Aviation Strategy

Issue no. 291

Jan/Feb 2026

Iran War: The Gentler Scenario

THERE seem to be two basic scenarios for the development of the Iranian war, which alas depend on what is going on in President Trump's head.

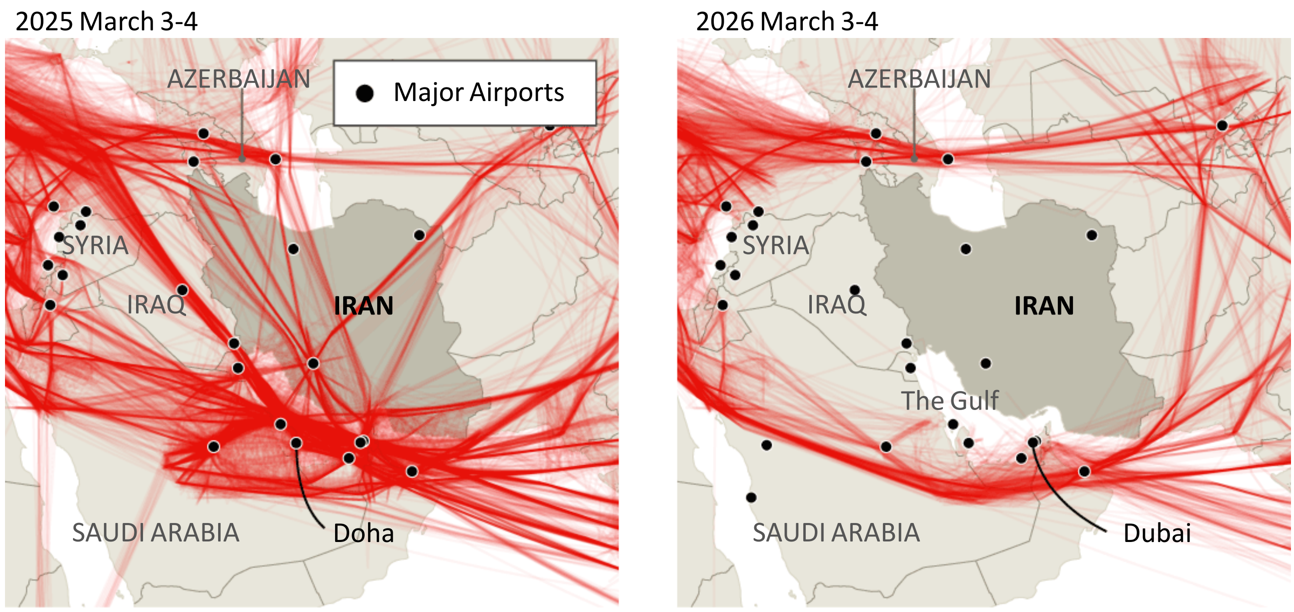
Escalation: US troops on the ground in Kharg Island, intensified bombing of Iran and retaliation by Iran and its proxies on Israel and the Gulf Arab states, complete closure of the Strait of Hormuz and pipeline attacks, while Houthis attack in the Red Sea. The consequences for the global economy and political stability are simply unknowable, and the implications for the airline industry seem irrelevant.

Deescalation: US declares victory and withdraws its forces, missile strikes diminish, but a new hard-line theocratic regime remains in Tehran threatening ship movements through the Strait. This seems marginally more probable, and we can add a couple of observations from past experience.

That experience incidentally dates back to 1980 when the author was first engaged on an analysis of the oil tanker business resulting from a closure of Hormuz during the Iran/Iraq war. Then, as now, the Strait was never fully closed, and some shipowners were willing to make the transit. The part-closure was mitigated using pipelines, a logistic that may have been under-

This issue includes

ROUTE DIVERSIONS



Source: The Economist

Aviation Strategy

ISSN 2041-4021 (Online)

This newsletter is published at least six times a year by Aviation Strategy Limited. Our editorial policy is to analyse and cover contemporary aviation issues and airline strategies in a clear, original and objective manner. Aviation Strategy does not shy away from critical analysis, and takes a global perspective — with balanced coverage of the European, American and Asian markets.

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6 Langside Avenue
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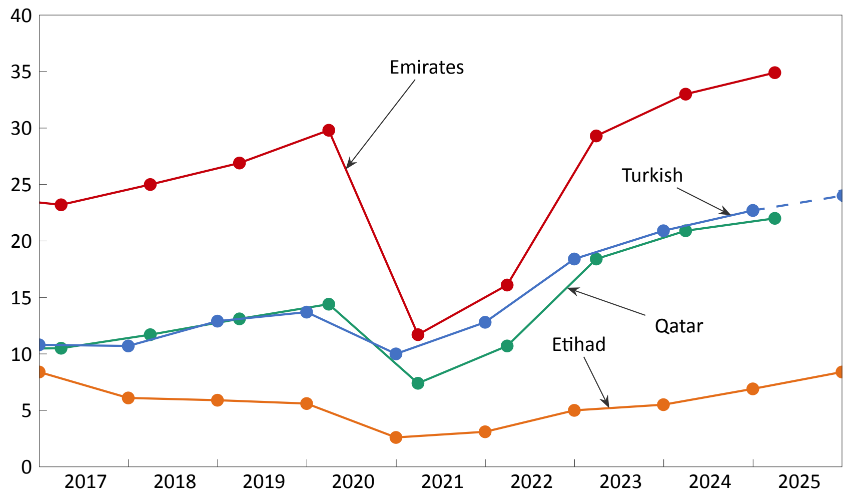
VAT No: GB 162 7100 38
ISSN 2041-4021 (Online)

Typeset in Calibri and Rockwell using XƎLaTeX

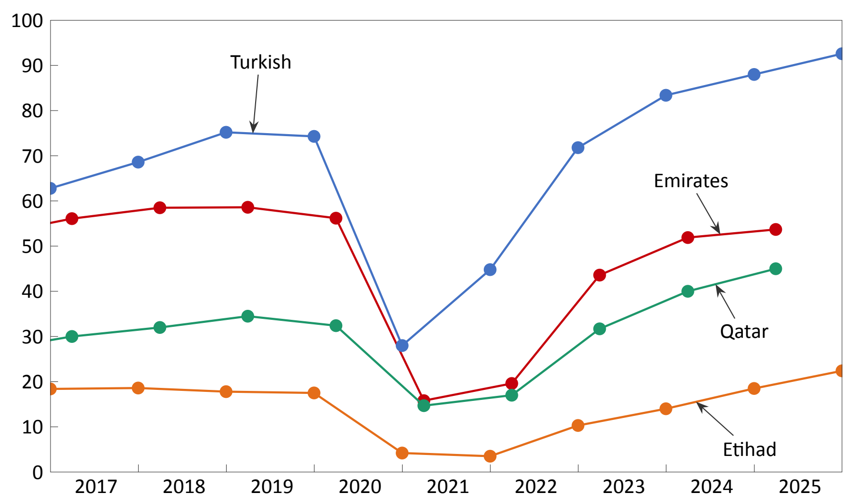
SUPERCONNECTORS' REVENUES ($bn)



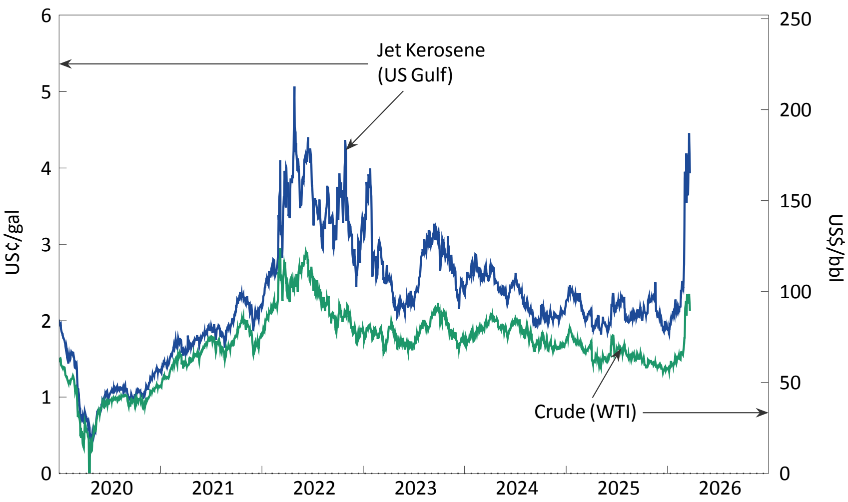
estimated this time. The Saudis can send most of their production from the northern oilfields through the Transarabian Pipeline to Yanbu on the Red Sea from where it can be carried to Asia directly in VLCCs or to Europe, via Suez or the parallel Sumed pipeline, in medium-size ships. From Kuwait there is a pipeline to Ceyhan in Turkey and from the UAE a pipeline to Fujairah in the Indian Ocean.

The huge spike in crude and jet kerosene prices is shown in the graph on the facing page with the differential between the two widening markedly as airlines scrambled for supplies. These are of course spot prices; the actual impact on individual airlines depends on their forward purchasing and hedging policies (generally well hedged for European airlines, not covered for US carriers).

SUPERCONNECTORS' PASSENGER TRAFFIC (millions)



JET KEROSENE PRICE DOUBLES



The spike is, however not as pronounced as that caused by the Russian invasion of Ukraine, and we would expect a relatively short period of high prices before the decline that always takes place once a crisis has passed.

The war banished civilian aircraft from around Iran, in effect shutting the mega-hubs of the Gulf — see maps on page 1. But by the end of March Emirates and Etihad had resumed some 60% of their schedules and Qatar 40%, albeit at load factors reported to be only around the 50% mark.

The graphs on the facing page are a reminder of the residence of the super-connectors which have recovered most of their traffic and all of their revenues since the pandemic. In that crisis it was speculated that the super-connector model would be fatally undermined as the global connecting systems would act as a global super-spreaders of viruses.

The systems may, nevertheless, concede some of their markets to THY and its super-capacity facilities at İstanbul. European and Asian network carriers expect to capture additional premium traffic on direct routes but they do not have the capacity to compete with the super-connectors on volume. Chinese airlines are building their own global connecting networks, and the Iran war might add to the advantages they already have by being able to fly through Russian airspace.

PIA: Will Privatisation Succeed?

PAKISTAN has had to go cap-in-hand to the International Monetary Fund for a bailout 24 times since joining it in 1950; and three times in the past six years (2019, 2023 and 2024) for a total of $11bn. One of the conditions in the 2023 agreement was the privatisation of the country's flag-carrier Pakistan International Airlines (PIA). After several aborted attempts this was finally achieved in December 2025, the Government selling a 75% stake for Rs135bn (US$482m) in a publicly televised auction in an Islamabad hotel to a consortium headed by the Arif Habib Corporation.

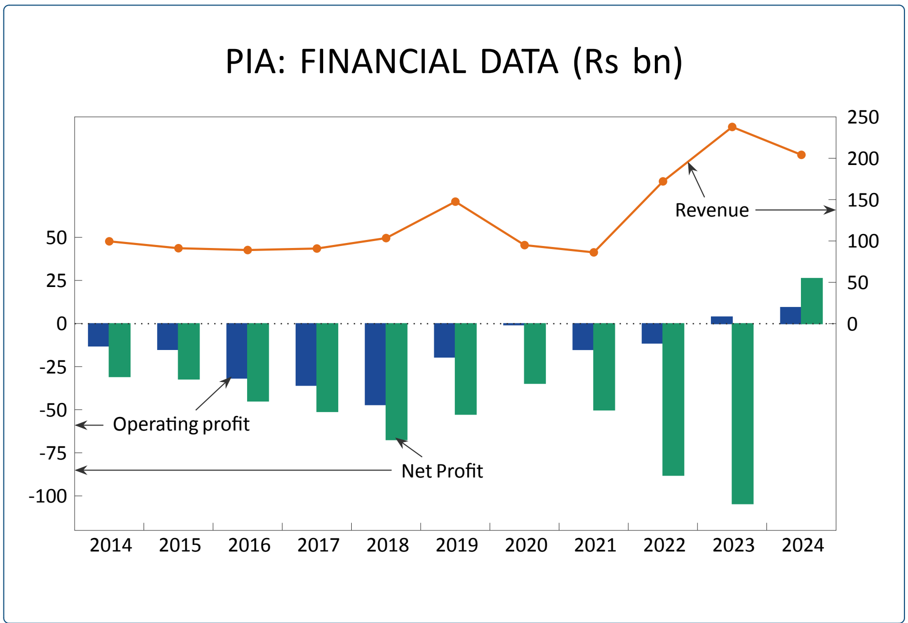
Founded in 1955 following the nationalisation of Orient Airways, PIA was once among Asia's most innovative carriers. It helped launch several aviation "firsts", including early jet operations in the region (a B707 leased from PanAm in 1960 and used on a route to London), the first airline to show films on international flights (in 1962 — TWA had pioneered the innovation on domestic US services the year before) and the establishment of training and engineering capabilities that supported other emerging airlines in Asia. It claimed the accolade of being "the second best airline in the world" in the 1960s.

For decades the airline served as a flagship enterprise for Pakistan's aviation ambitions. However, by the early 2000s the company had entered a prolonged period of decline characterised by chronic financial losses, political interference, significant overstaffing and, underinvestment in its fleet. It has been persistently loss-making at the operating and net level (see chart below) requiring constant funding top-ups from the State. Between 2014 and 2022 it achieved an annual average negative operating margin of -19%, and a -46% negative net margin. Between 2005 and 2023 it lost a total of Rs754bn (US$6.2bn) without having reported a positive result in any single year.

Over that period PIA allowed its natural dominance over the nation's air travel to fail. The domestic air travel market stagnated at at 6-7m passengers a year. New entrants arrived and PIA saw its domestic market share fall from 72% in 2010 to 29% in 2025 behind new entrant LCC Fly Jinnah (see graph on page 7). The International market in contrast had grown at a compound annual rate of over 7% between 2010 and 2019: and 2025 the 18m pax carried was 13% higher than the prepandemic peak in 2018. However, substantially, all that growth was on routes to the Arabian Peninsula to satisfy the Pakistani diaspora not only in the Gulf, but also, through the superconnecting hubs, that in the UK. PIA's international market share fell from 44% in 2010 to 16% in 2025 (see graph on page 7).

Operational inefficiencies were stark. At one point the airline employed over 450 staff per aircraft, far above international productivity benchmarks — Delta for example gets by with a staff-to-plane ratio of 100+, and low cost paragon Ryanair with around 20. The average number of employees has fallen by two-thirds since 2010 to 6,625 in 2024, but this is still equivalent to 210 staff per aircraft.

The company's problems worsened following the fatal crash of PIA Flight 8303 in May 2020, which exposed irregularities in pilot licensing oversight within Pakistan's aviation system. The aviation minister announced to Parliament in June of that year that 262 out of the 860 pilots in

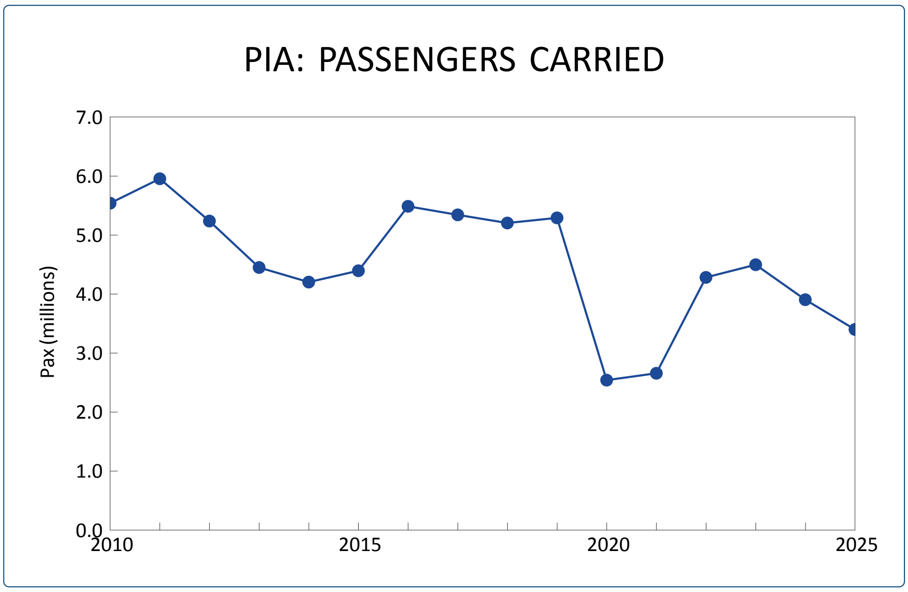


the country had bogus licences, alleging that they had paid someone else to take the exam for them. Regulatory authorities in Europe, the UK and USA subsequently banned the airline from operating to their markets. The EU ban was finally lifted in November 2024; the UK's in September 2025.

Restructuring before privatisation

The path to privatisation required significant financial and organisational restructuring. PIA had accumulated enormous liabilities over decades of government ownership. The 2023 accounts show total debt (including accrued interest, and pensions) of Rs570bn ($2bn) supported by a negative net worth of Rs(553)bn ($-2bn).

To make the airline attractive to investors, the Pakistani government transferred the airline into a subsidiary of a government owned PIA HoldCo, which retained all the long term debt and the "bad bits" of the former group, effectively recapitalising the airline prior to sale. The FY 2024 accounts showed net debt of Rs28.8bn ($103.5mn) and a net asset value of Rs3.6bn ($12.7mn). The airline even reported its first net profit in decades — all resulting from the write-back of deferred taxes.

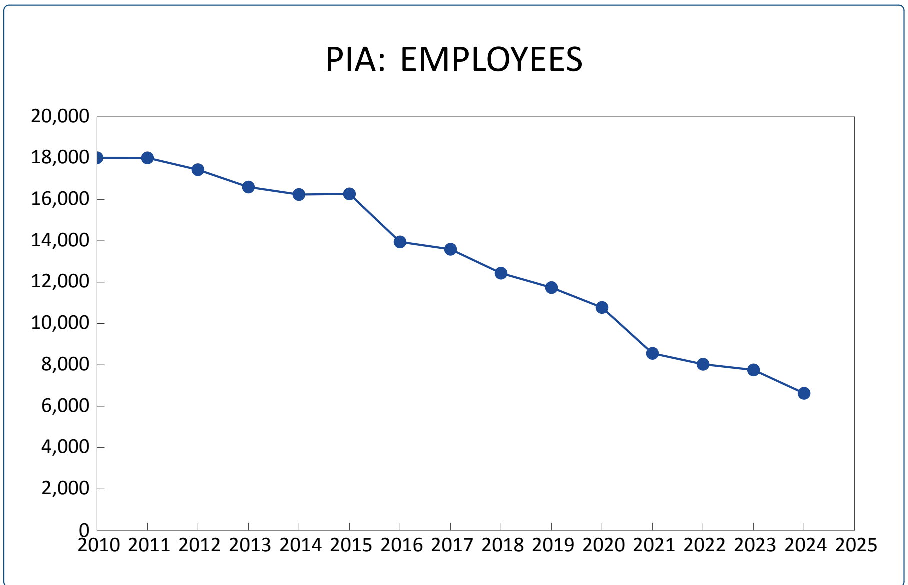


Structure of the deal

In December 2025, the Pakistani government sold a 75% majority stake in PIA to a consortium led by Arif Habib Corporation for Rs135bn. The majority of the funds will be used as a capital injection into the airline, with the government retaining Rs10bn of the cash. The first financial closing of the transaction is expected by the end of April. At that stage, the consortium will be required to pay about two-thirds of the bid amount. The investor group will also then indicate whether it intends to exercise the option to purchase the government's remaining 25% stake in PIA at a premium of 12%.

The consortium included companies from several sectors and include some unusual bedfellows:

- Arif Habib Corp is a major Pakistani holding company founded by Arif Habib, with a diversified portfolio in brokerage, investment, energy, and industry. A former head of the Karachi Stock Exchange he runs Pakistan's largest largest securities brokerage, investment banking, and research firm. He has also served (a decade ago) on the board of PIA;
- AKD Group Holdings Limited, founded by Aqeel Karim Dhedhi (who also started in stockbroking), is also a diversified conglomerate operating securities brokerage, investment banking, venture capital, private equity, telecoms, real estate development, oil & gas exploration and asset management;
- Fertiliser company Fatima Fertilizer, based in Lahore (a joint venture between Arif Habib Corp and Fatima



Corp);

✈ Private school network City Schools, and

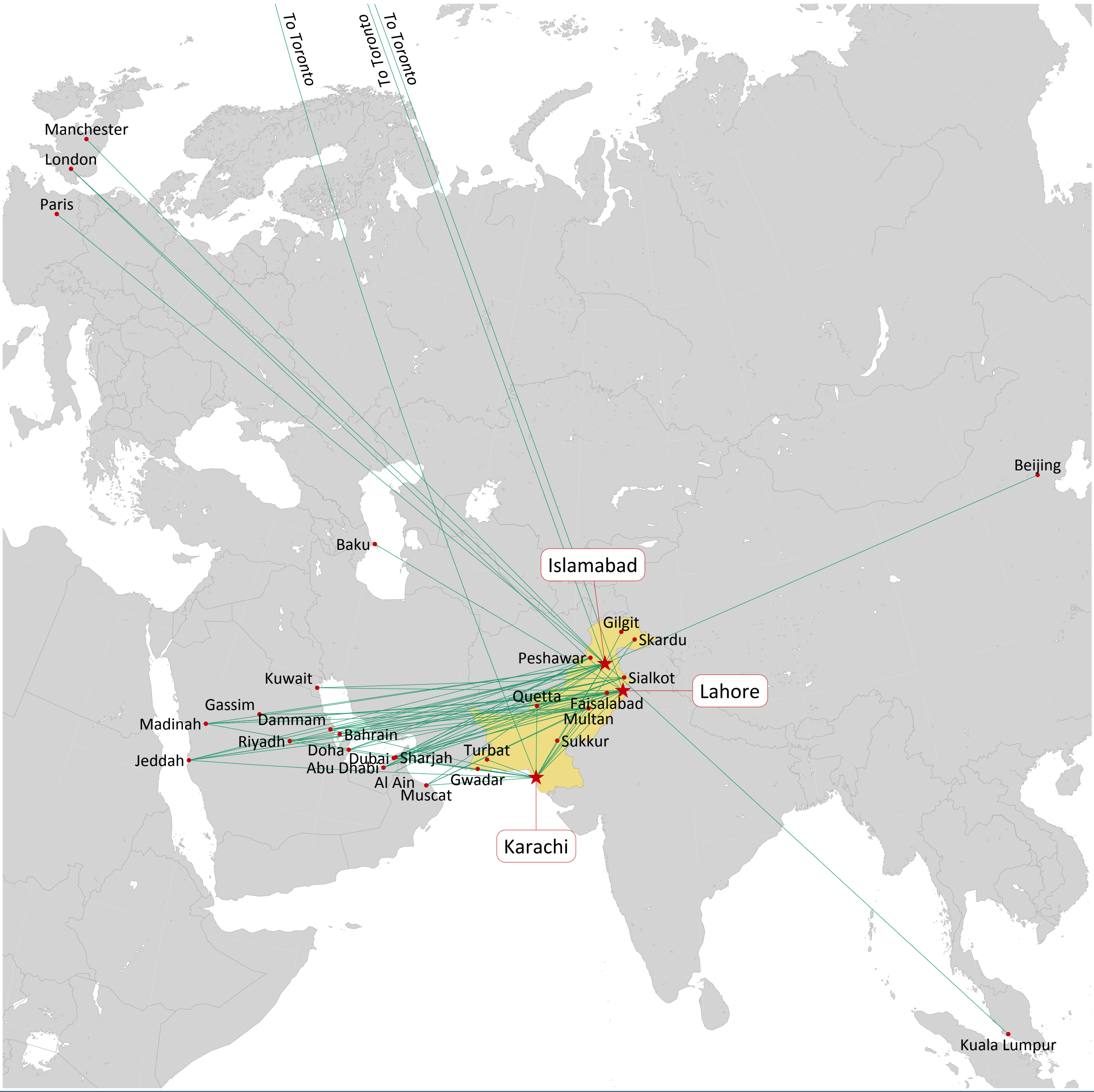
✈ Real estate firm Lake City Holdings Limited.

Another (military-backed) fertiliser conglomerate, and Pakistan's premier producer of urea, the Rawalpindi-based Fauji Fertilizer Company joined the consortium after the bid was accepted. (It's also into wind energy, food processing and banking).

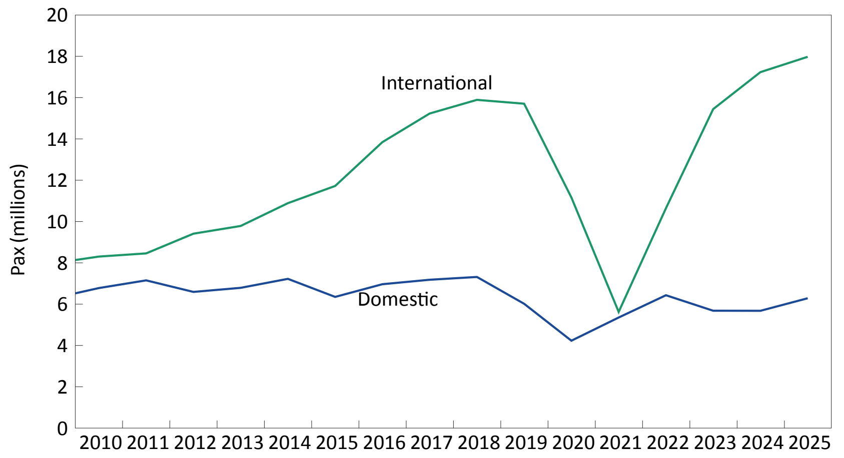
A successful privatisation serves multiple objectives for Pakistan's government: reduce fiscal burden of state-owned enterprises; satisfy reform commitments linked to IMF financing programmes; improve efficiency and service quality in the aviation sector.

From the investor perspective, the acquisition may represent a turnaround opportunity in a large

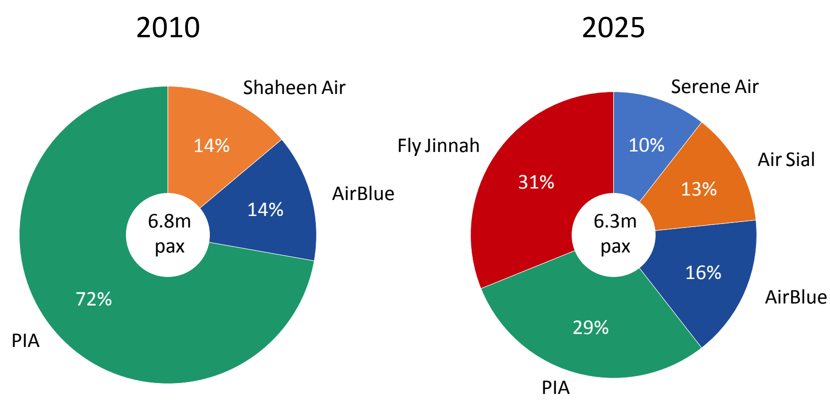
PIA: ROUTE NETWORK



PAKISTAN: AIR PASSENGERS



PAKISTAN: DOMESTIC MARKET SHARES



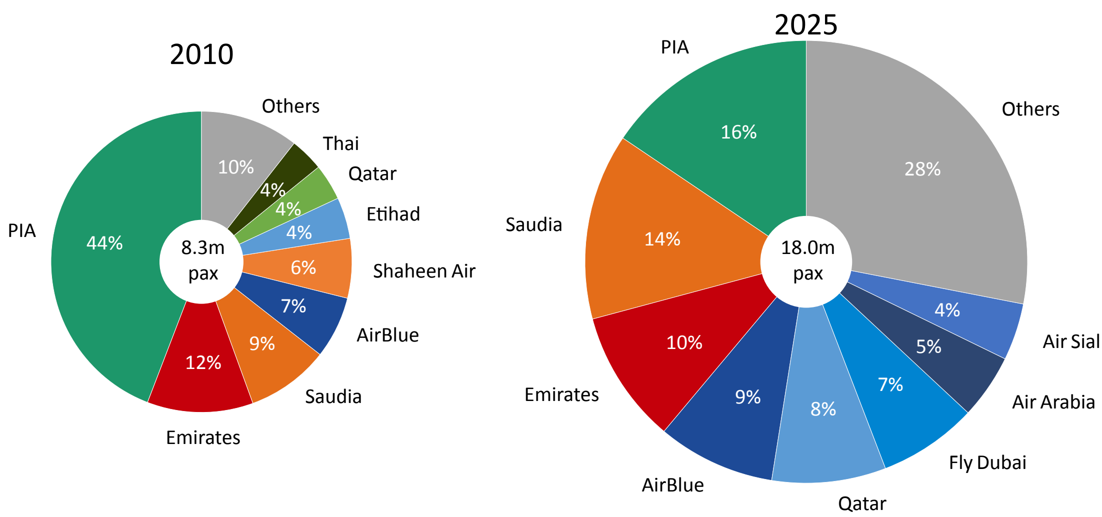
and underserved aviation market. Pakistan's population of more than 240 million, combined with strong labour migration flows to the Middle East and Europe, provides substantial demand for international air travel.

Quoted in a *Bloomberg* article, Aqeel Karim Dhedhi said: "There are no direct flights from Pakistan and currently passengers are taking transit flights from airlines based in Qatar, Abu Dhabi, Saudi Arabia and Turkey. We will take our business back from these airlines. Passengers who can have a direct flight would never want to take a transit flight."

Plans?

The airline currently has 32 aircraft, a mixture of 17 A320s, 12 777s and one ATR42. Of these 14 are currently in store (see table on the following page). The fleet is pretty ancient, with an average age of 18 years. And the fleet size is small relative to the airline's historic network footprint. Boeing's backlog shows it still has outstanding orders for five 777-300ERs, from an order the airline placed in 2012. But the 777-300 production line effectively closed following the

PAKISTAN INTERNATIONAL MARKET SHARES



PIA: FLEET

	In service	Parked	Total	Avg age	On order
A320ceo	11	6	17	*16.8*	
777-200	4	4	8	*21.0*	
777-300ER	2	2	4	*18.3*	5
ATr42	1	2	3	*19.4*	
Total	**18**	**14**	**32**	***18.0***	**5**

delivery of the last of the type to Ethiopian in late 2024, so these orders may be somewhat theoretical.

The airline currently serves 33 destinations in 13 countries (see map on page 6). (At its peak in 1999 it served 83 destinations in 39 countries). Apart from the route to Beijing, these mostly reflect the pressure of demand from the 10m strong Pakistani diaspora — London, Manchester, Toronto and the Gulf States. (Because of on-going diplomatic tensions there are no routes to India — both India and Pakistan having closed their airspace to the other's airlines). Somewhat surprisingly missing are destinations in the US — up to 2017 the airline tagged a route onto New York from Manchester — but PIA is waiting for a result of an audit by the FAA to allow it to resume services. Two other Islamic nations appear on its current route network: Azerbaijan and Malaysia.

The success of privatisation will depend largely on the new owners' ability to implement a coherent strategic transformation. Three priorities are likely to dominate the airline's agenda. Fleet renewal may represent the most urgent strategic requirement. The consortium apparently plans to bring back six of the aircraft in storage by the end of 2026 to give an operating fleet of 24 units, build that to 38 by end 2027 and aims to have 60 operational in five years time. The agreement requires it to plan for 65 units in the longer term.

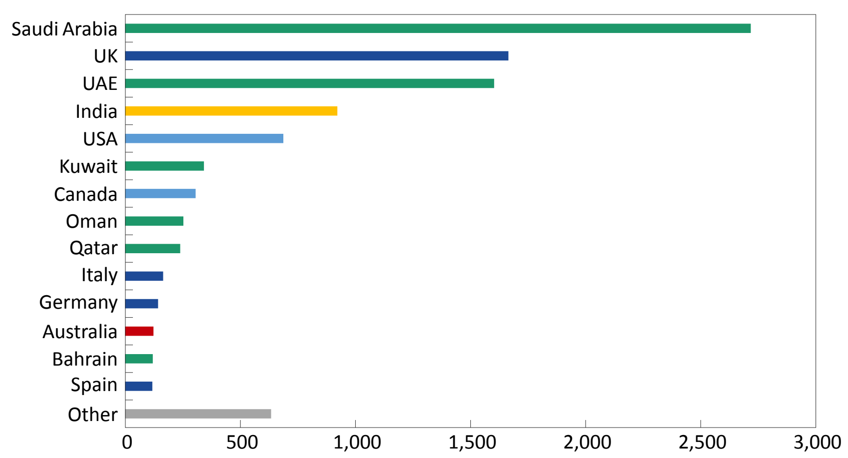
Dhedhi suggests that the consortium is in discussion with Airbus and Boeing for future orders, but since there is currently little availability for new aircraft before the early 2030s, PIA would get their help to secure interim second hand leases.

Historically, labour productivity has been one of PIA's greatest weaknesses. State ownership led to politically motivated hiring, resulting in an employee-to-aircraft ratio far above industry norms. Privatisation may create the opportunity for voluntary retirement programmes, productivity reforms, and new performance-based employment structures. However, labour restructuring remains politically sensitive, and the privatisation agreement reportedly requires the new owners to retain existing employees for at least one year. This suggests workforce reform will be gradual rather than immediate.

Perhaps the most difficult challenge facing PIA is reputational recovery. Over the past decade the airline's brand has suffered from safety controversies, operational disruptions, and dire financial instability. Rebuilding customer trust will require sustained improvements in onboard product, punctuality, service quality and may include investment in digital distribution and a loyalty programme. Brand repositioning may also involve relaunching PIA as a modern national carrier emphasising reliability and hospitality.

The consortium has suggested that it aims to float the airline on the Karachi stock exchange through an IPO later in 2026.

PAKISTANI DIASPORA ('000s)



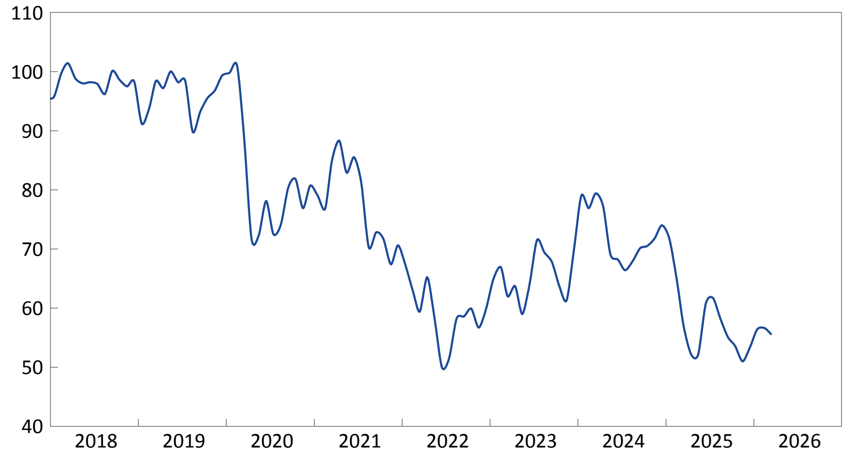
US Majors: Reasonable Financials but Consumers Doubtful

For the big three US network airlines, 2025 was a year that did not quite live up to optimistic expectations. Consumer sentiment showed a marked decline on the inauguration of the new administration, and overall market demand was affected by the Trump tariff roller-coaster. A fatal American Eagle crash into the Potomac in January, and a Delta Connection crash on arrival in Toronto in February might not have helped.

Then there was a six-week government shut-down from the beginning of October with severe knock-on effects for the industry as air traffic controllers and TSA security worked without pay (or didn't, and called in sick) leading to widespread flight disruptions and an FAA-mandated 10% cut to schedules at major airports. For the year as a whole, total domestic passenger numbers fell by 1.3% year on year — unusual in the absence of a technical recession. US GDP grew by 2.1% over the year, but the domestic passenger revenues of the top three carriers grew by a mere 1%.

On international services, Form 41 data shows the US airline industry as a whole saw minimal growth of 0.2% in the total number of passengers. The top three managed a 2% increase between them (offsetting the steep declines at LCCs Frontier and Spirit of -17% and -22% respectively). The weakness in inbound tourist arrivals noted by the ITA may have had a little to do with it (see next article on page 14), although for the top three over 80% of their international tickets have a US point of sale.

US CONSUMER SENTIMENT

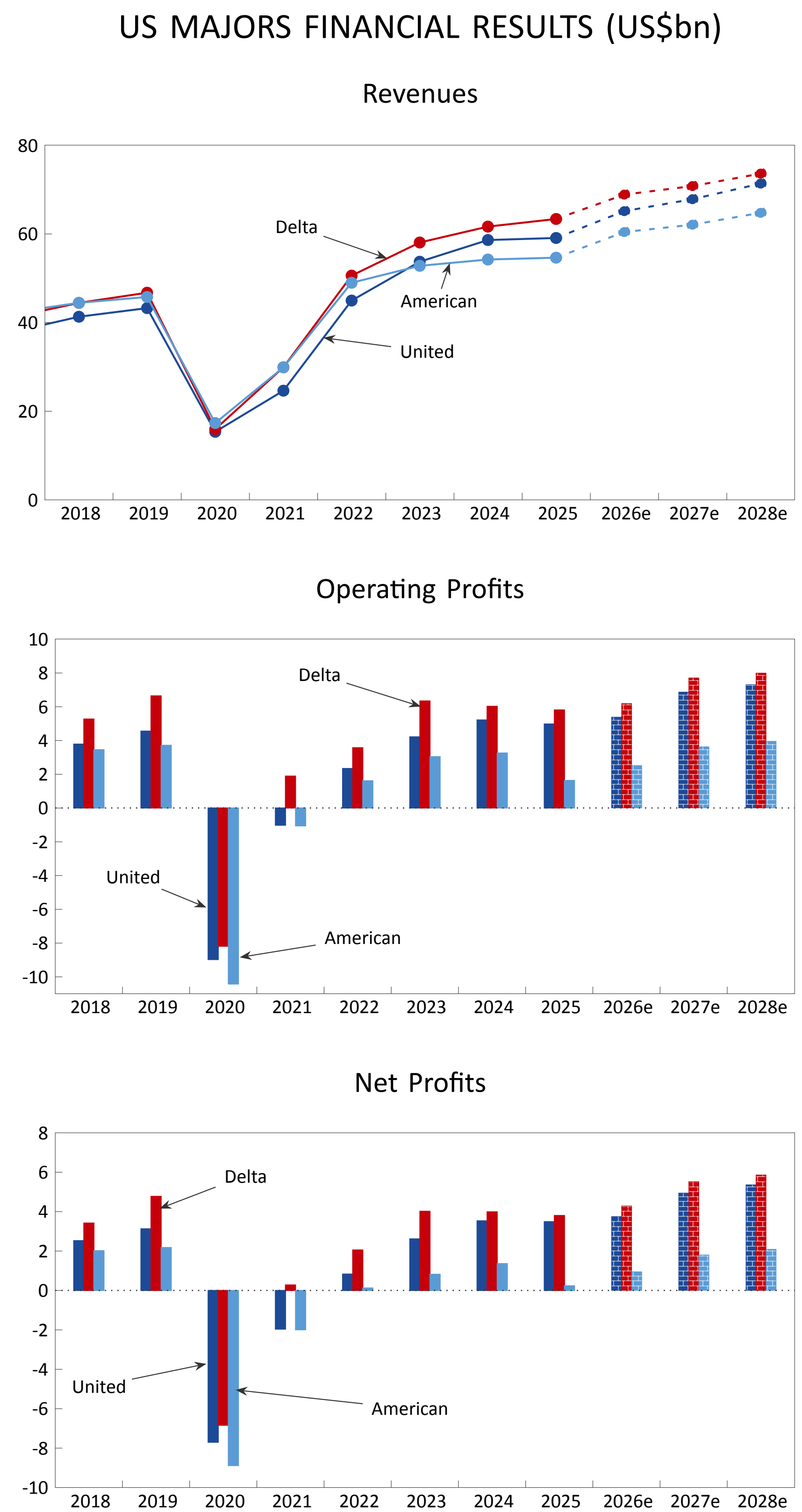


Source: University of Michigan

US MAJORS: KPI BY REGION 2025

$m	Domestic	Atlantic	Latin America	Pacific	Total
American					
Pax Revenues	35,201	6,583	6,440	1,415	49,639
Pct of total	71%	13%	13%	3%	
Y-on-Y %ch	-0.4%	1.5%	-1.8%	13.7%	0.0%
Unit Revenue∗	-2.90%	0.80%	-2.80%	-0.10%	-2.00%
Demand†	0.30%	3.10%	-1.20%	13.60%	0.60%
Delta					
Pax Revenues	35,731	9,270	3,980	2,787	51,768
Pct of total	69%	18%	8%	5%	
Y-on-Y %ch	1.4%	1.5%	-0.4%	9.7%	1.7%
Unit Revenue	-2.0%	-2.0%	-1.0%	0.0%	-2.0%
Demand	0.0%	2.0%	0.0%	16.0%	1.0%
United					
Pax Revenues	31,487	10,872	5,077	6,003	53,439
Pct of total	59%	20%	10%	11%	
Y-on-Y %ch	2.0%	4.9%	1.4%	7.5%	3.1%
Unit Revenue	-4.1%	-1.6%	-5.2%	3.0%	-2.9%
Demand	3.9%	5.7%	4.8%	9.4%	5.1%

Notes: ∗ (P)RASM y-y %ch; † RPM y-y %ch



Source: company filings. Forecast: Bernstein

Delta again produced the best margins, the cleanest strategic narrative and the most convincing balance between growth and returns. United extended its multi-year run of outperformance, showing that its bet on network breadth, premium segmentation and operational reliability is producing structurally higher earnings power than sceptics once believed. American, by contrast, remained (just) profitable but still looked like the least strategically coherent of the three: more dependent on the comestic market, less margin-rich than Delta, less momentum-driven than United, and still working through the consequences of a revenue strategy that had to be reset.

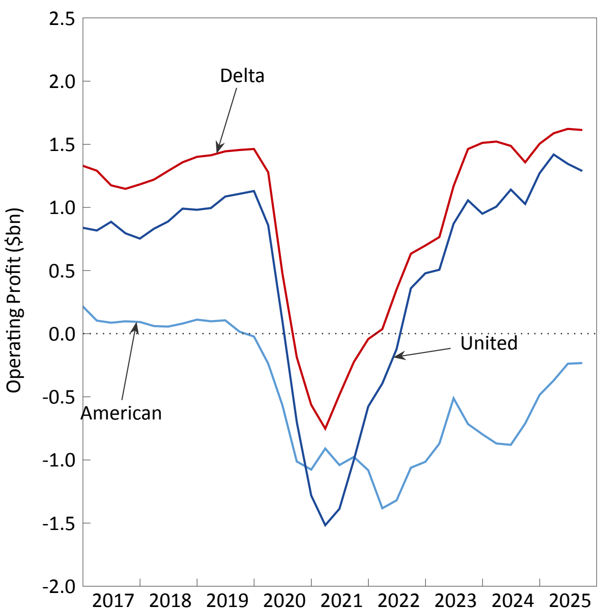
The headline numbers tell the story. Delta reported adjusted operating income of $5.8bn (-3.5% y/y), a 9.2% margin (-60bp) on revenues of $63.3bn (+2.8%). It achieved net profits of $3.5bn, a gnats whisker below those reported for 2024. Management framed the year as "challenging", but one of "durability", with record revenue and a double-digit return on invested capital.

United's 2025 results were also reasonable. It reported full-year revenue of $59.1bn (+0.8%), adjusted operating profits of $5.0bn (-4.5%) giving an operating margin of 8.4% (-50bp) and net profits of $3.5bn, just 1.2% down on the prior year. Management stressed that the carrier had exceeded expectations and was seeing the benefits of "brand-loyal" customer growth, a more reliable operation and stronger revenue diversification.

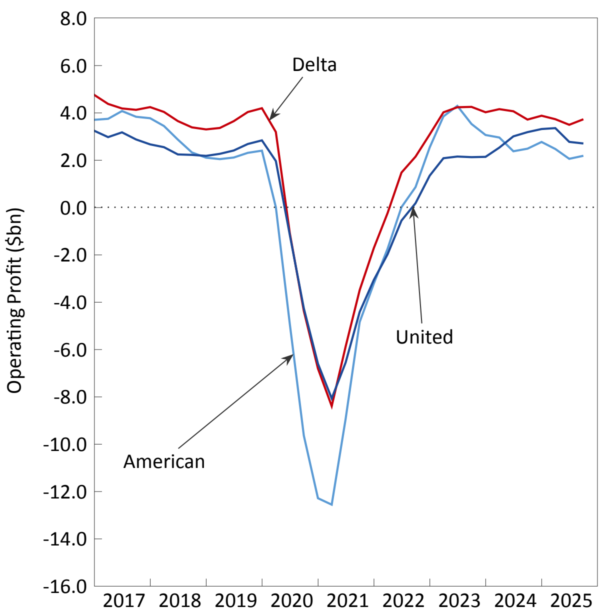
American also saw revenues rise by 0.8% to $54.6bn. Operating profits however were 50% lower than in 2024 at $1.6bn, giving a margin of 3.0% compared with 6.0% in the prior

US MAJORS: RESULTS BY REGION

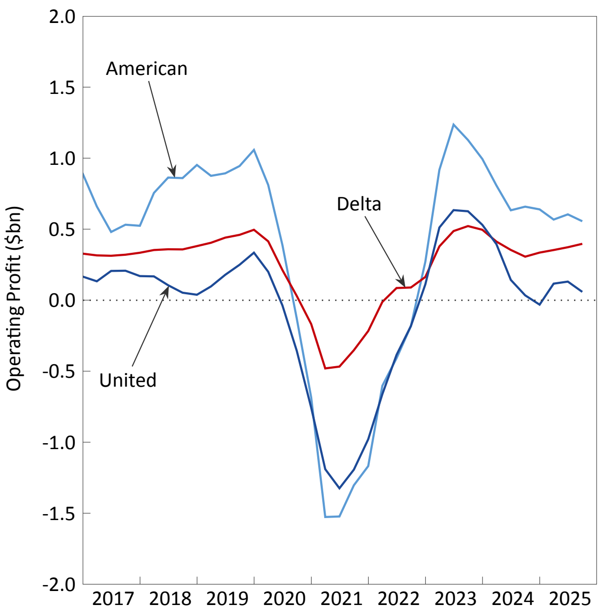
Atlantic



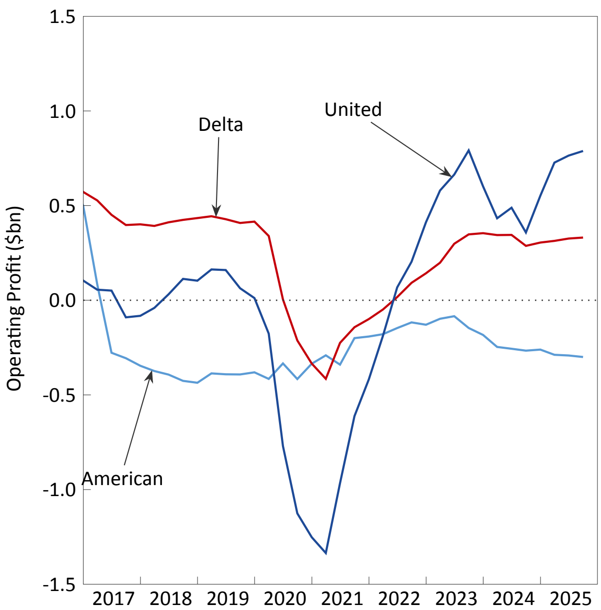
Domestic



LatAm



Pacific



Source: DoT Form 41. Latest twelve months trailing.

year. Net profits were effectively a break-even at $237m (-83%). American remains the most indebted of the three but paid off $2.1bn of its debt pile ending the year leaving it with gross debt of $36.5bn (and net debt of $30.7bn) and a ratio of net debt to EBITDA of 11x. On publication of the results, CEO Robert Isom emphasised that American "is positioned for significant upside in 2026 and beyond". Strategically, the carrier is still heavily dependant on domestic and short-haul demand without the same valuation of product and network advantages that investors now readily assign to Delta and United.

Optimism reigned in each carrier's outlook for 2026 highlighting very strong booking trends at the start of the year. Delta guided to full-year margin expansion and earnings growth of around 20%. United equally pointed to a 2026 increase of over 20% in net income. American expected that it could return to the 2.5% net operating margin it achieved in 2024.

Product segmentation and "Premiumization"

In the last decade the top three have shifted from operating simple cabin classes (coach and first) to a segmented "branded fares" product. Delta kicked off in 2012 with its basic economy fare to try to compete head on with the new generation of low cost carriers. (It was originally launched as a "Spirit-match" fare). It came with the same restrictions as the LCC's unbundled offering: no frills, no seat assignment, no baggage allowance. American and United followed suit in 2017, at the same time that Delta expanded its offering to four/five tiers of branded fares: First class (or Business on international long haul), premium economy, featuring wider seats, higher seat pitch and enhanced service, Comfort+ — seats in the main cabin with 3-4 inches more leg-room — as well the run-of-the-mill main cabin and Basic Economy for the bums on the seats at the back of the bus.

This development has accelerated in the recovery from the pandemic and has been particularly beneficial to Delta and United. In the fourth quarter of 2025 revenues from Delta's branded tickets exceeded main cabin income (the former up by 7%, the latter down by 7%).

United has adopted the strategy whole-heartedly and its premium revenues were up by 11% for the full year compared with a 5% growth in basic economy. CEO Scott Kirby insists: "we've proven that air travel is not a commodity". The airline is significantly increasing its premium offering aiming for the highest premium seat count of any US widebody aircraft. It is rolling out what it calls its "elevated" interior on the 20 787-9s being delivered in 2026: 64 lie-flat Polaris business suites (up from 28) designed with "privacy doors" (that currently have to be locked open until they recieve certification) including eight new over-sized "Polaris Studios" in the front row of the business cabins; 35 "Premium Plus" seats (up from 21) with 38 inch pitch, and 123 seats in economy (down from 158) including 33 "extra legroom Economy Plus seats (34 inches compared with 31 inch pitch).

American, with a relatively smaller intercontinental widebody network has been a bit late to the game. It is meanwhile retrofitting its new Flagship Business suites (with sliding privacy doors) to its 777 fleet. Along with an expanded premium economy cabin it see a 25% increase in premium seat offering. It is also installing the product on its new A321XLRs.

Loyalty pays

Hand in hand with this has been an increased focus on using the loyalty programs as a way of generating income. Rewards (miles) used to be provided depending on how far a passenger travelled. Increasingly they are are earned on the basis of how much the passenger spends, and how she spends. The loyalty model used to be that miles redeemed would be paid for by the airline by using the near zero marginal cost of an unsold seat. Now the funds are increasing provided by payments from banks in co-branded credit card deals with the airlines.

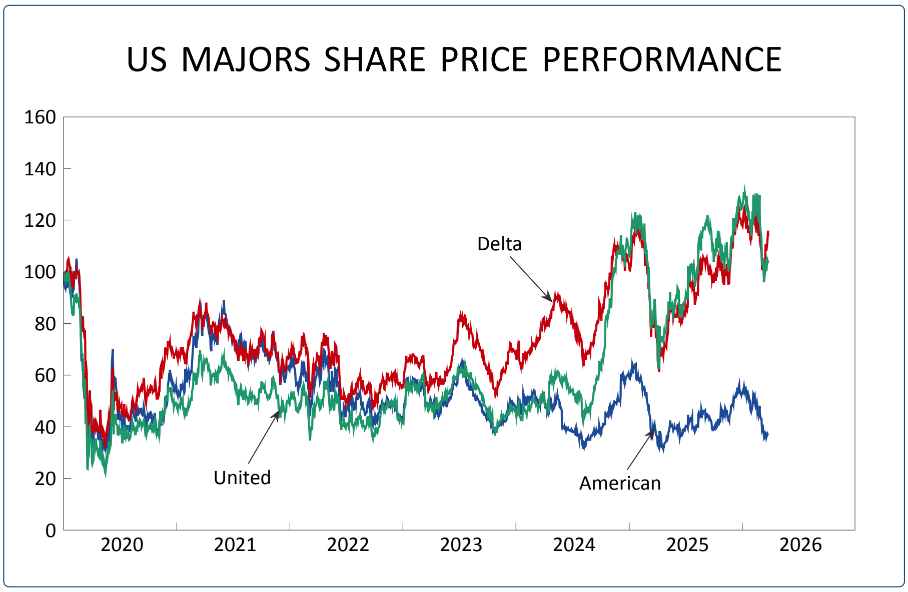
In 2025, Delta received $8.2bn in cash from American Express, 11% up on the prior year and accounting for 14% of adjusted revenues. United also recognised a healthy increase of 9% in royalty revenues. American is in the process of implementing a new deal with Citi. That cash is funded from the annual credit card fees as well as a proportion of the interchange fees the card companies charge merchants (and therefore the customer).

There is a Bill being considered in Washington to limit credit card interest rates. That, if enacted, may not noticeably affect the airline passengers who hold co-branded cards: those who can afford the high annual fees that give them lounge access are likely to be the "haves" and be able to pay off the balance each month; but it might reduce the availability of credit to the "have-nots". Of more concern for the industry is another Bill (under discussion for the past two years) that would put a limit on credit card interchange fees. If that were to be enacted, it could undermine the loyalty programmes' business models.

K-shaped economy

The development of the US industry in 2025 leads into a popular theme that the economy is K-shaped — upper-income earners and asset-owners thrive (upward stroke), while low- and middle-income households fall behind because of inflation and rising living costs (downward stroke). The major network carriers did well in 2025. The LCCs had a dire year (and Spirit collapsed again into bankruptcy). Those at the upper quartiles of income and wealth, boosted by buoyant stock market returns, are spending happily (premium leisure, more legroom, extra comfort), and those at the bottom of the wealth pyramid — the budget-conscious travellers — are finding it difficult to make ends meet and can't even afford a cheap ticket on a low cost carrier.

All three of the major network carriers expressed optimism for strong financial returns in 2026. That optimism may have been dented a little after Trump decided to go to war: jet fuel prices have doubled. The US carriers in general do not hedge their fuel costs (although Delta with its in-house fuel refinery can be said to hedge the crack-spread) and will bear the full force of the increase in costs.



But all three are reporting that the strength of demand appears more than sufficient to absorb the necessarily higher fares required to pay for fuel: both Delta and American upped their Q1 revenue forecasts. United — expecting a $4.6bn jump in fuel costs this year — said it was cutting some capacity on weak-performing flights but that recent fares booked were 15%-20% up on the year before. *Reuters* quoted Scott Kirby's continuing optimism. "At least as the environment sits today," he said, carriers could recover "100% of that increase in fuel price."

Yet, while demand may be strong, there is the added problem of a continuing partial government shutdown severely affecting airline passengers: TSA security agents are once again are working unpaid (or calling in sick) while Washington argues over the budget for the Department of Homeland Security.

US Tourism Downturn

THE USA did a good job at discouraging tourist visitors in 2025. Preliminary figures for December from the Washington-based International Trade Administration (ITA) show that the number of "overseas" visitors (ie all international visitors save those from Canada and Mexico) fell by 1.3% year on year giving a full year total of 34.3m, 2.5% below the prior year levels and 15% below the previous peak in 2019. The trend continues with another 4% decline in January 2026.

The ITA ironically relies on Statistics Canada and Mexico's INEGI respectively for the arrivals by air and land for the data from the countries bordering the US. The two normally account for 50% of visitors to the US. These numbers are not yet available for December or January. For the the eleven months to November total international visitor arrivals had declined by 5.5% from prior year levels.

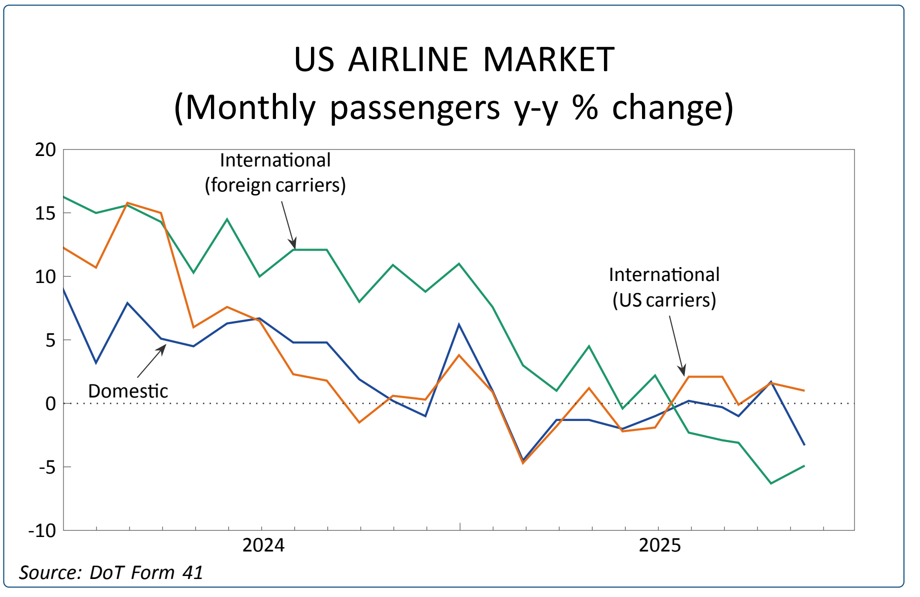
And 2025 was a year that, according to preliminary figures from the UN's World Tourism Organization, saw a global year-on-year increase in international tourist arrivals of 4% to 1.52bn — firmly exceeding 2019 levels for the first time since the pandemic. International tourist receipts it estimates grew by 5-6% in real terms to $1.9trn. North America, it noted, was one of the few regions that registered a decline.

We show the monthly progression by major regions in the charts on the next page.

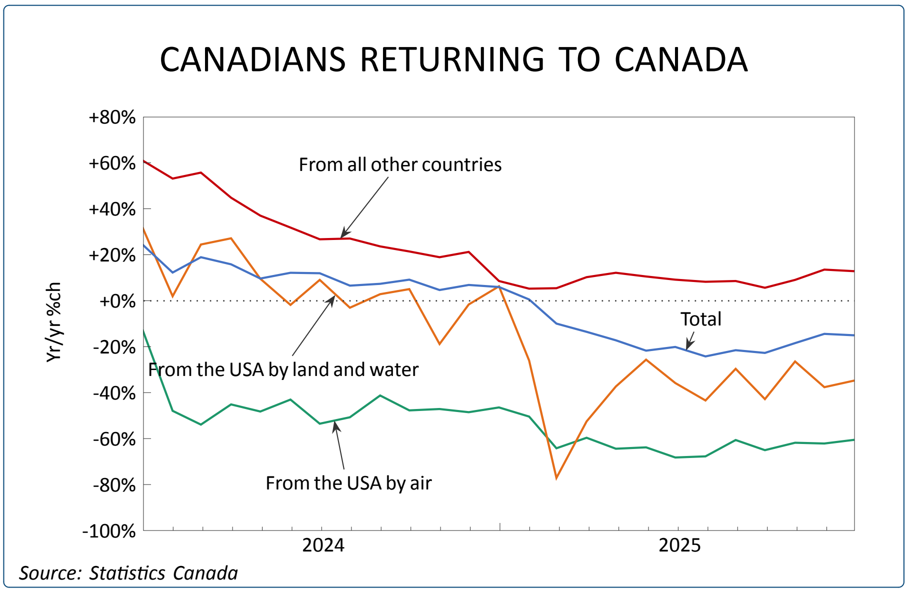
Mexico has held up reasonably well, but Canadians have reacted aggressively against the Trump Administration's tariffs and the suggestions of annexing a 51st state and voted with their feet. For most of 2025, Canadian visitors by surface transport have been 30-40% below prior year levels; by air some 15% down; and in total 25% below.

Figures from Statistics Canada (see chart below), while slightly at odds in detail with those from ITA, seem to confirm that Canadians have forsaken their neighbour to explore the Caribbean, Europe and Far East or decide (supported by discounts from the Canada Strong campaign) to vacation within Canada.

The numbers of visitors from Western Europe, the next largest



Source: DoT Form 41



Source: Statistics Canada

source, have also been weak down by 3.7% for the year as a whole. Those arriving from the UK and Italy have held up reasonably well, but those from Germany and France were well down by 11% and 7% respectively. The numbers of visitors from Denmark fell by 24%.

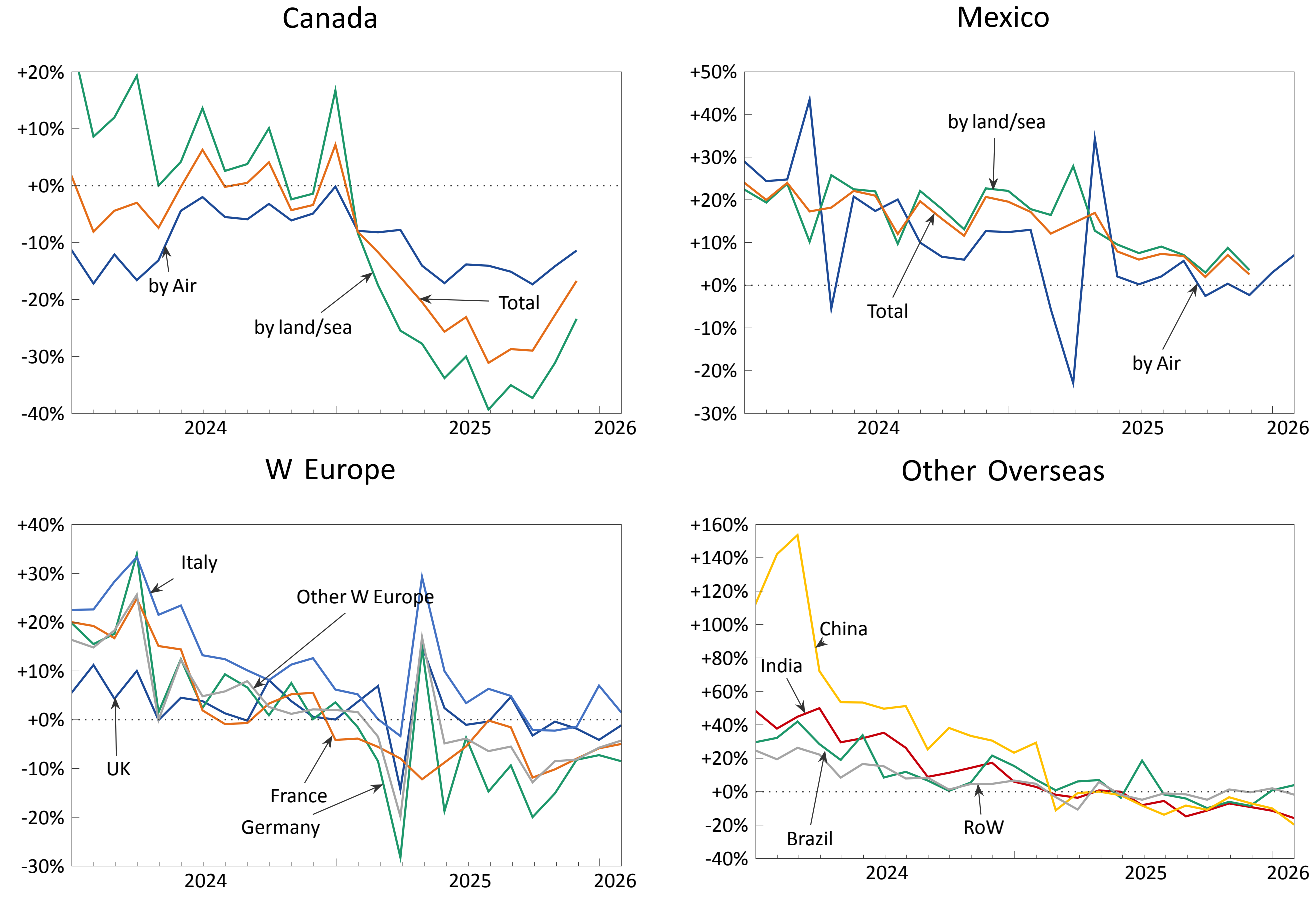
It is intriguing to tie this in with the data from the DoT's Form 41 on the preceding page. From mid-year 2025 there appears to have been an accelerating decline in the rate of growth of passengers carried by non US airlines on International routes. However, International passengers account for only 12% of the US airline market.

As exports go, tourism may not be a priority to the administration in Washington. But in 2024 it is said to have accounted for 7-9% of total exports of goods and services (and 22% of services exports).

The USA is the third largest tourist destination country in the world. And there should be enough over the next few years to encourage a resumption of growth in visitors. As the main host nations of the FIFA World Cup, it should be an automatic draw for hordes of fans (assuming the teams can get visas, and the stadiums can get the money to plan security). This year is also the 250th anniversary of the Declaration of Independence; and it's the 100th anniversary of the establishment of the iconic 2,448-mile Route 66 from Chicago to California. And then in 2028 there should be the summer Olympics in Los Angeles.

The WTO is expecting continued modest 3-4% growth in tourist arrivals in 2026. Overall 58% of its "Panel of Experts" foresee better or much better tourism results and only 11% expecting a worse outcome. But of the respondents to that survey in the Americas, only 37% appear optimistic, while 26% forecast a worse, and 2% a much worse environment.

USA: INBOUND TOURISTS BY ORIGIN
(year on year % ch)



Source: International Trade Administration.
Note: W Europe figures heavily affected by timing of Easter (March in 2024; April in 2025).

Air Canada: Flag-carrier of the 51st State, Not

Air Canada has had to rapidly refocus its strategy following the collapse of its transborder markets thanks to President Trump's unpredictable politics. It also has to streamline its somewhat complex structure.

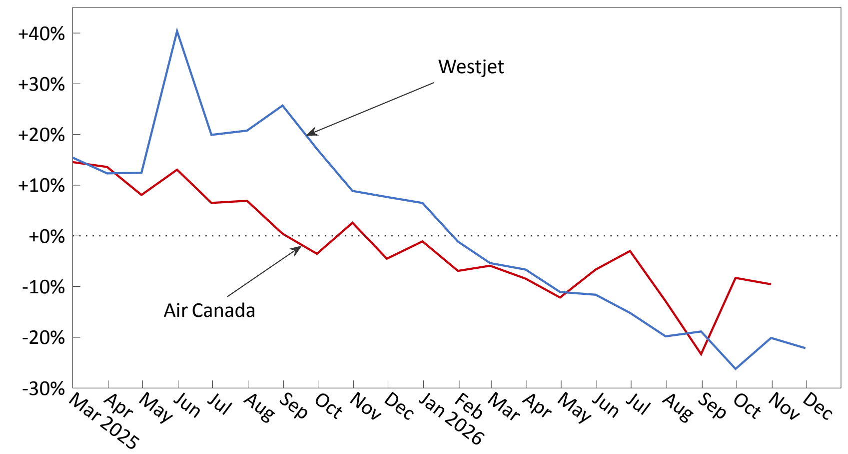
In the middle of the pandemic, it appeared possible that Air Canada might be renationalised (it was privatised in 1988). The federal government provided C$4bn in guaranteed loans and injected C$500m of capital into the company, taking a 6% equity stake. However, the airline recovered strongly in 2023, reporting record net profits of C$2.3bn, a 10.4% margin on revenues of C$21.8bn. Profits slipped in 2024 — C$1.7bn on revenues of C$22.2bn — but were still reasonable.

The federal government has now sold all its shares in the carrier, so Air Canada is again 100% privately owned, including by institutional investors such as the Canada Pension Plan Investment Board (CPPIB), Vanguard Group, BlackRock and RBC. While having a no-dividend policy, the company has embarked on a major share buy-back programme — spending C$1.3bn during 2024/25 on retiring shares, roughly 60% of its free cashflow during these two years. Unfortunately, the share price has not responded — as of mid-March the share was trading around C$19 compared to C$51 in January 2020 immediately before the pandemic hit.

2025 was a disappointment. Total passengers dropped to 45.3m from 45.9m in the previous year, while capacity was up by about 1%, resulting in an 84.6% system load factor.

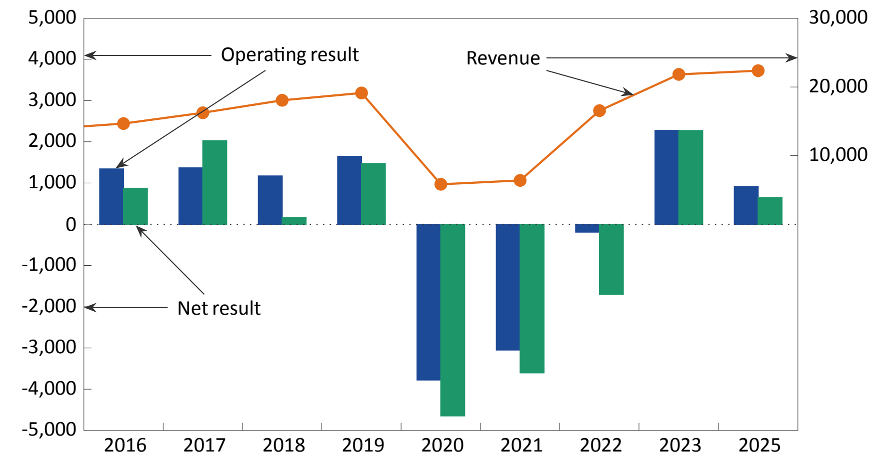
Net profits slumped to C$644m (US$463m), a 2.9% margin on C$22.3bn (US$16.0bn) of revenue. The impact of a protracted flight attendants strike in the summer was a contributory factor. The airline estimated a net loss of C$375m due to lost revenue and compensation payments in the third quarter, but a significant portion of the lost revenue was recovered in an unexpectedly strong fourth quarter.

CANADIAN AIRLINES' TRANSBORDER TRAFFIC



Source: DoT Form 41

AIR CANADA FINANCIAL RESULTS (C$m)



Source: Company reports

AIR CANADA REVENUES: REGIONAL SPLIT
(C$ millions)

	Pax & Cargo		Change		Shares	
	2025	2024	(C$)	(%)	2025	2024
Canada	5,399	5,361	38	0.7%	26.2%	25.8%
US Transborder	3,884	4,333	-449	-10.4%	18.8%	20.9%
Atlantic	6,345	6,129	216	3.5%	30.7%	29.5%
Pacific	3,025	3,103	-78	-2.5%	14.7%	15.0%
Other	1,984	1,825	159	8.7%	9.6%	8.8%
System Total	**20,637**	**20,751**	**-114**	**-0.5%**	**100.0%**	**100.0%**

Labour conflict continues to bedevil the airline. The attendants have not yet agreed the August pay and conditions offer, and the dispute remains under arbitration. Further difficult pay negotiations are due this year, with the mechanics and airport staff.

Trump effect

The external blow to Air Canada came from President Trump whose tariff policy consisted of imposing punitive taxes one day and reducing them the next when it became apparent that they were self-harming and that the two economies were intertwined — for instance, the car manufacturing business based at Detroit and Windsor is deeply integrated with components passing the border up to eight times in the production of a car. Then there were the tirades about Canada being the 51st state of the USA, a policy probably inspired by watching South Park [an utterly tasteless, but often funny and pointed American cartoon series depicting the citizens of a northern US town who blame Canada, and other liberals, when things go wrong].

The economic impact of President Donald Trump's tariffs on the Canadian economy has been estimated by RBC and others at as cutting GDP growth by C$2-6bn or 0.1% to 0.3% in 2025 and 2026. This is significant in the context of Canada's insipid economic performance — the IMF estimates 1.2% real GDP growth for 2025 and predicted 1.5% for 2026 before the Iranian war.

For Air Canada and WestJet, a booming transborder market was turned into a plummeting one — the latest available months indicating 30% annual falls — resulting from curtailed business travel and Canadians refusing to vacation in the USA. Winter destinations like Florida and Arizona have been particularly affected, with leisure travellers staying in Canada or diverting to the Caribbean, though a favoured destination, Cuba, is no longer possible because the US oil embargo means that there is no jet fuel available at Havana.

The table above reveals the impact on Air Canada's finances: US transborder revenue fell by 10.4% to C$3.9bn in 2025, the C$499m decline contrasting with a C$335m increase in all other regions.

Remarkably, at Air Canada's 2025 results presentation, held at the end of February, there was no mention of the "T" word, either from the management or the equity analysts. The main comment on the transborder market (18% of revenues) was that management expected conditions to remain the same, with no significant improvement or decline anticipated. The airline's short-term plans are, however, driven by the collapse of the transborder market. According to CEO Michael Rousseau: Air Canada has "reallocated capacity, moving to markets where demand was greater and de-risking our profile. Our established global footprint and fleet allowed us to adapt to travel trends and capitalise on them".

A mitigating factor for Air Canada is that its local rivals have cut transborder capacity more sharply (though this also means they have increased Atlantic capacity). Air Transat will cease all US flying in mid-2026, in effect closing what was once a network of nine routes. WestJet plans to suspend 16 routes, about 10 % of its transborder capacity.

Domestic concerns

Air Canada has always been enmeshed in domestic politics, with a perpetual discussion on the optimal level of competition in the country. Last year the Canadian Competition Bureau published a report in which it criticised the Air Canada/WestJet duopoly and recommended raising the foreign ownership limit for a single entity from 25% to 49% and allowing foreigners to completely own domestic carriers. President Trump has probably put paid to those proposals.

The pandemic put paid to a central element of Air Canada's strategy: the take-over of the country's number three airline, Air Transat, for a proposed C$720m. The takeover became incompatible with government support for both carriers. Air Transat has staged a recovery, reporting a net profit of C$242m on revenues of C$4.0bn in FY 2025 (to October 2025).

ULCC competition in Canada is provided by Flair Air, based at Edmonton, the capital of Alberta. Its current fleet comprises 20 737NGs and MAXes, carrying an estimated 5m passengers in 2025. No financials are available. The fleet was supposed to have grown to 50 units by 2026 but plans are uncertain, partly due to the airline's doubtful association with international financiers. A founding investor in and lessor to Flair was 777 Partners, a Miami-based investment firm and leasing company, which also invested in Bonza, an Australian LCC which went bankrupt after two years of operation. There is currently a US court case brought by the SEC against 777 Partners alleging multiple frauds. Meanwhile, 777's stake in Flair has been reduced from 25% to 10%.

Domestically, Air Canada retains a strong position, controlling over half of total capacity while WestJet has over 30%. It aims to grow domestic capacity by about 5% in 2026 focusing on its main hubs at Montréal and Toronto, while maintaining capacity in the western markets where WestJet dominates, though there will be a new Rouge base at Vancouver.

Rouge was originally conceived as a lower cost subsidiary operating A320 family aircraft. Now it resembles something rather different: a full-service 737 MAX operator, albeit still focused on leisure markets.

52 MAXes are to move from the mainline carrier to Rouge by the end of this year, where they will be reconfigured with 12 Business Class seats, 18 Economy-plus and 147 Economy seats. There will be reclining seats, seatback entertainment and free Wi-Fi, plus complimentary drinks and food on flights throughout North America. The Rouge A320s are to go in the opposite direction to mainline Air Canada where they will be reconfigured to mainline specs. Indeed, the entire mainline fleet and the regional subsidiary, Air Canada Express (Jazz), is going through a refurbishment programme.

It is difficult to see where Rouge will achieve significantly lower costs. The new configuration totals to 177 seats per MAX compared to 187 at WestJet. A relatively minor cost advantage come from the flight attendant pay scales which were about 33% lower at Rouge than at the mainline carrier, but that differential has been eroded by the recent pay negotiations. There is no difference in cockpit crew scales.

Air Canada also has a dedicated high-cost operation, its premium charter unit, Jetz, with four 70-seat A320s, aimed at the corporate market and sports teams. Jetz concentrates on flights within the Toronto-Ottawa-Montréal triangle, linking to New York. In also operates in the west between Vancouver, Calgary and Edmonton, plus charters to US cities.

AIR CANADA: FLEET

	In service	*Avg Age*	On Order	2026 Plan
Air Canada				
A220	40	*4.0*	20	60
A320	18	*23.1*		18
A321ceo	21	*19.7*		20
A321neo			30	16
A330	20	*19.1*		20
A350			8	
737MAX-8	47	*6.0*		
767	6	*32.8*		6
777	25	*16.1*		25
787	40	*8.9*	10	42
	217	***12.2***	**68**	**207**
Air Canada Rouge				
737MAX-8				52
A319	17	*27.4*		
A320	5	*18.4*		
A321	13	*10.3*		8
	35	***19.8***		**60**
Air Canada Jetz				
A320	4	*33.3*		**4**
Air Canada Express				
CRJ-900	32	*14.3*		30
Dash 8	41	*12.9*		41
ERJ-170	25	*19.3*		25
	98	***15.1***		**96**
Group Total	**354**	*13.8*	**68**	**367**

Atlantic and Pacific prospects

Air Canada growth prospects depend on the Atlantic and Pacific markets (31% and 15% of total revenues respectively). In 2026 Toronto will become the second largest transatlantic hub in North America by seat capacity and Montréal the fifth-largest (and additional services are planned from Ottawa and Halifax in Nova Scotia). Vancouver claims to be the second largest transpacific hub.

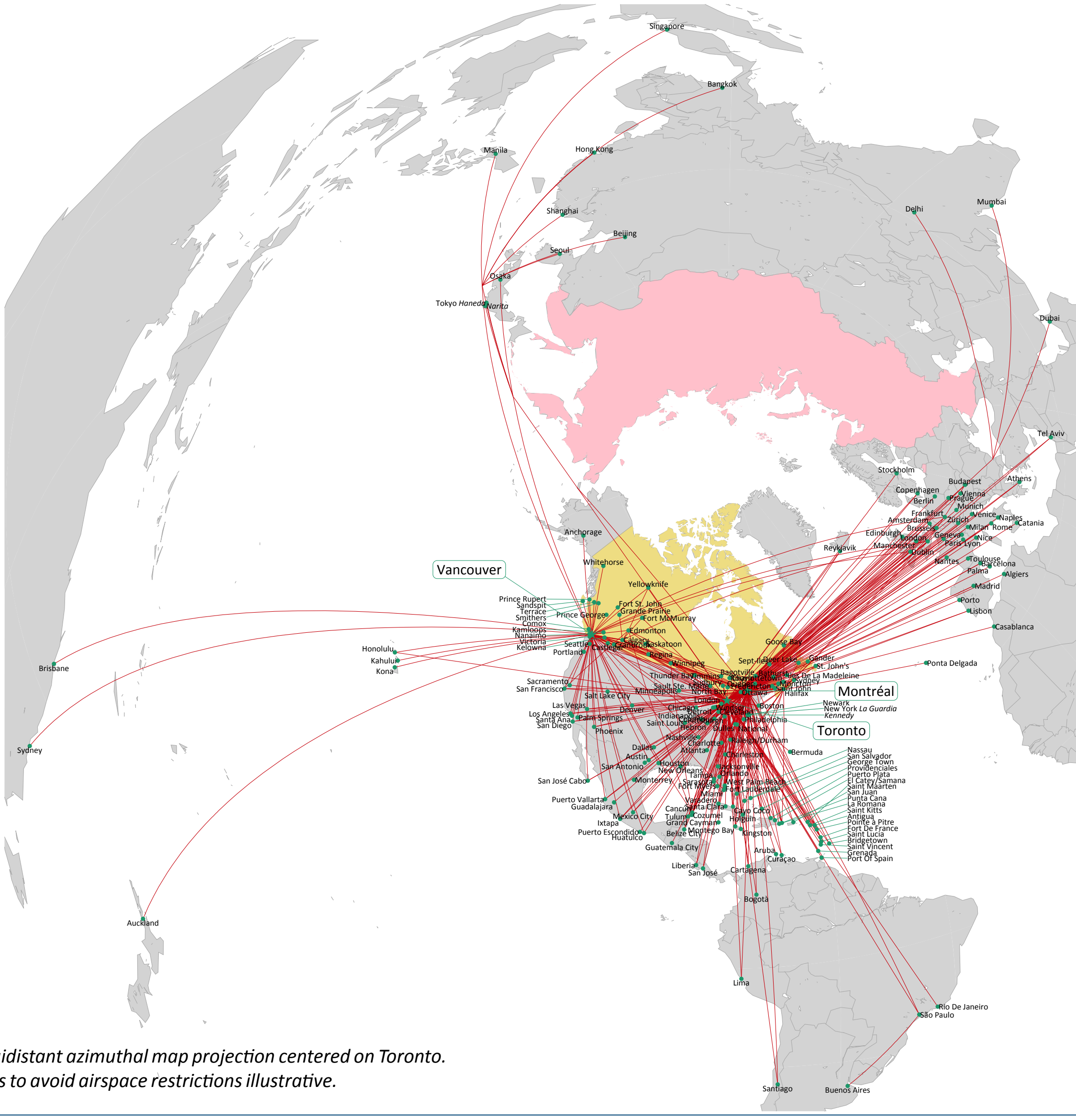
According to an analysis by Cirium, Air Canada will schedule 326 MAX flights to Europe in the third quarter of 2026, a 31% increase on 2025 and a 34% increase in seat capacity because of the new Rouge configuration. Some of the new destinations — Budapest, Catania, Nantes, Edinburgh, Copenhagen, among others — are likely to test the viability of thin long-hauls operated at low frequency.

The airline is also preparing for the A321XLR (14 fold-flat premium seats and 168 Economy), 15 of which will be delivered through 2026-27. These will extend Air Canada's range in eastern and southern Europe, and also are intended to appeal to business travellers.

One of new Prime Minister Mark Carney's initiatives this year, partly responding to the US polices, was to visit China in an attempt to normalise relations; he has also visited India, Malaysia, South Korea and Japan. Vancouver is part of the Pacific Rim economy and has a large Asian-origin population, so Air Canada sees the Pacific as its major growth opportunity and the focus of its widebody operation.

Last year Air Canada resumed service to Beijing which had been

AIR CANADA: ROUTE NETWORK



Note: Equidistant azimuthal map projection centered on Toronto. Diversions to avoid airspace restrictions illustrative.

AIR CANADA: FINANCIAL DATA (C$bn)

	2021	2022	2023	2024	2025
Revenue	6.40	16.56	21.83	22.26	22.37
Net income	(3.60)	(1.70)	2.28	1.72	0.64
Operating cash flow	(1.50)	2.37	4.32	3.93	3.66
Net capex	(1.87)	(2.50)	(3.55)	(2.64)	(2.82)
Free cash flow	(3.37)	(0.13)	0.78	1.29	0.84
Inc in debt	(1.01)	(1.54)	(2.37)	(2.40)	(1.51)
Equity raised	0.56	0.01	0.00	0.00	0.00
Share buy backs				(0.47)	(0.86)
Total cash flow	**(7.19)**	**(1.79)**	**(0.82)**	**(1.11)**	**(0.67)**

	Dec-25
Fleet and fixed assets	14.52
Intangilbles	4.53
Cash	5.52
Other current assets	6.64
Total assets	31.21
Long term debt	8.61
Current liabilities	14.13
Other liabilities and provisions	5.88
Total liabilities	28.62
Shareholders equity	**2.59**

suspended in 2020. This year new start-up routes include Singapore and Manila with increased frequency to Hong Kong and Bangkok. Responding to the Iran war, it has doubled capacity to India.

This is mostly a 787 market while 777-300s are allocated to Japan and South Korea. The airline recently announced that it was the purchaser of eight A350-1000s, previously marked as undisclosed. These aircraft are due for delivery in 2030 and will replace ageing 777s, and enable allowing non-stop flights of up to 9,000nm.

Air Canada has taken to emphasising its role as a sixth freedom carrier, connecting flows from Europe and Asia through to Mexico, the Caribbean and South America. It states that sixth freedom revenues have grown strongly but has not provided any detail on the absolute volumes. It must be said that Air Canada is not traditionally thought of as a sixth freedom carrier, and it will face intense competition from the mega-hubs of the leading US network carriers. Air Canada is less than a quarter the size of Delta in terms of traffic and revenues, and is close in size to Alaska Airlines.

Air Canada has shown resilience and has responded quickly to the transborder crisis but there is a lingering impression of a carrier that has not totally shed its state ownership legacy and is cautious in its growth plans — its 2030 “aspiration” is for revenues to reach C$30bn, compared to C$23bn now. For its size the airline is remarkably complex; it has four different brands (Air Canada, Air Canada Rouge, Jazz and Jetz) and it operates just about every type of widebody, narrowbody and regional jet (see table on page 18). And English/French tension is always in the background: Michael Rousseau’s tenure as CEO may be under threat not because of weaknesses in Air Canada’s strategy but because, despite his name and years spent in Montréal, he cannot communicate in French.

WestJet: Hidden within Onex

WestJet, one of David Neeleman’s airlines, was seen in the 2000s as the dynamic newcomer challenging staid Air Canada. It is based at Calgary, the largest city in Alberta where the economy is driven the hydrocarbons industry and whose citizens, uniquely among Canada’s provinces, do show some support for the 51st State concept.

WestJet went through a transition from a pure LCC to a hybrid, expanding internationally with 787s and 737MAXs, and setting up a ULCC subsidiary (Swoop, which was reintegrated into the mainline carrier in 2023). The transition process eroded WestJet’s profitability, and the unit cost gap between WestJet and Air Canada almost disappeared.

In 2019 Onex, a Canadian private investment fund, made a successful bid for WestJet, offering C$3.5bn (US$2.6bn) cash, roughly 67% above the C$2.1bn that the Toronto stockmarket had been valuing the airline at that time. The Onex deal was driven by Gerry Schwartz, the former CEO of the $59bn AUM fund, who back in 1999 had launched a bid for Air Canada, with the intention of merging the flag-carrier with Canadian, but that bid was blocked at the last minute.

WestJet's management fully welcomed the take-over, but the deal went through just before the pandemic struck. Since then, WestJet has been buried within Onex. It has issued zero financial information on the airline since the takeover. Apart from occasional on-time performance stats, it has issued no revenue, capacity or traffic results, and had made only the broadest press statements. For 2025 it was reported in the Canadian press that it carried 22.6m passengers, which would be a decline of about 10% from the 2019 peak of 25m. (For comparison, Air Canada's 2025 total of 45.5m was 12% down on the pre-pandemic 2019 figure of 51.5m.)

Immediate plans look similar to Air Canada Rouge, retreating from the US transborder market and concentrating 737MAX-8s on thinner routes in Europe: new 2026 services include Toronto-Cardiff, and Halifax to Madrid, Lisbon, and Copenhagen. New South American points include Medellin in Columbia and São Paulo in Brazil. It also has to integrate the 18 737s it acquired from its takeover of the charter carrier Sunwing in 2025.

Private equity companies make their profits from exiting — selling or refloating purchased companies, having turned their operations around, usually through cost cutting. Onex's overall target return on investment is 20% pa over a 5-8 year period, but that timescale will have been disrupted by the pandemic. That RoI would imply target price for WestJet of at least C$10bn, or about twice Air Canada's current stockmarket value.

CEO of WestJet is Alexis von Hoensbroech, appointed in 2022 and previously CEO of Austrian Airlines. The board also contains a number of ex-CEOs with formidable Network, LCC and Hybrid experience: Alex Cruz (Vueling and BA), Ben Smith (Air France, Air Canada and Rouge), Christoph Mueller (Aer Lingus) and Bob Fornaro (Spirit).

WestJet's ordering activity is consistent with its ambitions. Last September WestJet announced the purchase of 60 737-10 MAX aircraft, with options for an additional 25, plus seven 787-9s with options for four more. This brought the total firm orderbook to 123 aircraft, compared to Air Canada's 68.

However, to achieve its goals Onex, acting like all private equity companies, must load WestJet with debt and sell assets. This leverages the return on equity, if the company improves its financial performance (the opposite effect if the financial situation deteriorates).

Onex is obliged to share private WestJet financials with the credit rating agencies in order to obtain a rating for its bonds. Last June Fitch rated WestJet's long-term debt as just "B" (same as JetBlue) and revised its outlook to negative.

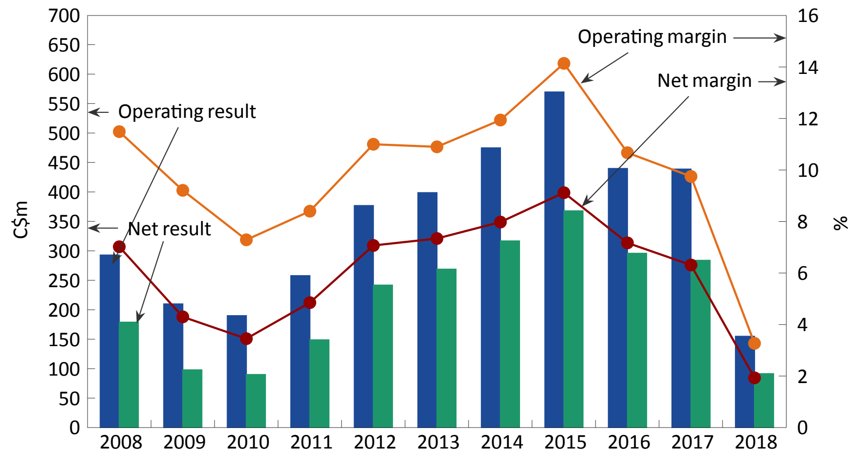
Fitch commented, just before the extent of the transborder traffic decline became apparent, that it expected WestJet's margins to come under pressure and remarked specifically about its financial structure:

"Gross adjusted leverage may rise towards 7x in 2025 from 5.9x at YE 2024. EBITDAR fixed charge coverage is projected to remain weak for the rating, potentially falling near 1x this year. WestJet has heavily engaged in sale-leasebacks in recent years, allowing it to raise significant liquidity through the pandemic years and beyond, but drove up lease-related charges. Lease liabilities have risen to C$3.5bn as at March 2025 from C$2.2bn in 2022 ... failure to restore fixed charge coverage to around 1.5x

WESTJET FLEET

	In service	*Avg Age*	Orders
737-700	36	*19.5*	
737-800	58	*13.0*	
737MAX	57	*5.0*	116
787-9	7	*5.9*	7
	158	***11.3***	**123**

WESTJET: PROFITS AND MARGINS



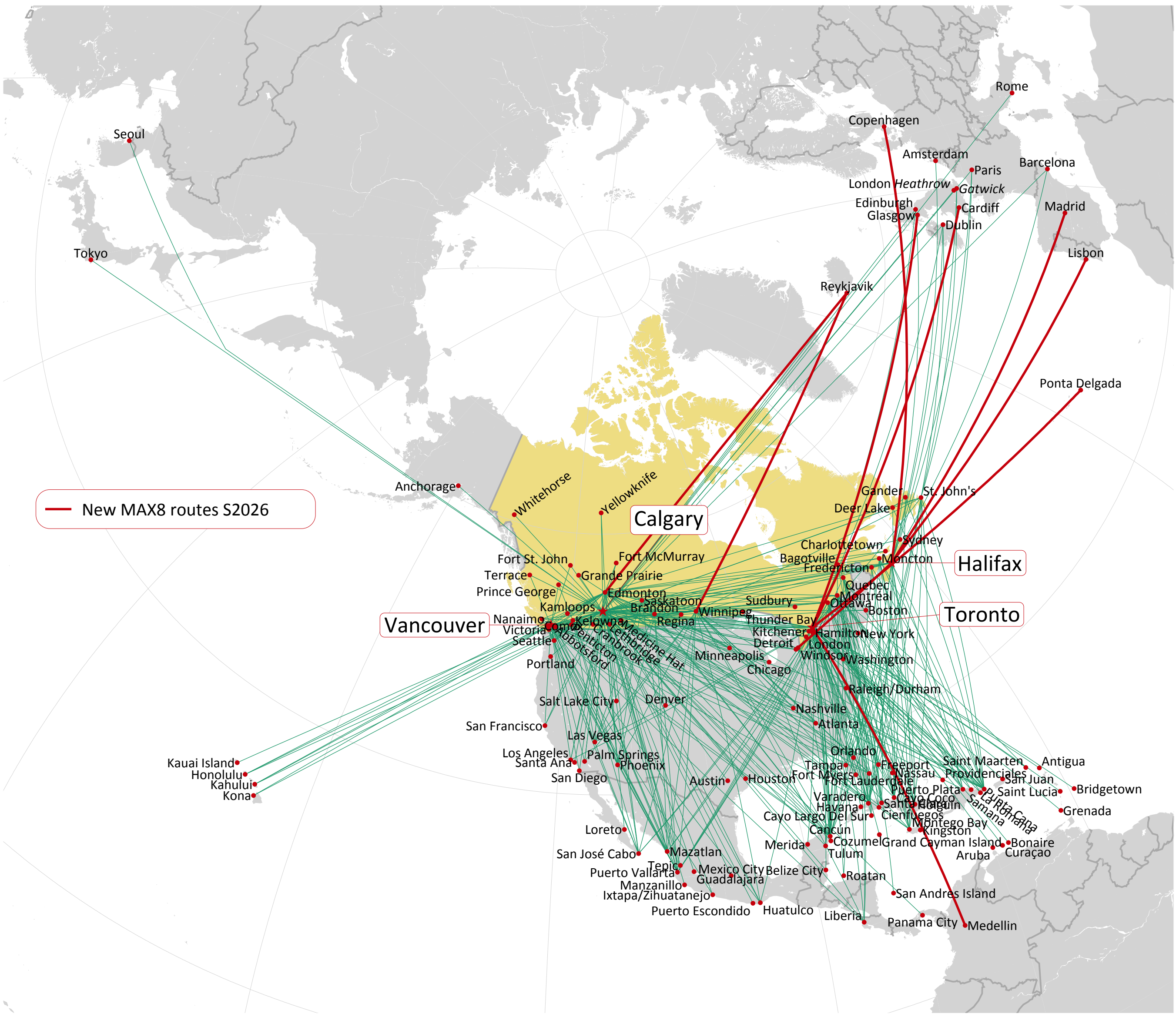
could trigger a negative rating action...

"WestJet's 'B' rating is three notches below its primary domestic competitor, Air Canada (BB/Stable). This difference reflects WestJet's higher near-term leverage prospects, more limited financial flexibility, and smaller relative size".

However, Fitch and the other agencies have not taken into account the role WestJet may play within the SkyTeam global alliance. In May 2025 Delta acquired a 12.7% equity stake in WestJet from the Onex Group, with Air France-KLM taking up a further 2.3% and Korean Air buying 10%, leaving Onex with 75%.

The full significance of this ownership structure is unclear but Alexis von Hoensbroech sounded optimistic: "A milestone in our airline partnerships, building on existing relationships and reflecting confidence in WestJet's strategy, performance, and people."

WESTJET ROUTE NETWORK



Note: Azimuthal equidistant map projection centred on Calgary.

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