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European LCCs: Is this the "bloodbath"?

The hyperbolic prediction earlier this year by Ryanair CEO Michael O'Leary that there would be a "bloodbath" in the European LCC sector this winter has had the desired effect of unnerving LCC investors. Partly as a consequence, several of the weaker LCCs have gone bankrupt; others will follow.

The most recent casualty is Warsaw-based LCC **Air Polonia**, which suspended flights in early December and as *Aviation Strategy* went to press was urgently searching for a new injection of funds from either LOT or private investors. Air Polonia ran into trouble after it couldn't afford a $800,000 instalment on the lease of its aircraft, followed by the collapse of a planned €10m loan from an existing Irish investor group. The airline is believed to have debts of around €7m.

Air Polonia was launched as a charter carrier in 2001 but adopted an LCC business model in December 2003. It operated three 737s, three Let L410s and an An-28 on routes from six Polish cities to secondary airports in five European countries, including London Stansted and Paris Beauvais.

Air Polonia's demise represents a rationalisation of the east/central European LCC market where three players - Air Polonia, Wizz Air and SkyEurope - were at least one too many. Hungarian/Polish airline Wizz now appears to be safe following an injection of €25m from US investor Indigo Partners. Wizz Air operates six A320s on services across Europe, and is now planning a major expansion in 2005, with 10 new routes from Budapest, Katowice and Gdansk.

Air Polonia also wasn't helped by the problems of alliance partner **Volare**, the Italian group that includes LCC Volareweb.com and charter carrier Air Europe. The Milan-based Volare Group has 1,400 employees and was founded back in 1994, and its LCC subsidiary operated 17 A320s to France, Spain, the UK, Germany and Belgium.

The group declared itself insolvent at the end of November after it couldn't pay lease fees, its debt reached the dizzy heights of €300m and attempts to find emergency funding of €60m failed. Volare chairman Mauro Gambaro wants the government to bail out the group but, ironically, Italian law prohibits the state from bailing out troubled companies unless their debt reaches €1bn.

To make matters worse, in November Italian prosecutors began informal questioning of Andrea Molinari, Volare's former CEO, about potential false accounting and misuse of funds at the group, although no charges have yet been laid. Apparently Deloitte & Touche claim they warned Volare about the precarious nature of its finances as early as 2002. Volare is owned 39% by Argentinean businessman Eduardo Eurnekian and 25% by Ginni Zoccai, former president of Volare. Eurnekian has reportedly agreed an option to buy Zoccai's stake in March 2007 for €35m, though unless there is a bailout and a remarkable turnaround the option will be worthless.

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The government has appointed an administrator, Carlo Rinaldi, to try and rescue the group, and he attempted to put together a rescue plan for the Italian civil aviation authority by a deadline of December 10. On that day the CAA stated a rescue plan had been submitted by Volare, but that it lacked sufficient detail on finances. However, the CAA gave Volare one last chance, by extending the deadline to December 15. If a rescue plan is approved, Volare flights will resume for the Christmas and New Year period, but if it isn't accepted by the CAA, then other airlines could be authorised to take over Volare's routes.

In late October, Dutch LCC **V Bird** went bankrupt owing around €39m to creditors. The airline was launched by Dutch and US investors (including former Air Exel chief Roberto Stinga) in October 2003, but collapsed after the Exel Aviation Group reportedly declined to inject further funds to save the airline.

V Bird employed 190 people and operated a fleet of three A320s - leased from ILFC - to 17 destinations in Europe. V Bird's main hub was at Niederrhein, a former military airport based just over the border in Germany, and it flew around 700,000 passengers in 2004 before collapsing, claiming a load factor of more than 70%. Talks with potential rescuers for V Bird appear to have petered out, and Germanwings is in negotiations with ILFC to take over V Bird's leases.

V Bird had hoped to establish itself as a European version of JetBlue, but never achieved much of a profile, blamed on lack of an advertising budget but probably also related to the unattractiveness of its airport base.

A putative long-haul LCC has also failed - Civair which was to have flown 747s between London Stansted and South Africa did not start up in early December as planned, following the withdrawal of backers.

easyJet/Ryanair: expansion and cashflow

Rationalisation through bankruptcy is a rapid process in Europe, the reverse of the explosion of LCCs many of which, though not all, had weak business plans and/or were underfunded. For easyJet and Ryanair, the development is welcome - they will need the space to expand into as they continue to take two or so new aircraft a month (see *Aviation Strategy*, June 2004). Their expansion has now taken on a momentum of its own through their sale and leaseback activity: as aircraft are delivered these LCCs have the opportunity of monetising the deep discounts they received from Airbus and Boeing, by selling the aircraft at market values to leasing companies then leasing them back; in other words, each aircraft delivery potentially boosts the airlines' cashflow.

Aer Lingus: the effect of government indecision and procrastination

The sudden resignation of the highly regarded and successful top management team at Aer Lingus, the Irish state-owned airline, raises a number of questions about the role of the Irish government with regard to the most financially successful of the AEA airlines.

The decision of Chief Executive Willie Walsh, Financial Director Brian Dunne and Chief Operating Officer Seamus Kearney to jump ship is a clear indication of frustration at the Irish government's continuing delay in implementing its commitment to privatisation made as far back as December 1999. It also reflects management's perception of less than full-hearted shareholder support for its latest cost reduction plan which calls for a further loss of 1,325 jobs (on top of 2,000-plus jobs shed over the last two years thus reducing employment by over 50% since 2001). This would involve an increased level of outsourcing, which is anathema to the unions, which are regarded as social partners by the government.

Over the last decade the government's position on state ownership of Aer Lingus has waxed and waned, influenced by political expedience rather than the needs of the airline or the management's views. Here is a potted history.

• Since the mid 1960s, when a minority shareholding held by BEA was acquired, the Irish state has been the 100% shareholder in Aer Lingus.
• Following the worldwide recession in the early 1990s the airline undertook a major restructuring programme involving considerable staff and other cost reductions, a disposal plan for non-airline subsidiaries and a state aid last time equity injection of IR£175m ($120m). In return for cooperation on the restructuring plan staff were granted access to a 5% shareholding in 1995.
• In autumn 1997 the government directed management to begin a competitive process to find a strategic alliance partner with or without an equity element. This was clearly interpreted as an initial key step towards privatisation although the government was not prepared to acknowledge this publicly for political reasons.
• Political indecision, the requirement to convince the unions of the benefits of a strategic alliance together with top management changes at the airline led to a long drawn-out process which was not completed until mid 1999. Bilateral alliances were signed with both American Airlines and British Airways (leading to membership of the oneworld alliance in 2000). An equity element was proposed but this was not acceptable to the government or unions.
• In December 1999 the government eventually made a commitment to privatise Aer Lingus. This was to be in the form of an Initial Public Offering (IPO) and good progress was made in the preparations necessary for a public flotation of shares in the airline. The legislation passed all stages in the Seanad (senate or lower house) and discussions began with staff representatives on the structure of Employee Share Option Scheme (ESOP) which would be part of the IPO.
• Discussions between the government and staff representatives proved to be long and difficult and little progress was made over a number of months. Management was effectively sidelined during this process, which led to a fair measure of frustration.
• By mid-2000, market conditions for IPOs had deteriorated and the government now asked its advisers to look at alternative sale options for the airline, thus adding further delay to the sale process. Not surprisingly, the advisers found a considerable degree of interest from potential institutional and private investors but this only led to further procrastination by the government.
• By summer 2001 management had lost faith in the government's privatisation intentions, and several senior executives decided to move on or retire. Then came the September 11 catastrophe, the Aer Lingus survival plan and the appointment of Willie Walsh as chief executive.
• The successful implementation of the survival plan by Walsh, Dunne and Kearney and further radical restructuring over the last two years was detailed in the July/August edition of *Aviation Strategy*. Aer Lingus is forecast to record profits in excess of €100m this year and a profit margin over 10%, the highest of all of the AEA airlines.
• Management and shareholder are agreed that the airline needs access to equity funding to strengthen the balance sheet and to expand and replace the long haul fleet. Government policy is not to invest further in the airline yet, despite a renewed undertaking to the airline Board and management in September 2003 by the Minister of Transport that the ownership issue would immediately be addressed, no decision has been taken to date.
• Increasing frustration at government's inaction prompted the management trio in June to formally request permission to develop an investment proposal for the airline. This was interpreted by many as a potential MBO request. Whatever, it was clearly designed to force a decision from government on the ownership/funding issues.
• The government responded by setting up a Cabinet sub-committee to consider the future of Aer Lingus. It then appointed Goldman Sachs to report on the strategic issues and options to be considered in the context of ownership change. Although that report has been with government for some months, it has not been published nor been addressed to date by the Cabinet sub-committee.
• The government, however, did set up an ESOP this summer. Staff now have a 14.9% shareholding in the airline.
• Negative feedback on government's attitude to management and its further restructuring

plans (particularly relating to outsourcing) led to management withdrawing its request for permission to develop an investment proposal at the end of October and this was followed some two weeks later by the resignation announcement by Walsh, Dunne and Kearney. The loss of the three executives, widely acknowledged as responsible for one of the most successful turnarounds in airline history, leaves the future of Aer Lingus in some disarray. Although the trio have offered to stay on board until the and of May next year their potential effectiveness in managing the airline, not to mention delivering further transformation, must be in serious doubt particularly in the light of the Taoiseach's (Prime Minister) recent comments to the Dail (Parliament) where he clearly sided with union resistance and criticised the management for their personal ambitions of wealth from the sale of a state asset. Although Walsh has robustly rejected this criticism, the damage has been done. Rumours are that Walsh will resurface next year as the chief executive of a leading LCC.

• Another issue is that the Aer Lingus chairman Tom Mulcahy resigned this summer. John Sharman was appointed acting chairman initially for a three-week period but later extended until the end of 2004, after a number of prominent Irish businessmen turned down the chairmanship. Thus Aer Lingus today has a lame-duck management and a temporary chairman.

• Latest reports from reliable sources in Dublin suggest that a decision will be made before Christmas to float 51% of Aer Lingus shares. That decision however will not be acted on until a new chief executive is in place and market conditions are favourable - so yet more delays.

The case for investing in airports

The case for investing in airports still remains a strong one. They promise long-term volume growth and typically have low cash flow and low earnings volatility. At the recent Global Airport Development conference held in Prague, the state of the sector and investment cases were discussed.

Airports are regulated monopolies with robust EBITDA margins, which have in most cases withstood external pressures like September 11, SARS and even the demise of flag carriers (for example Sabena at Brussels). At successful airports, non-aeronautical revenues typically grow at twice the rate of the regulated aeronautical revenues. Within the sector it is clear that there is a difference of emphasis between the investment models of the key investors - airports and financial buyers.

Airport operator investment model

The major airport operators (BAA, Fraport, Vienna International, Copenhagen Airports and TBI) have had their appetites for investments somewhat reduced post September 11. It has been a period where the airports have had to concentrate on cost cutting and deal with increased security requirements. Also, shareholders have shown a lukewarm reaction to investments made by airport operators where they have been unable to secure a controlling stake and have historically underestimated the political risk involved (for example, Fraport's investment in Manila, where contractual disputes culminated in a mult-million dollar loss for Fraport). Copenhagen Airports is still receiving criticism for its 49% investment in Newcastle Airport, which cost Copenhagen £95m in May of 2001, at the time that was a hefty 18.5 times EBITDA.

BAA makes as much money from the Heathrow Express (an express rail link serving the airport and central London) as it does from its total airport investments in Melbourne, Perth and Naples. These airport investments account for only 2% of BAA's

AIRPORTS: THE FOUR DIVISIONS	Example	Key Characteristics	Airline	No. of airports
International hubs	**Atlanta 79m pax**	• High share of transfer traffic • Large catchment area • Pax in excess of 40m	• Main hub of major international airline • Leadership role in alliance	**18**
International O and Ds	**Sydney 22m pax**	• Lower share of transfer traffic • Large catchment area • Pax in excess of 20m	• Main hub of int'l long haul airline or secondary hub of major airline • Subordinate or niche player in alliance	**32**
Secondary hubs and O and Ds	**Vienna 12m pax**	• Low share of transfer traffic • Sizeable catchment area, often overlapping • Pax around 10m	• Main hub of regional airline or secondary hub of major airline • Subordinate role in alliance	**c. 150**
Regionals	**Albany International Airport 1.5m pax**	• No transfer traffic • Smaller or remote catchment areas • Pax below 10m	• Regional airlines • LCCs	**c. 2,400**

Source: Boston Consulting Group

group pre-tax profits. Few airports also have major free cash flow to invest; for example, BAA's gearing will rise to around 50% at the peak of its investment in Heathrow's Terminal 5. Rather than just bricks and mortar, BAA is happy to expand its international activities through retail contracts, where there has been no equity investment but an upside poptential through profit sharing.

However, activity in the airport sector is resuming again, reflecting the general upturn in aviation. Recently, Abertis, the Spanish toll road group and AENA, the Spanish airports authority, have acquired 29.9% of TBI and have binding offers for another 19.5% of the shares. Last month, Macquarie Airports acquired a 70% equity interest of Brussels Zaventem airport for € 735m ($953m) from the Belgian state-run BIAC and a number of other shareholders .

Macquarie Airports: the financial investment model

Macquarie Airports, a listed globally diversified airport fund, looks to invest in developed assets. They focus on dominant airports within a strong catchment area, airports with above average traffic growth and strong EBITDA margins. Also crucial for the investment case is a strong commercial upside, light-handed regulation at the airport and preferably no large future capex programme. Macquarie has expertise in financial restructuring rather than managing, they prefer to apply their aviation knowledge as a shareholder not a manager and so unlike an airport operator there are no management fees. Their skill lies in managing the airport's capital base and using sophisticated financial instruments to fund new acquisitions or to refinance existing debt (which Macquarie is preparing to do at Bristol Airport).

Macquarie prefers to apply their aviation expertise as a shareholder rather than as a manager, this tactic seems to be paying off. The Macquarie Airports fund is now trading at 14 times EBITDA, while the average EV/EBITDA of the quoted European airport sector is currently at around 8.

The future

The sellers, which are usually governments, are becoming increasingly sophisticated in how they sell their airport assets and competitive auctions are producing high prices. In Europe, Budapest Ferihegy Airport has issued a tender publication for a privatisation adviser and Aeroports de Paris are in the initial stages of restructuring ahead of a planned privatisation (the French government however are set to retain a majority stake).

Determining who will be the winners and losers is becoming harder in this more complicated investment environment. In Europe, it is clear that three super-hubs (Heathrow, Charles de Gaulle and Frankfurt) have true pricing power and our set to dominate. It is less clear whether any of the mini-hubs will make good investments. Take for example, the case of both Prague and

Budapest airports, both slated for future privatisation and both are keen to challenge Vienna as the hub for eastern Europe. But, Prague and Budapest have much less pricing power and often need to discount to attract passengers, a situation that is comparable to the contrast between Frankfurt and Frankfurt-Hahn airports.

Schiphol Airport is also facing some uncertainty regarding the dual-hub strategy that has been implemented following the Air France/KLM merger. Schiphol's future is secure, at least for the next five years according to the merger terms, however investors will tread warily over the future of the weaker hub.

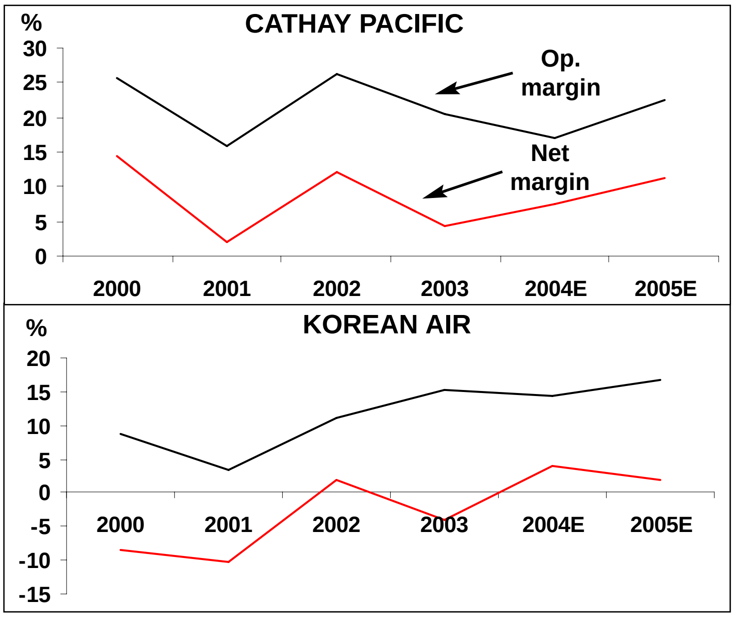
Other challenges facing airport investors are the instability of traffic flows, in the US hubs are collapsing and in Europe flag carriers, such as Swissair and Sabena, have failed. Also, historic travel patterns are being challenged by the LCCs. At regional airports, LCC growth is now typically growing ten times faster than the legacy carriers. In Germany, hubs such as Frankfurt and Munich recorded high growth rates for 2003 and the early months of 2004, however the most dramatic growth rates came from regional hubs boosted by the LCCs such as Berlin Schonefeld, Frankfurt-Hahn, Nurenburg and Stuttgart.

At the same time, investors will have to take a view on the survival of core carriers. Prague Airport is served by 14 LCCs momentarily, the figure was 15 before the recent collapse of Volare. However, there have been 20 LCC failures in the last two years.

Added to this volatility, future travel patterns are likely to be distorted by the arrival of new aircraft types. The A380 will be good for super-hubs but Boeing's 7E7 will suit smaller hubs and larger regional airports.

Robust results in Asia/Pacific region

In a recent research note by Deutsche Bank it is reported that the global airline industry will likely lose (according to IATA) over $3bn this year, due largely to escalating fuel prices. This comes as no surprise, but it is important to separate the Asian carriers, which are seeing some of the most robust travel demand in years, from the US and European carriers, which continue to face yield pressures and are operating on thinner margins. Most major Asian airlines will remain profitable in 2004.



Cathay Pacific

Deutsche Bank forecasts Cathay's net profit for the 2004 financial year at around HK$3.7bn ($480m) with the 2005 forecast coming in at HK$4.8bn. The bank assumes that passenger yields will rise 6.8% year-on-year in the 2004 financial year. From this assumed profit base of HK$3.7bn, there is now upside surprise potential, as yields and/or surcharges could come in stronger than expected.

Korean Air

The 2004 financial year forecast for net profits was W51bn ($48m) and net profits for

2005 were forecast at W143bn. These forecasts reflect higher fuel price assumptions, which are partially offset by assumed higher yields. Passenger and cargo yield assumptions for the 2004 financial year were raised by 1% in November, and Korean Air is expected to make a small profit of W72bn in the second half of 2004 (versus a W22bn loss in the first half of 2004).

Malaysia Airlines

Malaysia Airlines still looks likely to record a small net profit of around RM29m ($7m) for 2005, compared to 2004's RM481m ($126m). The airline's overall traffic growth looks healthy and Deutsche Bank forecasts a RPK growth of 20% for the 2005 financial year. however the net financial result will be close to break-even.

Qantas Airways Ltd.

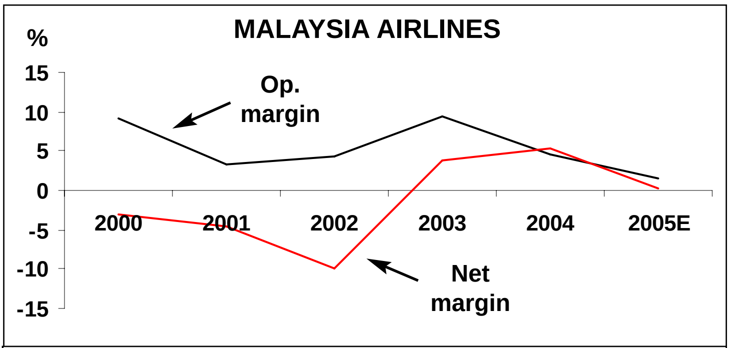
Excellent hedging, fuel surcharges and the rising strength of the Australian dollar are all mitigating the fuel price impact for Qantas in the 2005 financial year. Despite domestic yield pressure, a net profit of A$765m ($573m) is forecast for 2005, compared to the announced A$648m in 2004. This expected strong result is also due to improving yields and strong growth in its international business.

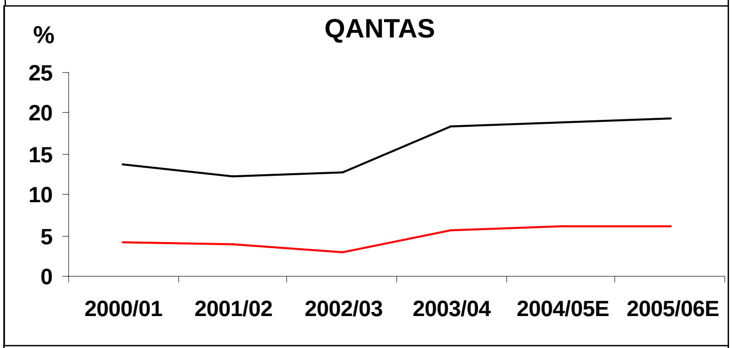
Singapore Airlines

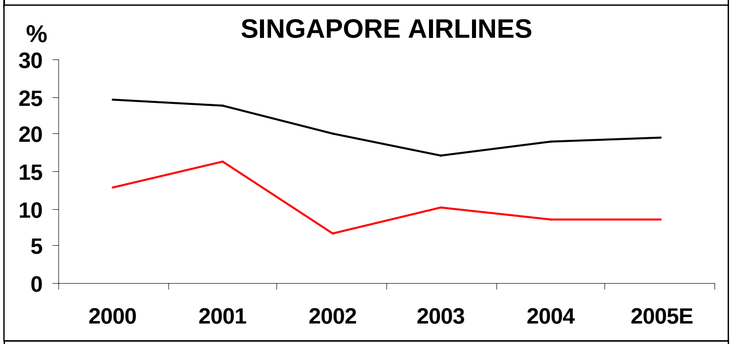
Showing sequential growth despite rising fuel prices, SIA net profits are forecast at S$1,041m ($632m) for 2005 against 2004's S$849m. Cargo yields grew 7% for the second quarter 2005 over the first quarter with passenger yields three points up, suggesting that fare hikes and surcharges are being passed through. With better hedging the fuel expense was lower than Deutsche Bank had expected.

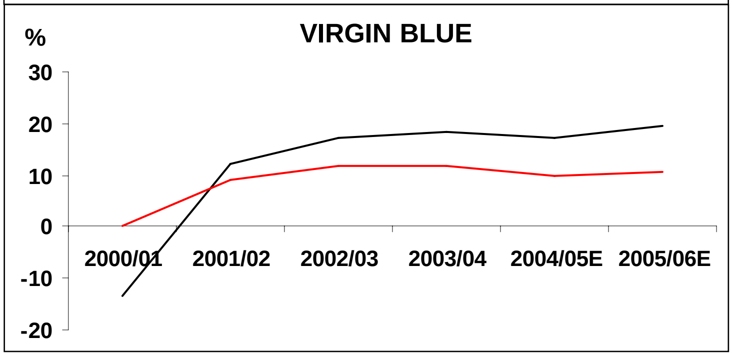
Virgin Blue Holdings

Virgin Blue is forecast to make a net profit of A$165m ($125m) in the financial year 2004/05 and A$200m in 2005/06. The current leisure focus of Virgin Blue makes it more difficult to pass on rising fuel costs to passengers via surcharges than for Qantas, leaving it at some risk. Also, higher than expected domestic yield pressure is affecting Virgin Blue as well as Qantas.









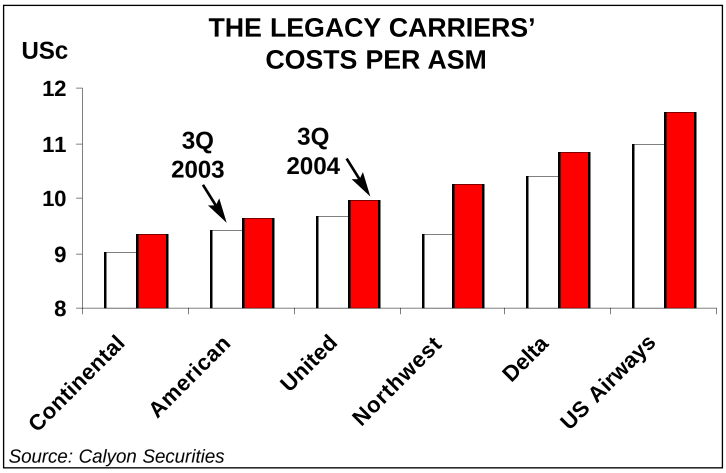
Lessons in labour negotiation from Continental

In late November Continental became the last of the top six US legacy carriers to seek wage concessions in the post-September 11 environment. The airline announced that it would begin "accelerated discussions" with its work groups to achieve a $500m reduction in its annual payroll and benefit costs by the end of February. This would be in addition to the previously announced target of $1.1bn annual cost savings and revenue enhancements.

The move obviously reflects worsened industry fundamentals (oil and the domestic revenue environment), continued significant financial losses and fears of a liquidity crunch this winter. However, aside from that, it is probably the best piece of news that has emerged from the legacy carrier camp in recent memory.

This is because Continental is expected to succeed in its efforts (though some analysts doubt it will meet the February 28 target date). Securing wage cuts is never easy, but the Houston-based carrier should be able to accomplish it without too much acrimony, perhaps even teaching the industry a few lessons about post-2001 labour negotiation.

It would certainly contrast with the latest developments at United and US Airways - both are now seeking approval in bankruptcy court to terminate labour contracts, while some of their unions are preparing for it by sending out strike ballots. This is the first time that substantive strike talk has surfaced since September 11.



Source: Calyon Securities

Most significantly, however, wage cuts at Continental should put considerable pressure on American and Northwest - and probably make it easier for both - to secure the additional cost cuts that they need. Overall, the odds now seem higher that the currently solvent legacy carriers will attain competitive cost structures outside of Chapter 11.

In the first place, Continental is likely to succeed because of its amicable labour relations. As testimony to that, in September the airline signed what it described as an "unprecedented partnership accord" with its ALPA-represented pilots. The deal formalised a commitment to work together and seek common solutions through a difficult industry climate. It was a culmination of more than a year's efforts to "develop a relationship based on providing each other with accurate, factual information and considering each other's input regarding operational and other issues". The process has already helped resolve some important issues, including the recent recall of 310 furloughed pilots "without imposing burdensome costs on the carrier".

Ironically, Continental is relatively healthy now only because it sought extensive help from Chapter 11 in the past. In chairman/CEO Gordon Bethune's words, it was a "good example of a company that ripped its labour contracts and stiffed its creditors" in the mid-1980s (under Frank Lorenzo's rule) and while in Chapter 11 again in 1990-93. (Lorenzo's labour moves were so abhorrent that they actually led to the revision of the Chapter 11 code, making it tougher for companies to terminate labour contracts in bankruptcy.)

Continental emerged from Chapter 11 in April 1993 with low unit costs but rock-bottom morale. However, Bethune, who is retiring at year-end, made improving employee relations and the corporate culture his priority throughout his ten-year tenure.

The key part of the process was to gradually restore wages to industry standards (achieved by the turn of the decade), while maintaining the productivity advantages established in Chapter 11. It was a feat to stay disciplined with the wage-restoration process in the late 1990s, when United allowed its labour costs to soar and other legacy carriers followed suit.

It has been suggested that Continental may be rushing the start of the wage concession talks so that popular CEO Bethune can play a role in the process before Larry Kellner takes over. One analyst argued that it might have been better for Kellner to spend his initial months "building new bridges with labour". However, Kellner is a well-established member of the top management team and the bridges with labour may already be there.

If the management and the pilots (the key group) stick to the provisions of the September accord, and if Continental genuinely needs the wage concessions (meaning it can prove the need), the odds are for a successful outcome. The deal addressed labour unions' traditional grievances fairly comprehensively, emphasising trust, mutual respect, proper documentation and open and honest communication. It also formalised the pilots' requirement for a "fair share" of financial rewards when the airline returns to profitability. The union also agreed to "temper our communications". When the deal was signed, ALPA's president Duane Woerth suggested that it could be a model for the industry.

Explaining the key concepts at a recent conference, Bethune noted that "it is always difficult to ask people for money, but if you have it well documented, it means you're not guessing". He emphasised that it is important to do it only once, rather than keep going back to ask for more (like US Airways and United have done). Bethune also made the point that it takes years to build trust.

One particularly nice aspect of Continental's move is that the top management will take the lead in pay reductions. Kellner will take a 25% cut in salary and performance compensation, and four other top executives will take 20% cuts, effective from February 28.

The company expects about half of the $500m savings to come from productivity enhancements and benefit changes and the other half from wage rate cuts. The latter would be on a progressive scale, with lower-paid employees being asked for a lesser amount. There would be enhanced profit sharing and continuation of on-time performance and other incentive programmes.

Potential liquidity issues

Continental is in no immediate danger of bankruptcy. Its financial results have consistently been better than those of its legacy peers, as it has outperformed the industry on both the revenue and cost fronts. Its CASM, at 9.35 cents per ASM in the third quarter, is the lowest among the large network carriers. Remarkably, its quarterly cash position has remained virtually unchanged (in the $1.5-1.6bn range) in recent years - a reflection of strong financial management. It still expects to end the year with $1.4-1.5bn of unrestricted cash - and it still holds a sizable stake in regional carrier ExpressJet that could be monetised.

However, Continental is meeting its liquidity targets only because it missed a $245m pension payment in September, and because it is collecting $80m from the disposition of its Orbitz holdings in the current quarter. Missing the pension payment was totally legitimate - the company took advantage of the temporary relief provided by Congress in April, which allowed airlines to delay some of their near-term pension obligations. Continental still intends to keep its plan up to 90% funded on a current liability basis; instead of paying $245m in September and $40m in 2005, it will now pay around $300m in 2005.

Continental may not be able to maintain satisfactory liquidity through the weakest part of the winter in the current fuel and fare environment, and selling the ExpressJet stake is probably being kept as an emergency option or "plan B".

But even if liquidity does not become an issue this winter, Continental needs labour concessions to avoid losing its competitive advantage. It is clear that United's and US Airways' cost cuts in Chapter 11, as well as the concessions American obtained on the courthouse steps in spring 2003, have narrowed the labour cost gap. In any case, all of Continental's three major union contracts are now amendable, meaning that negotiations would take place anyway.

More clarity about wage benchmarks

Until recently, the big frustration for Continental was that it could see competitors gaining ground on the labour cost front but it did not know where the process would stop. The goal posts have been shifting continuously since September 11. The airline was waiting for more clarity before responding, because it is determined to make wage concessions a one-time event.

The decision to seek $500m of labour concessions means that Continental feels that there is finally some level of clarity as to where the new wage benchmarks might be. However, it was a little disconcerting to see Bethune also note in the press release that "competitive financial analysis would support our asking for substantially larger reductions" (though that remark was obviously meant for employees).

The following is a summary of the key labour developments at the other large legacy carriers:

United is the airline everyone, including Continental, is really watching. It was the one that raised the bar for the rest of the industry in 2000 - not just in terms of pilot pay but right across employee groups - and it now has to lower the bar. Having been in Chapter 11 since December 2002, United is trying to prepare for a successful (much-delayed) exit from bankruptcy in 2005. After already shaving $5bn from its annual expenses, the airline says that it needs $2bn more to secure exit-financing and long-term survival.

The $2bn cuts would come from additional labour concessions ($725m), termination of pension plans ($650m) and non-labour sources ($655m). Of the $725m labour total, pilots would contribute $191.2m, machinists $180m, flight attendants $137.6m and salaried workers and management $111.8m.

Consequently, United is in the middle of its second round of labour concession talks. Having already agreed to $2.56bn of givebacks, the unions have not responded well. There was a watershed development on November 24, when United filed a Section 1113 motion, asking for permission to reject union contracts if consensual agreements on the $725m cuts have not been secured by mid-January. Significantly, the judge agreed to consider the motion, scheduling a hearing on it for January 10. United is also seeking a 4% company-wide pay reduction from January 1 until Chapter 11 exit.

The impression gained is that it was essentially the substantial size of United's proposed cuts and the Section 1113 filing that clarified the situation enough and prompted Continental to act (to the extent that it is responding to competitors' moves).

As regards to pilot pay, competitors can now easily calculate the new benchmark. United's pilots first took a 30% pay cut; now they will see a further 18% reduction - either a straight pay cut or a combination of pay reduction and work rule changes.

US Airways has set important precedents in its two Chapter 11 filings that cannot be ignored by competitors. However, the implications are made much less significant by the fact that the company still faces high risk of liquidation this winter (and it is smaller than the other legacy carriers).

The airline entered Chapter 11 in mid-September - for the second time in two years - as most of its unions rejected a plan to cut labour costs by a further $950m, after $1bn of concessions agreed to in 2002. Only pilots and some small unions had agreed to additional concessions totaling $340m. After imposing temporary 21% pay cuts, in mid-November US Airways filed motions to terminate three union contracts (covering ground workers, mechanics and flight attendants) and its remaining defined-benefit pension plans. Hearings on those motions began on December 2.

US Airways is in danger of not making it past January or February because of weak cash reserves and covenant and other issues with loans and financing agreements. In addition, its flight attendants and ground workers have threatened to strike in the event that the collective bargaining agreements are abrogated - any strike would effectively be a death sentence. However, if US Airways gets all the targeted cost savings and makes it through the winter, it could emerge from Chapter 11 with a cost structure similar to that of LCCs. It would have cut its labour costs by 60% from the 2000 level.

American is expected to go into a second round of concessions talks to stay competitive, in response to United's cuts and especially now that Continental has joined the fray. The airline has come a long way since April 2003, when it averted Chapter 11 by securing $1.8bn of annual wage and benefit concessions. Now one of the financially healthiest legacy carriers, American has noted on several occasions recently that the $4bn-plus annual cost savings achieved since September 11 are not enough. Significantly, its pilots have also acknowledged that.

Northwest has so far secured only $300m of its overall goal of $950m annual labour cost savings. The bulk of those came from a recent interim contract with pilots, which cuts pay by 15% annually over two years and leaves the pilots among the best paid in the industry. The annual saving is $265m, instead of the $440m asked for. Northwest is in a relatively strong financial position, but it needs to reduce labour costs to remain competitive. It accepted an interim deal, first, because it had financial covenant issues - it was subsequently able to renegotiate a $975m credit agreement. Second, Northwest wanted the pilot deal as a "bridge strategy", to help get concessions from other groups, mainly mechanics and flight attendants. The airline has told its pilots that it will have to ask for more concessions in the future.

Delta, which has been fighting to stay out of bankruptcy, recently secured a new pilot contract that will result in $1bn annual cost savings through wage cuts and benefit and work rule changes. Many of the key provisions took effect on December 1. The deal was part of efforts to achieve $5bn in annual financial benefits from a multitude of sources, as compared to the 2002 level. Some recent successes on the debt restructuring front have done much to avert the threat of Chapter 11 for the near term. However, the pilot cost cuts are probably not enough to give Delta a competitive pilot cost structure (it does not have a cost problem with other work groups).

Even though some of the legacy carriers will inevitably find it tough to get their labour costs competitive, there is now a sense that the industry wage bar is falling faster than anticipated. One consequence noted by JP Morgan analyst Jamie Baker: "As wage rates fall, the economics of legacy airlines and LCCs continue to converge". Baker suggested that valuations would converge as well, meaning lower valuations for LCCs and higher valuations for the "rapidly rejuvenating" legacies.

The trend of the economics converging may be accentuated by changes in the age profiles of work forces. LCCs have lower labour costs for two main reasons: better work rules and younger workers on lower pay scales. While the work rule gap is obviously lessening, some of the cost differential is eroding as LCCs' employees age and the legacies reduce their work forces (particularly through early retirement and other voluntary programmes).

The other area where costs will be converging is pensions. There is now a consensus among legacy airline managements that the traditional defined-benefit plans will have to go. But there are no clear solutions on how pension reform could be implemented without disadvantaging employees or affecting the competitive positions of airlines. The industry is waiting to hear how the bankruptcy court will rule on UAL's request to terminate its four pension plans. Also, Continental made the point that there should be congressional leadership on that issue in 2005.

By Heini Nuutinen

Opportunities at Chicago Midway

ATA Airlines' decision to sell its Chicago Midway hub operations - announced in conjunction with its Chapter 11 filing on October 26 - has opened up a uniquely attractive growth opportunity for one or more of the financially stronger LCCs. While AirTran is the front runner, having already signed a $90m asset acquisition agreement with ATA, Southwest and America West may also submit bids for all or part of the bankrupt carrier.

The deadline for the bids is December 10, and ATA's bankruptcy judge is expected to pick winner on December 16. However, there is potential for complications and delays, because the decision will also have to be approved by the City of Chicago - the party that ultimately decides how the Midway gates are reallocated.

If AirTran emerges as the winner - a potentially good scenario for all ATA stakeholders except possibly employees - the competitive implications are significant. It would set the stage for a mighty clash with Southwest, which is Midway's largest operator with a 42% passenger share (compared to ATA's 39% share, plus 5% held by its commuter unit Chicago Express Airlines) and is keen to expand significantly at that airport. It would be the first major confrontation between a strong new-generation (post-1990) LCC and Southwest.

After ATA's bankruptcy filing, Southwest immediately announced that its number one priority is Chicago Midway. It has some room to grow there within its existing 19 gates and has already announced plans to add 24 new daily flights in the first quarter, to boost its total Midway frequencies from 145 to 169. Essentially all of its 10 new 737-700s scheduled for delivery in the first quarter will go to Midway.

If Southwest gets the 6-7 additional gates it is believed to be seeking, it could over time build Midway into its largest hub. This would obviously have negative impact on United's and American's important Chicago O'Hare hub.

America West is known to be interested in ATA's 14 Midway gates, as well as its ETOPS certification. It does not currently serve Midway (only O'Hare) and would like a mid-continent hub. However, it may not be able to justify it to its shareholders. The scenario of America West successfully bidding for all or a substantial part of ATA has met with disapproval in the financial community. This is mainly because of the substantial risk involved in integrating the acquisition, including employees and a new fleet type - a risk that seems unacceptable in the current industry environment. Also, although America West is used to competing with Southwest in Phoenix and Las Vegas, it might be a better idea to diversify away from that exposure.

JetBlue has also been mentioned as a potential bidder for some of ATA's gates. However, building Chicago operations is not a priority for the New York City-based carrier, which has lots of exciting growth opportunities lined up elsewhere for its rapidly growing A320 fleet. It is also busy planning for the start of E190 operations in the latter part of 2005.

Mesa's name was also mentioned earlier in the ATA context, partly because the large regional is an old hand at M&A and partly because it is looking to diversify risk away from US Airways, United and Delta feeder operations. The most likely way it would get into Chicago would be as America West's feeder partner.

For its part, ATA has certainly played its cards right. It may or may not succeed in reorganising, but the bankruptcy process will at least give it a chance. Chapter 11 will enable it to implement a fleet and aircraft lease restructuring - ATA's 737-800s are too large for the Midway markets, and its leases exceed market rates to the tune of $100m annually.

With the AirTran deal, ATA secured a buyer and a good price for the assets that it feels it can part with, while still keeping the door open for better offers. The Bankruptcy Code generally provides for an auction to allow higher and better offers - from the point of view of all stakeholders - when a company in Chapter 11 seeks to sell assets. AirTran will be the "stalking horse" bidder, but it will be able to collect a $3.75m termination fee and up to $1bn of expenses if another offer is accepted.

Selling the Midway operation will enable ATA to focus on its home base and main hub at Indianapolis. It also plans to continue operating Hawaii service, military charters and some commercial charters. The ATSB has provided some flexibility in respect of ATA's $168m partially government-guaranteed loan, while Indiana Transportation Finance Authority has provided a $15.5m secured DIP financing (via an aircraft-part sale-leaseback transaction).

The deal with AirTran, which the two parties hope to close by December 23, would mean the Orlando-based carrier taking over ATA's gate leases and routes at Midway, as well as slots at New York LaGuardia and Washington National. Initially, AirTran would wetlease up to 12 of ATA's 18 leased 737-800s for the routes, before introducing its own 137-seat 737-700s from June 2005. ATA's 3,200 employees in Chicago would not be guaranteed jobs with AirTran, but many would obviously be taken on. The two airlines would forge marketing and code-share pacts, including a link between Chicago Express and AirTran.

The deal would provide an immediate liquidity boost. AirTran would pay $42m in cash to ATA at closing, plus $7m to the City of Chicago to retire airport facility debt, followed by $19m of further payments to ATA by April. The remaining $22m of the $90m purchase price would be paid over an eight-year period, subject to AirTran being able to continue to use ATA's slot exemptions at LaGuardia and National (over which there is some uncertainty).

This is a very attractive opportunity for AirTran to diversify risk away from Atlanta, get a second hub, establish a significant presence in one of the nation's largest travel markets, and find somewhere to put the 100 737-700s it has on order or option. Currently, the airline operates just one gate at Midway, though it is able to add a second gate and some new flights in January, independent of the ATA transaction. The ATA deal would enable AirTran to reduce Atlanta's share of its total capacity from 70% at present to 55% by the end of 2005.

AirTran expects to operate the ATA routes profitably, thanks to its smaller aircraft and better lease terms. It will minimise risk and start-up hassles by entering the markets gradually - and not having to integrate aircraft and employees in the longer term. Analysts do not expect the transaction to have negative profit impact in 2005, and in the longer term it should significantly boost AirTran's earnings. Since the deal was announced, AirTran's share price has surged from around $10 to the $12-13 range.

Credit rating agencies have not been quite as negative about AirTran's proposed transaction as they usually are about acquisitions. Notably, Moody's reportedly acknowledged that it is not every day that gates and capacity become available at one of the country's most desirable airports, and that the airlines need to take the opportunity as it arises. But AirTran's credit ratings now have negative outlooks, as the agencies worry about AirTran's debt leverage, Southwest and other risks.

Among equity analysts, UBS' Robert Ashcroft has probably taken the most negative view. He downgraded his AirTran stock rating in late November, partly on valuation and partly because he felt that AirTran has underestimated the risk of contracting with ATA in the interim and the pain that Southwest can cause. Ashcroft suggested that AirTran should give Southwest some of the gates and only build an 8-10 gate Midway operation, which would "provide AirTran with sufficient shelter from the storm in 2005 while exposing it to less risk".

AirTran executives have brushed off concerns about Southwest, saying that AirTran has a similar low cost structure and has competed very successfully with Southwest in East Coast markets. A heavy exposure to Delta in Atlanta is also risky, and Chicago would not become AirTran's primary hub. Also, as president Robert Fornaro pointed out in a recent conference call: "Southwest will be everywhere eventually, so you have to be able to compete with them".

Some analysts have made the point that the AirTran deal might be the best for the industry, because it would remove capacity from the domestic market through the use of smaller aircraft.

While Southwest and America West are also mainly interested in Midway gates, they could also bid for some of ATA's 737-800s. Southwest's CEO Gary Kelly noted recently that the airline might have to add a different 737 model, such as the 800-series, for any additional near-term growth, because there are not many 737-700s available in the used market. However, bidding for ATA's 737-800s will not improve an offer's chances, because the lessors should have no difficulty placing those aircraft with new customers.

But the situation is obviously different regarding employees. The City of Chicago has reportedly said that it wants any gate bidder to also take on ATA employees. This is one area where there could be significant disagreement, with ATA and its creditors backing the AirTran bid but the City preferring one from America West.

Regardless of who ultimately wins, the ATA bankruptcy process offers some pointers for things to come further down the airline consolidation road, for example with US Airways. First of all, it is becoming clear that the immediate beneficiaries from airline failures will be the LCCs, rather than the legacy carriers.

Second, consolidation is likely to take place through asset buyouts, not mergers. Most airline mergers have been difficult and expensive, with complicated fleet and labour issues, and have typically not created value for shareholders. Now there is also a lack of investment funds, lack of management time (with focus still on liquidity and survival issues) and lack of goodwill on the part of employees (after all the sacrifices made).

Third, Southwest is definitely becoming more aggressive and is likely to play a greater role in the industry consolidation process. Whether this is because a more assertive CEO is at the helm, because other LCCs are gaining ground or because good opportunities are presenting themselves (mainly the latter two), Southwest's ASM growth is likely to well exceed its customary 10% annual rate in the next few years. Currently, its plans still envisage 10% growth in 2005, following 6.9% this year. Calling this a "period of unbelievable change in the airline industry", Kelly said recently that the company is keeping an eye on growth opportunities that may open if other airlines sell assets.

By Heini Nuutinen

Air Berlin battles through Germany's LCC wars

Air Berlin has grown steadily to become not just the second-largest airline in Germany in terms of passengers carried, but also the third-largest LCC in the whole of Europe. But can the Tegel-based airline retain its independence against the onslaught of easyJet and Ryanair into the lucrative German market?

Air Berlin was founded by Kim Lundgren in 1978 as a charter airline based in the US, since only aircraft owned by the Second World War's Allied nations were allowed to land in Berlin. Once this rule ended, German investors bought into the company in 1992, and today Air Berlin is owned by Reidun and Kim Lundgren (26%), Severin and Rudolf Schulte (25%), Hans-Joachim Knieps (25%), Werner Huehn (15%) and Joachim Hunold (9%), who is also the airline's managing partner.

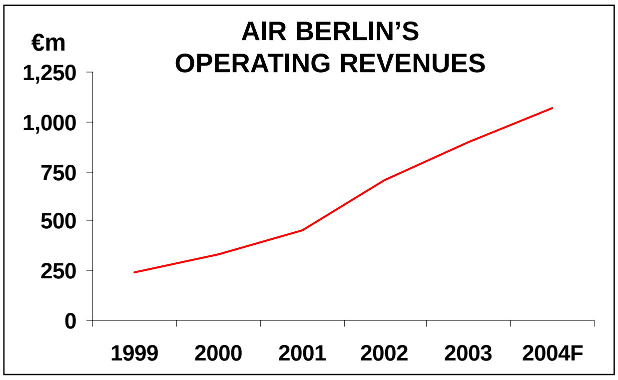
Originally Air Berlin sold its capacity to German package tour operators, but seat-only tickets began to be sold direct to the public once the airline had built up frequencies on key routes such as the so-called "Majorca Shuttle", which today links the popular Balearic island with 12 cities across Germany through more than 200 flights a week in the summer season. Mallorca is also a major hub for Air Berlin, and the island is linked with 12 destinations in the Iberian peninsula as well as to Austria, Switzerland and the UK. In the rest of its charter network, Air Berlin connects 16 German cities with holiday destinations across the Mediterranean and north Africa.

However, in the early 2000s Air Berlin realised that prospects for the charter market were not good - both in the short-term, given the recession in the German economy and in the long-term given the structural drift away from packaged holidays - and in October 2002 the airline launched the first of its City Shuttle services. The shuttles provide daily services between key cities and offer both business passengers and leisure travellers a low fare product. Today there are shuttles between nine major German cities and Barcelona, Budapest, London Stansted, Manchester, Madrid (starting December 18), Milan Bergamo, Rome, Southampton, Warsaw, Vienna and Zurich. Air Berlin claims that its City Shuttle services have already recouped their initial investment, and are profitable.

Altogether, as both a charter airline and a low fare carrier, Air Berlin operates to 57 destinations across Europe, and in 2003 carried 9.6m passengers - a substantial 43% rise on 2002. Of those, 4.8m were scheduled passengers (2.3m in 2002), making Air Berlin second only to Lufthansa in the German market in the non-charter market (Lufthansa carried 45.4m passengers in 2003), and ahead of DBA, which carried 3.1m passengers in 2003. But though scheduled passengers are now the future for Air Berlin, the charter sector is still substantial, and in 2003 the number of passengers carried to Mallorca rose by 53%, to 2.9m.

Air Berlin expects to carry around 11.6m passengers this year, and in January-September passengers carried rose 38.5% compared with the same period in 2003. In September the airline's load factor reached 87%, and for the first nine months of the year load factor was 81%, two percentage points up on the same period in 2003.

The airline has 2,200 employees, half of whom originate from the former East German state, but as Air Berlin is privately owned, its financial position is difficult to assess. Although revenue rose 26% in 2003 to €894m, it is believed to have made a small net loss that year thanks to the Gulf war and a downturn in tour operator business. For 2004 the airline is expecting revenue to top the €1bn mark (€1.07bn is the latest forecast), and in the first three-quarters of the year revenue rose by 19% to €797m - though this is still dwarfed by Lufthansa's annual turnover of €15.9bn. Full-year profit of up to €40m is forecast, though Air Berlin says 2004 profits would have topped the €100m level if it were not for the increase in fuel prices - a statement that implies Air Berlin has little hedging against fuel price rises.



The Lauda link

In January 2004 Air Berlin bought a 24% stake in Niki, the airline launched by Niki Lauda in November 2003 out of the Austrian assets of failed German charter airline Aero Lloyd. At the start of 2004 Niki operated just one A320 and one A321 on charter flights from Vienna and Salzburg to Mediterranean holiday destinations, but the link with Air Berlin enabled Lauda to move the airline towards the LCC model.

Air Berlin and Niki agreed to co-operate in a number of areas, including shared sales and marketing, CRS, co-ordination of schedules and joint logistics. Following the partnership, Niki acquired two more A320s and in May launched City Shuttle services from Vienna to Rome, Warsaw and Zurich. A fourth city shuttle came in November with the launch of a daily Vienna-London Stansted route, while a daily Vienna-Paris service will start in February 2005. Niki's flights to Mallorca have also been integrated into Air Berlin's hub operation there.

Up until October 31st, Niki carried 970,000 passengers and had revenue of €70m, producing a small net profit, it is believed. Both airlines state that Air Berlin has no plans to raise its stake in Niki in the future, and in any case Lauda would be reluctant to lose a controlling stake.

From Air Berlin's point of view, the partnership secures access to the Austrian market and enables the airlines to co-ordinate the launch of new routes into eastern Europe, where growing demand from the new EU nations is still outstripping capacity being added by western airlines. Air Berlin operates to Warsaw (from BerlinTegel) and Budapest (from Berlin Tegel, Dusseldorf and Munich), both of which commenced in the summer after Poland and Hungary joined the EU, while Air Berlin and Niki are examining services out of Vienna to Russia sometime in 2005.

The fleet

Air Berlin operates a fleet of 42 737s with an average age of less than three years, around half of which are leased. Air Berlin also wet leases three Fokker 100s from Germania as part of deal to operate Germania Express (Germania's LCC) routes from Berlin Tegel, Hamburg, Munich and Dusseldorf to Vienna and Zurich.

In 2003 Air Berlin experimented with the wet lease of three BAe 146s on a City Shuttle route out of Monchengladbach (also known as Dusseldorf Express Airport), but switched the service to 737s out of nearby Dusseldorf airport after finding the aircraft "very expensive".

After months of speculation, in November 2004 Air Berlin announced it had completed what was a "complex decision" and was ordering up to 70 A320 family aircraft - 60 for its fleet and 10 for partner Niki - with options for another 40 aircraft. All the aircraft will contain 174 seats in a single-class configuration. Niki currently operates two A321s and three A320s, but these will all be replaced by the new arrivals, so its fleet will expand to 10 aircraft. For Air Berlin, the move away from Boeing to Airbus is a major change, and yet another blow for Boeing, which had expected - at worst - that the order would be split between the two manufacturers. Inevitably, Boeing claims that Airbus only won the order after dropping its price per aircraft to a very low level - though Air Berlin insists that other issues, such as delivery slots, were an issue. A decision on engines has yet to be made, and again there is a difference between the prior policies of the two airlines: Niki's Airbuses use International Aero Engines V2500s, while Air Berlin's Boeing fleet uses CFM engines.

The firm order is believed to be worth around €3.4bn, and aircraft will start arriving in the third quarter of 2005, continuing until 2011. A consortium of banks is financing the order, and it is believed that Air Berlin will buy around half of the new aircraft and lease the other half. Final decisions on the models have yet to be made, and Air Berlin has not yet made clear how many of the 60 A320s will immediately replace existing 737s (some of which are leased) and how many will be for fleet expansion - though it's likely that many of the aircraft will be used for new routes and extra frequencies on existing services. Air Berlin has already announced it is expanding its workforce by hiring another 350 flight personnel in 2005.

Seven extra aircraft will be available by the end of summer 2005, bringing the fleet up to 52, and this capacity will be used on routes to eastern Europe, and - in a direct challenge to easyJet - on extra flights to London Stansted, Manchester and Southampton. This will come on top of four new routes launched to the UK in November 2004 - daily flights on Berlin Tegel-Manchester and Dusseldorf-Manchester, a three-times-a week service on Paderborn-Southampton and a four-times-a-week service on Paderborn-Manchester. The Dusseldorf-Manchester route competes against both Lufthansa and British Airways CitiExpress, while Berlin Tegel-Manchester is also served by CitiExpress. These routes joined Air Berlin's existing services to the UK - routes from six German cities and Mallorca, all to London Stansted, and which between them generated almost three quarters of a million passengers in 2003.

Air Berlin is also expanding its Spanish operations. In September Air Berlin announced it would build up Madrid airport into a hub operation, connecting the airport to 24 destinations in Germany, Switzerland and Austria, with all routes going via Mallorca. And in the same month Air Berlin launched a Bilbao-Mallorca route, allowing passengers from Bilbao to connect with 18 destinations in Germany, Austria and Switzerland.

Air Berlin is launching a daily Berlin-Madrid shuttle on December 18, though in September it complained about the inefficiency of Spanish airports, which was forcing it to increase fares by up to 8% on routes to the country, as well as the need to improve the facilities at Palma airport on Mallorca, home of its hub operation.

Air Berlin is looking to build hubs elsewhere in Europe. Basel is one destination under consideration, and the airline is believed to be talking to the airport authorities there. However, this appears a pretty unlikely candidate for major operations, given its proximity to Niki's operations in Zurich - unless Basel airport can come up with lower airport charges.

AIR BERLIN'S FLEET

	Fleet	Orders (options)
737-400	5	
737-700	3	
737-800	34	(2)
A320 family		60 (40*)
F100	3	
Total	**45**	**60 (42)**

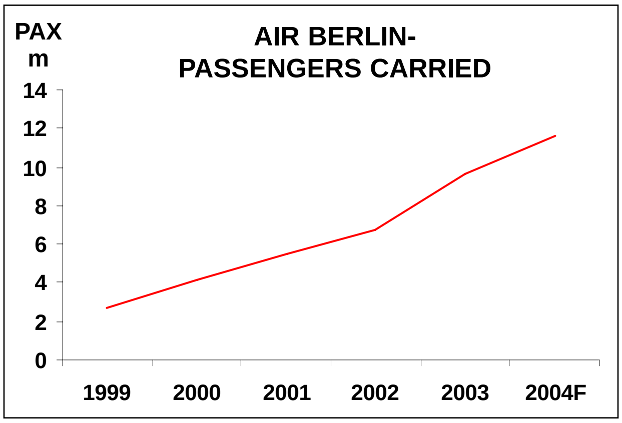
Note: *Options shared with Niki

A real LCC?

With lots of capacity being added and with tour operator business looking less than robust in the long-term (as the trend towards self-assembly holidays continues), Air Berlin will expand its City Shuttle network of low fare routes aggressively. Although its City Shuttles are a recent concept, in many ways Air Berlin has been ahead of its time. Before the LCC model came to Europe, Air Berlin was offering flights from secondary German airports such as Dresden, Munster/Osnabruck, Paderborn and Nuremberg, although now its strategy is much more about major city-to-city routes popular with business travellers than flying between secondary airports. Another difference with the traditional LCC business model is that Air Berlin has a strategy of signing simple partnerships (it dislikes what it calls complex interline deals) with other airlines. These deals feature one partner completely taking over services from the other on selected routes, and vice versa.

But is Air Berlin a true low cost airline? Given the lack of publicly available information, it's difficult to verify, but Air Berlin probably does have the lowest cost base of any airline in Germany, thanks to (at the moment) a young, all 737-fleet and relatively low labour costs. But as much as Air Berlin says it is now targeting Lufthansa on city-to-city routes, it's not the costs of the German flag carrier that Air Berlin has to beat, but those of easyJet and Ryanair. Certainly in terms of productivity, Air Berlin lags behind easyJet - Air Berlin's passengers carried per employee will be around 5,300 in 2004, compared with approximately 10,000 for easyJet (and 1,300 at Lufthansa, albeit on a global network).

The question of how low Air Berlin's costs are is crucial, since LCCs are starting to flood a market where fares have traditionally been



high. Rivals include not only German competitors such as Hapag-Lloyd Express and German Wings, but also foreign LCCs, crucially easyJet and Ryanair.

Michael O'Leary, CEO of Ryanair, says that there will be a "mother and father of all wars" in the German aviation industry, while Ray Webster, CEO of easyJet, has stated "it is not possible for small companies to survive in Germany". easyJet entered the German market in a big way in 2004 (after not taking up its option to buy DBA) by opening a hub at Berlin Schonefeld (also known as Brandenburg International) in April - a direct challenge to Air Berlin, Germania and Condor, all of which operate out of the airport (as well as out of Tegel). Six easyJet aircraft are stationed at Schonefeld, operating to 20 destinations throughout Europe. The latest tranche of routes were launched on November 25, with services between Berlin and Bratislava, Geneva, Ljubljana, and Riga. After Berlin, easyJet started operating out of Dortmund in July (and now operates to 9 destinations from there) and it also has four routes from Munich and Cologne/Bonn to the UK.

Ryanair started flying to Germany way back in 1999, and in July 2004 passed a total of 10m passengers carried to-from Germany. It has a major base at Frankfurt Hahn airport, (with five aircraft operating to 22 destinations), plus smaller operations at Dusseldorf Weeze airport (five destinations), Hamburg/Lubeck (five destinations). It also flies into Karlsruhe/Baden, Friedrichshafen, Berlin Schonefeld, Altenburg/Leipzig and Erfurt (though its London Stansted-Erfurt route is closing in January as part of a "weeding out of under-performing routes").

It is almost inevitable that there will be casualties in the German LCC sector. According to some analysts, there is overcapacity of more than 20% in the German low-fare market, and that's before easyJet's full entry - it alone expects to carry 1.5m passengers to and from Germany in the first 12 months of business. easyJet says that its average fare (across all routes) is €58, whereas it claims Air Berlin's average fare is €93, DBA's is €111 and Lufthansa's is €268.

However, the growth of foreign LCCs in the German market is starting to unite domestic airlines that otherwise would be loathe to co-operate with each other. Initially, Air Berlin was on its own in resisting easyJet. In February 2004 Air Berlin said it might pull out of Dortmund airport (its second most important German base) in favour of Paderborn or Munster/Osnabruck, after easyJet stated it would establish a hub there as well as Berlin Schonefeld. But once easyJet started operations in Dortmund, Air Berlin was quickly backed up by Lufthansa, and the two rivals complained about what they saw as the more favourable charges levied by the airport on easyJet. Air Berlin and Lufthansa - and then Hapag-Lloyd - unilaterally declared they would not pay Dortmund airport the same fee per passenger they had previously been paying - whether the airport agreed or not - and would instead only pay landing fees in line with the charges being levied on easyJet.

In Air Berlin's case, in September it declared it would pay €2 per passenger instead of the €15 per passenger it had been charged previously. Between them, Air Berlin and Lufthansa account for two-thirds of Dortmund's 0.9m passenger movements per year, and the unilateral fees reduction is forecast to cost Dortmund airport around €12m per year. Whether Dortmund airport will fight these unilateral reductions, accept them or (as the German airlines may prefer) raise easyJet's fees, remains to be seen.

The battle against easyJet has spread to other German airports. Hapag-Lloyd - TUI's charter airline - threatened to leave its base at Hannover airport if the authorities allowed easyJet to also establish a hub there. Air Berlin and Germania Express backed up this threat.

TUI employs 1,100 staff at Hannover, and the airport announced that its overriding concern was to protect those positions. Shortly afterwards, in July, easyJet dropped its plans for Hannover operations.

The increasing threat from easyJet is a key factor between a growing relationship between Air Berlin and Hapag-Lloyd. Since July Air Berlin has been codesharing with Hapag-Lloyd on selected charter routes, and from November 2004 that was extended to the summer of 2005, with codesharing on approximately 300 flights on popular holiday routes out of Munich, Nurnberg and Stuttgart, with Air Berlin focusing on routes to Mallorca and mainland Spain, and Hapag-Lloyd focusing on services to the Canary Islands. The airlines are also selling each other's flights.

There was speculation over the summer that this might lead to a full merger, or at the very least that TUI would acquire a stake in Air Berlin. In the past Air Berlin has held talks about strategic partnerships with the giant tour operator, but that appears unlikely in the short- and medium term given that Air Berlin has the finances it needs for its large fleet order and it can get substantial benefits from codesharing with Hapag-Lloyd, without the need for equity ties. However, a growing relationship between Air Berlin and Hapag-Lloyd could spell the end for TUI's LCC, Hapag-Lloyd Express (HLX). Hapag-Lloyd Express was launched in December 2002 at a cost of €100m, but its ongoing cost base may well be higher than Air Berlin's.

Elsewhere, the battle against easyJet continues. In October 2004, after a complaint by Air Berlin, a German court ordered Berlin Schonefeld Airport to change the prices it charges to LCCs. Air Berlin argued that Schonefeld charged easyJet less than Air Berlin was being charged (by the same airport operator) at Berlin Tegel airport, and again, Lufthansa backed up Air Berlin's complaint. Air Berlin has hinted it might have to think hard about whether to switch all its Berlin services to Tegel, but this is not believed to be a serious option

In October 2004 Air Berlin also entered into talks over an expanded sales and marketing agreement with LCC Germania, building on the existing wet lease agreement between the two airlines.

Up for an IPO?

In early 2004 Air Berlin said it was considering a stock market listing in the next 18 months, in order to raise the capital needed for its impending fleet order, and reports out of Germany say it began preliminary discussions with UBS.

At the time the airline stated that its current owners could not afford to invest further into the company, so that was why an IPO was being examined. In September however, the airline announced it would not be seeking a listing in the short- and medium-term, as it had come to an agreement with a consortium of banks for financing of its impending fleet order. The owners, which include managing director Joachim Hunold, may be keen to keep the airline away from the scrutiny of analysts and financial reporting requirements, though German analysts believe there may be a split among the shareholders, with Hunold believed to be less cautious about a flotation that some of the others, such as the Schulte brothers.

A complicating factor is that Air Berlin is aggressively anti-union, and is reluctant to allow its workers to have representation. Through 2004, Vereinigung Cockpit, the German pilots' union, has been trying to unionise workers, though Air Berlin is deliberately organised into small business units, each of which are too small to come under the effect of Germany's union laws.

However, German law requires companies undergoing a flotation with more than 2,000 employees to allow workers' representatives to have half the seats on the supervisory board. A way round this would be to float in another country, though that would strain relations between management and workers even further. But with Hunold reportedly saying that "I'd destroy everything I built up if workers entered the boardroom", it's difficult to see how the relationship could get any worse.

If Air Berlin doesn't go for an IPO, then an alternative for long-term funding would be a partial trade sale. Given the right strategic investor, this would also secure Air Berlin's future, and so seems its most likely option.

		Group revenue US$m	Group costs US$m	Group op. profit US$m	Group net profit US$m	Operating margin	Net margin	Total ASK m	Total RPK m	Load factor	Total pax. 000s	Group employees
Alaska	**Year 2002**	**2,224**	**2,313**	**-89**	**-119**	**-4.0%**	**-5.4%**	**31,156**	**21,220**	**68.1%**	**14,154**	**10,142**
	Jul-Sep 03	702	623	79	41	11.3%	5.8%	8,380	5,911	72.5%	4,280	10,114
	Year 2003	**2,445**	**2,456**	**-11**	**13**	**-0.4%**	**0.5%**	**37,614**	**26,061**	**69.3%**	**19,981**	**13,401**
	Jan-Mar 04	598	657	-59	-43	-9.9%	-7.2%	8,333	5,761	69.1%	3,592	9,984
	Apr-Jun 04	699	719	-20	-2	-2.9%	-0.3%	9,068	6,605	72.8%	4,116	10,255
	Jul-Sep 04	702	626	76	41	10.8%	5.8%	9,675	7,356	76.0%	4,589	10,201
American	**Year 2002**	**17,299**	**20,629**	**-3,330**	**-3,511**	**-19.2%**	**-20.3%**	**277,121**	**195,927**	**70.7%**	**94,143**	**93,500**
	Oct-Dec 03	4,391	4,618	-227	-111	-5.2%	-2.5%	66,541	47,622	71.6%		90,600
	Year 2003	**17,440**	**18,284**	**-844**	**-1,128**	**-4.8%**	**-6.5%**	**279,706**	**202,521**	**72.4%**		**96,400**
	Jan-Mar 04	4,512	4,470	42	-166	0.9%	-3.7%	68,551	48,746	71.1%		
	Apr-Jun 04	4,830	4,634	196	6	4.1%	0.1%	70,804	53,627	75.7%		92,500
	Jul-Sep 04	4,762	4,789	-27	-214	-0.6%	-4.5%	71,638	55,777	77.9%		93,300
America West	**Year 2002**	**2,047**	**2,246**	**-199**	**-430**	**-9.7%**	**-21.0%**	**43,464**	**33,653**	**73.6%**	**19,454**	**13,000**
	Oct-Dec 03	563	551	13	7	2.3%	1.2%	11,265	8,508	75.5%	4,888	
	Year 2003	**2,255**	**2,222**	**33**	**57**	**1.5%**	**2.5%**	**44,880**	**34,270**	**76.4%**	**20,050**	**11,326**
	Jan-Mar 04	577	559	18	1	3.1%	0.2%	11,832	8,539	72.2%	4,897	11,827
	Apr-Jun 04	605	584	21	6	3.5%	1.0%	12,153	9,519	78.3%	5,343	11,936
	Jul-Sep 04	579	607	-28	-47	-4.8%	-8.1%	12,305	10,021	81.4%	5,556	11,936
Continental	**Year 2002**	**8,402**	**8,714**	**-312**	**-451**	**-3.7%**	**-5.4%**	**128,940**	**95,510**	**73.3%**	**41,014**	**40,713**
	Oct-Dec 03	2,248	2,232	16	47	0.7%	2.1%	31,528	23,789	74.9%	9,884	
	Year 2003	**8,870**	**8,667**	**203**	**38**	**2.3%**	**0.4%**	**139,703**	**104,498**	**74.8%**	**39,861**	**37,680**
	Jan-Mar 04	2,269	2,404	-135	-124	-5.9%	-5.5%	32,621	23,678	71.7%	9,735	
	Apr-Jun 04	2,514	2,471	43	-17	1.7%	-0.7%	34,676	27,083	77.6%	10,809	
	Jul-Sep 04	2,564	2,540	24	-16	0.9%	-0.6%	35,371	28,843	81.5%	11,182	
Delta	**Year 2002**	**13,305**	**14,614**	**-1,309**	**-1,272**	**-9.8%**	**-9.6%**	**228,068**	**172,735**	**71.9%**	**107,048**	**75,100**
	Oct-Dec 03	3,398	3,764	-366	-327	-10.8%	-9.6%	55,740	40,522	72.7%	26,514	70,600
	Year 2003	**13,303**	**14,089**	**-786**	**-773**	**-5.9%**	**-5.8%**	**216,263**	**158,796**	**73.4%**	**104,452**	**70,600**
	Jan-Mar 04	3,292	3,680	-388	-383	-11.8%	-11.6%	55,300	39,027	70.6%	25,343	69,900
	Apr-Jun 04	3,961	4,202	-241	-1,963	-6.1%	-49.6%	62,151	47,610	76.6%	28,616	70,300
	Jul-Sep 04	3,871	4,294	-423	-646	-10.9%	-16.7%	63,031	48,952	77.7%	28,247	69,700
Northwest	**Year 2002**	**9,489**	**10,335**	**-846**	**-798**	**-8.9%**	**-8.4%**	**150,355**	**115,913**	**77.1%**	**52,669**	**44,323**
	Oct-Dec 03	2,407	2,419	-12	370	-0.5%	15.4%	34,413	26,732	77.7%	12,821	
	Year 2003	**9,510**	**9,775**	**-265**	**248**	**-2.8%**	**2.6%**	**142,573**	**110,198**	**77.3%**	**51,900**	**39,100**
	Jan-Mar 04	2,603	2,711	-108	-223	-4.1%	-8.6%	35,133	26,883	76.5%	12,500	39,230
	Apr-Jun 04	2,871	2,923	-52	-175	-1.8%	-6.1%	36,634	30,215	82.5%	14,289	39,154
	Jul-Sep 04	3,052	2,973	79	-38	2.6%	-1.2%	38,324	31,774	82.9%	14,800	38,178
Southwest	**Year 2002**	**5,522**	**5,104**	**417**	**241**	**7.6%**	**4.4%**	**110,859**	**73,049**	**65.9%**	**63,046**	**33,705**
	Oct-Dec 03	1,517	1,406	111	66	7.3%	4.4%	29,439	18,771	63.8%	16,290	32,847
	Year 2003	**5,937**	**5,454**	**483**	**442**	**8.1%**	**7.4%**	**115,532**	**77,155**	**66.8%**	**65,674**	**32,847**
	Jan-Mar 04	1,484	1,438	46	26	3.1%	1.8%	29,582	18,977	64.2%	15,995	31,522
	Apr-Jun 04	1,716	1,519	197	113	11.5%	6.6%	30,212	23,054	76.3%	18,864	31,408
	Jul-Sep 04	1,674	1,483	191	119	11.4%	7.1%	31,359	22,794	72.7%	18,334	30,657
United	**Year 2002**	**14,286**	**17,123**	**-2,837**	**-3,212**	**-19.9%**	**-22.5%**	**238,569**	**176,152**	**73.5%**	**68,585**	**78,700**
	Oct-Dec 03	3,615	3,750	-135	-476	-3.7%	-13.2%	55,709	42,823	76.9%	16,448	58,900
	Year 2003	**13,274**	**15,084**	**-1,360**	**-2,808**	**-10.2%**	**-21.2%**	**219,878**	**168,114**	**76.5%**	**66,000**	**58,900**
	Jan-Mar 04	3,732	3,943	-211	-459	-5.7%	-12.3%	56,181	42,287	75.3%	15,923	
	Apr-Jun 04	4,041	4,034	7	-247	0.2%	-6.1%	58,313	47,840	82.0%	18,444	59,700
	Jul-Sep 04	4,305	4,385	-80	-274	-1.9%	-6.4%	61,403	50,439	82.1%	19,360	59,000
US Airways	**Year 2002**	**6,977**	**8,294**	**-1,317**	**-1,646**	**-18.9%**	**-23.6%**	**90,700**	**64,433**	**71.0%**	**47,155**	**30,585**
	Jul-Sep 03	1,771	1,808	-37	-90	-2.1%	-5.1%	21,615	16,611	76.9%	10,584	26,300
	Oct-Dec 03	1,764	1,838	-74	-98	-4.2%	-5.6%	23,550	16,759	71.2%	13,507	26,797
	Year 2003*	**5,312**	**5,356**	**-44**	**-174**	**-0.8%**	**-3.3%**	**85,673**	**62,408**	**72.8%**	**44,373**	**26,797**
	Jan-Mar 04	1,701	1,844	-143	-177	-8.4%	-10.4%	23,771	16,220	68.2%	12,700	26,854
	Apr-Jun 04	1,957	1,874	83	34	4.2%	1.7%	46,747	36,503	78.1%	25,953	26,880
JetBlue	**Year 2002**	**635**	**530**	**105**	**55**	**16.5%**	**8.7%**	**13,261**	**11,000**	**83.0%**	**5,752**	**3,823**
	Oct-Dec 03	263	228	35	20	13.3%	7.6%	6,021	5,002	83.1%	2,378	4,892
	Year 2003	**998**	**830**	**168**	**104**	**16.8%**	**10.4%**	**21,950**	**18,550**	**84.5%**	**9,012**	**4,892**
	Jan-Mar 04	289	256	33	15	11.4%	5.2%	6,790	5,427	79.9%	2,650	5,292
	Apr-Jun 04	320	275	45	21	14.1%	6.6%	7,494	6,333	84.5%	2,921	5,718
	Jul-Sep 04	323	300	23	8	7.1%	2.5%	7,950	6,753	84.9%	3,033	6,127

***Note**: US Airways' financial results are for the 9 months up to Dec 31, 2003. Operating statistics are for the full year.

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

		Group revenue US$m	Group costs US$m	Group op. profit US$m	Group net profit US$m	Operating margin	Net margin	Total ASK m	Total RPK m	Load factor	Total pax. 000s	Group employees
Air France												
YE 31/03	**Year 2002/03**	**13,702**	**13,495**	**207**	**130**	**1.5%**	**0.9%**	**131,247**	**99,960**	**76.2%**		**71,525**
	Jul-Sep 03	3,715	3,598	117	56	3.1%	1.5%	35,255	27,544	78.1%		
	Oct-Dec 03	3,933	3,855	78	35	2.0%	0.9%	33,380	25,329	75.9%		71,900
	Jan-Mar 04	3,668	3,680	-12	16	-0.3%	0.4%	33,917	25,026	73.8%		
	Year 2003/04	**15,024**	**14,855**	**169**	**113**	**1.1%**	**0.8%**	**134,444**	**101,644**	**75.6%**		
KLM												
YE 31/03	**Year 2002/03**	**7,004**	**7,147**	**-144**	**-449**	**-2.1%**	**-6.4%**	**87,647**	**69,016**	**78.7%**	**23,437**	**34,666**
	Jul-Sep 03	1,878	1,725	152	104	8.1%	5.5%	18,905	15,874	84.0%		32,853
	Oct-Dec 03	1,838	1,801	36	10	2.0%	0.5%	17,969	14,378	80.0%		31,804
	Jan-Mar 04	1,677	1,645	32	-24	1.9%	-1.4%	17,963	14,455	80.5%		
	Year 2003/04	**7,157**	**7,011**	**146**	**29**	**2.0%**	**0.4%**	**72,099**	**57,784**	**80.1%**		**31,077**
Air France/												
KLM Group*	Apr-Jun 04	5,394	5,205	189	115	3.5%	2.1%	48,944	38,025	77.7%		
	Jul-Sep 04	6,328	5,964	364	248	5.8%	3.9%	57,668	46,767	81.1%		
Alitalia												
YE 31/12	**Year 2001**	**4,745**	**5,007**	**-262**	**-818**	-5.5%	-17.2%	**51,392**	**36,391**	**70.8%**	**24,737**	**23,667**
	Year 2002	**5,279**	**4,934**	**-89**	**101**	**-1.7%**	**1.9%**	**42,224**	**29,917**	**70.8%**	**22,041**	**22,536**
	Jan-Mar 03	1,097	1,226	-187		-17.0%		10,503	6,959	66.3	4,993	21,984
BA												
YE 31/03	**Year 2002/03**	**12,490**	**12,011**	**543**	**117**	**4.3%**	**0.9%**	**139,172**	**100,112**	**71.9%**	**38,019**	**51,630**
	Jul-Sep 03	3,306	2,980	333	163	10.1%	4.9%	35,981	27,540	76.5%	9,739	47,702
	Oct-Dec 03	3,363	3,118	244	148	7.3%	4.4%	35,098	25,518	72.7%	8,453	46,952
	Jan-Mar 04	3,386	3,327	164	22	4.8%	0.6%	35,232	24,932	70.8%	8,142	46,551
	Year 2003/04	**13,806**	**13,067**	**739**	**237**	**5.4%**	**1.7%**	**141,273**	**103,092**	**73.0%**	**36,103**	**49,072**
	Apr-Jun 04	3,479	3,208	271	127	7.8%	3.7%	36,150	27,083	74.9%	9,288	46,280
	Jul-Sep 04	3,645	3,213	432	221	11.9%	6.1%	36,639	28,749	78.5%	9,822	46,179
Iberia												
YE 31/12	**Year 2002**	**5,123**	**4,852**	**272**	**174**	**5.3%**	**3.4%**	**55,633**	**40,647**	**73.0%**	**24,956**	**25,963**
	Apr-Jun 03	1,348	1,265	83	60	6.2%	4.5%	13,516	9,982	73.8%	6,472	
	Jul-Sep 03	1,434	1,301	133	93	9.3%	6.5%	14,819	11,846	79.9%	7,073	
	Year 2003	**5,800**	**4,459**	**202**	**180**	**3.5%**	**3.1%**	**56,145**	**42,100**	**75.0%**	**25,613**	
	Jan-Mar 04	1,325	1,356	-32	-1	-2.4%	-0.1%	14,563	10,721	73.6%	6,136	
	Apr-Jun 04	1,461	1,371	90	95	6.2%	6.5%	14,743	11,106	75.3%	6,913	
	Jul-Sep 04	1,593	1,452	141	110	8.9%	6.9%	16,053	12,699	79.1%	7,314	25,839
Lufthansa												
YE 31/12	**Year 2002**	**17,791**	**16,122**	**1,669**	**751**	**9.4%**	**4.2%**	**119,877**	**88,570**	**73.9%**	**43,900**	**94,135**
	Apr-Jun 03	4,423	4,214	209	-39	4.7%	-0.9%	30,597	22,315	71.7%	10,758	
	Jul-Sep 03	4,923	4,783	140	-20	2.8%	-0.4%	32,895	24,882		12,020	
	Year 2003	**20,037**	**20,222**	**-185**	**-1,236**	**-0.9%**	**-6.2%**	**124,000**	**90,700**	**73.1%**	**45,440**	**94,798**
	Jan-Mar 04	4,742	4,883	-141	76	-3.0%	1.6%	31,787	23,030	72.5%	11,414	93,479
	Apr-Jun 04	5,269	5,045	224	-28	4.3%	-0.5%	36,440	26,959	74.0%	13,336	
	Jul-Sep 04	5,511	5,164	347	154	6.3%	2.8%	38,115	28,883	75.8%	14,053	92,718
SAS												
YE 31/12	**Year 2002**	**7,430**	**7,024**	**78**	**-15**	**1.0%**	**-0.2%**	**47,168**	**30,882**	**68.2%**	**21,866**	
	Apr-Jun 03	1,906	1,705	201	8	10.5%	0.4%	12,278	7,855	64.0%	5,128	
	Jul-Sep 03	1,941	1,715	131	91	6.7%	4.7%	12,543	8,681	69.2%	8,301	34,856
	Year 2003	**7,978**	**8,100**	**-122**	**-195**	**-1.5%**	**-2.4%**	**47,881**	**30,402**	**63.5%**	**31,320**	**34,544**
	Jan-Mar 04	1,652	1,823	-171	-184	-10.4%	-11.1%	11,852	7,031	59.3%	7,238	
	Apr-Jun 04	2,007	1,979	27	13	1.3%	0.6%	13,456	8,960	66.6%	8,879	
	Jul-Sep 04	2,099	1,860	239	9	11.4%	0.4%	13,557	9,198	67.8%	8,591	
Ryanair												
YE 31/03	**Year 2002/03**	**910**	**625**	**285**	**259**	**31.3%**	**28.5%**			**84.0%**	**15,740**	**1,900**
	Apr-Jun 03	280	220	57	46	20.4%	16.4%			78.0%	5,100	2,135
	Jul-Sep 03	407	237	170	148	41.8%	36.4%				5,571	2,200
	Oct-Dec 03	320	253	67	51	20.9%	15.9%				6,100	2,356
	Year 2003/04	**1,308**	**978**	**330**	**252**	**25.2%**	**19.3%**			**81.0%**	**23,133**	**2,300**
	Apr-Jun 04	366	288	78	64	21.3%	17.5%			83.0%	6,600	2,444
	Jul-Sep 04	516	305	211	181	40.9%	35.1%			90.0%	7,400	2,531
easyJet												
YE 30/09	**Year 2001/02**	**864**	**656**	**111**	**77**	**12.8%**	**8.9%**	**10,769**	**9,218**	**84.8%**	**11,350**	**3,100**
	Oct-Mar 03	602	676	-74	-76	-12.3%	-12.6%	9,594	7,938	82.2%	9,347	
	Year 2002/03	**1,553**	**1,472**	**81**	**54**	**5.2%**	**3.5%**	**21,024**	**17,735**	**84.1%**	**20,300**	**3,372**
	Oct-Mar 04	803	861	-58	-36	-7.2%	-4.5%	10,991	9,175	83.3%	10,800	
	Year 2003/04	**1,963**	**1,871**	**92**	**74**	**4.7%**	**3.8%**	**25,448**	**21,566**	**84.5%**	**24,300**	

Note: Annual figures may not add up to sum of interim results due to adjustments and consolidation. * = Preliminary consolidated figures for Air France Group from April-June, KLM Group from May-June

		Group revenue US$m	Group costs US$m	Group op. profit US$m	Group net profit US$m	Operating margin	Net margin	Total ASK m	Total RPK m	Load factor	Total pax. 000s	Group employees
ANA												
YE 31/03	**Year 2001/02**	**9,714**	**9,529**	**185**	**-76**	**1.9%**	**-0.8%**	**87,908**	**57,904**	**64.7%**	**49,306**	
	Apr-Sep 02	5,322	5,194	127	-69	2.4%	-1.3%	44,429	29,627	66.7%	25,341	
	Year 2002/03	**10,116**	**10,137**	**-22**	**-235**	**-0.2%**	**-2.3%**	**88,539**	**59,107**	**66.7%**	**50,916**	**14,506**
	Apr-Sep 03	5,493	5,362	131	186	2.4%	3.4%	32,494	19,838	61.1%	22,866	
Cathay Pacific												
YE 31/12	**Year 2002**	**4,243**	**3,634**	**609**	**513**	**14.4%**	**12.1%**	**63,050**		**77.8%**		**14,600**
	Jan-Jun 03	1,575	1,672	-97	-159	-6.2%	-10.1%	26,831		64.4%	4,019	14,800
	Year 2003	**3,810**	**3,523**	**287**	**168**	**7.5%**	**4.4%**	**59,280**	**42,774**	**72.2%**	**12,322**	**14,673**
	Jan-Jun 04	2,331	2,046	285	233	12.2%	10.0%	35,250		76.1%	6,404	
JAL												
YE 31/03	**Year 2000/01**	**13,740**	**13,106**	**634**	**331**	**4.6%**	**2.4%**	**129,435**	**95,264**	**73.6%**	**38,700**	**17,514**
	Year 2001/02	**9,607**	**9,741**	**-135**	**-286**	**-1.4%**	**-3.0%**				**37,183**	
	Year 2002/03	**17,387**	**17,298**	**88**	**97**	**0.5%**	**0.6%**	**145,944**	**99,190**	**68.0%**	**56,022**	
Korean Air												
YE 31/12	**Year 2001**	**4,309**	**4,468**	**-159**	**-448**	**-3.7%**	**-10.4%**	**55,802**	**38,452**		**21,638**	
	Year 2002	**5,206**	**4,960**	**246**	**93**	**4.7%**	**1.8%**	**58,310**	**41,818**	**71.7%**		
	Year 2003	**5,172**	**4,911**	**261**	**-202**	**5.0%**	**-3.9%**	**59,074**	**40,507**	**68.6%**	**21,811**	
Malaysian												
YE 31/03	**Year 2000/01**	**2,357**	**2,178**	**179**	**-351**	**7.6%**	**-14.9%**	**52,329**	**39,142**	**74.8%**	**16,590**	**21,518**
	Year 2001/02	**2,228**	**2,518**	**-204**	**-220**	**-9.2%**	**-9.9%**	**52,595**	**34,709**	**66.0%**	**15,734**	**21,438**
	Year 2002/03	**2,350**	**2,343**	**7**	**89**	**0.3%**	**3.8%**	**54,266**	**37,653**	**69.4%**		**21,916**
Qantas												
YE 30/06	**Year 2001/02**	**6,133**	**5,785**	**348**	**232**	**5.7%**	**3.8%**	**95,944**	**75,134**	**78.3%**	**27,128**	**33,044**
	Jul-Dec 02	3,429	3,126	303	200	8.8%	5.8%	50,948	40,743	80.0%	15,161	34,770
	Year 2002/03	**7,588**	**7,217**	**335**	**231**	**4.4%**	**3.0%**	**99,509**	**77,225**	**77.6%**	**28,884**	**34,872**
	Jul-Dec 03	4,348	3,898	450	269	10.3%	6.2%	50,685	40,419	79.7%	15,107	33,552
	Year 2003/04	**7,838**	**7,079**	**759**	**448**	**9.7%**	**5.7%**	**104,200**	**81,276**	**78.0%**	**30,076**	**33,862**
Singapore												
YE 31/03	**Year 2001/02**	**5,399**	**4,837**	**562**	**395**	**10.4%**	**7.3%**	**94,559**	**69,995**	**74.0%**	**14,765**	**29,422**
	Year 2002/03	**5,936**	**5,531**	**405**	**601**	**6.8%**	**10.1%**	**99,566**	**74,183**	**74.5%**	**15,326**	**30,243**
	Year 2003/04	**5,732**	**5,332**	**400**	**525**	**7.0%**	**9.2%**	**88,253**	**64,685**	**73.3%**	**13,278**	**29,734**
	Apr-Jun 04	1,588	1,409	179	159	11.3%	10.0%	25,249	18,167	71.9%	3,800	
	Jul-Sep 04	1,780	1,587	193	215	10.8%	12.1%	26,357	19,959	75.7%	4,050	

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

AIRCRAFT AVAILABLE FOR SALE OR LEASE

	Old narrowbodies	Old widebodies	Total old	New narrowbodies	New widebodies	Total new	Total
1999	243	134	377	101	53	154	531
2000	302	172	474	160	42	202	676
2001	368	188	556	291	101	392	948
2002	366	144	510	273	102	375	885
2003	275	117	392	274	131	405	797
2004-March	227	94	321	249	110	359	680

AIRCRAFT SOLD OR LEASED

	Old narrowbodies	Old widebodies	Total old	New narrowbodies	New widebodies	Total new	Total
1999	582	230	812	989	170	1,159	1,971
2000	475	205	680	895	223	1,118	1,798
2001	286	142	428	1,055	198	1,253	1,681
2002	439	213	652	1,205	246	1,451	2,103
2003	408	94	502	1,119	212	1,331	1,833
2004-March	32	13	45	215	32	247	292

Source: *BACK* **Notes:** *As at end year; Old narrowbodies = 707, DC8, DC9, 727,737-100/200, F28, BAC 1-11, Caravelle; Old widebodies = L1011, DC10, 747-100/200, A300B4; New narrow-bodies = 737-300+, 757. A320 types, BAe 146, F100, RJ; New widebodies = 747-300+, 767, 777. A600, A310, A330, A340.*

EUROPEAN SCHEDULED TRAFFIC

	Intra-Europe			North Atlantic			Europe-Far East			Total long-haul			Total Int'l		
	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %
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
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
Oct 04	19.5	13.2	67.7	19.4	15.7	81.0	13.6	11.0	81.1	46.0	37.3	81.2	68.9	52.9	76.8
Ann. chng	7.6%	5.8%	-1.1	2.4%	4.0%	1.2	15.3%	12.8%	-1.8	6.7%	7.7%	0.8	7.2%	7.0%	-0.1
Jan-Oct 04	185.9	123.8	66.6	190.5	156.7	82.3	127.6	99.9	78.3	447.9	360.6	80.5	667.1	507.8	76.1
Ann. chng	6.4%	7.9%	0.9	5.2%	8.7%	2.7	17.9%	21.1%	2.1	8.3%	11.2%	2.1	8.1%	10.7%	1.7

Source: AEA

US MAJORS' SCHEDULED TRAFFIC

	Domestic			North Atlantic			Pacific			Latin America			Total Int'l		
	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %	ASK bn	RPK bn	LF %
1996	925.7	634.4	68.5	132.6	101.9	76.8	118.0	89.2	75.6	66.1	42.3	64.0	316.7	233.3	73.7
1997	953.3	663.7	69.6	138.1	108.9	78.9	122.0	91.2	74.7	71.3	46.4	65.1	331.2	246.5	74.4
1998	960.8	678.8	70.7	150.5	117.8	78.3	112.7	82.5	73.2	83.5	52.4	62.8	346.7	252.7	72.9
1999	1,007.3	707.5	70.2	164.2	128.2	78.1	113.2	84.7	74.8	81.3	54.3	66.8	358.7	267.2	74.5
2000	1,033.5	740.1	71.6	178.9	141.4	79.0	127.7	97.7	76.5	83.0	57.6	69.4	380.9	289.9	76.1
2001	1,025.4	712.2	69.5	173.7	128.8	74.2	120.1	88.0	73.3	83.4	56.9	68.2	377.2	273.7	72.6
2002	990.0	701.6	70.9	159.0	125.7	67.2	103.0	83.0	80.5	84.1	56.8	67.5	346.1	265.5	76.7
2003	963.1	706.6	73.4	148.3	117.6	79.3	94.8	74.0	80.5	84.2	59.3	70.5	327.2	251.0	76.7
Oct - 04	85.2	63.8	74.9	14.8	12.0	81.4	9.1	7.5	82.0	7.2	4.8	66.4	31.1	24.3	78.1
Ann. chng	4.3%	8.7%	3.1	9.9%	13.1%	2.4	11.5%	10.1%	-1.1	10.0%	14.3%	2.5	10.4%	12.4%	1.4
Jan-Oct 04	847.2	640.2	75.6	138.3	113.6	82.2	86.6	73.0	84.4	79.3	56.1	70.7	304.3	242.8	79.8
Ann. chng	5.6%	8.3%	1.9	11.0%	15.3%	3.1	10.2%	20.6%	7.3	14.6%	15.1%	0.3	11.7%	16.8%	3.5

Note: US Majors = Aloha, Alaska, American, Am. West, American Transair, Continental, Cont. Micronesia, Delta, Hawaiian JetBlue, MidWest Express, Northwest,Southwest, United and US Airways **Source**: ATA

JET ORDERS

	Date	Buyer	Order	Delivery	Other information/engines
Boeing	22 Nov	WestJet	1 x 737-600	2006	
Airbus	08 Dec	Lufthansa	7 x A340-600	2006	
	08 Dec	Vietnam Airlines	10 x A321	1Q/2006 onwards	
	06 Dec	CASG	23 x A320 family		
	24 Nov	EVA Air	1 x A330-200		
Embraer	12 Nov	Air Canada	15 x ERJ-175	07/05 onwards	plus 15 options
Bombardier					

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

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