AIRLINES FINANCIAL MONITOR

KEY POINTS

AUGUST – SEPTEMBER 2018

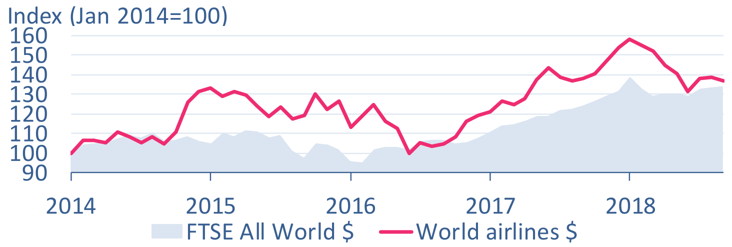
- The final Q2 2018 airline financial data confirm a decline in airline profitability compared to the same quarter a year ago. Industry-wide cash flows are better than a year ago, but this masks considerable regional differences.
- Global airline share prices eased lower in September, despite a 1.0% gain in the North American sub-index and notwithstanding a small gain in global equities overall. Over the past year, North American airline shares continue to outperform the wider equities market.
- Oil and jet fuel prices both moved solidly higher in September, driven mainly by supply concerns. Oil prices have risen by around 40% over the past year and jet fuel prices averaged more than US$90bbl in September.
- Global (total) passenger yields (base fare only) have moved a little higher in recent months, with premium cabin yields continuing to show more resilience than those of the economy cabin and helping to offset some of the impact of rising input prices.
- Passenger demand remained solid into the peak northern hemisphere summer period. Although freight demand has recently eased to a modest pace, yields appear to be holding up.

Financial indicators

Global airline shares dip in September, underperforming the wider equities market

Airline Share Prices

US$ indices (Jan 2014=100)	Index Sep 28th	% change on one month	% change on one year	% change on start of year
World airlines	**137.1**	**-1.0%**	**-0.8%**	**-10.8%**
Asia Pacific airlines	115.5	-1.5%	-1.6%	-11.4%
European airlines	115.8	-4.3%	-11.2%	-19.9%
North American airlines	183.8	+1.0%	+12.3%	-0.7%
FTSE All World $	**134.1**	**+0.3%**	**+7.6%**	**+2.0%**



Source: Thomson Reuters Datastream

- Global airline share prices fell by an even 1.0% in September, following two consecutive months of gains. The global equity index increased by a modest 0.3% in the month.
- The fall in global airline share prices was mainly due to the European sub-index which was down 4.3% in September. Asia Pacific airline shares fell by 1.5%, with both more than offsetting a 1.0% increase in the Nth American airline share price index.
- Over the past year, airline shares have fallen moderately, down 0.8%, and in contrast with the solid 7.6% increase in the overall global equities market.

The final Q2 2018 data confirm a decline in airline profitability

Airline Financial Results

Number of airlines in sample	Regions	Q2 2017 EBIT margin[1]	Q2 2017 Net post-tax profit[2]	Q2 2018 EBIT margin[1]	Q2 2018 Net post-tax profit[2]
38	North America	14.0%	6,313	11.2%	5,064
30	Asia-Pacific	5.0%	1,421	2.8%	656
16	Europe	9.7%	3,820	8.3%	3,874
10	Latin America	4.4%	-302	-1.0%	-548
5	Others	6.4%	59	0.9%	2
99	**Sample total**	**10.3%**	**11,311**	**7.8%**	**9,048**

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

Note: Includes half-year results of Flybe, Fastjet and Easyjet

Sources: The Airline Analyst, IATA

Note: Includes half-year results of Cathay Pacific Airways, Royal Jordania and Transavia

- The final airline financial data for Q2 2018 confirm the decline in profitability compared with the performance of a year ago. The EBIT margin for our sample of 99 airlines dipped to 7.8% in Q2 2018, from 10.3% a year ago while net post-tax profits are around $2.3bn lower.
- The dip in EBIT margin is broad-based, across all regions, as airlines confront ongoing increases in a number of key input costs. The largest impact on industry-wide profits is coming from North America and the Asia Pacific, although the EBIT margin of airlines in the former region remains robust.

Industry cash flows better than a year ago, despite sizeable regional differences

Airline Cash Flow[1]

Number of airlines in sample	Regions	Q2 2017 Net cash flow[2]	Q2 2017 Capex	Q2 2017 Free cash flow	Q2 2018 Net cash flow[2]	Q2 2018 Capex	Q2 2018 Free cash flow
17	North America	17.3%	12.5%	4.8%	19.5%	10.9%	8.7%
21	Asia-Pacific	13.5%	18.0%	-4.5%	14.8%	16.5%	-1.7%
13	Europe	22.4%	9.3%	13.1%	19.3%	13.9%	5.3%
8	Latin America	7.9%	7.3%	0.6%	9.9%	10.0%	-0.1%
4	Others	23.9%	9.0%	14.9%	16.4%	19.1%	-2.7%
63	**Sample total**	**17.1%**	**12.8%**	**4.3%**	**17.9%**	**12.9%**	**4.9%**

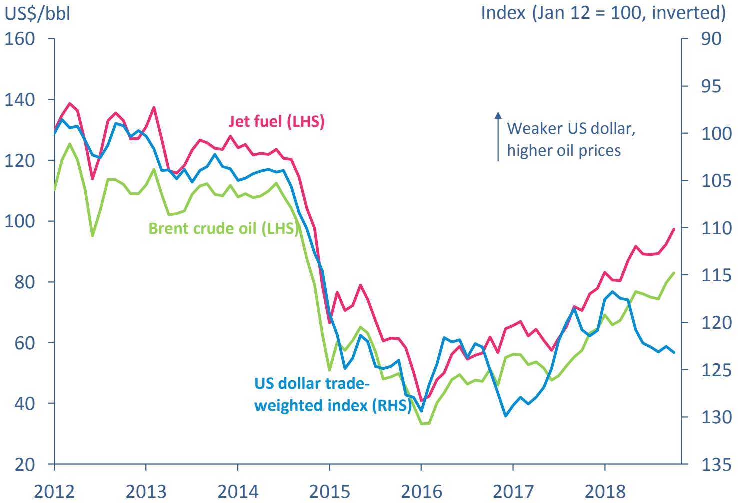
[1] % of revenues *[2] From operating activities*
Note: Includes half-year results of Agean Airlines, Fastjet and Easyjet

Sources: The Airline Analyst, IATA

- Our final Q2 sample of 63 airlines reporting cash flow data shows a moderate improvement in both industry-wide net and free cash flow vs a year ago.
- Net cash flow is currently 17.9% of revenues (up from 17.1% a year ago) and free cash flow 4.9% (vs 4.3%). Capex spend is essentially unchanged at just under 13% of revenues.
- Regionally, performance varies considerably. Free cash flows are currently strongest for Nth America (8.7%) and Europe (5.3%).

Fuel costs

Oil and jet fuel prices both moved higher in September

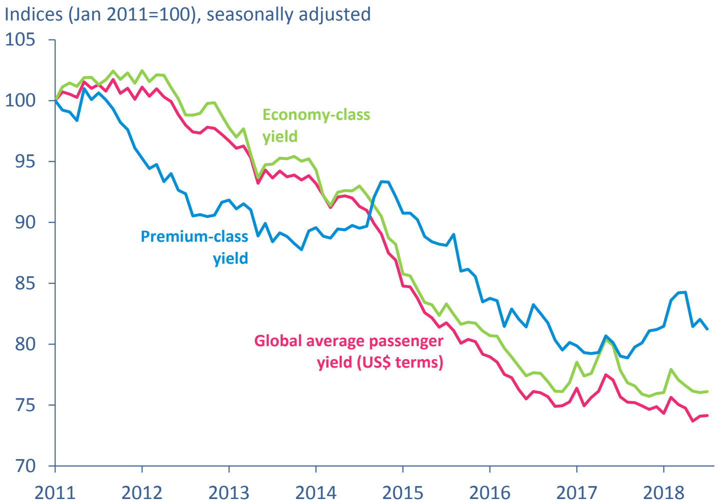


Sources: Platts, Thomson Reuters Datastream

- Crude oil and jet fuel prices both pushed higher in September. Crude prices reached their highest level since 2014, boosted by OPEC's refusal to increase output, even with the US sanctions on Iran likely to reduce global supply.
- The Brent crude benchmark lifted above US$80/bbl in September and ended the month averaging only slightly below that level. Crude oil prices have risen by around 40% on a year ago.
- Jet fuel prices also moved solidly higher in the month, increasing by around 3.5%, and pushing through the $US90/bbl level to average around $92 for the month of September overall.

Yields and premium revenues

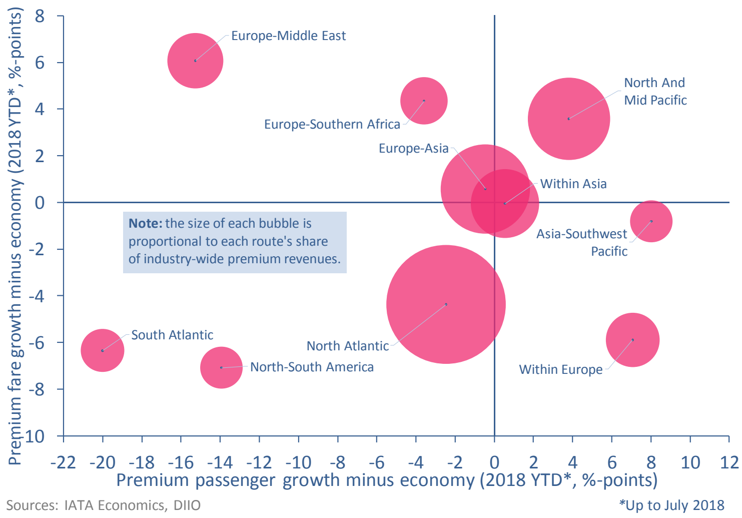
Premium and economy-cabin passenger yields continue to diverge



Sources: IATA Economics, IATA Travel Intelligence

- Global (total) passenger yields ($US terms) have moved a little higher over recent months, as airlines try to recover some of the rising input costs through airfares.
- Recall that these data reflect developments in the 'base' airfare only and exclude revenue from surcharges and ancillary services.
- The gap between the premium and economy cabin yields – which started to become clear around mid-2017 – has been maintained in the latest monthly data.
- The IMF's recent downgrade to the global economic outlook, combined with widening trade tensions could see yields come under renewed downward pressure in the months ahead.

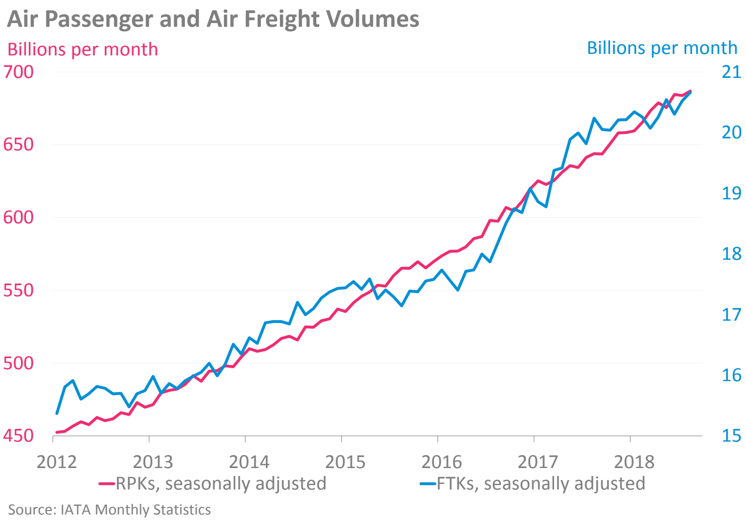
International premium traffic and revenue shares remain stable over the year-to-date



- Premium-class passengers accounted for 5.2% of total international origin-destination traffic in the first seven months of 2018. This proportion was unchanged from the same period a year ago.
- In terms of revenue, premium-class passengers accounted for 30.4% of total passenger revenues over the first seven months of 2018, down only marginally on the outcome for the same period a year ago.
- Premium passenger growth over the year-to-date has outperformed its economy counterpart most visibly on the Asia-Southwest Pacific and Within Europe markets. The largest outperformance of premium fares (vs economy) has been in the Europe-Middle East market.

Demand

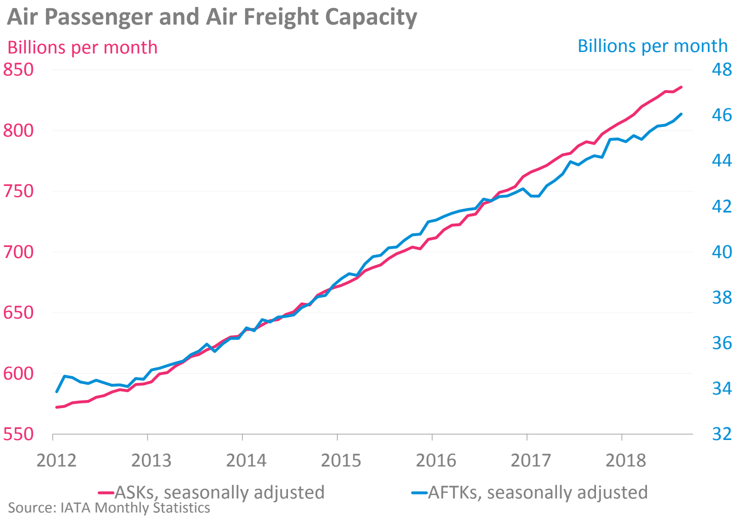
Passenger demand remains solid into the peak season, freight performance is more modest



- Year-on-year growth in industry-wide revenue passenger kilometres (RPKs) increased to 6.4% in August, up from 6.1% in July.
- The latest data provide further evidence of solid growth in RPKs during the peak period of passenger demand over the northern hemisphere summer.
- Industry-wide FTKs increased by 2.3% year-on-year in August – unchanged from July and less than half the five-year average pace (5.1%).
- As we have noted previously, this slowdown in FTK growth is consistent with the typical pattern following a business inventory-led upturn, such as that observed in 2017.

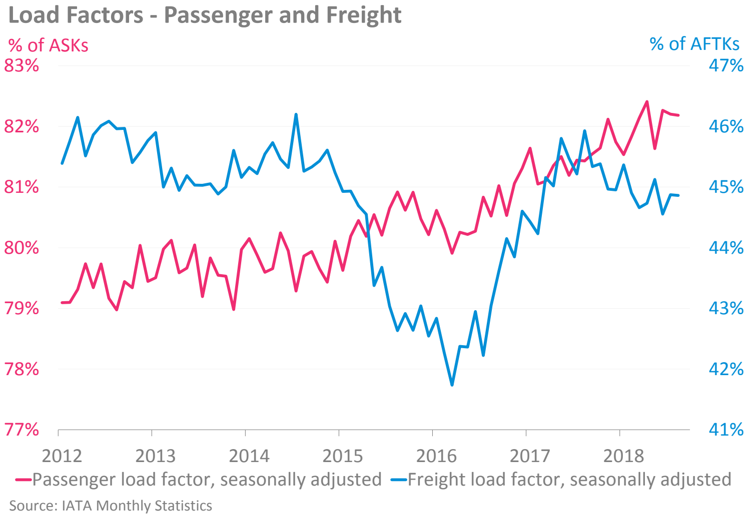
Capacity

Demand outpacing capacity for passenger but not freight



- Industry-wide available seat kilometres (ASKs) grew by 5.5% year-on-year in August.
- Passenger demand is continuing to trend upwards in seasonally adjusted terms at a slightly faster rate than capacity.
- On the freight side, available freight tonne kilometres (AFTKs) grew by 4.5% year-on-year in August, up from 3.9% in July and faster than the corresponding annual demand growth rate for the sixth month in a row.

The divergent trends in air passenger and freight load factors remain clear



- With demand continuing to outpace capacity, the industry-wide passenger load factor rose by 0.7 percentage points relative to August 2017, to an all-time (unadjusted) record high of 85.3%. (Note that the chart depicts seasonally adjusted data.)
- The load factor rose in annual terms in August in all regions except the Middle East and Latin America.
- For freight, faster capacity growth compared to demand has seen the industry-wide load factor fall by 0.9 percentage points compared to August 2017.
- That said, capacity and demand are now both currently trending upwards in seasonally adjusted terms at a similar pace, and freight yields appear to be holding up.

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