

AIRLINE BUSINESS CONFIDENCE INDEX

JANUARY 2017 SURVEY

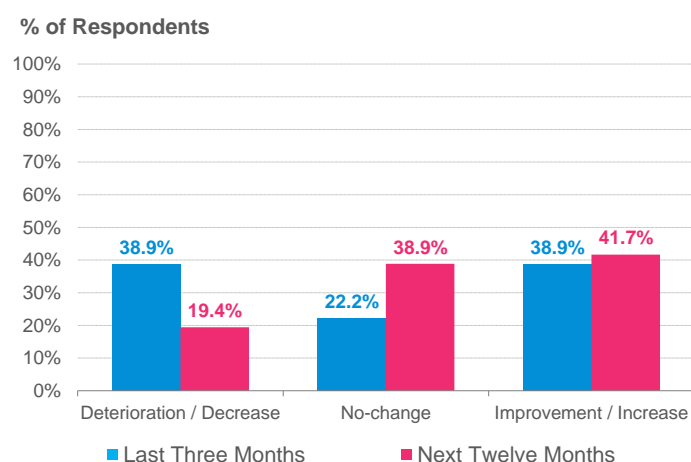
KEY POINTS

- ➔ When surveyed in early-January for our quarterly business confidence survey, airline CFOs and heads of cargo reported that profitability was unchanged in Q4 2016 compared to that in the same period of 2015;
- ➔ Industry heads were slightly more optimistic about the outlook for profits over the coming 12 months than they were in October's survey. But set against a more difficult operating backdrop, the latest survey results continue to indicate that momentum in the profitability cycle has weakened;
- ➔ The responses on the demand side were broadly consistent with the trend pick-up in passenger volumes towards the end of last year, as well as the stronger-than-expected 2016 peak season for air freight. Our participants remain very positive about the outlook for passenger (especially) and cargo demand over the 12 months ahead;
- ➔ 31% of respondents reported an annual increase in operating costs in Q4 2016 (the highest proportion since July 2014). With a rebalancing in the oil market slowly taking place, and some signs of emerging labor cost pressures, the forward-looking weighted-average score remained above the 50-mark for just the second time in the past 10 surveys, pointing to a further increase in input costs over the coming year;
- ➔ Nearly two-thirds of respondents reported lower passenger yields in Q4 2016 compared to the same period in 2015, underlining the challenging profitability environment. On the freight side, ongoing concerns about future capacity growth, particularly related to belly-hold capacity from additions to the passenger fleet, mean that respondents remain negative on the prospects for freight yield over the coming 12 months;
- ➔ Airline employment activity increased for the eighth consecutive quarter in Q4 2016. Half of the respondents expect to keep employment levels unchanged at current levels over the next 12 months.

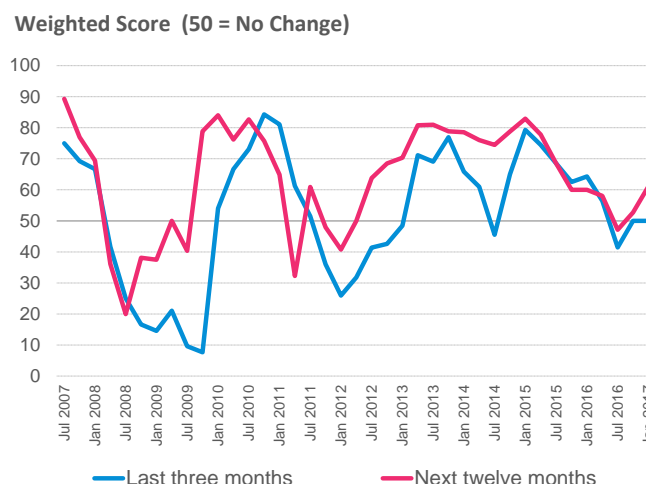
PROFITABILITY OUTLOOK

How has profitability changed? How do you expect it to change over the next twelve months?

a) January 2017 survey



b) Compared to previous surveys



- ➔ When surveyed in early-January, airline CFOs and heads of cargo reported that profitability was unchanged in Q4 2016 compared to the same period in 2015. As was the case in the previous quarter's survey, the responses were evenly balanced, with 39% of respondents reporting an increase in profits and 39% reporting a decrease. The latest survey results reflect an operating environment that has become more challenging since mid-2016, with fuel prices trending higher but yields continuing to trend downwards.

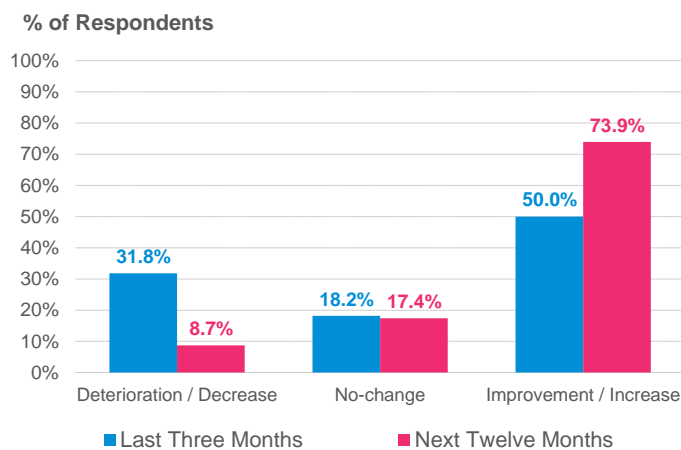
- ➔ The weighted-average score for profitability over the next 12 months increased again in the January survey, taking it to a six-quarter high. The majority of respondents (42%) expect profits to increase over the next 12 months – the first time this has been the case since the April 2016 survey. But this proportion is some way below the 60-70% level that was the norm a few years ago, and momentum in the profitability cycle has weakened.

DEMAND GROWTH

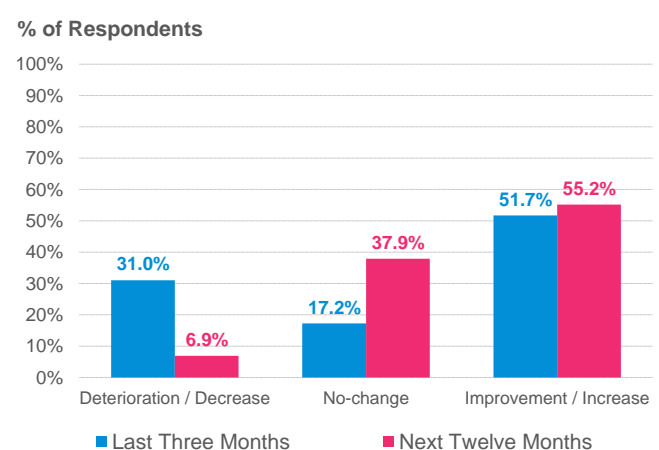
- ➔ Half of the respondents reported a year-on-year increase in passenger traffic during Q4 2016. This ties in with a pick-up in the upward trend in seasonally-adjusted passenger traffic in the latest monthly data from the period. However, ongoing disruption and uncertainty in certain markets, particularly Turkey, was noted by a number of participants, and the backward-looking weighted-average score dipped to its lowest level in four years.
- ➔ Given the recent pick-up in the economic cycle, the majority (74%) of respondents expect passenger volumes to increase over the next 12 months – the highest proportion since October 2013. All told, the forward-looking weighted-average score remained stable at a high level, broadly in line with its five-year average.
- ➔ In keeping with signs of a strong 2016 peak season for air freight, 52% of respondents reported an annual increase in cargo volumes in the final quarter of last year. The wider global trade backdrop remains weak, but the weighted-average score for volumes over the next 12 months increased again in the January survey.

Recent and expected change in traffic volumes

a) Passenger



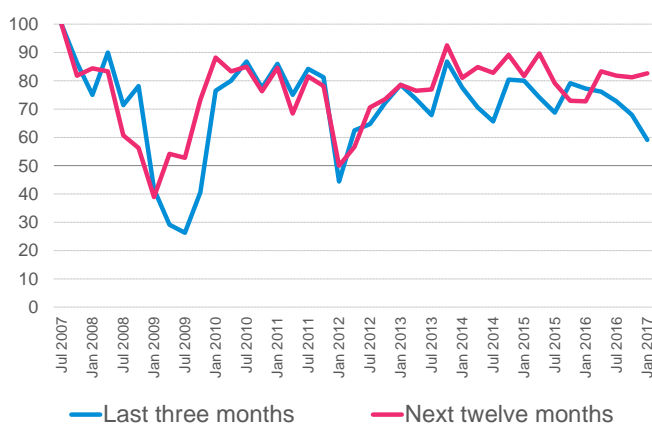
b) Cargo



Compared to previous surveys

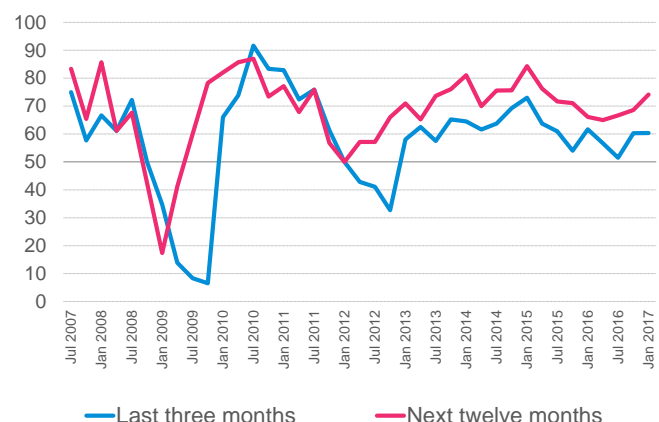
a) Passenger

Weighted Score (50 = No Change)



b) Cargo

Weighted Score (50 = No Change)

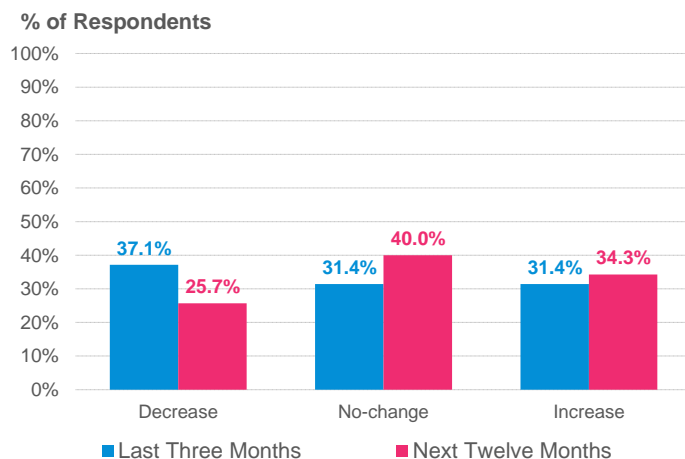


INPUT COSTS

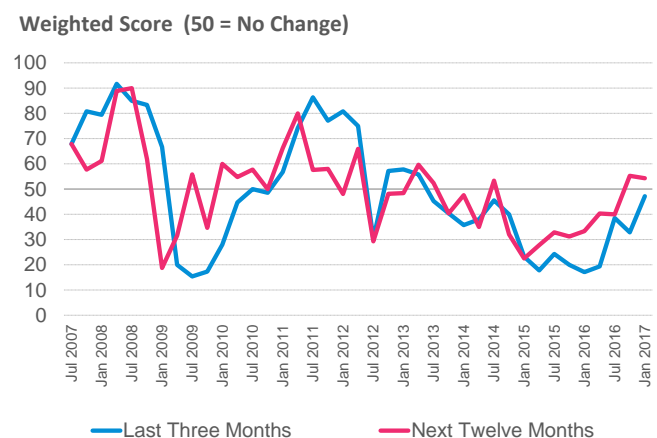
- ➔ Oil prices increased over the course of 2016 and are currently around twice the 12-year low level reached in January 2016. Fuel accounts for just under one-third of total industry costs, and 31% of respondents reported an annual increase in input costs in Q4 2016 – the highest proportion since July 2014. But different hedging practices within the industry, as well as differing movements in exchange rates against the US dollar in which oil prices tend to be quoted, mean that there was a wide range in responses amongst our survey participants.
- ➔ With a rebalancing in the oil market slowly taking place, and some signs of emerging labor cost pressures, 34% of respondents expect input costs to increase over the coming 12 months. Indeed, the forward-looking weighted-average score remained above the 50-mark for only the second time in the past 10 surveys.

How have your unit input costs changed? How do you expect them to change over the next twelve months?

a) January 2017 survey



b) Compared to previous surveys

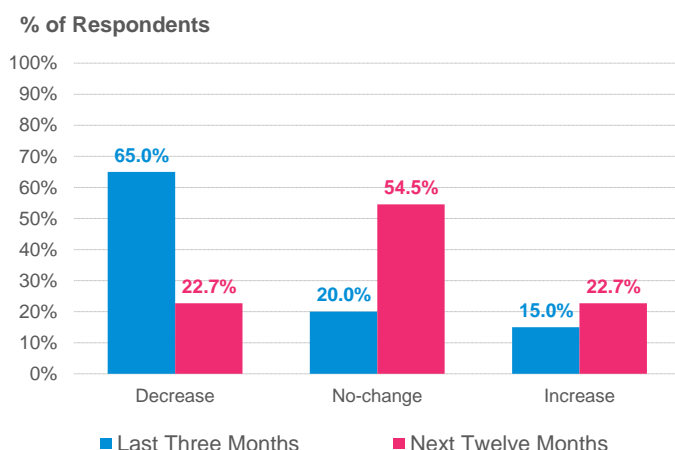


YIELD ENVIRONMENT

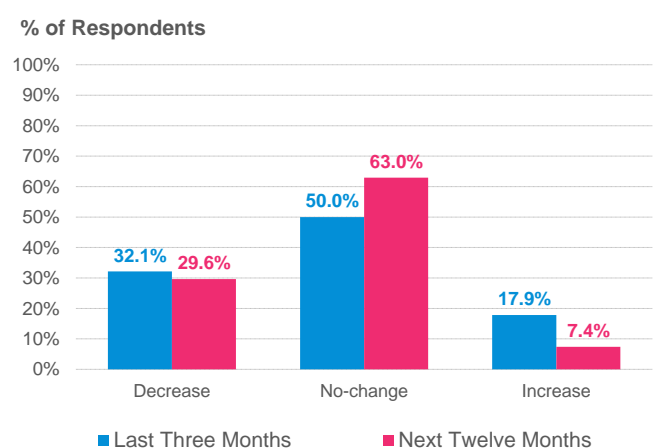
- ➔ Nearly two-thirds of respondents reported lower passenger yields in Q4 2016 compared to the same period in 2015. 23% of respondents expect yields to rise over the year ahead – the highest proportion since January 2016, reflecting optimism that airlines can reverse the trend in unit revenues in certain key markets. But more than three-quarters of respondents expect yields to either remain unchanged or to fall further in the year ahead.
- ➔ With the stronger-than-expected 2016 peak season boosting demand on certain routes, 18% of respondents reported an annual increase in freight yields in Q4 2016 – the highest share in two years. But ongoing concerns about future growth in industry-wide capacity continue to weigh on expectations for cargo yields. Over 90% of respondents expect cargo yields to remain unchanged or to fall further over the year ahead.

Recent and expected change in yields

a) Passenger



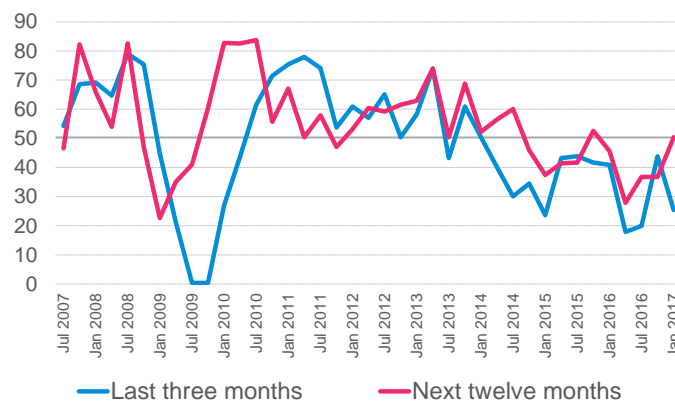
b) Cargo



Compared to previous surveys

a) Passenger

Weighted Score (50 = No Change)



b) Cargo

Weighted Score (50 = No Change)



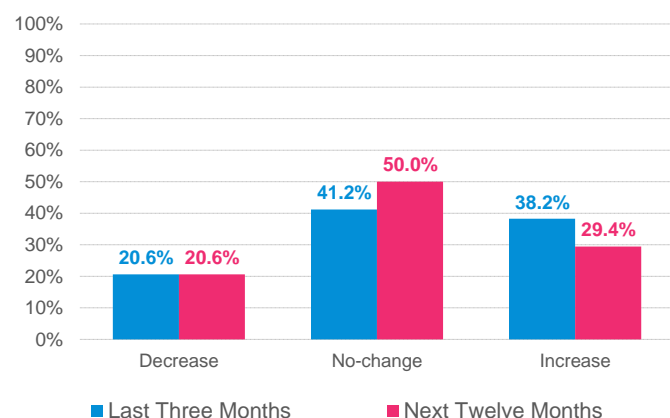
EMPLOYMENT

- ➔ 38% of survey respondents reported an increase in employment levels in Q4 2016 compared to the same period in 2015. The weighted-average score for employment activity over the past three months eased slightly from that in October's survey, but it has now been above the 50-mark for the past two years.
- ➔ Half of the respondents reported that they expect to keep employment levels unchanged over the next 12 months. Having dipped below the 50-mark in the October survey, the weighted-average score for employment levels over the next twelve months increased slightly, taking it back into expansionary territory.

How has your employment level changed? How do you expect it to change over the next twelve months?

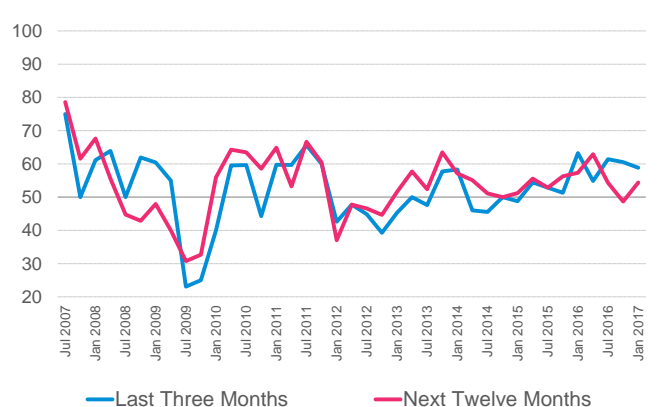
a) January 2017 survey

% of Respondents



b) Compared to previous surveys

Weighted Score (50 = No Change)



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