

IATA ECONOMICS BRIEFING

AIRLINE BUSINESS CONFIDENCE INDEX

JUNE 2006

KEY POINTS

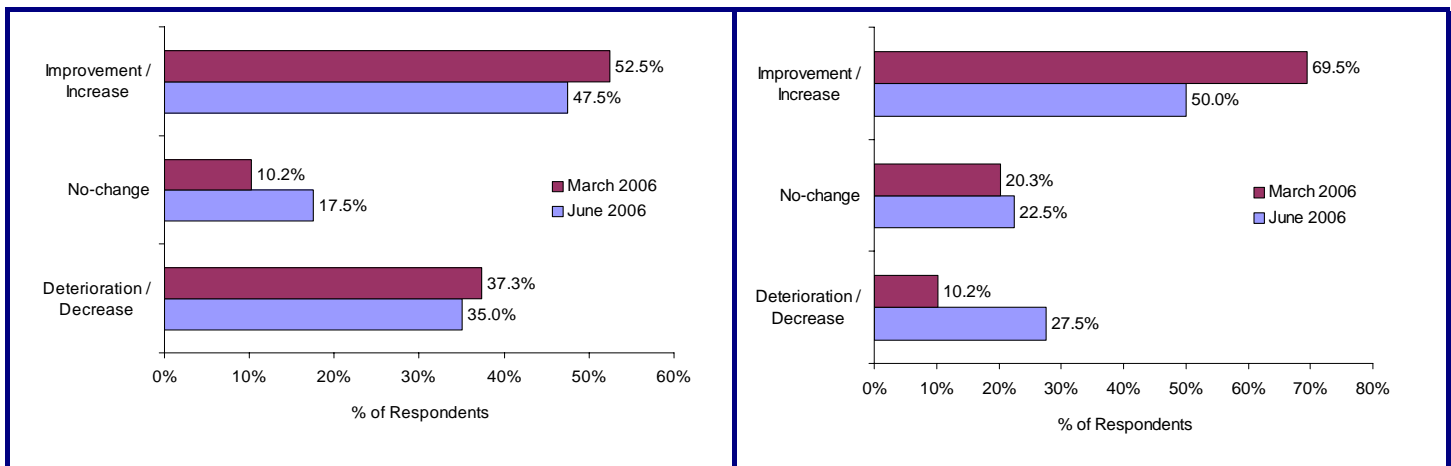
- Airline business confidence has reduced since the last survey in March, hit by a 25% increase in fuel prices over the period. Nevertheless, the overall balance is still positive. Half of the respondents still expect profitability to increase over the next twelve months, compared to just over a quarter that expect profitability to fall.
- Indeed, while many respondents to IATA's survey of airline CFOs expressed concern at the impact of higher fuel prices, there were still positive views on the scope for further demand growth, additional non-fuel cost efficiencies and higher yields through fuel surcharges.
- The demand environment remains very supportive. All regions expect to see strong volume growth over the next year, with a number of airlines looking to expand capacity. However, the positive demand outlook remains exposed to risks such as a slowdown in the global economic growth or avian flu impacts.
- The positive demand environment has allowed some airlines to pass on a proportion of the higher fuel costs to customers through fuel surcharges. However, strong competition means that yields excluding the fuel surcharges remain under pressure. Airlines will continue to seek further yield improvements, though are also aware of the constraints on further surcharges – not least through a negative impact on demand.
- Airlines are also making substantial progress in delivering non-fuel cost efficiencies. Even with the recent rise in fuel prices, nearly 45% have managed to reduce total input costs over the last three months, with nearly 60% expecting to see no change or lower total input costs over the next year.

AIRLINES ARE LESS CONFIDENT IN THE OUTLOOK FOR PROFITABILITY

- Despite significantly higher fuel costs, nearly half of respondents reported an improvement in profitability over the last three months, down only slightly from the previous survey in March. However, airlines have become less confident about the outlook for profitability over the next year. Only half of all respondents expect profitability to improve, down from 70% in the March survey. At the same time, the nearly 30% of airlines expect lower profits over the next twelve months, up from 10% in March. Fuel costs are the main cause for concern.

How has profitability changed in the last three months compared with the same period last year?

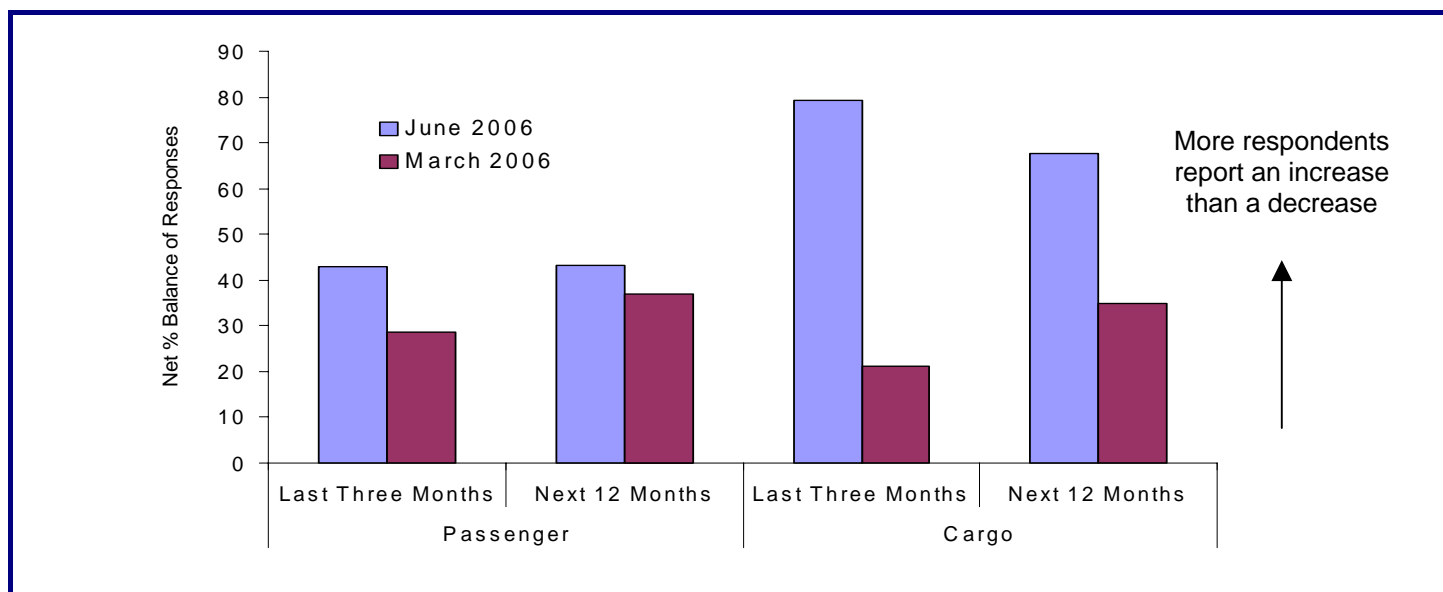
How do you expect profitability to change over the next twelve months?



BUT THE DEMAND ENVIRONMENT REMAINS POSITIVE

- Airlines are even more confident of demand growth – for both passenger and cargo traffic – than they were in the previous survey. A net balance of over 40% of responses (i.e. those responding higher volumes minus those responding lower volumes) have seen passenger demand increase in the last three months and expect it to continue to grow over the next year. An even higher net balance of nearly 80% have seen cargo traffic increase over the last three months, with most of these also expecting to see further growth over the next year.

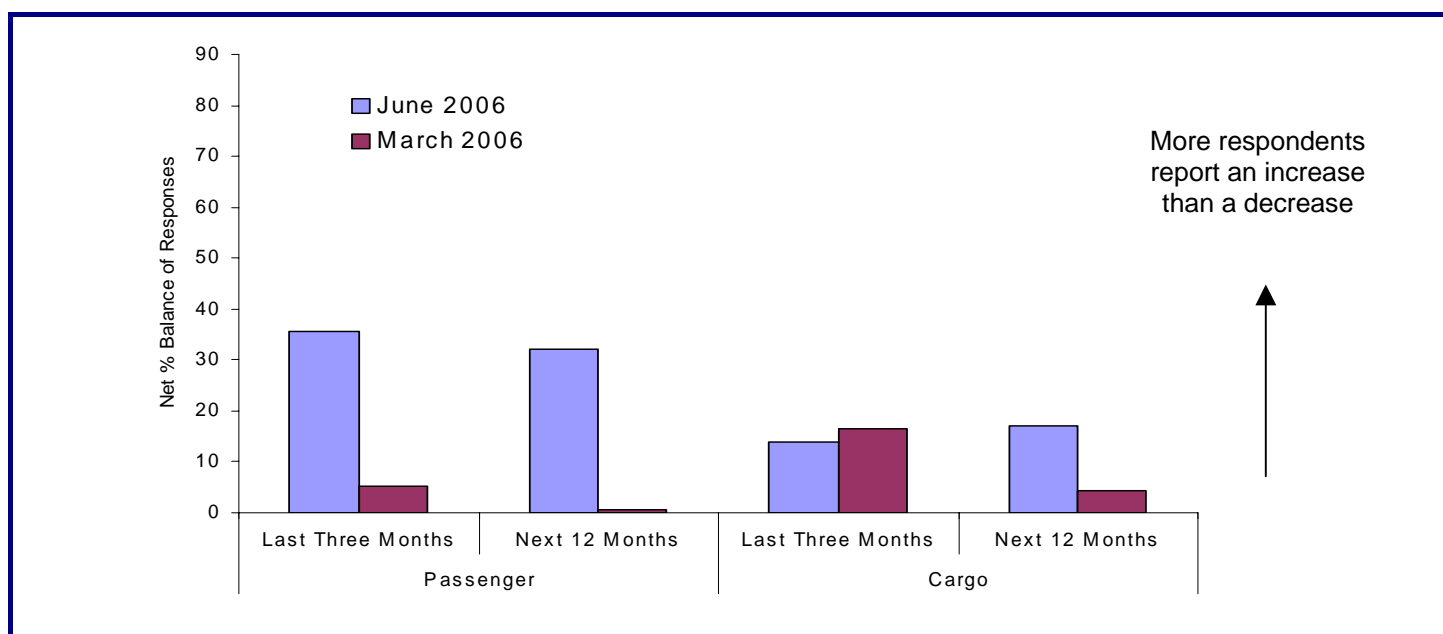
The actual and expected change in traffic volumes (a net % balance of zero equals no change)



FUEL SURCHARGES HAVE HELPED TO IMPROVE YIELDS SLIGHTLY

- The positive demand environment has allowed some airlines to introduce or increase fuel surcharges over the last three months, passing on some but not all of the higher fuel costs to customers. Higher fuel costs mean that many airlines will continue to seek yield improvements over the next year, though many recognise that this may not be possible, especially if demand growth begins to weaken. Strong competition continues to place downward pressure on base yields (i.e. excluding fuel surcharges).

The actual and expected change in yields (a net % balance of zero equals no change)

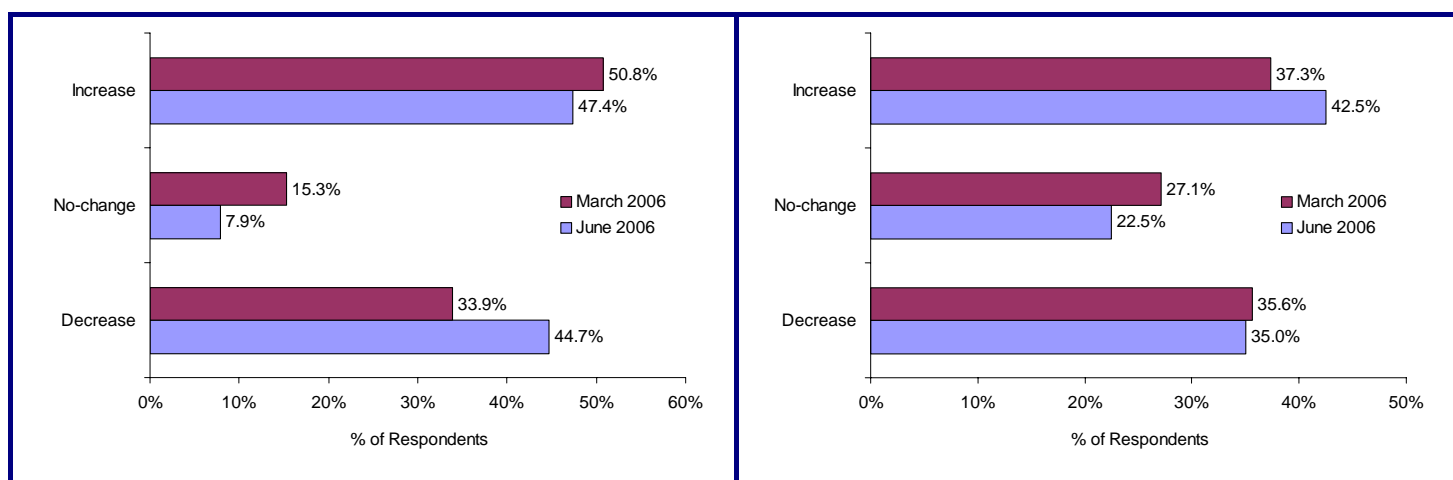


NON-FUEL COST EFFICIENCIES HELP TO OFFSET HIGHER FUEL COSTS

- Even with the 25% rise in fuel prices over the last three months, several airlines are successfully using non-fuel cost efficiencies and fuel price hedging strategies to keep control of unit costs. Indeed, the proportion of airlines seeing an increase in input costs over the last three months fell slightly compared to the March survey, while proportion of airlines seeing lower input costs increased.
- Nevertheless, airlines are still aware of the need to deliver further cost efficiencies, especially in the current volatile fuel price environment. A slightly higher proportion of airlines expect input costs to increase over the next year than in the March survey, but nearly 60% of respondents still expect restructuring and/or improvements in both fuel and non-fuel efficiency to result in no-change or lower input costs.

How have your input costs changed in the last three months compared with the same period last year?

How do you expect your input costs to change over the next twelve months?



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