STATE OF THE REGION: EUROPE

SEPTEMBER 2017

Economy

GDP growth, selected countries

%change on a yr ago	2016	2016Q4	2017Q1	2017Q2
Germany	1.9	1.9	1.9	2.1
Russia	-0.2	0.3	0.5	2.5
France	1.1	1.2	1.1	1.8
UK	1.8	1.6	1.8	1.5
Italy	1.0	1.2	1.2	1.5
Spain	3.2	3.0	3.0	3.1
Turkey	3.2	4.2	5.2	5.1
Israel	3.9	4.7	3.7	2.9
Euro zone	1.8	1.9	2.0	2.3
World*	**2.3**	**2.6**	**2.6**	**2.8**

Source: Datastream * Market exchange rate basis † Estimate

Exchange rates

end of period, # per US$	2016	Jun-17	Jul-17	Aug-17
US$ broad index	127.7	122.3	120.7	119.3
European euro (EUR)	0.95	0.88	0.85	0.84
Russian ruble (RUB)	60.4	59.1	60.1	58.1
British pound (GBP)	0.81	0.77	0.76	0.78
Turkish lira (TRY)	3.52	3.52	3.52	3.46
Israeli shekel (ILS)	3.84	3.49	3.56	3.58

Source: Datastream, XE

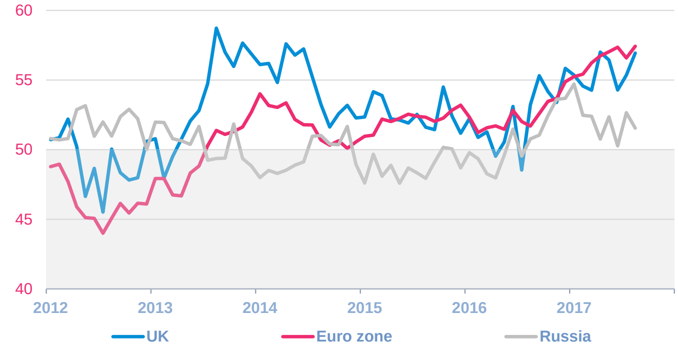
World oil and jet fuel price

US$/barrel	2016	Jun-17	Jul-17	Aug-17
Crude oil (Brent)	52.4	46.4	48.5	51.7
Jet fuel	64.0	54.4	59.5	65.6

Source: Platts, EIA Monthly average data

Business confidence - manufacturing PMIs

50=no change, seasonally adjusted



Source: Markit

- Business confidence remains elevated in both the Eurozone & UK, but last month's sizeable gain for Russia was partly unwound this month, despite the further rise in world oil prices (see below).
- On a trade-weighted basis, the US$ eased further in Aug, down 1.1% in the month & continuing its recent downtrend. Of the main regional currencies, the RUB & TRY were the strongest performers in Aug, gaining ~3% & 2%, respectively vs the US$. In contrast, the GBP fell by 2% on renewed financial mkt concerns over Brexit.
- Brent crude oil & jet fuel prices rose again in Aug, stepping up by 7-10%; the former moving back above US$50/bbl & the latter above US$65/bbl. The crack spread also widened further this month.

Market

Revenue passenger kilometers (RPKs)

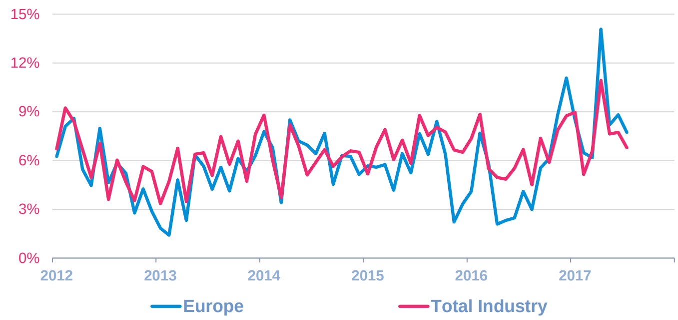
%change on a yr ago	2016	May-17	Jun-17	Jul-17
Region (registration basis)				
Europe	4.6	8.2	8.8	7.7
World	6.4	7.6	7.7	6.8
Routes (segment basis)				
Russia domestic	2.5	12.6	9.7	9.1
Within Europe	7.7	9.5	10.2	9.4
Europe - North America	2.5	4.7	5.3	2.7
Europe - Asia	1.8	15.4	10.6	6.4
Europe - Middle East	9.9	1.5	7.4	7.7
Europe - Africa	1.8	3.5	8.0	7.5
Europe - South America	3.5	7.5	8.4	3.7

Source: IATA Statistics Note: historical data may be subject to revision

- Global RPKs grew by a robust 6.8%yoy in Jul, easing from 7.7% in Jun. For the European carriers, pax volume growth also eased moderately, to (a still robust) 7.7%yoy & maintaining the gap over the industry-wide pace.
- Russia domestic RPKs grew by 9.1%yoy in Jul, broadly in line with the 5yr average pace. RPK growth for this market has eased in recent months, consistent with developments in business confidence.
- Amongst the main international markets for the region's carriers, Within Europe is the strongest performer at present, with yoy growth in pax volumes of 9.4%. This outcome is consistent with the broad-based improvement observed in the European economy.
- The Middle East & Africa markets follow with growth of 7.7% & 7.5%, respectively. Growth has slowed significantly for the Asia market; at 6.4%yoy currently, the rate is down 9pp in just two months.

Growth in air passenger volumes

RPKs, % Growth year-on-year



Source: IATA Statistics

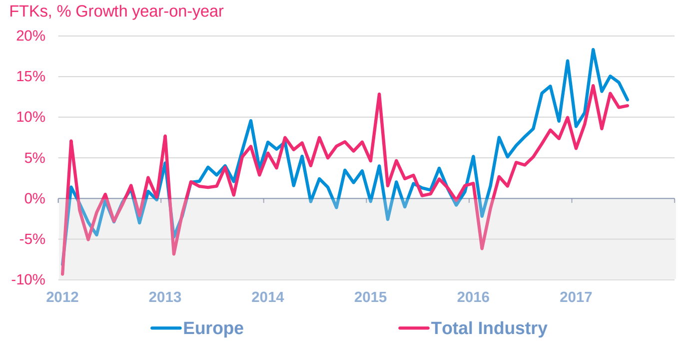
Freight tonne kilometers (FTKs)

%change on a yr ago	2016	May-17	Jun-17	Jul-17
Region (registration basis)				
Europe	7.9	15.1	14.3	12.1
World	3.9	12.9	11.2	11.4
Routes (segment basis)				
Europe - Asia	3.9	15.1	13.8	11.1
Europe - North America	2.5	13.1	12.9	12.9
Europe - Middle East	7.1	14.9	14.3	17.8
Europe - Africa	-5.5	6.0	4.2	7.9
Europe - South America	1.2	0.5	6.7	4.1
Within Europe	23.3	48.3	33.5	40.1

Source: IATA Statistics Note: historical data may be subject to revision

- Global FTK growth ticked up slightly in Jul, to 11.4%yoy – recording a double-digit annual growth rate for the 4th time in 5 months. Growth in freight volumes for the European carriers eased a little this month, but at 12.1%yoy, it continues to show stronger growth than the industry-wide performance.
- The fastest growing market continues to be (the smaller) Within Europe, where freight volumes are up ~40% on their level of a year ago. As we have noted previously, this strong performance is being driven by gains from carriers including Turkish Airlines.
- Each of the three largest international freight markets for the region are currently showing double-digit FTK growth. Routes to & from the Middle East are currently the standout, with growth stepping up to 17.8%yoy in Jul, ahead of both the Nth America (12.9%yoy) & Asia (11.1%yoy) markets.

Growth in air freight volumes



Source: IATA Statistics

Industry

Capacity growth and load factors

ASK/AFTK: %ch on a yr ago, LF: % of ASK/AFTK		2016	May-17	Jun-17	Jul-17
Passenger					
Europe	ASK	4.8	6.1	6.7	6.2
	PLF	*82.4*	*82.2*	*85.4*	*88.5*
World	ASK	6.4	6.2	6.4	6.1
	PLF	*80.5*	*80.0*	*81.9*	*84.7*
Freight					
Europe	AFTK	7.3	5.6	6.1	5.5
	FLF	*44.4*	*46.6*	*45.9*	*44.2*
World	AFTK	5.4	4.9	4.8	3.7
	FLF	*43.0*	*45.4*	*45.2*	*43.7*

Source: IATA Statistics. Note: LF=seasonally adjusted load factor. ASK=available seat kilometers. AFTK=available freight tonne kilometers

- The industry-wide pax load factor increased to a strong 84.7% in Jul. But even so, the PLF for the European carriers still managed to outperform, at 88.5%, & is easily the highest amongst all regions.
- A similar story is evident on the freight side, where the FLF for the European carriers remains a little above that of the industry-wide figure, at 44.2% vs 43.7%.
- The latest Q2 financial data further suggest that the squeeze on margins has eased somewhat from Q1. At the industry level, the EBIT margin is currently 9.5%, down from 10.2% in 2Q16. The European airlines have shown significant improvement compared with last year (8.6% currently vs 4.5% in 2Q16), with the performance now only ~1pp below the industry-wide result.
- Global pax yields (in US$ terms) have continued to trend modestly upwards in recent months. This trend is broadly reflected at the regional level, with only the Europe-Nth America & Europe-Africa markets still reporting lower yields (in yoy terms) currently. The strongest performers are the Russia domestic & Europe-Sth America markets where yields have risen by a substantial 12% & 10%, respectively, over the past year.

Airline operating (EBIT) margins*

%revenues	2015	2016	2016Q2	2017Q2
Europe	5.4	6.1	4.5	8.6
Industry	8.5	8.8	10.2	9.5

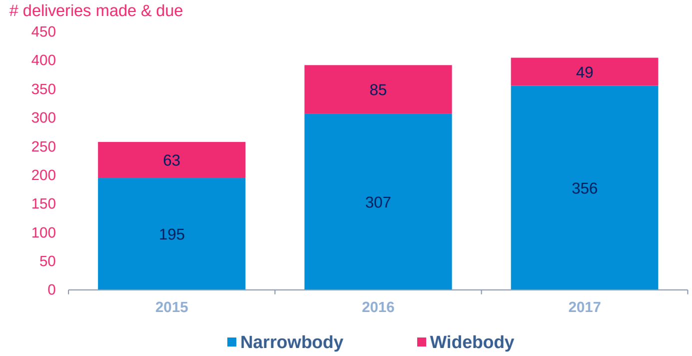
Source: Airline Analyst * constant sample basis, not seasonally adjusted

Passenger yields (US$, excl. surcharges & ancillaries)

%change on a yr ago	2016	May-17	Jun-17	Jul-17
Russia domestic	5.2	10.0	7.1	11.9
Within Europe	-7.6	-3.0	-2.5	3.0
Europe - North America	-8.3	-3.1	-3.5	-2.3
Europe - Asia	-10.3	1.5	1.7	4.7
Europe - Middle East	-11.5	1.2	-5.7	2.5
Europe - Africa	-8.3	-6.9	-5.0	-1.4
Europe - South America	-17.5	3.9	8.7	10.0

Source: IATA PaxIS Note: historical data may be subject to revision

Aircraft deliveries to Europe (2Q17 data)



Source: Ascend