bail out–or buy a share?

THIS COULD BE JUST THE TIME TO DO EITHER. IT ALL DEPENDS ON YOUR SITUATION_by James D. Butler

IS THIS A GOOD TIME to buy a fractional share? Or to sell the one you own? The answer, depending on your situation, could be yes to either question.

Let's talk first about those who should consider bailing out. If you're a fractional owner, you've invested a significant sum with a provider that has agreed to buy back your share at its fair market value. The attempt by some fractional companies to delay repurchase tells me that capital is tight. If you're wary that financial problems may cause your provider to fail, you should seriously consider selling your share now. (Recall the nightmare that was FractionAir–a company that ceased operations a couple of years ago, leaving shareowners in the lurch. Some aircraft reportedly were scavenged for parts to keep other aircraft flying, and owners were offered pennies on the dollar for their shares).

JOHN T. LEWIS

Indeed this is an important moment with respect to the value of fractional shares. The market for preowned aircraft is poor. Asking prices for all aircraft have dropped, but high-time fractional aircraft will be especially affected because an uncommon number of low-time, nonfractional aircraft are entering the market.

As an analogy, if you're looking for a used car and all the ones on the market have 100,000 miles on them, they should all hold their relative value and sell within a reasonable time. But, if suddenly, plenty of cars are available with 10,000 miles on them, the 100,000-mile ones will be less attractive and so will sit longer, further depressing their value. That's what I suspect will happen as corporate aircraft, having been flown on average 400 hours per year, flood the market. Fractional aircraft, which usually are flown 1,100 or more hours per year, will become even less attractive and will decline in value more than the market as a whole.

At the moment, preowned aircraft sales are slow. Thus, if you sell your fractional share back to your provider now, you'll enjoy the benefit of older comparable sales that reflect higher values, while fractional owners who wait could suffer the effect of comparable sales that likely will reflect a significant decline in their aircraft's value.

At this critical time, it's worth considering whether to reclaim your capital and use another private flying option, such as fractional jet cards (which allow you to employ the same fractional fleet) or even traditional charter (which has lots of excess capacity). As you do so, beware of lowball offers from your fractional provider for your share. In tough times like these, and with stakes so high, it's important that you receive fair value for your share.

SO WHO WOULD WANT to buy a fractional share during such a difficult period? Perhaps you. For some, as Baron Rothschild reputedly said, "The best time to buy is when there is blood in the streets." Or perhaps

PLANNING TO BUY? HEED THIS ADVICE

CONSIDER PREOWNED SHARES. The jet market has been particularly unkind to older jets. Fractional programs that have repurchased shares in these aircraft are finding them harder to sell than shares in new aircraft. This combination of factors means that you may find favorable pricing on preowned shares. It's worth considering, though, that the operating costs of older, out-of-warranty aircraft will be higher than those of newer aircraft, which could reduce resale value. Also, the market for older aircraft may come back more slowly than the market for newer aircraft, which would also negatively affect the price you receive when you sell back your share.

NEGOTIATE! NEGOTIATE! NEGOTIATE! Slow share sales, rising redemptions and tight credit mean fractional providers are motivated to make deals. But it's important that you negotiate concessions that add value for you. A short-leg waiver (billing a flight of less than one hour at its actual flight time as opposed to the standard one-hour minimum) is of no worth to you if all your flights are more than one hour. Similarly, a guaranteed upgrade to a larger aircraft does you no good if you never need the larger aircraft. Consider carefully the concessions that will truly add value to your investment and make these the focus of your negotiations.

INVEST IN A PROVEN PROGRAM. Make sure that your fractional program is financially sound and has a record of excellent customer service, especially in difficult times. Investing in a fractional program is like investing in a limited partnership. As a limited partner, you make a large capital investment up front and you rely on the provider, as the general partner, to operate the program well and to buy you out when the time comes. That's why it's essential that you invest with a program that has a track record and the financial wherewithal to make it through a down economy.–*J.D.B.*

more to the point with respect to fractionals, as Warren Buffett has said, "Be fearful when others are greedy, and be greedy when others are fearful."

Well, there's certainly no shortage of blood or fear in the streets these days. So let's investigate whether this is a good time for you to buy a fractional jet share.

First things first. Regardless of the economic circumstances, you need to make certain that fractional ownership is the right investment to satisfy your travel needs, preferences and budget. That depends on a wide variety of factors, including how much you fly per year, the length of your typical flights, your financial situation and more. For help with the decision, see "Flying Privately without Buying a Jet" in the 2009 edition of **BJT**'s **Buyers' Guide**, which you can find at www.bjtonline.com.

If your travel profile, preferences and budget are best suited to the fractional model, you then need to consider how long an investment horizon you have. This is important because while the current economic downturn may provide an opportunity for you to take advantage of lower aircraft pricing that has resulted from declines in the market value of aircraft, this decrease may continue for some time and so the value of your aircraft, and thus your share, may drop over the next couple of years.

The private jet market tends to be cyclical, and so values likely will come back with the economy, but this will take time. It's also worth considering that many fractional programs require that you hold your share for at least two years before you'll have the right to sell it back. Thus, a three- to five-year investment horizon is the best way to approach the fractional market now.

If your needs and time horizon seem suited to a fractional share, you may indeed do well by following the sage advice of Baron Rothschild and Warren Buffett. And if these titans of finance aren't enough to convince you, perhaps you should take the advice of no less an authority than Rodney Dangerfield in the classic film *Caddyshack*. Told that everyone else was selling, Dangerfield screamed, "Then buy! Buy! Buy!"

James Butler welcomes comments and suggestions at: jbutler@bjtonline.com.

CAN'T GET OUT? HERE ARE SOME OPTIONS

Most standard fractional contracts include a 24- to 30-month period during which you're not entitled to sell your share back to the provider. It's wise to negotiate changes to this provision to provide additional liquidity, but if your contract already includes such a provision, consider these exit strategies.

SHARE YOUR SHARE. Find someone who doesn't want to own an entire share, but wants to purchase hours (paying the hourly rate and a portion of the management fees). Such an arrangement, if structured carefully so as not to run afoul of FAA regulations and your fractional contract, can help defray your costs until you're able to sell.

STAY IN...BUT STEP BACK. Negotiate both a buyout and a continuing relationship that takes advantage of another service offered by your fractional provider, such as a jet card or traditional charter. In this win/win arrangement, you can secure your capital while your provider retains a customer.–*J.D.B.*