



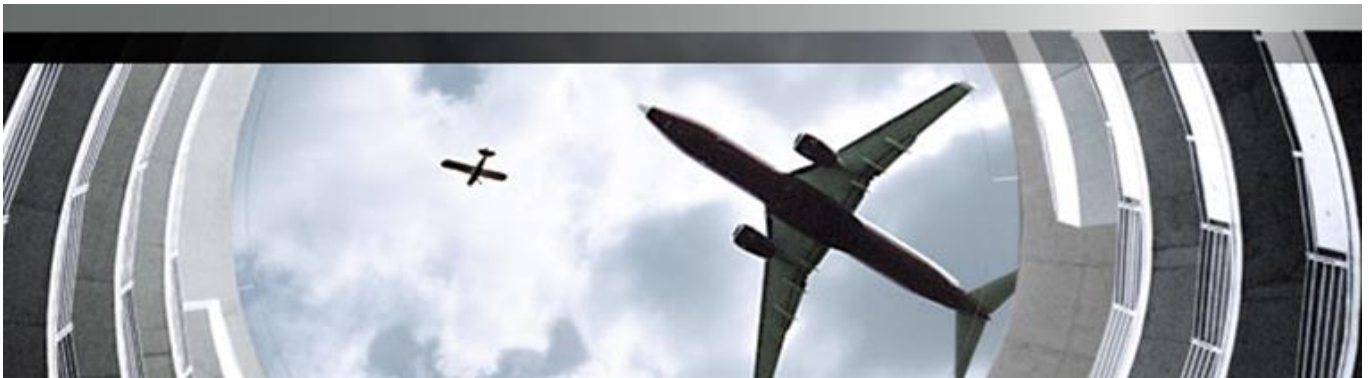
Aviation Debt

Newsletter Q2 2020

Global Aviation Q2 2020 Overview

- > Covid-19 is still dominating the aviation sector. Governments, airlines and airports are working towards travel concepts, in order to allow tourists to go on summer holidays. Airlines operate on a significantly decreased level compared to the same period in 2019.
- > Based on an estimate by IATA it could take until 2024 to reach the levels of 2019. This estimate also takes into consideration the poor handling of the pandemic in the US and in some regions of South America.
- > Prime Capital closed one transaction in the second quarter. The deal is a shorter term financing for a portfolio of narrow-body aircraft, at an LTV around 65% and pricing of up to 400 Bps. The transaction is part of a sale and lease back transaction of a Tier 1 carrier. The pipeline currently consists of five opportunities, with Tier 1 names, attractive collateral and conservative terms. Some transactions even include an investment grade guarantee. The average spread of the Pipeline is around 360 Bps.
- > **Conclusion:** Airlines are slowly starting to recover in some regions. The risk of a second wave of infection remains and subsequent lockdowns could follow. It can be however expected, that this will only impact smaller regions with Covid-19 hotspots. Most countries have set up testing programs for travelers and thus infections can be spotted early on. Spreads remain at elevated levels with some transactions pricing at 400+ Bps. Deals for Tier 2 or 3 airlines, are currently rare and Tier 1 names continue looking for secured financing. We currently see a generic spread for a narrow-body loan around 380 Bps, but with significantly improved credit on the airline side.





Aviation Debt – Q2 Summary

The second quarter of 2020 was dominated by the Covid-19 pandemic, which has affected the airline sector globally.

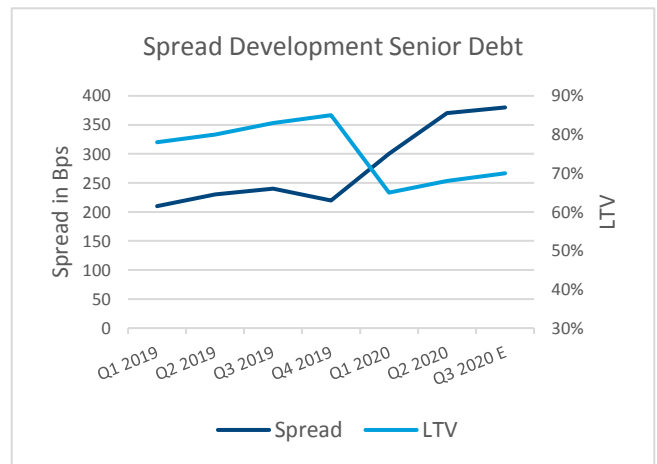
However, air travel demand continued to show signs of recovery, towards the end of Q2 2020, from the low point in April but remains significantly below pre-COVID levels. According to IATA Industry-wide revenue passenger-kilometres (RPKs) fell by 86.5% year-on-year in June, compared with a 91.0% year-on-year contraction in May. Seasonally adjusted RPKs rose modestly for the second consecutive month. The rebound continues to be dominated by rising domestic demand. International RPKs contracted for another month. However, some improvement is expected in July as international travel restrictions have been lifted in some parts of the world including the Schengen Area.

South America has experienced a series of chapter 11 filings of large carriers like Avianca, LATAM and AeroMexico. Some smaller airlines have declared bankruptcy across Europe and Asia. The majority of airlines has managed to negotiate payment deferrals for lease- and debt payments in order to preserve liquidity. This has been additionally supported by bank loans and government support in some regions.

IATA has released an updated global passenger forecast predicting that air travel will not return to pre-COVID-19 levels until 2024, a year later than previously projected. IATA says that the more pessimistic recovery outlook is based on a number of recent trends: Slow virus containment in the US and developing economies, reduced corporate travel as well as weak consumer confidence.

Financing Terms

There has been little activity in the capital markets in terms of aviation. The exception being several large airlines and OEM's coming to market for additional debt, which they were able to raise, despite the current challenges for the aviation industry. This underlines, that the market is divided between Tier 1 airlines and airlines, which are struggling to access new liquidity without government support.



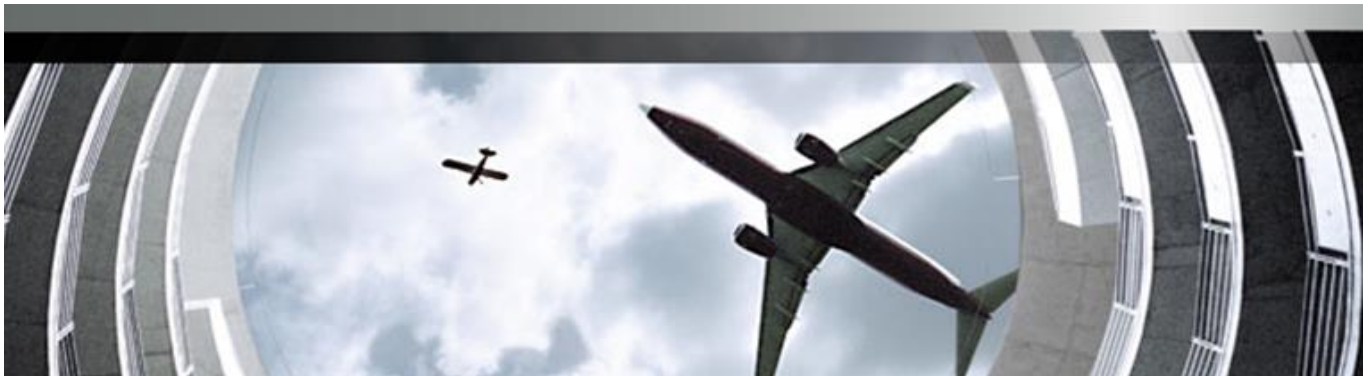
Source: Prime Capital

In contrast to the capital markets, transaction volumes in private markets have significantly picked up since the first quarter, with more transactions coming to the market. Transactions can be broadly categorised in three categories: sale and leasebacks to access additional liquidity, bridge financings and financing new deliveries. Distressed transactions have not been very visible in the market so far, despite several chapter 11 filings and bankruptcies.

The first half of the quarter was dominated by transactions focused on short term liquidity, by either airlines or leasing companies. These transactions usually had short tenors and low LTV's. Recent transactions are longer term focused, financing new deliveries. There have been transactions with tenors of up to 12 years, however day-1 LTV's remain low between 65% and 75%. These figures are however theoretical as appraisers only slowly incorporate the current market into their assessment, so the H1 2020 are the first ones to show a decline. It can be expected, that it will take several quarters until appraisers have fully incorporated their assessment into their values. Hence LTV's will be lagging actual transaction prices.

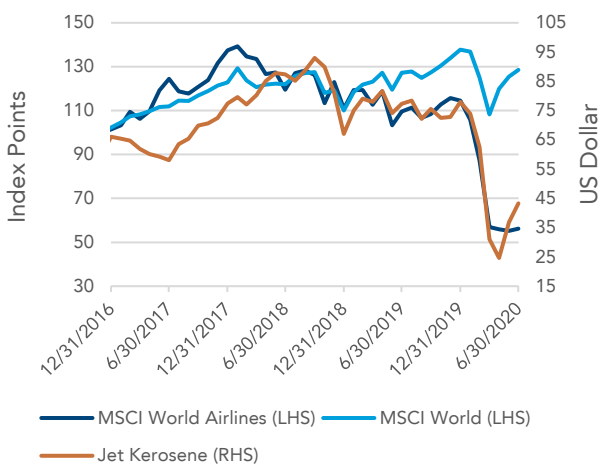
Airline Market

While the stock market has mostly recovered from the drop in March and April, Airline stocks are still trading at depressed levels. Based on a number of insolvencies and an uncertain short term outlook for the sector, investors are



very cautious and are relying on government support. Government support is unequally distributed, with the majority (in total terms) granted in the US and the EU. South American airlines have seen very little support from their local governments. Liquidity remains an important factor for airlines operating at significantly decreased levels.

Airline Equity Market



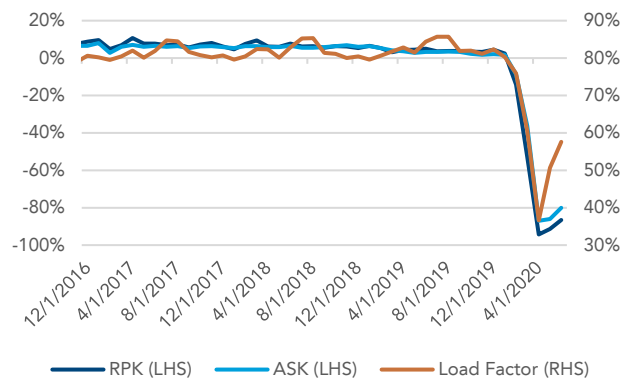
Source: Bloomberg

Kerosene has started to recover, based on the increasing oil price. However, given the sharp decrease and hedging in place at the airline level, a significant impact of rising fuel costs is not expected, given the relative increase from a low level and low volume of flights. Airlines have mentioned, that the efficiency of new technology aircraft becomes irrelevant at the current price levels.

Commercial Aviation

The Covid pandemic has caused severe drops in passenger numbers and load factors, with international traffic almost non-existent in April and May.

RPK vs ASK



Source: IATA, Air Passenger Market Analysis June 2019, P.1. Available [here](#).

Global RPKs measuring the total demand of passenger traffic, fell by a historic 86.5% year-on-year in June down from already -52.9% year-on-year in March. Available seat kilometers (ASK) dropped in line with RPK's by -80.1% year-on-year in March, while the load factors decreased to 57.6% down from their all-time highs around 80% during 2019. The recovery is dominated by rising demand in domestic markets. International RPKs contracted by close to 100% for another month. Some improvement is expected in July as international travel restrictions have been lifted in some parts of the world, including the Schengen Area. Airlines continue to restart their fleets, however local travel restrictions might inhibit the recovery until the already slow winter schedule.

Prime Capital Aviation Debt Expertise

- > Advice and support for aviation direct investments, portfolio strategy and sector allocation
- > Access to leading European and global aviation finance partners for sourcing as well as direct lending activities
- > Investments in Senior and Mezzanine debt

Further information about Prime Capital AG can be found on the web site
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