JANUARY 2019 SURVEY

AIRLINE BUSINESS CONFIDENCE INDEX

KEY POINTS

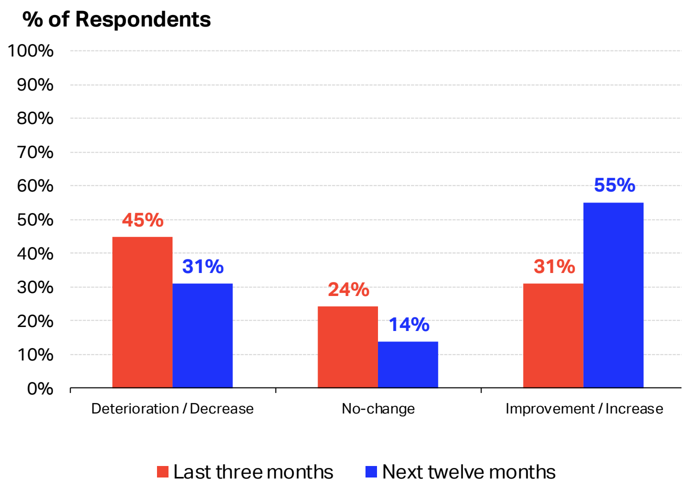
- The January 2019 survey of airline CFOs and Heads of Cargo indicates that the challenging business environment continued in Q4 2018, with 45% of respondents reporting a decrease in profits compared with the same period a year ago. In the next twelve months however, the majority (55%) expect to see an improvement in profitability, indicating that confidence has risen since the previous survey in October.
- Passenger and freight demand growth has been strong for most respondents in the past three months and is expected to remain so in the year ahead, despite risks of slowing global economic growth and concerns over a possible trade war.
- 62% of survey respondents saw an increase in input costs in Q4 2018 compared to Q4 2017, citing fuel prices and unfavourable foreign exchange movements as key factors. In the coming year, 48% of respondents still expect costs to increase, though this share fell markedly from 63% in October, in response to the sharp fall in fuel prices.
- Yield developments have been mixed for both pax & freight, with only slightly more than 1/3 of respondents seeing an increase in yields in Q4. Looking ahead, only 33% of those surveyed expect passenger yields to increase over the year ahead while for freight, the share is even lower, at just 20%.
- The industry employment outlook remains very positive; 55% of respondents reported an increase in their labour force in Q4 2018, and only 7% expect to decrease their work force next year, a record low since the launch of the survey in 2006.

PROFITABILITY OUTLOOK

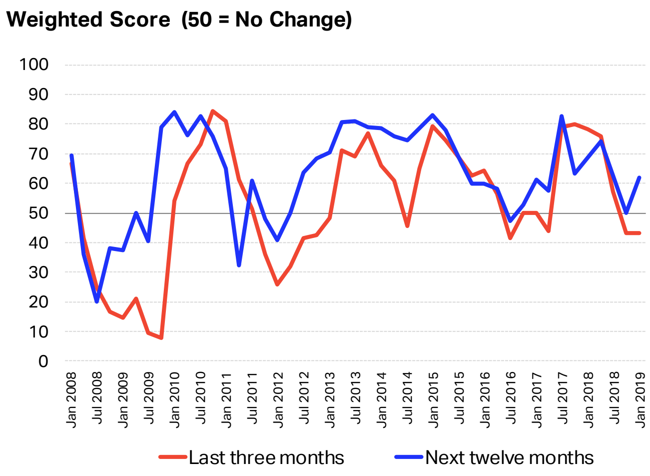
- The results of our latest survey of airline CFOs and Heads of Cargo suggest that the squeeze on profitability, evident through the first three quarters of 2018, continued in Q4. 45% of respondents saw a decrease in their profitability in Q4 2018 compared with the same period in 2017. Responses suggest the profit squeeze is primarily coming from cost pressures and, in some cases, tentative signs of faltering demand growth.
- However, the proportion of respondents who believe that profits will improve over the next year bounced back in the latest survey, to 55%, a strong 15 percentage points above the Q3 outcome. Respondents mentioned improving business conditions and better management as sources of optimism.

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

a) January 2019 survey



b) Compared to previous surveys

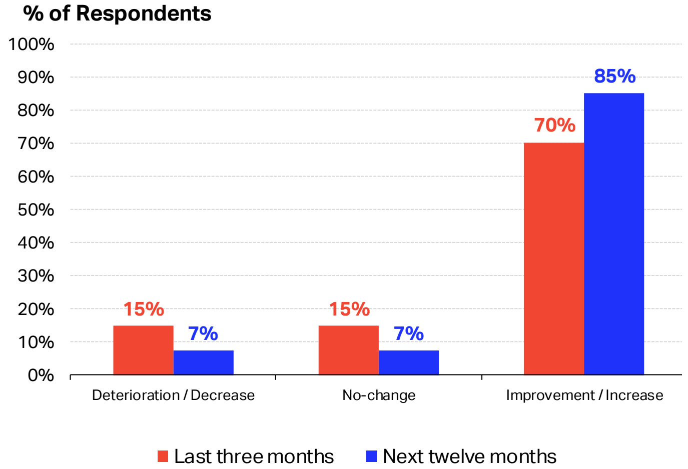


DEMAND GROWTH

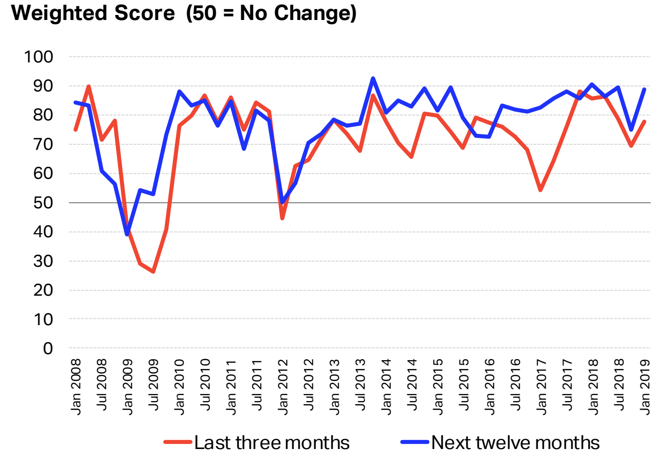
- On the passenger side, the results from the January survey point to a rebound in demand growth in Q4, with 70% of respondents reporting increasing passenger volumes compared to a year ago. This was up from a short-lived dip to 65% last quarter. Consequently, the weighted score trended back to 78, slightly above the 5-year average.
- Turning to the next twelve months, optimism has returned here as well, with 85% expecting a pick-up in demand growth over the year ahead. The 14% of surveyed individuals expecting either a decrease or no change in year-on-year passenger demand growth, compares to more than 40% in October 2018. The weighted score therefore trended upwards to 89, unwinding the loss of confidence observed in Q2 and Q3. Lower oil prices and expectations of a favourable global economic outlook have supported industry confidence.

Passenger

a) Recent and expected change in traffic volumes



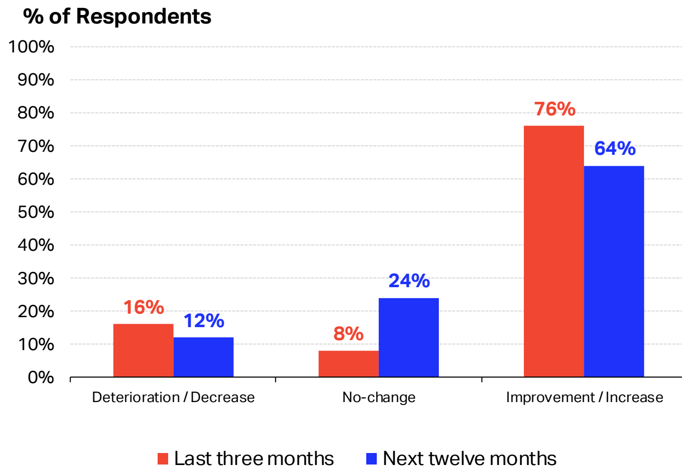
b) Compared to previous surveys



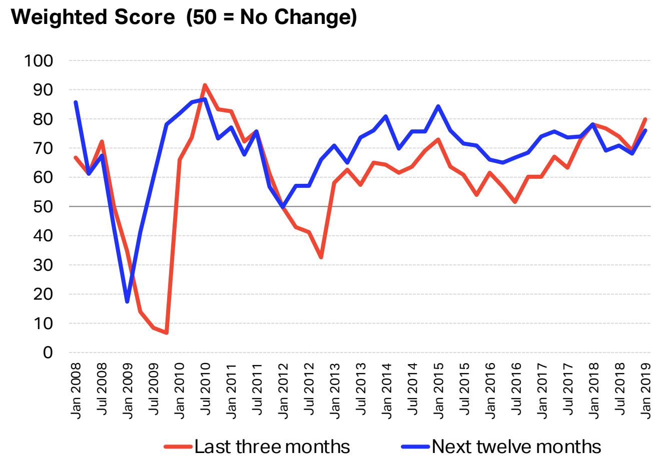
- As for air freight demand, 76% of respondents registered an increase in cargo volumes in Q4 2018, up from 58% in Q3. This represents the highest proportion since January 2011. Even though 16% of respondents still reported a decrease in demand in Q4 (down from 19% in Q3), the weighted average score also reached its highest level in the past eight years.
- Looking ahead, the outlook for the air cargo segment is not quite as bright as that expected on the passenger side, with 64% expecting stronger demand over the next year and a further 24% expecting similar conditions to now. The weighted average score also improved this quarter, to 76, back above the 5-year average. Despite the positive survey results, respondents remain particularly wary of possible risks of relating to international trade tensions.

Cargo

a) Recent and expected change in traffic volumes



b) Compared to previous surveys

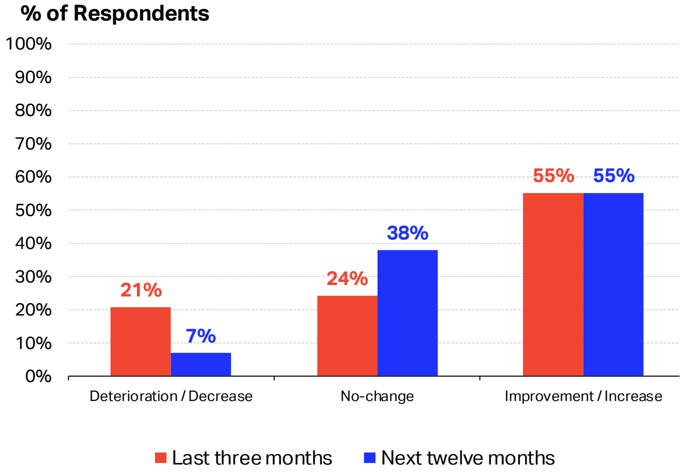


EMPLOYMENT

- The majority (55%) of survey respondents cited an increase in the size of their workforce in Q4 2018 compared with the same period a year ago, the highest proportion in more than a decade (since July 2007). This is the fourth consecutive quarterly increase in the proportion and as a result the backward-looking weighted score continued trending upwards, reaching a score of 67 – a level not seen since the global financial crisis.
- Importantly, the positive employment story is expected to continue over the year ahead, with the same proportion of respondents (55%) planning to increase their workforce further over the coming 12 months. Just 7% expect to shrink the size of their workforce – a record low outcome since the launch of the Business Confidence Survey in 2006. Consequently, the forward-looking weighted score lifted further, to 74.

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

a) January 2019 survey



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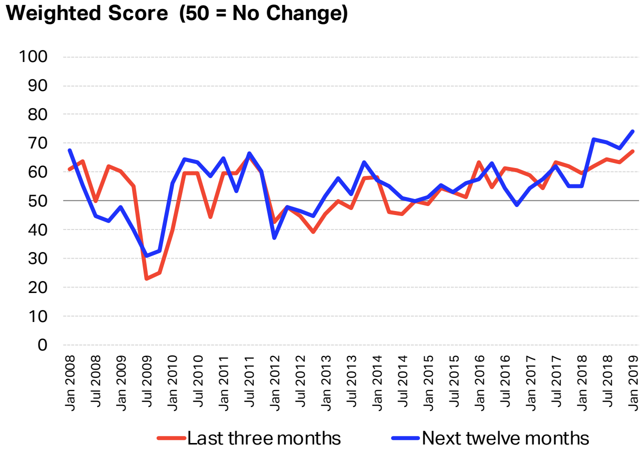
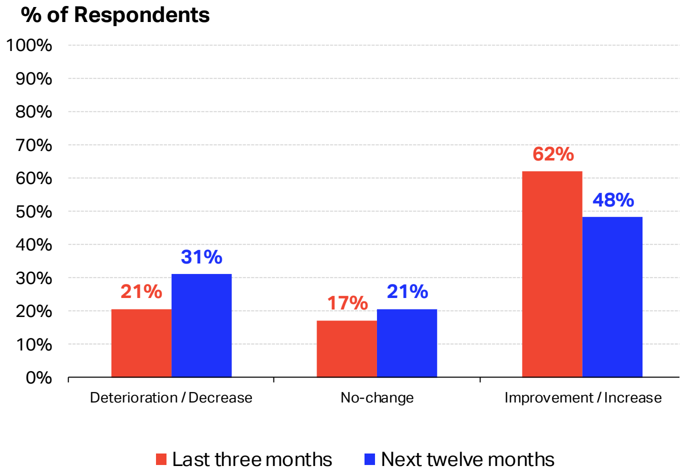


INPUT COSTS

- 62% of surveyed individuals noted an increase in input costs over the last three months of 2018, down from 73% in October. In parallel, the backward-looking weighted-average score eased a little further on this occasion, from its high level of 83 in July 2018, currently at 71. Respondents pointed to higher fuel prices and wages, as well as unfavourable hedging and exchange rate effects.
- The outlook over the twelve months to come is more upbeat. 31 % of respondents expect input costs to be lower over the year ahead, double the proportion of just three months ago and driven by lower fuel costs and efficiency gains. Of the 48% of respondents still expecting costs to increase, most point to economy-wide inflationary pressures and some also noted unfavourable hedging positions.

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

a) January 2019 survey



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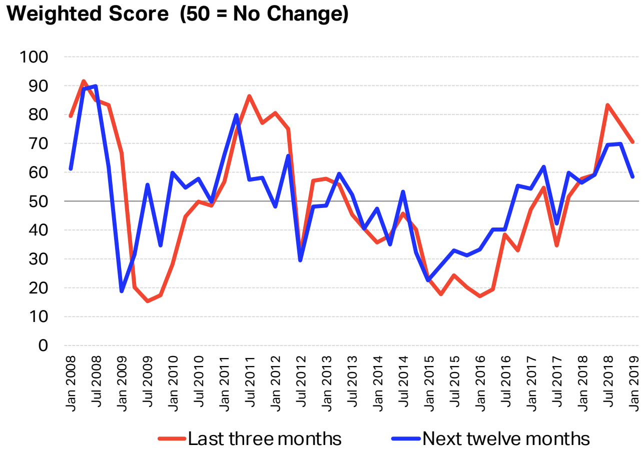
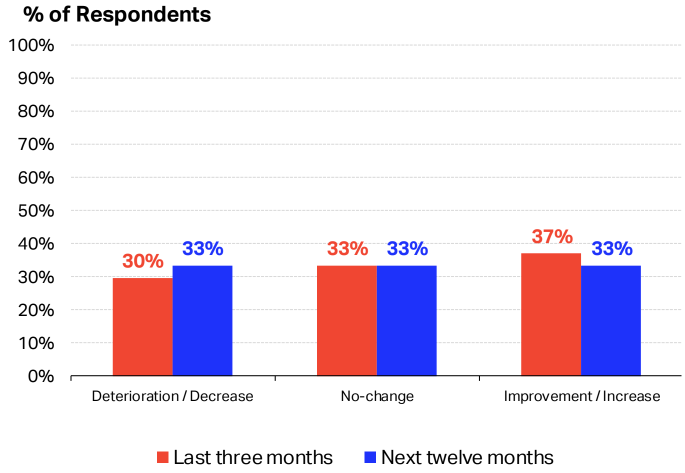


YIELD ENVIRONMENT

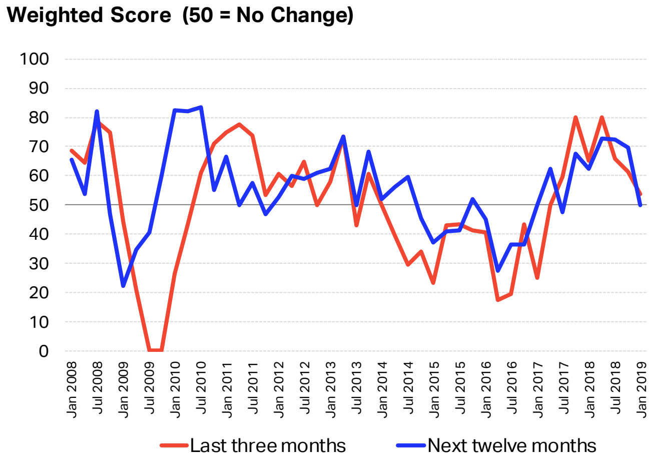
- For the passenger segment, yield outcomes in the latest survey were mixed. 37% of respondents reported higher yields in Q4 2018 compared to Q4 2017 – down from 50% in last quarter's survey – while a further 30% indicated that yields had declined over the same period. Looking to expectations for yield developments over the year ahead, the survey results were evenly spread; exactly 1/3 of respondents expect yields to be higher, lower and unchanged, respectively. Both the backward and forward-looking weighted average measures eased slightly this quarter, continuing the broad trends observed over the past year.

Passenger

a) Recent and expected change in yields



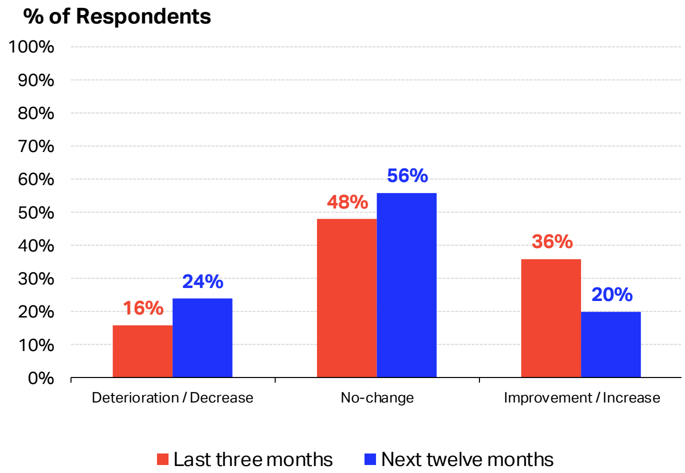
b) Compared to previous surveys



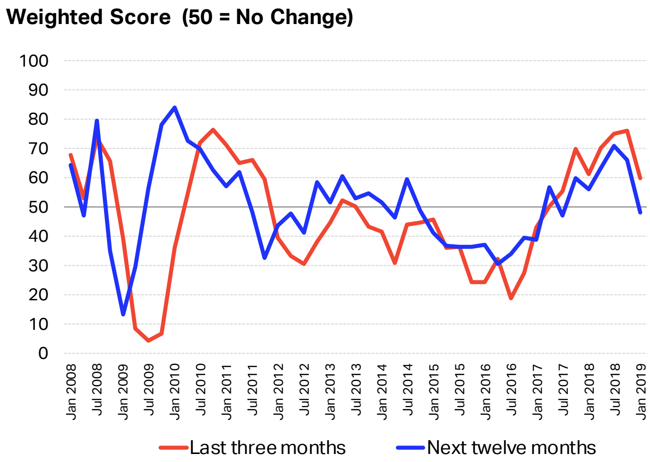
- Turning to freight yields, 36% of surveyed individuals reported an increase in cargo yield in Q4 2018 vs Q4 2017. Although this is down from 60% for Q3, it remains above the 5-year average of 25%. For the year ahead, the share of respondents expecting higher yields fell to 20% (down from its recent peak of 56% in October 2018) with the majority (56%) expecting yields will be unchanged over the next twelve months.
- With most respondents noting higher input costs in Q4 but a much smaller proportion indicating higher yields over the same period, the squeeze on profits reported earlier in unsurprising. A number of respondents pointed to more intense competition in their key markets as a key contributing factor.

Cargo

a) Recent and expected change in yields



b) Compared to previous surveys



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