

## RATING ACTION COMMENTARY

# Fitch Affirms SMBC Aviation Capital at 'BBB+'; Outlook Stable

Fri 16 Jun, 2023 - 15:18 ET

Fitch Ratings - Chicago - 16 Jun 2023: Fitch Ratings has affirmed SMBC Aviation Capital Limited's (SMBC AC) and SMBC Aviation Capital Finance DAC's Long-Term Issuer Default Ratings (IDRs) at 'BBB+' and its Shareholder Support Rating (SSR) of 'bbb+'. Fitch has also affirmed SMBC Aviation Capital Finance DAC's senior unsecured debt at 'BBB+'. The Rating Outlook is Stable.

These rating actions are being taken in conjunction with a global aircraft leasing sector review, covering 10 publicly rated companies (for more information on the sector review, see 'Fitch Ratings Completes Aircraft Lessor Peer Review, Sector Outlook Remains Neutral', available at [www.fitchratings.com](http://www.fitchratings.com)).

## KEY RATING DRIVERS

**IDR Driven by Support:** The rating affirmation primarily reflects Fitch's expectation of continuing support, in case of need, for SMBC AC from Sumitomo Mitsui Financial Group, Inc. (SMFG; A-/Stable), which has a 66% beneficial ownership of SMBC AC. Fitch views SMBC AC as a strategically important (but not core) subsidiary of the group and rates it one notch below SMFG's Long-Term IDR. The Stable Outlook is aligned with the Outlook of SMFG, reflecting Fitch's expectation that the companies' ratings would move in tandem.

**Sound Standalone Credit Profile:** SMBC AC's standalone creditworthiness is supported by its leading market position in global aircraft leasing, a young and liquid fleet and good access to market funding. These strengths are counterbalanced by the monoline nature of the business, vulnerability to exogenous shocks, exposure to residual-value risk, high leverage, and dependence on wholesale funding sources. SMBC AC's creditworthiness is also susceptible to the continuing post-pandemic recovery of the global commercial aviation industry.

**Strong Franchise:** At end-1Q 2023 SMBC AC's fleet included 497 owned aircraft (with book value of USD 22 billion) and 208 managed aircraft. The company's order book

included 189 committed aircraft amounting to USD10 billion to be delivered during 2023- 2027. Fitch believes that SMBC AC's scale provides the company with greater purchasing and negotiating power, diversification benefits and broader re-leasing options compared to smaller peers.

**Low Risks Assets:** SMBC AC's fleet composition is among the most liquid in the peer group with a young and predominantly narrow-body aircraft with a high share of new-tech aircraft. Post-Goshawk acquisition the company improved the already good diversification of its lessee base by airline and geography.

**Recovering Profitability:** SMBC reported improved profitability in FYE1Q23, recovering over half of the capital erosion in the previous year. Yet performance (as measured by pre-tax income/ average assets) remains below pre-pandemic levels. We expect an improvement in operating performance stemming primarily from continuing recovery of lease yields but also supported by stronger gains on aircraft sales in 2023-2024, modestly offset by higher funding costs in the current environment.

**High Leverage:** SMBC AC's gross debt-to-tangible equity ratio (with a USD300 million subordinated loan included in tangible equity) at 4.0x at end-1Q 2023 was notably above the peer average. SMBC group injected USD1.4 billion capital in 2022 to finance the acquisition of Goshawk Aviation Limited which underpinned capital adequacy. We expect SMBC AC to pursue growth in 2023-2024, and thus a further leverage decrease would be conditional on enhancing profitability. SMBC AC has stated that it plans to adhere to its no dividend policy in the foreseeable future, which helps capital generation.

**Wholesale Funding Backed by Parent:** SMBC AC relies on a number of funding sources but has maintained uninterrupted access to both parental and external funding under various market conditions. Parental funding (USD8 billion) represented 44% of total debt at end-1Q 2023. All of SMBC AC's debt is unsecured, except for financial lease liabilities, which are negligible. SMBC AC's liquidity standing benefits robust available sources of USD9 billion and staggered repayment profile.

**Strategically Important for Group:** Fitch's view of SMFG's propensity to support SMBC AC considers the subsidiary's record of profitability, an integrated strategy, funding from SMFG, common branding, and parent company representation on the subsidiary's board of directors. Fitch believes that SMBC AC remains an important part of SMFG's product origination-and-distribution business strategy, despite the subsidiary operating in a different jurisdiction and its small size relative to SMFG.

## **RATING SENSITIVITIES**

## **Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade**

-A downgrade of SMFG's Long-Term IDR would lead to a downgrade of SMBC AC's, reflecting a weakening ability to provide support;

-A material weakening of SMFG's propensity to support SMBC AC, for example, due to decreasing integration or diminishing strategic importance of SMBC AC, may result in a widening of the rating differential;

-Although not expected by Fitch, SMBC AC's ratings could be adversely affected should SMFG seek to dispose of, or reduce its equity stake in SMBC AC, resulting in significant influence by minority shareholders, or by any other developments within SMFG that Fitch perceives as adversely altering its willingness or ability to provide support to SMBC AC;

-Negative rating action could also occur if SMBC AC's operating performance deteriorates significantly, thereby not delivering the return on investment envisaged by SMFG. This could adversely affect Fitch's assessment of the propensity of SMFG to provide support to SMBC AC, in case of need.

## **Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade**

-An upgrade of SMFG's Long-Term IDR would lead to an upgrade of SMBC AC's, reflecting an increased ability to support;

-Closer integration within and increased importance of SMBC AC to SMFG could lead to an equalisation of the ratings.

## **DEBT AND OTHER INSTRUMENT RATINGS: RATING SENSITIVITIES**

SMBC Aviation Capital Finance DAC's IDR is equalised with SMBC AC's, reflecting the full and unconditional guarantee of SMBC Aviation Capital Finance DAC's obligations by SMBC AC.

The senior unsecured note rating is equalised with SMBC AC's Long-Term IDR, reflecting Fitch's expectation of average recovery prospects given that the majority of the company's consolidated debt is unsecured.

The rating on the senior unsecured notes is sensitive to changes in SMBC AC's IDR and the level of unencumbered balance-sheet assets available in a stress scenario, relative to outstanding unsecured debt. A decline in the level of unencumbered asset coverage

combined with a material increase in the use of secured debt could result in the unsecured debt being notched down from the IDR.

## BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

## REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

## PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

SMBC AC's IDR is based on support from SMBC group.

## ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg)

## RATING ACTIONS

| ENTITY / DEBT ⚡               | RATING ⚡   | PRIOR ⚡                    |
|-------------------------------|--|----------------------------|
| SMBC Aviation Capital Limited | LT IDR    BBB+ Rating Outlook Stable<br>Affirmed | BBB+ Rating Outlook Stable |

Shareholder Support    bbb+    Affirmed    bbb+

---

SMBC Aviation Capital  
Finance DAC    LT IDR    BBB+ Rating Outlook Stable    BBB+ Rating  
Outlook  
Stable  
Affirmed

---

senior unsecured    LT    BBB+    Affirmed    BBB+

---

[VIEW ADDITIONAL RATING DETAILS](#)

**FITCH RATINGS ANALYSTS**

**Johann Juan**

Senior Director

Primary Rating Analyst

+1 312 368 3339

johann.juan@fitchratings.com

Fitch Ratings, Inc.

One North Wacker Drive Chicago, IL 60606

**Aslan Tavitov**

Senior Director

Secondary Rating Analyst

+44 20 3530 1788

aslan.tavitov@fitchratings.com

**Dafina Dunmore**

Senior Director

Committee Chairperson

+1 312 368 3136

dafina.dunmore@fitchratings.com

**MEDIA CONTACTS**

**Anne Wilhelm**

New York

+1 212 908 0530

anne.wilhelm@thefitchgroup.com

**Sandro Scenga**

New York

+1 212 908 0278

sandro.scenga@thefitchgroup.com

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

## **PARTICIPATION STATUS**

The rated entity (and/or its agents) or, in the case of structured finance, one or more of the transaction parties participated in the rating process except that the following issuer(s), if any, did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure.

## **APPLICABLE CRITERIA**

[Non-Bank Financial Institutions Rating Criteria - Effective from 5 May 2023 to 17 January 2024 \(pub. 05 May 2023\) \(including rating assumption sensitivity\)](#)

## **ADDITIONAL DISCLOSURES**

[Dodd-Frank Rating Information Disclosure Form](#)

[Solicitation Status](#)

[Endorsement Policy](#)

## **ENDORSEMENT STATUS**

SMBC Aviation Capital Finance DAC

EU Endorsed, UK Endorsed

SMBC Aviation Capital Limited

EU Endorsed, UK Endorsed

## **DISCLAIMER & DISCLOSURES**

All Fitch Ratings (Fitch) credit ratings are subject to certain limitations and disclaimers.

Please read these limitations and disclaimers by following this link:

<https://www.fitchratings.com/understandingcreditratings>. In addition, the following <https://www.fitchratings.com/rating-definitions-document> details Fitch's rating definitions for each rating scale and rating categories, including definitions relating to default. ESMA and the FCA are required to publish historical default rates in a central repository in accordance with Articles 11(2) of Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 and The Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019 respectively.

Published ratings, criteria, and methodologies are available from this site at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance, and other relevant policies and procedures are also available from the Code of Conduct

section of this site. Directors and shareholders' relevant interests are available at <https://www.fitchratings.com/site/regulatory>. Fitch may have provided another permissible or ancillary service to the rated entity or its related third parties. Details of permissible or ancillary service(s) for which the lead analyst is based in an ESMA- or FCA-registered Fitch Ratings company (or branch of such a company) can be found on the entity summary page for this issuer on the Fitch Ratings website.

In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously

evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001. Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.



dv01, a Fitch Solutions company, and an affiliate of Fitch Ratings, may from time to time serve as loan data agent on certain structured finance transactions rated by Fitch Ratings.

Copyright © 2023 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved.

[READ LESS](#)

## **SOLICITATION STATUS**

The ratings above were solicited and assigned or maintained by Fitch at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

## **ENDORSEMENT POLICY**

Fitch's international credit ratings produced outside the EU or the UK, as the case may be, are endorsed for use by regulated entities within the EU or the UK, respectively, for regulatory purposes, pursuant to the terms of the EU CRA Regulation or the UK Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019, as the case may be.

Fitch's approach to endorsement in the EU and the UK can be found on Fitch's [Regulatory Affairs](#) page on Fitch's website. The endorsement status of international credit ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.