

Airlines Financial Monitor

January 2019 – February 2019

Key points

- The latest Q4 2018 financial data indicate that the intense squeeze on industry-wide airline profitability has moderated in the final quarter, with North American carriers seeing much smaller declines in EBIT margin compared to Q3 and Q2.
- Airline share price movements were generally muted in February, underperforming the global equity index on both the industry-wide and regional level.
- Oil and jet fuel prices both moved higher for a second consecutive month, averaging around US\$64/bbl and US\$80/bbl, respectively in February. Given OPEC's supply cuts and the Venezuela & Iran sanctions on one side and rising shale production in the US and indications of a moderation in global economic activity on the other, the oil price outlook remains uncertain.
- There was a modest rise in overall base fare yields (excluding ancillaries and surcharges) this month, but the downwards trend remains in place. For the less price-sensitive premium cabin yields, airlines have been able to recover some of the previous rise in fuel and other costs. Guidance on yields for Q1 was positive, at least in the US.
- Passenger demand started the year on a positive note, with both seasonally adjusted (SA) volumes and year-on-year growth ticking up modestly compared to a year ago. Meanwhile, the story is less positive on the freight side, with annual growth in industry-wide freight tonne kilometres remaining in negative territory and SA volumes trending downwards.

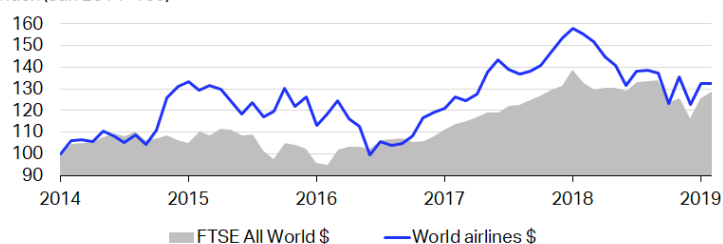
Financial indicators

Airline share price developments generally muted in February...

Airline Share Prices

US\$ indices (Jan 2014=100)	Index Feb 28th	% change on		
		one month	one year	start of year
World airlines	132.3	+0.0%	-14.7%	+7.8%
Asia Pacific airlines	119.4	+1.8%	-14.7%	+7.7%
European airlines	110.5	-0.5%	-24.3%	+7.7%
North American airlines	163.6	-0.9%	-7.4%	+6.9%
FTSE All World \$	128.7	+2.4%	-3.1%	+10.3%

Index (Jan 2014=100)



Source: Thomson Reuters Datastream

- The industry-wide airline share price index was unchanged in February, following the period of high volatility seen over Q4 2018 and into early-2019. The global equity index increased by a moderate 2.4% in the month.
- This month's stability in airline share prices points to a stabilisation in investor sentiment regarding the broader industry outlook following the recent volatility. At the regional level, the movements were mixed, but generally muted.
- Since the beginning of the year, airlines shares are up almost 8%, largely driven by a strong price pick-up in January. However, in year-on-year terms, the prices are almost 15% below their level of a year ago, compared with a decline of 3% in the global equities index.

Downward pressure on profit margins has moderated in the final quarter of 2018

Airline Financial Results

Number of airlines in sample	Regions	Q4 2017		Q4 2018	
		EBIT	Net post-tax	EBIT	Net post-tax
		margin ¹	profit ²	margin ¹	profit ²
16	North America	9.7%	4,174	9.2%	2,986
17	Asia-Pacific	10.2%	1,616	6.0%	869
9	Europe	4.3%	-601	-0.4%	-178
5	Latin America	5.0%	156	2.6%	160
2	Others	3.2%	10	10.2%	-123
49	Sample total	8.4%	5,355	6.0%	3,714

¹% of revenues ²US\$ million

Sources: The Airline Analyst, IATA

- The latest airline financial data from the final quarter of 2018 indicate that the intense downward pressure on industry-wide EBIT margin in the middle of the year has moderated recently; -2.4ppt over the year to Q4 vs -3.5ppt observed in Q3.
- That said, the data show mixed performance at the regional level. While airline profitability in North America recorded signs of improvement with a solid slowdown in the profit squeeze versus the previous two quarters, airlines based in Asia Pacific and Europe showed the opposite trend with EBIT margin remaining generally unchanged (former) or falling further (latter) vs Q3.

Decline in industry free cash flow driven mostly by lower net cash flow generation

Airline Cash Flow¹

Number of airlines in sample	Regions	Q4 2017			Q4 2018		
		Net cash flow ²	Capex	Free cash flow	Net cash flow ²	Capex	Free cash flow
16	North America	10.2%	13.6%	-3.4%	11.0%	13.1%	-2.0%
11	Asia-Pacific	15.8%	20.6%	-4.8%	10.2%	16.8%	-6.6%
7	Europe	12.2%	15.1%	-2.9%	5.3%	15.8%	-10.5%
4	Latin America	1.0%	3.4%	-2.3%	12.8%	14.0%	-1.2%
38	Sample total	11.1%	14.5%	-3.4%	9.9%	14.2%	-4.3%

¹% of revenues

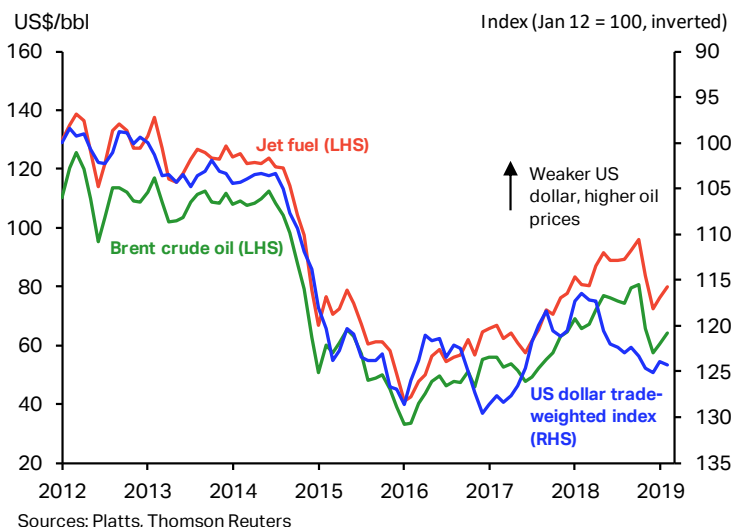
²From operating activities

Sources: The Airline Analyst, IATA

- The initial Q4 2018 sample of 38 airlines shows a modest fall in both industry-wide net and free cashflow compared to the same period a year ago.
- Net cash flow is currently 9.9% of revenues (down from 11.1% seen in Q4 2017). Meanwhile, capex spend – a business expense used by airlines for expansion and new investment deals – remains generally unchanged at just above 14% of revenues.
- Regionally, performance remains subdued in terms of free cashflow, with airlines based in Europe showing the poorest performance (-10.5%), followed by carriers in Asia-Pacific (-6.6%).

Fuel costs

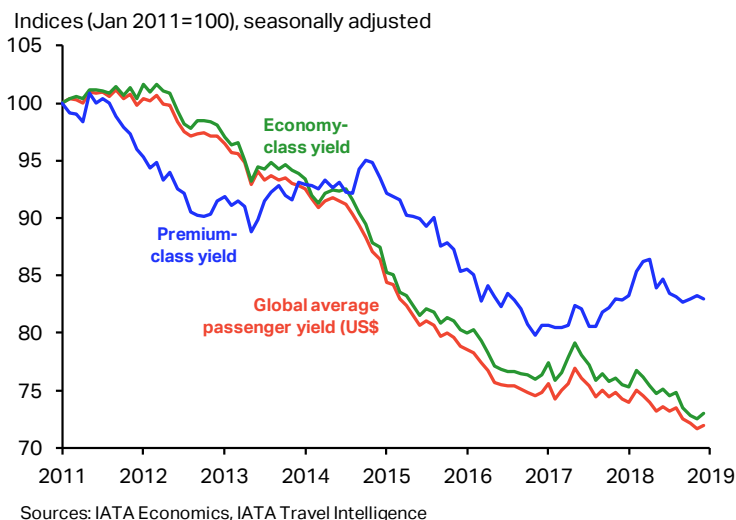
Oil and jet fuel prices continued to move higher in February...



- The average monthly price of Brent crude oil and jet fuel trended upwards for a second consecutive month in February, following a sharp contraction observed over Q4 2018 amidst rising oil supplies.
- The recent pick-up in prices reflects the decision of OPEC countries, led by Saudi Arabia, to cut oil supplies and the effect of sanctions that the US imposed on Iran and Venezuela. That said, with increased production from the shale industry in the US, the outlook for oil prices remains unclear.
- At the time of writing this report, the price of Brent crude oil hovers around US\$66-67/bbl and the jet fuel price is close to US\$80/bbl – both remain well below the elevated levels seen in early October 2018. For more information on oil price developments, check out our weekly [Jet Fuel Price Monitor](#).

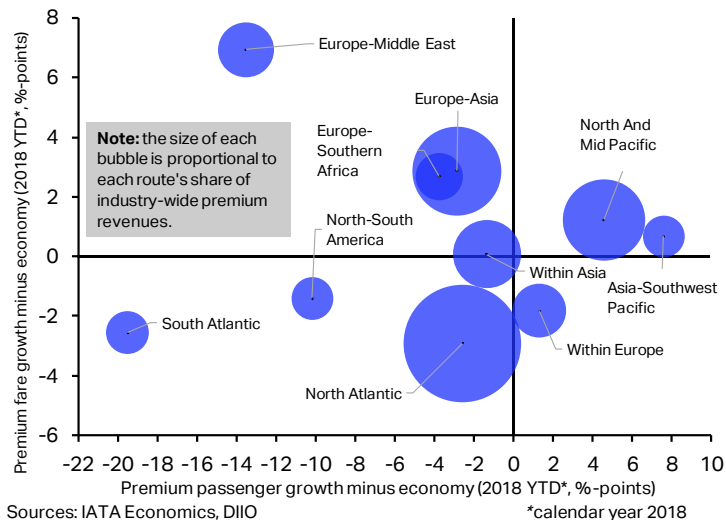
Yields and premium revenues

Airlines were able to partially recover costs through premium-cabin yields



- Global 'base fare' passenger yields (i.e. excluding surcharges and the revenue that airlines generate from ancillary services) rose a little in US dollar terms in December (latest available data).
- Despite that, total base fare yields have trended downwards in seasonally adjusted terms over 2018 and are currently about 4% lower compared to the same period a year ago.
- That said, premium-class yields have trended upwards as airlines were able to partly recover rising fuel costs in this less price-sensitive segment of the market. That ability seemed to peak in early 2018. Since then, premium class base fare yields have declined, though by much less than those in the economy cabin.

Premium class pax and revenue shares generally unchanged from 2017

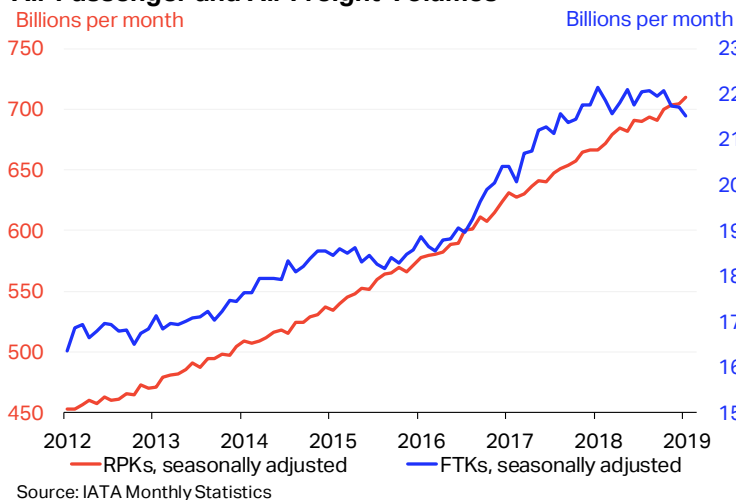


- Premium-class passengers accounted for a modest 5.2% of the total number of international origin-destination passengers over the course of 2018 but a much more significant 30.0% of total airline revenues. These shares are generally unchanged from 2017, underpinned by a relatively solid economic and demand backdrop, especially in the first three quarters of 2018.
- Premium passenger growth over the past year has outperformed its economy counterpart most notably on the Asia-Southwest and North & Mid Pacific markets. These markets also recorded solid gains in premium vs economy fares (top right-hand quadrant). Premium class demand has lagged behind in a number of cases, especially for the South Atlantic and Europe-Middle East markets.

Demand

Passenger demand ticked-up but freight demand continues to trend downwards

Air Passenger and Air Freight Volumes

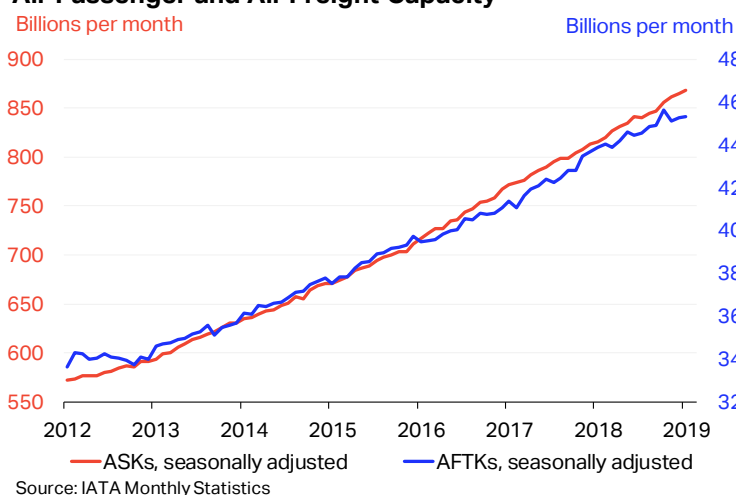


- Industry-wide revenue passenger kilometers (RPKs) started 2019 on a positive note, increasing by 6.5% year-on-year. The seasonally adjusted (SA) upward trend in RPKs also ticked up slightly this month, following the moderation seen over the second half of 2018, but it is too early to think that this month's pick-up represents a sustained shift in the growth trend.
- In contrast to the RPK performance, industry-wide freight tonne kilometres (FTKs) began the new year on a much softer note, currently 1.8% lower than their level of January 2018 and the slowest annual rate of growth in around three years. In seasonally-adjusted terms, seven of the past 12 months have recorded a fall in month-on-month FTK growth.

Capacity

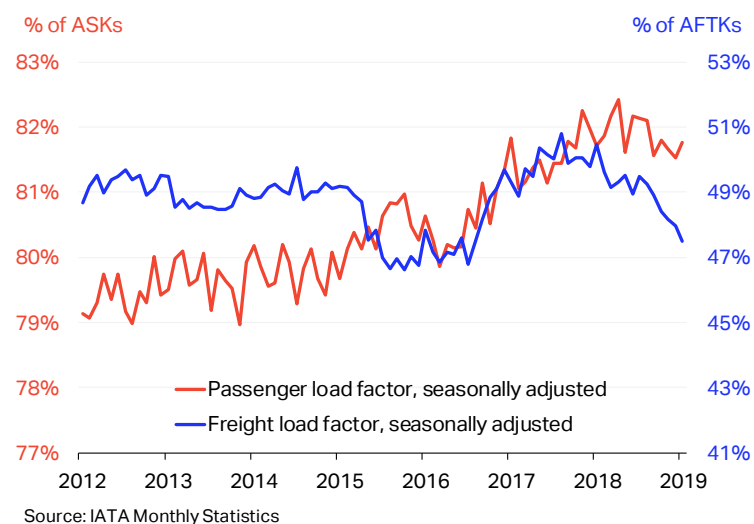
Capacity has been outpacing both passenger and freight demand

Air Passenger and Air Freight Capacity



- Industry-wide available seat kilometres (ASKs) grew by a brisk 6.4% year-on-year in early-2019.
- In seasonally adjusted (SA) terms, passenger capacity has been trending upwards slightly faster than demand. Capacity has now risen at an annualized rate of around 5.5% since mid-2018 – around 1 percentage point faster than overall demand over the same period.
- Meanwhile, available freight tonne kilometres (AFTKs) rose by a more modest 4% year-on-year in January but nonetheless much faster than the corresponding annual demand growth rate (-1.8%).

Passenger and freight load factors remain trending downwards in the long term...



- The industry-wide passenger load factor was essentially unchanged in January 2019 from the same period a year ago, at 79.6%. In seasonally adjusted terms, the load factor ticked-up slightly this month, although the modest downward trend since early-2018 remains in place, as capacity growth has outpaced passenger demand.
- Similarly on the freight side, having peaked in the middle of 2017 in seasonally adjusted terms, buoyed by the global inventory restocking cycle, the load factor continues to trend lower and is currently back at the levels last seen in late-2016. In annual terms, the freight load factor fell by 2.7 percentage points in January compared to the same month a year ago.

IATA Economics
economics@iata.org
20th March 2019

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