

IATA ECONOMICS BRIEFING

AIRLINE BUSINESS CONFIDENCE INDEX

JANUARY 2011 SURVEY

KEY POINTS

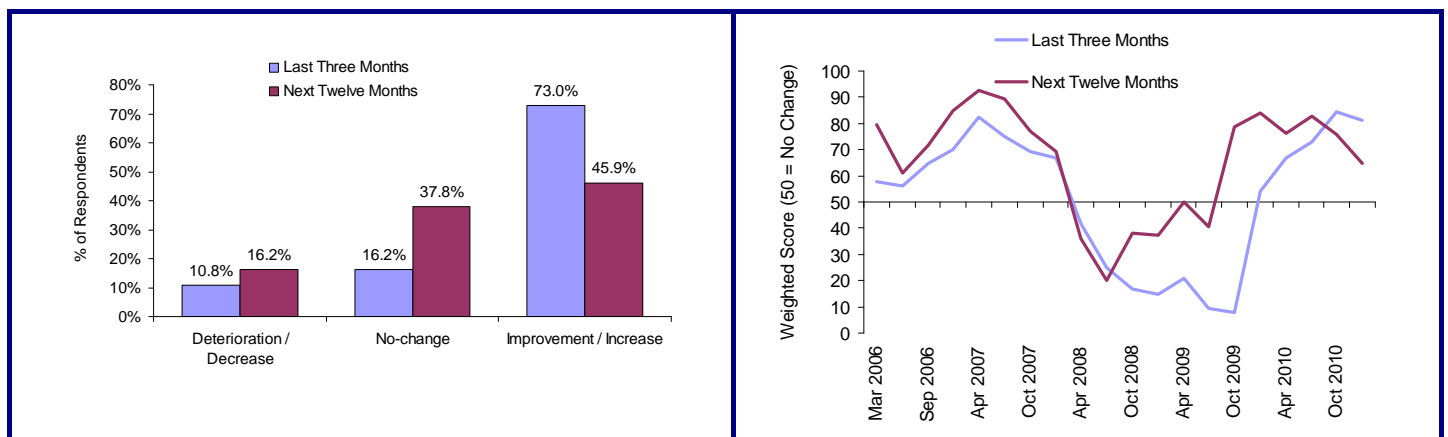
- Results from IATA’s quarterly survey conducted in January indicate that strong business conditions continued through the end of 2010. For 2011, while another profitable year is expected, confidence in further significant improvement is diminishing. Almost three-quarters of respondents reported improved profitability during the last quarter, driven by a strong traffic and yield improvement. The outlook for the 12 months ahead remains positive, although loosening demand-supply conditions and upward fuel cost pressures mean that momentum for further boosts to profitability is slowing. In December IATA revised up its forecast for 2010 industry profits to US\$15.1 billion but takes a somewhat more conservative view of 2011 with profits at US\$9.1 billion.
- Both cargo and passenger demand continued to improve during the final quarter of 2010. Increases in passenger demand were reported by 80% of respondents and, on the cargo side of the business, more than three-quarters reported increases. Expectations for further improvements in demand over the 12 months ahead are still high and indicate that the current expansion of air travel and air freight markets has further to run – albeit at closer to trend growth rates rather than the higher rates seen in the early post-recession recovery period.
- Yields are reported to have increased by the majority of respondents in Q4 driven by increased demand and relatively tight demand-supply conditions. The outlook for further yield improvement continues to trend back towards the 50 ‘no-change’ mark, pointing to stability in the year ahead rather than further increases. Cost pressures are on the rise, driven mainly by concerns over fuel prices. However, recovering rates of fleet utilization combined with increasing fuel hedging activity may help offset some of the upward rise in unit costs over the year ahead.
- On balance, industry employment expanded in the last quarter of 2010, however regional variation is evident. Less than 40% of respondents in Europe reported employment increases; in the Americas over 60% were hiring. The outlook for the next 12 months is for expansion in employment, although almost a quarter of respondents report seeking to find further reductions in headcount.

PROFITABILITY OUTLOOK

How has profitability changed? How do you expect it to change over the next twelve months?

a) January 2011 survey

b) Compared to previous surveys



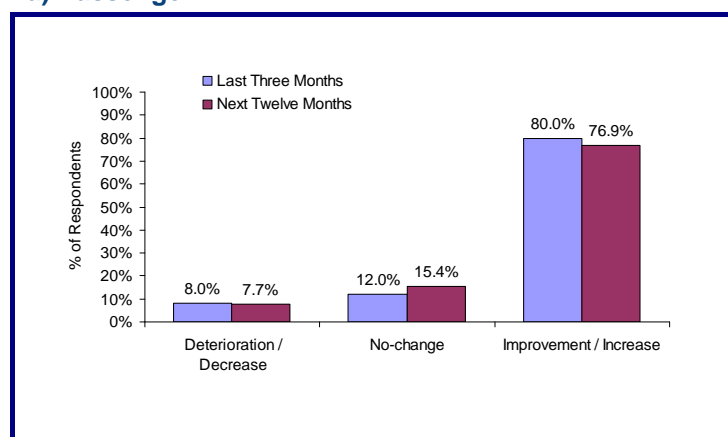
- At the beginning of 2011 airlines remained relatively confident about prospects for profitability over the year ahead, although expectations have softened somewhat from the high levels seen for most of 2010. Almost three-quarters of respondents reported improved profitability during the final quarter of 2010. Just under half expect further improvement over the 12 months ahead, down from 60% in the October 2010 survey. Continued strong demand growth and a positive yield environment helped drive increased revenues. Better fleet utilization helped offset some of the upward pressure on fuel costs. While adverse weather and industrial action hit profitability for some, overall most respondents reported improved profitability. On a weighted average basis (with 50 representing no-change, and values above 50 signaling a greater balance of positive views), the score for profitability over the previous three months is 81.1 – not far from the high reported in October last year.
- The majority of respondents in each region report improvements in profitability. More than 60% of respondents from Europe reported improved profitability and a further 30% no-change, indicating better conditions in this region compared to previous surveys. Respondents from the Americas were unanimous in reporting increases, driven by improving economic conditions and the benefits of industry restructuring during the recession.
- The balance of respondents still expect further improvement in profits during 2011, however the extent of improvement may be moderate. The weighted average measure of expectations for profits fluctuated between 75-85 during 2010 but has stepped down to 65 this survey, moving back towards the 50 'no-change' mark. More challenging demand-supply conditions, as capacity and competition increase on key routes, will tend to soften revenue growth and underlying profits. Respondents still report concern over the pace and durability of ongoing economic recovery and are increasingly wary of upward pressures on fuel costs. While expectations on traffic point to continued expansion in demand, responses to the latest survey indicate that profitability may be stabilizing rather than increasing further. Respondents from the Americas are more positive, with 56% reporting expectations of further profitability increases. Just under half of European respondents expect the same. A lower 42% proportion in the Asia Pacific point to further increase and the same again report 'no-change', consistent with the earlier recovery seen in this region.

DEMAND GROWTH

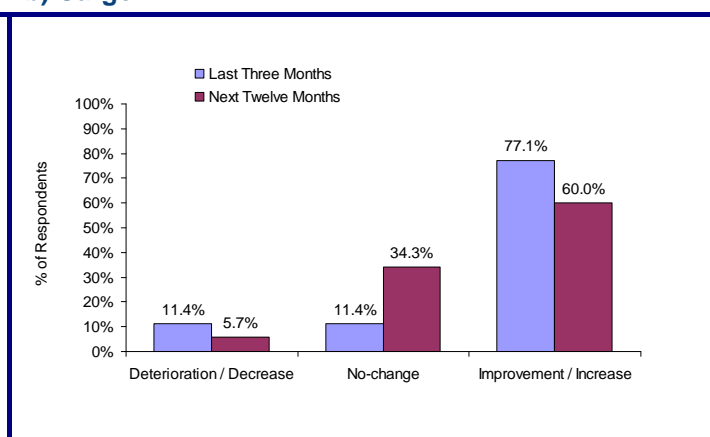
- The large majority of respondents continued to report improved traffic volumes on both the passenger and cargo sides of the business during the last quarter of 2010. Both air travel and air freight markets are well up on previous year levels. November 2010 international revenue passenger kilometer data shows traffic had recovered to 4% above the level seen prior to the recession. In this latest survey, 80% of respondents reported increased passenger traffic during Q4 2010, up from the 70% in the previous survey. Support was broad-based across the regions, although in Europe there were still a quarter of respondents reporting 'no-change'. The outlook for passenger traffic over the 12 months ahead remains positive with more than three-quarters expecting increases over that period on the back of continued demand growth and capacity expansion. A weighted average score of 84.6 indicates that respondents expect there is further to run in the current expansion of air travel markets over the year ahead. It is likely that this expansion will be more in line with historical trend growth rates rather than continuing the more rapid pick up seen during the recession recovery period.

Recent and expected change in traffic volumes

a) Passenger



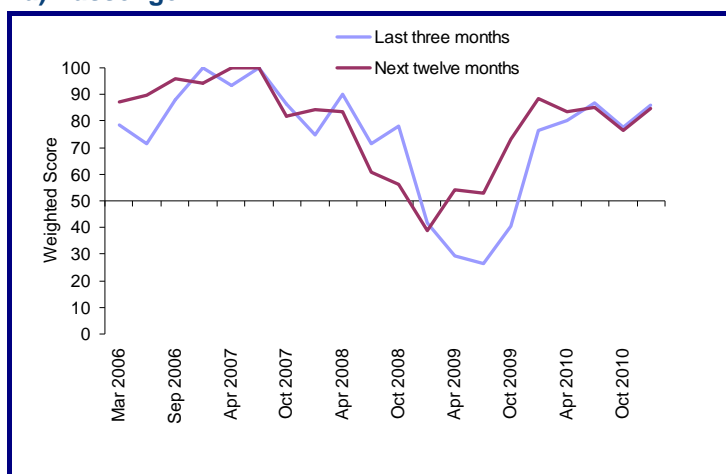
b) Cargo



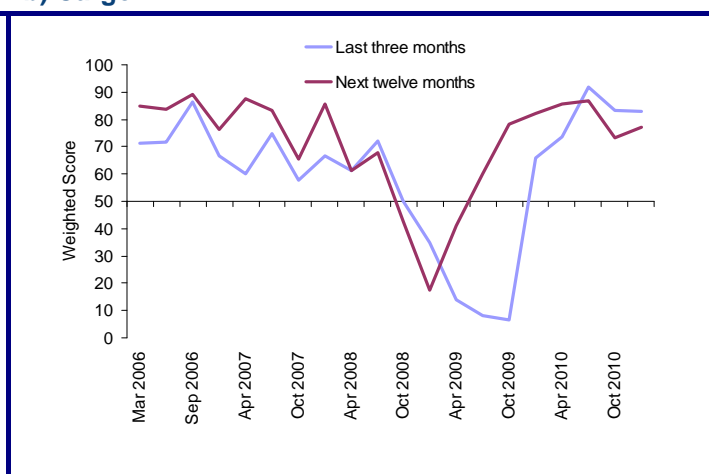
➤ Over three quarters of respondents reported stronger cargo traffic in the last quarter, a similar proportion to that seen in the October 2010 survey. By November 2010 the volume of international freight tonne kilometers was up more than 20% on a year-to-date basis compared to the same period in 2009. The recovery in traffic, driven by the pickup in world trade, has almost been as sharp as the fall experienced going into the recession. Freight volumes reached a new post-recession peak in May 2010 but dropped back a notch by mid-year as the restocking phase of the inventory cycle came to a close. Since then volumes have stabilized in line with the level seen immediately prior to the recession. However in our latest survey, the proportion of respondents expecting further improvement in air freight volumes over the 12 months ahead remains around 60% – indicating that continued growth beyond restocking stimulus is seen as likely this year. At a weighted average level of 77.1, confidence in the outlook for freight volumes is still positive, although growth rates will certainly be slower than the double digit rates seen in the recovery period thus far.

Compared to previous surveys

a) Passenger



b) Cargo

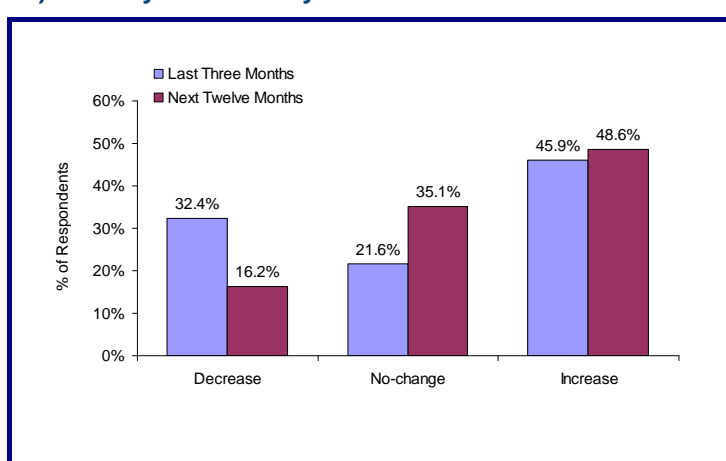


INPUT COSTS

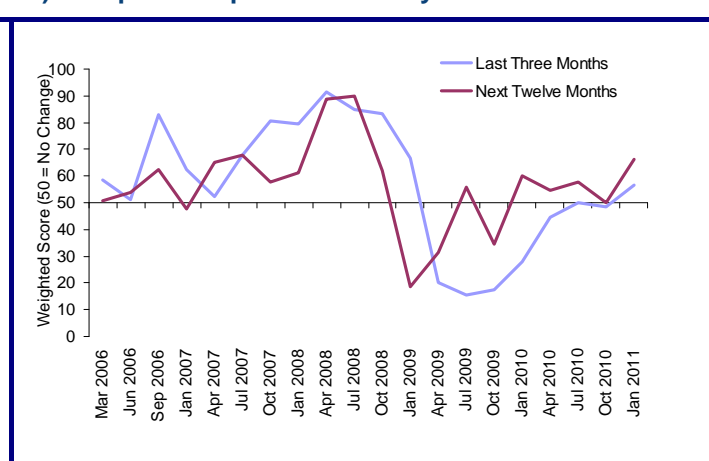
➤ Input unit costs ticked up above the 50 'no-change' line during the final quarter of 2010 – indicating rising costs. This follows almost two years where the balance of responses on input costs showed either falling or steady costs for airlines. Although the weighted average score of 56.8 is 'above the line' there is still significant variation across airlines. Almost a third of respondents are still experiencing unit cost decreases due to better fleet utilization and being on the right side of exchange rate moves. However 46% – up from the 37% last survey – now report increases. This is primarily driven by upward pressure on fuel costs but rises in employment and infrastructure costs are also cited.

How have your unit input costs changed? How do you expect them to change over the next twelve months?

a) January 2011 survey



b) Compared to previous surveys



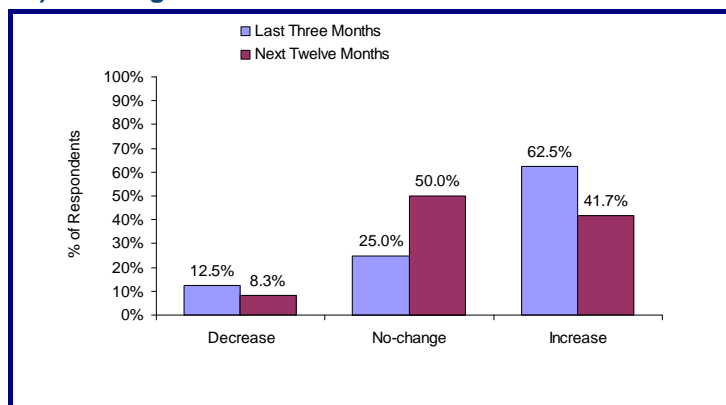
➤ Almost half of respondents in the latest survey expect increases in unit costs over the 12 months ahead – up significantly from the 29% last survey. The weighted average score for expectations going forward has climbed to 66.2, the highest level in two years. The prospect of increased fuel cost remains the major concern, although many airlines are hedged against dramatic rises – in the short term at least – which may be helping to moderate expectations of upward movements in input costs somewhat.

YIELD ENVIRONMENT

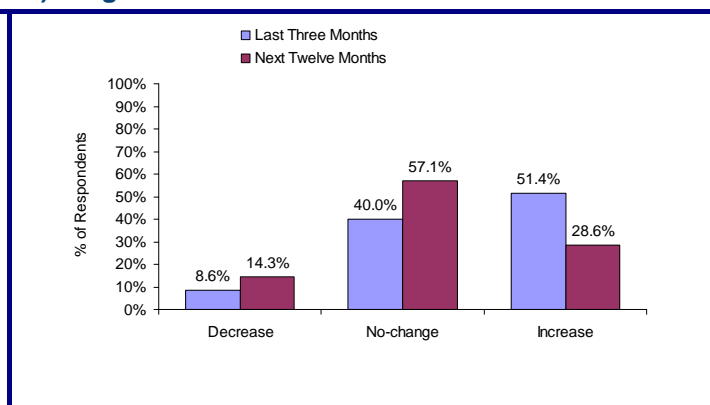
- Both passenger and cargo transport businesses saw improving yield performance during the final quarter of 2010, however the outlook for 2011 is trending towards stability rather than further improvement. Just over 60% of respondents reported passenger yield increases in Q4 2010. Demand-supply conditions remained relatively tight and supported an improvement in the yield environment. However part of the rise in yields is associated with fuel surcharges driven by higher fuel costs. Overall, on weighted average basis, the score for yield performance over the last quarter was 75 – close to a new high. Rising yields have been a major factor in improving profitability for airlines in 2010. Even so, average fares are still around 10% below the level reached in early 2008 prior to the recession.
- The outlook for yield performance over the year ahead is trending back towards the 50 ‘no-change’ line, consistent with a flattening off of yield growth in 2011. Although the weighted average score for passenger yields going forward ticked up to 67 this survey, this is well below the 80s seen for much of 2010. Half the respondents to the latest survey expect ‘no-change’ in yields over the year ahead. Passenger mix is expected to continue to improve which will help support yields. However competition is increasing on key routes as additional capacity enters the market, which limits the extent to which further fare increases can be made. It may also reduce scope for recouping additional fuel costs which would dampen profitability in the year ahead.

Recent and expected change in yields

a) Passenger

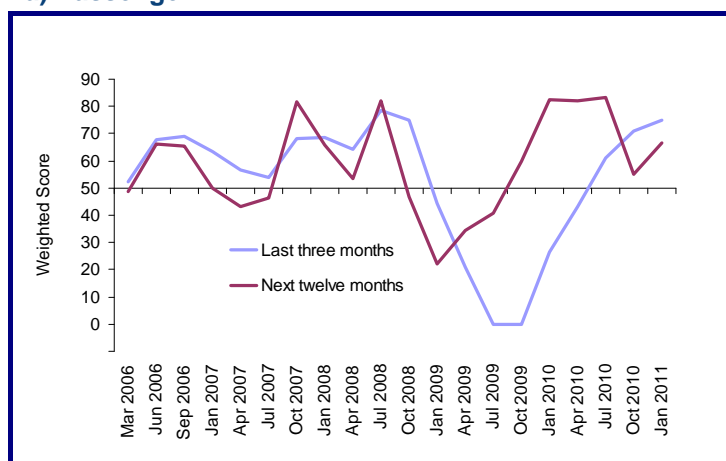


b) Cargo

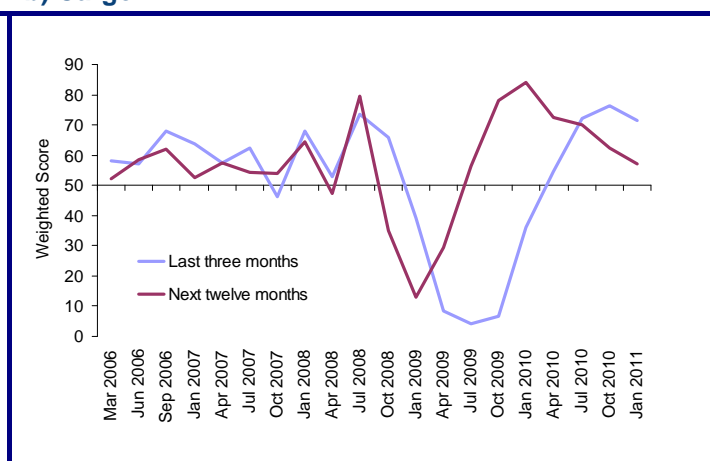


Compared to previous surveys

a) Passenger



b) Cargo



➤ Just over half of respondents to the latest survey still reported increases in cargo yields through the end of 2010. Most of the rest reported stability. This helped the weighted average score to remain high at 71.4. As for passenger markets, demand-conditions remained fairly tight which supported yields. However some respondents reported loosening. Expectations for cargo yields over the 12 months ahead point to stability with 57% of respondents reporting 'no-change' likely. Freight growth is moderating back towards the rate of world trade growth while capacity is entering at a faster rate which will put downward pressure on load factors and temper further rises in yields. The weighed average score for cargo yield movement over the next 12 months sits at 57.1 – still in positive territory but pointing to stability rather than significant further upward movement. IATA's own forecast is for flat yield growth in the cargo and passenger sides of the business during 2011.

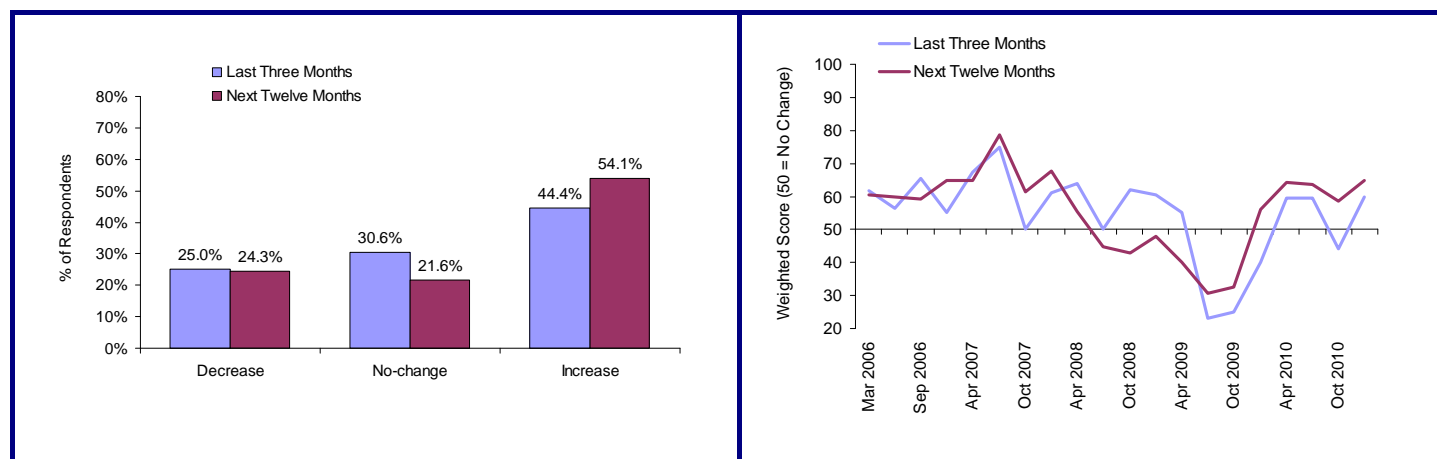
EMPLOYMENT

- Almost a third of respondents reported stability in employment numbers in Q4 2010 while 44% hired additional staff and a quarter cut back. This brought the weighted average for last quarter to 59.7 – indicating expansion in employment on balance – reversing the dip seen last survey. Renewed network expansion or additional capacity introduction is driving the increase. The regional split of responses is consistent with the differing stages of recovery of operations across the globe. Just over 60% of respondents in the Americas were expanding employment. In Asia half were expanding while a quarter were holding steady. In Europe almost 40% were still cutting back given the slower traffic recovery in that region while a similar proportion were increasing.
- The outlook over the next 12 months continues to be, on balance, for increases in employment levels. The weighted average score of 64.9 is in line with the level seen for most of 2010. Drivers of this outlook remain the continued recovery of traffic back to, and beyond, pre-recession levels as well as the return to market expansion through the establishment of new services. However many respondents amongst the quarter who see employment reductions over the year ahead are still seeking ways to 'do more with less'.

How has your employment level changed? How do you expect it to change over the next twelve months?

a) January 2011 survey

b) Compared to previous surveys



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FURTHER ANALYSIS AND DATA

Access video commentary and chart data related to this briefing through the Enhanced Edition: www.iata.org/business-confidence