

# AVIATION INDUSTRY FACED WITH A DEBT FINANCING CLIFF : WHICH WAY OUT ?

## *Executive Summary*

SEPTEMBER 2022



**ARTHUR D LITTLE**



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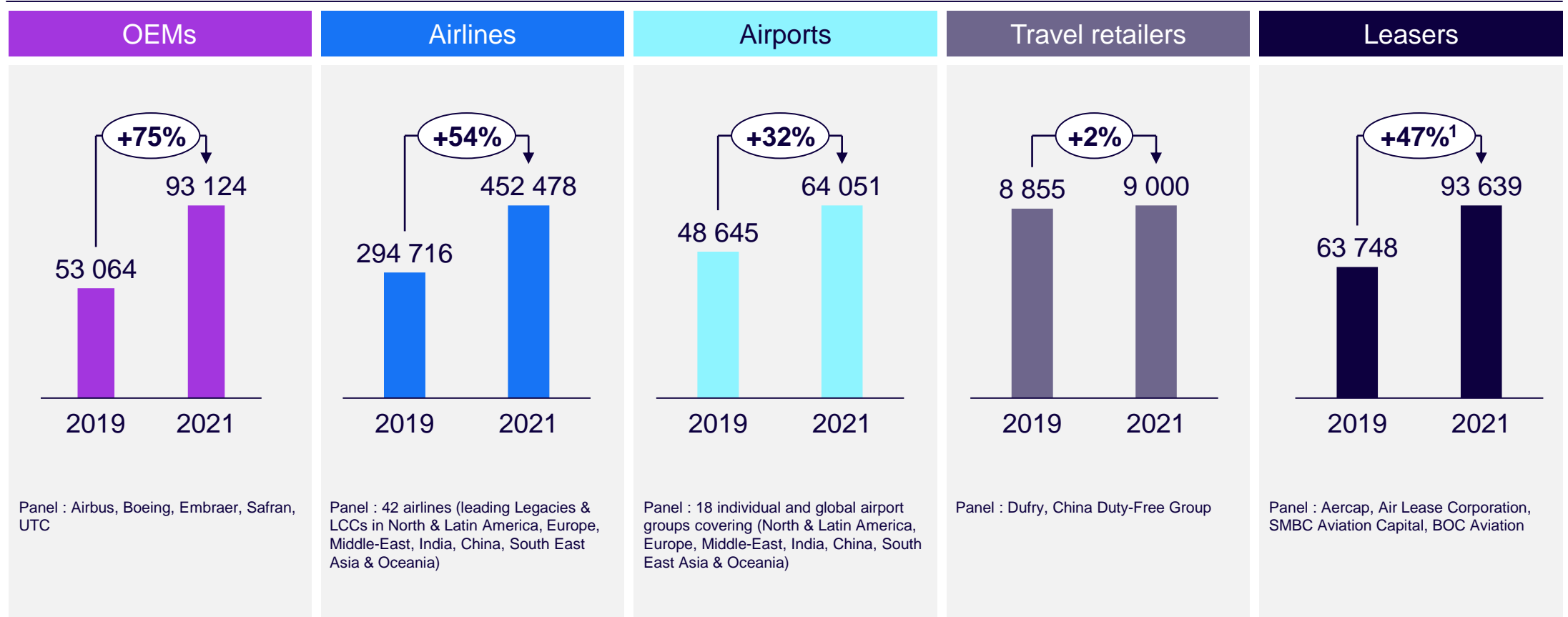
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# A “ONCE IN A LIFE” TRANSFORMATION CHALLENGE FOR THE AVIATION INDUSTRY

# Indebtness of all parties in the Aviation ecosystem increased significantly during COVID

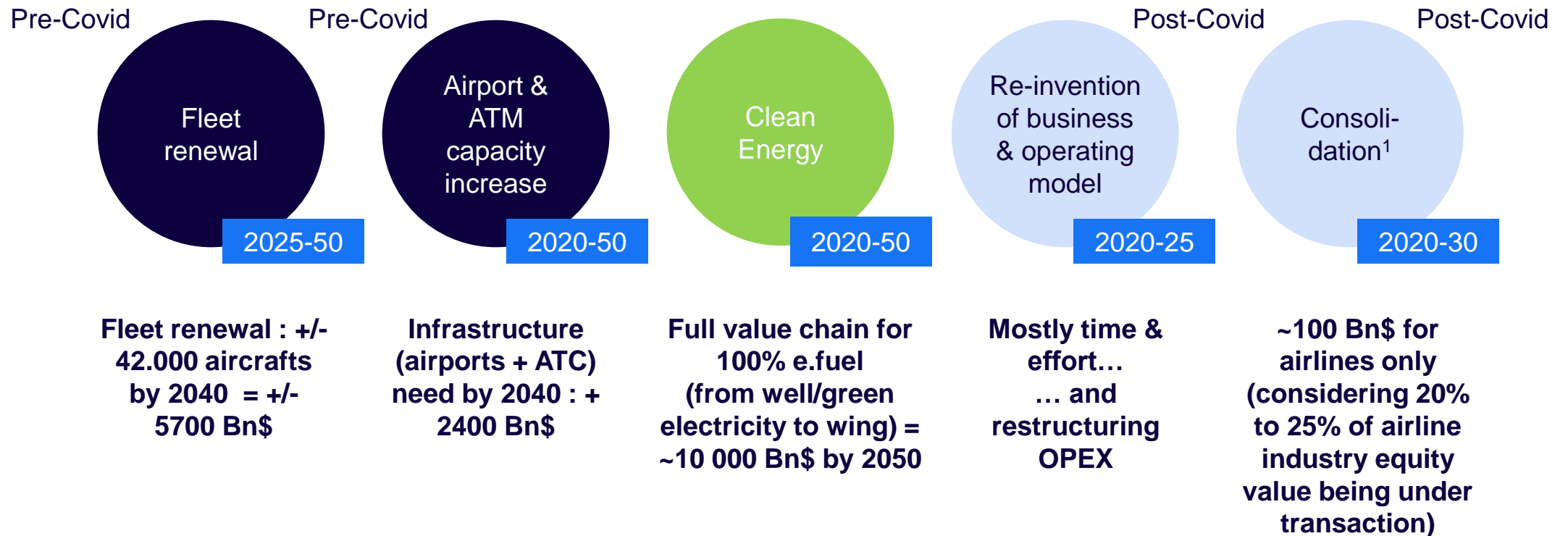
## Evolution of debt for selected players

2019 – 2021, in USDm 2021



Note: 1) GCAS Acquisition debt in October and November 2021 , AerCap emitted \$22bn of debt to acquire GECAS  
 Source : EIKON, Orbis, Companies' Annual reports, Arthur D Little

... whilst the industry has to **finance ~18.000-20.000 Bn\$ in next 20-30 years** to achieve a “once in a life time” transformation, in almost all domains of the business



Sources :

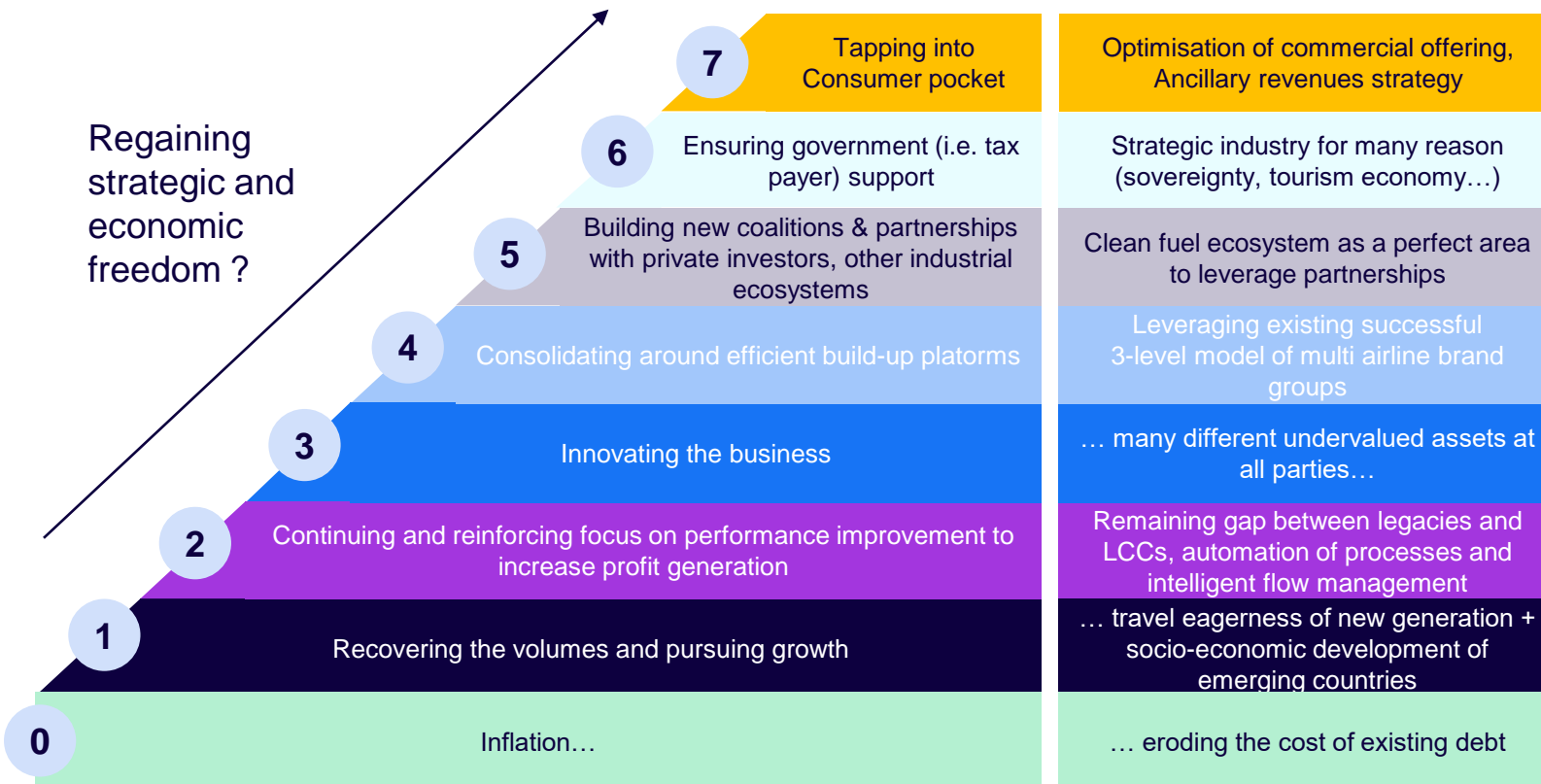
Airbus, World Economic Forum, ACI, IATA, UE, Arthur D. Little analysis

<sup>1</sup>current EV EBITDA multiple of large public airline groups considering gearing ration of 60%, Arthur D. Little estimate of % of airline equity to be under M&A process

# The industry will have to **leverage all options** to overcome the financing of its debt and of its transformation whilst facing many obstacles

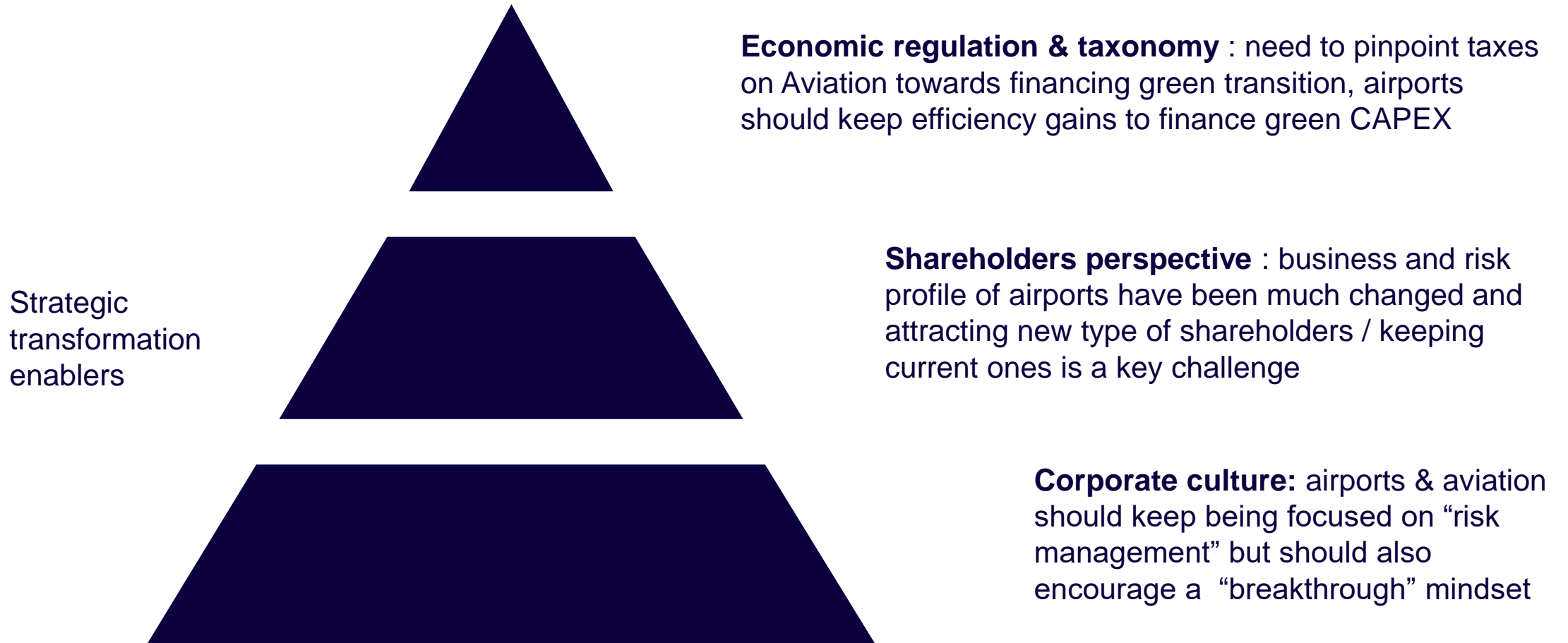
Many options and levers to activate...

... but many obstacles to overcome:



- ... hyper-competition among airlines hampering price discipline, impact of digital on travel retail
- ... other priorities than transport @ governments given long-lasting effect of current social and energy crisis ?
- ... habit of economic self-sufficiency in Aviation industry
- ... strict ownership regulations and strong corporate cultures among Aviation players
- ... cash constraints and risk aversion culture of the industry
- ... non-fuel cost productivity is slowing significantly as marginal gains are more difficult to achieve
- ... uncertain recovery of business travel, impact of flyshame in developed economies
- ... changes in Fx rate \$ vs other currencies, higher financing cost ahead

### 3 others dimensions as **key enablers to the strategic transformation of Aviation**

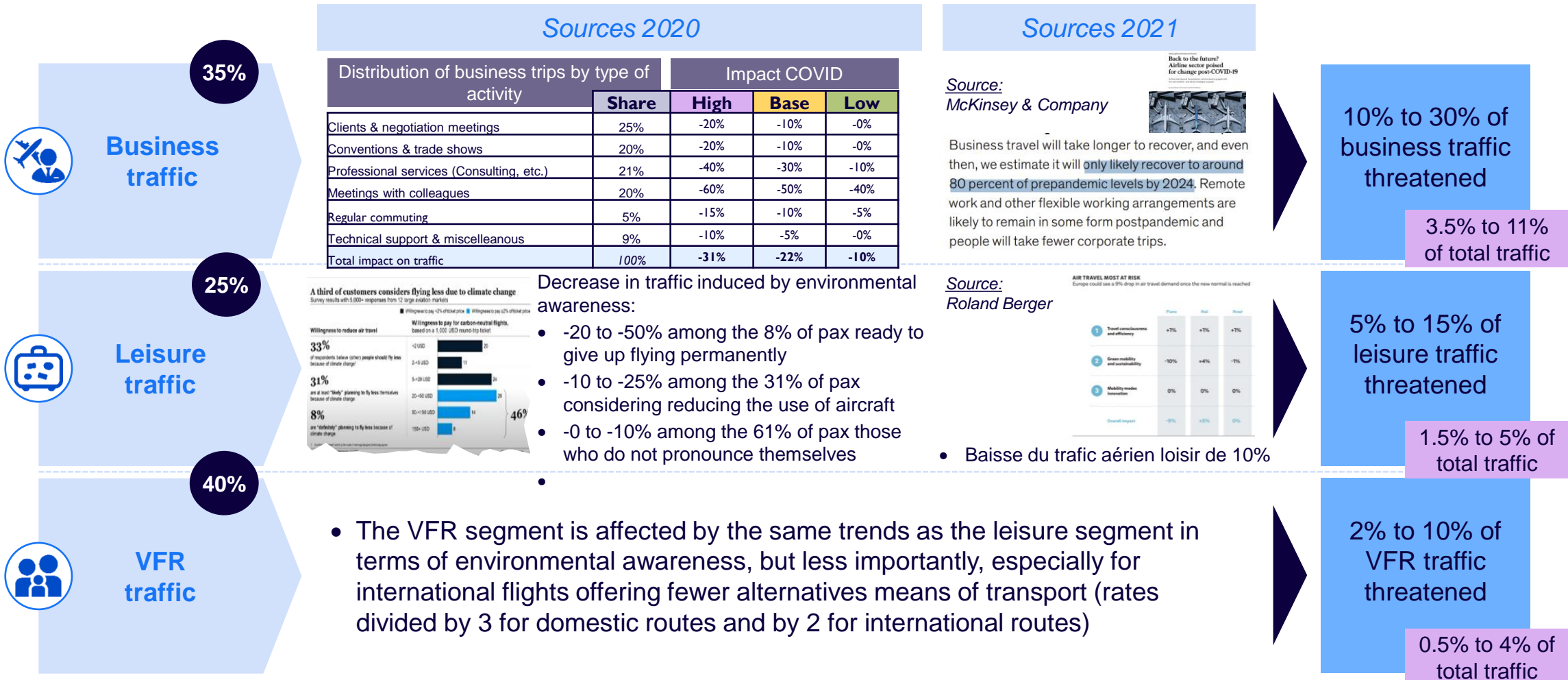


# **QUICK OVERVIEW OF AVIATION'S OPTIONS TO FACE THE DEBT AND INVESTMENT CLIFF AHEAD**



1

# Recovering the volumes: how to reduce the risk of losing up to 30% of business traffic and 15% of leisure traffic?



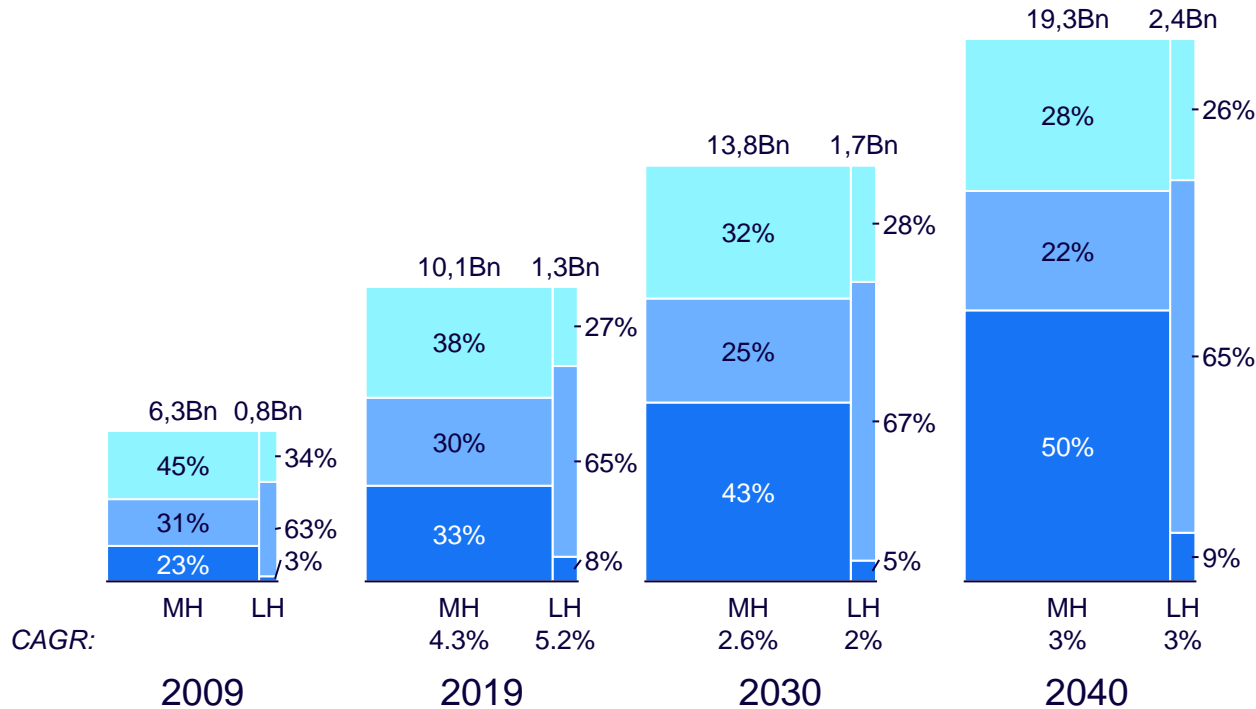
1

# Recovering the volumes: full Service Airlines may be severely impacted by COVID; LCCs grab market shares on Medium Haul, and Long Haul demand will be slower to recover

Market share per airline type

Billion Seats, 2009-2040

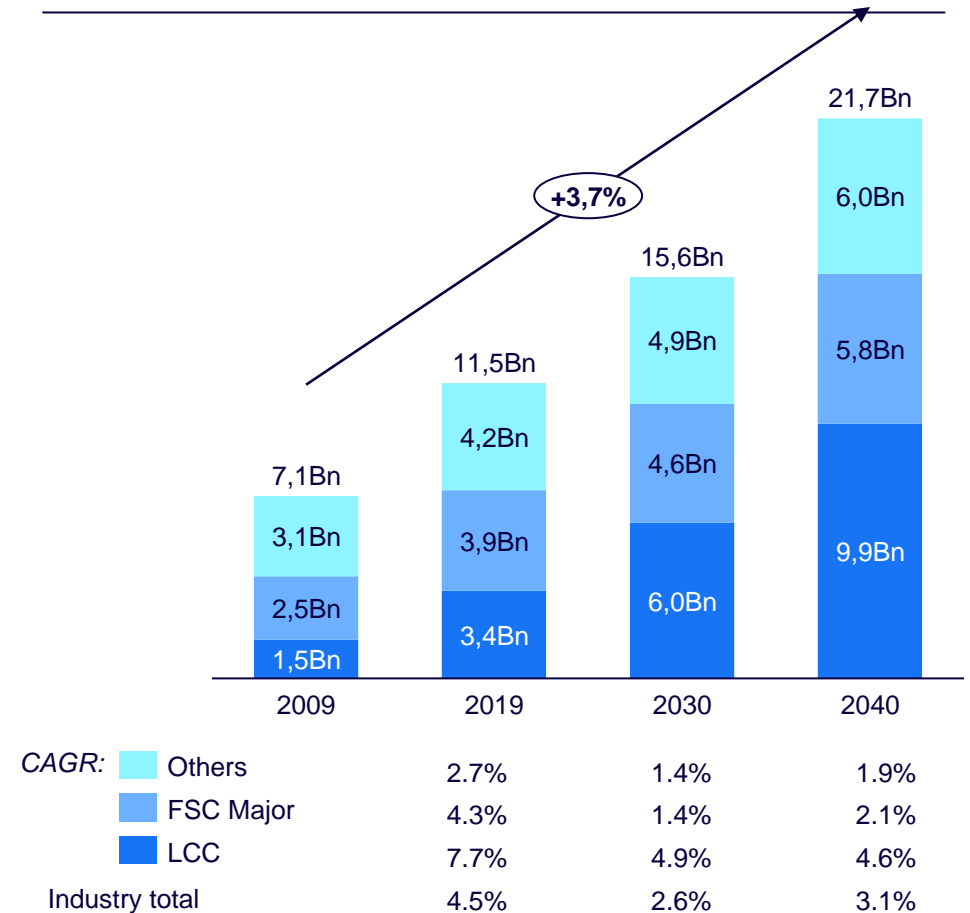
Others FSC Major LCC



Sources: SRS, Arthur D. Little  
 MH : Medium Haul (<3500km); LH : Long Haul  
 LCC : Low cost carrier  
 FSC : Full service carrier

Market share & CAGR per airline type

Billion Seats, 2009-2040

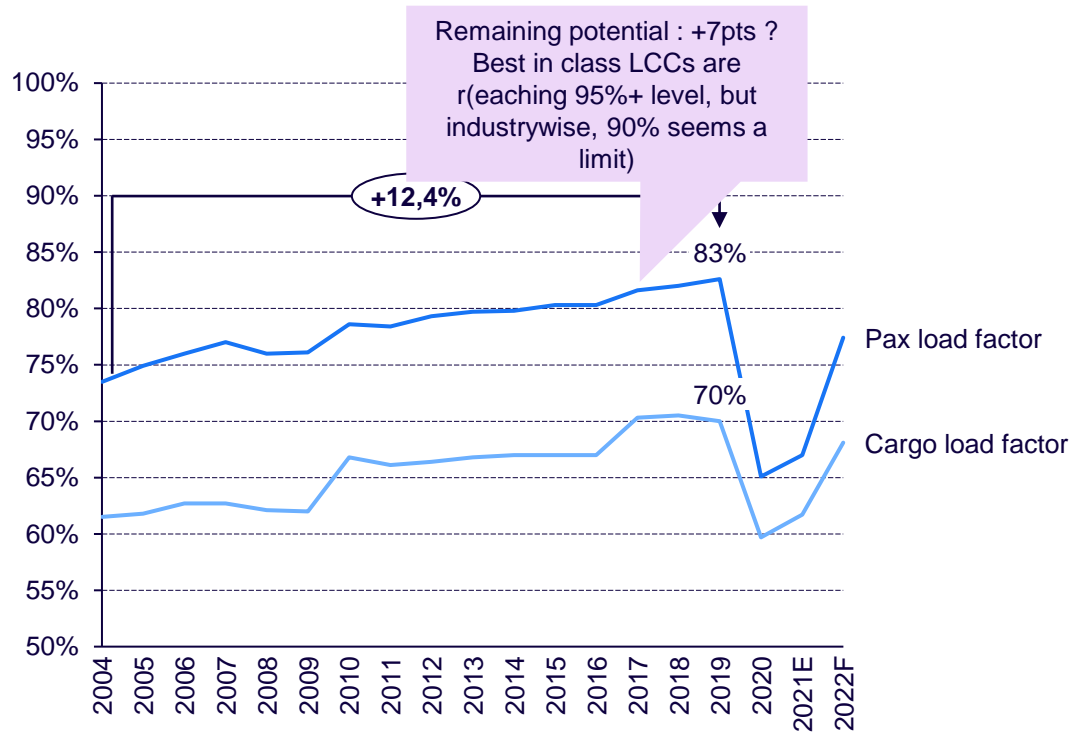


2

## Improving performance: the opportunity window to improve airlines manageable costs (i.e. utilisation of aircrafts & crews, non-fuel costs...) is narrowing

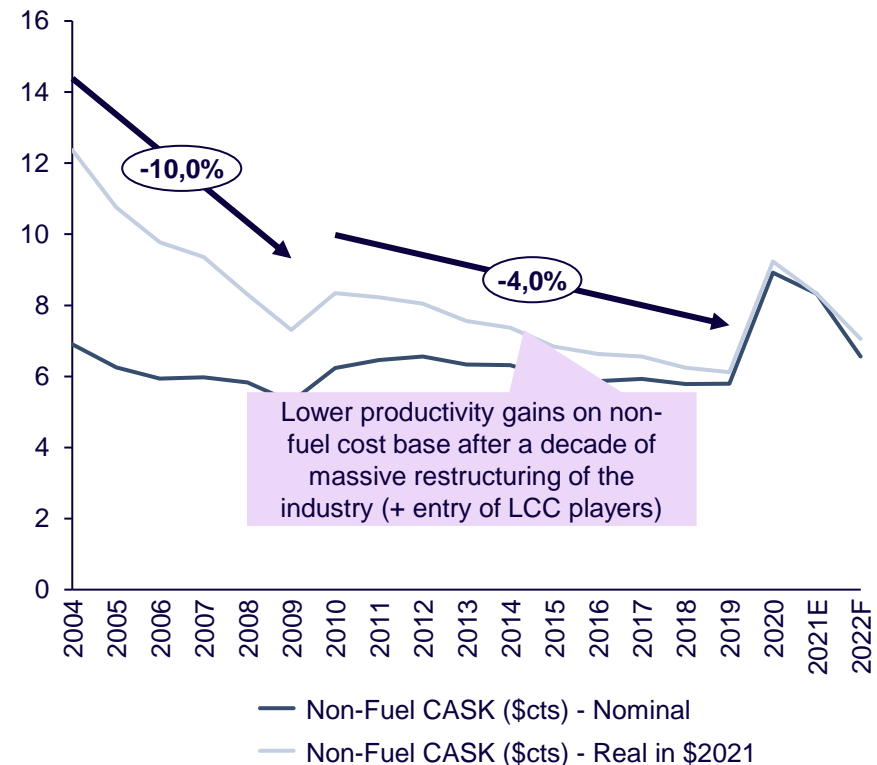
### Load factor evolution in pax & cargo segments

- World, in BnUS\$ -



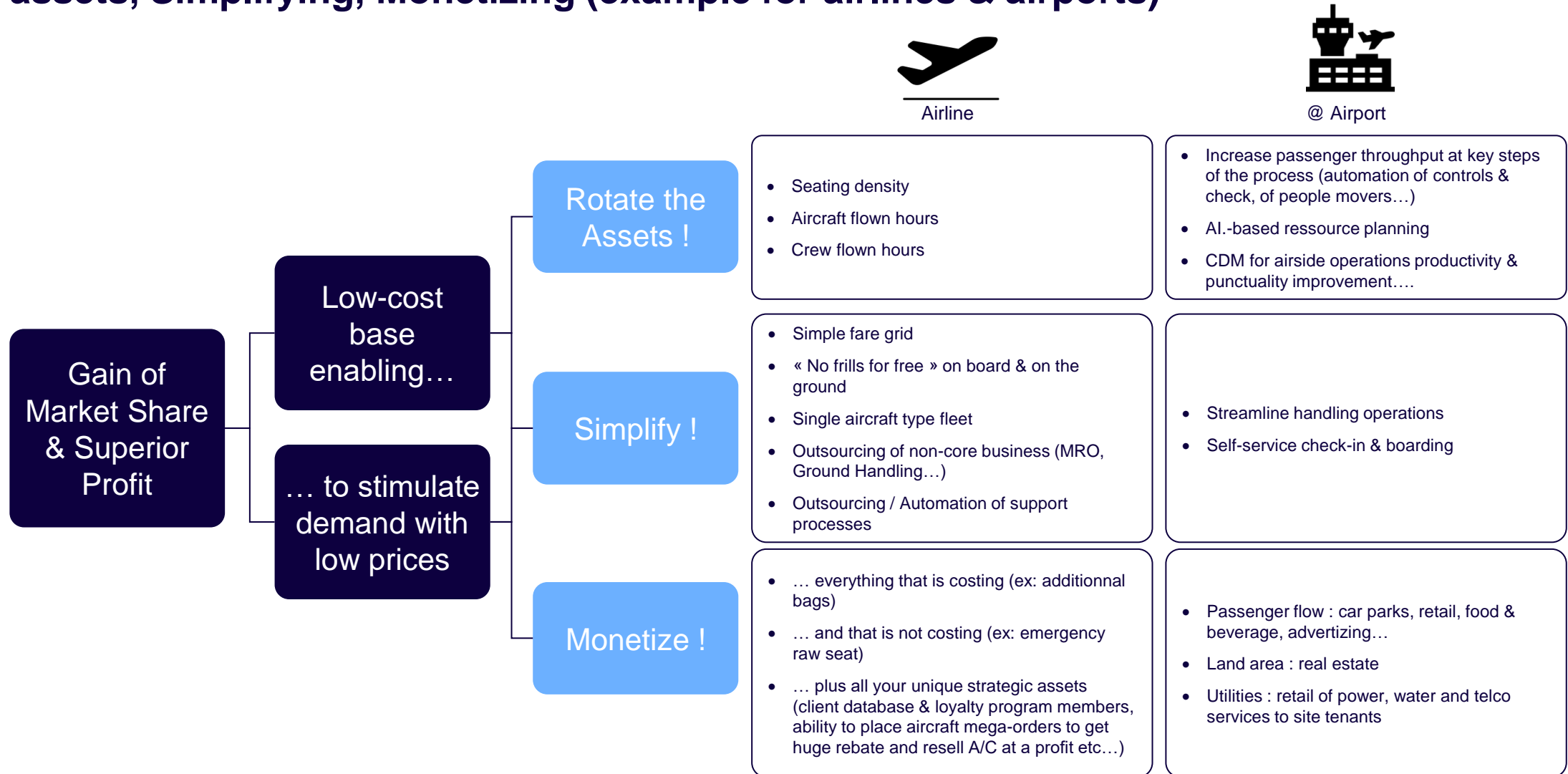
### Evolution of non-Fuel costs

- World, CASK excl. Fuel in cts US\$ -



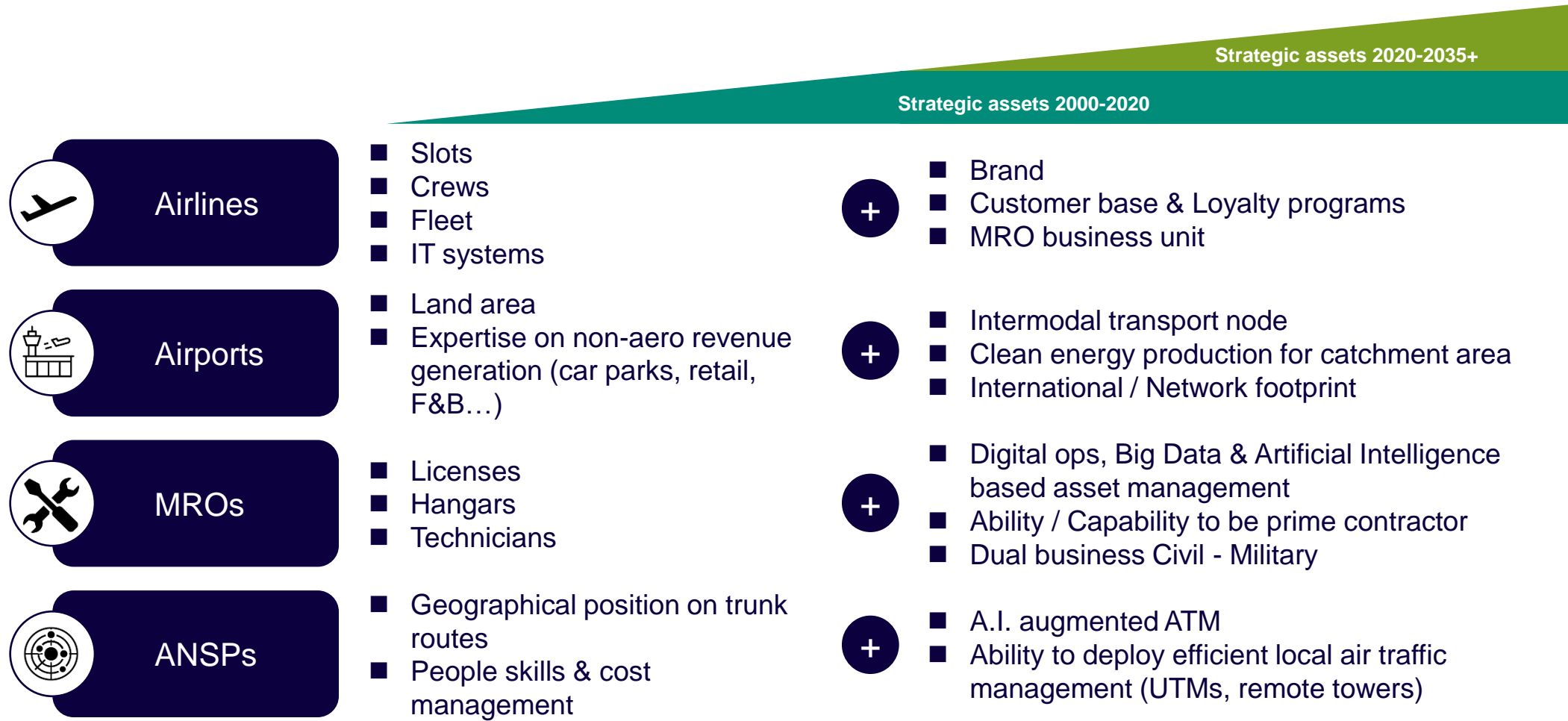
2

## Improving performance: the usual 3 tactical business golden rules = Sweating the assets, Simplifying, Monetizing (example for airlines & airports)



3

## Innovating the business: leveraging & monetizing new assets in order to augment the business model of each party ?



4

# An upcoming consolidation among airlines should happen, shifting the bargaining power in their favor and increase competition among, airports to attract traffic

## The case for further consolidation in Europe ?

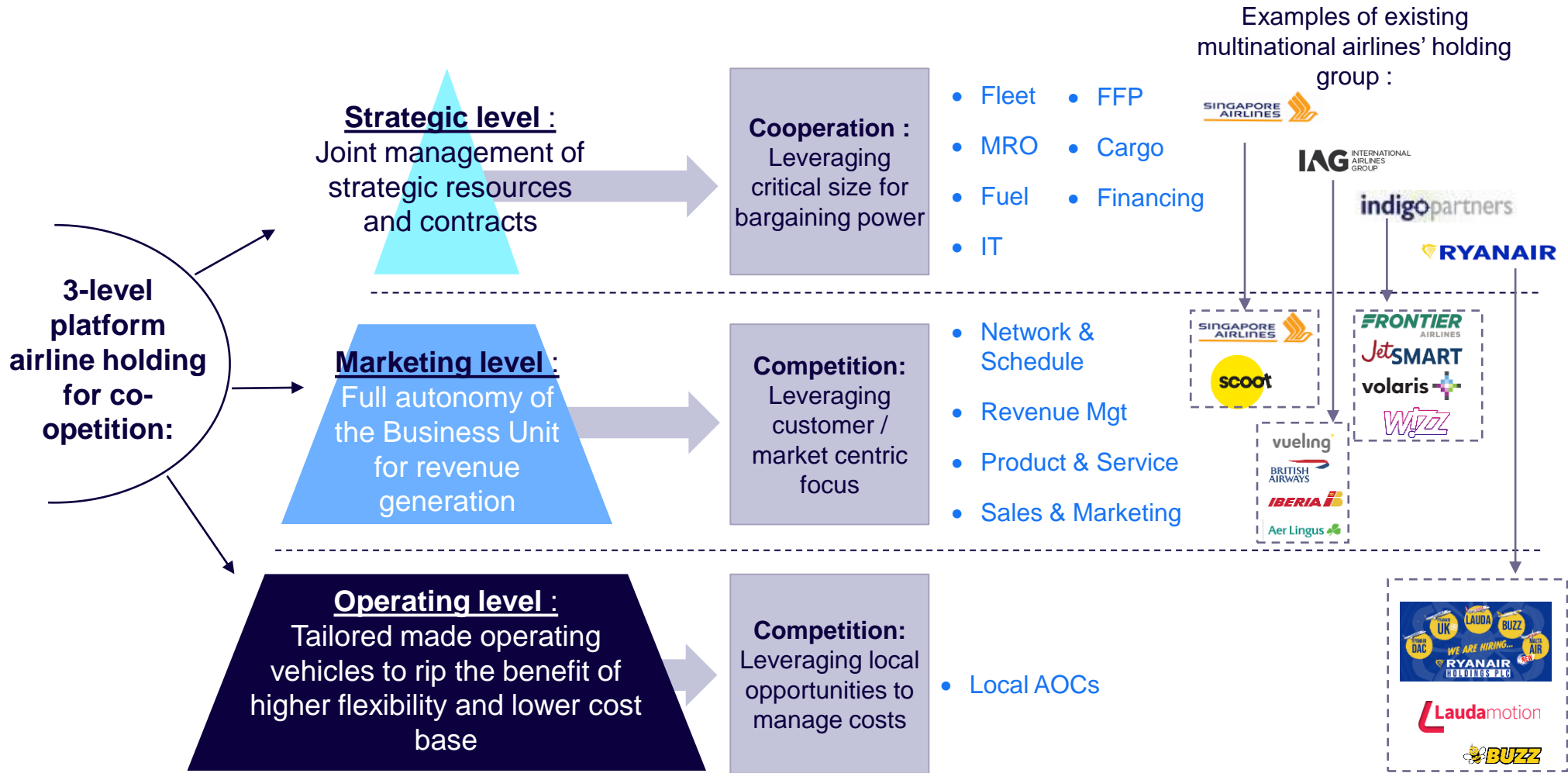
## Candidates for consolidation in European sky ?

Share of intra-Europe/intra-US traffic by actors in 2019 (in %)



4

# A game changer for airlines would be to reach critical size, by creating “ad-hoc JVs” or by partnering with a performing multi-airline brand holding group





4

## Consolidation trend among Ground Support Services providers is also on going and should accelerate

### Critical size advantages

#### COST OPTIMIZATION

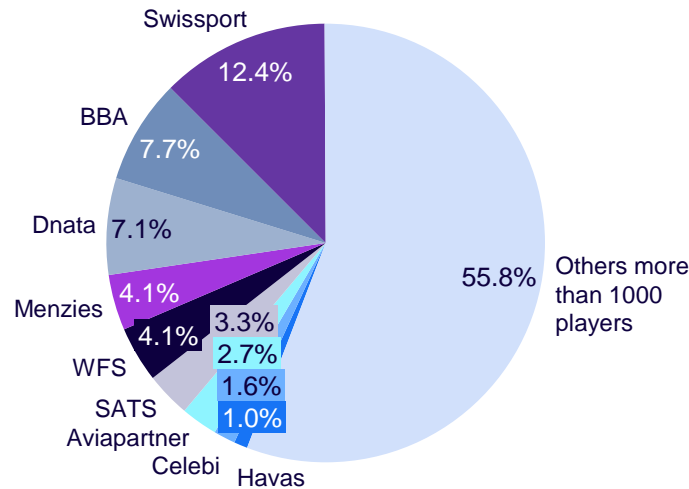
- Ability to lower procurement costs
- Ability to standardize operational processes & practices and to leverage IT / Digital solutions
- Ability to mutualize asset utilization across stations
- Ability to leverage shared service centers

#### REVENUE PROTECTION

- Geographical risk mitigation at global level
- Customer risk mitigation at global & local level

### Ground Handling Industry

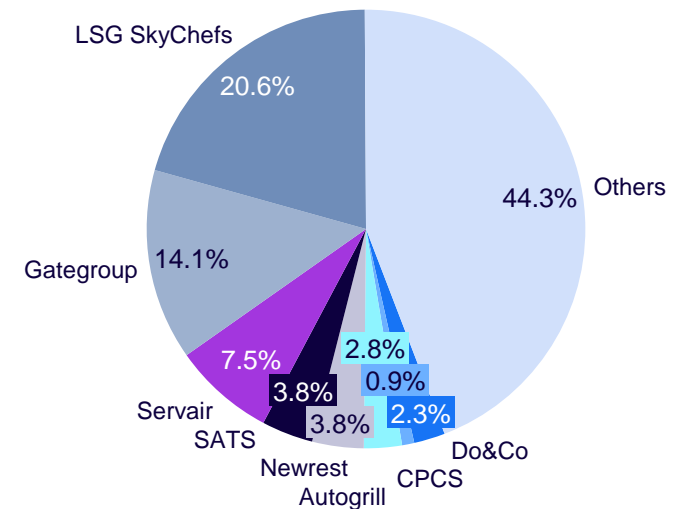
Total open market value : ~15Bn\$  
(open market : ~45%)



**Top 9 = 45% of global market**

### Catering Industry

Total market value : ~20 Bn\$



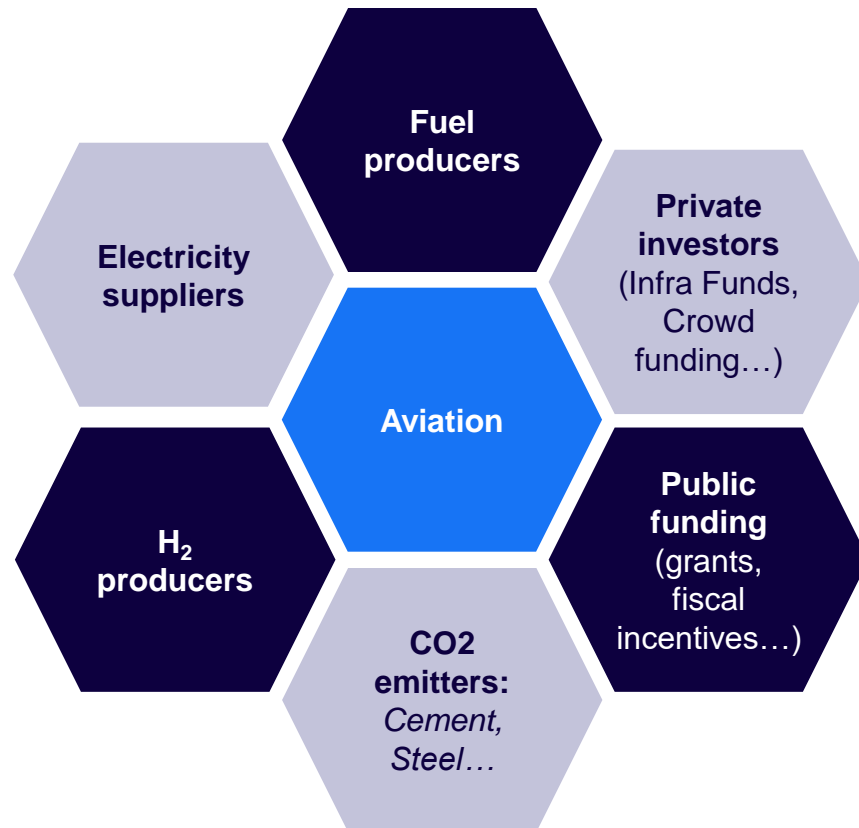
**Top 8 = 50% of global market**



5

# Aviation should build **new coalitions** to invest in the transformation towards Clean Energy and accelerate it

The perfect coalition for Clean Energy in Aviation ?



Case study : main partners in Project WESTKÜSTE100... without Aviation !



Where is Aviation ?

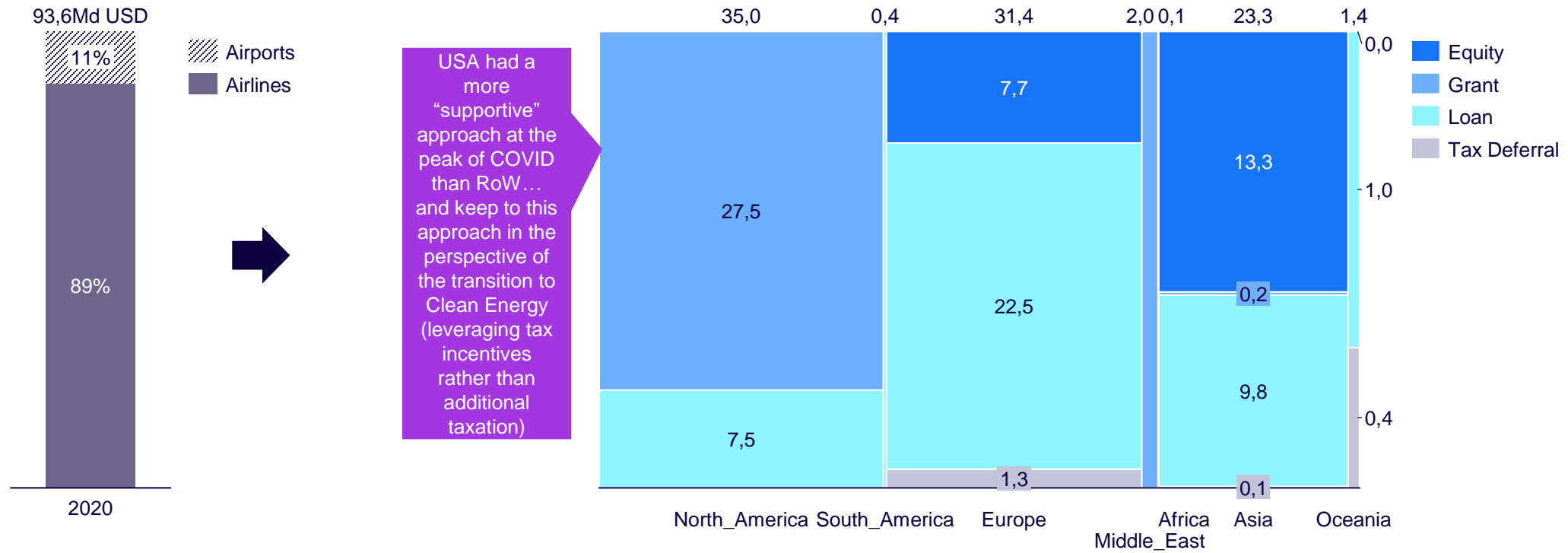
6

# Government « invested » ~90bn\$+ in the air transport industry during COVID, with airlines grabbing >90% of it... but with debt dominating, except in the USA

## Governmental support to the aviation industry per geography and per financial instrument type

- April 2020 -

Not considering Wage subsidy schemes

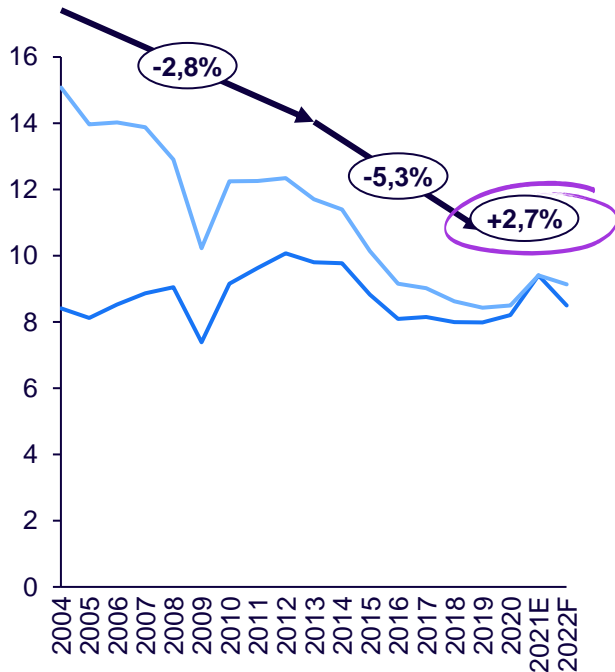


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**Consumer pocket (airlines): ability to increase prices will be key, whilst in COVID period airlines were not capable to repeat their past performance in terms of increasing profit generation**

**Price evolution**

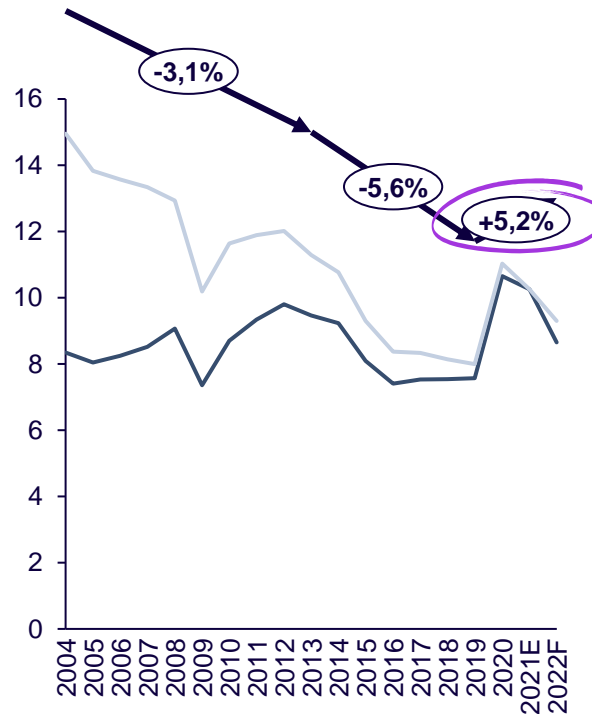
(revenue per ASK, US\$ cts ,world)



— RASK (\$cts) - Nominal  
— RASK (\$cts) - Real in \$2021

**Expenses evolution**

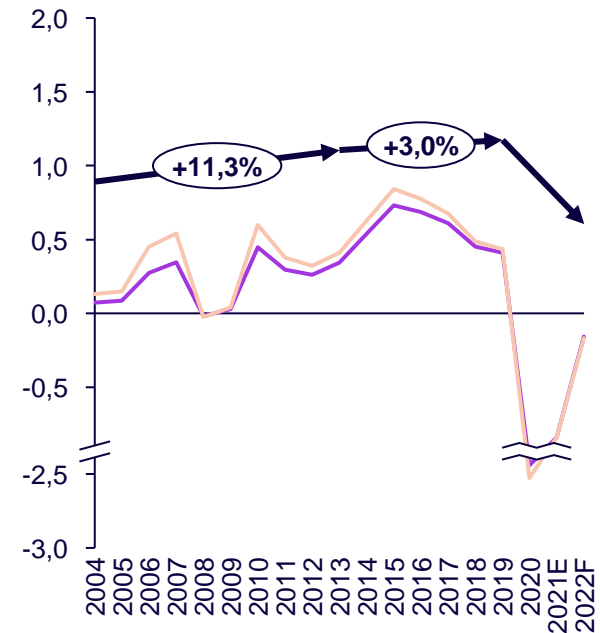
(Expenses per ASK, US\$ cts ,world)



— CASK (\$cts) - Nominal  
— CASK (\$cts) - Real in \$2021

**Operating profit evolution**

(Op. profit per ASK, US\$ cts ,world)



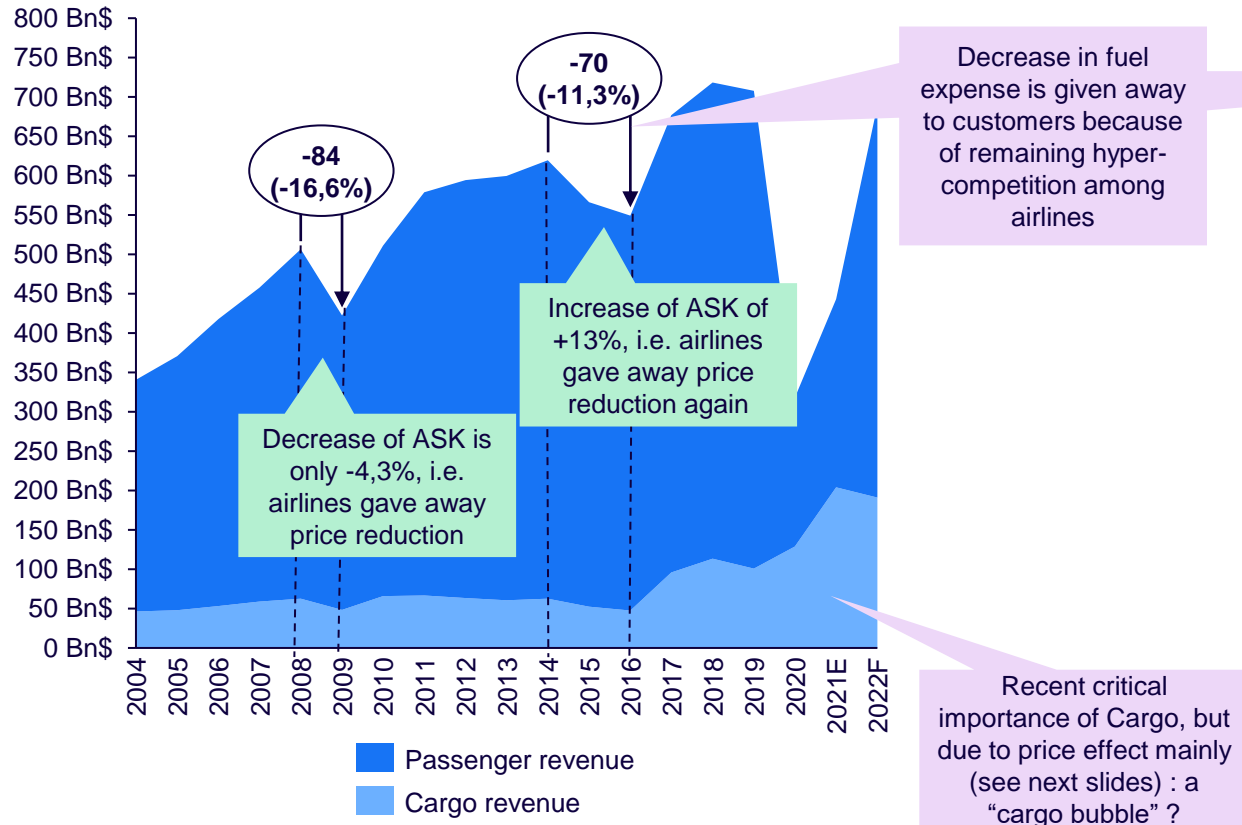
— Op. Profit per ASK (\$cts) - Nominal  
— Op. Profit per ASK (\$cts) - Real in \$2021

7

## Consumer pocket (airlines): hypercompetition prevents airlines to pocket-in gains from lower fuel cost and is hampering profitability of the industry, consolidation will be key

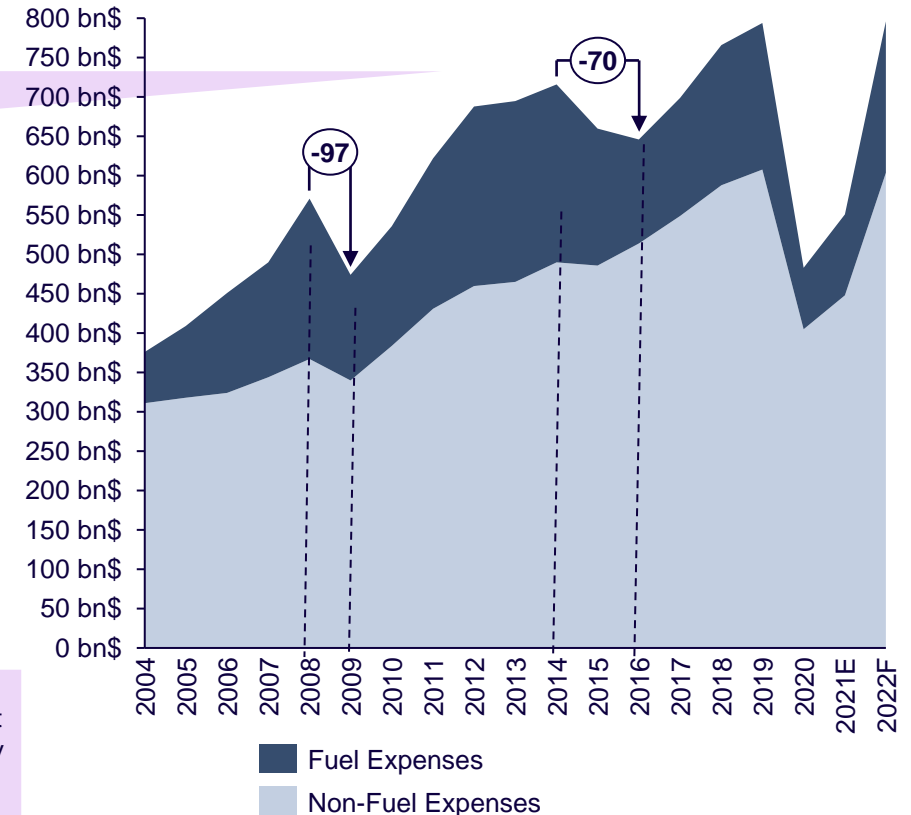
Historical airlines revenues per activity

- World, in BnUS\$ -



Historical airlines Expenses

- World, in BnUS\$ -

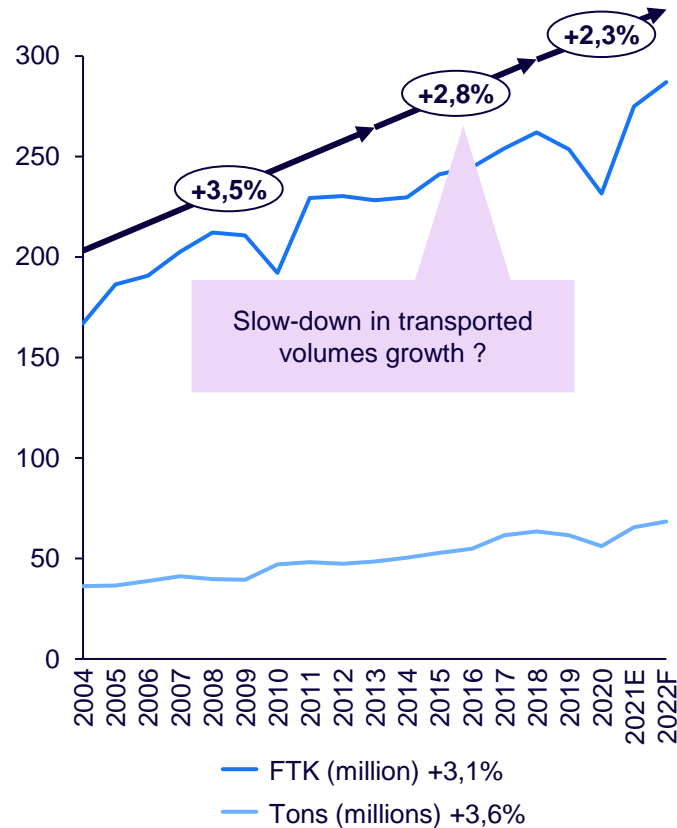


7

# Consumer pocket (cargo): the next bubble ? Historically slowering growth, flat yields... but recent hike thanks to capacity gap belly vs full cargo: what if with pax recovery and global trade slow down ?

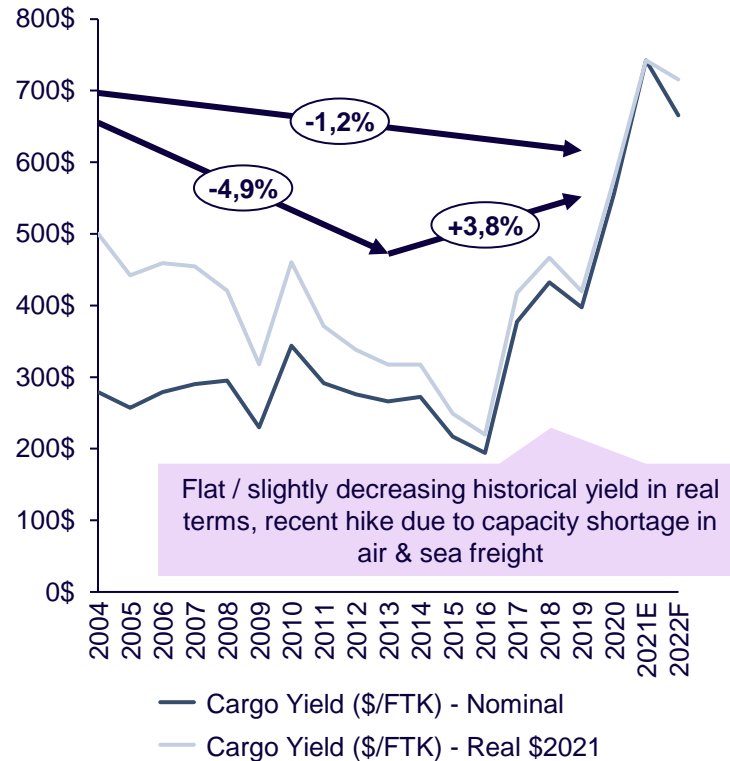
## Airline industry cargo volumes

- World, in FTK produced and Tons transported -



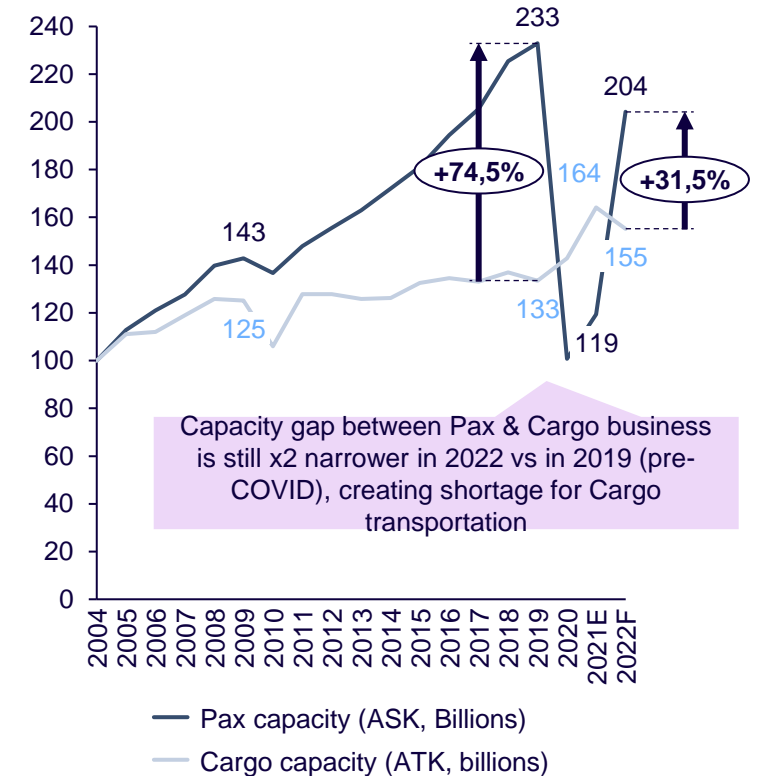
## Airline industry cargo yield

- World, in US\$ per FTK -



## Capacity gap Pax vs Cargo

- World, ASK vs ATK index 100 in 2004 -

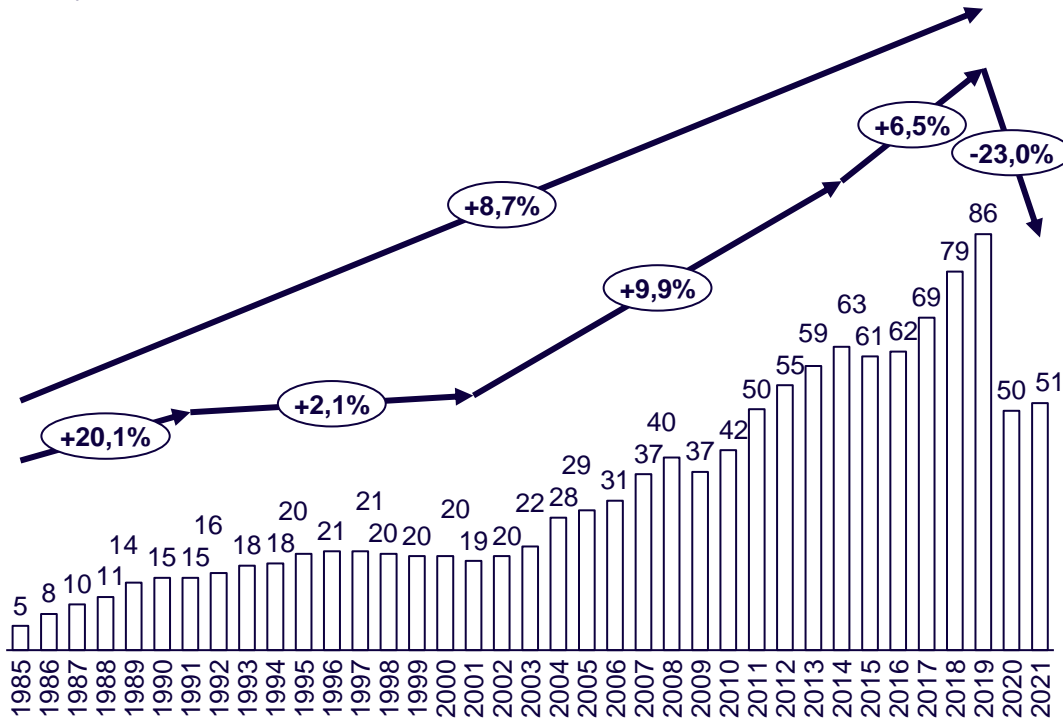


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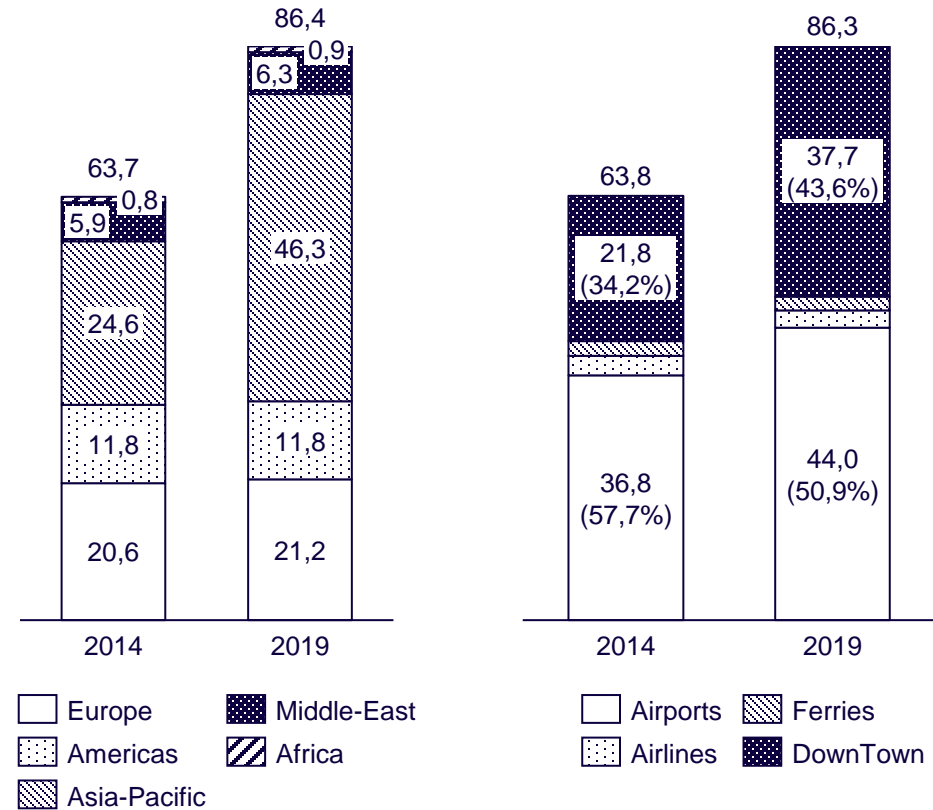
**Consumer pocket (airports):** Travel retail experienced a tremendous growth in 2001-2019... but started to slow down in 2015 and was pulled by Asia & DownTown rather by Airport channel

**Duty-Free market :  
an exceptional growth post 2001**

Duty Free market value, Bn\$ and CAGR



**Duty-Free market :  
growth engines since 2014**



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