



Restructuring Lifecycle

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Early Warning Signs

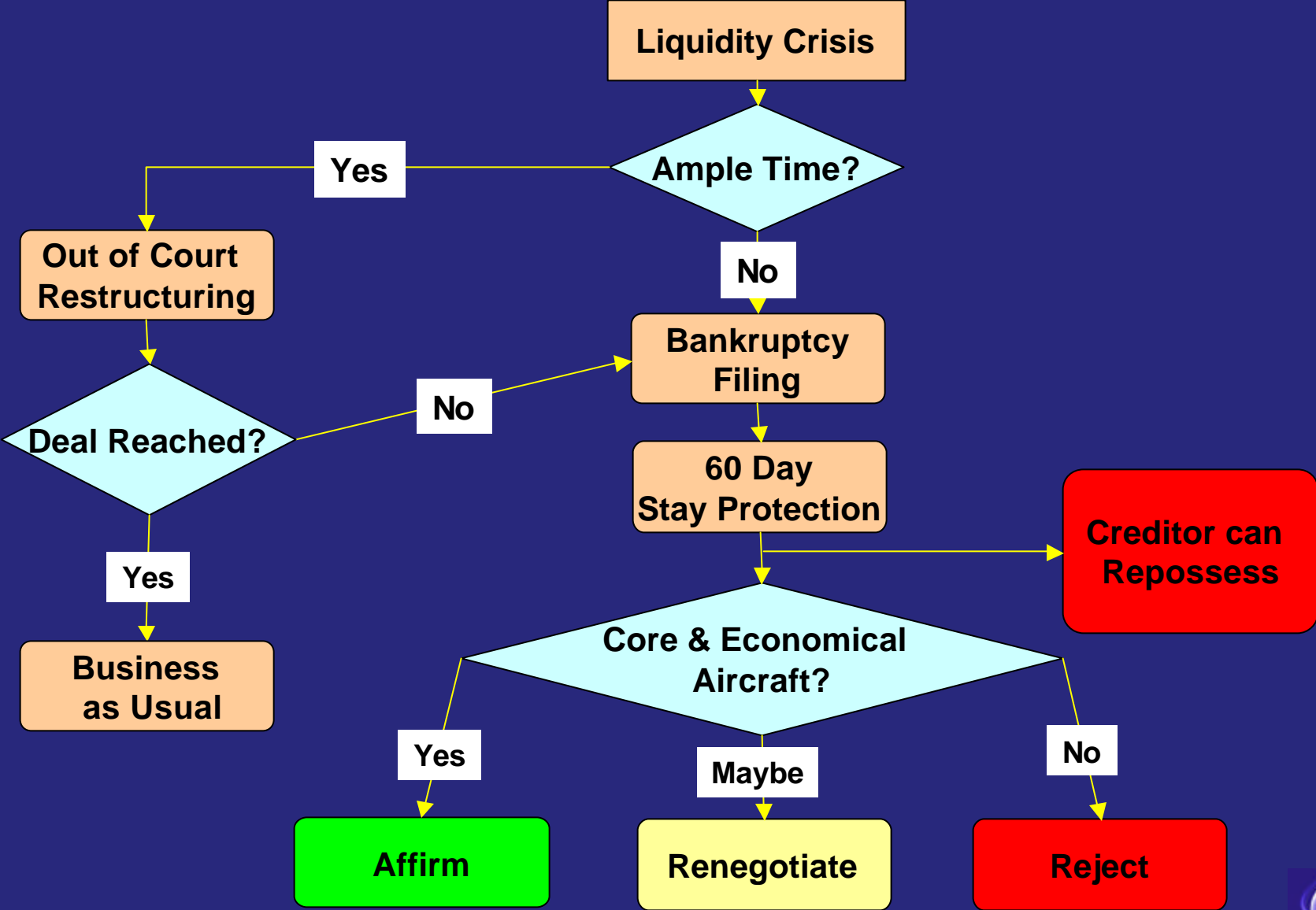
- Airlines usually die the “death of a thousand cuts”
- Deterioration in performance and credit protection measures
 - credit ratings, debt maturities, cash drain usually caused by an event- economic downturn, etc
- Monitor bond pricing and spreads
 - How distressed is it?
- Under Fair Disclosure Act, Management is generally required to disclose the possibility of a bankruptcy once it becomes likely
 - Is there a DIP financing in the market?
 - Have bankruptcy counsel or financial advisors been hired?



Necessary Actions

- Assess your exposure
 - Consider the “what if” scenario
- Inform Senior Management
 - No Surprises.
- Appoint Advisors
 - Re-marketing, Technical, Legal
- Consider possible sale of exposure
- Exercise inspection rights
 - If documents allow, have aircraft inspected and obtain maintenance records on aircraft and title engines
- At this point, you remain bound by the documents





Out of Court Restructuring

- Generally an attempt to restructure before a possible bankruptcy filing
- Many airlines seek out of court lender / lessor concessions
 - America West, AMR, UAL, ATA and US Airways
- Out of court restructuring is more difficult, but preferred to an in court restructuring
 - Very expensive and time consuming
 - Can sour relationships
 - Customer perspective is negative



Out of Court Restructuring

- Leverage- Prior to bankruptcy, the creditor is in control
 - The airline must honor its contractual commitments
 - In a syndicated transaction, amendments to pricing and paydowns require 100% consent agreement of all creditors
 - EETC's not usually affected
 - Too many parties to deal with
 - Consents difficult to obtain
- Do not be afraid to stand your ground



Out of Court Restructuring

- Concessions
 - A deferral of principal and interest
 - Principal forgiveness
- Considerations
 - You have leverage- **USE IT**- inspect your aircraft
 - Don't be fooled by relationship plays
 - Conceding now does not offer protection if bankruptcy ensues
 - Airlines will not offer "most-favoured nation status"
 - Lenders may be stuck with higher outstandings and LTVs



Considerations for Out of Court Restructuring

- How material is your participation?
 - AMR 10% (\$200 million) of concessions came from creditors, 90% (\$1.8 billion) came from unions
- What will happen to your assets if the airline files?
 - Affirmed, negotiated or rejected
- If concessions are made
 - Higher loan to value to a weak credit
 - If the company survives, your loan will ultimately be repaid
 - If the company subsequently files then you are in a worse position



The Next Step - Bankruptcy Filing

- The airline is in control
- All deals are up for re-negotiation
- The relationship becomes adversarial
- Stay on payments for 60 days
- Be prepared for a long hard struggle!



Parties Involved

- Creditors
 - Lessors
 - Lenders
 - Advisors
 - Agent Banks, Lawyers, Technical advisors, Re-marketing Agents
- Trustees
 - Act as instructed, according to documents
- Lender / Lessee
 - Airline
 - Airlines Advisors
 - Lease Advisors, Bankruptcy Advisors, Lawyers, Technical Advisors



Protection for Lenders and Lessors

- Section 1110
 - The section stipulates that an airline must resume payments and cure all defaults on aircraft financings within 60 days of filing or risk repossession of the aircraft
 - This Stay for 60 days may be extended by mutual agreement between airline and creditor
 - Very important- has not been successfully challenged in the US as yet- cornerstone of the EETC market



Protection for Lenders and Lessors

- Section 1110 allows for four scenarios
 - S1110A- Airline maintains contractual payments and creditor may not take aircraft back - “Affirmation”
 - S1110B- Airline does not make payments, but agrees with the creditor to extend the stay period. In this case creditor chooses not to take back the aircraft - “Re-negotiation”
 - S1110C- Creditor seeks the return of the aircraft as attempts at renegotiation fail
 - Rejection: The airline files a motion to reject the lease as it is considered uneconomical to maintain it in the fleet
- These concepts exist in most airline bankruptcies
 - In the US it has a legal form
 - In other jurisdictions it is a practical matter



Protection for Lenders and Lessors

- If aircraft is core to the fleet and economical- Airline will generally opt to affirm the leases and file motions for S1110A.
- If aircraft is core to the fleet, but the lease rates/payments are too high - Airline will seek to renegotiate and file for S1110B.
 - **Seeks to retain aircraft assuming new deal can be cut- often conversion from finance to operating lease.**
 - **Usually involves older aircraft.**
- If airline seeks to renegotiate, but terms are unattractive, the creditor may seek repossession and file S1110C motions.
- Rejection of aircraft airline does not want happens quickly. An initial wave of rejections followed by rejections over time.



Strategic Considerations

- Do You Want Your Aircraft Back?
 - Combination of type of aircraft and re-marketability
 - Some lenders do not want the aircraft back under any circumstances
- How much control have you?
 - After a default - Simple majority. What are the views of your co-lenders?
- Is my aircraft of value to the airline?
 - Core fleet?
 - Is it useful to anyone else?
 - B767-400ER?



Negotiating Tactics

- The EETC investors are diverse and have to interact through the trustee in order to negotiate, hence they generally organize to establish a controlling interest
- The private lenders tend to negotiate on their own
 - Try and cut a single aircraft deal
- If it can be made to work, a group is preferable
 - So many differing agendas very difficult to implement.
- The airline's strategy is generally to divide and conquer



Possible Outcomes

- Affirmation- Original payment stream continues
- S1110A-Without Affirmation of the lease
 - Airline maintains the option to reject aircraft or renegotiate
 - May make payments but seek deferrals, cash flow relief
 - Fact that they are making payments means that creditor has no ability to repossess
 - Generally represents a desire to keep the aircraft



Negotiation Tactic

- The Advisor/Airline contacts the lenders with proposal / term sheet
- The proposal is an attempt to “mark the transaction to market”
- Significant pressure will be applied to “do the deal quickly”
- No real incentive
 - Airline is not committed to the transaction and can change terms
 - Finality very difficult to achieve
- Note that if a change of structure is contemplated then a “rejection” may occur
- If the airline is negotiating then it wants the aircraft assuming a deal can be reached



Negotiating Tactics

- At this point the airline will be trying to lock in the best deal for itself for the future. It will be an attempt to lock in a deal at the cheapest cost possible
- Expect terms and conditions that are unacceptable in a normal market.
 - Return Conditions
 - Lease Rates
 - Tenor
 - Insurance
- The airline will try to shift all costs and most of the risk to the lenders
- Group negotiations are favorable



Rejection / Repossession

- Rejections based on a proposed fleet plan
 - Likely to reject the most expensive and least efficient older aircraft
- Airlines consider return conditions as per original contract to be non-binding
 - Aircraft will be delivered in an “as-is”, “where is” condition
- Lenders may be faced with pilot, crew, fuel, insurance costs
- Squeezing out equity/ unraveling structures can be time consuming
- Deals are often struck post rejection
 - Often only the truly surplus aircraft are rejected at the end of the day



Final Stages

Once the fate of the aircraft is determined:

- Term Sheets/MOUs are drafted, for aircraft to be retained
- Motions to reject aircraft are filed
- Administrative claims are determined and negotiated
- Final documentation is negotiated and completed, once the deal is approved by the court
- Airline files a plan of reorganization and once approved by the court, it emerges from bankruptcy protection



Hierarchy of Claims

- Secured Credit/DIP
- Administrative Claims
- Priority Claims
 - Wages, taxes (previously owed), etc.,
- Unsecured Pre-petition Claims
- Equity Interests



Pre-Petition Claims

- Claims made based on contract in place prior to the date of filing
- On the return of an aircraft post rejection
 - Costs incurred in restoring aircraft to the condition which is described as “return conditions” in the documents become part of the pre-petition claim
- The Proof of Claim is filed with the Bankruptcy Court and generally receives 5-10 cents on the dollar



Administrative Claims

- Claim based on actions taken post bankruptcy (i.e. airline continuing to fly aircraft after the initial 60 day stay period)
- Airline cannot emerge from bankruptcy without having settled the administrative claims
 - The administrative claims are part of the re-organization plan
 - Paid at 100 cents on the dollar on the permitted amount



Summary

- **DON'T PANIC!** It will be awful and is likely take a long time, just deal with it!
- **Know Your Assets, Do your homework!**
 - \$25,000 spent pre-bankruptcy on an inspection is minimal compared to the cost of bankruptcy
- **Use leverage in the pre-bankruptcy stage to prepare for bankruptcy**
 - Assess if you have any leverage during bankruptcy
- **Know your co-lenders and their views, don't waste time fighting battles that cannot be won**



Conclusion

- The odds are in favor of the airline, unless you have unusual leverage
- Your goal is to ensure that you do as well or better than other creditors in a similar situation



Questions

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