



AIRCRAFT, ENGINE & PARTS MANUFACTURING

TARIFF ALERT

CURRENT TRENDS

- Cancellations of Boeing 737 Max orders have ramped up, including 150 cancellations in March 2020.
- The United States increased tariffs from 10% to 15% on European aircraft and aircraft parts, effective March 18, 2020.
- Global air travel has dropped by 95% due to worldwide stay-at-home orders.
- The coronavirus pandemic is projected to cost the airline industry \$63 to \$113 billion in lost revenue.

PROJECTED VALUES (12-MONTH OUTLOOK)



APPROXIMATE NET RECOVERY ON COST*

80-100%

FG subject to an order

60-80%

FG subject to aftermarket demand

0-20%

surplus FG

0-10%

WIP as-is

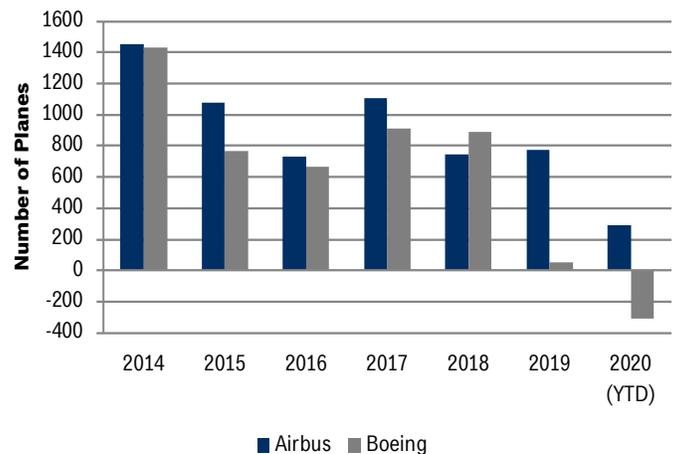
40-60%

metal stock, mill size

50-70%

detail parts in demand

ANNUAL JET ORDERS (NET IN YEAR OF CANCELLATION)



40-60%

hardware in demand

0-20%

surplus details and hardware

*737 MAX inventory (-10 to -15 pt. decrease)

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ONGOING ORDER CANCELLATIONS AND HIGHER TARIFFS

IMPACT THE INDUSTRY: Boeing continues to see backlash due to the grounding of the 737 Max. In the month of March 2020 alone, Boeing customers cancelled 150 737 Max orders, the most cancellations the company has seen in over a decade. In particular, aircraft-leasing firm Avalon cancelled 75 orders worth close to \$8 billion because of the growing uncertainty around the reliability of the 737 Max and the increasing concern from the spread of the coronavirus. Adding to the pressure on the company, Alafco Aviation Lease and Finance Co., a Kuwaiti aviation leasing company, sued Boeing in April 2020 for the return of \$336 million that it paid in advance for 40 of the still-grounded 737 Max planes.

The company faults Boeing for failing to deliver its planes on time and refusing to return advance payments on a now-cancelled order for 40 aircraft. As the 737 Max remains grounded, additional orders are not being fulfilled on-time, allowing customers to cancel orders without penalty. The timeframe for the 737 Max to be back in the air remains unclear. At the beginning of 2020, there was an expectation that the certification test flights would occur in the spring or early summer; that has now been delayed and test flights are now expected to begin in the fall of 2020. Year-to-date net 737 Max orders were negative 314 through the end of March 2020.

On February 14, 2020, the Trump administration announced it would increase tariffs on aircraft imported from the European Union from 10 to 15 percent in an attempt to help domestic companies compete more effectively. The tariffs went into effect on March 18, 2020, amid the continuing spread of the coronavirus and increasing fears of a subsequent recession. The tariff increase was driven by an almost 16-year dispute over the subsidies European governments gave Airbus that put Boeing at a disadvantage. The European Union is looking to settle the issue, and it remains to be seen if the United States and the European Union can come to a resolution on the conflict.

MARKET IMPACT OF CORONAVIRUS: The spread of coronavirus has had serious impacts across the air travel industry. Companies like Boeing and Airbus have been forced to temporarily halt production on some aircraft and have even gone as far as shutting down entire factories. In early April 2020, Boeing suspended production of its 787 Dreamliner in Charleston, South Carolina due to the fear of spreading the virus among workers in the factories. The Boeing production plant in Seattle, Washington also suspended operations, effectively halting commercial aircraft production. Boeing reported deliveries of 50 commercial aircraft in the first quarter of 2020 as well as 39 defense-related aircraft. However, the cancellations of 196 aircraft during that same period represents a significant issue for Boeing.

The Expert: Alex Sutton



Alex Sutton oversees Gordon Brothers' global industrial inventory valuations. He previously headed AccuVal-LiquiTec's Inventory Valuation practice, which was acquired by Gordon Brothers in 2015, where his team produced reports used primarily for financing and financial reporting. Read his full bio [here](#)

Airbus has also shut down many of its factories in the United States and abroad due to the spread of the coronavirus, including pausing production at its facility in Mobile, Alabama and its facility in Germany. On April 8, 2020, Airbus announced that it was reducing its production rates for the A320 by 33 percent, the A330 by 66 percent, and the A350 by 40 percent. Airbus reported delivering 122 aircraft in the first quarter of 2020. For the same period, Airbus booked orders for 356 aircraft and cancelled 66 orders.

In addition to halting production across the globe, strict stay-at-home orders have caused many airlines to ground the majority of their flights. This has had a severe impact on the commercial aviation industry as airline companies struggle for cash and have been forced to furlough staff or ask employees to take voluntary pay cuts. With air passenger miles flown dropping by more than 84 percent in the second half of March 2020, it is easy to see why companies like Delta and United have reported their first losses in over five years and adjusted their spring schedules downward to attempt to right size demand. Delta's CEO has stated that revenue in the current quarter is projected to be 90 percent lower than anticipated, and the business could take two to three years to recover.

The same struggles are being seen abroad with Lufthansa, the German international airline company. Lufthansa received a \$10 billion bailout from the German government and has seen a dramatic revenue drop due to global travel restrictions; it is projected that the company is generating losses of approximately \$1 million every hour. The International Air Transport Association has forecasted that global passenger numbers will fall 55 percent in 2020 compared with 2019. With the number of flights declining, a similar fate is presenting for the ancillary companies that supply and support airline corporations. With fewer flights each day, the need for companies to repair and maintain current aircraft fleets has dropped significantly. As a result, companies like Boeing and Airbus have seen staggering drops in activity and revenue.

A study released in late March 2020 by consulting firm Oliver Wyman estimated the total global impact of the coronavirus on maintenance, repair, and operations to be between \$17 and \$35 billion, a 19 to 39 percent reduction from its original \$91 billion forecast for 2020. It remains to be seen how much more the coronavirus will impact the entire aviation industry, and how long it will take the industry to recover.

INDUSTRY OUTLOOK: The outlook for the commercial aviation industry is difficult to gauge due to the growing concerns and complications of the spread of the coronavirus and the associated global travel shutdown. Global air travel has dropped by 95 percent due to worldwide stay-at-home orders, and the pandemic is projected to cost the airline industry from \$63 billion to as much as \$113 billion in lost revenue.

Prior to the outbreak, the industry was continuing to grow as the economy grew and more people spent disposable income on travel. However, even before the outbreak the Federal Aviation Administration projected that the number of general aviation and air taxi aircraft would decline, causing the overall fleet to become younger and require fewer repairs and less maintenance, thus negatively affecting the industry. Despite the downturn on the commercial side, manufacturers on the defense aviation side of the business are expected to remain stable.



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