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Economic Impact: Are We Recession-Proof?

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Optimists believe structural changes in the industry have made helicopters largely immune to the current economic turmoil. Here's a rundown of leading indicators that will tell whether they're right.

Pam Holm isn't Chicken Little.

Holm was the only one of 14 members of Houston's City Council to vote against an April proposal to more than double the size of the police department's helicopter unit. She's not an opponent of the unit or its operations. In fact, she is considered a supporter even among members of the unit. But she had questions about the proposal, particularly how they city would pay for the fuel the added helicopters would burn (given the prospect of oil staying at record prices) and how it could justify their purchase and operating costs when the police department also needs hundreds of police cruisers.

"I want everyone to know that it is not the program that is being questioned," Holm told a Houston radio station after the April 30 vote. "It's my capacity to understanding the funding of it at this time."

Holm's doubts reflect just one set of economic concerns that would seem to hang over the helicopter industry. Even in Houston, an oil town benefiting from that commodity's boom, municipal officials must balance budgets against tax bases. In other U.S. towns, government leaders are wrestling with doing that as a housing slump and recession shrink real-estate, consumer sales, and other taxes that provide their revenues. Commercial operators must figure how much of their higher fuel costs can be passed on to customers (while private operators are stuck in that regard) and how doubts about the economy's heading might hurt their businesses.

The economic downturn, triggered by a U.S. mortgage crisis that started in mid-2007 and has extended to broader credit markets around the world, is aggravated by oil's booms and skyrocketing food prices. Withering investor confidence has pushed financial institutions such as Bear Stearns and Switzerland's UBS to the brink of collapse. Corporations like CIT Group have been forced to sell off major chunks to stay solvent. Amid the turmoil, international lenders have been prompted to replace their traditional benchmark for loan rates, the London Interbank Offered Rate (LIBOR), because they doubt it is still an accurate measure of the cost of borrowing money.

The rising prices and negative news have robbed consumers of confidence in their prospects and those of the economy. Economists and lay people fear a return of inflation to major economies in North America and Europe, or worse, the onset of stagflation, the condition in which economic activity flatlines while prices rise. Last month, for instance, the Bank of England reported inflation had crept up in May to 3.3 percent — its highest level since 1992 — and that it is expected to exceed 4 percent in the second half of this year.

Perhaps the most unsettling aspect of the current economic turmoil has been the speed at which bad news has come. A glaring example was the corporate giant and business icon General Electric. In early April, the company issued a first-quarter report that its earnings were 44 cents a share. Wall Street expected it to earn 51 cents a share, and GE's CEO, Jeffrey Immelt, less than a month earlier, had said the company was on track to meet those expectations.

Yet for all the negative macroeconomic news, helicopter industry officials remain confident that they can make their way through the general downturn without much harm.

"Nobody is really looking at anything in terms of a dramatic decline or offset," Matt Zuccaro, president of the Helicopter Assn International, said during an Apr. 24 webinar sponsored by *Rotor & Wing* and Aviation Today. "There might be a slight dip due to the economic situation going on, but I think the next 10 years for this industry look spectacular, quite frankly."

Zuccaro pointed to the group's Heli-Expo gathering in Houston last February. Vendors reported sales of nearly \$2 billion during the three days of the show, which had record attendance, including what Zuccaro considered the most important measure: a nearly 30 percent rise in the number of international visitors from overseas.

Zuccaro's is a commonly held view. But some in the industry are skeptical that helicopters are "recession-proof."

Which group is right, and what signs would provide early indications of an answer to that question? *Rotor & Wing*, in the past several months, has polled operators, manufacturers and analysts to find out.

Clearly the economic turmoil is having some effect on the industry. At least two U.S. corporations, under pressure from shareholders to improve their financial performance, have sold off their corporate helicopters. Bristow Academy, the flight training arm of Bristow Group, has added a fuel surcharge to its fee schedule for students.

More broadly, helicopter operators and the businesses that support them are finding it harder to get financing for aircraft acquisitions and other initiatives.

"It's going to be harder for buyers to get financing now," said Sharon Desfor, president of Wauconda, Ill.-based HeliValue\$, publisher of *The Official Helicopter Blue Book*. The root problem is a lack of liquidity in financial markets. "You've really only got a couple of big banks that have liquidity," Desfor said, which means businesses and aircraft buyers are going to have to go to second-tier and regional banks to find financing.

That means the cost of borrowing money is going up. Add to that a general tightening of credit standards and financing becomes even more challenging. Outfits with marginal credit ratings "are going to find it hard to get a loan or lease," Desfor said, and large operators with orders for 10, 20 or more helicopters will be forced to pursue syndicated loans from institutions in more than one country.

"It's going to take a lot more time and a lot more work to get the funding," she said. Still, she doesn't see the credit crunch as driving operators to go out of business or pass on contract bids because they can't get aircraft to cover the work.

"I don't think it's going to hit that point yet," she said. "Hopefully, we'll see more liquidity before it gets to that point."

Which brings us to what is widely considered the first leading indicator of a market downturn: a reduction in the extensive backlog of orders that manufacturers hold and the 12-24-month lead times that their customers face in getting new aircraft. They would shrink as new orders stop keeping pace with deliveries on current ones. But no one admits to any sign that such a development is occurring.

The watch area here is not orders from the "very, very important people" segment of the market — billionaires and top-end millionaires. They are truly considered recession-proof since they have the money to keep buying regardless of market conditions. The sensitive market segment is those acquiring helicopters as a business expense or tool; analysts consider them more likely to back off from new orders or cancel existing ones as the economic outlook worsens.

[Eurocopter](#) reports not a single order cancellation attributable directly to the economic downturn. The multinational manufacturer has seen the rate of new orders ease a bit, said Executive Vice President Phillippe Harache, but that may not be a bad thing.

"The acceleration of orders has been reduced," he said. "That's basically due to the uncertainties everyone can feel about the economy. But we are more looking at the stabilization at a high level of bookings than a complete market turn."

Given its large backlog, unabated orders would further extend delivery times. "A little bit of cooling down of the market is not bad news," Harache said. "As long as the trend remains positive, we have no real concern."

At the other end of the manufacturing scale, Menominee, Mich.-based Enstrom Helicopter Corp reports customers who have expressed interest in its products haven't appeared to have any problem getting financing for acquisitions. Tracy Biegler, the company's director of sales and marketing, said a downturn would show up as a drop in the number of requests for quotations on new aircraft prices. "That has not happened yet."

Another leading indicator that the economic woes are starting to affect the helicopter industry would be a drop in asking and actual sale prices for used helicopters.

"These prices have been one of the best indicators to date of the health of the industry," one longtime industry analyst said. "Good used aircraft have become scarce. The prices of some have exceeded those of new products because they were available to operators sooner."

Consider a few examples. For one, [Bell Helicopter](#) last year raised the price of new Model 206s because production-line units were available for less than used ones. For another, one dealer reports a Bell 412 that had been completely submerged after an accident in the Gulf of Mexico and had undergone a complete overhaul is getting interest from potential buyers at an asking price of \$7.3 million. Add another million to that and an operator could purchase a new 2007 412EP. Lastly, the used aircraft that [Sikorsky Aircraft](#) takes in on trade for new sales generally "are resold before they come into our possession," said Bruce McKinney, vice president of Sikorsky Europe.

A factor that would provide a finer and more immediate leading indicator of a downturn is the utilization, or hours flown, of current helicopter fleets. Operators and manufacturers, however, generally hold those numbers very close. Still, Harache said he hasn't noticed a decrease in utilization of the fielded [Eurocopter](#) fleet and McKinney said the general economic problems "are not having any impact from Sikorsky's perspective."

How could that all be so? Zuccaro said "We're kind of in our own little world here." What justifies a "recession-proof" claim?

A number of things, including the high price of oil. Oil's record level (approaching \$140 a barrel at press time) doesn't just bolster the offshore support segment. One corporate operator of an [AgustaWestland](#) AW139 is justifying that aircraft based largely on the time and auto fuel that it saves by allowing executives to avoid a car commute from Manhattan to the corporate jet at nearby Teterboro Airport in New Jersey. Other corporate operators are finding other, utility missions when their helicopters are not carrying executives to increase the aircraft's value to the company.

Other elements that contribute to the economic turmoil also are helping helicopters. The low exchange rate of the dollar with other currencies is helping export sales of U.S.-built helicopters and attracting foreign tourists to the United States. Many treat themselves to a sightseeing flight on a helicopter, aiding the market segment perhaps most vulnerable to an economic downturn and high fuel prices.

The weak dollar also is boosting demand for U.S. crops. That, in turn, increases demand for aerial application of seeds, fertilizer and insecticides. Greater demand in general for crops also spurs farmers to cultivate even small plots of land of sizes

and configurations that are best covered with aerial application by helicopter.

The emergency medical services segment is aided in the United States by the development of new, advanced medical treatments that require patients to be transported to hospitals that specialize in them. Continued consolidation of health care networks into large regional facilities is increasing the need for helicopter transports of patients in more remote areas.

In the public service sector, airborne law enforcement is benefitting around the world from growing recognition of the need for greater homeland security and defense capabilities and the unique contributions helicopters can make to improving them. In the United States, the drop in real-estate tax collections that underwrite police helicopter units has been offset largely by that recognition and a multitude of homeland security grant programs.

Lastly, the helicopter industry is less dependent on the U.S. economy.

"Normally, a U.S. economic slowdown would be disastrous for the civil helicopter industry," said Ray Jaworowski, senior aerospace analyst with Newtown, Conn.-based Forecast International during our Apr. 24 webinar. "But the industry is a little more insulated from the U.S. economy...largely because of the greater diversity in geographic demand. While North America remains the largest regional market for civil helicopters, customers outside of North America now account for more than half of new sales," adding "we're finding that demand is strong in nearly all regions of the world, especially Europe and Asia."

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