure on some airlines, particularly in developing countries, who have to service aircraft-backed debt and buy fuel tied to \$.</p>

Airlines

Key Risks and Opportunities

1	<p>Geopolitical events could cause oil prices to spike</p> <p>A sudden price spike caused by a Middle Eastern crisis or other events could overcome airlines' ability to react particularly if it causes an economic slowdown. U.S. airlines are more exposed because of little fuel hedging, but have greater pricing power to raise fares. Separately, International Maritime Organization regulations mandating cleaner ship fuel could cause a temporary spike in prices of other fuels 4Q19-1Q20</p>
2	<p>Brexit causes a bumpy ride</p> <p>The U.K. will have to negotiate new bilateral aviation treaties. U.S. and U.K., and EU and U.K. have agreed on an interim agreements to avoid interruption of service. Airlines with EU operating certificate must be majority EU owned. Weakened £ hurts outbound UK travel demand.</p>
3	<p>“When the cycle turns”</p> <p>Airlines are in some ways better prepared but still cyclical. Global air traffic growth would likely slow but remain positive, but pricing would suffer and earnings drop significantly. Lower fuel prices would be a significant offset. We think that in a “normal” recession, the large U.S. airlines would remain profitable, a first.</p>

Peer Analysis - Selected Rated Airlines

		Financial Risk						
		minimal	modest	intermediate	significant	aggressive	highly leveraged	
Business Risk of Airlines*	satisfactory	excellent	 		 			
	fair	strong						
		satisfactory			 			
	weak	fair				 		
		weak					 	
vulnerable	vulnerable							

- investment grade

* not exposed to high risk countries

Assessments as of September 23, 2019

Aircraft Leasing

Aircraft Lessors

Sector Outlook:

- Global air traffic growth continues strong and above long-term trends
- Demand remains strong for narrowbody (single-aisle) planes, somewhat softer for widebody (twin-aisle)
- Oil price decline from several years ago has narrowed lease rate premium for fuel efficient new technology planes, but demand remains strong for them
- Lessors have so far managed bankruptcies and repossessions well
- Consolidation, aircraft portfolio sales

Credit Outlook:

- Relatively stable credit metrics forecast; all rating outlooks positive or stable
- Better asset/liability matching
- More unencumbered assets
- Rising interest rates should not present a problem, so long as they are not sudden and unexpected
- Potential Chinese tariffs on Boeing aircraft
- Potential impact of Boeing 737 MAX grounding
- Ample liquidity has driven up values and driven down lease rates; some risk of disruption when new entrants face a downturn with limited staff and experience

Aircraft Lessors Issuer Credit Ratings

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	Intermediate	Significant	Aggressive	Highly Leveraged
Excellent						
Strong						
Satisfactory			BOC Aviation Ltd. (A-)* Air Lease Corp. (BBB)	Aviation Capital Group Corp. (A-)* SMBC Aviation Capital Ltd. (A-)* AerCap Holdings N.V. (BBB-) Aircastle Ltd. (BBB-) Avolon Holdings Ltd. (BBB-) Dubai Aerospace Enterprise Ltd. (BB+)		
Fair					Fly Leasing Ltd. (BB-)	
Weak				Avation PLC (B+)	Voyager (Intrepid) (B+)	
Vulnerable						

As of 9/23/2019

* Incorporates three notches of parent support