An Avinode Business Intelligence White Paper
February 17, 2014
A year just like any other?

Since the market crashed, in late 2008, the industry has been looking for signs of recovery. In the time since, industry analysts and professionals have released copious forecasts predicting an imminent turnaround; observable signals, however, have been scarce. Throughout 2012, flight activity numbers remained depressed, jet deliveries declined, high levels of used aircraft inventory further reduced re-sale values and manufacturers delayed or cancelled new models. Even the seemingly steady roar of the Chinese dragon seemed to be fading into white noise.
Then came 2013, and despite numerous predictions to the contrary, it did not start out all that differently than previous years. Positive forecasts were still released but, although they were tempered by five years of disappointment, the numbers remained in the red.

Then, halfway through the year, something changed. US flight activity, which had been hovering around breakeven for a while, started to stabilize. The numbers were still far from ’08 levels but at least they had stopped dropping. Europe, which was busy playing out a discouraging story of its own, finally broke back into the black in August. New aircraft models were released, finalized and delivered. Used jet inventories began to decrease giving aircraft prices a small push. Press releases announced new ventures, co-operations and company acquisitions. The US economy even began to slowly, but steadily, stabilize driving up the GDP, stock markets and corporate profits.

While it’s true that we can’t discern a full story from only 6 months of data, the question is whether 6 positive months are enough to confirm that we are finally seeing the light at the end of the proverbial tunnel. This is the question we will explore in this white paper by piecing together industry trends and news to create a clearer picture of what actually happened in 2013 and what it means for 2014 and beyond.
In October 2012 Avinode Business Intelligence released its 2013 business jet activity forecast. Our projections showed an expected decrease of 0.1% in US activity in 2013, from 2012 numbers, and a 3.2% decrease in European activity. Looking back from our January vantage point we can see that this has turned out to be very close to the truth.

US Business Jet Activity - back in the black!

The 2013 year-end figures for the US were not too far off the Avinode forecast as flight activity in the country ended 0.3% up from 2012. However, when you break the figures down by month the results vary significantly. The year began with 3 months of decline, including February’s 5.0% decrease, which was the low point of 2013. This was followed by 5 months that were basically on par with 2012 numbers and then 4 months of positive figures. Overall, the 2013 numbers were encouraging and seem to indicate that the industry may have already begun stabilizing around a new norm in 2012.

On the regional level, we can see that the Midwest continued to struggle in 2013 with a year-over-decline of 2.1% from 2012. Cities like St. Louis (-7.3%) and Indianapolis (-9.3%) appear to be the main drivers of this decline in activity.
How did US bizjet travelers fly in 2013?

Business Jet activity can be divided into three sectors: Part 91, which covers corporate use and ownership by companies like GE and Pepsi; Part 91K, which is a variant of corporate ownership covering fractional ownership, as characterized by NetJets and the like; and Part 135, which covers the charter of business jet aircraft by companies such as XOJET and Solaris. Part 135 accounts for roughly 40% of flown activity in the US.

In 2013 activity varied between these sectors with activity in Part 91K diverging from that of the charter market. The impact of CitationAir’s exit from the fractional market⁶ and Avantair’s bankruptcy⁷ meant that the Part 91K sector had a difficult year overall. Charter also faced declines, ending the year 0.7% down after spending most of 2013 in the red.

The West and South remained in the black for the year, and the Northeast rebounded into positive figures. In addition to being the most positive indicator of the upswing, the return of the Northeast appears to signify that business travel from the region is finally picking up.

Growth in the Northeast was spread between Teterboro (+3.6%), Boston (+3.8%), Philadelphia (+4.0%) and Farmingdale (+5.0%). All of which are heavily used for business related traffic. The entertainment and tech driven West Coast showed continued growth driven partly by Burbank Airport, which noted an impressive 14% increase in traffic. The leisure (Florida) and energy (Texas) driven South also had a good 2013 with continually improving figures throughout the year.
European Business Jet Activity – rebounding!

In the middle of 2013 the outlook for European business jet activity was bleak. The year had started the same way that 2012 ended, in a vast sea of red. Activity continued to decline, and many in the industry wondered if we would ever see the end of it. Business jet departures out of Europe dropped an average of 3.3% from 2012 numbers, and in March alone they fell 8.2%.

In August, however, fortunes changed. Departures started to increase and with that hope finally returned to the aviation community. September, October and November continued this positive trend by finishing on par with 2012 numbers. December took it one step further by finishing 2.2% ahead of the same month in 2012, which left the total activity level of 2013 down only 1.7% from 2012.
Finishing the year with positive figures is, of course, great, but it’s important to remember that these 4 months of growth followed 3 years of constant decline. From 2011 to 2013 the total number of business jet departures decreased by approximately 5.6%, and 2013 brought more disappointment to an already suffering market. That said, the worst of the Euro crisis seems to be over and, although 4 months of stable activity is not nearly enough to cement a turnaround, we do believe that we’re now seeing the first steps of a very slow stabilization and recovery. While we don’t anticipate a return to ’07/’08 levels in the near future we do expect that growth will return.

On a regional level both Northern and Southern Europe struggled in 2013, with Northern Europe suffering more than Southern Europe. Departures out of Northern Europe (E) decreased by 2.9% during the year, while Southern Europe only saw a 0.9% decrease in activity. This is due in part to the fact that Southern Europe is coming back from relatively low numbers after suffering substantial declines in 2012.

Below: Change in business jet flight activity in Northern and Southern Europe between 2012 and 2013. Source: FAA
The discrepancy between Northern and Southern Europe, however, may also be due to the fact that the business travelers are still reluctant to spend company money on a private jet while the leisure travelers are slowly returning to the sector.

In Northern Europe there were few shining stars in 2013. Countries, like the UK (-2.2%) and Germany (-3.5%), that rely heavily on business traffic all saw declines, but Sweden went against the grain with a 4.4% increase in departures. This upturn was mainly due to sizable flight activity increases in the cities of Malmo (+26%) and Linkoping (+16%).

On the southern half of the continent, France (+0.4%), Greece (+3.4%) & Spain (+0.4%) finally came out of the doldrums with positive figures in 2013. It’s interesting to note that growth did not come from the capitals in any of these countries but instead from more leisure focused locations like Nice (+3.3%), Mikonos (+25%) and Malaga (+5.7%).
In January 2012, the fractional market consisted of five main players: NetJets, Flight Options, Flexjet, Avantair & CitationAir. At the time two of them were up for sale, but all five were still operational. As of January 2014 only one of them remains as is, and only two are still operating. (Flight Options and Flexjet are currently maintaining separate brands under the same owner, Directional Aviation Capital.) The Fractional market, in the U.S., has been brutal over the past two years. Those who were not competitive enough either decided to leave the market voluntarily, like CitationAir, or were forced into bankruptcy, like Avantair. The resulting consolidation is remarkable for both the extent and the speed at which it occurred.
Since the launch of NetJets, in 1986, fractional operators have been industry leaders. They are one of the most important buyers, if not the single most important buyer, of new jets and subsequently provide a healthy flow of used aircraft to the secondary market. Their reach is also more widely felt via the millions of dollars worth of business they bring to service suppliers around the globe. In addition, they’ve made many important ‘best practices’ contributions to the industry.

The question now is whether the fractional industry is once again leading the way and therefore foreshadowing a wave of consolidation in the industry at large, or if the fractional business model is outdated and the future of business aviation will be found elsewhere? The truth is likely somewhere in between. While the fractional business model will probably be subject to modification in the future, it does seem that consolidation is already beginning to take place in the charter industry, as evidenced by AirClub; and the VistaJet, Jet Aviation and Wheels Up Cooperation.

The future of seat sharing?
Over the years numerous ventures, such as Earth Jet and Green Jet in the US, have explored the possibility of sharing private jets to bring down the cost per seat and at the same time increase capacity utilization. Three years ago, Tennessee-based, Social Flights attempted to use Facebook to facilitate a sharing arrangement, but this experiment came to an end in 2013. The arrival of BlackJet, brainchild of UBER co-founder Garret Camp, in February 2013 seemed to be the start of a new phase in terms of both technology and financial resources. The company, however, only lasted a year before being grounded in December 2013.

Surf Air, a recently launched seat-sharing venture whose ambition is to sell flights on a smaller scale by operating fixed routes in California on Pilatus PC-12 aircraft, has approached the business model from another angle and is targeting a different audience than BlackJet. Operations for the subscription-based airline commenced in summer of 2013. It will be interesting to see how their take on seat sharing develops over time.
So what does this tell us about the future? First of all, the investments that are once again flowing into the industry are a great sign for the future. Secondly, one should definitely be wary of seat-sharing models attempting to create large-scale demand within a largely undefined audience. The Surf Air model seems promising and we will watch its development with interest. The BlackJet model however is one we do not believe will ever really work. To quote an anonymous former BlackJet employee “you can’t fly somebody for $3500 coast-to-coast and guarantee them a seat when it costs you $20,000 to fly the plane. Often, planes flew mostly empty. And if you had eight people on the flight, nobody was happy and it was crowded.”

A lot of the benefits of flying a private jet, like on demand service and complete privacy, are lost with the seat sharing model. When the price per seat is on par with, or higher than, a first class ticket and the business jet only serves a few fixed routes it simply cannot be competitive.
Autumn 2013: A new chapter begins?

The autumn of 2013 was an interesting period and the events that unfolded have the potential to reshape the industry. It began with Kenny Dichter, the founder of Marquis Jet, launching Wheels Up, a new private membership company aimed at “truly democratiz(ing) business aviation.” In only 5 months, the company managed to secure a significant amount of financing, launch its operations, secure 9 King Airs and over 100 members, and sign cooperation deals with both VistaJet and JetSuite. Wheels Up plans to take delivery of 10 additional King Airs in 2014, and forecasts project it will have over 10,000 members by 2020.14,15,16,17,18,19,20,21

During the same period Directional Aviation Capital (DAC), headed by Kenn Ricci, announced the purchase of the fractional company Flexjet from Bombardier, as discussed previously in the fractional section. DAC, owner of Flight Options, Sentient Jet§ and Nextant Aerospace, has, over the course of a few years, developed into one of the most important players in the industry.8,22
VistaJet announced, during the same period, that it would be moving into the biggest charter market in the world, the United States. Wheels Up will work as their exclusive sales agent and Jet Aviation Flight Services will operate their fleet in the region.\textsuperscript{19, 23, 24}

The fall also saw continued movement towards consolidation from other players. The European operator alliance AirClub continued working on their membership structure and launched their online booking platform in January of this year.\textsuperscript{25} XOJET and Travel Management Company (TMC) announced an alliance agreement in which XOJET would sell charter on seven of TMC’s Hawker 800XPs. With this deal in place XOJET will be able to offer a wider variety of aircraft to its clients while at the same time being able to focus on expanding its own fleet in the Super Midsize segment.\textsuperscript{10, 26}

In the final days of the year, Textron announced that it would be purchasing Beechcraft for $1.4 billion. The deal, which is not set to close until mid-2014, is extremely rational from a Textron perspective and yet another sign of industry consolidation. \textsuperscript{27, 28}

We believe this consolidation trend will continue into 2014 as the industry grows increasingly aware of the benefits inherent to economies of scale. Whether consolidation will succeed, in an industry where economics are skewed by high levels of owner-managed aircraft and tax concessions, is uncertain. However, this process is underway and will likely force many companies to review their business models to keep up with the major industry alliances.
The Dragon of the East

As the sky turned darker in the West during 2012 and early 2013 there was still hope in the industry that Asia, particularly China, would be our savior and make sure the industry would keep growing at the pace to which we’d become accustomed.

A lot of interesting developments in the region occurred during 2013. NetJets continued working on its Chinese joint venture, which is set for approval during Q1 2014. This will not take the form of a fractional company, but will instead be a management company offering charter flights. DeerJet, China’s largest management company, went the other way and started selling fractional shares on a G450 and a G550. Minsheng Financial Leasing, Asia’s biggest leasing firm, managed to float under
the radar. Then, to everyone’s surprise, they launched a management company at ABACE. They have a bold vision for the future, aiming at a fleet of over 400 aircraft in five years’ time and are clearly gunning for the position of China’s largest charter management company.31

Despite these ventures, the Chinese economy had already begun to slow during early 2013, and industry rumors at the time told of aircraft manufacturers having difficulties converting firm orders to actual deliveries. Here it once again became apparent that 2013 might turn out to be the year we got a glimpse of our future reality. In July, Asian Sky group released their half-year report stating that fleet growth in the region had slowed. The report attributed much of the slowdown to the cooling economy and government austerity measures. Some of the slowing, however, was also attributed to natural market maturation. According to the report, Chinese buyers have become more seasoned, taking added time with their purchasing, making more educated decisions and gaining a new appreciation for the value of pre-owned jets.32

Asia will continue developing into an increasingly important market with China leading the way. However, while growth in the region has been spectacular, the market slowdown of 2013 awakened us to the fact that Asia is still a small player from a global perspective. That said it has an important strategic position in the market.
One could say 2013 started just like all the other years since 2008, but ended up turning a new page for the industry. Flight activity numbers stabilized in both the US and Europe. Inventory in the secondary market started decreasing and prices finally stabilized. The fractional market consolidated and the charter market followed suit. New ventures started popping up and the first sighs of relief could be heard from professionals across the industry. It seemed that the downturn was finally over, but what does this mean for the future?

In Conclusion:
What does this tell us about 2014 and beyond?
Here is our take on what the events of 2013 mean for the years to come.

**Conclusion 1 – Welcome to our new reality**
While a few healthy souls have already forgotten about the golden days, many still steadfastly compare today’s market to that of 2007. It is our belief that the bullish days of 2007 won’t be back for quite a while. Instead, we as an industry must adjust our mindset to the market we’re in right now, with growth rates of 1 to 2%, as it will be with us for the next few years. This is our new reality and this is foundation from which to build our forecasts.

**Conclusion 2 – Consolidation is happening**
The signs of consolidation have been obvious for a while, but in 2013 what was previously only an indication has now become a trend. As is often the case in this industry, the fractional operators took the lead, but others have now begun to follow suit bringing the industry together in new and innovative ways. Consolidation was bound to happen in our industry, as it has in most every other, so now it’s time for us, as an industry, to take a look at how a new, consolidated charter market will affect our business models.

**Conclusion 3 – Belief in the industry is back**
During 2013 a steady influx of innovation and money started flowing back into business aviation. VistaJet, Wheels Up and Directional Aviation Capital all came to the forefront by reinvesting in the industry with new business ventures and ideas. There were also signs that venture capitalists were flocking back to the industry as Jefferies & Company sourced capital to the Wheels Up venture and AFC provided financing to IALT SA, a new leasing company founded by Vista Jet’s Thomas Flohr. Seeing capital and innovation flowing back into our industry is a sign of health, and we believe we will see more of this in the future.
Sources


14. Alasdair Whyte, “Wheels Up is more than a start-up, it is a movement,” Corporate Jet Investor (Blog), November 29, 2013, http://www.corporatejetinvestor.com/articles/wheels-up-is-more-than-a-start-up-it-is-a-movement-234/


Avinode Business Intelligence

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Avinode provides up-to-the-minute market data and trend reports for the business aviation community through Avinode Business Intelligence.

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