Q2 2024 Earnings Call

Company Participants

- Aengus Kelly, Chief Executive Officer & Executive Director
- Joseph McGinley, Head of Investor Relations
- Peter Juhas, Chief Financial Officer

Other Participants

- Anthony Berni, Susquehanna Financial Group
- Hillary Cacanando, Deutsche Bank
- Jamie Baker, J.P. Morgan
- Kristine Liwag, Morgan Stanley
- Mariana Perez Mora, Bank of America
- Moshe Orenbuch, TD Cowen
- Stephen Trent, Citi
- Terry Ma, Barclays

Presentation

Operator

Good day, and welcome to the AerCap's Q2 2024 Financial Results. Today's conference is being recorded and a transcript will be available following the call on the company's website.

At this time, I would like to turn the conference over to Joseph McGinley, Head of Investor Relations. Please go ahead, sir.

Joseph McGinley {BIO 17672898 <GO>}

Thank you, operator, and hello, everyone. Welcome to our second quarter 2024 conference call. With me today is our Chief Executive Officer, Aengus Kelly; and our Chief Financial Officer, Peter Juhas.

Before we begin today's call, I would like to remind you that some statements made during this conference call, which are not historical facts may be forward-looking statements. Forward-looking statements involve risks and uncertainties that may cause actual results or events to differ materially from those expressed or implied in such statements. AerCap undertakes no obligation other than that imposed by law to publicly update or revise any forward-looking statements to reflect future events information or circumstances that arise after this call.

Further information concerning issues that could materially affect performance can be found in AerCap's earnings release dated August 1, 2024. A copy of the earnings release and conference call presentation are available on our website at aercap.com. This call is open to the public and is being webcast simultaneously at aercap.com and will be archived for replay. We will shortly run through our earnings presentation, and we'll allow time at the end for Q&A. As a reminder, I would ask that analysts limit themselves to one question and one follow-up.

I will now turn the call over to Aengus Kelly.

Aengus Kelly {BIO 2460371 <GO>}

Thank you for joining us for our second quarter 2024 earnings call. I am pleased to report another quarter of strong earnings for AerCap, generating adjusted net income of $592 million and adjusted earnings per share of $3.01. These results reflect widespread demand for our assets, strong cash collections and our constant focus on execution. As a result, I am pleased to increase our earnings guidance for the year from $9.20 to approximately $10.25, not including gains on sale in the second half of the year.

On capital allocation, I am delighted to announce more organic growth this quarter with the closing of a 36-aircraft transaction with our customer Spirit Airlines. This is the third transaction in the last seven months that we have closed on a bilateral basis with the customer, taking the total purchase commitments to over 50 NEO and MAX aircraft. This is, of course, in addition to the transaction for 150 CFM LEAP engines with SES that we announced at our capital markets date.

Year-to-date, we have spent $3.2 billion on flight equipment and returned over $720 million to our shareholders in the form of stock repurchases and dividends. Importantly, this was all done without levering up our balance sheet. We are also announcing another dividend of $0.25 per share for Q2, which will be payable in early September. These highlights showcase the power of the AerCap platform.

As I mentioned, demand for aviation assets continues to be robust as reflected in our consistently high levels of activity. Over the last three months, AerCap executed 246 transactions across aircraft, engines, and helicopters, comprising of 162 lease agreements, 47 purchases, and 37 sales. The rate of aircraft extensions, which we discussed at our recent Capital Markets Day, continues to be elevated at over 80% in Q2.

On the sales side, the shortage of aircraft in the system is supporting strong gains on sale, leading to unlevered margins of over 20% in the quarter, our approximately 1.7x book equity. 90% of our sales revenue was generated from sales to airlines and other leasing companies who are keen to gain access to aircraft. And I expected to continue to be the case for some time.

Of note, at the end of Q2, the U.S. is now our largest market at 14.6% of revenues. This is due to the combination of strong placements of aircraft into the U.S., as well as strong demand from buyers for our Chinese aircraft. As a result, China now represents 14% of our assets down from over 20% at its peak.

On the purchase side, our investment in new technology equipment continued with the delivery of 25 new aircraft, including A320neos, 737 MAXs, A220s, 787s, and A330neos from our order book. We also took delivery of a further 20 engines, which were mostly new technology LEAP engines for CFM.

As I said at the beginning of the call, one particularly notable deal that we signed just this week was with Airbus and Spirit Airlines in the U.S. We have agreed to purchase 36 A320neo family aircraft. This transaction results in AerCap assuming 36 aircraft from Spirit's order book and the related pre-delivery payments. This is the third example in the last seven months where we've been able to execute a bilateral transaction to acquire aircraft with a customer that results in a win-win outcome for our customer and for AerCap.

These aircraft are set to deliver in 2027 and 2028, which match well with the profile of our existing order book and is far sooner than we would otherwise have been able to negotiate directly with Airbus and gives us an opportunity to support a long-term customer simultaneously.

Furthermore, we will also backstop up to 52 A320neo family aircraft in Spirit's order book if needed. These additional aircraft would deliver from 2029 onwards. This deal takes our total aircraft added this year to over 50, and I am confident there will be similar opportunities for organic growth to come.

The smaller number of aircraft delivering into the system as a result of the OEM delays has provided some respite to airlines from a financing perspective, but this will change over time and AerCap is well-positioned to take advantage of it. This is another example of where AerCap sets itself apart with its customers. We can step in when others cannot because of the ability, speed, and experience to execute rapidly and in scale.

Similar to our approach to share repurchases and dividends, our approach to organic growth is also measured and disciplined and ensures that we generate strong, long-term returns for our shareholders with an appropriate level of risk.

AerCap's cash flows are the strongest in the industry, not just on an absolute basis, but on a relative basis also. We are generating approximately 25% more operating cash flow per dollar of assets than any of the other large leasing companies, and this also sets us apart.

This discipline, along with the ongoing strength in our cash flows, was recently recognized by all three major credit rating agencies, where AerCap was upgraded to Baa1 by Moody's, BBB+ by S&P, and our BBB Flat rating was put in positive output by

Fitch. These are the highest ratings of any aircraft lessor in the world on a standalone basis, and are a clear appreciation of how we run the company in a balanced and sustainable way.

So in summary, this was another great quarter for AerCap, with broad-based demand for assets, strong cash generation, and positive momentum on our credit ratings. We continue to see attractive opportunities to deploy capital through opportunistic organic investment, the delivery of our order book, ongoing share repurchases, and quarterly dividends, and look forward to showing the evidence of this strategy in the quarters and years to come.

With that, I will hand the call over to Pete for a detailed review for financial performance and favorable outlook for 2024. Thank you.

Peter Juhas {BIO 16582554 <GO>}

Thanks, Gus. Good morning, everyone. Our GAAP net income for the second quarter was $448 million, or $2.28 per share. The impact of purchase accounting adjustments was $169 million for the quarter, or $0.86 a share. That included lease premium amortization of $32 million, which reduced basic lease rents, maintenance rights amortization of $99 million, which reduced maintenance revenue, and maintenance rights amortization of $37 million, which increased leasing expenses. The tax effect of these purchase accounting adjustments was $25 million, or $0.13 per share. So, taking all of that into account, our adjusted net income for the second quarter was $592 million, or $3.01 per share.

I'll briefly go through the main drivers that affected our results for the second quarter. Basic lease rents were $1,568 million. That's a slight decrease from last quarter, which is primarily due to aircraft coming off power-by-the-hour rent arrangements, as I've mentioned on previous earnings calls. Basic lease rents reflected $32 million of lease premium amortization, which reduces basic lease rents.

Lease premium assets are amortized over the remaining term of the lease as a reduction to basic lease rents. Maintenance revenues for the second quarter were $180 million. That reflects $99 million in maintenance rights assets that were amortized to maintenance revenue during the quarter. So in other words, maintenance revenue would have been $99 million higher or $279 million without this amortization.

Maintenance revenues were higher-than-normal this quarter, primarily due to higher amounts of end of lease payments that we received during the quarter, and that's due to the timing of lease maturities. Net gain on sale of assets was $129 million for the second quarter. We sold 31 of our owned assets during the quarter for total sales revenue of $793 million. That resulted in an unlevered gain on sale margin of 20% for the quarter.

As of June 30, we had $105 million worth of assets held for sale. Other income was $81 million for the quarter, which consisted primarily of interest income and certain one-time items. Interest income has been higher this year. We're seeing higher interest income on our cash balances due to the higher interest rate environment.

It's worth pointing out that our calculation of net spread includes interest expenses, but does not include any interest income. If we were to include interest income, that would increase our net spread for the second quarter by around 35 basis points, which is a greater impact than it has been historically. For example, in 2019, prior to COVID, this impact would have been only around 10 basis points.

During the second quarter, we recorded asset impairments of $28 million, and these related primarily to returns of older aircraft where we received end of lease compensation payments, and they were more than offset by related maintenance revenues. Interest expense was $478 million for the quarter, which included $5 million of mark-to-market losses on interest rate derivatives. Leasing expenses were $173 million for the quarter, including $37 million in maintenance rights amortization expenses. And finally, income tax expense for the second quarter was $76 million, which represented an effective tax rate of 15.5%.

We continue to maintain a strong liquidity position. As of June 30, our total sources of liquidity, including unsecured revolvers, other committed facilities, cash, and operating cash flow and estimated sales over the next 12 months was approximately $20 billion. That compares to uses of cash of around $12 billion, resulting in next 12 months sources uses coverage ratio of around 1.7x. We've increased our target coverage ratio from 1.2x to 1.5x, which is closer to where we've generally been running over the past couple of years. And as you can see today, we're still well above this revised target with excess cash coverage of around $8 billion.

Our leverage ratio at the end of the quarter was 2.4 to 1, basically the same as last quarter. Our operating cash flow was approximately $1.4 billion for the second quarter, which was driven by continued strong cash collections. Our secured debt to total assets ratio was 12% at the end of June, that's down from 14% last quarter due to the reduction in the size of some of our secured facilities. Our average cost of debt was 3.8% for the second quarter, which is down slightly from the first quarter, primarily due to the refinancing of some term loans at lower margins.

During the second quarter, we repurchased 3.9 million shares at an average price of $88.66 for a total of $345 million. We also paid our first quarterly dividend of $0.25 a share in the second quarter. And our book value per share was $89.47 as of June 30, which is an increase of 25% over the last 12 months.

In February, we projected adjusted earnings per share of $7.50 to $8.50 for the full year 2024, not including any gains on sale. On our last earnings call, given the strong performance in the first quarter, including higher maintenance revenues, we raised our guidance to the top end of that range.

Given our strong performance during the second quarter, including higher lease revenue and higher maintenance revenue, and our positive outlook for the rest of the year, we're now raising our guidance for full year 2024 to approximately $9 of adjusted EPS, not including any gains on sale. We've had around $1.25 of gains on sale in the first half of the year, so when we add those gains, that takes us to a new estimate of approximately $10.25 of adjusted EPS for full year 2024, not including any gains on sale for the second half of the year.

So overall, AerCap continued to perform very well during the second quarter. We continue to see a strong environment for leasing as well as for asset sales, which is reflected in both the volume of sales and the gain on sale margin this quarter. We're deploying capital towards attractive opportunities across all of our businesses, particularly in aircraft and engine leasing, and we continue to buyback stock and pay our first quarterly dividend.

We continue to generate strong cash flows that in turn result in greater profitability and greater financial flexibility. This quarter, we were upgraded by Moody's to Baa1 and by S&P to BBB+, and we were put on Positive Outlook by Fitch, and that continues the positive rating trajectory that we've now had for several years. With these strong results and with a positive outlook going forward, we're now raising our guidance for full year 2024.

With that, operator, we can now open up the call for Q&A.

Questions And Answers

Operator

(Question And Answer)

Thank you. (Operator Instructions) We'll go first to Jamie Baker with JP Morgan.

Q - Jamie Baker {BIO 3406456 <GO>}

Hey, good afternoon, gentlemen. So, Gus, you called out the Spirit deal for 36 airplanes, the backstop on another, I think you said 52. I mean, look, Spirit's a weaker credit. I'm not asking you to deride a customer, but we have to wonder what additional steps you've taken, to protect against a deferral or potential insolvencies. So, how's this deal different from a more plain vanilla transaction? And if it's not, I guess you just believe you can handle the remarketing effort if it comes to that?

A - Aengus Kelly {BIO 2460371 <GO>}

Look, I think, Jamie, here, this is a win-win for ourselves and for Spirit. It provides them, as you allude to, some much-needed liquidity. It provides us with extremely attractive, the most attractive aircraft in the world, the 321neo, in a time slot that would be impossible to get it in 2027 and 2028, of what we believe are attractive terms for our shareholders. So that's the genesis, really, behind it, Jamie. And, like, we move an airplane every 24 hours somewhere in the world.

Q - Jamie Baker {BIO 3406456 <GO>}

Okay. Fair enough. And then, second, so Mark and I are, we all keep hearing about how tight global aircraft supply is, and we don't disagree. But at the same time, you have these massive guides down from several U.S. airlines, you've got some Western airlines, both discounted and full service, that are guiding down, the Singapore results yesterday were soft. I mean, we're trying to reconcile airline results with aircraft supply, and -- well, quite honestly, we're having a hard time. How do you reconcile those two realities? Thanks in advance.

A - Aengus Kelly {BIO 2460371 <GO>}

That's a very fair point to make, Jamie. How, on one hand, can you say that there's tremendous shortage of aircraft when a number of the carriers are saying there's excess capacity in a very large market like the United States? One of the huge challenges the airlines have at the moment, and Allegiant called it out yesterday, Allegiant is a much smaller airline, but they had a 30 million cost just associated with not having the MAX aircraft. What they also have, which is very hard to explain to the analysts, is the complexity of trying to keep extending a fleet that you want to get out of. It's very inefficient within the airline.

So if you're an airline now and you're short the NEOs or the MAXs or the 787s, you will have trained pilots. You will have bought spare parts. You will have geared up your operation for the entry of those aircraft. When they don't come, your pilots don't sit at home, but effectively they do because you wouldn't have hired them, so you've lower hours being worked overall on average than otherwise you would have. So there are these hidden costs in the airline that they have, and they're having to keep prolonging the life of assets they prefer not to have that are older, that are more complex from a maintenance standpoint, that are more complex from a cabin configuration standpoint, leading to inefficiencies in the airline sector.

So when we say shortage of aircraft, we're looking, we're saying particularly new aircraft because if the airlines could accelerate their transformation into a single type of asset, so that they're only operating one asset, that would give the maximum operational leverage and efficiency. When they're operating multiple fleets, particularly older ones, that's harder to do.

So the next thing then is, well, okay, that's fine, but then how can you're seeing such a strong bid for older aircraft? We're seeing such a strong bid for older aircraft driven by engines, candidly, Jamie. It's really driven by the engines. If you have a 20-year-old airplane and you're an airline and you're saying to yourself, am I going to put this thing through the shop and spend $20 million on overhauling? If it's a full performance restoration, LLPs, am I going to do that? That makes no sense to do that. But I do know the problems with Boeing and Airbus are going to last through the end of the decade. Is there a way I can avoid that massive spend by buying half-life engines or aircraft that have half-life engines off them and thereby avoid the shop business with the engine OEMs?

So these are the things -- there's hidden inefficiency in the airlines due to the lack of the delivery of the new aircraft. And that's a cost that's very hard for them to explain and get across, but we can see it upfront when we're dealing with the airlines day in, day out of the cost of that complexity. So that's what you're seeing is a big drag on their cost line, because it's also fair for people to point out to the airlines, well, your yields are still extremely high. But that is a hidden -- I'm not questioning it, airlines in some cases could do better on costs. There's no question about that. But on a global basis, that's what we see.

Operator

We'll go next to Terry Ma with Barclays.

Q - Terry Ma {BIO 17247903 <GO>}

Hi. Thank you. Good afternoon. So you mentioned you've done kind of three bilateral transactions, similar to the one with Spirit. Are you seeing more of those opportunities come to the market and maybe just talk about what's driving that? And aside from timing differences compared to an OEM order or a particular aircraft type, are there any other advantages like returns or pricing you're getting?

A - Aengus Kelly {BIO 2460371 <GO>}

Well, obviously, we talk to the OEMs on orders, and as you know, we have not been able to reach terms with the OEMs over the last few years, which is, as I've always said, fine by me. I don't care if we never buy another airplane again. I care about deploying your capital, our capital, the shareholders, at the best risk-reward return for the long term of the business.

Certainly, if we got an option -- opportunity with the OEMs where it made sense for a regular order, we'd do that. In an instance like the Spirit deal and earlier on with the gold transaction, it was a situation where we were able to provide assistance to a long-time customer, and we were able to get what we felt were attractive assets, well-priced. So we're getting assets, we felt, in the time frame and at economic terms that made a lot of sense for our shareholders.

Q - Terry Ma {BIO 17247903 <GO>}

Got it. And then a question for Pete, for the net spread. I know you guys don't manage to that, but it's outperformed a bit the last two quarters. So how should we think about that for the rest of the year, taking into account any remaining power by the hour, cash collections, and bond refinancing?

And on the bonds, you have a few lower-cost bonds coming due later this year, which I'm sure you contemplated into your interest expense guidance at the beginning of the year. But credit spreads have also come in by about 40 basis points. So maybe just put all that together. How should we think about the net spread? Thank you.

A - Peter Juhas {BIO 16582554 <GO>}

Sure. Sure. Well, you're right about that. So obviously we factored in all of our plans for raising debt later this year into our Net Spread guidance. So basically, as I mentioned before, the main driver of that recently has been those power by the hour leases coming off and reverting to regular lease arrangements. So that's basically all happened now. So we're not going to see any further impact of that from this quarter onwards.

So all I would say, I think for the balance of this year, we should be around where we were for the second quarter. Because as you said, there are countervailing effects, on the one hand, you've got higher rents coming in, on the other, you have some higher interest expense as well. But I think we'll be around where we are today.

Operator

We'll go next to Moshe Orenbuch with TD Cowen.

Q - Moshe Orenbuck

Great. Thanks. Maybe kind of following up a similar line of questioning. Given all the things that you do see, do you think that the balance sheet is going to be sort of larger or kind of stable over the next few quarters? Like, how do you see that evolving? I mean, are there other opportunities, things that might come up kind of on a spot basis or anything like that?

A - Peter Juhas {BIO 16582554 <GO>}

Sure. Well, first, welcome back, Moshe. It's good to have you on the call again. So in terms of the balance sheet, we would expect it to grow somewhat during the second half of the year, and that's primarily due to CapEx we had about $3 billion of CapEx during the first half of the year, we're expecting a little over $4 billion during the remainder. Now, we don't know if all that will come through. But as Gus mentioned, we've also done some incremental deals as well. So that's really going to be the driver of the balance sheet increasing for the balance of 2024, and then somewhat in -- it will also increase in '25 as well, as we look at it, or CapEx and factoring in some level of sales as well.

Q - Moshe Orenbuck

Perfect. Thanks. And, congratulations on the recent upgrades and -- but it's also true that your leverage ratio has actually improved over the course of the first half of the year. Can you talk about your thoughts as to, as to how you might, how you might manage that in the current environment? Obviously, you've started the dividend. How do you think about share repurchase and other forms of capital deployment over the next several quarters?

A - Peter Juhas {BIO 16582554 <GO>}

Sure. So as you mentioned, look, this quarter we're at 2.4 to 1 net debt to equity. So that is below our target level. It's about where we were last quarter as well. So it's been obviously very positive to get to that point. I think during the remainder of the year, we'll still run below our target, but I think it will be somewhat closer to that. It really depends on how much we do deploy. Obviously, some of it depends on the CapEx because we have more CapEx coming in the second half of the year. You create a little less excess capital.

Similarly, we've done a lot of sales in the first half. So we've done we've done $1.7 billion of sales so far this year. I think we'll probably do $2.5 billion for the full year, give or take. So that's been front end loaded. But I think that it will trend up somewhat, our leverage ratio, but I don't think we'll get to $2.7. Billion.

Q - Moshe Orenbuck

Thanks.

Operator

We'll go next to Stephen Trent with Citi.

Q - Stephen Trent {BIO 5581382 <GO>}

Yes. Good afternoon, everybody, and thank you very much for taking my question. Actually, the first sort of a follow up on Moshe's question, the credit rating side looks really good. Longer term, do you guys have any sort of bogey in mind, roughly speaking, where you'd hope to be with Moody's and S&P?

A - Aengus Kelly {BIO 2460371 <GO>}

Look, I think I think we're very happy with BBB+, Baa1, which is the highest rated, less independent, lessor there is in the world. And we certainly are want to push Fitch over the line as well. They're on outlook positive. I think this provides extremely competitive funding. If I look at our five-year unsecured spread today, it's around 95, 96 basis points, which is about 20 basis points north of someone like JP Morgan or Wells Fargo. So that's extremely competitive.

We're always very conscious of the balance between return on equity for our shareholders and making sure that we have access to very flexible debt and significant pools of debt. But, at some point, of course, if we went much lower, then that would significantly dilute the returns to our shareholders. And we're very conscious of those, how we deploy the capital for our shareholders. And today you saw, again, organic growth. We've returned $3.4 billion, though, to our shareholders in '23 and '24. We have a remaining $600 million left in our share buyback current authorization. And so it's a balance between all those items, but I think I'm very happy with where the rating is today.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Aengus, very helpful. And just one other quick, my follow-up here. I appreciate you guys mentioned the U.S. being the biggest market and you've done some drawdown in China. Could you refresh my memory, geographically speaking, if there's any areas of the world where you're seeing, really good momentum at the moment? Thank you.

A - Aengus Kelly {BIO 2460371 <GO>}

I think at the moment, there's pretty robust demand from the airlines that certainly want to keep what they have. That's true across the world. And you saw that in the extension levels, 80%. So on a global basis, we're extending the vast majority of the assets, a very good indicator to start with.

In terms of placement and growth, we're certainly seeing strength out of the Middle East. And we will continue to -- I think we're going to see strength out of Asia-Pacific because the Asia-Pacific recovery out of COVID has been slower than the Americas or the European market, the two other major markets. And I think that's where we'll see a recovery.

If we look at global traffic in June, we exceeded June 2019 by 3%, despite international traffic being down. And that international traffic is predominantly driven, the decline in international traffic is predominantly driven in the Asia-Pacific region, which is down about 10, 11 points on 2019. So there's lots of room to come back. I suspect that we'll see it in that region.

But of course, from our perspective, as we said, look, we will buy, sell or lease 1,000 aviation assets a year. So from AerCap's perspective, we have the infrastructure, the capability to rapidly move assets from an underperforming region to a performing region if needs be. But at the moment, it's reasonably robust around the world.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Really appreciate it. Thank you.

Operator

We'll go next to Hillary Cacanando with Deutsche Bank.

Q - Hillary Cacanando {BIO 18940405 <GO>}

Hi, thank you for taking my questions. Just regarding your transaction with Spirit, obviously, you're taking deliveries before 2030, since they're from Spirit's order book. But I was just wondering how long the wait would be at this point, if you were to place an order directly with Airbus for narrow-bodies, and, what would the wait time be for the widebodies? I would imagine it's past 2030, but just wanted to see what they were actually at this point.

A - Aengus Kelly {BIO 2460371 <GO>}

I would imagine it is past 2030, Hillary. I mean, any airline orders we've seen recently, particularly on the Airbus side have deliveries commencing in 2030, and moving, and not getting many airplanes in 2030, either. Really, the heart of those orders is 2032, 2033, and beyond. So the -- from our perspective, that's a very long way out there. The '27, '28 timeframe, we feel is a, is a much more attractive timeframe.

Q - Hillary Cacanando {BIO 18940405 <GO>}

And you would say that's the case for widebodies as well, and same with Boeing, and at Boeing as well, in terms of being sold out until 2030?

A - Aengus Kelly {BIO 2460371 <GO>}

I mean, it's more -- on the widebodies, you might get one or two before 2030, but it won't be many. Hillary, like, so I wouldn't, if you went for an order, I wouldn't imagine that there'd be much available on the 787 line, to be fair, before 2030. And it's a function of the ramp-up, too, how they get on. But not much would be the short answer.

Q - Hillary Cacanando {BIO 18940405 <GO>}

Got it. And then, just a follow-up question, your share buyback strategy, obviously, has been very accretive, very successful with the stock trading below book value in the past. But I was wondering how we should think about your buyback strategy when the stock is obviously it's trading above your book value, and I guess going forward as well. Does that change your strategy at all, or not much?

A - Aengus Kelly {BIO 2460371 <GO>}

Well, look, Hillary, I mean, we've been, as you can see, we kept buying shares throughout the year. We've deployed $700 million for when a lot of the year was above book, and we've $600 million in our authorization. So -- and we're selling assets at very big premiums to book equities. You can see this quarter was another quarter where we sold at 170% of book.

But again, look, what we always look at is what's the best use of our capital? Is it debt paydown? Is it buybacks? Is it M&A? Is it buying aircraft for organic growth or engines for that matter? And we've done a lot of the latter in the last few months between the big engine transaction and then the aircraft transaction. So, we always just try and pick what will generate the best long-term risk-adjusted return for our shareholders.

Q - Hillary Cacanando {BIO 18940405 <GO>}

Got it. Thank you. And looking forward to seeing you at our conference in September.

A - Aengus Kelly {BIO 2460371 <GO>}

You bet.

Operator

We'll go next to Kristine Liwag with Morgan Stanley.

Q - Kristine Liwag {BIO 21935865 <GO>}

Hey, Gus, Peter. there's very strong demand for next generation engines and can you discuss how you think about the mature size for the Shannon engine support JV with Safran? How large could this be? And can you provide more details about the economics of spare engine leasing versus more of your traditional aircraft leasing?

A - Aengus Kelly {BIO 2460371 <GO>}

I think the way to think about the spares business is there's I mean it's big but it's not unlimited potential for growth in that business because if you think about there's about 22,000, 23,000 large commercial aircraft in the world I'm excluding turboprops and small aircraft there you've got about say 46,000 engines in service the sparing ratio depending on the engine type is 12% to 15%. So that's your spares portfolio if you say 46,000 in service take 13%, 14% that's 5,000 engines and change maybe 5,500 engines that's the sparing size as the world fleet of aircraft grows then you will have the spares requirement will grow by 12% to 15%.

So that's how it works so there's not an unlimited it's different to aircraft because I said it's only sparing. When it comes to the economics of the engine business model slightly different to the aircraft business model because an engine really holds its value over the long term as its overhauled and the market value of the engine doesn't tend to depreciate a tremendous amount if you've got the right engine. So -- and the engines it's fair to say because of the slower depreciation of the asset your value in the engine business is created over time whereas on the aircraft side you make a lot of your money on the first lease to be fair and then at the back end you're managing engines so I would say that there's a timing difference in how the two businesses work.

Q - Kristine Liwag {BIO 21935865 <GO>}

Great. That's very helpful and as a follow-up I mean we're starting to see other business models capitalize or try to monetize this engine shortage with an engine leasing company doing more MRO type work, either in modules or full exchanges I was wondering how interested are you in expanding into something like that I mean we're seeing EBITDA margins for those kinds of businesses be at like 35% or plus but at the same time it is a lot more labor intensive and it's more a wrench turning type job. So just checking to see what's your appetite for that do you see that attractive and would that be a lateral shift as you expand out the spare engine leasing business.

A - Aengus Kelly {BIO 2460371 <GO>}

I don't think we're going to get into ever overhauling engines but things like engine swapping we do that all the time, we've been doing that for 20 years and that's nothing new and you do it to manage your cost base, I'm sure if you looked at our

EBITDA margin as a company it would be huge, P, what is our EBITDA margin? But while I'm talking, you work it out there, P. But I would say when it comes to the module swaps, of course you're doing all those things.

For example, our biggest department internally is maintenance, our technical department, how we manage it, because it's our biggest controllable cost. And it's an important part of how you drive, AerCap's profitability. Every time there's an engine going to shop, every single month for every engine, we'll track all the usage of that engine. We'll be looking at that engine a year out. When it's going into the shop, we'll be saying what parts of it need to be repaired. What will work with the airline, and say, okay, we want your estimate of work that needs to be done on the engine. We'll go through that.

Then when the engine is in the shop, we'll be on site to make sure that the work that we want done is being done and there's not excess work being done on the engine. So -- and we'd have experts in every engine type, which many wouldn't have, they'd have generalists. You really have to know inside out, high-pressure, low-pressure turbines of every engine type in your portfolio in order to manage your shop visit costs. But so, yes, I would say that we do all those things. Pete, what's EBITDA margin?

A - Peter Juhas {BIO 16582554 <GO>}

Yes. It's around 90%.

A - Aengus Kelly {BIO 2460371 <GO>}

90%. Okay.

A - Peter Juhas {BIO 16582554 <GO>}

It's a bit unfair to look at an EBITDA margin for a financial business because interest is obviously a big component, but yes, it would be around 90%.

Q - Kristine Liwag {BIO 21935865 <GO>}

And sorry, if I could do a follow-up on that 90%. If you were just to capture your engine exchange business, is that also at 90% EBITDA margin? I just want to make sure we're looking at that.

A - Peter Juhas {BIO 16582554 <GO>}

Engine exchange is part and parcel of every day. I am sorry, Kristine, engine exchange is just part and parcel of what we do every single day in the business. It's reflected there. There's nothing new about that, to be fair. Everybody does it. I mean, we sell engines to a lot of people who do exchanges.

Q - Kristine Liwag {BIO 21935865 <GO>}

Great. Well, thank you very much. And great to hear you guys.

A - Peter Juhas {BIO 16582554 <GO>}

Sure.

A - Aengus Kelly {BIO 2460371 <GO>}

Thanks, Kristine.

Operator

We'll take our next question from Anthony Burney with Susquehanna Financial Group.

Q - Anthony Burney {BIO 6355350 <GO>}

Good afternoon. This is Anthony Owen for Chris. Thanks for taking our questions. The adjustments for maintenance rights were a little elevated this quarter relative to recent historicals. I know you mentioned that was due to the timing of lease returns. Should we just treat this as a one-time bump, or do you expect elevated maintenance revenue going forward?

A - Peter Juhas {BIO 16582554 <GO>}

Well, there are two elements of that that I would mention here. So we had higher maintenance revenue this quarter. And I do think that we also had that in the first quarter of the year. And really that has been due to more events happening. These are return of some aircraft from on their existing leases and then going on a new leases. So those some of those were pretty chunky during the quarter.

And so if I look at overall, I'd say, that probably boosted our first half earnings by call it $80 million or so maybe $100 million relative and some of that is really timing. So I think that it's been higher in the first half of the year. Some of that was just brought it just happened to be lumpy there.

The normal run rate normally we would think of like maintenance revenues, less leasing expenses on an adjusted basis of around $30 million to $40 million a quarter. So it's certainly been high the last couple of quarters. But again, that's just timing. And then in terms of the maintenance rights amortization, that has also been high this quarter. And again, that's really driven by events. When the events happen, that amortization is high. So you generally see those things happening in tandem.

Q - Anthony Burney {BIO 6355350 <GO>}

Got it. That's very helpful. Thank you. One more on the adjustment. The leasing expenses were down almost 20% year-over-year and 1Q is down a solid 10% year-over-year as well. Are you doing anything differently to control costs on that line? And should we expect kind of year-over-year declines in the second half as well?

A - Peter Juhas {BIO 16582554 <GO>}

Well, we are, , that is one of the areas that we've highlighted before in terms of when we are able to use some of our existing spare engines to avoid engine swaps, right? So you put an engine in, swap it in and avoid engine overhauls and other costs. That's the way to drive down those leasing expenses. And I'd say that is one of the things that from a strategic standpoint is a key benefit of having the engine leasing business, because obviously we've got a much bigger pool of engines that you can utilize for that purpose.

Q - Anthony Burney {BIO 6355350 <GO>}

Great. Thank you so much.

A - Aengus Kelly {BIO 2460371 <GO>}

Sure.

Operator

We'll take our next question from Mariana Perez Mora with Bank of America.

Q - Mariana Perez Mora {BIO 16856823 <GO>}

Good morning, everyone. So I'm going to tap again on the U.S. airline's weakness and them trying to actually retire at this unprofitable capacity, but also recovery to the global traffic. Can you give us some color around like how these rates look like today versus a year ago for like the different assets like engines and particularly the current generation aircraft where you have like an average of what, like 15 years old average? However, what type of rates are you seeing there versus a year ago?

A - Aengus Kelly {BIO 2460371 <GO>}

Well, you're certainly continuing to see increases there. And we laid a lot of that out in the charts on our Capital Markets Day where you could see the material increases that we've seen over the last few years across the Board. And that continues to be the case. The real driver of that for those 15 to 20 year old assets is what we've just been speaking about in my mind is, why are airlines willing to pay so much because they have, it's cheaper to do that than have a shop visit on an engine.

There's no point paying, as I said, $10 million to overhaul a 7B engine if you need the aircraft and the engine for the next four or five years, not the next 10 years, which is what you'd need to recover that type of investment. And you'd probably have to overhaul the cabin as well, to be honest, if you're going to try and keep that airplane flying for another 10 years. So to me, that's what I see as a big driver. And that's -- and it's likely to stay that way, as I've said before, till the end of the decade, because it will take time for the ramp-up to occur on the new technology assets.

Q - Mariana Perez Mora {BIO 16856823 <GO>}

If we were to see this, I'll say like slow down on how strong is the demand, and it's mostly about replacement going forward, how do you manage what you sell versus what you actually extend the lease on for these like older aircraft particularly, not just engines?

A - Aengus Kelly {BIO 2460371 <GO>}

Well, it depends on how we view the assets. Is it an asset that we would like to be out of? And then we'll be more inclined to sell the asset. But I think you can see through our behavior over the last, must be now nearly 18 years, 20 years, public company, that the average age of the assets we sell has always been towards on an average base around 15 year mark, which is what we sell. So because we do feel that at some point, even though the values are very strong today, as we get to the end of the decade, those values are likely to decline.

And again, that's why we've shown you our strategy in several Investor Day presentations, the sunset strategy of how the portfolio is created. We often say to you that people should never look at the average age of a portfolio of a leasing company. It's utterly meaningless. The key is to look at the average age of the components of the business. If you have a young fleet of 777s or 737s, you will lose money because those planes will not be flying in 2035, 2038. And if you bought them in 2015, that's what you need to happen.

And at AerCap, you could see, we've had a tremendous discipline in that regard over the last 12 years, never ordering those type of aircraft. And we have been exiting that type. And you can see that in the charts that we provided as well on the Investor Day.

Q - Mariana Perez Mora {BIO 16856823 <GO>}

Thank you. And last one from me. If you were to see more opportunities like the one with Spirit Airlines, where you can actually get orders of new aircraft in the near term, like, I imagine, like, you have, how do you manage your strong balance sheet? And how much are you willing to lever upon, like actually taking the opportunity of this environment, if it were to happen?

A - Aengus Kelly {BIO 2460371 <GO>}

Well, I think, look, we have plenty of capacity on our balance sheet to take advantage of any opportunity that comes in. I'm not concerned about that. It's just having the discipline to pick the right opportunities. We're looking at many different asset acquisition opportunities on a daily basis, but we hit very few of them. The ones we've managed to do are ones where we've worked on a bilateral basis with a partner, a customer who's been a partner for a long time, and tried to do something that works for them and for AerCap.

Operator

This concludes the question-and-answer session. I would like to hand the call back over to Aengus Kelly for any final remarks.

A - Aengus Kelly {BIO 2460371 <GO>}

Well, look, thank you all for joining us today on the call. We look forward to giving an update in three months time. Thank you.

Operator

This does conclude today's conference call. You may now disconnect.