IATA ECONOMICS BRIEFING

AIRLINE BUSINESS CONFIDENCE INDEX

SEPTEMBER 2006

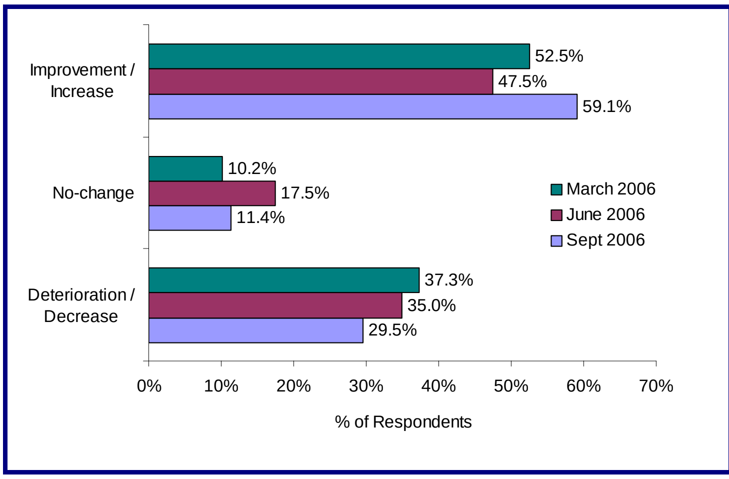
KEY POINTS

- Airline business confidence has improved since the last survey in June, with over 60% of respondents expecting to see an improvement in profitability over the next 12 months (up from 50% in June). The outlook for profitability appears to be strongly linked with the prevailing fuel price, with the recent easing in oil and jet fuel prices helping to boost confidence.
- The demand environment remains very supportive. Indeed, the outlook for the next 12 months is expected to be even stronger than the positive boost to demand seen in the last quarter. 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.
- 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 overall yields remain under pressure. Over 55% of respondents expect to see no-change or a decline in passenger yields over the next 12 months, with over 65% of respondents expecting to see no-change or a decline in cargo yields.

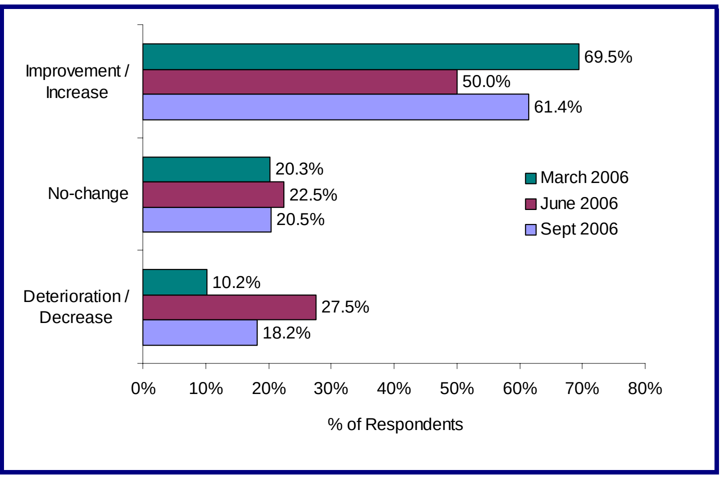
THE OUTLOOK FOR PROFITABILITY IMPROVES AS THE OIL PRICE EASES

- Airlines have become more confident in the outlook for profitability, with the recovery in confidence since the June 2006 survey largely influenced by the recent easing in oil and jet fuel prices. Over 60% of respondents expect profitability to increase over the next 12 months, up from 50% of respondents in June's survey. Less than 20% of respondents now expect profitability to fall. Profitability performance in the last three months has also been stronger than in the previous quarter. Even though airlines have faced much higher fuel costs in the last three months, a positive demand environment and non-fuel cost efficiencies have seen almost 60% of respondents increase their profitability.

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?

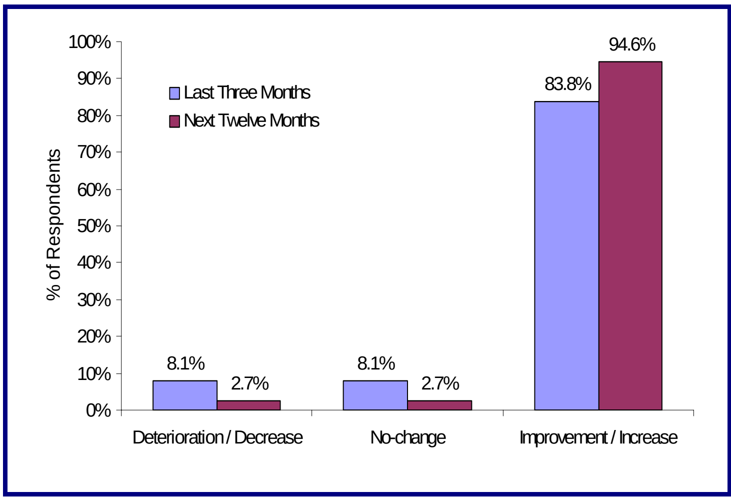


THE DEMAND ENVIRONMENT REMAINS POSITIVE

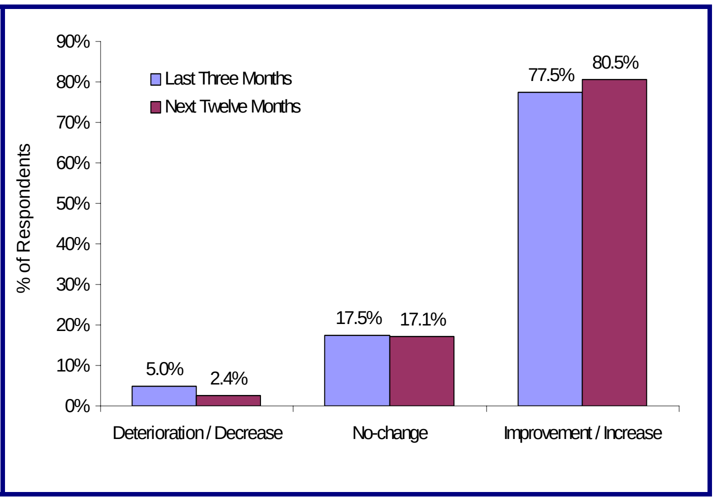
- Airlines remain confident of demand growth – for both passenger and cargo traffic – with the outlook for the next 12 months expected to be even stronger than the boost to demand seen in the last three months. Nearly 95% of respondents expect their passenger traffic to increase over the next 12 months, while over 80% of respondents also expect an increase in cargo volumes. The rate of demand growth is likely to slow from the peak levels for this cycle seen in 2004 and 2005, but the fundamental factors driving growth for both passengers and freight remain reasonably positive.

The actual and expected change in traffic volumes

a) Passenger



b) Cargo

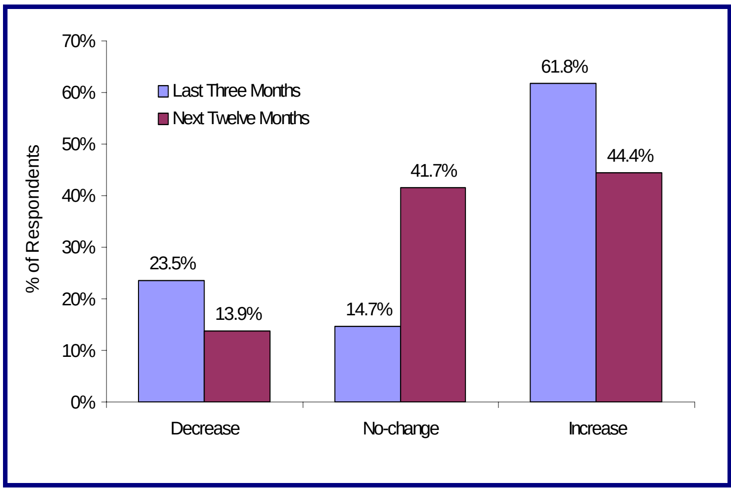


YIELDS HAVE IMPROVED BUT FURTHER GROWTH IS LIMITED

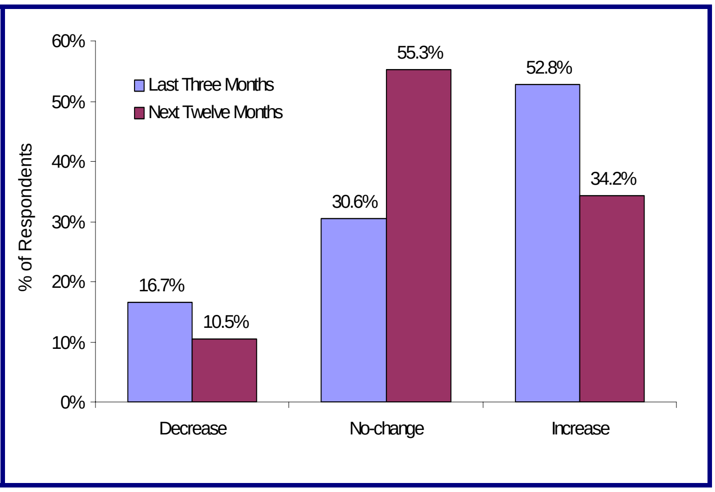
- The positive demand environment has allowed some airlines to introduce or increase fuel surcharges over the last three months, passing on some but not all of the higher fuel costs to customers. Consequently, over 60% of respondents have seen an increase in passenger yields and over 50% an increase in cargo yields over the last three months. However, strong competition also continues to place downward pressure on overall yields. Over 55% of respondents expect to see no-change or a decline in passenger yields over the next 12 months, with over 65% of respondents expecting to see no-change or a decline in cargo yields.

The actual and expected change in yields

a) Passenger



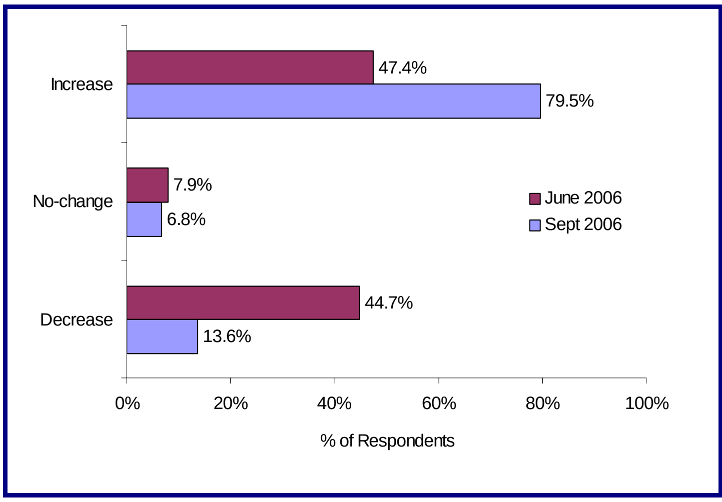
b) Cargo



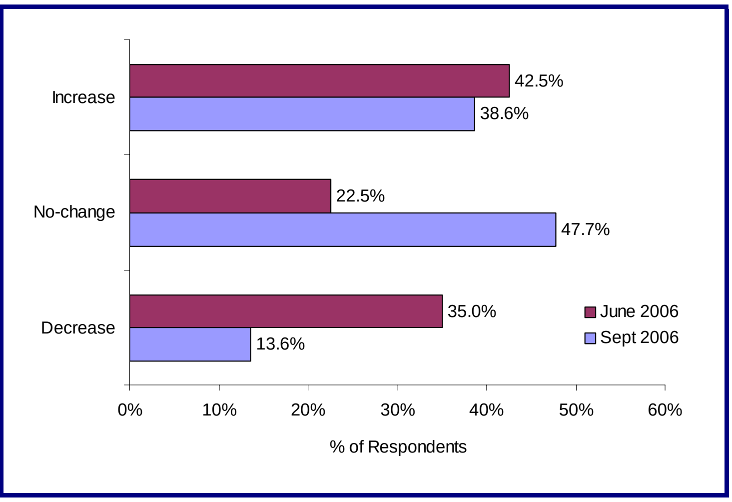
HIGHER FUEL COSTS HAVE INCREASED OVERALL INPUT COSTS

- The sharp rise in oil and jet fuel prices in the first half of 2006 has placed significant upward pressure on the cost base of airlines. Non-fuel cost efficiencies and fuel price hedging strategies have been used to offset some of the impact of higher fuel costs, though have been unable to prevent an overall increase. Nearly 80% of respondents saw unit costs increase in the last three months, up from just under 50% in the previous quarter.
- The easing back of oil and fuel prices in August and September means that the upward pressure on costs should begin to ease slightly. Nevertheless, nearly 40% of respondents expect input costs to increase further over the next 12 months, especially in Asia Pacific where fuel accounts for a higher proportion of the overall cost base. In addition, airlines are aware that they must continue to deliver further cost efficiencies. Though upward pressure on costs may ease, nearly 50% of respondents expect that further efficiency is necessary just to stabilise unit costs, with less than one in seven of respondents expecting to see a more favourable (i.e. lower) cost base in a year's time.

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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22nd September 2006
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