



ABS Deal of the Year: **JOL Air \$554m ABS for 15 Aircraft**

Borrower/Issuer: JOL-Air Limited

Structure: Asset-backed securitisation

Arranger/Servicer: Stratos

Amount: \$554 million

Collateral: 15 aircraft

Banks: Goldman Sachs acted as lead structuring agent and lead left bookrunner, Deutsche Bank Securities as joint structuring agent and joint lead bookrunner. Natixis Securities Americas acted as joint lead bookrunner and liquidity provider while Mizuho Securities USA and SMBC Nikko Securities Americas acted as joint bookrunners and arrangers

Lawyers (and roles): Milbank as issuer's law firm advising on the structuring, issuance and acted on behalf of the warehouse borrower. Clifford Chance advised the lenders on the warehouse facility and acted as ABS counsel. K&L Gates as acquisition and novation process adviser. Walkers as Cayman Island counsel, Nishimura & Asahi as Japanese counsel. Multiple local counsels supported the novation and ABS transition including Hogan Lovells, Stephenson Harwood, HFW, Blakes, Tay and Partners, Sycip, Dentons, Arias, Morris & James and DFPJH

Equity underwriter: JP Lease Products and Services

Advisers: KPMG advised on ABS due diligence accounting and tax advice. Phoenix American Financial Services (Ireland) as managing agent. Wilmington Trust as facility agent, security trustee, operating bank and trustee

Rating Agencies: KBRA, Standard & Poor's

Date closed: 29 May 2019

This year's asset-backed securities (ABS) Deal of the Year winner marks an innovative transaction: it was the first ABS to feature securitised debt with equity sourced from the Japanese operating lease (Jol) market.

Stratos issued JOL-Air 2019-1 in May 2019 and, up to that point, Jol equity had only ever been offered on single aircraft investments.

Equity investors are traditionally credit sensitive, asset conservative and very sophisticated. Arranging a cross-collateralised pool of aircraft equity sell-down into the Japanese aircraft had never been attempted prior to the JOL-Air issuance.

ABS lenders are also very conservative about such structures, and want to avoid Japanese bankruptcy remoteness risks. Consequently, this structure was designed to look like any normal ABS from a debt perspective.

The transaction marked the first aircraft securitisation issued by Stratos and the first time Jol investors were introduced to a cross-collateralised pool of aircraft.

"From a Jol equity perspective, the major benefit of JOL-Air is portfolio exposure – as opposed to investing in an individual asset that can be rejected on a standalone basis – which brings diversification and stability on the overall portfolio performance that covers for one aircraft, if rejected," says aircraft investment firm Stratos chief executive officer Gary Fitzgerald.

Stratos arranged the equity, acquisition and novation of the aircraft, the debt bridge funding, warehouse loan and ABS issuance, and will service the portfolio through to lease maturity. JP Lease sponsored and underwrote the equity and arranged the sell-down to a diversified pool of Japanese corporate clients. The lead structuring agent on the bridge and warehouse was Deutsche Bank and Goldman Sachs was joint structuring agent. The securitisation, led by Goldman Sachs and Deutsche Bank, featured A and B notes totalling \$530 million.

The ABS comprised a 4% \$456 million class A debt tranche, a 5% \$73.8 million class B debt tranche and \$20 million class C tranche. The debt portion was distributed to 40 lenders in the USA, mainly insurers and fund managers. Stratos and JP Lease retained the C notes which are non-rated, non-amortised and carries a nominal coupon of 7%. The Japanese equity placement amounting to about \$300 million, which is unique in the transaction, is provided by over 200 Japanese investors via the Jol structure.

Benefits of JOL-Air

In addition to the unique Jol structuring and the tax benefits for Japanese investors, the transaction included a number of innovative features, such as a 100% cash sweep at the bottom of the waterfall (for the benefit of the class A and class B notes) before the equity is paid. Jol investments are time sensitive because of the fiscal nature of the investment. As a result, Stratos needed to arrange the novation of all aircraft on the same day into the same Japanese structure. The rating agencies were obliged to hire outside counsel to advise on the structure as they had never been presented with such novel underlying economics.

Fitzgerald says the transaction was the most complex deal the firm had arranged. In an interview with *Airfinance Journal*, he recalls its genesis. According to him, JOL-Air was initiated in August 2018, when Stratos was challenged on the economical aspect of some Jol transactions. "Every single Jol transaction needs a separate loan for funding and this is not optimal," comments Fitzgerald.

"Jol investors focus on the credit and young assets but over time it becomes challenging to buy sufficient numbers of these prime assets without paying a substantial premium," he adds.

Context also helped to initiate the JOL-Air structure, because, in August 2018, Japan was about to change tax laws. "We proposed a portfolio of aircraft to be financed in the capital markets along with the \$300 million equity commitment," he says. One of the big hurdles to overcome was convincing Japanese investors to invest in multi-credits. "Japanese investors had become comfortable with multi-asset aircraft investments, but never multi-credits," he says. The 15 securitised aircraft were acquired from two separate sellers, GECAS and Standard Chartered, and have leases attached to Air Canada, Scoot, Qatar Airways, Flydubai, Gulf Air, AirAsia, Malindo, Philippine Airlines, TACA, Brussels Airlines and Batik Air. Fitzgerald says the \$300 million equity commitment limited the portfolio to 15 aircraft, which is the lowest number of aircraft ever securitised via ABS.

The composition of the portfolio consists of 13 narrowbody aircraft (63.4% by value) and two widebody aircraft (36.6% by value).

Fitzgerald says widebodies are difficult to include in ABS transactions and so Stratos opted for new-technology aircraft: the 787-9 and A350-900 models.

Another pair of aircraft, two A320neo units, are also new-technology aircraft.

"We wanted to make sure that more than 50%, in value terms, were new-technology aircraft. Environmental, social, and governance is becoming a hot topic, especially for Japanese investors," he says.

The JOL-Air transaction has seen little secondary trading since issuance, with an estimated \$40 million of transactions on both tranches. By the time of the Covid-19 peak, a small number of A notes were trading at 96 cents on the dollar.

"There is uncertainty at the moment in the aviation industry but JOL-Air has performed extremely well. We are ahead of schedule in terms of amortisation of the A and B tranches," says Fitzgerald. Could the transaction be replicated? "JOL-Air 2 Limited will be done, but we are waiting for market conditions to return," says Fitzgerald.

He adds: "The transaction received a phenomenal reception and today we are not short of debt for another transaction. There is also interest on the equity side, but the credit situation needs to improve before we can venture back into JOL-Air 2. In the meantime, we're keeping busy working for various airlines, investors and lenders to manage their way through this crisis and mitigate losses insofar as possible. ▲"