

## Buyers' Guide Articles

**Financing Your Business Jet**

By Jeff Wieand - July 2010

Business jet finance probably hit bottom in early 2009. Loans have become much more available since then, but we've yet to return to the halcyon days of 2007, when you could readily arrange 100 percent financing for aircraft at purchase prices that today seem grossly inflated. As Bank of America's Michael Amalfitano pointed out, "The days of aggressive deals at thin pricing are over."

Nevertheless, things are looking up, and financial institutions are returning to the market. First Republic Bank's Jim Simpson reported that he hasn't been this busy in 18 months. And PNC Bank had its best year ever in terms of the dollars of aircraft financing, said the bank's aircraft lending chief, Wayne Starling.

A key factor in aircraft finance since 2008 has been the backlog of repossessed airplanes. When borrowers began to default on loans and walk away from leased aircraft in 2008 and 2009, financial institutions found themselves with a swollen inventory of repossessed jets, which have been hard to sell at anywhere near the amount of the institution's investment in them. Given the many available aircraft and today's lower prices, lenders and other jet owners often look for people willing to lease the airplanes for a few years to allow time for values to recover or at least let the owner postpone recognizing a loss.

Suitably chastened, lenders are extremely cautious—probably too cautious—about aircraft values. This caution is exemplified by an increase in the amount of due diligence financial institutions require to make sure the airplanes they finance are worth the prices clients are paying.

Concern about values has also affected lenders' appetites for certain models and vintages. As jet values fell over the last 18 months and more aircraft were listed for sale, the lower end of the market—older business jets and models—took an especial beating. As one lender told me, "We want to stay with aircraft in the five- to 10-year-old range or newer, if possible." This is particularly true when the financial institution is buying the jet to lease it back to the customer. An airplane that's 10 years old today may be 20 years old when the lease ends, and no lender wants to own an aged and potentially unsellable business jet.

The good news about the decline in aircraft prices is that it has encouraged buyers who were waiting in the wings to come forward. Thus, for some aircraft models, especially large and long-range jets, prices have actually started recovering, though they have yet to return to pre-2008 levels. Even so, lenders are likely to require a careful look at the value of the airplane being acquired.

Lenders are also doing their homework on buyers. As one industry pundit noted, while a buyer with "pristine credit" will engender a "feeding frenzy" among lenders, other buyers are unlikely to encounter similar enthusiasm. Those coming from a troubled industry, like real estate, may face special scrutiny. Lenders are also taking a hard look at their own previous experience with the potential borrower. Has the borrower over-extended itself in the past or missed payments on other credit facilities? What changes have occurred in its financial position over the life of the relationship? Lenders are interested, too, in whether the buyer has another aircraft it will be trying to sell after taking delivery of the new jet—not only with regard to the buyer's ability to bear the financial burden of two airplanes, but also because the lender may already have credit exposure on the first one.

The message in all this fuss about values and credit is simple: don't wait until the last minute to seek financing. Finalizing an aircraft finance deal is no longer simply a question of preparing paperwork. Lenders need time to assess the airplane and the customer. What formerly could be accomplished in a week or two can now take a month—or longer (though as one industry expert observed, if the financing can't be finalized in a month, it probably won't get done at all). As the process drags on, many creditworthy borrowers lose patience and end up forgoing financing and paying cash. So if financing is important to your acquisition, plan ahead.

Probably the biggest challenge in today's market is arranging 100 percent financing. It's not impossible, and many financial institutions claim to offer it for clients with "strong" credit, but in fact most transactions involve 10 percent down or more. One lender told me that he routinely begins with a request for 15 percent down, which he hopes he can reduce to 10 percent based on the customer's credit position. The down payment may effectively be 100 percent at the outset if you're financing progress payments on a factory-new aircraft. Many lenders will want you to have enough of your own money in the deal to cover any damages to which the aircraft manufacturer might be entitled if you default.

Interest-rate spreads are also much larger than before the 2008 market crash, but the rates themselves still represent a pretty good deal. As of this writing, 30-day LIBOR is well below 50 basis points, so even though the spreads are many times their pre-crash multiples, the overall interest rate remains relatively low—somewhere between 300 and 700 basis points, depending on the credit and whether the deal is fixed or floating. For this reason, said Joe Boles at Siemens Financial Services, “Most aircraft buyers today are choosing fixed rates.” Alternatively, borrowers should consider taking advantage of currently low floating rates and negotiate an option to switch to fixed rates if they become attractive.

Of course, the flip side of low rates is low returns on investments. Thus, according to Michael Amalfitano at Bank of America, “Cash is now being used for about 75 percent of private aircraft purchases, versus about 50 percent prior to the downturn, because returns for idle money are not as high as in the past.”

Similarly, the term of financings these days is often relatively short. “Although amortization schedules today are longer,” said Sean Patrick at Commerce Bank’s CBI Leasing, “many of our business aircraft customers want shorter-term deals because the rates are lower.” He sees most lease financings at CBI in the five- to seven-year range and loan financings in the three- to five-year range.

Where should you look for jet financing today—banks, which common wisdom says are in trouble now, or financial institutions connected to aircraft manufacturers, insurance companies or other businesses?

It’s an important question. Some banks shy away from aircraft lease financing while others actively look for it. A bank may also require you to be an existing or about-to-be significant client. In any case, being an existing customer can speed the credit approval process and encourage the bank to put an attractive offer on the table.

But it also can kill the deal. If the bank and its affiliates are already burdened by a layer of relationships with you (such as margin loans, loans against real estate or, in the case of corporate clients, membership in a bank loan syndicate), the bank may conclude that it has enough credit exposure to you already. A non-bank aircraft financial institution, on the other hand, is unlikely to have other credit relationships with you (except, perhaps, on an existing aircraft) and won’t be requiring deposits or some prior relationship to get the deal done. And some banks, such as Key Equipment Finance, attempt to insulate the aircraft lending business from their other credit exposures. In the end, both kinds of institutions may have something to offer and they both deserve consideration.

Specialized financing needs may narrow the field. Borrowers interested in non-recourse financing, for example, will be turned away at many banks, but not at PNC Aviation Finance, a leader in this area. Though you can count on having to make a hefty down payment with non-recourse financing, the actual interest rate can be close enough to recourse rates to make the deal appealing.

With financing becoming more challenging to obtain, it’s wise to solicit proposals from several institutions. You might also seek advice from a consultant. “We not only help find the best rates and terms,” said Stan Yockey of Strategic Aircraft Solutions, “we can also find financing where none appeared available.” Some consultants, like Mike Gaffney at JetEquity Solutions, have many years of experience working for corporate aviation lenders and know the business from the inside.

These are sobering days for aircraft finance. Lenders aren’t giving it away, but with a little effort, you should be able to find financing that is right for you.