

# AIRLINES FINANCIAL MONITOR

## KEY POINTS

July 2016 – August 2016

- ➔ The latest financial results from Q2 2016 point to another solid quarter for industry profitability and cash flow, although CFOs report that they no longer expect further improvement in profitability over the next 12 months;
- ➔ Global airline share prices fell by 1.6% in August, and remain well down on where they started the year;
- ➔ Brent crude oil prices rallied during much of August, but fell back to US\$47/bbl by the end of the month. The futures market and oil analysts continue to expect prices to remain below \$55/bbl for the foreseeable future;
- ➔ Downward pressure on yields has intensified over the past six months or so, in line with the moderation in demand;
- ➔ Premium airfares have held up better than their economy counterparts on many of the key premium routes so far this year, and the segment continues to offer a buffer for overall airline financial performance;
- ➔ The global air passenger market showed resilience into the peak summer period, with lower fares helping to offset more negative influences on demand. The (SA) industry-wide load factor edged down in July, but remains high;
- ➔ Conditions for air freight have improved from the weak patch seen in early-2016, but there remain reasons to be cautious. Low freight loads are keeping downward pressure on cargo yields and revenues.

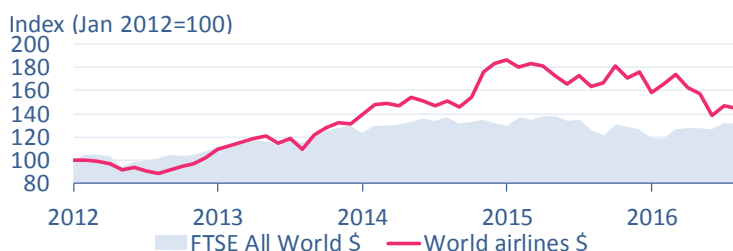
## Financial indicators

### Global airline share prices fell by 1.6% in August

#### Airline Share Prices

US\$ indices (Jan 2012=100)	Index Aug 31st	% change on		
		one month	one year	start of year
<b>World airlines</b>	<b>144.8</b>	<b>-1.6%</b>	<b>-11.5%</b>	<b>-17.9%</b>
Asia Pacific airlines	81.0	-2.2%	-2.7%	-7.7%
European airlines	165.6	-0.9%	-22.1%	-29.1%
North American airlines	305.9	-0.9%	-12.1%	-19.2%
<b>FTSE All World \$</b>	<b>132.1</b>	<b>+0.1%</b>	<b>+5.1%</b>	<b>+4.3%</b>

- ➔ Having jumped by 5.9% in July, global airline share prices fell by 1.6% in August. The index of Asia Pacific carriers saw the biggest decline during the month (2.2%), while European and North American airline shares both fell more modestly (0.9%).
- ➔ Heightened uncertainty from a range of factors, including the 'Brexit' vote and the impacts of terrorism and political instability in Europe and elsewhere, has added to existing investor concerns about the impact of falling unit revenues on profitability. Global airline shares ended the month almost 18% lower than their level at the start of 2016 and have underperformed the wider equity market by a considerable margin so far this year.



Source: Thomson Reuters Datastream

### Annual improvement in profitability slows, and performance still dominated by N.America

#### Airline Financial Results

Number of airlines in sample	Regions	Q2 2015		Q2 2016	
		EBIT margin <sup>1</sup>	Net post-tax profit <sup>2</sup>	EBIT margin <sup>1</sup>	Net post-tax profit <sup>2</sup>
18	North America	16.6%	5,958	17.1%	4,687
28	Asia-Pacific	4.9%	885	4.9%	518
11	Europe	6.6%	1,474	6.3%	1,159
6	Latin America	0.3%	-107	0.9%	59
3	Africa & Middle East	4.1%	17	8.2%	44
<b>66</b>	<b>Sample total</b>	<b>9.7%</b>	<b>8,227</b>	<b>9.9%</b>	<b>6,467</b>

- ➔ The latest financial results from Q2 2016 point to another solid quarter for industry profitability. Net post-tax profits in our sample in Q2 2016 were more than 20% lower in dollar terms than in Q2 2015, but the EBIT margin edged up to 9.9%.
- ➔ While the EBIT margin in Q2 was high by historical standards, it was just a small improvement from that in Q2 2015, and was driven by North American airlines: the margin in Asia Pacific was unchanged in year-on-year terms, while that in Europe fell slightly. Moreover, when surveyed in early July, airline CFOs and heads of cargo reported that they no longer expected further improvement in profitability over the next 12 months.

<sup>1</sup> % of revenues <sup>2</sup> US\$ million

Note: Includes Air New Zealand, Cathay Pacific, Qantas Airways, Regional Express Holdings, Shandong Airlines & Virgin Australia half-year results.

Sources: The Airline Analyst, IATA

## Free cash flow edges down in Q2 2016, following a pick-up in capital investment

### Airline Cash Flow<sup>1</sup>

Number of airlines in sample	Regions	Q2 2015			Q2 2016		
		Net cash flow <sup>2</sup>	Capex	Free cash flow	Net cash flow <sup>2</sup>	Capex	Free cash flow
17	North America	20.9%	12.6%	8.3%	24.4%	14.1%	10.3%
21	Asia-Pacific	17.4%	14.9%	2.4%	17.5%	17.2%	0.3%
10	Europe	18.4%	12.1%	6.3%	19.9%	18.5%	1.4%
5	Latin America	9.4%	9.6%	-0.2%	8.7%	5.1%	3.6%
2	Africa & Middle East	0.8%	0.9%	-0.1%	1.4%	0.7%	0.6%
<b>55</b>	<b>Sample total</b>	<b>15.5%</b>	<b>10.5%</b>	<b>5.0%</b>	<b>17.3%</b>	<b>12.8%</b>	<b>4.5%</b>

<sup>1</sup> % of revenues<sup>2</sup> From operating activities

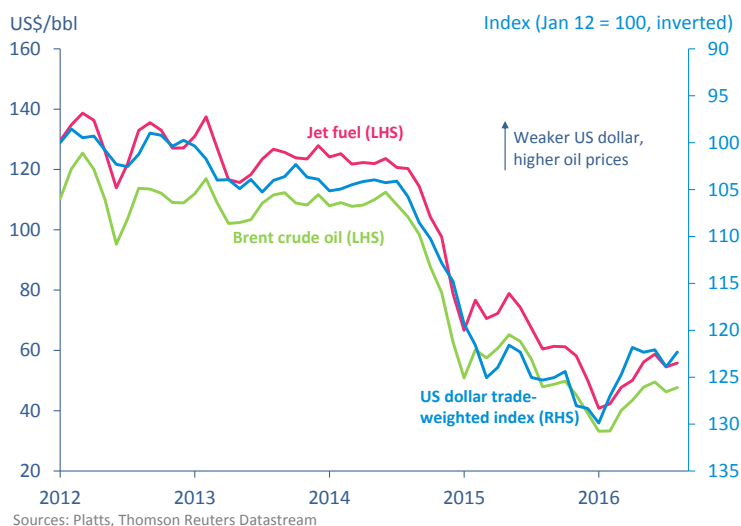
Note: Includes Air New Zealand, Precision Air, Qantas Airways, Regional Express Holdings, & Virgin Australia half-year results.

Sources: The Airline Analyst, IATA

- Net cash flow in our sample of 55 airlines rose to 17.3% of revenues in Q2 2016, up from 15.5% in the same period last year. Net cash flow increased in all regions except Latin America.
- Airlines increased capital expenditure as a share of revenues to a greater extent over the period, most notably in Asia Pacific and Europe. As a result, free cash flow in the sample edged down to 4.5% of revenues from 5.0%. Free cash flow gives airlines the flexibility to return cash to investors or to repair their balance sheets by paying down debt.

## Fuel costs

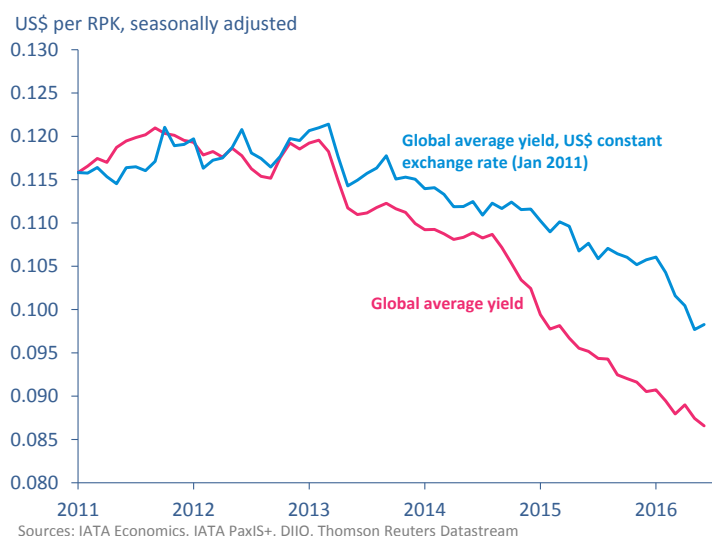
### Brent crude prices rallied during much of August, but remain around US\$45-50/bbl



- Brent crude oil prices rallied during much of August, driven by expectations that major producers may act to freeze supply. But concerns about oversupply resurfaced towards the end of the month, and oil prices ended August back around US\$47/bbl.
- The futures market and oil analysts continue to expect oil prices to remain below US\$55/bbl for the foreseeable future. However, given the profile of previous price falls, the annual comparison is becoming less favorable; oil prices ended the month of August nearly 6% lower year-on-year, but prices at the time of writing in early-September were slightly higher than they were in September 2015.

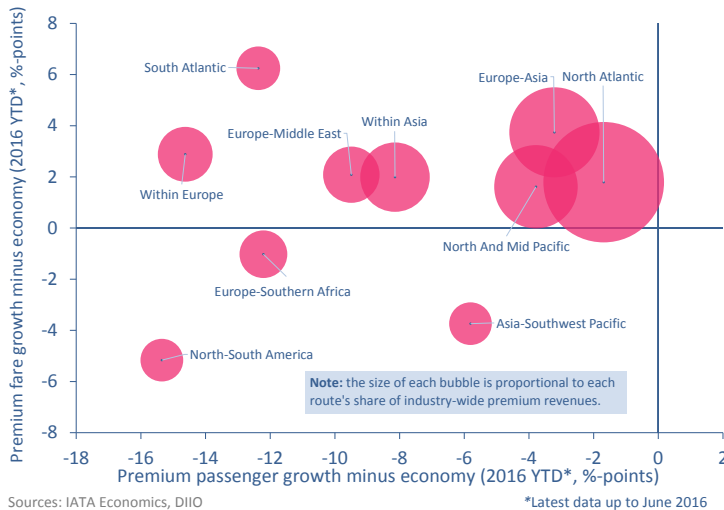
## Yields and premium revenues

### Pressure on industry-wide yields has intensified, while dollar distortions shift into reverse



- The average global yield in reported US dollar terms has continued to trend downwards so far this year (the latest data are up to June and exclude taxes, fees and surcharges).
- However, adjusting for distortions associated with movements in the US dollar shows that downward pressure on underlying (ie, constant exchange rate) yields has actually intensified over the past six months or so. This ties in with the moderation in demand conditions seen during the first half of 2016, and is reflected in the easing in the seasonally-adjusted passenger load factor (albeit from a record high). The constant exchange rate yield series edged up for the first time in five months in June, but the movement was within the range of normal monthly variation.

## Premium segment continues to offer a buffer for airline financial performance

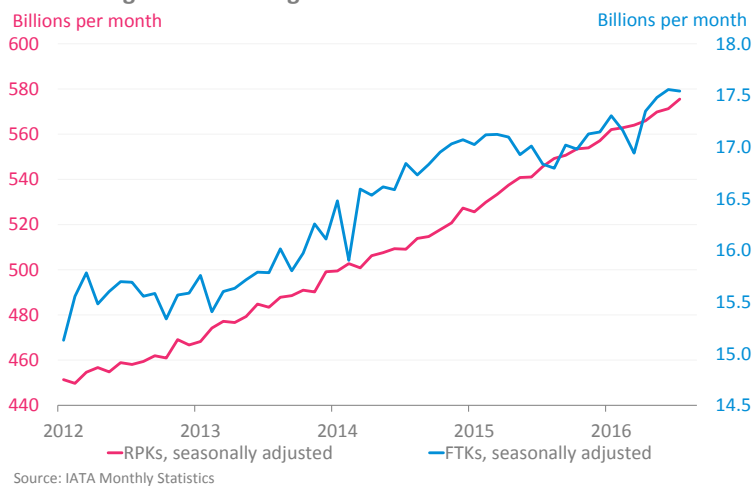


- ➔ Growth in premium international passenger traffic has continued to lag behind that of economy. O-D premium international journeys accounted for 5.4% of the total over the first half of 2016, down from 5.8% in the same period of 2015.
- ➔ However, premium fares have held up better than those in economy on most of the top-10 premium routes. In fact, premium's share of revenues has *risen* slightly so far this year on the North Atlantic and Europe-Asia markets (which accounted for nearly two-fifths of industry-wide premium revenues combined in 2015). In the current environment, the high-yielding premium segment offers an important buffer for airline financial performance.

## Demand

### Passenger traffic resilient into peak period, alongside a modest improvement for freight

#### Air Passenger and Air Freight Volumes

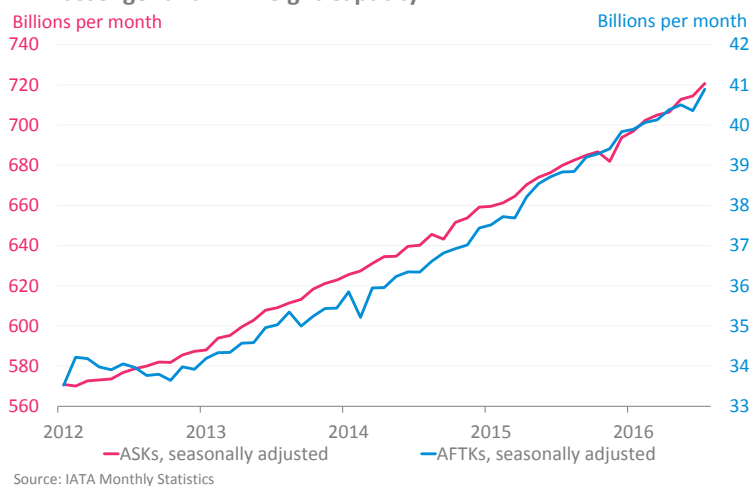


- ➔ After a period of moderation in demand growth, the global passenger market showed resilience into the peak summer period. Annual growth in industry-wide traffic accelerated to 5.9% year-on-year in July – its fastest pace in five months. The latest results indicate that the stimulatory impacts of lower fares on demand are currently outweighing negative headwinds, including those from the subdued global economic backdrop.
- ➔ Meanwhile, conditions for air freight have improved since the weak patch seen earlier in the year. However, there remain reasons to be cautious about the outlook, particularly given broader weakness in global trade volumes.

## Capacity

### Passenger and freight capacity has continued to trend upwards

#### Air Passenger and Air Freight Capacity

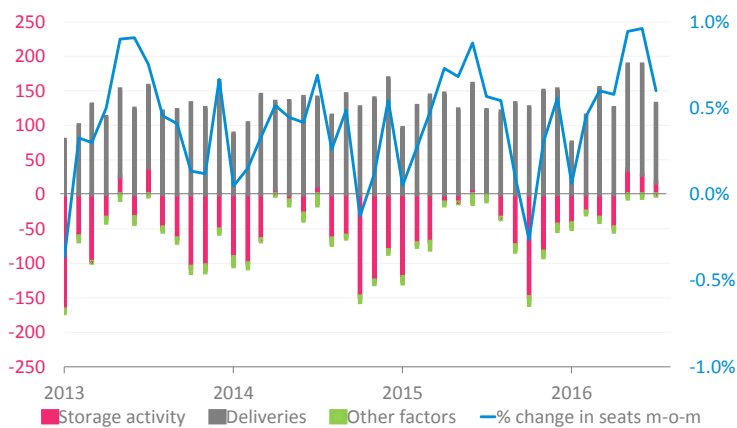


- ➔ Available seat kilometres grew by 6.0% year-on-year in July. Airlines have slowed capacity growth somewhat in recent months in line with the moderation in growth seen during H1 2016.
- ➔ Industry-wide available freight capacity increased by 5.2% year-on-year in July. Ongoing impetus to belly capacity from additions to the wide-body passenger fleet mean that annual growth in industry-wide freight capacity has now exceeded annual growth in volumes for 17 consecutive months. African carriers are seeing the fastest growth in capacity, with AFTKs up more than 31% year-on-year in July (although they comprise just a small share of the overall freight market).

## Net storage activity continues to contribute positively to fleet growth

### Airline Fleet Development

Change in operating fleet (a/c per month)

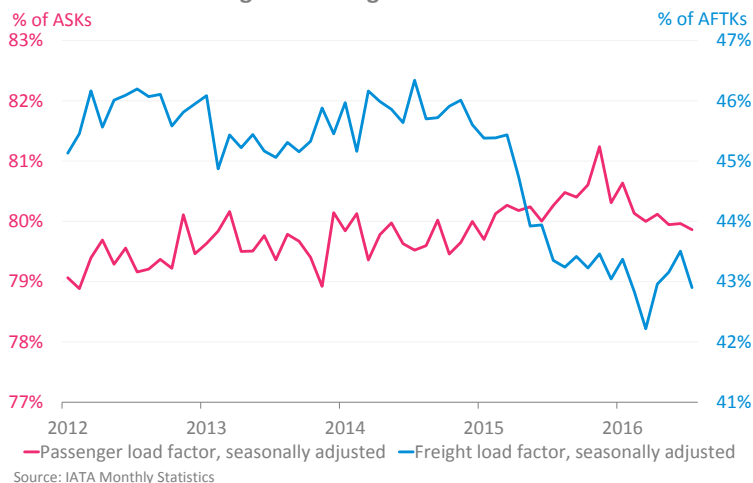


Source: Ascend

- ➔ The number of available seats in the global airline fleet increased by 0.6% in July compared to the previous month, and by 5.6% year-on-year.
- ➔ 114 new aircraft were delivered in July – slightly fewer than were delivered in July 2015 (122). Net storage activity made another positive contribution to the fleet size, driven mainly by fewer aircraft going into storage. Lower oil prices and robust demand have made it economical to keep flying less fuel-efficient aircraft. 70 aircraft were removed from the global fleet in July 2016, compared to 110 that left in June 2015.

## Passenger loads remain in a narrow band at a high level, but freight loads stay weak

### Load Factors - Passenger and Freight



Source: IATA Monthly Statistics

- ➔ The industry-wide passenger load factor was 83.7% in July 2016 – just 0.1 percentage point lower than the record July high reached last year. Despite edging down in July, the industry has managed to keep the seasonally-adjusted load factor in a reasonably narrow band around 80% since February.
- ➔ Having fallen sharply during the middle months of 2015, carriers have stabilized the seasonally-adjusted industry-wide freight load factor over the past six months or so, albeit at a historically-low level. Low freight loads continue to exert downward pressure on yields and revenues – a particular headwind for Asia Pacific carriers, for whom cargo is a key part of their business.

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13<sup>th</sup> September 2016

### Get the data

Access data related to this briefing through IATA's Monthly Statistics publication:

[www.iata.org/monthly-traffic-statistics](http://www.iata.org/monthly-traffic-statistics)

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