MONTHLY TRAFFIC ANALYSIS
MAY 2009

KEY POINTS

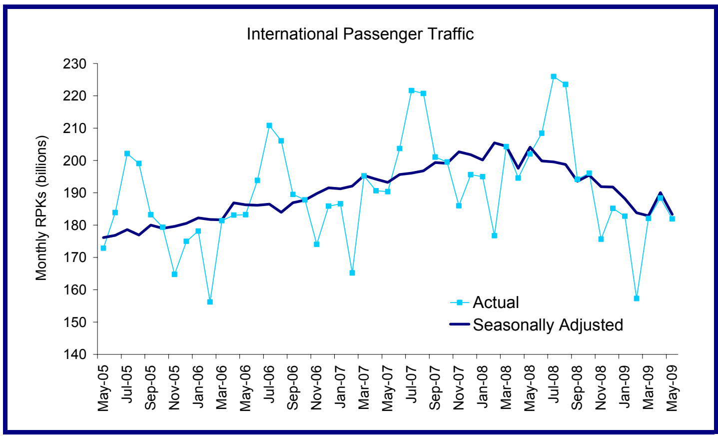
- Passenger kilometers flown on international markets fell at a faster pace of 9.3% in May, following the more moderate 3.1% decline in April and the 11.1% March fall.
- There has been considerable volatility in the data in recent months and the impact of swine flu accounted for about 1% point of the decline in May. But there is now tentative evidence that the low point in passenger travel volumes may have been reached in March. Although still much lower than last year, the level of passenger kilometers flown in May were marginally higher than levels in March suggesting that a floor has now been reached, unless the impact of swine flu increases significantly.
- Swine flu or influenza H1N1 had a clear negative impact on passenger demand for airlines in Latin and North America and some effect on Asia Pacific airlines. The impact of the recession appears to stabilising but strong headwinds from debt and low asset prices are expected to weaken and delay any significant recovery.
- Air freight tonne kilometers flown were down 17.4% in May, compared to a decline of 21.7% in April. Freight volumes had been moving sideways from month to month since hitting their low point in December. May marked the first month of noticable improvement, as manufacturers increased shipments, beginning to add to inventories in anticipation of economic recovery.
- Despite the apparent stabilisation of travel and freight volumes the same is not true for revenues. Passenger and freight yields are falling at an accelerating pace as excess capacity emerges, intensifying competition. As capacity cuts continue to lag behind the slump in demand, passenger load factors fell by 3.3% points in the 12 months to May, while freight load factors fell a further 3.6% points. We estimate that passenger revenues on international markets fell by 25-30% in May, following a decline of around 20% in the first quarter.

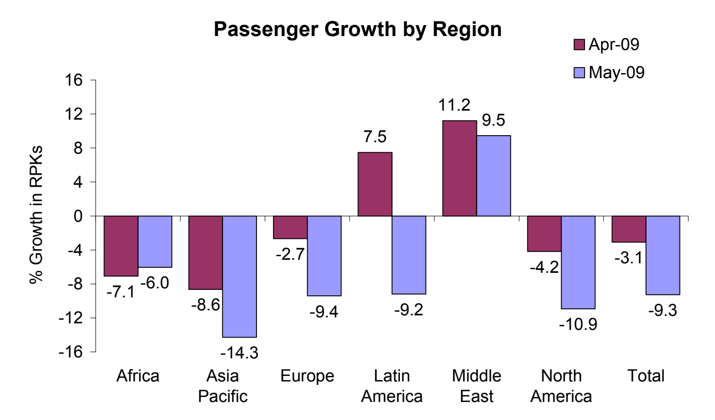
	May 09 vs. May 08						YTD 2009 vs. YTD 2008					
	RPK Growth	*ASK Growth*	*PLF*	*FTK Growth*	*AFTK Growth*	*FLF*	*RPK Growth*	*ASK Growth*	*PLF*	*FTK Growth*	*AFTK Growth*	*FLF*
Africa	-6.0%	-4.8%	69.3	-20.0%	-15.7%	26.6	-8.8%	-6.4%	70.0%	-23.1%	-21.0%	25.1
Asia/Pacific	-14.3%	-9.3%	66.8	-18.1%	-15.9%	59.5	-11.5%	-7.5%	70.7%	-23.5%	-16.6%	56.0
Europe	-9.4%	-6.5%	73.6	-19.2%	-10.9%	45.2	-7.8%	-4.8%	72.7%	-21.9%	-9.2%	44.3
Latin America	-9.2%	0.2%	64.7	-21.0%	-7.5%	30.4	-2.6%	1.3%	70.6%	-20.7%	-8.7%	29.8
Middle East	9.5%	14.5%	69.4	-3.7%	14.1%	39.3	6.0%	11.8%	70.6%	-6.6%	11.4%	39.7
North America	-10.9%	-6.6%	77.3	-18.8%	-11.9%	35.8	-9.4%	-5.2%	75.2%	-22.2%	-9.8%	33.9
Industry	-9.3%	-5.0%	71.2	-17.4%	-9.7%	46.7	-7.7%	-3.9%	72.1%	-21.3%	-10.4%	44.9

INTERNATIONAL PASSENGER TRAFFIC MAY HAVE REACHED A FLOOR

- There was a renewed acceleration in the decline of passenger kilometers flown during May to a level 9.3% lower than a year earlier, following the slower decline of 3.1% experience in April.
- The important question is what does this say about the trend in passenger travel? May marks the first month since January that there have been no major distortions to the comparison with the same month a year earlier. The leap year and the timing of Easter have made the interpretation of year-over-year growth rates difficult in the preceding three months – boosting growth in April but depressing growth rates in February and March. Adjusting for these distortions showed Q1 growth in passenger travel of 7-8%, so May's 9.3% decline is a deterioration from the average first quarter performance. However, that does not take into account the decline during the first quarter – in March traffic was down 11.1%.

- The seasonally adjusted data in the chart below gives a good idea of the trend, because it overcomes the disortions of comparisons with the same month a year earlier and removes the large seasonal month-to-month fluctuations in travel. This data shows that the level of passenger kilometers flown was just over 1% lower in May than the average for the first quarter. However, travel was declining sharply through the first quarter as economic conditions were still deteriorating fast. March appears to mark the low point for passenger travel. Passenger kilometers flown in May were in fact marginally higher than March despite being down on April levels.





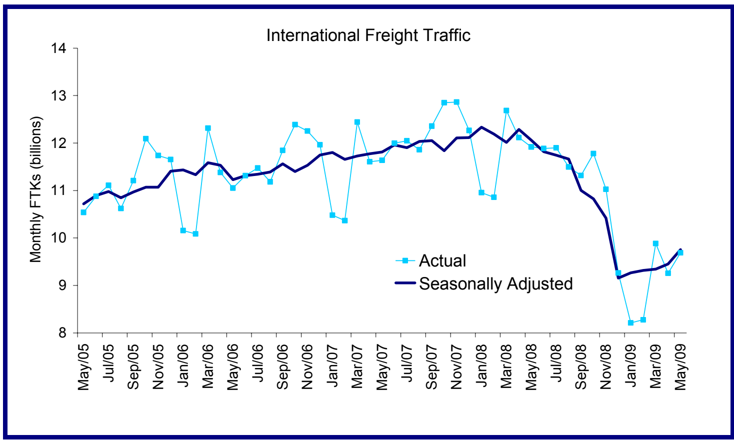
- The impact of swine flu is complicating interpretation of the data. May is the first full month during which the virus has been impacting air travel. The Mexican airlines saw their passenger traffic on international markets fall almost 40% in May, while the Latin American airlines as a whole have seen a deterioration from a near 4% decline in the first quarter to a decline of 9.2% in May. US airlines saw traffic to Latin America fall 14.7% in May from a 7% decline in the first quarter, according the ATA. We estimate that the impact on airlines from these two regions may have reduced passenger kilometers flown on international markets in May by a bit less than 1% point. There is also some evidence of an impact on travel from Asia in addition.
- Even with the 1% point or so impact from swine flu in May the level of passenger kilometers flown, adjusted for seasonal fluctuations, was marginally higher than the March low point. Provisional data on the first half of June for AEA airlines suggests that the level of air travel, again adjusted for seasonality, was similar if not up a little on May. After two months of slightly stronger data it now looks as though a floor to the thirteen month long decline in passenger travel has been reached.
- This is positive news but there is little visibility of when significant recovery might take place and the volume of air travel is still 10% lower than its early 2008 peak. Moreover this understates the loss relative to what had been expected. Forecasts for 5% annual growth made in early 2008 imply that we have already lost several years of growth and that RPKs flown in May this year are over 20% lower than previously forecast.
- The Latin and N American airlines have the largest exposure to swine flu, while passengers in Asia are perhaps sensitised to the potential risks, following their experience of SARS in 2003, leading to some effect on travel already. Yet European airlines saw a similar decline in travel during May. This suggests that the boost in April was temporary and the renewed fall back in May was largely driven by economic factors. Data on European airlines from the AEA shows that markets to Asia were weakest in May with an 11.9% decline while travel across the N Atlantic fell just under 10%. ATA data confirm the weakness originating from Asia in May, with US airlines seeing Pacific travel volumes fall by over 20% while across the Atlantic the decline moderated to a fall of 4%.
- There has also been some loss of market share from the full service network airlines to the no-frills LCCs in some regions, as price-sensitivity increases in recession. The largest impact will be in Europe where the LCCs seat share is largest. Indeed there was some growth in the international traffic carried by LCCs in Europe during May, but only by 2.1%. Including the LCCs in the European totals above reduces the decline in passenger traffic from 9.4% to 7.9%. Significant but the picture of continuing, if stabilising, economic weakness remains.
- Airlines in Africa and the Middle East continue to be driven more by local or strategic influences. African airlines saw some further improvement – or rather less of a decline – with a 6% reduction in travel volumes compared to an 11% decline in the first quarter and a 7% fall in April. Middle Eastern airlines continue to pursue an

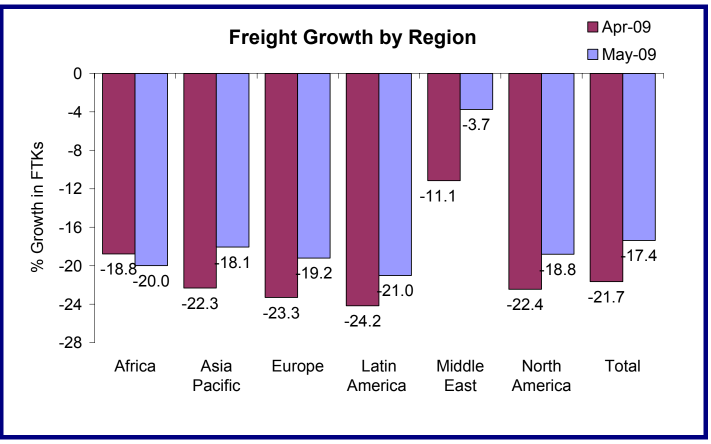
expansionary strategy and managed to grow their passenger kilometers flown by 9.5%, which is a marked improvement on the less than 3% growth achieved in the first quarter and builds on the 11.2% growth of April.

- Looking ahead to future months there still appear to be considerable headwinds to any significant recovery. Consumer confidence has improved but unemployment is still rising and debt remains high – consumers are already repaying debt instead of increasing spending. Since the decline in travel began early last year the year-over-year percentage declines will get smaller even if passenger numbers stay unchanged. But current economic forecasts for 2010 suggest any recovery then will be much weaker than normally experienced.

AIR FREIGHT VOLUMES SHOW SIGNS OF MODERATE GROWTH

- Air freight volumes are now showing signs of a moderate revival, having stagnated since reaching a low point in December. The year-over-year comparison shows the decline has moderated from a 21.7% decline in April to a 17.4% fall in May.
- The seasonally adjusted level of freight tonne kilometres flown in the chart below gives the clearest indication of trend. After the precipitous decline at the end of last year, freight volumes moved broadly sideways for the first part of this year having hit bottom in December. In May freight volumes rose by around 3% above April level as manufacturers begin to add a little to their inventories in anticipation of an economic recovery.
- This up-tick in air freight is one of the first physical signs of the economic recovery that is being anticipated in equity markets and surveys of business and consumer confidence. Air freight has been shown to be a very timely indicator of world trade and the inventory up-cycle that normally precedes a recovery in consumer and business spending. Surveys of purchasing managers have been showing improved confidence and pointing to an improvement in air freight volumes for some months now.
- However, the level of inventories is still 10-15% higher than normal in relation to sales levels so a strong revival in shipments to restock warehouses and shops, of the sort that would normally be experienced just before an economic recovery, remains some way off. Nonetheless purchasing managers surveys are suggesting some further revival of air freight volumes in June and July of a similar scale to the rise in May, to a level around 12-15% lower than a year earlier.



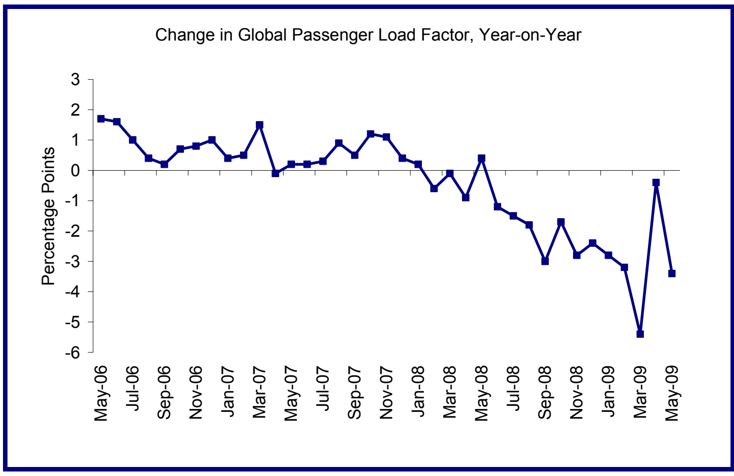


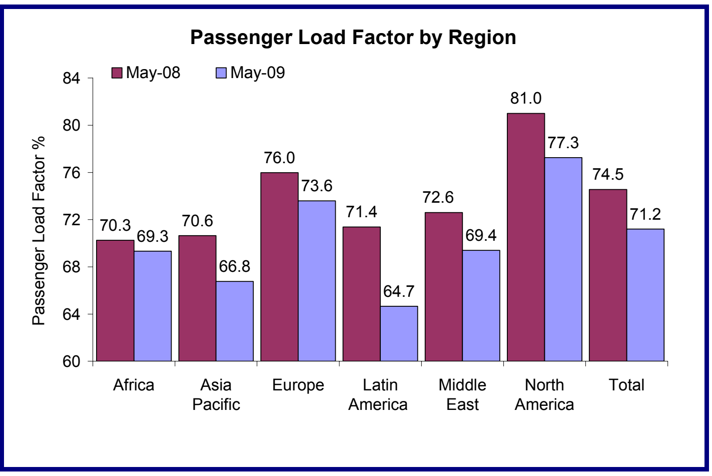
PASSENGER LOAD FACTORS CONTINUE TO FALL AT 3% POINT RATE

- Despite the apparent stabilisation in passenger traffic, capacity cuts continue to lag some way behind. While total passenger kilometres flown on international markets shrank by 9.3% in May, the available passenger kilometres provided by airlines was cut by only 5%. As a result load factors fell by a further 3.3% points to 71.2%. Aside from the March/April fluctuation caused by the timing of Easter the chart below shows that, since September last year, airline capacity cuts have been consistently 3-4% points behind the decline in demand.
- In other words there has been a steady rise in excess capacity over the past nine months. The only major exception is in the US domestic market. Elswhere there has been a sharp intensification of competition and airlines are anyway very actively seeking to boost dwindling cash flows by trying to attract passengers to fill empty seats. As a result fares are falling fast, particularly for first and business seats. Premium travel numbers

are also falling faster than economy, despite the introduction of intermediate classes to try to capture williness to pay for more leg room. As a result passenger yields for airlines are falling faster than fares. Data from the ATA show a sharp acceleration in the yield decline in May, with fall of 24% across the Atlantic and almost 18% across the Pacific. In January the falls were just 7.5% and 1.4% respectively.

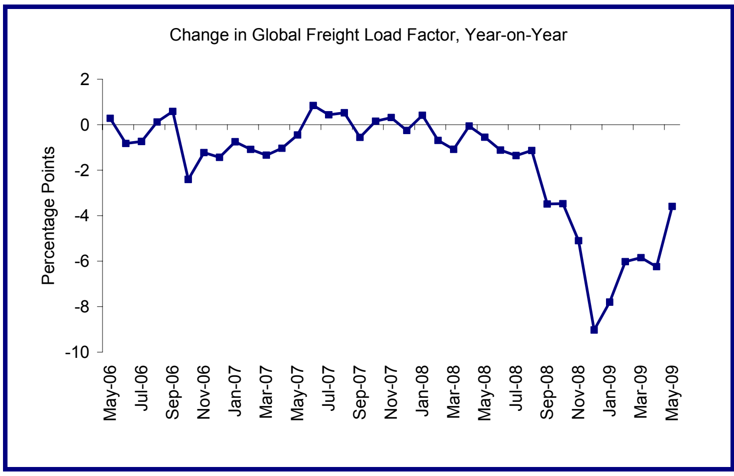
- So even if passenger numbers are stabilising, revenues are not. Having declined around 20% in the first quarter passenger revenues from international markets look as though they fell 25-30% year-over-year in May.

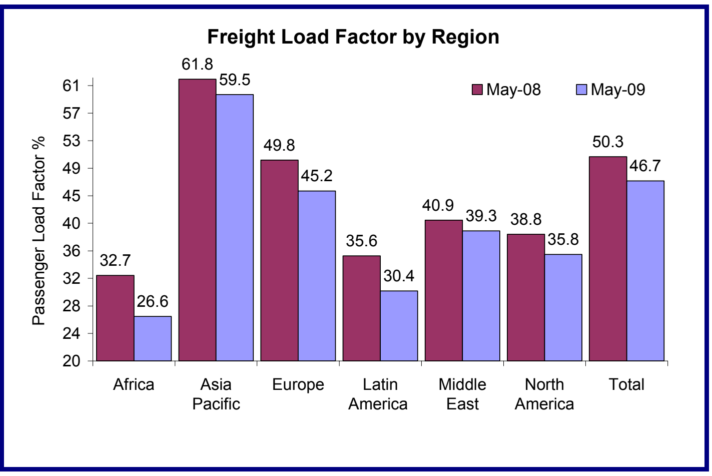




FREIGHT LOAD FACTORS STILL FALLING BUT AT SLOWER RATE

- Rapidly growing excess capacity is even more of a problem in the air freight market, though there has been an improvement in recent months. As freight tonne kilometers flown sank to their low point in December freight load factors fell almost 10% points. Since then freight capacity cuts have been catching up with demand to a greater extent than in the passenger business. Available capacity in freight tonne kilometers has been cut by twice the extent of passenger capacity, with a 9.7% decline in May.
- Excess freight capacity is narrowing but load factors are still 3.6% points lower than a year ago. Moreover, in absolute terms, the less than 50% utilisation rates show that excess capacity is even more of an issue in freight than the passenger business. Freight rates are falling sharply as a result. We know freight yields fell 17% in the first quarter, reducing revenues by over 35%. Although volumes improved in May this is no guarantee that there was any improvement in revenues, given the continuing downward pressure on yields.





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