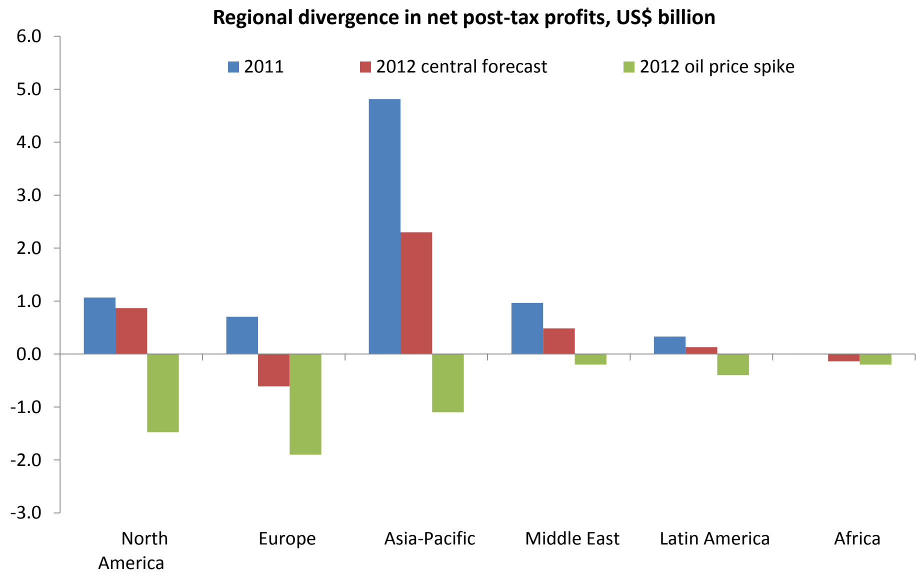
FINANCIAL FORECAST

March 2012

FRAGILE OUTLOOK FOR AIRLINE PROFITABILITY

- We have cut our forecast for airline profits in 2012. Not by a lot, but the sharp rise in oil and fuel prices since the December forecast has caused us to downgrade our forecast for net profits this year from $3.5 billion to $3 billion. The downgrade would have been larger but macro-economic conditions appear to have improved. The major risk we feared in December, of a significant worsening in the Eurozone crisis, appears to have been averted for a while, with the provision of liquidity by the European Central Bank and a second bailout for Greece. The US economy and the confidence of the US consumer also have improved. This has limited the downside for growth in air travel and cargo. Support for profitability this year has also come from slower growth in capacity, based on announced schedules, than we had previously expected. We now expect load factors to marginally improve this year, rather than decline, supporting both yields and unit revenues.



Source: IATA

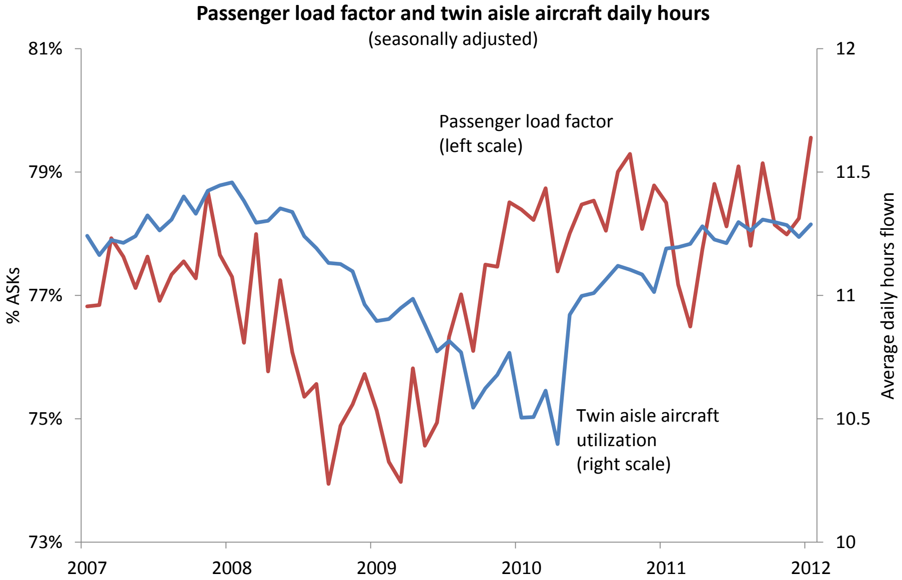
- Asia-Pacific airlines have performed well in this environment, particularly the Chinese airlines, raising our estimate for industry net profits in 2011 to $7.9 billion. European airlines have been under downward pressure from weak economic growth in the euro-zone. The average oil price we expect this year has been revised up from $99/b to $115/b in our central forecast, and we estimate the impact of a spike to $150/b in the second half of 2012 (resulting in a $135/b average). Because global economic growth has already slowed near the 2% rate at which the industry has historically slipped from profit to loss, the extra cost this would bring, in the 'oil price spike' scenario, could push the airline industry into losses exceeding $5 billion.

System-wide global commercial airlines	EBIT margin, % revenues					Net profits, $ billion				
	2009	2010	2011E	2012F		2009	2010	2011E	2012F	
				Central forecast	Oil price spike				Central forecast	Oil price spike
Global	**0.4%**	**4.0%**	**2.7%**	**1.3%**	**-0.6%**	**-4.6**	**15.8**	**7.9**	**3.0**	**-5.3**
Regions										
North America	1.2%	4.7%	2.7%	2.0%	0.0%	-2.7	4.1	1.1	0.9	-1.5
Europe	-2.2%	1.9%	1.1%	0.3%	-1.6%	-4.3	1.9	0.7	-0.6	-1.9
Asia-Pacific	2.8%	6.0%	4.7%	2.0%	0.0%	2.6	8.0	4.8	2.3	-1.1
Middle East	-1.5%	3.6%	3.4%	1.9%	0.1%	-0.6	0.9	1.0	0.5	-0.2
Latin America	2.8%	5.0%	2.4%	1.8%	0.0%	0.5	0.9	0.3	0.1	-0.4
Africa	-1.2%	1.6%	0.8%	-0.3%	-1.2%	-0.1	0.1	0.0	-0.1	-0.2

Source: ICAO data 2009-10. IATA estimates for regions in 2010. IATA estimates for 2011 and forecasts for 2012.
Note: ICAO have substantially revised 2008 and 2009 data. Regions may not add exactly to global totals due to rounding.

ASSET UTILIZATION SUSTAINED SO FAR

- A key reason for the relatively good performance of the passenger business in most regions during 2011 was that airlines managed to sustain asset utilization. As with all capital intensive industries with significant fixed costs, keeping the utilization of assets high is always critical for profitability – unless yields have been slashed to do so, and there is little evidence of that to date. Early in 2011 load factors were depressed by shocks hitting Japan and North Africa, but during the second half of the year airlines managed to pull load factors and aircraft utilization close to or above pre-recession levels.

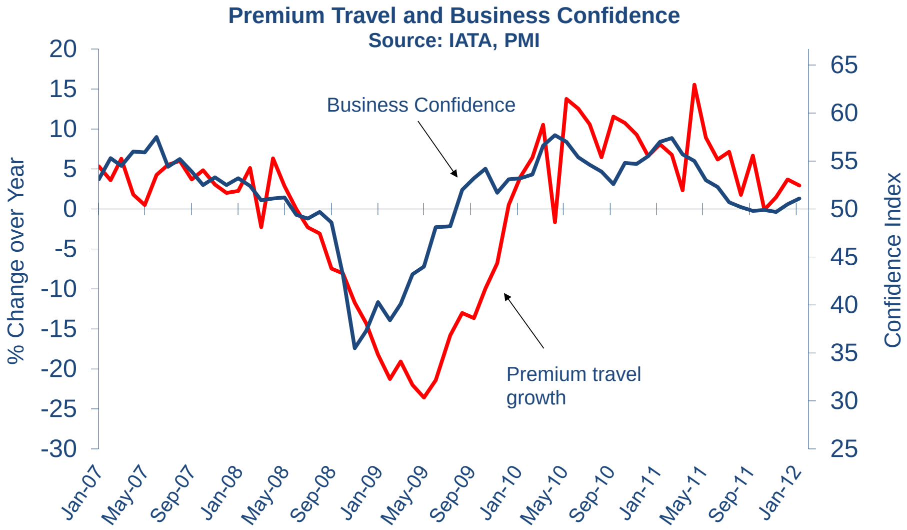


Source: IATA, Boeing

- Utilization rates have been much harder to sustain in the cargo business, despite some decline in yields during the second half of the year. Freight load factors were 6% points lower in January this year than the 2010 peak and average hours flown by freighters were down 11%. Falling asset utilization, declining yields from mid-year and the second half weakness in freight markets made cargo a more difficult business in which to sustain profitability than the passenger business.

SIGNS OF SUPPORT FOR BUSINESS TRAVEL

- One important development since our December forecast has been a modest improvement in business confidence in many of the larger economies. Companies in the US have been creating jobs at a faster pace and the threat of a significant deterioration in the Eurozone crisis seems to have been averted for a while (we assume throughout 2012). As the chart shows, this uptick in confidence is consistent with further growth, albeit in low single figures, of business travel and the important premium travel segment.



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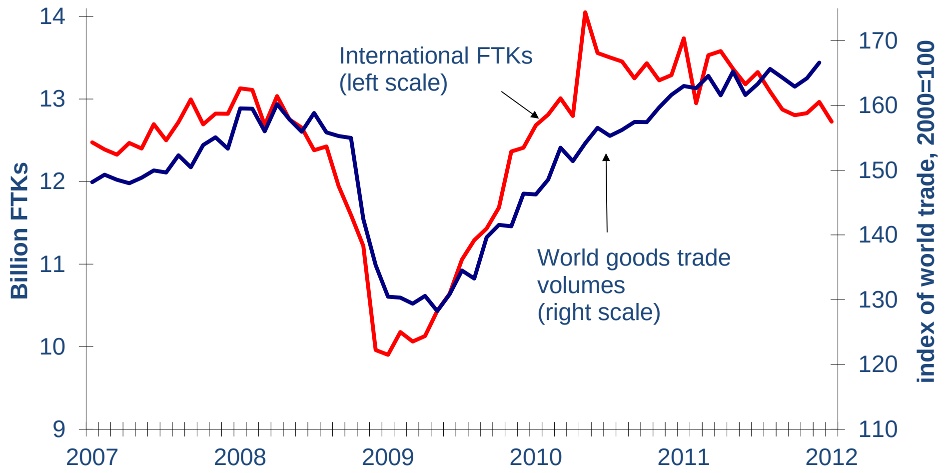
Source: IATA

FREIGHT MARKETS STABILIZING

- As well as a stabilization of the slowdown in business travel, there were also signs that the shrinkage of freight volumes was leveling out at the end of last year. The picture was clouded in January by the impact of January factory closures due to the earlier Chinese New Year, but once that is allowed for, the Q4 stability looks to have carried over into early 2012.

World trade in goods and air FTKs
Source: Netherlands CPB and IATA



Source: IATA, Netherlands CPB

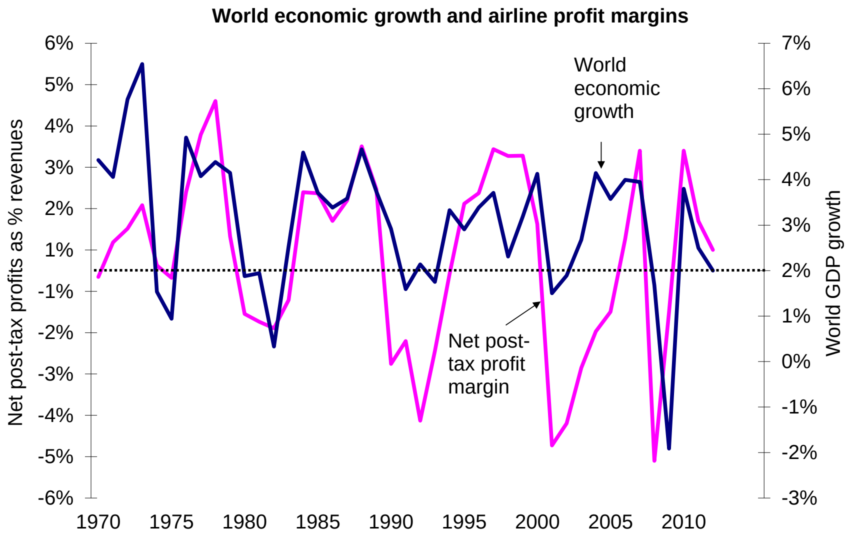
- A decline in air freight is often seen as a precursor to weakness in passenger markets and the wider economy. That does not seem to be the case this time. Although air freight has shrunk during the second half of last year, world trade overall continued to expand. There is also no sign of any business inventory overhang that would usually precipitate a substantial cutback in air freight. This pattern of falling air freight but rising sea freight looks to be due to the current pattern of economic growth, with strong Asian economies buying bulk commodities but weak western consumer spending on high value/ low volume goods.
- Purchasing managers have signaled that they are less pessimistic than they were in the third quarter. The next few months for air freight are likely to be flat. However, while Europe remains weak, the confidence of US consumers has risen significantly in recent months. The second half of 2012 is expected to bring a moderate upturn in air freight volumes as a result.
- There will also be the rebounds from the impact of Japan's tsunami and earthquake to give a boost to Asia-Pacific RTKs (cargo + passengers) in 2012, and a similar boost to traffic for African airlines from the rebound in travel following the civil unrest earlier in 2011. All other regions will see slower traffic volume growth this year, in line with slower economic activity. The North American airlines are expected to see the slowest growth in volumes, but that is partly due to restraint on the capacity side. European airlines will suffer the impact of many European economies being in deep recession this year.
- One significant change in this forecast from December is on the capacity side. In December we had expected weaker economic growth to undermine demand faster than airlines would be able to slow capacity growth. Judging from the schedules published for 2012, we underestimated the responsiveness of the industry. In this forecast we expect capacity to grow at a slower pace than demand, producing a supply-demand environment that will limit the damage to profitability from high jet fuel prices in our central forecast. That situation does however change for the worse in the 'oil price spike' scenario.

System-wide global commercial airlines	Traffic (RTK), % change over year					Capacity (ATK), % change over year				
	2009	2010	2011E	2012F		2009	2010	2011E	2012F	
				Central forecast	Oil price spike				Central forecast	Oil price spike
Global	-4.3	10.4	4.0	3.6	2.9	-3.5	5.2	5.6	3.2	2.8
Regions										
North America	-6.3	9.9	1.7	1.7	1.0	-5.6	3.9	2.8	0.5	0.0
Europe	-7.7	5.0	6.7	2.6	1.9	-5.4	1.5	8.5	2.9	2.5
Asia-Pacific	-2.2	12.6	2.5	4.5	3.7	-4.8	5.8	4.3	3.9	3.5
Middle East	9.5	20.0	8.3	8.8	8.1	11.1	15.8	10.5	8.5	8.1
Latin America	0.0	14.5	9.8	7.2	6.4	1.4	9.6	8.2	6.7	6.3
Africa	-5.4	15.0	-0.7	4.5	3.8	-1.5	9.5	2.5	3.9	3.5

Source: ICAO data to 2009. IATA 2010-11 estimates, 2012 forecasts. Dom.and int. traffic. Includes pax and cargo by weight.

BUT OUTLOOK PUT AT RISK BY OIL PRICES

- In December we saw the major risk facing the outlook to airline profitability as coming from the sovereign debt crisis in the euro-zone. Liquidity from the European Central Bank and a second Greek bailout has not resolved this problem, but has probably pushed this risk beyond 2012. However, sharply rising oil prices have replaced Eurozone debt as the major downside risk in 2012. We have already revised up our central forecast for oil prices to $115/b. However, a number of commentators have pointed to a scenario where an escalation of the crisis in Iran, with the closure of the Straits of Hormuz, pushes oil prices to $150/b in the second half of the year. That would mean an average of $135/b for 2012.
- The 'oil price spike' scenario below shows that, since global GDP growth is already close to the 2% rate at which airline profits have turned to loss, we estimate a $135/b oil price could lead to losses of $5.3 billion.



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Source: IATA, ICAO, Haver

System-wide global commercial airlines	2003	2004	2005	2006	2007	2008	2009	2010	2011E	2012F	
										Central forecast	Oil price spike
REVENUES, $ billion	322	379	413	465	510	570	476	547	598	633	637
% change	5.2	17.7	9.1	12.5	9.6	11.7	-16.5	14.9	9.4	5.9	6.5
Passenger	249	294	323	365	399	444	374	425	468	498	500
Cargo	40	47	48	53	59	63	48	66	69	72	73
Traffic volumes											
Passenger growth, tkp, %	2.3	14.9	7.0	5.0	6.4	1.5	-2.1	7.3	5.9	4.2	3.2
Sched passenger numbers, millions	1,849	2,064	2,211	2,325	2,518	2,507	2,479	2,681	2,835	2,948	2,920
Cargo growth, tkp, %	3.9	7.9	0.4	4.8	4.8	-1.0	-9.8	18.7	-0.6	2.2	2.0
Freight tonnes, millions	33.5	36.7	37.6	40.0	42.0	41.0	40.7	48.0	47.6	48.6	48.5
World economic growth, %	2.8	4.2	3.4	4.0	3.8	1.7	-2.3	3.9	2.5	2.0	1.7
Passenger yield, %	2.4	2.6	2.7	7.8	2.7	9.5	-14.0	6.1	4.0	2.0	3.5
Cargo yield %	2.0	7.4	2.4	5.9	5.5	7.4	-14.2	15.0	5.5	2.0	3.5
EXPENSES, $ billion	323	376	409	450	490	571	474	525	582	625	641
% change	4.0	16.2	8.9	10.1	8.8	16.5	-16.9	10.7	10.8	7.5	10.1
Fuel	44	65	91	117	135	189	125	139	177	213	231
% of expenses	14	17	22	26	28	33	26	26	30	34	36
Crude oil price, Brent, $/b	28.8	38.3	54.5	65.1	73.0	99.0	62.0	79.4	111.2	115.0	135.0
Jet kerosene price, $/b	34.7	49.7	71.0	81.9	90.0	126.7	71.1	91.4	127.5	132.3	155.3
Non-Fuel	279	311	318	333	355	382	349	386	405	413	410
cents per atk (non-fuel unit cost)	38.9	39.5	38.6	38.9	39.3	41.8	39.6	41.6	41.3	40.8	40.7
% change	0.3	1.4	-2.1	0.8	0.8	6.4	-5.2	5.1	-0.7	-1.3	-1.5
Break-even weight load factor, %	61.1	61.9	62.0	61.2	60.9	63.2	62.3	63.1	62.9	64.1	65.1
Weight load factor achieved, %	60.8	62.5	62.6	63.3	63.4	63.1	62.6	65.7	64.7	65.0	64.7
Passenger load factor achieved, %	71.5	73.4	74.9	76.1	77.7	76.0	76.0	78.4	78.1	78.7	78.2
OPERATING PROFIT, $ billion	-1.4	3.3	4.4	15.0	19.9	-1.1	1.9	21.7	16.2	8.2	-3.7
% margin	-0.4	0.9	1.1	3.2	3.9	-0.2	0.4	4.0	2.7	1.3	-0.6
NET PROFIT, $ billion	-7.5	-5.6	-4.1	5.0	14.7	-26.1	-4.6	15.8	7.9	3.0	-5.3
% margin	-2.3	-1.5	-1.0	1.1	2.9	-4.6	-1.0	2.9	1.3	0.5	-0.8

Source: ICAO data to 2009-10. IATA some 2010 estimates. IATA estimates for 2011 and forecasts for 2012. Passenger and freight numbers are global system-wide collected by IATA, including some non-ICAO states. Note ICAO has substantially revised their 2008-09 financial data. Their recent release of 2010 financial data replaces IATA's estimate.