

Article



Aircraft Asset Backed Securitizations: Soaring New Heights

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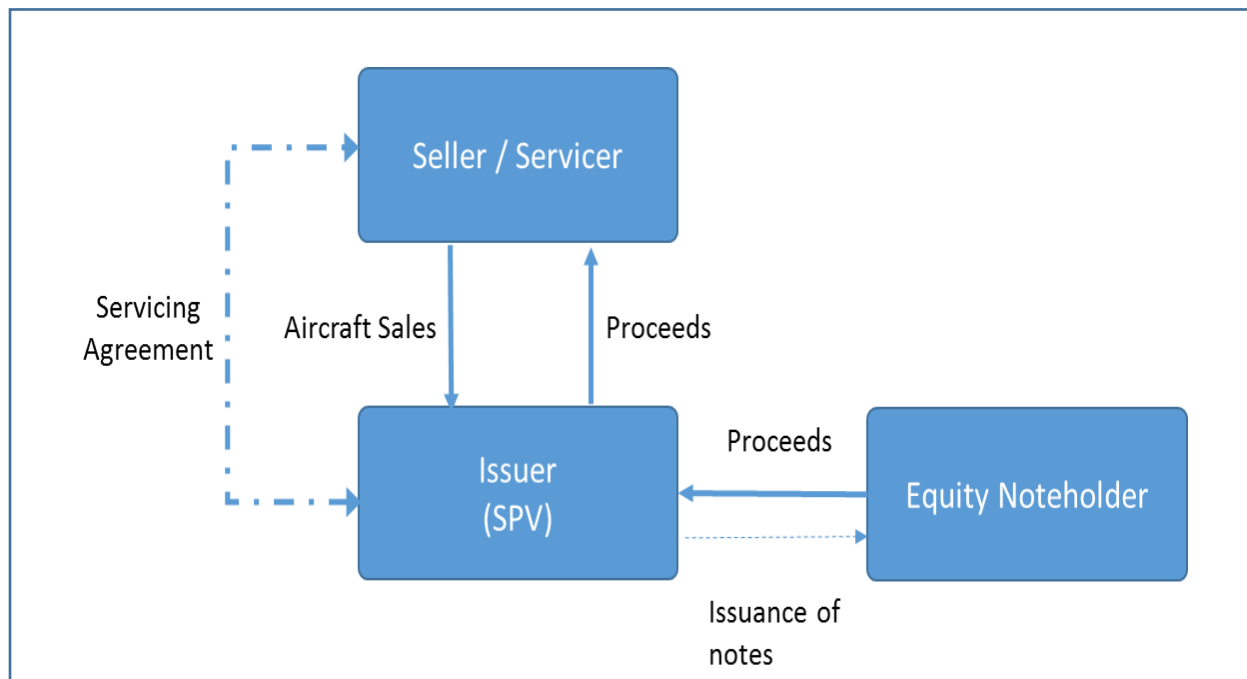


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2015 saw Asia's first aircraft securitisation, wherein Singapore-based BOC Aviation Pte Ltd sold \$747.44 m worth class A notes and \$60.53m worth class B notes¹. Class A and B notes carried a coupon rate of 4.75% and 5.75% respectively. The transaction contained a portfolio of 24 aircrafts and their associated operating leases. The transaction is an addition to the increasing demand for aircraft based securities.

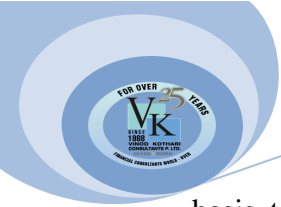
What is aircraft asset based securitisation?

In case of aircraft securitisation the aircrafts let out on lease are sold to the SPV. The pool of aircrafts along with the lease rentals receivables are used to pay the asset-backed securities. The diagram below shows a simple aircraft securitisation structure:



The transaction structures that are prevalent in aircraft securitisation are enhanced equipment trust certificate ("EETC") securitization and the portfolio securitization. Under EETC structures a single corporates/ lessees' creditworthiness is enhanced by using tranching, liquidity support and the residual value of the aircrafts. Traditional equipment trust certificates ("ETCs"), backed by an aircraft and its lease rentals. The first EETC transaction was done in 1994 by Northwest Airlines. Outside of the US, the first transaction was the 1998 issue of Ansett Australia. Contrary to this, under portfolio securitisation, the assets comprises of pool of aircrafts on operating lease

¹ <http://www.globalcapital.com/article/trpqgmmp0d2j/boc-aviation-soars-with-asias-first-aircraft-abs>



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basis to a number of airline companies. The first portfolio securitization was Aircraft Lease Portfolio Securitisation Limited 92-1. In essence, portfolio securitisation are backed by the functioning of the aircraft lease market on the whole and the expected residual value of various aircrafts in the portfolio whereas EETC concentrates on enhancing the creditworthiness of a single lessee. Both the structures are fairly established structures and commonly used in aircraft securitisation.

Recent aircraft securitisation structures²

Earlier, the structuring of the securitisation transactions were such that the lease rental receivables were considered as the only source of fund to repay the investors in an aircraft securitisation transaction. However, the same was not feasible for investors in the securitisation transaction, since they were interested in holding the aircraft for a shorter period and disposing the same once it did not fit their investment profile. Keeping the same in mind, nowadays, transactions are structured in a manner that more reliance is placed on the revenue to be collected from the sale of aircrafts rather than the lease rentals.

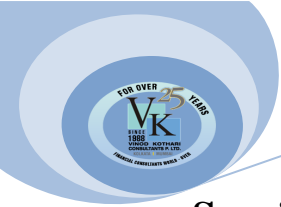
Further, the asset pool has become diversified, which was not the case erstwhile where only balance of Boeing and Airbus narrow-body and wide-body aircraft, with an overall aircraft portfolio age of less than seven years at closing formed part of the portfolio. Also, new securitisation transactions are providing servicer incentive fees in addition to the fees paid to the services under the service agreement. This incentive is provided with the intent of increasing the efficiency of the servicers in performing the timely collection of rent and other ancillary services pertaining to the lease of the aircraft. Even though such fee is subordinate to the payment of debt service, it will not be wrong to say that it is highly likely that due to the additional incentive fees a servicer may receive double the servicing fees over the life of the transaction.

Another interesting reform is of providing step-up interest on obligations that have remained outstanding post the scheduled final payment date. Such was not the case earlier and as a result, investors were receiving very low rate of return, calculated over the life of the transaction. Also, securitisation transactions containing aircrafts with an older weighted average life are structured in a manner that they provide for accelerated amortisation starting mostly on the fifth year of the issuance. This has been done with the intention to protect investors.

Further, these days' securitisation transactions are required to have a minimum debt service coverage ratio requirement. Thus when a securitisation is unable to generate enough cash during any consecutive payment dates in order to meet the debt service coverage ratio requirement, issuers may trap all excess cash remaining after the payment of all senior notes to meet the same. This results in providing a collateral for the shortfall of cash flow generated by the securitisation.

In the past few years, the spree of reforms have resulted in favoring aircraft securitisations, thereby making the same more appealing to leasing companies and aircraft portfolio owners.

² https://www.kattenlaw.com/files/127053_Aircraft_portfolio_securitisation_innovations_and_regulations.pdf



Soaring Heights

In the past years, aircraft securitizations were mainly undertaken in the US wherein the same was promoted by the operators and attracted a vast investor base. The rest of the world did not catch up with the same until 2013, when various non US entities namely Air Canada, British Airways and Virgin Australia undertook EETC securitisation transactions amounting to a total of \$3 billion³. Popularity of aircraft securitizations mainly depends on the demand of the underlying assets, favorable rate of returns and various promising credit enhancement features. With the addition of the first Asian aircraft securitisation, the aggregate transaction value of aircraft securitisation reached a soaring height of US \$4.5bn⁴, approximately, in the year 2015. It is expected that the same will continue to rise in the current year as well.

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³ <http://www.airfinancejournal.com/Article/3441268/Analysis-Non-US-EETCs-enter-the-market.html>

⁴ http://www.tmf-group.com/en/media-centre/news-and-insights/january-2016/aircraft-abs?utm_source=Mondaq&utm_medium=syndication&utm_campaign=View-Original