Airlines Financial Monitor

November-December 2020

Key points

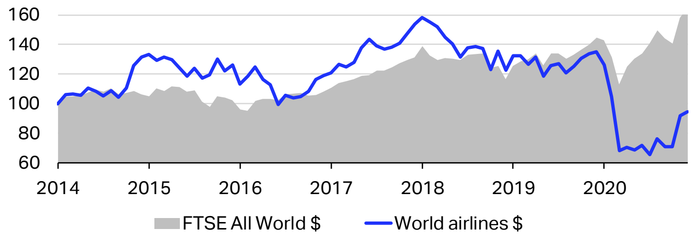
- Our final Q3 financial results show that airlines continued to suffer from very weak travel demand and burnt cash, albeit at a slower rate compared to Q2 with the help of cost cutting measures and robust cargo revenues. Initial Q4 2020 earnings announcements indicate that airlines continued to burn cash as the recovery in demand stalled. However, the vaccine news makes us estimate that airlines could achieve cash break-even towards the end of 2021.
- The global airline share price index rose in December but still lagged wider equity markets as the resurgence of the virus weighed on the travel demand recovery. Looking forward, the widespread availability of vaccines and implementation of successful testing regimes will be key for the recovery in travel demand and airline share prices.
- Oil and jet fuel prices went up in January on the back of U.S. fiscal stimulus expectations. However, the near-term outlook for global jet fuel demand is still uncertain as lockdowns and border closures to contain the pandemic remain in place.

European airlines supported the global airline equity index in December

Airline Share Prices

US$ indices (Jan 2014=100)	Index Dec 31st	% change on one month	one year	start of year
World airlines	**94.4**	**+2.9%**	**-30.2%**	**-30.2%**
Asia Pacific airlines	77.5	-2.4%	-29.5%	-29.5%
European airlines	85.2	+9.6%	-24.7%	-24.7%
North American airlines	115.0	+0.9%	-31.5%	-31.5%
FTSE All World $	**165.0**	**+4.5%**	**+14.1%**	**+14.1%**

Index (Jan 2014=100)



Source: Refinitiv Eikon Datastream

- Following the vaccine rally in November, airline shares with the exception of European airlines underperformed wider equity markets in December. While the expectation of fast rollout of vaccines is reflected positively in European carriers, Asia-Pacific airline shares declined as the resurgence of the virus halted the recovery in demand in main Asian markets.
- Overall, global airline shares ended the year 2020 down by 30% diverging from the wider equity markets (+14.1%) as the pandemic caused travel demand to plummet. 2021 will also be a challenging year for airlines. The widespread availability of vaccines and implementation of successful testing regimes will be key for the recovery in travel demand and share prices.

Airline industry continues to report deep losses and cash burn

Airline Financial Results

Number of airlines in sample	Regions	Q3 2019 EBIT margin[1]	Q3 2019 Net post-tax profit[2]	Q3 2020 EBIT margin[1]	Q3 2020 Net post-tax profit[2]
27	North America	11.7%	5,433	-43%	-10,975
29	Asia-Pacific	6.3%	485	-41%	-5,647
15	Europe	17.3%	6,076	-45%	-8,095
8	Latin America	11.2%	2	-94%	-1,772
4	Others	17.0%	220	-83%	-234
83	**Sample total**	**12.1%**	**12,216**	**-45%**	**-26,723**

[1]% of revenues [2]US$ million
Sources: The Airline Analyst, IATA

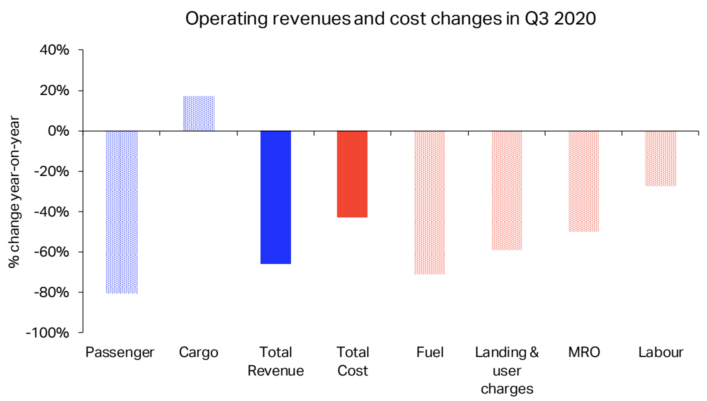
Airline Cash Flow[1]

Number of airlines in sample	Regions	Q3 2019 Net cash flow[2]	Q3 2019 Capex	Q3 2019 Free cash flow	Q3 2020 Net cash flow[2]	Q3 2020 Capex	Q3 2020 Free cash flow
13	North America	12.4%	8.8%	3.6%	-68.8%	20.6%	-89.4%
24	Asia-Pacific	9.7%	11.2%	-1.5%	-17.0%	4.6%	-21.5%
11	Europe	8.8%	9.6%	-0.8%	-61.0%	14.5%	-75.5%
6	Latin America	12.4%	8.5%	3.9%	-46.6%	14.3%	-60.9%
4	Others	16.6%	8.2%	8.4%	-46.6%	21.8%	-68.4%
58	**Sample total**	**10.8%**	**9.5%**	**1.3%**	**-51.4%**	**14.1%**	**-65.6%**

[1]% of revenues [2]From operating activities
Sources: The Airline Analyst, IATA

- Latest airline financial data for Q3 shows that airlines in all regions posted another quarter of net loss. While North America reported the largest net loss, Asia-Pacific airlines' net loss declined compared to the previous quarter amid the recovery in large domestic markets and the strong cargo revenues.
- The industry continued to burn cash in Q3. Net cash outflow from operating activities rose to 51% of revenues as the decline in operating costs was not enough to compensate for the revenue loss. Capital expenditures rose to 14% of revenues although airlines were deferring aircraft deliveries. Among all regions, Asia-Pacific was in a relatively better position in limiting free cash outflow.
- Looking forward, airlines will continue to suffer from subdued demand and turning cash positive will be the key target for the industry. We see a possibility of turning cash positive at aggregate level in Q4 but until then further support for survival from governments will be critical for survival.

Matching costs with lower revenues remains a challenge



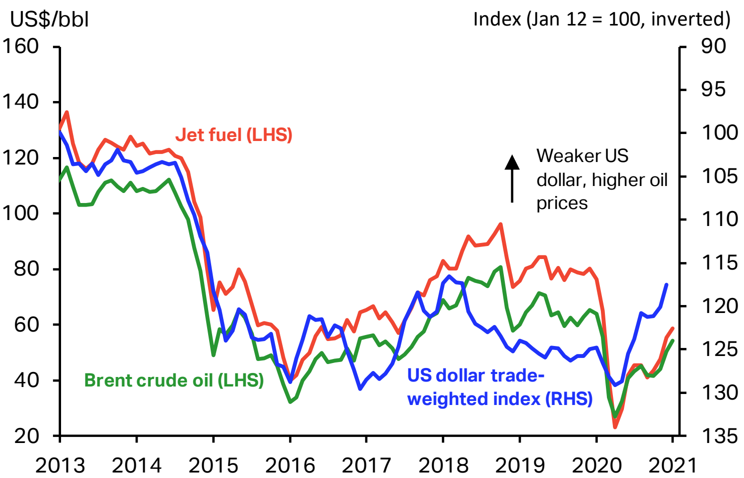
Airline Operating Costs Details

Number of airlines in sample	Regions	Operating Costs* Q3 2020 vs Q3 2019 (Year-on-year change)				
		Fuel	Employee	Maintenance & Engineering	Landing fees & user charges	Selling & distribution
28	North America	-70%	-21%	-37%	-46%	-81%
23	Asia Pacific	-77%	-29%	-54%	-69%	-72%
15	Europe	-69%	-36%	-60%	-59%	-73%
8	Latin America	-77%	-54%	-44%	-68%	-64%
4	Middle East	-83%	-44%	-31%	-72%	-81%
78	**Sample total**	**-71%**	**-27%**	**-50%**	**-59%**	**-76%**

*Sub categories are included in the sample if reported
Sources: The Airline Analyst, IATA

- Airlines in all regions posted sharp declines (-80%) in passenger revenues in Q3 2020 as the recovery in air travel demand was limited, and airlines aimed to stimulate demand by lowering fares.
- On the other hand, cargo revenues were strong since the economic activity rebounded quickly during post lock-down period. In addition to the rebound in cargo demand, cargo yields soared since the recovery in belly cargo capacity was limited and the conversion of passenger aircraft to cargo aircraft was not enough to compensate the loss in belly cargo capacity. As a result, cargo revenues in our sample of airlines improved by 17% year-on-year.
- Reducing operating costs was the main focus of airlines since the pandemic hit. However, the decline in operating costs (-43% in our sample) was much lower than the loss on the revenue side (-66% in our sample). Variable costs such as fuel and selling distribution declined in parallel with the loss in revenues. Also, airlines took initiatives to reduce their fixed or semi-fixed costs, e.g. employment costs were reduced by 27% in 3Q20 compared to 3Q19.

Oil and jet fuel price rose on U.S. fiscal stimulus expectations



Sources: Platts, Refinitiv Eikon Datastream, as of January 12th

- Oil and jet fuel price further strengthened in January amid hopes that the new U.S. administration would announce a stimulus package that would be supportive for oil demand. At the time of writing, Brent crude oil and the jet fuel price were US$56/bbl and US$61/bbl, respectively.
- Despite the recent strengthening in prices, lockdowns and border closures to contain the pandemic remain in place, raising concerns about the near-term oil demand. Taking into account weaker demand prospects in the near future, OPEC+ decided to delay a further easing of supply cuts in January. Although the recovery in oil demand is fragile in the near-term, a widespread vaccination and an acceleration in economic activity is expected to support demand in the second half of the year.

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