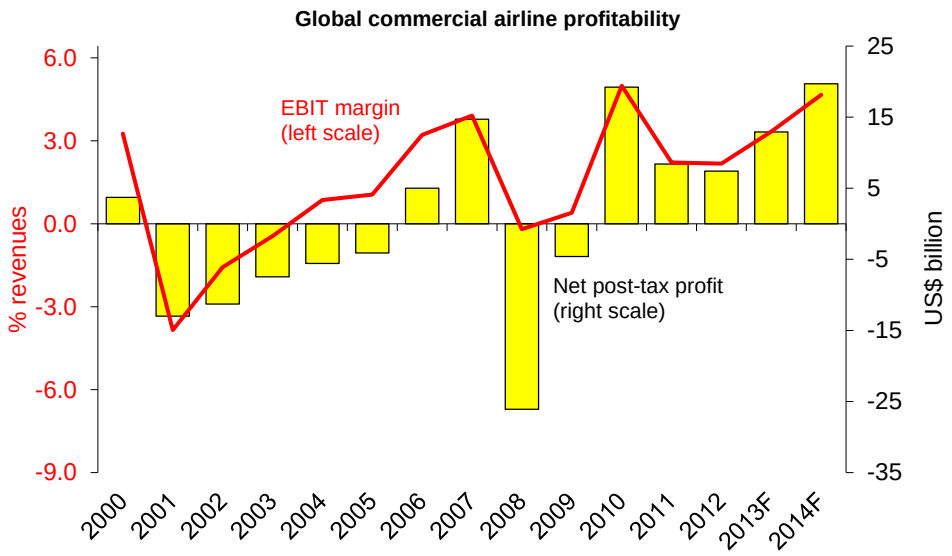
FINANCIAL FORECAST

December 2013

UPGRADED OUTLOOK FOR AIRLINE PERFORMANCE

- We now expect the global commercial airline industry to generate net post-tax profits of $12.9 billion this year and $19.7 billion, or 2.6% of revenues, next year. This represents an upward revision of $1.2 billion in 2013 and $3.3 billion in 2014, which reflects the impact of lower jet fuel prices over the forecast period and the improvements to industry structure and efficiency already visible in quarterly results this year.



Source:
ICAO (history),
IATA (forecast)

- The outlook for revenues is unchanged but its composition is different, with stronger passenger markets but weaker cargo. The robustness of air travel, despite high oil prices and relatively weak economic growth, is one of the positive developments in recent years. However, we are concerned that the weakness of air cargo markets may persist for some time. A downward revision in the outlook for costs reflects a slightly lower trajectory for crude oil prices, a narrower crack spread with jet fuel prices and also slower growth in capacity, reflecting the changes in industry structure and an associated focus on improving efficiency and the utilization of aircraft. We are now forecasting worldwide passenger load factors to exceed 81% in 2014 for the first time.

- The pattern of economic growth, with improving developed economies and relatively disappointing growth in the BRICs next year will also influence airline performance. A stronger US economy coinciding with a consolidated airline industry at home and on the North Atlantic is expected to produce a much improved performance for N. American airlines next year. Note that there will be considerable variation in performance between individual airlines. Asia-Pacific airlines will still generate the second largest net profit, but the weakness of cargo and key Asian growth markets will subdue performance in this region. European airlines are still hampered by weak home markets in parts of the Eurozone, but the performance of joint ventures on the N. Atlantic will help to improve profitability. Airlines in the Middle East and Latin America are forecast to be 2nd and 3rd to N. America in terms of margins. Africa does little better than break-even.

System-wide global commercial airlines	EBIT margin, % revenues					Net profits, $ billion				
	2010	2011	2012	2013F	2014F	2010	2011	2012	2013F	2014F
Global	**5.0%**	**2.2%**	**2.2%**	**3.3%**	**4.7%**	**19.2**	**8.4**	**7.4**	**12.9**	**19.7**
Regions										
North America	5.7%	3.0%	3.4%	4.8%	6.4%	4.2	1.7	2.3	5.8	8.3
Europe	2.4%	0.8%	0.7%	1.3%	2.0%	1.9	0.3	0.4	1.7	3.2
Asia-Pacific	8.0%	3.5%	3.3%	4.1%	4.4%	11.1	5.1	4.0	3.2	4.1
Middle East	3.7%	3.1%	3.0%	3.8%	4.7%	0.9	1.0	1.0	1.6	2.4
Latin America	5.1%	2.0%	1.5%	3.1%	5.1%	1.0	0.2	-0.2	0.7	1.5
Africa	1.7%	0.6%	-0.4%	-0.5%	0.7%	0.1	0.0	-0.1	-0.1	0.1

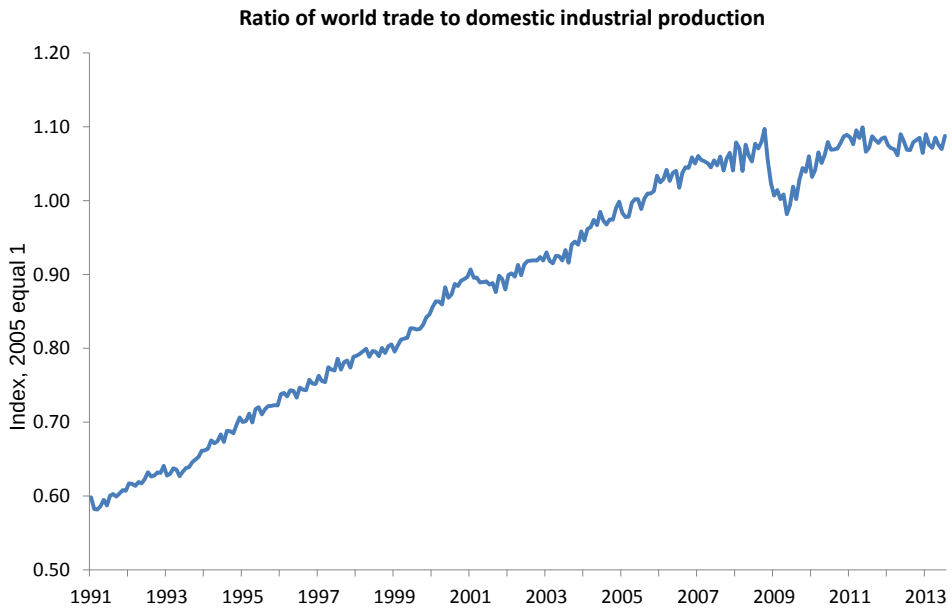
Source: ICAO revised data 2009-11. IATA estimates for regions in 2011. IATA estimate for 2012 and forecast for 2013-14.
Note: bankruptcy reorganization costs are excluded. Also ICAO made some substantial revisions to historic data in their 2013 Annual Report to the Council.

BUSINESS ENVIRONMENT IMPROVING BUT…

- The fortunes of the commercial airline industry are inextricably linked to the strength of global economic development. After the post-recession 2010 peak, economic activity slowed in both 2011 and 2012. Airline industry profits fell in both years, after its 2010 peak. The improvement visible in financial performance during 2013 is in part due to the upturn of economic growth, first signaled by rising business confidence in 2012Q4 and then followed by a slow but significant upturn in industrial production and world trade growth.

Source: Netherlands CPB, Markit

- But the most worrying recent economic development has been the apparent halt to globalization. World trade has slowed, since the recession, to grow no faster than domestic industrial production.

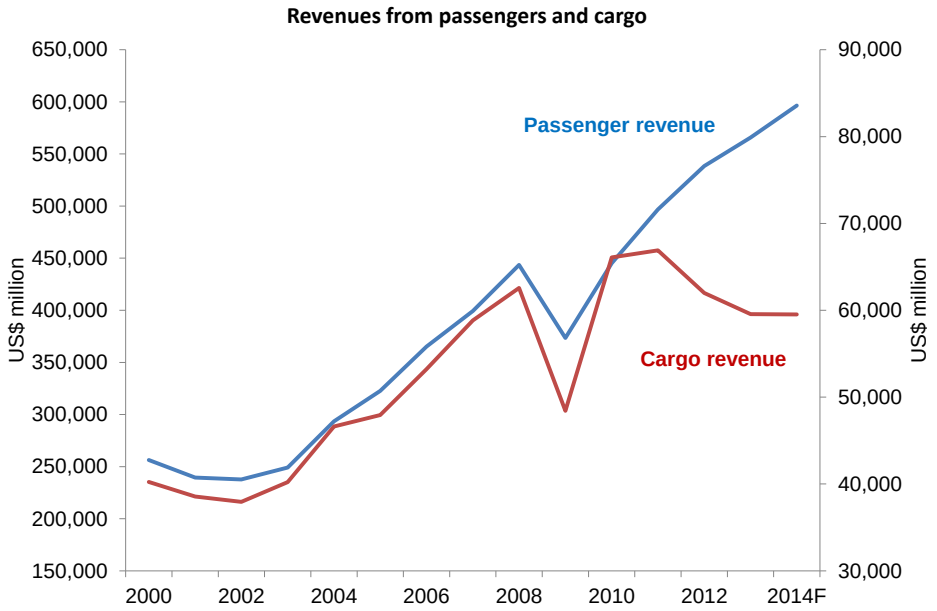


Source: Netherlands CPB, IATA

- Since the 1950s commercial aviation has flourished with post-war trade liberalization and the globalization of supply chains; the vertical disintegration of production we see most visible in the products of companies like Apple and Dell. The growth of air travel and air cargo is much more closely linked to the expansion of international trade than to GDP. An end to the rapid growth of international trade, if that persists, would mean much slower growth of air transport in the future.
- Production is being 'on-shored' partly because of rising trade barriers since the recession – which could potentially be resisted and reversed – and partly due to a market driven slowdown to further globalization – the effects of earlier trade liberalization are fading and low labour cost locations are becoming less important

or more costly. Hopefully, the Bali trade deal just concluded will fire up the engines of international trade once more. However, that might take some time to come about and lift air cargo growth significantly.

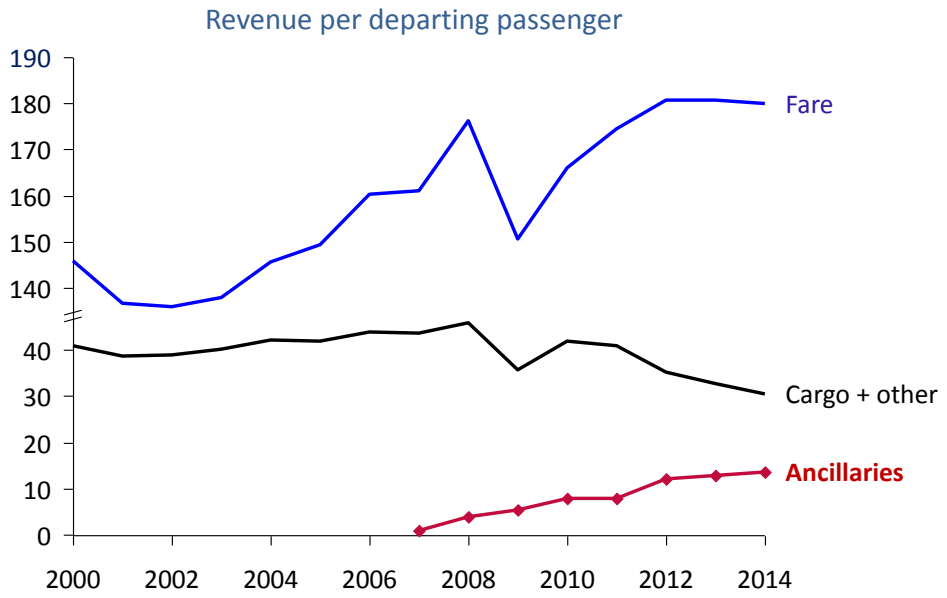
- The adverse consequences for air cargo volumes in the short term are clear. But the impact on cargo revenues has been made worse by the belly capacity arriving from the improving passenger business, which is adding to the downward pressure on cargo yields. We expect the moderate improvement in cargo volumes next year to be offset by lower yields.



Source:
ICAO (history),
IATA (forecast)

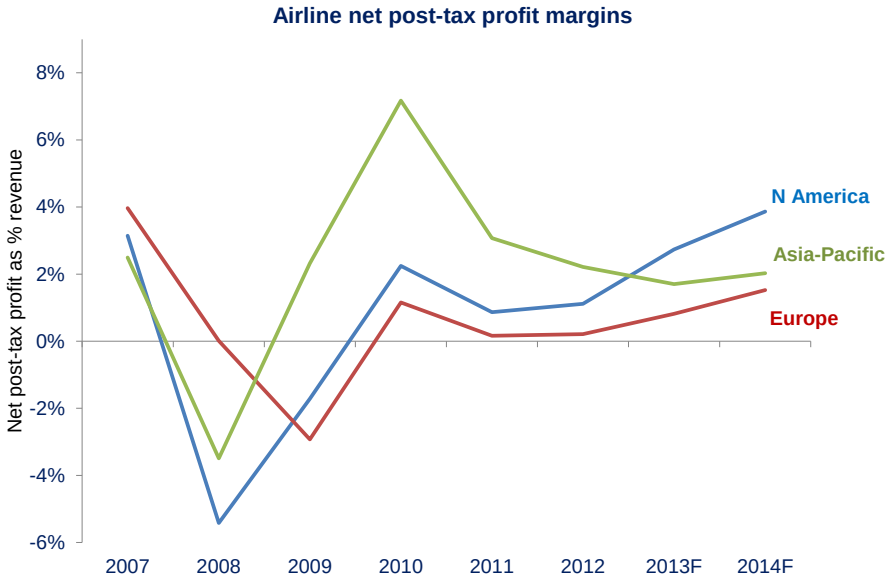
CONSOLIDATION AND ANCILLARIES ARE KEY

- Improved industry structure and efficiency gains should allow the industry to leverage the improving economic cycle to boost profitability significantly in 2014. Airlines in North America, where consolidation has progressed furthest, are expected to generate the largest profits next year. European airlines, still suffering from weak home markets in much of the eurozone, will benefit from the success of JVs on the North Atlantic.



Source:
IATA, IdeaWorks 2007-2012 historic data for ancillary total revenues, IATA adjustment to per passenger and forecast)

- Ancillaries have been the second key factor behind better financial performance. Worldwide ancillaries are forecast to rise to an estimated average of $13 per passenger. Their share in airline revenues has been boosted even further by the recent weakness of cargo revenues, a key factor behind the relatively weak performance of the Asia-Pacific airlines this year and next. But even with ancillaries, industry net profits next year of $19.7 billion are still only $5.94 per passenger, a margin vulnerable to shocks from regulatory costs or market developments.



Source:
ICAO (history)
IATA (forecast)

System-wide global commercial airlines	Passenger traffic (RPK), % change over year					Passenger capacity (ASK), % change over year				
	2010	2011	2012	2013F	2014F	2010	2011	2012	2013F	2014F
Global	7.9	6.2	5.3	5.3	6.0	4.5	6.5	4.0	4.4	5.2
Regions										
North America	4.5	2.8	1.3	2.0	2.5	2.3	2.8	0.4	1.6	2.0
Europe	4.1	8.2	4.7	3.9	4.7	1.6	8.6	2.8	2.5	4.5
Asia-Pacific	11.8	6.6	6.2	7.6	7.4	6.3	7.0	5.4	7.1	7.0
Middle East	17.8	9.8	15.1	10.8	13.0	13.3	9.8	12.4	11.4	12.0
Latin America	12.3	11.2	9.6	6.5	8.5	6.8	9.3	7.6	4.6	6.5
Africa	12.5	1.6	7.5	6.8	7.8	9.3	3.2	6.4	5.0	6.5

Source: IATA. Domestic and international traffic.

System-wide global commercial airlines	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013F	2014F
REVENUES, $ billion	379	413	465	510	570	476	579	636	679	708	743
% change	17.7	9.1	12.5	9.6	11.7	-16.5	21.8	9.7	6.9	4.3	4.9
Passenger, $ billion	294	323	365	399	444	374	445	497	538	566	596
Cargo, $ billion	47	48	53	59	63	48	66	67	62	60	60
Traffic volumes											
Passenger growth, rpk, %	13.6	8.1	6.2	7.5	2.7	-2.4	8.8	6.2	5.3	5.3	6.0
Sched passenger numbers, millions	2,014	2,157	2,277	2,478	2,515	2,479	2,681	2,845	2,977	3,129	3,312
Cargo growth, ftk, %	10.3	2.5	6.3	4.7	-0.7	-8.8	19.4	-0.1	-1.6	1.0	2.1
Freight tonnes, millions	38.4	39.4	41.8	44.4	42.9	42.6	50.7	51.4	51.1	51.6	52.5
World economic growth, %	4.2	3.4	4.0	3.8	1.7	-2.3	4.0	2.6	2.2	2.0	2.7
Passenger yield, %	3.7	1.7	6.6	1.7	8.2	-13.7	9.6	5.0	2.9	-0.2	-0.6
Cargo yield %	5.1	0.3	4.4	5.6	7.0	-15.2	14.4	1.3	-5.8	-4.9	-2.1
EXPENSES, $ billion	376	409	450	490	571	474	550	622	665	685	708
% change	16.2	8.9	10.1	8.8	16.5	-16.9	16.1	12.9	7.0	3.0	3.5
Fuel, $ billion	65	91	116	133	187	123	139	176	210	211	210
% of expenses	17	22	26	27	33	26	25	28	32	31	30
Crude oil price, Brent, $/b	38.3	54.5	65.1	73.0	99.0	62.0	79.4	111.2	111.8	108.2	104.5
Jet kerosene price, $/b	49.7	71.0	81.9	90.0	126.7	71.1	91.4	127.5	129.6	124.0	120.6
Fuel consumption, billion gallons	65	68	68	70	69	66	69	71	72	74	76
CO_2 emissions, million tonnes	623	645	651	666	661	628	658	679	689	705	726
Non-fuel, $ billion	311	318	334	356	384	351	412	446	455	473	498
cents per atk (non-fuel unit cost)	40.1	38.9	39.0	39.0	40.9	39.0	43.3	44.6	44.3	44.4	44.6
% change	1.4	-3.0	0.2	0.1	4.9	-4.7	11.2	2.8	-0.5	0.1	0.5
Capacity growth, atk, %	9.7	5.7	4.8	6.6	2.7	-4.2	5.5	5.3	2.7	3.9	4.7
Flights, million	23.8	24.9	25.5	26.7	26.5	25.9	26.7	27.6	28.3	29.3	30.6
Break-even weight load factor, %	60.6	60.8	60.3	59.9	61.8	61.4	62.0	63.2	63.7	63.0	62.4
Weight load factor achieved, %	61.1	61.5	62.3	62.4	61.7	61.6	65.3	64.7	65.1	65.2	65.4
Passenger load factor achieved, %	73.4	74.9	76.0	77.0	75.9	76.0	78.5	78.3	79.2	80.3	81.3
OPERATING PROFIT, $ billion	3.3	4.4	15.0	19.9	-1.1	1.9	28.9	14.1	14.8	23.6	34.7
% margin	0.9	1.1	3.2	3.9	-0.2	0.4	5.0	2.2	2.2	3.3	4.7
NET PROFIT, $ billion	-5.6	-4.1	5.0	14.7	-26.1	-4.6	19.2	8.4	7.4	12.9	19.7
% margin	-1.5	-1.0	1.1	2.9	-4.6	-1.0	3.3	1.3	1.1	1.8	2.6
per departing passenger, $	-2.77	-1.91	2.20	5.93	-10.38	-1.86	7.16	2.95	2.49	4.13	5.94
RETURN ON INVESTED CAPITAL, %	2.9	3.0	4.6	5.5	1.4	2.0	6.3	4.7	3.9	4.7	5.7

Source: ICAO data to 2009-11 (note revisions to 2009 and 2010 data). IATA estimate for 2012 and forecast for 2013-14. Passenger and freight numbers are global system-wide collected by IATA, including some non-ICAO states. Bankruptcy reorganization charges excluded.