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December 2007

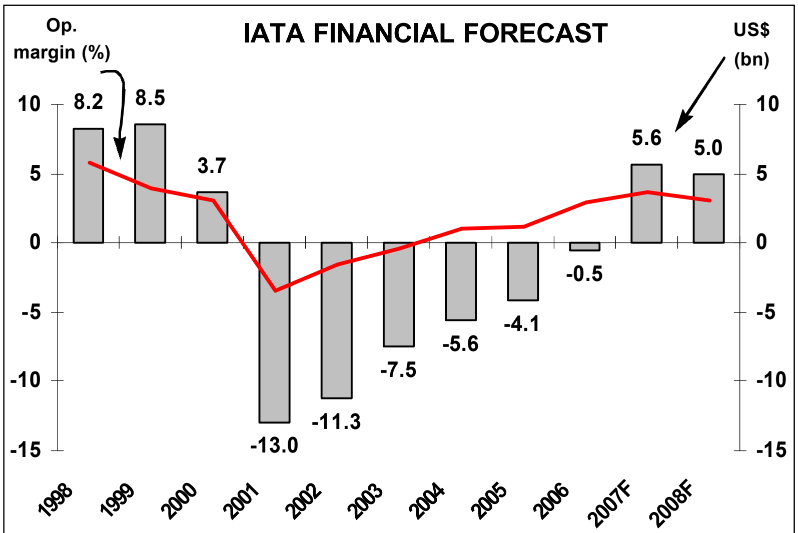
## Cycles in perspective

Crunching credit and soaring fuel is clearly not a good combination for the aviation industry. Citing these adverse developments, IATA has come out with a forecast that sees a cyclical downturn in 2008 and identifies 2007 as the peak of the market.

This means, using IATA's definition of the cycle in terms of global net profit/loss, that the recent upturn is very truncated. However, it is becoming more difficult to interpret the significance of an agglomerated forecast in an aviation world that is becoming less and less homogenous.

One of the features of the aviation scene in recent years has been the contrast between the US network carrier sector - which has been characterised by low growth, drawn-out labour negotiations and downsizing by the Legacy carriers, with minimal investment in new equipment - and the rest of the developed world. This is a huge generalisation of course, but in Europe the main network carriers are all enjoying success with variations on the global hub strategy, the Middle East super-connectors remain overwhelmingly ambitious, and SIA is pioneering the A380. Even the US LCC sector, despite the continued solid performance of Southwest and the innovative alliance strategies of JetBlue, has not been anywhere near as dynamic as Europe, where Ryanair continues to produce excellent financial results, expand its network and continuously minimalise the short haul product, to the dismay of some, to the delight of others.

It is disturbing that IATA reckons that the North America region's net profit will fall from an estimated \$2.7bn in 2007 to \$2.2bn in 2008 (this decline accounts for almost all of the forecast global downturn). This certainly goes against the perception that some of




Source: IATA, December 2007

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## CONTENTS



## PUBLISHER

***Aviation Economics***

James House, 1st Floor
22/24 Corsham Street
London N1 6DR

Tel: +44 (0) 20 7490 5215
Fax: +44 (0) 20 7490 5218

*e-mail: info@aviationeconomics.com*

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is published 10 times a year
by ***Aviation Economics***

**Editor:**
Keith McMullan
kgm@aviationeconomics.com

**Contributing Editor:**
Heini Nuutinen

**Contributing Editor:**
Nick Moreno

**Sub-editor:**
Julian Longin
jil@aviationeconomics.com

**Subscriptions**:
info@aviationeconomics.com

Tel: +44 (0)20 7490 5215

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***Aviation Economics***
Registered No: 2967706
(England)

**Registered Office:**
James House, 1st Floor
22/24 Corsham St
London N1 6DR
VAT No: 701780947

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the Legacies are now in a strong position to reap benefits from their Chapter 11 restructurings.

Then IATA is projecting a paltry $2bn net profit for Europe. But the four network carriers' (Air France/KLM, BA, Lufthansa and Iberia) combined net profits for next year are currently being forecast by equity analysts at around $6.5bn while the big two LCCs - Ryanair and easyJet - will add a further $1.1bn or so. One wonders who is going to make the counterbalancing massive losses - Alitalia can't do it all on its own.

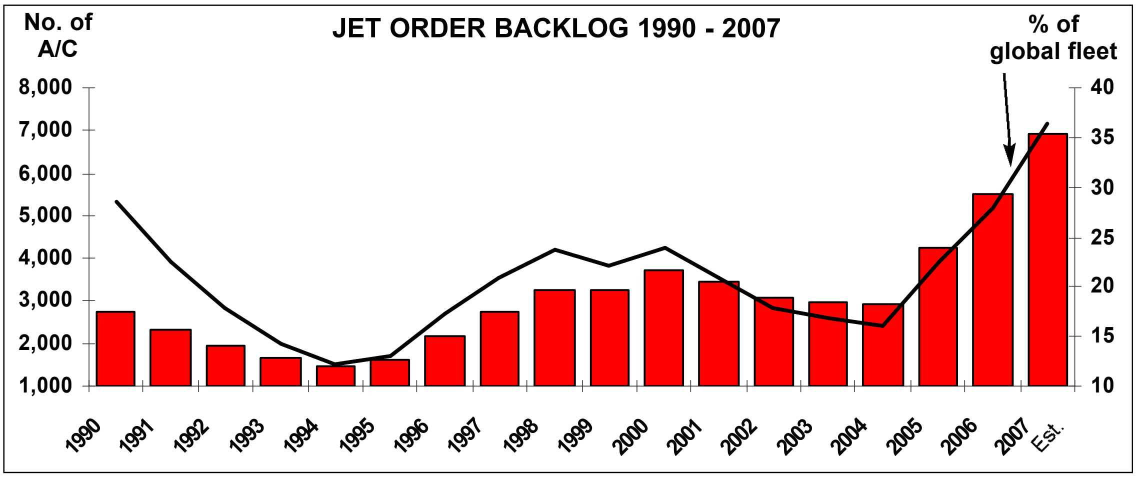
The US/rest of the world split is also reflected in apparently contrasting views of the state of the aircraft market. In the US many leading airline executives and financiers attribute the lack of profitability in the Legacy sector to systemic overcapacity and plead the case for mergers to rationalise the business. In Europe and particularly in the emergent aviation markets of the Middle East, India and China, there is a widespread view of the aircraft market as being undersupplied relative to demand, which has resulted in lease rates for modern narrowbodies doubling over the past five years, a strong escalation in second-hand prices and excessively long waiting periods for deliveries of new orders. From this perspective, a cyclical peak probably has been reached, and a slowdown would even be beneficial in taking some of the heat out of the market.

There is no sign of a slowdown in ordering activity as yet; indeed, 2007 looks to have been another record year with 2,348 firm orders booked by Airbus and Boeing (in the ratio 47/53). This compares to 1,834 last

**AIRBUS ORDERS 2007**

| | A320 family | A330 | A340 | A350 | A380 | Total |
|---|---|---|---|---|---|---|
| Aegean Airlines | 6 | | | | | **6** |
| Aercap | | 10 | | | | **10** |
| Aeroflot | 5 | | | 22 | | **27** |
| Aircastle Advisor Ltd | | 15 | | | | **15** |
| Air France | | | | | 2 | **2** |
| Avion Aircraft Trading | | 8 | | | | **8** |
| BAA Jet Management | 1 | | | | | **1** |
| British Airways | 4 | | | | | **4** |
| Comlux Aviation | 2 | | | | | **2** |
| CSA Czech Airlines | 8 | | | | | **8** |
| easyJet | 35 | | | | | **35** |
| Finnair | | | 7 | 11 | | **18** |
| Iberia | | | 3 | | | **3** |
| Israir | 3 | | | | | **3** |
| KLM | | 2 | | | | **2** |
| Lufthansa | 30 | | | | | **30** |
| MNG Airlines | | 2 | | | | **2** |
| S7 Group | 25 | | | | | **25** |
| SWISS | 2 | 9 | | | | **11** |
| TAP Air Portugal | | | | 12 | | **12** |
| Ural Airlines | 7 | | | | | **7** |
| Uzbekistan Airways | 6 | | | | | **6** |
| Vista Jet | 3 | | | | | **3** |
| Wizz Air | 50 | | | | | **50** |
| **European Total** | **187** | **46** | **10** | **45** | **2** | **290** |
| Aviation Capital Group | 45 | | | | | **45** |
| CIT Leasing | 25 | | 5 | 2 | | **32** |
| GECAS | 60 | | | | | **60** |
| Guggenheim | | 6 | | | | **6** |
| ILFC | | | | 20 | | **20** |
| Intrepid Aviation | | 20 | | | | **20** |
| Jet Alliance | 2 | | | | | **2** |
| Petters | 6 | | | | | **6** |
| Spirit Airlines | 30 | | | | | **30** |
| US Airways | 60 | 15 | | 22 | | **97** |
| **N.American Total** | **228** | **41** | **5** | **44** | **0** | **318** |
| Air Caraibes | | 2 | | | | **2** |
| Avianca | 20 | 10 | | | | **30** |
| LAN Airlines | 15 | | | | | **15** |
| Volaris | 14 | | | | | **14** |
| **L. American Total** | **49** | **12** | **0** | **0** | **0** | **61** |
| Air Asia | 50 | | | | | **50** |
| Air Blue | 8 | | | | | **8** |
| C Jet | 1 | | | | | **1** |
| Cebu Pacific | 10 | | | | | **10** |
| Fly Asian Xpress | | 15 | | | | **15** |
| Flyington Freighters | | 12 | | | | **12** |
| Go Air | 3 | | | | | **3** |
| Hong Kong Airlines | 31 | 20 | | | | **51** |
| Mandala Airlines | 25 | | | | | **25** |
| Singapore Airlines | | | | 20 | | **20** |
| Thai Airways | | 8 | | | | **8** |
| Tiger Airways | 20 | | | | | **20** |
| **Asian Total** | **148** | **55** | **0** | **20** | **0** | **223** |
| Afriqiyah Airways | 5 | | | | | **5** |
| Air Arabia | 34 | | | | | **34** |
| ALAFCO | 7 | | | 12 | | **19** |
| Al Jaber Group | 2 | | | | | **2** |
| Egyptair | | 5 | | | | **5** |
| Emirates | | | | 70 | 15 | **85** |
| Etihad | | 8 | 4 | | | **12** |
| Jazeera Airways | 30 | | | | | **30** |
| Kingdom Holding | | | | | 1 | **1** |
| Middle East Airlines | 2 | | | | | **2** |
| National Air Services | 20 | | | | | **20** |
| Nouvelair | 2 | | | | | **2** |
| Oman Air | | 5 | | | | **5** |
| RAF Oman | 2 | | | | | **2** |
| Qatar Airways | 2 | | | 80 | 3 | **85** |
| Yemenia | | | | 10 | | **10** |
| **Africa/M.East Total** | **106** | **18** | **4** | **172** | **19** | **319** |
| **Private Customer** | **8** | 1 | 4 | | | **13** |
| **Unidentified Total** | **0** | | | | | **0** |
| **Gross Total** | **726** | **173** | **23** | **281** | **21** | **1224** |

Note: Firm orders as of December 17 *Source: Airbus*




year and 2,057 in 2005, which was confidently identified as the peak of the ordering cycle.

LCCs from all continents, leasing companies and the super-connectors - notably Emirates - were the main players, though US Airways did firm up a significant refleeting programme.

**BOEING ORDERS 2007**

| | 737 NG | 747 | 767 | 777 | 787 | Total |
|---|---|---|---|---|---|---|
| Aeroflot | | | | | 22 | **22** |
| Aerosvit | 7 | | | | | **7** |
| Air Berlin | | | | | 25 | **25** |
| Air France | | | | 9 | | **9** |
| AWAS | 31 | | | | | **31** |
| Azerbaijan Airlines | 2 | | | | 3 | **5** |
| British Airways | | | | 4 | | **4** |
| Cargolux Airlines | | 3 | | | | **3** |
| DHL International | | | 6 | | | **6** |
| First Choice Airways | | | | | 4 | **4** |
| KLM Royal Dutch | 13 | | | 4 | | **17** |
| LOT Polish Airlines | | | | | 1 | **1** |
| Norwegian Air Shuttle | 42 | | | | | **42** |
| Ryanair | 27 | | | | | **27** |
| S7 Group | | | | | 15 | **15** |
| SAS | 2 | | | | | **2** |
| SkyEurope | 5 | | | | | **5** |
| Transavia Airlines | 7 | | | | | **7** |
| Travel Service | | | | | 1 | **1** |
| Uzbekistan Airways | | | | | 2 | **2** |
| Virgin Atlantic | | | | | 15 | **15** |
| **European Total** | **136** | **3** | **6** | **17** | **88** | **250** |
| Air Canada | | | | | 23 | **23** |
| AirTran | 15 | | | | | **15** |
| Alaska Airlines | 5 | | | | | **5** |
| American Airlines | 1 | | | | | **1** |
| Aviation Capital Group | 30 | | | | 5 | **35** |
| Babcock & Brown | 20 | | | | | **20** |
| Boeing Business Jet | 16 | 1 | | | 3 | **20** |
| CIT Leasing Corp. | 5 | | | | 5 | **10** |
| Continental Airlines | 4 | | | | 5 | **9** |
| Delta Air Lines | | | | 1 | | **1** |
| GECAS | 53 | | | 6 | | **59** |
| Guggenheim Av. Partners | | | | 3 | | **3** |
| ILFC | 10 | | | 1 | 52 | **63** |

| **N. America (cont.)** | **737 NG** | **747** | **767** | **777** | **787** | **Total** |
|---|---|---|---|---|---|---|
| Oak Hill Capital Partners | | | | 8 | | **8** |
| Pegasus Airlines | 6 | | | | | **6** |
| Southwest | 28 | | | | | **28** |
| UPS | | | 27 | | | **27** |
| WestJet | 20 | | | | | **20** |
| **N.American Total** | **213** | **1** | **27** | **19** | **93** | **353** |
| Copa Airlines | 4 | | | | | **4** |
| LAN Airlines | | | 3 | 2 | 26 | **31** |
| TAM | | | | 8 | | **8** |
| **L. American Total** | **4** | **0** | **3** | **10** | **26** | **43** |
| Air New Zealand | | | | 4 | 4 | **8** |
| All Nippon Airways | | | | 4 | | **4** |
| Cathay Pacific | | 10 | | 12 | | **22** |
| China Southern Airlines | 55 | | | 6 | | **61** |
| JAL International | | | | | 5 | **5** |
| Jet Airways | 20 | | | 3 | | **23** |
| Lion Air | 88 | | | | | **88** |
| Nippon Cargo Airlines | | 6 | | | | **6** |
| Philippine Airlines | | | | 4 | | **4** |
| Sky Peace Ltd. | | | | | 1 | **1** |
| SpiceJet | 10 | | | | | **10** |
| Virgin Australia | | | | 6 | | **6** |
| Virgin Blue | 10 | | | | | **10** |
| Xiamen Airlines | 25 | | | | | **25** |
| **Asian Total** | **208** | **16** | **0** | **39** | **10** | **273** |
| ALAFCO | 6 | | | | 16 | **22** |
| Arik Air | 10 | | | 5 | 7 | **22** |
| Emirates | | | | 12 | | **12** |
| LCAL | | | | | 6 | **6** |
| Qatar Airways | | | | 5 | 30 | **35** |
| Royal Jordanian | | | | | 4 | **4** |
| **Africa/M.East Total** | **16** | **0** | **0** | **22** | **63** | **101** |
| **Unidentified Total** | **62** | | | **20** | **12** | **94** |
| **Gross Total** | **639** | **20** | **36** | **127** | **292** | **1114** |
| Changes | -4 | -4 | | -2 | | -10 |
| **2007 Net Total** | **635** | **16** | **36** | **125** | **292** | **1104** |

Note: Firm orders as of December 17 *Source: Boeing*

# Europe's charter industry and the internet generation

The continuing decline of the western European package holiday market spurred the merger of four large tour operators into two giants in 2007 - Thomas Cook/MyTravel and TUI/First Choice. What does this mean for the groups' charter airlines, and for the other remaining charter carriers in Europe? In the first of a two-part series, *Aviation Strategy* looks at the overall market and the new Thomas Cook Group.

Although many tour operators initially buried their heads about the issue, today the steady shrinkage of the all-inclusive tour (AIT) market in western Europe is recognised by everyone. While tour operators release statistics that prove the overall European AIT market is growing, that's only because their definitions now include the new east European markets (and whether the mainstream tour operators can really win a significant share of those emerging markets is open to doubt). But the contributing factors for the decline in the western European market are all too obvious: the impact of the LCCs, the rise of internet booking, a change in preference for certain holiday destinations and - perhaps most important of all - a rejection by holidaymakers of the one-size-fits-all package holiday (for a more in-depth discussion of these trends, see *Aviation Strategy*, June 2005).

What's making the situation worse for the handful of giant tour operators that remain in Europe is that some of these structural changes have become even more pronounced in the last couple of years, and most particularly the rise of holidays booked via the internet. For example, internet penetration in the UK and Germany - the two largest AIT markets in Europe - continues to grow, and in 2007 42m Germans have regular internet access (representing 51% of the population), compared with 37.2m in the UK (61.2%). Research shows that it's the more wealthy, those with free time (for example, the so-called “empty-nesters” - those whose children have left home) and young urban professionals who use the internet to arrange holidays more than other groups, and those same groups now tend to book three or more shorter holidays per year rather than the single one- or two-week package that was traditional a couple of decades ago.

The core problem for tour operators is the continuing penetration of internet bookings into overall travel bookings. As can been seen in the chart, opposite, the proportion of travel expenditure made online has risen from nothing 10 years ago to 15.5% in 2006, where €38.3bn of travel bookings in Europe were made online, out of a total European travel spend of €247bn. That's a staggering amount of online expenditure, and that percentage is forecast to rise to 21.1% by the end of 2008. Of this total travel market, 56% is for air travel, 16% for hotels and 16% for package tours.

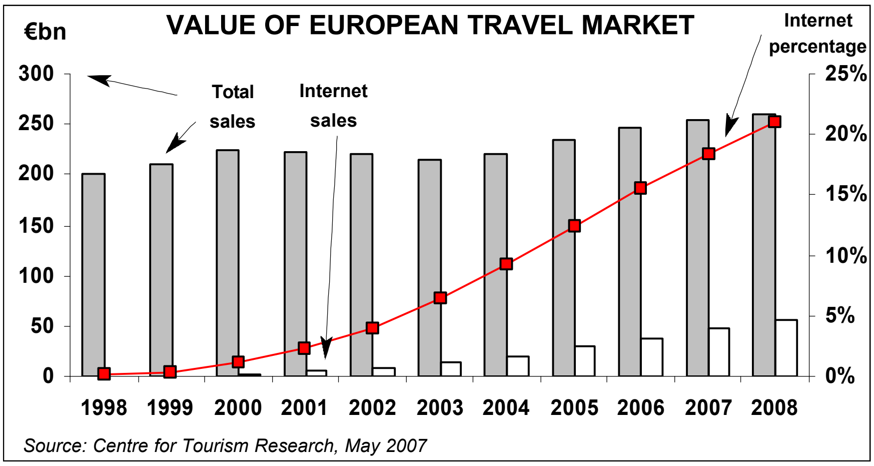
Internet booking on its own would not be a such a problem for the tour operators if it was "just" another distribution channel, but of course the major disadvantage for suppliers (and the major advantage for consumers) is that the internet facilitates simple price comparisons, and research shows that customers who buy online tend (whether they initially intend to or not) to pick products with the cheapest price. And consumers now use the web much more for actually booking travel than merely for research purposes (i.e. gathering information prior to booking a trip offline). Certainly the future of the high-street travel agent looks doomed: according to a survey by travelsupermarket.com, whereas 50% of 25-34 year olds booked a holiday via a travel agent in 1999, in 2007 only 16% did so; the rest preferred to book via the internet (68%) or through other means, such as call centres.

At the very least, the way that consumers now routinely use the internet to book holidays appears irreversible, although there are differences in the main European markets, Germany and the UK (Eurostat data shows that more than 50% of all outbound holiday trips by EU citizens are taken by German and British holidaymakers - around 77m trips a year by Germans and 48m trips by the British). According to research from IPK International, in 2006 45% of all UK outbound trips involved online booking for at least part of the trip, while another 10% of trips used information found on the internet - so that the overall "online market share" can be stated as 55%. The respective online market share in Germany is lower: 30% (which is beaten by the 40% in the Scandinavian market), and this reflects a relative reluctance by Germans consumers to use credit cards online or other e-payment mechanisms, as well as the lower internet penetration rate in Germany compared with the UK.

As a result, "in the UK more than twice as many online buyers and regular internet users buy travel than in Germany", according to a report by PhoCusWright released in September 2007, and while the German and UK markets combined accounted for 54% of the €38.3bn online travel market in Europe in 2006, the UK's spend was €13bn (34%) compared with Germany's €7.7bn (20%). This, however, is only a relative difference - in absolute terms, even in Germany this translates into 35.1m holidays booked online by Germans in 2006 (see chart, right).

But there are other differences. According to Eurostat, in 2005 (the latest year for which data is available), 69% of German holiday trips were for four nights or more and 31% for three nights or fewer, while for UK holidays, 54% were for four nights or more and 46% were for three nights or fewer. That gap is rising as UK holidaymakers increasingly use the internet to book short breaks in European cities as well as further afield. In terms of destinations, in 2005 UK holidaymakers headed for Spain (31.8%), followed by France (11.5%) and then the US (7.4%), while for Germans the spread of top destinations is more even: Spain (15.9%), Italy (14.4%) and Austria (14.4%).

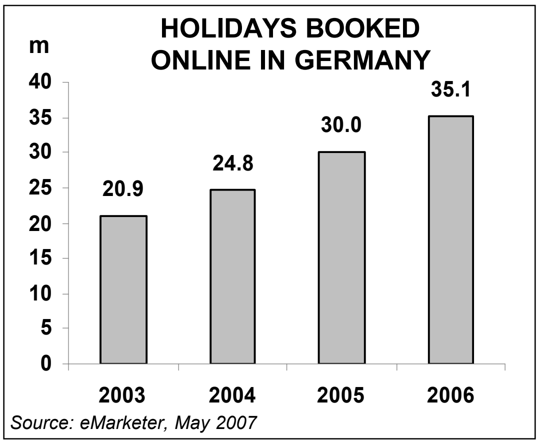
Those differences between the UK and German market are important, because they are encouraging the remaining tour operator giants to treat those countries in subtly different ways, even given the underlying structural changes in the AIT market.



Source: Centre for Tourism Research, May 2007

## The fight back?

What, if anything, can the tour operators do in the face of these structural changes, other than manage a declining market as best as possible? PhoCusWright says that tour operators have been late in responding to online distribution although they are now catching up fast, and adds the big two UK tour operators are "extremely powerful" and are a threat to online sites such as Expedia and Travelocity. Indeed while in 2002 46% of all online internet holiday bookings were made through third-party sites such as Expedia, and 54% though suppliers' (i.e. tour operators' and airlines') own websites;



Source: eMarketer, May 2007

by 2005 the suppliers' percentage had risen to 65%.

But that misses the point somewhat - while Expedia and the third-party sites are of course a competitor for tour operators, it is the airline sites (and specifically those of easyJet, Ryanair, Air Berlin etc.) that have been peeling away large amounts of business from the tour operators. This summer easyJet launched easyJetHolidays.com, which competes directly against the mainstream tour operators (and online rivals such as lastminute.com and Expedia) by packaging flights with hotel accommodation.

Tour operators, however, are working on their strategies. Peter Long, CEO of First Choice prior to the merger and now CEO of the new TUI Travel, believes that air travel is not the first item that holidaymakers buy when putting together a trip, but rather it is accommodation. That's why the latest buzzword in the tour operating industry is so-called "dynamic packaging", which allows customers to bolt together a holiday package, based primarily around choosing accommodation. This is undoubtedly a more sophisticated response by tour operators to the challenges they face, and is at the very least a recognition that seat-only sales by charter airlines is simply no longer good enough in today's ultra-competitive holiday market.

At the Thomas Cook Group, the other new tour operator giant, which continues to adhere to traditional assumptions about the European holiday market. In a strategy presentation given in November this year, TCG argued that that traditional tour operators in general - and TCG in particular - are still well placed in the overall market now (and for the future) since internet retailers have limited access to content and no packaging expertise, while the LCCs also have limited access to content, and offer a commoditised product.

This seems to miss the point that neither internet retailer nor LCCs need to have all-encompassing product as it is the customer who now has all the tools needed for the buying process, and he/she simply wants to put together whatever package of travel and accommodation he or she wants from whatever sources can provide them. TCG's new strategy of being relatively asset-light and having access to product rather than owning all of it (see below) is simply not the same as giving access to a much wider range of products - which customers can easily do themselves by using the internet.

The key question, however, is whether dynamic packaging, asset-light strategies or anything else will shore up the wafer-thin margins of tour operators? 2006 was a tough season for the European charter holiday industry, with margins under pressure even despite a relatively disciplined restraint in capacity by the major players, and this pattern was repeated in the summer of 2007, when the slowdown in demand for package holidays was most marked at the cheaper end of the market, where margins are the thinnest anyway. That's a result of even the most technophobic of holidaymaker realising that it is a simple process to book a flight and a self-catering apartment at almost any destination online, and even at the very last minute.

## Acquisitions merry-go-round

Against this background, 2007 saw the biggest upheaval in the AIT industry since the early 2000s, when TUI/Preussag bought the Thomson Travel group and C&N Touristic bought Thomas Cook (before also adopting its name).

The latest merry-go-round of acquisitions started with attempts by both the MyTravel Group and Thomas Cook AG to buy the "mainstream" holiday business of UK-based First Choice Holidays in November 2006. First Choice had previously built up a presence in the specialist and niche holiday sectors (such as activity holidays) in order to lessen its dependence on classic AIT products, and in 2006 decided to offload its low-margin mainstream business. Preliminary talks were held between First Choice and a number of interested parties, but Thomas Cook and MyTravel dropped out of the running after announcing their merger in February 2007. The only other substantial bidder for First Choice mainstream assets was reported to be Virgin Holidays, but they too pulled out in February, and in the same month First Choice issued a terse statement saying that "talks regarding the possible sale of the mainstream business have been terminated." First Choice then went on to agree a merger with TUI AG, thus completing a massive restructuring of the European AIT industry into two giant blocks - and one that if not successful will surely be followed by the merger of even these two giants into one company in the long-term.

# The new Thomas Cook Group

The EC approved the merger of Thomas Cook and MyTravel in May, even though it said there would be significant overlap in the package holiday market in the UK and Ireland. However, the EC was acutely aware of the structural decline of the AIT market and had been criticised previously for blocking a bid by Airtours (which has since become MyTravel) for First Choice in 1999 after its decision was overturned in 2002 - too late for that deal to happen.

The new Thomas Cook Group (TCG) is listed on the London stock exchange and is a gigantic concern, employing 33,000 and with 3,000 travel agency outlets and almost 50 hotels and resort properties around the world. This year TCG will have revenue of just under €12bn and carry around 19m people on holiday, with most of that business originating in the European market.

However, MyTravel (previously known as Airtours) almost collapsed in 2003, and although it had gradually recovered since then, according to some analysts Thomas Cook had the upper hand in the merger negotiations with MyTravel, in which TCG is owned 52% by German retailer Arcandor (formerly known as KarstadtQuelle, and which acquired the 50% of Thomas Cook that it didn't previously own from Lufthansa in January 2007 for €800m) and 48% by the former shareholders of MyTravel.

TCG was formally launched in June, but over the next few months a string of senior MyTravel executives announced they were leaving the merged group, including Peter McHugh, who was previously the CEO of MyTravel and then joint CEO of TCG. The last ex-MyTravel senior executive to go was John Bloodworth, formerly the managing director of MyTravel UK and (briefly) the new CEO of Thomas Cook's UK and Ireland operation, who resigned in September after what was called a "difference in management approach".

Those differences are believed to stem from the strategic emphasis of TCG's two founding partners, with the new group saying it will operate different business models in the various territories it operates in. In the UK, the primary business model will be "vertically integrated charter tour operations, based on airline ownership, committed air capacity and controlled retail distribution", but in continental European markets, "different market conditions make the vertically integrated model less effective" - which means that group-owned charter airlines are no longer considered a prerequisite for successful tour operations on the continent, unlike in the UK.

This apparently contradictory strategy will have profound effects for the group's airlines, which pre-merger operated a total fleet of 97 aircraft, although this has already been trimmed back to 92 as of December 2007 (see table, below), of which a majority are leased.

In the UK, the Thomas Cook/MyTravel merger saw the group's airlines (Thomas Cook Airlines and MyTravel Airways) come

**THOMAS COOK GROUP FLEET**

| | Thomas Cook Airlines | MyTravel Airways Denmark | Thomas Cook Airlines Belgium | Condor | Condor Berlin |
|---|---|---|---|---|---|
| A320-200 | 10 | 2 | 6 | | 13 |
| A321-200 | 4 | 5 | | | |
| A330 | 7 | 3 | | | |
| 757-200 | 16 | | | | |
| 757-300 | 2 | | | 13 | |
| 767-300ER | 2 | | | 9 | |
| **Total** | **41** | **10** | **6** | **22** | **13** |

together under the Thomas Cook Airlines brand from November of this year. Manchester-based Thomas Cook Airlines dates back to 2000 when JMC Airlines was formed from the integration of Flying Colour Airline and Caledonian Airways, the respective airlines of Carlson Leisure and Thomas Cook (which merged in 1998). JMC was renamed as Thomas Cook Airlines in 2003 and in 2006 the airline carried 4.9m passengers to more than 60 European and long-haul holiday destinations. Prior to the merger it operated a fleet of 24 aircraft, including three A320s, three A321s and 18 757s.

MyTravel Airways operated a fleet of 19 aircraft, and the disappearance of MyTravel Airways as a standalone airline ends an entity that started life as Airtours International in 1991 before absorbing European Airways in 1993 and merging with Danish airline Premiair under the name MyTravel Airways in 2002. TCG's combined UK fleet initially totalled 43 aircraft, but the enlarged Thomas Cook Airlines will not remain at that size despite the group's commitment to retain a vertically-integrated operation in the UK. TCG says that the merger of MyTravel Airways and Thomas Cook Airlines will deliver significant savings thanks to reduction in overhead and direct operating costs, and that a reduction in the size of the combined fleet should be achievable - although the extent of that shrinkage is not yet known.

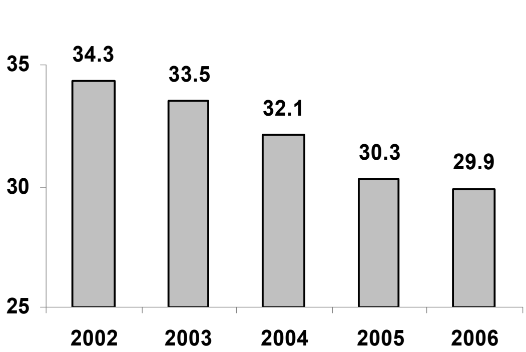
A clue, however, is given by the cuts that TCG is pushing though at its UK operations outside of the airlines. 35% of TCG revenue comes from the UK, but of the 33,000 staff employed by MyTravel and Thomas Cook pre-merger no less than 18,800 were in the UK, where the two companies had a substantial 950 travel agencies. The merger document for Thomas Cook/MyTravel admits a "relative decline in demand for package holidays" in the UK, and figures from the UK CAA show just how rapid that decline is - passengers carried by charter airlines have gradually fallen from 34.3m in 2002 to 29.9m in 2006 (see chart, below). Put another way, charter capacity as a percentage of all UK airline capacity has declined from 37% in the late 1980s to just 26% in 2006 (see chart, right).

Therefore it's no surprise that TCG is pushing through huge cuts in its operations in the UK, with around 150 travel agencies being closed and up to 3,000 staff losing their jobs. Though it's an unscientific comparison, applying a similar size of reduction to aircraft capacity would see the UK fleet trimmed by around six or seven to 36 or 37 aircraft, which could be achieved easily as current leases expire.

TCG's situation in the UK was not helped by the doubling of airport passenger duty in February 2007 as well as by the impending changes in the UK government's scheme that insures against the collapse of tour operators. The previous system relied on bonds paid by tour operators themselves, but this hasn't raised enough money to fund compensation claims, and the new scheme from April 2008 instead levies a £1 fee on all passengers booking a package holiday. This will raise at least £25m a year, but some tour operators are unhappy at the scheme (which will be run by the UK CAA) as it still does include LCCs, with which many customers book flights that are bolted on to accommodation bookings.

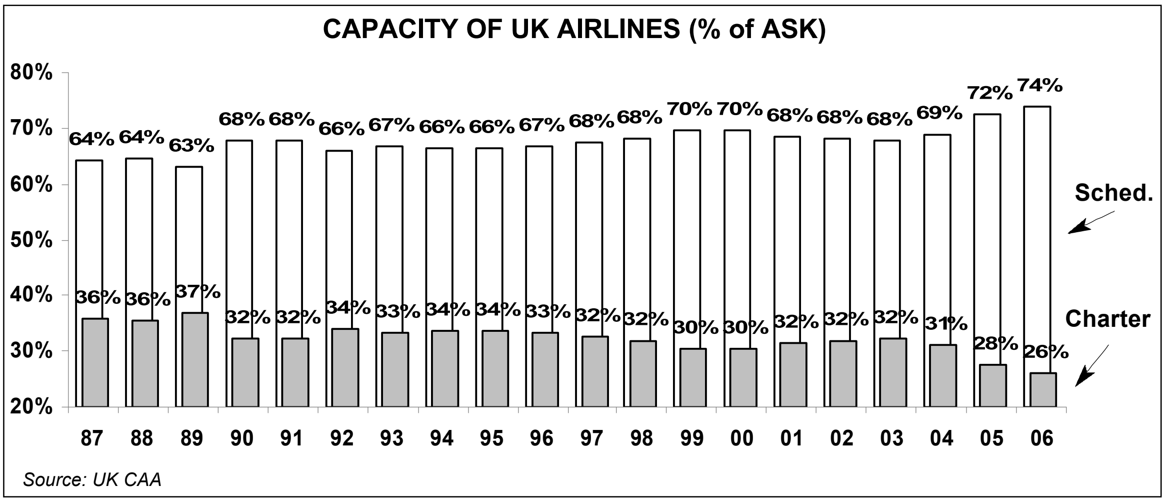
In Germany, TCG announced a deal to sell Condor to Air Berlin in September (see *Aviation Strategy*, November 2007), which is in line with TCG's new "asset-light" and non-vertical strategy in the country, which helps reduce risk and maximise flexibility (although, ironically, TCG now says it expects Condor to post record profits for the year to the end of October 2007). However, in November 2007 the Bundeskartellamt -

UK CHARTER PASSENGERS




Source: UK CAA

the German competition regulator - said it was deepening its investigation into the proposed deal, and this "second phase", as the regulator puts it, will not be completed until February 2008. Worryingly for Air Berlin, some observers believe this is possibly an indication that the Bundeskartellamt has serious concerns about the sale (since Air Berlin also owns LTU, another large German charter airline).



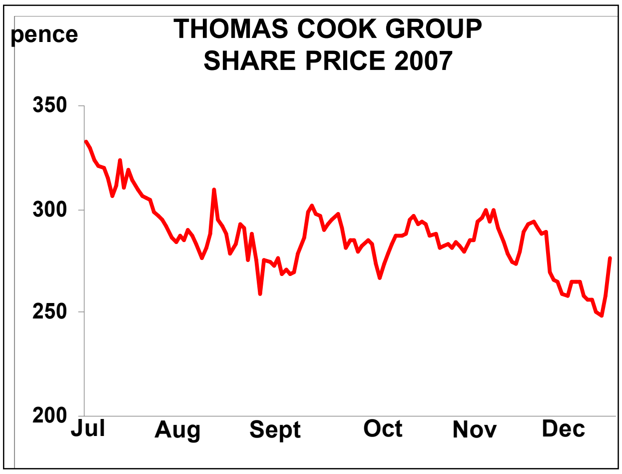

But assuming the deal is approved, while the sale will generate cash for TCG, reduce its asset base and offload a substantial €451m of financial obligations at Condor (comprising €266m of pensions and €185m of debt) what does this mean for TCG's aviation capacity out of the German market? TCG says that Air Berlin will remain a "long-term strategic partner, providing Thomas Cook with continued access to flying capacity", but the deal does make TCG vulnerable to changes in Condor's pricing, particularly if TCG offloads its shares in Air Berlin after the proposed lock-in period expires in February 2011, perhaps in order to give shareholders a special dividend.

Condor started back in 1956 and for one brief (and confusing) year in the early 2000s changed its name to "Thomas Cook - powered by Condor". It operates 35 aircraft on charter flights to 80 leisure destinations, of which more than 40 are long haul (and largely to North America, the Indian Ocean region and the Caribbean). It will carry at least 7m passengers in 2007, of which 40% will be on behalf of Thomas Cook. The rest of Condor's capacity is either sold direct via seat-only sales (36%) or to other tour operators (24%, with 6.6% sold to Alltours, 5.7% to TUI, 3.2% to Rewe and 8.5% to other companies).

As Condor has always operated on an "arm's length" basis to Thomas Cook, its sale to Air Berlin can be regarded as a sensible move given the long-term decline of the AIT market (assuming TCG can always access the capacity it needs out of the German market at a sensible price), and the deal is perhaps an indication of what may happen in the UK in the longer-term.

Elsewhere in continental Europe, TCG has six A320s at Thomas Cook Airlines Belgium and 10 A320s, A321s and A330s at MyTravel Airways Denmark, and also owns 50% of Turkish charter airline SunExpress, which operates 14 aircraft. The future for these airlines depends largely on how successful the new TCG will be. TCG talks about "improving the value proposition" to customers, which means a wider choice of distribution channel, and offering "more exclusive" accommodation. Interestingly, TCG says that in the next couple of years it plans to replace its traditional mass of printed brochures with a new system, which will replace lengthy price tables in brochures (which holidaymakers find confusing) with "continuously-updated" dynamic price calculations. Whether that will arrest the structural decline in the AIT market remains to be seen, and in the short- and medium-term much more critical for the group's future (and the future of its airlines) will be the cost savings that TCG hopes to achieve.

TCG originally forecasted merger synergies of at least €140m a year, (although there will be one-off integration costs of up to €185m), and in November TCG upgraded this to €200m, to be achieved sometime in




the next 18-24 months. Those savings may be ploughed back into acquisitions - TCG has been linked with a potential bid for Swiss operator Kuoni, which has built up revenue on independent travel and niche areas, although interest is denied by TCG, and Kuoni says it would fight off any hostile takeover bid. However, TCG also says that it is seeking shareholder permission for €375m worth of share buy backs in mid-2008, which while pleasing to hard-pressed shareholders also reduces the cash pile for acquisitions, and implies that TCG's management can't see significant value-adding opportunities at the moment. Indeed despite TCG's bullishness, the market has been unsure about the success of the merger. TCG's share price has drifted down from the 333p of its June debut to 250p in early December, although the December trading statement now appears to be sparking a revival (see graph, above).

In that trading statement released in mid-December, TCG said that early indication for summer 2008 bookings out of the UK were good, with bookings and average prices ahead of 2007, even though 2008 capacity out of the UK will be lower (by an estimated 5%) as the group was "adjusting the combined flying programmes to exit unprofitable business and optimise yield management". TCG says bookings out of Northern Europe for summer 2008 have also started strongly, although - ominously - TCG declines to give any guidance for summer 2008 bookings out of Continental Europe. The German market is more difficult for TCG because of overall overcapacity, and alongside a reduction in its own capacity TCG is also increasing commission to German travel agents in order to encourage them to sell more TCG packages.

Alongside the trading statement, TCG released unaudited pro forma results for the year to the end of October 2007, and revealed a provisional set of financial results that were higher than market expectations. While revenue fell by 1% to €11.7bn over the year compared with 2005/06, operating profit rose 26% to €375.3m, and of that €121.5m came from the UK (+36% year-on-year) and €109.7m from Northern Europe (+18%). But whereas the "Airlines Germany" segment (i.e. Condor, which TCG is selling) saw its unaudited operating profit rise 79% in 2006/07 to €68.1m, profits at Continental Europe (which includes the vital German market) were virtually flat at €99.5m. While TCG made an overall operating margin of 3.2% (compared with 2.5% in 2005/06), there was a strong contrast between the 9.2% margin in the Northern Europe market, the 8.9% margin of the soon-to-be-gone Airlines Germany/Condor, and the 2.6% and 2.2% margins in the UK and Continental Europe respectively.

So while analysts were impressed with the overall figures, the margin situation in the key UK and Continental Europe markets is still not great, and where those margins go in the current financial year will be a crucial indicator of the success (or otherwise) of the enlarged TCG's strategy, and whether the group can really achieve a stretching target of at least a €620m operating profit in 2009/10. While TCG aims to increase revenue from independent travel to 25% of total targeted revenue of €13bn in 2009/10, TCG will still be dangerously exposed to the mass package travel market (which will still represent 72% of all revenue in 2009/10, compared with 80% in 2005/06). Any improvement or erosion of margins in the key mass AIT markets of the UK and Germany will have significant effects on TCG's overall performance, and hence on its long-term future.

# Grupo Marsans: building a South Atlantic empire

Grupo Marsans, the Spanish transport and tourism giant, astonished the aviation industry by signing an MoU for 61 Airbus aircraft in October, with a list price of more than €5bn. What are Marsans' long-term ambitions, and how will the expansion of its airlines impact on Iberia, the group's key competitor?

The origin of Marsans dated back to 1910 but today the group is owned by entrepreneurs Gonzalo Pascual and Gerardo Diaz and encompasses businesses across the whole of the travel and tourism industry, from tour operators and travel agencies to hotels and airlines.

Until recently, however, Marsans' airline operation has been seen as just one part of the group's many travel and tourism businesses (last year Marsans had revenue of €4.5bn, of which 40% - €1.8bn - came from the group's airlines), and one that had relatively little impact on the global aviation industry - but that all changed in October this year.

The MoU agreed that month is for 12 A319s, 25 A320s, five A321s, five A330-200s, 10 A350-900s and four A380s, and along with an existing order for 12 A330-200s placed in December 2006, this brings the total order book for Marsans to 73 aircraft.

Though timetables are not definitive until the MoU is formally turned into an order, it is believed that the A380s (for which Marsans will become the launch customer in both Spain and Latin America) will be delivered from 2010, with two aircraft destined for each of Air Comet and Aerolineas Argentinas, the main parts of Marsans' aviation division, with two aircraft stationed at Buenos Aires and two at El Prat airport in Barcelona. The A350s will arrive in 2013-2014, while the other aircraft will be delivered over 2008-2014, although Marsans has not yet disclosed precisely where these aircraft will be placed among its airlines.

However, what is known is that the new fleet will be used to build up a substantial operation based around hubs in Madrid, Barcelona and Buenos Aires in a direct challenge to the majors operating on European-South American routes, and specifically to Iberia.

The rationale for Marsans' aggressive expansion is straightforward: the group's management has identified Spain-Latin America as a high margin, growing market, with relatively little competition to the established flag carriers on the sector.

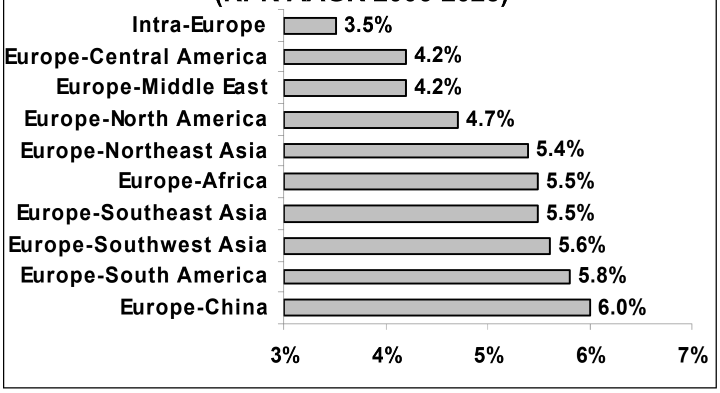
**GRUPO MARSANS FLEET**

| | Fleet | Orders | Options |
|---|---|---|---|
| **Aerolineas Argentinas** | | | |
| **A310** | 2 | | |
| **A340** | 5 | | |
| **737-200** | 18 | | |
| **737-500** | 13 | | |
| **747-200B** | 1 | | |
| **747-400** | 2 | | |
| **Total** | **41** | **0** | **0** |
| **Austral Lineas Aereas** | | | |
| **MD-80** | **16** | **0** | **0** |
| **Air Comet Chile** | | | |
| **737-200** | **5** | **0** | **0** |
| **Air Comet** | | | |
| **A310** | 4 | | |
| **A320** | 3 | | |
| **A330** | 3 | | |
| **A340** | 3 | | |
| **Total** | **13** | **0** | **0** |
| **Unassigned orders** | | | |
| **A319** | | 12 | |
| **A320** | | 25 | |
| **A321** | | 5 | |
| **A330-200** | | 17 | 10 |
| **A350-900** | | 10 | |
| **A380** | | 4 | |
| **Grupo Marsans Total** | **75** | **73** | **10** |

## A booming market

A key driver is demographics, with the latest forecasts showing that Latin America's population is expected to increase by almost 50% over the next 50 years - compared with an expected popula-

**BOEING'S EUROPEAN MARKET FORECASTS (RPK AAGR 2006-2025)**

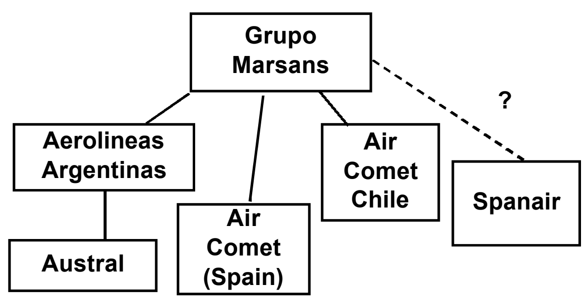



tion decrease over the same period in Europe.

Also crucial is the economic resurgence in much of Latin America, which is nudging upwards the disposable income of the expanding "middle classes" in the region. Although politically much of Latin America has turned leftwards in protest at what is seen as the patronising attitude of the Bush administration towards the continent, more often than not this is being accompanied by economic liberalisation from the region's governments. As Boeing puts it, better access to private capital is having "a profound impact", and "the ability to fund new aircraft purchases is allowing airlines to revitalize their fleets and pursue growth strategies".

Gradual liberalisation of the aviation regulatory regime in Latin America (including the spread of fifth freedoms) is also helping, and the emergence of a wave of LCCs has transformed the two largest markets in Latin America: Brazil and Mexico. Boeing's latest market forecast, released in the summer of 2007, forecasts a 6.6% average annual growth rate in intra-Latin American traffic over the 2006-2025 period, well above the global growth rate of 5% p.a.

**GRUPO MARSANS GROUP STRUCTURE**




But much more exciting from Marsans' point of view is the potential for traffic growth to/from Latin America, and the overall Latin America-Europe market is expected to have above average traffic growth over the next 20 years. Traditionally, the largest continental traffic flow has been to North America, accounting for up to 60% of all international traffic to/from Latin America, with Europe at around 20% - but Europe's share is rising. According to Airbus, traffic between Western Europe and South America will see average annual traffic growth of 6.4% over the 2006-2025 period, which by 2025 will make it the fourth-largest intra-continental passenger market in the world, behind Western Europe-North America, Asia/Pacific-North America and Western Europe-Asia/Pacific. Over 2006-2025, Boeing forecasts the European-South American market will have the second-highest growth rate of any international market out of Europe (see table, left), behind only the Europe-China market.

What is even better news for Marsans is that a large part of this Latin America-Europe traffic passes through or arrives at/departs from Spain. According to data from Iberia, in 2006 there were 4.8m passengers carried between Spain and Latin America, and this flow to/from Spain represented a hefty 30% of all passengers between Europe and Latin America (the country with the next biggest share was the UK, with 13%). Spain's share has grown from 20% since 1999, with Spain-Latin America traffic increasing by an average annual growth rate of 8.3% over the last seven years, compared with a 1.3% growth rate in traffic between Latin America and the rest of Europe.

Iberia says that 10% of passengers carried on the Europe-Latin America sector are business travellers, of which Spain-Latin America has a 23% market share (16% in 1999), and again there has been a greater increase in business traffic on routes to/from Spain and Latin America (6.6%

growth p.a. over 1999-2006) than between the rest of Europe and Latin America (0.7% annual growth).

Spain's share of the Europe-Latin America market is set to keep growing, fuelled by trends in business (Spain is the single most important foreign investor in the whole of South America, and the number one foreign investor in Argentina) and - crucially - by immigration. The booming Spanish economy, along with the fact that Spain's birth rate is the lowest in Europe, has forced the government to encourage migration. An estimated 300,000 Argentines entered Spain in 2001 following the country's economic collapse then, and Spain's socialist administration (elected in 2004) has granted an amnesty for up to 1m illegal immigrants living in the country. But according to the United Nations Population Division, Spain needs a substantial 12m immigrants from 2004 until 2050 in order to maintain the labour force level it needs.

It's against this background of increasing demand on Spanish-Latin America routes that Marsans placed the largest ever aircraft order by a Spanish company, which are destined for the group's various airline interests:

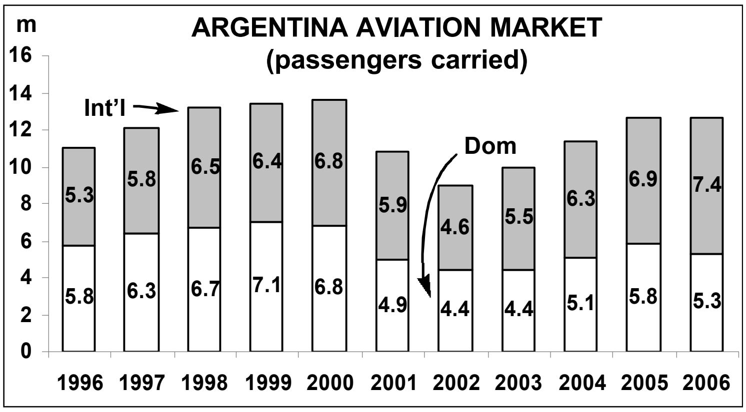
## Aerolineas Argentinas

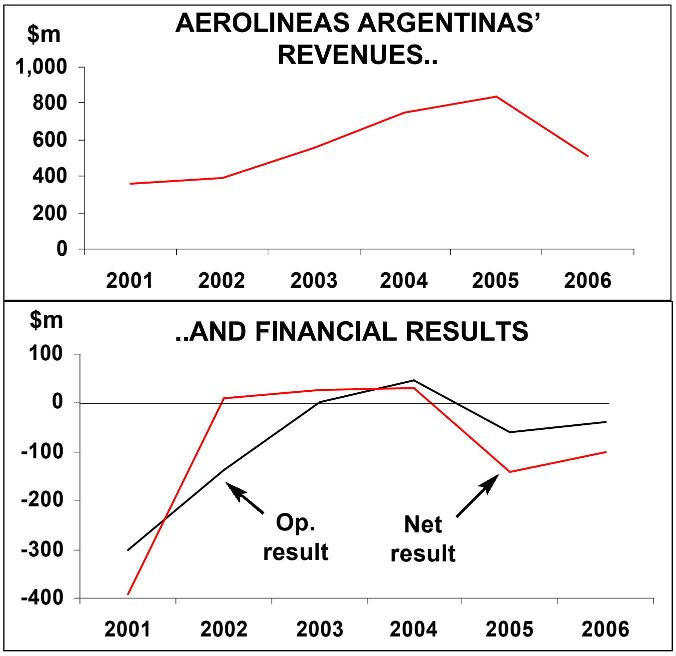
Aerolineas Argentinas was launched back in 1949 and privatised in 1990, but despite Iberia and then American Airlines taking stakes and investing substantial sums, dismal management meant that the airline lurched from one crisis to another, culminating in the events of 2001 when the airline went into bankruptcy protection, suspended all long-haul flights and sold aircraft and other assets in a desperate attempt to keep operating.

Air Comet/Marsans acquired a 92.1% stake in Aerolineas in October 2001 in exchange for assuming the airline's $1.8bn debt. Marsans also injected €40m and - helped by the devaluation of the Argentine peso, an increase in tourism and new management - the airline came out of administration in 2002. Fleet renewal was started in 2004, and for the last few years the airline has been expanding its route network, particularly in South America. Today the airline has approximately 7,000 employees, which operate a fleet of 41 aircraft to 33 domestic and 22 international destinations, of which 11 are in South America, four in North America, five in Europe and two in the Asia/Pacific region.

Aerolineas is based in Buenos Aires (where 11.5m people live, out of a total population of 38.5m) and carried 2.4m passengers in 2006. But despite the resurgence in the Latin American aviation industry in general and a reduction in the airline's net loss to $100m in 2006 (see charts, page 14), all is not well at the carrier.

Firstly, Aerolineas had expected to break even in 2006, but the latest forecast is for this to occur no earlier than 2008, and the main reason for this is that the economic recovery in Argentina - though impressive - has still not returned the economy to the strength it had back in the 1990s. While GDP has grown in Argentina by at least 8% a year since 2002, this has to be set against the context of the staggering 62% collapse in GDP in 2002 compared with 2001, which means that Argentina's annual GDP is still below the levels recorded in 1990s. This pattern has repeated itself in terms of aviation demand, and although traffic has recovered through the 2000s, while international traffic has recovered to (and beaten) the 2000 figure, domestic traffic still lags behind the levels achieved in the 1990s (see chart, below). Indeed Argentina's domestic traffic fell in 2006 compared with 2005 due to industry labour conflicts and safety issues in the domestic aviation infrastructure (when radars had to be operated manually). As






Aerolineas Argentinas and its affiliate Austral (see page 15) have just under an 80% share of the domestic market, this sluggishness in non-international traffic has slowed the airline's return to profitability.

To make matters worse, the relatively weak challenge that Aerolineas and Austral have faced from competitors cannot last forever. While Latin American airlines only provide 25% of international capacity to/from Latin America as a whole, in 2006 Aerolineas had an approximate 33% market share of international traffic to/from Argentina. Aerolineas is still increasing international capacity; for example, a daily Buenos Aires-Asuncion (Paraguay) route was restarted in August after being axed back in 2001, while Aerolineas increased frequency over the summer on routes to Auckland and Sydney. However, Aerolineas's international market share is vulnerable.

Currently the main competitor to Aerolineas is LAN Argentina, which started operations in 2005 and today operates a fleet of five A320s and two 767-300ERs to nine domestic and five international destinations. It had a 20% domestic market share in 2006 but has substantial expansion plans, and has applied to serve another four domestic and 20 international destinations. The Argentine government has complained previously about Aerolineas's scaling back of services to secondary domestic destinations, and is keen to encourage new services. Unlike the situation in Brazil and Mexico, Aerolineas has never faced a challenge from a LCC (Aerolineas signed an interline deal with Brazilian LCC Gol over the summer), but a number of new airlines have applied for permission to launch domestic operations in Argentina, including Silver Sky, Sudamerica Air and Crucero del Norte. It's inevitable that some of these will operate an LCC business model, and one low cost competitor will definitely be AirPampas, which former Aerolineas Argentinas president Antonio Mata aims to launch with a fleet of MD-80s before the end of the year.

Additionally, while Aerolineas still benefits from the government's policy of subsiding fuel costs for domestic airlines, in other areas the government is liberalising, and in 2006 restrictions on foreign ownership of airlines were abolished, which will only encourage foreign airlines to launch operations in Argentina.

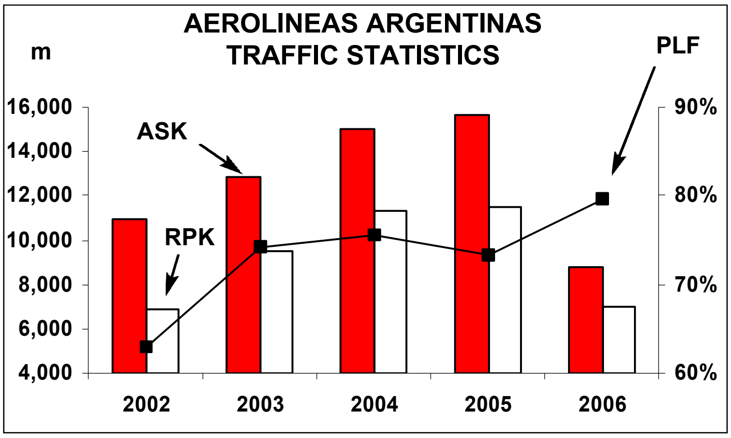
Marsans has long had a troubled relationship with the Argentine government and unions over Aerolineas, which was only improved in 2006 after a restructuring of management, when Mata - the previous president - was replaced by direct control from Marsans' owners Pascual and Diaz. In an unofficial agreement, Marsans (via a holding company called Interinvest) gave some of its shareholding to the Argentine government (increasing its share from 1.4% to 5%) and granted the government a second seat on the airline's 12-strong board in exchange for the government's permission for a 20% -plus rise in domestic and international fares (the government controls fares as part of fiscal efforts to control the inflation rate) and approval of the airline's accounts. The government had previously refused to approve any of Aerolineas's accounts since 2001 after the airline reduced the debt it owed to the Argentinean air force as part of the bankruptcy process,

The 2006 accounts were also approved in July this year, but there were objections from employee shareholders (who own 3%), which reflects that fact that although the government and Marsans may have agreed a "ceasefire", large differences still remain between Aerolineas's workforce and Marsans.

Management concluded a round of pay talks with unions earlier this year, but a 16.5% pay rise for pilots, engineers and ground staff came about only after industrial action by check-in staff in June, which was initially countered by a threat of dismissal by the airline. That episode left resentment among the seven major unions that represent staff at Aerolineas, and this increased after Pascual stated that aircraft from the recent order will only be given to Aerolineas if the unions, management and Argentine government sign an "accord" that will ensure stability at the airline over the next few years. Negotiations are ongoing with unions, and Marsans expects to sign a pact before Christmas, but it is unclear what exactly this accord will contain, although union sources suggest it will cover a five-year period and that at its heart is a no-strike clause that management wants from unions. For unions that are naturally suspicious about Spanish control over a South American airline, this may be a concession too far.

The continuing tension between staff, management and the government has encouraged some observers to believe that Marsans would prefer to exit from Aerolineas at some point in the not-so-distant future. By doing this, Marsans wouldn't just free itself from the never-ending financial and labour problems of Aerolineas, but it would also raise funds for its aircraft orders and possible bids for other airlines.

By making an exit Marsans would also escape the need to continue fleet renewal at Aerolineas, whose aircraft still have an average age of just less than 20 years; in 2006 the airline had to temporarily suspend its key Buenos Aires-New York route following a shortage of aircraft. In the summer of 2007 Aerolineas leased a number of A320s, A330s and A340s, which are replacing 747-200s and 737-300s. Of the current 41-strong fleet 18 are 737-200s, although there are now 13 737-500s, of which seven were added on leases this year (three of which




came from BCI). Two A340s-300s and two A310s were also added to Aerolineas's fleet in 2007, again all on leases.

With sources indicating that as many as 40 of the 73 aircraft Marsans has on order could be destined for Aerolineas Argentinas, if Marsans did sell its stake in the airline this would free up a tremendous amount of capacity that Marsans could place elsewhere in its growing aviation empire.

Marsans continues to deny that it wants to sell Aerolineas, but there have been tentative plans for a partial float of between 20%-25% of the airline since early 2006. However, complicating the issue is the fact that in November the Argentine government said it was exercising an option to acquire another 15% in Aerolineas (which will bring its stake to 20%). The method is yet to be confirmed, but will be either via an issue of new shares or by acquiring some of Marsans' stake. Sources indicate that Marsans would prefer to sell 15% of its stake for cash, whereas the Argentine government would prefer to "pay" for the shares by writing off Aerolineas's tax liabilities. But before this can happen the wide gulf in the airline's estimated value will have to be bridged, with the government's reported estimate of around $400m being significantly lower than the $1bn-plus that Marsans is believed to value Aerolineas at.

## Austral

Speculation over Marsans' commitment to Aerolineas has only been encouraged by developments at Austral Lineas Aereas, the

Buenos Aires-based regional subsidiary of Aerolineas that was launched in 1971 and which merged with Aerolineas Argentinas in 1999. The airline operates a fleet of 16 MD-80s on regional and feed routes to around 18 domestic destinations, and carried 1.8m passengers in 2006.

If Marsans did want to sell Aerolineas, then a logical first step would be to separate out Austral from Aerolineas, because Marsans could then use Austral as a feeder into the long-haul routes offered by Air Comet, which could be upgraded to be the main transatlantic airline for Marsans. And indeed Marsans now appears to be separating out the previously integrated operations of Aerolineas and Austral, with a reshuffling of fleet that has turned Austral into an all MD-80 operator, with its former 737-200s and 737-500s being transferred to Aerolineas - although in the medium-term the MD-80s may be replaced by the A320s on order by Marsans. Additionally, from this summer Austral aircraft have dropped the AA condor logo on their livery, replacing it with AU letters.

## Air Comet Chile

Marsans' other asset in Latin America is Air Comet Chile, which was launched by Marsans as a domestic carrier called Aerolineas del Sur in 2004. However, it was rebranded in September this year as Air Comet Chile, and accompanying the new name was a change in strategy, with a much greater focus on feeding passengers into Air Comet and Aerolineas Argentinas at Buenos Aires and elsewhere in Latin America.

Air Comet Chile has just under a 20% market share of the domestic Chilean market, having overtaken rival Sky Airlines (with which Marsans has been linked as a potential acquisition), although it is substantially behind LAN, which has a 65% domestic market share. Air Comet Chile has expansion plans, and has been opening new routes (both domestic and international) at the rate of around one per month this year, with international routes to Buenos Aires and Lima planned before the end of 2007. The airline currently operates five 737-200s on six domestic routes.

## Air Comet

Madrid-based Air Comet is a scheduled airline that was originally launched as a long-haul charter carrier in 1997, operating out of Madrid and Palma de Mallorca under the name Air Plus Comet. Marsans acquired 100% last year after buying the 30% owned by Antonio Mata for a reported €100m, which followed Mata's exit as Aerolineas's president in order to cool the worsening relations between that airline and the Argentine government.

It became Air Comet in January 2007, relaunching itself as a full-service, scheduled airline with a new livery and logo. At the same time it was designated as an airline between Latin America and Spain after taking over the Latin American routes operated by LCC Air Madrid, which collapsed in December 2006.

At that time Air Comet transported home 5,600 passengers stranded throughout South America for a flat fee of €200, but although the airline agreed with the Spanish ministry of industry to hire half of the Air Madrid workforce (578 out of 1,156), in actual fact Air Comet only took on 247, thanks to fewer staff than anticipated wanting to transfer across, as well as the rejection of "unsuitable" people.

While Air Madrid was a LCC, Air Comet relaunched itself as a full service airline, even though only a few months earlier - in September 2006 - Pascual said Air Plus Comet would restructure itself as a LCC. Precisely when the change of strategy came about is uncertain, but it must have been made between September and December, when the order for the initial 12 A330s was placed, and when Marsans first started to exploit synergies between its carriers in a meaningful way. Certainly before late 2006 there was no sign that Marsans was pursing a group strategy for its aviation assets, and until then Air Plus Comet, Air Pullmantur (a small charter carrier and associated cruise ship business that Marsans sold in 2006 for €450m) and Aerolineas Argentinas had operated independently.

Today Air Comet operates a fleet of 13 aircraft, and these are used on 13 routes out of Madrid to Latin America (Buenos Aires, Santiago de Chile, Bogotá, Lima, Quito, Guayaquil, Havana, Santo Domingo, San Jose, Santa Cruz) and Europe (Paris CDG, Rome and London Gatwick). Since January Air Comet has steadily been launching further routes and frequencies as it seeks to build up a network of daily flights to "all the important business centres in Latin America" (although it also operates some charter flights out of Madrid and Barcelona to Latin America and the Canary Islands). For example in March it launched a three-times-a-week service between Madrid and Santiago de Chile in competition - naturally - against Iberia.

And that's the key to Air Comet's (and Marsans') long-term strategy: a focus on constructing a network of routes out of Spain to all the main city destinations in Latin America. While the A380s it will receive (at least two and possibly four if Marsans exits from Aerolineas Argentinas) are likely to be used on shuttle routes between Madrid and Buenos Aires (but only if Madrid Barajas can handle them) and possibly to other destinations such as Sao Paulo and Mexico City, it is the A330s and A350s that will be at the heart of Air Comet's strategy as it constructs a dense network of routes into Latin America.

In 2008 Air Comet will increase frequency on Madrid-Lima to a daily service and on Madrid-Bogota to a five-a-week service, and new routes under consideration include Madrid-Cartegena-Medellin. This would be worrying enough for Iberia on its own, but Marsans also intends to outflank the flag carrier by building up a long-haul hub not only at Madrid but at Barcelona as well. In fact Marsans intends to build Barcelona's El Prat airport into its prime European hub, with long-haul flights to Latin America, North America and the Asia/Pacific region connecting in with European feed flights.

For historical reasons Barcelona versus Madrid issues are sensitive in Spain, but Barcelona is better suited to be the prime hub in Spain for a variety of reasons, including geography (Barcelona is closer to the centre of Europe than Madrid); business travellers (given the concentration of commerce in Catalonia, Barcelona has a better catchment area for business passengers than Madrid) and infrastructure (according to Marsans, Madrid's Barajas airport is not prepared for A380 operations, unlike El Prat).

On long-haul, Marsans is analysing a number of routes out of Barcelona, with Buenos Aires, Mexico City, Lima and Quito on a long list of destinations under consideration, but of course what Marsans does not have at Barcelona is the depth of domestic and European feeder flights that Iberia has at Madrid, and creating such a network is a priority with Marsans. It's possible that a large part of the 42 A320-family aircraft on order will be heading for Air Comet, but the only definite European destination among the large number that Air Comet is believed to be considering is Milan. However, growing Air Comet organically is not the only option that Marsans has in building a European network.

## The Spanair bid

Spanair is second-largest Spanish airline after Iberia, employing 3,600 and carrying 18.8m passengers in 2006. It's currently owned 100% by SAS, but in June the Scandinavian group announced it would sell the airline as part of restructuring (see *Aviation Strategy*, May 2007).That decision appears unrelated to labour unrest at the airline, where cabin crew unions staged industrial action in the summer over disagreements on the implementation of a collective pay deal (although the dispute was settled after a month).

Pascual and Diaz, the owners of Marsans, co-founded Spanair with SAS in 1986, but gradually sold off their 51% stake to SAS in late 2001 and 2003. In a move to simplify the process of a full bid, in June this year Marsans sold its remaining 5.1% stake in Spanair (held via an affiliated company called Tenvier) to SAS for an undisclosed sum, with Marsans saying it now had an "all or nothing" strategy for Spanair.

Gonzalo Pascual, the president of Marsans, also stepped down as chairman of Spanair in October this year in order to prepare the Marsans bid for Spanair without having a conflict of interest, and his departure followed the resignation of Gerardo Diaz as

CEO of Spanair.

The acquisition of Spanair would increase Marsans' aviation revenue by two-thirds - in 2006 Spanair had turnover of €1.2bn (and an operating profit of €23m). More importantly, the move would make strategic sense for Marsans: Spanair is based in Palma de Mallorca and operates a fleet of 60 aircraft domestically and within Europe to almost 40 destinations, (of which 20 are in Spain). There would have to be a reshuffling of services, but Spanair would deliver large amount of feed for Air Comet's long-haul network, although Pascual says that if Marsans acquires Spanair, it will be changed from being a feeder airline only into a classic short-and long-haul network carrier. Spanair used to operate long-haul routes to North America with 767s, but SAS closed down the routes in 2002 because of the intensive competition on the sector.

A Marsans-owned Spanair would restart long-haul routes, though the precise destinations will depend on the co-ordinated network strategy with Air Comet (and Aerolineas Argentinas, if it remains part of the Marsans group).

Spanair is part of Star (it joined in 2003), and Marsans hints that not only would Spanair remain in the global alliance if the group succeeds in acquiring it, but that both Air Comet and Aerolineas could join Star in the future. Star has a gap in its South American network following Varig's forced withdrawal from Star earlier this year, and the Marsans group would be an attractive addition to the existing Star members.

However, Marsans acquisition of Spanair is not 100% certain, even though in October Marsans (via Tenvier) paid SAS €43.5m for 55% of Newco, which provides ground handling services to Spanair and other airlines at a number of Spanish airports, including Barcelona. In June (at the time of the sale of Marsans' last 5% in Spanair) Pascual said that a formal bid for Spanair would be launched by the end of September, but this did not happen, and the timetable for a completion now appears to have slipped to early 2008 at best, and is more likely to happen in the second quarter of 2008. In October SAS appointed a foreign bank to look for other bidders for Spanair (Air Berlin was reported as being interested in Spanair, although the airline denies this), but this may be a means of getting a higher price from Marsans, with the airline believed to be valued at around €0.5bn.

Even though the Marsans acquisition is still expected to go through in 2008, Pascual has warned publicly that Marsans will not pay an inflated price for Spanair, and that if SAS holds out for too much money Marsans will walk away.

Intriguingly, Marsans says it may bid for Iberia if the Spanair bid fails, but this may be an attempt to warn off Iberia, which itself is said to be interested in buying Spanair - though a flag carrier bid for Spanair would surely be blocked by Spanish or EU regulatory authorities. But what is certain is that if Marsans does buy Spanair then the challenge to Iberia from the Marsans group will be even greater.

## Iberia danger

Even without the Spanair factor, Marsans' plans are a huge problem for Iberia. Spain-Latin America is the area where the Spanish flag carrier earns its highest margins, and the airline want to expand significantly on the sector while cutting back on unprofitable short-haul routes in Europe (see *Aviation Strategy*, December 2006).

Sources suggest that growth of Air Madrid's long-haul routes out of Barajas airport prior to its collapse in December 2006 had significantly worried senior Iberia management, but that once the airlines' routes were rescued by Air Comet, some Iberia executives believed that the competitive threat would be minimal. However, now that Marsans has committed to a huge Airbus order and large capacity increases on Spain-Latin America routes, Iberia's executives are no doubt scurrying to analyse how they can react. Iberia will be desperate to avoid fare wars on routes out of Madrid, but maybe even more of a worry in the long-term will Marsans' commitment to building a long-haul hub out of Barcelona, because if a significant chunk of business travellers get used to flying out of Barcelona there will be relatively little that Iberia can do about it.

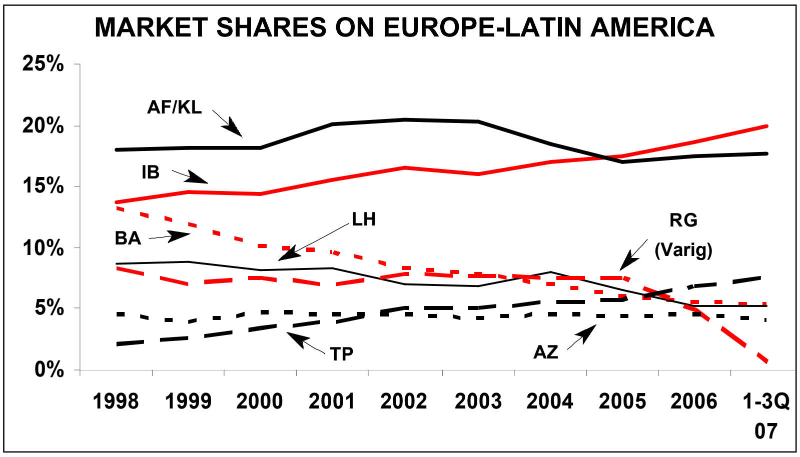
Iberia has steadily increased its market share on Europe-Latin America routes to 20% in the January-September 2007 period (see chart, left), helped by Lufthansa's strategic retreat from South America-European routes and the crisis at Varig, but given the Marsans push it's inevitable that Iberia's market share will start to retreat in the near future. The vital question, of course, is what will happen to margins? If - and it's a big if - Marsans' deep pockets encourage cut-throat price competition on routes out of Madrid in order to win market share and/or damage Iberia, then Iberia will be in deep trouble given the contribution that this sector makes to Iberia's bottom line.

Interestingly, in an exhaustive 134 slide presentation given by Iberia to analysts and investors in early November, Marsans was not mentioned at all and Air Comet referred to only once (and only as a maintenance customer). In terms of competitors, the focus of that presentation was almost exclusively on flag carriers - but this doesn't necessarily mean that Iberia is underestimating the threat from Marsans.

Though Iberia has been adding larger capacity aircraft on its routes to Argentina through 2007, the prospect of Air Comet (and Aerolineas Argentinas) potentially operating A380s on the key Madrid-Buenos Aires route (the most lucrative long-haul market out of Spain) cannot be pleasant for Iberia's management. Currently Iberia operates 30 direct flights a week on Madrid-Buenos Aires, competing against 10 flights a week from Air Comet and 32 from Aerolineas Argentinas.

In the January-September 2007 period 68% of Iberia's long-haul traffic at Madrid connected to domestic or European destinations, and it is this connecting network that Marsans is trying to replicate through Air Comet and - if successful - via the acquisition of Spanair.

Within Spain there is speculation that Marsans' ultimate goal really is to make a bid for Iberia, and now that the BA/Texas Pacific bid for Iberia has been withdrawn, then irrespective of what happens with Spanair, Marsans may move for Iberia. All Marsans will say on the record is that it does have the




ability to make a bid for Iberia, although there are unconfirmed reports that it has lined up a major bank to advise it on a bid for Iberia.

## Flexibility

Whether Marsans will make a serious bid to acquire Iberia is unknown at this stage, but the key to understanding Marsans' future strategy is to realise that while its vision is clear - of building a substantial Spain-Latin America network, with feeder routes at both ends - Marsans' tactics in achieving this goal are flexible.

The giant Airbus order gives Marsans assured capacity over the next decade, and just which airline is operating those aircraft - whether Air Comet, Spanair, Aerolineas Argentinas or anyone else - is unimportant. What does count is where those aircraft operate to/from and, on the European side, building up a network at Barcelona (and to a lesser extent at Madrid) is the priority, no matter what livery the aircraft fly under. If the Spanair deal does not come off, then Marsans will simply use many of the 42 A320 family aircraft on order to build up large feed network in Spain via Air Comet regardless.

Marsans executives confirm that the size of the Airbus order will not be altered according to whether the Spanair deal succeeds or fails, and indeed they hint that further aircraft orders are likely, possibly as early as next year, with the emphasis being on even more long-haul capacity. For Iberia's management, that's not good news at all.

| | | Group revenue US$m | Group costs US$m | Group op. profit US$m | Group net profit US$m | Operating margin | Net margin | Total ASK m | Total RPK m | Load factor | Total pax. 000s | Group emp. |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Alaska** | Apr-Jun 06 | 710 | 639 | 71 | 49 | 10.0% | 6.9% | 9,389 | 7,440 | 79.2% | 4,443 | 9,347 |
| | Jul-Sep 06 | 760 | 789 | -29 | -20 | -3.8% | -2.6% | 9,895 | 7,842 | 79.3% | 4,710 | 9,467 |
| | Oct-Dec 06 | 790 | 808 | -18 | -12 | -2.3% | -1.5% | 9,261 | 6,828 | 73.7% | 4,107 | 9,485 |
| | **Year 2006** | **3,334** | **3,422** | **-87** | **-53** | **-2.6%** | **-1.6%** | **43,306** | **33,012** | **76.2%** | **24,025** | **12,933** |
| | Jan-Mar 07 | 759 | 778 | -18 | -10 | -2.4% | -1.3% | 10,652 | 7,552 | 71.0% | 5,471 | 13,236 |
| | Apr-Jun 07 | 904 | 827 | 78 | 46 | 8.6% | 5.1% | 10,448 | 8,196 | 78.5% | 5,329 | 9,748 |
| | Jul-Sep 07 | 995 | 852 | 143 | 86 | 14.4% | 8.6% | 10,225 | 8,154 | 79.7% | 4,878 | 9,753 |
| **American** | Apr-Jun 06 | 5,975 | 5,499 | 476 | 291 | 8.0% | 4.9% | 71,774 | 59,314 | 82.6% | 25,879 | 86,500 |
| | Jul-Sep 06 | 5,830 | 5,610 | 220 | 1 | 3.8% | 0.0% | 71,641 | 58,526 | 81.7% | 24,977 | 86,400 |
| | Oct-Dec 06 | 5,397 | 5,212 | 185 | 17 | 3.4% | 0.3% | 67,813 | 53,430 | 78.8% | 23,606 | 85,200 |
| | **Year 2006** | **22,563** | **21,503** | **1,060** | **231** | **4.7%** | **1.0%** | **280,052** | **224,423** | **80.1%** | **98,139** | **86,600** |
| | Jan-Mar 07 | 5,427 | 5,179 | 248 | 81 | 4.6% | 1.5% | 72,362 | 56,063 | 77.5% | 23,299 | 85,100 |
| | Apr-Jun 07 | 5,879 | 5,412 | 467 | 317 | 7.9% | 5.4% | 68,632 | 57,402 | 83.6% | 25,301 | 85,500 |
| | Jul-Sep 07 | 5,946 | 5,627 | 319 | 175 | 5.4% | 2.9% | 69,636 | 58,401 | 83.9% | 25,448 | 85,800 |
| **Continental** | Apr-Jun 06 | 3,507 | 3,263 | 244 | 198 | 7.0% | 5.6% | 45,477 | 37,605 | 82.7% | 17,596 | 43,450 |
| | Jul-Sep 06 | 3,518 | 3,326 | 192 | 237 | 5.5% | 6.7% | 47,091 | 38,691 | 82.2% | 17,328 | 41,500 |
| | Oct-Dec 06 | 3,157 | 3,137 | 20 | -26 | 0.6% | -0.8% | 43,903 | 35,036 | 79.8% | 16,603 | |
| | **Year 2006** | **13,128** | **12,660** | **468** | **343** | **3.6%** | **2.6%** | **178,500** | **144,060** | **80.7%** | **67,119** | **44,000** |
| | Jan-Mar 07 | 3,179 | 3,115 | 64 | 22 | 2.0% | 0.7% | 43,853 | 34,519 | 78.7% | 16,176 | |
| | Apr-Jun 07 | 3,710 | 3,447 | 263 | 228 | 7.1% | 6.1% | 47,622 | 39,626 | 83.2% | 18,120 | 45,000 |
| | Jul-Sep 07 | 3,820 | 3,540 | 280 | 241 | 7.3% | 6.3% | 48,836 | 40,912 | 83.8% | 17,901 | |
| **Delta** | Apr-Jun 06 | 4,655 | 4,286 | 369 | -2,205 | 7.9% | -47.4% | 60,699 | 48,364 | 79.7% | 27,221 | 51,700 |
| | Jul-Sep 06 | 4,659 | 4,491 | 168 | 52 | 3.6% | 1.1% | 63,797 | 51,150 | 80.2% | 27,556 | 51,000 |
| | **Year 2006** | **17,171** | **17,113** | **58** | **-6,203** | **0.3%** | **-36.1%** | **238,168** | **186,892** | **78.5%** | **106,649** | **51,300** |
| | Jan-Mar 07 | 4,144 | 3,989 | 155 | -130 | 3.7% | -3.1% | 56,774 | 43,794 | 77.1% | 25,325 | 52,260 |
| | Apr-Jun 07*** | 5,003 | 4,513 | 490 | 1,592 | nm | nm | 61,358 | 50,818 | 82.8% | 28,305 | 55,542 |
| | Jul-Sep 07 | 5,227 | 4,774 | 453 | 220 | 8.7% | 4.2% | 65,889 | 54,774 | 83.1% | 28,987 | 55,022 |
| **Northwest** | Apr-Jun 06 | 3,291 | 2,996 | 295 | -285 | 9.0% | -8.7% | 37,743 | 32,593 | 86.4% | 14,300 | 31,267 |
| | Jul-Sep 06 | 3,407 | 3,041 | 366 | -1,179 | 10.7% | -34.6% | 38,741 | 33,024 | 85.2% | 17,600 | 32,760 |
| | Oct-Dec 06 | 2,980 | 2,886 | 94 | -267 | 3.2% | -9.0% | 37,386 | 30,564 | 81.8% | 16,600 | 30,484 |
| | **Year 2006** | **12,568** | **11,828** | **740** | **-2,835** | **5.9%** | **-22.6%** | **149,575** | **125,596** | **84.0%** | **67,600** | **30,484** |
| | Jan-Mar 07 | 2,873 | 2,672 | 201 | -292 | 7.0% | -10.2% | 36,845 | 29,964 | 81.3% | 15,600 | 30,008 |
| | Apr-Jun 07** | 3,181 | 2,824 | 357 | 2,149 | nm | nm | 38,070 | 32,495 | 85.9% | 17,400 | 29,589 |
| | Jul-Sep 07 | 3,378 | 2,919 | 459 | 244 | 13.6% | 7.2% | 38,445 | 33,222 | 86.4% | 17,300 | 29,579 |
| **Southwest** | Apr-Jun 06 | 2,449 | 2,047 | 402 | 333 | 16.4% | 13.6% | 36,827 | 28,716 | 78.0% | 21,999 | 31,734 |
| | Jul-Sep 06 | 2,342 | 2,081 | 261 | 48 | 11.1% | 2.0% | 38,276 | 28,592 | 74.7% | 21,559 | 32,144 |
| | Oct-Dec 06 | 2,276 | 2,102 | 174 | 57 | 7.6% | 2.5% | 38,486 | 27,036 | 70.2% | 21,057 | 32,664 |
| | **Year 2006** | **9,086** | **8,152** | **934** | **499** | **10.3%** | **5.5%** | **149,123** | **108,936** | **73.1%** | **96,277** | **32,664** |
| | Jan-Mar 07 | 2,198 | 2,114 | 84 | 93 | 3.8% | 4.2% | 38,105 | 25,924 | 68.0% | 19,960 | 33,195 |
| | Apr-Jun 07 | 2,583 | 2,255 | 328 | 278 | 12.7% | 10.8% | 40,204 | 30,606 | 76.1% | 23,442 | 33,261 |
| | Jul-Sep 07 | 2,588 | 2,337 | 251 | 162 | 9.7% | 6.3% | 41,385 | 31,680 | 76.5% | 23,533 | 33,787 |
| **United** | Apr-Jun 06 | 5,113 | 4,853 | 260 | 119 | 5.1% | 2.3% | 64,499 | 54,541 | 84.6% | 18,228 | 53,500 |
| | Jul-Sep 06 | 5,176 | 4,841 | 335 | 190 | 6.5% | 3.7% | 66,377 | 55,165 | 83.1% | 18,099 | |
| | Oct-Dec 06 | 4,586 | 4,563 | 23 | -61 | 0.5% | -1.3% | 63,226 | 50,324 | 79.6% | 16,704 | 51,700 |
| | **Year 2006** | **19,340** | **18,893** | **447** | **22,876** | **2.3%** | **118.3%** | **255,613** | **208,769** | **81.7%** | **69,325** | **53,000** |
| | Jan-Mar 07 | 4,373 | 4,465 | -92 | -152 | -2.1% | -3.5% | 61,900 | 49,415 | 79.8% | 16,350 | 51,500 |
| | Apr-Jun 07 | 5,213 | 4,676 | 537 | 274 | 10.3% | 5.3% | 64,451 | 55,049 | 85.4% | 18,190 | 51,400 |
| | Jul-Sep 07 | 5,527 | 4,871 | 656 | 334 | 11.9% | 6.0% | 65,547 | 55,089 | 84.0% | 17,804 | 51,800 |
| **US Airways Group** | | | | | | | | | | | | |
| | **Year 2006** | **11,557** | **10,999** | **558** | **304** | **4.8%** | **2.6%** | **123,889** | **97,667** | **78.8%** | **57,345** | **32,459** |
| | Jan-Mar 07 | 2,732 | 2,616 | 116 | 66 | 4.2% | 2.4% | 35,411 | 27,039 | 76.4% | 19,935 | 36,000 |
| | Apr-Jun 07 | 3,155 | 2,866 | 289 | 263 | 9.2% | 8.3% | 37,144 | 30,631 | 82.5% | 22,232 | 35,485 |
| | Jul-Sep 07 | 3,036 | 2,834 | 202 | 177 | 6.7% | 5.8% | 31,653 | 26,385 | 83.4% | 14,965 | 34,321 |
| **JetBlue** | Apr-Jun 06 | 612 | 565 | 47 | 14 | 7.7% | 2.3% | 11,590 | 9,533 | 82.2% | 4,525 | 9,377 |
| | Jul-Sep 06 | 628 | 587 | 41 | -0.5 | 6.5% | -0.1% | 12,129 | 9,756 | 80.4% | 4,773 | 9,223 |
| | Oct-Dec 06 | 633 | 569 | 64 | 17 | 10.1% | 2.7% | 11,712 | 9,331 | 79.7% | 4,932 | 9,265 |
| | **Year 2006** | **2,363** | **2,236** | **127** | **-1** | **5.4%** | **0.0%** | **46,016** | **37,522** | **81.6%** | **18,565** | **9,265** |
| | Jan-Mar 07 | 608 | 621 | -13 | -22 | -2.1% | -3.6% | 11,861 | 9,562 | 80.6% | 5,091 | 9,260 |
| | Apr-Jun 07 | 730 | 657 | 73 | 21 | 10.0% | 2.9% | 12,981 | 10,840 | 83.5% | 5,587 | 9,421 |
| | Jul-Sep 07 | 765 | 686 | 79 | 23 | 10.3% | 3.0% | 13,446 | 11,020 | 82.0% | 5,528 | 9,301 |

**Notes:** ** = April to May Predecessor Company, June Successor Company; ***= April Predecessor Company, May to June Successor Company - During Q2, Delta and United were emerging from Chapter 11

**Note:** Annual figures may not add up to sum of interim results due to adjustments and consolidation. 1 ASM = 1.6093 ASK. All US airline Financial Year Ends are 31/12.

| | | Group revenue US$m | Group costs US$m | Group op. profit US$m | Group net profit US$m | Operating margin | Net margin | Total ASK m | Total RPK m | Load factor | Total pax. 000s | Group employees |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Air France/** | Apr-Jun 05 | 6,257 | 5,982 | 275 | 135 | 4.4% | 2.2% | 57,936 | 46,041 | 79.5% | 17,948 | 101,886 |
| **KLM Group** | Jul-Sep 05 | 6,790 | 6,154 | 636 | 864 | 9.4% | 12.7% | 60,472 | 50,961 | 84.2% | 18,705 | |
| **YE 31/03** | Oct-Dec 05 | 6,430 | 6,205 | 225 | 91 | 3.5% | 1.4% | 58,266 | 46,644 | 80.0% | 17,120 | 102,291 |
| | **Year 2005/06** | **25,901** | **24,771** | **1,136** | **1108** | **4.4%** | **4.3%** | **234,669** | **189,253** | **80.6%** | **70,020** | **102,422** |
| | Apr-Jun 06 | 7,282 | 6,766 | 516 | 306 | 7.1% | 4.2% | 60,839 | 49,596 | 81.5% | 19,049 | |
| | Jul-Sep 06 | 7,779 | 7,058 | 721 | 475 | 9.3% | 6.1% | 63,616 | 53,611 | 84.2% | 19,600 | |
| | Oct-Dec 06 | 7,593 | 7,260 | 333 | 302 | 4.4% | 4.0% | 60,999 | 48,663 | 79.8% | 17,829 | |
| | **Year 2006/07** | **30,773** | **29,129** | **1,644** | **1183** | **5.3%** | **3.8%** | **245,066** | **199,510** | **81.4%** | **73,484** | **103,050** |
| | Apr-Jun 07 | 8,011 | 7,486 | 724 | 566 | 9.0% | 7.1% | 63,376 | 51,567 | 81.4% | 19,325 | 103,978 |
| **BA** | Jan-Mar 06 | 3,692 | 3,530 | 162 | 144 | 4.4% | 3.9% | 36,657 | 26,780 | 73.1% | 8,160 | 45,171 |
| **YE 31/03** | **Year 2005/06** | **14,585** | **13,352** | **1,233** | **829** | **8.5%** | **5.7%** | **144,194** | **109,713** | **76.1%** | **35,634** | **47,012** |
| | Apr-Jun 06 | 4,208 | 3,825 | 383 | 280 | 9.1% | 6.7% | 38,222 | 29,909 | 78.3% | 9,569 | 45,100 |
| | Jul-Sep 06 | 4,331 | 4,080 | 251 | 315 | 5.8% | 7.3% | 38,727 | 30,872 | 79.7% | 9,935 | 45,058 |
| | Oct-Dec 06 | 4,051 | 3,798 | 253 | 210 | 6.2% | 5.2% | 36,563 | 27,073 | 74.0% | 7,878 | 42,197 |
| | Jan-Mar 07 | 3,792 | 3,731 | 61 | -140 | 1.6% | -3.7% | 36,405 | 26,003 | 71.4% | 7,269 | 42,073 |
| | **Year 2006/07** | **16,149** | **15,004** | **1,145** | **578** | **7.1%** | **3.6%** | **148,321** | **112,851** | **76.1%** | **33,068** | **43,501** |
| | Apr-Jun 07 | 4,395 | 3,868 | 527 | 539 | 12.0% | 12.3% | 37,514 | 28,836 | 76.9% | 8,648 | |
| | Jul-Sep 07 | 4,729 | | 611 | 458 | 12.9% | 9.7% | 38,191 | 30,500 | 79.9% | 9,206 | 42,024 |
| **Iberia** | **Year 2005** | **5,894** | **5,426** | **468** | **490** | **7.9%** | **8.3%** | **63,628** | **49,060** | **77.1%** | **27,675** | **24,160** |
| **YE 31/12** | Jan-Mar 06 | 1,457 | 1,536 | -79 | -54 | -5.4% | -3.7% | 15,689 | 11,876 | 75.7% | 6,300 | 23,772 |
| | Apr-Jun 06 | 1,816 | 1,753 | 63 | 44 | 3.5% | 2.4% | 16,809 | 13,420 | 79.8% | 7,461 | 24,109 |
| | Jul-Sep 06 | 1,825 | 1,700 | 125 | 96 | 6.8% | 5.3% | 16,846 | 14,065 | 83.5% | 7,354 | 22,721 |
| | Oct-Dec 06 | 1,811 | 1,750 | 61 | -12 | 3.4% | -0.7% | 16,458 | 13,132 | 79.8% | 6,682 | |
| | **Year 2006** | **6,545** | **6,391** | **154** | **72** | **2.4%** | **1.1%** | **65,802** | **52,493** | **79.8%** | **27,799** | **23,901** |
| | Jan-Mar 07 | 1,745 | 1,734 | 16 | 16 | 0.9% | 0.9% | 16,104 | 12,798 | 79.5% | 6,318 | 22,661 |
| | Apr-Jun 07 | 1,829 | 1,752 | 75 | 83 | 4.1% | 4.5% | 16,458 | 13,307 | 80.9% | 6,863 | 22,324 |
| | Jul-Sep 07 | 2,080 | 1,882 | 198 | 211 | 9.5% | 10.1% | 17,119 | 14,653 | 85.6% | 7,216 | 22,803 |
| **Lufthansa** | **Year 2005** | **22,371** | **21,656** | **715** | **561** | **3.2%** | **2.5%** | **144,182** | **108,185** | **75.0%** | **51,260** | **90,811** |
| **YE 31/12** | Jan-Mar 06 | 5,369 | 5,460 | -91 | -118 | -1.7% | -2.2% | 33,494 | 24,044 | 71.8% | 11,442 | |
| | Apr-Jun 06 | 6,529 | 6,203 | 326 | 142 | 5.0% | 2.2% | 37,797 | 28,603 | 75.7% | 14,106 | |
| | Jul-Sep 06 | 6,765 | 6,188 | 577 | 461 | 8.5% | 6.8% | 39,225 | 30,627 | 78.1% | 14,781 | |
| | **Year 2006** | **24,979** | **23,913** | **1,066** | **1,014** | **4.3%** | **4.1%** | **146,720** | **110,330** | **75.2%** | **53,432** | **93,541** |
| | Jan-Mar 07 | 6,258 | 6,184 | 74 | 593 | 1.2% | 9.5% | 35,028 | 26,109 | 74.5% | 12,329 | 95,696 |
| | Apr-Jun 07 | 7,267 | 6,506 | 761 | 663 | 10.5% | 9.1% | 39,573 | 30,544 | 77.2% | 14,629 | 97,067 |
| | Jul-Sep 07 * | 8,960 | 8,004 | 956 | 843 | 10.7% | 9.4% | 48,662 | 39,112 | 80.4% | 18,836 | |
| **SAS** | **Year 2005** | **4,877** | **4,796** | **81** | **-6** | **1.7%** | **-0.1%** | **38,454** | **26,487** | **68.9%** | **23,799** | **32,363** |
| **YE 31/12** | Jan-Mar 06 | 1,078 | 1,064 | -150 | -137 | -13.9% | -12.7% | 12,275 | 8,179 | 66.6% | 8,532 | 31,528 |
| | Apr-Jun 06 | 2,439 | 2,319 | 120 | 75 | 4.9% | 3.1% | 14,005 | 10,325 | 74.0% | 10,325 | 32,622 |
| | Jul-Sep 06 | 2,476 | 2,318 | 158 | 83 | 6.4% | 3.4% | 14,086 | 10,745 | 76.3% | 10,141 | 32,772 |
| | Oct-Dec 06 | 2,215 | 2,121 | 94 | 679 | 4.2% | 30.7% | 13,405 | 9,162 | 68.4% | 9,611 | 25,534 |
| | **Year 2006** | **5,270** | **5,010** | **260** | **169** | **4.9%** | **3.2%** | **36,971** | **27,506** | **74.4%** | **25,100** | **31,965** |
| | Jan-Mar 07 | 1,978 | 2,025 | -47 | -7 | -2.4% | -0.4% | 12,844 | 8,543 | 66.5% | 9,088 | 26,136 |
| | Apr-Jun 07 | 2,383 | 2,247 | 136 | 89 | 5.7% | 3.7% | 15,091 | 10,915 | 72.3% | 11,045 | 26,916 |
| | Jul-Sep 07 | 2,612 | 2,518 | 94 | 109 | 3.6% | 4.2% | 15,352 | 11,890 | 77.4% | 11,031 | 27,447 |
| **Ryanair** | Jul-Sep 05 | 652 | 409 | 244 | 208 | 37.4% | 31.9% | | | | 9,500 | 2,987 |
| **YE 31/03** | Oct-Dec 05 | 439 | 381 | 58 | 44 | 13.2% | 10.0% | | | 83.0% | 8,600 | 2,963 |
| | **Year 2005/06** | **2,096** | **1,639** | **457** | **380** | **21.8%** | **18.1%** | **39,070** | **30,302** | **83.0%** | **34,768** | **3,063** |
| | Apr-Jun 06 | 711 | 539 | 172 | 146 | 24.2% | 20.5% | | | | 10,700 | |
| | Jul-Sep 06 | 864 | 553 | 313 | 268 | 36.2% | 31.0% | | | | 11,481 | 3,881 |
| | Oct-Dec 06 | 651 | 575 | 76 | 63 | 11.7% | 9.7% | | | 82.0% | 10,300 | 4,209 |
| | **Year 2006/07** | **2,887** | **2,278** | **609** | **518** | **21.1%** | **17.9%** | **48,924** | **40,118** | **82.0%** | **42,500** | |
| | Apr-Jun 07 | 934 | 722 | 212 | 187 | 22.7% | 20.0% | | | 82.0% | 12,600 | |
| | Jul-Sep 07 | 1,229 | 795 | 434 | 384 | 35.3% | 31.2% | | | 86.0% | 13,952 | |
| **easyJet** | Oct-Mar 05 | 1,039 | 1,116 | -77 | -41 | -7.4% | -3.9% | 14,526 | 12,150 | 83.8% | 13,500 | |
| **YE 30/09** | **Year 2004/05** | **2,478** | **2,356** | **122** | **109** | **4.9%** | **4.4%** | **32,141** | **27,448** | **85.2%** | **29,600** | **4,152** |
| | Oct-Mar 06 | 1,095 | 1,177 | -82 | -50 | -7.5% | -4.6% | 16,672 | 13,642 | 81.8% | 14,900 | |
| | **Year 2005/06** | **2,917** | **2,705** | **212** | **170** | **7.3%** | **5.8%** | **37,088** | **31,621** | **84.8%** | **33,000** | **4,859** |
| | Oct-Mar 07 | 1,411 | 1,333 | -47 | -25 | -3.3% | -1.8% | 19,108 | 15,790 | 81.2% | 16,400 | |
| | **Year 2006/07** | **3,679** | **3,069** | **610** | **311** | **16.6%** | **8.5%** | **43,501** | **36,976** | **83.7%** | **37,200** | |

**Note:** * Lufthansa Group including SWISS

**Note:** Annual figures may not add up to sum of interim results due to adjustments and consolidation.

| | | Group revenue US$m | Group costs US$m | Group op. profit US$m | Group net profit US$m | Operating margin | Net margin | Total ASK m | Total RPK m | Load factor | Total pax. 000s | Group employees |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **ANA** | | | | | | | | | | | | |
| **YE 31/03** | **Year 2003/04** | **11,529** | **11,204** | **325** | **234** | **2.8%** | **2.0%** | **87,772** | **55,807** | **63.6%** | **44,800** | **28,870** |
| | **Year 2004/05** | **12,024** | **11,301** | **723** | **251** | **6.0%** | **2.1%** | **85,838** | **55,807** | **65.0%** | **48,860** | **29,098** |
| | **Year 2005/06** | **12,040** | **11,259** | **781** | **235** | **6.5%** | **2.0%** | **86,933** | **58,949** | **67.8%** | **49,920** | **30,322** |
| | **Year 2006/07** | **12,763** | **11,973** | **790** | **280** | **6.2%** | **2.2%** | **85,728** | **58,456** | **68.2%** | **49,500** | **32,460** |
| **Cathay Pacific** | **Year 2004** | **5,024** | **4,350** | **674** | **581** | **13.4%** | **11.6%** | **74,062** | **57,283** | **77.3%** | **13,664** | **15,054** |
| **YE 31/12** | Jan-Jun 05 | 3,074 | 2,799 | 275 | 225 | 8.9% | 7.3% | 39,535 | 30,877 | 78.1% | 7,333 | 15,400 |
| | **Year 2005** | **6,548** | **6,015** | **533** | **424** | **8.1%** | **6.5%** | **82,766** | **65,110** | **78.7%** | **15,440** | **15,447** |
| | Jan-Jun 06 | 3,473 | 3,201 | 272 | 225 | 7.8% | 6.5% | 43,814 | 34,657 | 79.1% | 8,144 | |
| | **Year 2006** | **7,824** | **7,274** | **550** | **526** | **7.0%** | **6.7%** | **89,117** | **71,171** | **79.9%** | **16,730** | |
| | Jan-Jun 07 | 4,440 | 4,031 | 409 | 341 | 9.2% | 7.7% | 49,836 | 38,938 | 79.6% | 8,474 | 19,207 |
| **JAL** | | | | | | | | | | | | |
| **YE 31/03** | **Year 2003/04** | **18,398** | **19,042** | **-644** | **-844** | **-3.5%** | **-4.6%** | **145,900** | **93,847** | **64.3%** | **58,241** | **21,197** |
| | **Year 2004/05** | **19,905** | **19,381** | **524** | **281** | **2.6%** | **1.4%** | **151,902** | **102,354** | **67.4%** | **59,448** | **53,962** |
| | **Year 2005/06** | **19,346** | **19,582** | **-236** | **-416** | **-1.2%** | **-2.2%** | **148,591** | **100,345** | **67.5%** | **58,040** | **53,010** |
| **Korean Air** | | | | | | | | | | | | |
| **YE 31/12** | **Year 2003** | **5,172** | **4,911** | **261** | **-202** | **5.0%** | **-3.9%** | **59,074** | **40,507** | **68.6%** | **21,811** | **15,352** |
| | **Year 2004** | **6,332** | **5,994** | **338** | **414** | **5.3%** | **6.5%** | **64,533** | **45,879** | **71.1%** | **21,280** | **14,994** |
| | **Year 2005** | **7,439** | **7,016** | **423** | **198** | **5.7%** | **2.7%** | **66,658** | **49,046** | **71.4%** | **21,710** | **17,573** |
| | **Year 2006** | **8,498** | **7,975** | **523** | **363** | **6.2%** | **4.3%** | **71,895** | **52,178** | **72.6%** | **22,140** | **16,623** |
| **Malaysian** | | | | | | | | | | | | |
| **YE 31/03** | **Year 2003/04** | **3,061** | **3,012** | **49** | **86** | **1.6%** | **2.8%** | **55,692** | **37,659** | **67.6%** | **15,375** | **20,789** |
| | **Year 2004/05** | **3,141** | **3,555** | **-414** | **-421** | **-13.2%** | **-13.4%** | **64,115** | **44,226** | **69.0%** | **17,536** | **22,513** |
| | **Year 2005/06** | **3,602** | **3,685** | **-83** | **-37** | **-2.3%** | **-1.0%** | **65,099** | **46,122** | **70.8%** | **17,910** | **20,324** |
| **Qantas** | **Year 2003/04** | **7,838** | **7,079** | **759** | **448** | **9.7%** | **5.7%** | **104,200** | **81,276** | **78.0%** | **30,076** | **33,862** |
| **YE 30/06** | Jul-Dec 04 | 5,017 | 4,493 | 524 | 358 | 10.4% | 7.1% | 57,402 | 43,907 | 76.5% | 16,548 | 35,310 |
| | **Year 2004/05** | **9,524** | **8,679** | **845** | **575** | **8.9%** | **6.0%** | **114,003** | **86,986** | **76.3%** | **32,660** | **35,520** |
| | Jul-Dec 05 | 4,999 | 4,626 | 373 | 258 | 7.5% | 5.2% | 59,074 | 45,794 | 77.5% | 17,260 | 35,158 |
| | **Year 2005/06** | **10,186** | **8,711** | **1,475** | **542** | **14.5%** | **5.3%** | **118,070** | **90,899** | **77.0%** | **34,080** | **34,832** |
| | Jul-Dec 06 | 6,099 | 5,588 | 511 | 283 | 8.4% | 4.6% | 61,272 | 49,160 | 80.2% | 18,538 | 33,725 |
| | **Year 2006/07** | **11,975** | **11,106** | **869** | **568** | **7.3%** | **4.7%** | **112,119** | **97,622** | **80.0%** | **36,450** | **34,267** |
| **Singapore** | | | | | | | | | | | | |
| **YE 31/03** | **Year 2003/04** | **5,732** | **5,332** | **400** | **525** | **7.0%** | **9.2%** | **88,253** | **64,685** | **73.3%** | **13,278** | **14,010** |
| | **Year 2004/05** | **7,276** | **6,455** | **821** | **841** | **11.3%** | **11.6%** | **104,662** | **77,594** | **74.1%** | **15,944** | **13,572** |
| | **Year 2005/06** | **6,201** | **5,809** | **392** | **449** | **6.3%** | **7.2%** | **109,484** | **82,742** | **75.6%** | **17,000** | **13,729** |
| | **Year 2006/07** | **9,555** | **8,688** | **866** | **1,403** | **9.1%** | **14.7%** | **112,544** | **89,149** | **79.2%** | **18,346** | **13,847** |
| **Air China** | | | | | | | | | | | | |
| **YE 31/03** | **Year 2004** | **4,050** | **3,508** | **542** | **288** | **13.4%** | **7.1%** | **64,894** | **46,644** | **71.9%** | **24,500** | **29,133** |
| | **Year 2005** | **4,681** | **4,232** | **449** | **294** | **9.6%** | **6.3%** | **70,670** | **52,453** | **74.2%** | **27,690** | **18,447** |
| | **Year 2006** | **5,647** | **5,331** | **316** | **338** | **5.6%** | **6.0%** | **79,383** | **60,276** | **75.9%** | **31,490** | **18,872** |
| **China Southern** | | | | | | | | | | | | |
| **YE 31/03** | **Year 2004** | **2,897** | **2,787** | **110** | **19** | **3.8%** | **0.7%** | **53,769** | **37,196** | **69.2%** | **28,210** | **18,221** |
| | **Year 2005** | **4,682** | **4,842** | **-160** | **-226** | **-3.4%** | **-4.8%** | **88,361** | **61,923** | **70.1%** | **44,120** | **34,417** |
| | **Year 2006** | **5,808** | **5,769** | **39** | **26** | **0.7%** | **0.4%** | **97,044** | **69,575** | **71.7%** | **49,200** | **45,000** |
| **China Eastern** | | | | | | | | | | | | |
| **YE 31/03** | **Year 2004** | **2,584** | **2,524** | **60** | **39** | **2.3%** | **1.5%** | **41,599** | **27,581** | **66.3%** | **17,710** | **20,817** |
| | **Year 2005** | **3,356** | **3,372** | **-16** | **-57** | **-0.5%** | **-1.7%** | **52,428** | **36,381** | **69.4%** | **24,290** | **29,746** |
| | **Year 2006** | **3,825** | **4,201** | **-376** | **-416** | **-9.8%** | **-10.9%** | **70,428** | **50,243** | **71.3%** | **35,020** | **35,000** |
| **Air Asia** | | | | | | | | | | | | |
| **YE 30/06** | **Year 2005** | **152** | **122** | **30** | **25** | **19.7%** | **16.4%** | **6,525** | **4,881** | **74.8%** | **4,410** | **2,016** |
| | **Year 2006** | **230** | **173** | **57** | **34** | **24.8%** | **14.8%** | **8,646** | **6,702** | **77.5%** | **5,720** | **2,224** |

**Note:** Annual figures may not add up to sum of interim results due to adjustments and consolidation. 1 ASM = 1.6093 ASK

## EUROPEAN SCHEDULED TRAFFIC

| | Intra-Europe | | | North Atlantic | | | Europe-Far East | | | Total long-haul | | | Total Int'l | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % |
| **2000** | 208.2 | 132.8 | 63.8 | 229.9 | 179.4 | 78.1 | 137.8 | 108.0 | 78.3 | 508.9 | 396.5 | 77.9 | 755.0 | 555.2 | 73.5 |
| **2001** | 212.9 | 133.4 | 62.7 | 217.6 | 161.3 | 74.1 | 131.7 | 100.9 | 76.6 | 492.2 | 372.6 | 75.7 | 743.3 | 530.5 | 71.4 |
| **2002** | 197.2 | 129.3 | 65.6 | 181.0 | 144.4 | 79.8 | 129.1 | 104.4 | 80.9 | 447.8 | 355.1 | 79.3 | 679.2 | 507.7 | 74.7 |
| **2003** | 210.7 | 136.7 | 64.9 | 215.0 | 171.3 | 79.7 | 131.7 | 101.2 | 76.8 | 497.2 | 390.8 | 78.6 | 742.6 | 551.3 | 74.2 |
| **2004** | 220.6 | 144.2 | 65.4 | 224.0 | 182.9 | 81.6 | 153.6 | 119.9 | 78.0 | 535.2 | 428.7 | 80.1 | 795.7 | 600.7 | 75.5 |
| **2005** | 309.3 | 207.7 | 67.2 | 225.9 | 186.6 | 82.6 | 168.6 | 134.4 | 79.7 | 562.6 | 456.4 | 81.1 | 830.8 | 639.3 | 76.9 |
| **2006** | 329.9 | 226.6 | 68.7 | 230.5 | 188.0 | 81.5 | 182.7 | 147.5 | 80.7 | 588.2 | 478.4 | 81.3 | 874.6 | 677.3 | 77.4 |
| **Oct 07** | 30.4 | 21.8 | 71.6 | 21.2 | 17.1 | 80.6 | 15.6 | 13.3 | 85.2 | 52.0 | 42.8 | 82.2 | 78.6 | 62.1 | 78.9 |
| **Ann. change** | 4.0% | 6.0% | 1.3 | 4.0% | 5.9% | 1.4 | -1.5% | 1.3% | 2.4 | 2.3% | 3.8% | 1.2 | 3.2% | 5.2% | 1.5 |
| **Jan-Oct 07** | 292.0 | 205.0 | 70.2 | 205.3 | 167.3 | 81.5 | 153.2 | 127.3 | 83.1 | 509.9 | 419.9 | 82.3 | 765.8 | 602.1 | 78.6 |
| **Ann. change** | 4.9% | 5.6% | 0.5 | 4.8% | 4.0% | -0.6 | 0.6% | 3.2% | 2.1 | 3.6% | 4.5% | 0.7 | 4.5% | 5.4% | 0.7 |

**Source:** AEA

## EIGHT LARGEST US PASSENGER AIRLINES' SCHEDULED TRAFFIC

| | Domestic | | | North Atlantic | | | Pacific | | | Latin America | | | Total Int'l | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % | ASK bn | RPK bn | LF % |
| Q3 | 239.1 | 192.4 | 80.4 | 49.5 | 42.2 | 85.3 | 28.9 | 24.2 | 83.7 | 25.0 | 18.8 | 75.2 | 103.4 | 85.2 | 82.4 |
| Q4 | 225.1 | 172.2 | 76.4 | 41.9 | 33.2 | 79.2 | 27.4 | 22.3 | 81.4 | 24.2 | 17.2 | 71.1 | 93.5 | 72.7 | 77.8 |
| **2005** | **464.2** | **364.6** | **77.8** | **91.4** | **75.4** | **82.1** | **56.3** | **46.5** | **82.7** | **49.2** | **36.0** | **72.7** | **196.9** | **157.9** | **79.8** |
| 2006 Q1 | 219.2 | 169.3 | 77.2 | 39.6 | 29.7 | 75.0 | 26.1 | 21.7 | 83.2 | 28.2 | 21.1 | 74.8 | 93.9 | 72.5 | 77.2 |
| Q2 | 228.1 | 188.3 | 82.6 | 49.7 | 42.1 | 84.7 | 28.2 | 23.9 | 84.7 | 26.3 | 20.4 | 77.6 | 104.2 | 86.4 | 82.9 |
| Q3 | 232.2 | 187.9 | 80.9 | 54.0 | 45.3 | 83.9 | 28.7 | 24.4 | 85.0 | 26.3 | 20.4 | 77.6 | 109.0 | 90.1 | 82.7 |
| Q4 | 223.2 | 174.3 | 78.1 | 46.0 | 36.1 | 78.5 | 27.8 | 22.8 | 81.9 | 25.8 | 19.2 | 74.2 | 99.6 | 78.1 | 78.4 |
| **2006** | **902.7** | **719.7** | **79.7** | **189.2** | **153.2** | **81.0** | **110.8** | **92.8** | **83.7** | **106.6** | **81.1** | **75.7** | **406.7** | **327.1** | **80.4** |
| 2007 Q1 | 217.4 | 169.6 | 77.5 | 42.9 | 32.5 | 75.5 | 27.0 | 22.5 | 83.4 | 29.5 | 22.7 | 76.8 | 99.4 | 77.7 | 78.2 |
| Q2 | 226.6 | 189.9 | 83.8 | 53.7 | 44.9 | 83.6 | 28.1 | 23.5 | 83.8 | 27.1 | 20.8 | 76.8 | 108.9 | 89.2 | 81.9 |

**Note:** Legacy airlines plus Alaska and Southwest.

## JET ORDERS

| | Date | Buyer | Order | Delivery | Other information/engines |
|---|---|---|---|---|---|
| **Boeing** | 22 Nov | KLM | 3 x 737-700, 2 x 777-300ER | | |
| | 04 Dec | Lion Air | 22 x 737-900 | | |
| | 10 Dec | B&B Ass Mngmt | 20 x 737-800 | | |
| | 13 Dec | GECAS | 53 x 737-800, 2 x 777-300ER | | |
| | 14 Dec | AWAS | 31 x 737-800 | | |
| **Airbus** | 21 Nov | US Airways | 5 x A330-200 | | |
| | 22 Nov | KLM | 2 x A330-200 | | |
| | 26 Nov | TAP Air Portugal | 12 x A350-800XWB | | |
| | 12 Dec | Finnair | 1 x A330-300 | | |
| | 18 Dec | Tiger Airways | 20 x A320 | | |
| **Embraer** | 30 Nov | Suzuyo Group | 2 x E170 | | |
| **Bombardier** | 30 Nov | SkyWest | 18 x CRJ700NG, 4 x CRJ900NG | | |

**Note:** Only firm orders from identifiable airlines/lessors are included. *Source: Manufacturers*

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Aviation Economics
James House, 1st Floor, 22/24 Corsham Street, London N1 6DR
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