

IATA ECONOMIC BRIEFING

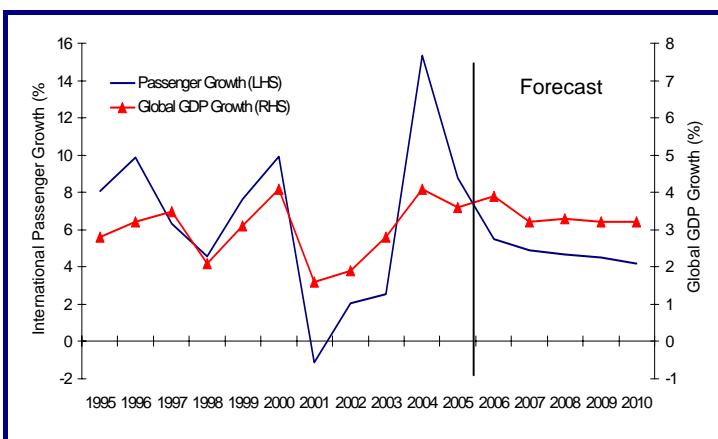
SEPTEMBER 2006

PASSENGER AND FREIGHT FORECASTS 2006 TO 2010

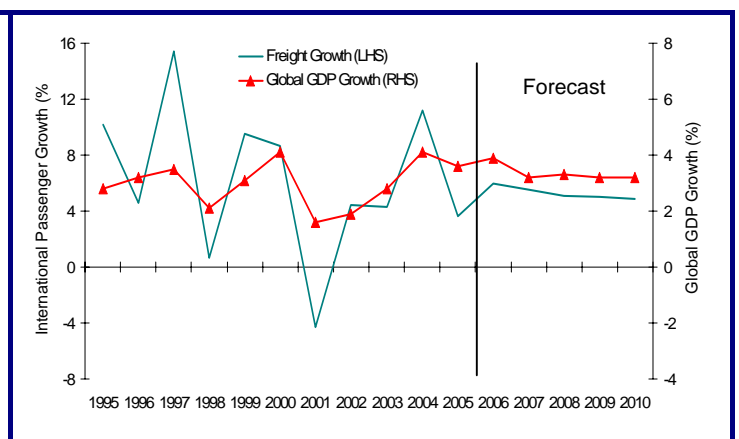
KEY POINTS

- The airline industry is forecast to see a period of slower but more profitable growth over the next five years. Demand growth will slow from the peak levels for this cycle seen in 2004 and 2005 but will continue to provide a positive boost to airline revenues. The forecast also reflects a more cautious approach to capacity growth among airlines, as they pursue profitable and efficient growth, rather than just volume growth.
- International air passenger traffic will increase at an average annual growth rate (AAGR) of **4.8%** between 2006 and 2010, lower than its AAGR of 6.5% experienced between 1995 and 2005. Over the same period, international air freight traffic is forecast to increase at an AAGR of **5.3%**, also lower than its AAGR of 5.7% experienced between 1995 and 2005. These forecasts are based upon a comprehensive survey of the airline industry.
- On the passenger side, demand continues to be driven by global economic growth, the liberalisation of markets and the emergence of new routes and services. Passenger demand growth has regained a strong relationship with global GDP growth following the disruption to this link between 2001 and 2003.
- However, the nature of this relationship and the multiple on growth may have changed. Over the next five years, developing economies such as China and India will make a greater contribution towards global economic growth. But because average incomes in these countries are growing from low levels, the multiple of air traffic growth to GDP growth may be lower than in previous cycles, when growth was driven by high income developed countries.
- On the freight side, demand is driven by economic growth, globalisation and trade. The most dynamic freight markets are those associated with economies that are both fast-growing and rapidly integrating into the global economy.
- The risks faced by the global airline industry, several of which are beyond its direct control, mean that further volatility cannot be discounted, but the fundamental factors driving growth for both passengers and freight remain reasonably positive. The industry has responded to the shocks of the last five years by improving cost efficiency and by restructuring operations. Further cost efficiencies, rational capacity management and greater operational flexibility (the latter driven by further liberalisation) are necessary to translate the improvements already achieved into a stable and profitable industry over the next five years.

i) International Passenger Growth and Global GDP



i) International Freight Growth and Global GDP



OUTLOOK BY REGION

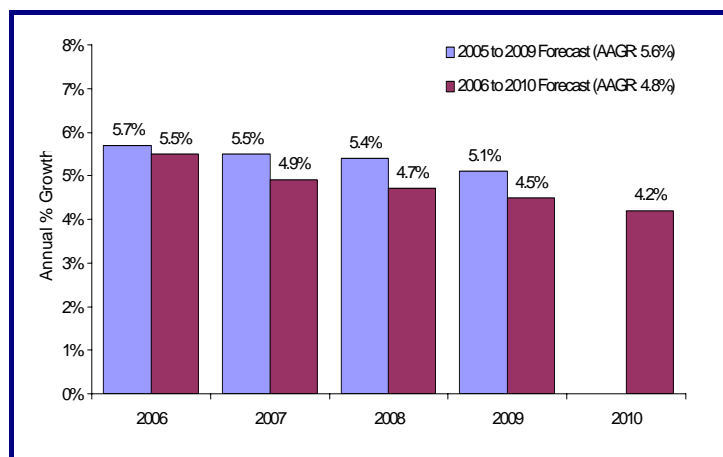
- Regional differences in passenger growth rates will largely reflect differences in regional economic growth and the structure of each regional market. Asia and the Middle East will be boosted by strong GDP growth, along with significant new capacity and new routes. Africa and Latin America will also be boosted by improved GDP growth and, in the case of the latter, further growth in the no-frills airline sector. European growth is relatively low, though Eastern Europe will see a more rapid expansion. North America is expected to be the slowest growing region, reflecting both mature markets and a slower period of growth in the US economy.
- The pattern of forecast growth in freight traffic closely follows expected growth in regional economies and trade flows. Routes linked with Asia Pacific, and China and India in particular, are forecast to show particular strength. Middle Eastern air freight is also expected to show strong growth, as the region's carriers take advantage of the current strong purchasing power for the region provided by high oil prices to increase capacity on existing and new routes.

	Average Annual Growth Rate (AAGR) 2006 to 2010	
	Passenger Numbers	Freight Tonnes
TOTAL INTERNATIONAL	4.8%	5.3%
Africa	5.1%	5.0%
Asia Pacific	5.7%	6.0%
Europe	4.4%	4.6%
Latin America/Caribbean	4.6%	4.3%
Middle East	6.9%	5.8%
North America	4.3%	4.5%

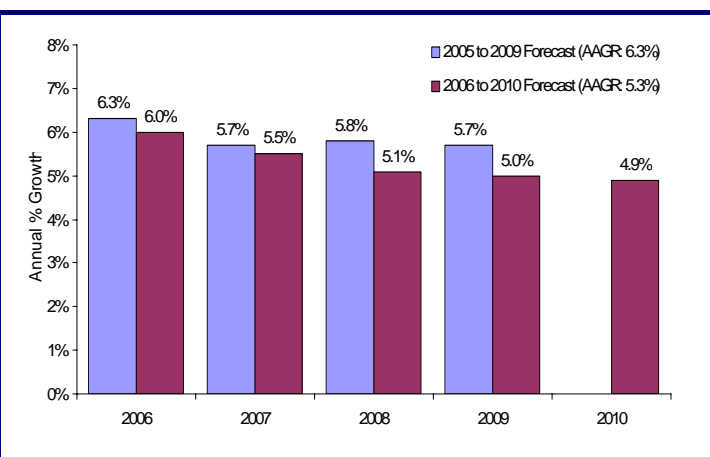
COMPARISON WITH LAST YEAR'S FORECAST

- The 4.8% AAGR passenger forecast for 2006 to 2010 is slightly lower than the 5.6% AAGR forecast last year for the period 2005 to 2009. This partly reflects the removal of above-average growth in 2005 from the forecast period, but may also reflect a more cautious approach to capacity growth among airlines. In particular, greater cost control at airlines has led to a shift in emphasis towards profitable growth rather than just market share growth.
- The 5.3% AAGR freight forecast for 2006 to 2010 is slightly lower than the 6.3% AAGR forecast last year for the period 2005 to 2009. This also partly reflects the removal of above-average growth in 2005 from the forecast period (even though actual 2005 freight growth was lower than forecast). It also reflects slightly lower expectations for the impact of global economic growth on air freight demand.

i) Comparison of Passenger Forecasts



ii) Comparison of Freight Forecasts



KEY DEMAND DRIVERS AND KEY RISKS

- Demand is driven by economic growth, the liberalisation of markets and the emergence of new routes and services. Global GDP growth is forecast to slow from levels of around 5% seen in 2004 and 2005 but will remain above its long-term average rate during the forecast period. US economic growth is expected to slow from recent buoyant levels, but this could be offset by stronger growth in Europe and Japan and by the continued strong growth in emerging economies such as China and India.
- Passenger demand growth has regained a positive relationship with global GDP growth following the disruption to this link between 2001 and 2003. However, the nature of this relationship and the multiple on growth may have changed. Previously, as global growth was driven by developed economies such as the US and Europe it provided a strong boost for air traffic as incomes grew from an already high level. However, over the next five years, developing economies such as China and India will make a greater contribution towards global economic growth. But because average incomes in these countries are growing from much lower levels, the multiple of air traffic growth to GDP growth is likely to be lower than in previous cycles.
- Deregulation can provide substantial benefits for passengers, businesses and the wider economy. The accessibility to global markets – provided by market liberalisation – also provides a boost to investment decisions. However, partial deregulation – that lowers barriers to entry but retains high constraints on adjusting existing capacity – can reduce prices to unsustainable levels. As such, further deregulation is required in both operational and ownership & control restrictions.
- Economic growth boosts air freight directly, as higher economic activity feeds through into higher trade and higher traffic volumes. Strong growth in high-value, time-sensitive sectors also boost demand for air freight over other transport modes.
- However, the airline industry continues to face risks that could negatively impact upon its forecast growth path, 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. International trade imbalances may also pose a risk to future air freight growth if they lead to calls for trade barriers and/or currency realignments. The suspension of the "Doha round" of trade liberalisation talks is also bad news in terms of the loss of potential future traffic growth for airlines. Previous trade liberalisation rounds have boosted global trade and economic growth.
- Even under the forecast growth scenario, the return on capital invested in the airline industry will still be below its cost of capital, i.e. the competitive and sustainable level of return for investors. It is a measure of the challenges faced by the airline industry that even with significant improvement in revenues and cost efficiency it has been unable to generate a sufficient return on capital. Liberalisation, efficiency and greater sharing of risk and reward in the wider aviation industry are required to ensure that long-term investment – and the substantial benefits for customers and the wider economy this brings – is attracted in a sustainable manner.

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APPENDIX

Traffic Growth by Major Route Area.

	Average Annual Growth Rate (AAGR) 2006 to 2010	
	Passenger Numbers	Freight Tonnes
TOTAL INTERNATIONAL	4.8%	5.3%
North Atlantic	4.1%	4.0%
North & Mid Pacific	5.0%	5.2%
Europe – Far East	6.1%	5.5%
Europe – Middle East	5.9%	4.7%
Europe – Africa	5.1%	4.7%
Within Europe	4.0%	3.7%
Within Far East	5.9%	6.9%
Within North America	3.9%	5.4%
Middle East – Far East	7.9%	7.6%
North America – Central America	4.3%	3.6%
North America – South America	4.9%	4.3%
Far East – Southwest Pacific	3.2%	4.4%

Top 10 Countries Ranked by AAGR 2006 to 2010.

Passenger Numbers ¹		Freight Tonnes ²	
Country	AAGR 2006 to 2010	Country	AAGR 2006 to 2010
Poland	9.2%	China	11.6%
Oman	9.0%	Pakistan	8.8%
Bahrain	8.3%	Korea (Republic of)	8.2%
Pakistan	8.2%	India	8.2%
China	8.1%	Bahrain	8.0%
United Arab Emirates	7.9%	Turkey	7.8%
India	7.9%	Sri Lanka	7.4%
Colombia	7.7%	Thailand	6.3%
Ukraine	7.7%	Saudi Arabia	5.9%
Romania	7.5%	Indonesia	5.8%

¹ Only includes countries with traffic in excess of 2 million annual passengers in 2005.

² Only includes countries with traffic in excess of 100,000 tonnes in 2005.