

# EETCs undermined by lack of repossession threat

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The Covid-19 crisis has undermined the Enhanced Equipment Trust Certificates (EETC) market by removing the threat of repossession, according to panellists on an *Airfinance Journal* webinar.

Speaking on the 'What are the capital markets trying to tell us?' webinar on 1 July, Mark Streeter, head of transportation and real estate credit research at J.P Morgan, says that LATAM's rejection of 19 aircraft under an EETC via its Chapter 11 proceedings, illustrates that the threat of repossession had diminished.

"It sounds like they are not even trying to play chicken, they are literally, basically telling the EETC holders 'you can't get those aircraft fast enough at this point in time'," he says.

Streeter says that EETC lenders would find it challenging to gather the resources to repossess aircraft, while the lack of global demand would make it difficult to place the assets elsewhere. As such, "all of the leverage right now is in the case of the debtor", he believes.

"The entire EETC market is based on having a structure in place that allows for creditors to have that credible threat of repossession in order to make sure there is a level playing field. Well, right now the field is not level," he notes.

The decision by LATAM to reject the aircraft was made despite them including Airbus A321s, 787-9s and A350s, which Streeter describes as attractive aircraft types.

Bryson Monteleone, senior advisor at PwC, says that a "paradigm shift" is occurring, whereby the EETC structure, which was previously considered "sacrosanct" has been reversed to become "unstructured", allowing assets to be "cherry picked".

Andy Mansell, a partner at Split Rock Aviation, suggests one option in the lessor's tool box, when presented by the risk of rejected Boeing 787 aircraft for example, would be to try to convince existing 777 operators with a short stub life remaining on the aircraft to swap them for the 787s.

Streeter says that prior thinking in the EETC market was that "if you have low coupons and you have young aircraft, then these deals are effectively bulletproof because they are cross-collateralising, cross-defaulting".

But he adds: "The problem is during a pandemic you have to throw that out of the window. If you have a deal where the bottom tranche is at 105% loan to value in bankruptcy, that deal doesn't get affirmed, everything gets rejected because there is no credible threat of repossession," he says.

Streeter believes that one flaw of the EETC market is that too little attention is paid to airline credit metrics and too much is paid to aircraft values, due to the "laziness" of underwriters.

He gives the example of Norwegian, where he says the business model of the airline was overlooked in favour of the versatility of the 737-800s in its fleet.

"A EETC is not about the aircraft per se...but what dictates EETC trading and performance is the underlying airline issuer," he says.

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