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Frequent Flyer Programmes: Why So Very Valuable?

IN DECEMBER, American Airlines announced a long-awaited renegotiation of its co-branded credit card agreement. In a ten-year exclusive deal, Citigroup will be the sole supplier of cards linked to American's AAdvantage frequent flyer programme.

The company stated that "the agreement creates an innovative alignment between the Citi ThankYou and AAdvantage card programs and is designed to drive incremental value for both companies and produce a significantly expanded loyalty and rewards offering for AAdvantage members and Citi-branded cardmembers. As exclusive issuer, Citi will take on all American Airlines acquisition channels, including inflight and at airports."

As a legacy from the merger with US Airways and emergence from Chapter 11 in 2013, American unusually had two credit card suppliers: Citi and Barclays. Each supplied different benefits to FFP members for spending in different areas, which some punters — understandably — may have found confusing. From January 2026 Citi will acquire the Barclays' portfolio of card holders.

American mentioned that it expects to achieve an annual 10% growth in remuneration from its co-branded credit cards — which it said amounted to $5.6bn in the twelve months ended Sep 2024 — and that once this revenue stream approaches $10bn (by 2030?), it expects an increment in pretax profits of $1.5bn a year — a pretty hefty 35% margin — and roughly equivalent to the total pretax profit it is expected to report for the whole of 2024. The numbers do not quite tie up with figures in the official accounts (shown in the table on the following page) because of the subtle arts of accountancy; and American does not intend to update the markets on specific results of its affinity programmes.

This issue includes

TOP TEN AIRLINE LOYALTY PROGRAMMES BY VALUE ($bn)

Programme	Airline	Programme Value	% of Airline Market Cap	Implied Airline Value
SkyMiles	Delta	27.9	70%	12.1
AAdvantage	American	23.9	206%	-12.3
MileagePlus	United	22.0	66%	11.2
Rapid Rewards	Southwest	8.8	45%	10.8
Miles & More	Lufthansa Group	8.0	107%	-0.5
Avios	IAG	7.1	37%	11.8
Flying Blue	Air France-KLM	6.9	323%	-4.8
Aeroplan	Air Canada	6.8	137%	-1.9
SkyPass	Korean	4.6	78%	1.3
Cathay	Cathay Pacific	4.6	57%	3.4

Source: On Point Loyalty Jan 2023

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LOYALTY PAYS

$bn	Loyalty Revenue: Passenger†	Loyalty Revenue: Marketing	Loyalty Revenue: Total	% of group	Group Revenue 2023
American	3.6	2.9	6.5	12%	52.8
Delta	3.5	3.1	6.6	11%	58.0
United	2.7	2.7	5.4	10%	53.7

Source: 10K reports.
Note: † miles redeemed.

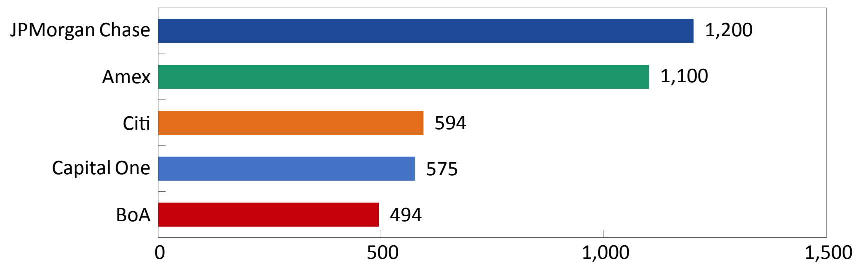
The deal may increase the perceived value of AAdvantage. According to the latest Jan 2023 report from On Point Loyalty, the consultancy valued American's AAdvantage programme at $23.9bn (see table on the previous page), more than twice the airline group's current market capitalisation (the methodology behind the valuation is a bit opaque).

It may also help American catch up with Delta. Its arch rival has a long-standing exclusive deal with American Express and the SkyMiles FFP from which it achieved $6.8bn in remuneration in 2023, and which is said to generate half its annual profits. It too has targets to grow revenues towards the $10bn mark. (Delta bizarrely also has its own Amex charge card, carrying a $1.1bn credit limit, for the purpose of buying fuel and crude oil.)

The credit (or blame) for the first frequent flyer programme — as with many of the developments of the industry in the deregulated era — has been laid at the door of Bob Crandall, former President and CEO of AMR Corp. American's programme AAdvantage was indeed established in 1981, and swiftly followed by United's MileagePlus and Delta's Frequent Flyer (since renamed SkyMiles). The FFP virus spread round the world in the following decade.

At the start the FFPs were relatively simple marketing tools designed to encourage and reward loyalty to a brand — for a product (a seat from *A* to *B*) that is essentially a commodity. Passengers were awarded credit for the miles flown on the airline and rewarded with the ability to use this credit to book "free" flights or upgrade class of service. For the airline the cost of providing the "reward" was in effect

US Credit Card Purchase
Volumes by Issuer (US$bn, 2023)



a very modest discount to the original fare — in the early 1980s the industry was operating on load factors of 65%, and the marginal cost of carrying a passenger in a seat that would otherwise be unfilled is minuscule — while for the passenger the benefit of the reward fulfilled aspirational goals.

The airline could keep track of its most treasured customers, the frequent flyers, and added status levels to the FFP with incremental additional personal benefits, depending on the total number of flights or miles flown, such as lounge access, pre-boarding and free upgrades, to add further cachet to the plan. And thus it provided a useful tool to stave off the encroachment of start-up airlines. And it worked.

But that was over forty years ago, and much has changed in the intervening years.

The air travel market has grown hugely — from 750m passengers in 1981 to an estimated 4.9bn in 2024 with system load factors up from 63% to 83% over the period, reducing the availability of the marginal empty seat. So most FFPs have progressed from allocating programme miles simply on the basis of distance flown to rewards based on dollar spending.

The methods for allowing frequent flyers to "burn" their accumulated miles have also changed. The airlines opaquely control the exchange rate — which currently in the USA is estimated to be between 1¢ and 1.6¢ a mile — and are increasingly moving to dynamic pricing models (akin to yield management models).

Spending patterns have also changed. There has been an explosion in the ownership of credit cards and their use for payment transactions. Since 2014, the total number of transactions performed by the world's card payment systems has grown by compound average 15% a year to end 2023 at 687bn.

Historically the largest player, Visa has seen annual growth in transactions of 10%; at the end of 2023 it had 4.4bn cards in issue and the total monetary volume reached $15.1trn. China's state-owned UnionPay has seen transaction growth of 31% a year over the period and overtook Visa in the value of payments processed in 2015, ending 2023 with purchase volumes of $14.7tn and 9.6bn cards issued — but 99.5% of this is purely domestic China.

GLOBAL PAYMENT SYSTEMS

	Payment volume ($bn)	Total† volume ($bn)	Transactions (bn)	Cards (m)
Visa	12,620	15,114	284	4,484
UnionPay	14,718	15,104	215	9,576
Amex	1,665	1,680	12	141
Diners/Discover	256	272	4	72
JCB	321	329	7	156
Mastercard	7,344	9,029	184	2,948

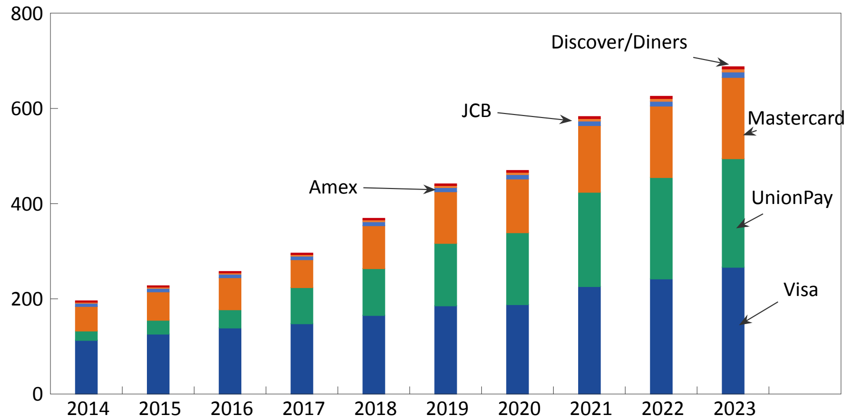
Source: Nilson Report, VISA Inc.
Notes: † includes cash and forex

Visa and Mastercard systems

The accounts for Visa Inc and Mastercard, the largest systems in the Western world, make interesting reading.

For its financial year ended Sept 2024, Visa Inc achieved net revenues of $35.9bn, operating profits of $23.5bn (an enviable 66% margin), and net income of $19.7bn (55% margin). Its net revenues have grown at a compound annual average of 15% over the past 20 years. Mastercard generated $25.1bn revenues in its FY 2023, an operating margin of 58% and net income of $11.6bn. Its revenues have grown by 13%pa over the same period

GLOBAL PAYMENT SYSTEMS
ANNUAL TRANSACTIONS (bn)



The absolute numbers are huge, but in Visa's case its revenues derive from fees of just around 12¢ per transaction, and represent 0.2% of the total $15tr monetary value transacted on its cards.

Most credit cards operate as a four-party system encompassing the issuing bank, consumer, merchant, and acquiring bank. The issuer contracts with the consumer providing the card, issuing bills, etc. The acquirer contracts with the merchant, making payment. The rules of the system are set by the network operator (such as Visa or Mastercard), which also facilitates settlement between the issuer and acquirer. The issuer charges the acquirer an "interchange fee" (set by the network operator) that is then incorporated into the fees those acquirers charge to merchants (called a "merchant-discount rate"). There are also three-party systems (such as provided by American Express or Discover/Diners) where the card network operator acts as both issuer and acquiror, and charges the merchant a percentage of the transaction as a card processing fee.

The first airline FFP co-branded credit card was launched by Continental in partnership with Marine Midland Bank (now part of HSBC) in 1986, followed a year later by American in partnership with Citibank.

The concept again was simple: the issuing bank uses some of the interchange fee to buy "miles" in the airline's FFP allocating them to the credit card holder depending on the level of expenditure and the merchant where the money was spent — emphasising the airline and any other affinity members of the frequent flyer programme (such as hotel chains or car hire). The rate per mile that the issuing bank pays for these miles is a commercial secret — but possibly runs at twice the redemption value.

Over the years, the numbers and types of cards have proliferated: with varied benefits (such as the number of miles allocated per dollar spent, access to airline lounges, priority boarding) sometimes dependent on the annual card fee charged to the consumer.

One of the AAdvantage cards currently recommended by *The Points Guy* comes with an annual fee of $595, gives a sign-on bonus of 70,000 miles, 4 miles and 1 Loyalty point per dollar spent on American Airlines (and one mile per dollar spent on other purchases), lounge access, free checked bag, fast track through security, priority boarding and 25% discount on inflight spending. Oh!... and a 20.24%-29.24% APR.

Consumer protection

The US has some of the highest credit card interchange fees in the world — ranging from about 1.4% to 3.5%, while the average is approximately 2.2%.

In 2023 a Senate bill, The Credit Card Competition Act 2023, was introduced (with bipartisan support) aimed at what were described as the anti-competitive actions of the card processors (notably Visa and Mastercard — which between them process 75% of all credit card purchases in the US) and designed to drive down interchange fees. Among other things, the Act would require the the largest credit-card issuers — those with assets over $100 billion — to enable at least two credit card networks to be used on their cards. At least one of those networks would have to be outside the two dominant suppliers, Visa and Mastercard.

The proposed Act may never pass into law. Scott Kirby, CEO of United, believes that it would make the airline frequent flyer programmes unviable, saying in Sept last year: "84% of US consumers have a rewards card in their wallet... they love these programs, they love getting those three million miles [issued by MileagePlus] to travel all over the world, and that act, if it passed, would eliminate that ability to earn miles for all those people."

It probably didn't help his humour at the time that the DoT had launched an inquiry into the rewards programmes of the four largest US carriers "aimed at protecting rewards customers from potential unfair, deceptive, or anticompetitive practices".

The proposed Act goes further than measures enacted in Europe and Australia where fees were legally capped (at 0.3% and 0.8% respectively — although for four-party systems only). Interestingly, in those jurisdictions various studies suggest that the cost of the rewards to the issuing bank exceed the interchange fees they earn. But, the issuers have raised credit card fees and increased card credit interest rates to compensate.

It may be that the banks' main interests are in the substantial flows of money the partnerships offer, and what they crave is the frequent *buyer*. Qantas has boasted that 35% of all credit card spend in Australia is on a Qantas or Qantas Frequent Flyer co-branded credit card.

As the *Financial Times* succinctly put it: "In essence, airlines have two businesses: the first flies people between destinations, and the second peddles those people to banks for a fee." But these loyalty programmes may have no value at all without the airline.

KPIs Pre- and Post-Pandemic

GLOBAL air passenger volumes in 2024 have surpassed the 2019 total by about 7%, though the growth trajectory now appears to be at a lower level. Nevertheless, this is an industry that now generates $1tr in annual revenues.

Some airlines have emerged stronger from the pandemic, others greatly weakened. Here we present a brief summary of some KPIs for six US and six European carriers, both Legacy/Network carriers and LCC/ULCCs, comparing the last 12 months data with the pre-pandemic 2019 results.

Passenger volumes for the US Legacies were up 5% while European Legacies were down 5%, but the big change has been in revenues. In a higher cost/yield environment US Legacy revenues were up 25% and European 11%. The US LCCs increased traffic by 10% and revenues by 22%, but Europe showed a more dramatic change: European LCC passengers up 21%, revenues up a remarkable 60%.

Operating margins fell to some degree across all the airline sectors between 2019 and 2024. But the US LCCs experienced a severe collapse in operating results, turning double digit operating profit margins into losses, or at best break-even. Ryanair and IAG were the best performers each achieving 12% margins in 2024, just slightly down on the pre-pandemic situation.

Despite the tight labour markets, the percentage of labour costs in total costs was generally up only one or two percentage points for the European carriers and the US Legacies. But there was a major change in the cost structure of the US LCCs: labour costs increased by 4-7 percentage points.

The US Legacies have emerged from the pandemic with a significantly higher level of net debt — up $9.4bn or 16%, largely the result of government guaranteed loans during the pandemic. The European Legacies as a group managed to reduce their net debt by $1.5bn over this period.

The European LCCs total net debt increased from $1.5bn to $4.2bn between 2019 and 2024, entirely due to the poor financial performance of Wizzair whose pandemic growth strategy went badly wrong. The US LCCs' net debt position deteriorated markedly from $1.2bn to $8.2bn, partly due to JetBlue and Frontier becoming entangled in futile merger battles.

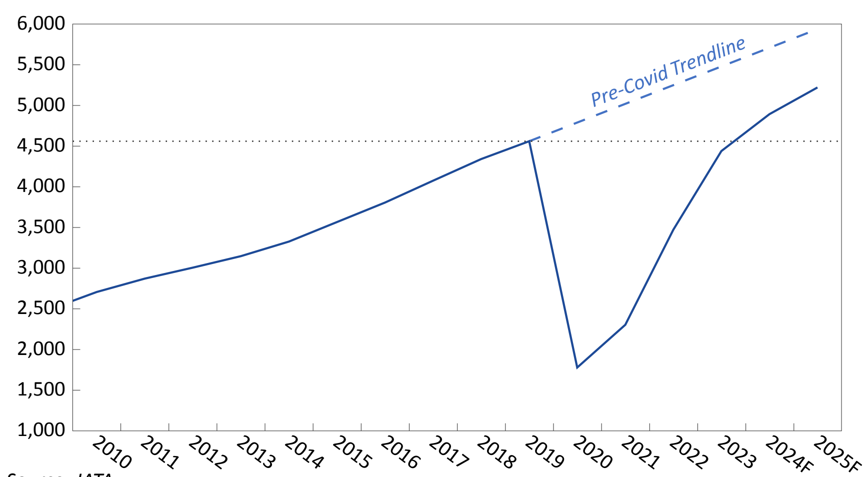
Stockmarket capitalisations should in theory reflect the relative financial performances and the airlines' perceived prospects.

Among the US Legacies United's share price has bounced, up 43% on pre-pandemic valuations, attributed to competent management and the view that it is best positioned to take advantage of the resurgence in long-haul markets, especially the Atlantic. By contrast, American has lost its strategic direction, and its market capitalisation is 25% down on 2019. Air France-KLM has been heavily discounted — valued at 54% less in 2024 than in 2019. Perhaps surprisingly, IAG shares have recovered to just 8% above 2019 levels.

There has been a general loss of investor confidence in the LCCs, especially the beleaguered US carriers — valuations are down 31-69%. Wizzair too has lost much of its value, share prices down 66%.

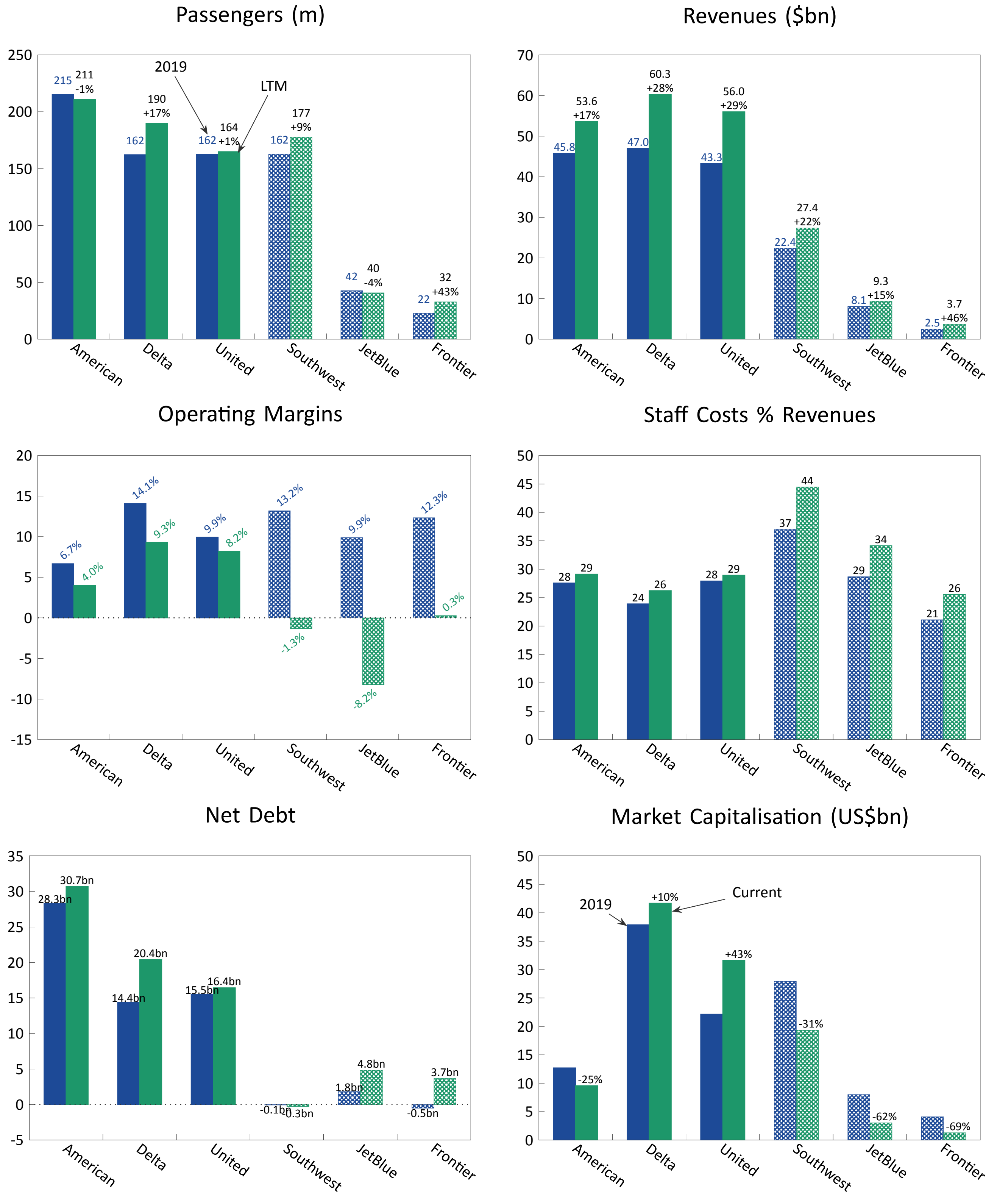
Ryanair is the happy exception — market capitalisation 24% higher in 2024 compared to 2019. Across all these KPIs Ryanair looks like the overall winner.

WORLD AIRLINE PASSENGERS (mn)



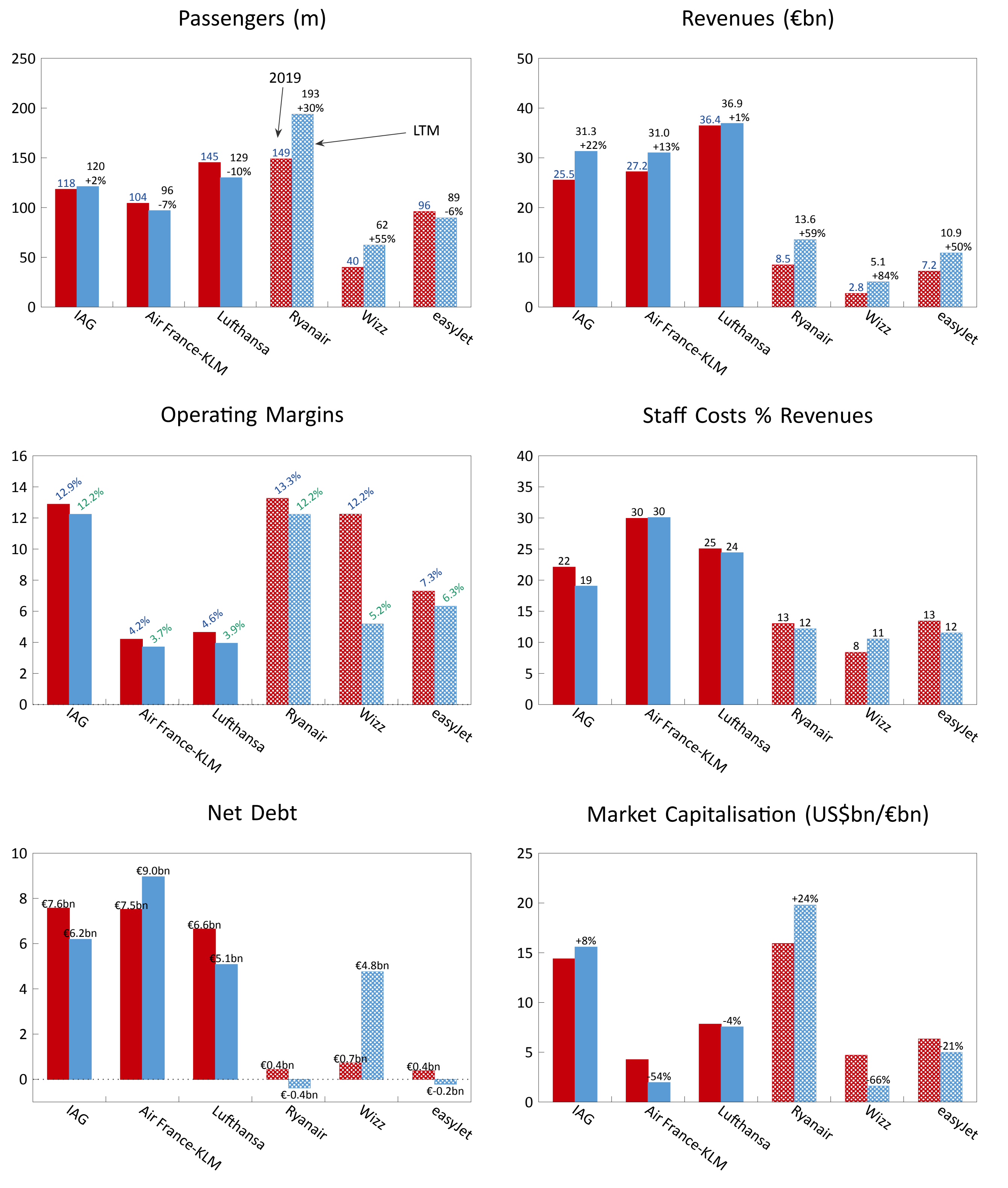
Source: IATA

USA AIRLINES KPI: 2019 AND 2024



Note: LTM 12 months to end Sept 2024 (or latest available)

EUROPEAN AIRLINES KPI: 2019 AND 2024



Note: LTM 12 months to end Sept 2024 (or latest available).

GOL Linhas Aéreas Inteligentes: Mirroring Avianca

BRAZIL'S third largest airline, GOL, was heading towards sustained profitability out of the country's 2014-16 recession and political turmoil (and its own restructuring) when the covid pandemic hit.

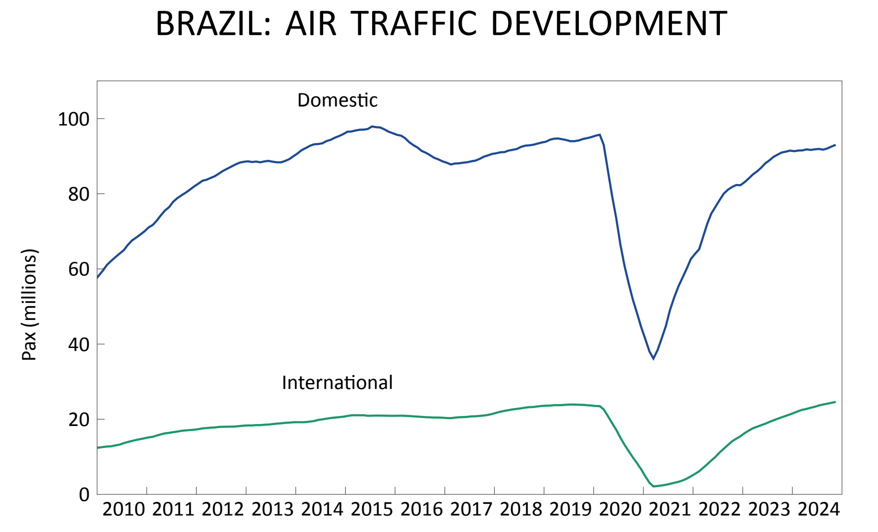
The following three years were as torrid for the carrier as any other airline worldwide: but the collapse of traffic and revenues (with minimal government support) were exacerbated by a 30% devaluation of the Real to the US Dollar. Over 2020-21 GOL lost a total of R$13bn ($2.5bn).

The majority of its operations are domestic, so it benefited from the early recovery in the large domestic market: revenues in 2022 exceeded those it had achieved in 2019, and by 2023 it was able to report an operating margin of 17.8% — its best since 2006.

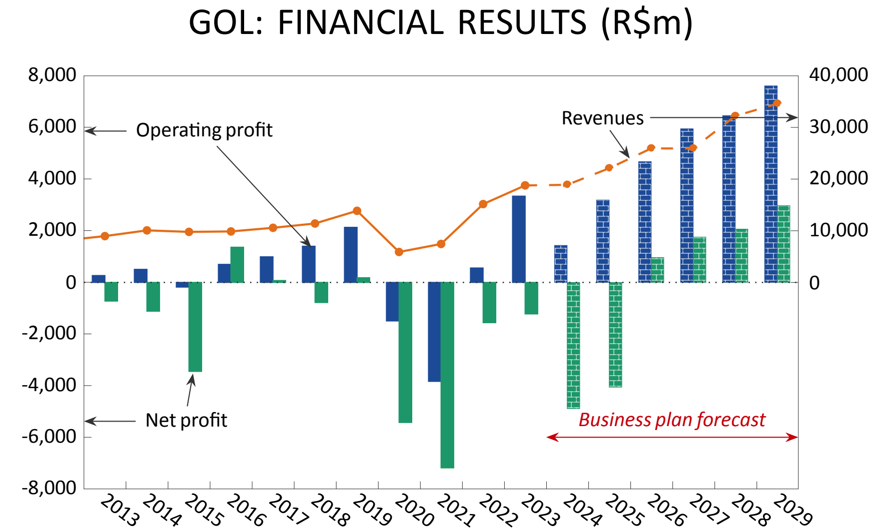
However, it ended 2023 in a very weak financial position: its total debt including lease liabilities had ballooned to R$17bn ($3.5bn) from R$4bn ($960m) at the end of 2019, and cash stood at a mere R$639m — 3% of revenues. Total liabilities exceeded assets and the group had a net shareholders' deficit of R$23bn.

At the beginning of 2024 it filed for Chapter 11 protection and restructuring in New York, benefiting from the experience of its friends at Avianca.

Avianca had filed for Chapter 11 in May 2020, emerging in December 2021 a much leaner, and possibly low cost carrier, with the new holding company (bizarrely) registered in the UK. In 2022 Avianca and GOL announced the intention to combine forces in a new Abra Group Ltd (also registered in England). The major shareholders of the billionaire controllers in each respective airline — Roberto Kriete and his family of Avianca and the Constantino family who had set up GOL — were placed in Abra. Constantino de Oliveira took on the chairmanship of the new company; Adrian Neuhauser, who had been CEO of Avianca through the



Source: ANAC.
Note: trailing 12 month total



GOL FINANCIAL DATA

R$m	2019	2020	2021	2022	2023	Jan-Sep 2024
Revenue	13,864	6,372	7,433	15,199	18,774	13,611
Net Income	179	(5,895)	(7,184)	(1,561)	(1,222)	(912)
Operating cash flow	2,461	754	706	2,169	1,822	(772)
Net Capex	(253)	32	(180)	(788)	(872)	(1,218)
Free cash flow	2,208	786	526	1,381	950	(1,990)
Financing	(612)	(1,873)	(834)	(2,621)	(723)	2,945
Dividends	(210)	(64)	(260)	948	2	
Equity issued	(70)	2	422		95	3
Exchange Rate diff	5	167	(30)	(25)	(168)	240
Total cash flow	1,321	(983)	(177)	(317)	155	1,199
BRL/USD	3.94	5.15	5.39	5.16	4.99	5.23

@ end	Sep 2024
Fixed assets	9,845
Intangibles	2,016
Other LT Assets	2,922
Current Assets	7,046
of which Cash	*1,738*
Current Liabilities	(23,206)
Total Assets	(1,377)
Debt and Lease Liabilities	(17,809)
Other LT Liabilities	(4,845)
Shareholders' Equity	(24,031)

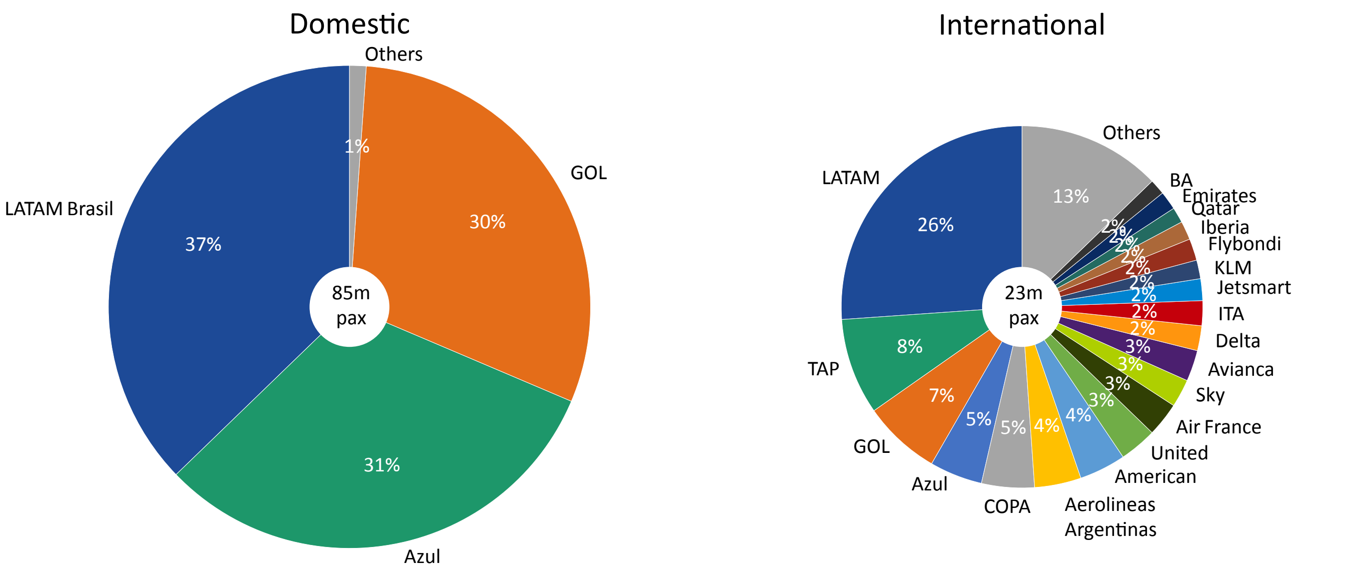
bankruptcy process, went in as CEO. The two carriers, it was said, would retain their brand identities.

GOL's restructuring 5-year business plan, published in May 2024, bears an uncanny resemblance to the plan that Avianca itself had produced in 2020. By 2029 it illustrates a return to the 20%+ operating margins it enjoyed in the early 2000s.

The GOL plan is "underpinned by a robust engine investment program to return aircraft to revenue service, a steady stream of new 737 MAX aircraft, a strategic expansion of its network, and the pursuit of a cR$1 billion profit improvement program".

Part of the plan requires restructuring commitments to lessors. They hope to achieve some R$5.9bn from renegotiating end-of-lease obligations, reduction in rents, and getting new money financing from Lessors to address engine heavy maintenance as well as sourcing sale and leaseback financing on new 737MAX deliveries (of which it has 93 on order).

BRAZIL PASSENGER MARKET SHARES 2024

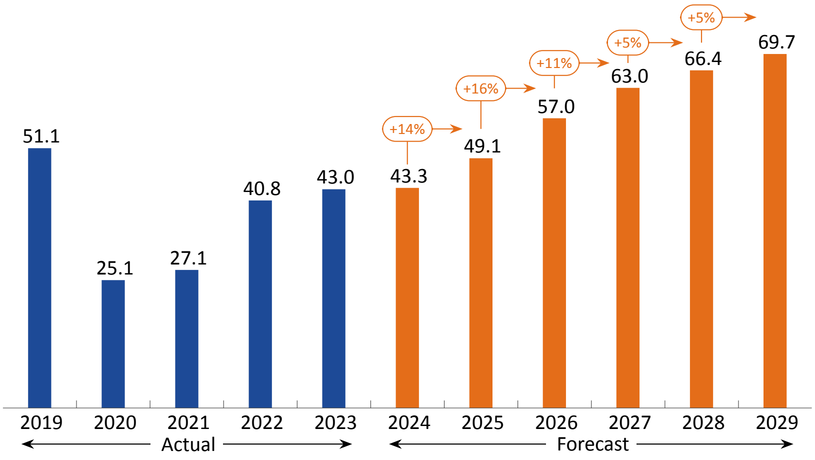


It aims to apply re-amortisation of lessor-secured obligations, and suggests that future 737MAX deliveries would be funded through sale and leaseback transactions.

The plan as it is set out sees GOL increasing its fleet of 137 737s by 20% over the next six years (see figure on the facing page). It appears to be planning the introduction of 80 new routes by 2029, "leveraging its significant market position in Brazil's principal cities to build up its network". Aircraft utilisation is projected to increase by 10% to 12.8 hours a day over the period and capacity in ASK terms is expected to grow strongly by around 15% a year between 2024

ABRA GROUP ROUTE NETWORK

GOL: CAPACITY PLANS (ASKbn)



and 2027 before settling to an annual growth of 5% (see figure above). A large part of the growth in the short run is expected to be international: the group does not expect its domestic offering to reach pre-pandemic levels until 2026.

The company states that it and its lessors are investing in its older 737NG fleet to repair engines and restore optimal capacity, which would unlock additional growth both domestically and internationally with a focus on maximising profits.

Without any real details it says that it will implement a "R$1 billion annual run rate profit-improvement program" in order to "further improve the airline's industry leading unit cost levels".

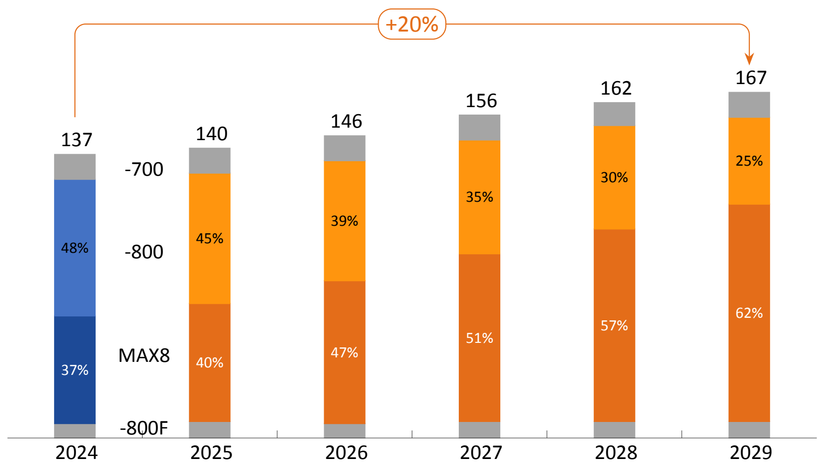
GOL received $1bn debtor-in-possession financing (which explains why the Q3 balance sheet snapshot in the table on page 9 looks so dire) and announced in November last year an agreement reached with Abra Group for a further support agreement including $950m secured debt convertible into new GOL equity in collaboration with GOL's unsecured creditors committee. The agreement suggested that financial restructuring would reduce GOL's obligations by around $2.5bn and allow for an exit facility of up to $1.85bn equity.

The details are far from clear, but it is likely that many of the financial concerns that supported Avianca in its restructuring (such as activist hedge fund manager Elliott) have been brought on board to support GOL in its efforts.

The wording of the public announcements are possibly obfuscated by design. The details of the new Abra Group are also particularly obscure. Its latest accounts filed with the UK's Companies' House (for the year ended 2022) were done on a "micro-entity" basis: no revenues, no employees and an equity deficit. The group has so far failed to file accounts due for 2023 (no worry: the fine for so doing is only £150). When founded, it was hawked as furthering consolidation in Latin America to create a group to rival LATAM. Avianca's attempt to acquire Viva Air was effectively blocked, but that pushed Viva into liquidation, creating the desired effect. It has apparently acquired an interest in Spanish ACMI operator Wamos Air. And now Abra has signed a non-binding MoU with GOL's domestic competitor Azul to combine the Brazilian operations (while retaining the brands). This could give Abra Group airlines 60% of the domestic market.

GOL expects to be able to exit Chapter 11 in May 2025, a leaner, fitter and more financially secure airline. Abra Group will probably look to raise funds through an IPO. Then we might find out more about this enigmatic new airline group.

GOL: 737 FLEET PLAN



Avia Solutions Group: ACMI Visionary

Avia Solutions Group (ASG) can now claim to be Ireland's second largest aviation business, after Ryanair, having relocated its headquarters from Vilnius in Lithuania to Dublin in 2023. ASG plans to be as disruptive in the wet-leasing sector as Ryanair has been in the European airline industry.

ASG is the world's largest ACMI (aircraft, crew, maintenance, and insurance) lessor in the world with a fleet expected to total 240 aircraft by the end of 2025 and a total annual revenue of well over €3bn. Moving the company's headquarters to Dublin was "strategically important", according to CEO Jonas Janukenas positioning ASG at a major European aviation hub and at the global centre for operating leasing. Corporate taxation was not an important consideration as Lithuania has a similar regime to Ireland.

ASG dates back to the former Lithuanian flag-carrier FlyLAL, which was privatised in 2005, then merged into a management-owned group including Baltic Ground Services (ground handling) and FL Technics (aviation maintenance, repair, and operations). It has grown through adding new charter airlines in Europe and elsewhere and taking over various maintenance and support facilities. By the end of 2024 it held 11 AOCs and over 500 maintenance and repair licences.

Its client base is over 2,000, none of which accounts for more than 6% of total revenue. Among its ACMI clients are easyJet, IndiGo, THY, TUI and Vueling; for maintenance services, Lufthansa, SAS, TAP and Wizz; for ground handling, Lufthansa, Norwegian and Ryanair; and for cargo chartering, Amazon, DHL and Tesla. Europe accounts for 55% of its revenue base and Asia for 28%, but only 11% for the Americas.

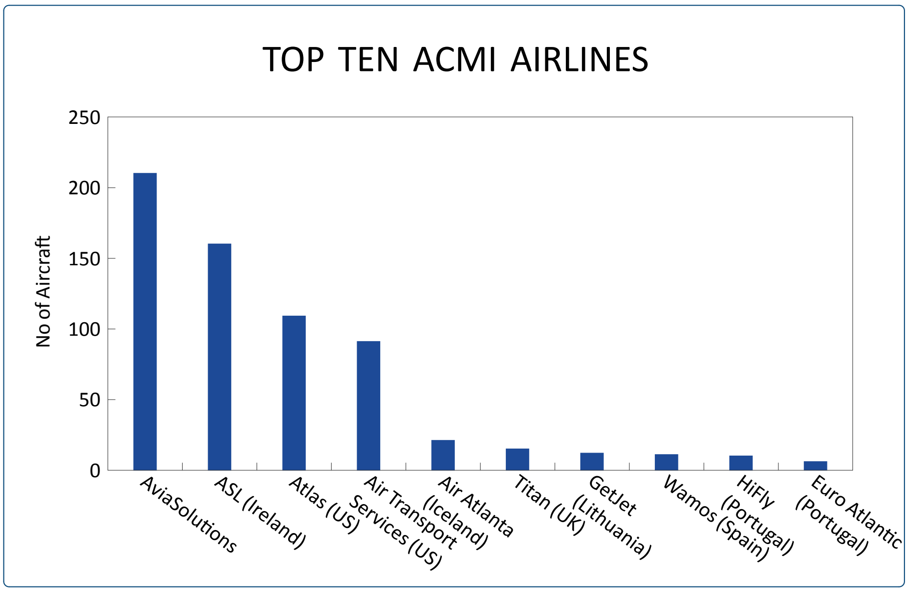
Structure and ownership

ASG has two main business units:

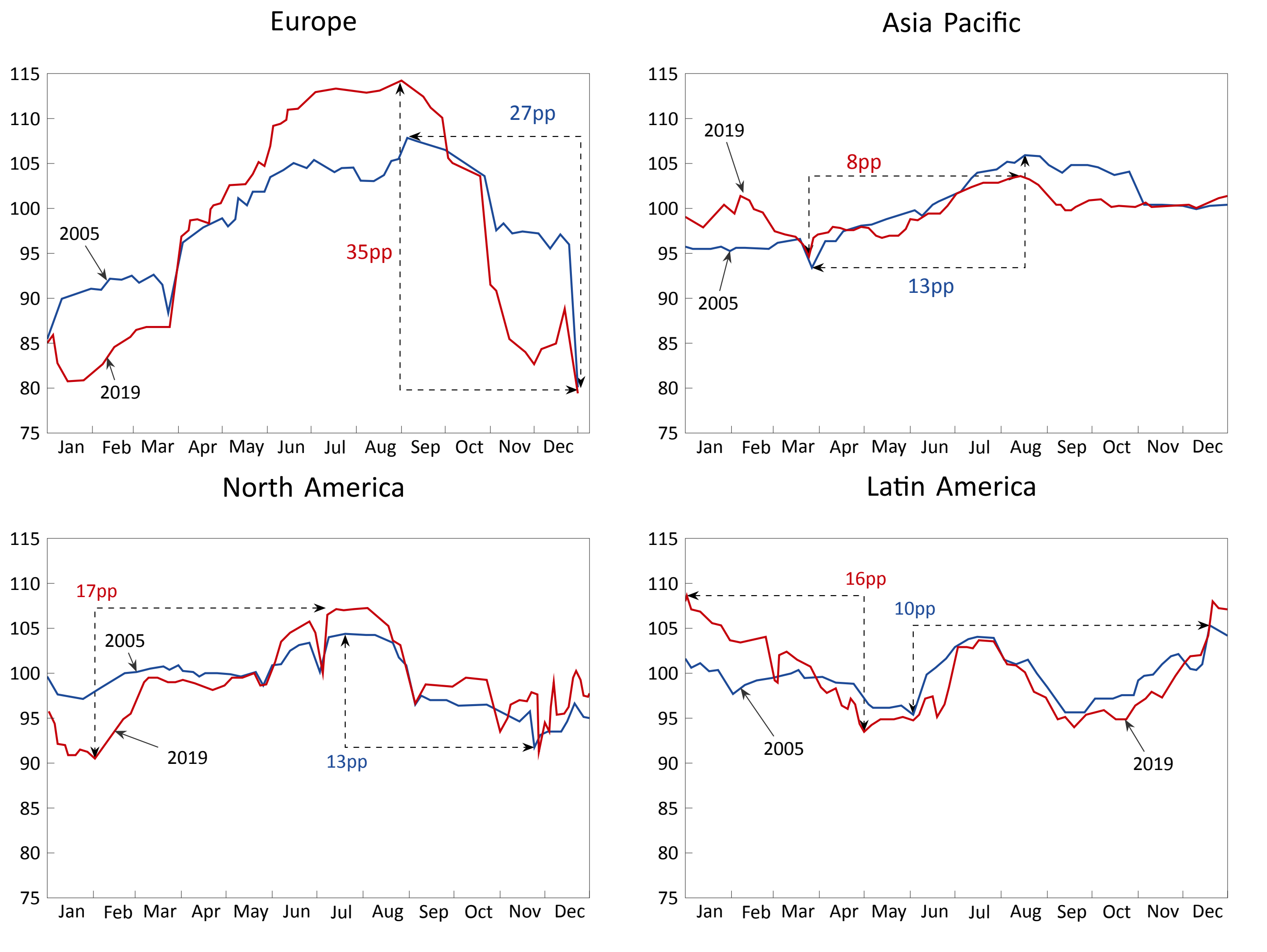
Logistics and Distribution Services — a range of passenger and cargo ACMI and other charters, plus private jet operations and specialist air delivery cargo services, including On Board Courier (OBC). Operating airlines, owned or partly owned by ASG, include: SmartLynx, Avion Express, AirExplore, KlasJet, Magma Aviation, Ascend Airways and SkyTrans. In the first nine months of 2025 Logistics accounted for $1.5bn or 71% of revenues and $96m or 62% of operating profits.

Support Services — concentrates on aircraft maintenance, mainly through FL Technics, including repair, overhaul and spare parts management. It also provides aircraft handling and passenger handling and into-plane fuelling, with 100 line maintenance stations plus heavy maintenance centres in Lithuania, the UK and Indonesia. Support Services operates the largest independent pilot training organisation, BAA Training, with schools in Spain, France, Lithuania, and Vietnam. Support Services accounted for $593m or 29% of revenues and $59m or 38% of operating profits in the first nine months of 2024.

Many of ASG's top managers have been with the group in its various incarnations since the beginning. Chairman Gediminas Žiemelis (more below) owns 55% of the business while other top managers led by CEO Janukenas have a further 4%. Having converted bonds into $300m of equity in 2021, Centares/Knighthead control 20% of ASG.



SEASONALITY COMPOUNDING ACROSS REGIONS



Source: Avia Solutions Group.
Note: Daily scheduled seats indexed to median daily seats across the year.

Certares is a New York- based private investment company with about $9.9bn of assets under management. Its investments in the aviation industry include LATAM and Azul. Following the equity injection, Certares appointed Tom Kein, a former CEO of Sabre, to ASG's board. Certares has an alliance with Knighthead Capital Management LLC, a US private equity and debt provider, with $13.4bn in assets under management. It is a major investor in Wheels Up, the private jet charter operator.

Certares' strategic role is to help ASG develop in the North American market, especially in the US where it currently has a limited presence, though this may bring intensified competition from Atlas and Air Transport Service, the two big US wet-lessors. In another move ASG has entered into a partnership with Impact Investments, a New York strategic and financial advisory firm, chaired by former Secretary of State Mike Pompeo.

Finances

ASG's financial' expansion has been impressive. Revenues have been grown at a remarkable compound rate of 30% pa between 2019 and 2023, the result of takeovers and organic growth.

It has reported positive operating and net results (albeit with lowish average margins of 6.0% and 1.2%) throughout this period with the exception of the first pandemic year, 2020, when it reported a net loss of €18m. The next two years saw a rapid return to strong operating cash generation and profitability, which ASG attributed to its flexible operating model. It was able to offload 20% of its passenger aircraft during the pandemic and replace them

AVIA SOLUTIONS: FLEET AND AOC BASES

Airline	Base	Operations	737NG	737 MAX	A320/21	Turboprops	TOTAL
Avion Express	Malta	ACMI Charter			41		41
SmartLynx	Malta	ACMI Charter	13		26		39
SmartLynx	Latvia	ACMI Charter			24		24
SmartLynx	Estonia	ACMI Charter			20		20
Air Explore	Slokavia	ACMI Charter	16				16
SkyTrans	Australia	ACMI Charter				13	13
Avion Express	Lithuania	ACMI Charter			13		13
KLasJet	Lithuania	Private Jet/ACMI	13				13
BBN	Turkey	ACMI Charter			10		10
BBN	Indonesia	ACMI Charter	9				9
Aircus Airlogistic	Germany	OBC				2	2
Ascend Airways	UK	ACMI Charter	1	1			2
Ascend Airways	Malaysia	In Development					
Avion Express	Brazil	In Development					
Avion Express	Philippines	In Development					
SmartLynx	Thailand	In Development					
TOTAL			**52**	**1**	**134**	**15**	**202**
Firm Orders				40			40
Options				40			40
TOTAL				**80**			**80**

Note: As at Sept 2024. ASG reported total fleet of 212 units as at year end

with freighters, as well as renegotiating about 70% of its operating leases from fixed monthly to Power by the Hour (PBT) payments. In 2021 Certares injected $300m in equity.

2023 saw revenues increased to €2.3bn, as the company added another 27 aircraft to its fleet and established new bases in Asia, while net profit totalled €68m, a margin of 3.0%. A €26m dividend was paid, similar to the previous year.

In the first nine months the group's revenue grew by 25%, to €2.1bn, and is officially expected to top $3bn for the whole year. ASG added another eight aircraft during the nine months but reported some setbacks with the performance of narrowbody cargo sub-segment and the and a failure by a major external MRO provider, but was still able to report a net profit of €83m, a net margin of 4.0%.

In May 2024 ASG completed a $300m bond issue, $180m of which replaced expiring debt. These were five-year senior unsecured bonds bearing a quite expensive interest rate of 9.75%, rated by Fitch as BB, below investment grade but towards the top of the speculative range (interestingly, Fitch highlighted key person risk relating to Žiemelis' majority control of the company).

ASG's balance sheet as at the end of September 2024 showed €1.3bn of long-term debt and lease liabilities against €724m of shareholders' equity, a ratio of 1.9:1. Cash and equivalents stood at a reasonable €300m.

SEGMENT ANALYSIS
€ millions, Jan-Sept 2024

	Revenues	Operating Result	Margin
Logistics	1,466	96	6.5%
Support Services	593	59	9.9%
Others (inc inter-segment)	(2)		
Total	**2,059**	**155**	**7.5%**

The Žiemelis effect

The chairman and majority shareholder of ASG, 47-year-old Gediminas Žiemelis, is reputed to be Lithuania's richest person, with assets estimated at €2.5bn. A high-profile serial entrepreneur, he has been involved in over 100 start-ups and four IPOs. He also owns the Vilnius Wolves, Lithuania's top basketball team (basketball is very big in the Baltics).

Žiemelis has a bold vision for ACMI, supported by a report produced by McKinsey (which may or may not be regarded as a good thing). McKinsey drew up the charts on page 13 showing the variation in seasonality in air passenger traffic among the main regions of the world and indicating that over the long-term seasonality effects have increased.

The implication, according to McKinsey: "In a world with increased seasonality — and sharper focus on maximizing aircraft utilisation — considering a longer-term partnership in which outsourced capacity providers help deal with peaks could be an attractive move. If the ACMI market grows as a result, it could in turn become a more frictionless capacity management solution for airlines.

"Wet leasing might look expensive at first glance, but in weighing this option airlines should consider the value loss that would be incurred if excess owned aircraft are kept idle all winter. To be worthwhile, any outsourcing option would of course need to offer a suitable combination of cost, service reliability, and passenger experience."

The suggestion is that about 10% of global airline capacity could be cross-utilised to equalise peaks in regional demand and maximise efficiency. Žiemelis, at a conference for ASG leaders in December, made an interesting analogy with the avian world; "There are 50 billion birds in the world, and 10% of them migrate," he noted.

Žiemelis has commented regularly and evangelically about the merits of ACMI in recent times. Some of his key points:

✈ "ACMI leasing is emerging as a key strategy, energising airlines to harness the air travel demand rebound. It infuses the post-pandemic aviation sphere with financial and operational agility, acting as a safeguard amidst market volatility, empowering airlines to navigate the unpredictable currents with adaptable fleet management and staffing solutions".

✈ In airline fleet planning, ideally a *modest* proportion — somewhere between 6% to 15% — of aircraft should be under ACMI leases.

✈ A successful ACMI provider needs to operate across six continents to leverage counter-seasonal demand.

✈ Because of the regulatory environment, this means building up multiple AOCs, each operating at least 10 aircraft in its respective country or region.

✈ Seasonal ACMI capacity, added during peak periods, is effective for airlines only if it is equivalent to at least 10% of the airline's total fleet capacity.

✈ ACMI creates financial value for scheduled carriers when used for a maximum of six months per financial year, aligning with peak demand seasons.

✈ No single market can match Europe's scale, but ASG aims to match the European total in all its other operating regions by 2026.

✈ ACMI leasing addresses the labour shortages facing the industry, allowing airlines to tap into a broader pool of aviation talent, mitigating staffing challenges.

✈ The ACMI market is projected to be approximately $25bn by 2030 and ASG aims to capture a 50% share.

AVIASOLUTIONS GROUP FINANCIAL DATA (€m)

						Jan-Sept	
FY (Jan-Dec)	**2019**	**2020**	**2021**	**2022**	**2023**	**2023**	**2024**
Revenues	607	695	1,014	1,852	2,262	1,642	2,057
Net result	12	(51)	34	12	68	71	83
Operating Cashflow	39	97	42	175	268	204	303
Net Capex and Investments	(41)	(84)	(293)	85	(180)	(121)	(142)
Free Cashflow	(2)	13	(251)	260	88	83	161
Financing	231	(47)	(13)	(122)	(182)	(124)	(77)
Share Placement			300				
Dividends				(30)	(26)		
Total Cashflow	**229**	**(34)**	**36**	**108**	**(120)**	**(41)**	**84**

End Sept	**2024**
Fleet and other Fixed Assets	2,074
Current Assets	618
Cash	*301*
Total Assets	**2,993**
Long Term debt and lease liabilities	1,330
Current liabilities	939
Total Liabilities	**2,269**
Shareholders' Equity	**724**

This last point needs a reality check, not least because it implies a future ASG fleet of about 700 aircraft. It is not clear where the $25bn figure comes from; a forecast by Business Research Insights last year indicated that the global ACMI market, valued at $5.46bn in 2023 based on an analysis of the leading players, would grow at a CAGR of 6.9% to $10bn in 2032. In terms of aircraft, ASG currently accounts for about a third of the global fleet of ACMI operators (see chart on page 12) and in terms of revenue might account for about 40% of the total (which does not include wet leasing between scheduled airlines). On the other hand, a McKinsey-type observation would be that $25bn is only equivalent to 2.5% of 2024 global airline revenues, as against the theoretical 10% potential.

It is also worth remembering that traditional airline management does not particularly like ACMI. ACMI tends to be needed when the planning process has failed to anticipate a higher level of demand or when something technical has gone wrong. Lufthansa has become a significant user of A220 ACMI charters from airBaltic (see *Aviation Strategy*, Sep/Oct 2024) but this was largely because it lost capacity as its P&W GTF-powered Airbuses had to be grounded.

From an airline perspective, the ACMI rate it pays to the lessor is almost always above the sum of its own internal A, C, M and I costs because the lease rate includes an element for overhead and profit. ASG would counter that the decision to wet lease should be based on a risk-adjusted assessment of marginal unit costs and revenues at peak times.

There may also be concerns about brand damage. With an ACMI lease, flying crew come into direct contact with passengers, and the airline would have a problem if the service provided is seen as inferior to the normal service level. The airline would have a bigger problem if the ACMI service level is perceived as superior.

ASG's jet fleet is overwhelmingly older-technology A320 CEOs and 737-800s, with a solitary MAX 8 being operated by UK-based Ascend Airways (with a further two units due to be leased in in the first half of 2025). As an example of the complications of ACMI marketing: the MAX is being offered either with 189 all-economy seats or in a two-class cabin layout, with 12 business class and 150 economy seats.

In November 2024 ASG placed a firm order for 40 737 MAX8s, with options for a further 40 units which the lessor is confident will be taken up. The order was the first one placed after the eight-week industrial action at Boeing, so ASG should have achieved a good price; we would estimate the price for the firm orders to be around $2bn. However, the MAXes are not scheduled for delivery until 2030, at which time ASG expects a rather modest 20% of its fleet to be new-technology aircraft. The plan is to fund the order by pre-delivery payment (PDP) financing starting in 2028, then sell and lease back the MAXes.

ASG is supremely ambitious, not only in the overall rate of growth but also in its geographical spread and business complexity. In 2024, ASG set up new airlines in Australia, Turkey, the UK, and Indonesia. In the first half of 2025 new airline ventures are scheduled for completion in Brazil, Thailand, the Philippines, and Malaysia. Managing this growth will be difficult, but ASG's clear aim is to dominate the global ACMI business.

Musings of an Aviation Investor Low-Cost US vs Europe — A tale of two markets

The bifurcation of airline performance across the North Atlantic continued through Summer 2024 from the prior year.

In the US domestic market, it would not have been thought possible after the material yield and fare declines experienced in the summer of 2023, but further declines transpired into 2024 hitting airline profitability, particularly the LCCs.

In 2023 these players blamed shifting demand to international flying. In the most recent period, the blame has shifted with the LCCs exclaiming that passengers now demand extra comfort and were prepared to pay for the premium product offerings from the Majors.

With high density basic products, the LCCs impugned that they lost traffic and resultantly during 2024 decided to shift strategy away from their core business models to include premium seat offering. This deviation from their cost focus resulted in them incurring substantial expense of interior aircraft refits but also higher marketing / distribution expenses directed towards attracting these discerning new customers.

The real causes of margin erosion should be pointed towards the simple paradigm of capacity. There was a continued deployment/delivery of new aircraft far in excess of what the networks could successfully incorporate, depressing yields, while costs from the excessive labour pay awards post-pandemic had pushed unit costs above acceptable thresholds for these cost driven LCC strategies.

Carriers relented on capacity too late in the day and finally began to rein in schedules mid-year. This began to have a positive impact on yields in late Summer and into the fourth quarter but too late for Spirit, which filed for Ch.11 bankruptcy protection in November. Management could and should have taken corrective action early in the year.

With global narrowbody capacity at a premium Spirit could have more aggressively drawn down schedules for the Spring/Summer periods at a time when it could have secured alternative homes for excess aircraft at the handsome market lease rates then available. So, mismanagement a valid concern and subsequent executive bonuses distributed when Spirit equity had been toasted demonstrated a capitalist system injustice of the highest order.

Low-cost airlines in Europe on the other hand performed admirably particularly after scares and profit warnings mid-year (Ryanair being the protagonist with its July profits warning that muted the whole sector) that hit share prices hard, but in the outturn the concerns were overly pessimistic.

Operating margins for the all-important Summer quarter were reasonable, albeit reduced from the prior year.

Impressively two of the important UK players, Jet2 and easyJet, managed to maintain operating margins driven by a buoyant package holiday market.

Most of the other main LCC players incurred margin contractions year-on-year with cost increases outpacing flat yields. Many had overstaffed for Summer 2024 ahead of expected higher aircraft capacity, which finally did not arrive due to manufacturer induced delivery delays and/or continuing groundings due to Pratt & Whitney GTF engines.

The decent financial performances in Europe have assisted the further recovery in European carrier balance sheets which had been decimated during Covid. This has allowed several airlines to increase dividends and for some to institute share buybacks.

What really heightened the divergent performance across the Atlantic for the Low-Cost participants was seat capacities.

LCC OPERATING MARGINS

Jun-Sept Quarter 2024	
N. America	
Spirit	-24.8%
Frontier∗	-5.7%
Europe	
Ryanair	32.5%
easyJet†	15.3%
Wizz	16.9%
Jet2†	13.8%
Norwegian	18.4%

Note: † easyJet and Jet2 fiscal periods are half-year to end of September 2024. ∗ Frontier margin adjusted to remove aircraft SLB profits

The increases in the US over the last 24 months were just too much for that market to bear and attempts to reign in schedules were too late, while in Europe perhaps out of some good fortune, new aircraft deliveries streams were tempered and a little behind US counterparts and PW GTF engine issues impacted only one of the major players, Wizz.

The Wizz share price performance has been dismal. Albeit, unlucky with its exposure to Israel and with high GTF groundings, management must take its share of the blame. József Váradi, the CEO and founder, has been instrumental in the carrier's massive growth and success, but there is a concern that he has lost his grip on key operational issues. An expensive commitment to wet lease capacity the carrier did not need in the second half of 2024 together with likely problems arising from a move of the airline's commercial team from Geneva to Budapest are bad signs.

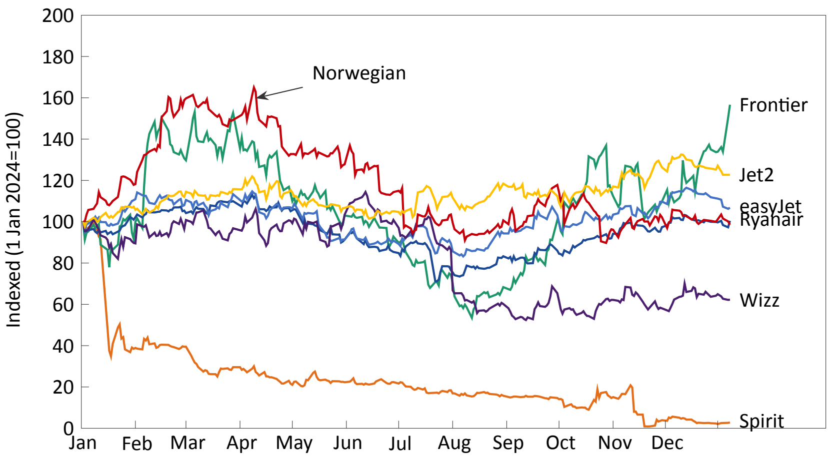
Much weaker operating margins YoY for the Summer 2024 Quarter dropping from 24% in 2023 to 17% and the loss of the coveted Investment Grade credit rating have assisted a share price decline from £22 at the start of the year to end at £14.39 by 31 December. Váradi may not be finished, and he is a sage hand, so performance in 2025 will be the telling factor and Wizz should not be written off just yet.

Share prices for US carriers had already been hit hard after weak performance in 2023, so 2024 price directionality was better while in Europe stock prices were volatile taking a big mid-year plunge prior to recovery after the release of the Summer quarter results, so somewhat treading water on average. Jet2 and IAG were the standouts for a substantial uplift in share valuation over the calendar year.

The market overall (both US and Europe) looks promising going into 2025 and airline share price recovery in 2024 should continue driven by strong passenger booking momentum, continuing aircraft supply constraints that will not be solved in the next 12 months as well as a tailwind on fuel prices particularly for those European based carriers that have hedged Summer 2025 consumption.

There will be a labour cost tailwind in Europe for those airlines that had prematurely staffed up for Summer 2024, with such excess staff becoming efficiently deployed in 2025. A strong US dollar post the Trump election victory is a negative to non-US carriers and there are plenty of unknown impacts from tariffs and a changed US Foreign policy under Trump which makes for a volatile space, but with airline stocks on an earnings basis being considerably undervalued versus the overall market, prospects for 2025 growth momentum are reasonably positive.

LCC SHARE PRICE PERFORMANCE 2024



By The Irrational Investor.

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Boeing and Airbus: Orders, Deliveries and Production 2024

AIRBUS trounced its duopolist arch rival Boeing in the 2024 annual order and delivery race.

Both manufacturers continued to have supply-chain bottlenecks limiting the ability to build production rates. But Airbus did not have the additional problem of its regulator breathing down its neck in annoyance (and embarassment) at certification errors.

In 2024 Airbus managed to deliver 766 aircraft, slightly up from the 735 sold in 2023. It still plans to build production rates of its A320 workhorse to 75 a month by 2027, but last year they went out the door of the production line at the rate of 50 a month. Airlines in the Asia/Pacific and European regions and leasing companies were each recipients of around a quarter of the company's output, North American carriers a bit below this level.

Boeing shipped less than half that volume: 348 units down from the 528 it sent to customers in 2023. Airlines in Asia/Pacific and North America each accounted for 30% of the total; European carriers and lessors a mere 15% each.

Airbus has decisively outsold Boeing in each of the past six years — since the quality issues of the 737MAX8 and 787 emerged.

This performance is also reflected in the order profile for 2024. Boeing registered 569 gross orders — dominated by 737 orders in Europe and widebody oders in the Middle East. But after accounting for cancellations net orders plumeted to 377 from the

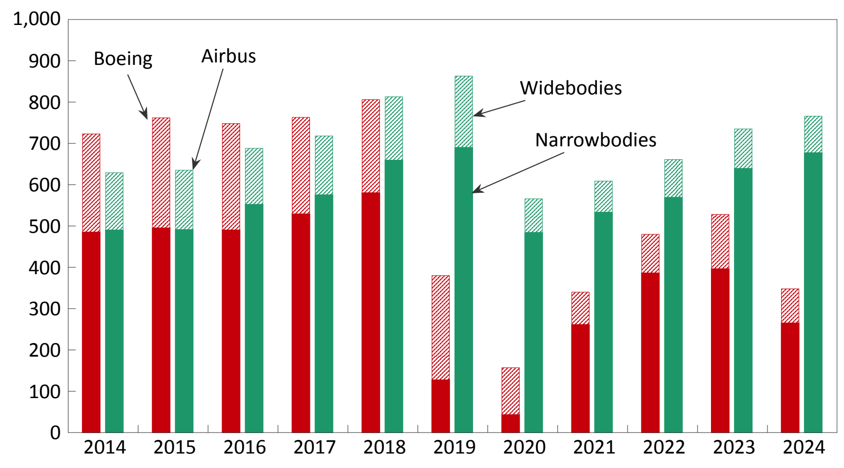
BOEING DELIVERIES 2024

Region	737	767	777	787	Total	
Asia/Pacific	75		5	18	**98**	30%
Europe	44		5	6	**55**	17%
Latin America	14				**14**	4%
MEAF	11		3	9	**23**	7%
North America	80	10		6	**96**	29%
Lessors	33		1	12	**46**	14%
Commercial deliveries	**257**	**10**	**14**	**51**	**332**	
Government	6	8			**14**	
Unidentified	2				**2**	
Total	**265**	**18**	**14**	**51**	**348**	

AIRBUS DELIVERIES 2024

Region	A220	A320	A330	A350	Total	
Asia/Pacific	4	171	3	16	**194**	25%
Europe	17	120	6	25	**168**	22%
Latin America		28			**28**	4%
MEAF		18	1	5	**24**	3%
North America	35	87	5	7	**134**	18%
Lessors	19	175	15	4	**213**	28%
Commercial Deliveries	**75**	**599**	**30**	**57**	**761**	
Airbus Defence and Space			2		**2**	
Private		3			**3**	
Total	**75**	**602**	**32**	**57**	**766**	

OEM DELIVERIES



prior year level of 1,311. It still has a backlog of 6,245 aircraft, including 4,778 737MAX8.

Airbus in contrast garnered 876 new orders (826 after accounting for cancellations). 40% of the orders came from airlines in the Asia/Pacific region, and surprisingly only 10% from leasing companies. The company retains an unfulfilled backlog of 8,658 aircraft at the end of 2024, including 7,210 orders for its A320 family.

BOEING ORDERS 2024

	Customer	737	767	777	787	Total Result	
Asia/Pacific	EVA Air				4	4	
	Japan Airlines				10	10	
	Royal Brunei				4	4	
	Silk Way West			1		1	
	Asia/Pacific Total			1	18	19	3%
Europe	Avia Solutions	40				40	
	Luxair	2				2	
	Pegasus	100				100	
	TUI Travel	10				10	
	Turkish			4		4	
	Europe Total	152		4		156	27%
MEAF	EL AL	20			3	23	
	Emirates			10		10	
	Ethiopian			8		8	
	flydubai				30	30	
	Qatar			20		20	
	MEAF Total	20		38	33	91	16%
N America	Alaska	6				6	
	American	85				85	
	National			4		4	
	North America Total	91		4		95	17%
	LATAM				10	10	
	South America Total				10	10	2%
Lessors	BOC Aviation	14				14	
	Altavair			1		1	
	Aviation Capital	35				35	
	Macquarie	20				20	
	Lessors Total	69		1		70	12%
	Unidentified	83	8	16	2	109	
	Government/Military	2	15	2		19	
	Gross Orders	**417**	**23**	**66**	**63**	**569**	
	Changes/Cancelled	173		4	15	192	
	Net Orders	**244**	**23**	**62**	**48**	**377**	
	Backlog	**4,778**	**109**	**562**	**796**	**6,245**	

AIRBUS ORDERS 2024

	Customer	A220	A320	A330	A350	A350F	Total Result	
Asia/Pacific	Air India		90		10		100	
	AirCalin				2		2	
	Cathay Pacific			30			30	
	Cebu Pacific		70				70	
	Druk Air		5				5	
	Indigo		10		30		40	
	JAL		11		21		32	
	Korean				33		33	
	Starlux			3		5	8	
	Uzbekistan		2				2	
	Vietjet			20			20	
	Asia/Pacific total		188	53	96	5	342	39%
Europe	AirBaltic	10					10	
	British Airways		5				5	
	Iberia				1		1	
	Jet2		36				36	
	Virgin Atlantic			7			7	
	Europe total	10	41	7	1		59	7%
MEAF	Air Algerie			3			3	
	Berniq		6				6	
	Ethiopian				11		11	
	Riyadh Air		60				60	
	Royal Jet		3				3	
	Saudia		51				51	
	MEAF total		120	3	11		134	15%
N America	Air Canada	5					5	
	American		86				86	
	Delta				20		20	
	N America total	5	86		20		111	13%
Lessors	CDB Leasing		80				80	
	Nordic Aviation Capital		7				7	
	Lessors total		87				87	10%
	Undisclosed		110	15	6		131	
	Private Customer		5		3		8	
	Airbus Defence and Space			4			4	
	Gross Orders	**15**	**637**	**82**	**137**	**5**	**876**	
	Changes/Cancellations	24	22		4		50	
	Net Orders	**-9**	**615**	**82**	**133**	**5**	**826**	
	Backlog	**516**	**7,210**	**230**	**647**	**55**	**8,658**	

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