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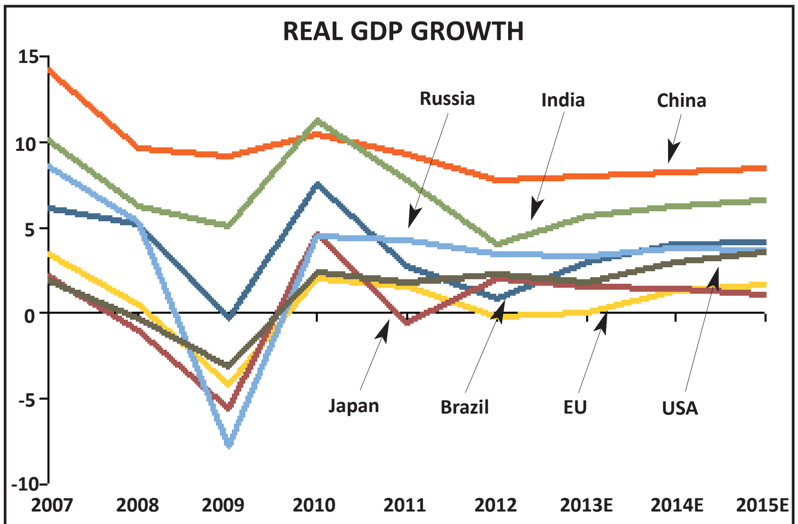
BRICs and mortar

According to the latest update to the IMF's World Economic Outlook in April the two speed global economy is fragmenting a little. The august establishment suggests that there are real signs of recovery developing in the US (despite or even in spite of "sequestration"), while the developing economies continue to provide the major engine of world economic growth, albeit at a slightly lower rate than recently. Europe continues to stagnate although the threats of a Euro break-up may be dissipating. It suggests that we are now in a "three speed" environment.

The update lowered the IMF's central forecasts. It expects that world real GDP will grow by only 3.3% in 2013, down slightly from its forecast of 3.5% growth made six months ago - developing and emerging economies generating around 5% in both 2013 and 2014; the US growing by 1.9% this year but starting to accelerate to generate 3% growth in 2014; the Eurozone remaining in recession this year before returning to 1% economic growth in the next. The only area where the group has raised its forecasts is for Japan; the impact of Abenomics allowing that economy to improve by around 1.5% in this and next year - figures up by 40bp from the last forecast update.

The BRIC nations have taken a lot of attention in recent years as being the prime engine of global economic growth. The designator of that soubriquet, Jim O'Neill of Goldman Sachs, may soon be retiring and there may be concerns that the growth rates in China, Brazil, India and Russia are under pressure, but as *The Economist* pointed out in a recent article, all these economies have been maturing - and as growth matures growth rates decline. In particular there has been a global upheaval as India and China have moved to regain a share of the world economy they last saw in the 17th Century; but after the sprint of a catch-up in the past three decades the rate of growth will naturally decline.

The four main BRIC nations all saw a "tough" 2012 (in relative



Source: IMF

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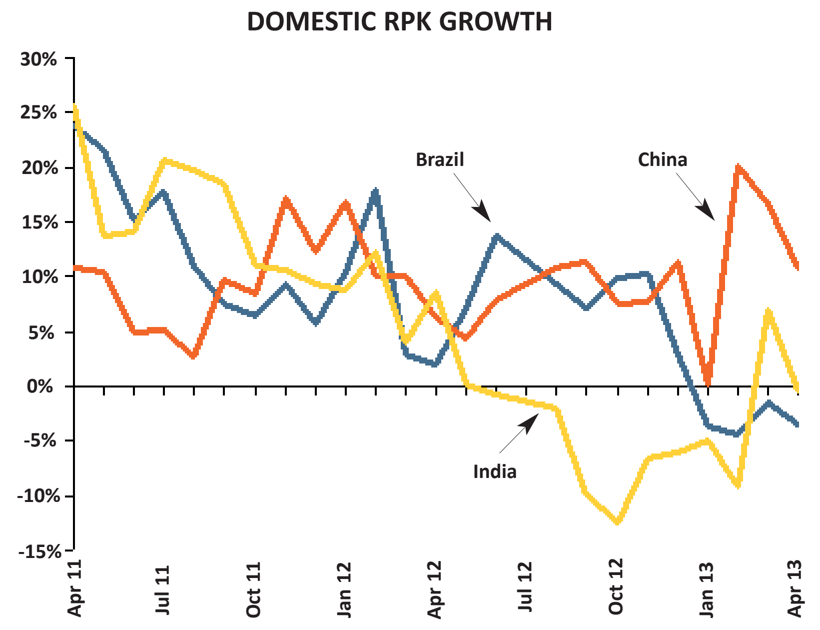
terms), as their economies could not find the markets for goods in the stagnated western world. Russia, as an energy producer fared reasonably well with growth of 3.4% down from 4.3% the year before and China's growth only declined to 7.8% from 9.3%; but India slumped from 7.7% to a mere 4% growth and Brazil to 0.9% from 2.7%. They all suffered relatively high inflation as energy, wage and food price pressures increased.



Source: *IATA*

Given that GDP is a prime determinant of air traffic demand it is perhaps remarkable that there has been a distinct difference between them in aviation terms. China's domestic air traffic (including traffic between mainland China, Hong Kong, Macau and Taiwan) grew by 8.8% in RPK terms in 2012 similar to its GDP growth and despite what seems to have been a small decline in yields. The wild variations in the monthly performance in the chart above relate to the incidence of national holidays and the Chinese New Year, but current growth rates appear consistent. Russia's total air traffic in 2012 grew by 15% year on year in passenger numbers (according to Aeroflot), while (according to IATA) domestic traffic in RPKs increased by just under 8% after similar growth rates in the previous two years.

By contrast Brazilian and Indian growth rates have dipped considerably; in both cases following several years of strong expansion. In Brazil total domestic demand growth slipped to 7.9% in RPK terms from the double digit rates of growth in previous years. Since the beginning of 2013 this has gone into negative territory with both GOL and TAM cutting capacity dramatically - and in the first three months domestic demand has fallen by 1.3%. In India, total domestic demand actually fell in 2012 by 2.2% in RPK terms according to IATA - in part due to the collapse of Kingfisher, but also in face of air fare increases. In both cases the domestic industries had been overheating with significant excess capacity driving down yields at a time when fuel costs have been really hurting. With the cuts in capacity - both voluntary and forced - the evidence suggests that yields and unit revenues are now rising strongly (GOL achieved a near 14% year on year increase in yields in the first quarter); but growth is restrained.

It is not just economic performance that will decide the development of aviation; regulation and politics play important parts. China remains highly regulated - with its command based communist economy and restrictions on personal freedoms. Russia, as a former command-based communist economy retains many internally focussed restrictions. However, it is investigating the idea of encouraging LCC development to spur air travel demand and appears to be looking to invite non-Russian airlines to help. India also has a highly regulated domestic industry but is now relaxing ownership restrictions - with Tony Fernandes's Air Asia planning to move into the sub-continent to provide further disruption. Meanwhile in Brazil, the overheated local environment is succumbing to the realities of the consolidation that has taken place in the Mercosur. With the developed world in stagnation is the aviation industry relying too much on the developing world to provide the growth?

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Brazil's airlines: Azul and Avianca Brazil rise to challenge Gol-TAM duopoly

The Brazilian aviation market has seen significant change in the past year or so, as demand growth has weakened, an unprecedented capacity discipline has taken hold and industry consolidation has reached new heights. Faced with financial losses domestically, the two leading airlines have been restructuring operations and have adopted many new strategies. How are the four main players – Gol, TAM (now part of Latam), Azul-TRIP and Avianca Brazil – now positioned for the remainder of 2013 and for the longer term? Is Azul, which filed for a global IPO in late May, on the verge of becoming a "third force" in Brazilian aviation? Will Avianca Brazil bid for Portugal's TAP and also become a major player in Brazil?

The past year's upheavals come in the wake of a tumultuous decade in the Brazilian airline industry. The 2000s witnessed the arrival of Gol as Brazil's first LCC to stimulate and revolutionise air travel (2001), the demise of old-timers such as Transbrasil, VASP and Varig (the latter was acquired by Gol in 2007) and TAM's rapid emergence as Brazil's flag carrier on long-haul international routes.

The late 2000s saw the rise of a new generation of LCCs. Webjet, launched in 2005, and older-established small carriers such as TRIP and BRA ramped up growth (BRA did not make it, ceasing operations in late 2007). Azul, David Neeleman's well-funded start-up, took to the air with JetBlue-style E190/195 operations in December 2008. And in 2010 Synergy Group began in earnest to build up Avianca Brazil, a small operator previously known as Oceanair.

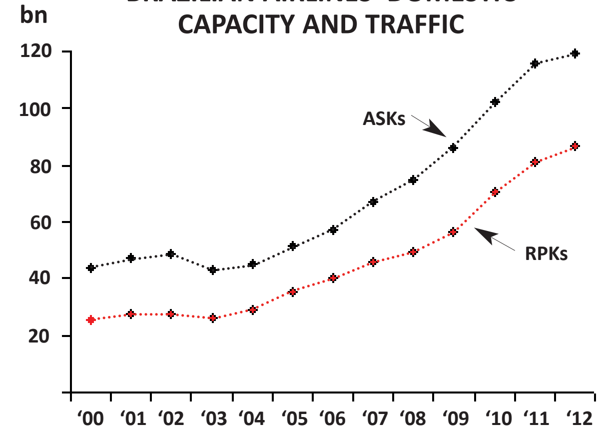
The decade witnessed the beginning of the rapid rise of Brazil's new middle class, made up of many people who had not flown before. The "C class" has expanded as a result of healthy GDP growth, rising incomes and effective anti-poverty policies. Definitions are not always clear, but according to data presented in Azul's IPO prospectus from IBGE (Brazil's Institute of Geography and Statistics), between 2005 and 2010 nearly 40m Brazilians entered the middle class and an additional 16m entered the upper income classes. The C class included 102m people in 2010, more than half of Brazil's 192m population.

The Brazilian market was ripe for air travel stimulation also because long-distance travel alternatives are limited. Brazil is geographically similar in size to the continental US, but it has no interstate rail system and the road infrastructure is poor. Buses have traditionally been the only low-cost option for long-distance travel, but that mode is extremely time-consuming. Tapping that segment with low fares was the cornerstone of Gol's strategy from the start (and a key theme later adopted also by other Brazilian carriers).

The growing middle-income segment, rising incomes and increasing availability of low air fares led to a surge in air travel. Domestic air passenger numbers in Brazil have increased from 28m in 2000 to over 92m in 2012, overtaking the bus passenger volumes in 2009. Growth was especially strong in the 2005-2010 period, when industry domestic RPKs doubled. 2010 and 2011 saw 24% and 16% RPK growth, respectively.

Not surprisingly, Brazil has struggled to cope with the sudden high air traffic volumes. Terrible ATC and infrastructure problems, exacerbated by two fatal accidents, reared their ugly head in the mid-2000s, setting the

BRAZILIAN AIRLINES' DOMESTIC CAPACITY AND TRAFFIC



Source: ANAC

BRAZILIAN AIRLINES' DOMESTIC MARKET SHARES		
	% of total domestic RPKs	
	April 2013	April 2012
TAM	38.4%	39.9%
GOL	36.2%	34.8%
Webjet	0.0%	5.3%
GOL+Webjet	36.2%	40.1%
Azul	13.4%	9.9%
TRIP	4.1%	4.3%
Azul+TRIP	17.5%	14.2%
Avianca Brazil	7.1%	5.0%
Others	0.7%	0.8%
TOTAL	100%	100%

Source: *ANAC*

government on a course for infrastructure provision and improvements. Progress on that front has been disappointingly slow (until recently, at least), but it must be remembered that Brazil did not even have the proper federal agencies or entities in place to oversee the development of commercial aviation. ANAC, the civil aviation authority, was only created in 2005 (it took over from the military). A more comprehensive regulatory framework did not emerge until 2011, when the following entities were created: CONAC (an advisory body on policies), CONAERO (to coordinate airport efficiency and safety) and SAC (Civil Aviation Secretariat, to oversee ANAC and INFRAERO).

Of course, a major part of the traffic boom especially in 2009-2011 was the result of significant capacity addition and intense fare wars, as Gol, TAM and the aggressive new-entrant LCCs battled for domestic market share. (In Brazil airlines are allowed to establish their own domestic fares without prior approval, though under 2010 regulations they are required to report their fares monthly to ANAC.)

In 2011, a combination of overcapacity, declining yields and a 30% hike in fuel costs led Gol and Tam to start losing money in domestic operations – a situation that has remained to this day. The airlines actually began to rein in capacity growth in late 2011, which led to a somewhat healthier pricing environment. But by then Brazil's economic growth was stalling, which in combination with the higher fares led to reduced travel demand.

Brazil's GDP growth stalled alarmingly in 2012 – just 0.9%, compared to the government's forecast of 4.5% at the beginning of last year. This followed 2.7% growth in 2011, 7.5% growth in 2010 and a 0.3% dip in 2009 (the global recession year). Air travel demand (domestic RPK) growth in Brazil has also slowed dramatically: from 16% in 2011 to 6.8% in 2012 and into negative territory this year (down 1% in 1Q13 and down 3.4% in April).

So, Brazilian airlines now find themselves in a very different economic and demand environment. Over the past 12 months or so they have taken extensive remedial action, including capacity cuts. The key questions are: How long will the weak economic conditions last in Brazil? And have the airlines adjusted sufficiently to restore profitability in 2013?

Industry consolidation

The past couple of years have also seen a major industry consolidation phase in Brazil or involving Brazilian carriers. The biggest of the deals was LAN's takeover of TAM, announced in August 2010 and completed in June 2012. TAM is now part of the powerful Latam Airlines Group, which dominates the Latin America region and could in the future capture market share from competitors in Brazil. On the other hand, the deal helped the overcapacity situation in Brazil. Latam has adopted very rational strategies for TAM Brazil, which it has kept as a separate business division.

Gol, having absorbed Varig in the late 2000s, took over Webjet, Brazil's fourth largest carrier, in 2011. Since securing all the necessary regulatory approvals late last year, Gol has fully integrated the small low-cost carrier.

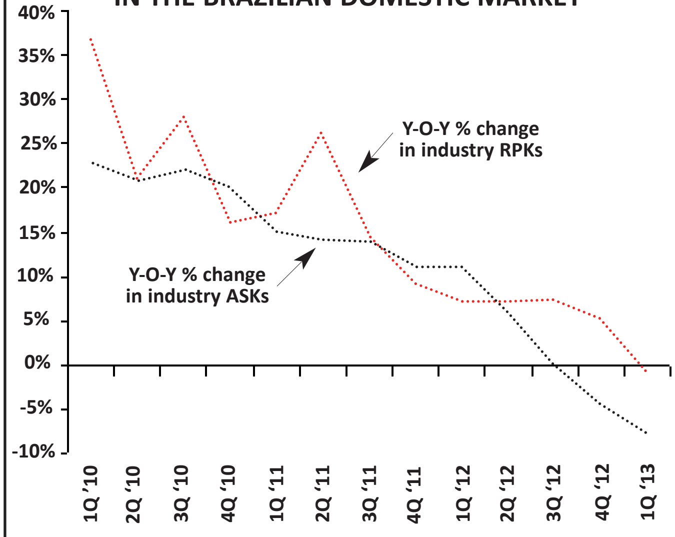
Azul, Brazil's third largest airline, acquired regional carrier TRIP in May 2012. The two received their final antitrust approval in March and have been integrating under the Azul brand.

When the dust settles, the industry implications of these deals look likely to be as follows. First, there will obviously be fewer players in Brazil – something that should help the airlines cope better with the slower-growth period.

Second, the Azul-TRIP union has created what could soon be described as a "third force" in Brazilian aviation. It has weakened the TAM-Gol domestic duopoly, which had already declined steadily because of the rapid growth of Azul and other carriers but which still accounted for a combined 74.6% of domestic RPKs in April. Azul has described the TRIP acquisition as being equivalent to about four years of growth. The Azul-TRIP combine had 17.5% of the domestic market in April, and the share could be 20% or higher in full-year 2013, helped by Gol's and TAM's cutbacks.

Third, as a result of the consolidation, virtually all (99.3%) of Brazil's domestic traffic is carried by four airlines. The "small LCC upstart/other carrier" segment, which contributed significantly to the price wars in recent years, has temporarily disappeared. Of course, in the longer term there are bound to be new entrants, especially when airport capacity constraints ease. (It is hard to picture there not being a "Virgin Brazil" eventually.)

POST-1Q12 CAPACITY RATIONALISATION IN THE BRAZILIAN DOMESTIC MARKET



Source: GOL

Post-1Q12 recovery efforts

In early 2012 Brazil's airlines were feeling the effects of multiple negative factors. In addition to the weaker domestic travel demand, fuel prices were high, labour costs had risen, airport charges had gone up by 150% in 2011, and the Brazilian real had depreciated against the US dollar (increasing the airlines' dollar-denominated liabilities).

Gol, which also had serious balance sheet issues, began to take remedial action in March 2012 - scale back expansion, slash costs and raise capital. With the merger transaction completed, Latam's new management followed Gol's example in August 2012 and began to rein in TAM's growth plans.

The result has been an unprecedented capacity discipline in Brazilian aviation. Gol's domestic ASKs fell by 5.4% last year. The decision to dispose of Webjet's fleet in December facilitated an even bigger reduction in this year's first quarter: the combined Gol-Webjet ASKs were down by 15.7%. TAM's domestic ASKs fell by 1% in 2012 and 9% in 1Q13. The airlines are now projecting domestic capacity declines of "up to 7%" (Gol) and 5-7% (TAM) in 2013.

The smaller carriers too are moderating their capacity growth. Last year Azul's ASKs increased by 28%, but the combined Azul-TRIP capacity was up by only 11.2% in the first four months of this year. After almost doubling in size last year (up 82%), Avianca Brazil slowed its ASK growth to 30% in January-April.

The result was a remarkable 7.8% decline in domestic industry capacity in Brazil in this year's first quarter. However, Webjet's closure was a special factor in that period, and April saw a more modest 4.1% decline in industry capacity.

The capacity cuts have led to impressive load factor improvements. TAM, whose new Brazil strategy has emphasised yield management, has since the summer consistently seen monthly load factors running at least 10 points above the year-earlier levels. The pricing and yield environment has improved, restoring unit revenue growth. Gol has recorded 13 consecutive months of unit revenue growth and has seen double-digit PRASK and yield increases in recent months. Gol has also undertaken impressive cost cutting; its drastic measures have included a 20% workforce reduction over the past year.

The downside has been the weak demand (the Brazilian market is highly price-sensitive). Also, Gol's and TAM's actions came too late to rescue last year's financial results. Gol had a horrendous R$1.5bn ($750m) net loss in 2012, its second consecutive unprofitable year. Operating margin was a negative 11.2%, compared to 2011's negative 3.2% and 2010's positive 10%. TAM's 2012 net loss was US$45.2m (on revenues of US$3.6bn); while more detailed results were not reported separately from Latam's, it is known that TAM lost money in its domestic Brazil operations last year.

Azul disclosed in its preliminary IPO prospectus that it has had marginal operating profits but continued net losses in the past two years. Last year it earned a R$8.6m (US$4.3m) operating profit and a R$170.8m (US$85.4m) net loss on revenues of R$2.7bn (US$1.4bn). The operating margin was only 0.3%, down from 1.5% in 2011. In the past three years, Azul's net losses have totalled R$373.9m (US$187m).

According to the prospectus, TRIP (which is now part of Azul) had operating losses of R$131.2m and R$99.4m in 2012 and 2011, respectively, on revenues of R$1.4bn (US$700m) and R$1.1bn. However, TRIP had a R$70.7m operating profit in 2010 (9.4% of revenues).

While Avianca Brazil does not formally disclose its financial results, according to local press reports, it has not yet attained profitability. Its revenues reportedly grew from US$575m in 2010 to US$1.35bn in 2012, making it about the same size as Azul before TRIP.

But all of the airlines are now anticipating positive results in 2013. Latam executives have made it clear in recent conference calls that they expect TAM to be profitable in Brazil this year. In late April Avianca Brazil executives were widely quoted saying that they expected 2013 to be the airline's first profitable year. Gol, the only carrier to disclose specific targets, was in mid-May projecting a 1-3% operating margin in 2013.

Outlook: 2013 vs. longer-term

But the near-term outlook for Brazil's airlines is not encouraging. Over the past 9-10 months GDP growth forecasts have been steadily revised down. The economy grew by only 1.9% in the first quarter. In early June S&P cut its outlook on Brazil to "negative", noting that the country is seeing modest economic growth for a third consecutive year, with GDP currently projected to expand by only 2.5% in 2013. S&P also warned of a risk of a "more persistent slowdown in household spending" in Brazil. Despite the slow growth, inflation remains high at around 6%.

Brazil's airlines continue to face significant cost pressures, in part because of unfavourable exchange rate developments. In May and early June the Brazilian real weakened further against the US dollar, continuing a trend that has been evident for some time. Since March the real/dollar exchange rate has moved from R$1.94 to around R$2.14 (up 10%).

All of this has dampened Brazilian carriers' near-term profit prospects. 2.5% GDP growth represents the bottom end of the range that Gol's 1-3% operating margin forwcast is based on. One analyst estimated that if the real/dollar exchange rate remained at R$2.13, Gol's 2013 operating margin would be one percentage point lower (thus in the 0-2% range) and its 2013 net loss would increase from R$161m to R$387m.

Also, even though Gol and TAM seem committed to continued capacity discipline, it could fall apart. It is now low season in Brazil (the second quarter is historically the weakest) and there have been instances of aggressive fare discounting. The airlines have all adopted different revenue strategies. As some analysts have noted, it is a point of concern that Gol wants to maximise the yield and TAM seems to want to maximise the load factor. This has meant TAM gaining domestic market share – something that may not be acceptable to Gol.

But there are indications that the Brazilian airline industry is reaching a new level of maturity and wants to focus on sustainable growth. Last year the airlines got their act together to create their own association, ABEAR, which has taken on key industry issues such as airport costs and fuel taxes.

Of course, because of the burgeoning middles class, air travel in Brazil is expected to continue growing this year. ABEAR's latest forecast projects 7% demand growth in 2013 (in line with the historical relationship of traffic growth exceeding GDP growth two or three times), down from an earlier forecast of 9%. Also, this year and in the medium-term, there will be the boost provided by the major international sports events hosted by Brazil – the FIFA Confederations Cup this summer (June 15-30), the World Cup in 2014 and the Olympics in 2016.

In the longer term, Brazil continues to be one of the most attractive aviation markets in the world because of its size and growth potential. Total (international and domestic) enplanements per capita are still relatively low - about 0.5, compared to the US's 2.3. In 2010 Brazilians still boarded interstate buses 67m times instead of flying. According to Azul's IPO documents (citing *Business Monitor*), Brazilian nominal GDP per capita, having risen from US$7,200 in 2007 to US$11,354 in 2012, is projected to reach US$20,564 by 2020. And an increasing share of the GDP is going to the middle or lower income classes.

In the Brazilian international markets, open skies ASAs with key world regions should help keep traffic growing at a robust rate. A Brazil-US open skies ASA is being implemented in stages and should be fully in force by 2015. A Brazil-EU open skies ASA is expected to come into force in 2014.

While Gol and TAM are well positioned for long-term growth in Brazil because of their many competitive advantages, including formidable slot holdings at the main airports, Azul and Avianca Brazil also have good prospects. First, the domestic market is so large that there is probably enough traffic for everyone. Second, the smaller carriers tend to focus on different segments or specific niches – something that will help them survive (though there is enough overlap to ensure competition). This is especially true with Azul, which focuses on regional routes and currently operates only E190/195s.

Third, the Brazilian government is determined to level the playing field a little, to ensure competition and low fares. Much of the attention has focused on Sao Paulo's Congonhas, the busiest domestic airport in Brazil and currently the only one where slots are necessary. The airport, which cannot be expanded because it is bound by built-up areas of the city on all sides, is dominated by TAM and Gol (90% of the slots), but newcomers like Azul are keen to secure a foothold there.

After years of studies, SAC recently came up with proposals on redistributing slots at Congonhas and held public consultations earlier this year. BofA Merrill Lynch analysts estimated in February that Gol and TAM could lose perhaps 27 daily slots to the smaller carriers, which would see their slot share increase from 9% to 20%. But the exercise is fraught with difficulty. For example, a slot transfer to Azul would have the undesirable effect of reducing total seats offered at the capacity-constrained airport, because Azul operates smaller aircraft. The government may be hesitant to hurt TAM and Gol when they are losing money or to rock the boat too much just before Brazil hosts a series of major international sports events. Nevertheless, SAC now intends to release the findings of the public hearings by the end of June and to come up with slot distribution rules this year that can be applied to any airport that reaches saturation.

As an interesting twist, in late May DECEA (Department of Airspace Control) submitted a study commissioned by SAC suggesting that Congonhas has room for 25% expansion. All that the government would need to do would be to reverse restrictions imposed after a 2007 fatal crash and to ban non-commercial flights at the airport. The study reportedly argues that Congonhas could safely handle 38 movements per hour, four more than currently, and that its annual passenger handling capacity could rise from 16.7m to 20.7m.

Separately, the Brazilian government is concerned about the airlines' continued financial losses. In early April SAC asked ANAC and BNDES (the state-owned bank) to carry out studies on the financial health of Brazil's airlines and to suggest ways to help the industry. The results of those studies are not yet known. There are also moves in Congress to try to ease the airlines' fuel tax burden.

In recent months Brazil's airlines have been campaigning through ABEAR for reductions in VAT rates on jet fuel. In Brazil VAT ("ICMS" tax) is set and collected at state level and varies greatly by state and by product (7%-25%). In April the state of Brasilia reduced its VAT rate on jet fuel from 25% to 12%, the same as in Rio de Janeiro. The airlines now want the state of Sao Paulo to also reduce its VAT rate on fuel from 25% to 12%. This would have material positive impact on most airlines' finances, because SP is the country's most important hub and a large part of the fleet is refuelled there. ABEAR's longer-term goal is to equalise the VAT at 12% throughout Brazil.

On the foreign ownership front, Azul suggested in its IPO documents that there was a "significant possibility" that the Brazilian Aeronautical Code could be amended in 2013 or 2014 to permit foreign investors to hold up to 49% of the voting shares of Brazilian carriers (compared to a maximum of 20% at present). The issue has been under discussion since 2009 and there is a draft bill making its way through the Brazilian House of Representatives. In the short term the impact would be minimal, because under the existing rules Brazil's airlines can issue preferred shares to raise more equity from foreigners. But in the longer term it would obviously make it more attractive for foreign investors to help launch new airlines in Brazil.

Infrastructure provision

The biggest single factor that could limit Brazil's airlines is inadequate airport infrastructure. A particularly damning assessment of the situation came in late May in a presentation from CADE. A senior executive from the agency reportedly argued that without major investments in the next two years, competition at the country's eight largest airports will be "near-impossible". Sao Paulo's Congonhas and Rio's Santos Dumont (the two main domestic airports, both operated by INFRAERO) are already effectively closed to new entrants, but growth in air travel in the next two years will mean that six other airports too will not be able to accommodate new entrants or additional air service. Those airports are Belo Horizonte's Confins, Brasilia, Campinas, Curitiba and the international airports in Sao Paulo and Rio (Guarulhos and Galeao).

Fortunately, three of those six airports (Guarulhos, Campinas and Brasilia) were handed over to private consortia on 20-30 year concessions in 2012, and another two airports (Confins and Galeao) are due to be privatised this autumn, leaving only Curitiba under INFRAERO's management. Substantial and timely capital investments to expand the airports and improve their facilities were a key condition in the transactions. The three airports privatised in 2012, which handle some 30% of the country's passengers, will get a combined minimum investment of R$18.1bn (US$9.1bn), of which R$2.9bn (US$1.4bn) must be in time for the World Cup. Each of those airports will get a new terminal, as well as expanded runways, aprons and parking areas.

Under the preliminary terms released for this year's privatisations, Galeao will get a R$5.2bn investment over 25 years, to facilitate its growth from the current 17.5m passengers a year to a projected 60m by 2038. Confins will get a R$3.5bn investment over 30 years, to take it from its current 10.4m passengers a year to 43m by 2043.

The government pocketed R$24.5bn from the first three privatisations and has said that it will use part of the funds to improve airport infrastructure across the country. According to Azul, of the 67 Brazilian airports managed directly or indirectly by INFRAERO, some 13 airports are currently receiving infrastructure investments and upgrades. This year INFRAERO is boosting its own airport investments by 40% to R$2.8bn.

Starting in 2014, much of the revenue collected from the large privatised hubs will be invested in regional airports. It will be part of a comprehensive package of incentives for the regional aviation industry that the government announced in December 2012. The package includes investments of up to R$7.3bn in regional aviation infrastructure, expanding the number of commercial airports from 129 to 270 in the next ten years, and subsidies and airport fee exemptions for regional flights.

There has been much speculation about whether all the facilities currently under construction will be ready for the World Cup. But some important benefits are already evident. The new expansion projects at Sao Paulo's Campinas since its privatisation in February 2012, which include R$1.4bn worth of investments by 2014 and a new runway by 2017, have already created attractive potential growth opportunities for Gol and TAM. Gol recently filed with ANAC to begin six new daily flights from Campinas, which would double its operations at the airport; the goal is to attract new traffic from the Campinas area, rather than divert traffic from Sao Paulo. TAM is reportedly also studying expansion at Campinas.

It seems that Brazil is at long last fully committed to ensuring adequate airport capacity and facilities. Improving airport infrastructure is a major focus of the "Growth Acceleration Program" launched by President Dilma Rousseff's government. INFRAERO expects Brazil's annual passenger traffic (domestic and international) to more than double between 2014 and 2030, from 146m to 310m passengers.

Gol: Recovery in 2013?

Gol has staged quite an impressive restructuring in the past year, much like it did in 2009-2010 following the Varig acquisition, which many considered a strategic mistake. This time, though, the top management has changed. In June 2012 founder Constantino de Oliveira Jr. stepped down as CEO, and Paulo Kakinoff, formerly Audi's Brazil head and a Gol board director, took over. The idea was to have a truly experienced industry executive steer Gol back to profitability.

Despite the sharp reduction in ASKs and many cost headwinds, Gol managed to keep its ex-fuel unit costs flat in the first quarter. This feat was attributed mainly to a 20% headcount reduction. Analysts say that there is still room for improvement on the cost front.

Despite the contraction, Gol's revenues declined by only 4% in 1Q. The load factor improvement was much smaller than competitors', but the low-70s load factors are adequate and Gol is outperforming its peers in yield and RASK.

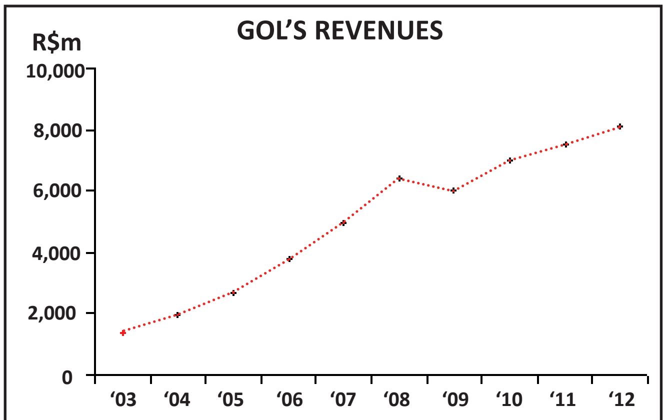
The main benefit of the R$70m Webjet acquisition was that it strengthened Gol's slot holdings at six key airports: Guarulhos, Brasilia, Galeao, Santos Dumont, Confins and Porto Alegre's Salgado Filho. It was also a defensive move. And the acquisition helped in the rationalisation efforts, because Gol opted to end Webjet's operations and dispose of its 20 "uneconomic" 737-300s. It seems to have been a relatively quick and successful integration. Brazil's antitrust regulator CADE made it a condition that the Gol-Webjet combine meet certain performance standards – namely that they operate from Santos Dumont with "85% efficiency" (a measure of the frequency a slot is used, on-time performance and load factor).

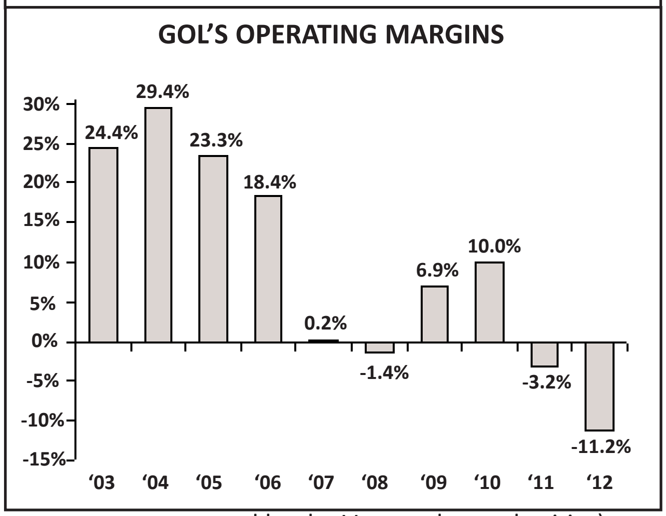
Earlier this year Gol implemented what it described as a "new route network" – a collection of changes and strategy refinements to coincide with the merger of the Gol and Webjet networks. Gol has eliminated some routes, reduced night flights, strengthened Guarulhos hub operations, improved connectivity with partners (especially at GRU) and increased focus on the corporate market. As of late February, the Gol-Webjet network covered 51 domestic and 14 international destinations.

Gol is currently keen to expand internationally, to diversify revenue sources (given the sluggish demand in Brazil) and to gain a natural exchange rate hedge. It is indicative that while cutting capacity domestically this year, in January-April Gol's and TAM's combined international capacity was up by 15.6%.

Notably, in December 2012 Gol entered the Brazil-US market with daily Sao Paulo-Orlando and Rio-Miami flights, which are operated via Santo Domingo (Dominican Republic) because the 737-800s need a fuel stop. The flights are timed to arrive in Santo Domingo at about the same time, allowing passengers to switch. In 2007 Gol briefly tried to maintain Varig's Brazil-US 767 fights but the services were not viable.

Gol has good reasons to be in the Brazil-US market. As the management explained recently, the idea is to exploit what has been a high-growth market, offer customers more options and "reroute domestic capacity to the international market". But Gol faces many challenges in those operations. It has less of a cost advantage on long haul and international routes, the US operations are more expensive and the one-stop economics are questionable. TAM and American have nonstop flights in those markets and offer more frequencies and a better product, so Gol has to discount very aggressively. TAM will also soon be able to connect to American's huge domestic network at Miami, where Gol's partner Delta does not have much of a presence. Gol's daytime flights do not even connect effectively with its own vast network in Brazil. Santo Domingo does not have much of a local market, certainly less than Caracas, which was Gol's original choice for the intermediate stop (before those plans were





scuppered by the Venezuelan authorities).

But Gol executives called the first five months' results in the US operations "encouraging" and noted that load factors were in the mid-80s. Gol is sticking to its plans to build a hub in the Dominican Republic and has already presented its expansion plans to the DR government, which were "very positively received".

In late May Gol announced another unusual-sounding expansion idea: scheduled flights to Africa. The airline is studying the possibility of adding a Recife-Lagos route, which it would be able to operate with 737-800s. It would be Gol's first long-haul inter-continental route. At first glance this would seem like a totally unnecessary diversion from the "back to basics" strategy of being an LCC, but Gol has already diverted from that model with the US and DR operations. It could be another useful way to diversify. Brazil and Nigeria have strong ties and there is longstanding demand from businesses for direct air links, which could prove lucrative.

Gol has also continued to add new intra-Latin America international service. Last year it benefited from the demise of two small carriers, Uruguay's Pluna and Bolivia's Aerosur, which gave it the opportunity to serve Montevideo and San Cruz from Sao Paulo. Gol is only interested in markets that can be operated with 737s and is looking to grow its international operations to eventually account for 15-16% of its total capacity, compared to 8% at present.

This year Gol is also building its code-shares with Delta, which in December 2011 paid $100m for a 3% stake in Gol, also securing a board seat, an exclusive codeshare agreement in the Brazil-US market and two 767s. From September all of Delta's services to Brazil will be connected to Gol's network and sales channels. Otherwise, Gol has an "open architecture" type alliance strategy similar to JetBlue's and WestJet's and is not interested in entering into a global alliance.

Gol does not have any liquidity issues, because it has made it a policy to maintain strong cash reserves ever since it narrowly escaped the post-Varig cash crunch. Including the R$1.1bn ($550m) proceeds from the late-April IPO of its Smiles FFP unit and another R$400m ($200m) of proceeds from a separate mileage sale, Gol will have around R$3.1bn ($1.6bn) in cash at the end of June – a very healthy 39% of lagging 12-month revenues and roughly the same amount it has in debt obligations.

Gol remains highly leveraged, though, with adjusted gross debt (including leases) of R$9.7bn ($4.9bn) at year-end 2012. But since there are no major repayments due in 2013-2014, Gol merely intends to "prepay what is reasonable" and due in the short term while keeping a strong cash position. The airline hopes that growth in EBITDAR will reduce its debt ratios to satisfactory levels.

The management feels that the fleet plan has been trimmed to what is needed in the next few years. Gol is taking 16 new aircraft in 2013, some on sale-leasebacks. In October 2012 Gol ordered 60 737 MAXs, for delivery from 2018. The $6bn order did not go down well with analysts, given Gol's losses, but the aircraft will be mainly for replacement and will ensure competitive costs in the long term.

It seems likely that Gol's losses bottomed out in the fourth quarter, when the EBIT loss margin sank to a dismal -16.9%. The March quarter saw a promising 4.9% positive operating margin. If the economy and exchange rates cooperate, Gol has a chance to roughly break even operationally in 2013. However, a net loss is expected for a third consecutive year.

TAM: The new Brazil strategy

The Brazilian market is very important to Latam because it accounts for 30% of the group's revenues. Brazil was also one of the key areas where Latam hoped to grow and obtain early merger synergies (the other was cargo), so it became an immediate focus after the merger closed. However, turning around the Brazil passenger operations has been Latam's biggest challenge.

Among the first integration moves, Latam strengthened its intra-Brazil cargo operations by blending LAN subsidiary ABSA Cargo's Brazil operations and two 767-300Fs into TAM Cargo and investing in cargo infrastructure in Brazil. In turn, TAM Cargo's international operations were blended into LAN Cargo's international operations. As a result, Latam is now a stronger cargo force in Brazil and internationally, better able to capitalise on growth opportunities when the cargo sector recovers.

On the passenger side, Latam's TAM Brazil unit has followed Gol's example and sharply cut capacity in the domestic market. But TAM follows a different strategy from Gol in that it is trying to boost revenues through higher load factors and better yield management. Like Gol, it is striving to cut costs and improve efficiency. As a result, TAM's load factors have risen to around 80% from the 65-70% historical range and recent months have seen low double-digit PRASK growth.

But it is hard to assess the financial success of that strategy because Latam no longer discloses yield, cost and operating margin information for TAM. In a February 19 report, JP Morgan analysts said that they believed the Brazil domestic operations were still unprofitable - that most of TAM's PRASK improvement has been driven by ASK reductions, rather than passenger revenue improvement.

In recent conference calls, Latam's management has merely stated that TAM Brazil has made significant progress in its turnaround and seen sequential improvement. The executives have said that they remain convinced that capacity discipline and adequate market segmentation are the key. The strategy makes sense when considering that TAM has always been a full-service carrier, trying to cater for all segments. And it obviously has benefited from LAN's expertise in market segmentation.

It would seem that much work remains to be done on the cost front. According to Latam's 2012 annual report, the group is exploring opportunities to apply aspects of the low-cost model that LAN has utilised in other Latin American countries to TAM's domestic operations in Brazil.

LAN launched its version of the low-cost business model in 2007 to increase the efficiency of its domestic operations in Chile, Peru, Ecuador, Colombia and to some extent Argentina. The model features higher aircraft utilisation through more point-to-point services, more night flights and faster turnarounds; use of a standardised fleet of A320-family aircraft; lower sales and distribution costs through higher internet bookings, reduced agency commissions and increased self check-in; and simplification in back-office and support functions. Some of the cost savings are passed to consumers through fare reductions, which has stimulated traffic and enhanced profitability.

There is obviously nothing unique about this model – just a collection of the best and perhaps easiest-to-apply components of the standard LCC business model – but it has worked well for LAN in the Spanish-speaking domestic markets, as indicated by Latam's continued rapid capacity addition in those countries. If the model can be applied to TAM Brazil, Gol better watch out.

Of course, in addition to its 42-point network in Brazil (as of February 28), Latam has international operations out of Sao Paulo and Rio. From Brazil it operates to eight other Latin American countries, as well as the US, France, Germany, the UK and Italy. The management has reportedly said that one of their dreams is to turn Sao Paulo into a major international hub.

Last year, as Brazil's domestic growth slowed, Europe stagnated and TAM was expecting four new 777-300ERs, Latam expanded significantly in the Brazil-US market. Among other things, TAM added a Rio-Orlando route and boosted seats on Sao Paulo-Miami by upgauging from A330s to 777s. This strategy backfired when competitors grew just as recklessly, leading to excess capacity and heavy discounting. Latam has seen sharp falls in its international load factor and RASK in the past two quarters, which was largely attributed to the long haul routes from Brazil.

As a result, Latam is now scaling down international expansion from Brazil. It has terminated the Rio-Orlando route and in August will pull out of the Rio-Paris and Rio-Frankfurt markets (opting to route those passengers via Sao Paulo).

Latam feels that the US growth was justified because most of the routes are strategic and will be profitable in the long run. The performance of the long haul network from Brazil is expected to improve in the second half of this year, in part because of the remedial actions and because of the planned TAM-American codeshares.

Latam announced its long-awaited global alliance decision on March 7, opting to remain in oneworld and for TAM to leave Star and join oneworld (expected in 2Q14). Although there are likely to be negative implications for the combine's Brazil-Europe business, the decision was a major positive for the group's Brazil-US operations. The US is the number one international destination for Brazilians. American is the largest carrier on those routes and operates a major hub in Miami, the key destination for Brazilians. TAM will benefit enormously from the codeshares with American (which secured final regulatory approvals in May), because it will get significant feed from American's domestic network through Miami and New York. Star may be a bigger global alliance, but it has not helped TAM penetrate the US market, because United does not have a hub in Miami.

Latam is only just getting started in the process of realising the projected $600-700m annual merger synergies (not expected in full until June 2016), so there is much scope for financial improvement in many areas, including Brazil. While LAN's and TAM's fleet plans have already been rationalised as a result of the merger, Latam is in the process of further adjusting the fleet plan to match the weaker demand trends in Brazil.

TAM's financial results and balance sheet have already benefited from the merger in various ways. All hedging and new aircraft financing are done at the consolidated level, and TAM's aircraft and related debt are likely to be moved to the Latam balance sheet, which has the US dollar as its functional currency. This reduces earnings volatility caused by external factors such as foreign exchange. Even with the loss of Latam's investment-grade credit rating (the biggest negative in the merger), TAM's aircraft financing costs have been reduced. Latam is working to recover the investment-grade ratings, though it could take a couple of years. Following approval from shareholders in early June, the company is planning a $1bn equity offering in the second half of 2013.

Azul-Trip: the emerging "third force"

Azul was uniquely well-funded when it began operations in December 2008, having attracted US$200m in capital from US and Brazilian investors. It has also grown extremely rapidly, achieving $1bn revenues in its third year (2011) and capturing a 13.4% domestic market share in April – or 17.5% when its Webjet acquisition is included. Even though it has only attained marginal profitability (and only on an operating basis), the story is compelling enough for an IPO. Azul filed plans on May 24 to list preferred shares in Brazil and the US in offerings that could raise up to R$1.1bn (US$550m) mainly for fleet expansion.

Azul has been able to grow so rapidly, first, because it has developed a new hub at Viracopos Airport in the city of Campinas, about 70 miles from Sao Paulo. Second, Azul has avoided too much overlap with Gol and TAM, because it focuses on regional markets and operates smaller aircraft (E190/195s and ATR72s).

Third, Azul has been well-received by Brazil's travelling public. Its low fares, nonstop flights that bypass hubs and reduce travel time, superior JetBlue-style offerings (leather seats, more legroom, free LiveTV at every seat) and its customer-focus and fresh approach have gone down well in the marketplace. Like JetBlue, its has built a strong brand.

According to the preliminary IPO prospectus, Azul's model is to stimulate demand by providing frequent and affordable air service to underserved markets throughout Brazil. Because it operates smaller aircraft, it can serve cities the larger competitors cannot. These attributes have enabled it to attract both business traffic and cost-conscious leisure travellers, build the largest airline network in Brazil in terms of destinations (103 – roughly the same as Gol and TAM combined in Brazil) and dominate the markets where it is present. Azul is the only airline on 70.7% of its routes and the frequency-leader on another 10.1% of its routes.

The leading network position has enabled Azul to achieve significantly higher unit revenues than the other domestic carriers. The PRASK premium, load factors consistently around the 80% mark, high efficiency and a competitive cost structure offset the poorer economics of smaller aircraft. Azul also gives credit to its "proprietary yield management system" for maximising revenue generation.

Brazil may be an especially suitable market for this type of business model, because it has a large number of medium-sized cities scattered around the huge country that have much economic power, and hence travel demand, but cannot support regular operations with 150-seat aircraft. Azul has tapped opportunities in such underserved regional markets, many of which had considerable pent-up demand and have continued to see double-digit growth even as Brazil's GDP growth has slowed.

Azul seems intent on focusing on such markets at least for the medium term, first, because in 2010 it ordered up to 40 ATR 72-600s. The 70-seat aircraft enable it to add regional routes that are too small even for its 106-seat E190s and 118-seat E195s. Second, there was the May 2012 acquisition of regional carrier TRIP.

The all-stock merger with TRIP offered cost savings and major revenue benefits through the expanded network. The two airlines had uniform fleets, similar strategies and little overlap. TRIP brought 46 additional cities, strategic slots at Guarulhos and Santo Dumont, a leading position in Belo Horizonte (Brazil's third largest metro area) and substantially improved network connectivity all around. Azul and TRIP have codeshared since December, received final antitrust approval from CADE in March, have fully integrated all administration and back-office functions and expect to receive a single operating certificate from ANAC by July.

At the end of March, Azul and TRIP had a combined operating fleet of 118 aircraft – 41 E-195s, 22 E-190s, five E-175s, 39 ATR 72s and 11 ATR 42s. Firm order commitments totalled R$2.4bn – 23 E-jets and 20 ATR 72s, for delivery in 2013-2016.

Since Azul-TRIP will continue growing in 2013, albeit at a somewhat slower rate, while Gol and TAM contract, the combine could have 20% or more of the domestic market by the end of this year. Azul is keen to gain better access to Sao Paulo's centrally-located Congonhas Airport, and it could be a major beneficiary if the slot redistribution takes place. Longer-term progress will depend on the infrastructure being there at the mid-sized cities to facilitate growth, though the government seems to be making regional air services and infrastructure a priority and Azul does not anticipate any problems.

The interesting question now is how soon Azul-TRIP will order a third, larger aircraft type and/or venture into the intra-South America international markets. Neeleman indicated last year that the fleet plans were set through 2015 but that after that the airline could consider other aircraft types.

The IPO will enable key investors such as the US private equity firm TPG, which bought a 10% stake in Azul in January 2010, to exit, if they so choose. But Neeleman, who currently holds 67% of Azul's stock and voting rights, will remain firmly in control. He will continue to control all shareholder decisions, including the ability to appoint the majority of the board of directors. Neeleman, who was also

JetBlue's visionary founder, has indicated in several interviews in recent years that he did not like the way he was ousted from the New York-based carrier by its board of directors after one fateful snowstorm in early 2007.

Avianca Brazil: Future link with TAP?

While industry consolidation has left Avianca Brazil in a more distant fourth place in the domestic market, this airline too has potential to be a major player in Brazil. First, it has grown extremely rapidly in the past couple of years, to account for 7.1% of the domestic market in April. Second, when TAM leaves Star, Avianca Brazil could play a key role in ensuring other Star members access to Brazil. Third, Avianca Brazil is a potential future bidder (or a partner) for Portugal's TAP.

Compared to Azul's impeccable pedigree, Avianca Brazil's background is more colourful. Established in 1998 as an air taxi company, Oceanair began scheduled services in 2002. Brazil's Synergy Group acquired it in 2004 and grew it rapidly in the wake of Varig's contraction in late 2007, even taking it to international markets with 767-600s. That was a mistake and led to a sharp contraction in 2008. Oceanair ended international flights and shed its 737s, 757s and 767s, leaving only a fleet of 14 Fokker 100s. There was no growth in 2008-2009.

In early 2010 Oceanair was rebranded as Avianca Brazil (its 100%-owners also hold a controlling 60% stake in AviancaTaca Holdings). The airline resumed expansion with the help of A318s leased from GECAS and with A319s and A320s that came from its sister company. Its fleet has grown from 14 aircraft at year-end 2009 to 32 at present.

The business model is slightly unusual and not proven. Avianca Brazil is very up-market, offering full service even on the shortest hauls. It operates single-class but offers the most generous domestic economy seat pitch, superior in-fight entertainment and free meals. It has won many "best airline" type awards. It achieves extremely high load factors - usually around the 80% mark; in March the load factor was 82.2%, 11 points above the industry average. In other words, by offering a better product at the same price as competitors, Avianca Brazil captures more traffic, which it claims covers the higher costs.

Avianca Brazil benefits from extensive slot holdings at key airports. This has enabled it to build a 24-point network focusing on trunk routes. It has a large operation at Sao Paulo's Guarulhos airport (its main base) and it operates on the lucrative Rio de Janeiro-Sao Paulo shuttle route, offering 10 or so daily flights in each direction.

Since profitability has been elusive, the management is trying to rein in growth in the short term. Or, as Synergy's owner German Efromovich recently put it, the airline has a plan of "orderly and sustained" growth. Avianca Brazil is committed to taking five A318s in 2013 – the last batch of the 15 aircraft coming from GECAS. But there is much flexibility with the Fokker 100 retirement schedule, which is now being accelerated to keep the fleet size roughly flat (though there will still be 30%-plus ASK growth as the A318s replace the smaller aircraft).

Should it become desirable to boost the growth rate – say, if Gol's and TAM's cutbacks lead to attractive market opportunities – Avianca Brazil could also receive more A320s from its sister company. Synergy and AviancaTaca have a strong A320 orderbook, so Avianca Brazil need never be short of aircraft.

In the longer-term Avianca Brazil is likely to reintroduce international services. It is not part of the recently-launched AviancaTaca single brand, but it is considering joining the FFP and at some future point is likely to be integrated into that group. But even before that happens, Avianca Brazil is expected to join the Star alliance and fulfil an important role as possibly the only Star member in Brazil. Because of its presence at Brazil's main airports, it is well placed to connect to other Star carriers.

There is also the intriguing possibility that Avianca Brazil could secure TAP as a sister company – or even be a bidder for TAP - when the Portuguese carrier's privatisation process restarts, which could be this autumn. TAP's extensive service to Brazil would be a great match with Avianca Brazil's domestic network.

By Heini Nuutinen
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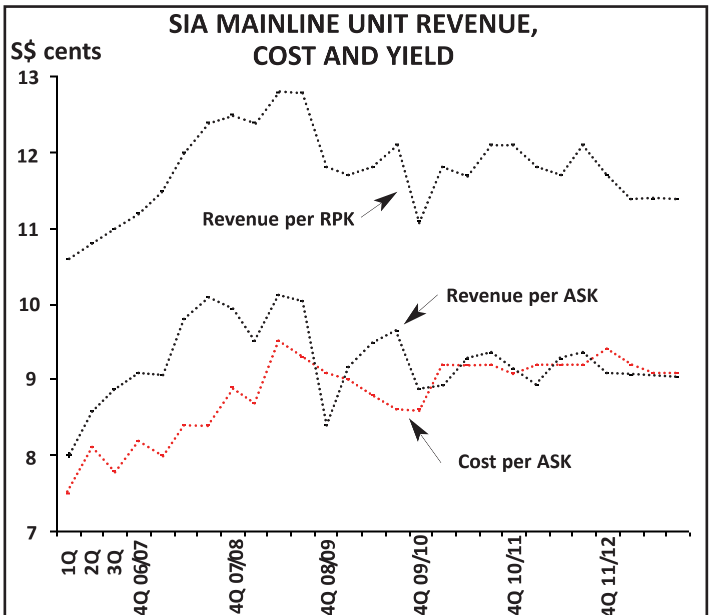
Singapore Airlines: Under pressure

With increasing competition to its mainline resulting in a fall in operating profits of a third in its latest quarterly results, the Singapore Airlines Group is now urgently pursuing a "portfolio strategy" of different brands for different segments of the market. Will the change in strategy be enough to fend off the challenge of LCCs within Asia and from mainlines on intercontinental routes?

The Singaporean flag-carrier's history dates back to the 1940s, but today it is facing perhaps its most serious challenge yet. In the third quarter of its 2012/13 financial year (the three months ending December 31st 2012), after a 0.4% drop in revenue the SIA group's operating profit fell 17% to S$131m (US$105m). Net profit in the period rose 6% to S$158m thanks to the sale of aircraft and other equipment as well as higher net interest income, although the group was hit by a $$20m provision in the period for SIA Cargo due to penalties owed to the Australian Competition and Consumer Commission for its role in cargo price-fixing in Australia and New Zealand.



Note: Financial YE is March 31st.

What was particularly worrying in the third quarter results was a significant fall in operating profit at the mainline to S$86.8m – a reduction of SS$50m year-on-year (or 36.5%). This mainline profit erosion was due largely to a rise in non-fuel expenditure (hedging helped offset the rise in fuel costs), and specifically staff costs (up S$25m, or 6.8%), aircraft depreciation and rental costs (up S$20m/4.6%) and "passenger" costs (SS$15m/9.7%).

SIA said the outlook for the rest of 2013 was challenging due to the depressed cargo market, the troubled European economy and weak recovery in the US, with "loads and yields of both passenger and cargo businesses expected to remain under pressure". Yield is a key problem for SIA. In the third quarter of its financial year the mainline saw a 7.4% rise in RPKs outstrip a 4.6% increase in ASKs, leading to a 2.1 percentage point rise in load factor to 79.3%, but yield fell by a huge 0.7 S$ Cents per RPK (to 11.4 Cents) compared with the same quarter of the previous financial year (October-December 2011).

Yield problem

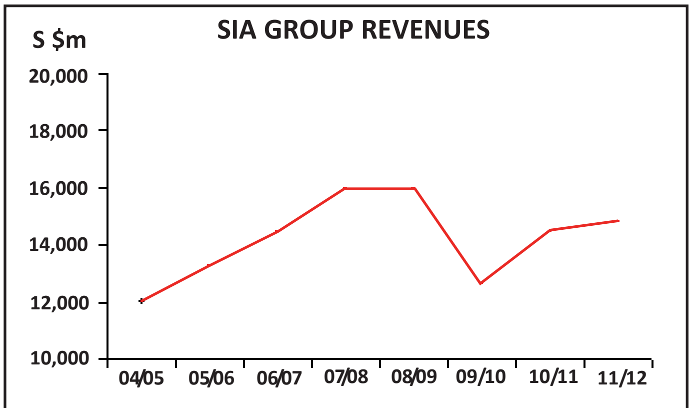
As can be seen in the chart, on the left, the yield fall in the third quarter is just the continuation of a steady erosion from a high of almost 13 S$ Cents per RPK in the second half of 2008. At the unit level of analysis, the graph shows the dangerous coming together of unit revenue and unit costs lines - again since 2008 - that has the mainline on the brink of an operating loss almost every quarter. Looking at another measure, despite recent improvement the mainline's passenger load factor trend line has been virtually flat for the last six years.

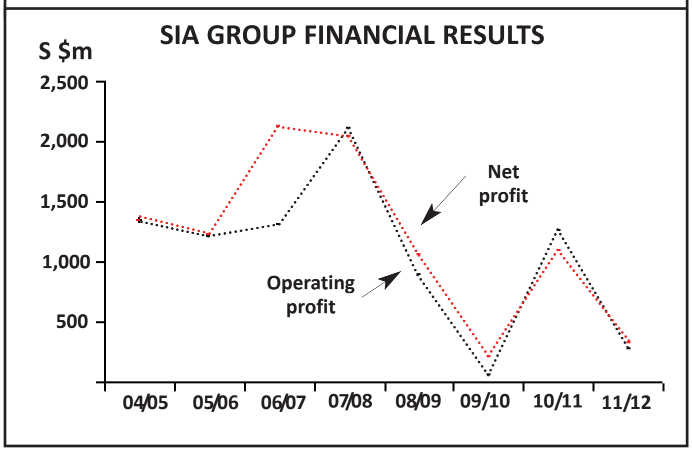
The reason for these worrying KPIs at the mainline is increasing competition. The percentage of Changi airport's traffic that comes comes from LCCs has risen from nothing to 25% in seven years, but as well as LCCs such as AirAsia within the Asia/Pacific region, the SIA mainline is facing an increasing threat from Middle Eastern airlines that are increasing capacity to/from the area. For example, Qantas has ended its 15 year joint venture with British Airways and instead is partnering with Emirates, which means that Qantas's flights between London and Sydney and Melbourne will route via Dubai rather than Singapore, which will inevitably affect the popularity of Changi as a connecting hub.

While the SIA group is still (just) profitable and its position can by no means be regarded as dire, a strategic response from the group towards its challenges came late last year when it publicly acknowledged it was now following a "portfolio strategy" in order to compete better across differing market segments. Under this "four-brand" strategy, the SIA mainline and its regional subsidiary Silk Air will continue to cater for premium leisure and business passengers while two other airlines - Tiger Airways and Scoot - are targeting budget travellers. As one analyst puts it, this strategy "is hardly rocket science" and in fact strategically the SIA group is playing catch up with major rivals in the Asia/Pacific region, many of whom implemented similar portfolio strategies years ago.

On the full service side, the mainline SIA fleet currently has 101 aircraft, comprising 58 777s, 19 A330s, five A340s and 19 A380s, with an average fleet age of less than seven years. These operate a scheduled network through the Asia/Pacific region, Europe, Africa, the Middle East and North America. There are currently 68 aircraft on firm order for the mainline – eight 777s, 15 A330s, 40 A350s and five A380s. This January SIA firmed up an order for five A380s and 20 A350-900s, bringing its total order book to 40 A350s, which will start being delivered from 2015. At the end of May SIA ordered 30 A350-900s with 20 options, which will replace the 32-strong 777-200 fleet, which has an average age of 11 years.

Given that the mainline supplied fewer ASKs in 2012 than it did in 2008, the airline





is cautious on expansion. In this summer's schedule the mainline is increasing frequency to Adelaide and Melbourne, bringing the total group flights to Australia to 133 per week. Services to Fukuoka and Osaka will also increase over the summer, as well flights to Copenhagen and on the Singapore-Moscow-Houston route. On the other hand, non-stop services between Singapore and Los Angeles and between Singapore and Newark will close by the end of 2013 - in October and November respectively – although in March SIA extended a codeshare deal with Virgin America (that started in December 2012) to include an FFP partnership.

The direction of travel for the mainline is clear. Despite suspending the recruitment of cadet pilots and implementing a range of other measures such as voluntary unpaid leave, SIA currently has too many pilots on its books and is releasing 76 of them when their fixed term contracts expire through to the end of June this year. However, the mainline has also been investing significant-

SIA GROUP FLEETS	In service	On order
SIA mainline		
777-200	19	
777-200ER	13	
777-300	7	
777-300ER	19	8
A330-300	19	15
A340-500	5	
A350-900		40
A380-800	19	5
Total	**101**	**68**
Silkair		
A319	6	
A320	16	2
737-800		23
737 MAX-8		31
Total	**22**	**56**

ly in upgrading its product via cabin redesigns, revamping in-flight entertainment systems and improving lounges, so contraction on the mainline side is being accompanied by improvement to product, in line with the new portfolio strategy.

Regional services for the SIA group are operated by Silk Air, which has 16 A320s and six A319s that will be replaced by outstanding orders for 23 737-800s and 31 737 Max 8s. Silk Air currently operates to more than 40 scheduled destinations out of Singapore, as well as to a handful of charter destinations for the SIA group tour operators. Also in the SIA group is SIA Cargo, which has 12 747-400 freighters (which will need to be replaced at some stage).

The SIA group's LCCs

Tiger Airways was launched as an LCC in September 2004 by SIA, Indigo Partners, Irelandia Investments and Temasek Holdings (the investment vehicle of the Singapore government), and today the SIA group owns 32.7% of parent company Tiger Airways Holdings.

The Tiger group operates to more than 50 destinations in the Asia/Pacific region across 13 countries from bases in Singapore, Indonesia, the Philippines and Australia, using a fleet of A320 family aircraft. It has 19 aircraft stationed in Singapore and 11 at Tiger Australia, based in Melbourne. Tiger also has two associate airlines in Indonesia and the Philippines.

In the calendar year 2012, the Tiger group carried 6.3m passengers (compared with 5.7m in 2011), with 4.2m of them flying with Tiger Airways Singapore and the rest with the Australian operation. In the nine month period ending December 2012, despite a 36.9% rise in revenue to S$625.6m Tiger Airways Holdings made an operating loss of S$5.4m and a net loss of S$30m. However, whereas in the third quarter (October to December 2012) Tiger Singapore made an operating profit of S$27m on revenue of SS173m, Tiger Australia made a S$13m operating loss on revenue of S$73m, which Tiger said was "largely due to a 11.5% drop in yield due to stiff competition in the domestic market, and rising costs of operations".

In fact Tiger Australia has never made a profit since launching in 2007 (instead recording accumulated losses of S$230m), and hopes of a turnaround recently disappeared when the airline was grounded by civil aviation authorities in Australia for six weeks in 2011 following safety fears, with ongoing capacity restrictions on Tiger Australia only lifted in the fourth quarter of 2012.

A partial solution to the problem was found when in October 2012 Virgin Australia announced a deal to buy 60% of Tiger Airways Australia (which is currently a 100% subsidiary of Tiger Airways Holdings) for approximately S$45.5m, with a plan for Virgin and Tiger to subsequently operate Tiger Australia as a joint venture in the domestic Australian market (though Virgin would be responsible for day-to-day operations), where it would compete against Qantas's Jetstar. Under the terms of the agreement Virgin and Tiger would jointly invest S$65.6m into Tiger Australia to fund growth from 11 to 35 aircraft by 2018.

The deal was obviously subject to regulatory approval, and in January the ACCC (the Australian competition regulator) asked for further details after saying its initial analysis indicated that the agreement might reduce competition in the Australian market to just two groups (Qantas and Jetstar versus Virgin and Tiger). In March this year the ACCC postponed a decision yet again (it's now likely to be given in May), and the longer the delay the more the likelihood is that the regulator will not allow the deal to go through unless conditions on guaranteeing or even increasing seat numbers on domestic routes are met.

If approved the deal is due to be completed by the end of June, which in the words of one local analyst would allows Tiger to "partially dump" Tiger Australia and focus in on more promising markets elsewhere in Asia (though previous attempts to launch subsidiaries or associates in South Korea and Thailand have come to nothing). But if the deal is not approved by the ACCC then it's not clear what Tiger Airways Holdings would do next - although closing down the entire Australian operation may be the least bad option.

It's critical that the Australian problem is sorted out one way or the other. Tiger carried out an IPO three years ago but the share is trading at levels around half the issue price, and although it raised another S$158m as recently as September 2011 (and only 20 months after it IPO'd), that cash has effectively been burned through by the troubles at Tiger Australia.

In March this year Tiger Airways Holdings revealed plans to raise S$77m through a rights issue and a further S$220m through an offer of convertible securities to existing shareholders. The funds raised will strengthen the balance sheet and repay debt (up to S$100m) and fund the airline's expansion (with S$70m-S$90m going to the affiliate airlines and S$60m-S$80m to pay for aircraft). Tiger has 29 A320s on order, although at least eight of which will go to the Australian operation and others to the two affiliate airlines. SIA will subscribe for its full entitlement and has agreed to buy any excess not taken up by other shareholders (with a maximum limit of a 49.9% share) when the funding round is completed in May.

Before expanding elsewhere (and assuming the Australian problem is sorted out), of prime concern for the Tiger group is getting its associate airlines into profitability. Tiger group chairman Joseph Pillay says that the group has to "expand beyond the shores of Singapore in order to safeguard the future of the Tiger group… Indonesia and the Philippines are the two largest countries in Asean, where we believe our destiny lies."

Mandala Airlines was launched in Indonesia in 1969 but went bankrupt before Tiger Airways bought a 33% stake in January 2012, after which the carrier was relaunched as a LCC in April of that year. Indonesian-based Saratoga Capital controls 51% of the airline, with the rest split among creditors of the airline. Today Mandala operates seven A320s, and the fleet will rise to 10-15 by the end of this year and 25 by 2015. It has 25 A320s on order, although in April this year Saratoga Capital said Mandala would convert Tiger Airways' options for 18 A320 aircraft into firm orders, bringing the order book to 43.

Although Indonesia is a huge market, it is very competitive one and Mandala has to compete against LCCs that include Indonesia AirAsia and Lion Air, the latter of which has 88 737s and in February placed a firm order for 29 737-900ERs and 201 737 MAX aircraft, worth some US$24bn at list prices. That was the largest ever aircraft order in history until Lion Air placed another order, in March, for 234 Airbus aircraft worth approximately another $24bn at list prices.

Competition from LCCs is also an issue at Tiger's other affiliate – the Philippine-based Southeast Asian Airlines (known as SEAir). SEAir was launched in 1995 and today operates two A319s and three A320s on domestic routes out of Manila and on international routes out of Clark airport to Singapore, Hong Kong, Thailand and Malaysia. Tiger Airways Holdings increased its stake in SEAir from 32.5% to 40% in August 2012 for S$2.5m (the rest of the equity is held by Filipino investors), although Tiger is also providing working capital of up to S$$40m over a five year period. However, SEAir has to compete against Cebu Pacific Air, which operates 48 aircraft and has more than 59 on firm order.

Some analysts worry that SEAir and Mandala will prove to be problematical for the Tiger group given the high level of LCC competition in these countries. Indeed Tiger recently stated that the two airlines "are unlikely to contribute positively to the group's performance" for the financial year ending 31 March. In the quarter ending December 2012 SEAir contributed a S$8.3m share of losses to Tiger Airways, and Tiger adds that it “has not recognised its share of cumulative losses of Mandala amounting to S$14.3m as at 31 December”.

Tiger has been shaking up its senior management team recently - Koay Peng Yen (a shipping industry executive) became CEO of Tiger Airways Holdings in August 2012 and Ho Yuen Sang (previously COO of Jetstar Asia) was appointed managing director of Tiger Airways Singapore in December last year and they undoubtedly have a major challenge in sorting out this part of the SIA group.

Additionally, under the group’s new strategic doctrine Tiger has been tasked with working more closely with fellow LCC Scoot, although this was made easier when the terminal for budget airlines at Singapore’s Changi airport closed in September last year (so that it can be replaced by a brand new terminal in 2017), with Tiger Airways switching operations to Terminal 2, where Scoot is based.

Scoot

Ironically when plans for medium-haul LCC subsidiary Scoot were announced by Goh Choon Phong, CEO of the SIA group, there was considerable opposition from some SIA group executives, who were worried that the airline would cannibalise revenues at the mainline. But of course the risk of doing nothing as a response to the rise of AirAsia X and others is far greater, and Scoot is managing to win completely new (cost-conscious) customers for the group – which itself partly spurred the move to the new portfolio strategy.

Based at Changi airport, Scoot was launched in June 2012 and offers a two-class service with frills available on a paid-for basis. Today it operates four 777-200s (acquired from SIA and refurbished) to Bangkok, Tianjin, Taipei, Sydney and Tokyo, with routes to Shenyang and Qingdao due to commence in November. Although a fifth 777 will arrive in May or June ,Scoot has 20 787-9s on order, which were originally ordered by its parent SIA, although some of these may be swapped for 787-8 and 787-10 variants. The aircraft will arrive from late 2014 onwards and will replace the 777s in order to underpin substantial growth in its network, with ambitions for routes to Africa, Europe, India and the Middle East in the medium- to long-term.

With Scoot operating medium-and long-haul routes of more than five hours’ flying time (and where its main competition is AirAsia X and Jetstar) and Tiger Airways concentrating on short-haul, given the new group portfolio strategy it was no surprise when last October Tiger and Scoot agreed a wide-ranging partnership deal. The first phase of which includes joint itineraries on certain routes in the Asia/Pacific region. However both airlines are being somewhat cautious in how fast they expand this partnership, as they want to avoid having to obtain anti-trust immunity.

Too little too late?

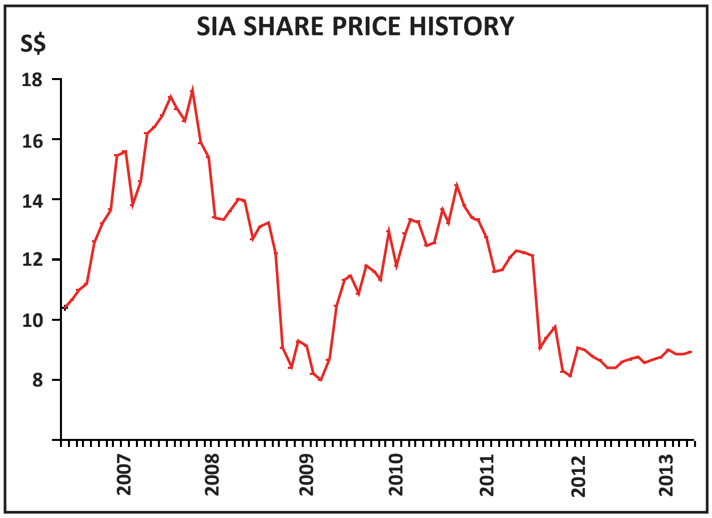
Full-year results (for the 12 months ending March 31st) are due to be released by the SIA group sometime in mid-May, but that set of financials will be too early to tell just how effective the new portfolio strategy will prove to be. Investors are yet to be persuaded – as can be seen in the graph, xxx, the share price has plunged since 2007 and it has remained flat since the new portfolio strategy was announced in late 2012.

As an analyst note from Citigroup in February puts it, the portfolio strategy and improvements to the SIA group’s mainline product are “necessarily defensive in mitigating the structural headwinds, but not effective in overcoming them”. Specifically Citigroup says that the “SIA/SilkAir premium business is on a structural decline”, so in effect what SIA is doing – although correct – may be too little, too late. At the very least the fact that the SIA group has had to announce such a strategy is an admittance that it had previously been poor in co-ordinating the operations and schedules of similar carriers in the group, whether within the full-service or LCC segments

Nevertheless the group has little option other than to press ahead with this new direction, and hope that the rate at which its full service business declines is compensated for as much as possible by its LCC operations. That's made all the more important by the much anticipated "Open Skies" policy that is scheduled to be adopted by the Association of Southeast Asian Nations in 2015, where the current restrictions on airlines operating outside of their home country will be lifted, and which may encourage the SIA group to combine organic growth with another acquisition.

Last December SIA agreed to sell its 49% stake in Virgin Atlantic to Delta Air Lines for US$360m, subject to regulatory approval but expected to be completed by the end of 2013. SIA's stake in the UK-based airline has never quite provided the strategic benefits and synergies that SIA had hoped for, and the group will recover far less than the US$975m it paid out back in March 2000. However the Virgin investment had already been fully written off in SIA's balance sheet, and so the deal will generate cash for SIA that can be invested in new aircraft. After booking a profit on its disposal, ties between the airlines such as FFPs and codesharing will remain in place for at least the short-term.

After hopefully learning lessons from the Virgin deal, Goh Choon Phong says that SIA is "open" to making investments in other airlines, particularly within the Asia/Pacific area. Late last year SIA complete the purchase of a 10% stake in Virgin Australia for S$109m. The two airlines have co-operated since 2011, in a deal that has included joint market, schedule co-ordination, codesharing and reciprocal FFP benefits. SIA has recently agreed to top-up its stake in Virgin Australia by another 9.9%, in a move increasing its stake to 19.9%. The purchased is subject to approval from Australia's Foreign Investment Review Board but the move does illustrate SIA's commitment to the Australian market (notwithstanding the the proposed Tiger Airways Australia deal). Virgin Australia is challenging Qantas hard in the domestic Australian market and its shareholders also include the Virgin Group (26%), Air New Zealand (19.9%) and Etihad Airways (10%). Virgin Australia specialises in the business travel market within Australia, which is in contrast to the "budget" travellers targeted by Tiger Australia.



The SIA group says that the Virgin Australia deal will not be the last as it is "actively pursuing partnership opportunities in India, China and Southeast Asia", according to Goh Choon Phong. Its choices are limited however. A joint venture between Tata and SIA to buy a stake in Air India was put forward 13 years ago but came to nothing and expansion into India now may be too late given that Etihad Airways aims to buy a minority stake in Jet Airways and AirAsia is launching a joint venture Indian airline in which it will have a 49% share and the Tata Group 30%.

The big prize remains China, where in 2008 SIA failed in a bid to acquire 15% of China Eastern Airlines after Air China successfully lobbied the Chinese government against the deal. Those "political" barriers to an entry into the Chinese market have not gone away, but some analysts believe that - free from the distraction that was Virgin Atlantic - SIA still has an appetite to take a stake in a Chinese airline.

		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.
Air France/	Year 2010/11	31,219	19,236	1,171	810	3.8%	2.6%	250,836	204,737	81.6%	71,320	102,012
KLM Group	Apr-Jun 11	8,947	9,153	-206	-283	-2.3%	-3.2%	66,531	53,931	81.1%	19,653	
YE 31/12	Apr -Sep 11	18,600	18,240	360	-257	1.9%	-1.4%	137,282	114,846	83.7%	40,605	102,516
	Year 2011	33,923	34,415	-492	-1,126	-1.4%	-3.3%	264,895	217,169	81.8%	59,513	102,012
	Jan - Mar 12	7,400	8,058	-658	-482	-8.9%	-6.5%	63,391	51,733	81.6%	17,463	101,222
	Apr - Jun 12	8,351	8,920	-569	-1,150	-6.8%	-13.8%	67,456	55,820	82.8%	19,980	
	Jul - Sep 12	8,989	8,356	633	383	7.0%	4.3%	72,246	62,098	86.0%	21,279	
	Oct - Dec 12	8,176	8,361	-185	-305	-2.3%	-3.7%	66,206	54,236	81.9%	18,734	
	Year 2012	32,959	33,345	-386	-1,533	-1.2%	-4.7%	269,299	223,887	83.1%	77,448	
IAG Group	Apr-Jun 11	5,951	5,678	273	135	4.6%	2.3%	53,425	42,635	79.8%	13,288	56,649
YE 31/12	Jul - Sep 11	6,356	5,842	514	401	8.1%	6.3%	55,661	47,022	84.5%	14,553	57,575
	Year 2011	22,781	22,105	676	735	3.0%	3.2%	213,193	168,617	79.1%	51,687	56,791
	Jan - Mar 12	5,136	5,463	-326	-240	-6.4%	-4.7%	51,425	39,140	76.1%	11,384	56,532
	Apr - Jun 12	5,926	5,931	-5	-72	-0.1%	-1.2%	55,851	45,421	81.3%	14,347	60,418
	Jul - Sep 12	6,326	5,988	338	304	5.3%	4.8%	58,260	49,343	84.7%	15,760	61,340
	Oct - Dec 12	5,874	5,926	-52	-540	-0.9%	-9.2%	53,607	42,168	78.7%	13,117	59,506
	Year 2012	23,295	24,083	-788	-1,187	-3.4%	-5.1%	219,172	176,102	80.3%	54,600	59,574
	Jan - Mar 13	5,046	5,800	-755	-807	-15.0%	-16.0%	50,359	38,975	77.4%	11,772	58,065
Lufthansa	Year 2010	36,057	34,420	1,636	1,492	4.5%	4.1%	235,837	187,700	79.3%	91,157	117,019
YE 31/12	Apr-Jun 11	10,967	10,636	331	433	3.0%	3.9%	68,763	53,603	78.0%	28,147	118,766
	Jul- Sep 11	11,430	10,616	814	699	7.1%	6.1%	73,674	60,216	81.7%	30,408	120,110
	Year 2011	40,064	38,920	1,143	-18	2.9%	0.0%	268,939	207,536	77.2%	106,335	120,055
	Jan - Mar 12	8,675	9,174	-499	-520	-5.8%	-6.0%	59,648	44,242	74.2%	21,867	120,898
	Apr - Jun 12	10,136	9,673	464	294	4.6%	2.9%	69,228	53,384	77.1%	27,483	117,416
	Jul - Sep 12	10,400	9,538	862	803	8.3%	7.7%	71,197	59,410	83.4%	29,433	114,022
	Year 2012	37,584	36,931	654	1,235	1.7%	3.3%	259,861	204,775	78.8%	103,051	116,957
	Jan - Mar 13	8,311	8,761	-450	-576	-5.4%	-6.9%	58,111	44,247	76.1%	21,631	116,516
SAS	Year 2010	5,660	5,930	-270	-308	-4.8%	-5.4%	34,660	25,711	74.2%	25,228	15,559
YE 31/12	Jan-Mar 11	1,336	1,395	-59	-54	-4.4%	-4.0%	8,528	5,655	66.3%	6,093	14,972
	Apr-Jun 11	1,793	1,648	145	88	8.1%	4.9%	9,848	7,494	76.1%	7,397	15,264
	Jul-Sep 11	1,642	1,565	77	33	4.7%	2.0%	9,609	7,579	78.9%	6,928	15,375
	Oct-Dec 11	1,507	1,559	-51	-308	-3.4%	-20.5%	9,019	6,446	71.5%	6,788	14,958
	Year 2011	6,386	6,286	100	-260	1.6%	-4.1%	37,003	27,174	73.4%	27,206	15,142
	Jan - Mar 12	1,419	1,548	-128	-108	-9.0%	-7.6%	8,701	5,943	68.3%	6,416	14,836
	Apr - Jun 12	1,642	1,551	91	46	5.5%	2.8%	10,300	7,936	77.0%	7,625	14,985
	Jul - Sep 12	1,644	1,517	128	64	7.8%	3.9%	10,154	8,158	80.3%	7,243	14,969
FY Jan - Oct 2012	Year 2012	5,297	5,339	-42	-145	-0.8%	-2.7%	36,126	27,702	76.7%	25,916	14,897
Ryanair	Year 2009/10	4,244	3,656	568	431	13.5%	10.2%			82.0%	66,500	
YE 31/03	Apr-Jun 10	1,145	992	152	120	13.3%	10.5%			83.0%	18,000	7,828
	Jul-Sep 10	1,658	1,150	508	426	30.7%	25.7%			85.0%	22,000	8,100
	Oct-Dec 10	1,015	1,016	-1	-14	-0.1%	-1.3%			85.0%	17,060	8,045
	Year 2010/11	4,797	4,114	682	530	14.2%	11.0%			83.0%	72,100	
	Apr-Jun 11	1,661	1,418	245	201	14.7%	12.1%			83.0%	21,300	
	Jul-Sep 11	2,204	1,523	681	572	30.9%	25.9%			87.0%	23,000	
	Oct - Dec 11	1,139	1,099	39	20	3.4%	1.8%			81.0%		
	Year 2011/12	6,053	5,112	942	772	15.6%	12.8%			82.0%	75,800	
	Apr - Jun 12	1,648	1,480	170	127	10.3%	7.7%			82.0%	22,500	
	Jul - Sep 12	2,280	1,554	727	622	31.9%	23.7%			87.0%	25,460	
	Oct - Dec 12	1,219	1,175	44	23	3.6%	1.9%			82.0%	17,300	
	Year 2012/13	6,103	5,205	897	711	14.7%	11.7%			82.0%	79,300	
easyJet	Year 2007/08	4,662	4,483	180	164	3.9%	3.5%	55,687	47,690	85.6%	43,700	6,107
YE 30/09	Oct 08-Mar 09	1,557	1,731	-174	-130	-11.2%	-8.3%	24,754	21,017	84.9%	19,400	
	Year 2008/09	4,138	3,789	93	110	2.3%	2.7%	58,165	50,566	86.9%	45,200	
	Oct 09 - Mar10	1,871	1,995	-106	-94	-5.6%	-5.0%	27,077	23,633	87.3%	21,500	
	Year 2009/10	4,635	4,364	271	240	5.9%	5.2%	62,945	56,128	87.0%	48,800	
	Oct 10 - Mar 11	1,950	2,243	-229	-181	-11.7%	-9.3%	29,988	26,085	87.0%	23,900	
	Year 2010/11	5,548	5,115	432	362	7.8%	6.5%	69,318	61,347	88.5%	54,500	
	Oct 11 - Mar 12	2,302	2,458	-156	-141	-6.8%	-6.1%	30,785	27,329	88.8%	25,200	
	Year 2011/12	6,076	5,554	522	402	8.6%	6.6%	72,182	65,227	88.7%	58,400	
	Oct 12 - Mar 13	2,453	2,515	-61	-72	-2.5%	-2.9%	31,241	28,395	88.7%	26,600	

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 emp.
Alaska	**Year 2010**	**3,832**	**3,361**	**472**	**251**	**12.3%**	**6.6%**	**44,636**	**36,758**	**82.4%**	**23,334**	**11,696**
	Year 2011	**4,318**	**3,869**	**449**	**245**	**10.4%**	**5.7%**	**47,679**	**40,284**	**84.5%**	**24,790**	**11,840**
	Jan - Mar 12	1,039	967	72	41	6.9%	3.9%	11,819	10,029	84.9%	5,995	11,832
	Apr- Jun 12	1,213	1,087	116	68	9.6%	5.6%	12,776	11,054	86.5%	6,565	11,965
	Jul - Sep 12	1,272	1,003	269	163	21.1%	12.8%	13,315	11,654	87.5%	6,950	12,035
	Oct - Dec 12	1,132	1,058	74	44	6.5%	3.9%	12,665	10,814	85.4%	6,387	11,984
	Year 2012	**4,657**	**4,125**	**532**	**316**	**11.4%**	**6.8%**	**50,577**	**43,462**	**85.9%**	**25,896**	**11,955**
	Jan - Mar 13	1,133	1,069	64	37	5.6%	3.3%	12,847	10,937	85.1%	6,346	12,013
American	**Year 2010**	**22,170**	**21,862**	**308**	**-471**	**1.4%**	**-2.1%**	**246,611**	**201,945**	**81.9%**	**86,130**	**78,250**
	Jan - Mar 11	5,533	5,765	-232	-436	-4.2%	-7.9%	60,912	46,935	77.1%	20,102	79,000
	Apr-Jun 11	6,114	6,192	-78	-286	-1.3%	-4.7%	63,130	52,766	83.6%	22,188	80,500
	Jul- Sep 11	6,376	6,337	39	-162	0.6%	-2.5%	64,269	54,552	84.9%	22,674	80,600
Chapt. 11 from Nov 29	**Year 2011**	**23,957**	**25,127**	**-1,170**	**-1,965**	**-4.9%**	**-8.2%**	**248,349**	**203,562**	**83.9%**		
	Jan - Mar 12	6,037	6,126	-89	-1,660	-1.5%	-27.5%	61,021	50,722	83.1%		
	Apr - Jun 12	6,452	6,310	142	-241	2.2%	-3.7%	61,618	52,441	85.1%		78,100
	Jul - Sep 12	6,429	6,378	51	-238	0.8%	-3.7%	62,690	53,593	85.5%		77,900
	Oct - Dec 12	5,937	5,933	4	262	0.1%	4.4%	65,680	53,216	81.0%		76,200
Delta	**Year 2010**	**31,755**	**29,538**	**2,217**	**593**	**7.0%**	**1.9%**	**374,458**	**310,867**	**83.0%**	**162,620**	**79,684**
	Year 2011	**35,115**	**33,140**	**1,975**	**854**	**5.6%**	**2.4%**	**377,642**	**310,228**	**82.1%**	**163,838**	**78,392**
	Jan - Mar 12	8,413	8,031	382	124	4.5%	1.5%	87,559	69,765	79.7%	37,557	78,761
	Apr - Jun 12	9,732	9,598	134	-164	1.4%	-1.7%	95,563	80,497	84.2%		80,646
	Jul - Sep 12	9,923	8,615	1,308	1,047	13.2%	10.6%	100,232	86,625	86.4%		76,626
	Oct - Dec 12	8,602	8,250	352	7	4.1%	0.1%	87,453	72,861	83.3%		73,561
	Year 2012	**36,670**	**34,495**	**2,175**	**1,009**	**5.9%**	**2.8%**	**370,807**	**310,533**	**83.7%**		
	Jan - Mar 13	8,500	8,278	222	7	2.6%	0.1%	85,328	69,325	81.2%		73,430
Southwest	**Year 2010**	**12,104**	**11,116**	**988**	**459**	**8.2%**	**3.8%**	**158,415**	**125,601**	**79.3%**	**88,191**	**34,901**
	Year 2011	**15,658**	**14,965**	**693**	**178**	**4.4%**	**1.1%**	**194,048**	**157,040**	**80.9%**	**103,974**	**45,392**
	Jan - Mar 12	3,991	3,969	22	98	0.6%	2.5%	49,298	38,116	77.3%	25,561	46,227
	Apr - Jun 12	4,616	4,156	460	228	10.0%	4.9%	53,623	43,783	81.6%	28,859	46,128
	Jul - Sep 12	4,309	4,258	51	16	1.2%	0.4%	53,237	43,713	82.1%	28,319	46,048
	Oct - Dec 12	4,173	4,082	91	78	2.2%	1.9%	50,199	39,944	79.6%	26,607	45,861
	Year 2012	**17,088**	**16,465**	**623**	**421**	**3.6%**	**2.5%**	**206,211**	**165,555**	**80.3%**	**109,346**	**45,861**
	Jan - Mar 13	4,084	4,014	70	59	1.7%	1.4%	49,568	38,231	77.1%	25,203	45,791
United/Continental	**Year 2010**	**34,013**	**32,195**	**1,818**	**854**	**5.3%**	**2.5%**	**407,304**	**338,824**	**83.2%**	**145,550**	**81,500**
	Year 2011	**37,110**	**35,288**	**1,822**	**840**	**4.9%**	**2.3%**	**406,393**	**333,977**	**82.2%**	**141,799**	**81,600**
	Jan - Mar 12	8,602	8,873	-271	-448	-3.2%	-5.2%	97,112	75,809	78.1%	32,527	83,700
	Apr - Jun 12	9,939	9,364	575	339	5.8%	3.4%	103,986	87,692	84.3%	37,071	84,500
	Jul - Sep 12	9,909	9,709	200	6	2.0%	0.1%	105,786	90,155	85.2%	37,588	85,400
	Oct - Dec 12	8,702	9,167	-465	-620	-5.3%	-7.1%	93,606	77,031	82.3%	33,255	84,500
(including special charges)	**Year 2012**	**37,152**	**37,113**	**39**	**-723**	**0.1%**	**-1.9%**	**400,490**	**330,687**	**82.6%**	**140,441**	**84,600**
	Jan - Mar 13	8,721	8,985	-264	-417	-3.0%	-4.8%	92,329	74,903	81.1%	32,355	84,300
US Airways Group	**Year 2010**	**11,908**	**11,127**	**781**	**502**	**6.6%**	**4.2%**	**138,107**	**111,996**	**81.1%**	**79,560**	**30,871**
	Year 2011	**13,055**	**12,629**	**426**	**71**	**3.3%**	**0.5%**	**139,483**	**114,777**	**82.3%**	**80,572**	**31,548**
	Jan - Mar 12	3,266	3,207	59	48	1.8%	1.5%	34,032	26,970	79.2%	19,822	31,186
	Apr - Jun 12	3,754	3,350	404	306	10.8%	8.2%	37,072	30,908	83.4%	21,206	31,467
	Jul - Sep 12	3,533	3,265	268	245	7.6%	6.9%	37,342	31,719	84.9%	21,065	30,845
	Oct - Dec 12	3,278	3,153	125	37	3.8%	1.1%	33,856	28,390	83.9%	20,453	31,236
	Year 2012	**13,831**	**12,975**	**856**	**637**	**6.2%**	**4.6%**	**143,302**	**117,991**	**82.3%**	**82,546**	**31,236**
	Jan - Mar 13	3,380	3,277	103	44	3.0%	1.3%	34,466	18,145	81.7%	20,160	32,138
JetBlue	**Year 2010**	**3,779**	**3,446**	**333**	**97**	**8.8%**	**2.6%**	**55,914**	**45,509**	**81.4%**	**24,254**	**11,121**
	Year 2011	**4,504**	**4,182**	**322**	**86**	**7.1%**	**1.9%**	**59,917**	**49,402**	**82.5%**	**26,370**	**11,733**
	Jan - Mar 12	1,203	1,114	89	30	7.4%	2.5%	15,346	12,726	82.9%	6,853	11,965
	Apr - Jun 12	1,277	1,147	130	52	10.2%	4.1%	16,030	13,674	85.3%	7,338	12,308
	Jul - Sep 12	1,308	1,195	113	45	8.6%	3.4%	17,226	14,604	84.8%	7,747	11,797
	Oct - Dec 12	1,194	1,150	44	1	3.7%	0.1%	15,890	13,008	81.9%	7,018	12,070
	Year 2012	**4,982**	**4,606**	**376**	**209**	**7.5%**	**4.2%**	**64,493**	**54,013**	**83.8%**	**28,956**	**12,070**
	Jan - Mar 13	1,299	1,240	59	14	4.5%	1.1%	16,318	13,689	83.9%	7,300	12,385

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 December 31st.

		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.
ANA	Year 2007/08	13,063	12,322	740	563	5.7%	4.3%	90,936	61,219	67.3%	50,384	
YE 31/03	Year 2008/09	13,925	13,849	75	-42	0.5%	-0.3%	87,127	56,957	65.4%	47,185	
	Year 2009/10	13,238	13,831	-582	-614	-4.4%	-4.6%	83,827	55,617	66.3%	44,560	
	Year 2010/11	15,889	15,093	796	269	5.0%	1.7%	85,562	59,458	69.5%	45,748	33,000
	Year 2011/12	16,008	14,887	1,121	347	7.0%	2.2%	91,162	59,940	65.8%	44,903	
	Year 2012/13	17,363	16,146	1,217	503	7.0%	2.9%	96,456	64,879	67.3%	47,366	33,000
Cathay Pacific	Year 2008	11,119	12,138	-1,018	-1,070	-9.2%	-9.6%	115,478	90,975	78.8%	24,959	18,718
YE 31/12	Year 2009	8,640	7,901	740	627	8.6%	7.3%	111,167	96,382	86.7%	24,558	18,511
	Year 2010	11,522	10,099	1,813	1,790	15.7%	15.5%	115,748	96,548	84.0%	26,796	21,592
	Year 2011	12,635	11,929	706	706	5.6%	5.6%	126,340	101,535	79.3%	27,581	
	Year 2012	12,810	12,579	230	118	1.8%	0.9%	129,595	103,837	80.1%	28,961	20,749
JAL	Year 2005/06	19,346	19,582	-236	-416	-1.2%	-2.2%	148,591	100,345	67.5%	58,040	53,010
YE 31/03	Year 2006/07	19,723	19,527	196	-139	1.0%	-0.7%	139,851	95,786	68.5%	57,510	
	Year 2007/08	19,583	18,793	790	148	4.0%	0.8%	134,214	92,173	68.7%	55,273	
	Year 2008/09	19,512	20,020	-508	-632	-2.6%	-3.2%	128,744	83,487	64.8%	52,858	
	Year 2010/11	16,018	13,802	2,216		13.8%		86,690	59,740	68.9%	34,795	
	Year 2011/12	14,166	12,117	2,049	2,194	14.5%	15.5%	71,202	48,217	67.7%	25,441	32,000
Korean Air	Year 2007	9,496	8,809	687	12	7.2%	0.1%	76,181	55,354	72.7%	22,830	16,825
YE 31/12	Year 2008	9,498	9,590	-92	-1,806	-1.0%	-19.0%	77,139	55,054	71.4%	21,960	18,600
	Year 2009	7,421	7,316	105	-49	1.4%	-0.7%	80,139	55,138	68.8%	20,750	19,178
	Year 2010	10,313	8,116	120	421	1.2%	4.1%	79,457	60,553	76.2%	22,930	
	Year 2011	11,094	10,678	416	-89	3.7%	-0.8%	84,285	64,483	76.9%	22,934	
	Year 2012	11,455	11,165	290	230	2.5%	2.0%	88,304	68,818	77.9%		
Malaysian	Year 2007	4,464	4,208	256	248	5.7%	5.6%	56,104	40,096	71.5%	13,962	19,423
YE 31/12	Year2008	4,671	4,579	92	74	2.0%	1.6%	52,868	35,868	67.8%	12,630	19,094
	Year 2009	3,296	3,475	-179	140	-5.4%	4.3%	42,790	32,894	76.9%	11,950	19,147
	Year 2010	4,237	4,155	82	73	1.9%	1.7%	49,624	37,838	76.2%	13,110	
	Year 2011	4,549	5,300	-751	-825	-16.5%	-18.1%	52,998	39,731	75.0%	13,301	
	Year 2012	4,442	4,558	-117	-139	-2.6%	-3.1%	49,742	37,170	74.7%	13,389	
Qantas	Year 2007/08	14,515	13,283	1,232	869	8.5%	6.0%	127,019	102,466	80.7%	38,621	33,670
YE 30/6	Year 2008/09	10,855	10,733	152	92	1.4%	0.8%	124,595	99,176	79.6%	38,348	33,966
	Year 2009/10	12,150	11,926	223	102	1.8%	0.8%	124,717	100,727	80.8%	41,428	32,490
	Year 2010/11	14,842	14,200	642	249	4.3%	1.7%	133,281	106,759	80.1%	44,456	32,629
	Year 2011/12	16,232	16,410	-179	-252	-1.1%	-1.6%	139,423	111,692	80.1%	46,707	33,584
Singapore	Year 2006/07	9,555	8,688	866	1,403	9.1%	14.7%	112,544	89,149	79.2%	18,346	13,847
YE 31/03	Year 2007/08	10,831	9,390	1,441	1,449	13.3%	13.4%	113,919	91,485	80.3%	19,120	14,071
	Year 2008/09	11,135	10,506	629	798	5.6%	7.2%	117,789	90,128	76.5%	18,293	14,343
	Year 2009/10	8,908	8,864	44	196	0.5%	2.2%	105,674	82,882	78.4%	16,480	
	Year 2010/11	10,911	9,956	955	863	8.8%	7.9%	108,060	81,801	75.7%	16,647	
	Year 2011/12	9,664	9,519	145	270	1.5%	2.8%	113,410	87,824	77.4%	17,155	13,893
Air China	Year 2007	6,770	6,264	506	558	7.5%	8.2%	85,257	66,986	78.6%	34,830	19,334
YE 31/12	Year 2008	7,627	7,902	-275	-1,350	-3.6%	-17.7%	88,078	66,013	74.9%	34,250	19,972
	Year 2009	7,523	6,718	805	710	10.7%	9.4%	95,489	73,374	76.8%	39,840	23,506
	Year 2010	12,203	10,587	1,616	1,825	13.2%	15.0%	107,404	86,193	80.3%	46,420	
	Year 2011	15,260	14,289	971	1,095	6.4%	7.2%	113,987	93,185	81.8%	48,671	
China Southern	Year 2007	7,188	6,974	214	272	3.0%	3.8%	109,733	81,172	74.0%	56,910	45,474
YE 31/12	Year 2008	7,970	8,912	-942	-690	-11.8%	-8.7%	112,767	83,184	73.8%	58,240	46,209
	Year 2009	8,022	7,811	211	48	2.6%	0.6%	123,440	93,000	75.3%	66,280	50,412
	Year 2010	11,317	10,387	930	857	8.2%	7.6%	140,498	111,328	79.2%	76,460	
	Year 2011	14,017	13,342	675	944	4.8%	6.7%	151,074	122,342	81.0%	80,674	
China Eastern	Year 2007	5,608	5,603	5	32	0.1%	0.6%	77,713	57,180	73.6%	39,160	40,477
YE 31/12	Year 2008	6,018	8,192	-2,174	-2,201	-36.1%	-36.6%	75,919	53,754	70.8%	37,220	44,153
	Year 2009	5,896	5,629	267	25	4.5%	0.4%	84,422	60,918	72.2%	44,030	45,938
	Year 2010	11,089	10,248	841	734	7.6%	6.6%	119,451	93,153	78.0%	64,930	
	Year 2011	12,943	12,296	647	689	5.0%	5.3%	127,700	100,744	78.9%	68,681	57,096
Air Asia (Malaysia)	Year 2008	796	592	203	-142	25.5%	-17.9%	14,353	10,515	73.3%	9,183	4,593
YE 31/12	Year 2009	905	539	366	156	40.4%	17.3%	21,977	15,432	70.2%	14,253	
	Year 2010	1,245	887	358	333	28.8%	26.7%	24,362	18,499	75.9%	16,050	
	Year 2011	1,464	1,072	392	185	26.8%	12.6%	26,074	21,307	81.7%	17,986	
	Year 2012	1,613	1,239	374	606	23.2%	37.6%	28,379	22,731	80.1%	19,679	

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

	Intra-Europe			North Atlantic			Europe-Far East			Total long-haul			Total International		
	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 %
1993	137.8	79.8	57.9	145.1	102.0	70.3	96.3	68.1	70.7	319.1	223.7	70.1	479.7	318.0	66.3
1994	144.7	87.7	60.6	150.3	108.8	72.4	102.8	76.1	74.0	334.0	243.6	72.9	503.7	346.7	68.8
1995	154.8	94.9	61.3	154.1	117.6	76.3	111.1	81.1	73.0	362.6	269.5	74.3	532.8	373.7	70.1
1996	165.1	100.8	61.1	163.9	126.4	77.1	121.1	88.8	73.3	391.9	292.8	74.7	583.5	410.9	70.4
1997	174.8	110.9	63.4	176.5	138.2	78.3	130.4	96.9	74.3	419.0	320.5	76.5	621.9	450.2	72.4
1998	188.3	120.3	63.9	194.2	149.7	77.1	135.4	100.6	74.3	453.6	344.2	75.9	673.2	484.8	72.0
1999	200.0	124.9	62.5	218.9	166.5	76.1	134.5	103.1	76.7	492.3	371.0	75.4	727.2	519.5	71.4
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
2007	346.6	239.9	69.2	241.4	196.1	81.2	184.2	152.1	82.6	610.6	500.4	81.9	915.2	713.9	78.0
2008	354.8	241.5	68.1	244.8	199.2	81.4	191.1	153.8	80.5	634.7	512.4	80.7	955.7	735.0	76.9
2009	322.1	219.3	68.1	227.8	187.7	82.4	181.2	145.8	80.5	603.8	488.7	80.9	912.7	701.1	76.8
2010	332.3	232.6	70.0	224.2	188.1	83.9	180.2	150.0	83.2	604.1	500.4	82.8	922.7	752.8	78.7
2011	349.6	248.8	71.2	248.5	205.4	82.7	204.9	163.3	79.7	670.3	544.9	81.3	1,006.8	785.0	78.0
2012	348.9	254.6	73.0	249.4	211.6	84.8	211.8	172.2	81.3	686.9	569.3	82.9	1,024.2	817.2	79.8
Mar '13	26.9	19.8	73.6	19.1	16.4	85.6	17.6	14.5	82.9	56.2	47.0	83.6	82.3	66.7	81.0
Annual change	-1.6%	3.4%	3.5	1.1%	3.8%	2.2	1.4%	2.7%	1.1	1.2%	3.5%	1.9	0.8%	4.2%	2.7
Jan - Mar '13	74.9	51.9	69.4	52.4	41.9	80.0	49.7	40.6	81.7	159.3	130.0	81.6	232.3	181.3	78.0
Annual change	-1.5%	2.1%	2.5	-0.6%	2.2%	2.2	0.2%	2.5%	1.8	-0.2%	1.9%	1.7	-0.1%	2.6%	2.1

JET ORDERS

	Date	Buyer	Order	Delivery/other information
Boeing	14 May	Turkish A/L	40 x 737-MAX8, 10 x 737-MAX9, 20 x 737-800	
Airbus	30 May	Singapore A/L	30 x A350-900	plus 20 options
	22 May	Oman Air	3 x A330-300	

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

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