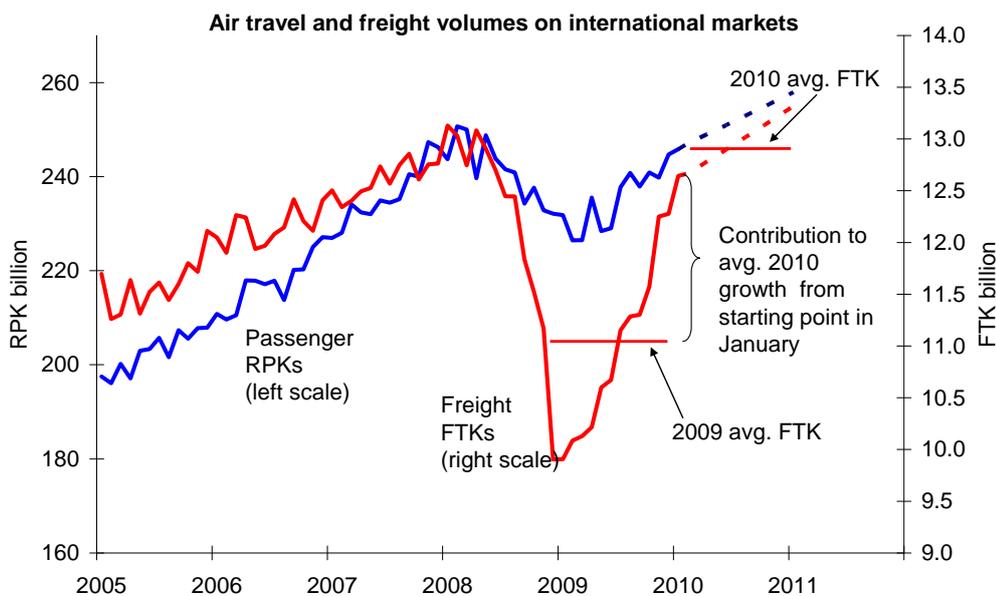


# FINANCIAL FORECAST

March 2010

## RECOVERY PICKS UP PACE BUT STILL 2-SPEED

➤ Airline markets rose strongly at the end of last year and early in 2010, but growth remains concentrated in the emerging markets of Asia, Latin America and the Middle East, with benefits accruing mainly to airlines in these regions; highlighting the problems caused by ownership rules. Airlines in the large developed markets of Europe and North America face much more sluggish market growth. This 2-speed recovery in economies, freight and travel markets is reflected in the divergent performance of airlines in different regions. Helped by the strong year end we have cut our estimate of 2009 net losses from US\$11 billion to US\$9.4 billion. More significantly we now forecast smaller losses in 2010 of US\$2.8 billion, compared to our previous forecast of US\$5.6 billion; with the largest improvements benefiting airlines in Asia and Latin America.



Source: IATA

➤ One notable change has been to average traffic growth, which is now expected to be much stronger in 2010 – with a 5.6% rise in air travel volumes and a 12% rise in air freight – mostly due to the very strong recent gains, as the chart above demonstrates. In addition forecasts for economic growth in 2010 have been revised up, with the notable exception of Europe; causing airlines in this region to be the poorest performing.

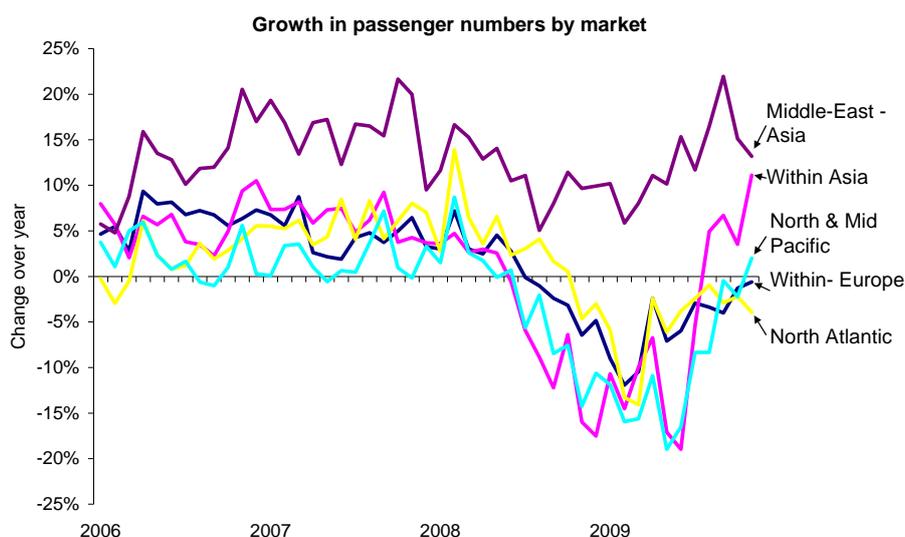
System-wide global commercial airlines	2007	2008	2009E	2010F	2007	2008	2009E	2010F
	<b>EBIT margin, % revenues</b>				<b>Net profits, \$ billion</b>			
<b>Global</b>	3.9%	-1.6%	-0.1%	1.6%	12.9	-15.9	-9.4	-2.8
including exceptional items					14.7	-36.0	-9.4	-2.8
<b>Regions</b>								
North America	5.5%	-1.8%	1.3%	1.9%	3.7	-9.5	-3.1	-1.8
including exceptional items					5.5	-24.3	-3.1	-1.8
Europe	4.0%	0.1%	-1.9%	-0.6%	6.4	0.1	-3.8	-2.2
including exceptional items					6.4	-0.9	-3.8	-2.2
Asia-Pacific	2.9%	-4.7%	0.0%	3.7%	3.0	-5.0	-2.7	0.9
including exceptional items					3.0	-9.0	-2.7	0.9
Middle East	0.0%	1.0%	-0.9%	0.2%	-0.1	-0.3	-0.5	-0.4
Latin America	2.0%	2.3%	3.9%	4.1%	0.1	-1.2	0.8	0.8
including exceptional items					0.1	-1.5	0.8	0.8
Africa	1.0%	-0.9%	-1.7%	-0.6%	-0.2	-0.1	-0.2	-0.1

Source: ICAO data to 2007-8. IATA estimates for 2009 and forecasts for 2010.

Exceptional items include revaluations of goodwill associated with restructuring and of 'mark to market' fuel hedging.

## DEMAND REVIVAL UNEVEN ACROSS REGIONS

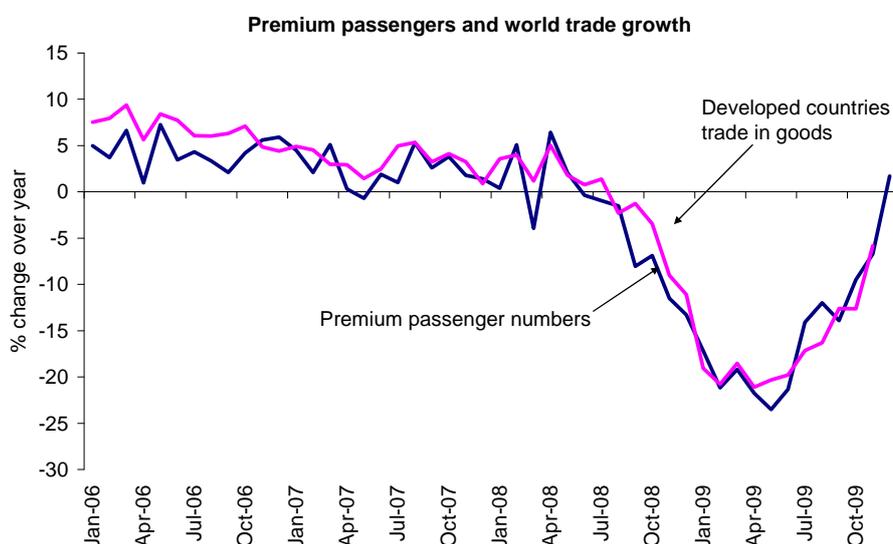
As one of the most cyclical industries it is not surprising that the financial performance of airlines is closely tied to economic growth in the network areas they serve. But it is unique to this industry that those network areas are tied to local conditions. Although there has been further development of alliance co-operation, joint ventures and some mergers & acquisitions it is the case that airlines are still highly dependent on the traffic generated by their local economies and trade lanes. This is in contrast to many of the companies listed on major stock exchanges that generate their earnings from across the globe; these companies are not restricted by the market and ownership rules that constrain airlines. As a result the airlines doing well in today's environment are those in Asia and Latin America where economic growth has revived the most. The weakest markets in the chart below are clearly across the North Atlantic and within Europe, where the economic recovery has faltered, under pressure from consumer debt and still weak bank balance sheets.



Source:  
PaxIS

## PREMIUM DECLINE CYCLICAL BUT STILL WEAK

Travel has diverged dramatically by seat class as well as market. Economy travel is within a few percentage points of its early 2008 peak levels. Premium travel remains 17% below. The concern had been that this was a permanent shift by business travelers to cheaper seats. The good news is that the decline in premium appears to be due to the unprecedented cyclical decline in world trade and financial markets, and some upturn is evident, as the chart below indicates. The bad news is that the cyclical upturn is not expected to regain the pre-'Great Recession' trend line, given debt problems in the West. Moreover, yields may have suffered some structural decline. Business travelers still want full service on long-haul, but corporate buyers are not prepared to pay as much. Premium yields have picked up but are still 20% below early 2008 levels.



Source: IATA,  
Netherlands CPB

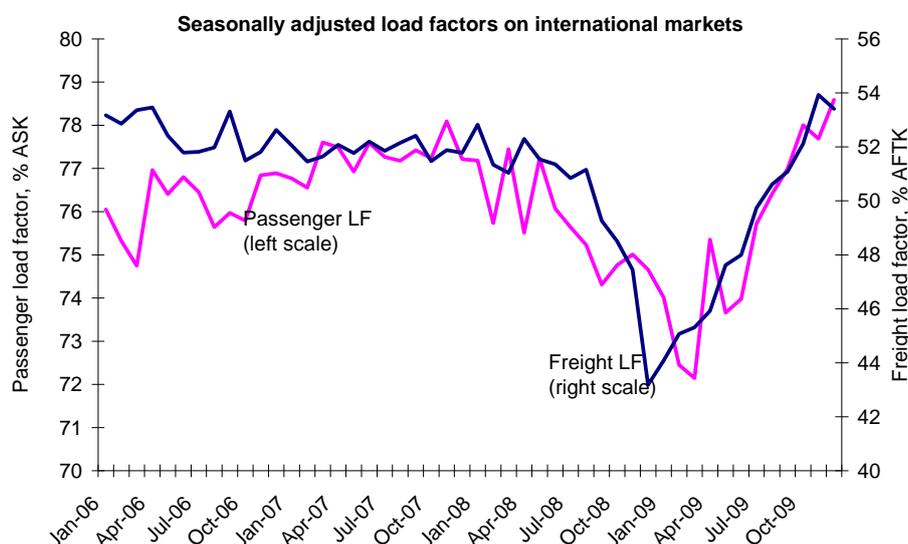
- Growth rates on most travel and freight markets are going to be much higher than expected just a few months ago because of the high starting point effect illustrated in the chart on the front page. But the stimulus, or not, of economic growth through 2010 is also shown in strong regional differences. Double figures market growth is likely this year in the emerging markets of Asia, Latin America and the Middle East. But the larger, developed, markets of Europe and North America are expected to show relatively weak growth. Even so underlying growth of 3% in these regions will be boosted by 50-100% in 2010 as a result of the January starting point generated by the end-2009 upturn.

System-wide global commercial airlines	2007	2008	2009E	2010F	2007	2008	2009E	2010F
<b>Global</b>	<b>Traffic (TKP), % change over year</b>				<b>Capacity (ATK), % change over year</b>			
	5.2	-0.1	-5.2	7.3	5.2	0.7	-4.9	4.0
<b>Regions</b>								
North America	3.5	-4.3	-6.1	6.2	3.2	-3.4	-7.4	3.3
Europe	2.1	0.9	-8.7	4.2	3.5	2.9	-5.6	-1.0
Asia-Pacific	7.8	-0.2	-3.2	12.0	6.9	0.6	-7.4	7.3
Middle East	16.4	3.6	8.5	15.2	14.5	4.7	11.1	14.5
Latin America	9.9	3.3	0.0	12.2	6.9	3.2	1.3	8.1
Africa	4.5	5.1	-5.4	7.4	5.8	7.2	1.6	7.8

Source: ICAO data to 2008. IATA 2009 estimates, 2010 forecasts. Dom. and int. traffic. Includes pax and cargo by weight.

## RECORD LOAD FACTORS AS CAPACITY LAGS

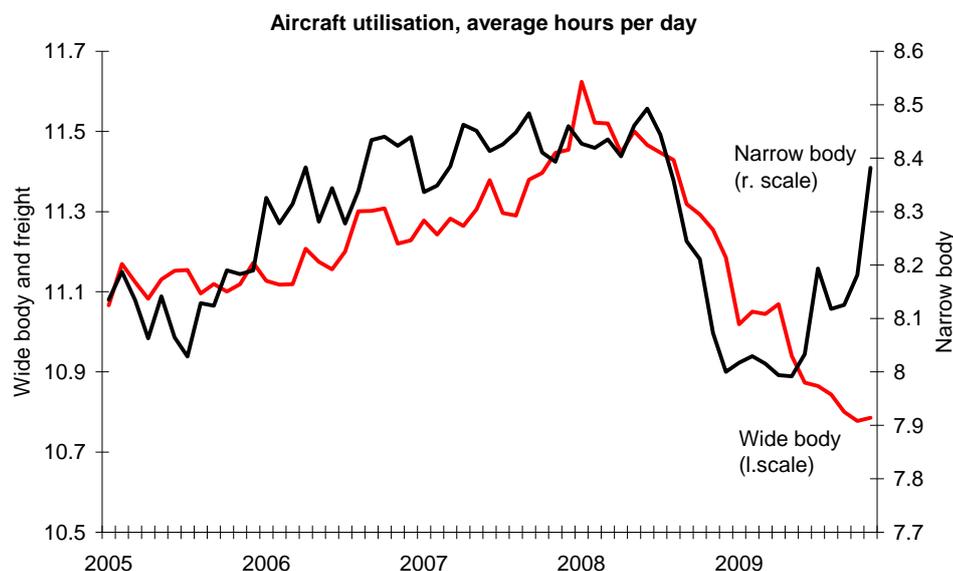
- Capacity cuts lagged the downturn in demand, with the exception of the US domestic market in late 2008 and early 2009. Load factors fell sharply. In a highly capital intensive industry high asset utilization is critical for profitability. Losses mounted. However, the subsequent capacity cuts were unusually deep and durable. As a result the recent upturn in demand for both air travel and freight has led to a sharp rise in load factors to record levels, on average.



Source:  
IATA

- Tighter supply-demand conditions on some markets, particularly those originating in Asia, are pulling fares and cargo rates higher. Airlines in those regions are seeing the benefits. But both fares and cargo yields are still 10-20% lower than early 2008 levels. Moreover, it remains to be seen whether these conditions of relatively scarce capacity will persist. There are 1,400 jets and turboprops scheduled to be delivered this year which, if no aircraft were taken out of service, would add 5-6% to the fleet. The other potential source of additional capacity is from the underutilized existing fleet. The chart below shows that there has been a pick-up in single aisle aircraft utilization, on short haul markets, but twin-aisle utilization remains 7-8% down on early 2008 levels. We have become slightly more positive on yields in 2010 as a result of stronger demand, but latent capacity remains an overhang that will limit the upside for yields this year.
- Low long-haul utilization also suggests that these markets will be the most difficult in which to restore profitability. But there is also significant geographical difference underneath these aggregate trends. Short/medium haul markets in Asia and Latin America have picked up while utilization in US domestic markets has been boosted by capacity cuts. This will help profitability to recover. North Atlantic markets are

facing weak demand but capacity is being cut substantially at both ends. Long haul air freight originating from Asia has risen so sharply that there is a shortage of capacity.



## GETTING INTO SHAPE FOR THE UPTURN

➤ Stronger economic growth is boosting revenues but it is also pulling oil prices up. In line with the futures curve we have raised our 2010 forecast for oil prices from US\$75 a barrel to US\$79. Airlines need to take out other costs now before labor and other markets tighten to the point where this becomes impossible. Unions are already pushing back at attempts to improve working practices. Restructuring of capacity will be part of this process and there is a lot of alliance and merger activity. But without active loosening of ownership restrictions along the lines suggested by Agenda for Freedom it is hard to see much real progress being made. Cyclical conditions are now improving but the structural challenges to financial sustainability remain.

System-wide global commercial airlines	2001	2002	2003	2004	2005	2006	2007	2008	2009E	2010F
<b>REVENUES, \$ billion</b>	307	306	322	379	413	465	510	564	479	522
% change	-6.4	-0.5	5.2	17.7	9.1	12.6	9.6	10.5	-15.0	8.8
Passenger	239	238	249	294	323	365	398	439	367	395
Cargo	39	38	40	47	48	53	59	64	49	56
Traffic volumes										
Passenger growth, tkp, %	-2.3	-1.0	1.4	16.7	7.0	5.4	5.7	0.4	-2.9	5.6
Passenger numbers, millions	1640	1639	1691	1888	2022	2124	2281	2271	2206	2330
Cargo growth, tkp, %	-6.0	8.7	3.9	7.9	0.4	3.9	4.0	-1.2	-11.1	12.0
Freight tonnes, millions	28.8	31.4	33.5	36.7	37.6	39.8	41.8	40.5	36.0	40.3
World economic growth, %	2.2	2.7	2.8	4.2	3.4	4.0	3.8	1.7	-2.2	2.8
Passenger yield, %	-4.4	0.3	3.3	1.0	2.7	7.4	3.0	9.9	-14.0	2.0
Cargo yield %	1.9	-9.5	2.0	7.4	2.4	6.9	5.9	10.2	-14.2	3.1
<b>EXPENSES, \$ billion</b>	319	311	323	376	409	450	490	573	480	513
% change	0.5	-2.7	4.0	16.2	8.9	10.1	8.8	16.9	-16.2	7.0
Fuel	43	40	44	65	91	107	134	189	113	132
% of expenses	13	13	14	17	22	24	27	33	24	26
Crude oil price, Brent, \$/b	24.7	25.1	28.8	38.3	54.5	65.1	73.0	99.0	62.0	79.0
Non-Fuel	276	270	279	311	318	343	356	384	367	382
cents per atk (non-fuel unit cost)	39.4	39.0	39.2	39.5	38.6	40.1	39.6	42.4	42.6	42.6
% change	0.9	-1.0	0.7	0.6	-2.1	3.9	-1.4	7.2	0.5	0.0
Break-even weight load factor, %	61.3	61.9	60.9	61.9	62.0	61.3	60.8	63.8	62.6	63.6
Weight load factor achieved, %	59.0	60.9	60.7	62.5	62.6	63.3	63.3	62.8	62.6	64.6
<b>OPERATING PROFIT, \$ billion</b>	-11.8	-4.8	-1.4	3.3	4.3	15.0	19.9	-8.9	-0.4	8.2
% margin	-3.8	-1.6	-0.4	0.9	1.0	3.2	3.9	-1.6	-0.1	1.6
<b>NET PROFIT, \$ billion</b>	-13.0	-11.3	-7.5	-5.6	-4.1	3.6	12.9	-15.9	-9.4	-2.8
% margin	-4.2	-3.7	-2.3	-1.5	-1.0	0.8	2.5	-2.8	-2.0	-0.5

Source: ICAO data to 2008. IATA 2009 estimates and 2010 forecasts. Excludes exceptional accounting items and mark-to-market fuel hedging losses from net profits