HOW MUCH DOES OWNERSHIP REALLY COST AN INVESTOR?

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VP SUSTAINABILITY & STRATEGY

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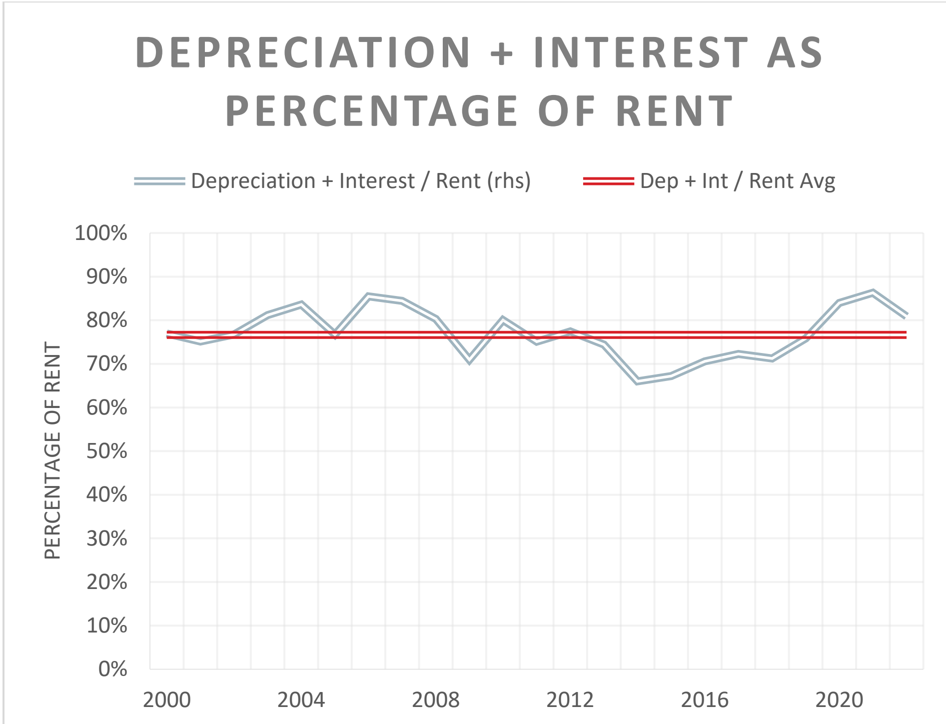
The cost of aircraft ownership plays a significant factor in investment decisions. In an aircraft leasing transaction, most of the rent paid by the airline goes towards aircraft depreciation and funding.

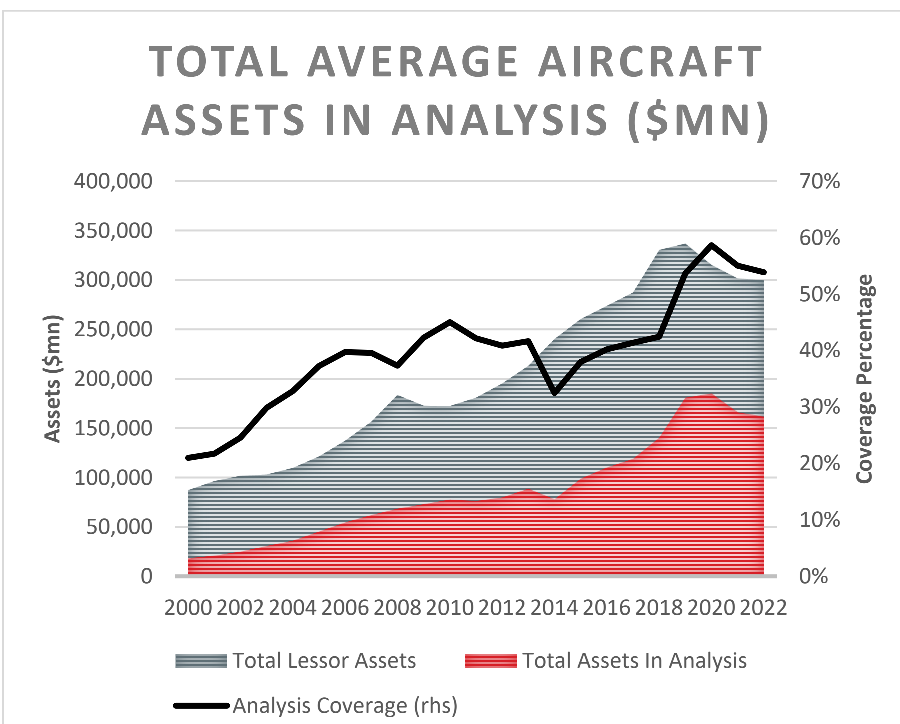
Source: Leasing companies' financial filings, mba analysis

Historically, leasing companies' asset yield (calculated by dividing rent by asset value) has been 10.0%, of which 76.0% went to pay debt and depreciation, which is why these components gather the most attention when deals are structured and analyzed. These two costs tend to be driven by external factors that are difficult to control. Financing costs are primarily a function of interest rates, whereas depreciation costs generally follow a standard depreciation policy that sees limited change from one leasing company to another. Financing and depreciation costs will be subjects of future mba Aviation's research papers as there are strategies lessors can employ to move the needle in their direction.



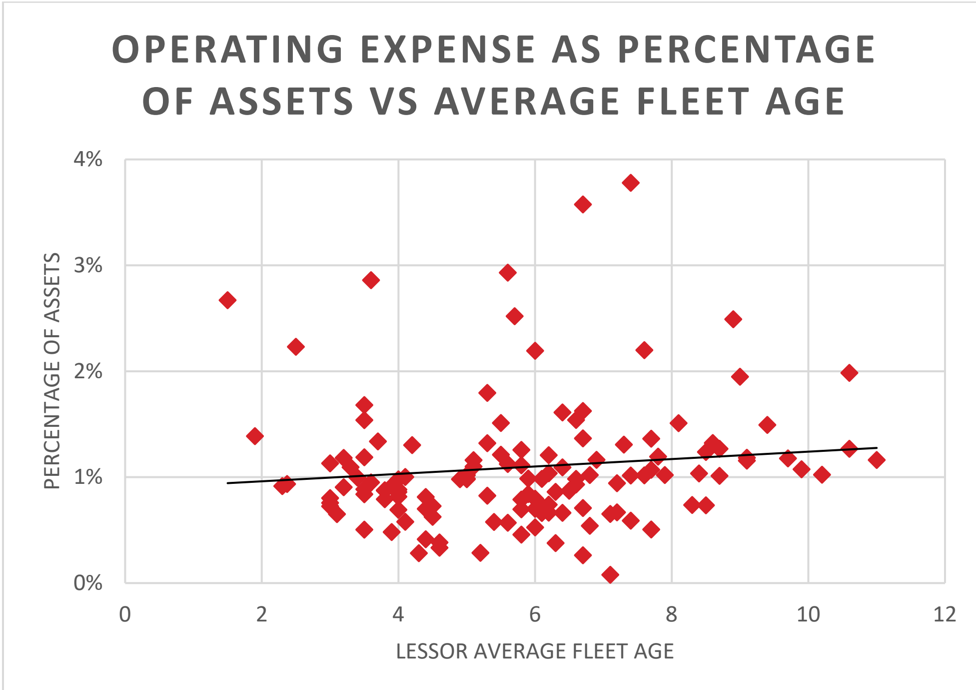
Source: Leasing companies' financial filings, mba analysis

Assembling a snapshot of every publicly available financial statement that an aircraft leasing company published over the last twenty years, mba Aviation can identify some unique business characteristics. The universe covered by this database is quite broad – each year since 2000 has, on average, nine leasing companies represented in the database, with asset sizes ranging from <$1bn to >$60bn. The total number of assets covered by the database reached almost $200bn at its peak in 2020. On average, the analysis covers 40.0% of all leased assets in history. This wide net can be used to provide us with a representative analysis of the industry and come up with relatively sound conclusions.



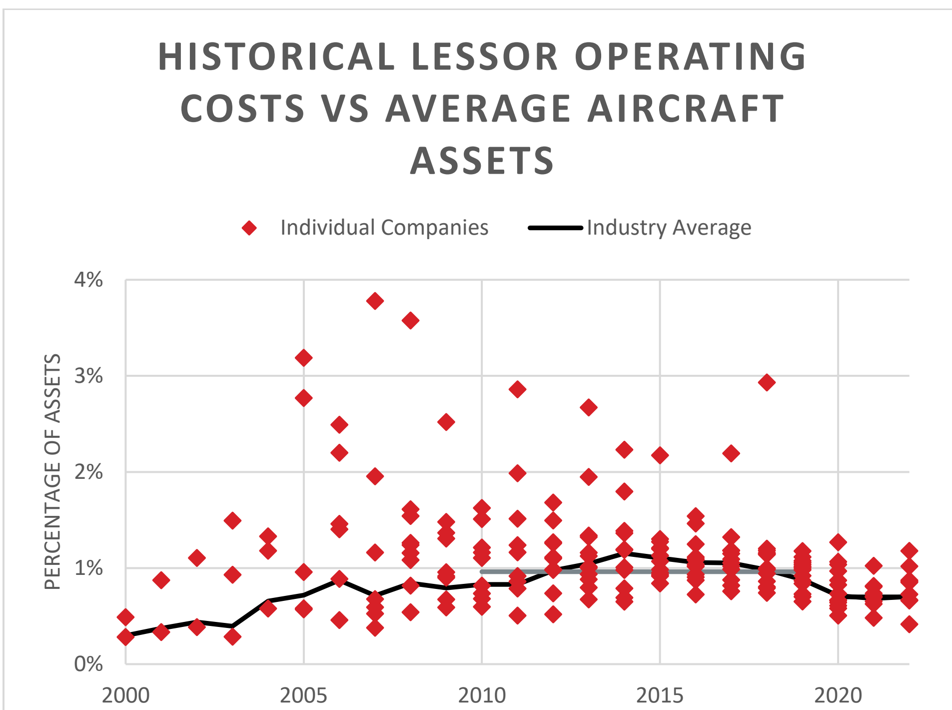
Source: Leasing companies' financial filings, mba analysis

Focusing on the operating costs, a significant variability is observed across the data sample on an individual company basis. Individual strategy can often explain much of the divergence; for example, a lessor specializing in older assets will have lower book values and require additional aircraft management expenses, generally compensated by an increase in average aircraft rental yield.



Source: Leasing companies' financial filings, mba analysis

The industry has been running steadily on costs– at least pre-pandemic, and in the 11 years between the GFC and the COVID pandemic, lessor operating costs averaged ca. 1.0% of assets.



Source: Leasing companies' financial filings, mba analysis.

mba Aviation has seen a significant shift in those costs since the pandemic as lessors were forced to curtail their travel budgets and other costs. The operating costs have averaged 0.7% since the pandemic, compared to the pre-pandemic 1.0% average. Not enough companies' financial statements provide travel expense information with a sufficient level of detail to make this statement definitive but given the fact that travel costs are responsible for roughly 40.0% of all operating expenses, a significant slowdown of travel could be enough for a 30.0% movement in average operating costs for the whole industry. It remains to be seen if this shift has become permanent, as a 30bps change in total costs would significantly boost lessor ROEs (1.2p.p. increase assuming 75% leverage). Staff costs will also have a significant impact – bonus deferrals and hiring freezes introduced during the pandemic have helped keep the costs down, but that may be temporary relief. Outsourcing some of the functions, especially for smaller or newer lessors, might help keep costs below the 1.0% average.

This recent behavior highlights the importance of operating costs when leasing aircraft, especially for smaller lessors where asset size does not allow for significant spending from the bottom line. One way to curtail that spending is to outsource tasks to experts who can streamline deliverables and use their economies of scale to offer cheaper solutions.

If you have any questions or comments or would like to discuss any of the above topics in more detail, please contact the mba Aviation team at mba@mba.aero