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Orient aviation

MALAYSIA AIRLINE'S MARKETING MAN

The first marketing campaign in recent memory is bringing back passengers to a re-invented Malaysia Airlines says the carrier's boss, Peter Bellew

Orient aviation 23 YEARS

IATA attracts two Asian budget carriers to its membership

Delta Air Lines and Korean Air kiss and make up

Destructive capacity war threatens full service Firefly

Industry insight: Ascendancy of Chinese lessors in global aviation

Orient aviation 23 YEARS

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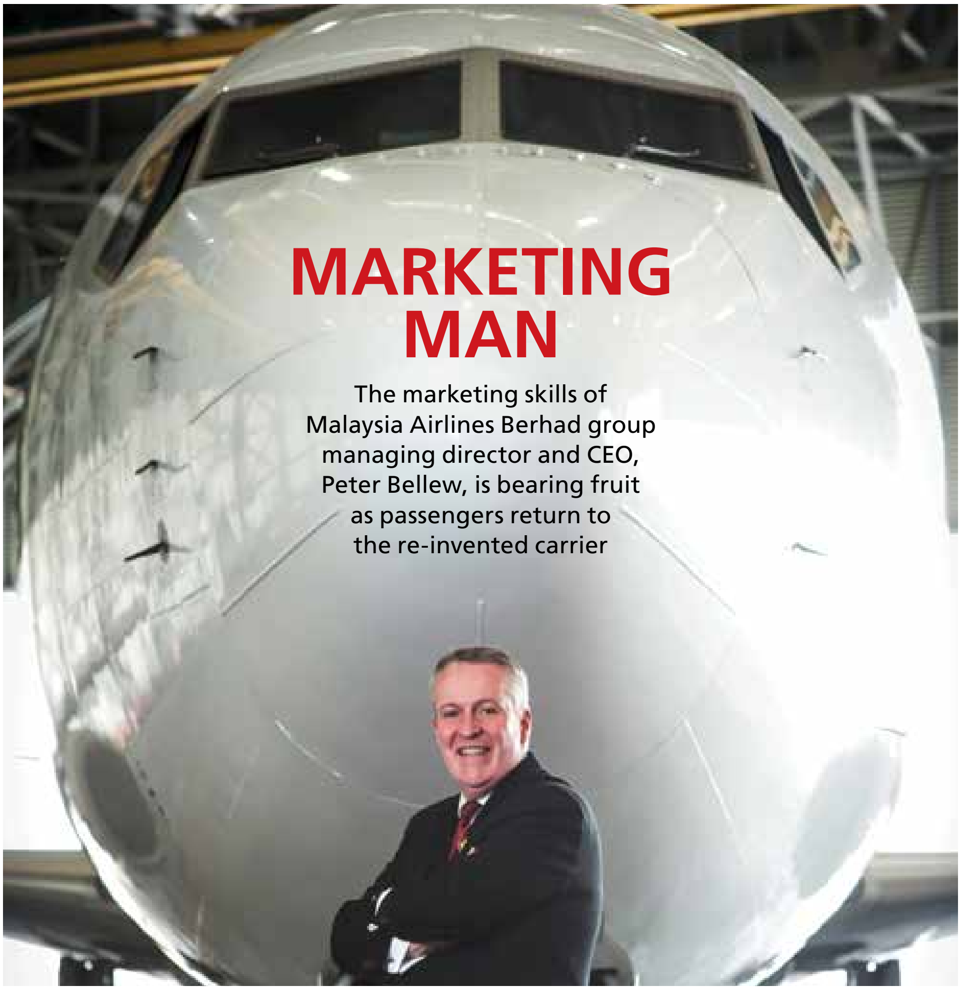

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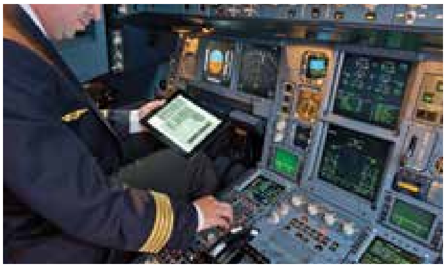

INDUSTRY INSIGHT SPECIAL REPORT

Airlines filling gap in safety oversight

Safety is every airline's absolute priority. And in this region, the news is good. There were no fatal commercial jet accidents last year and none so far this year. But the industry must still deal with the fact that some Asia-Pacific regulators are not meeting the required standards of oversight.

An example is the disappointing fact that more than half of the nations of the Asia-Pacific have not reached the International Civil Aviation Organization's (ICAO) target of 60% for effective implementation of safety oversight.

But even where there is weak or non-existent regulation and regulatory oversight, the industry delivers an exemplary safety record, said the Association of Asia-Pacific Airlines director general, Andrew Herdman, in Tokyo last month. "So that points to the fact that regulatory oversight is essential, but not having it is not a show stopper," he said.

Herdman agreed bad apples had to be weeded out and regulatory rules followed. His point was that the industry is safe because airlines themselves place a great deal of focus on safety.

Many carriers in the region have seconded dozens of their own personnel to some of Asia's regulators because these emerging countries cannot attract, pay and retain qualified pilot/inspectors to staff their regulatory bodies.

But the fact remains that in a region with huge momentum in air traffic growth, regulators have to rethink the way they monitor and regulate air safety. They must strive to get past that 60% target put in place by ICAO. In a region of our wealth, this should not be happening. ■

TOM BALLANTYNE
Chief Correspondent
Orient Aviation Media Group

COMING UP IN NOVEMBER

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IATA attracts two Asian low-cost carriers

Traditionally, cost-conscious budget carriers have shied away from joining the International Air Transport Association. But now, two of Asia's fastest growing budget airline groups have become members of the global airline organization.

Last month, **Thai Lion Air (TLA)** and Vietnamese LCC, **VietJet**, joined the global industry club, decisions that would support their growth, the carriers said.

TLA managing director, **Captain Darsito Hendro**, said IATA membership, the first for a Thai-registered LCC, will be instrumental in the airline's expansion. "Thai Lion is expanding internationally, already covering Singapore, Indonesia and Myanmar, with Vietnam next and India and Australia on our radar screen," he said.

He said the multiple membership benefits of IATA allowed it to expand through IATA-based travel agents, via global distribution systems and bank settlement plans. The fees for both systems are lower for IATA member airlines.

IATA membership also will motivate Thai Lion to step up to best business practices in the industry and develop interline and code-share opportunities to bring more tourists to Thailand. Thai Lion hoped it would attract business from big international companies as most of them appoint IATA member airlines as their official travel carriers.

TLA and VietJet were two of five members officially welcomed into IATA last month. Their fellow new IATA members are China's **Loong Air**, **Lao Airlines** and **Mauritania Airlines International**.

Loong Air, which is based at Xiaoshan International Airport in Hangzhou, Zhejiang province, was formerly CDI Cargo Airlines. It launched domestic passenger flights in 2013 and commenced international service, to Vietnam, earlier this year. It flies a fleet of 15 A320s and three B737 freighters.

Lao Air operates four A320s and eight ATR 72-500 and -600 turboprops. IATA offers membership to airlines operating scheduled and non-scheduled air services that are on the registry of the association's operational safety audit list, or IOSA. Only airlines that have passed the IOSA audit can join IATA. "We have always welcomed all airline business models as members, including low-cost carriers," said an IATA spokesman.

Airlines pay a non-refundable application fee of $15,000 for IATA membership and another $15,000 when the application is accepted. Annual membership dues begin at $14,450 (reviewed annually). Big airlines that perform more than five million International Revenue Tonne Kilometres (RTKMs) per year pay a combination of the fixed fee and an additional variable charge. The variable dues are calculated on the basis of the carrier's RTKMs for the previous two years.

IATA was founded with 57 airlines in 1945 and now has 265 members operating in 117 countries worldwide. Its airline members carry 83% of the world's air traffic. ■

Delta's smooth talking Ed woos estranged Korean Air

They were founding members of the **SkyTeam** alliance in 2000, but relations between **Korean Air (KAL)** and **Delta Air Lines** have been frosty, to say the least. The reason? Some years ago, KAL shunned an approach from its U.S. partner to forge a deeper joint venture agreement across the Pacific.

The proposed deal would have gone far beyond code-sharing and involved gaining anti-trust immunity so the carriers could share revenue and work together on pricing for flights. It was an arrangement Delta was extremely keen to consummate. Its major trans-Pacific rivals already had joint-ventures in North Asia: United Airlines with Japan's All Nippon Airways and American Airlines with Japan Airlines.

While both carriers publicly played down a rift, Delta made KAL a weaker partner than other SkyTeam members such as **Air France** and **KLM**. It became harder for Delta customers to earn frequent flyer miles on KAL and each airline made it more difficult to sell flights on the other carrier. The U.S. carrier also appeared to change its strategy when it purchased a 3.55% stake in **China Eastern Airlines** and talked about connecting passengers through a Shanghai hub instead of Seoul.

But now it appears there is a thaw in relations following the announcement last month that KAL and Delta were increasing the routes on which they code-share from 32 to 147. It represented a significant deepening of a relationship that apparently has been developed by Delta's new chief executive, Ed Bastian. As well as more shared flights, Delta is launching a non-stop service from its Atlanta headquarters to Seoul.

While Delta is still talking about its partnership with Shanghai-based China Eastern, it is understood it wanted to strengthen its relationship with KAL so it could offer its passengers easier access to secondary cities within Asia by flying through Seoul and avoiding China's notorious air traffic delays.

Under the new arrangements, KAL can sell tickets on 115 of Delta's routes within the U.S. and Canada and Delta can sell tickets directly for 32 KAL destinations beyond Seoul, including Taipei, Osaka, Singapore, Nagoya and Okinawa. ■

Garuda moves closer to U.S. flights in 2017

Garuda Indonesia has begun a feasibility study of the U.S. market with the intention of launching flights across the Pacific, following the U.S.'s **Federal Aviation Administration (FAA)** restoration of category one safety status to Indonesian carriers last August.

In a statement issued in Jakarta, Garuda Indonesia vice president corporate communications, Benny S. Butarbutar, said there was a potential annual market of 400,000 passengers on routes to Los Angeles and New York from Indonesia, with the B777-300ER flights to operate via Japan.

Since 2014, Garuda has been flying to Los Angeles and Seattle via Haneda Tokyo by selling tickets through its code share and **SkyTeam** alliance partner, **Delta Air Lines**.

"The plan to fly a U.S. route is a business expansion decision to strengthen Garuda Indonesia's position as a global aviation player. We are taking all actions necessary to realize the plan," said Butarbutar. The new routes would be served through Tokyo's Narita airport, he said. ■

Airline profits may slow says IATA

The airline industry's record forecast profit of US$39.4 billion for 2016, "a very good year", may slow in the next 12 months, the **International Air Transport Association** cautioned in Singapore last month.

Speaking at the association's World Financial Symposium, the new **IATA director general and CEO, Alexandre de Juniac**, who took over from Tony Tyler on September 1, said the feedback from airlines was that the high level picture was satisfactory, but there was strong downward pressure on unit revenues.

"There is very strong pressure everywhere and it is not an easy situation. It is a business that has to deal with very big macro-economics," he said. Factors effecting future airline profits included the impact of foreign exchange rates, oil price fluctuations and Britain's planned exit (Brexit) from the European Union, de Juniac said.

At the Singapore symposium, **IATA's chief economist, Brian Pearce**, said this year's record profit was largely due to the North American carriers' results and that this trend would likely continue. Elsewhere in the world, positive results were less evenly spread, he said.

Pearce said the present industry cycle is pointing to a peaking in profits and that passenger growth will be slower in 2017, especially as demand has been moderating since mid-year.

One off circumstances that have boosted profits included a sharp drop in fuel prices, which produced cheaper fares, and an increase in budget carriers, especially in the Asia-Pacific, that accelerated passenger growth.

Air freight has continued in the doldrums, said Pearce, and has never recovered from the global financial crisis of 2008-2009. "This is mostly because there has been little growth in world trade [for almost a decade], but also because of fierce competition from the shipping industry, which is in turbulence. Talk of trade protectionism by some governments is also a concern," the economist said.

IATA said the global economy remains in fragile condition and that could result in reduced passenger demand and lead to a lower growth environment in the immediate future. ■

Saved again: Merpati's second coming?

Indonesia's State Enterprises Ministry has said cash-strapped and state-owned **Merpati Nusantara Airlines**, which ceased flying in 2014, will re-start services next year after restructuring.

"We hope it can resume operations in 2017 if, in the remaining one year, the airline receives a privatization permit from the finance minister and investors are ready to invest in it," said the ministry's deputy for business restructuring and development, **Aloysius K. Ro**. Some 1,500 Merpati employees lost their jobs when the carrier collapsed.

The government has injected $30 million into the airline as part of the restructuring. The operational and financial re-engineering of Merpati includes encouraging operational cooperation between **Garuda Maintenance Facility (GMF)** and **Merpati Maintenance Facility (MMF)**. "This is a big step. GMF will manage MMF to increase the capacity of domestic aircraft maintenance business," said Ro.

In the first half of next year, Merpati will go to the market to seek investors for its planned return to the skies. Ro conceded that "it is not easy to find investors to engage in flight business even under normal circumstances". ■

Q

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PANDORA'S BOX OF AIR SAFETY REGULATION

Air safety's record has never been better. But in Asia systemic problems persist as too few government dollars are chasing too few qualified pilot/inspectors.

Tom Ballantyne reports from Tokyo

Lack of professional oversight. Staff shortages. European black bans. Federal Aviation Administration downgrades. International Civil Aviation Organization red flags. The headlines have been damning about some of Asia's aviation regulators.

But when 160 plus safety professionals from 37 airlines, as well as industry regulators, airframe manufacturers and service providers, gathered in Tokyo last month for a regional air safety conference, they heard none of that.

"What is the problem?" asked Andrew Herdman, director general of the Association of Asia Pacific Airlines (AAPA). "What is extraordinary is that even with weak or non-existent regulation and regulatory oversight in some locations or some States [in the Asia-Pacific] the industry delivers this exemplary safety record. This pointed to the fact that regulatory oversight is essential, but being without it is not a show-stopper."

Herdman was part of a panel that discussed "Balancing Growth and Oversight" at the AAPA's Asia-Pacific Aviation Safety Seminar (APASS). It is a pivotal topic in a region with high projected passenger growth, increasing airport and air traffic congestion and chronic shortages of pilots, engineers, technicians and safety and regulatory inspectors.

In Boeing's most recent forecast, the manufacturer said there would be global demand for 39,620 planes, worth $5.9 trillion, in the next 20 years, with 15,130 of the aircraft destined for Asia-Pacific airlines. As well, many of the planes delivered elsewhere in the world would be earmarked for services into the region.

At APASS, Airbus senior vice president and chief product safety officer, Yannick Malinge, said the European-headquartered manufacturer had 9,000 planes completing 25,000 flights per day, or about 10 million per year, across the world.

"By 2019, Boeing and Airbus, as well as Embraer and Bombardier, will be putting more than 2,000 new jets into service every year. This means about 20,000 pilots, mechanics and cabin crew a year [will be needed]." Malinge said despite all this flying the accident rate is remarkable, at only one per 10 million departures.

"All of us have to be afraid of one risk: complacency. It's not going to happen to me. This is wrong, of course. One of the challenges in Asia is the growing fleet."

Herdman agreed and emphasized he was not suggesting regulators were superfluous, but said the issue must be put in perspective. "We have talked a lot about the weaknesses of

Pilots prefer flying to regulating

At a press conference at the International Air Transport Association annual general meeting in June, former pilot and now CEO of the International Airlines Group, Willie Walsh, said he "had been in the business for 38 years and never seen a pilot shortage".

He makes a good point that also applies to regulators. Pilots around the world, especially experienced captains, are in constant demand and earn high incomes with good working conditions and career prospects. There are shortages of experienced pilots, particularly captains, in countries where salaries fail to meet the going global rate for cockpit crew and aviation engineers and technicians.

The air safety oversight and aviation regulatory community worldwide relies largely on pilots to to perform their work. But these pilots can earn much more and advance more quickly at an airline than they can if they work for a government department.

Director general of the aviation and security department of the Japan Civil Aviation Bureau (JCAB), Shigeni Takano, told delegates at the recent Asia-Pacific Air Safety Seminar (APASS) that like most other regulators JCAB was experiencing a shortage of qualified staff to maintain quality airline safety oversight.

"Airlines pay more than regulators, so obviously that makes it difficult and pilots obviously tend to want to fly more than to be inspectors. But we need more experienced pilots in the bureau."

Herdman said: "It is a major concern in developing countries where the gap between private sector salaries and government salaries is immense and not just in our sector. The situation has led to developments such as regulators being split off from the civil service pay scale and placed in a corporatized body, which recognizes the salary will be different," Herdman said. Vietnam did this and doubled the salary of its inspectors.

Tay said attracting enough experts into the regulatory community was not new. "It has existed since I joined the industry. Regulators always find it hard to recruit from the industry. You have to compete for talent and find ways to increase your line of experts within the regulator," he said.

"It is important to offer a good salary package for these positions, together with a meaningful career proposition. We should not think money is the main driver. We need to create a good career for them."

Regulators should look beyond the aviation industry to find qualified staff APASS delegates were advised. "In some cases, you can re-define the job of the regulator to be less dependent on the scarce resources of pilots. Some inspections need not be done by pilots per se. But we have to make those changes in the proper way that would help relieve the shortage among regulators," Tay said.

Thai Airways International A380 captain, Amornvaj Mansumitchai,who also is the executive vice president of the International Federation of Airline Pilots Association in the region, said at the Tokyo conference that even if the regulator matched the salary of an airline for qualified staff, potential candidates would not leave the airline.

"It's more than money. It is clear. It is much more difficult for the regulator to retain or attract people because a pilot wants to fly the aircraft. We see a lot of civil aviation authority inspectors quit to join an airline."

regulatory oversight. It is tempting to say or believe the industry must act urgently because this situation represents an acute safety threat," he said.

"But that's not the case. The fantastic safety performance this industry has delivered is the collective success of manufacturers, airlines, airports, air navigation service providers and regulators, good and bad.

"My instinct is to say regulatory oversight is a quality assurance requirement. It's not quality control. Quality control comes from every player in the industry trying to be safe."

The purpose of regulatory oversight is "to make sure that bad actors [airlines] aren't tempted to enter the industry or good airlines, which are competing in the industry, are not tempted to cut corners", Herdman said.

"You can have a very weak or non-existent regulator and have exemplary safety performance from the operators, including airlines and others."

Civil Aviation Authority of Singapore (CAAS) deputy director general, Tay Tiang Guan, agreed there could be countries with weak oversight yet airlines [in the country] were performing well.

"That can be explained by understanding that air travel is a supply chain with many parts in it. So it could well be the regulator is weak, but the airline is strong. I agree we should not generalize and say the situation is very dire and we need to fix the regulatory oversight before we can get better safety performance," he said.

"I don't think that's the correct conclusion. All parties need to play a part in making sure safety assurance is in place."

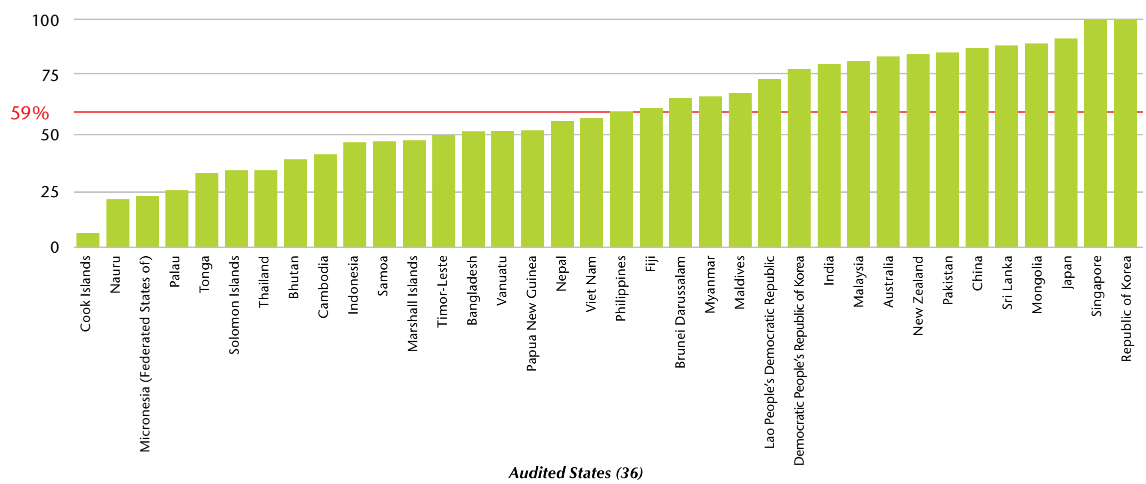
There was, however, universal agreement at the conference that oversight needs to be strengthened. Tay is co-chair of the Asia-Pacific Regional Aviation Safety Team (APRAST) that was formed by ICAO in 2011 to contribute to its Global Aviation Safety Plan (GASP). Speaking in this role at the conference he said the team publishes an annual safety report that compares the Asia-Pacific with other regions.

"We have a good strategy to improve safety in the region, but more has to be done. More than half of the (Asia-Pacific) states are below the (ICAO) target of 60% in terms of effective implementation of safety oversight," he said.

"More importantly, this region has not shown improvement in its effective implementation score compared

ICAO safety audit results for APAC

Effective implementation of safety oversight systems by state



with other regions in the last three years. It is the only region that has not shown improvement so there is a lot of pressure in this fast growth and dynamic Asia-Pacific to improve safety. Much more needs to be done."

Tay said that after five years of existence, APRAST is getting lower than expected participation from nations as well as from the industry in its activities. "There was a lot of enthusiasm at the start, but this has changed. Commitment by the industry is critical to advance safety in the region.

"The industry has deep knowledge in aviation functions. They need to be there to drive some of the key initiatives. Airlines can help drive that and bring about the changes with regulators to meet these challenges."

Thai Airways International (THAI) A380 captain, Amornvaj Mansumitchai, who also is executive vice president Asia-Pacific for the International Federation of Airline Pilots Associations (IFALPA) said another issue that needs attention is the system for monitoring the safety oversight of flight and technical training organisations.

In Thailand, which has been red flagged by ICAO for lack of safety oversight, one training organization has had three fatal accidents in the past year, he said. "So we have a real problem here. Even without the growth, and not only in Thailand, many regulators in Asia have a problem in conducting their safety oversight properly. The growth will make the situation worse."

The THAI A380 captain said that in Thailand the Department of Civil Aviation (DCA) receives only 1%-2% of the Ministry of Transport's budget. Land transport is allocated 35%. "It is going to take quite a long time to correct this," he said.

Herdman said carriers are volunteering to second dozens of people to regulatory bodies. "I had a meeting with a few chief executives and one happened to mention he'd seconded 15 people to help the regulator," he said.

"And a couple of the other CEOs said: 'Huh, that's nothing. I have seconded 40 people'. If you seconded the expertise they can't regulate you. They are helping to raise standards, to train and share expertise and they may be involved in auditing other airlines, which again is uncomfortable."

Boeing forecasts that 1.5 million cockpit crew and technicians will be required to keep airline fleets in the air in the next two decades. With this demand, can authorities stop the "brain drain" of pilots, engineers and other experts from government jobs to airlines or competing regulators that offer better salaries and career prospects?

"That touches on the constitutional question of freedom of movement," said JCAB's Takano. "We can't stop pilots from doing so, from going to the Gulf or elsewhere. What we can do is

> "If you look at the figures carefully, in European countries the unemployment rate of pilots is 16.5%. In some countries it is up to 25%. There are a lot of pilots out there who are not renewing their licences after three years. Everybody says there's a shortage of pilots in the U.S. Actually it's not a shortage. There is a shortage of senior pilots"
>
> **Amornvaj Mansumitchai**
> Thai Airways International A380 captain


Shaping tomorrow's regional aviation

make it more attractive for them to stay in terms of money and the working environment."

THAI's Amornvaj said the issue was more complicated than a shortage of pilots. "If you look at the figures carefully, in European countries the unemployment rate of pilots is 16.5%. In some countries it is up to 25%. There are a lot of pilots out there who are not renewing their licences after three years. Everybody says there's a shortage of pilots in the U.S. Actually it's not a shortage. There is a shortage of senior pilots.

"In Asia, different countries have a different profile of pilot shortages. In my country of Thailand the government has formed a committee to examine this issue, but we are talking about how to increase the quantity not the quality."

Herdman said while the industry is going to grow enormously in the next twenty years, he was optimistic it would find solutions to these problems. "Capacity will be found. I've never come across a situation where we have a prolonged pilot shortage where pilot training is a private sector activity. The opportunity is there and I'm quite sure the private sector will find solutions," he said.

Airbus's Malinge added it was not only about pilots, but about everyone from top management to the bottom level. "It's a matter of ensuring everyone has the right aviation experience. In this region, we have an increasing level of operations but with a variety of aviation backgrounds, in particular from the authorities.

"It leads to the challenge of having oversight capability to sustain this growth. It's not only about pilots, mechanics and cabin crew. It's also about the infrastructure, the ATC, Navaids and airport capability and its about the oversight authorities making sure they support the growth in an appropriate manner.

"We need to think about the big picture and the tens of millions of flights that will be performed every year. It is all about working better together. We have to invest in people and ensure everyone does support the growth."

Tanaka said the industry, including regulators, must believe it can do better and that tomorrow can be safer than today. "There has to be good conversation between industry and government. We should enhance communication everywhere in the aviation community."

Herdman said: "As an industry we support the ICAO 'No Country Left Behind' campaign, which aimed to address evident disparities in the quality of regulatory oversight amongst different states through improved implementation and compliance. It's indefensible that you should have such low levels of compliance, but please don't think we have acute safety problems. We don't. The industry is in good shape." ■

Turboprop accident rate concerns safety experts

Constant crew turnover, dangerous flying conditions and under-equipped airports are some of the problems that airlines flying turboprop fleets face in the Asia-Pacific.

By Tom Ballantyne

In its analysis of the turboprop market, released at the Farnborough Air Show in July, European aircraft manufacturer, ATR, announced that in the next two decades sales of turboprop airplanes would be heavily tilted towards the Asia-Pacific.

It forecast that 27% of the 2,800 turboprops scheduled to be delivered in the next 20 years were destined for the Asia-Pacific and another 11% would be delivered to China. The aircraft would support the launching of 3,000 plus routes of which 1,400 of the new destinations would be in the Asia-Pacific, said ATR.

As the volume of turboprop flying increases, aviation safety experts have called for a renewed focus on turboprop safety. "Turboprop operations represent 20% of global operations, but make up almost 60% of the industry's hull losses. It is quite an alarming number when you think about it," the technical director of the Association of Asia Pacific Airlines (AAPA), Martin Eran-Tasker, told delegates at the organization's annual aviation safety seminar (APASS) held last month in Tokyo.

"If we actually look at the turboprops, we have seen an increase within the region. We have seen a significant number of orders and a lot more operations. You see turboprops more often in a domestic operation, but in the Asia-Pacific we are seeing them operating more regionally," said the AAPA technical director.

"They fly in jungles, into small islands or in mountain ranges in very extreme conditions, which explains some of the challenges they have. So we need to have a separate focus on these sorts of operations to identify the priorities they are experiencing."

There has been on one major turboprop accident in the region this year. In Nepal, a Tara Air Twin Otter crashed in Solighopte in the Myagdi district, killing all 23 passengers and crew. Nepal has had several accidents in recent years. As a result, the country has been identified as a significant safety concern by the International Civil Aviation Organization (ICAO), which is working with Nepal's aviation department to improve regulatory oversight.

In Taiwan, a TransAsia Airways ATR 72-600 crashed into the Keelung River in February last year shortly after taking off from Taipei Songshan Airport. There were 53 passengers and five crew on board and only 15 survived. Seven months earlier, another TransAsia ATR slammed into a building during an approach in bad weather at Magong Airport on Penghu Island. The accident took the lives of 48 of the 58 people on board.

Eran-Tasker displayed a graph at the Tokyo conference that showed major jet accidents have been declining to a record low level, but turboprop accidents have been rising worldwide. "If we look at performance over many years, we can see the (graph) lines are diverging. It's not the sort of picture we want to see," he said.

"Fortunately, in the last 12 months, there has been a significant improvement. It is starting to come together, but we can only wait to see if that trend is consistent over time. There is a strong message here. We need to look a little closer at some of the turboprop operations."

AAPA director general, Andrew Herdman, said: "Turboprops and small regional jets play an important role in serving short-haul destinations and are a key part of what this industry provides to the public.

"These types of operations have some unique characteristics – difficult terrain, maybe small islands, maybe mountainous areas. Often, they are flying into airports that cannot be served by larger jet aircraft. Some of these airports are not well equipped with the latest navigation aids.

"What we have said is that it is helpful to focus on regional operations and turboprop operations and to share best practice about these types of operations."

One of the big challenges for turboprop operators was cockpit crew retention, said Herdman. "Turboprop carriers often are hiring young pilots and many of them take the job to work their way up to jets. So you have quite a lot of turnover. Experience levels and training is a constant challenge." ■

The Association of Asia-Pacific Airlines (AAPA) is organizing a series of safety workshops specifically aimed at the turboprop sector. At its Asia-Pacific Air Safety Seminar (APASS) last month, subjects ranged from safety management system (SMS) implementation to flight crew training as well as other vital aspects of safe turboprop flying.

Asia's travel agents a lifeline for GDS?

Global Distribution Systems (GDS) are feeling the heat now that airlines are selling directly through their own platforms or via the International Air Transport Association's (IATA) New Distribution Capability (NDC).

Dominic Lalk reports from Beijing

As transaction network operators for travel service providers and agencies, Global Distribution Systems (GDS) are facing obsolescence, but they are not giving in to the forecasts of doom. Instead, they are gearing for a fight to retain their business with every technological breakthrough in their arsenal.

In late September, GDS provider, Sabre, held the Travel Technology Exchange (TTX) in Beijing. More than 500 travel agent clients, airline and supplier representatives and members of the region's travel industry were briefed on new technologies and changing industry perspectives in the sector.

There was a good reason behind the venue: "A lot of the 425,000 travel agency subscribers to Sabre's global travel marketplace are selling travel to China today, and this includes many of our travel agency customers in the Asia-Pacific," said the company's senior vice president for the Asia-Pacific, Roshan Mendis.

He said an average of 500 bookings are made in the Asia-Pacific every second of every day at the moment, and the number is growing.

"We are redoubling our efforts at innovation," Mendis said. He believed virtual reality (VR) is a worthy investment for tomorrow's booking environment, in which GDS will continue to play its role in his view. "Imagine walking into an agency, unsure of what airline you want to fly with, and in which cabin. In the future, you just put on your VR headsets to experience the different cabins. This is particularly relevant for first and business class travel."

Technology aside, Sabre and its GDS competitors, Amadeus and Travelport, know that there are approximately two trillion airfares on the market at any given moment. The savvy business traveller might whittle down the options by frequent flyer benefits or timeliness, but as the latest statistics suggest less experienced travellers in emerging markets like China and India may lose themselves in the labyrinthine fare structures and resort to indirect channels.

"On average, 67% of business and first class bookings come from indirect distribution, and yield from the indirect channel is on average 42% higher than the direct channel," said Hazem Hussein, Executive Vice President (Airline Commercial) of Amadeus Asia Pacific. Hussein pointed out that GDSs were instrumental to an airline's cost management. "The cost of each GDS transaction remains very low compared with other industries. Especially when you compare it with the direct online traffic acquisition costs per traveller."

However, challenges and opportunities remain. "There's a need to sell ancillaries better through the GDS," said Mendis. But airlines accuse GDSs of a lack of vision, interest and execution when it comes to handling the burgeoning market of airline merchandising.

Ancillary sales among the top ten performers grew from $8.4 billion to $26 billion between 2008 to 2015, according to the 2016 CarTrawler Yearbook of Ancillary Revenue. United Airlines, American Airlines and Delta Air Lines came out on top at $6.2 billion, $ 4.7 billion and $3.8 billion, respectively.

Qantas Airways affiliate, Qantas Loyalty, ranked ninth worldwide, but was the regional champion at $1.2 billion. By per passenger spend, budget carriers sold the most ancillaries in 2016. U.S. airlines topped the list, largely because they charge their passengers for everything except the seat. Qantas ranked fifth followed by Korean Air and AirAsia X was eighth. China Eastern Airlines and China Southern Airlines lagged well behind at 3.7% and 0.6%, respectively, of total revenues from ancillary sales.

However, most of these transactions were handled by the airlines directly. The same report noted that in the Asia-Pacific, only Qantas and Virgin Australia engaged all three major GDSs for ancillaries. Most LCCs, including Cebu Pacific Air, Hong Kong Express and IndiGo Airlines, as well as legacy carrier Japan Airlines (JAL), chose to handle à la carte services exclusively through their own channels, at the expense of GDSs and their agency lifelines.

LCCs are an easy "vernacular" to use, Hans Belle, Sabre vice-president and general manager for the Asia-Pacific told Orient Aviation, but challenges remain with respect to LCC-GDS collaboration. "Once you scratch the surface, LCC is a whole bunch of things. It's nearly all hybrid. Hybridization carries a whole lot of different attributes that you try to play to. Trying to make sure that they understand our full offering, the value of the GDS, (and) the value of the travel agency community is important," he said.

Airlines have complained about not getting value for money from the GDS providers, claiming they are not training their agents to use the ancillaries for upselling. Conversely GDS providers and agents are up in arms about ancillaries being exempted from the commission that airlines pay. The spat between airlines and GDS providers reached its climax in June 2015, when the Lufthansa Group, fed up with fee hikes and complacency, announced it was imposing an additional charge of €16 when booking through a GDS rather than their own systems, arguing that the costs of using external systems was several times higher than that of their own.

Emirates Airline Group announced it is developing its own digital retailing platform. Speaking at last month's Aviation Festival in London, Emirates president, Sir Tim Clark, said "there are too many parasites" taking value from airlines to support their own business models. "I have been banging the drum about the way we are an industry constrained by the legacy distribution systems," Clark declared, and added he was "not satisfied that the GDS systems of distribution on offer are fit for purpose for the next five or ten years, particularly in light of what has been going on in the digital world".

Speaking to Orient Aviation at the TTX in Beijing, All Nippon Airways (ANA) vice-president for marketing planning, Kikuo Watanabe, took a softer approach. As the ANA man in charge of GDSs, Watanabe said his carrier continued to rely on the aggregators and that only 20% of its international bookings are made through the airline's direct channels.

"Japanese customers are accustomed to using travel agencies," Watanabe said, singling out older travellers who preferred organized group and package trips. "As long as travel agencies exist, GDS companies such as Sabre are inevitable," Watanabe said, but added "of course we'd like to ask the GDS to moderate their pricing".

It has been a brave new world for GDS ever since IATA premiered its NDC in 2012. Initially, GDSs fretted that the NDC Standard would render them obsolete altogether. While most of their concerns are being addressed, industry players are still divided about its implementation.

"We are still trying to fully understand NDC," Watanabe said. He said initially NDC was directed at airlines, but now IATA has begun to involve GDSs. The ANA executive said the airline has yet to adopt the NDC Standard. "We like to watch and see; the typical Japanese approach of see the other carriers and learn from their mistakes," he laughed. He said it would be good if IATA dispatched NDC experts to individual carriers to educate them on the Standard and facilitate implementation.

In a nutshell, the NDC Standard lays out the grammar for a common electronic language between airlines and travel agents. Anyone can acquire and use the Standard, and GDS providers can also communicate with one another in NDC Standard-compliant, XML-based data transmissions.

The radical development is marketed by IATA as a modernisation of 40-year-old data exchange standards for ticket distribution developed before the Internet was invented. IATA believes the NDC enables innovation in travel technology solutions and apps by giving GDSs ammunition to drive sales.

NDC is contentious. Some airlines feel short-changed by GDS providers and claim that they are not training their own travel agents to use airline ancillary products to upsell to passengers. GDS providers and agents retort that ancillaries do not attract commissions from airlines.

"From Sabre's perspective, we aren't waiting on IATA NDC to deliver merchandising solutions to airlines," said Kathy Morgan, Sabre's director of airline products, who added the firm has been enabling airlines to sell their products in new and different ways through both direct and indirect channels for many years, and would continue to utilize emerging technologies in a way that benefits everyone in the travel ecosystem.

While these GDS innovation drives will surely benefit the end customer, there is a palpable tension between their commercial goals and IATA's well-grounded aim to create a consistent environment where airlines will be able to uniformly distribute the entirety of their product portfolio, including ancillaries, across all channels that are direct or otherwise.

But then again, IATA is aware NDC isn't a perfect solution. As Tony Tyler, former IATA director-general, put it, "NDC will never finish. We have set up standards for the development of distribution through the indirect channel and other ways which will now presumably carry on until someone else betters it." ■

The New Distribution Capability

The International Air Transport Association's New Distribution Capability (NDC) is intended to offer potential customers a direct line of booking via airline websites for all their travel needs. It has three independent certifications: Shopping, Order Management and Airline Profile.

A shopping schema allows stakeholders to transmit all information relevant to the end traveller in a consistent 'standard' form. It includes on-board food and beverages sales, checking of baggage and excess baggage, assigned or better seats, call centre support for reservations, fees charged for purchases made with credit or debit cards, priority check-in and screening, early boarding benefits, on-board entertainment systems and WiFi access.

NDC Order Management enables everyone, including GDSs, to manage NDC-driven orders throughout the entire lifecycle, from booking to fulfilment by collecting and passing on payment details. It also allows them to request accountable documents issuance to fulfil NDC-driven orders.

The NDC Airline Profile gives airlines the ability to identify and respond to the customers in markets they want to attract.

MARKETING THE NEW MALAYSIA AIRLINES

Malaysia Airlines Berhad is emerging from the most traumatic period in its seven decade history. After the loss of MH370 and the shooting down of MH17 in 2014 passengers abandoned the carrier in their millions, forcing the Malaysian government to rescue the near extinct airline. Last month, MAB's group managing director and CEO, Peter Bellew, told *Orient Aviation chief correspondent, Tom Ballantyne,* ***that passengers are returning to the airline, including Mainland customers who deserted the carrier two years ago.***

Ask Malaysia Airlines (MAB) Irish-born group managing director and chief executive, Peter Bellew, where the carrier sits in its turnaround program and he turns to a football analogy to reply. "I'd say we are about twenty minutes into the first half of the match and we've just started breaking out of our own half," he said.

"A lot of the work we have done in the last twelve months was about reducing costs, dealing with contracts, restructuring finances and generating cash on the balance sheet. Now, we are moving into the maximizing revenue stage."

The first good news on that front arrived with the results for last February. The airline made its first monthly profit in several years. But the figures weakened in the second quarter because the religious month of Ramadam, when adult Muslims must fast for 17 hours a day and are encouraged not to travel, began on June 7. At least 60% of Malaysians are Muslim.

Load factors have been disappointing at below 70%, Bellew said, but "forward booking patterns strengthened in the third quarter. We expect an improved performance in business class loads in the fourth quarter", he said.

"We've gone on a massive marketing drive and it's paying off. In the last eight weeks, our load factors have picked up fairly dramatically," he said. "Somewhere like London, where we have fairly vicious competition from British Airways, Etihad, Emirates and Qatar Airways - who are offering extraordinarily low fares - we have pulled back eight per cent in market share.

"We are winning business in a whole load of places. That's purely from being very public and doing more advertising than we've probably done for five years."

Before he took charge at MAB on July 1, following the unexpected resignation of his predecessor, Christoph Mueller, Bellew was COO at the carrier and was instrumental in planning its rehabilitation. In fact, Mueller and Bellew have made history at the airline as the only two non-Malaysians to have headed the flag carrier.

As CEO, Bellew has not skipped a beat. A largely successful $1.5 billion restructuring program has encouraged him to believe the 2018 target for profitability at the airline can be achieved.

"There is no line of revenue we are not trying to maximize and no line of cost we are not trying to reduce. Literally, every hour of every day we are chasing revenue. In the past, the company traditionally had a very medium to long-term view on planning and marketing," he said.

"It's not enough anymore to publish your summer schedule nine months in advance, throw out a bit of advertising and hope business will come to you. We have to be much more flexible in our approach, be proactive

and reactive simultaneously, which we have not been doing for the longest time.

"We've been very aggressive on our sales and marketing in the last eight or nine weeks and we'll continue to do that for as long as we are in business. Our revenues and our average fares are holding up pretty well at the moment."

There's another significant development that will underpin the airline's balance sheet if, as planned, it hits that return to profit date: a fleet modernization that will benefit the bottom line.

At one stage, MAB had 17 B777s, as well as 20 B747-400s. They have now gone from the fleet.

Next to go will be MAB's six A380s. They will be replaced by six A350s, with the first of the new aircraft type scheduled for delivery in Kuala Lumpur in the first quarter of 2018. "The A350, in particular on the London route, will make a significant difference to us. We are an operator with one of the longest flights every day in the world - 14 hours - to London twice a day. It is an expensive run for fuel and quite a competitively priced route," he said.

At the Farnborough Air Show last July, MAB added to its re-fleeting plan with an order for 25 B737MAX 8s, with options for another 25. The list price was US$5.5 billion, but that is not what MAB is paying for the planes.

"The B737 MAX aircraft we bought cost about 40% less than the current B737-800s and they use 15% less fuel. This is going to be an absolute game changer for Malaysia Airlines. The economics of the airline will be transformed from late 2018 to 2020. It will be night and day in cost structure," he said.

Not long before he spoke to Orient Aviation last month, Bellew had looked at the airline's projected budgets for the third and fourth quarters of 2018. "We saw immediately the massive changes in fuel efficiency once we shift from the A380 to the A350 in those quarters," he said.

"At the same time, every other cost item [at the carrier] we will attack day by day, week by week and month by month between now and then to achieve modern cost levels."

There has long been speculation about the fate of MAB's A380s as the airline reduced its long-haul network and focused on Asia. Bellew repeated his intentions, made clear in recent interviews, that the carrier would operate some of the A380s through to the Hajj in 2018 and then exit them from the fleet in the second and third quarters of 2018.

"We're talking to people about sales, wet lease, dry lease and combinations of that. Two years from now is not very far away in the aviation life cycle. We will have to find a way of cost effectively managing those aircraft over their life cycle.

"We are trying to sell them. We have interest in some of the aircraft, but the market is challenging for a plane that size in the short-term." However, Bellew said there are airlines interested in "dipping their toe in the water with the A380".

MAB has the ability to provide support for the aircraft, with fixed base simulators in Kuala Lumpur, engineering capacity, painting, electronic and component shops as well as instructors, pilots and cabin crew, he said.

"We will be in a position to work with the government and a third party customer, whether it's wet leases, dry leases or any combination of assistance needed to ensure the aircraft keep flying. It's the solution you need to offer in today's world," he said.

"I don't think you can just stick an advert in Orient Aviation or Flight International and expect people to come banging your door down."

One of the critical factors in MAB's restructuring has been the renegotiation of contracts with suppliers. "We have not touched the service elements at all," said Bellew.

"In fact, we've improved them. Malaysia Airlines had been cutting costs, but sometimes paying a higher price for a reduced service. So in every element of the procurement process we are including very strict service level agreements. They are quite common in Europe, but less common here.

"We have increased the amount of food and the quality of food we are giving people, but we are paying a lower price for it. We have generally reduced the cost of ground handling by significant amounts and we have put in new service level agreements on punctuality, turnaround times, ground service equipment quality and the like," he said.

"Now, a lot of procurement is about ensuring we receive the quality produce we are paying for. Previously, we were paying far too much. There were no penalty clauses for suppliers who basically gave us poor service levels."

In the last six months, MAB has done "a massive deep clean" on the fleet, said Bellew, including new business class seats on its wide-bodies, rejuvenating lounges, upgrading facilities at its various locations and sprucing up the carrier's visual image. "The product is much better than it was a year ago and we are paying a lot less at every touch point for that quality," he said.

The next step in Bellew's strategy is making a big push for a greater presence with the region's travel agents. "It is incredibly important in Asia. It's probably the last market in the world where travel agents completely dominate the business travel market. For us, in the next five years, it will

probably differentiate us from a lot of the competition because we have a significant business class product.

"We've gone to great lengths, and we will continue to do so in the next couple of years, to improve MAB's business class," he said.

One bright spot in MAB's battle to achieve profitability is a recovery in its Chinese business, a market badly hit by the still unresolved loss of MH370 in March 2014, with 239 people on board, and the shooting down of MH17 in the following July, killing all of its 298 passengers and crew.

"Our business from China is really, really strong at the moment. If I had another four or five A330s today I could start routes into China very quickly and they would be successful. No doubt," said Bellew.

"We are talking to a number of airports in Mainland China. We hope to put in place some new routes on the Mainland and announce them by the end of this month."

A deep code share partnership with Emirates Airline also is a winner. "Emirates is a very good partner. We are on a code share on a lot of routes to Europe and it's working very well for us. It is very different to the partnership Emirates has with Qantas," he said.

"Qantas literally flies a lot of metal to Dubai, finishes the flights and transfers its passengers on to Emirates to all over the world. We don't fly to Dubai. We actually quit flying to Dubai as part of the code share process. So we sell a lot of people on Emirates metal and they likewise are selling people on to our metal.

"It's more akin to a traditional code share rather that a major metal partnership, for want of a better phase," Bellew said. "The arrangement is giving MAB customers a range of choices they had not had, with great connectivity through Dubai twice or three times a day to many European destinations. Emirates has four flights to Kuala Lumpur daily, including two with A380s. They are operating capacity of 605 seats. They have a lot of seats here at great prices."

MAB faces fierce competition across its network, particularly with regional rivals and Southeast Asian budget carriers. "It's good fun," said Bellew. "There's never a dull day in KL. You can fly with Malaysia Airlines to places around the region for 99 ringgit, which is basically US$25, and that's a fully inclusive price.

"There are a lot of sneaky charges imposed on passengers by many airlines in the region. You might pay $1 for your ticket, but you can be charged another $50 by the time you add the extras and taxes. Yes, it's tough. But we are in a unique position. We have a substantial and very profitable business class that we have not aggressively marketed for a number of years.

"We have that on all our fleet. Down the back, we have been operating at less than 70% load factor and we have seats we can take a view on. We have been using more modern revenue management techniques in the last couple of months so we have a number of seats we can book early at the lower fare and then progressively go higher.

"There is tough competition here, probably some of the toughest in the world. There's a lot of capacity, but we have a strong brand in the region. We have a nice airport with plenty of capacity. We have a relatively modern fleet. We have great, experienced well-trained staff so we play to all our strengths.

"If you take a three to five year view of things, we think we will be on the soccer pitch long enough and we'll score some goals. Maybe some other people will score some own goals or will be sold. Or there will be consolidation in the region. But we'll still be standing."

MAB has returned to fuel hedging after a hiatus forced on the carrier by its poor financial performance. "We are about 60% hedged to the end of this year. We are planning to, and are close enough to getting that in place for the first quarter of next year as well. We have a fairly conservative hedging policy, rolling a year ahead and trying to always be around 60%," he said.

Currency fluctuations are another challenge. MAB cannot readily mount a defence against a decline in the country's currency because of its weak balance sheet. "We were not in a position to have a counter party for any hedging we wanted to do. We don't have any natural hedge against the [US] dollar because we have no revenue in dollars, nothing remotely significant.

"But our budget has actually been pretty close to what the exchange rate has ended up being although when we were doing it the Ringgit was in a different place. We called that pretty well. There is stability about the Ringgit now, at a relatively bad rate. That is what we are budgeting for in the next couple of years."

One management issue that has settled down is staff morale, which clearly took a beating after the two aircraft losses and the deep staff cuts demanded by the turnaround plan. "It's been a really interesting experience for me because I come from rural Ireland where family is everything," he said.

"In fact, often in Ireland all you interact with on long winter nights is your family and your extended family," he

> Our business from China is really, really strong at the moment. If I had another four or five A330s today I could start routes into China very quickly and they would be successful, no doubt
>
> **Peter Bellew**
> MAB's group managing director and CEO

said. "When I came to work here, I thought I was here to turn around an airline. I realized fairly quickly that Malaysia Airlines is one giant family.

"A lot of the people that work here are genuinely related to each other. If they are not, they know each other and they've had parents and grandparents, uncles and aunts (working) here. So there is a certain camaraderie here.

"Through all the difficult times the company has experienced, in many different ways there is a great tenacity about the family sticking together. It is what I have experienced here. I think morale is really, really good at the moment. Everybody is giving it their best shot. Everybody is supporting each other and they are doing it for the family.

"This is something we can develop and it is going to make the place different. As we are now coming out of the bad times, it's much more that success will keep us together. It will keep us level headed so we don't start doing stupid stuff."

As for the challenges ahead, Bellew recognized there are plenty. "The aviation business is remarkable. Long-term planning sometimes is Friday and everything changes on Tuesday," he said. "You use your crystal ball.

"I think fuel prices are going to go back up. Fuel costs, relative to our overall cost base, are not nearly as significant for us as they are for a low-cost airline. We face competition from the so-called low-cost long-haul airlines. I don't see that model working, but we have to bear with that for a few years.

"As fuel prices rise - and I'm sure they'll go through the roof within three or four years – there will be consolidation among the budget long-haul airlines back into mainline carriers.

"If you don't have a business class product, it's very hard to consistently operate routes twelve months of the year over a number of years and bear the costs of long-haul operation. That's one challenge we face, but I see it changing over time."

Another pressure Bellew believed would increase is insufficient air traffic control capacity. "Already, we are seeing certain days going into some Asian countries where you are almost locked out because the weather is bad and the ATC has problems. There's just no capacity. You have to divert or turn back and that's an issue," he said.

"Look at the order books in Malaysia and Indonesia. There are twice as many aircraft on order with these countries - nearly 800 - as there are in all of China at the moment. If only half of those aircraft arrive in the system in the next five years, there will be no air traffic control capacity for those aircraft and there will be no runways for them to land or take off."

But for Malaysia Airlines, Bellew said, the biggest challenge of all is complacency and lack of hard work. "That's our biggest threat. So that's up to me, to make sure I get out of bed early in the morning and to make sure everybody else does as well," he said. ■

Destructive capacity war threatens Malaysia's Firefly

Asia's turboprop airlines and their jet equipped rivals share a problem of over capacity in the market Firefly CEO, Ignatius Ong, told *Tom Ballantyne* in Tokyo.

Firefly CEO, Ignatius Ong, is full of optimism about his regional carrier's long-term future, but for now he is putting network expansion on hold.

"We are in consolidation mode," he told Orient Aviation last month. "We will maintain our fleet size but rejig some routes. There will not be any new destinations this year."

The 100% Malaysian Airlines-owned full service carrier operates 18 ATR turboprops, both 72-500s and 72-600s. As part of its present strategy, Ong has postponed the delivery of two ATRs that were due to arrive at the airline this year.

"We have spoken to ATR. Whatever we have ordered from them is postponed for the time being. Whether or not delivery will happen next year will depend on the performance of the market," he said.

Ong expected Firefly, which focusses on domestic destinations, but also flies to Singapore, Banda Aceh and Medan in Indonesia and Koh Samui, Krabi and Phuket in Thailand, to carry around 2.3 million passengers in 2016, matching the numbers of last year.

There are good reasons for the flattening of the airline's growth, Ong told Orient Aviation in Tokyo, where he spoke at an aviation safety conference in September.

A weak Malaysian currency, the ringgit, and a slowing economy in Malaysia have contributed to the carrier's decreased demand, with load factor now averaging between 68% and 75%.

But the biggest reason for the leveling off of Firefly's expansion is overcapacity in its market sector. Launched in 2007 and initially intended to be Malaysia Airlines budget subsidiary, the carrier had the domestic market to itself for several years.

With hubs at the Sultan Abdul Aziz Shah Airport, Subang, close to downtown Kuala Lumpur, Selangor and Penang International Airport, it has attracted mainly high-end travelers flying between Malaysia's second and third tier destinations.

Then, in 2013, along came Malindo, 49%-owned by aggressive Indonesian group, Lion Air. Malindo, also a full service airline, quickly threw more ATRs into the market. "They grew really fast, to 11 aircraft. It gave my plans a little bit of a dent," said Ong.

"I'm not saying no to competition, but they must have a good business plan. At one point, I was at saturation level yet you are telling me you are going to put another 11 aircraft into the market? Has the population doubled overnight?" Ong said.

The capacity war has not gone away. Ong said the situation might be good for the travelling public, but it forced Firefly into offering fares that are untenable. "My competitor and Firefly have to sell tickets at 49 ringgit (US$11.89).

"For crying out loud, it does not make sense, but we have no choice but to compete. There's no such thing as cost base pricing. If your competitor is going to drop its price, let's say to 49 ringgit, if I put it at 59 ringgit ($14.32), Malaysians and most Asians will say 'hey I'm still going to Penang. I'll save the ten bucks'.

"The other issue is we have a lot of high-end travelers, but they are company travelers and many have a rule of taking the best price on the day."

In this overheated operating environment, Ong has three major goals. He wants responsible, fair competition where competing airlines are realistic about passenger demand. He also would like the Malaysian government to think of a way to put extra ringgit in people's pockets.

"The Malaysian public has less money to spend today compared with last year or two years ago. The general public really needs to have another ringgit in their pocket. If they don't, growth is not going to happen," he said.

The third factor is stability for the country's currency. A weak ringgit is making it expensive for Malaysians to travel to Firefly's international destinations such as Singapore. "So currency is very important. And I would like to make another point. Recently, a journalist said to me: 'Your flying is predominantly domestic so you won't be affected by a lower currency'," Ong said.

"But I am the worst impacted. I am collecting revenue in ringgit and paying my bills in U.S. dollars. The Malaysian economy needs to pick up and competition needs to be a lot more tactical and responsible."

While no new routes will be introduced this year, the carrier will not drop any destinations. Ong said frequencies will be reduced to destinations that are unprofitable. "If possible, we will develop the routes of good performers such as Penang, Alor Setar, Kota Baru and Johor," he said.

"We need to make sure we are sizing ourselves correctly and not taking on too much on the back of weak consumer sentiment." Asked about profitability, Ong said Firefly is "still alright for now… certain routes are profitable. It's fair to say profitability is tough at the moment in a general sense".

Despite its full service model, Firefly has been innovative in attracting ancillary revenue, which now accounts for around 10% of the airline's income. Check-in baggage is free, but only up to 20 kilograms. It sells car insurance. The ATRs are not equipped with ovens so the airline has an arrangement with a food outlet at Subang where passengers can pre-book a meal and eat before they board their flights. Companies can purchase display advertising on Firefly aircraft and the website is designed for shopping.

"Some of these high end travelers buy three phones. I don't know whether it's for themselves or for their girlfriends. I don't care. As long as I can capture a bit of the market and make commission from selling," Ong said. ■

Chinese lessors on the global hunt

China's hunger for dominance in aviation goes beyond rapid airline expansion and building its own jets. Funded by billion dollar investment from their banking parents, Mainland lessors have moved into aircraft leasing's top league from a standing start only a few years ago.

If anything reflected Chinese aircraft lessors' appetite for a dominant role in the sector, it was Bohai Leasing's consummation of the $2.6 billion deal to acquire 100% of Avolon. The Dublin-headquartered lessor is now fully owned by Shenzhen listed Bohai, which in turn is controlled by the HNA Group, a Fortune Global 500 group that also owns China's largest private carrier, Hainan Airlines.

The true price of the acquisition was $7 billion, after Avolon's debt was included, and it was a landmark moment in the leasing industry.

It was the first time a Mainland controlled lessor had succeeded in taking over a western lessor. It followed the failed attempt by a Chinese consortium to buy the world's largest lessor, ILFC, in 2012.

The Avolon purchase is set to take Bohai's aircraft under management, including current and forthcoming fleet at its Hong Kong Aviation Capital and Changjiang Leasing subsidiaries, to 525 planes worth close to US$20 billion at today's prices.

At the time, Bohai's chief operating officer, Ren Weidong, told media: "In the future, Chinese lessors will account for a larger share of the global leasing market, How we differ from other Chinese lessors is specialization internationalization."

Weidong was right on the first count, but he was stretching a point to suggest Bohai differs from other Chinese lessors. His rivals too have set their sights on specialization and internationalization. Data provider, Dealogic, said Chinese buyers in the aircraft leasing sector made up $159.24 billion in outbound deals so far this year, compared with $105.71 billion for all of 2015.

London-based consultants and analysts, Ishka Global, said: "Building a Chinese presence in the (global) aircraft leasing industry is a stated long-term intention of the Chinese government. Bearing that in mind, the 'new' leasing companies have been making some smart strategic moves. They have bought readymade aircraft portfolios from a variety of sources, bought whole leasing companies; formed joint-ventures to leverage management experience and to test the various ways of operating in this sector.

Perhaps most importantly, they have been building relationships with the lessor community and with airlines. Whether they have bought the right assets, paid the right price or acquired the right credits/airlines in the right proportions will depend on how the market evolves."

The drive by Chinese banks and other investors to put big money into leasing companies is hardly surprising because leasing a plane can be far more lucrative than flying one. Bloomberg says operating margins at AerCap Holdings, the world's biggest listed lessor, averaged 34% in the last three years. The extravagant returns compare with 7.8% for the Bloomberg World Airlines Index.

In the last 30 years, aircraft owned by operating lessors worldwide has risen 11% annually. As a result, more than 40% of the world airline fleet is now leased.

It is certainly paying off, if the China Aircraft Leasing Group (CALC), the largest independent aircraft operating lessor in China,

is any gauge. Its interim profit, to June 30, increased by 105.7% over the same period in 2015 and its leasing portfolio expanded to 70 airplanes.

In reality, aircraft leasing on a large scale is still in its embryonic stage in China. The sector only took off in 2007 when China's financial regulator gave banks the green light to enter the sector. Development has been rapid.

Chinese financial institutions have ceaselessly encouraged their leasing subsidiaries and now have at least 80% of local market share. ICBC Leasing alone, owned by the Industrial and Commercial Bank of China, has enlarged its aircraft fleet by more than seven times, to around 450 aircraft, in the last seven years.

The leasing subsidiaries of the remaining "Big Four" Chinese banks - CCB Financial Leasing Corporation (China Construction Bank), ABC Financial Leasing Co. (Agricultural Bank of China) and BOC Aviation (Bank of China) – are actively seeking opportunities outside their home market for growth. Coming up behind them are important players like CDB Leasing Company and China Aircraft Leasing as well as very ambitious but smaller new lessors.

"Potential 'larger' lessor portfolios being offered for sale are gradually diminishing, although there are a few possible targets that could satisfy the growth requirements of all the Chinese-backed institutions," the Ishka consultancy said.

Chinese success in the lessor sector has been helped by the constraints of the tougher capital requirements being imposed on western banks. Possible targets for Chinese buyers could be a subsidiary of North American insurer, Pacific Life Insurance, Aviation Capital Group. Private-equity group, Terra Firma Capital

Partners, owns AWAS Aviation Capital. The leasing subsidiary reportedly has an aircraft portfolio valued at $5 billion and has often been the subject of speculation about either being sold or listed.

Also in play is the U.S.-listed CIT Group and its $11 billion aircraft leasing portfolio. Among those stalking the purchase are Bohai Leasing- controlled Avolon and China's ICBC Leasing. At press time, the lessor world was waiting to hear who won the CIT lessor beauty parade.

Chinese lessors certainly have grand ambitions. The country's largest domestic aircraft lessor, ICBC Financial Leasing (ICBCL), intends to double its fleet by delivering more than 300 aircraft to various customers by year end 2017.

Chinese lessors have big aircraft orders in place to cater for the expected demand at home and abroad for aircraft. It is forecast by analysts that lessors will supply almost 70% of the 6,000 plus planes expected to be delivered to Chinese airlines in the next 20 years.

At the same time, some western lessors forming partnerships with aviation companies in China. As recently as July, a Lithuanian lessor, AviaAM Leasing signed a joint venture with the Henan Civil Aviation Development and Investment Company (HNCA), to build and manage narrow-body aircraft worth of up to $900 million. Our partners at HNCA will provide access to favourable financing terms required for the JV's fleet development," said the chairman and chief executive of AviaAM, Tadas Goberis.

For investors, splashing out money on leasing companies rather than airlines is highly attractive. Bank of China-owned and Singapore-based BOC Aviation Ltd raised $1.1 billion from an initial public offering (IPO) in Hong Kong that was completed on June 1. his year, money it will use to but more planes. The IPO attracted 11 cornerstone investors, including Boeing, sovereign wealth fund China Investment Corp and the government of Singopore's Temasek Holdings Fullerton Fund Management.

Now BOC Aviation Ltd, the lessor posted record net income of $343 million last year, one per cent more than a year earlier, with revenue up 10%, to $1.09 billion. In August, it announced an interim net profit of US$212 million, a 24% increase over the same months in 2015. "Asia-Pacific is a growth market," said CEO, Robert Martin. "The rise of the middle class is going to drive demand for travel. That is going to drive demand for aircraft."

In the same month, China Aircraft Leasing Group Holdings Limited (CALC) announced its initial foray into Japan, a market dominated by local banks and fund managers as well as western investors with close ties to Japanese leasing companies. CALC signed an agreement with ANA Holdings for an A320 that will be subleased to the airline group's budget carrier, Vanilla Air, with the aircraft scheduled for delivery to the carrier next August.

But analysts warn there are issues ahead in this broiling market. Chinese leasing firms eager to acquire established Western lessors in the wake of the Avolon buy out, could pay beyond premium levels for the lessors' assets.

Potential risks include knowledgeable operation of leased aircraft and their condition, maintenance, registration, insurance, transition process and costs and associated residual values. "The delivery of a large number of aircraft from orders made by Chinese lessors and airlines after 2011 is due to peak by 2018," said Ishka.

"While the lessors remain in a honeymoon period as aircraft run through their primary leases, those lessors who don't possess the necessary expertise to tackle the aforementioned issues are going to face a turbulent ride and a steep learning curve," it said.

But there is little doubt that Chinese lessors will play a bigger role in global aircraft leasing than they do today. Analysts forecast there will be more consolidation in the industry and more Western leasing companies up for sale in the next few years, Chinese lessors are expected to be at the head of the queue to snap up the best on offer. ■