January 2020 SURVEY

AIRLINE BUSINESS CONFIDENCE INDEX

KEY POINTS

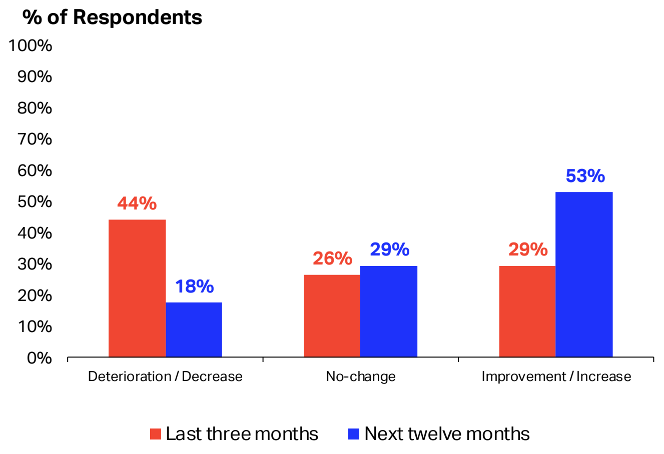
- Our January 2020 survey of airline CFOs and Heads of Cargo shows that both demand and profitability for airlines weakened in Q4 2019 but expectations for the future in terms of demand and profitability improved compared to the previous survey.
- Passenger and cargo yields improved in the last quarter of the year and looking forward they are expected to increase further, underpinned by an improvement in demand conditions. On the cost side, lower fuel prices were supportive in Q4, and costs are expected to be broadly steady for the coming year. Respondents identified inflation, currency depreciation and volatility in fuel prices as key risks to the cost outlook.
- Profits in the last quarter of 2019 were weaker than the previous year but for the next twelve months more than half of respondents expect profitability to improve. Airline employment increased during Q4 2019 compared to a year ago and the industry became slightly more optimistic about employment for the year ahead, with almost 80% of respondents expecting either no change or to increase the level of employment.

PROFITABILITY OUTLOOK

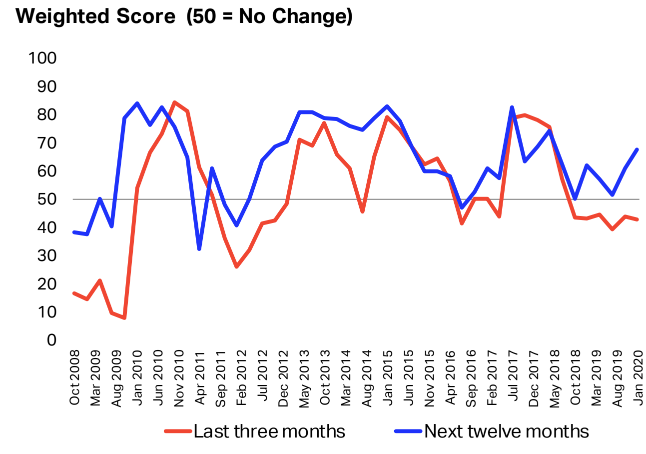
- The results of our latest survey of airline CFOs and Heads of Cargo, conducted in mid-January, showed that profitability remained under pressure during the last quarter of 2019. The weighted index remained in contractionary territory (below the 50-mark) and the share of respondents reporting improved profitability declined by a sizeable 9.6pp to 29% compared to the previous survey. However, the share of respondents reporting a decline in their profitability (44%) contracted, as well. Higher yields supported by stronger passenger demand in some markets, along with low oil prices were the main factors identified as being supportive for profitability. On the other hand, trade tensions and weaker economic growth continued to put downward pressure on profitability in some regions.
- Forward looking profitability expectations continue to strengthen with more than half (53%) of our respondents expecting profits to improve, driven by strategic capacity and route management decisions together with better yields. Moreover, only 18% of respondents expect profits to be lower in the year ahead (c.9pp lower than the past survey) mainly on concerns of a further slowing in economic activity. As a result, the weighted average forward-looking score jumped up sharply this quarter.

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

a) January 2020 survey



b) Compared to previous surveys

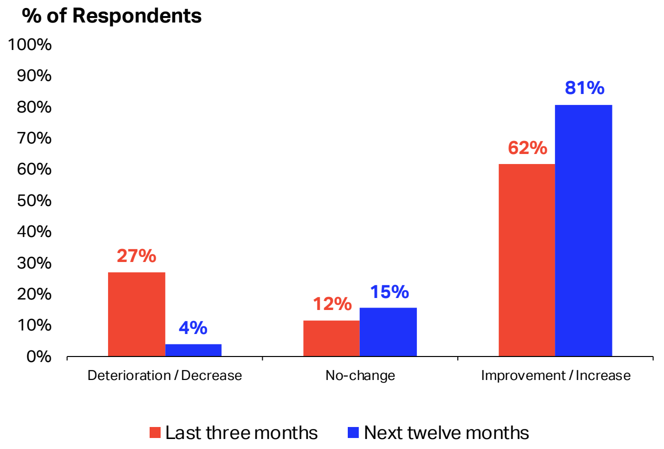


DEMAND GROWTH

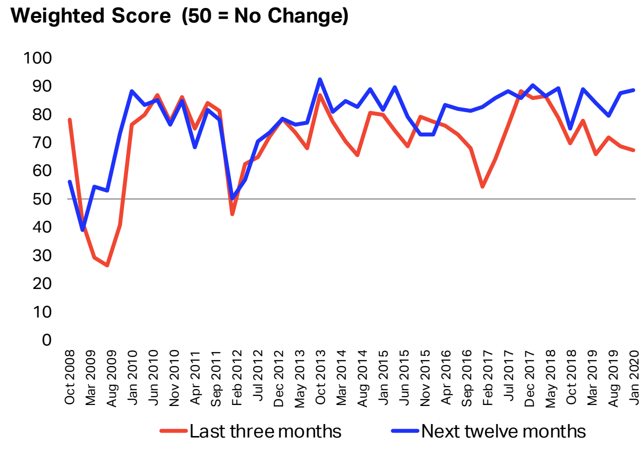
- The January survey shows that passenger demand moderated in Q4 2019. While 62% of respondents experienced an increase in year-on-year demand (up from 59% in last quarter's survey). The ratio of respondents reporting a deterioration in pax volumes also increased, to 27% from 22% previously, slower economic growth and the Max groundings impacted some airlines. Overall, the weighted backward-looking score declined modestly, continuing the recent downward trend.
- For the next twelve months, the ratio of respondents expecting an improvement in passenger volumes stabilized at 81%, while the ratio expecting a reduction in demand declined further to just 4%. Although several respondents stated concerns regarding the slowdown in economic activity and trade tensions, there are airlines that are expecting an increase in passenger numbers with the support of new routes and marketing campaigns over the next 12 months. Overall, the forward-looking weighted-average index inched up and the score remains elevated at 89.

Passenger

a) Recent and expected change in traffic volumes



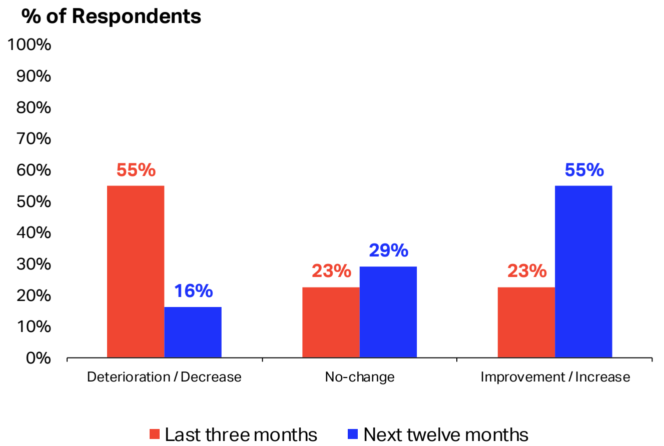
b) Compared to previous surveys



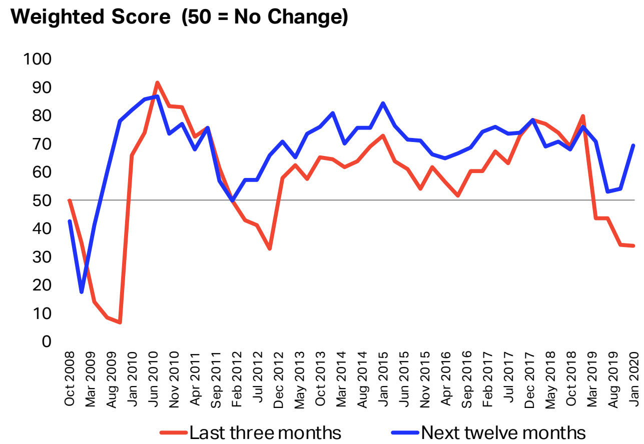
- For freight, more than half (55%) of the respondents reported a decrease in cargo volumes in Q4 2019, the largest share since the October 2012 survey. On the other hand, the share of respondents reporting an improvement in their cargo business increased from 18% to 23%. As a result, the weighted score remained stable at 34, the lowest reading over the last seven years as trade tensions and slowing global economic activity continued to pressure air cargo volumes.
- Looking forward, there is a sharp improvement in expectations for freight volumes with the easing of trade tensions. The percentage of respondents expecting higher freight volumes in the coming period rose to 55%, from 39% in Q4. Moreover, only 16% of respondents expect a further deterioration in freight volumes compared to 32% of the respondents previously. As a result, the weighted score jumped to 69.

Cargo

a) Recent and expected change in traffic volumes



b) Compared to previous surveys

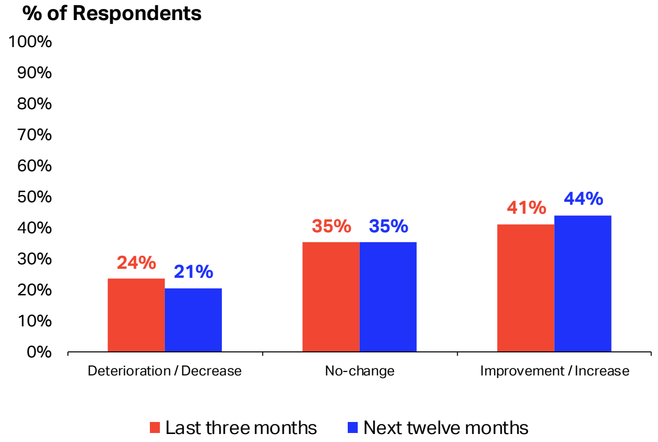


EMPLOYMENT

- In the January survey, 41% of respondents indicated an increase in employment which is c. 9pp higher compared to the October survey. However, the percentage of respondents that noted a decline in their workforce also increased – by 11pp to 24%. As a result, the weighted backward-looking score eased to 58.8.
- Looking forward, the industry employment outlook remains softer compared to first half of 2019 despite the rise of survey participants who expect higher employment in the next 12 months (44%, up from 34% recorded in the last quarter's survey). The percentage expecting to reduce employment also increased on this occasion, from 17% to 21%. The weighted forward-looking score remains relatively low at 62.0.

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

a) January 2020 survey



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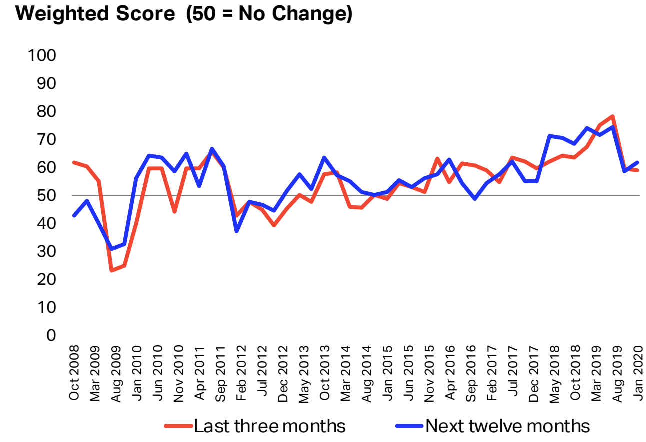
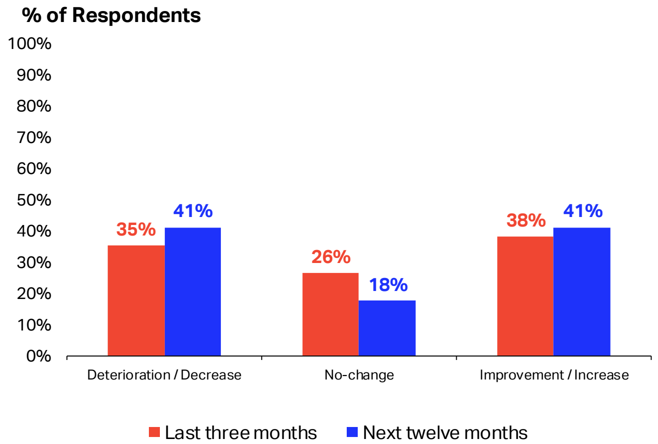


INPUT COSTS

- A higher share of respondents (35% vs 20% in October survey) experienced a decline in input costs over the past three months with the support of lower oil prices and specific measures taken to limit cost increases. At the same time, the share of respondents reporting higher unit costs continued to decline (38% vs 44% in October survey). As a result, the weighted average backward-looking score declined. While aircraft groundings, currency depreciation and inflation were reported as the main reasons behind higher unit costs, a number of airlines indicated that they have implemented various cost optimization projects.
- Expectations for the next 12 months, point to input costs being largely unchanged. However, this masks considerable difference in respondent views, with 41% expecting costs to increase and the same proportion to see a decrease. Both of these are higher than we observed in last quarter's survey. Overall, a rise in airport charges, inflation, currency depreciation and volatility in fuel prices are viewed as the main challenges for the industry to manage costs in the coming year.

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

a) January 2020 survey



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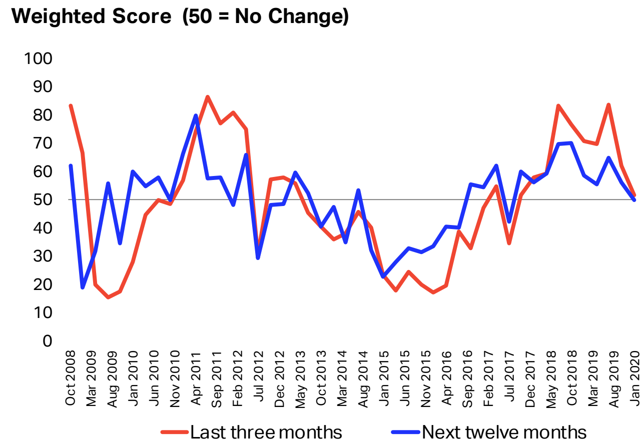
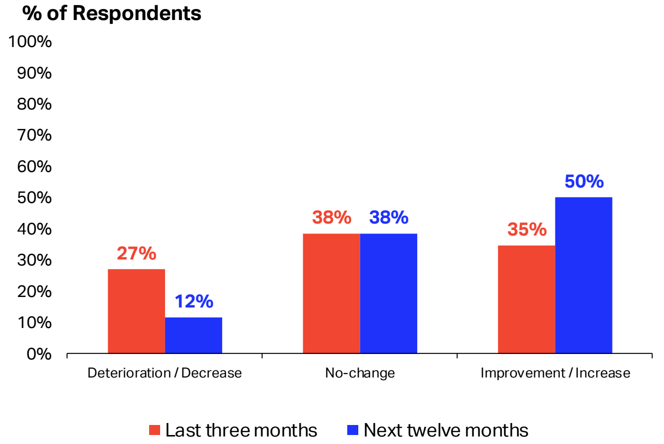


YIELD ENVIRONMENT

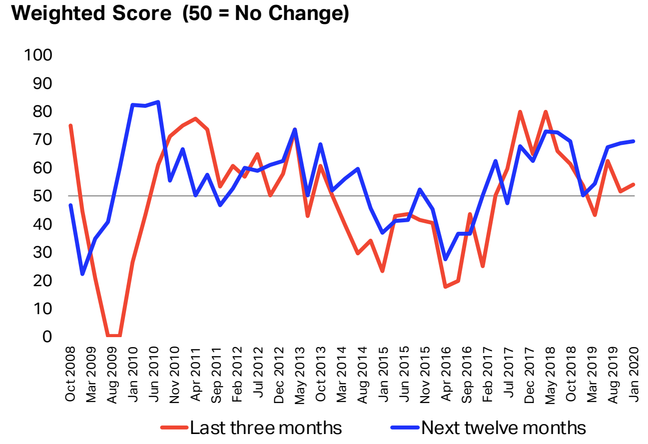
- Passenger yields for the past three months improved slightly in the January survey (the weighted index increased from 52.0 in October, to 54.0) as respondents reported better demand conditions in key markets supported yields. Both the share of respondents reporting improvement and deterioration in yields eased in the past three months.
- Looking ahead, 89% of respondents expect passenger yields to remain steady or improve over the year ahead. The share of respondents expecting a decline eased to 12%. As a result, the weighted average index maintained its modest upward trend on this occasion. A number of airlines that expect passenger yields to increase over the coming year point to improved demand conditions as the main driver.

Passenger

a) Recent and expected change in yields



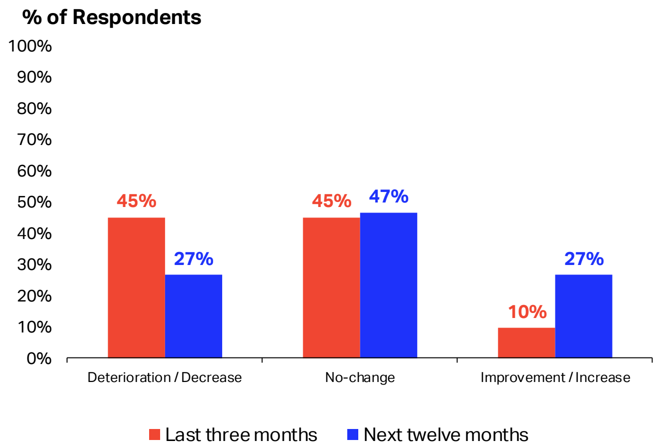
b) Compared to previous surveys



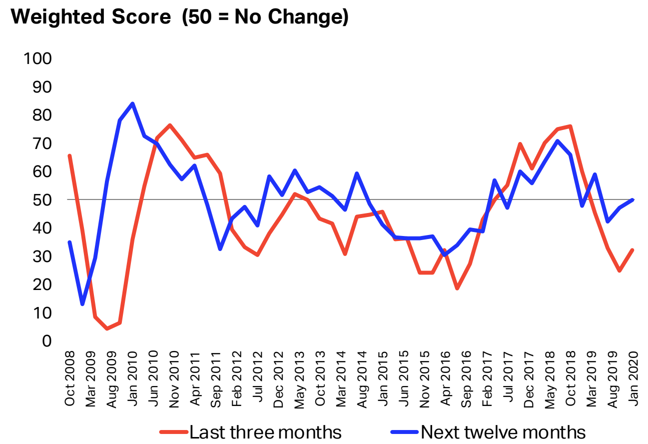
- Cargo yields remained under pressure in Q4 2019 despite the slight improvement in the weighted score of the index (index remains below the 50-level). The share of respondents reporting higher yields rose to 10%, while the share of respondents indicating deteriorating yields declined by 13 ppt to 45%.
- Forward expectations also picked up compared to the previous quarter, reaching the 50-mark. The share of respondents expecting higher yields over the next 12 months rose to 27%, with a similar proportion now expecting yields to deteriorate over the year ahead (down from 30% in the previous survey).

Cargo

a) Recent and expected change in yields



b) Compared to previous surveys



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