The first A380 has been broke for parts, and is just 11 years old. This was after failure to re-lease it, indicating weak demand for the type.

First A380 parted-out as final option for investors

The first A380, an early version of the aircraft, has been dismantled and will be sold as spare parts. A new lessee or buyer could not be found following expiry of the 10-year lease to Singapore Airlines (SIA) in October 2017.

While original investors in the aircraft will not lose money, the return on investment is likely to be more modest than original expectations.

In the past 10 years more than half of retail investments in German aircraft funds were devoted to the A380.

The aircraft is owned by DS 129, a closed-end fund launched in 2007 by fund provider Dr Peters. A closed-end fund raises a prescribed amount of capital for an investment, in this case a single A380 aircraft.

The yield on a closed-end aircraft fund is essentially derived from two sources: income generated from aircraft leasing, and disposal of the asset once the fund matures.

While none of the lessees have defaulted on lease payments, giving investors a regular revenue stream, proceeds from disposal of the A380 has been the decisive factor in assessing how good an investment the superjumbo has been. If A380 aircraft could be sold for a good price at lease expiry, investors would receive a high final pay-out.

Unfortunately, there is almost no demand for the A380 in the secondary market, and operators have opted not to re-lease the aircraft at the expiry of the initial lease.

Management of the DS 129 closed-end fund that owns the aircraft, and which leased it to SIA, outlined three scenarios, with possible sale revenues of between $64 million and $74 million.

Investors should receive payouts in 2019 and 2020, following repayment of the remaining senior loans.

"On the plus side, even the most pessimistic scenario presented by Dr Peters should result in positive returns for investors, albeit well below the 7% to 8% annual returns anticipated at the time of the fund's launch," said Frank Netscher, associate director for alternative investments at Scope, in a report. "But while investors are unlikely to suffer losses, the scenarios outlined are uncertain because no A380 has yet been parted-out."

Additionally, the fund's term in all three scenarios has been reduced by four years compared with the originally planned term. Secondary investors in closed-end funds are also reacting to the decision to part-out.

Sale of components

Leasing of engines provisionally secures liquidity and debt service. The engines, however, were leased to manufacturer Rolls-Royce, so liquidity and scheduled debt repayments are secure for the time being.

Nevertheless, this solution provided no cost-covering and, therefore, is not a long-term solution because of debt service yet to be performed on the bank loans.

Fund management had three options:

- Lease the A380 to an airline
- Sell the aircraft
- Sell the aircraft in individual parts (part-out).

According to Dr Peters, no new lessee could be found at short notice; potential lessees either had no current demand for the A380 or were unable to present a convincing plan.

It was also not possible to sell the A380. The option to sell the aircraft in parts was presented to investors as the only viable alternative.

DS 129 shareholders, and those of its equally affected sister fund, agreed to part-out the A380 by overwhelming majorities, that is, more than 99%.

The decision to part-out means the engine lease agreement with Rolls-Royce will be extended until the end of 2020 under existing conditions, after which the engines will be sold.

The rest of the A380's components are also expected to be sold by the end of 2020.

The fund's management has outlined three possible capital return scenarios:

- Scenario A: Sales revenues of $64 million ($40 million from sale of the components, in addition to four x $6 million from sale of the engines).
- Scenario B: Sales revenues of $69

The ex-SIA A380 that has been parted out was an early-built model, having entered service in 2007. The aircraft was just 10 years old, but could not be re-marketed to another airline.

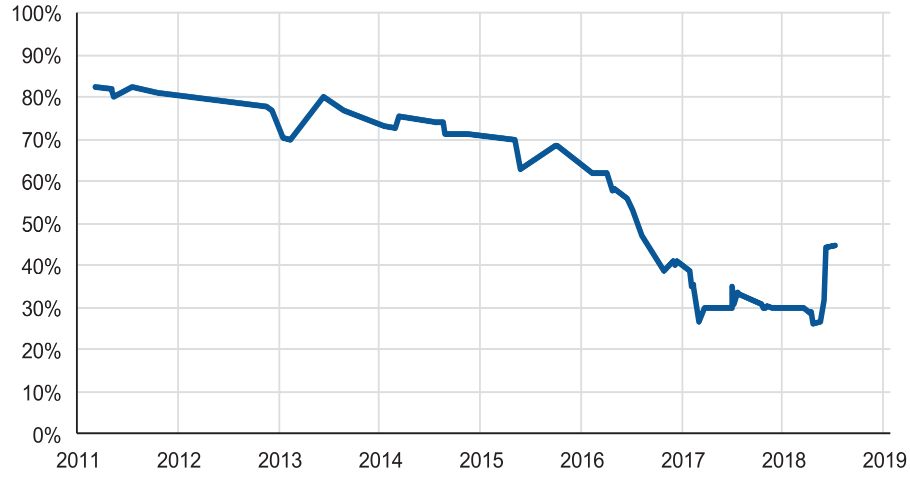
million ($45 million from sale of the components, in addition to four x $6 million from sale of the engines).

- Scenario C: Sales revenues of $74 million ($50 million from sale of the components, in addition to four x $6 million from sale of the engines).

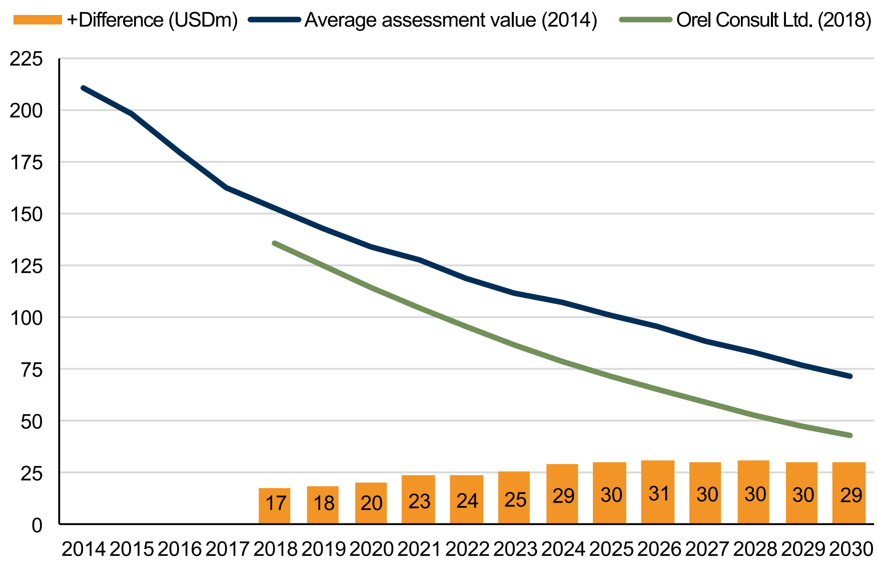
Should the weakest (A) of the three scenarios occur (distributions of 14.5% in 2019 and 53.25% in 2020), secondary market investors could still expect a very high gross return, even at an entry price of 45% in July 2018 (at the current annual level of around 20%).

The parting out of the aircraft shows that the market still lacks sufficient historical values to validly estimate prices for A380 components.

A380 fund historical price performance



Difference between 2014 & 2018 A380 valuations



A380 valuations fall further

The challenge presented by the lack of historical values concerns not only individual components, but also the whole A380 aircraft. The chart shows the forecast future base values of a significantly newer A380 built in 2014. The A380 that was parted-out was built in 2007.

The chart shows that expert valuations have fallen in the past four years, even though views on the A380 had turned gloomy by 2014 and there was a strong sense that the aircraft would not match original expectations.

This was considered in the evaluations at the time. Expert assessments from 2007 would have assumed more positive developments.

The chart shows both the average value from three assessments in 2014, as well as the current valuation for the same aircraft from July 2018.

The bars in the graphic show the differences between the two time series in millions of US dollars.

Assuming a typically-structured financing for this A380, equity capital of around $100 million can be expected. The difference between the time series, therefore, shows a possible pay-out difference of up to 31% for investors in the event of the sale of the aircraft.

A380 history

The A380 made its first flight on 27 April 2005, and entered commercial service on 25 October 2007 with SIA, between Sydney and Singapore Airlines (SIA). SIA placed orders for 24 A380 aircraft, all of which have been delivered.

Dubai-based Emirates was the second airline to receive the A380, and commenced service between Dubai and New York in August 2008.

Emirates is the biggest A380 customer, with 162 ordered of which 104 have been delivered.

Australian flag carrier Qantas followed, with flights between Melbourne and Los Angeles in October 2008. Qantas placed orders for 12 A380 aircraft, all of which have been delivered.

As of July 2018, Airbus had received 331 firm orders and delivered 229 A380s.

Emirates A380 lifeline

The UAE carrier threw the A380 a lifeline by committing to purchase 20 more of the aircraft, with an options for 16 more, in January 2018, in a deal worth up to $15 billion.

While the overall order is significant, Airbus had pinned its hopes on a firm order for the 36 A380s. Deliveries of the firm order aircraft are scheduled to begin in 2020.

Ultimately, the Emirates deal buys time for Airbus to attempt to persuade other airlines that the A380 can be a profitable addition to their mix of aircraft.

Hi Fly operates used A380

While Airbus and the operating lessors have had a difficult time finding buyers for used A380s, the sixth such superjumbo to come off the manufacturer's production line was acquired by Portuguese widebody wet lessor Hi Fly in early July. The 12-year old A380, previously operated by SIA, was registered 9H-MIP in the name of Hi Fly's Maltese subsidiary.

Thomas Cook Airlines Scandinavia became the first carrier to use Hi Fly's A380 aircraft to operate flights from Copenhagen to Larnaca and back, and from Oslo to Palma de Mallorca and back on 2nd August 2018.

Norwegian Air Shuttle became the second customer for the aircraft, wet leasing the A380 from Hi Fly to operate the carrier's London-New York evening route in August. AC

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