

AIRLINES FINANCIAL MONITOR

KEY POINTS

APRIL – MAY 2018

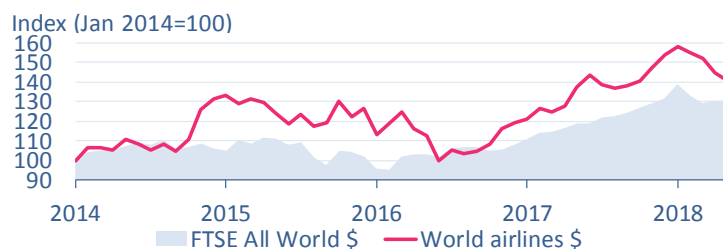
- ➔ The latest airline financial data continue to show that industry profitability improved in Q1 2018 relative to the same period a year ago. The pick-up in industry-level performance was driven by a turnaround for European airlines.
- ➔ Nonetheless, investor concerns about the impact of rising fuel prices on future airline financial performance saw global airline share prices fall for the fourth month in a row in May. The global airline share price index has now fallen by 8.5% since the start of the year, continuing to underperform the global equity market.
- ➔ Oil prices climbed again in May, driven by tighter market supply and ongoing geo-political tensions. At the time of writing the Brent crude oil price is currently sitting around US\$76/bbl – almost 60% higher than a year ago.
- ➔ The seasonally adjusted trends in passenger and freight demand have continued to diverge. All told, while the industry-wide passenger load factor has continued to set new record highs in seasonally adjusted terms in recent months, the corresponding freight load factor has fallen back to levels last seen at the start of 2017.
- ➔ The premium cabin's share of international passenger revenues fell to 30.6% in Q1 2018, from 31.1% a year ago. Nonetheless, the cabin continues to provide an important buffer for airline financial performance.

Financial indicators

Airline shares fell for the 4th month in a row in May, continuing to lag behind global equities

Airline Share Prices

US\$ indices (Jan 2014=100)	Index May 31st	% change on		
		one month	one year	start of year
World airlines	140.6	-2.8%	+2.1%	-8.5%
Asia Pacific airlines	128.9	-3.0%	+17.7%	-1.2%
European airlines	133.0	-1.4%	+10.6%	-8.0%
North American airlines	163.8	+0.4%	-9.3%	-11.5%
FTSE All World \$	130.3	-0.3%	+9.6%	-0.9%



Source: Thomson Reuters Datastream

- ➔ Global airline share prices fell by a further 2.8% in May – the fourth monthly decline in a row – to leave them 8.5% lower than where they started the year. While the wider equity market also fell in May, the global airline share price index has underperformed by a margin over the past year, mainly upon investor concerns of the impact of rising fuel prices.
- ➔ The decline in the global airline index in May was driven by falls in Asia Pacific and European airline shares (-3.0% and -1.4%, respectively).
- ➔ Meanwhile, although the North America index rose slightly over the month (+0.4%), airline shares in the region have fallen the most since the start of 2018, reflecting specific investor concerns of the impact of rising capacity growth in the region.

Industry financial performance improved in Q1 2018, driven by European airlines

Airline Financial Results

Number of airlines in sample	Regions	Q1 2017		Q1 2018	
		EBIT margin ¹	Net post-tax profit ²	EBIT margin ¹	Net post-tax profit ²
16	North America	7.9%	1,619	7.7%	1,636
30	Asia-Pacific	6.4%	2,311	6.3%	2,231
14	Europe	-2.2%	-1,125	2.0%	103
7	Latin America	6.9%	143	8.9%	232
6	Others	1.4%	52	3.2%	169
73	Sample total	4.7%	3,000	5.7%	4,371

¹% of revenues ²US\$ million
Note: Includes half-year results of Easyjet

Sources: The Airline Analyst, IATA

- ➔ Despite the ongoing pressure on airline equities, the latest financial results from Q1 2018 have continued to point to a pick-up in industry-wide financial performance relative to the same period a year ago. The EBIT margin in our sample of 73 airlines rose to 5.7%, from 4.7% a year ago.
- ➔ The improvement at an industry level was driven by a pick-up in performance in Europe (despite the first quarter of the year being a seasonally weak period for European airline profitability), alongside stronger showings from airlines based in Latin America and parts of the Middle East.

Pick-up in net cash flow in Q1 2018 underpinned a rise in free cash flow at an industry level

Airline Cash Flow¹

Number of airlines in sample	Regions	Q1 2017			Q1 2018		
		Net cash flow ²	Capex	Free cash flow	Net cash flow ²	Capex	Free cash flow
15	North America	14.9%	15.3%	-0.4%	19.8%	13.1%	6.7%
13	Asia-Pacific	15.9%	14.7%	1.2%	13.2%	14.6%	-1.4%
8	Europe	20.4%	13.8%	6.6%	25.2%	21.9%	3.3%
5	Latin America	6.7%	5.2%	1.4%	5.9%	6.9%	-1.0%
4	Others	12.3%	14.9%	-2.6%	10.9%	19.3%	-8.4%
45	Sample total	15.4%	14.2%	1.1%	18.4%	14.6%	3.8%

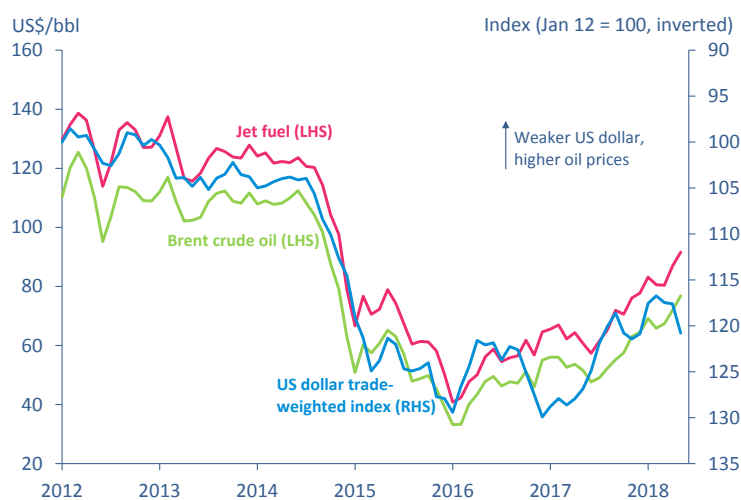
¹% of revenues ²From operating activities
Note: Includes half-year results of Easyjet

Sources: The Airline Analyst, IATA

- Our sample of 45 airlines indicates that free cash flow also improved at an industry-wide level in Q1 2018 compared to the same period a year ago (to 3.8% of revenues, up from 1.1% a year ago).
- This outcome mainly reflected an increase in net cash flow from operations (to 18.4% of revenue in our sample, from 15.4%), offset by a 0.4 percentage point pick-up in capex spending (to 14.6%).
- The industry-wide estimate masked a range in performance at the regional level. European airline free cash flow declined in annual terms following a sharp pick-up in capital investment, while airlines in Asia Pacific saw a moderate decline in net cash flow generation in the quarter relative to Q1 2017.

Fuel costs

Oil prices rose above US\$80/bbl during May, and remain 55-60% higher than a year ago

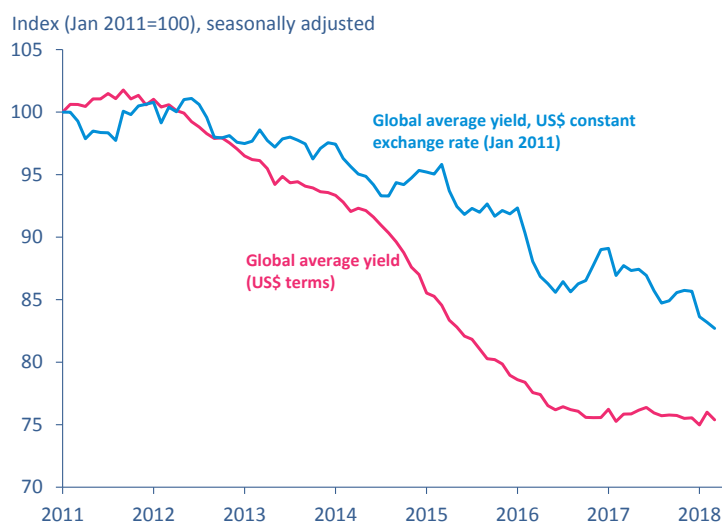


Sources: Platts, Thomson Reuters Datastream

- The upward trend in global oil prices continued into May, with the Brent crude benchmark breaching the US\$80/bbl mark during the month for the first time since November 2014. Oil prices fell back towards end-May, but still rose by around US\$4/bbl during the month as a whole and remain almost 60% higher in year-on-year terms.
- The upward trend in oil prices has been driven by a combination of a gradual reduction in global oil inventories on the back of a tightening in supply, as well as ongoing geo-political concerns.
- Nonetheless, while the futures curve has shifted up in recent months, it is still consistent with a modest decline in oil prices over the coming years. The current curve has the oil price falling back below the US\$70/bbl mark by the middle of 2020.

Yields and premium revenues

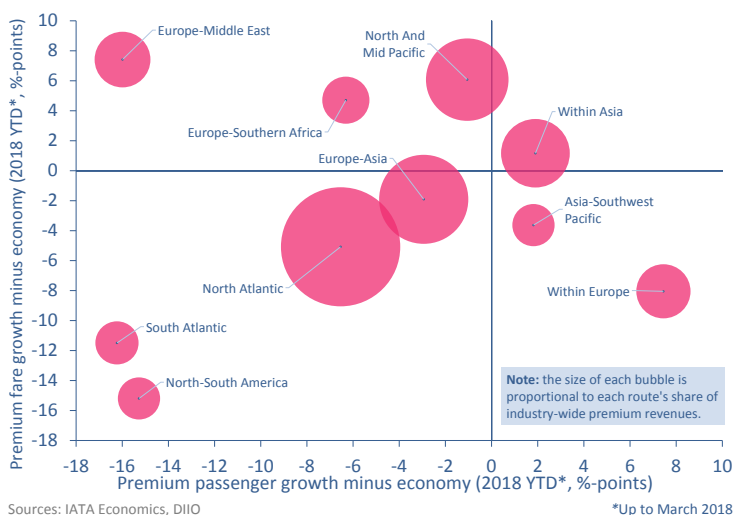
Passenger yields (excl. surcharges & ancillaries) broadly unchanged in annual terms in Q1



Sources: IATA Economics, IATA Travel Intelligence, Thomson Reuters Datastream

- Having risen strongly in month-on-month terms in February, the global passenger yield fell back during March. In any case, the bigger picture is that passenger yields have continued to track broadly sideways in SA terms, as they have now done so since early-2017. In year-on-year terms, the global passenger yield was broadly unchanged in Q1 2018 relative to the same period a year ago.
- As we have noted before, the passenger yield data presented here relate to developments in the 'base' airfare only and exclude revenue from surcharges and ancillary services. These additional sources of passenger revenue look to be playing a key role in supporting the ongoing robust financial performance of the industry.

Premium traffic share was broadly unchanged in Q1'18 vs. year ago, but revenue share fell

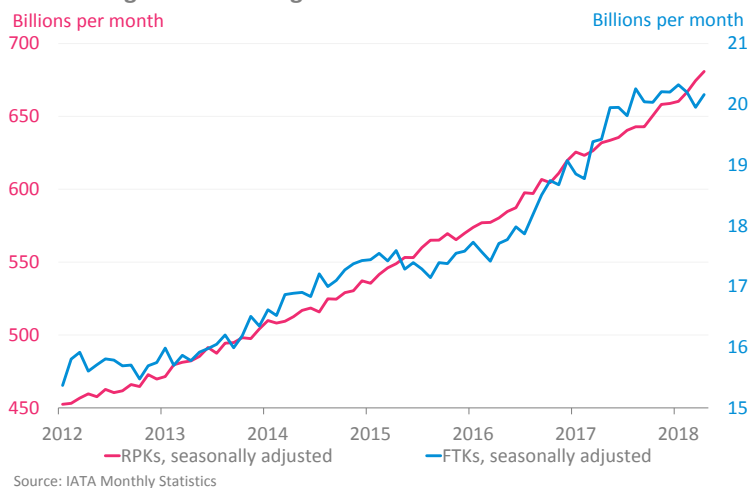


- ➔ Premium-class passengers accounted for 5.5% of total international origin-destination traffic in the first quarter of 2018 – unchanged from the share seen in the same period of 2017.
- ➔ The premium cabin provides an important buffer for airline financial performance, and accounted for 30.6% of total international revenues in Q1 2018. However, this share was slightly lower than that seen in the same period a year ago (31.1%).
- ➔ This mainly reflected developments in the two-largest markets in terms of premium revenues – the North Atlantic and Europe-Asia – where both demand and fare growth have lagged behind their economy-class counterparts so far this year.

Demand

Trends in passenger and freight volumes have continued to diverge in recent months

Air Passenger and Air Freight Volumes

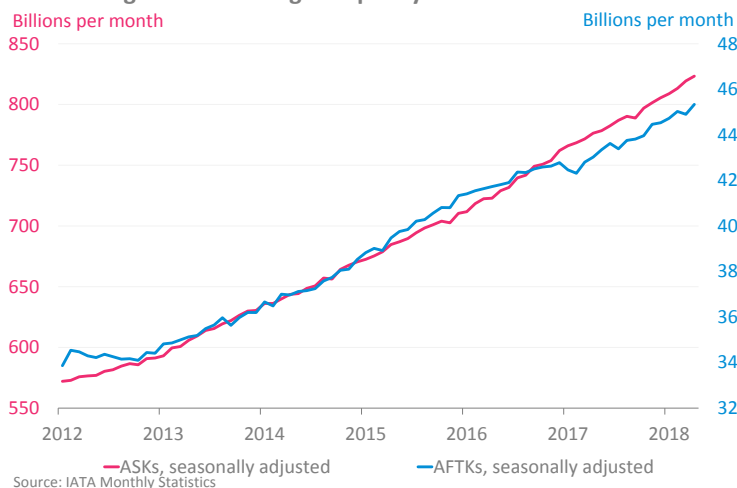


- ➔ Industry-wide revenue passenger kilometres (RPKs) increased by 6.2% year-on-year in April 2018. This was a slowdown from the 12-month high of 9.7% seen in March, but this largely reflected developments a year ago – particularly the comparatively late timing of Easter in 2017. The bigger picture is that the upward trend in seasonally adjusted traffic has strengthened over the past three months.
- ➔ By contrast, while year-on-year growth in industry-wide freight tonne kilometres (FTKs) recovered to 4.1% in April, freight volumes have now trended broadly sideways since August last year. Unless we see a pick-up in the demand trend in the coming months, annual FTK growth will slow once again towards mid-2018.

Capacity

Passenger and freight capacity are now both trending upwards at similar rates

Air Passenger and Air Freight Capacity

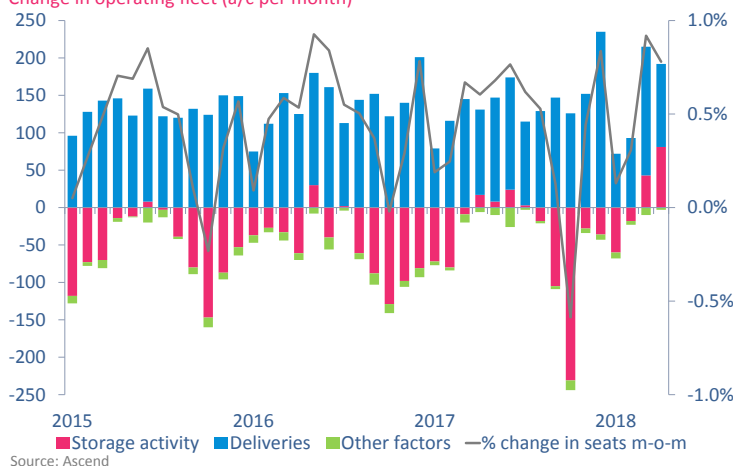


- ➔ Industry-wide available seat kilometres (ASKs) increased by 5.9% year-on-year in April. Given the recent pick-up in the SA industry-wide demand trend noted above, demand is once again rising slightly ahead of capacity.
- ➔ Meanwhile, available freight tonne kilometres (AFTKs) rose by 5.1% year-on-year in April 2018, down from 6.3% in the previous month.
- ➔ The upward trend in SA FTKs has fallen below that of AFTKs over the past eight months or so. In fact, April was just the second time in 21 months in which the annual pace of capacity growth has exceeded that of demand.

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

Airline Fleet Development

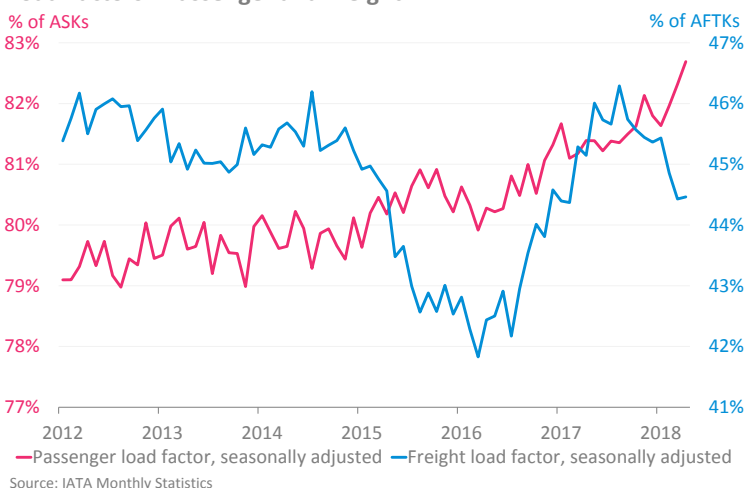
Change in operating fleet (a/c per month)



- The number of available seats in the global airline fleet increased by 0.8% in month-on-month terms in April, and by 5.7% compared to the same month in 2017.
- 111 aircraft were delivered in the month – slightly fewer than the 114 delivered in the same period a year ago. Altogether, the number of aircraft delivered in the first four months of 2018 was slightly lower than that seen in the same period last year (448 vs. 454).
- Just 51 aircraft left the fleet to go into storage in April – around one-third of the amount that left in April 2017. With 132 aircraft returning to the fleet from storage in the month, net storage activity made its biggest contribution to fleet growth in at least four years.

Passenger load factor rose to a fresh all-time high in April, as freight loads slipped further

Load Factors - Passenger and Freight



- The passenger load factor increased by 0.2 percentage points in April relative to the same month a year ago, taking it to a record high for the month (82.3%). The load factor also reached a fresh all-time high on a SA basis.
- Meanwhile, the industry-wide freight load factor fell by 0.5 percentage points compared to April 2017. The slowdown in the upward trend in freight volumes since mid-2017 has continued to be reflected in a corresponding decline in the SA load factor. The series is currently back to levels last seen in early-2017.

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