OPINION: FOUR FINANCE LESSONS FROM DUBLIN

News / Finance

Last week, two major events in Dublin brought the biggest guns from the aviation finance community together to swap notes, debate the major issues and assess the outlook for 2016. Flightglobal – as ever – was close to the action, and these are four key themes we believe will set the agenda for the industry for the year ahead.

1. This is (still) as good as it gets

At last year's Airline Economics Global Frontiers conference, our chief economist Peter Morris declared that "this is as good as it gets" for the industry. One year on, our view has not changed. In a keynote speech this time, Morris told delegates that oil prices were not – as some feared – deterring airlines from ordering new fuel-efficient aircraft, and he sees little prospect of that changing even if prices stay low. Instead, carriers are enjoying a double windfall of new, more economical aircraft – including the A320neo and 737 Max – becoming available at the same time as tumbling fuel costs make opening up previously marginal routes more viable (of which more later). And while falling oil revenues may be impacting several formerly turbocharged economies, cheaper fuel is also helping to boost the disposable incomes of many consumers. Airbus and Boeing saw a fall in orders in 2015, but the previous year's bumper numbers were more to do with the wave of early adopters buying into latest-generation aircraft programmes than with a peaking of demand. We do not see any evidence of widescale order cancellations or deferrals as airlines decide to hold onto older equipment. The commercial airliner backlog remains at a record high and – even with Airbus and Boeing deliveries ramping up – we do not foresee that eroding significantly over 2016 and into 2017.

2. Low oil prices create opportunities

After oil prices peaked in 2008, airlines endured several years of pain. Now that prices have plummeted – and show little short-term sign of rebounding to the highs of the previous decade – carriers are making hay. But while the industry has returned to profitability, operators have largely resisted the temptation to discount on fares and have instead focused on using their improved

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liquidity to expand capacity by introducing new routes and frequencies. This has, in turn, helped to feed demand for equipment, and we see this continuing through this year.

3. There is no sign that the sea of capital is drying up

Over the past few years, investors have in increasing numbers turned to commercial aircraft assets, drawn by their strong residual value performance and attractive potential returns compared with alternative asset classes. The industry continues to remain attractive for the world's money. The consensus from Dublin was that despite headwinds in the global economy generally, there was little sign of liquidity drying up in the capital markets, with continued confidence about investment returns from aviation. We forecast no major consolidation in the leasing market in the coming 12 months with plenty providers chasing every deal and giving airlines access to reasonably cheap finance. Conversely for investors, competition will continue to remain strong, and margins will thus continue to be pressured.

4. There might be a secondary market for the A380

Perhaps one of the biggest surprises going into 2016 is evidence of a secondary market for the A380, despite Airbus's ongoing struggles to find customers for production-line versions of its largest widebody. IAG chief executive Willie Walsh's revelation at the Airline Economics Global Frontiers event that British Airways was looking to add "five or six" leased second-hand superjumbos, with Iberia interested too, makes the UK-based group the first major operator to express an interest in tapping the secondary market for A380s, early examples of which should become available in the next 30 months or so. For Airbus, the problem remains shifting new A380s. With the airframer having secured just two net orders in 2015, the backlog is reducing fast, and a new A380 remains an expensive proposition for many airlines. Walsh – who describes the type as a "fantastic but inflexible" aircraft – has said again that BA will not be exercising its options for new A380s at the price being offered by Airbus. Toulouse, in turn, cannot discount without prolonging the programme's break-even point. However, one stumbling block to the viability of the secondary market remains the cost of refurbishing such a big aircraft, which must be deducted from the selling price. If costs are in the several tens of millions, it will significantly add to the on-ramp cost to the operator.

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