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Outlook 2023

Turning around a turbulent industry

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There is a positive outlook in the heavy maintenance space. © *Rusada*

An optimistic **outlook** despite looming industry headwinds

Several MROs are upbeat about the general outlook for 2023 but a lingering pandemic in China, labour shortages, geopolitical issues in Europe and a strong US dollar are all discussions that will proceed in the new year.

By Keith Mwanalushi

Following a global airline industry loss of nearly US$220 billion dollars since the start of the pandemic, a recent report by aviation analysts at *Cirium* shows that demand has been recovering, with global revenues up by 70% for the first six months of 2022, bringing the total to within 20% of 2019 levels.

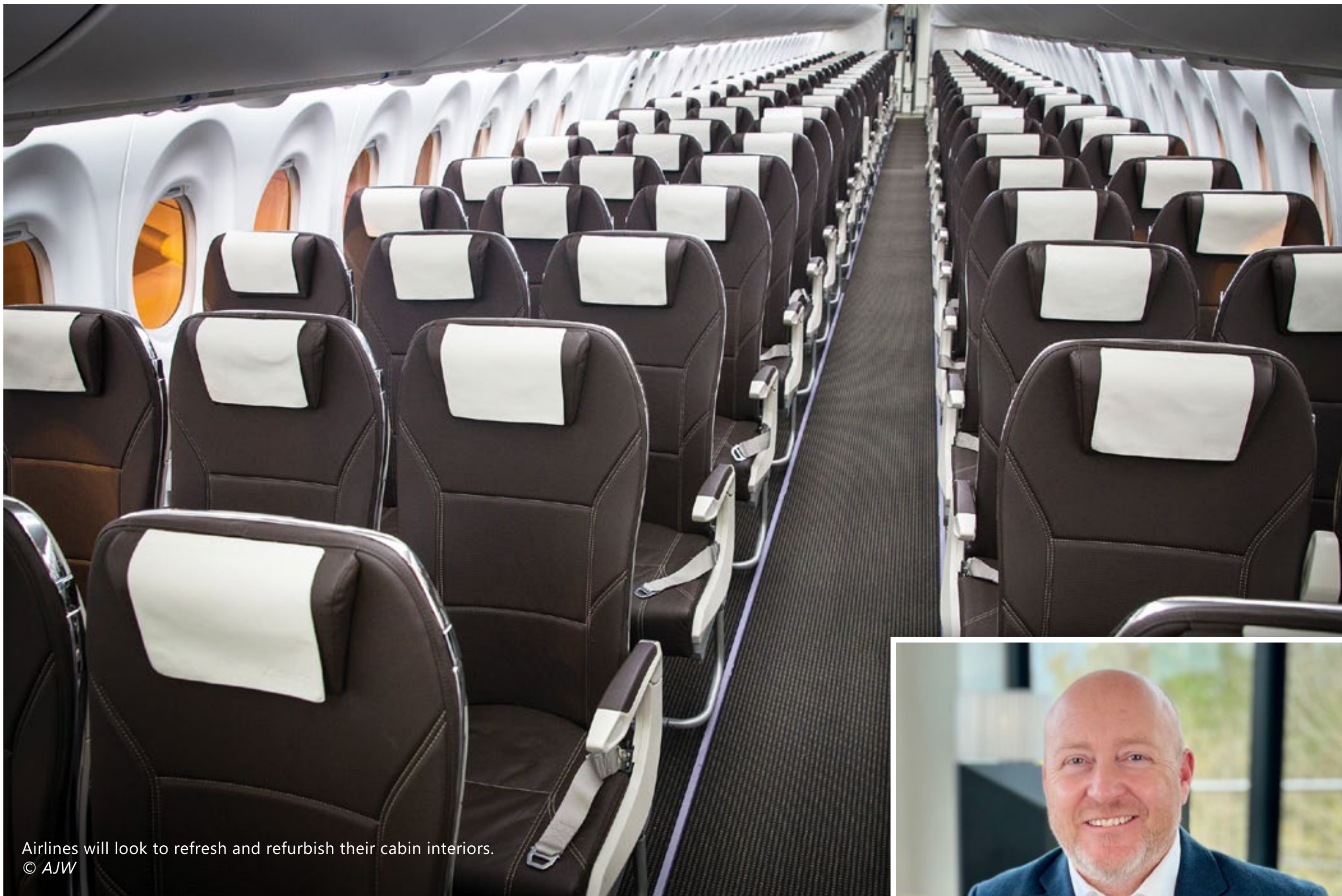
The US industry is on course to return to profitability in 2022, with Delta Air Lines leading the profitability trail. In the first half of 2022, the European passenger demand was running at around 95% of pre-pandemic levels however, losses appear to be worsening in China as the Covid pandemic resurges dampening growth in the recovery of the Asia-Pacific region.

There is a strong possibility that the industry may break even in the second half of 2022, led by US and European airline groups, experts have suggested.

Recent surveys indicate that MRO sales are up across the industry, led by sales in Europe and Asia, which are the strongest they have been over the past year and continue to strengthen. This bodes well for the AJW Group as they expand MRO capabilities establishing regional support hubs across Europe to meet the growing demands of operators in the region.

AJW Technique Europe has seen opportunities for growth beyond its centre for battery excellence in Slinfold, UK, and now has regional support hubs in AJW Remarketing, and AJW Türkiye, which provides full support services and solutions in the Eurasia region.

Clyde Buntrock, the Chief Executive at AJW Group tells *AviTrader MRO* he sees growing opportunities on the interiors side as airlines look to refresh



Airlines will look to refresh and refurbish their cabin interiors.
© *AJW*

and refurbish their cabin interiors, which have been neglected over the past few years. "With the renewed interest in travel, airlines are looking to upgrade existing fleets while still recovering from financial losses due to the pandemic. They are looking closely at their bottom line and using MRO services to entice customers with fresh-looking aircraft interiors. As such the remarketing and interior services provided by AJW Group, are in demand and this holds optimistic outcomes for us," he states.

AJW remains positive about the strength in commercial aircraft maintenance and the services it offers to its global customer base, even though labour shortages, supply chain fracture, spare part availability and lead times, and the ongoing Russia-Ukraine conflict are still affecting recovery. "In conjunction, the impending economic pressures and weakening consumer confidence are also influencing the deteriorating MRO aftermarket sector, but the aviation industry is steadily growing, and we maintain an optimistic outlook for the coming year," Buntrock indicates.

Lewis Prebble, President for Airlines and Fleets at StandardAero agrees that the general outlook for 2023 is healthy, despite the headwinds faced on a number of fronts. "We see that 2022 has continued to witness a recovery in terms of passenger traffic, aircraft orders and MRO demand, and while some industry observers are now projecting a one-year slip in the date for a full recovery to pre-Covid levels of traffic, there is no indication that a full recovery won't be attained."

Clyde Buntrock, Chief Executive at AJW Group

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>
> *Clyde Buntrock, AJW Group*

Technician shortages are most noticeably in North America.
© AAR

As Prebble places emphasis, the industry has again proven its resiliency by weathering the impact of Russia's invasion of Ukraine, the spike in Jet-A costs, and the pilot and technician shortages which have been seen most noticeably in North America. After several boom years, the air cargo industry is now also reporting a softening of demand, due to both the increased availability of belly hold capacity – a direct consequence in the continued recovery in long-haul passenger flight – and to a weakening economic outlook in some areas.

Lewis Prebble President - Airlines and Fleets at StandardAero

"Some passenger airlines have also tempered their traffic expectations for the 2022 to 2023 winter period in response to the current economic outlook, though most operators continue to predict a continued return to health in 2023," Prebble notes.

James Bennett, AerFin's Senior Vice President Sales mentions that much of the maintenance activity that was deferred during the height of the pandemic is now either taking place or is scheduled for 2023. "Our MRO customer base in particular has robust forecast activity to share and is now starting to purchase inventory in order to get themselves ready."

Bennett says this was not happening in volume through 2020, 2021 and the first half of 2022. Coupled with this is a much more cost-conscious operator base, keen to seek out options to reduce maintenance cost, one of the key drivers being material.

He indicates that companies like AerFin are well positioned to capitalise on these initiatives. Secondly, Bennett reminds that with increased demand, many of the MROs are struggling to ramp up labour and capacity. "As such, we are involved in discussions with some MROs as to how we can support activity through our quick

> **"As such, we would expect the CFM56-7B MRO market to remain robust, especially with the 737 NG family benefiting from a parallel surge in demand from cargo operators currently replacing their 737F classics."**
>
> *Lewis Prebble, StandardAero*

There is opportunity in the component overhaul sector.
© AFI KLM E&M Patrick Delapierre

turn engine maintenance capability we have in our Cardiff based facility. This is another key opportunity area for us," he states.

From a CFM56 engine MRO perspective, Aero Norway has recently observed that operators are pursuing the 'flying green time' strategy to a maximum i.e., flying down the core LLPs to zero.

James Bennett, AerFin's Senior Vice President Sales

From a design perspective and depending on where the engine is in operation, this is technically feasible. However, Ramon Peters, Global Sales and Marketing Director at Aero Norway explains that this policy has resulted in a shortage of used material on specific air foils and LLPs since few CFM56-5B and -7B have been dismantled for spare parts purposes and building the available pool of used serviceable material (USM).

"Currently USM is scarce and some new components and parts have long lead times. Also, we are seeing that some owners or operators prefer not to shop-visit their engine and seek an exchange engine to buy instead."

Peters further indicates that this market dynamic has two dimensions – "In the short term while there is a low market demand for heavy and core performance restoration shop visits, many operators are seeking lighter hospital repair visits. Over the longer term, the green time strategy will end and with little USM market availability, a higher demand and need for new material will be generated. This will result in lower shop visit costs in the short term, however higher cost will be inevitable for the longer run."

Meanwhile, there is lots of positive outlook in the heavy maintenance space," comments Scott Butler, Chief Commercial Officer at Ascent Aviation Services. He says they have seen demand pick up in 2022 for narrowbody maintenance, but now also a resurgence in widebody work. "There is also a lot of opportunity in the component overhaul such as landing gears where costly maintenance was deferred during the pandemic," he observes.

The repercussions of a strong dollar

Industry experts are suggesting the strength of the U.S dollar will create additional cost challenges for global aviation, for instance, engine and component cost per flight hour agreements sold in $USD will equal to higher maintenance costs in the coming year.

Obviously, for MROs based in the US, like Ascent Aviation, all their services are in USD but the higher rates will make it harder to compete with some international bases, and the maintenance will cost more for foreign carriers of which Butler is fully aware. "However, it is good when buying OEM components from Europe as our buying power is increased," he comments.

Ramon Peters, Global Sales & Marketing Director, Aero Norway

Higher US dollar rates will make it harder to compete with some international bases.
© *Ascent Aviation Services*

Elsewhere, the strength of US dollar is putting pressure on airlines by driving up the cost of everything from fuel to components, and aircraft themselves. "The knock-on effect of the strengthening dollar is that it has sent previously strong currencies such as the British pound and the Chinese yen plummeting this year," says Buntrock from AJW.

The pound has also been affected by the looming energy and economic crisis as well as ongoing geo-political unrest in the region.

As Buntrock mentions, aircraft purchase deals made before the pandemic, may have been pushed back due to lack of revenue, but the deals were signed, escalation clauses will have kicked in and the aircraft are currently more expensive than initially expected. "Airlines now need to deal with balancing flying schedules and pricing amidst reduced passenger confidence in the industry as it is. Cost per flight contracts signed a few years ago, will also have been escalated, again affecting countries who are balancing their revenue and expenditure currencies."

However, he says things look good for global companies who are making sales in dollars as their capital expenditure is paid in dollars as well, and this bodes well for their investors.

Buntrock adds: "Companies that receive payment in local currency but have capital expenditure expenses in dollars are the ones who will struggle in the current economic climate."

Foreign exchange rates will certainly be one of the considerations facing the industry in 2023, acknowledges Prebble from StandardAero. As a global MRO provider with locations on six continents, he feels the company is able to offer operators some relief from such foreign exchange impacts. Given the current strength of the U.S. Dollar, Prebble says the facilities outside of the country – including the CFM56/CF34 overhaul facility in Winnipeg and the PT6A/PW100 overhaul facility in Summerside – actually enjoy a competitive advantage when selling services to U.S.-based operators.

Steven Ades, AerFin's Chief Strategy Officer

StandardAero has already seen some operators temper their 2023 forecasts due to concerns over the economic outlook, reflecting the fragile state of the industry's recovery in some areas. As Prebble analysed, when combined with the supply chain issues which have been constraining the ramp-up in production of the 737 MAX and A320neo, this is likely to benefit the 737 NG family (and A320ceo) as some operators postpone capital investment in new platforms while others face delays in delivery of their aircraft.

"As such, we would expect the CFM56-7B MRO market to remain robust, especially with the 737 NG family benefiting from a parallel surge in demand from cargo operators currently replacing their 737F classics," Prebble states.

A strong USD undoubtedly adds an increased level of cost pressure for operators and owners of assets who generate income in other currencies.

AerFin sees continued strong demand for cost per flight hour agreements due to the visibility they give operators to better forecast their maintenance costs and put appropriate hedges in place to reduce currency risk.

Steven Ades, AerFin's Chief Strategy Officer indicates that on the whole, cost pressures experienced by operators, whether driven by currency, labour rates or the price of raw materials create an environment of cost consciousness which drives the need for operators to access AerFin's services which not only deliver demonstrable savings but also provide a range of options. Ades says USM can save in excess of 40% from buying new, and also allows partners to access piece part repair pricing through scale agreements. "Our MRO lite services extend the life of engines and defer costly engine overhauls to a time where cost pressures will hopefully be less pronounced," he highlights.

As Peters from Aero Norway sums up, European MROs that buy material in a strong USD market but have labour and general administrative costs in local currency, will likely see an effect on earnings as this cost dynamic is difficult to shift to customers.