

COVID-19: CATALYST FOR A BUSINESS JET REINVENTION, OR TRIGGER FOR ANOTHER DECADE OF MISERY?

The AlixPartners A&D Minute

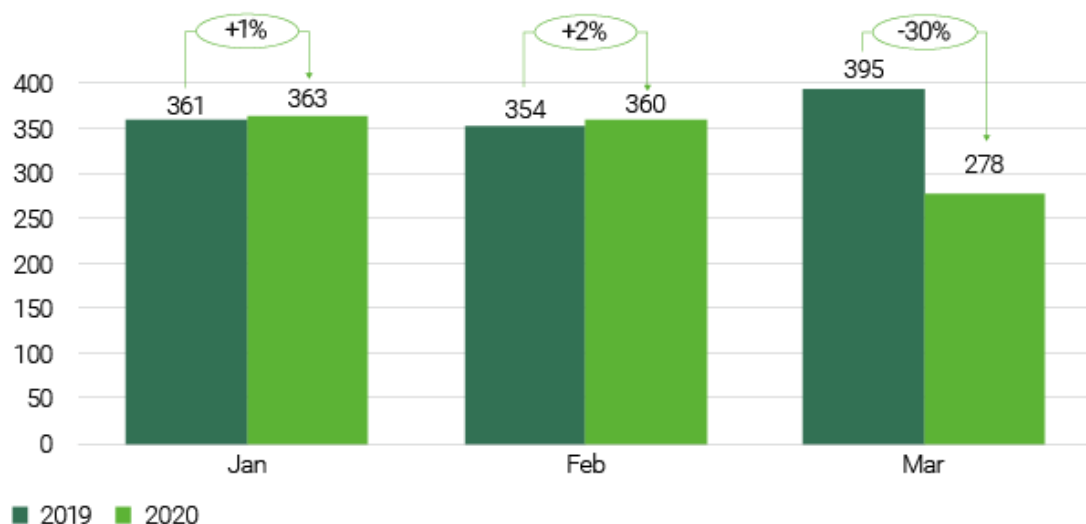
COVID-19 has caused immense global health and economic disruption. There are several sustained and widespread impacts of the crisis. One that is expected to last involves fundamental changes to how consumers travel. Both business and personal travel volumes are still at drastically reduced levels around the globe. While making predictions around timing is foolish, it is unlikely that commercial air travel will go back to pre-crisis levels anytime soon.

Could an unexpected beneficiary of changing consumer behaviors be the business jet industry? The trend of reduced discretionary travel to minimize potential exposure to the coronavirus is likely to continue for the foreseeable future. This may be an opportunity for business aviation to expand its value proposition beyond its traditional clientele.

Business jet sales have been stagnant over the last few years; having still not recovered to pre-2008 levels. This is because of their prohibitively high operating costs versus commercial flights, plus the public perception of business jets only catering to the excesses of the uber-wealthy.

In terms of utilization, the latest Federal Aviation Authority (FAA) figures from March indicate a 30% drop in US business jet operations (Figure 1). This decline was largely a result of COVID-19 halting virtually all discretionary travel. Early data point to a more pronounced drop continuing into April. According to one report, US business jet operations were **down 75%** year-on-year in the 30 days ending April 15.

FIGURE 1: MONTHLY GLOBAL BUSINESS JET OPERATIONS

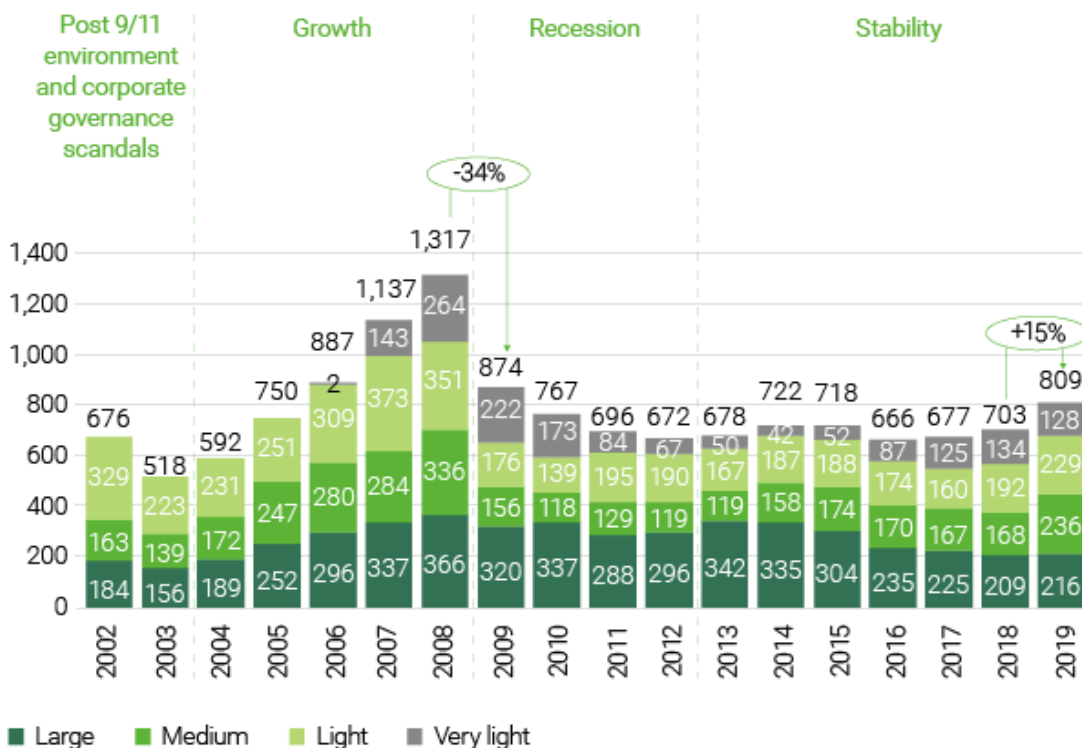


Note: One operation = one takeoff/landing. Figures are in thousands
Source: Federal Aviation Authority; AlixPartners analysis

CURRENT STATE OF THE MARKET

Business jet deliveries maxed out at 1,317 units in 2008, right before the Great Recession. Since then, annual deliveries have been stagnant at around ~700 aircraft (Figure 2). In 2019, they broke through the 800 level, but only because of the introduction of new models such as Bombardier’s Global 7500 and 5500/6500, Textron’s Cessna Citation Longitude, and Embraer’s Praetor 500/600.

FIGURE 2: BUSINESS JET DELIVERIES BY SEGMENT BETWEEN 2002 AND 2019



Note: Segments by maximum take-off weight: large (> 40,000 lbs), medium (20,000 to 40,000 lbs), light (12,000 to 18,000 lbs), very light (< 10,000 lbs)
 Sources: General Aviation Manufacturers Association, public sources; AlixPartners analysis

Manufacturers have responded to stagnant sales by developing more luxurious and mission-capable top-of-the-line models. These are marketed to high net-worth individuals who are not put off by the high cost or the extravagant image of business jet travel. This strategy has been particularly successful for Bombardier and Gulfstream.

Meanwhile, unit sales and profit margins for small-to-medium business jets are flat. New entrants to the market – Cirrus, Pilatus, and Honda – could add further downward pressure to unit sales and margins.

While the 2019 metrics were a source of optimism, it now seems that the industry may be looking at another potential decade-long malaise.

- In the **short term**, the economic turmoil brought on by COVID-19 will suppress deliveries and operations.
- Strapped for cash, corporations and liquidators will likely put up company jets for sale. The resulting influx of lightly used business jets in the marketplace will act to suppress new deliveries in the **medium term**.

- Finally, in the **long term**, there are other threats to the industry, such as loss of talent, potentially greater FAA scrutiny on the certification process as a result of the 737MAX crisis, and slow growth in China, which has been an increasingly important market.

NAVIGATING THE CURRENT CRISIS

As the threat of the virus leads people to reconsider their comfort level with commercial air travel, business jet operators have an opportunity to expand their value proposition. To manage through the COVID-induced crisis, there are several important tactics that the business jet sector should consider over the next weeks and months:

- **Redefine “business-efficient” travel:** To break out of the flat delivery cycle, the industry must expand its customer base by appealing to those outside of the typical roster of high net-worth individuals and C-suites of large corporations. For example, many business leaders and executives have high travel requirements to meet with customers and suppliers, often in remote locations. These new customers may be willing to embrace higher travel costs in return for greater efficiency, flexibility, and control over their surroundings.
- **Adopt innovative business models:** Jet cards, all-you-can-fly plans, instant booking apps, and membership programs, such as those offered by Wheels Up, Magellan, and NetJets, are good enablers for further democratizing business aviation. But operators need to go farther to reduce the cost of business aviation and should borrow concepts from technology-enabled disruptors like Uber and Airbnb for greater asset utilization.
- **Rethink the fleet:** Corporations willing to adopt a business aviation strategy for its second-level executives should consider a mix that doesn't just rely on business jets and its associated costs. Large turboprops such as the Pilatus PC-12 and Textron's King Airs are viable lower-cost options, particularly for short hops, while allowing the same flexibility as business jets.
- **Close the cost gap:** For decades the sector has been plagued by prohibitively high total ownership costs of business jets, which is why it has not kept pace with the overall growth in commercial air travel. This is largely driven by the fact that there are too many lower-end models in the market, each driving significant overhead and development costs for manufacturers. In the high-volume Light and Medium categories, there are currently seven manufacturers offering close to 20 models. In a good year, all these models are competing for a share of 500-600 deliveries. This is not sustainable, particularly for legacy providers with high overhead costs, such as Textron and Bombardier. For a given model, potential cost levers are standardizing aircraft configurations to reduce ad hoc engineering and adopting principles of agile engineering for new programs.

Historically, business jet utilization and new jet deliveries have been correlated with US corporate profit growth, but this need not be the future scenario. Will the enhanced convenience, efficiency, and hygiene of private aviation help it to overcome the negative effects of the COVID crisis? And could this be the trigger for the potential consolidation of business jet manufacturers?

FOR A DEEPER DISCUSSION ABOUT THE CHALLENGES WITHIN THE BUSINESS JET SECTOR AND SOLUTIONS ASSOCIATED WITH THE COVID-19 CRISIS, CONTACT:

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