

IATA ECONOMIC BRIEFING

FEBRUARY 2010

AIRLINE FUEL AND LABOUR COST SHARE

- In 2008, fuel continued to be the largest single cost item for the global airline industry. Based on a sample of 45 major global passenger airlines, fuel represented about 32.3% of the total operating cost, up from 27.4% in 2007. These numbers are consistent with global industry fuel share so this sample can be taken to be representative. The share of labour (including pension) expenses fell from 22.8% in 2007 to 20.1% in 2008.
- The rise of the share of the fuels costs reflects the sharp increase in fuel prices faced by airlines. The **share of fuel costs was 12-13% between 2001 and 2003 but has more than doubled** as the average price of jet fuel per barrel rose from US\$34.7 in 2003 to US\$126.7 in 2008. The rise in the fuel price follows the increase in the price of crude oil over the period, but also reflects a widening in the refinery margin between crude oil and jet fuel due largely to capacity constraints at refineries. The widening of the refinery margin alone added an extra US\$34.5 billion to the industry's fuel cost in 2008, although this margin has narrowed in 2009 due to excess refinery capacity.
- Airlines have responded to high fuel costs and severe financial pressures since 2001 by operating more fuel efficient aircraft and by achieving large productivity and efficiency gains in non-fuel cost items. In particular, labour productivity (in terms of employees per available tonne kilometre) has improved by 42% over the period. As a result, **labour's share of total operating costs has fallen from 28.3% in 2001 to 20.1% in 2008**. Airlines have also achieved significant cost efficiencies in other areas such as distribution, including those delivered by IATA's simplifying the business project, that have reduced the share of "other" costs (i.e. excluding payments to labour, fuel and capital) from 46.4% in 2001 to 38.3% in 2008.

REGIONAL DIFFERENCES IN FUEL AND LABOUR COST SHARES

- There are significant regional differences between the shares of fuel and labour costs within total operating costs (see Table 1). In 2008, **labour's share of airline operating costs was 22-25% in North America and Europe but only 14.7% in Asia Pacific**, reflecting the relatively lower wage level in that region. However, with relatively lower labour costs, fuel accounts for a much higher proportion of total costs (36.7%) in Asia Pacific than elsewhere.

Table 1: Percentage Share of Airline Operating Costs, by Region of Airline Registration

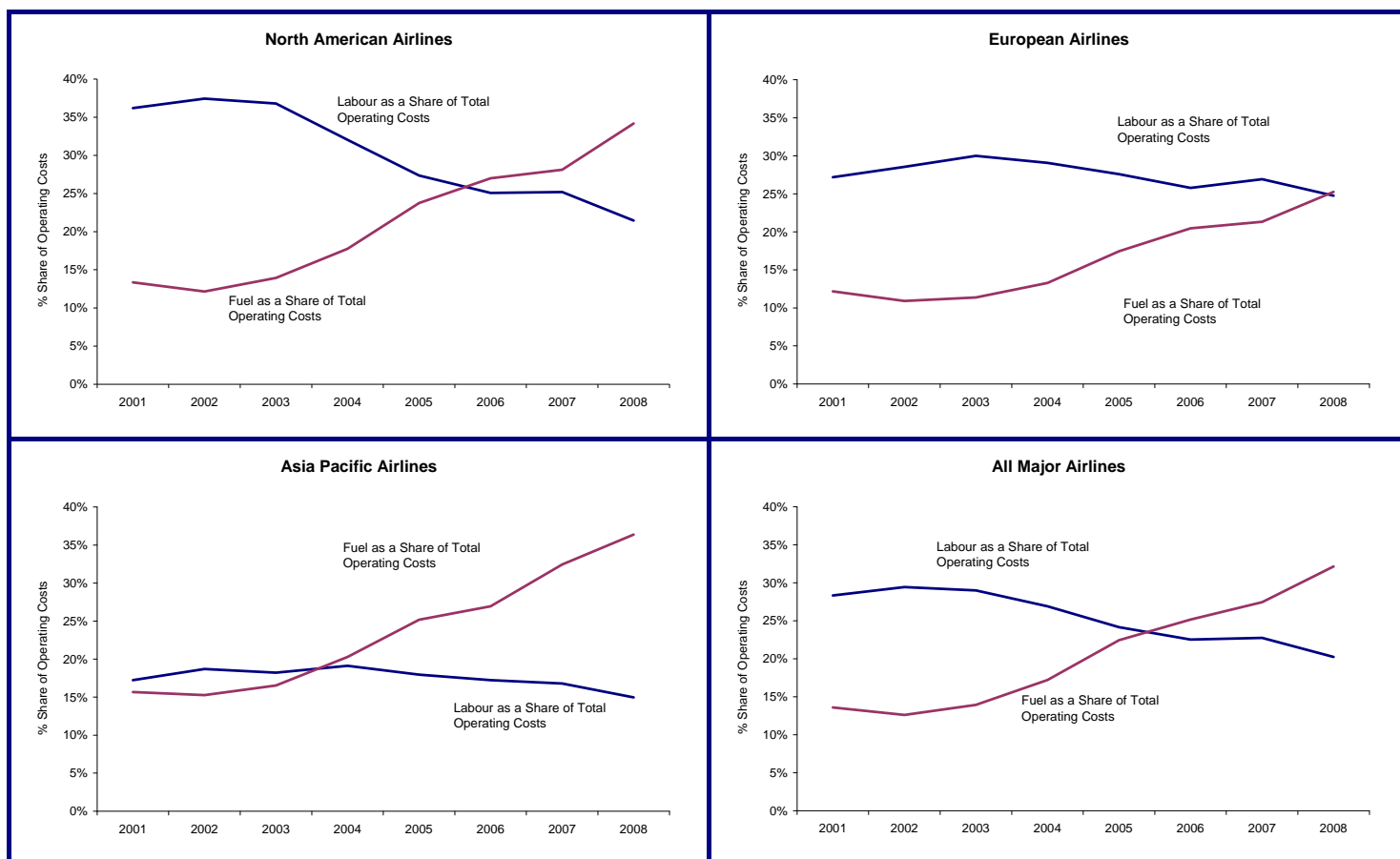
	North America		Europe		Asia Pacific		All Major Airlines	
	2001	2008	2001	2008	2001	2008	2001	2008
Labour	36.2%	21.5%	27.2%	24.8%	17.2%	14.7%	28.3%	20.1%
Fuel	13.4%	34.2%	12.2%	25.3%	15.7%	36.7%	13.6%	32.3%
Aircraft Rentals	5.5%	3.0%	2.9%	2.5%	6.3%	4.5%	5.0%	3.5%
Depreciation and Amortisation	6.0%	4.5%	7.1%	5.7%	7.4%	7.8%	6.7%	5.9%
Other	38.9%	36.9%	50.7%	41.8%	53.4%	36.3%	46.4%	38.2%

Source: Company Reports

- The large scale restructuring of North American airlines since 2001 – in some cases involving a period under Chapter 11 bankruptcy protection – has enabled them to achieve significant improvements in labour productivity and reductions in total labour costs. **Labour's share of total operating costs for North American airlines has fallen sharply from 36.2% in 2001 to 21.5% in 2008**. This reflects a sharp rise in the share of fuel costs over the same period, but also reflects much lower labour costs (including lower pension liabilities as a result of Chapter 11).

- In 2008, the first time since 2001, fuel cost accounted for a higher proportion of operating costs than labour for European airlines. Labour accounted for 24.8% of operating costs, while fuel about 25.3%. The gap between fuel and labour cost narrowed significantly since 2001 (see Figure 1). This partly reflects the greater commercial flexibility for European airlines to undertake financial hedging of their fuel costs that has provided some protection from the sharp rise in fuel costs. However, it is also likely to partly reflect the more diversified nature of some European airlines (e.g. Lufthansa), where more labour-intensive activities such as ground-handling and maintenance are included within the parent company's financial accounts.
- With relatively low labour costs (in developing economies rather than in Japan, Australia and New Zealand), fuel has accounted for a higher share of costs than labour for Asia Pacific airlines since 2004. As such, on a proportionate basis, Asia Pacific airlines have been more exposed to higher fuel costs than airlines in North America and Europe. In 2008, fuel expenses accounted on average for 36.7% of operating costs for Asia Pacific airlines and were higher than 50% for some airlines based in this region. The region shows also a higher share of aircraft costs (rentals and depreciation-amortisation) compared to North America and Europe.

Figure 1: Labour and Fuel Cost Shares, by Region of Airline Registration



OUTLOOK

- IATA's December 2009 Financial Forecast (see: www.iata.org/economics) expects that fuel prices will increase, but on average remain lower than 2008, over the next two years, with an average price per barrel of jet fuel of US\$87.0 in 2010 and US\$90.0 in 2011. At a global level, **fuel's share of total operating costs is expected to decrease slightly to 26% in 2010 before growing to 27% in 2011**. The decline in 2010 reflects a combination of lower fuel prices (compared to 2008 level), greater efficiencies in fuel use and cost reduction as the industry facing lower demand and revenue. High unemployment should keep wages from rising and economic recovery should improve productivity. Labour costs should not rise much in absolute terms, but labour share may increase.