MonteCristoAir

Department Primer for: Finance

At MonteCristoAir, the Finance Department includes the following functions:

- Treasury
- Financial Planning / Analysis
- Revenue Accounting

Responsibilities include:

- Measuring and monitoring of airline financial performance, including financial statement preparation and analysis
- Business case preparation for acquisition of capital (including lease versus buy and financing)
- Development and monitoring of productivity and cost reduction initiatives

<u>Departmental Perspective on the Challenges and Opportunities</u>

We believe things are not as bad as some people in this company think they are. It's true we struggled in the early years after de-regulation and the economic downturn hurt us like everyone else. We managed to stay in the black most of the time, even if our margins were small. Despite the recent price wars which admittedly hurt us, MonteCristoAir has demonstrated improved profitability recently and now maintains a solid financial position. As MonteCristoAir's original airline, we shouldn't try to be like the new carriers anyhow. We should build upon our legacy and position ourselves as the State flag carrier. People are patriotic here—they'll fly us.

Let's also remember that we have a good relationship with our leasing company. Leasing has been and will continue to be the simplest and most flexible method of getting airplanes. While we have an aging fleet, it has been well maintained and we can take our time phasing in new aircraft. New aircraft acquisitions will strain our financial situation. However, we will evaluate direct purchase with debt financing as well as leasing. Preliminary discussions with financial institutions indicate that debt financing could be for 12 years at fair market rates. Alternatively, leases are at about 1% of net price per month.

We should not rush to change everything all at once. Instead we need to carefully and methodically manage our growth.

<u>Specific Departmental Assignment:</u>

In addition to the items stated in the MonteCristoAir overview, by the end of the training program you should also incorporate ideas into the final presentation to address the following:

- What should the Board consider regarding financing options for adding fleet
- How should MonteCristoAir maximize the value of the current fleet

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Senior Management Weekly Meeting

Action Item For: **Finance Department**

Subject: **Ratio Analysis**

We would like the MonteCristoAir Board to better understand what these numbers mean as we plan our future strategy. Please include an explanation in your presentation.

MonteCristoAir Ratio Analysis

	2009	2010	2011	2012	2013	2014
Growth Rates						
Revenue Growth	7.71%	6.36%	10.33%	10.26%	12.71%	8.00%
Capacity Growth (ASKs)	NA	0.00%	0.00%	8.68%	0.00%	0.00%
Asset Growth	3.60%	-1.07%	8.24%	-0.13%	16.19%	21.31%
Profit Margins						
Operating	-3.7%	-0.9%	4.2%	0.0%	6.2%	9.5%
Net Pre-Tax	-5.2%	-1.5%	3.6%	-0.4%	5.8%	9.1%
Net Margin	-5.2%	-1.5%	2.9%	-0.4%	4.6%	7.3%
Yield (c/RPK)	13.80	13.91	14.25	14.59	15.27	15.27
Yield (c/ASK)	7.85	8.35	9.21	9.35	10.53	11.38
Cost (c/ASK)	8.79	9.10	9.54	10.10	10.67	11.12
Load Factor	56.9%	60.0%	64.7%	64.1%	69.0%	74.5%
Leverage						
Debt to Equity	0.34	0.32	0.24	0.20	0.13	0.07
Debt to Equity with Leases	1.28	1.31	1.12	1.25	0.98	0.71
Debt to Capital	25.5%	24.1%	19.4%	17.0%	11.7%	7.0%
Debt to Capital with Leases	56.1%	56.7%	52.8%	55.5%	49.4%	41.6%
Book Assets to Equity	1.78	1.87	1.79	1.83	1.72	1.57

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Coverage						
Times Interest Earned	-2.29	-1.36	6.92	-0.09	14.77	26.03
Cash Flow to Total Debt	-10.8%	19.1%	87.7%	35.8%	227.4%	439.1%
Cash Flow to Total Debt with Leases	-2.9%	4.6%	18.8%	5.9%	30.8%	46.2%
Liquidity						
Days Cash	14.6	19.6	39.6	40.4	67.8	106.0
Activity						
Asset Turns	2.05	2.20	2.24	2.48	2.40	2.14
Return on Investment						
Net Income/Assets	-10.6%	-3.2%	6.4%	-1.1%	11.2%	15.5%
Net Income/Equity	-19.0%	-6.0%	11.5%	-2.0%	19.1%	24.4%

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Internal Company Document

To: Finance Department
Subject: Aircraft Pricing

MonteCristoAir is awaiting proposals from Boeing and Airbus for new aircraft. The catalog prices are listed below, but we hope to get reasonable discounts. Alternatively, we could work with leasing companies and acquire new aircraft through operating leases. Below are the current monthly lease rates we've been offered. Typically, to estimate an aircraft net price from a monthly lease rate, we divide the lease rate by 1% (E.G., $300K/.01=$30M). This should give us a reasonable estimate of what the OEMs may offer us regarding pricing, but of course, in this market, we can't be sure.

Besides picking the right aircraft for our operations, we need to make sure we choose the right method for financing. Use the data from the tables below for our lease versus buy analysis.

MonteCristoAir
Fleet Study Development -- New Single-Aisle Airplanes

Airplane Type	737-700W	737-800W	737-900ERW	A319	A320-200	A321-200
Catalog Price	76	90	95	80	92	111
MonteCristoAir Discount	???	???	???	???	???	???
Monthly Lease Rate ($ in 000s)	300	350	370	300	330	370

Airplane Type	737-7	737-8	737-9	A319NEO	A320NEO	A321-NEO
Catalog Price	87	102	109	89	99	110
MonteCristoAir Discount	???	???	???	???	???	???
Monthly Lease Rate ($ in 000s)	330	380	400	330	360	400

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Fleet Study Development -- New Twin-Aisle Airplanes

Airplane Type	B767-300ER	B787-8	B787-9	B777-200ER	A330-200	A330-300	A350-900
Catalog Price	200	215	252	266	124	217	289
MonteCristoAir Discount	???	???	???	???	???	???	???
Monthly Lease Rate ($ in 000s)	400	1100	1300	700	600	800	1200

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E-mail Message

From: L. Koins, Chief Financial Officer
To: Operations, Finance, and Fleet Evaluation Departments

Subject: Jet Fuel Prices

Team - as you are aware, these past years have brought us both high and volatile jet fuel prices. This means that fuel is now one of our biggest cost items. I believe that the future will see continued fuel price volatility. Therefore, it is critical that fuel costs be controlled, and for us to find some way to reduce the risk of volatility.

We need to improve our fuel burn as well as to keep our jet fuel prices down!

1. Operations Department: please assess our operations and provide your ideas to reduce fuel burn.
2. Finance Department: please provide your recommendations for stabilizing and lowering our jet fuel prices and risk.
3. Fleet Evaluation Department: please evaluate the single-aisle fleet options for the most fuel-efficient products.

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Internal Company Document

To: **Finance Department**

Subject: Aircraft Finance Market

- **Leasing Companies:** Aircraft lessors are expected to support the largest share of deliveries as the higher cost of export credit and limitations in commercial bank debt make leasing a better economical alternative for more airlines. Leasing companies shifted the bulk of their leverage from commercial bank debt to more efficient capital markets funding. This expanded capital markets liquidity is attracting new institutional investors and reducing leasing companies' cost of capital. The sale and lease-back market will remain very competitive for new deliveries, even as many lessors maintain strong order books directly with manufacturers.

- **Capital Markets:** An expanding investor base, a healthy balance between secured and unsecured funding, innovative financing structures, and a growing private placement market are helping to propel the growth of capital markets in aircraft finance. The capital markets are expected to support nearly a third of new deliveries through both secured and unsecured funding. Access to public markets will be limited to airlines with public credit ratings in favorable jurisdictions (e.g. the U.S. or countries that've implemented the Cape Town Treaty) with the private placement market providing access to a broader population of airlines.

- **Commercial Bank Debt:** Secured debt from commercial banks remains a significant source of financing for new airplane deliveries. The rise of new lenders, especially from the U.S. and Australia, along with the continued participation of existing banks, should help maintain balance, diversity and strength in the bank markets. First-tier airlines with strong Balance Sheets will benefit from robust competition among banks with plentiful availability of competitively priced debt. Access to commercial bank debt for comparably weaker airlines will be limited.

- **Export Credit:** Commercial market strength and the higher fees and equity requirements resulting from the 2011 Aircraft Sector Understanding are expected to keep export credit usage at historically low levels. Usage will be limited to airlines emerging markets, with a modest amount of funding for diversification by more established carriers.

- **Manufacturers:** Political uncertainty surrounding export credit continues to drive demand for backstop financing from airframe and engine manufacturers.

- **Country Credit:** The country credit is A.