IMPACT OF COVID ON AIRCRAFT VALUES

Piiq Perspective
Volume 12 November 2021

Change in Current Market Values

As the table below shows, the COVID crisis has precipitated the most drastic drop on record in appraisers' current market valuations (**CMVs**) of most aircraft types. Due to the pandemic, airlines had to place significant portions of their fleet into storage, and cancel considerable swathes of their flight schedules as international movement was restricted. In addition, OEMs reduced their production rates as they agreed delivery deferrals with their customers. Appraisers have accounted for this rupture in the trading of aircraft through a significant readjustment of CMVs, with the impact to widebody values expected to continue longer than narrowbodies. Any Aircraft acquisitions in both the new and the used market have been limited and driven by fleet renewal or financial leverage strategy rather than growth capacity.

Consequently, the fall in the appraisers' CMVs of the aircraft can be deceiving. This drop actually reflects the relative illiquidity of the market, rather than the price at which aircraft were and are being traded. The price being

Aircraft Values	Pre-Pandemic 2019	Height of Pandemic 2020	Today 2021
New Widebody CMVs	A350-900 $115.32M A350-1000 $172.76M B787-8 $118.40M B787-9 $148.77M B787-10 $154.39	A350-900 $109.55M (-5%) A350-1000 $162.39M (-6%) B787-8 $102.99 (-13%) B787-9 $139.84 (-6%) B787-10 $143.58M (-7%)	A350-900 $109.55M (-5%) A350-1000 $161.53M (-7%) B787-8 $101.43M (-14%) B787-9 $139.84M (-6%) B787-10 $143.58M (-7%)
New Narrowbody CMVs	A320NEO $52.0M A321NEO $59.86M B737 MAX 8 $50.78M B737 MAX 9 $52.73M	A320NEO $48.88M (-6%) A321NEO $56.27M (-6%) B737 MAX 8 $45.19M (-11%) B737 MAX 9 $46.4M (-12%)	A320NEO $48.88M (-6%) A321NEO $56.27M (-6%) B737 MAX 8 $45.2M (-11%) B737 MAX 9 $46.4M (-12%)
Used Narrowbody CMVs 5 years of age	A320-200 $32.89M A321-200 $35.69M B737-800 $34.8M B737-900ER $34.96M	A320-200 $26.31M (-20%) A321-200 $29.62M (-17%) B737-800 $28.89M (-17%) B737-900ER $29.02M (-17%)	A320-200 $26.16M (-20%) A321-200 $29.91M (-16%) B737-800 $28.62M (-18%) B737-900ER $28.82M (-18%)
Used Narrowbody CMVs 10 years of age	A320-200 $22.99M A321-200 $26.10M B737-800 $25.81M B737-900ER $25.25M	A320-200 $16.55M (-28%) A321-200 $20.62M (-21%) B737-800 $19.36M (-25%) B737-900ER $19.44M (-23%)	A320-200 $16.44M (-28%) A321-200 $20.48M (-22%) B737-800 $19.26M (-25%) B737-900ER $19.31M (-24%)
Used Narrowbody CMVs 15 years of age	A320-200 $15.97M A321-200 $18.72M B737-800 $18.46M	A320-200 $10.38M (-35%) A321-200 $14.23M (-24%) B737-800 $12.92M (-30%)	

SOURCE IBA (InsightIQ Module)

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asked by the seller and being bid by the purchaser have been so wide apart that aircraft trade largely dried-up at the height of the pandemic, as sellers (particularly lessors who have weathered the pandemic better than predicted) have opted to hold onto their assets, wait until demand returns and bids and asks more closely realign.

Similarly, in contrast to previous crises that have hit the aviation industry (2008 financial crisis, SARS, 9/11) during 2020 and 2021 OEMs have substantially decreased their delivery output, decreasing the number of new aircraft on the market. While demand is depressed there is also no abundance of supply of aircraft for sale at current market values.

Change in Base Values

An argument can be made that a truer reflection of asset prices are the appraisers' Base Values (namely the appraiser's opinion of the underlying economic value of an aircraft in an open, unrestricted, stable market environment with a reasonable balance of supply and demand), as they represent the value at which sellers would be more willing to trade.

As demonstrated below, Base Values have moved far less dramatically than CMVs, particularly in the narrowbody space. This is because the COVID crisis is perceived as a transient one that the world will learn to live with, rather than a fundamental shift in the dynamics of the aircraft market.

Short-haul travel is forecast to be the first to return, with demand scheduled to return to 2019 levels in 2022, and this is reflected in a much less volatile change in the Base Values provided in the table below. However, despite the improvement in the market, many aircraft will remain in storage which accounts for the minimal improvement in narrowbody Base Values in 2021 although the newest aircraft have seen values increasing as more of these aircraft have been returned to service.

	Pre-Pandemic 2019	Pandemic 2020	Today 2021
New Narrowbody values	Base Value +2%	Base Value no change	Base Value no change
New Widebody values	Base Value +2%	Base values -5% to -8%	Base values -8% to -15%
Used Narrowbody Values	Base Value +1%	Base Value no change	Base value minor change on some current gen aircraft

SOURCE IBA (InsightIQ Module)

The outlook for widebody aircraft is much less certain. Long haul travel requires lengthy planning for travelers and operators resulting in a lengthier restoration of services. There is anticipated to be a change in travel patterns with a period of depressed business travel and increased dependency on virtual communication, lesser initial economic activity and restrictions on company travel budgets. Long-haul travel demand is currently anticipated to return to 2019 levels by 2024, though this could be sooner if the current international boarder restrictions become less cumbersome for passengers). All this uncertainty is reflected in more depressed Base Values.

Implications of the fall in Aircraft Values

Financiers / NPI Insurers: For new aircraft financings while advances are returning to pre-pandemic rates, the depressed CMVs (and to a certain extent Base Values) will mean that the dollar amounts advanced generally remain lower than pre-pandemic. This means that financiers (including insurers participating in insurance wrapped aircraft financings) are able to secure deals on a historically low absolute exposure basis. The dramatic fall in CMVs means that today's advance rates (and consequently insurance Non-payment Insurance risk exposure) are also at historical lows and will look extraordinary as the CMVs revert to mean (Base Values) over the course of the next 18 months to two years.

Note however that some lessors and financiers are currently willing to base their advance rates on the Base Values as they take the view that this is closer to true market pricing, and with the return of short-haul travel aircraft lease rates and consequently loan margins are swiftly returning to pre-pandemic levels.

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The fall in values will also impact financiers' portfolios by leading to higher LTVs and therefore higher capital reserve requirements. Financiers can seek to off-set this while remaining active in the market by utilizing insurance wrapped aircraft finance products, such as the iFLI product provided by Piiq to reduce their capital reserve requirements.

Lessors: One consequence of COVID has been to increase the proportion of the world fleet held by lessors. As airlines seek to generate much-needed liquidity, airlines continue to resort to sale-and-leaseback deals with lessors. In addition, the fall in both CMV means that Lessors who have managed to weather the crisis in relatively good order are able to acquire aircraft at historically low prices with the anticipation that the value of their portfolio will improve as values return to Base Values.

The relationship between OEMs and lessors is likely to get more complicated. OEMs will compete fiercely for new orders as airlines start emerging from the crisis. At the same time, with a view returning to their fleet renewal programs, lessors will work hard to push their assets into the market. There is a risk that this could lead to prices falling as aircraft start to trade more regularly again, and the entire supply chain feeling the heat. This could lead to a longer-term depreciation of mid-life and older aircraft which have already taken the brunt of the fall in aircraft values.

However, this could be mitigated by airlines' resumption of their fleet rejuvenation programs and a return to fleet growth. This is already being seen in demand for new narrowbodies which has removed the white tail fleet previously held by the OEMs. Older fleets except freighters—in high demand since the pandemic outbreak—also represent a risk, which can be partially mitigated by lessors' management capabilities or ability to monetize end-of-life assets.

Airline Insurance teams: should be aware of the impact that falling asset values will have on their aircraft insurance requirements under their financing obligations. Insurance thresholds in finance documents tend to be tied to the outstanding amount of the loan at that time. However, if an airline is managing its own insurance obligations by reference to the value of the aircraft, with tightening LTVs airlines may want to check they are not inadvertently in breach under their financings.

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Prior to joining the Piiq Team as head of legal structuring and General Counsel for Piiq iFLI, Luke was a senior associate in the Structured and Asset Finance team of Allen & Overy. He has in-depth experience advising on a wide variety of cross-border aviation transactions including private insurance ANPI cover debt financing, leasing, tax leasing and warehouse finance transactions. He has acted for clients including lenders, insurers, export credit agencies, lessors and airlines.

Luke has been actively involved and a member of the steering committee for the Future of Export Finance (FEX) group, which brings together the younger generation of financiers, insurers and lawyers involved in export finance for networking and educational events. Luke been recognized by AirFinance-Journal as a 'Rising star in Aviation' and was nominated for Euromoney's 'Rising star in Aviation' award.

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Mark joined Piiq in May 2020 to lead underwriting for the insurance backed aircraft finance business, Piiq iFLI.

Mark started in the Political Risk and Structured Credits market in 2002. In his previous role at Sompo International (previously Endurance) he managed the Asset Finance Credit Risk Solutions team with particular focus on AFIC, an Insurance backed Aviation Finance product.

Mark was also the Deputy Head of the Political & Financial Risk team at Sompo International providing Credit and Sovereign Risk Solutions primarily to Financial Institutions and large Corporates with a particular focus on Structured Commodity Finance, Export Finance & Project Finance.