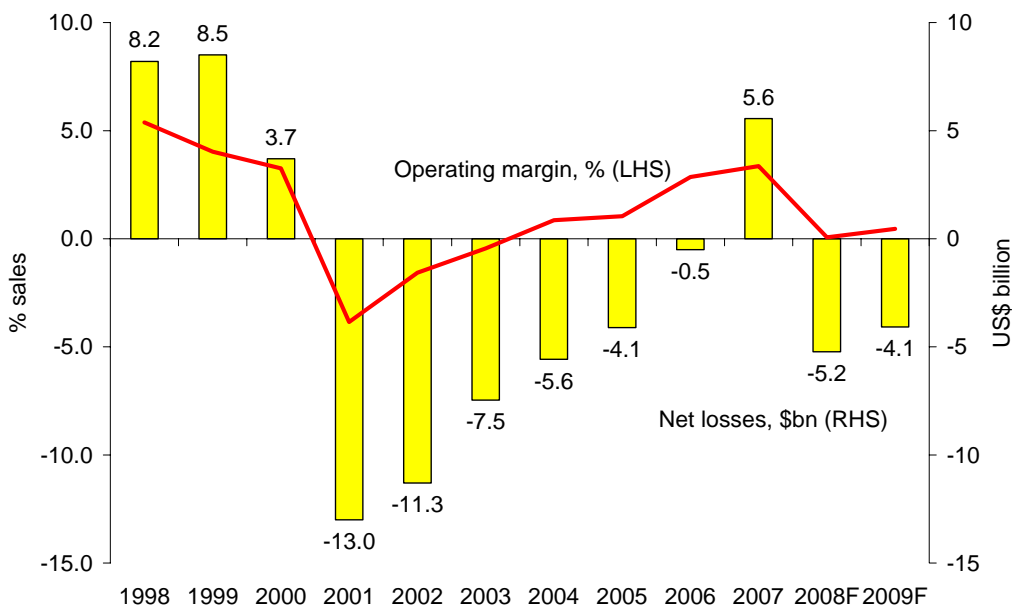


# FINANCIAL FORECAST

September 2008

## SIGNIFICANT LOSSES CONTINUE INTO 2009

- We now forecast that airline industry net losses will total \$5.2 billion this year and weak financial performance will continue into 2009, with further net losses of \$4.1 billion.
- Our last forecast in early June was made during a period of extreme uncertainty over oil prices. As a result we presented two scenarios. One based on oil prices of \$106.5 a barrel and the other on futures market prices at the time (\$135/b) producing an average of \$122/b for 2008. Net losses for 2008 were forecast at \$2.3-\$6.1 billion. Oil prices have since fallen substantially and are not expected to regain levels that had been feared; but the average we now expect of \$113/b this year is still 55% higher than last year.
- A new development has been weaker economic growth outside the US, reflected in a deterioration in the outlook for air travel and freight. We have significantly revised down our forecast for traffic growth. As a result our new forecast of losses this year, at \$5.2 billion is close to the top of the June range.



Source:  
ICAO,  
IATA

- Industry restructuring will produce some benefits in 2009 but the weaker economic outlook will also slow growth of traffic. Oil prices may also be slightly lower at \$110/b but net losses will still be high at \$4.1 billion.

Industry profits, US\$ billion	2006	2007	2008F	2009F	2006	2007	2008F	2009F
	<b>Operating profits</b>				<b>Net profits</b>			
<b>Global</b>	<b>12.9</b>	<b>16.3</b>	<b>0.3</b>	<b>2.6</b>	<b>-0.5</b>	<b>5.6</b>	<b>-5.2</b>	<b>-4.1</b>
excluding restructuring costs					3.1	5.6	-5.2	-4.1
<b>Regions</b>								
North America	7.3	9.9	-0.8	0.3	-2.7	2.8	-5.0	-4.0
excluding restructuring costs					0.9	2.8	-5.0	-4.0
Europe	5.4	5.8	1.8	1.8	1.8	2.1	0.3	0.0
Asia-Pacific	0.9	0.7	0.0	0.4	0.8	0.9	0.3	0.1
Middle East	0.1	0.3	0.2	0.3	0.2	0.3	0.2	0.2
Latin America	-0.7	-0.3	-0.4	-0.2	-0.2	-0.1	-0.3	-0.2
Africa	0.0	-0.1	-0.4	-0.1	-0.4	-0.4	-0.7	-0.3

Source: ICAO data for operating profits to 2007. IATA estimate for 2006-07 net profits and 2008-09 forecasts. Excludes 'fresh-start' items.

## FIRST HALF LOSSES HAVE EXCEEDED \$2.7 BN

Half year results		H1 2007		H1 2008	
		US \$ million			
Region	Nb Airlines	Op. profits	Net profits	Op. profits	Net profits
US*	10	3705	4756	-911	-2476
Europe	10	2392	2704	1791	-36
Asia - Pacific	6	1123	1939	1151	-207
Other	2	337	134	278	42
	28	7,557	9,533	2,310	-2,677

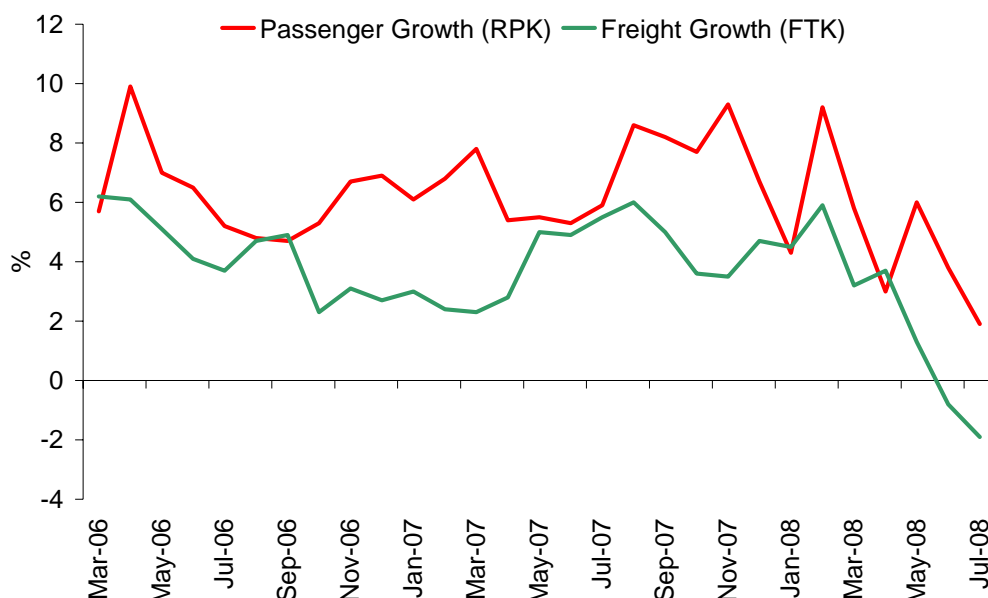
\* Excluding reorganisation costs

Source: company reports

Note: these are corporate wide results, whereas our forecasts are for airline-only results.

- Profitability deteriorated dramatically in the first half of 2008. Results from a sample of 28 major airlines show operating profits have fallen from \$7.6 billion in the first half of 2007 to \$2.3 billion in the first half of this year. The decline of net profits has been even sharper with losses of \$2.7 billion in the first half of 2008.
- The largest deterioration, with net losses so far this year of \$2.5 billion, has been for US airlines. The US industry has been sharply squeezed from rising fuel costs and shrinking domestic markets. Relatively low hedging levels left airlines fully exposed to the rise in dollar fuel prices, while the collapse to 28 year lows in US consumer confidence led to a fall in travel on domestic markets.
- The deterioration of operating profits has not been as severe for airlines in other regions. During the first half of the year hedging and US dollar weakness provided some offset to the rise in fuel prices. Moreover, economic growth started the year strongly in Europe and Asia. That growth is now slowing sharply and, although fuel prices have fallen, hedging levels are diminishing and the US dollar is strengthening.
- Results so far are consistent with our new forecast for industry net losses this year of \$5.2 billion.

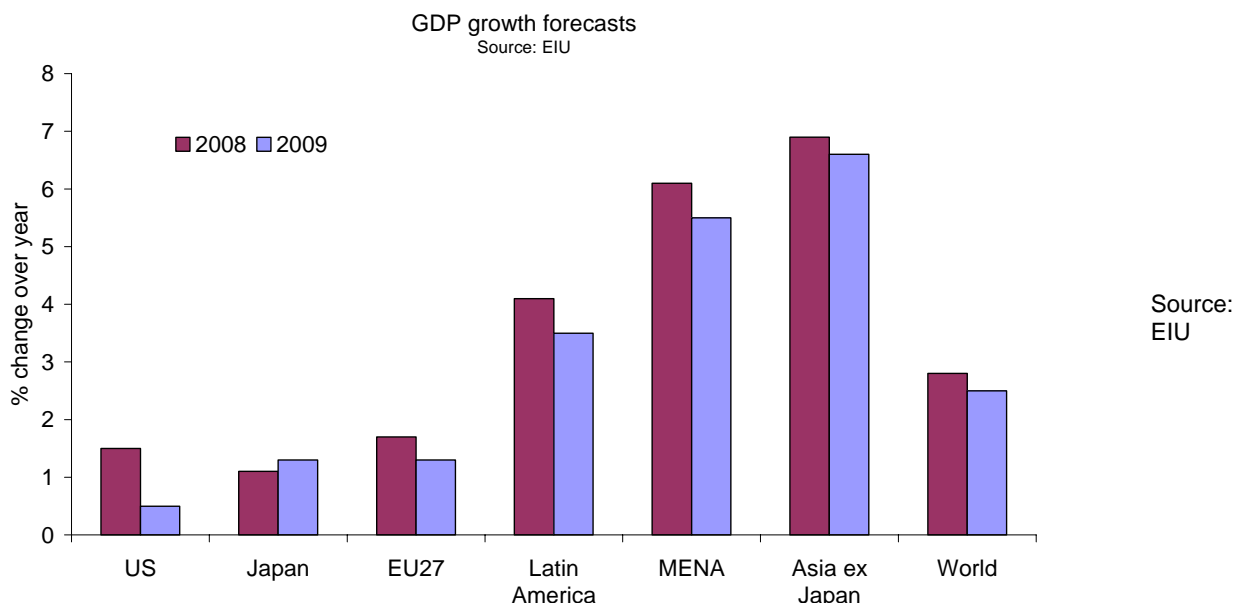
## TRAVEL AND FREIGHT TURNED DOWN SHARPLY



Source: IATA

- The biggest change in the outlook has been the sharper than expected deterioration in air travel and air freight growth. After a relatively robust first five months of the year, international traffic growth has slowed considerably in June and July, with absolute declines in air freight volumes. Domestic traffic has been shrinking all year in the US but also slowed sharply in other markets by mid-year.
- Economic growth in the developed economies was a fairly robust 2.5% in the first quarter but then slowed sharply in the second quarter, particularly in Europe but also in Asia. Recent surveys of both business and consumer confidence have shown sharp declines. Consumer confidence in the US, which fell first from late last year, appears to have bottomed out but at a level consistent with a fall in consumer spending (and travel). This suggests travel and air freight markets will remain weak in the second half of 2008.

## THE ECONOMIC OUTLOOK IS WEAKER IN 2009



- When we produced our last forecast in early June most economic forecasters were suggesting the second half of this year would be the low point, with stronger economic growth in the US and globally in 2009. Now forecasts anticipate a much longer period before recovery to normal economic growth. Next year is expected to be weaker than this, particularly in the US economy but also in Europe and most emerging markets. Growth is forecast to be weaker in 2009 but expansion remains relatively strong in many emerging markets which should provide more support for travel and air freight than in the developed markets.
- One of the reasons for the weaker outlook for economic growth in 2009 is that the increase in inflation has prevented central banks, outside the US, from cutting interest rates to offset the spreading impact of the credit crunch and the squeeze on disposable incomes from higher food and energy prices. A recovery to more normal economic growth rates is now not expected until 2010.

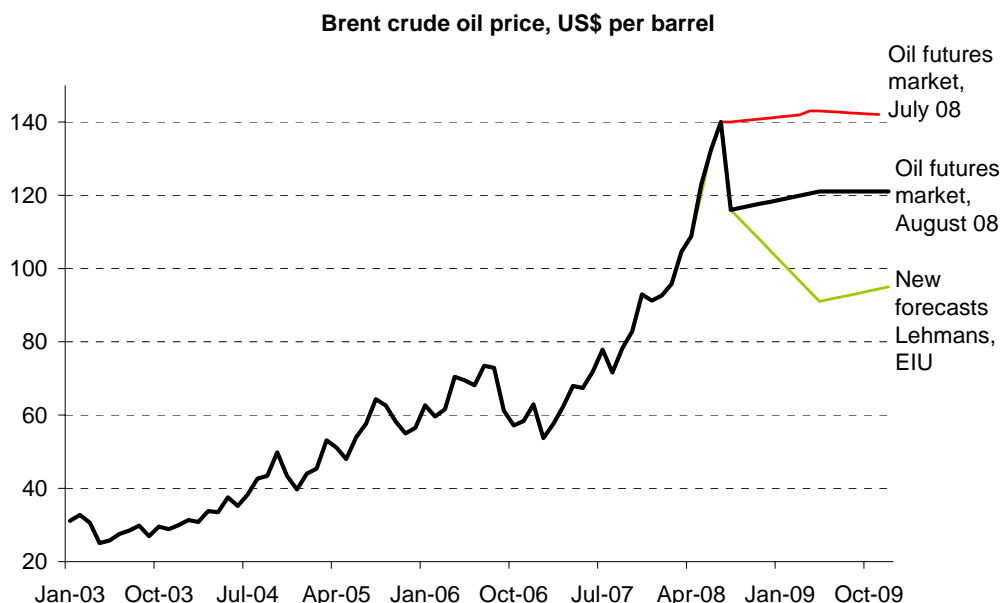
## TRAFFIC AND CAPACITY GROWTH MUCH WEAKER

Annual average growth rates, %	2006	2007	2008F	2009F	2006	2007	2008F	2009F
	Traffic volumes (tkp)				Capacity (atk)			
<b>Global</b>	5.3	5.3	2.8	2.9	4.1	5.0	4.0	2.2
<b>Regions</b>								
North America	3.6	2.9	0.1	-0.6	1.2	3.1	2.3	-3.4
Europe	4.9	4.7	3.2	2.9	3.9	3.2	3.9	2.8
Asia-Pacific	7.6	6.8	3.3	3.9	6.9	7.0	4.1	4.3
Middle East	11.8	15.1	10.8	7.9	12.6	12.8	10.9	9.3
Latin America	-3.4	5.7	5.6	4.2	1.5	6.9	5.5	5.1
Africa	7.0	5.9	-1.4	2.9	1.8	5.2	-0.9	2.2

Source: ICAO data to 2007. IATA 2008-09 forecasts. Domestic and international traffic. Includes passenger and cargo by weight.

- We have significant revised down our forecasts for traffic growth this year and next, in response to the weaker economic outlook. This year traffic volume growth has been reduced from 3.9% in our June forecast to 2.8%, and for 2009 from growth of 4.5% down to just 2.9%. North American airlines are expected to see an absolute reduction in traffic carried in 2009, in response to the weak economy and capacity cuts.
- Airlines are responding to this outlook by announcing cuts or less growth in capacity. In North America we forecast capacity will shrink by 3.4% in 2009, as most of the cuts already proposed are implemented. At the level of oil prices forecast this will allow some reduction of forecast losses for airlines in the region. Overall we expect capacity growth to slow to just 2.2%, allowing a small recovery in load factors.

## OIL PRICES EASE BACK BUT REMAIN HIGH



Source:  
RBS,  
Bloomberg

- Spot oil prices fell back \$30 a barrel from their peak of \$147/b in July, as part of the futures market-driven bubble generated in May-July was deflated by profit-taking and growing concern about economic weakness. The much weaker economic outlook has led to a fall in all commodity prices and few now expect oil prices to return to July peaks over the next 18 months. Some major forecasters are now projecting oil prices at \$91-94/b in 2009. Oil futures markets have fallen from 2009 prices of over \$140/b to around \$120/b. Our oil price forecast, based on a consensus of experts, is \$110/b for 2009 following an average of \$113/b this year.
- This oil price is still very high, implying jet fuel prices of \$136/b in 2009. Moreover, hedging will offer less protection. As a result the fuel bill is forecast to rise to \$186 billion or 36% of operating costs this year, but then further to \$223 billion or 40% of operating costs in 2009.

System-wide global commercial aviation	2000	2001	2002	2003	2004	2005	2006	2007	2008F	2009F
<b>REVENUES, \$ billion</b>	329	307	306	322	379	413	452	485	520	557
Passenger	256	239	238	249	294	323	355	384	412	441
Cargo	40	39	38	40	47	48	52	54	57	60
Traffic volumes										
Passenger growth, tkp, %	8.6	-2.7	1.0	2.3	14.9	7.0	5.9	5.9	3.2	3.0
Passenger numbers, millions	1672	1640	1639	1691	1888	2022	2124	2260	2321	2379
Cargo growth, tkp, %	9.1	-6.0	8.7	3.9	7.9	0.4	3.9	4.0	1.8	2.5
Freight tonnes, millions	30.4	28.8	31.4	33.5	36.7	37.6	39.8	41.6	42.4	43.4
World economic growth, %	4.7	1.6	1.9	2.7	4.1	3.5	4.0	3.8	2.8	2.6
Yield growth, %	-1.1	-2.8	-3.7	2.3	4.5	4.0	4.0	1.7	4.4	4.2
Yield growth, inflation/ex rate adjusted %	-2.3	-2.9	-5.9	-5.3	-2.0	0.1	0.5	-3.2	-3.2	1.8
<b>EXPENSES, \$ billion</b>	318	319	311	323	376	409	440	468	520	555
Fuel	46	43	40	44	61	90	111	136	186	223
% of expenses	14	13	13	14	16	22	26	29	36	40
Crude oil price, Brent, \$/b	28.8	24.7	25.1	28.8	38.3	54.5	65.1	73.0	113.0	110.0
Non-Fuel	272	276	270	279	314	319	328	332	333	331
cents per atk (non-fuel unit cost)	39.2	39.7	38.8	38.9	39.9	38.8	38.3	36.9	35.6	34.6
% change	-2.3	1.4	-2.3	0.3	2.6	-2.9	-1.3	-3.5	-3.5	-2.8
% change, adjusted for ex rate	-0.2	4.1	-3.0	-5.0	-1.2	-3.5	-1.7	-5.5	-6.4	-2.0
Break-even weight load factor, %	60.8	61.5	63.2	62.3	63.4	63.3	62.9	62.8	63.5	63.7
Weight load factor achieved, %	61.5	59.0	60.9	60.8	62.5	62.6	63.3	63.6	62.8	63.2
<b>OPERATING PROFIT, \$ billion</b>	10.7	-11.8	-4.8	-1.4	3.3	4.3	12.9	16.3	0.3	2.6
% margin	3.3	-3.8	-1.6	-0.4	0.9	1.0	2.9	3.4	0.1	0.5
<b>NET PROFIT, \$ billion</b>	3.7	-13.0	-11.3	-7.5	-5.6	-4.1	-0.5	5.6	-5.2	-4.1
% margin	1.1	-4.2	-3.7	-2.3	-1.5	-1.0	-0.1	1.1	-1.0	-0.7

Source: ICAO data for key items to 2007. IATA estimate 2006-7 net profits and 2008-9 forecasts. Excludes 'fresh-start' accounting items.

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