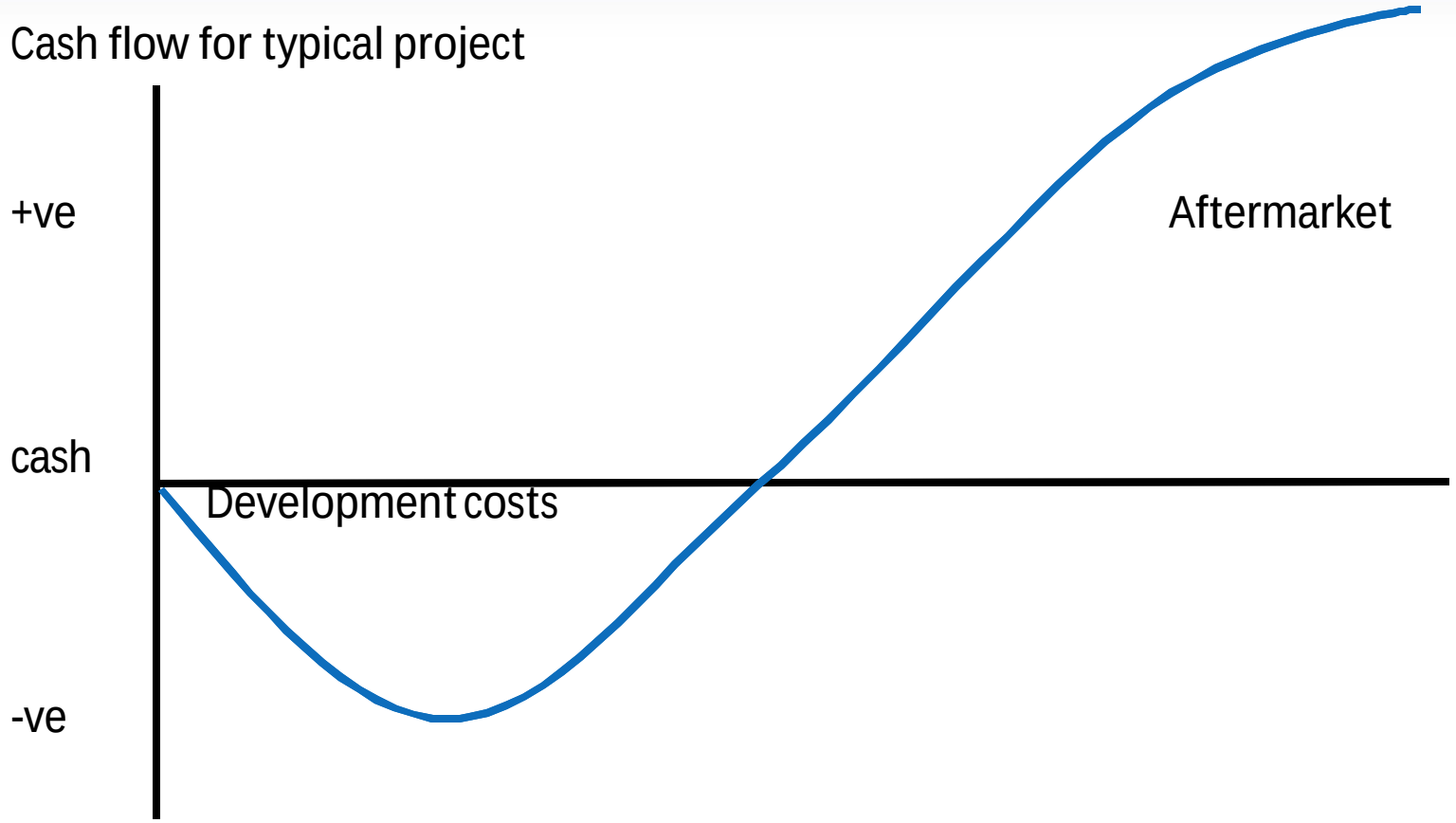
WENCOR GROUP

The Latest OEM DefenseTactics

San Diego- March 22, 2012

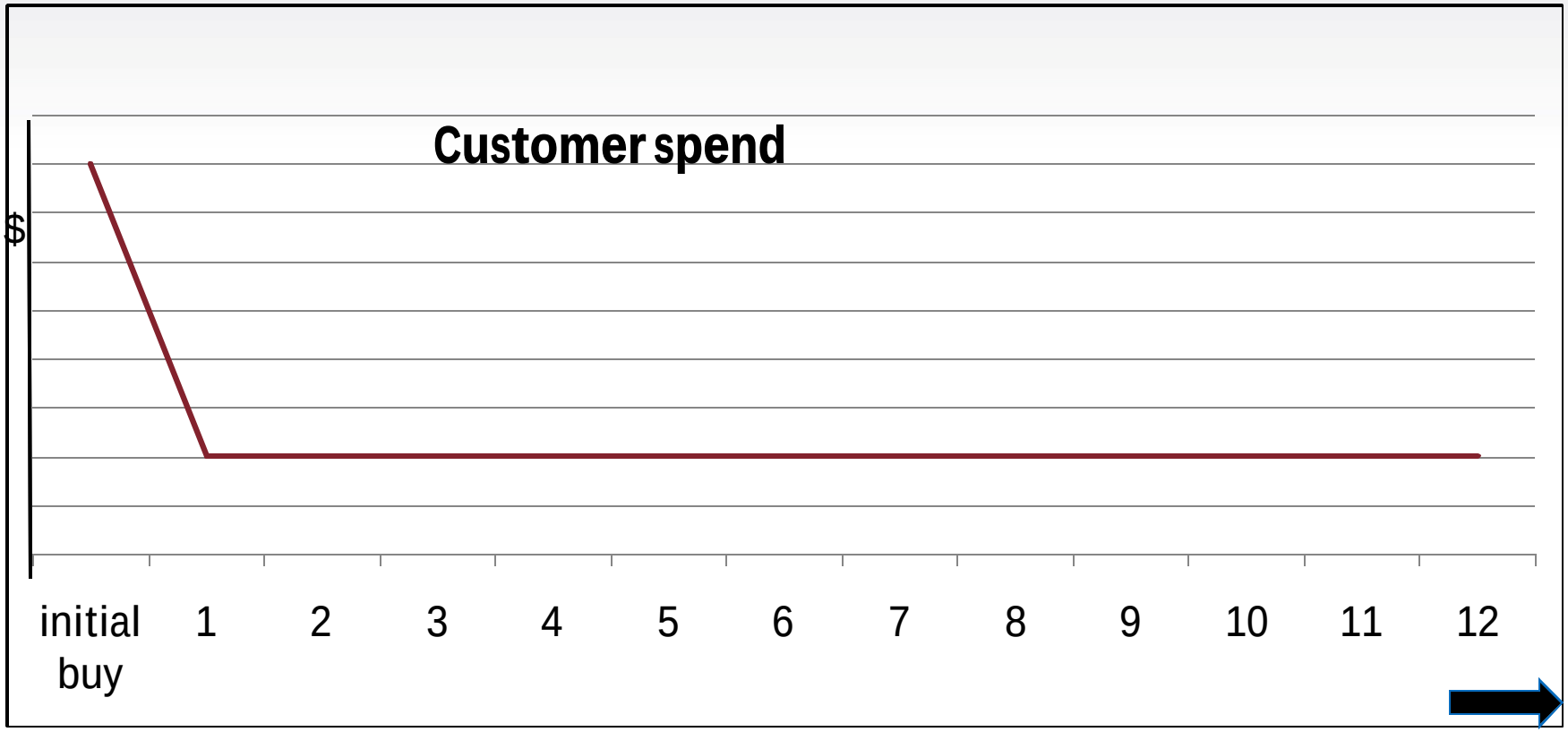
OEMs and the Aftermarket



The OEM Landscape

- B787
  - Total investment to date - $32 billion
  - $15 billion in development costs
  - $16.3 billion to build 40 aircraft
  - Break even 1000+ aircraft
  - Positive cash flow “hoped” for in 2019
- A380
  - Original break even: 250 aircraft
  - Current estimated break even: 420 aircraft

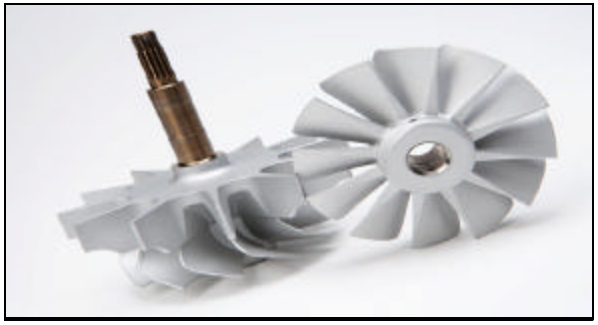
Long Term Maintenance Contracts



- Customer buys insurance - pays fee/flying hour + escalation clause
- Risk of shop visit costs/timing/frequency are borne by OEM
- OEM now incentivised to keep engine on-wing and minimise cost of ownership

Hamilton Sundstrand and the 787

- ECS
- Fire Detection and Suppresion
- NGS
- APU
- EPGSS
- RPDS
- PPDS
- RAT
- EMP
- Trent 1000 Gearbox



JAL/Hamilton Sundstrand care & maintenance contract – 10 years renewable for 10 more: valued at $350 million

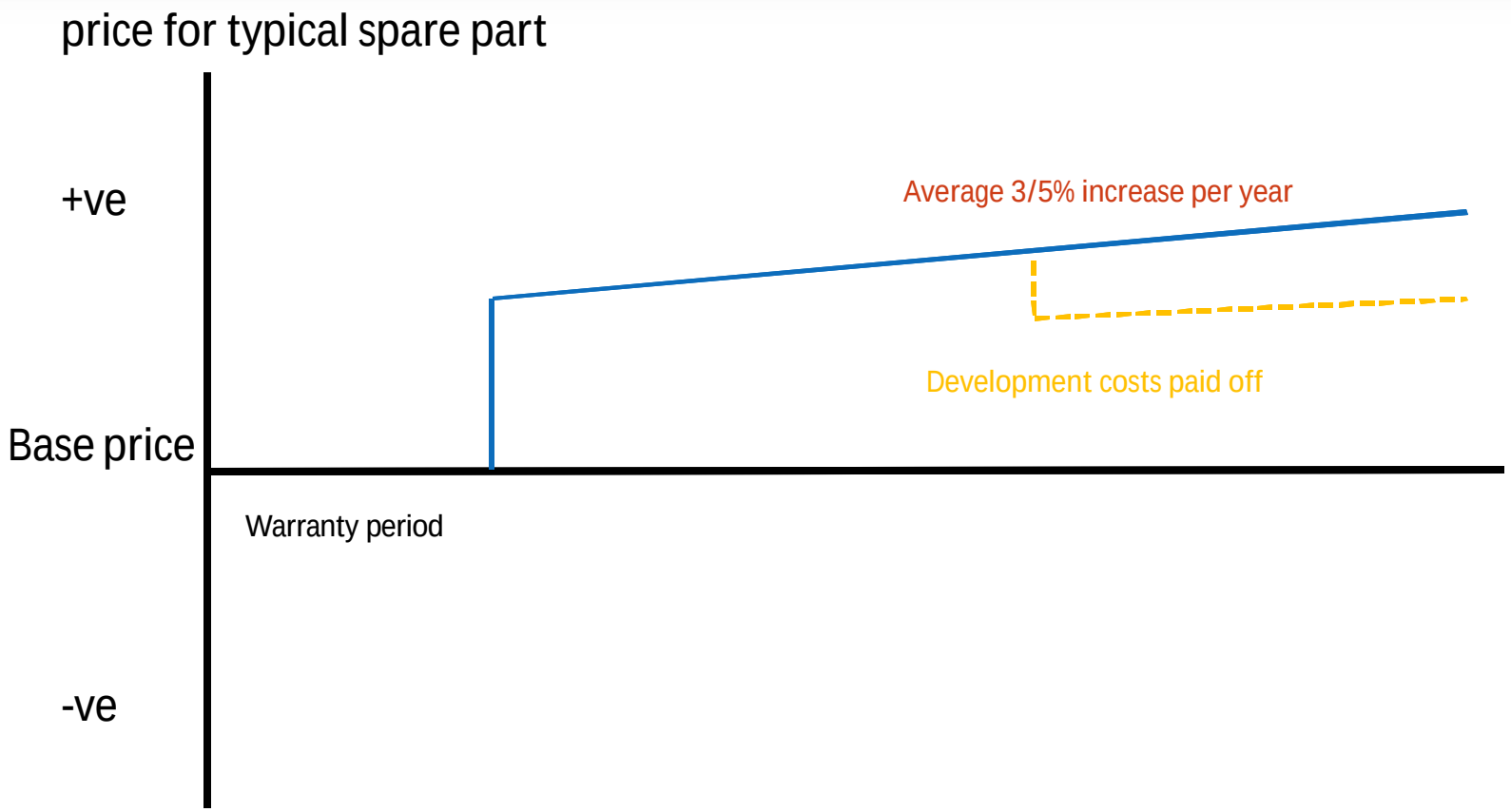
What's the Catch

?

In 10 years time How Will I feel?

- Commitment to the company you already have “issues with”
  - Quality/Availability/Responsiveness
- No alternates, at the will of the OEM
- Increasing availability of PMA re-baselines maintenance costs
- Non OEM DER repairs banned
- Labor rates
- Material rates
- Loss of third party work
- No reward for learning curve improvements
- No incentive on OEM to do better – fixed price contract with escalations
- Keep the unit on wing – never mind the maintenance actions!!!!

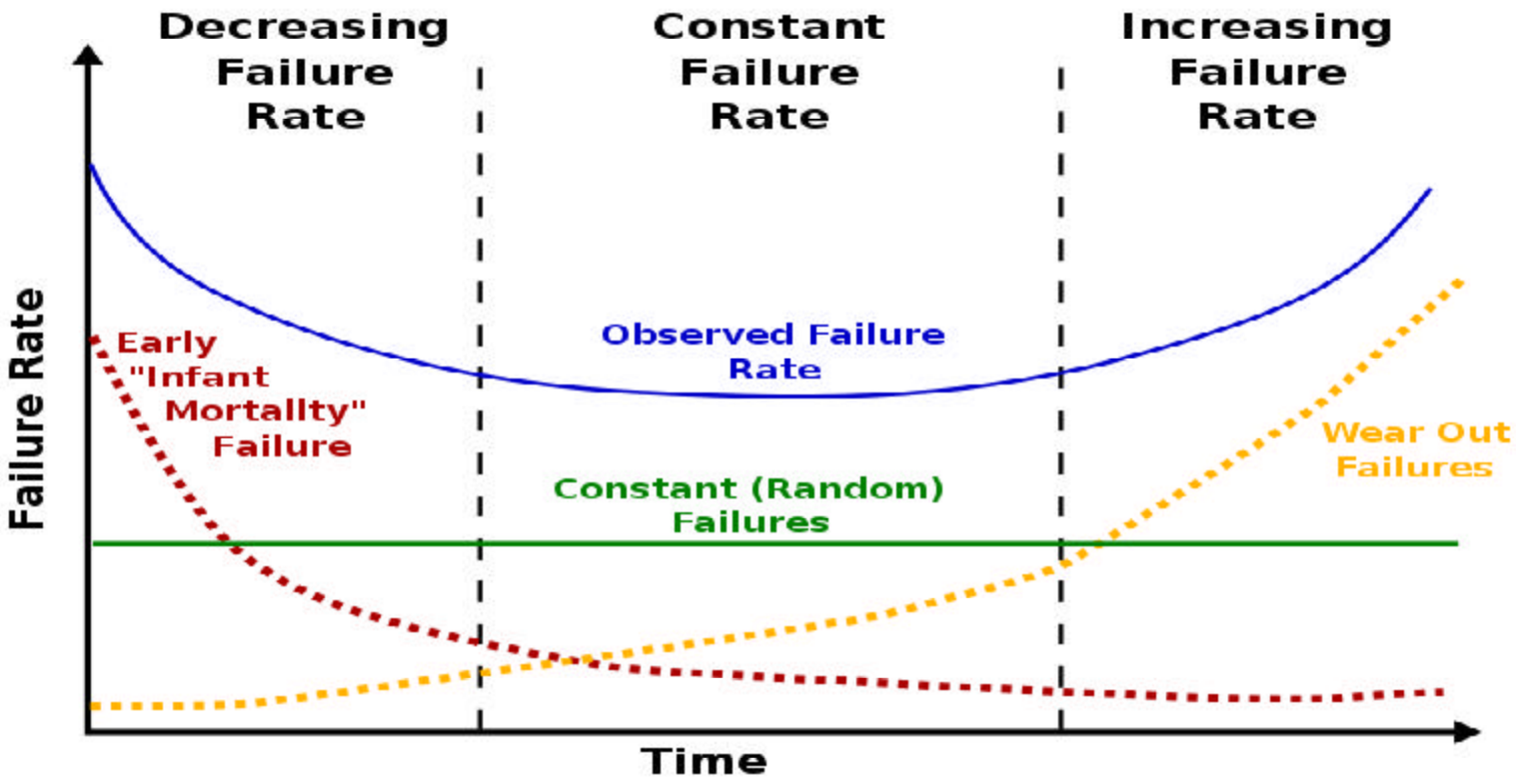
The Spare Part Story



"PMA shouldn't be allowed because we have to earn back our development costs"

When does the price break happen?

The Reliability Excuse



- Unless you are the launch airline you should typically be operating in the stable region of the curve.
- If performance is poor airframers will insist on improvments, you'll get whatever design improvements are made anyway

The Reliability Excuse

"PMA parts aren't as reliable because they aren't OEM supported"

1. PMA developers have the benefit of understanding the OEM's short comings
2. PMA developers often have newer materials, manufacturing methods and hold tighter tolerances due to the re-engineering process
3. PMA companies focussed on this market, not moving their engineers to the "next big platform"
4. Generally PMA developers avoid major problem areas that AD's or major service bulletins have been written against

The Warranty Play

"Your warranty will be denied if you use a PMA part"
If your equipment is under warranty why would you be using a PMA part?

"In the event of downstream damage, warranty will be denied if there's a PMA present"
Try getting downstream damage from an OEM UNLESS you have a big sales order pending!

The IP Smoke Screen

While not exhaustive, the FAA does not find the following DAH practices acceptable under the provisions of 14 CFR §21.50(b) and related ICA airworthiness requirements:

- Requiring the use (installation) of only DAH-produced or authorized replacement parts, articles, appliances, or materials.
- Requiring that alterations or repairs must be provided or otherwise authorized by the DAH.
- Requiring the use of only repair stations or other persons authorized by the DAH to implement the ICA.
- Establishing, or attempting to establish, any restriction on the right of the owner/operator to disclose or provide the ICA to persons authorized by the FAA to implement the ICA.

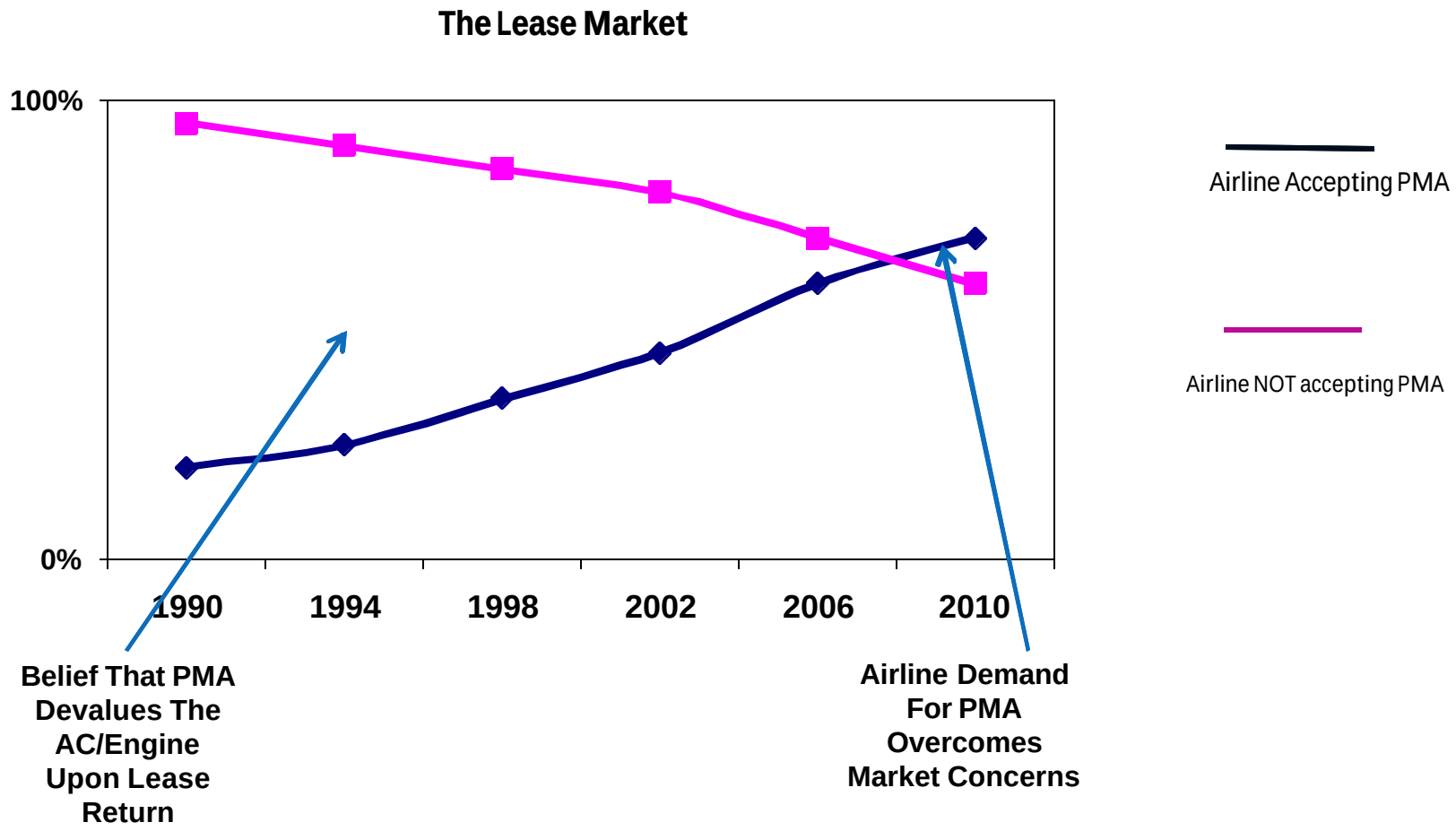
Source: FAA Draft Memo - Policy Statement, PS-AIR-21.50-01: Inappropriate DAH Restrictions on the Use and Availability of ICA

The Leasor Holder Trump Card

- Aircraft residual value reduction
- Inability to move aircraft across geographical boundaries (where regulatory rules are different on PMA)
- Inability to obtain financing: lack of understanding of PMA by banks

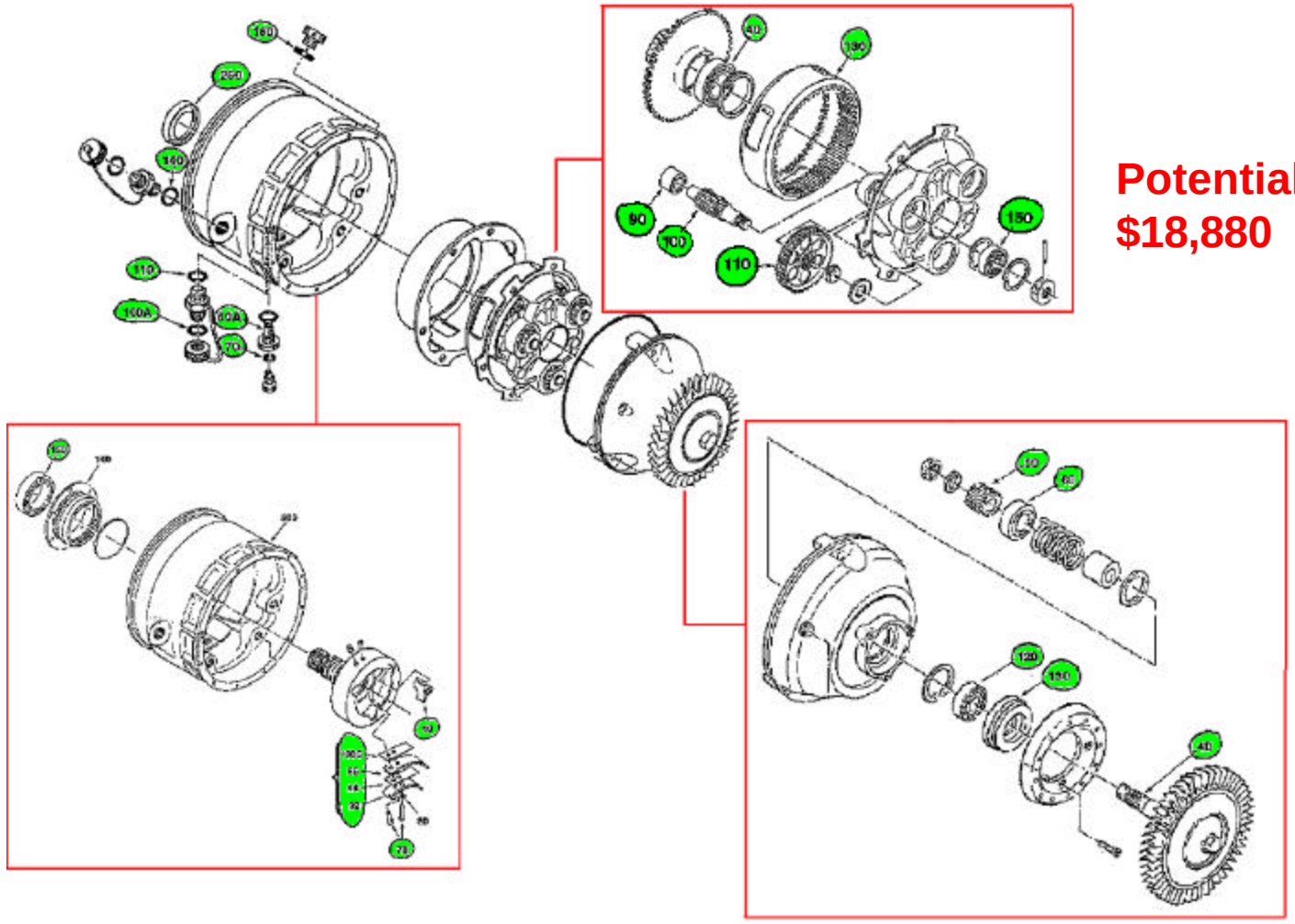
Negotiating Tip: If a lease holder asks you to sign a no PMA lease, ask him/her to prove to you that there's no PMA already on the aircraft

The Argument for PMA



PMA Speak for themselves!

Engine Starter Example (Honeywell 3505488)



Potential Savings
$18,880

Conclusions

- Long term Care/maintenance agreements are great for finance people
- Power by the hour and similar programs limit flexibility of operation
- The IP argument is a total non-starter and the FAA is reacting to limit illegal business practices
- PMAs continue to deliver equal or better reliability than OEM
- Non-PMA accepting airlines are now moving towards minority
- PMA coverage is increasing and remains a great competitive strategy

Questions?