

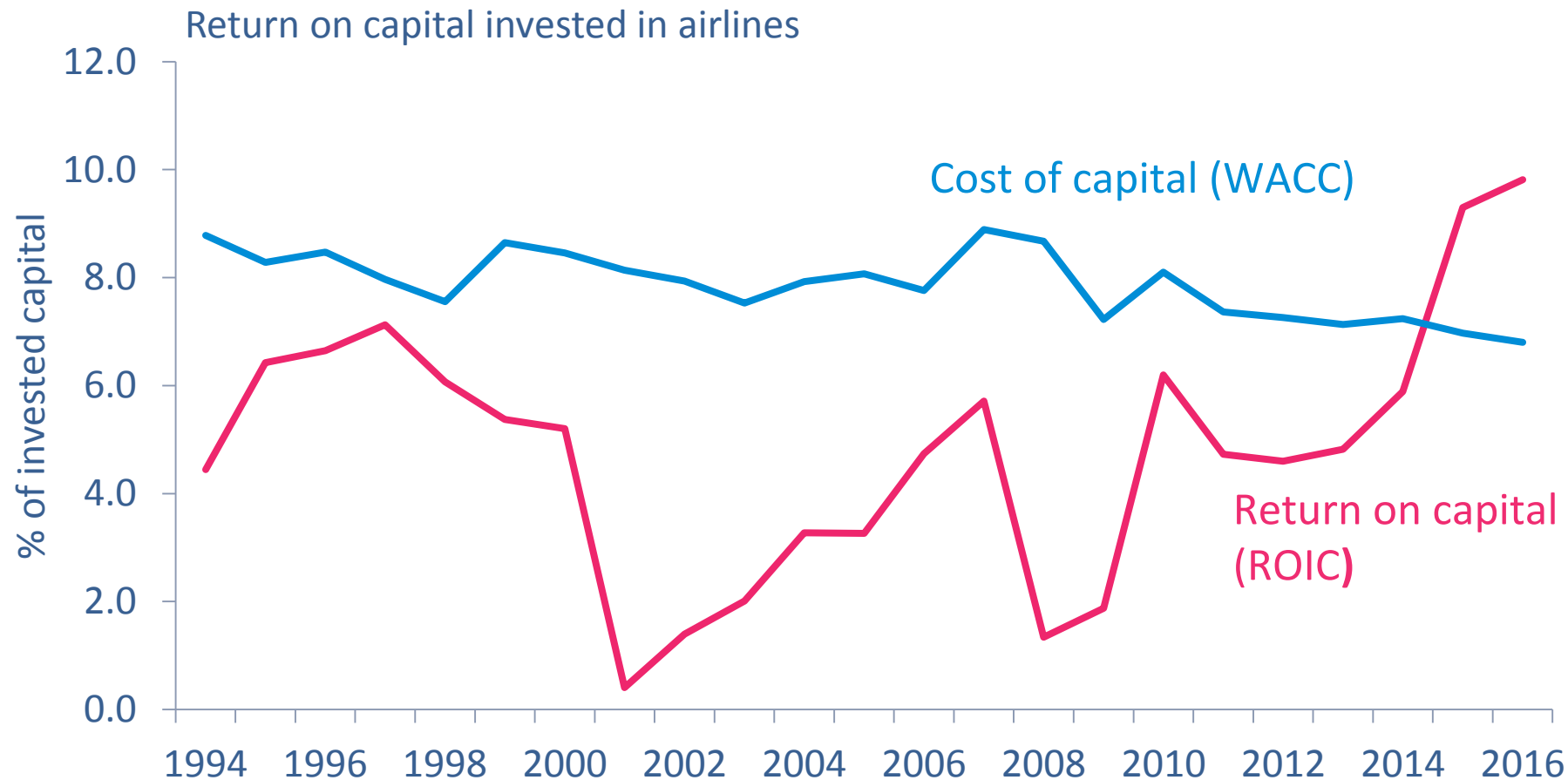


Industry Financial Health – narrowly based and facing challenges

September 2016

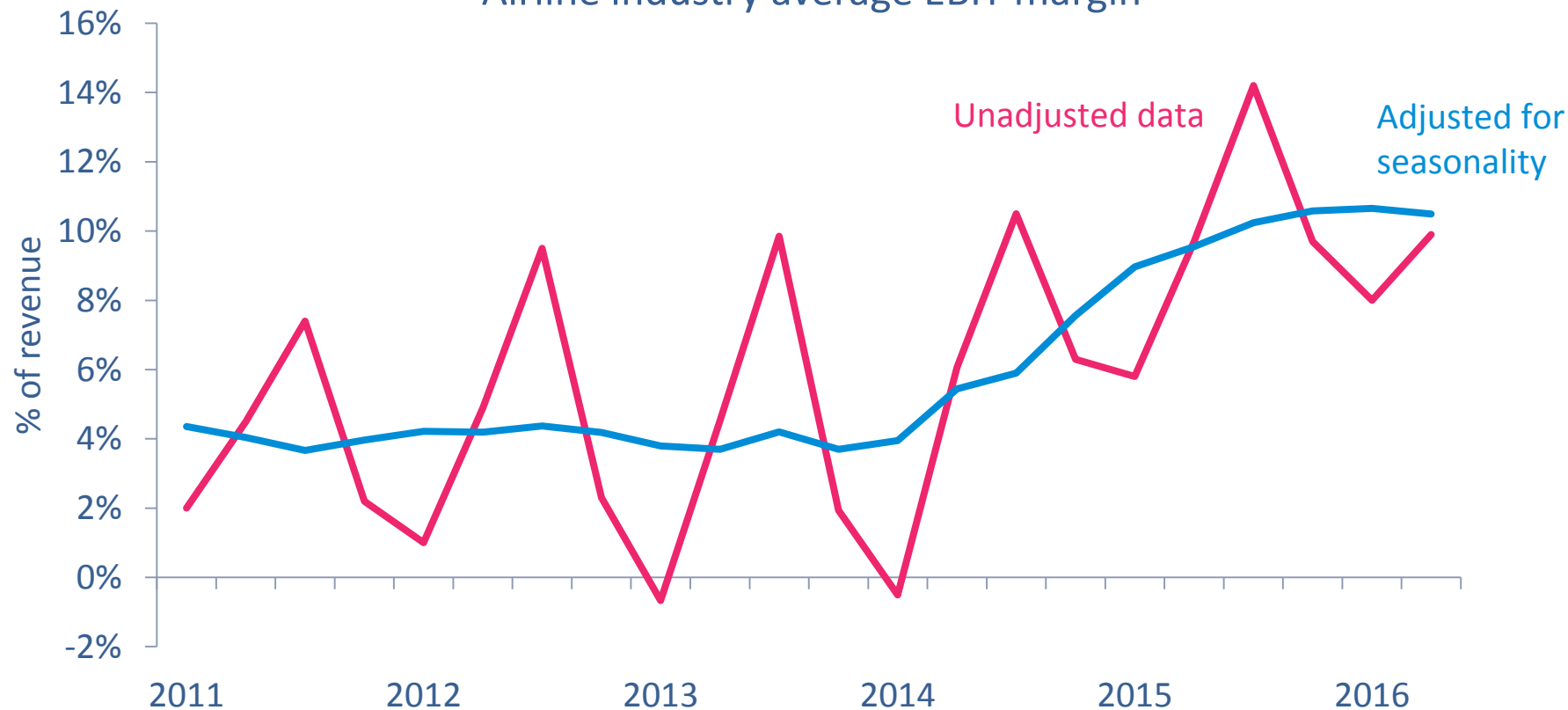
Brian Pearce
Chief Economist, IATA

2016 another year of above WACC returns

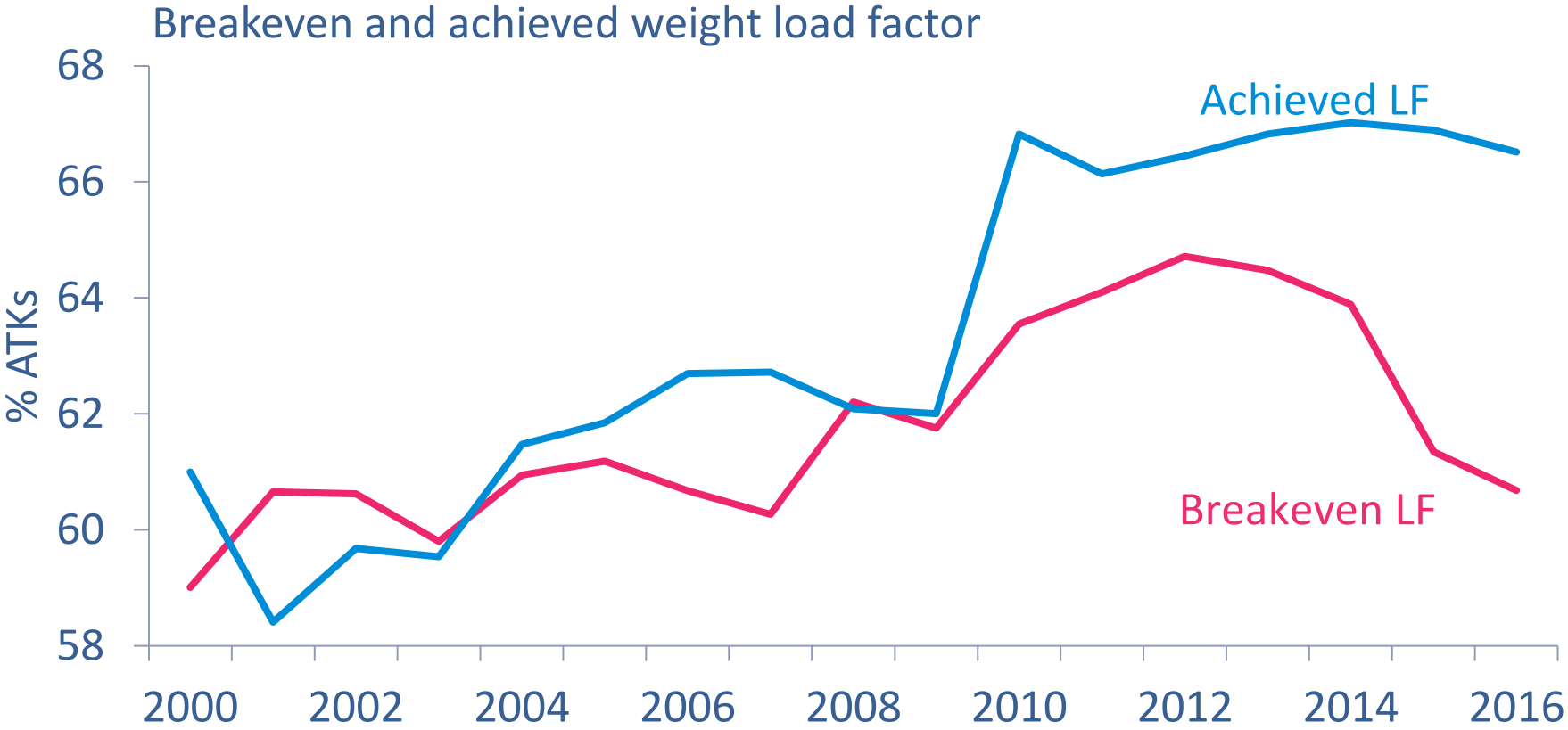


Profits cycle now showing signs of peaking

Airline industry average EBIT margin

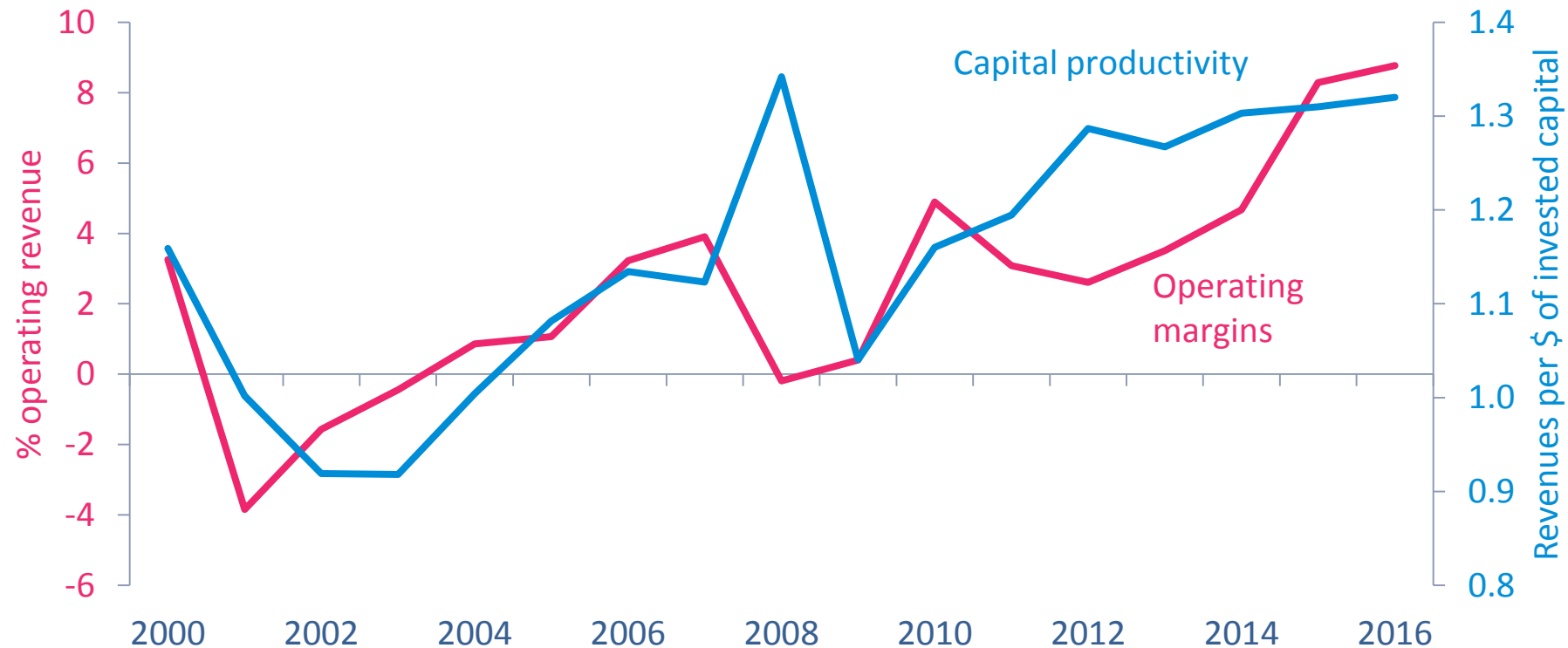


Widening asset utilization gap driving returns



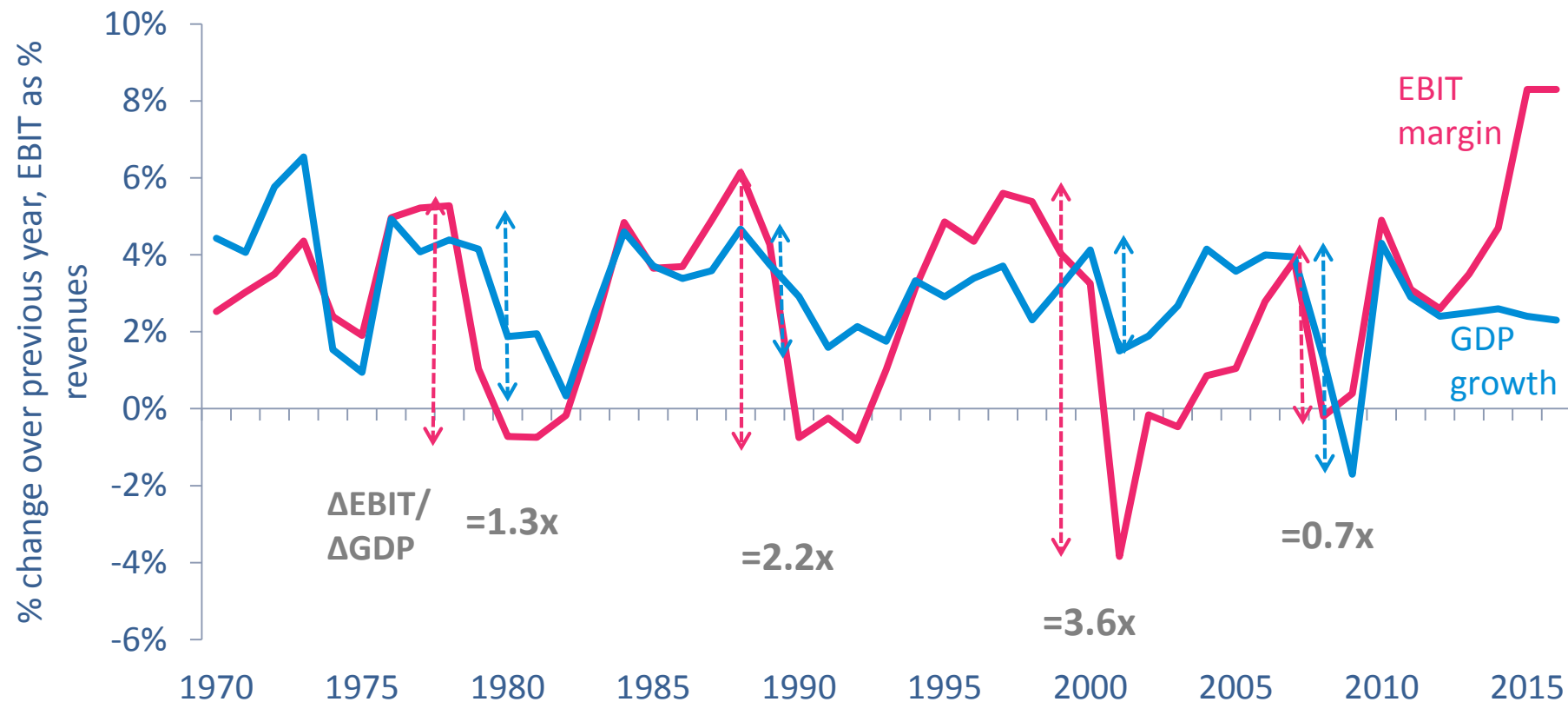
Better capital productivity also driving returns

Capital productivity and operating margins



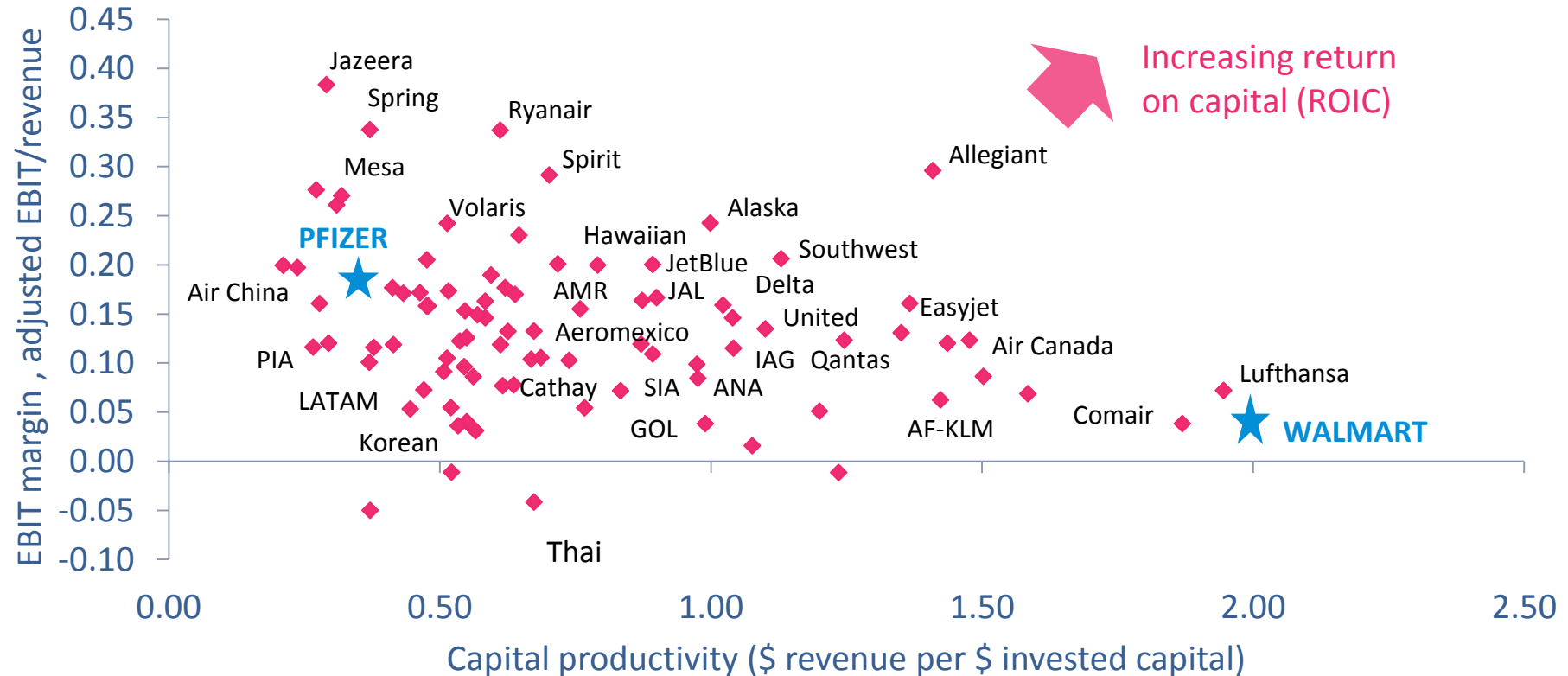
Margins now less leveraged to economic cycle?

World airline EBIT margin and global GDP growth

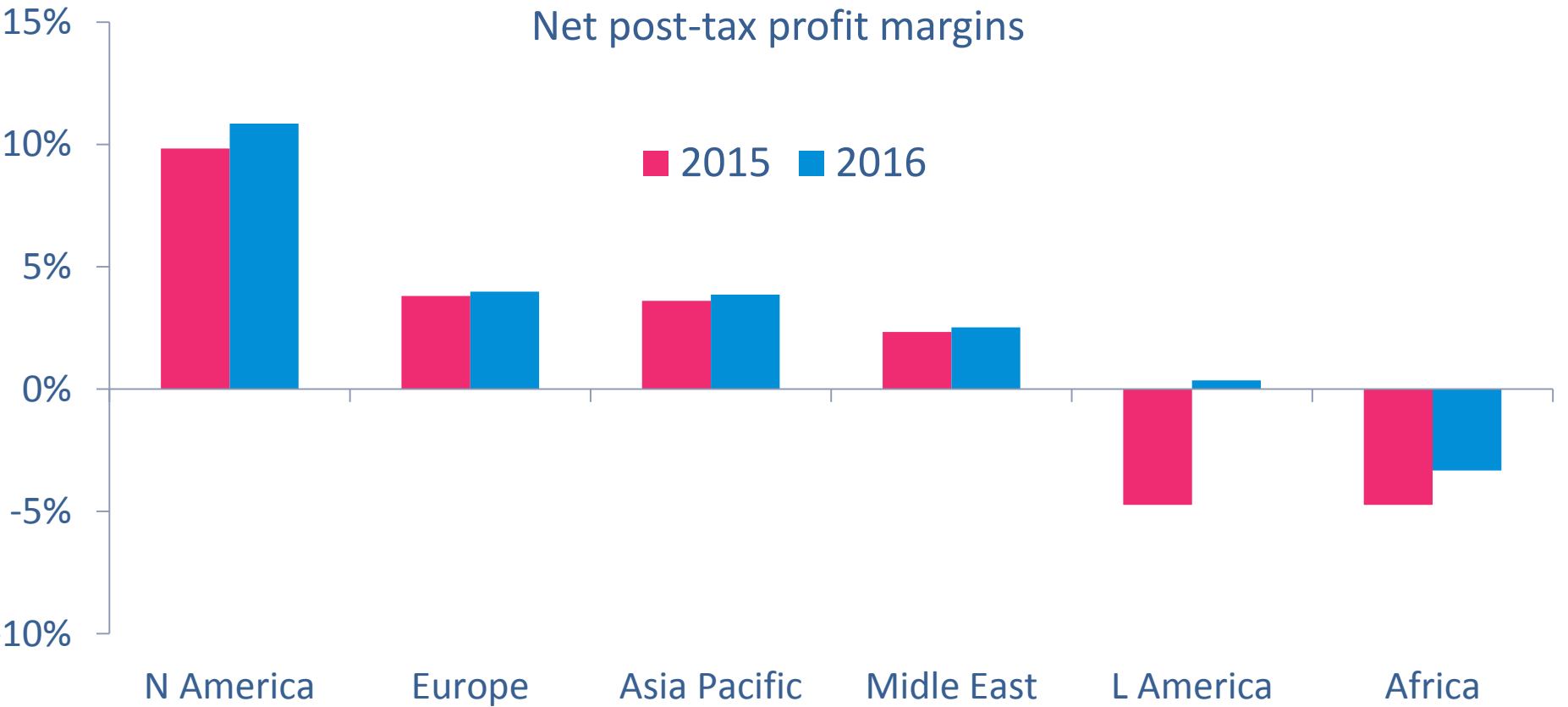


Industry totals hide enormous diversity

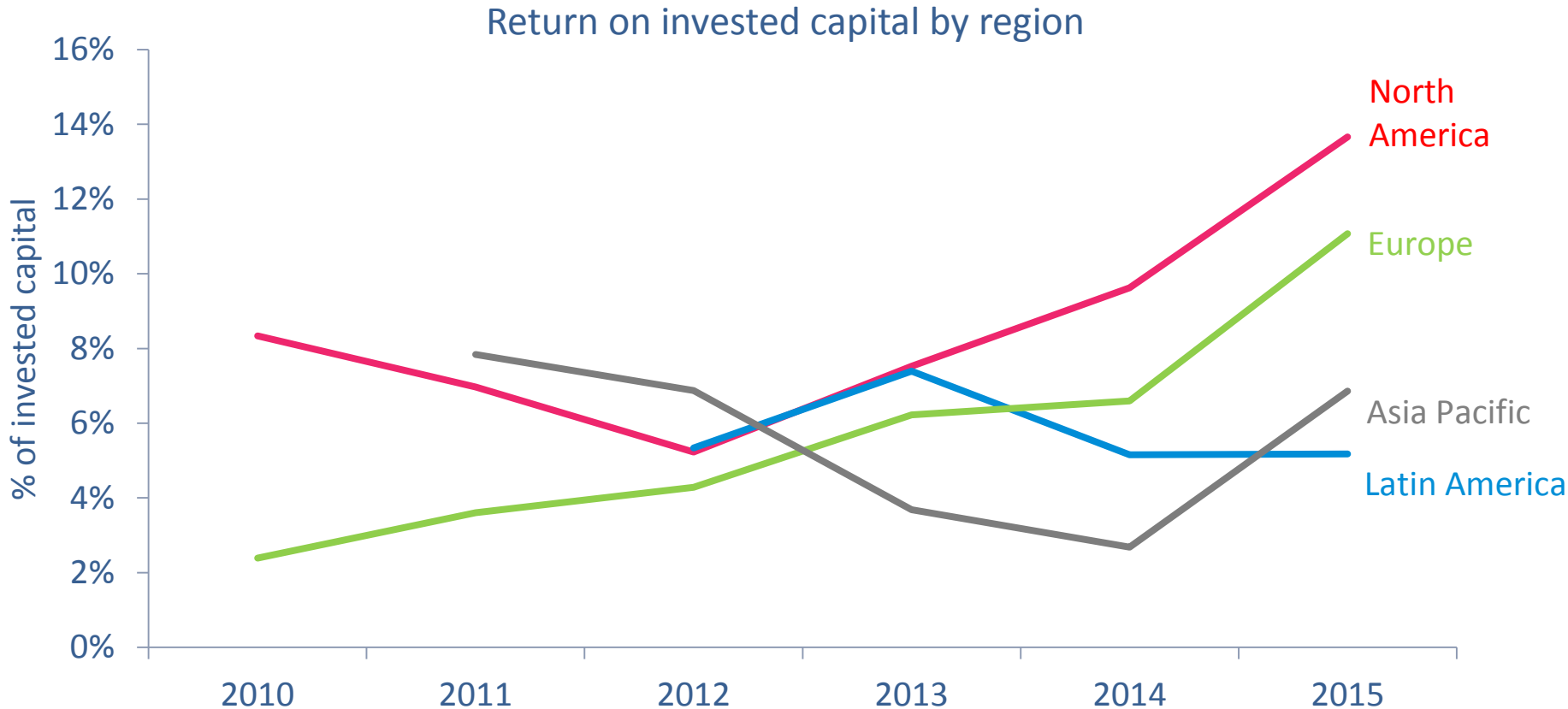
2015 ROIC = adjusted EBIT/revenue * revenue/invested capital



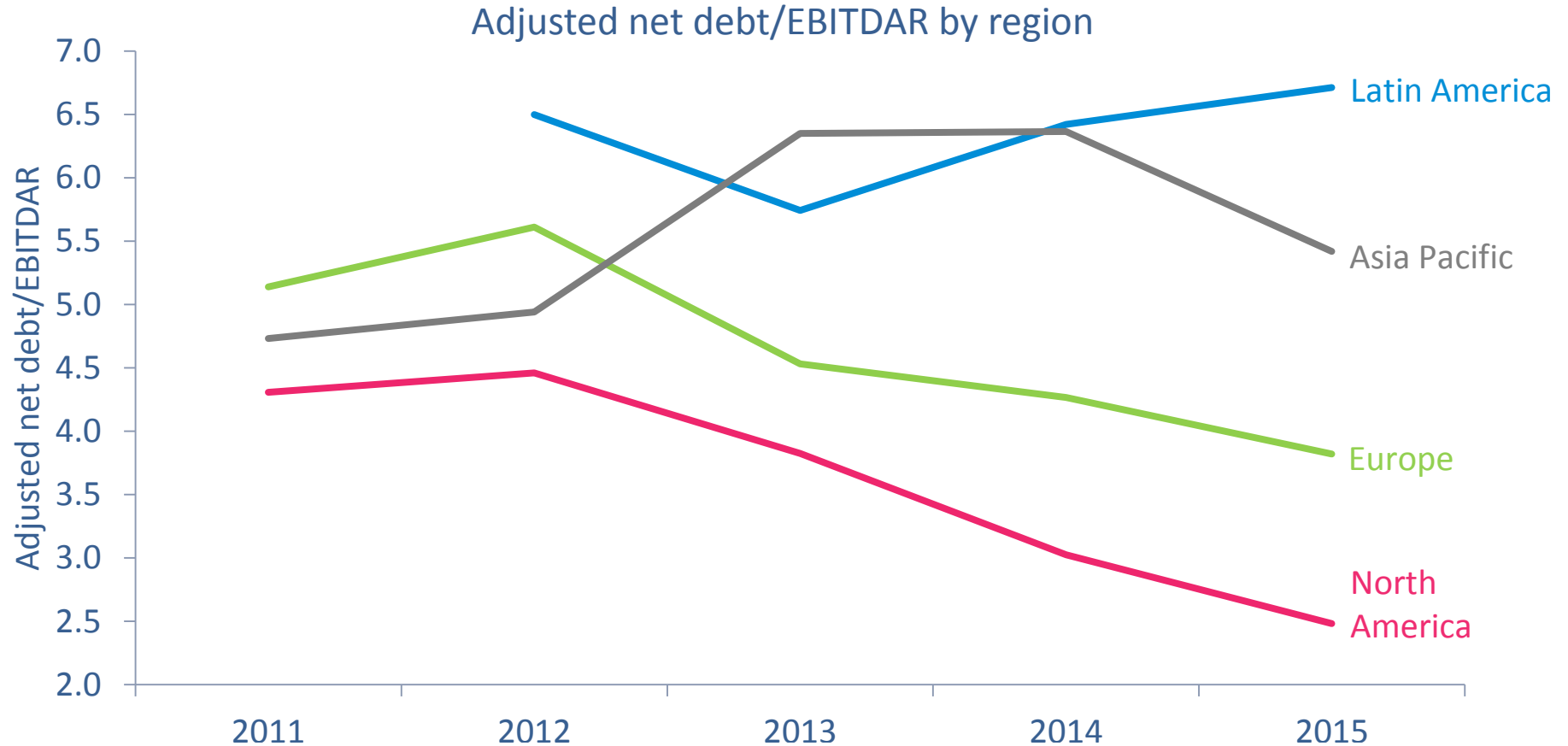
It's largely N America driving industry results



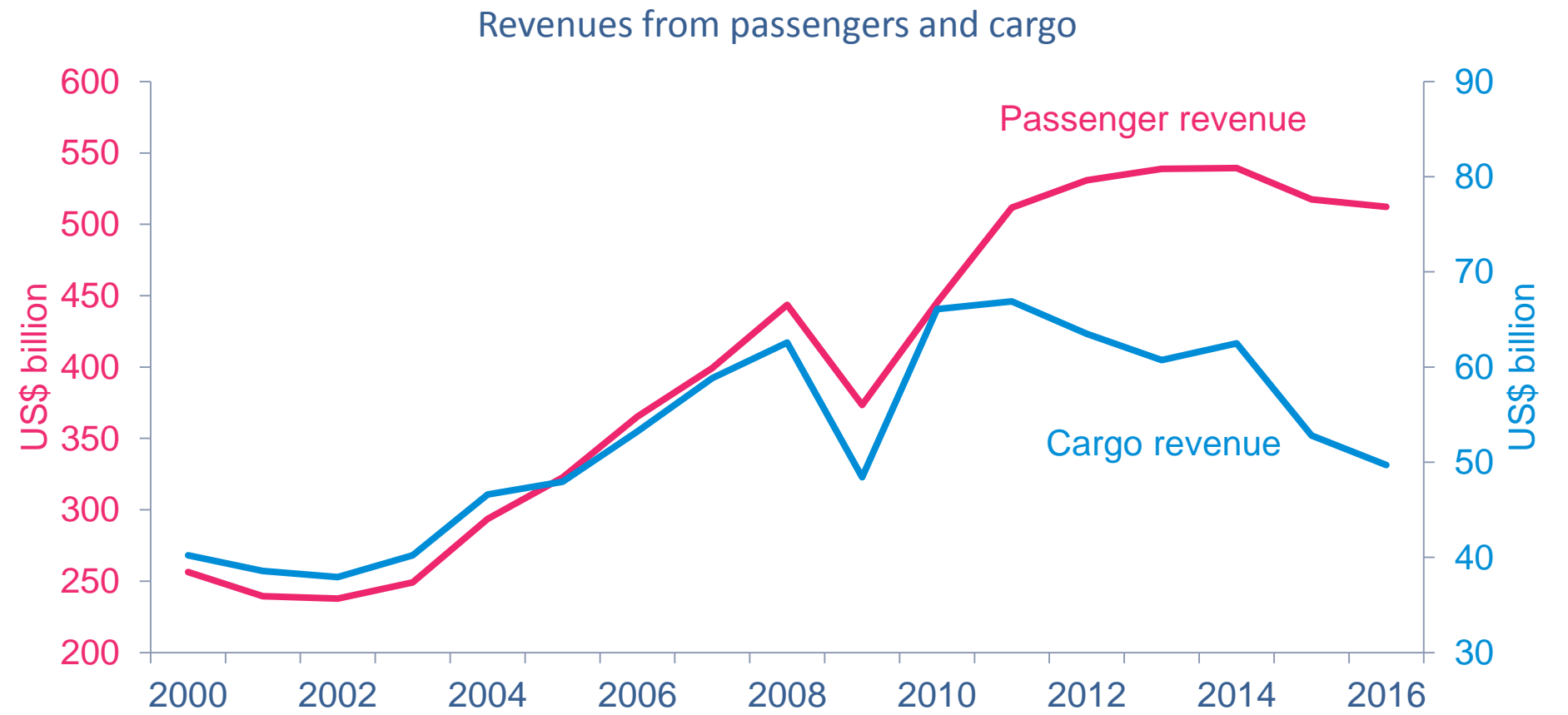
Parts of Europe also performing well but not elsewhere



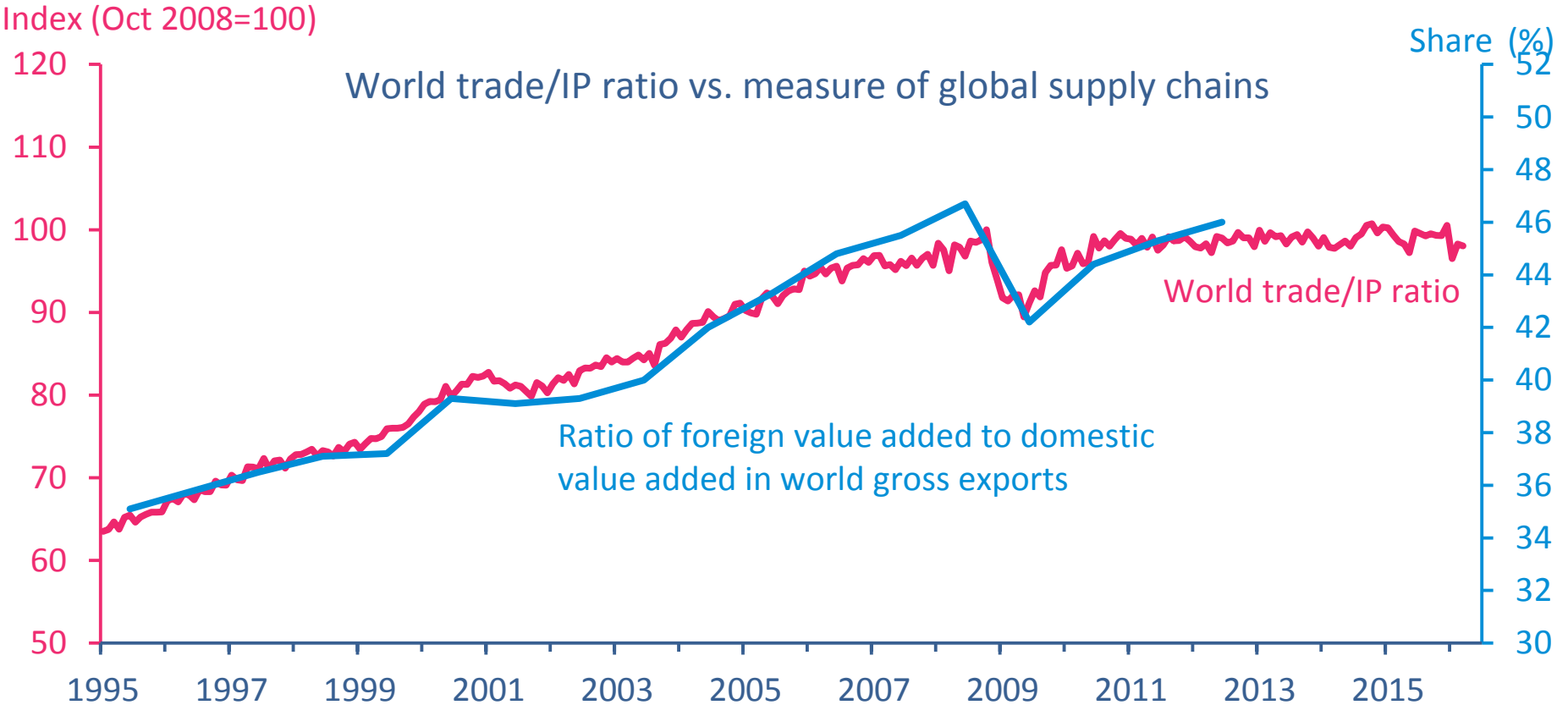
Balance sheets show the diversity of financial health



And performance is uneven across markets

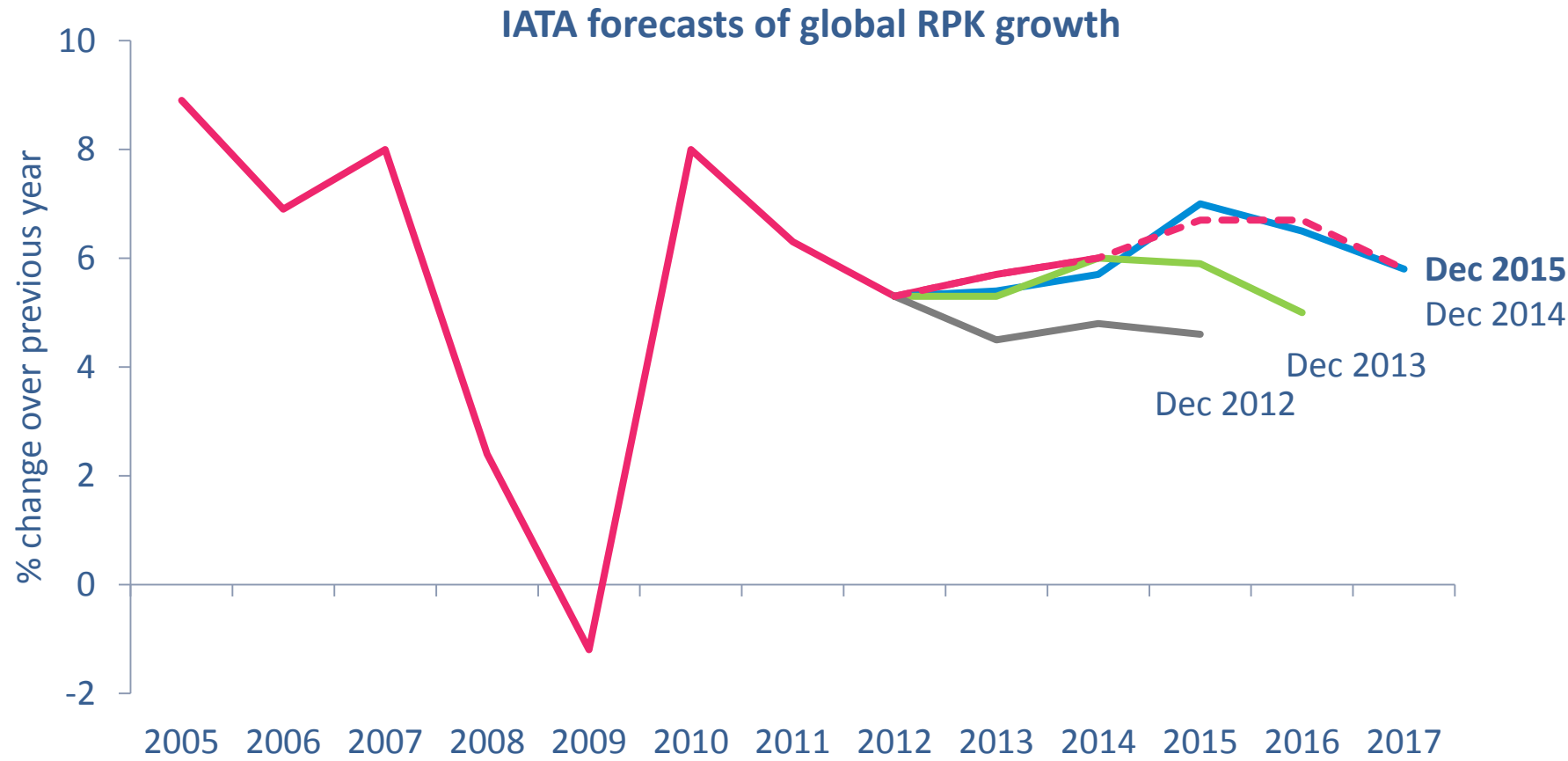


Globalization paused and threatened?



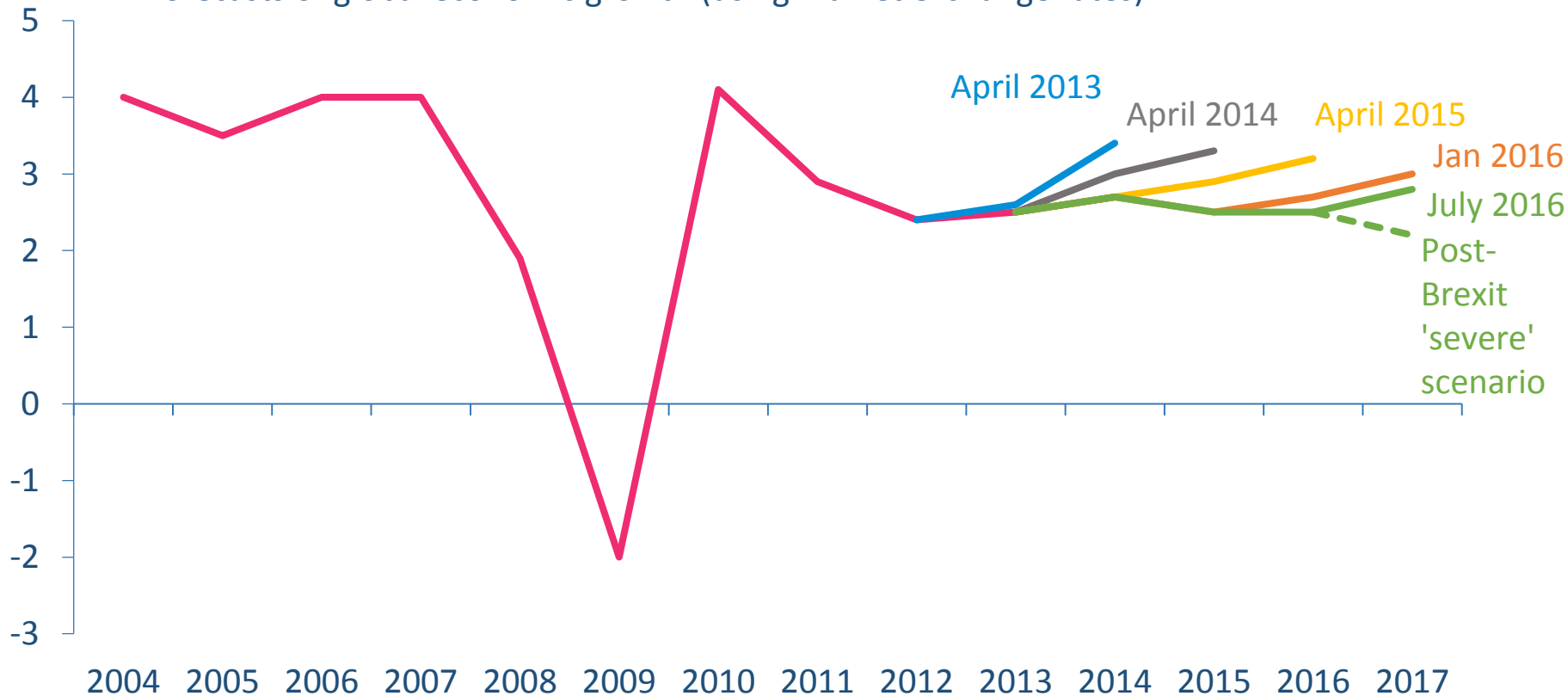
Sources: IATA, Netherlands CPB, OECD-WTO TiVA database

Air travel growth has surprised on the upside

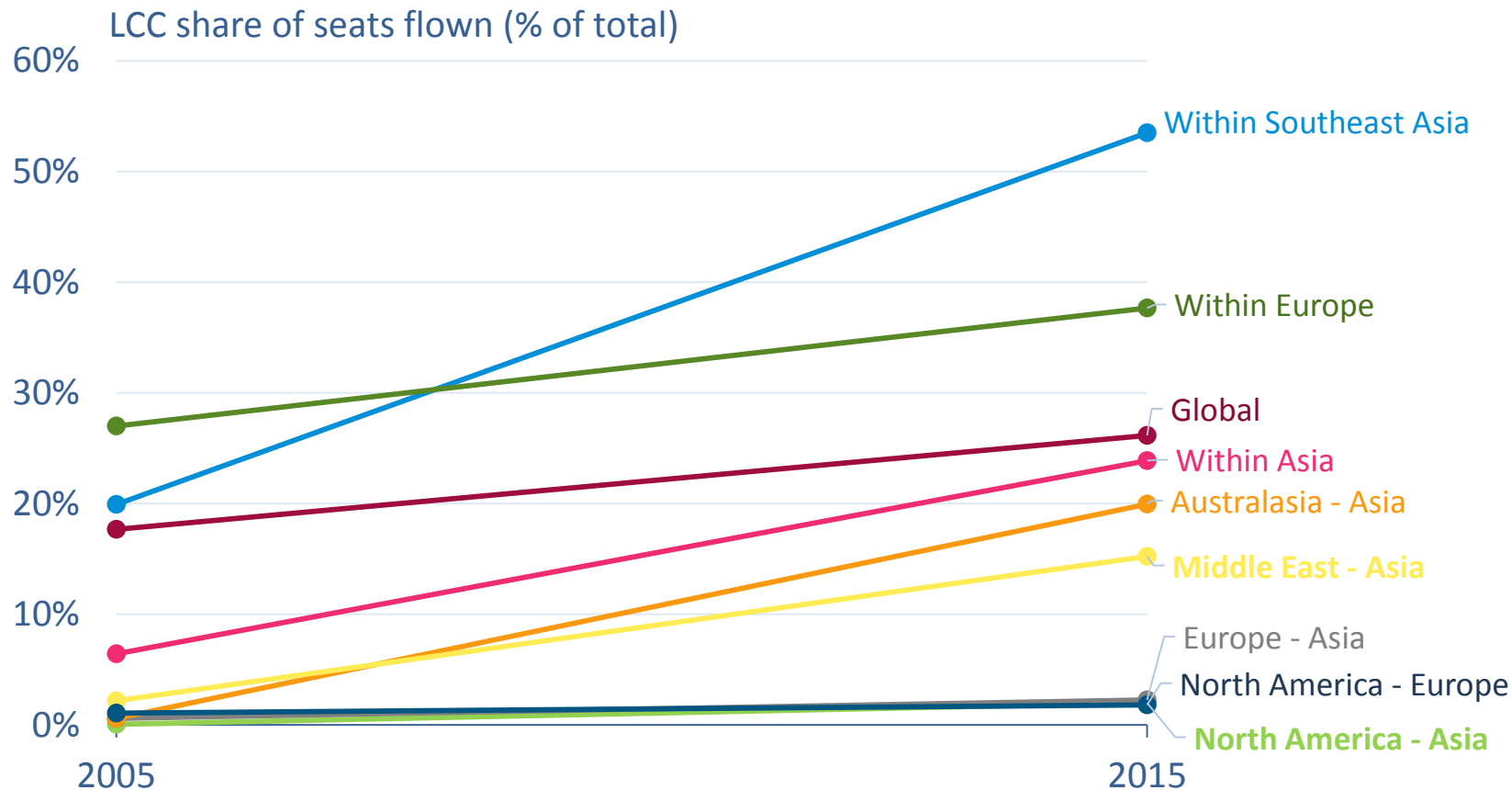


But world stuck in a low economic growth path

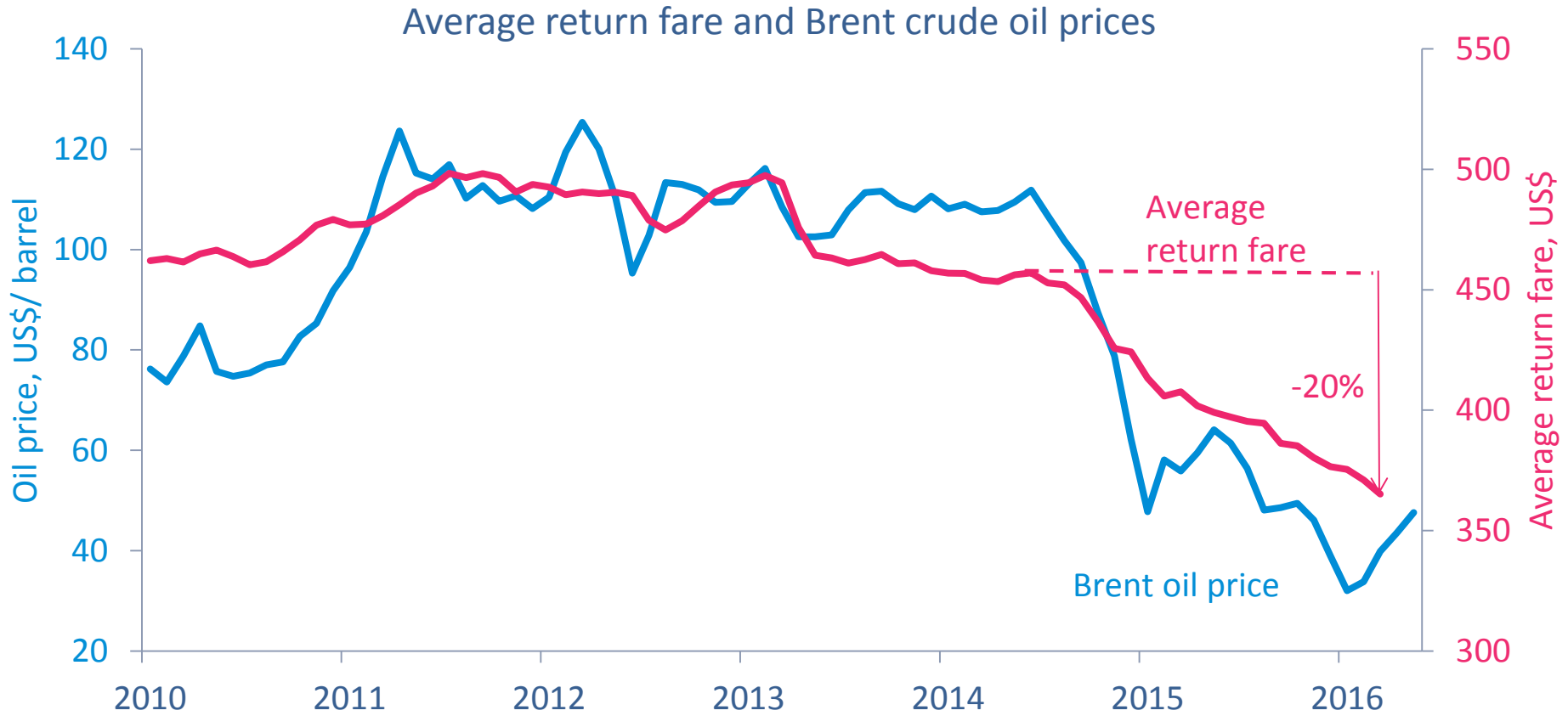
IMF forecasts of global economic growth (using market exchange rates)



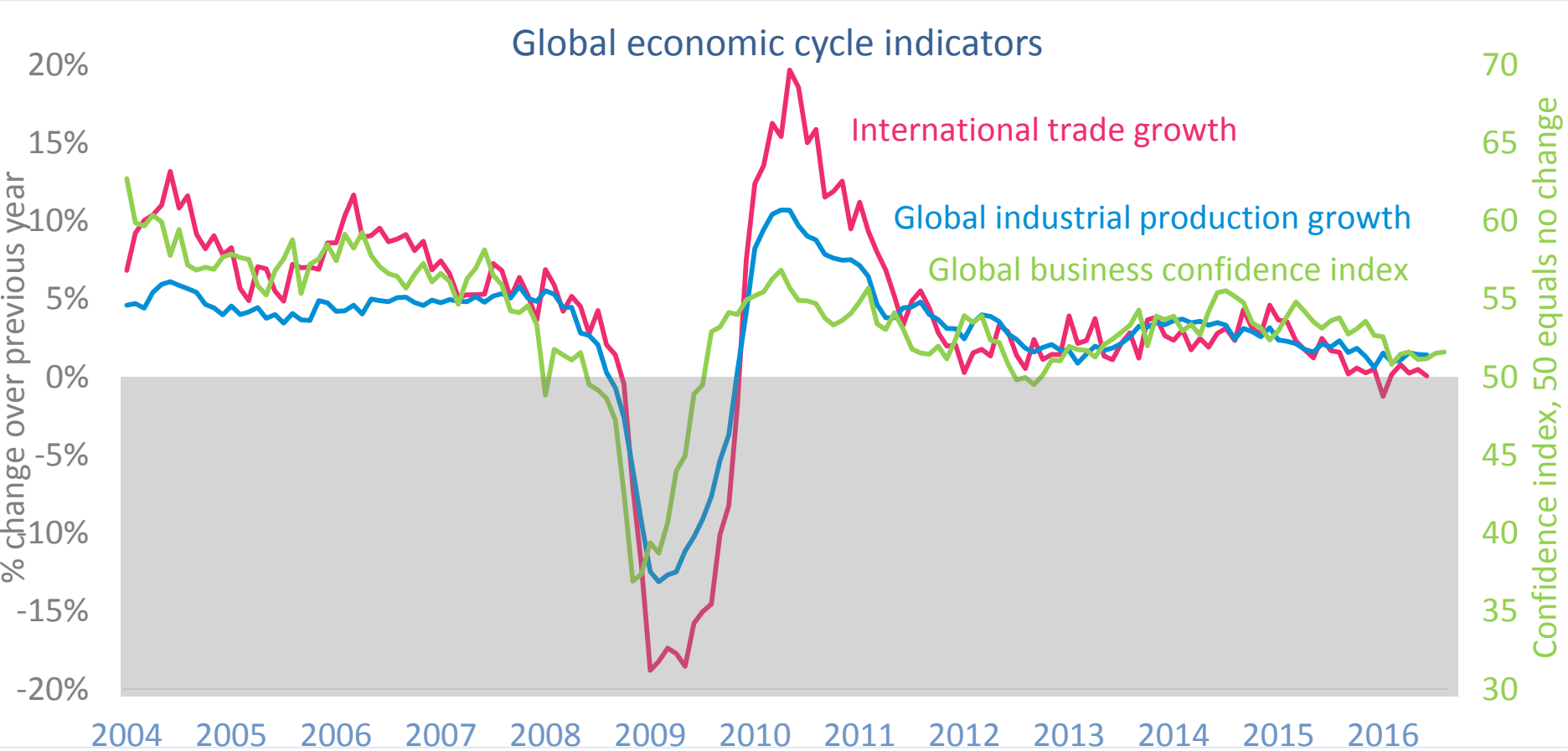
Price stimulation from LCC entry in significant markets



Significant price stimulation from fuel cost pass-through

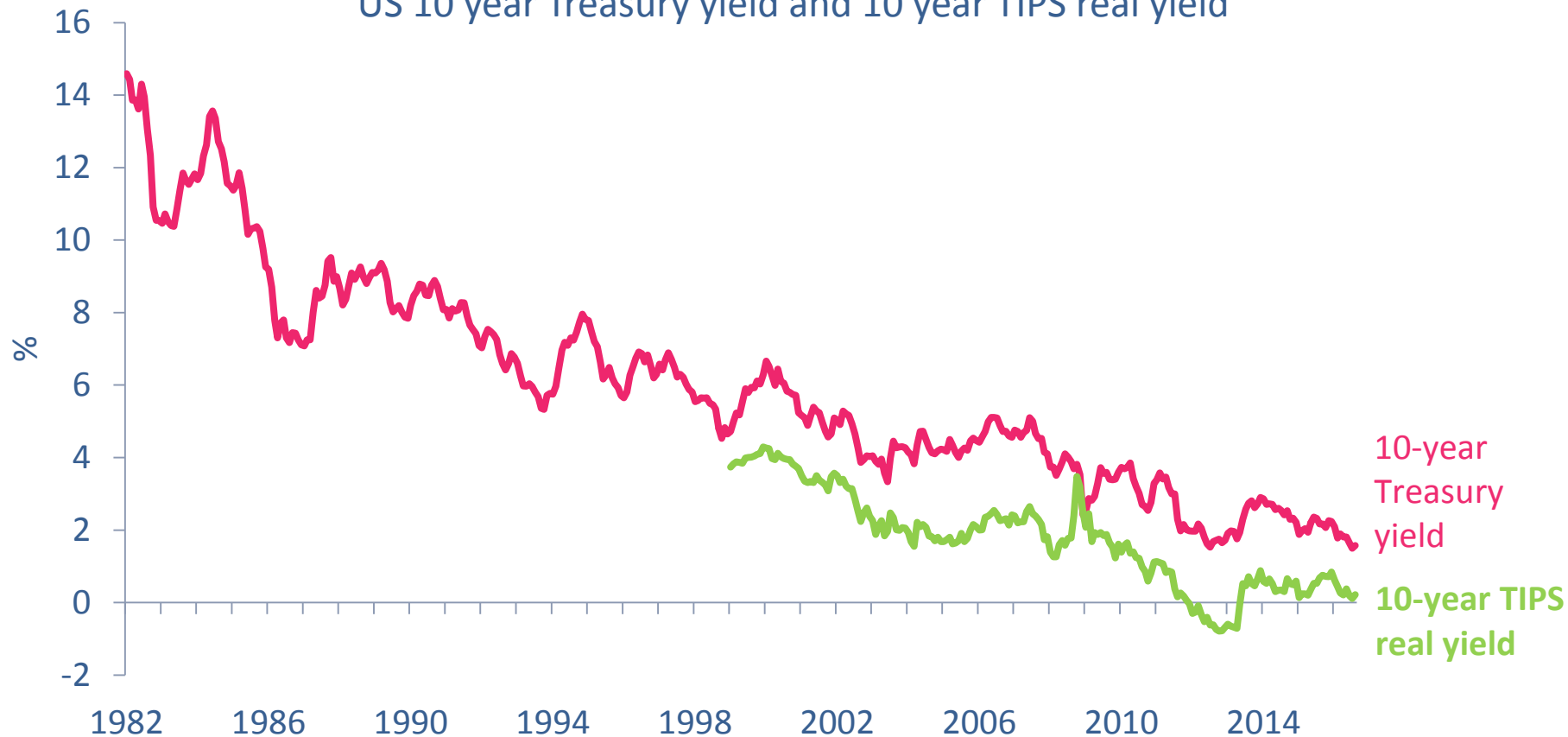


But lackluster economic cycle now seems to be slowing

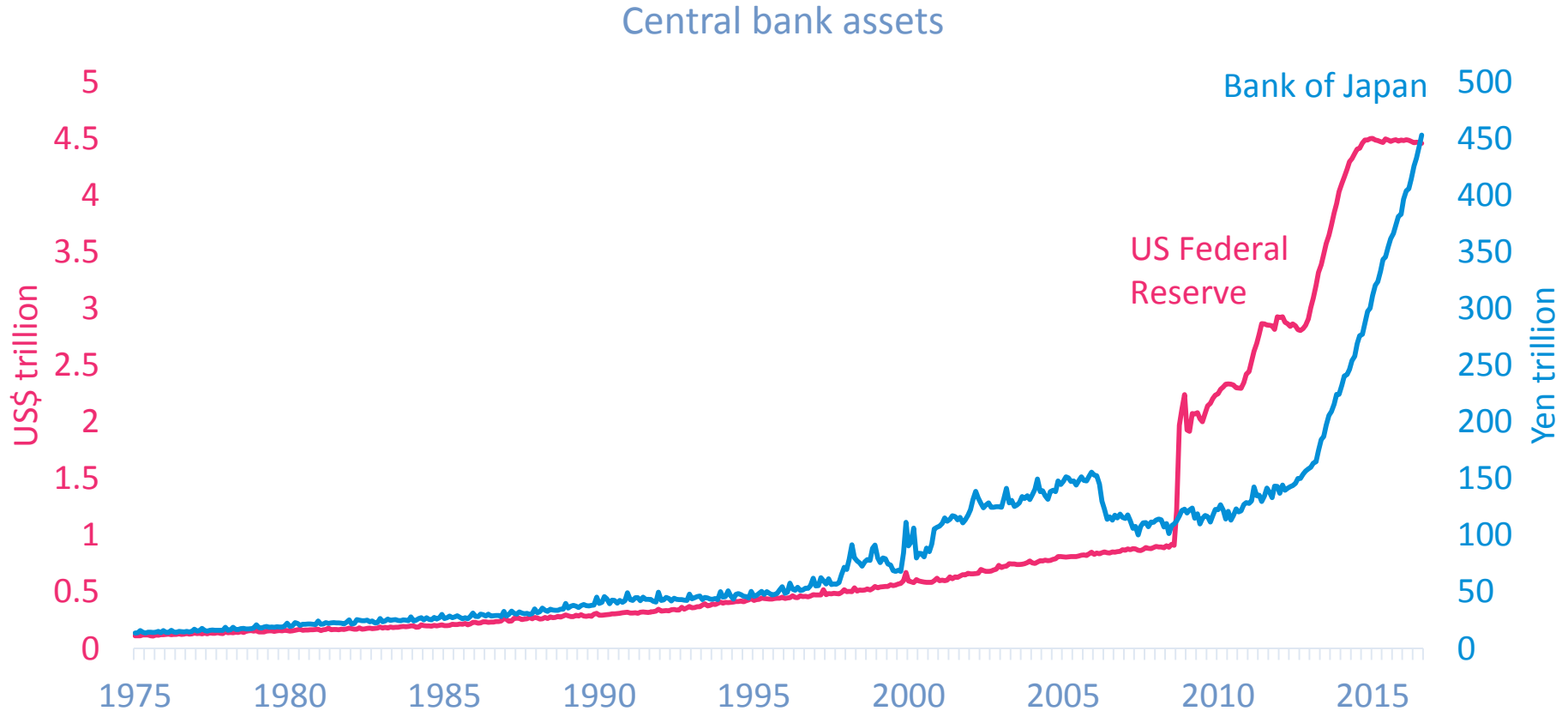


World awash with savings and short of investment

US 10 year Treasury yield and 10 year TIPS real yield

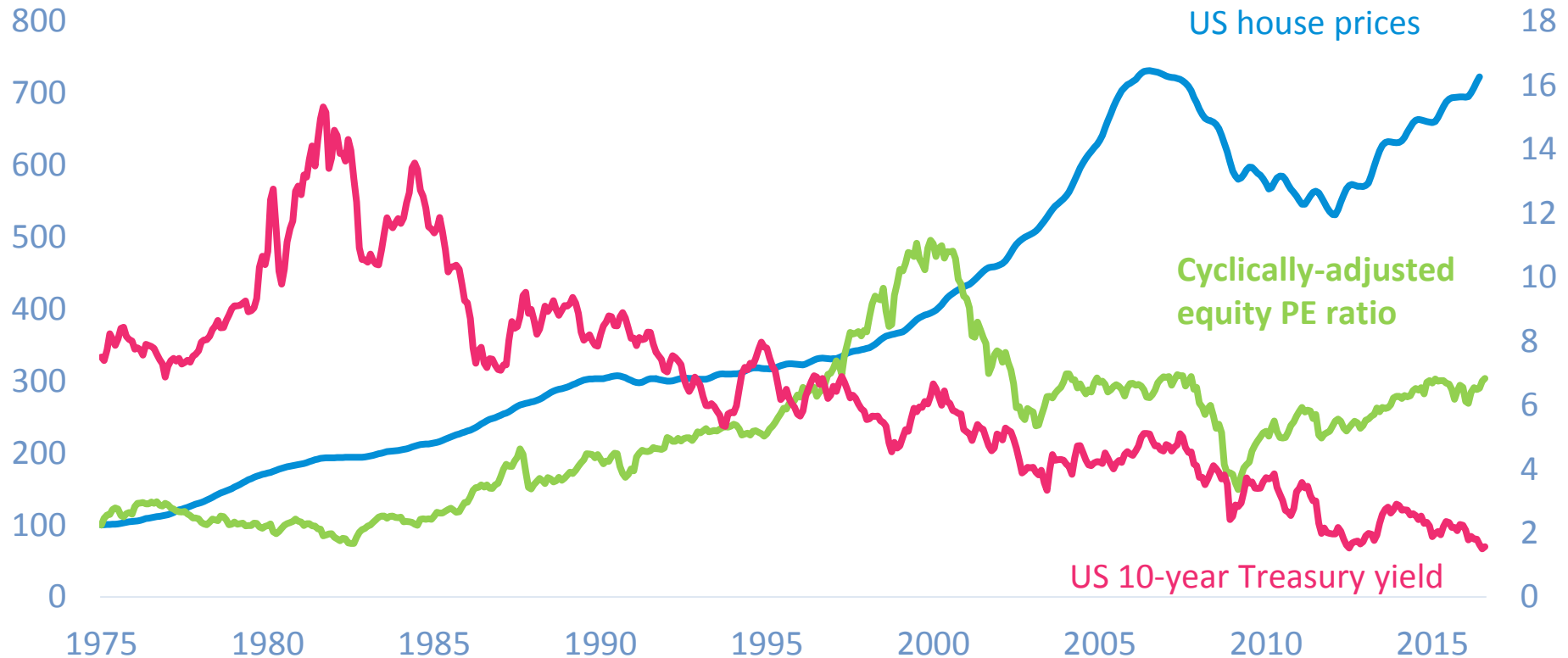


Central banks continue to print money



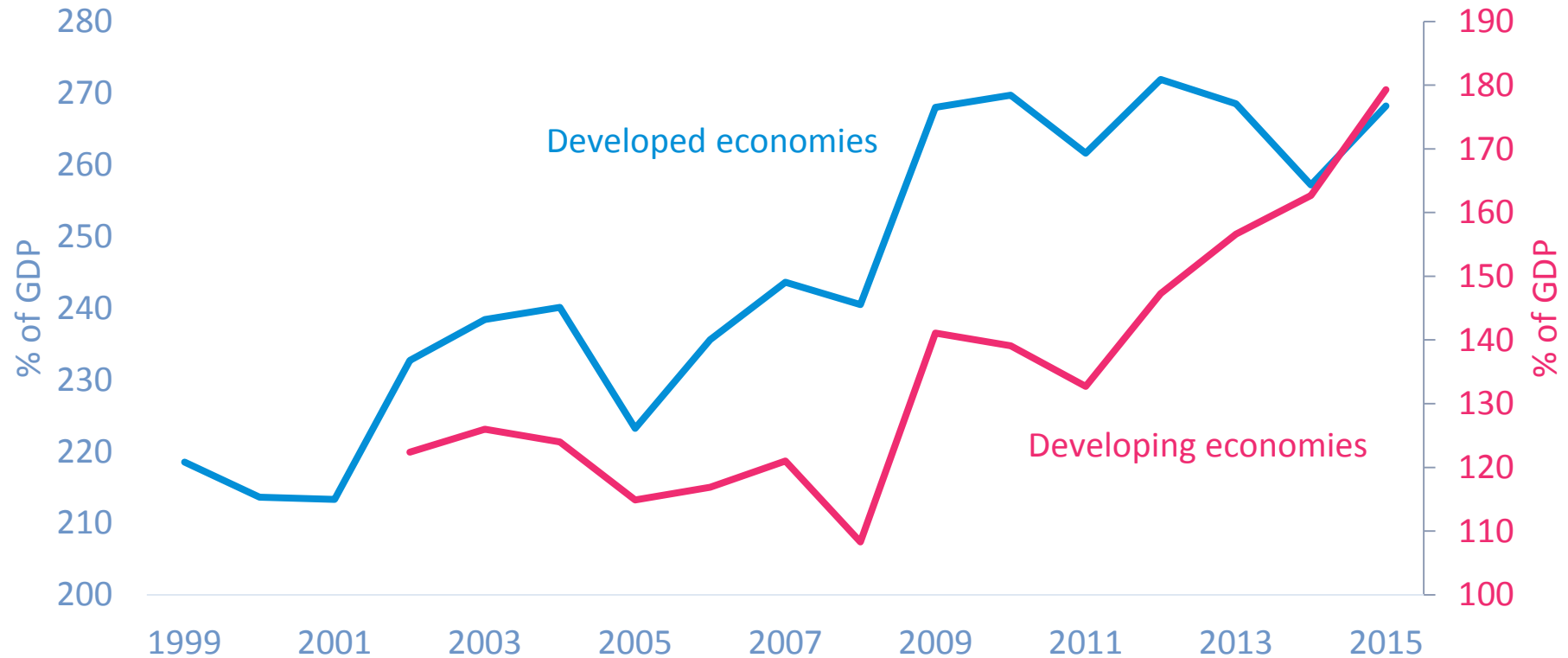
Asset price valuations back to pre-GFC levels or more

US Treasury yields, house prices and equity values



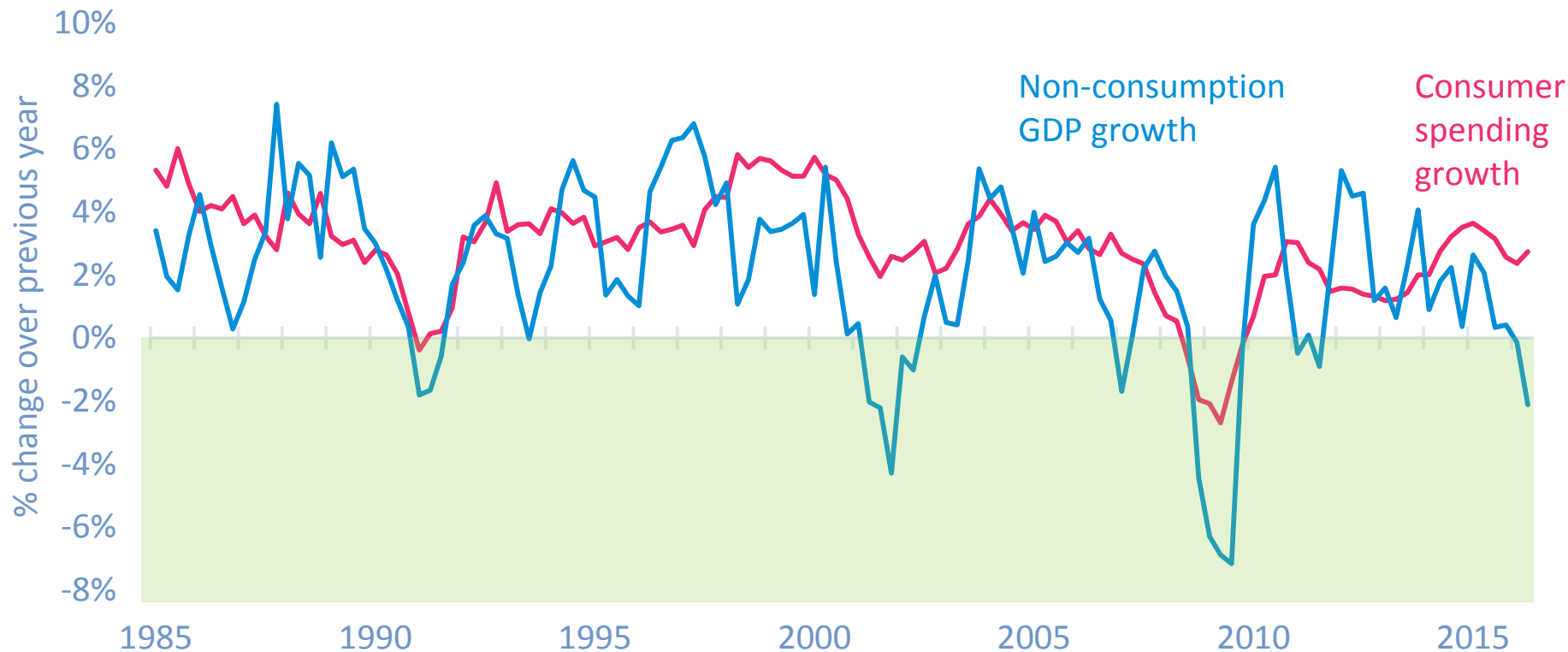
Debt continues to grow, despite Global Financial Crisis

Outstanding debt of non-financial sector, % of GDP



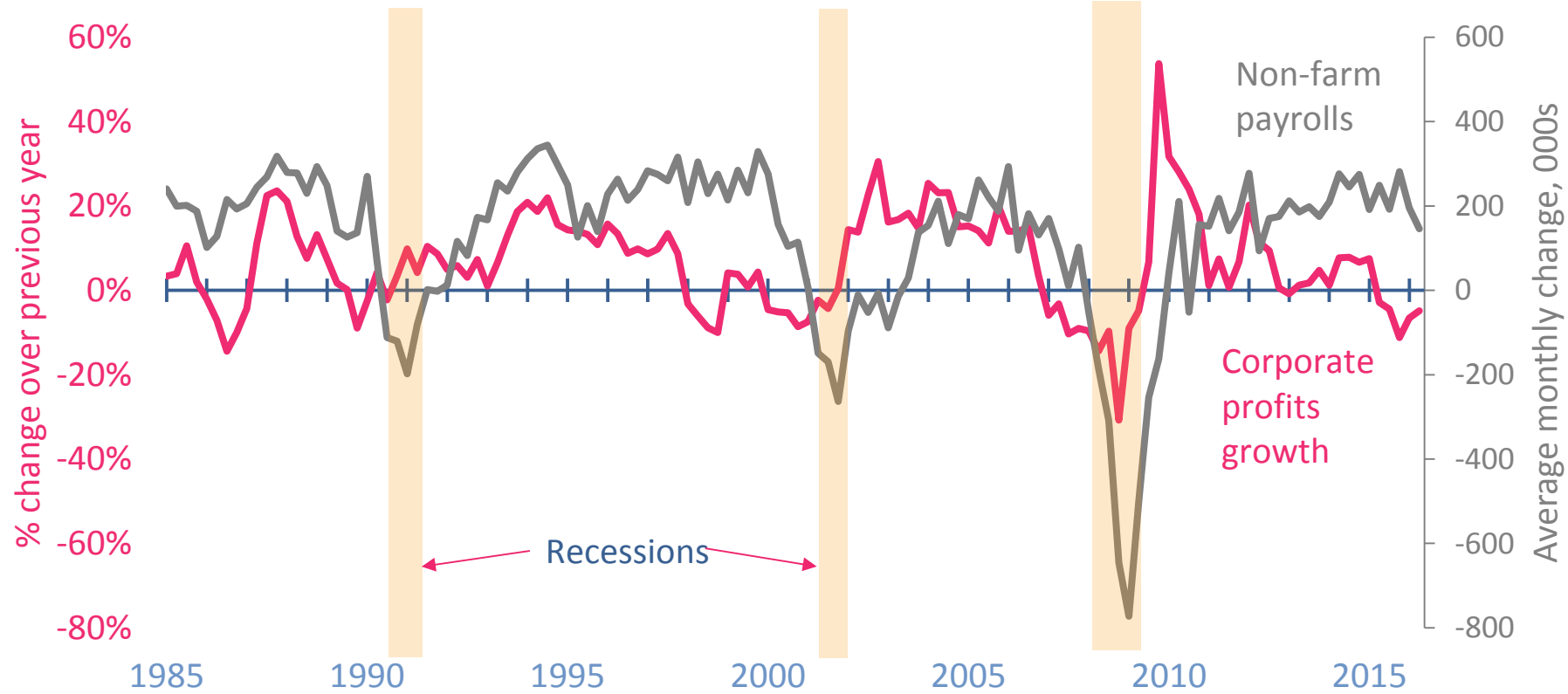
Only the consumer is keeping US GDP growth positive

US consumer spending and non-consumption GDP growth



Can payrolls keep growing while corporate profits shrink?

US fixed investment growth and change in non-farm payrolls



World economy (and aviation markets) at a cross-roads

- Central banks creating asset bubbles not economic growth
- Dangerous levels of indebtedness
- Brexit, support for populism, symptoms of rising inequality
- Two main scenarios:
 - Pessimistic: renewed debt deflation + protectionism; supply-side damage
 - Optimistic: incumbent governments respond to threats from populism and embrace reflationary policies

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