
**MARKET ANALYSIS:
INFLATION OFFERING ORDERBOOK
SOLUTIONS?**

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These services include:

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- Intangible Assets
- Enterprise Valuations.

Analytical:

Recognized as a premier aviation consulting firm, mba's team brings over 150 years of combined industry experience to public and private clients.

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mba's Asset Management Team is comprised of seasoned aviation professionals encompassing years of experience within flight operations, engineering, and maintenance.

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The Paris Air Show will likely see a slew of new orders for commercial airliners again. The post-pandemic travel rebound is happening and will continue strong in the long-term according to mba aviation's expectations. Together with the relative shortage of aircraft caused by supply chain and other issues over the last few years this has made both airlines and lessors come to the OEM's bargaining table yet again. The outcome of these discussions will be announced over the next few days.

Ordering aircraft is a complicated matter. It involves forecasting demand years into the future and negotiating on multiple items in the contract, including but not limited to:

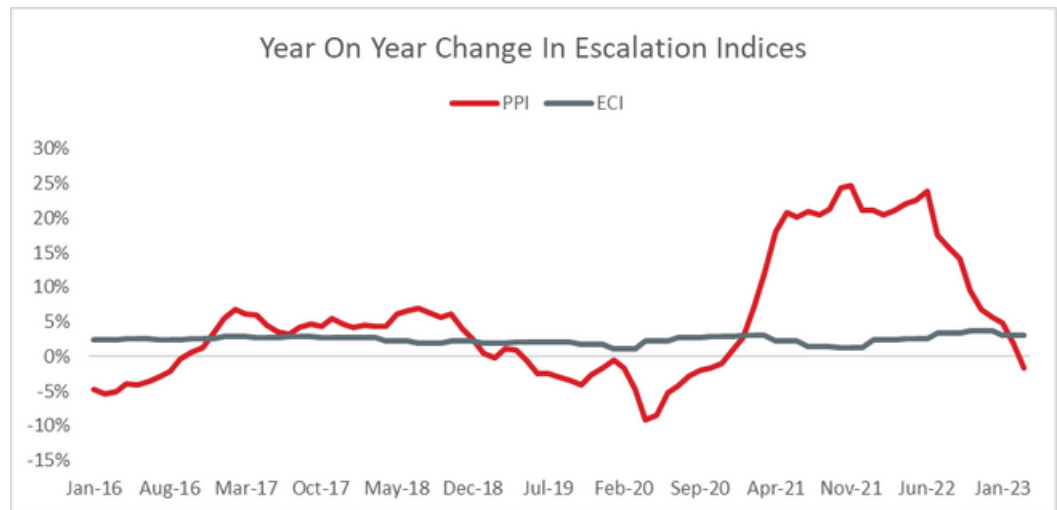
- Base price and discount levels – including non-monetary assistance like training, support, etc.
- Basic spec and the cost of adjustments
- Timing of deliveries, escalation formulas and potential different caps to that escalation

With manufacturers struggling to deliver certain aircraft according to the agreed schedule right now – a problem originating from the pandemic, deferral agreements, cuts to production rates and supply chain issues – the industry has been presented with a temporary solution that enables players to flex their agreements and align better with their wants and needs.

Most aircraft orders are signed with deliveries happening a few years in the future and include escalation clauses to cover inflation in manufacturers costs. These are generally linked to two price indices:

- the employment cost index and
- the PPI industry commodities index

Both published by the US Bureau of Labor Statistics. Employment index (wages) is generally stable, while commodities have their own much larger volatility.



These two are averaged according to agreed-upon formulas and recalculated to represent the price growth from the base month of the contract. Because of the way these are calculated, both manufacturers and their customers get certainty of price about 9 months in advance of the final delivery date and this means that we can analyze the orderbook pricing including all of 2023 deliveries.

Using mba aviation's redbook fleet database and publicly available orderbook information we were able to break down the orderbook for the last few years by year of delivery vs year of order for both of the large manufacturers.

		Order Year				
		2018	2019	2020	2021	2022
Delivery Year	2018	57				
	2019	51	55			
	2020	62	21	47		
	2021	91	41	13	63	
	2022	101	60	40	157	44
	2023	142	99	98	232	58

One important feature of the order contracts is the ability for both manufacturer and customer to walk away from the transaction if the final price escalates by more than a certain cap. That number is obviously different for each customer, but mba aviation can suggest that number to be between 4.5 and 5.5% per year. In other words, for any order placed, should the average compound annual escalation rate exceed that figure each party has a walk-away right. Given the inflation of the last few years, this is now a possibility.

		Order Year				
Escalation		2018	2019	2020	2021	2022
Delivery Year	2018					
	2019	4.2%				
	2020	2.4%	0.7%			
	2021	1.9%	0.7%	0.7%		
	2022	3.7%	3.5%	4.9%	9.3%	
	2023	4.7%	4.8%	6.3%	9.2%	9.0%

We have not seen 2022 cancellations in the numbers suggested above (around 76 aircraft were at risk) and exceeding the cap doesn't automatically result in a termination, but this analysis suggests that every 2023 delivery ordered after 2018 will have optionality around it. There are reasons for why customers do not avail of that option despite prices increasing and general shortage of aircraft in a growing market is one of them.

This provides both parties with another tool to use in the negotiations surrounding moving slots around as manufacturers manage their skyline in light of all the issues they are facing mentioned at the beginning.

If you have any questions, comments or would like to discuss any of the above topics in more detail, please contact mba Aviation team at mba@mba.aero.