CARGO E-CHARTBOOK Q2 2009

KEY POINTS

- Developments since the first quarter eChartbook have been mixed. On a positive note air freight volumes do seem to have found a floor and have broadly moved sideways for the past four months. Markets and forecasters are now looking ahead to recovery, rather than further decline, but there is no visibility yet of any robust improvement though leading indicators are positive. On the negative side yields have slumped as capacity is trimmed rather than slashed and the strain is taken by much lower utilisation rates. Ocean shipping is gaining market share at the expense of air freight. Fuel costs are 60% down on last year but there is now a worrying rise in oil prices. First quarter results were very weak and with revenues likely to be down very sharply air cargo profitability may well deteriorate further in the short-term.

HEADLINES BY SECTION

Economic Outlook (page 2)

- Substantial stimulus from central banks and governments now seems to be getting the banks and financial markets working again. Credit spreads have narrowed. Recession may have reached a floor but a robust recovery remains uncertain.

Traffic Growth (page 3)

- Air freight volumes seem to have stabilised after hitting a low point in December. International markets are twice as weak as domestic but there is no protection from geographical diversification as falls are widespread.

Demand Environment (page 4)

- Leading indicators offer a moderately encouraging picture. Purchasing managers point to some rise in air freight volumes in the next few months. However, inventory overhang remains major headwind to recovery.

Revenue and Yields (page 5)

- Cargo volumes may be stabilising but excess capacity caused a 17% slump in yields in the first quarter. Revenues from cargo are expected to show a record decline in 2009 on both lower volumes and yields.

Costs (page 6)

- Jet fuel prices are 60% lower than a year ago and little higher than the start of the year, but crude oil prices are already $20/b up so far this year. Aircraft and labour costs falling but some airport charges are rising.

Capacity (page 7)

- Freighter fleet reduced by 99 aircraft so far this year but widebody capacity is up, as older aircraft are no longer being parked. Most of the strain of 20% loss of volumes is being taken by a 7% point fall in freight load factors.

Competition (page 8)

- Bulk commodity rates anticipate recovery but ocean container rates were down 39% in February. Container demand slumped in 2009Q1 but 15% falls are less than air freight as ocean shipping gains market share.

Profitability (page 9)

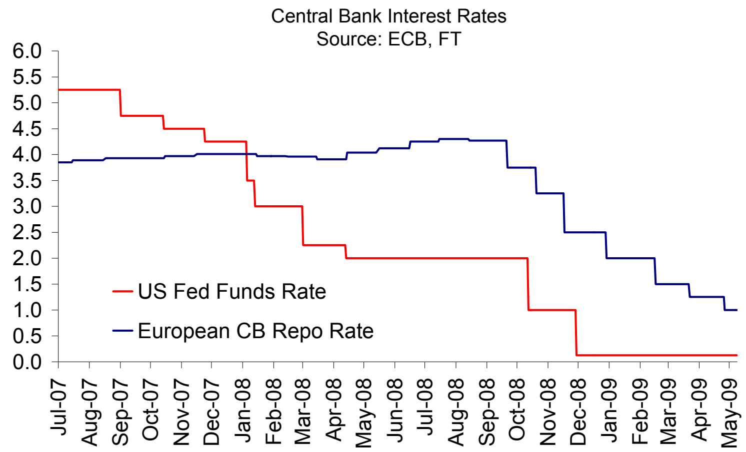
- Cargo profitability has been under extreme pressure from collapsing volumes and yields in the past six months. US cargo airlines have seen profits fall sharply and large losses have been reported in 2009Q1.

Economic Outlook

Key Issue:

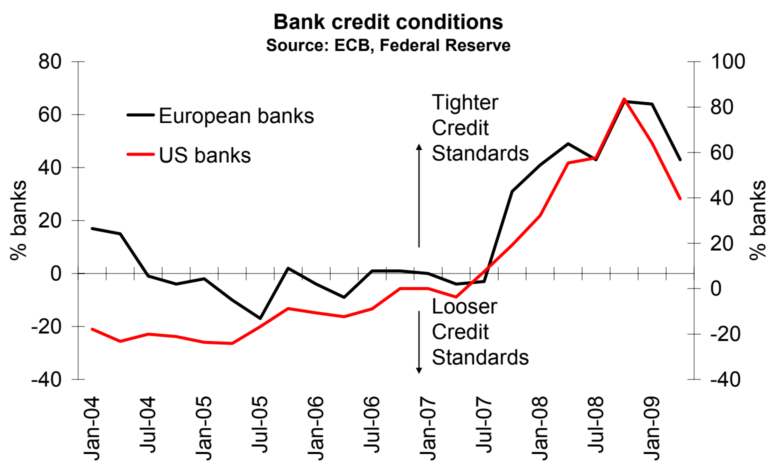
- Substantial stimulus from central banks and governments now seems to be getting the banks and financial markets working again. Credit spreads have narrowed. Recession may have reached a floor but a robust recovery remains uncertain.

Official interest rates cut to emergency levels and credit spreads now narrowing



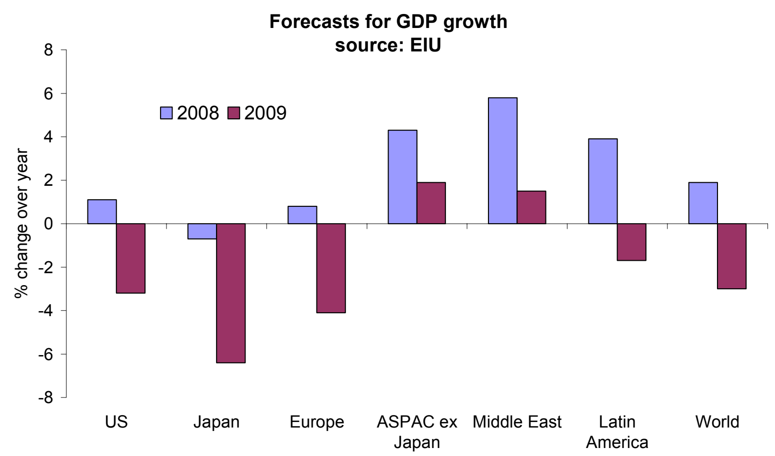
- Central banks around the world have now cut lending rates to zero or historically low levels, in an attempt to get bank credit flowing again. Additional monetary stimulus has been provided through ‘quantitative easing’ as central banks have directly injected liquidity by buying longer dated assets.
- The cost of debt is easing as government bond yields and credit spreads fall back. However, BB+ borrowers are still paying 7% for 10-year debt and 350bp over US treasuries.

The credit crunch is now starting to ease



- Bank credit and capital markets are starting to function in a more normal manner. A majority of banks are now easing credit conditions in the US and European banks are not far behind. Companies, including airlines, are also now starting to raise funds in debt and equity markets.
- However, with asset prices down 30% or so many households and firms will want to reduce debt, not borrow more. This will prove a major headwind to the recovery in spending and air freight.

The deepest recession since the 1930s is now forecast for this year



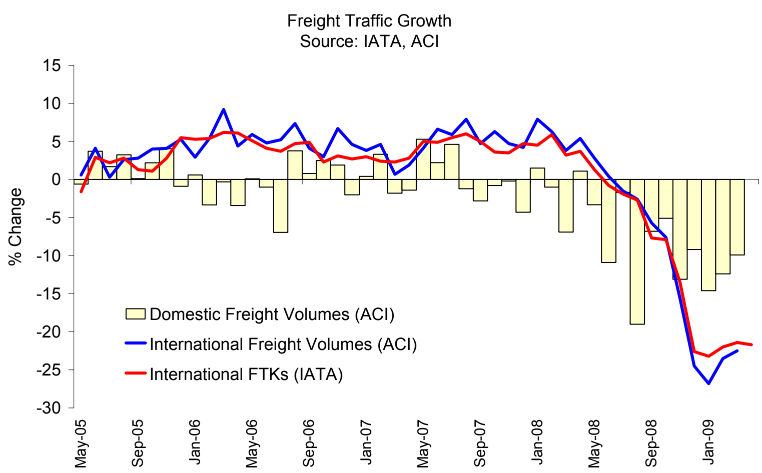
- Economic growth turned sharply negative in the final quarter of 2008 for most developed economies. In many cases 2009Q1 was also extremely weak with, for example, Japan’s economy shrinking at an annualised rate of over 15%, Germany by 14% and the US by 6%.
- Most forecasts expect output to now move sideways for some time with few expecting any upturn before the end of the year. Forecasts for 2010 are for an extremely weak upturn in growth.

Traffic Growth

Key Changes in the data this quarter:

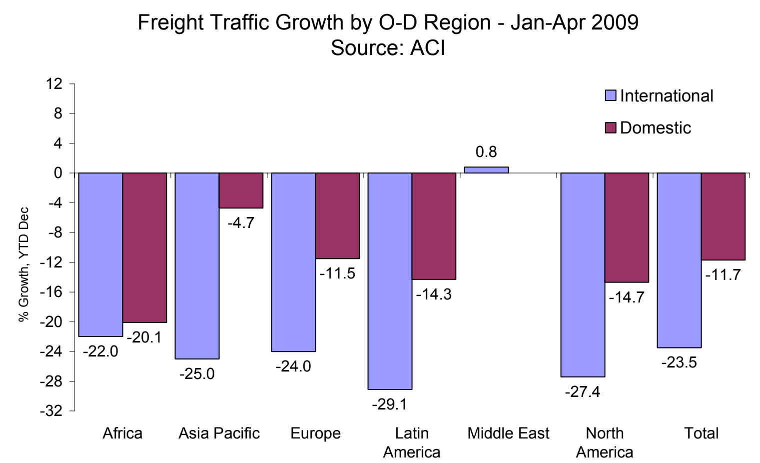
- Air freight volumes seem to have stabilised after hitting a low point in December. International markets are twice as weak as domestic but there is no protection from geographical diversification as falls widespread.

Air freight volumes seem to have found a floor after the precipitous decline



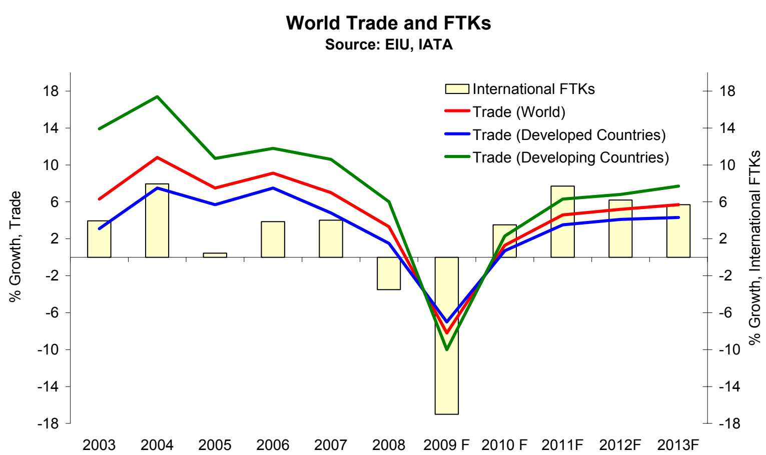
- December 2008 appears to mark the low point for air freight volumes in this extraordinary down-cycle. Year-on-year comparisons continue to show volumes down 20% or so but the level of FTKs has moved sideways for the past four months.
- International freight has fallen around twice the decline in domestic freight, reflecting the 'trade multiplier' caused by the integration of international supply chains in recent years. A floor to both may have been reached but so far a recovery is yet to be seen.

Weakness spread across emerging as well as developed markets



- The recession may have started in the financial sectors of the US and Europe but as consumers and businesses retrenched the major exporting economies were hit. Global supply chain and trade linkages have meant all regions have seen steep declines in air freight, with the exception of the Middle East.
- The one positive to draw from this alarming decline is that the worst appears to have already happened, with volumes now moving sideways.

International trade shrinks this year with relatively weak rebound forecast



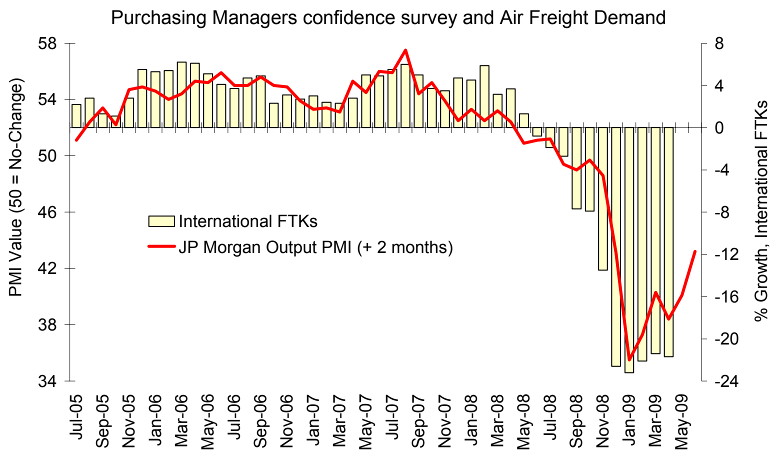
- Air freight is a good leading indicator of world trade movements, since shippers tend to switch to air when speed is more important than cost – at the start of an upturn – and switch to ocean in a recession. As a result air freight is first into recession but usually is first out.
- This will be the case again but forecasts of world trade suggest an unusually weak recovery next year, as inventories are rebuilt but final demand from consumers and businesses remains soft until 2011 or 2012.

Demand Environment

Key Changes in the data this quarter:

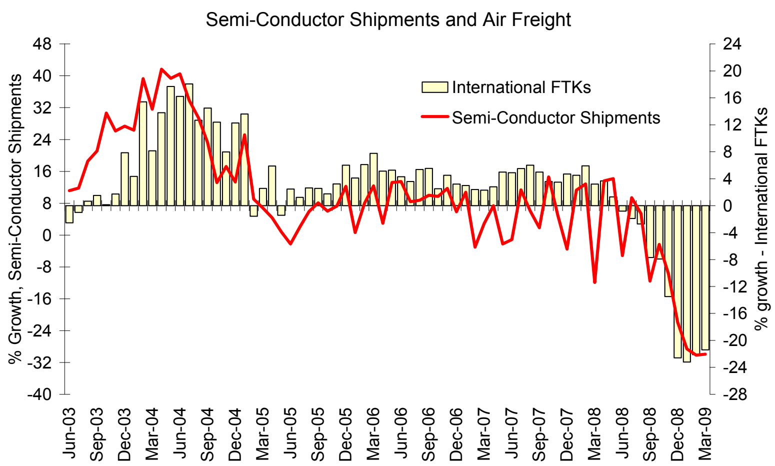
- Leading indicators offer a moderately encouraging picture. Purchasing managers point to some rise in air freight volumes in the next few months. However, inventory overhang remains major headwind to recovery.

Purchasing managers confidence points to a modest pick up in air freight volumes



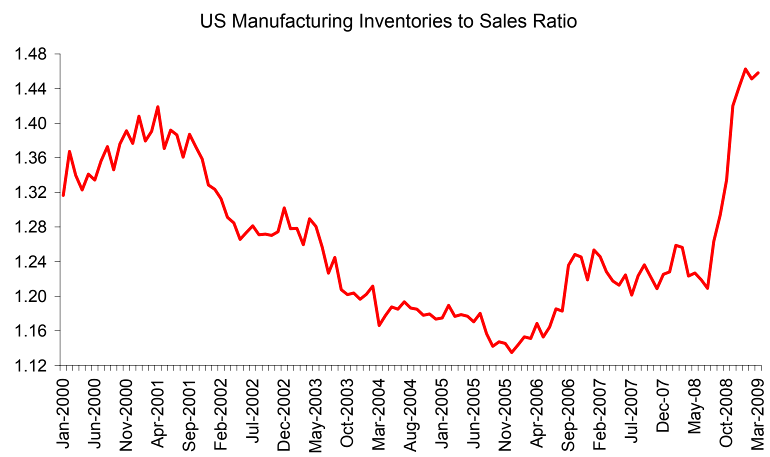
- Surveys in major economies around the world of purchasing managers' confidence have provided a good leading indicator, by 2 months or so, of turning points in air freight volumes.
- JP Morgan aggregate these surveys and their index has improved ever since a low point was reached in November. The improvement is consistent with air freight declines moderating to around 12% in the next few months.

Semi-conductor shipments also seem to be stabilising



- Shipments of semi-conductors, most of which are by air freight, plummeted to levels 30% lower than a year ago in the early months of this year. They now appear to be stabilising.
- The semi-conductor industry is an important customer for air freight. Moreover since over half of goods shipped by air are components or capital goods it is a good indicator of overall air freight volumes. These shipments may now be finding a floor but there is no sign as yet of recovery.

Inventory overhang stops growing but it needs to be reduced significantly



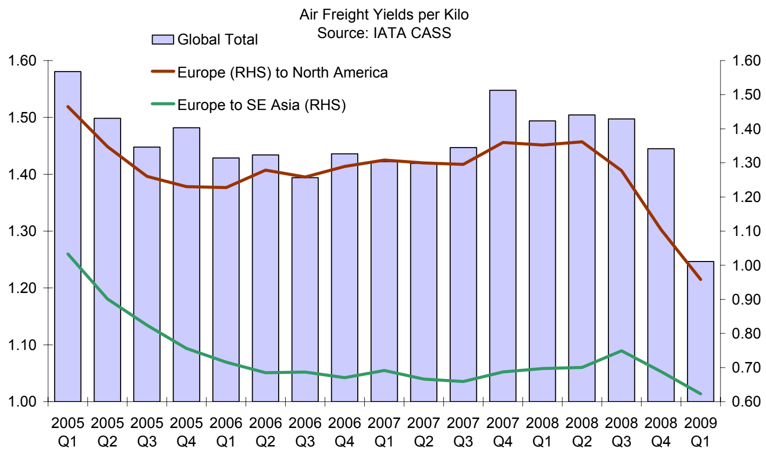
- Air freight slumped so sharply at the end of last year because of the extraordinary inventory overhang that emerged in manufacturing in many major economies. The good news is that inventory-sales ratios are no longer growing. This is why air freight volumes have stabilised.
- The bad news is that this inventory overhang needs to be reduced before shipments by air will recover significantly.

Revenues and Yields

Key Changes in the data this quarter:

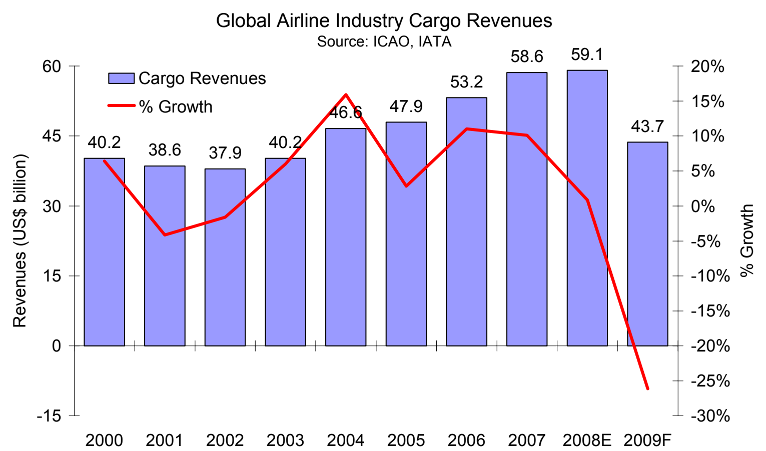
- Cargo volumes may be stabilising but excess capacity caused a 17% slump in yields in the first quarter. Revenues from cargo will see a record decline in 2009 on both lower volumes and yields.

Cargo yields falling sharply as excess capacity grows



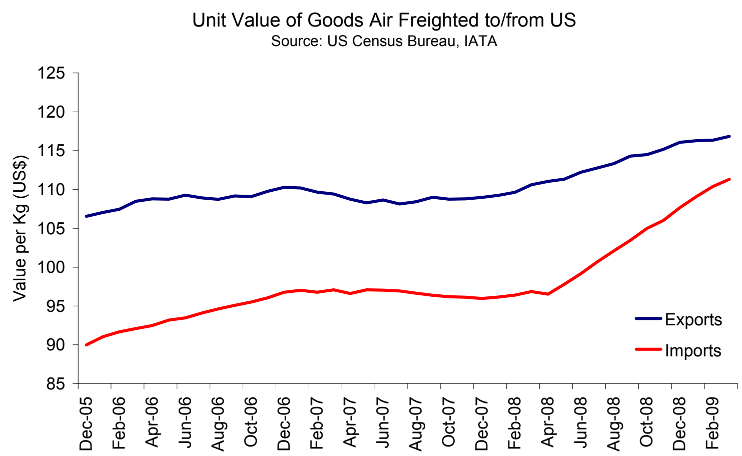
- Cargo volumes may now be stabilizing as the recession hits its low point, but yields are now falling fast. This process had already begun in the second half of last year when yields eased back 3%, following yield growth of 5% in the first half when volumes were still strong.
- But the first quarter of this year saw a 17% slump in average yields. Although cargo volumes have now stabilized there remains a lot of capacity chasing that business.

Cargo revenues will fall sharply with lower volumes and yields



- Both volumes and yields are likely to see the largest year-on-year declines in the first half of this year, with smaller percentage declines even if both move sideways.
- In the first quarter cargo revenues fell in excess of 35% with a 20% fall in volumes and a 17% fall in yield. A modest inventory-led rebound in the second half is expected to still leave cargo revenues in 2009 as a whole down on 2008 levels by a record amount.

A significant shift towards higher value air freighted goods into the US in the downturn



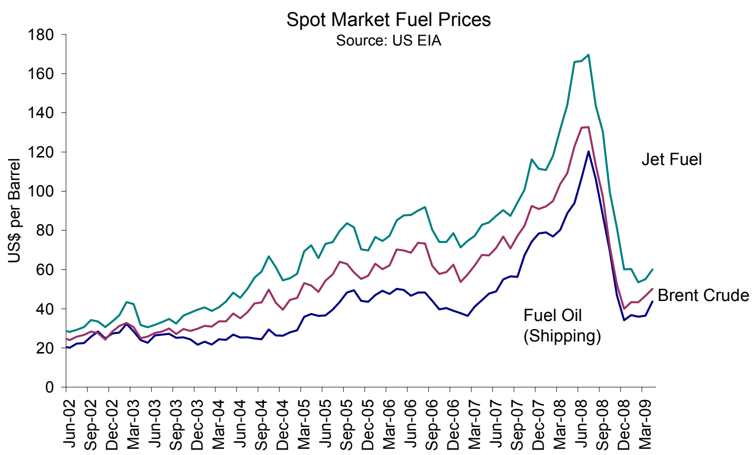
- As the recession hit the US significantly in early 2008 it appears that shippers diverted lower unit value goods from air freight to other, cheaper though slower, modes of transport.
- Despite the rise in the US dollar last year reducing the US$ cost of imported manufactures, the value per kilo of goods imported into the US by air have risen 15% in the 12 months to March. This is likely due to a composition effect as lower value goods are shipped by other modes and make up a smaller proportion of air freight.

Costs

Key Changes in the data this quarter:

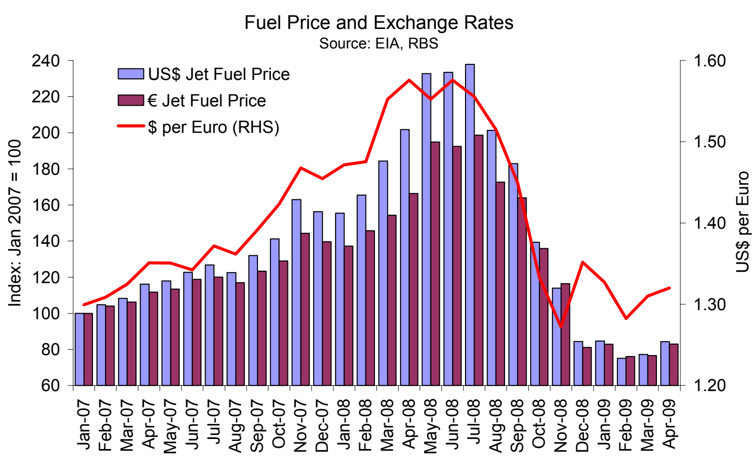
- Jet fuel prices are 60% lower than a year ago and little higher than the start of the year, but crude oil prices are already $20/b up so far this year. Aircraft and labour costs falling but some airport charges are rising.

.Oil price pulled $20/b higher by futures markets anticipating recovery



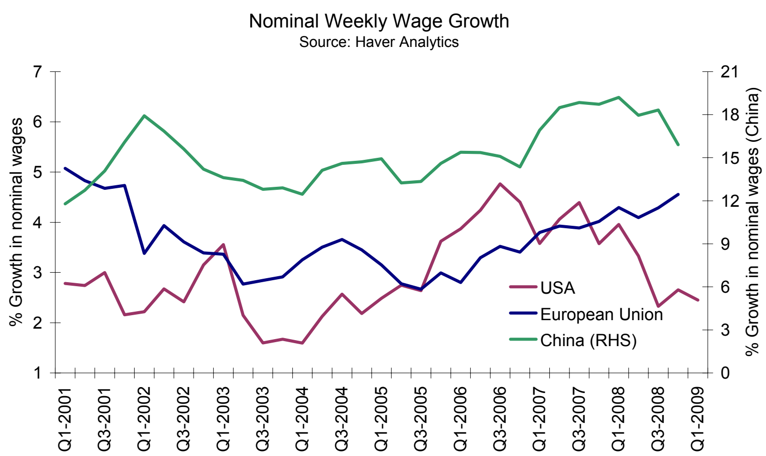
- Oil prices hit a low point around the same time as air freight volumes, late last year, briefly dipping below $40 a barrel. Crude oil prices are now back above $60 a barrel. Jet fuel prices are only a little higher than at the start of the year, but the 'crack spread' is unlikely to narrow further.
- Yet oil fundamentals are weak with high levels of stocks and demand down 3%. There is clearly no near-term shortage of oil on spot markets. The price for spot oil seems to be pulled up by the front futures contract as the market anticipates economic recovery.

After appreciating 15% against the € late last year the US$ has since moved sideways



- In the second half of last year the strengthening of the US dollar, along with the impact of some hedging contracts, reduced some of the benefit of lower spot oil prices to European and some Asian airlines.
- So far this year the US dollar has fluctuated around a flat trend, so all regions have equally felt the impact of the rise in oil prices. By April oil prices were down 58% over the year in US$ terms and by 50% in €.

Looser labour markets are reducing wage pressures in most regions



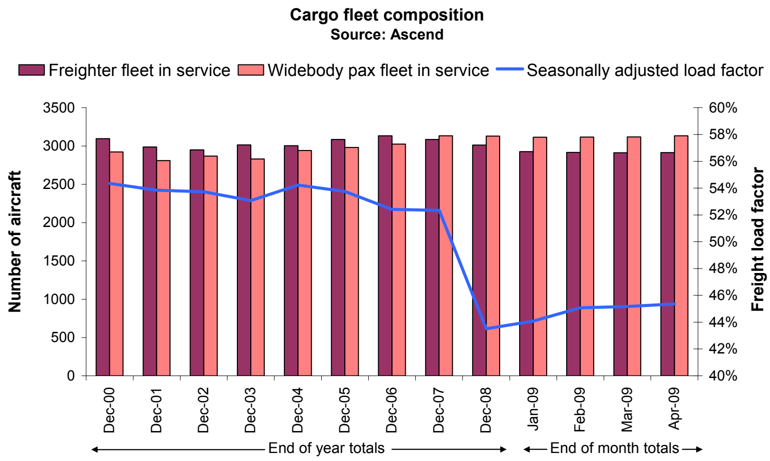
- While fuel prices are now starting to edge higher, other major costs such as aircraft prices and lease rates and labour costs are easing due to the recession. Wage growth is slowing significantly in the US and China. The exception is Europe but the recent sharp rise in unemployment should be soon reflected in slower wage growth.
- One area where supplier costs are rising is infrastructure charges, as many airports seek to recover fixed costs on reduced passenger numbers..

Capacity

Key Changes in the data this quarter:

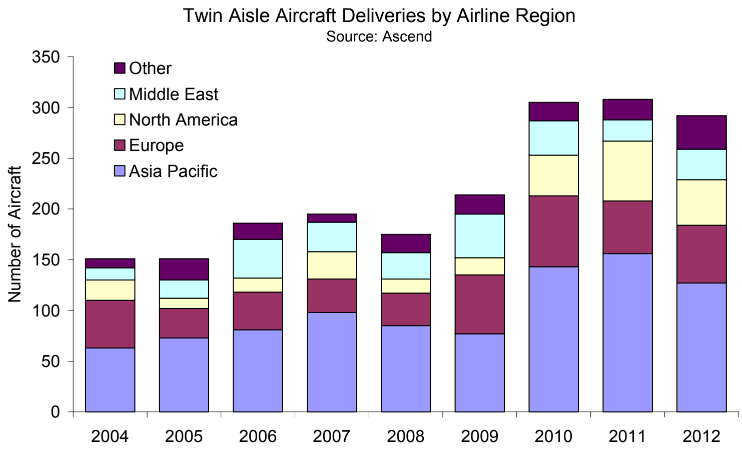
- Freighter fleet reduced by 99 aircraft so far this year but widebody capacity is up, as older aircraft no longer being parked. Most of strain of 20% loss of volumes is being taken by 7% point fall in freight load factors.

.Freighters being parked but load factors take most of the strain of recession



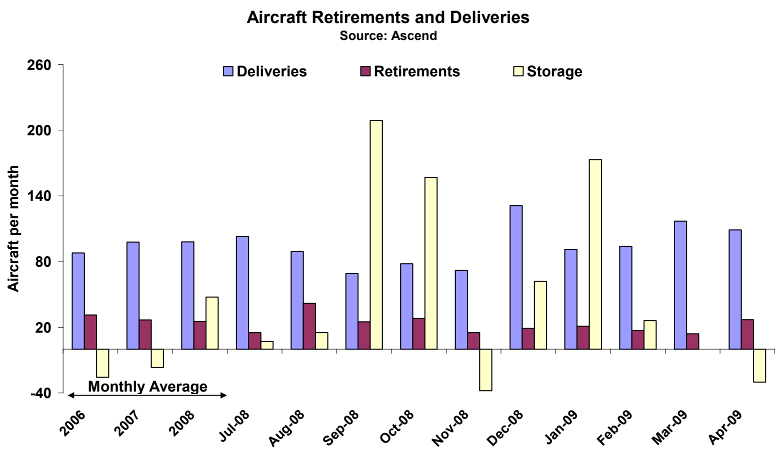
- Air freight volumes are down 20% but it would seem the pressure has largely been taken by cutting aircraft utilisation rather than parking fleet. Some 99 freighters have been taken out of the fleet so far this year, but that's just 5% of the freighter fleet. Widebody passenger aircraft, with around 50% of freight capacity, are up by a net 3.
- In fact freight load factors have edged up so far this year to a seasonally adjusted 45% by April, but that's 7% points lower than previous utilisation.

New aircraft deliveries adding to capacity pressures



- Air freight capacity pressures were eased a little in 2008 by the problems at Boeing that led to 20 fewer aircraft delivered than in 2007. However, that reverses this year with over 200 widebodies scheduled for delivery.
- Regional pressures will vary with fewer delivered to Asia this year but more to European and Middle Eastern airlines. With a significant demand recovery still not visible there must be a question mark over planned 2010 deliveries, which would add around 5% to the fleet

Fleet expanding as older aircraft no longer being parked



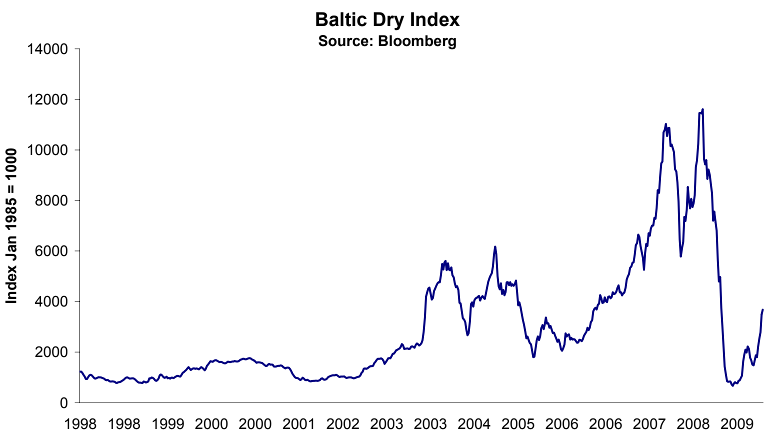
- The commercial aircraft fleet shrank between September last year and January as the earlier fuel price spike led to around 600 aircraft being parked or retired. But since February there has not been a net positive number of older aircraft being parked, partly due to changing economics after the decline in fuel prices.
- However, with new deliveries of around 100 a month the fleet is once more expanding despite airlines seeking to cut capacity in the face of recession. Lower utilisation is the result.

Competition

Key Changes in the data this quarter:

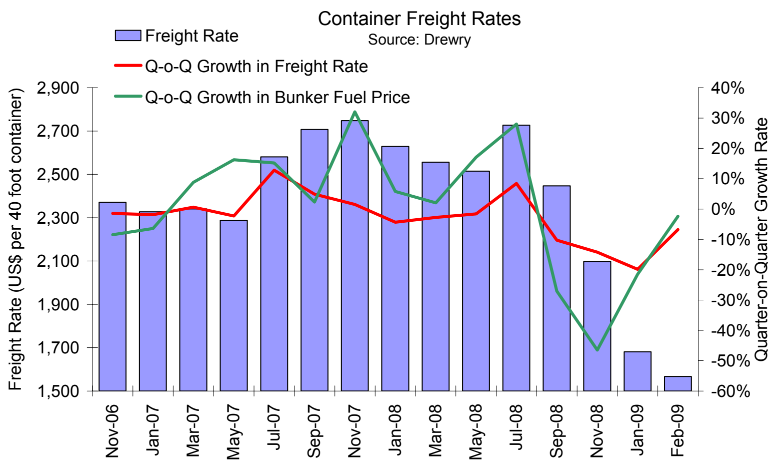
- Bulk commodity rates anticipate recovery but ocean container rates were down 39% in February. Container demand slumped in 2009Q1 but 15% falls are less than air freight as ocean shipping gains market share.

.Cost of shipping bulk commodities is back to 2006 levels in anticipation of recovery



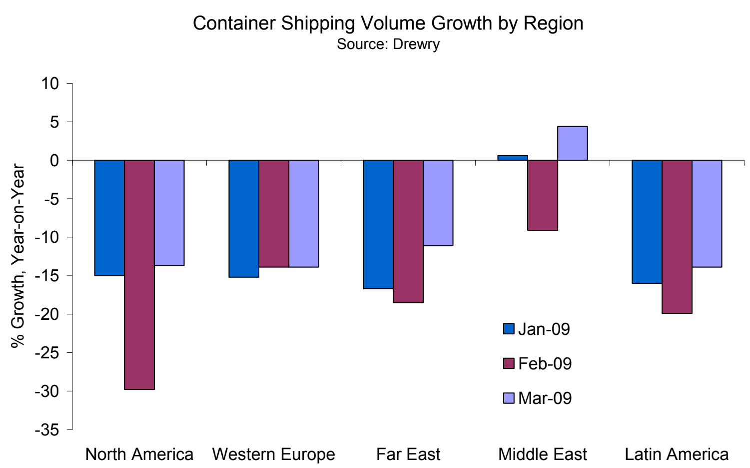
- The bulk commodity shipping industry also seems to have found a floor. The shipping rates for transporting commodities such as metals and grain are no longer close to zero and are back to levels normal before the boom and bust of the past three years.
- However, this shipping price index – the Baltic Dry Index – is like oil anticipating recovery since there is no sign yet of any widespread upturn in actual shipments of bulk commodities.

Container freight rates fell 39% in the 12 months to February



- The containerised shipping industry – the nearest competitor to air on many shipping lanes – is still experiencing sharply falling yields.
- In February container freight rates were 39% lower than a year ago, after a 36% decline in January. With a decline in freight rates faster and twice the scale of air, it is clear than ocean freight has improved its competitiveness against air freight in the past six months.

Container demand has slumped but not as much as the fall in air freight



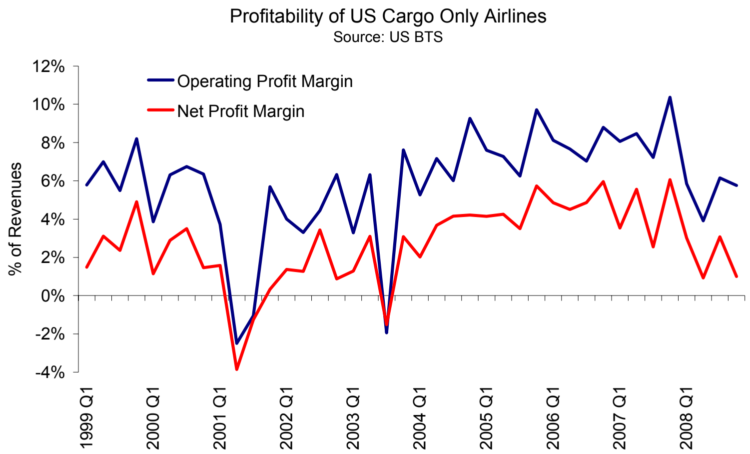
- The experience of the first quarter of 2009 in the ocean freight industry shows the severity of the collapse in world trade, as also seen in air freight.
- However, falls in the region of 15% are somewhat less than the 20%+ declines seen for air freight. Ocean freight has gained competitiveness and market share from air freight not just because of larger cuts in rates but also because time is less important in recession, when most companies are destocking.
- When recovery does eventually arrive time will be more important and some of this freight will switch back to air.

Profitability

Key Changes in the data this quarter:

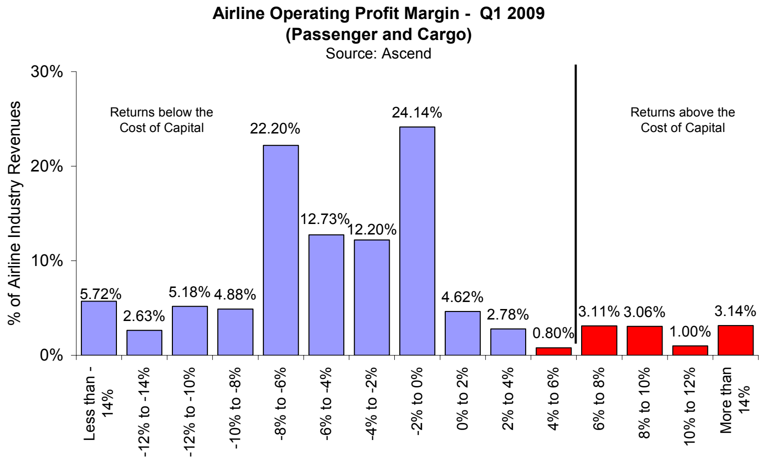
- Cargo profitability has been under extreme pressure from collapsing volumes and yields in the past six months. US cargo airlines have seen profits fall sharply and large losses have been reported in 2009Q1.

Cargo profitability falling in the US but, impressively, was still positive in Q4



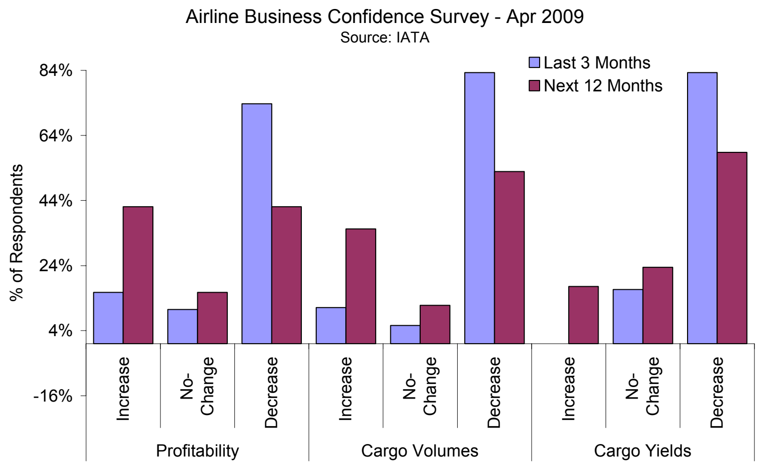
- The slump in freight volumes and, to a lesser extent yields, at the end of last year was reflected in a sharp fall in the net profits of all-cargo airlines in the US. The paradox is that freight markets weakened faster and deeper than passenger markets yet the US passenger airlines have been reporting large losses throughout 2008.
- The answer lies partly with the dominance of the express carriers. However, the revenue environment deteriorated very sharply in 2009Q1, so US losses may emerge early this year.

Operating losses were widespread during the first quarter of 2009



- The operating profitability of airlines carrying both passengers and cargo deteriorated further during the first quarter of this year, as the impact of recession exceeded the benefits of lower spot fuel prices.
- Less than 20% of airlines reporting so far were profitable in Q1 and over 40% made losses in excess of 6% of sales. The first quarter is usually weak for seasonal reasons but the fact that it was much worse than last year reveals the challenge facing the industry.

Business confidence slightly improved but big revenue decline expected



- When we surveyed airline heads of cargo and CFOs in April there was a reduction in the extreme pessimism over future profitability that emerged in the middle of last year. 74% reported larger losses in Q1 but only 42% expected a further deterioration over the next 12 months.
- The reduced pessimism comes from lower costs. More than half of those surveyed expect a further deterioration in both volumes and yields, implying a further slump in revenues.

Air Freight Routes and Direction

International Freight Volume Growth by Route Area (Source: IATA ODS statistics)

Route Area	% Growth in Freight Tonnes, year-on-year					
	Oct 2008	Nov 2008	Dec 2008	Jan 2009	Feb 2009	Mar 2009
Africa - Middle East	-3.5%	1.3%	-3.0%	2.2%	-8.4%	-1.8%
Europe - Far East (Except Polar)	-8.0%	-12.2%	-28.9%	-27.9%	-52.0%	-35.2%
Europe - Middle East	6.9%	-3.3%	-13.8%	12.3%	-8.4%	9.3%
Within Far East	-10.6%	-20.5%	-33.4%	-28.8%	-26.7%	-22.0%
Within Middle East	-5.9%	13.7%	2.2%	-10.7%	-7.7%	-6.7%
Within South America	-7.6%	-7.1%	-20.2%	-24.3%	-30.7%	-31.7%
Mid Atlantic	-5.7%	-10.5%	-16.7%	-18.0%	-32.1%	-35.7%
Middle East - Far East	14.9%	2.7%	-6.1%	6.5%	-0.7%	-10.3%
North Atlantic	-6.7%	-9.4%	-20.7%	38.4%	-37.0%	9.4%
North America-Central America	-5.2%	-16.4%	-17.1%	-34.5%	-25.0%	-24.2%
Europe - Africa	0.2%	-5.5%	-6.3%	2.9%	-2.8%	4.1%
North America - South America	-3.0%	-6.1%	-18.0%	-46.5%	-33.0%	-37.9%
Far East - Southwest Pacific	-4.8%	-11.0%	-13.1%	-3.2%	-21.0%	-9.9%
North and Mid Pacific	-13.0%	-24.6%	-35.5%	-17.5%	-18.1%	-14.8%
South Atlantic	-12.4%	-17.9%	-28.6%	-20.4%	-22.0%	-14.2%
Within Europe	-3.3%	-11.1%	-23.1%	-2.9%	-2.3%	-2.2%

Outbound CASS Market Revenues

Origin Region	US$m	% Growth in Air Freight Revenues, year-on-year					
	Q1 2009	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009
Africa	33.5	25.3	10.4	9.4	5.9	2.2	-8.0
Caribbean	4.6	8.4	20.7	8.9	7.3	-6.8	-7.3
Central America	40.3	6.4	12.0	9.1	9.2	-19.9	-15.8
Europe	913.1	12.4	8.2	9.2	-1.1	-23.9	-37.0
Japan & Korea	417.4	6.3	6.3	-4.1	-23.5	-41.6	-55.6
Middle East	70.2	77.9	65.9	15.2	26.7	23.2	49.4
North America	508.5	15.0	13.8	13.8	7.3	-15.1	-23.7
South America	171.2	7.6	9.5	12.8	11.0	-6.1	-20.8
South East Asia	562.8	151.9	30.6	27.2	27.2	-2.3	-27.2
South West Pacific	102.9	15.8	10.7	10.8	-0.3	-27.2	-30.0

Inbound CASS Market Revenues

Destination Region	US$m	% Growth in Air Freight Revenues, year-on-year					
	Q1 2009	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009
Africa	238.5	22.6	16.2	17.2	10.8	-5.9	-12.5
Caribbean	25.2	12.2	10.6	11.2	6.3	-10.2	-27.9
Central America	58.8	17.5	9.9	14.7	-6.2	-25.4	-37.1
Europe	821.1	34.0	15.6	8.4	2.3	-17.3	-33.6
Japan & Korea	167.4	15.4	0.7	-2.0	-13.2	-31.8	-41.2
Middle East	242.0	18.6	19.8	17.8	18.7	-2.4	-12.3
North America	485.7	21.8	4.1	2.2	-7.9	-31.0	-45.6
South America	200.1	33.3	30.8	28.7	24.7	-14.1	-33.9
South Asia	101.1	30.8	17.8	30.2	18.4	-3.9	-16.0
South East Asia	330.1	16.7	8.6	6.8	-5.5	-26.7	-42.4
South West Pacific	158.5	30.3	29.2	26.2	4.9	-25.1	-34.9

IATA Economics
June 2009