Airlines Financial Monitor

March 2019 – April 2019

Key points

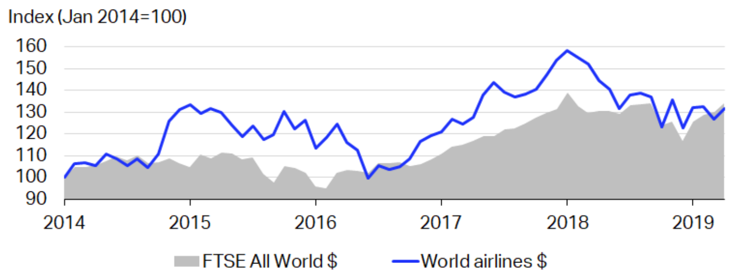
- Initial financial results for Q1 2019 indicate a further fall in aggregate profits for the airline industry compared to the same period of previous year. The outcome is mixed at the regional level, with broad stability in North and Latin America, improvement in Asia Pacific but a significant weakening in Europe, although the sample so far is small.
- The global airline share index outperformed the wider equities market in April with better than expected earnings outcomes and earnings guidance in some regions.
- Oil and jet fuel prices climbed again in April driven by the ending of US sanction waivers on Iranian oil imports. At the time of writing this note, the Brent crude oil price is hovering around US$72 bbl (36% higher than the end of 2018) as a result of increased tensions in the Middle East.
- Global base fare passenger yields continued to decline in February, with both premium and economy cabin yields under pressure.
- Annual growth in industry-wide revenue passenger kilometres (RPKs) eased to 3.1%; the weakest annual outcome since early-2010. For freight, volumes were 0.1% higher than their level a year ago, following the sharp annual fall of 4.9% in February.

Financial indicators

Airline shares outperformed global equities in April for the first time this year

Airline Share Prices

US$ indices (Jan 2014=100)	Index Apr 30th	% change on one month	one year	start of year
World airlines	**131.6**	**+3.9%**	**-9.0%**	**+7.2%**
Asia Pacific airlines	115.8	-2.8%	-12.8%	+4.4%
European airlines	103.4	+5.0%	-23.3%	+0.8%
North American airlines	170.6	+9.5%	+4.6%	+11.4%
FTSE All World $	**134.1**	**+3.2%**	**+2.7%**	**+15.0%**



Source: Thomson Reuters Datastream

- The global airline share price index rallied 3.9% in April, outperforming global equity index which went up by 3.2% in the same period. The global airline index has lagged the wider equity market since the beginning of this year (a 7.2% vs 15% increase in the first four months) as investors were concerned about Brexit uncertainty and the cost increases driven by higher oil prices and 737 Max groundings.
- In April, airline shares rebounded after Brexit was delayed and some airlines announced better than expected Q1 earnings results. The increase in the global airline index was driven by a surge in North American (9.5%) and European (+5.0%) airlines. On the other hand, Asia Pacific airlines continued to lose value (-2.8%) stemming from the concerns regarding Jet Airways potential bankruptcy and US-China trade war.

Industry-wide decline in profitability in Q1 2019, driven by European airlines

Airline Financial Results

Number of airlines in sample	Regions	Q1 2018 EBIT margin[1]	Q1 2018 Net post-tax profit[2]	Q1 2019 EBIT margin[1]	Q1 2019 Net post-tax profit[2]
8	North America	6.8%	1,395	6.4%	1,462
4	Asia-Pacific	2.7%	96	5.0%	506
4	Europe	-2.1%	-91	-6.0%	-651
4	Latin America	-4.2%	-23	-4.2%	-78
20	**Sample total**	**4.1%**	**1,377**	**3.6%**	**1,239**

[1]% of revenues [2]US$ million

Sources: The Airline Analyst, IATA

- Equity markets are forward looking. Looking back, the first quarter showed initial releases of airline financial results point to a moderate decline in airline profitability relative to the same period a year ago. The EBIT margin in our sample of 20 airlines has fallen to 3.6% from 4.1% a year ago.
- The deterioration at an industry-wide profit level was driven mainly by Europe (the first quarter of the year is always a weak period for European airlines). On the other hand, North America and Asia-Pacific regions recorded increase in net post-tax profits. While North America recorded strongest EBIT margin among all regions, EBIT margin improved remarkably to 5.0% in Asia-Pacific region.

Industry-wide cash flows higher compared to a year ago

Airline Cash Flow[1]

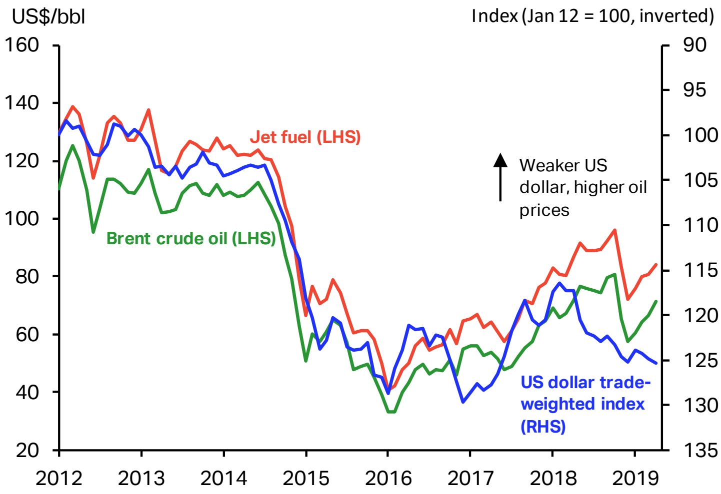
Number of airlines in sample	Regions	Q1 2018 Net cash flow[2]	Q1 2018 Capex	Q1 2018 Free cash flow	Q1 2019 Net cash flow[2]	Q1 2019 Capex	Q1 2019 Free cash flow
8	North America	19.6%	12.9%	6.7%	17.7%	10.7%	7.0%
3	Asia-Pacific	14.6%	14.5%	0.1%	7.8%	8.0%	-0.2%
4	Europe	13.9%	14.8%	-0.9%	17.6%	16.0%	1.6%
3	Latin America	18.1%	3.4%	14.6%	-2.1%	5.3%	-7.4%
18	**Sample total**	**17.8%**	**13.2%**	**4.5%**	**16.0%**	**11.3%**	**4.7%**

[1]% of revenues [2]From operating activities
Sources: The Airline Analyst, IATA

- The initial Q1 2019 sample of 18 airlines indicates improvement (0.2 percentage points, from 4.5% to 4.7%) in industry-wide free cash flow compared to the same period a year ago.
- While there was a modest decline in net cash flow from operations (from 17.8% to 16.0% of revenues), the slow-down in capex spending supported free cash flow.
- At the regional level, capital spending fell in North America and Asia-Pacific, while carriers based in Europe and Latin America increased their capital spending compared to a year ago.
- All in all, negative FCF outcomes in Latin America and Asia-Pacific were offset by positive outcomes in other regions.

Fuel costs

Oil and jet fuel prices trending higher for a fifth consecutive month

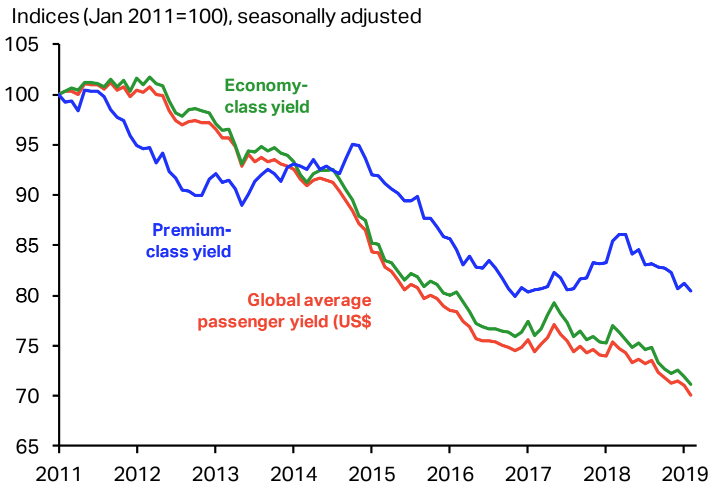


Sources: Platts, Thomson Reuters

- The average monthly price of Brent crude oil and jet fuel continued to trend upwards in April following the US decision to end sanction waivers on Iran oil imports. Oil prices remain under pressure as the fears of supply disruption augmented amid heightened tensions in the Middle East.
- At the time of writing this report, the price of Brent crude oil hovers around US$72/bbl and the jet fuel price is around US$85/bbl – the highest level since November. For more data on oil price developments, check out our weekly Jet Fuel Price Monitor.
- The futures market still indicates oil prices to remain relatively stable in the rest of the year, December 2019 future contracts hover around US$69-70/bbl.

Yields and premium revenues

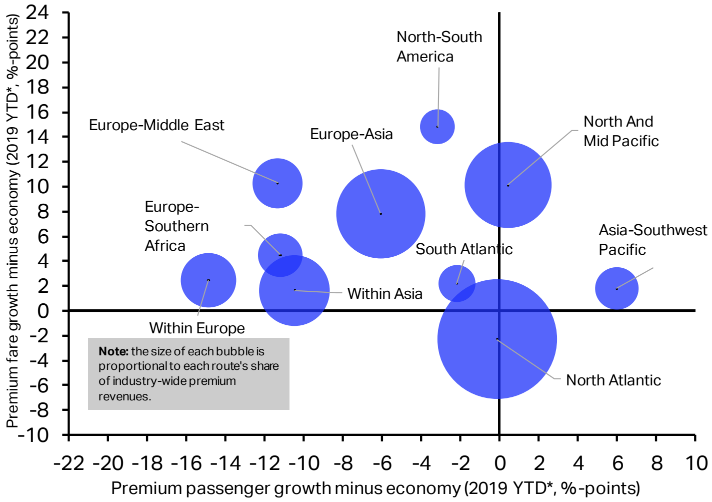
Premium and economy cabin passenger yields continue to decline in early-2019



Sources: IATA Economics, IATA Travel Intelligence

- Downward pressure on global 'base fare' passenger yields (i.e. excluding surcharges and the revenue that airlines generate from ancillary services) persisted in February as airlines struggle to recover rising operating costs. In US$ terms, yields in February were 7.0% lower than the same month in 2018.
- In February, both premium and economy cabin yields were under pressure. Premium cabin yields went down by 1.1% compared to the prior month even though typically airlines are able to pass through cost increases to this less price-sensitive class. Similarly, economy cabin yields declined by 1.2%.

Premium revenue share improved despite diminishing premium traffic share



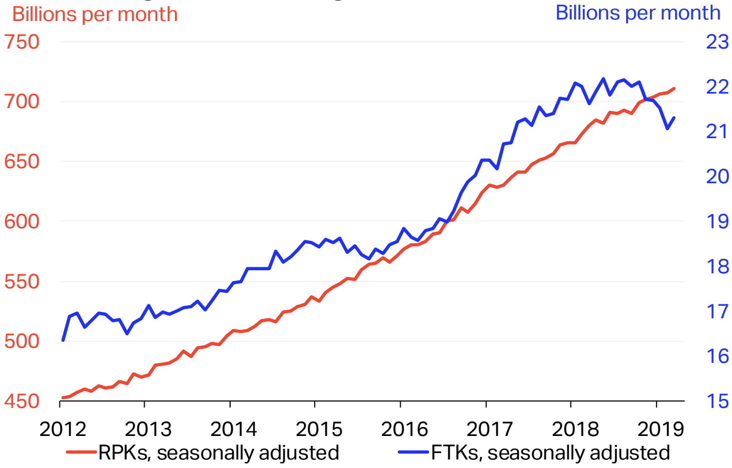
Sources: IATA Economics, DIIO *Up to February 2019

- Premium-class passengers constituted 4.1% of the total number of international origin-destination traffic in the first two months of 2019, down from 4.3% observed a year ago.
- In terms of revenue, premium-class passengers accounted for 27.3% of total international passenger revenues in Jan-Feb 2019, which was slightly higher compared to the same period a year ago (27.1%).
- Premium passenger traffic growth has outperformed its economy counterpart only in the Asia-Southwest Pacific and North-Mid Pacific regions. By contrast, premium class fare growth outpaced economy counterpart in all regions apart from North Atlantic.

Demand

Freight demand remains weak but passenger volumes continue to trend upwards

Air Passenger and Air Freight Volumes



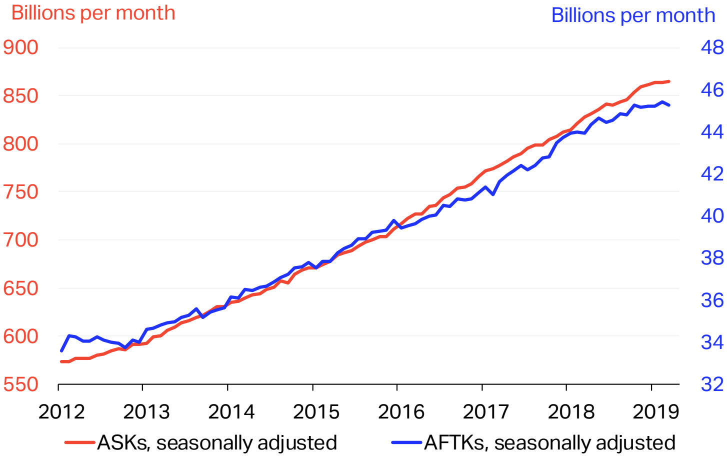
Source: IATA Monthly Statistics

- Annual growth in industry-wide revenue passenger kilometres (RPKs) eased to 3.1%; the weakest annual outcome since early-2010. Having said that, this month's result was impacted by the earlier timing of the 2018 Easter holiday period, which boosted demand in March last year. All told, solid upward trend in seasonally adjusted (SA) volumes remains in place.
- Growth in industry-wide freight tonne kilometres (FTKs) bounced back to a positive territory in March; freight volumes were 0.1% higher than their level a year ago, compared with the annual fall of 4.9% recorded in February. Although SA FTKs lifted modestly, it would be too soon to conclude that this month's uptick represents a change in the recent downward trend.

Capacity

Passenger and freight capacity trends diverged this month

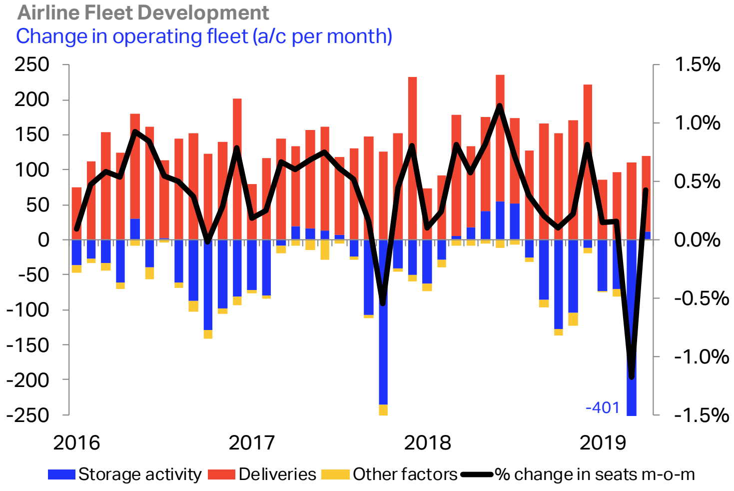
Air Passenger and Air Freight Capacity



Source: IATA Monthly Statistics

- Industry-wide available seat kilometres (ASKs) grew by 4.2% year-on-year in March, outpacing growth in revenue passenger kilometres by ~1 percentage point.
- The story is different in seasonally adjusted terms; although ASKs ticked-up modestly this month, the pace was slower compared to SA RPKs.
- Industry-wide capacity, measured by available freight tonne kilometres (AFTKs), increased by a moderate 3.1% year-on-year in March. Over the course of the past year or so, the rate of capacity growth has clearly moderated; indeed, annualized pace of growth over the past six months is down at ~2%, compared to 3.9% earlier in the year.

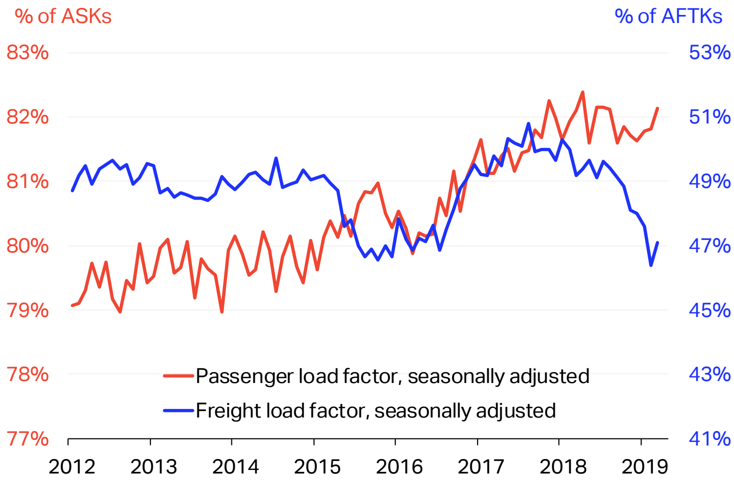
Net storage activity made a large contribution to fleet growth in April



Source: Ascend

- The number of available seats in the global airline fleet increased by 0.4% in month-on-month terms in April following a sharp decline in March (-1.2%) due to 737 Max groundings. In year-on year terms growth eased by 0.2 ppt to 4.0%, lowest annual increase since May 2013.
- 107 aircraft were delivered in the month – fewer than the 117 delivered in the same period a year ago. Altogether, the number of aircraft delivered in the first four months of 2019 was much lower than that seen in the same period last year (399 vs. 455). Note that on average 462 aircrafts delivered in the first four months of the years between 2013-2018.
- 118 aircraft returned to the fleet from storage while 106 aircraft left the fleet in April 2018. Net storage activity made a small positive contribution to fleet growth following sharp decline (-401 aircrafts) in March.

Load factor being maintained in passenger market but down for freight



Source: IATA Monthly Statistics

- Seasonally adjusted data point to airlines responding to the demand slowdown by slowing capacity growth sufficiently to maintain passenger load factors near the 82% level. However, the base fare data suggests that may have been achieved through prices stimulus to the detriment of profitability
- Freight load factor (FLF) for the industry is currently 1.5 percentage points lower than the level of March 2018, at 49.5%. Although SA FLF rose a little this month, the key takeaway remains that downward trend, which started in mid-2017, remains in place.

IATA Economics
economics@iata.org
20th May 2019

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