

## Air Lease Corporation

# Emphasis on delevering and sales pipeline; reiterate Buy

Reiterate Rating: BUY | PO: 60.00 USD | Price: 42.26 USD

## Beneficiary to aircraft supply/demand imbalance

We continue to see Air Lease (AL) as well positioned to benefit from the external macro environment. We think the supply/demand mismatch across the aerospace industry provides opportunities for AL to benefit from 1) a general increase in lease rates and 2) more opportunities from aircraft sales. AL reported 3Q23 revenue from aircraft sales of \$55mn, beating BofAe of \$40mn. While interest rate expenses grew in 3Q23 (primarily driven by an uptick in the composite cost of funds), we think AL will be well insulated from interest rate movements in the immediate term due to a largely fixed rate balance sheet (85%) and investment grade rating. We reiterate our Buy rating and maintain our PO at \$60 as we expect the severity of the supply/demand imbalance to continue to bolster sales and ultimately support higher premiums. We raise our FY23 adj. EPS expectations to \$6.15 (vs. \$6.05 prior) to account for strong quarter activity and gains on sale. However, we lower 2024 and 2025 adj. EPS as we expect to see a higher average SG&A expenses and share-based compensation. See inside for details.

## Cautious about OEM delivery feasibility

Despite both major OEMs remaining confident in the 2023 aircraft delivery outlook (albeit Boeing decreasing its range to 375-400 737s), AL management is skeptical about the feasibility of the OEMs achieving their goals. Although AL management is trending on the more cautious side, they noted that there is not expected to be a large financial impact from delivery delays at the end of the year (a much larger financial impact is felt from delivery delays at the beginning of the year as it reduces the number of rental months in the remainder of the year).

## 4Q23 Activity Report

On January 9, 2023, Air Lease released its 4Q23 activity report. In the quarter, the company took delivery of 22 new aircraft from the order book to lease to customers and made \$1.2bn in aircraft investments. Air Lease sold seven aircraft to third party buyers for sales proceeds of ~\$440mn. While volumes were slightly lower than BofAe (17 dispositions expected), AL benefited from strong pricing (\$440mn vs. BofAe \$519mn despite significantly fewer aircraft sold). The company remained cautious and reiterated its 8-10% gain on sale margin for 2024.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	5.16	5.90	6.05	7.15	7.95
GAAP EPS	3.57	(1.24)	4.15	5.01	5.62
EPS Change (YoY)	-15.0%	14.3%	2.5%	18.2%	11.2%
Consensus EPS (Bloomberg)			4.35	4.76	5.46
DPS	0.67	0.76	0.82	0.90	0.99
Valuation (Dec)					
P/E	8.2x	7.2x	7.0x	5.9x	5.3x
GAAP P/E	11.8x	NM	10.2x	8.4x	7.5x
Dividend Yield	1.6%	1.8%	1.9%	2.1%	2.3%
EV / EBITDA*	13.1x	18.5x	10.5x	9.5x	8.5x
Free Cash Flow Yield*	-24.1%	-32.5%	-38.8%	-42.5%	-27.1%

\* For full definitions of *IQmethod*<sup>SM</sup> measures, see page 6.

26 January 2024

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### Stock Data

Price	42.26 USD
Price Objective	60.00 USD
Date Established	30-Aug-2023
Investment Opinion	B-1-7
52-Week Range	33.33 USD - 46.20 USD
Mkt Val (mn) / Shares Out (mn)	4,692 USD / 111.0
Free Float	93.1%
Average Daily Value (mn)	28.72 USD
BofA Ticker / Exchange	AL / NYS
Bloomberg / Reuters	AL US / ALN
ROE (2023E)	9.8%
Net Dbt to Eqty (Dec-2022A)	268.9%
ESGMeter <sup>TM</sup>	Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

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Timestamp: 26 January 2024 03:00AM EST

# iQprofile<sup>SM</sup> Air Lease Corporation

## iQmethod<sup>SM</sup> – Bus Performance\*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	1.7%	-0.4%	1.8%	2.0%	2.0%
Return on Equity	9.0%	9.7%	9.8%	10.9%	11.3%
Operating Margin	25.9%	-6.0%	23.8%	26.0%	26.1%
Free Cash Flow	(1,129)	(1,523)	(1,819)	(1,994)	(1,272)

## iQmethod<sup>SM</sup> – Quality of Earnings\*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	2.3x	2.1x	2.5x	1.7x	2.5x
Asset Replacement Ratio	2.8x	3.0x	3.3x	2.9x	2.8x
Tax Rate	19.3%	30.1%	20.0%	20.0%	20.0%
Net Debt-to-Equity Ratio	227.4%	268.9%	260.2%	269.6%	270.8%
Interest Cover	NA	NA	NA	NA	NA

## Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	2,088	2,317	2,645	2,890	3,219
% Change	3.6%	11.0%	14.1%	9.3%	11.4%
Gross Profit	2,088	2,317	2,645	2,890	3,219
% Change	3.6%	11.0%	14.1%	9.3%	11.4%
EBITDA	1,963	1,389	2,457	2,701	3,022
% Change	2.3%	-29.2%	76.9%	10.0%	11.9%
Net Interest & Other Income	0	0	0	0	0
<b>Net Income (Adjusted)</b>	<b>590</b>	<b>660</b>	<b>673</b>	<b>799</b>	<b>892</b>
<b>% Change</b>	<b>-14.8%</b>	<b>11.9%</b>	<b>2.0%</b>	<b>18.7%</b>	<b>11.6%</b>

## Free Cash Flow Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	437	(97)	503	601	672
Depreciation & Amortization	883	966	1,065	1,167	1,274
Change in Working Capital	(71)	(218)	(61)	(665)	24
Deferred Taxation Charge	97	(43)	124	150	168
Other Adjustments, Net	31	775	35	89	93
Capital Expenditure	(2,506)	(2,905)	(3,485)	(3,337)	(3,503)
<b>Free Cash Flow</b>	<b>-1,129</b>	<b>-1,523</b>	<b>-1,819</b>	<b>-1,994</b>	<b>-1,272</b>
<b>% Change</b>	<b>-108.6%</b>	<b>-34.8%</b>	<b>-19.4%</b>	<b>-9.7%</b>	<b>36.2%</b>
Share / Issue Repurchase	1	0	0	0	0
Cost of Dividends Paid	(101)	(125)	(112)	(101)	(111)
Change in Debt	451	567	214	(54)	(54)

## Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	1,087	766	513	903	689
Trade Receivables	0	0	0	0	0
Other Current Assets	22	14	4	4	4
Property, Plant & Equipment	1,509	1,345	1,187	1,095	1,289
Other Non-Current Assets	24,352	26,272	28,260	30,716	33,210
<b>Total Assets</b>	<b>26,969</b>	<b>28,397</b>	<b>29,964</b>	<b>32,719</b>	<b>35,192</b>
Short-Term Debt	0	0	0	0	0
Other Current Liabilities	612	697	1,325	645	652
Long-Term Debt	17,022	18,641	18,896	21,396	22,896
Other Non-Current Liabilities	2,326	2,412	2,677	3,077	3,443
<b>Total Liabilities</b>	<b>19,960</b>	<b>21,750</b>	<b>22,899</b>	<b>25,118</b>	<b>26,991</b>
<b>Total Equity</b>	<b>7,009</b>	<b>6,646</b>	<b>7,065</b>	<b>7,601</b>	<b>8,201</b>
<b>Total Equity &amp; Liabilities</b>	<b>26,969</b>	<b>28,397</b>	<b>29,964</b>	<b>32,719</b>	<b>35,192</b>

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 6.

## Company Sector

Aerospace

## Company Description

Air Lease Corporation is one of the fastest growing aircraft lessors. As of 31 March 2020, AL owned 300 aircraft (weighted average age 3.7 years, weighted average remaining lease term 7.2 years) and managed 82 aircraft. AL is an investment grade lessor based in Los Angeles, but with offices worldwide.

## Investment Rationale

AL is an aircraft leasing company with a young aircraft fleet, large order book, low financial leverage, favorable operating leverage, and renowned management team with strong industry connections. We expect AL's younger fleet to be more insulated from residual value risk, and therefore view AL as a relative outperformer.

## Stock Data

Average Daily Volume

679,661

## Quarterly Earnings Estimates

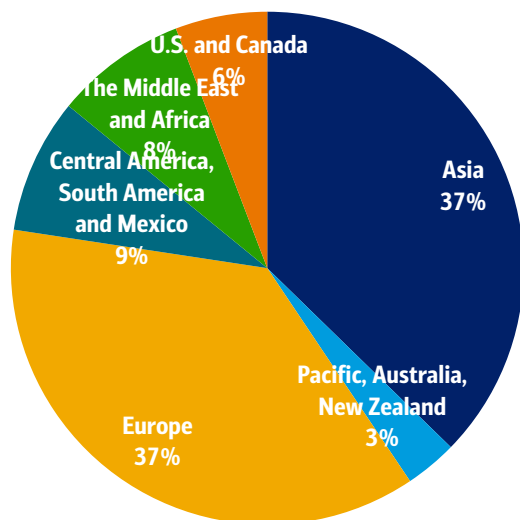
	2022	2023
Q1	1.76A	1.50A
Q2	1.39A	1.58A
Q3	1.32A	1.38E
Q4	1.42A	1.59E

## Geographic diversification de-risks US seasonal slowdown

As airlines work to shore up heightened post-pandemic demand, OEMs have been struggling with their production rate ramp. As demand (heightened) outpaces supply (constrained), we see opportunities for lease rates to increase on new and re-leased aircraft as well as opportunities for AL to benefit from higher gains on sale from aircraft. Management highlighted that the earliest delivery slots for new narrowbodies now extend into the 2030s and the pickup of international travel is pushing up widebody demand as well. Management expects that some of the signs of softening travel and discounted airfare noted by airlines are likely a reflection of a return to more normal seasonal fluctuations in North America and Europe. We look favorably on AL's geographically diverse fleet as we believe it will help de-risk any seasonal slowdowns seen in the Northern Hemisphere.

### Exhibit 1: Net book value by geography

AL has a well-diversified regional concentration of flight equipment subject to operating leases



Source: Company reports

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## Capital deployment focused on delevering (not buybacks)

AL reported a 3Q23 debt-to-equity ratio of 2.68x on a GAAP basis and 2.61x net of cash on the balance sheet. While leverage has been steadily declining quarter over quarter (down from 2.76x on a GAAP basis and 2.67x net of cash on the balance sheet in 2Q23), we note that AL's leverage ratio remains above the company's stated target of 2.5x. Debt-to-equity remains above target as a result of last year's Russian fleet write off. Management highlighted delevering as the key capital deployment focus. Unlike AerCap (AER) which has taken to repurchasing shares at below book value (read our note here), management said that share repurchases are not a priority for AL. We believe delevering will ultimately help strengthen AL's balance sheet and provide further insulation from potential macro events.

## Robust sales pipeline (\$1.8bn total, \$700mn firm)

We look positively on AL's robust sales pipeline and the company's ability to take advantage of the ongoing macro environment. Currently, AL has \$1.8bn in the pipeline, of which \$700mn is firm. The remaining \$1.1bn are on Letter of Intent (LOIs). While the LOI pipeline may be more uncertain, management was confident in their ability to execute on this pipeline. Additionally, we see opportunities for increased sales to newer lessors looking to expand their fleets, including Avalease and DAE.

## ST headwinds from duration mismatch

We see continued short term headwinds for AL given the current financial and rate



environment. While we expect AL to be able to capture higher lease rates due to the aircraft supply/demand imbalance, we note that the average remaining lease term is 7.0 years and higher lease rates may not be accessible until then (unless aircraft are sold before lease expiration). Debt (with an average duration of 3.25 years) is likely to become more expensive before then and it is likely that AL will have to access capital markets (at a higher interest rate) before lease rates can be repriced. The impact is particularly pronounced in an inverted yield curve environment.

## **2 aircraft in Israel insured by Israeli gov't**

Management highlighted that AL currently has two aircraft on lease to Israel. The government of Israel has stepped in to provide insurance on those aircraft. We expect it to be unlikely that AL will have to incur write downs as a result of its Israeli fleet. As to its Russian fleet, management noted they remain in discussions with US and Russian authorities but was unable to say much else. They see incremental benefits as legal proceedings between insurers and other aircraft lessors begin to settle.

## **Reiterate Buy on strong macro tailwinds**

We reiterate our Buy rating and maintain our PO at \$60. We raise our FY23 adj. EPS expectations to \$6.15 (vs. \$6.05 prior) to account for strong quarter activity and gains on sale. However, we lower 2024 and 2025 adj. EPS as we expect to see a higher average SG&A expenses and share-based compensation. We lower FY24e adj. EPS to \$6.65 (vs. \$7.15 prior) and FY25e adj. EPS to \$7.80 (vs. \$7.95 prior).

## Price objective basis & risk

### Air Lease Corporation (AL)

We derive our PO of \$60 using a 0.9x price-to-book value on our 2024 estimate of AL book value. We expect the percentage of net book value at risk to disappear by the end of 2023 due to improving market conditions (with commercial traffic recovering of pre-pandemic levels by the end of 2023) and sale of riskier assets as they come off lease.

Downside risks to our price PO are global economic weakness, fuel price spikes, inability to access capital markets at attractive terms, terrorism and geopolitical events, a downturn in aircraft values resulting from rising supply, flattening yield curve, continued sharp appreciation of the U.S. dollar, changes in equity risk premiums, and overall stock market and financial company valuations.

Upside risks to our PO are stronger than expected economic growth, faster than expected recovery to air travel demand, continued weakness in fuel prices, U.S. dollar depreciation, and easier access to credit at attractive rates.

## Analyst Certification

I, Ronald J. Epstein, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

### US - Aerospace and Defense Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	AerCap Holdings N.V.	AER	AER US	Ronald J. Epstein
	Air Lease Corporation	AL	AL US	Ronald J. Epstein
	Booz Allen Hamilton	BAH	BAH US	Mariana Perez Mora
	BWX Technologies, Inc.	BWXT	BWXT US	Ronald J. Epstein
	CACI International	CACI	CACI US	Mariana Perez Mora
	Cadre Holdings Inc	CDRE	CDRE US	Ronald J. Epstein
	Crane Co.	CR	CR US	Ronald J. Epstein
	Embraer	ERJ	ERJ US	Ronald J. Epstein
	General Dynamics	GD	GD US	Ronald J. Epstein
	HEICO Corporation	HEI	HEI US	Ronald J. Epstein
	Howmet Aerospace Inc.	HWM	HWM US	Ronald J. Epstein
	KBR	KBR	KBR US	Mariana Perez Mora
	Leidos Holdings	LDOS	LDOS US	Mariana Perez Mora
	Leonardo DRS, Inc.	DRS	DRS US	Ronald J. Epstein
	Northrop Grumman	NOC	NOC US	Ronald J. Epstein
	Palantir Technologies	PLTR	PLTR US	Mariana Perez Mora
	Parsons Corporation	PSN	PSN US	Mariana Perez Mora
	RBC Bearings Inc	RBC	RBC US	Ronald J. Epstein
	Rocket Lab	RKLB	RKLB US	Ronald J. Epstein
	Teledyne Technologies Inc	TDY	TDY US	Ronald J. Epstein
	TransDigm Group Inc.	TDG	TDG US	Ronald J. Epstein
	Triumph Group	TGI	TGI US	Ronald J. Epstein
<b>NEUTRAL</b>				
	Albany International	AIN	AIN US	Ronald J. Epstein
	Boeing	BA	BA US	Ronald J. Epstein
	Garmin	GRMN	GRMN US	Ronald J. Epstein
	Hexcel Corporation	HXL	HXL US	Ronald J. Epstein
	L3Harris	LHX	LHX US	Ronald J. Epstein
	Lockheed Martin	LMT	LMT US	Ronald J. Epstein
	RTX Corp	RTX	RTX US	Ronald J. Epstein
	Textron	TXT	TXT US	Ronald J. Epstein



**US - Aerospace and Defense Coverage Cluster**

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
<b>UNDERPERFORM</b>				
	Bombardier	BDRBF	BDRBF US	Ronald J. Epstein
	Bombardier Inc.	YBBD B	BBD/B CN	Ronald J. Epstein
	CAE Inc.	YCAE	CAE CN	Ronald J. Epstein
	CAE Inc.	CAE	CAE US	Ronald J. Epstein
	Huntington Ingalls Industries	HII	HII US	Ronald J. Epstein
	Mercury Systems	MRCY	MRCY US	Ronald J. Epstein
	Spirit AeroSys-A	SPR	SPR US	Ronald J. Epstein

**iQ<sup>method</sup>™ Measures Definitions****Business Performance**

Return On Capital Employed

Return On Equity  
Operating Margin  
Earnings Growth  
Free Cash Flow

**Quality of Earnings**

Cash Realization Ratio  
Asset Replacement Ratio  
Tax Rate  
Net Debt-To-Equity Ratio  
Interest Cover

**Valuation Toolkit**

Price / Earnings Ratio  
Price / Book Value  
Dividend Yield  
Free Cash Flow Yield  
Enterprise Value / Sales

EV / EBITDA

**Numerator**

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income  
Operating Profit  
Expected 5 Year CAGR From Latest Actual  
Cash Flow From Operations – Total Capex

**Numerator**

Cash Flow From Operations  
Capex  
Tax Charge  
Net Debt = Total Debt – Cash & Equivalents  
EBIT

**Numerator**

Current Share Price  
Current Share Price  
Annualised Declared Cash Dividend  
Cash Flow From Operations – Total Capex  
EV = Current Share Price × Current Shares + Minority Equity + Net Debt + Other LT Liabilities  
Enterprise Value

**Denominator**

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill  
Amortization  
Shareholders' Equity  
Sales  
N/A  
N/A

**Denominator**

Net Income  
Depreciation  
Pre-Tax Income  
Total Equity  
Interest Expense

**Denominator**

Diluted Earnings Per Share (Basis As Specified)  
Shareholders' Equity / Current Basic Shares  
Current Share Price  
Market Cap = Current Share Price × Current Basic Shares  
Sales

Basic EBIT + Depreciation + Amortization

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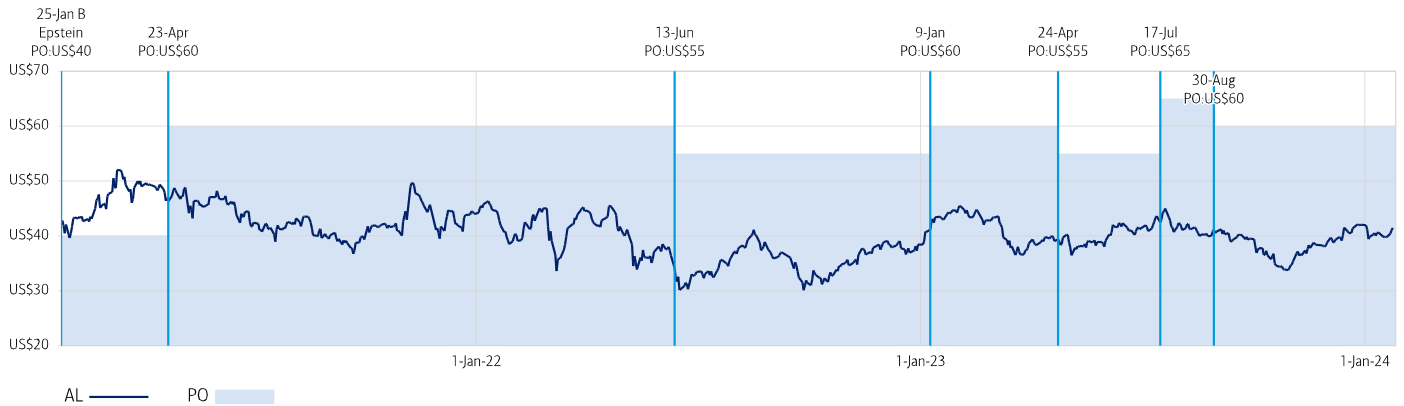
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# Disclosures

## Important Disclosures

### Air Lease Corp (AL) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

### Equity Investment Rating Distribution: Aerospace/Defense Electronics Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	31	62.00%	Buy	23	74.19%
Hold	11	22.00%	Hold	9	81.82%
Sell	8	16.00%	Sell	6	75.00%

### Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

<sup>R1</sup> Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster <sup>R2</sup>
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

<sup>R2</sup> Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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