

# IATA ECONOMICS BRIEFING

## AIRLINE BUSINESS CONFIDENCE INDEX

### OCTOBER 2009

#### KEY POINTS

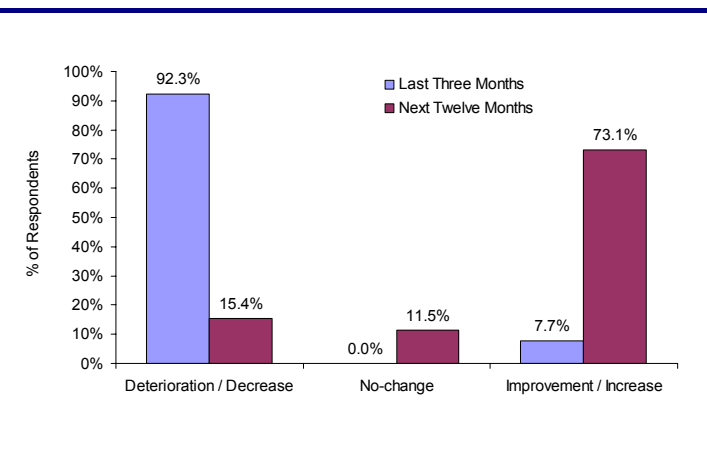
- Airlines reported further weakness in financial and market conditions during the third quarter. However, the rate of deterioration did appear to stabilise. Moreover, confidence among airline CFOs and heads of cargo that conditions will improve during the next twelve months rose markedly in October, compared to the previous survey in July.
- The charts below show clearly that the improvement in confidence so far is just that. With the exception of improved passenger numbers and freight tonnes, the experience of the third quarter was that at best there was no further deterioration. The gain in confidence for the future appears to be supported by evidence of rising economic growth and, so far, capacity restraint which is raising load factors and tightening supply-demand conditions. Both of these supports are fragile given the uncertainties still ahead.
- Most notable in these survey results is the size of the improvement in airline confidence for the next 12 months. Note however that some results need careful interpretation. Over 73% of airline CFOs said that profitability over the next 12 months will improve (the sample included major airlines in Asia, Europe and the Americas). That does not mean loss will turn into profit. It does mean that smaller losses are expected.
- Rising economic growth is boosting expectations of traffic volumes, which has started to occur. Improving load factors have generated confidence that yields will improve, which has yet to be seen. More stable fuel prices and further job cuts have stabilised both expected and reported costs. This does look like a turning point, but at present one more based on fragile expectations for the future than the reality of current market experience.

#### PROFITABILITY OUTLOOK

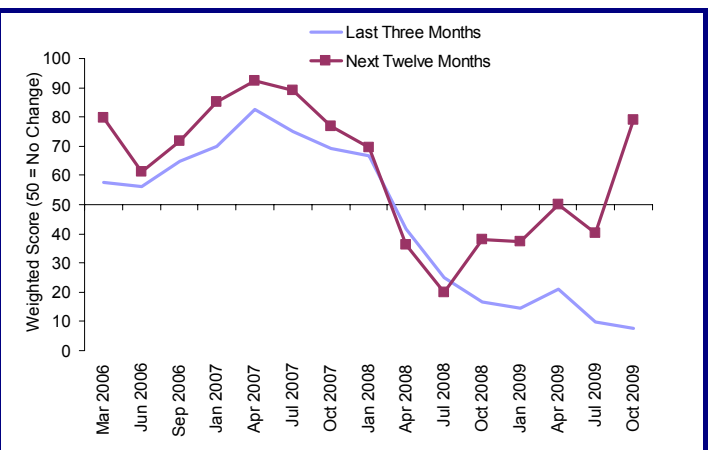
- Airline profitability continued to weaken through the third quarter. The ongoing effect of weak demand was compounded by low yield levels across the passenger and cargo business over the last quarter. More than 90% of respondents indicated that profitability fell. On a weighted average basis (with 50 representing no-change, and values below 50 signalling a greater balance of negative views), the score for profitability over the previous three months is 7.7, still well in negative territory.

**How has profitability changed? How do you expect it to change over the next twelve months?**

**a) October 2009 survey**



**b) Compared to previous surveys**



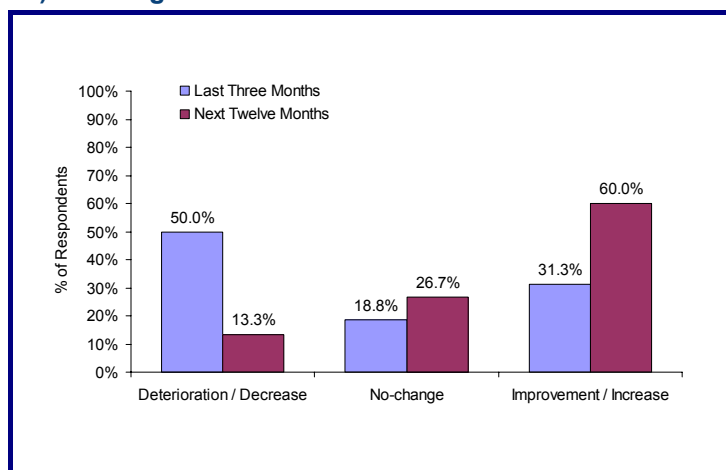
➤ The big change in this survey has been a swing from July when over 46% of airlines were expecting a further deterioration in profitability over the next year, to over 73% now expecting an improvement. Note that this does not mean that a return to profit is expected. It does mean that the majority are now expecting losses to diminish over the next 12 months. There was a positive majority in all regions surveyed. However, there was a notable difference in responses between airlines in Asia and Europe. All the airlines in Asia expected an improvement, whereas a significant minority of European airlines expected a further deterioration.

## DEMAND GROWTH

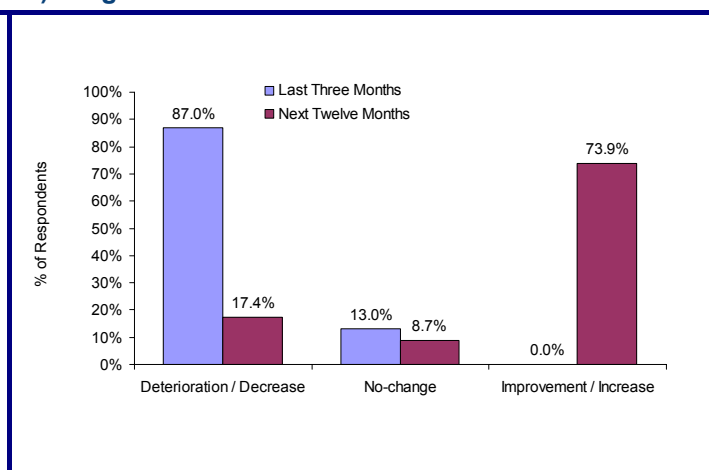
➤ Half of survey respondents still report declines in passenger volumes over the last three months – compared to levels in the same quarter a year ago. However this is a smaller number than recorded in our July survey and over 30% now report increases, consistent with the improvement seen in the data in recent months. The outlook for passenger traffic over the 12 months ahead is improving with 60% now expecting increases over that period. Respondents note improving economic outlook as the key driver of renewed optimism. On a weighted average basis, the outlook for passenger demand for the 12 months ahead is 73.3 – well up on July's first foray back above the '50' no change line. This is consistent with a continuation of the recent rise in passenger numbers.

### Recent and expected change in traffic volumes

#### a) Passenger

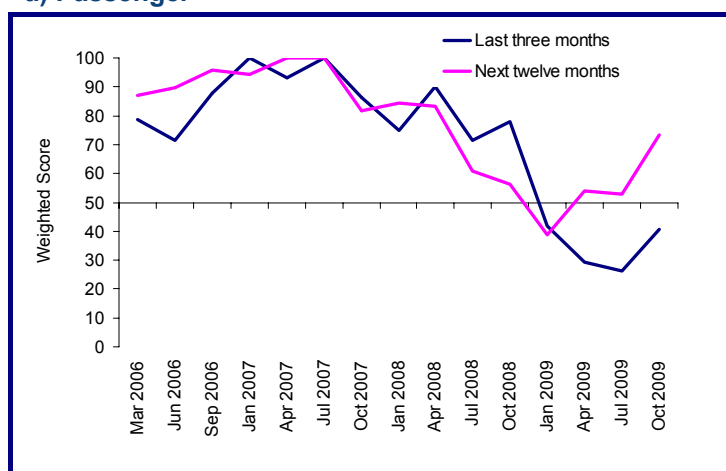


#### b) Cargo

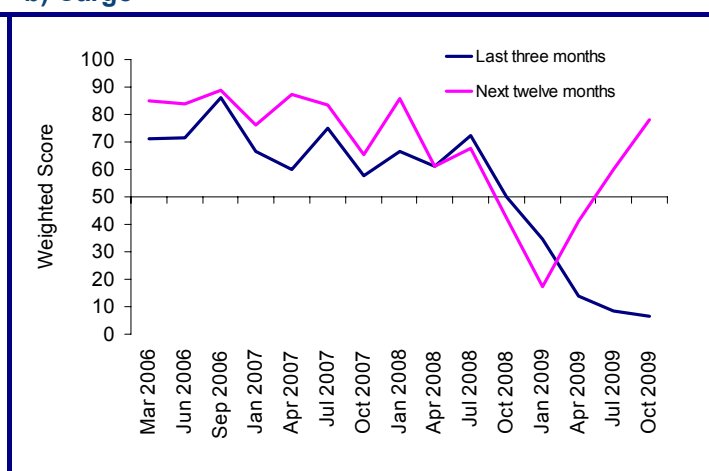


### Compared to previous surveys

#### a) Passenger



#### b) Cargo



➤ There has been a strong rise in outlook for cargo traffic. Almost three quarters of respondents now expect freight volumes to rise over the next year – up from just over half last survey. However, again the survey results need to be interpreted with care. The 'next 12 months' results report expectations of improvement relative to current levels. The improvement in responses to this question for cargo are back to 2007 levels, but that does not mean a return to 2007 cargo volumes. It does mean the same proportion of airlines today as in 2007 expect

cargo volumes to improve, but it will be some time before traffic volumes approach pre-recession levels once more.

- Air freight typically picks up early in the recovery cycle as businesses replenish inventories. A shift to holding less stock post-recession could also support air freight activity as more frequent, albeit smaller, shipments would be required. There was only a small fall in the proportion of respondents reporting decreased cargo volumes over the last three months. Conditions in the cargo market still remain difficult. Domestically focused fiscal stimulus measures may be contributing to the relative boost in passenger markets over trade-related freight volumes in the early part of this recovery.

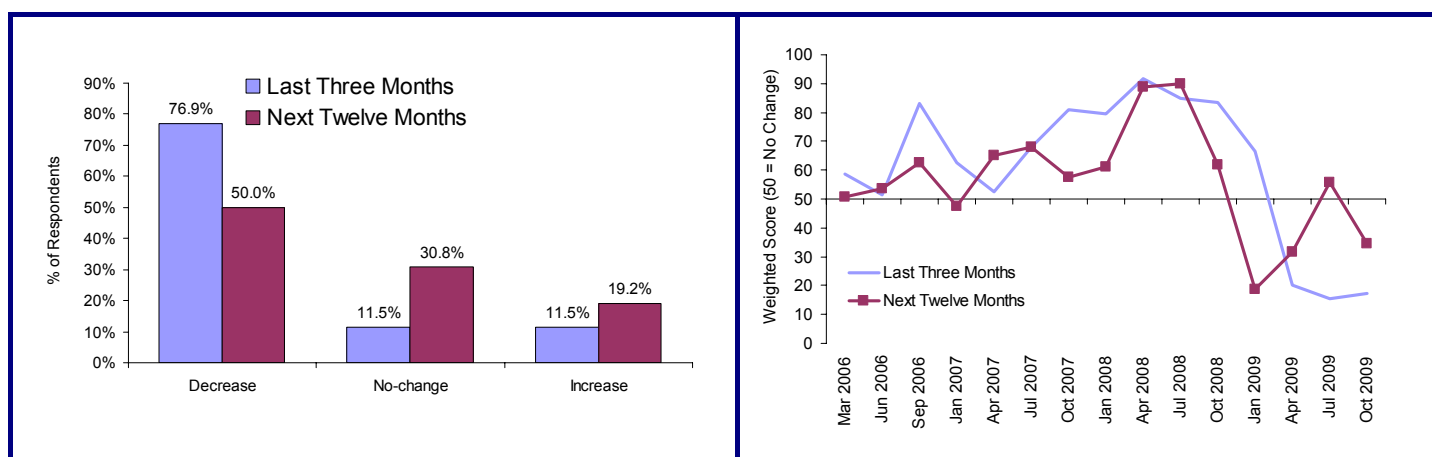
## INPUT COSTS

- Costs continued to fall for over three-quarters of respondents during the last three months. Airlines indicate that cost reduction initiatives launched earlier in the year continue to bear fruit. These mainly relate to network and staff restructuring. The fall in the US dollar has helped offset some of the recent rise in oil prices for many and jet fuel remains well below prices seen during the third quarter of 2008. On a weighted average basis, the score of 17.3 for the input cost trend is only slightly higher than indicated in July.
- Looking ahead, some respondents worry of further fuel price pressures related to increases energy demand during the recovery. However the balance of responses suggest that input costs will not rise rapidly over the year ahead. On a weighted average basis, the score for the outlook in unit input costs has moved below 50 again to 34.6 which reverses the trend evident during the first half of this year. Increasingly weak labor market conditions may offer airlines more opportunity to realise cost efficiencies in this area. Further capacity reductions may also offer savings if they can be achieved by removing aircraft from service rather than simply flying the existing fleet less. Spreading the same fixed aircraft costs over fewer flight hours will drive up unit costs.

How have your unit input costs changed? How do you expect them to change over the next twelve months?

a) October 2009 survey

b) Compared to previous surveys



## YIELD ENVIRONMENT

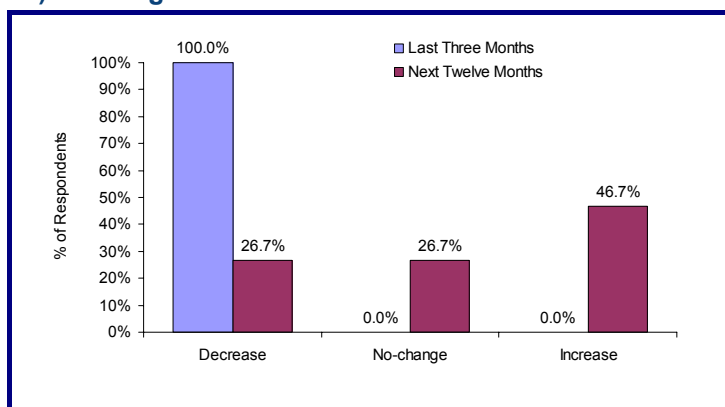
- Airlines continued to face severe downward pressure on passenger yields during the third quarter, compared with levels a year earlier. Respondents were unanimous in reporting declines in yield performance. Reduced fuel surcharges and recession led-demand weakness leading to low load factors were the key drivers. The critical need to generate cash during this crisis has also contributed as airlines have slashed premium and economy fares alike to fill seats and preserve cashflow.
- In contrast to current conditions, the outlook for the year ahead has improved with the balance of responses now indicating that yields should increase. On a weighted average basis, the score for the outlook in yields has moved up to 60 – above the 50 ‘no change’ mark for the first time since last year’s financial crisis. Load factors

have begun to return to more normal levels as capacity cuts meet the beginnings of traffic recovery and this will support stabilization of yields and – eventually – increases.

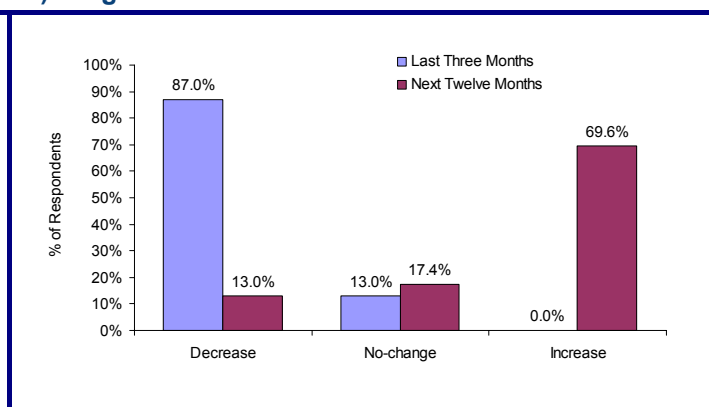
- Cargo yields also continued to fall over the last three months – relative to a year ago - with still more than 80 percent of respondents reporting decreases on the back of strong competition. However the outlook for the next 12 months has improved sharply with almost 70% of respondents expecting increases in freight rates. As in the passenger business, load factors are rising once more and, if it continues, this should provide the market conditions for some improvement in yields during the year ahead.

### Recent and expected change in yields

#### a) Passenger

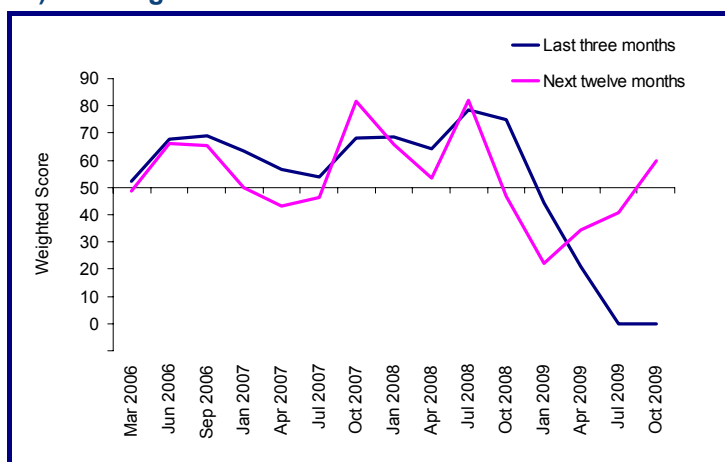


#### b) Cargo

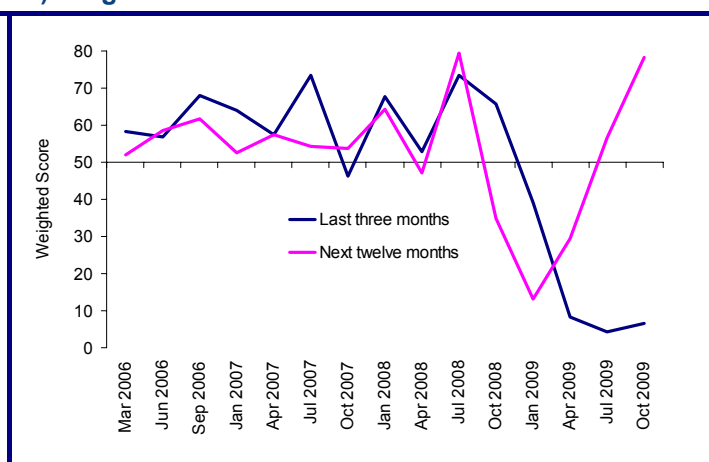


### Compared to previous surveys

#### a) Passenger



#### b) Cargo



## EMPLOYMENT

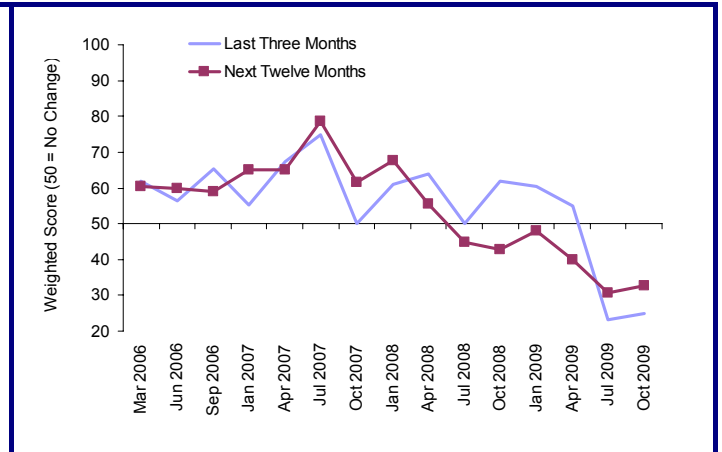
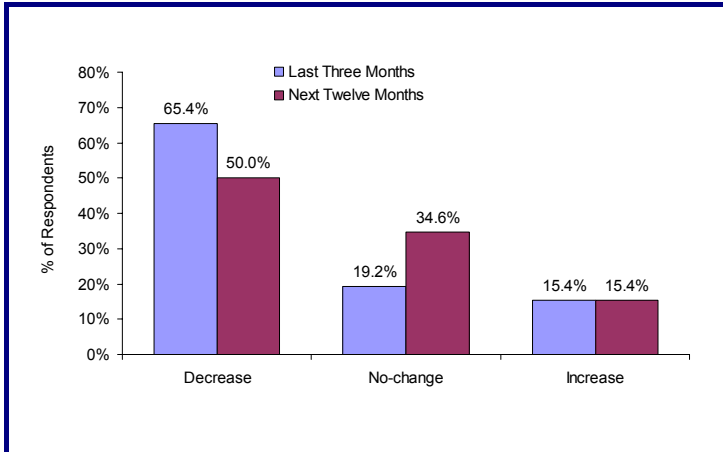
- Employment trends tend to lag the cycle in air traffic and airline profits, as airlines need to restructure after recessions to reduce losses. While there are early indications of an upturn in traffic volumes, the downward movement in employment levels reported in July has continued during the last quarter. A similar proportion of respondents reported employment reductions in this survey and the weighted average employment indicator remains well in negative territory. Recruitment freezes remain in place in many airlines leading to headcount reduction from normal staff turnover. However some carriers are explicitly executing strategies to become smaller and leaner to meet changing market conditions now and into the future.
- Half of all respondents expect to reduce headcount further over the year ahead. A further third expect 'no change' in employment levels over this period. This holds the weighted average score for change in employment levels near the lows reported in July's survey and does not bode well for employment prospects in the industry. Several respondents cite intentions to implement early retirement programs which will drive a part of expected reductions to come. Airlines, like employers in the wider economy, will also be seeking productivity

improvements from existing workforce before embarking on new hiring activities. This may delay an upturn in industry employment for some time.

**How has your employment level changed? How do you expect it to change over the next twelve months?**

**a) October 2009 survey**

**b) Compared to previous surveys**



IATA Economics  
October 2009  
E-Mail: [economics@iata.org](mailto:economics@iata.org)