AIRLINES FINANCIAL MONITOR

KEY POINTS

September 2016 – October 2016

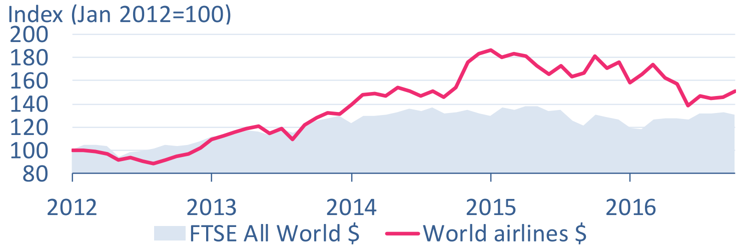
- The initial financial results from Q3 2016 point to another solid quarter for industry profitability and cash flow, although they add to earlier signs that the industry profitability cycle may have peaked;
- Global airline share prices rose by 3.6% in October, but have underperformed the wider equity market this year;
- Brent crude oil prices reached a 15-month high during October, but have fallen back so far in November. The oil market is slowly rebalancing, and prices are expected to trend upwards gradually over the coming years;
- There have been further signs that the intense downward pressure on passenger yields eased during the middle part of 2016, in keeping with the change in the trend of oil prices;
- The premium segment remains an important buffer for airline financial performance. Premium airfares have held up better than those in economy on many of the most important premium routes so far this year;
- Developments in passenger traffic continue to reflect the net influence of a number of factors. Traffic was resilient in September, and the seasonally-adjusted industry-wide load factor increased to a nine-month high;
- The upward trend in air freight volumes has accelerated in recent months, helped in part by one-off factors. Nonetheless, the load factor remains at a historically low level, and wider weakness of world trade is still a concern.

Financial indicators

Global airline share prices rose by 3.6% in October, outpacing the wider equity market again

Airline Share Prices

US$ indices (Jan 2012=100)	Index Oct 31st	% change on one month	one year	start of year
World airlines	**151.4**	**+3.6%**	**-16.7%**	**-14.2%**
Asia Pacific airlines	76.0	-1.5%	-17.4%	-13.4%
European airlines	168.5	+1.4%	-26.3%	-27.8%
North American airlines	339.7	+6.4%	-14.2%	-10.3%
FTSE All World $	**130.4**	**-1.7%**	**+0.1%**	**+3.0%**



Source: Thomson Reuters Datastream

- Global airline share prices rose by 3.6% in October. The index of North American carriers increased by 6.4% during the month, while the Asia Pacific index fell for the third month in a row (-1.5%). European airline shares rose by 1.4%, but have fallen the most since the start of 2016 (-28%).
- The global airline index has risen by almost 9% since the low reached following the 'Brexit' vote. Investor concerns about the impact of lower unit revenues on profitability, and labor costs in North America in particular, have weighed on share prices during much of 2016. Global airline shares ended the month more than 14% lower than their level at the start of 2016 and have lagged behind the wider equity market by a wide margin so far this year.

Robust financial performance, but further signs that the profit cycle may have peaked

Airline Financial Results

Number of airlines in sample	Regions	Q3 2015 EBIT margin[1]	Q3 2015 Net post-tax profit[2]	Q3 2016 EBIT margin[1]	Q3 2016 Net post-tax profit[2]
15	North America	19.6%	6,186	17.1%	3,847
5	Asia-Pacific	9.3%	405	12.2%	1,516
6	Europe	14.0%	2,597	13.8%	3,543
3	Others	5.7%	-7	9.3%	41
29	**Sample total**	**16.0%**	**9,181**	**15.1%**	**8,947**

[1] % of revenues [2] US$ million
Note: Includes Kenya Airways half-year results.
Sources: The Airline Analyst, IATA

- The initial financial results from Q3 2016 continue to indicate robust performance by historical standards. However, industry operating conditions are becoming more challenging, and the latest results are a further indication that the profitability cycle, while remaining robust, may have peaked.
- The EBIT margin in our sample of 29 airlines dipped to 15.1%, from 16.0% in the same period in 2015. Margins fell in North America, reflecting volatile fuel and labor costs. By contrast, margins improved in Asia Pacific and were broadly unchanged in Europe from a year ago.

Free cash flow edges down in Q3 2016, reflecting lower net cash flow and a pick-up in capex

Airline Cash Flow[1]

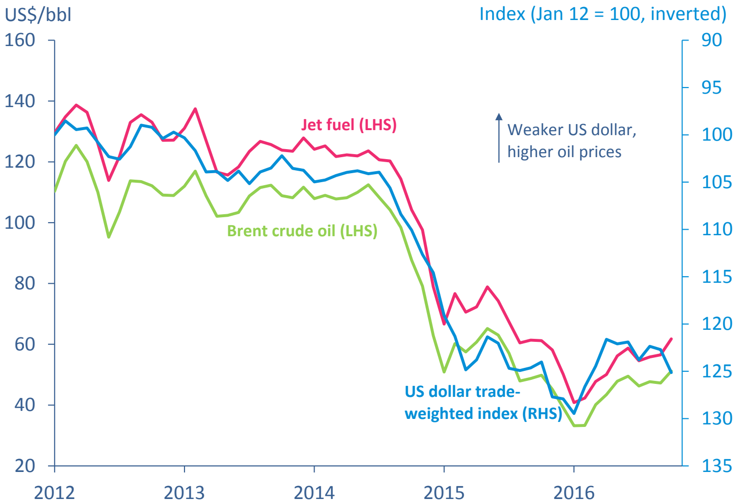
Number of airlines in sample	Regions	Q3 2015 Net cash flow[2]	Q3 2015 Capex	Q3 2015 Free cash flow	Q3 2016 Net cash flow[2]	Q3 2016 Capex	Q3 2016 Free cash flow
10	North America	15.0%	9.5%	5.5%	14.2%	9.6%	4.6%
1	Asia-Pacific	0.2%	-5.3%	5.5%	11.2%	1.4%	9.8%
3	Europe	5.1%	12.4%	-7.3%	1.6%	15.7%	-14.1%
2	Others	3.3%	3.1%	0.2%	4.1%	4.3%	-0.2%
16	**Sample total**	**13.9%**	**9.2%**	**4.7%**	**13.1%**	**9.7%**	**3.4%**

[1] % of revenues *[2] From operating activities*
Note: Includes Kenya Airways half-year results.
Sources: The Airline Analyst, IATA

- Net cash flow in our sample of 16 airlines eased to 13.1% of revenues in Q3 2016, from 13.9% in the same period last year. Regional differences will become clearer as more airline results become available in the coming weeks and months.
- Airlines in our sample increased capital expenditure slightly as a share of revenues in Q3 2016 compared to the same quarter in 2015. As a result, free cash flow in Q3 in the sample dropped to 3.4% of revenues from 4.7%. Free cash flow allows airlines to return cash to investors or to repair their balance sheets by paying down debt.

Fuel costs

Brent crude prices reached a 15-month high in October, but have fallen back in November

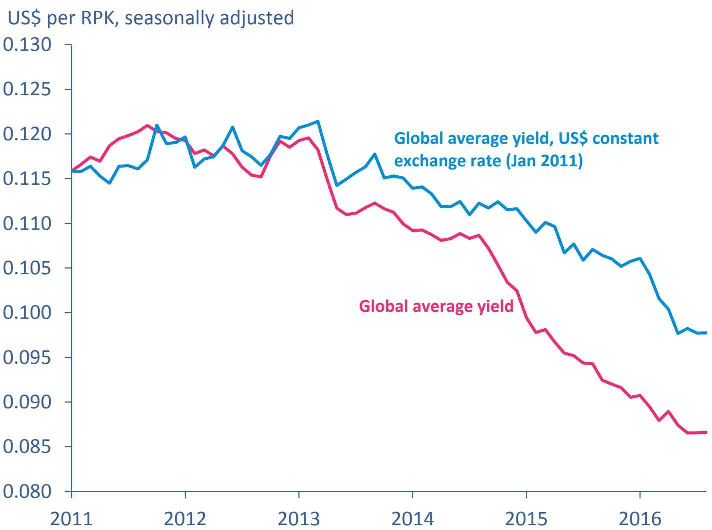


Sources: Platts, Thomson Reuters Datastream

- Brent crude oil prices climbed to a 15-month high during October following the agreement by OPEC in September to cut oil output in the months ahead. Nonetheless, stronger-than-expected oil inventory data out in the US, as well as skepticism as to whether OPEC will be able to limit production as planned, have seen oil prices slide back in early-November. Brent crude recently fell below $45/bbl for the first time since early-August.
- A rebalancing in the oil market is slowly taking pace, and the annual comparison will become increasingly unfavorable over the months ahead. The futures market and oil analysts expect a weak upward trend in oil prices over the foreseeable future, with prices remaining relatively low (around US$55/bbl) until 2020.

Yields and premium revenues

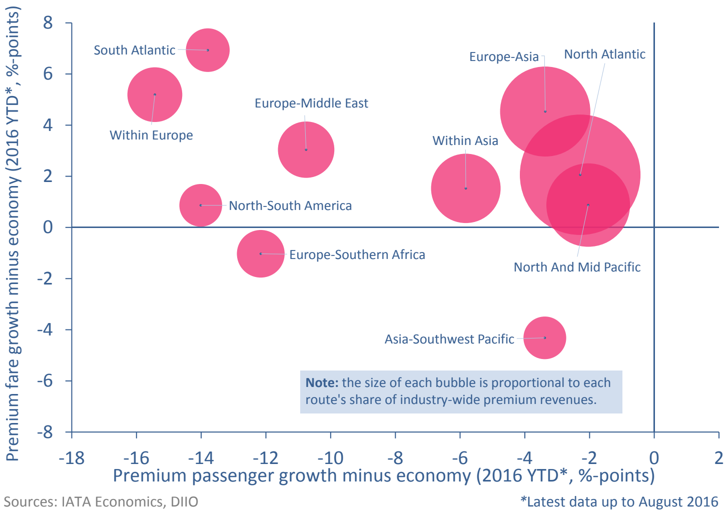
Further signs that downward pressure on underlying yields has eased



Sources: IATA Economics, IATA PaxIS+, DIIO, Thomson Reuters Datastream

- The global average yield in reported US dollar terms has trended downwards since late-2014. However, the trend has paused in seasonally-adjusted terms over the past few months (the latest data go up to August 2016 and exclude taxes, fees and surcharges). This ties in with the change in the trend in fuel prices over the past nine months or so.
- All told, the latest data provide additional evidence that the intense downward pressure on underlying (ie, constant exchange rate – the blue line) yields seen during the opening months of 2016 eased during the middle months of the year.

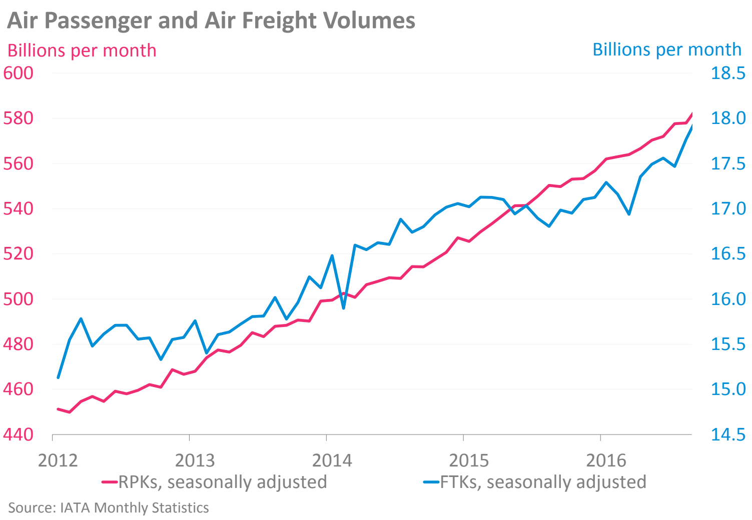
Premium traffic continues to offer an important buffer for airline financial performance



- O-D premium international journeys accounted for 5.2% of the total over the first eight months of 2016, down from 5.5% a year ago. Growth in premium international passenger traffic has continued to lag behind that of economy.
- However, as has been the case for some time, premium fares have held up better than those in economy on the majority of the top-10 premium routes. In fact, premium's share of revenues has *risen* slightly so far this year on the Europe-Asia and North Atlantic markets (these two routes accounted for nearly two-fifths of industry-wide premium revenues combined last year). All told, the high-yielding premium segment continues to offer an important buffer for airline financial performance.

Demand

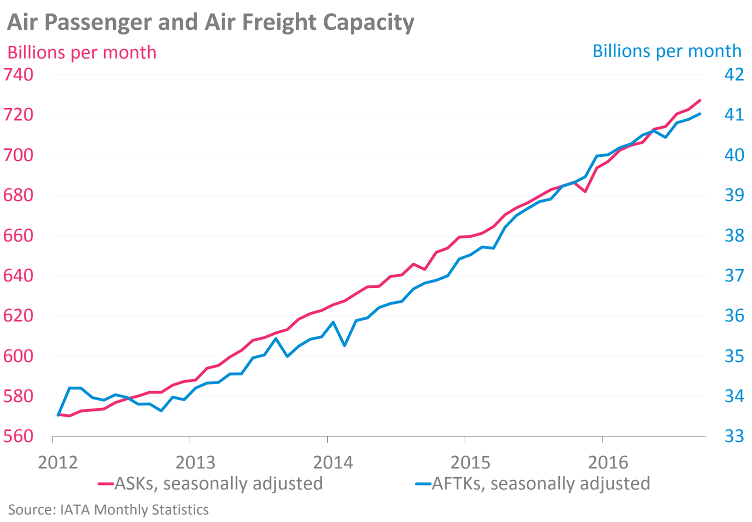
Passenger traffic was resilient in September, alongside a pick-up in conditions for freight



- Annual growth in industry-wide passenger traffic accelerated to 7.0% year-on-year in September – a seven-month high. Developments continue to reflect the net impact of a range of competing drivers, including the subdued global economic backdrop and lower air fares.
- Meanwhile, the upward trend in seasonally-adjusted air freight has strengthened of late, aided in part in September by one-off factors (including the rushed replacement of Galaxy Note 7 devices). However, the underlying weakness of world trade remains an ongoing concern for sustained growth in freight volumes. Against this backdrop, freight carriers need to look past the traditional drivers of growth (link).

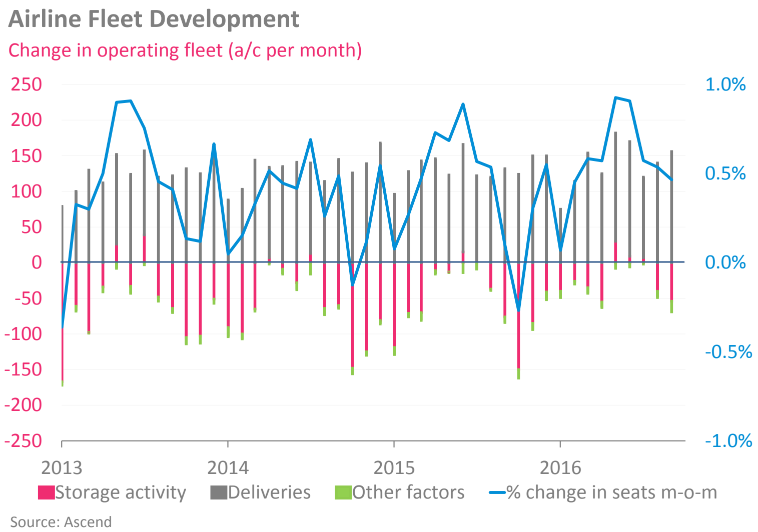
Capacity

Trends in capacity have moderated in recent months, particularly for freight



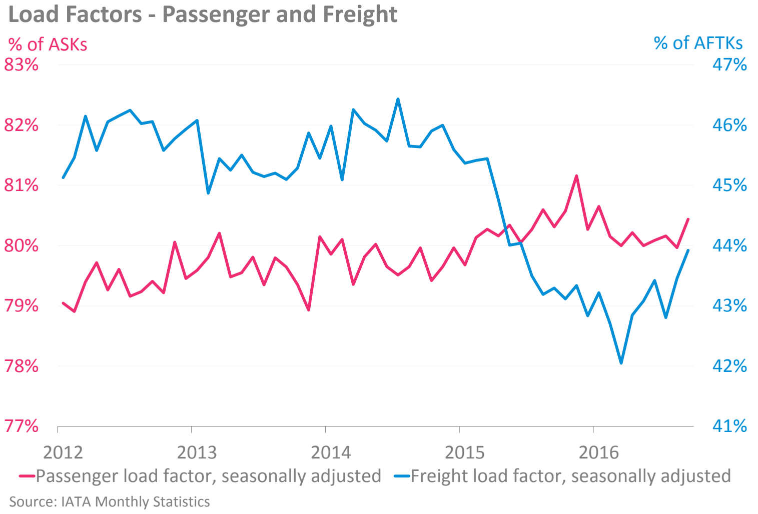
- Available seat kilometres grew by 6.6% year-on-year in September. Airlines have moderated capacity growth somewhat this year in line with the wider easing in growth momentum.
- The upward trend in available freight tonne kilometres has eased in recent months, in part owing to a slowdown in deliveries to the wide-body passenger fleet in 2016 (particularly in Asia Pacific). Capacity grew by 4.7% year-on-year in September, and lagged behind FTK growth for the first month since February 2015 (when disruption at US west coast seaports boosted demand for air freight).

Net storage activity makes another modest negative contribution to fleet growth



- The number of available seats in the global airline fleet increased by 0.5% in September compared to the previous month, and by 5.8% year-on-year.
- 156 new aircraft were delivered in September – 24 more than were delivered in September 2015 (132). Net storage activity made the biggest negative contribution (-54 in September) since April. This was driven by an increase in aircraft going into storage compared to what we saw during the middle of 2016.

Passenger and freight loads both increased in seasonally-adjusted terms in September



- The industry-wide passenger load factor rose by 0.6 percentage points in seasonally adjusted terms in September, taking it to its highest level since January. This was driven mainly by a pick-up on the demand side. The September load factor was at or very close to a record high in all regions expect the Middle East.
- The industry-wide freight load factor remains at a historically low level, and is continuing to put pressure on freight yields and revenues. However, given the acceleration in the upward trend in traffic in recent months, the seasonally-adjusted industry-wide load factor has risen by nearly two percentage points since its recent low in early 2016.

David Oxley
economics@iata.org
9th November 2016

Get the data
Access data related to this briefing through IATA's Monthly Statistics publication:
www.iata.org/monthly-traffic-statistics

20-year passenger forecasts
To find out more about our long-term passenger forecasts, and to sign up, visit:
www.iata.org/pax-forecast

IATA Economics Consulting
To find out more about our tailored economics consulting solutions, visit:
www.iata.org/consulting