

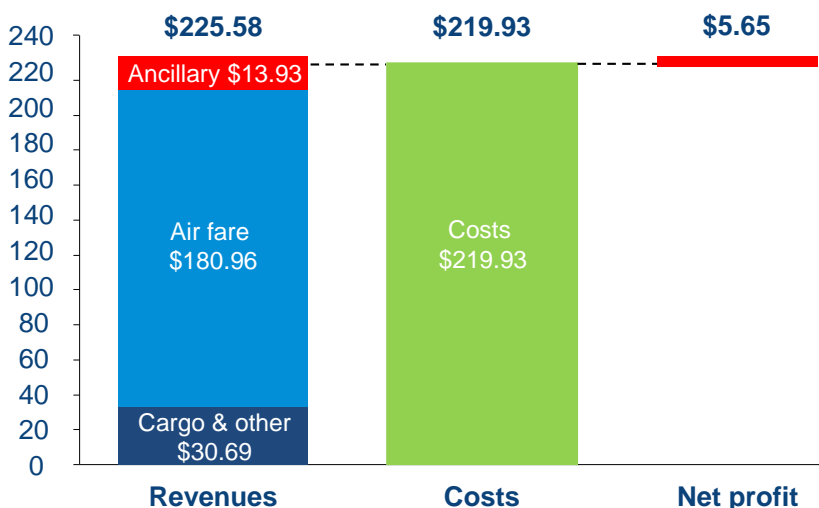
FINANCIAL FORECAST

March 2014

PROFITS STILL RISING BUT SO IS RISK

➤ We have made a small downgrade to our forecast for airline industry net profits in 2014, as a result of the impact of recent developments on jet fuel prices and emerging market growth. However, these adverse impacts have been offset somewhat by solid momentum in the recent cyclical economic upturn. We continue to expect a significant improvement in airline profits this year compared to 2013. Industry-wide net post-tax profits are forecast to rise from \$12.9 billion in 2013 to \$18.7 billion this year, downgraded from our previous forecast in December of \$19.7 billion for 2014. This appears to be a substantial profit but it's not for a \$745 billion industry; a margin of just 2.5%. This year the industry is forecast to make an average of \$5.65 per departing passenger. That's still a fragile margin in a risky business environment.

Forecast 2014 worldwide airline results per departing passenger



Source: IATA

➤ For the most part, the developments we expected at the time of our last forecast are happening: airlines have reported improving profits, the economic cycle is turning upwards and oil prices remain in the range of the past few years. In fact the economic cycle is looking stronger than expected, and that has helped to raise demand for air cargo by more than expected. The downside to recent events has been an increase in risk from a couple of sources. First, capital is flowing into US dollar assets causing problems for a number of emerging economies and slowing their growth. Second, the crisis in Ukraine has increased geo-political risk and put upward pressure on oil prices. The net impact on the profit forecast this year is a small negative.

➤ However, the regional picture varies. Most regions are forecast to improve by slightly less than we were expecting in December. The exception is North America, where we have revised up our projection for 2014 largely on the basis of a strong finish to 2013 and further evidence of structural improvements in this region.

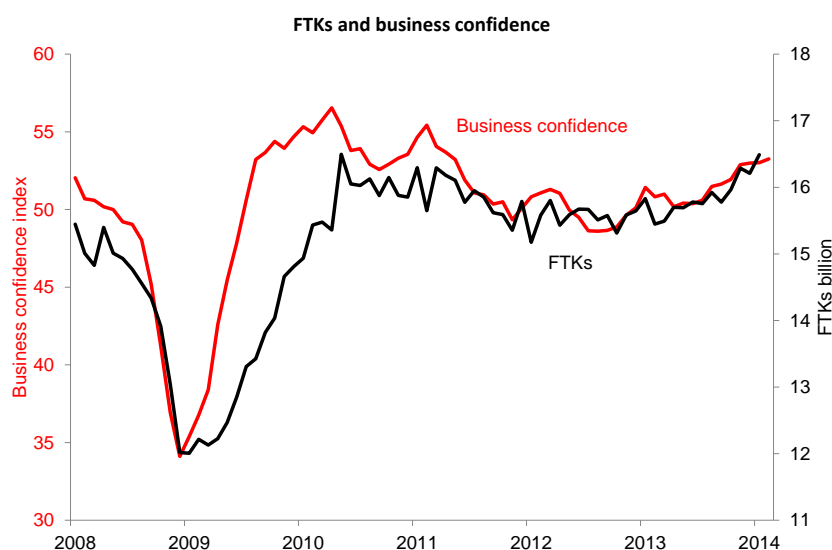
System-wide global commercial airlines	EBIT margin, % revenues					Net profits, \$ billion				
	2010	2011	2012	2013E	2014F	2010	2011	2012	2013E	2014F
Global	4.9%	2.3%	1.8%	3.0%	4.3%	17.3	7.5	6.1	12.9	18.7
Regions										
North America	5.7%	3.0%	3.4%	5.2%	6.5%	4.2	1.7	2.3	6.8	8.6
Europe	2.4%	0.8%	0.7%	1.1%	1.9%	1.9	0.3	0.4	1.2	3.1
Asia-Pacific	8.0%	3.8%	1.9%	2.9%	3.4%	9.2	4.2	2.7	3.0	3.7
Middle East	3.7%	3.1%	3.0%	3.8%	4.2%	0.9	1.0	1.0	1.6	2.2
Latin America	5.1%	2.0%	1.5%	2.2%	3.8%	1.0	0.2	-0.2	0.4	1.0
Africa	1.7%	0.6%	-0.4%	-0.5%	0.8%	0.1	0.0	-0.1	-0.1	0.1

Source: ICAO revised data 2010-12. IATA estimates for regions in 2011-12. IATA estimate for 2013 and forecast for 2014.

Note: bankruptcy reorganization costs are excluded. Also ICAO made some substantial revisions to historic data in their 2013 Annual Report to the Council.

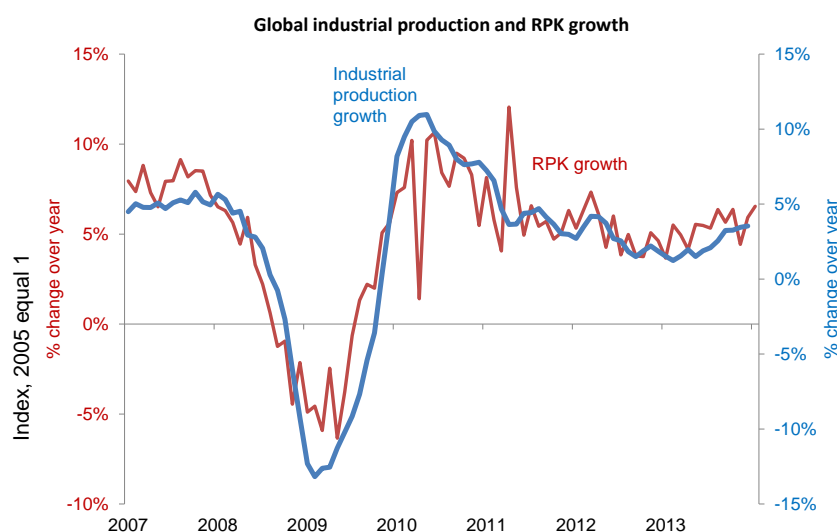
THE DEMAND CYCLE IS TURNING UP

- Evidence is strengthening that the cyclical economic upturn, evident from the second half of 2013, is more durable than the 'false dawns' of 2011 and 2012, when business confidence and economic activity started a promising rise, only to be forced down again by renewed economic crises. The Ukraine situation reminds us that shocks can and will occur unexpectedly. However, the major factors depressing economic growth after the financial crisis of 2008 have diminished substantially.
- Driving this cyclical upturn in the developed economies has been a reduction in the degree of budgetary tightening, continued loose monetary policy, and substantial progress in reducing the 'headwinds' from the financial crisis with much improved balance sheets in the household and banking sectors. This has boosted business confidence, domestic industrial production and international trade.
- Air cargo volumes (FTKs) closely track the ups and downs of business confidence. The decision to ship by air, more costly than surface transport, is very dependent on the confidence of businesses that there will be strong demand or the need to restock. The steady improvement of business confidence since mid-2013 led, a few months later, to a similar rise in worldwide FTKs. By January this year FTKs had risen back to the previous peak of early 2010.



Source: IATA, Markit

- This cyclical upturn is stronger than we anticipated back in December and we have raised our forecast for air cargo volume growth to 4%. However, world trade is still only growing in line with domestic industrial production. In normal cycles world trade grows 2x as fast as domestic output. Without the current degree of on-shoring and non-tariff protectionist measures we would be forecast cargo growth closer to 8%.



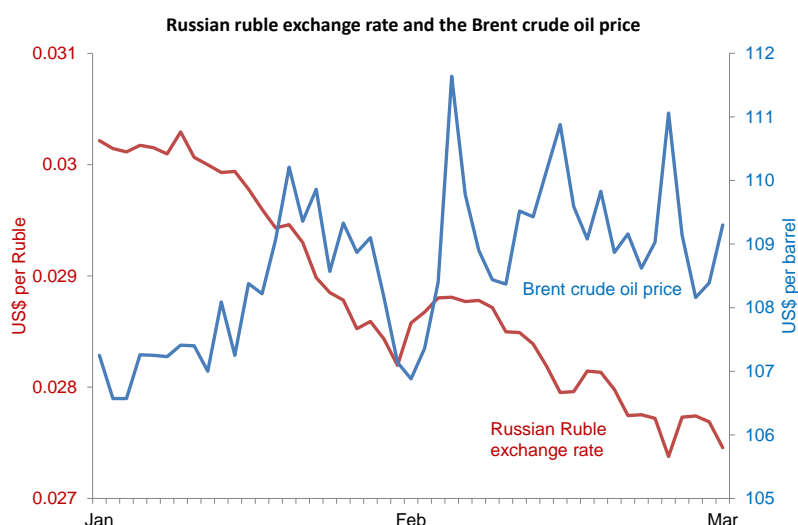
Source: Netherlands CPB, IATA

- Air travel is driven largely by the incomes and confidence of households and businesses, and is less affected by the weakness of international trade (although business travel is). There has been a slowdown in growth since the post-recession rebound in 2009/10 but the air travel market has remained much stronger

than air cargo throughout – because the economic conditions facing most passengers, proxied in the chart above by industrial production growth, continued to rise to a much greater extent than international trade. The acceleration of industrial production through 2013 has been matched by an acceleration of RPKs.

BUT SO ARE FINANCIAL AND POLITICAL RISKS

- A new set of risks have emerged in recent months. Capital has been flowing into US dollar assets, attracted by improving economic prospects in the US as well as the impact of the tapering of asset purchases by the US central bank. Emerging economies with large current account deficits, including growth markets such as Turkey, India, Indonesia, South Africa, have faced capital outflows and have been forced to tighten monetary policy to protect their exchange rates, which has slowed economic growth. Growth in these emerging markets generates proportionately more air travel than in mature developed travel markets. Consequently, the emerging market slowdown has caused a small reduction in our forecast for RPK growth this year.

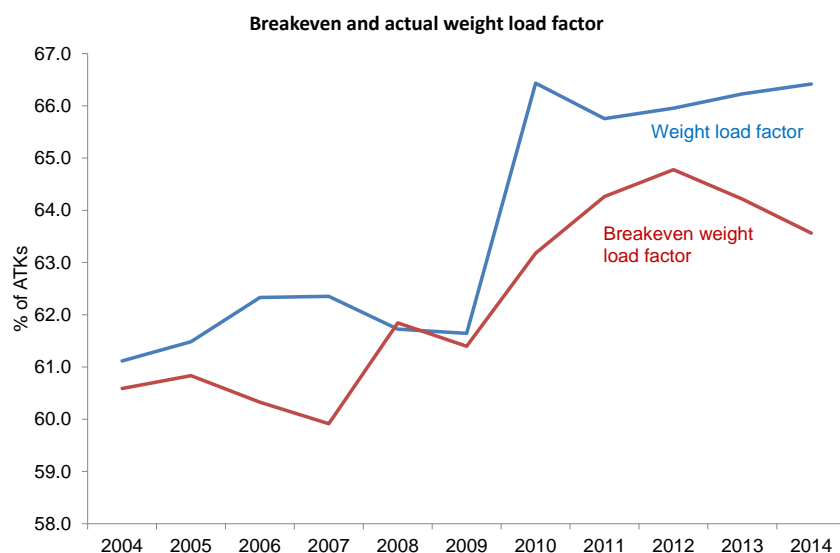


Source:
Haver

- The Ukraine crisis has, in addition to depressing the Russian Ruble, put upward pressure on oil prices. Reflecting the heightened uncertainty the oil futures price curve has shifted upwards. We have followed the market and raised our forecast for average crude oil prices this year from \$104.5/b to \$108/b.

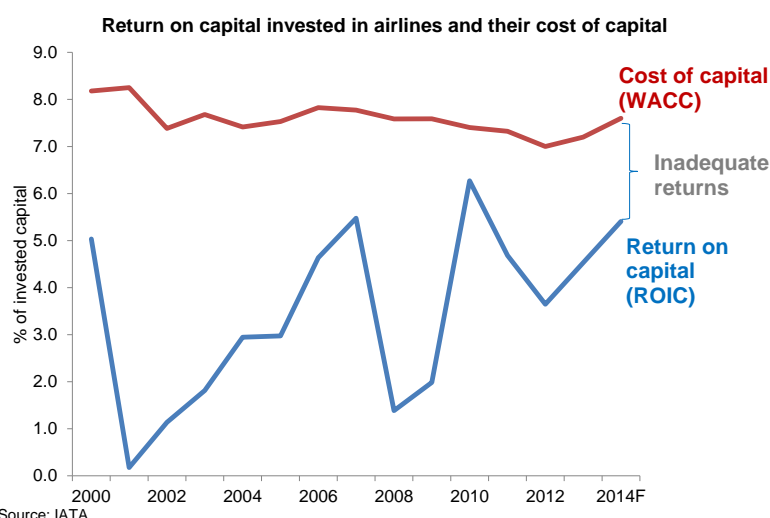
IMPROVEMENTS IN STRUCTURE ARE HELPING

- The financial results of the past year have shown airlines, particularly in the US, have been able to improve profitability despite a still difficult business environment. Consolidation on several large mature markets and the development of ancillary services have been key factors. Both are reflected below in the positive widening of the gap between breakeven load factors and the load factors achieved.



Source:
ICAO, IATA

- Structural improvements and the cyclical economic upturn are forecast to improve airline industry return on capital to 5.4% this year. The improvement is welcome but returns, on average, remain too low.



Source:
McKinsey, IATA

System-wide global commercial airlines	Passenger traffic (RPK), % change over year					Passenger capacity (ASK), % change over year				
	2010	2011	2012	2013E	2014F	2010	2011	2012	2013E	2014F
Global	8.0	6.3	5.3	5.2	5.8	4.5	6.6	4.0	4.8	5.5
Regions										
North America	4.5	2.9	1.0	2.2	2.7	2.3	2.8	0.4	1.6	2.0
Europe	4.3	8.4	4.5	4.0	4.7	1.6	8.6	2.8	2.5	4.5
Asia-Pacific	11.8	6.5	6.1	7.2	7.4	6.3	7.0	5.4	7.1	7.0
Middle East	17.8	9.9	14.7	11.9	13.0	13.3	9.8	12.4	11.4	13.0
Latin America	12.3	11.2	9.5	6.5	6.0	6.8	9.3	7.6	4.6	6.5
Africa	12.3	1.6	7.5	5.1	5.8	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	2013E	2014F
REVENUES, \$ billion	379	413	465	510	570	476	564	618	679	708	745
% change	17.7	9.1	12.5	9.6	11.7	-16.5	18.4	9.7	9.8	4.3	5.3
Passenger, \$ billion	294	323	365	399	444	374	445	500	539	567	598
Cargo, \$ billion	47	48	53	59	63	48	66	67	64	61	63
Traffic volumes											
Passenger growth, rpk, %	13.7	8.1	6.2	7.5	2.6	-2.4	8.8	6.9	4.9	5.3	5.8
Sched passenger numbers, millions	2,067	2,214	2,338	2,543	2,581	2,479	2,681	2,845	2,977	3,129	3,304
Cargo growth, ftk, %	10.3	2.5	6.4	4.7	-0.7	-8.8	19.4	0.4	-1.0	1.4	4.0
Freight tonnes, millions	36.8	37.7	40.1	42.5	41.1	40.8	48.6	49.7	49.2	49.8	51.7
World economic growth, %	4.3	3.9	4.4	4.3	1.8	-1.7	4.3	3.1	2.5	2.4	2.9
Passenger yield, %	3.7	1.7	6.6	1.7	8.2	-13.7	9.6	5.0	2.9	-0.2	-0.3
Cargo yield %	5.1	0.3	4.4	5.6	7.0	-15.2	14.4	0.8	-4.1	-4.9	-1.5
EXPENSES, \$ billion	376	409	450	490	571	474	536	604	667	686	713
% change	16.2	8.9	10.1	8.8	16.5	-16.9	13.1	12.7	10.4	2.9	3.9
Fuel, \$ billion	65	91	116	133	187	123	138	174	208	210	213
% of expenses	17	22	26	27	33	26	26	29	31	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	108.8	108.0
Jet kerosene price, \$/b	49.7	71.0	81.9	90.0	126.7	71.1	91.4	127.5	129.6	124.6	124.6
Fuel consumption, billion gallons	65	67	68	70	69	66	69	71	72	73	76
CO ₂ emissions, million tonnes	619	643	648	665	661	626	655	673	682	697	721
Non-fuel, \$ billion	311	318	335	357	384	351	398	430	459	477	501
cents per atk (non-fuel unit cost)	39.2	38.0	38.2	38.1	40.0	38.2	41.7	42.5	44.1	44.1	44.1
% change	1.4	-3.0	0.4	-0.1	4.9	-4.6	9.3	1.9	3.8	0.0	0.0
Capacity growth, atk, %	9.7	5.7	4.8	6.6	2.7	-4.2	3.7	6.0	2.9	3.8	5.0
Flights, million	23.8	24.9	25.5	26.7	26.5	25.9	27.8	30.1	31.2	32.6	34.3
Break-even weight load factor, %	60.6	60.8	60.3	59.9	61.8	61.4	63.2	64.3	64.8	64.2	63.6
Weight load factor achieved, %	61.1	61.5	62.3	62.4	61.7	61.6	66.4	65.8	66.0	66.2	66.4
Passenger load factor achieved, %	73.5	74.9	76.0	77.0	76.0	76.1	78.6	78.4	79.3	79.6	80.2
OPERATING PROFIT, \$ billion	3.3	4.4	15.0	19.9	-1.1	1.9	27.6	14.0	12.1	21.5	32.0
% margin	0.9	1.1	3.2	3.9	-0.2	0.4	4.9	2.3	1.8	3.0	4.3
NET PROFIT, \$ billion	-5.6	-4.1	5.0	14.7	-26.1	-4.6	17.3	7.5	6.1	12.9	18.7
% margin	-1.5	-1.0	1.1	2.9	-4.6	-1.0	3.1	1.2	0.9	1.8	2.5
per departing passenger, \$	-2.69	-1.86	2.14	5.78	-10.11	-1.86	6.45	2.64	2.05	4.13	5.65
RETURN ON INVESTED CAPITAL, %	2.9	3.0	4.6	5.5	1.4	2.0	6.3	4.7	3.6	4.5	5.4

Source: ICAO data to 2009-12 (note revisions to 2009 and 2011 data). IATA estimate for 2013 and forecast for 2014. Passenger and freight numbers are global system-wide collected by IATA, including some non-ICAO states. Bankruptcy reorganization charges excluded.