

Jolco transactions set for bright 2024 – SMFL

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The market for Japanese operating lease (Jol) and Japanese operating lease with call option (Jolco) aircraft financings is back, with the second half of last fiscal year, to 31 March 2024, producing especially good results.

Granted, the appetite for big ticket widebody financings remains moderate compared with before the pandemic, but overall volumes and confidence have returned among Japanese investors, with many targeting smaller or older assets to lower their corporate tax bills.

“The year 2023 was not a bad year. We got a good number of Jol transactions, even though the first half was a little bit challenging as many Jol investors were wondering if that was the right timing for making investments because of the weak Japanese yen against the US dollar,” Sumitomo Mitsui Finance and Leasing's (SMFL) managing executive officer and head of the transportation business unit, Shinichiro Watanabe, tells *Airfinance Journal*.

“We are now at approximately 150 yen for one US dollar, up from as low as 110 yen in exchange for one US dollar back in 2019, and I think we will stay around the 150 mark for quite some time, that is the expectation. And our investors have slowly come to accept that, so especially in the second half they were ready to provide investments again because they needed...tax solutions,” Watanabe says.

The SMFL executive notes similar stories from his competitors.

“Even in this exchange rate environment, from a tax savings perspective, aircraft investments still make sense for Japanese investors to lower their corporate tax bills,” Watanabe tells AFJ.

One trend that emerged in 2023 amid the strong US dollar was that Jol arrangers started doing more deals for smaller ticket items, like engines or used aircraft, because they were cheaper.

Watanabe highlights, however, that not all engine models are currently placeable.

“For a certain period now, we have suspended Pratt & Whitney GTF sales amid all their problems, so we have seen mostly CFM56 and Leap transactions, but also deals for IAE engines,” the financier says..

Japanese investors are also cautious about Boeing aircraft, Watanabe confirms.

“There are challenges with placing Boeing aircraft with Japanese investors, but we still see deals for 787 and 737 Max aircraft, although under a little bit tighter conditions, and the 737-800 remains popular. Generally speaking, however, the market prefers Airbus aircraft,” he tells AFJ.

Getting Japanese investor financing for a new widebody can prove difficult, especially in the current exchange rate environment.

“If it is a new widebody with a large price tag it is of course not easy to place. The buyers, the investors, are quite limited, like big ship owners, and also there were a few negative experiences during Covid, so investors are now ever more cautious, and this impacts on new widebody placements. Having said that, if the airline behind the aircraft is an excellent credit like British Airways or Cathay Pacific, then we still managed to create enough interest and get the investments required,” he says.

“However, most of the transactions we saw in the market last year were for much cheaper assets, including engines and used, quite old indeed wide- and narrowbodies, which under Japanese tax law means they can enjoy greater depreciation,” he explains.

As it transacted a wide array of assets in the Jol space, for Jolcos SMFL focuses mainly on new-technology aircraft, and in the second half the Tokyo-based firm closed mostly A350, A321neo, 787 and 737 Max financings.

Airfinance Journal's Fleet Tracker shows that the SMBC company closed on A321neo Jolco financings with Cathay Pacific Airways and British

Airways in the six months to 31 March, as well as A350-900 and A350-1000 Jolco financings for the same two carriers. In the Americas, Japanese investors financed another 737 Max 9 in a Jolco structure with Copa Airlines as operator.

Going forward, SMFL and its counterparties are looking at A220 investment opportunities, but the financial institution and its competitors are finding themselves in a fiercely competitive market.

“Regarding the A220, investors are showing good appetite, we are all looking at this asset. One of our competitors has been very active in arranging A220 Jol transactions, quite often undercutting and coming in with extremely aggressive pricing,” Watanabe tells AFJ.

Panellists at an AFJ 2021 conference had predicted that the market for Jol and Jolco financings could take up to five years to recover to pre-Covid levels as investors sought less volatile asset classes for their tax solutions.

Certain investors, in particular, were shocked to see rent deferral requests from airlines, and in certain cases and jurisdictions, particularly Southeast Asia, lessors felt the strain.

“Some airlines are desperate to come into the Jolco market because their cost of funding has been increasing. Of course, the established carriers continue to enjoy a low cost of debt, but the price of debt has been increasing a lot quicker for less stable operators, the Tier 2 airlines, so they are a lot more aggressive trying to gain acceptance in this market to lower their financing cost,” Watanabe tells AFJ.

“But the question is if the arrangers are really willing to risk bringing them in and introducing them to the investor market. It is my understanding, however, that we will see some new names this year with good balance sheets, including from the Latin America market,” the SMFL aircraft financier says.

SMFL works in conjunction with SMBC Aviation Capital, the second-largest aircraft operating lease company globally, with an owned, managed and committed fleet of over 900 aircraft.

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