**Lessors have a limited number of new aircraft available for lease in 2004 and 2005. They also have a normal number of aircraft returning off lease over the same period, indicating that supply of aircraft is tightening. All indications are that the leasing market will improve in 2004.**

# Limited aircraft availability points to brighter future for lessors

The immediate effect of a slump in traffic following the terrorist attacks of 11th September 2001 presented aircraft lessors with problems of lessees negotiating lower lease rates, aircraft being returned early off lease, forward leases being cancelled and a drop in demand for new aircraft for at least the following 18 months.

This came at a time when some lessors had a large amount of outstanding deliveries. This was coupled with the constant consideration to re-market aircraft that were due to come off lease in the following two years. Low lease rates were the only factor to provide relief to some lessors. Demand for aircraft would no doubt be suppressed and the number of aircraft that lessors would have to market in this period would exceed normal numbers.

With a recovery now under way, and an expected increase in demand for aircraft to follow, is the number of aircraft that major lessors will have to place still high, or has the market settled?

## Outstanding deliveries

Many lessors have followed the strategy of placing speculative orders with Airbus and Boeing and marketing these aircraft on the basis that a growing demand for operating leases and air traffic will be enough to prevent surplus capacity. Using accurate market forecasts and market intelligence lessors have devised strategies to market aircraft in advance of delivery, with these advance periods varying.

GECAS and ILFC place the largest orders and always have the largest number of due deliveries. These lessors are powerful enough to secure large discounts from the manufacturers and can pass these discounts on to lessees via low lease rentals. These lease rates are used by the lessors as an incentive to market their aircraft about 18 months prior to delivery.

Smaller lessors, such as CIT, Debis Airfinance and Orix will have shorter lead times to market new aircraft, since they will not be prepared to accept low lease rates, and will wait for lessees to increase their demand and sign at premium rates as their requirement for capacity gets closer.

Not all lessors acquire their aircraft by speculative orders, but rather by sale and leasebacks. These lessors therefore only have aircraft coming off lease to consider.

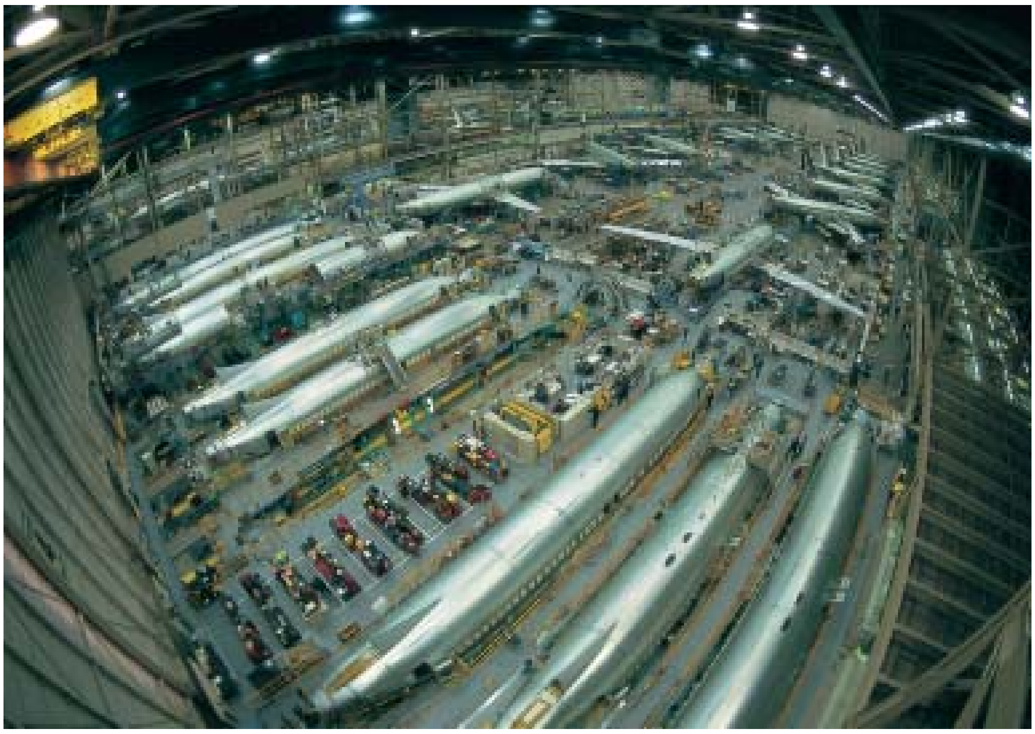
Analysis of lessors' outstanding deliveries which have not yet been placed with lessees has been made for those due for delivery during the remainder of 2003, 2004 and 2005. This has been made from the *BACK Aviation Solutions* database. This indicates a small number of aircraft still have to be placed by ILFC, Boullioun and CIT during the remainder of 2003 *(see table, this page)*. What should be appreciated is that there is a time lag between leases being signed and the database information being available, and so the actual number of aircraft yet to be placed will be less than shown. The number remaining to be placed for the rest of 2003 do not therefore present a problem to lessors.

**LESSORS' UNPLACED AIRCRAFT DUE FOR DELIVERY AND DUE TO RETURN OFF LEASE IN 2004 & 2005**

| Lessor | New aircraft due for delivery | | Aircraft coming off lease | | Total requiring placement | |
|---|---|---|---|---|---|---|
| | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 |
| Ansett Worldwide | 0 | 0 | 6 | 6 | 6 | 6 |
| Aviation Capital | 0 | 0 | 1 | 5 | 1 | 5 |
| Babcock & Brown | 0 | 0 | 9 | 6 | 9 | 6 |
| Boullioun | 6 | 8 | 1 | 3 | 7 | 11 |
| CIT | 16 | 17 | 6 | 2 | 22 | 19 |
| Debis Airfinance | 7 | 9 | 6 | 9 | 13 | 18 |
| GATX | 4 | 1 | 6 | 4 | 10 | 5 |
| GECAS | 0 | 9 | 50 | 60 | 50 | 69 |
| ILFC | 41 | 49 | 32 | 56 | 73 | 105 |
| Mitsui | 2 | 0 | 4 | 2 | 6 | 2 |
| Nissho Iwai | 2 | 2 | 4 | 2 | 6 | 4 |
| Orix | 0 | 0 | 2 | 0 | 2 | 0 |
| RRCC | 1 | 6 | 1 | 0 | 2 | 6 |
| SALE | 5 | 4 | 6 | 1 | 11 | 5 |
| Total | 84 | 105 | 134 | 157 | 218 | 264 |

*Source: BACK Aviation Solutions*

*Fortunately for lessors, their delivery schedules of popular narrowbodies were not as large in 2003 as they were in 2000/2001. In addition, Boeing reduced 737NG production rates which has helped firm lease rates.*



The number of aircraft shown as still available from lessors in 2004 amounts to 84 *(see table, page 6)*. The largest volumes are available from CIT and ILFC. A few other lessors only have small quantities of aircraft to place.

The aircraft ILFC still has available for delivery in 2004 are all 737NG and A320 family types.

ILFC has already placed a large number of the aircraft it will be taking delivery of in 2004 with a variety of lessees. Its 737NG deliveries will include carriers such as Malev, Aeromexico, Xiamen and Virgin Blue. Its A320 deliveries will be to Iberia, Air France, Air Malta, Mexicana, Finnair, Jetblue, Swiss, China Eastern, Air Portugal and Air New Zealand.

CIT has about 15 aircraft still available, with most being 737NG and A320 families, but it also has three A330-200s.

GECAS has a large number being delivered in 2004, but has now placed all of them. Lessees taking delivery of aircraft from GECAS in 2004 are AirTran, Frontier, Aeroflot, Air Canada, EVA, Qatar Airways, TAM and Alitalia.

Unplaced deliveries due in 2004 are also due to Boullioun, Debis Airfinance, GATX, Mitsui, Nissho Iwai, Rolls-Royce Capital Corporation (RRCC) and Singapore Aircraft Leasing Enterprise (SALE). These unplaced aircraft are all 737NG and A320 family types.

Numbers that have to be placed by individual lessors are small, however. Boullioun, for example, has 12 deliveries due on 2004, but only six aircraft left available. These are 737NGs and A320 family aircraft.

These lessors have all placed other aircraft with carriers such as Rio Sul, Mytravel Airways and British Midland.

A slightly higher number of 107 aircraft due for delivery in 2005 are still unplaced by lessors *(see table, page 6)*. Again, the majority of these are due to ILFC. All 49 aircraft, except four, are 737NG and A320 family aircraft. The remaining four are A330-200s. The 45 narrowbodies are split almost equally between Airbus and Boeing types.

GECAS has only nine aircraft still available. Eight are 737NG and A320 types and it also has one A330-200. GECAS has already placed some of its deliveries with LOT, AirTran, Frontier, EVA and Emirates.

CIT has a similar number available, and, like ILFC and GECAS, are mainly 737NG and A320 aircraft, but also a few A330-200s available, as is the case with its 2004 deliveries.

Lessors that have aircraft available in 2004 also have capacity in 2005. Boullioun has 737NGs and A320s, Debis A320s, Nissho Iwai 737-700s, RRCC 717s and SALE A320s; although the number of aircraft held between these lessors is only about 30 units.

Boullioun has another eight deliveries due in 2005, and all are available. These are A320 family and 737NGs.

The majority of new aircraft thus still available in 2004 and 2005 are 737NG and A320 family types. The number of 737NGs is about 55, while in the region of 70 A320 family aircraft are available; the majority of which are A320s.

Most of the remaining aircraft are A330-200s, although there are also a small number of 777s.

The number remaining available in 2004 and 2005 are not excessive, and the numbers look relatively small when ILFC's deliveries are removed. "The portion of deliveries going to lessors in 2003 and 2004 is less than it was on 2001," comments John Willingham, chief executive officer at Boullioun. "This was partly due to a strategic decision by lessors to reduce orders, but also delivery schedules to lessors were lighter in 2003/04 than they were in 2000/01."

What also has to be considered is that large airline orders can often include portions of aircraft already on order with the lessors. Large numbers of available aircraft with the lessors therefore get soaked up as these airline orders are placed.

## Aircraft due for return

The other consideration for lessors are aircraft coming available over the same period as current leases expire. These exceed the number of new aircraft being delivered, but are not excessive by industry standards. Aircraft coming off lease do, however, affect most lessors.

The total coming off lease in 2004 is only about 134, and about 160 for 2005. These are not high by industry norms. Moreover, lessors re-market many aircraft coming off lease with lease extensions. Lessees responded to the traffic slump following 11th September 2001 terrorist attacks by seeking lease concessions from lessors. The main requirement was for reduced lease rentals, followed by stepped increases. In return for these lowered lease rentals lessors demanded lease extensions, limiting the need to remarket aircraft in the most difficult period following the terrorist attacks. Some of these lease extensions may now be due to expire in 2004 and 2005, but the total number of aircraft coming off lease and due for delivery is not high compared to the 700-800 lease transactions completed each year in 2000 and 2001. This number does, however, include all lessors with older aircraft types.

Not surprisingly the lessors with the largest number of aircraft due to come off lease are ILFC and GECAS. GECAS has about 50 and 60 in 2004 and 2005 to re-market, and says its position regarding to returns is manageable.

Most of GECAS's aircraft are narrowbodies, including MD-80s, but the majority are 737-300/-500s, 737-800s and A320s. It also has a few 767-300ERs and MD-11s due back in 2004 and 2005.

Demand for 767-300s still seems strong, while MD-11s remain popular with freight carriers.

ILFC has 32 aircraft due for return in 2004 and about 56 due in 2005, putting it in a better position than GECAS. The majority are 737Classics, A320 family and 757-200s, but it also has a large number of various widebodies. This includes A310-300s, 767-300ERs, 777-200ERs, A330-300s and A340-300s. The number of A310-300s is small, however, and the balance of its widebodies are popular types still in demand with first tier passenger carriers.

Next to these largest groups are all other lessors with similar numbers of aircraft coming off lease over the same period *(see table, page 6)*. While many are narrowbodies, there are also appreciable numbers of widebodies.

The narrowbodies due to return off lease are a mixture of MD-80s, 737Classics, 757-200s, a smaller portion of A320 family aircraft and a few 737NGs. The A320 family and 737NG aircraft are more likely to have their leases extended, while airlines will seek to return MD-80s, 737Classics and 757s. Availability of 737Classics and 757-200s could therefore build up to the point that values are reduced over this period, leading to a higher volume of freighter conversions.

The widebodies that are due to come off lease over this period are a combination of A300-600s, A310-300s, 767-200s, 767-300s, A330-300s, A340-300s and a small number of 777-200s 747-400s. Lease expiries for A300-600s may finally put enough on the market to trigger freighter conversions, but the number of widebodies coming off lease from these lessors over this period is not excessive in relation to the market size.

## Market outlook

The total number of aircraft that lessors will have to market during 2004 and 2005 are about 220 and 264. These numbers do not represent a problem for the lessors, and the market is now seeing higher levels of interest and demand for aircraft. The market is probably in its strongest position since the 11th September 2001. This was followed by the Gulf War and SARS outbreak. Traffic is now recovering and load factors are strong, and yields and unit revenues are strengthening as a consequence. The knock-on effects of this are to make transactions generally less risky, although there are still wide variances in the financial performance between airlines.

Despite total numbers, the more critical issue is the number of different types. By far the largest numbers are the 737NG and A320 families, but these are replacing older generation narrowbodies at a high rate. Lessors find 737s particularly easy to re-market, especially when maintenance condition and technical records are up to date. It is felt by several lessors that the market is type-specific and that 737NG lease rates and values are now recovering faster than A320s'. Avitas, for example, puts the 737-800's current market value at base value, while it still puts the A320's current market value at a discount of 5-10% of base value.

"The supply of A320 family aircraft is still greater than demand," explains Willingham. "A320 production rates are still quite high, and so there are good deals to be had. There are also still some high delivery streams to lessors. There were also a few post-9/11 bankruptcies which put some A320s on the market. Demand is, however, increasing. The situation is different for 737NGs, since Boeing cut back on production rates after 9/11, and this has helped keep its supply tight. The low-cost airline sector has also been strong in recent years, which has helped keep overall supply of new generation narrowbodies low. Demand for popular narrowbodies should be even better in 2004."

This still leaves lessors the problems of older types like the MD-80 to deal with, and will not be as easy to re-market. The 737Classics will be easier to market, although the largest lessors are widening the base of carriers using new equipment, and making it harder to market older aircraft.

While some lease rates seem to be recovering, airlines are still able to take advantage of weaker rates for less popular types. There are, for example, a large number of 757-200s on the market and some carriers, in particular European charter airlines, are acquiring 757-200s in increments at extremely attractive rates for medium-term leases.

Various widebodies like the 767-200 and A310-300 are now being retired by primary carriers, and are less likely to be considered by lessors' primary customers, which may force the lessors to investigate the option of freight conversion and re-marketing to a new audience of freight carriers over the next two to three years.

The 767 market, for instance, is segmented between -200s and higher powered and younger -300ERs, and the supply of 767-200s is increasing. AC