



PROVIDING LIFT TO CORPORATE CANADA



A position report on Skyservice Business Aviation

By Frederick K. Larkin

THE TIME MACHINE COMES OF AGE

A corporation owning an aircraft is analogous to a family owning a car. The alternative for company employees is to rely upon the schedules of airlines. Depending on the destination, this can mean one or more connections en route.

Without a car, family members are open to the vagaries of public transit systems. An aircraft, like an automobile, provides its passengers with four precious intangibles: efficiency, security, privacy and flexibility.

The resurgence of North

America's post-war economy was enabled by the expansion of its transportation network. Corporate aircraft, like private automobiles, played a key role in that economic boom and their numbers multiplied as a result. Business aviation in Canada, as in the U.S., came

into its own during the 1950s. The "heavy iron" back then was represented by converted piston airliners. Examples were the Douglas DC-3, the Lockheed 18 Lodestar and the Convair 240 operated by Goodyear, Massey-Ferguson and Imperial Oil, respectively.

The industry matured further during the following decade, as evidenced by the incorporation of the Canadian Business Aviation Association on May 8, 1962. The 1960s saw the arrival of the first turbine-powered business aircraft to Canada and, as the decade ended, there was an established Canadian jet set.

A review of the Canadian Civil Aircraft Register dated Sept. 30, 1969, shows that 42 business jets were operating in Canada. These included 18 DH-125s, nine Jet Commanders, five Falcon 20s, three Jet-Stars, two Gulfstream IIs, two Sabreliners, two Learjet 23s and one MS-760 Paris. Today, the corporate jet fleet in Canada has reached approximately 350 aircraft. Clearly the productivity afforded companies utilizing these time machines has not gone unnoticed.

Rather than establishing their own flight departments, some companies preferred to outsource the duties associated with operating and maintaining their aircraft. This demand led to the creation of aircraft management companies that not only acted as the flight department for numerous corporations but made the aircraft available for charter by third parties. Of the business jets registered in Canada today, roughly a third are handled by about a dozen aircraft management companies. The largest of these companies is Skyservice Business Aviation (SBA).

The publicity surrounding the use of aircraft by executives of U.S. automotive and financial companies, who went begging for public funds from politicians in Washington, has led some to question the future of corporate aviation. Will

negative sentiment, never mind the weakened economic environment, have a detrimental impact on Skyservice Business Aviation? Before we attempt to answer that, let's briefly review its history.

THAT WAS THEN...

Back in the spring of 1986, L. Russell Payson purchased a fixed-base operation at YUL in Dorval, Que., that had been operated by Air Inuit. The new outfit that opened its doors on June 22 was named Sky Service F.B.O. Sound familiar? During the 1960s, the Texaco Sky Service division of Timmins Aviation had FBOs at YUL, YYZ (Mississauga, Ont.) and YYC (Calgary, Alta.) until they were sold to Atlantic Aviation of Wilmington, Del., on Jan. 1, 1967. Payson received permission from Texaco to use the Sky Service name. An important stage in the company's growth began in the spring of 1990, when it began managing executive aircraft for owners who did not wish to have their own flight department. The first airplane was nothing less than a Falcon 900. In June of that year, Skyservice initiated its air ambulance business with a Citation S/II.

The FBO operations expanded to YYZ in August 1993, when it acquired the facilities of Worldways Canada from its receiver. The architecturally enhanced facility debuted on Jan. 1, 1994.

Until the fall of that year, Skyservice was known primarily within the corporate aviation world. That changed on Oct. 26, 1994, when Skyservice Airlines took flight. Operating a pair of A320s leased from Monarch Airlines of

Luton, United Kingdom, the new carrier flew holiday-makers to southern destinations on behalf of Sunquest Vacations. Thus was the beginning of a major leisure-oriented airline that would become a household name. Skyservice Airlines leased aircraft during the busy North American winter season then returned them to the lessors in the spring. These aircraft would then be used by other leisure carriers to meet their seasonal capacity demands in Europe and elsewhere. As the airline grew its customer base and widened its geographic focus, its fleet was ever changing due to scheduling requirements. Skyservice added wide-body equipment to its fleet on May 7, 1997, when it took delivery of "C-FBUS" – the first Airbus A330 in North America.

While the Skyservice Airlines brand was largely associated with leisure travel, the carrier diversified its revenues by entering niche markets. It went after sports team charters with its Sport Hawk brand from 1998 until 2003. It later attempted to obtain a share of the scheduled business travel market with its Roots Air brand from March 26 to May 3 in 2001. Since its inception, Skyservice Airlines has at various times operated 28 Airbus A320-200s, 18 Boeing 757-200s, six A319-100s, five A330-300s, three 767-300s and two 727-200s.

While the airline was achieving significant growth, the original business (since renamed Skyservice Business Aviation) had expanded dramatically as well. The two FBOs regularly won awards from leading industry magazines in recognition of their

valued services. On June 14, 2005, Imperial Oil Aviation announced that Skyservice had been awarded the Esso Aviatat dealership at YYC in Calgary. It now had FBOs at the three busiest corporate airfields in Canada. In the meantime, the air ambulance unit had expanded to five Learjet 35s and operated medevac missions to destinations around the globe. The fastest growing department within the company proved to be the aircraft management group. From its start in early 1990, SBA has managed some 80 airplanes.

On Aug. 27, 2007, Skyservice Investments announced it was selling its interest in Skyservice Airlines to Gibralt Capital Corporation of Vancouver, B.C. At the time, the airline was flying more than one million passengers annually to 64 destinations in 25 countries aboard a fleet of 21 aircraft. The deal closed on Oct. 19, 2007 leaving Skyservice Investments with its 100 per cent interest in Skyservice Business Aviation. On May 28, 2008, Russ Payson ended his management role at the airline to concentrate on his position as chairman and chief executive officer of SBA.

THIS IS NOW...

Today, SBA's business is segmented into three activities: aircraft management and charter, aircraft maintenance, and fixed-base operations. The aircraft management group provides flight crews and performs missions for aircraft owners that have decided against investing in the assets and personnel required to create their own flight departments. The four dozen aircraft

under management are based at seven airports across Canada. This group also provides charters using many of the aircraft under management and provides consulting services related to the purchase and/or sale of aircraft.

The aircraft maintenance group performs airframe inspections, avionics repair and modifications, power plant removals and installations, and non-destructive testing. This work is done according to long-term contracts as well as in response to one-time repair requests. The company is an authorized service provider for Bombardier Learjet and Challenger aircraft; for Dassault Falcon 50/2000/900 models; and for Beech King Airs. It is also approved by Rolls-Royce to support Spey and Tay turboprops and is an authorized sales and service dealer for Rockwell Collins avionics.

The fixed-base operations provide fuel and hangar space for resident customers as well as for itinerant aircraft. In addition, numerous corporate flight departments operate from their rented offices within the FBO complexes. Executive lounges, courtesy offices and boardrooms, and ground transportation arrangements are some of the services provided for passengers at the FBOs. For the flight crews there are rest areas, computerized flight planning and weather briefing facilities, and in-flight catering services.

In order to gain a better understanding of any business model and therefore appreciate how a company may perform in the future, it is useful to perform a S.W.O.T. analysis (Strengths, Weaknesses, Opportunities and Threats).

Doing so with Skyservice Business Aviation provides the following insights:

S.W.O.T. ANALYSIS OF SKYSERVICE BUSINESS AVIATION



STRENGTHS:

Growth industry – The positive attributes of corporate aviation (improves productivity, while providing security, privacy and flexibility) pretty much guarantee ongoing demand for the range of services the company provides. Given the potential for more service reductions (fewer frequencies and/or withdrawal from communities) by scheduled carriers, the important role of business aircraft stands to be further enhanced in the future.

Barriers to entry – Capital for facilities and inventory, highly trained and motivated personnel, and longstanding customer relationships are all ingredients necessary for success and difficult to replicate.

Revenue diversification – The company's revenues are evenly divided between the aircraft management/charter unit, the maintenance activities and the fixed-base operations.

Enviably reputation – Since its inception, the company has worked to a business plan that is focused on the customer. Having successfully executed on that strategy, Skyservice has developed a reputation for providing quality service. Such goodwill is an invaluable tool in its efforts to win and retain clients.

Corporate culture – SBA's 470 employees have embraced the company's philosophy that the customer is the top priority. The team is not unionized and therefore flex-

ible in handling multiple tasks as required. Its high level of morale is confirmed by the low employee turnover.



WEAKNESSES:

Competitive environment – The corporate aircraft management industry in Canada is dominated by about a dozen major players of which Skyservice is the largest. While customer loyalty tends to be a hallmark of the business, there can be migration among managers. Given its growth, Skyservice appears to have been a net beneficiary of such changes during the past decade. Even so, the market demands that fees remain competitive and that operating costs be disciplined.

Currency exchange – Any Canadian company whose key inputs are priced in U.S. dollars, is exposed to foreign exchange risk. However, in the case of Skyservice, most of these costs are passed through to the customers.

Not part of a major FBO chain – The effort to capture itinerant traffic can be assisted by being part of a well-recognized organization. Unlike the largest industry players (such as Atlantic Aviation, Signature Flight Support and Landmark Aviation) that have 40 to 60 FBOs across North America, Skyservice is a regional operation. Having said that, Skyservice's FBOs are branded as ExxonMobil/Esso Avitats and therefore represent three of the nearly 70 Avitats in North America, Europe and the Middle East. Despite not having the North American profile that the three aforementioned chains enjoy, Skyservice has managed to capture the largest

share of itinerant business at each of its locations.



OPPORTUNITIES:

Maintenance business growth – While its main-

tenance activities currently relate to aircraft under management and some work for regional airlines, additional opportunities are on the horizon. As the average age of the business aircraft and regional jet fleets increase, there will be greater demand for maintenance on airframes and engine work. In order to be better equipped to efficiently process new business, the company is investing more than \$3 million in software for its maintenance unit.

Building the charter business – As more companies and individuals become aware of the attributes of business aircraft, the demand for air charter services is expected to increase. Whether the customer is an occasional user or an aircraft owner that is seeking supplemental lift, the convenience of a charter versus the schedules of airlines is becoming understood by a larger audience. As approximately 60 per cent of the aircraft it manages are available for charter, Skyservice has a wide range of equipment types at its disposal.

Expanding the FBO operation – The five largest Canadian corporate aviation markets are, in descending order, Toronto, Calgary, Montreal, Vancouver and Edmonton. With an established profile in the three largest centres, Skyservice has a solid domestic presence. Any expansion to other cities will likely be dictated by the incumbents wishing to divest. While that currently seems unlikely, the

industry has a history that suggests anything can happen – if you wait long enough.



THREATS:

Economic adversity – A weakened economy means decreased flight activity and deferred customer fleet upgrade decisions. This translates into lower fuel sales, reduced charter revenues and a pullback in maintenance work. The business aviation industry recently experienced the most prosperous period in its history. Once the economic cycle works its way through the current challenging phase, the level of activity is expected to rebound. To what extent and over what time frame are the two major uncertainties.

Environmental activism

– While the debate continues over the validity of the global warming theory, environmentalists are taking aim at the corporate aviation industry. By claiming that business aircraft are the most polluting method of transportation (in terms of the amount of carbon dioxide released per person-mile) they are attempting to portray the industry as irresponsible. Down the road there will be programs that enable corporate aircraft operators to repent for their footprints by purchasing carbon offsets – a tax by any other name.

Negative media attention

– The business aviation industry has always been a lightning rod for the media. Lately, the strikes have been coming fast and furious. Despite the proven productivity of corporate

aircraft, the media’s “airplane envy” can unduly influence key decision makers including significant investors, executives and politicians.

WHAT DOES THIS ALL MEAN?

The business aviation industry has seen significant growth during the past half century despite the cyclical behaviour of the economy. In recognition of the enhanced productivity, security, privacy and logistical flexibility associated with aircraft, many corporations and some families have utilized this mode of transport regardless of the economic environment.

In order to best serve this expanding niche market, Skyservice Business Aviation has become a fully integrated provider of services to meet the needs of both frequent and occasional travellers, be they corporate executives or private individuals. Having assembled a team that has diversified skills, the company has been able to generate revenues from a variety of activities that complement each other. This has resulted in an enviable financial performance and provided stability.

WHAT DOES THE FUTURE HOLD?

Earlier this year, on Jan. 30, SBA announced the sale of its air ambulance business to Emergency Medical Services Corporation (EMSC) of Greenwood, Colo. The deal is expected to close by May 30, if not sooner. Going forward SBA will manage the five Learjet 35 ambulances on behalf of EMSC’s American Medical Response subsidiary

for 10 years. With this transaction, SBA will have reduced its fixed assets, expanded its aircraft management business and secured a decade-long contract with a specialist in the recession-resistant health-care sector. The proceeds from the sale are to be used to finance expansion programs within each of SBA’s three groups. This will assist in attaining the company’s goal of exiting the current economic downturn in an even stronger competitive position. Given that it has been profitable in every year since its inception and has a debt free balance sheet, it is already in fighting form.

Even though he has been the pilot in command of this enterprise since its inception, Russ Payson (SBA’s chairman and CEO) still has the “fire in the belly” of a classic entrepreneur. When asked what makes him still want to be in the office as opposed to leading a life of leisure he responded, “I love to come to work because this is an exciting place to be, the company is going places, we have a great team and we have lots of fun!” Succession planning is an ongoing program at any well managed organization. The situation at SBA was clarified last fall when Marshall Myles was appointed president and became a significant shareholder on Nov. 1. Prior to that, Myles had spent 30 years with Roots Canada where he had served as president and CEO since December 2000. The aviation scene isn’t new to him as he served on the board of directors of Skyservice Airlines from September 2000 until it was sold and he has been on

the Skyservice Investments board since the spring of 2008. He commented on SBA’s outlook by saying, “We are a debt free company looking to grow by being aggressive in our core business, as well as being interested in acquisitions.”

CONCLUSION

With respect to the question we posed earlier, the Canadian situation differs from that south of the border. It appears that our leading corporations, while not immune to financial distress, have managed their affairs with greater fiscal discipline. This should translate into a relatively smoother ride for the Canadian economy and our bizav community.

Nineteen years ago, Skyservice began operating its first managed aircraft. Today, it looks after approximately 50 – roughly double the number managed by the second largest player. When asked what he attributes that dominant position to, Russ Payson replied, “Service and outstanding customer relationships.”

Skyservice Business Aviation has evolved from a single-location FBO to a well-diversified provider of services to the Canadian corporate aviation market, a transformation has made it the industry leader. Given its range of services, the high regard with which it is held within the industry and its financial fitness, Skyservice Business Aviation appears to be positioned to achieve prosperous growth over the foreseeable future. ✈