MONTHLY TRAFFIC ANALYSIS
DECEMBER 2008

KEY POINTS

- December saw an unprecedented 22.6% decline in air freight volumes, compared with the previous year. This was significantly worse than September 2001 when the grounding of much of the international fleet following the 9-11 terrorist attacks caused a 13.9% fall in air freight. The collapse in the airlines industry's freight business is a reflection of 20-30% declines in export and import volumes being reported across Asia, North America and Europe as the global recession plumbs new depths in December.
- Air freight had been expanding at a pace of around 4% earlier in the year but the precipitous fall in volumes during the second half took the level for 2008 as a whole 4% lower than 2007.
- Air travel did not fall quite so precipitously in December but that may only reflect booking made for travel in the holiday season several months earlier when the economic situation was not quite so bad. International passenger volumes (RPKs) fell 4.6% in the 12 months to December, led by a 9.7% decline for Asia-Pacific airlines. For the year as a whole 2008 saw an increase in passenger travel of just 1.6%, compared with the 7.4% pace of expansion seen during 2007.
- With the notable exception of the Middle East, and to a lesser extent Latin America, airlines around the world are now cutting capacity in an attempt to shrink their cost base to match dwindling revenues.
- However, attempts to cut capacity are lagging the slump in air travel and as a result load factors fell sharply in December, down 2.4% points to 73.8% on average with the largest falls for Asia-Pacific airlines, where travel demand fell almost 10%, and for Middle Eastern airlines, whose capacity expanded by 10%.
- The outlook for 2009 is bleak since there was no sign in the December data that a bottom has been reached, and forward-looking business and consumer confidence surveys suggest further weakness in the months ahead. Given the pace of deterioration at the end of 2008 the risks to our forecasts for 2009 (a 3% fall in passenger volumes, air freight down 5% and global airline revenues down 6.5%) are clearly on the downside.

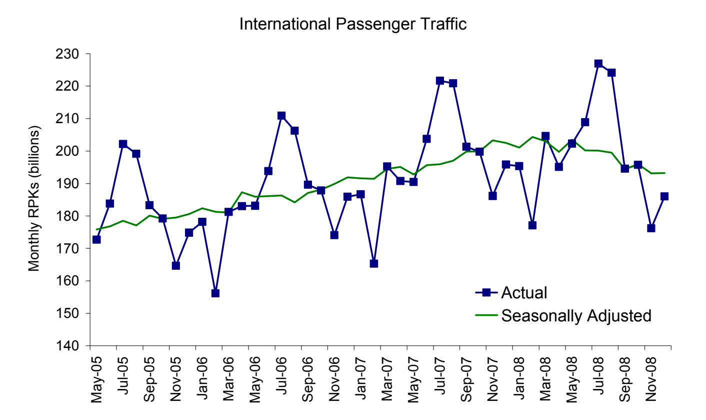
	Dec 2008 vs. Dec 2007					YTD 2008 vs. YTD 2007				
	RPK Growth	*ASK Growth*	*PLF*	*FTK Growth*	*ATK Growth*	*RPK Growth*	*ASK Growth*	*PLF*	*FTK Growth*	*ATK Growth*
Africa	-4.6%	-2.1%	68.5	-8.0%	-6.8%	-4.0%	-4.2%	70.2	-2.5%	-7.4%
Asia/Pacific	-9.7%	-5.6%	72.6	-26.0%	-10.7%	-1.5%	1.2%	73.9	-6.6%	-2.5%
Europe	-2.7%	-1.5%	73.8	-21.2%	-4.1%	1.8%	3.8%	76.6	-2.8%	2.9%
Latin America	1.1%	3.2%	71.9	-23.7%	-1.8%	10.2%	9.2%	74.0	-13.5%	5.7%
Middle East	3.9%	10.0%	73.0	-9.2%	5.1%	7.0%	8.6%	74.9	6.3%	8.5%
North America	-4.3%	-0.7%	78.1	-22.2%	-3.4%	2.9%	4.3%	79.8	-1.9%	3.4%
Industry	-4.6%	-1.5%	73.8	-22.6%	-5.4%	1.6%	3.5%	75.9	-4.0%	1.5%

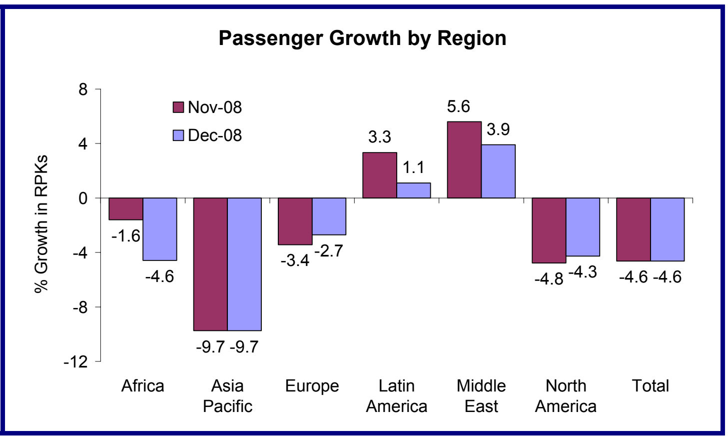
INTERNATIONAL PASSENGER TRAFFIC DOWN 4.6%

- There was a further significant decline in international air travel during December, with total international revenue passenger kilometres down 4.6% over the same month in the previous year. This follows a similar decline in November and brings the total for 2008 to a level just 1.6% higher than 2007. The slump in international air travel since the middle of last year has not yet matched the double-figure declines seen after 9-11 and SARS, but is considerably down on growth around 5% in the first half of last year and the 7.4% pace of growth in 2007.
- The largest decline at the end of last year was seen for Asia-Pacific airlines, whose traffic was down 9.7% on the year. The fall of air travel in this region has been so sharp in the past six months that total RPKs in 2008 carried

by Asia-Pacific airlines was actually 1.5% lower than in 2007, a result that would not have been expected earlier last year given the economic expansion of emerging economies such as China and India. However, while the credit crunch and ensuing economic crisis may have originated in the US, economies in Asia are now deteriorating extremely quickly. Korea's GDP fell 5.5% in the fourth quarter compared to the third i.e. the economy was shrinking at an annualised rate of over 20%. Chinese Taipei's economy also appears to be declining at an alarming pace with industrial production suggesting a 15% decline at the end of last year. Weakness is seen both in consumer spending in the region and particularly in foreign trade; export volumes during December were down 20% over the year in Singapore and by 35% in Japan. The Chinese economy does not seem to be shrinking but is certainly slowing, with surveys showing consumer confidence down to levels last seen during SARS.

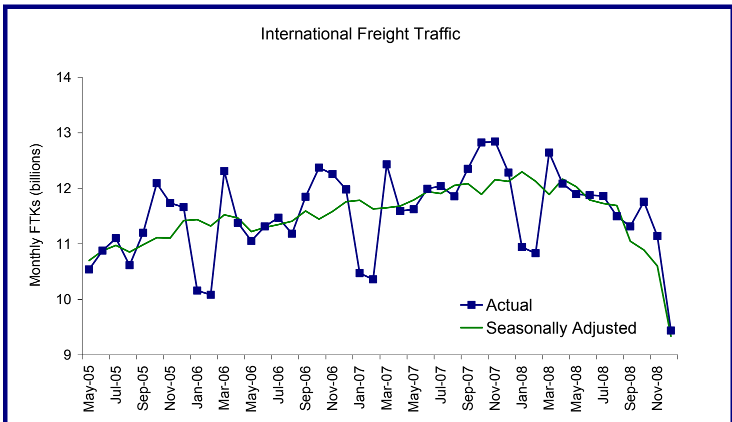
- Of the major regions, second weakest in December was traffic carried by North American airlines, whose international RPKs were 4.3% lower than a year earlier. US airlines have been pre-emptively cutting capacity on domestic markets at a rate of over 10% a year for several months now but were still adding capacity on international markets through November. December marked the first month the US airlines began to cut capacity on these markets but, unlike their actions on domestic markets, at a much slower pace than the slump in air travel demand. Much of the growth by US airlines has been on the newly liberalized N Atlantic markets with a 10% boost to capacity in 2008. However, this market was shrinking by 1.1% in December according to results from ATA airlines. Much weaker were markets across the Pacific, reflecting deepening recessions in both Asia and the US, with traffic carried by US airlines down 8.4% in December according to the ATA. The US economy was clearly worsening at the end of last year with retail spending down 9.8% on the year in December, and widespread expectations of a 5%+ fall in Q4 GDP.
- Airlines in Europe fared slightly better compared both to airlines in other major regions and their performance in November. It is not clear the extent to which this was a temporary effect due to pre-booked holiday travel. Nonetheless, with a 2.7% decline in international RPKs, the European airlines are facing very weak markets. More detail can be gleaned from the AEA data which shows the weakest markets being cross-border European travel, which was down 4.8% in December reflecting the weakness of European economies. Travel to the Far East was down 2.9% and across the N Atlantic by 2.2%. There is no reason for optimism about European travel markets for the next few months. Business confidence surveys are consistent with a 10% decline in industrial production and export orders suggest a fall in foreign trade of around 20%.
- In other regions of the world the picture was mixed but not much better. African airlines continued to see their traffic fall, despite rather more robust economies and travel to the continent than other regions. As market share continued to be lost these airlines saw international RPKs decline 4.6% in December, taking the total for 2008 to a level 4% down on the previous year. This has been a marked deterioration from the 8% growth enjoyed by African airlines in 2007. Latin American airlines are also finding markets considerably tougher but still managed to grow international traffic by 1.1% in December, taking their total for 2008 to an industry beating 10.2% which was even better than their 8.4% growth in 2007. Now that commodities demand and trade with their N American neighbour is falling so sharply the months ahead are likely to be rather harder for airlines in this region. Knocked from their number one spot in 2007 for growth are the Middle Eastern airlines. They are also continuing to expand, despite the increasingly global recession, and expanding their international RPKs by 3.9% in December. Their growth in 2008 was the second strongest region at 7%, but that is a very much slower expansion than the 18.1% growth seen in 2007. Oil revenues had been propelling a strong economic expansion in the Middle East and the regions airlines had been expanding 6th freedom services on long-haul markets. Both of these sources of growth are now in decline, at least for the next year or so.

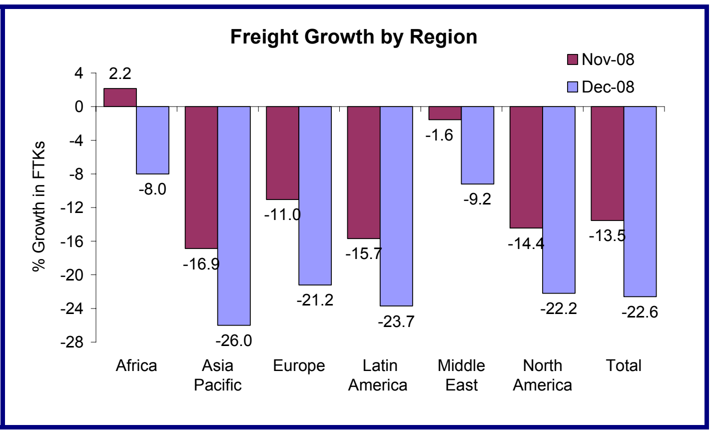




AIR FREIGHT VOLUMES COLLAPSE

- The most alarming decline in airline business was the unprecedented 22.6% fall in air freight volumes (FTKs) in December, compared to the same month the previous year. The largest monthly fall in the past 30 years was a 13.9% decline in September 2001 when the 9-11 terrorist attacks grounded so much capacity. Air freight is by no means recession proof but continued globalisation and differing economic cycles in different parts of the world had meant that, with the exception of 2001, volumes continued to grow or fell only modestly during economic downturns. However, this time it is clear that no region is providing any offsetting growth. Airlines in all three major regions saw their air freight volumes decline by more than 20% in December.
- International freight tonne kilometres began last year expanding at a pace of around 4% but so precipitous has been the decline since the middle of last year that the total for 2008 was 4% lower than 2007. There is no sign of a bottom as yet. The chart below shows the seasonally adjusted level of air freight which in December fell 22.6% over the previous December but 12% just in that month over November. Air freight is usually more volatile than world trade as shippers often shift to cheaper, though slower, transport modes as recessions reduce demand for time sensitive components. However, as described above the 20-30% year-on-year declines in export and import volumes in Europe, Asia and the US are consistent with the shrinkage seen in air freight.

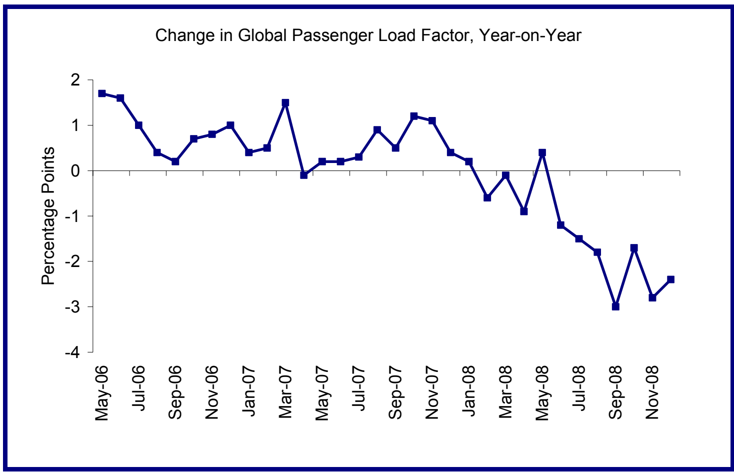


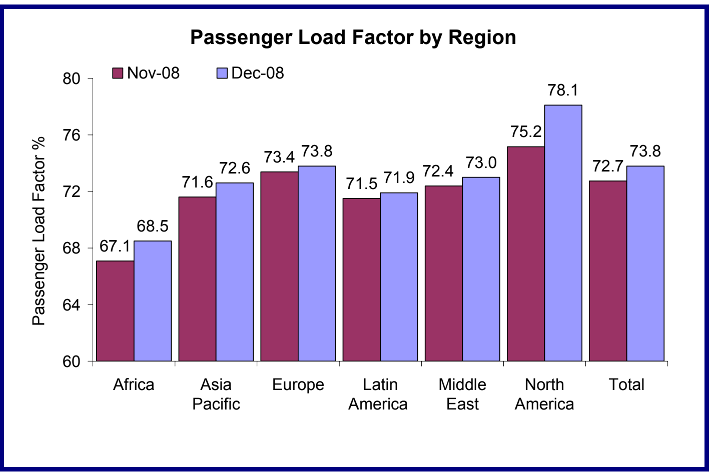


LOAD FACTORS DOWN AS FALLING DEMAND OUTPACES CAPACITY CUTS

- The slump in travel and air freight demand is causing a sharp fall in aircraft utilisation, despite the best efforts of airlines to shrink capacity to match demand, ending a significant trend increase in load factors from the lows of 2001. Overall capacity on international markets fell by 1.5% in December, which was over 3% points behind the 4.6% fall in demand. Regionally it is a more mixed picture but load factors are falling across the industry, with the exception of the US domestic market. Earlier in 2008 the industry was very much in an expansionary mode on international markets, particularly airlines from the US and the Middle East. It was not until the late summer, following the fuel price spike, that capacity plans were put sharply into reverse in most regions. As a result capacity on international markets was up 3.5% on average in 2008 but passenger load factors fell by 1.4% to an average of 75.9%.

- In the larger markets the biggest cuts in capacity during December were carried out by the airlines in the Asia-Pacific, with a 5.6% decline over the year. However, since traffic on international markets was shrinking by almost double that pace, these airlines saw the second largest regional fall in load factors with a 3.3% decline. The biggest fall was for Middle Eastern airlines who are continuing with their plans for expansion, despite the recession. A 10% rise in capacity in this region during December led to their load factors falling 4.3% points to 73%. Capacity is also still being expanded by Latin American airlines, with a 3.2% rise in December, but this is not quite so far from traffic demand and their load factors fell what by comparison seems a relatively modest 1.5%. The only market bucking this trend of falling load factors was the US domestic market where, according to ATA data, capacity was cut by 10.6% in the face of a 6.8% decline in traffic – boosting aircraft utilisation for US airlines on this market. However, the ATA also reported that yields fell in December for the first month in 2008. Lower fuel prices are helping to reduce travel costs but the fall in yields on both domestic US and international markets is a sign of the impact of the slump in travel demand, even in markets like the US domestic where airlines have been able to shrink the size of the industry even more than the fall in demand.
- Looking ahead into 2009 the signs are that travel will continue to shrink through the first half of the year, with few economic forecasts predicting any sort of upturn in the global economy before the third quarter. With yields now in decline the fall in airline revenues will be even larger than the fall in traffic volumes. Given the pace of deterioration at the end of 2008 the risks to our forecasts for 2009 (a 3% fall in passenger volumes, air freight down 5% and revenues down 6.5%) are clearly on the downside.





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