AIRFINANCE JOURNAL

NAC: After the restructuring

Laura Mueller

27/11/2023

Nearly 18 months after exiting from a Chapter 11 restructuring process, Nordic Aviation Capital (NAC) has emerged fitter, leaner and with a gaze set firmly beyond the regional market.

The efficient and pacy management style of former GECAS leasing veteran Norm Liu is paying off.

Unlike an airline, it is slightly unusual for an operating lessor to restructure formally. However, like any turnaround endeavour, a successful outcome is never guaranteed.

The main lesson from NAC's extensive overhaul is that the process is relentless, especially following a decade of cheap debt and ultra-low interest rates.

Since taking the helm in 2021 and with creditor backing for the restructuring exit, Liu has slashed NAC's fleet count, debt position and payroll to pivot to a profitable lessor with a broader asset focus.

"We now refer to ourselves as NAC 2.0. The management, board, processes and strategy are totally changed from NAC 1.0," says Liu. "We are generating profits again and ahead of plan. Our 2023 budget is $25 million, and we've done $53 million as of the end of September. Also, our liquidity is over $550 million."

Investment rework

Founded in 1990 in Denmark, NAC managed a sprawling array of regional aircraft that peaked in value at about $7 billion a decade later.

It ranked as the world's largest regional aircraft lessor and, by aircraft count, the fourth-largest aircraft leasing entity with 468 owned, managed and committed assets, including ATR42/72, De Haviland Canada Dash 8, Bombardier-MHI CRJ900/1000, A220 and Embraer E1 aircraft.

But it was saddled with a swelling debt position and grappled with exposure to multiple distressed carriers, including Far Eastern Air Transport, Flybe and Garuda Indonesia.

The lessor's financial situation suffered a bruising during the Covid-19 pandemic, with 80% of its customers seeking payment relief. It was also over-concentrated in aircraft types like the Dash 8, CRJ and E1, some of which were effectively out of production.

As a result, NAC obtained approval to enter a scheme of arrangement from the Irish High Court in July 2020 after securing creditor approval for an interim debt restructuring programme.

But as the Covid crisis continued, the lessor posted a $2.4 billion loss for the 12-month period between July 2020 and June 2021. In December 2021, it finally filed for a much more extensive Chapter 11 filing with the US bankruptcy court.

"This was the biggest aircraft leasing company that's ever been restructured. It's one thing when you're a financier working on an airline restructuring, which I've done many times, but it's another when you are the company that's being restructured," says Liu, who joined the NAC board in 2019.

"It was an interesting learning process, but I'm not sure I would suggest it to others. Liquidation during Covid was not really a good option, so instead, folks decided to use the existing business scale and infrastructure to build something new."

Chapter 11 enabled NAC to sharply write down its debts and aircraft book values, while "right-sizing" the fleet and the orderbook.

A central part of the fleet strategy has been to exit Dash 8s and E1s and focus the regional fleet on ATRs and A220s instead.

NAC's pullback from the regional market has also signalled a fresh start for the lessor, which was launched by Danish billionaire and entrepreneur Martin Moller. In 2022, Moller sold the last of his shares in the lessor.

Still, NAC's retreat from regional assets continues to make headlines.

In September, *Airfinance Journal* exclusively revealed that the lessor would further exit its Embraer fleet, selling 50 E1 aircraft in a process led by Greenhill.

The portfolio has attracted 10 bids, with a final shortlist expected soon. Liu says NAC hopes to have purchase documents ready by year-end.

Sources tell *Airfinance Journal* that Azorra Aviation is the lead bidder for the assets, but Liu will not be drawn on the suggestion.

Breeze Airways, LOT Polish Airlines, Portugalia, Royal Air Maroc and SA Airlink are the five largest lessees, according to an offering document reviewed by *Airfinance Journal*. Three Embraer 195s with 2018 build years are leased to Tianjin Airlines, which is part of the Hainan Airlines Group, through 2030.

"We had 180 E1s at the peak and have a package out there because we are exiting the type; we have 80 E1s left and hope to be down to 30 after this process," says Liu. "We are also down to under 15 Q400s [Dash 8s] from 90. Our aim is to have the best in class regional and narrowbody aircraft, with a simplified fleet of ATRs, A220s, 737s and A320s."

Build back better

NAC is ahead of its fleet exit strategy. It aimed to sell 100 out-of-production aircraft for roughly $400 million over a three-year period. But 18 months into the process, NAC has sold $500 million worth of assets and contracted about 135 aircraft and engines.

Liu attributes the "successful" transition to the team of ex-GECAS executives that he assembled to lead the revamp, including Mike Jones, Ed Sheard, Colin Joyce and David Farrell.

"Having so much of the leadership and team come from the same system is a big plus in the midst of a crisis. The remaining NAC 1.0 team members also rose to the challenge. You can effectuate change quickly and effectively when the teams have a shared purpose. We cleared our aircraft on ground from to the low single digits and sharply reduced receivables to below $50 million," he says. "We further invested time and money in risk management, pricing, governance and compliance processes so we have a solid foundation that can be readily scaled."

The leadership reorganisation also allowed NAC to exit Chapter 11 "quickly" in roughly six months, he adds.

Nearly all the NAC leadership team is now from GECAS except Jennifer Creevey, who is the ex-DAE Capital chief financial officer and who recently joined in the same capacity, and Gareth Halpin, who is ex-Avolon and serves as treasurer.

In addition, other ex-GECAS employees have joined NAC and now, roughly a third of the new NAC team has previously worked at GECAS.

Capping off a period of larger fleet count, NAC's total staff has been reduced to 100 from 220 personnel, which is "in line" with a portfolio of 300 units, he says.

Klaus Heinemann, the former Aercap CEO, is chairman of the board and John Higgins, Avolon's ex-president and chief commercial officer, is a new board member.

Backed with proceeds from asset sales and better cash flows from fewer AOGs, Liu says NAC is focused on a "balanced approach" to debt reduction and growth capital while staying liquid.

Yet roughly 40-50% of NAC's asset sales proceeds must sweep to the reinstated debt of the former creditor group as part of its restructuring process.

"We also have repurchased about $100 million of debt via a formal tender this summer and open market purchases more recently. At around 90 cents, it was a good ROI," Liu adds.

NAC has been contracted or awarded "around $830 million of growth capex" from sale and leaseback deals and order slots. "Around 80% is new technology, so neo, Max, and ATRs, and originated directly from airlines. The remainder are NGs and Ceos purchased in the secondary market."

Higher, longer

While NAC has diversified its asset investments and has a better debt position, it still faces a tough environment. One of its biggest challenges is to compete with lessors that have access to cheaper funding costs.

“We are not owned by an Asian bank, nor are we investment grade rated. Fortunately, we have access to a competitive bank warehouse facility like some other non-IG players. We have to play things a little differently. We can do new tech with top-tier credits, but we must mix in lesser credits to get a bit more margin," he says.

"ATRs and NG/Ceos are also higher yielding, so they must be part of the mix as well. We’re also doing some engine leasing, cargo and part-outs/trading. Can you make a killing? No, but you can make a living with this blended, full life cycle approach."

Helping NAC is also its modest investment target of $600 million per year.

"It represents decent double-digit growth on over $3 billion of assets. If you had to do several billion of investing with warehouse funding, that's not doable using our pricing assumptions. But you can do $600 million with a blended approach and working our long-standing relationships – it pencils out."

For now, NAC's existing debt on its legacy fleet is "in good shape” for the next few years.

Liu says 85% of NAC’s debt position is fixed rate or hedged, while the blended cost of funds is about 5.4%.

"Our capital stack is around $2.4 billion with minimal covenants, and we don't have a significant amount due until mid-2026. A large portion, around $900 million, is fixed at 4.75%. We also bought a rate cap in June 2022 when SOFR was only 3.5% versus over 5% today."

NAC recently also boosted its warehouse facility for growth capital expenditure from $400 million to $750 million. Wells Fargo, Fifth Third, and Mizuho have joined the original lending group, including Deutsche Bank, RBC and **Citi.**

Next steps

To maintain its momentum, Liu must keep costs under control and maintain investment in high-margin deals. Just as important, Liu must set out where future growth lies.

For that, the shareholder base will need to evolve.

Will NAC add shareholders or new growth capital?

"If you look at our shareholder group, there are two buckets. One is former insurance company bondholders, who received equity and reinstated debt during the restructuring. Another group includes hedge funds that bought in below par and got debt and equity. Neither invested with a long-term horizon for aircraft leasing. I think it's inevitable that we have to transition our shareholder base to move onto the next level of growth," says Liu.

He maintains that NAC's fleet recycling “seed cash” of $500 million and operating cash flow are sufficient to fund investments for the next few years.

“But we are sort of selling our used furniture to buy new, and eventually, we will have sold all. It’s basically self-help. Fundamentally, we need a longer-term shareholder base to realise the tremendous growth potential of the NAC platform."

Asked if an advisor, or specifically Goldman Sachs as sources tell *Airfinance Journal*, has been formally engaged to explore strategic options, Liu replies with no comment.

However, with a 2026 refinancing looming, Liu admits the lessor "would probably explore something before then”.

The alternatives could be a complete sale, a merger, or a growth capital infusion.

Liu notes that any investor would likely need to be comfortable with lower returns than the 15%-plus required by private equity.

"I call it the 10% crowd, which is what this space is all about now. But in our case, you aren't just buying aircraft but a full-scale platform. I believe our team is as good as any top 10 lessor. We just need the right capital to be scaled 3-4 times on a permanent capital basis. Sidecars are also a possibility."

Possibly benefiting this move, Liu maintains that elevated inflation in aerospace is "stickier" and could enhance returns on real assets like aircraft.

However, there are secular trends to consider beyond the near-term supply chain issues and product-related delays. "Every engine, airframe

OEM and MRO is struggling to get labour, and every infra project on the planet is looking for the same materials, such as aluminium and titanium."

While the aviation market has returned to a pre-Covid demand cycle, he stresses that interest rates and inflation are at "pre-financial crisis" levels.

"We are back to the 1970s, unfortunately, in terms of hot wars and a reemerged cold war schism. We now also have climate and rapid technological shifts to contend with."

But Liu sees a silver lining. "If you have been around for as long as I have, you know you can manage through things."

