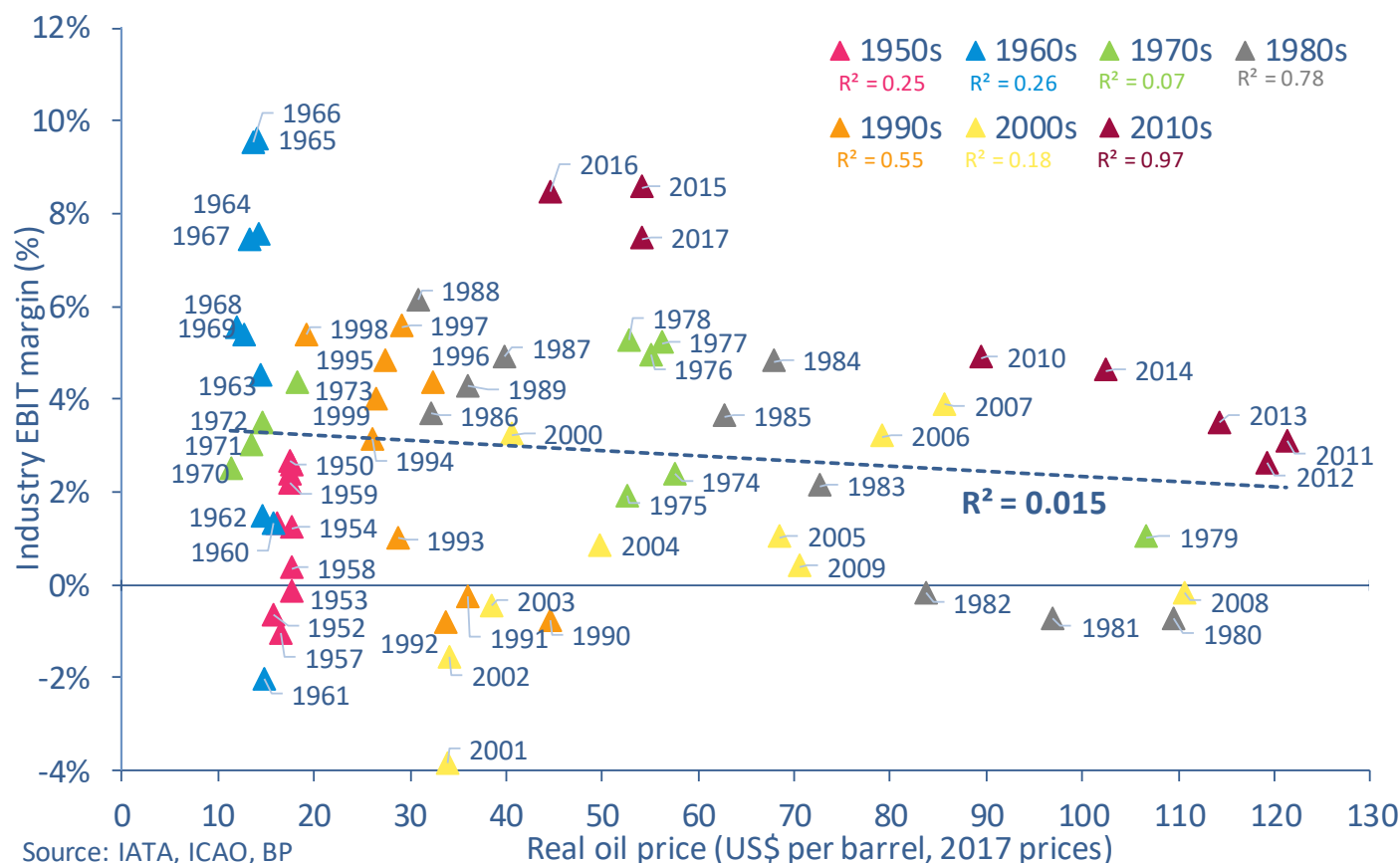




IATA ECONOMICS' CHART OF THE WEEK

9 NOVEMBER 2018

NO SIMPLE LINK BETWEEN OIL PRICES AND INDUSTRY PROFITABILITY



- This week's chart plots airline industry profitability – measured by the operating margin – and inflation-adjusted oil prices each year from 1950 to 2017. On average, as shown by the dashed line, higher oil prices have been associated with lower profitability over time. However, the key point is that the relationship is very weak: indeed, the level of oil prices explains just 1.5% of the variation in industry-wide profitability seen over the past 70 years.
- This is not to say that oil prices do not matter. Jet fuel is one of the highest cost items for airlines, accounting for 22.4% of total costs last year, and big movements in expenses can have large impacts in the short term. This is particularly the case for airlines with a large share of fixed costs that cannot be avoided by simply not operating flights. However, in general, today's chart suggests that fuel costs are typically passed through as and when capacity can adjust.
- The extent and speed to which airlines can pass changes in costs onto customers depend on factors such as the strength of the economic backdrop, each market's characteristics as well as airline-specific factors. The latter include the degree to which exchange rate movements and hedging strategies either cushion or exacerbate changes in oil prices from airline to airline. Such factors partly explain the different relationships observed across the past decades.
- Moreover, the extent and speed of the adjustment also depends on how quickly oil prices change: gradual changes are easier to deal with than large shocks, for example. Nonetheless, the key point is that *changes* in oil prices still explain only a tiny portion of the variation in industry profitability over time. The bigger picture is that there is no simple link between industry profitability and oil prices in the long run.

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