AVOLON: LESSOR ORDERBOOKS TO BE IN HIGH DEMAND

News / Finance

The value of new aircraft deliveries is expected to rise by over 15% to c.US$100 billion in 2024, according to a paper published today by Avolon, a leading global aviation finance company. The delivery of over 1,450 new large commercial aircraft will help drive airlines' passenger revenues up 12% to US$717 billion. Airlines' net profit is projected to rise by 10% to US$26 billion. 4.7 billion people are expected to fly in 2024, more than any year in history. Aircraft values and lease rates rose sharply in 2023 as a structural undersupply of both narrowbodies and widebodies was reflected in the market, and further increases are expected in 2024.

India, Saudi Arabia, and the UAE are emerging as key drivers of growth. Airlines and lessors that waited to commit to new orders to source new aircraft risk waiting into the next decade for supply. Domestic airline capacity has reached 106% of 2019-levels globally, whilst the international recovery lags slightly, at around 95%, largely due the slower than anticipated rebound in the

Chinese market and the knock-on impact this has had on previously busy routes in Southeast Asia.

Avolon 2024 Outlook: New Horizons paper, available here reviews the major trends in the aviation sector including the key findings:

- **Airlines:** In 2023 airline revenues accelerated 22% compared to a 3% rise in global GDP. A return to positive cashflows has enabled airlines to repay US$57 billion of government debt provided during the pandemic. The continued reopening of Chinese international travel will provide positive momentum for airlines through the year.
- **Manufacturers:** The undersupply of aircraft will take years to unwind, increasing the value of delivered aircraft, and extending their economic lives. The widebody production recovery is lagging behind narrowbodies resulting in a tighter market and longer wait times for twin-aisle aircraft.
- **Lessors:** With both aircraft and capital in short supply, the role of lessors is strengthening. Investment grade lessors that have secured attractive new aircraft orderbooks are best positioned for the years ahead. Market lease rates took time to adjust to higher interest rates, but they have risen as much as 35% in 2023 with further growth expected this year.
- **Innovation & Sustainability:** Momentum behind sustainable aviation fuel (SAF) is building and an estimated US$2 trillion of investment is required to scale up production to levels required to hit net zero goals. Flying will get more expensive this decade as airlines face tighter labour markets, increasing sustainability pressures, and engine durability challenges.
- **Risks:** The macroeconomic outlook is normalizing as inflation trends downwards, but softer demand threatens in the U.S. and potentially Europe. Political risk will be in focus in 2024, with conflicts in the Ukraine and the Middle East and ongoing tensions between China and the West. The production ramp up by OEMs is vulnerable to supply chain pressure and regulatory oversight.

Andy Cronin, CEO of Avolon, commented: “The economic and social benefits of travelling will continue to drive aviation and underpin the resilience of our sector. Airlines’ growth in 2024 will be supported by around US$100 billion in new aircraft deliveries, with lessor orderbooks and capital supporting fleet expansion plans. While geopolitical and economic risks remain, the market backdrop as we start the year is likely to drive lease rates and residual values higher.”

Jim Morrison, Chief Risk Officer of Avolon, said: “India, China and the Middle East are driving aviation’s growth. A structural undersupply of both narrowbodies and widebodies will take years to unwind. While new aircraft designs with step-change improvements in energy consumption will ultimately be required to decarbonise, in the short-term the industry must focus on scaling up sustainable aviation fuel production.”

The paper - co-authored by Avolon’s Chief Risk Officer, Jim Morrison, and SVP Portfolio Strategy, Marc Tembleque-Vilalta – makes eight forecasts:

Fearless Forecasts 2024

1.Engine-related AOGs peak in June

New technology engine durability challenges have been major disruptions to airline operations. Design and production quality issues will continue to persist in the fleet for years, but the operational impact will diminish following the peak mid-year.

2.Four airline mergers close. Four don’t pass regulatory approval.

Mergers can provide synergies, reducing overhead and increasing revenue potential, but sometimes at the expense of passenger choice and affordability. Several of the dozen or so currently proposed mergers will be approved, but some will be blocked, as seen by the recent US court decision on the JetBlue-Spirit merger.

3.More new aircraft deliver to China than any year this decade

Boeing’s first 787 delivery to China in four years in December 2023 marked the re-opening of a key export market. 737 MAX deliveries will follow as Chinese airlines need to access new aircraft to renew their fleets and return to growth. China is too big a market to not be a priority for Boeing and Airbus.

4.Widebody production skylines will sell out to the end of the decade

Mega-orders have filled up the manufacturers’ skylines. Asian airlines late to order risk missing out. The remaining slots will soon be sold, leading to increased demand for lessor slots and used widebodies.

5. At least two new passenger aircraft variants will be certified in 2024

Likely candidates to enter service are the Airbus A321XLR and the Boeing 737-7. The 737-10 and 777-9 act as further stretch targets to our forecast.

6. The next clean-sheet large commercial aircraft enters service in 2036

Given the 10-years plus it will take from program green light to certification, Boeing and Airbus will need to commit to their next designs soon. No new clean-sheet designs for the next decade protects the investment case of today’s new-technology aircraft.

7. Two investment grade lessors receive rating upgrades, again

Investment grade is a key differentiator for scale lessors. Rating agencies will continue to acknowledge the resilience of the lessor business model with ratings upgrades.

8. A global framework for a SAF book-and-claim system is agreed

Airlines and lessors will have access to verified SAF credits enabling them to leverage SAF without having to transport liquid fuels over long distances. Agreeing a framework will attract the capital required to kick-start SAF production.

28 JANUARY 2024

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