



Rating  
**Buy**

North America  
United States

Industrials  
Aircraft Leasing

Company  
**FLY Leasing Limited**

Reuters  
FLY.N

Bloomberg  
FLY US

Exchange  
NYS

Ticker  
FLY

Date  
23 August 2018

Results

Price at 23 Aug 2018 (USD)	14.75
Price Target	18.00
52-week range	14.87 - 11.62

## Solid June Q; AirAsia deal to stimulate LT earnings growth

### Solid June Q; AirAsia deal to stimulate LT organic earnings growth potential

FLY Leasing reported adjusted diluted EPS of \$0.90 for the June quarter, ahead of our \$0.45 estimate and consensus of \$0.74. The beat was driven by higher operating lease income, gains on trading and namely end of lease income, where FLY was able to maximize its economic gain by accepting cash compensation and capturing the full value of the maintenance reserve at the end of leases. Following commendable June Q results - which saw the stock trade up ~6% today - we shift our focus to the AirAsia transaction. We believe the transaction marks an inflection point for FLY as it helps to stimulate an organic pipeline for long-term earnings expansion through the acquisition of a highly valuable order book of in-demand, new technology A320neo aircraft, which are to be delivered from 2019 onwards. Given that we expect the company's fleet transition to drive earnings growth with a de-risked portfolio of aircraft, we reiterate our Buy rating.

### Conference call highlights

- In February, FLY entered a definitive agreement to acquire 54 Airbus narrowbody aircraft - including 34 A320ceo aircraft in the initial stage of the transaction and an additional 21 A320neo family aircraft which will be delivered new from the OEM between 2019-2021, and 7 CFM engines - from companies falling under the AirAsia Group umbrella. In addition, FLY acquired the rights to purchase 20 additional A320neo family aircraft (not subject to lease) directly from Airbus. In order to facilitate the AirAsia transaction, FLY has undertaken a number of financing initiatives, which includes a 1.3 million share issuance (at \$15 per share) to Onyx Corporation and the management of BBAM, as well as entering into a \$575 million term loan facility (from which it has drawn ~\$213 million thus far). FLY stressed that as a result of the transaction near term leverage (on a gross debt/equity basis) increases to ~4.7x on a temporary basis, although it anticipates delevering to 4.3x within a year and to 3.5x within three years.
- In an attempt to manage exposure to AirAsia, management had highlighted plans to divest ~\$150 million of assets in 2018, and plans to divest an additional \$150 million of assets related to AirAsia in 2019. FLY's divestiture strategy will focus on mid-life A320ceo family aircraft, which are 2006-2013 vintage. Further, FLY stated that at this time it will not look to divest any of its A320neo family aircraft. As a frame of reference,

### Valuation & Risks

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### Key changes

EPS (USD)	2.40 to 2.35	↓	-2.1%
Revenue (USDm)	385 to 403	↑	4.9%

Source: Deutsche Bank

### Price/price relative



Performance (%)	1m	3m	12m
Absolute	6.4	0.0	12.2
S&P 500 INDEX	2.0	4.7	17.1

Source: Deutsche Bank

### Stock option liquidity data

Market Cap (USD)	434.9
Shares outstanding (m)	29.5
Free float (%)	100
Volume (23 Aug 2018)	136,576
Option volume (und. shrs., 1M avg.)	-

Source: Deutsche Bank

23 August 2018  
Aircraft Leasing  
FLY Leasing Limited



assuming that no aircraft were to be divested following the transaction, FLY's exposure to AirAsia would be ~24%.

- With respect to heightening geopolitical concerns, FLY cited two specific areas of concern - Turkey and India, both on FX. However, FLY emphasized that its exposure to these markets is limited given it only had four aircraft in Turkey, of which one is already in-transition and a second is being re-marketed, also noting optimism about a longer term recovery in Turkey as it has been one of the more active participants in the aircraft leasing market over the last ten years. Meanwhile in India, FLY noted that aircraft on lease with Air India are backed by a government guarantee, while Jet Airways has not taken any action to restructure lease agreements thus far. Globally, demand for air travel remains strong and management emphasized they continue to see above average traffic growth worldwide - including in Europe and North America - and that they have not seen any material shifts to demand trends thus far, as a result of oil or other geopolitical factors.
- With respect to guidance, FLY reiterated its FY 2018 pre-tax income target range of \$75-\$80 million. In addition, FLY indicated it has closed on the acquisition of 13 aircraft (out of 34 to be acquired in conjunction with the AirAsia transaction) in the June Q and plans to complete the transfer of the remaining A320ceo family aircraft and 7 CFM engines by the end of the Sep Q.

#### Adjusting our 2018 outlook to account for the AirAsia transaction

We are lowering our 2018 EPS estimate from \$2.40 to \$2.35 (versus consensus of \$2.22) as we incorporate the June Q beat and account for additional interest expense and equity dilution as a result of the AirAsia transaction. However, we are maintaining our 2019 EPS estimate of \$3.00 (versus consensus of \$2.48), and our 2020 EPS estimate of \$3.40 (versus consensus of \$2.70).

#### Valuation and risks

We are maintaining our 12-month price target of \$18. We applied a ~1.0 P/B multiple (in-line with historical trading range) to arrive at our PT (versus its current 40% discount). A key risk for FLY is that FX volatility could become more widespread as trade disputes become more protracted and may result in a slowing of economic growth. See the next page for more valuation and risks.

23 August 2018

Aircraft Leasing

FLY Leasing Limited



# Company Outlook

## [Adjusting our 2018 outlook to account for the AirAsia transaction](#)

We are lowering our 2018 EPS estimate from \$2.40 to \$2.35 (versus consensus of \$2.22) as we incorporate the June Q beat and account for additional interest expense and equity dilution as a result of the AirAsia transaction. However, we are maintaining our 2019 EPS estimate of \$3.00 (versus consensus of \$2.48), and our 2020 EPS estimate of \$3.40 (versus consensus of \$2.70).

*For more details on the drivers behind our forecasts, see FLY's actual and projected income statement in Figure 1.*

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## Valuation and risks

We are maintaining our 12-month price target on FLY shares of \$18. We view FLY as a deep-value play on the sector as its valuation based on P/E and price to book (P/B) are both trading at attractive levels relative to peers and historical ranges. We applied slightly less than a 1.0 price to book multiple to arrive at our \$18 price target (versus its current 40% discount). Our price target implies a P/E multiple of 7.5x our 2018 EPS forecast.

A key risk for FLY is that FX volatility could become more widespread as trade disputes become more protracted and may result in a slowing of economic growth. That in turn would very likely mean reduced demand for aircraft potentially weighing on aircraft values and lease rates. Additionally, FLY has exposure to emerging markets, which have been a major source of growth in air travel. A slowing of the global economy could put pressure on those economies, and thereby adversely impact lessee airlines from those countries. Another risk is oversupply of aircraft negatively impacting values and lease rates, thereby putting downward pressure on FLY's asset values as well as future earnings power of its asset base. Furthermore, a change in depreciation/useful life assumptions or impairment charges on FLY's fleet could materially alter its return profile. Another risk is the company's small float.

Figure 1: FLY Leasing Limited Actual and Projected Income Statement

	2016		2017								2018				2018E				2019E					
	YEAR	% CHG	1ST Q	% CHG	2ND Q	% CHG	3RD Q	% CHG	4TH Q	% CHG	YEAR	% CHG	1ST Q	% CHG	2ND Q	% CHG	3RD Q	% CHG	4TH Q	% CHG	YEAR	% CHG	YEAR	% CHG
REVENUE:																								
Operating Lease Revenue	\$314	-28.9%	\$79	5.0%	\$79	3.8%	\$86	6.0%	\$103	26.7%	\$347	10.6%	\$87	10.6%	\$99	25.4%	\$98	14.0%	\$108	4.0%	\$391	12.8%	\$426	8.9%
Sales Revenue	27	1.4%	0	NM	0	NM	0	NM	4	NM	4	NM	0	NM	3	NM	2	NM	1	NM	6	56.7%	2	-60.1%
Interest Revenue	2	-23.9%	0	NM	0	NM	0	-19.9%	0	NM	1	-41.1%	1	NM	1	NM	1	NM	1	NM	4	NM	4	11.6%
Other Revenue	3	NM	0	-69.5%	0	-69.3%	0	66.3%	0	55.8%	1	-44.3%	0	-8.6%	(0)	NM	1	NM	1	NM	2	60.6%	3	13.3%
Non-Recurring	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM
TOTAL REVENUE:	345	-26.9%	79	-2.4%	80	2.4%	86	1.1%	108	7.3%	353	2.4%	89	12.0%	103	28.6%	101	17.5%	111	2.6%	403	14.2%	435	7.9%
OPERATING EXPENSES:																								
SG&A	30	-10.3%	8	0.3%	8	8.0%	7	-16.9%	7	23.0%	31	2.0%	9	3.8%	6	-20.2%	9	22.7%	11	44.4%	34	11.7%	43	24.4%
Depreciation	120	-26.2%	32	11.1%	33	15.4%	34	8.8%	34	7.6%	133	10.6%	34	5.2%	34	2.5%	37	7.6%	41	20.7%	145	9.1%	157	8.2%
Other Expenses	1	NM	0	-60.6%	1	NM	0	NM	1	NM	2	NM	1	64.8%	1	23.5%	1	NM	1	21.1%	4	55.7%	4	7.6%
Non-Recurring	97	35.1%	0	NM	0	NM	22	NM	0	NM	22	NM	0	NM	0	NM	0	NM	0	NM	0	NM	0	NM
TOTAL OPERATING EXPENSES:	249	-9.5%	41	6.5%	42	2.9%	64	58.6%	42	-67.4%	189	-24.3%	43	5.6%	41	-1.5%	46	-27.2%	53	24.5%	183	-2.7%	204	11.2%
OPER. INCOME (Margins in Box):	96	27.8%	38	48.5%	38	47.6%	23	26.3%	66	60.7%	165	46.6%	46	51.4%	61	59.9%	55	54.4%	58	52.3%	220	54.5%	231	53.2%
Op. Income Excl. Non-Recurring	193	56.0%	38	48.5%	38	47.6%	45	52.0%	66	60.8%	187	52.9%	46	51.4%	61	59.9%	55	54.4%	58	52.3%	220	54.5%	231	53.2%
OTHER INCOME (EXPENSE):																								
Other	4		6		0		(0)		0		5		74.074		2		0		0		2		10	
Interest Expense*	(121)	-7.7%	(32)	3.2%	(27)	-6.1%	(30)	6.6%	(28)	-16.5%	(117)	-3.6%	(33)	3.4%	(32)	18.2%	(36)	20.3%	(40)	45.8%	(141)	21.3%	(139)	-2.1%
Non-Recurring	(7)		(6)	-33.1%	(7)	NM	(5)		(24)		(42)		(3)	-54.4%	(1)	NM	0		0		(4)		0	
TOTAL OTHER INCOME:	(124)		(32)		(34)		(35)		(52)		(153)		(34)		(33)		(36)		(40)		(143)		(129)	
PRETAX INCOME (Margins in Box):	(28)	-8.0%	6	7.7%	4	4.8%	(12)	-14.5%	14	12.9%	11	3.2%	12	13.4%	28	27.5%	19	18.9%	18	15.9%	77	19.1%	103	23.6%
P-T Income Excl. Non-Recurring	76	22.1%	12	15.4%	11	13.3%	15	17.3%	38	35.2%	76	21.4%	15	16.5%	29	28.4%	19	18.9%	18	15.9%	81	20.0%	103	23.6%
INCOME TAXES (CREDIT):																								
Tax Rate	-5.9%		17.5%		24.7%		-0.1%		49.3%		78.2%		19.2%		13.8%		14.0%		14.0%		14.7%		14.0%	
NI of Investments and Other Gains / (Losses):	0		0		0		0		0		0		0		0		0		0		0		0	
NET INCOME TO COMMON S/HS:	(29)		\$5		\$3		(\$13)		\$7		\$2		\$10		\$24		\$16		\$15		\$66		\$89	
PRO FORMA NI TO COMMON S/HS:*	\$79	22.9%	\$11	14.0%	\$10	12.2%	\$15	17.3%	\$31	28.9%	\$67	18.9%	\$12	14.0%	\$25	24.6%	\$16	16.3%	\$15	13.7%	\$69	17.2%	\$89	20.3%
Shares Outstanding - Basic	33		32		31		29		28		30		28		28		30		32		29		30	
Shares Outstanding - Diluted	33		32		31		29		28		30		28		28		30		32		30		30	
GAAP EPS - Basic	(\$0.88)		\$0.16		\$0.09		(\$0.43)		\$0.25		\$0.08		\$0.34		\$0.87		\$0.55		\$0.47		\$2.23		\$2.95	
GAAP EPS - Diluted	(\$0.88)		\$0.16		\$0.09		(\$0.43)		\$0.25		\$0.08		\$0.34		\$0.87		\$0.55		\$0.47		\$2.22		\$3.00	
Pro Forma EPS - Diluted	\$2.38		\$0.34		\$0.31		\$0.51		\$1.09		\$2.19		\$0.44		\$0.90		\$0.55		\$0.47		\$2.35		\$3.00	
Dividends Paid	\$0.0		\$0.0		\$0.0		\$0.0		\$0.0		\$0.0		\$0.0		\$0.0		\$0.0		\$0.0		\$0.0		\$0.0	
Dividend per ADS	\$0.00		\$0.00		\$0.00		\$0.00		\$0.00		\$0.00		\$0.00		\$0.00		\$0.00		\$0.00		\$0.00		\$0.00	
EBIT & EBITDA Reconciliation:																								
Net Income (loss)	(\$29)		\$5		\$3		(\$13)		\$7		\$2		\$10		\$24		\$16		\$15		\$66		\$89	
Depreciation & Amortization	141		37		37		38		38		150		38		39		37		41		155		157	
Interest on Debt	121		32		27		30		28		117		33		32		36		40		141		139	
Provision for Income Taxes	(9)		1		1		2		1		5		2		4		3		2		11		14	
Other Non-Cash Charges	(27)		(0)		0		4		(4)		(4)		(4)		(4)		(2)		(1)		(6)		(2)	
EBITDA (EBITDA Margin in Box)	\$196	56.9%	\$74	93.7%	\$69	86.1%	\$62	72.1%	\$69	64.2%	\$270	76.6%	\$85	95.3%	\$95	92.5%	\$90	88.6%	\$98	88.3%	\$367	91.0%	\$396	91.0%

Source: Company filings and Deutsche Bank Research.



23 August 2018

Aircraft Leasing

FLY Leasing Limited



# Appendix 1

## Important Disclosures

\*Other information available upon request

Disclosure checklist			
Company	Ticker	Recent price*	Disclosure
FLY Leasing Limited	FLY.N	14.75 (USD) 23 Aug 2018	8, 14, 15

\*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Other information is sourced from Deutsche Bank, subject companies, and other sources. For disclosures pertaining to recommendations or estimates made on securities other than the primary subject of this research, please see the most recently published company report or visit our global disclosure look-up page on our website at <https://research.db.com/Research/Disclosures/CompanySearch>. Aside from within this report, important risk and conflict disclosures can also be found at <https://research.db.com/Research/Topics/Equities?topicId=RB0002>. Investors are strongly encouraged to review this information before investing.

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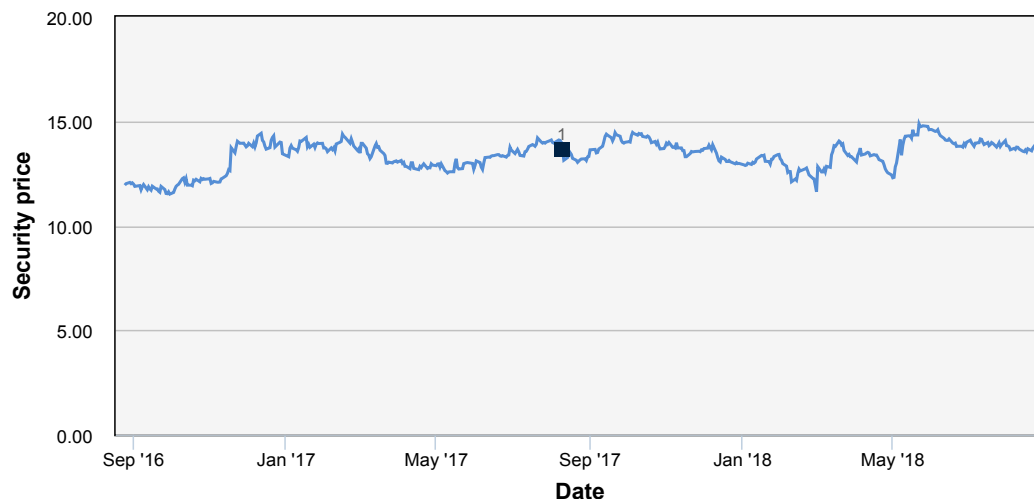
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23 August 2018  
Aircraft Leasing  
FLY Leasing Limited



## Historical recommendations and target price. FLY Leasing Limited (FLY.N)

(as of 08/23/2018)



### Current Recommendations

Buy  
Hold  
Sell  
Not Rated  
Suspended Rating

\*\* Analyst is no longer at Deutsche Bank

1. 08/10/2017 Buy, Target Price Change USD 18.00 Catherine O-Brien\*\*

## Equity Rating Key

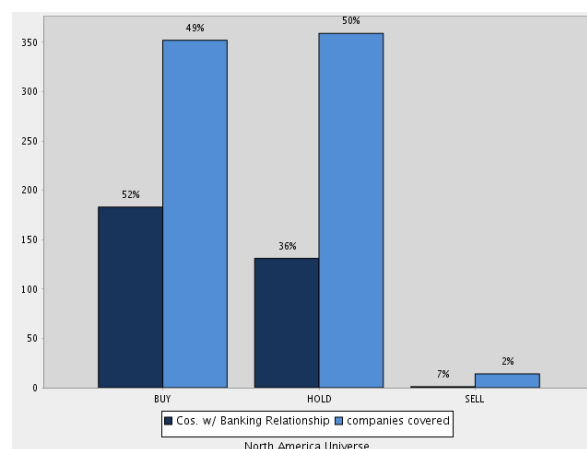
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**Sell:** Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock.

**Hold:** We take a neutral view on the stock 12-months out and, based on this time horizon, do not recommend either a Buy or Sell.

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## Equity rating dispersion and banking relationships



23 August 2018

Aircraft Leasing

FLY Leasing Limited



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23 August 2018  
Aircraft Leasing  
FLY Leasing Limited



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23 August 2018

Aircraft Leasing

FLY Leasing Limited



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23 August 2018  
Aircraft Leasing  
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