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Push and pull factors on aircraft lease rates 2025.

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Strategic and Market Analysis

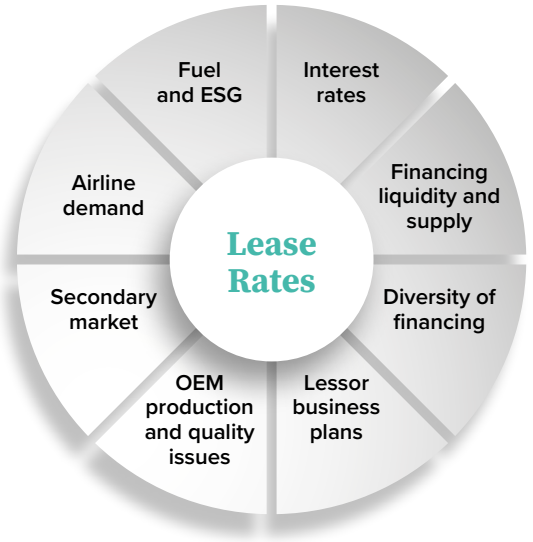
Introduction

In our annual update of push and pull factors on lease rates, we once again look at the same eight significant factors that we believe drive aircraft lease rates.

We retain our circle methodology as many of the factors interact and influence each other. At any given time, their relative importance can be larger than at other times, indeed we have seen this occur across 2024 and 2025 to date.

As before, we have colour coded the factors on a traffic light system ranging from *dark green* (very positive upward impact on lease rates) down to *red* (negative impact on lease rates). Please note that these colours do not represent a change versus last time, rather the current market conditions.

We conclude that the rental market is in a very similar position to last year pointing to sustained high lease rates in the primary and secondary space.



Traffic Light System

- Strong Positive Impact
- Positive Impact
- Neutral Impact
- Negative Impact

Interest Rates declining with further cuts expected, but when?

As a quick refresher from our prior paper, higher interest rates normally put an upward pressure on aircraft lease rates. This is primarily through the interest rate adjustment factor in leases and increased funding costs for lessors being passed across to airlines to meet minimum profitability targets.

By the end of 2024, economic news in most developed countries was positive with growth between mediocre and strong. Unemployment remains close to all-time lows and stock markets in 2024 were extremely robust. However, economic and geopolitical volatility has increased, so things can change rapidly in 2025.

When the US Fed began lowering interest rates in September, inflation had been steadily declining while the job market was showing some cooling. Since then, we have seen three consecutive cuts amounting to a full percentage point, yet inflation has ticked up each month.

As the dominant global economy moves by the US Fed demand closer attention. Fed policymakers are trying to strike a careful balance in timing their rate cuts. The economy remains strong, unemployment remains low and job growth has improved. However, President Trump has promised to impose steep tariffs on imports, restrict immigration and cut taxes - all policies that economists warn could push up prices further.

Following no rate cut at the most recent meeting, it is expected that the Fed will not rush into further cuts imminently, but the Bloomberg consensus forecasts 4.05% in Q2 of 2025, reducing further to 3.8% by the end of the year.

This is important for aircraft leasing as the 10Y Swap, which is a key rate for aircraft lessors, is 90% correlated with the Fed rate.

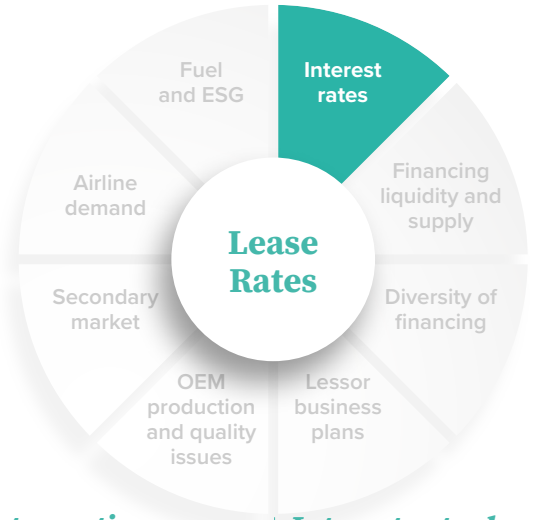
We previously commented that 2024 was set to be a significant year for debt maturities, with almost $18 billion of bonds falling due across eight IG-rated lessors, along with $5.5 billion of bank debt and RCFs. As of mid-December, there were $17.7 billion of bond issuances. On the bank debt side, $5.9 billion had been financed.

In addition, the sector had $9.1 billion of near-term capex needs relating to its orderbook commitments, down from $18.8 billion at the start of the year. Manufacturing delays at the OEMs shifted a portion of this to the right.

Sharp falls in interest rates are usually linked to economic downturns or shocks, which often reduce the supply of alternative financing sources at a time when airlines are seeking additional funding, as their business may be under stress.

At strong points in the economic cycle, interest rates typically increase to combat inflationary pressures. At such times, airline profitability usually benefits from the strong economy and alternative sources of (often cheaper) funding are plentiful.

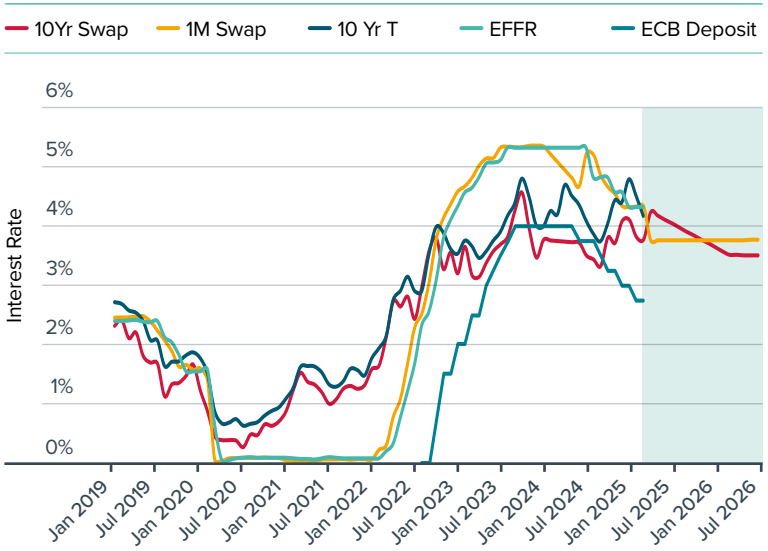
With the tempering of expectations for quicker and steeper interest rate cuts, we retain our opinion that interest rates will remain higher for longer, supporting higher lease rates.



Lessors to continue passing on increased funding costs.

Interest rates began reducing in H2 2024 although the rate of further cuts is uncertain.

Figure 1: Interest Rates



Source: Bloomberg. Forecast 10Y SOFR and 1M SOFR are per forward curves as-at March 2025

Industry financing options remain stable

SMBC AC forecast a financing environment in 2025, very similar to that experienced in 2024.

Money supply globally remained strong in 2024, and higher interest rates drove increased bank profitability, which may have further helped wider liquidity. As we look to the rest of 2025, there are no real signs that we will see any contraction, as most governments continue to look to stimulate their economies.

The funding requirement for 2024 proved to be less than expected for a number of reasons, not least of which was the lower-than-expected deliveries across the industry. However, we also saw an increased amount of airlines using their own cash to finance aircraft.

The finance needs of the airline industry are forecast to increase in 2025, as Boeing in particular ramps up production and Airbus is expected to exceed 800 deliveries in 2025.

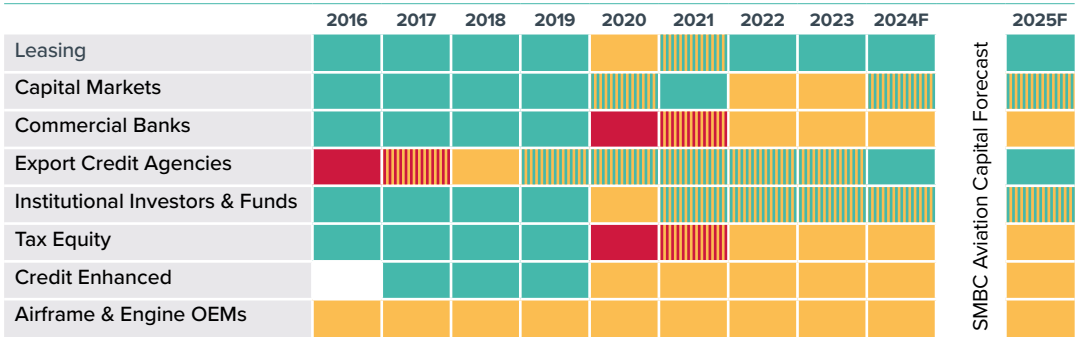
There has also been an uplift in ECA funding as airlines have looked to rebuild their balance sheets.

The ABS market has seen a resurgence in the second half of 2024, albeit just on the debt side, with sales of the equity remaining someway off. Demand is expected to continue through 2025 with total issuance in the region of $8-$10billion.

Financing outlook stable.

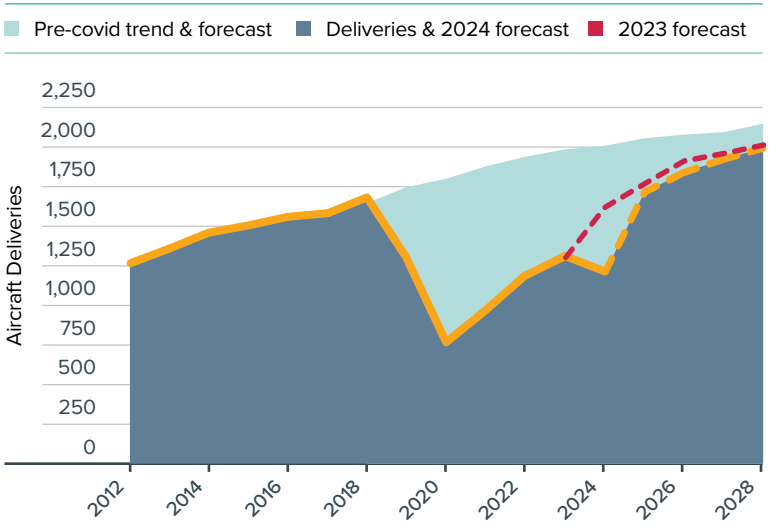
ABS debt issuances to increase.

Figure 2: Boeing Commercial Aircraft Finance Market Outlook (CAFMO) and SMBC Aviation Capital forecast



Source: Boeing Commercial Aircraft Finance Market Outlook & SMBC Aviation Capital Analysis

Figure 3: Deliveries & Forecast Supply



Source: Delivery Chart – Cirium Fleets Analyzer & SMBC Aviation Capital analysis

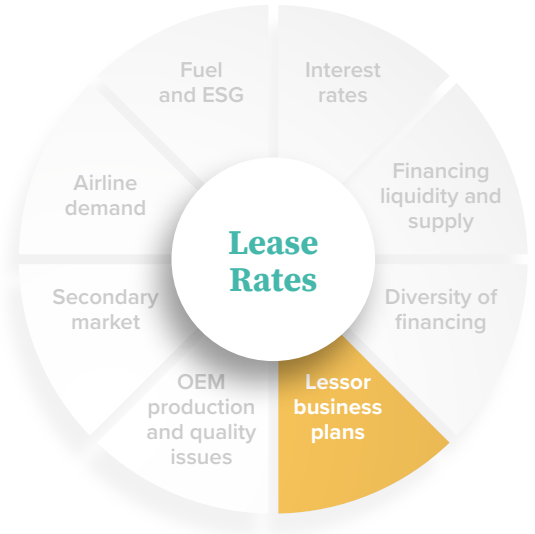
Lessor portfolio trading to increase

We have seen some lessors pull back on their expansion plans as they have either failed to reach critical size or execute on their wider business strategy. We also saw a number of lessor platforms put up for sale in 2024, but some did not sell as we saw more disciplined pricing from prospective purchasers. We believe that we will see further sales in 2025.

A reduction in the cost of borrowing should see an increase in portfolio trading amongst lessors. Some lessors have time limited funds which need to be deployed and in the absence of suitable portfolios, some turned to the SLB space. With increased portfolio churn, we expect to see a reduction in the number of purchasers in the SLB space, or a reduction in the amount of available capital to deploy.

This should help boost LRFs in the longer term but at the moment, SLB remains highly competitive.

During the MAX grounding and Covid-19 downturn, strongly capitalized lessors were able to take advantage and grow their books, which led to an above average share of deliveries for lessors. Across 2023 and 2024 this has reverted to mean, we would expect this to continue into 2025.



More disciplined pricing on lessor platform sales.

Figure 4: Lessor Cap-Ex

Source: Cirium Fleets Analyzer & SMBC AC analysis.
Western built jets, Narrowbody and Widebody aircraft.

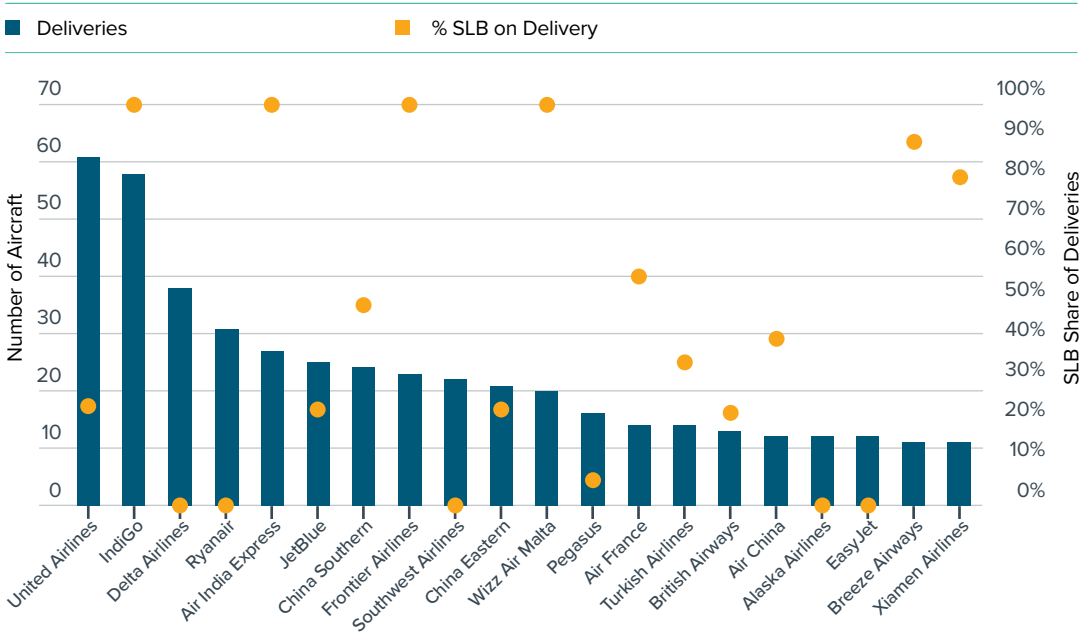
Lessor portfolio trading to increase continued

Specifically on those airlines taking delivery of new aircraft, the quantity of SLBs is determined by each airlines financing options. In 2024, airlines such as Delta, Ryanair and Alaska have not engaged in SLBs, while the likes of Wizz and Air India will SLB up to 100% of their deliveries. So, the demand for SLBs is not just a function of production rates, but driven by which airlines are taking delivery, and what is their financing strategy. These strategies can change in time, IndiGo were traditionally an off-balance sheet operator but are now diversifying into Finance Leases and other forms of on-balance sheet financing.

Given the potential for sustained inflation over the medium term, potential buyers may factor in more bullish outlook on residual values when analysing cash flows which would support trading volumes. This may however be slightly offset by higher discount rates given the interest rate volatility.

More disciplined pricing on lessor platform sales.

Figure 5: Airline Deliveries 2024 (Top 20)



Source: Cirium Fleets Analyzer & SMBC AC analysis. Western built jets, Narrowbody and Widebody aircraft.

New aircraft supply impeded by lower-than-expected deliveries

Supply of aircraft can either come as new aircraft deliveries from the OEMs, or as used aircraft transitions or extensions (aircraft can re-enter service from storage or can be extended instead of being retired).

In the new aircraft space total production for narrowbody and widebody aircraft in 2024 was just over 1,100 aircraft, disappointingly falling short of 2023 and similar to what was achieved in 2022.

Airbus at the beginning of the year forecast 800 deliveries, that number was revised down to around 770, driven by persistent supply-chain issues particularly cabin equipment, engines and aerostructures. Thanks to a very strong December, Airbus almost reached that figure, finishing the year with 766 deliveries. Since the trough in 2020, Airbus have successfully increased deliveries each year and they expect around 820 deliveries in 2025.

Boeing did not provide guidance at the start of the year due to the volatility in their output, but most forecasters had estimated deliveries at anywhere between 430 and 480, ultimately the final number for 2024 was just under 350. They were delivering over 30 MAX aircraft per month, including pre-built, prior to the strike but will be slow to rebuild to FAA limit of 38 per month. As a rough guide, one day of striking equals one aircraft not delivered, so the 53-day strike delays could lead to over 50 missed deliveries. This impact was further increased as production lines were slow to get back to their previous level of productivity.

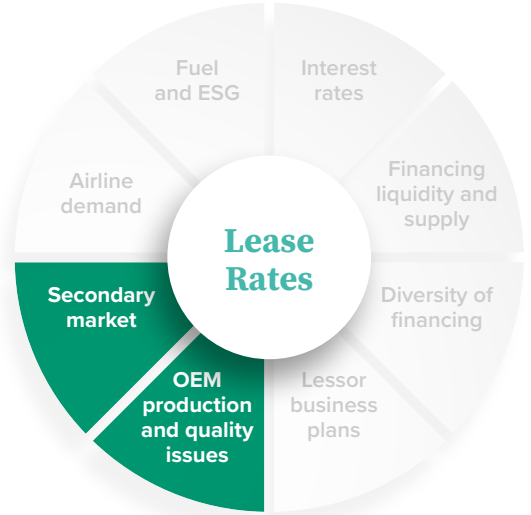
There are also currently around 100 MAX fuselages awaiting delivery from Spirit AeroSystems to Boeing, which is equivalent to five months of production. As of the time of publication, Boeing has yet to provide guidance for 2025 deliveries.

However, delivery rates and production rates are not the same thing. Using First Flight as a proxy for production, you can see in the chart that production is not linear, and for Airbus, it varied from 33 to 62 aircraft per month through 2024. Deliveries were broadly in line for Airbus aside from the year-end spike, but for Boeing that typical year-end spike never occurred.

Supply chain issues remain considerable and are expected to remain a challenge for the coming two to four years. Bottlenecks can be distilled to material and parts shortages, lack of skilled labour and underinvestment in additional capacity. As one example, forging capacity demand is set to increase by 20% in the next couple of years, yet Russia controls almost 20% of this space, much of which is going offline.

Airbus commercial chief, Christian Scherer, stated that 98% of their suppliers are delivering on time, but such is the nature of the supply-chain process that this 2% can cause bottlenecks. Longer term, production ramp-up to rate 75 for the A320neo family has slipped a year, until 2027.

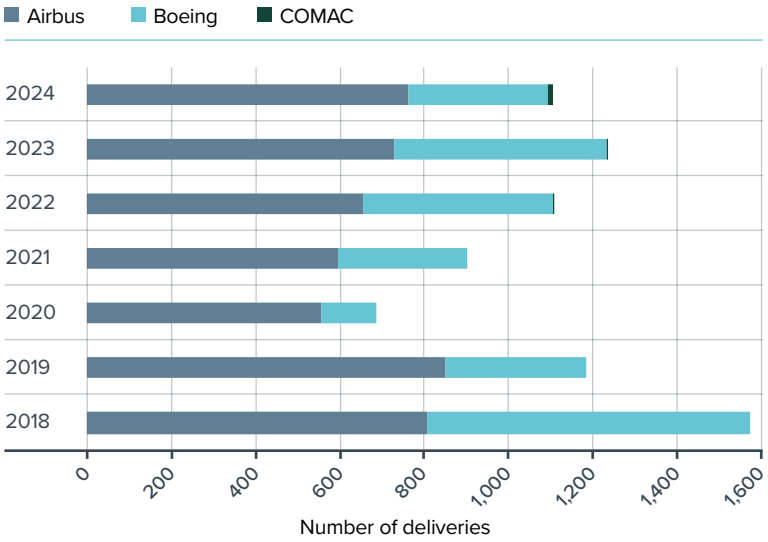
In July of 2024, Boeing announced that it had agreed to acquire Spirit AeroSystems, one of the major suppliers in the space. This should lead to a more streamlined and efficient production of fuselages and other components. Following the door plug incident Boeing will no longer accept fuselages from Spirit, unless they pass an inspection. This is to reduce the amount of rework needed on Boeing production line, along with reducing travelled work. To date this requirement seems to be working well in terms of the quality received by Boeing.



2024 deliveries fell below 2023, will rebound in 2025.

Supply chain issues continue.

Figure 6: Commercial Aircraft Deliveries



Source: Cirium Fleets Analyzer, SMBC Analysis. Narrowbody & widebody passenger and freighter aircraft.

Secondary market availability very tight

While supply chain issues are generally discussed around new deliveries, issues persist across the whole commercial aviation sphere.

Airlines are experiencing delays with retrofits, particularly due to seat issues. The increased complexity of first and business class seats has led to increased development time while overall demand has also increased in a supply constrained environment.

In the MRO world, there are delays receiving parts for engine overhauls. For example, the age profile of the 787 family means that some engines are reaching their second (heavier) performance restoration which are more part intensive. Particularly on the Trent 1000, the delay of parts being produced has led to extended Turn Around Times (TAT) at the engine shops.

Storage rates are approaching the pre-Covid average of 8% and currently sits at around 11%. Stored aircraft had been declining steadily from the 60% peak in April 2020, but has been stuck around the 11-13% mark since mid-2023 due to the PW issues on the A320neo, A220 and E2 families. There are currently c.600 PW powered aircraft in storage which is at peak and should stay around this number in the coming months as MSNs move in and out of storage before beginning to decline.

It is important to note that not all the aircraft that make up the 11% are available to re-enter service. Aircraft in storage could be awaiting freighter conversion, undergoing maintenance, parked awaiting part-out etc. When drilling down further on an MSN-by-MSN basis it is evident that less than 1% of both Single-Aisles and Twin-Aisles are actually available to re-enter service, illustrating the very constrained supply in the secondary market.

Aircraft extensions are extremely popular, running at up to 80% versus the more typical 50% rate experience pre-Covid. While extensions are increasingly popular, terms are also increasing. We are also seeing airlines looking to lock in extensions further in advance due to competition from multiple airlines wanting that aircraft. This reduced supply of used aircraft in the re-lease market increases competition and has maintained an upward pressure on lease rates.

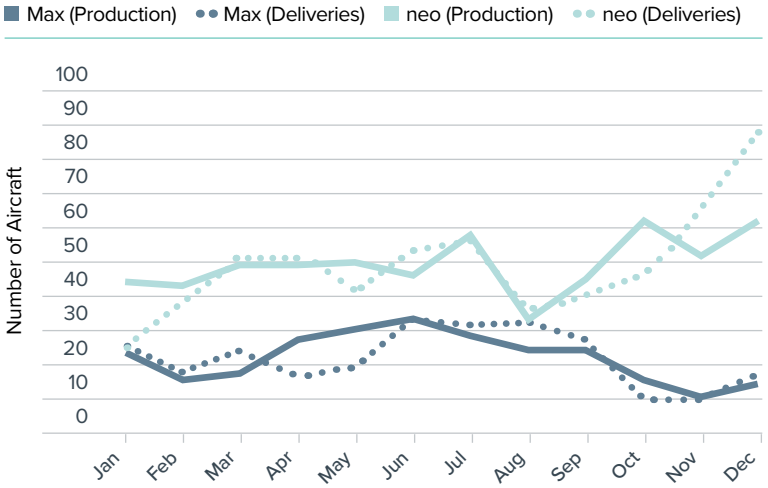
The Chinese market for new aircraft is an interesting one. One fifth of future deliveries are expected to be into China, but deliveries since 2020 are muted, in 2024 deliveries are down 75% versus the peak in 2018 representing under 15% of global deliveries. On a global basis, this eases the supply constraint but such an important market underdelivering versus the OEM forecast is one to pay attention to. However, any reversal of this trend would tighten supply even further.

Finally, much of this analysis is focused on an aircraft basis. If we consider the market on a seat basis, the up-gauging of aircraft (e.g. A320 to A321) and densification of cabins has increased available seat supply into the market and helped reduce the problem.

Aircraft availability very tight.

Extension rates running at record levels.

Figure 7: Single-Aisle Delivery & Production Rates



Source: Cirium Fleets Analyzer, SMBC Aviation Capital Analysis

Airline demand in 2024 was very robust, but profitability slipped

2024 was another strong year for airline profits, despite slipping a little YoY. However, IATA does forecast a rebound for 2025. Overall demand was strong, hitting record levels globally with an increase of 11.2%. This was primarily driven by emerging markets, particularly within APAC. Northeast Asia followed by Northern Africa and Eastern Europe showed the strongest growth.

In contrast to our optimism last year, long-haul markets remain constrained by Asia, with transpacific down 18% and China international down 22% versus the 2019 base, while the other markets have recovered. There are limited signs that this is going to reverse significantly in 2025.

One area which has remained strong is the premium cabin. Although premium passengers constitute 3% of all travellers, they represent 15% of passenger revenues. Growth in both cabins were aligned until Q3 2023 but since then growth in premium passengers pulled ahead significantly, indicating a resurgence in corporate travel.

Meanwhile across 2024, the ratio between the two fares has also widened, a welcome benefit to dual cabin operators. This trend has been especially visible in the US where the majors have seen very strong growth across their premium product. There are some signs that this might be plateauing on the back of increased economic uncertainty in the US. The move however does drive extra demand for aircraft as premium aircraft have less seats, so there may be an increase in aircraft to service some of the major routes.

For airlines with dedicated freighters or those generating revenue from belly cargo, 2024 was a very strong year. Cargo Tonne-Kilometers (CTKs) reached an all-time high with almost 12% growth. This was primarily driven by e-commerce growth and capacity limitations in ocean shipping, with this demand expected to continue to rise in 2025. Cargo will continue to represent around 15% of total airline revenue.

Costs for airlines rose across all non-fuel areas exacerbated by supply chain issues, salary increases, labour shortages and maintenance cost escalation. With reduced deliveries the global average age of the commercial fleet continues to increase, resulting in increased non-routine maintenance and higher fuel burn.

Along with overall traffic numbers, it is important to look at connectivity in terms of city pairs. The restoration of routes cut during Covid-aircraft, and the establishment of new routes means that there are now around 400 more connections than in 2019. International recovery lagged, but driven by a surge in APAC, international connectivity has returned to 2019 levels.

In a low-margin industry, airlines need to maximise the utilization of their assets. Adjusting for seasonality, utilization further improved in 2024, returning to 2019 levels, while load factors are at a record high.

Profitability in 2024 slipped versus 2023, recovery expected.

Figure 8: Global Airline Traffic and Profitability

	Traffic Growth (RPK)		Net Profit ($bn)	
	2024E	**2025F**	**2024E**	**2025F**
Global	11.2%	8.0%	$31.5	$36.6
N. America	5.3%	3.0%	$11.8	$13.8
Europe	8.7%	7.0%	$10.0	$11.9
Asia-Pacific	18.6%	11.7%	$3.2	$3.6
Middle East	10.2%	9.5%	$5.3	$5.9
L. America	8.5%	8.0%	$1.0	$1.3
Africa	13.5%	8.0%	$0.1	$0.2

Source: IATA

Airline demand in 2024 was very robust, but profitability slipped continued

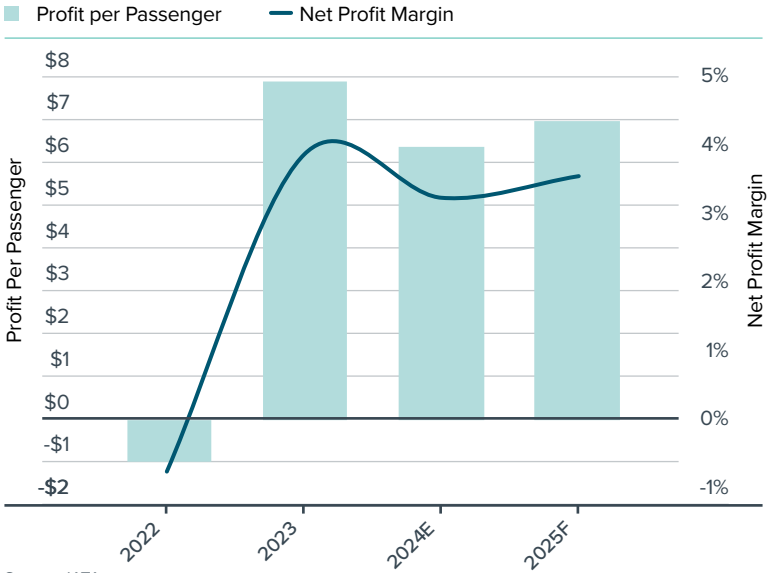
IATA forecast an 8% growth in traffic in 2025 but with aircraft availability tight and airlines at effective maximum utilization of their assets, growth will come from OEM deliveries alone so this target may be difficult to achieve due to production uncertainties. As mentioned before this uncertainty is driving an increased level of extensions and asset purchases by the airlines at lease end.

We have moved the rating on this sector to neutral on the basis that we see airline demand plateauing rather than peaking. The outlook for the industry remains strong and airlines continue to want aircraft but the rate of growth has levelled out.

One side effect of the tight market has been a fall-off in new entrants. According to analysis conducted by IBA, the number of airlines in existence has declined steadily from c.1,300 in 2008 to c.1,000 in 2024. The net change in 2024 is essentially flat with around 25 airlines entering operations and another 25 closing down, both the lowest number since the Global Financial Crisis.

Premium traffic driving airline revenue.

Figure 9: Global Airline Profitability



Source: IATA

Jet fuel prices stable, slight decline expected for 2025

Fuel as a percentage of operating costs at airlines declined to 30% in 2024 with a further decline forecast for 2025. According to IATA, the estimated jet fuel price drop of 15% to 25% from 2023 to 2025 could cause yields to decline by 7.5% to 12.5% as some of these savings are passed onto passengers.

Despite this fall, airlines are expected to remain focused on reducing their fuel consumption and their emissions especially in markets where government bodies have set reduction targets. Modern fuel-efficient aircraft will continue to be a core driver of this objective.

This pressure may have eased slightly, in that, throughout 2024, Brent averaged c.$80/b and has been quite stable compared to historic oil price volatility despite multiple geopolitical events. Meanwhile, the crack spread has averaged around $15/b, which is a welcome reduction for airlines compared to the average crack spread of $35/b across 2022 & 2023. An increase in refinery capacity has helped reduce the spread below the $20/b mark and it is expected to remain below this mark through the coming months.

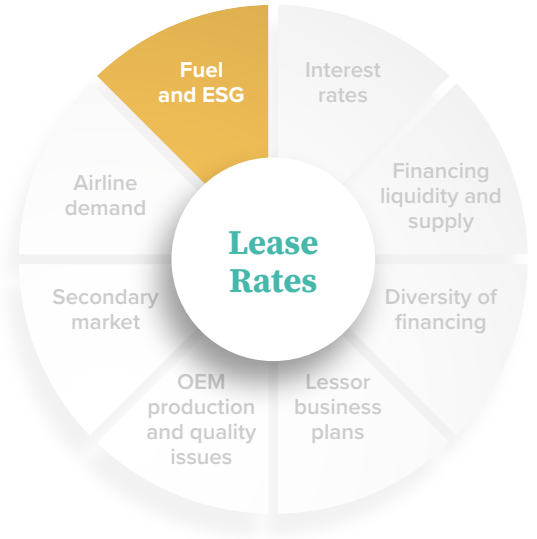
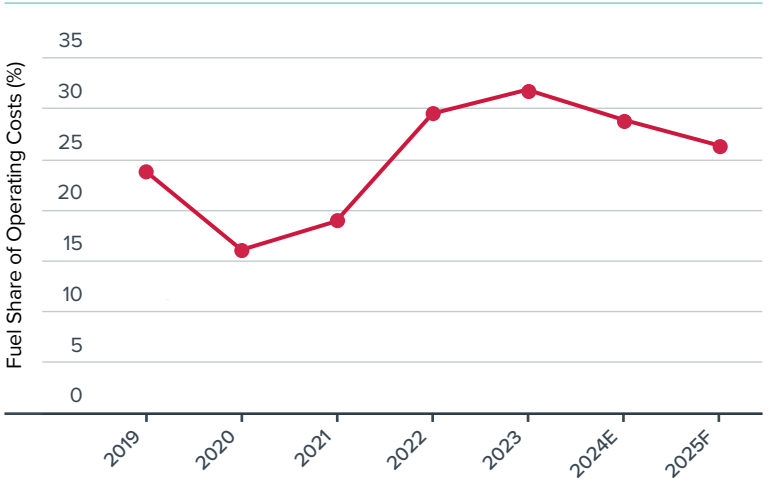


Figure 10: Fuel as a Share of Operating Costs



Source: IATA

Jet fuel prices stable, slight decline expected for 2025

S&P Global Ratings assumes moderately lower oil prices of $75/b in 2025 despite conflicts in the Middle East. Conflicts involving oil-producing nations or which are near transportation facilities add a risk premium to prices. Of course, supply is the key driver of price and OPEC Plus are a key supplier. They are currently holding back c.6 million barrels per day of output, equivalent to 5.7% of global supply, but there is an expectation they will increase production imminently.

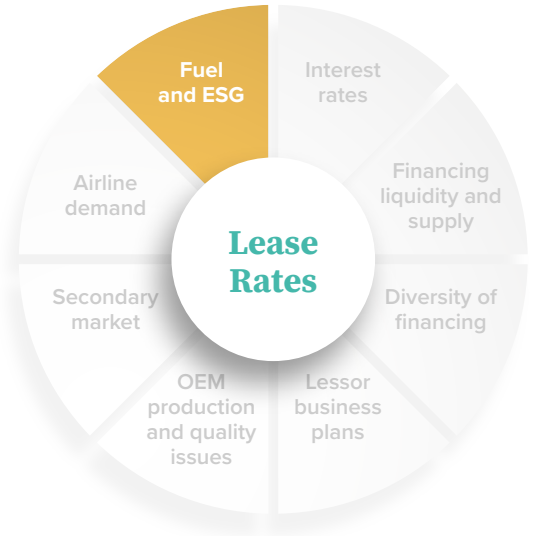
With Donald Trump now re-elected as President, US oil production is expected to increase after setting a target of 3 million additional barrels per day by 2028. However, that is unlikely as production is constrained by low oil prices; for example, shale firms have little incentive to drill unless oil prices reach $89 per barrel.

While operating new technology aircraft is key for reducing fuel burn, the increased use of Sustainable Aviation Fuels (SAF) is still key to reducing emissions over the longer term. Cost and supply remain the key issues to its uptake. According to IATA, in 2023 the industry consumed SAF at a cost of $2,500 per ton (or 2.8x jet fuel) adding c.$750 million to the industry fuel bill.

Currently, global SAF production is less than 1% of the total jet fuel market and while production increased 2-3x in 2024 versus 2023, it will need to scale up rapidly. There is still a very wide range as to what the ramp up might look like. According to BloombergNEF (BNEF) by 2030 SAF volume could be between 4 and 9 billion gallons per year, representing between 3 and 8% of global jet fuel.

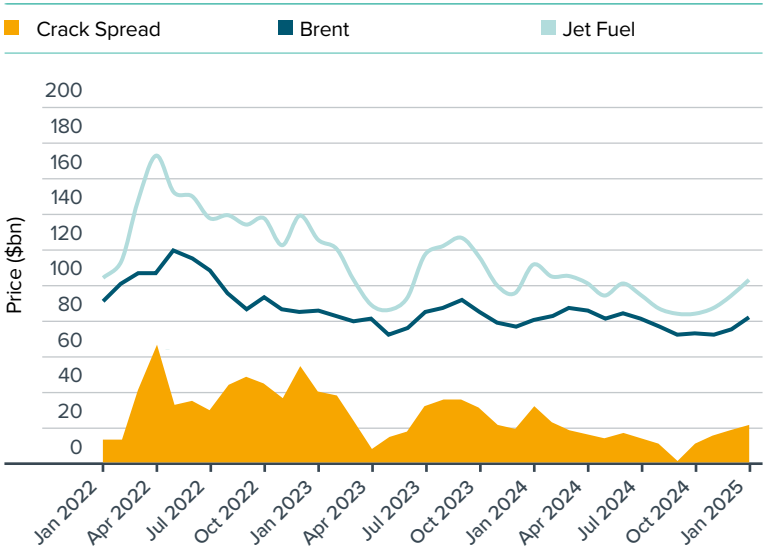
The price premium for SAF will likely impact air fares which could see increases of 5-20% but this is highly dependent on the blend ratio (ratio of jet fuel to SAF). It also depends on the type of SAF used, the premium could be 2–5 times the price of jet fuel depending on the feedstock or technology used to create SAF.

Increased investment is required in the clean energy space but capital is increasingly flowing to oil companies due to higher returns. Benchmarked against January 2021, the S&P Global Oil Index increased 60% while the S&P Global Clean Energy Index declined by the same amount.



Oil prices to decline slightly through 2025 with SAF production ramping up.

Figure 11: Fuel Prices



Source: Bloomberg. Brent price is BFO Brent, Jet fuel price is Jet Fuel 54

Summary: Push and pull factors on lease rates point to sustained higher rates

– Fuel outlook stable to declining
– Environmental considerations remain
– SAF ramp-up slower than expected

– The pace of interest rate reductions has been slower than expected with more upside risk than downside

– Traffic & Load Factors have recovered
– Continued focus on premium product
– Chinese international traffic continues to underwhelm

– No change to liquidity at government level which continues to support third party financiers and investors

– Availability essentially nil
– Extension rates remain very high with long terms and high rates
– New Tech engine issues persist

– Good access to debt markets
– Active ABS market (debt only)
– Weak Yen continues to impact JOL/JOLCO

– Both OEMs missed delivery targets in 2024
– Supply chain issues persist
– Ramp-up is ambitious

– Established lessors focus on returning profitability to pre-Covid levels
– Active portfolio sales

Traffic Light System Strong Positive Impact · Positive Impact · Neutral Impact · Negative Impact

Glossary

Asset Back Security (ABS)
Asset Backed Security uses a Special Purpose Vehicle (SPV) to purchase aircraft, typically sourced from the books of an existing lessor with the SPV holding the rights to lease payments to airlines. The SPV finances the purchase of the aircraft through the issuance of tranched Notes to investors.

Current Market Lease Rate (CMLR)
This relates to an operating lease rate, this is specifically a “net dry operating lease” rate. The lease of an aircraft whereby the lessor takes all of the risks and rewards of ownership, and the lessee takes all of the risks and rewards of operation.

EETC
Enhanced Equipment Trust Certificates are corporate debt securities structured though SPVs, typically issued by airlines and secured on aircraft.

ESG
Environmental Social and Governance is a framework that is used to determine how sustainable an organisation or company is

IATA
The International Air Transport Association is the trade association for the world’s airlines representing some 320 airlines or 83% of total air traffic

Japanese Operating Lease (JOL)
JOL is an operating lease funded by the equity investment from Japanese investor(s) and non-recourse debt from financial institution(s). This structure is used mainly in the aviation industry to provide airlines with 100% financing of aircraft. The equity investor(s) will enjoy tax benefits from the JOL structure and exposed to the residual value risk at the end of the lease.

Japanese Operating Lease with Call Option (JOLCO)
JOLCO is an operating lease which gives the lessee an option to purchase the asset at the end of the lease, or at some point during the lease period, at the purchase price determined at the commencement of the lease.

Narrowbody aircraft
Also known as a single aisle aircraft, allowing up to 6 abreast seating in a cabin less than 4m with a single aisle (passage between rows of seats)

Operating Lease
From a financial reporting perspective, a lease that has the characteristics of a usage agreement and also meets certain criteria established by the FASB. Such a lease is not required to be shown on the balance sheet of the lessee. The term also is used to refer to leases in which the lessor has taken a significant residual position in the lease pricing and- therefore- must salvage the equipment for a certain value at the end of the lease term in order to earn its rate of return.

Original Equipment Manufacturer (OEM)
Companies involved with the design, manufacture and assembly of aircraft e.g. Boeing, Airbus, CFM, P&W and Honeywell.

Sale-Lease Back (SLB)
A transaction that involves the sale of equipment to a leasing company and a subsequent lease of the same equipment back to the original owner who continues to use the equipment.

Widebody aircraft
Also known as a twin aisle aircraft, allowing at least 7 abreast seating in a cabin more than 5m with a two aisles (passage between rows of seats)

About the authors

Shane Matthews

Shane is Head of the Strategic and Market Analysis Team leading a team of six analysts who have responsibility for SMBC Aviation Capital's proprietary models, databases and market analysis. He joined the company in 2005 as a credit risk analyst covering customers in Asia Pacific. Shane spent 10 years as an equity analyst covering airlines with NCB Stockbrokers and HSBC Securities in Singapore. He holds a Bachelor of Commerce Degree and a Masters in Business Studies in Banking and Finance from University College Dublin.

Darren Naughton

Darren joined SMBC Aviation Capital in 2004 as a Residual Value Risk Analyst before joining the credit risk team covering airlines in Europe and North Africa. In 2014 he joined the Strategic and Market Analysis team with responsibility for industry analysis, forecasting and portfolio risk management. Prior to joining SMBC Aviation Capital, Darren worked in the semiconductor industry and has an Engineering Degree and an MBA from Trinity College Dublin.

David Griffin

David is VP Strategic and Market Analysis. He initially joined SMBC Aviation Capital in 2021 as a member of the Commercial Analysis team, with responsibility for assessment and evaluation of all company transactions including asset acquisitions, placements and trading before joining the SMA team in March 2023. Prior to joining SMBC Aviation Capital, David was a Valuation Consultant with Ascend by Cirium. David holds a Bachelor's Degree in Aeronautical Engineering and a Master's in Business Management, both from the University of Limerick. He is also an ISTAT Certified Appraiser.

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