

IATA ECONOMICS BRIEFING

AIRLINE BUSINESS CONFIDENCE INDEX

JANUARY 2007

KEY POINTS

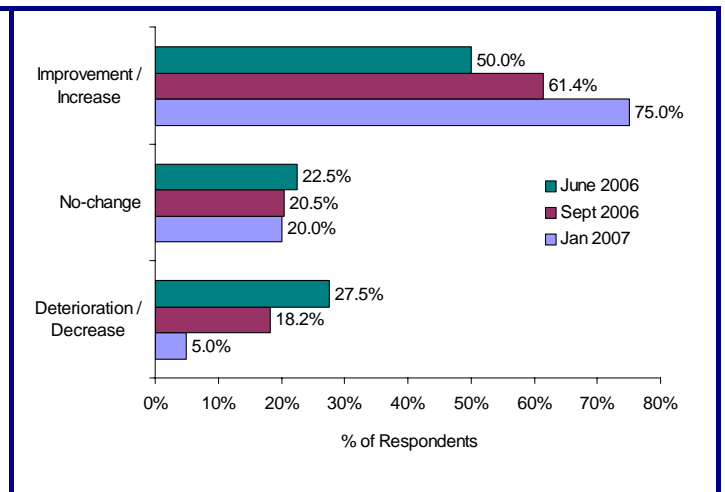
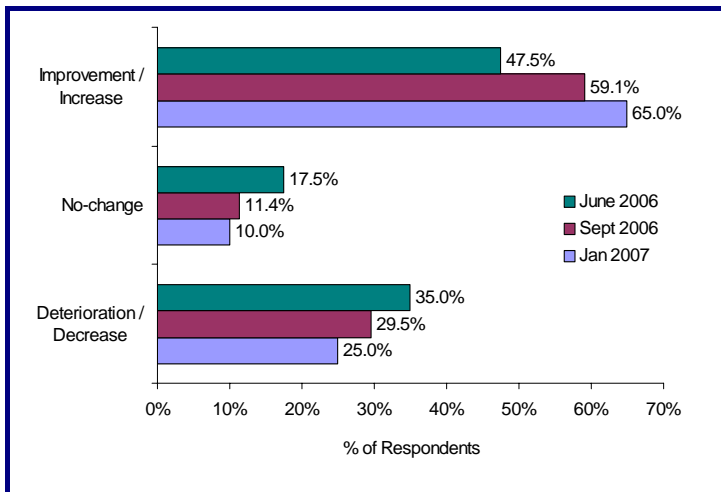
- Airlines are increasingly confident that the improvements in profitability can be sustained into 2007. Three-quarters of respondents expect profitability to improve in 2007, with only 5% expecting to see a deterioration. Increased confidence in future profitability is clearly linked to the fall of more than 25% fall in oil prices since August 2006, but is also boosted by further demand growth and by greater airline efficiency improvements.
- The demand environment remains positive for 2007, building upon the strong increases in volumes seen in the last quarter of 2006. Airlines continue to face risks that could upset the positive demand growth, many of which (e.g. a global economic slowdown, security incidents, an avian flu pandemic) are beyond its control. These risks cannot be removed, but airlines' flexibility to respond to them can be planned and managed.
- On average, airlines have been able to use the positive demand environment to increase yields, though some have already reduced yields through lower fuel surcharges as the oil price has eased. Looking ahead, the majority of respondents expect to see no-change in yields in 2007, though strong competition from LCC airlines will continue to place downward pressure on passenger yields in some markets.

PROFITABILITY IMPROVEMENT LINKED TO THE FALL IN OIL PRICES

- Airlines have become increasingly confident that the improvement in the industry's financial performance can be sustained into 2007. 75% respondents expect profitability to increase in 2007, with 20% expecting no change and just 5% expecting a decline. A positive demand environment and cost-cutting efforts are both providing a boost to profitability, though it is the fall of more than 25% in oil prices since their peak in August 2006 that is a key factor behind increased confidence. Indeed, the expectations of improved profitability has increased significantly from 50% of respondents in the June 2006 survey to 75% in this survey, as oil prices over the period have declined. Nevertheless, some airlines may still face higher fuel costs in 2007, as some older fuel hedging contracts expire and may be renewed at prices still higher than under the old contracts. In addition, others cite the ongoing constraint on profitability from strong competition from LCC airlines.

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?

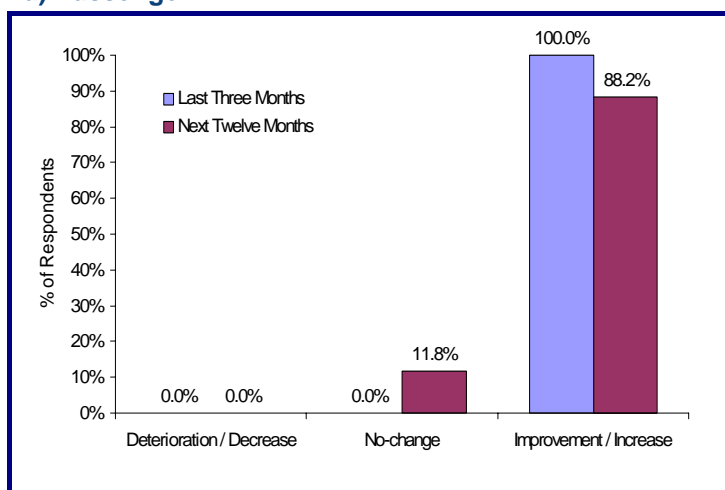


THE DEMAND FOR PASSENGER AND CARGO TRAFFIC CONTINUES TO GROW

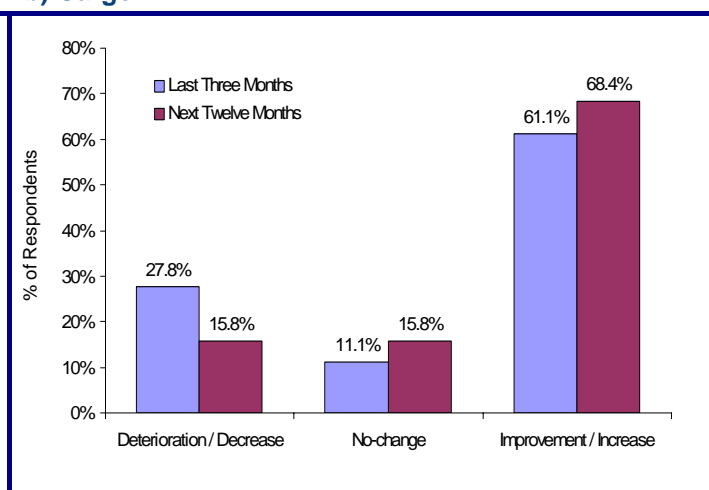
➤ The rate of demand growth is set to slow from the exceptional rates of growth seen in the last three years, but most airlines remain confident that demand growth – for both passenger and cargo traffic – will be positive in 2007. Nearly 90% of respondents expect an improvement in passenger volumes and nearly 70% expect an improvement in cargo volumes in 2007. The positive outlook for further growth builds upon the strong increases in volumes seen in the last quarter of 2006. It suggests that the fundamental factors driving growth, such as global economic growth and higher disposable incomes, continue to support airline demand, especially in fast-growing markets in Asia, the Middle East and Eastern Europe. However, some airlines noted a more difficult environment on the cargo side, with stronger competition and rationalisation of routes affecting volumes carried.

The actual and expected change in traffic volumes

a) Passenger



b) Cargo

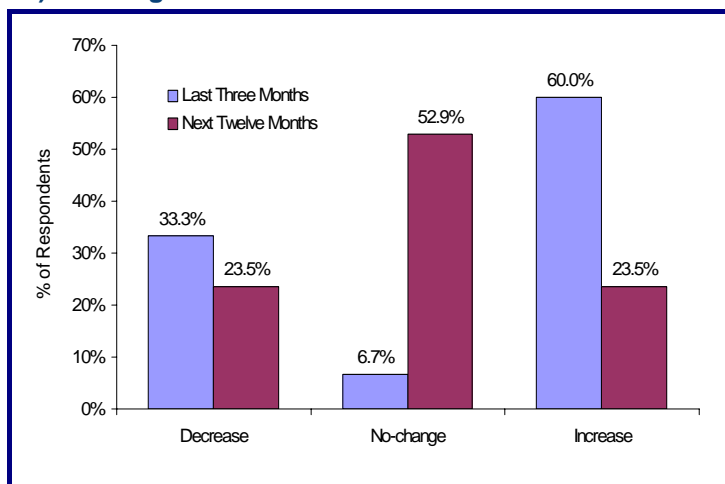


YIELDS EXPECTED TO STABILISE IN 2007

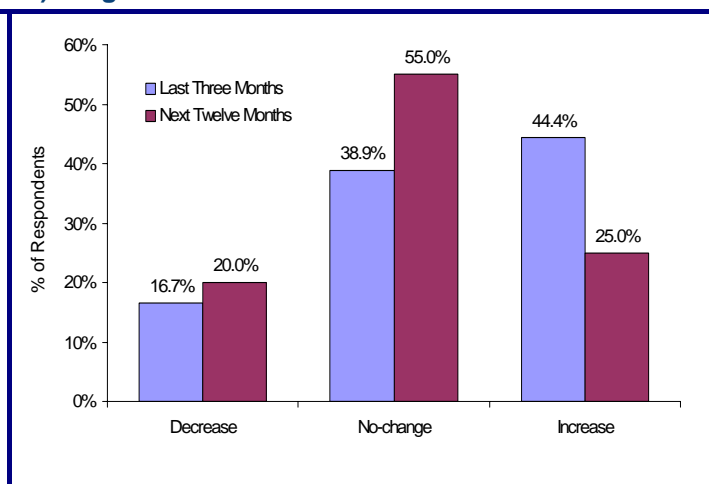
➤ Nearly 60% of respondents on the passenger side and 45% of respondents for cargo have managed to use the positive demand environment in the last quarter to raise load factors and to increase their yields. However, several respondents have also seen a fall in yields in the last quarter, largely reflecting reductions in fuel surcharges as the oil price has eased but also in some cases strong competition. Looking ahead, the majority of respondents expect to see no-change in yields in 2007, especially if the oil price begins to stabilise too. However, strong competition from LCC airlines will continue to place some downward pressure on passenger yields, particularly where LCCs are expanding into developing markets such as Eastern Europe.

The actual and expected change in yields

a) Passenger



b) Cargo

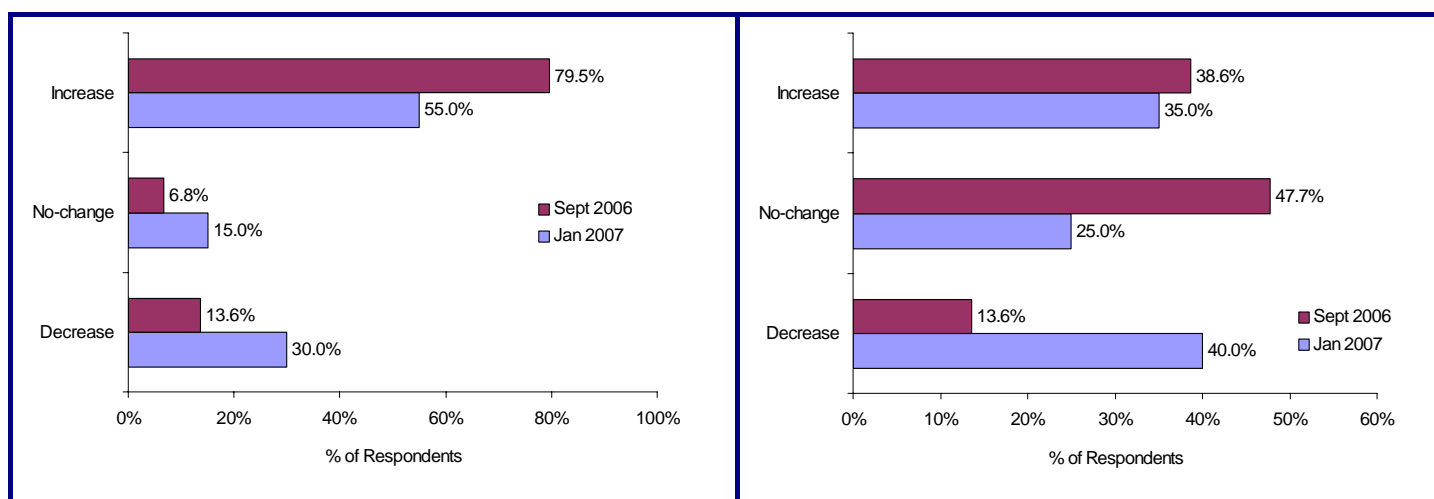


GREATER EFFICIENCIES AND LOWER OIL PRICES HELP TO LOWER COSTS

- The reduction in oil prices in the last three months have helped to reduce the upward pressure on input costs within the industry. 55% of the respondents saw unit input costs rise in the last quarter of 2006, compared to nearly 80% respondents who had seen unit costs rise in the September 2006 survey. Some of this cost increase was due to new services. Indeed, in some cases where costs rose in the last quarter, respondents cited expansion or restructuring plans, rather than external costs such as fuel, as the key factor behind higher costs. However, in other cases it reflected suppliers automatically passing higher costs through to airlines.
- Looking forward, major efforts at improving cost efficiency within the industry, combined with the easing of oil prices, means that 40% of respondents expect unit costs to fall in 2007, with a further 25% expecting no-change in unit costs. The proportion of respondents expecting a fall in unit costs has increased significantly since the September 2006 survey, with several citing that efficiency improvements planned and implemented in recent years are now beginning to provide clear benefits.

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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