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Operating lessors: Prospects for the upcycle

After three years of downturn, prospects are looking much better for the lessors, who are determined to make profits during the likely three or four years of the aviation upcycle.

The upturn started in early 2004, off the back of two years of strong passenger growth in some key sectors - LCCs just about everywhere, Asian markets, Europe-Far East and East Europe. But it's demand from Asia-Pacific airlines - both network carriers and LCCs - that is at the heart of the upturn for many lessors. According to Frost & Sullivan, the Asia-Pacific aircraft leasing market was worth some $24bn in 2004, but this will rise to $33bn by 2008 - a compound annual growth rate of more than 8%. China in particular is becoming a vital market for the lessors, and it's estimated that 30% of the Chinese fleet (more than 300 aircraft) is leased from outside of the country, with this proportion set to grow further.

India too is another growing Asian market, and its leased aircraft fleet has tripled in just two years, with GECAS, debis and SALE each believed to have more than $1bn worth of aircraft placed in India. However, if the Indian government goes ahead with a plan to end the tax exemption status for aircraft from April 2006, in effect this will increase lease rates for Indian airlines by up to 50%, so demand from India may slow next year.

But with tight supply of new aircraft (particularly of narrowbodies), growing demand for most aircraft types means that lessors are placing aircraft at rates not seen since before 2001 - and on longer-term contracts. This recovery in lease rates has been quicker than many in the industry forecast, although the bulk of contracts currently on the lessors' books were signed at a time when rates were lower, so the benefits of higher rates is filtering through only slowly into the lessors' financial results.

Nevertheless, growing confidence within the industry is evidenced by the order book. After a handful of orders in 2004, the leasing companies have started to place larger contracts this year, and the top lessors (see table, page 3) now have 662 outstanding orders, compared to 601 as at 12 months ago. As usual, the "Big Two" - GECAS and ILFC - continue their grip on the industry, with a combined fleet of 2,455 aircraft and outstanding orders of 463 (compared with 2,251 aircraft and 468 orders as at a year ago).

However, troubles in the US industry have particularly hit the newer leasing companies that sprang up pre-September 11 in order to take advantage of what they thought was a relatively easy source of profit, combined with advantageous tax benefits. This included companies as diverse as white goods maker Whirlpool, entertainment giant Walt Disney and telephone company AT&T - the latter two of which have had to take around $100m worth of charges for expo-

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sure to carriers such as Delta and Northwest.

Demand from US airlines for leased aircraft is still poor, and Babcock and Brown warns that "the liquidation of a major US legacy carrier under bankruptcy protection could temporarily depress lease rates and aircraft values as their fleets are reabsorbed by other airlines". There's no doubt that lessors with aircraft placed with Delta and Northwest - which entered into Chapter 11 bankruptcy protection in September - are exposed, but the affected lessors are acting more aggressively with troubled US airline than they have done previously when rearranging existing lease deals.

Chris Partridge, Director at Deutsche Bank, says: "The Chapter 11 carriers are increasingly looking to reject older asset types and are additionally trying to convert some of their finance leases into operating leases. However, with supply so tight the lessors are playing hardball this time around, as they know the better quality aircraft at the troubled US airlines can be placed with clients elsewhere in the world, at higher rates."

Fuel prices are the other major oncern, in September this year AWAS said that "once again, the airline industry finds itself teetering on the edge. We believe that the situation, whilst currently just bearable, will begin to deteriorate materially in the face of further oil price increases." On the other hand, AWAS says that growing market uncertainty is leading to a rise in lease rates as airlines seek to increase their adjustable capacity, and this is now beginning to feed through to improved values for more liquid aircraft types.

Ownership changes

As the leasing upturn continues the traditional merry-go-round in the ownership of lessors has started again, with parent companies that have been eager to offload their leasing subsidiaries since 2001 now being able to find a buyer. German bank WestLB had been trying to sell its aircraft leasing subsidiary Boullioun Aviation Services since mid-2004, but eventually found a buyer (Aviation Capital Group) in the summer of 2005. In July, DaimlerChrysler and four German banks also used the upturn to dispose of their stakes in debis AirFinance (which they had previously tried to sell in 2001), with acquirer Cerberus Capital Management paying an unknown sum for the lessor and "all of its liabilities".

Following these transactions, in August this year Morgan Stanley said it would dispose of lessor subsidiary AWAS after receiving "expressions of interest" from certain companies and stating that the aircraft leasing business was no longer part of the investment bank's core business. Morgan Stanley will have to book a loss of at least $1bn on the asset value of its fleet. Many new entrant financial companies see leasing companies as a simple directional play on the assets - i.e. they buy low and hope to sell high.

At the top of the list of potential buyers for AWAS will be private equity funds, particularly those who failed in bids for debis AirFinance and Boullioun, as the relatively old age of AWAS's fleet may put off bids from other lessors. Nevertheless, the AWAS sale will indicate just how bullish the leasing industry really is. The Boullioun disposal took a year to complete, but Morgan Stanley will be hoping for a much speedier sale - depending, of course, on the price it is willing to accept (see AWAS section, below).

General Electric Capital Aviation Services (GECAS)

GECAS, part of General Electric, has a fleet of more than 1,300 owned aircraft, placed with 200 airline customers in 60 countries, and manages another 300 aircraft for clients.

Over the last year GECAS has placed an increasing amount of new orders, bringing its outstanding order book to 153 aircraft, compared with 111 12 months' previously. Thanks to rising demand for narrowbodies, in June GECAS placed an order for 40 A320 family aircraft as well as 20 737NGs, the latter for delivery in 2006-2008 and worth $1.1bn at list prices. Also in June GECAS signed an LoI for 10 A350-800s, (convertible to larger A350-900s) for delivery from 2010 onwards, although this has not been firmed up yet. In the same month GECAS placed an LoI for 20 Emb-190/195s, for delivery from 2006 onwards, which builds on an order placed in

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2000 for 50 Emb-170s.

This year GECAS has opened up a series of new offices around the world, including Mexico City, New Delhi, Sao Paulo and Shanghai - partly in order to take advantage of growing demand in these regions, and partly so that it lessens its reliance on the US market. A Moscow office was opened in 2004 and a Dubai office in 2003, and brings to 22 the number of GECAS offices worldwide. And with a presence in Beijing, Shanghai and Hong Kong, GECAS has been making a particularly big push into the Chinese market. This year it signed contracts to lease four A320 family aircraft to United Eagle Airlines and three A320s to start-up Spring Air, bringing to 80 the total aircraft on lease with 12 different Chinese airlines.

THE TOP 23 AIRCRAFT LEASING COMPANIES

Company	Owned	Managed/ part-owned	Total	Boeing orders	Airbus orders	Total orders
GECAS	1300	300	1,600	79	74	153
ILFC	735	120	855	103	207	310
BCC			500			0
CIT			325	6	51	57
Pegasus Aviation			250	6		6
AerCap			238		22	22
GATX	160	60	220		4	4
ACG			220		11	11
RBS			161	20	20	40
AWAS			155			0
Pembroke	27	114	141			0
Babcock			144			0
ORIX			80			0
BCI Aircraft Leasing			78			0
SALE	59	8	67	20	8	28
Q Aviation			54			0
Aergo Capital			36			0
Bavaria			30	5		5
Guggenheim			20	6		6
Oasis			20			0
Sunrock			18	2		2
Alafco			11		12	12
LCAL			0	6		6
Total	**2,281**	**602**	**5,223**	**253**	**409**	**662**

International Lease Finance Corporation (ILFC)

ILFC is a subsidiary of US insurance and financial services giant AIG, and has a portfolio of 735 owned aircraft, worth approximately $41bn. Traditionally ILFC has had the biggest order book of all the lessors, but although this is still the case, its outstanding orders have fallen from 357 as of 12 months ago to 310 at present, although this still commits the lessor to an investment of more than $22bn.

In October ILFC ordered 20 787-8s and 787-9s (with options for another four aircraft), worth $2.4bn at list prices, for delivery from 2010 onwards. The lessor had been considering its options for new medium widebodies to replace older models in its fleet for more than a year, with the 787 competing against the A350, but ILFC now seems to be hedging its bets as it followed up the 787 order with an order for 12 A350s in November. ILFC also has 10 A380s on order (five passenger and five freighter versions), with two of the former placed with Emirates. ILFC believes it will place the others with Asian airlines, and earlier this year held negotiations with Air China for at least two of the aircraft, which the Chinese carrier would like to put into service prior to the 2008 Beijing Olympics. In June ILFC also ordered 20 737-700/800s, six 777-300ERs and two 777-200ERs, with the 737s being delivered from 2008 and the 777s in 2006-2008.

For 2004 ILFC reported a net profit of $502m, a 1% fall compared with 2003 despite a 10% rise in revenue to $3.3bn. However, in August this year ILFC admitted it needed to restate its historical results following a review by parent AIG that found a series of accounting discrepancies, including incorrect reporting of some lease revenue.

Although this restatement reduced ILFC's net income by just $2.6m in the years to the end of 2004, shareholder equity had to be lowered substantially, and this was a major embarrassment to ILFC. In a filing with the US SEC the company stated that "AIG and its subsidiaries will make a capital contribution of approximately $400m by August 12 2005 to offset the reduction in our shareholders' equity resulting from the restatement." The incident followed the resignation of AIG CEO and chairman Maurice Greenberg earlier in 2005 and series of regulatory investigations.

In the first half of 2005, ILFC posted a net profit of $124m, 4% up on January-June 2004, and revenue of $893m, 15% up on 1H 2004 due to an increase in the owned fleet.

ILFC's lease margin rose slightly in the half-year, by 0.9% (to 19.1%), but the lessor says that "the strengthening of lease rates is starting to materialise in our results … [although] some airlines continue to experience financial difficulties".

ILFC has been reducing its exposure to the US market, which is "under stress", and its proportion of revenue that comes from non-US customers has risen from 86% in 2002 to 90% in 2004. ILFC also has exposure to 11 aircraft placed with Varig, and relations between the two companies have deteriorated since the airline filed for bankruptcy in June 2005. ILFC claims that earlier this year the airline had committed to return all the aircraft and repay all its outstanding lease payments, but in September the Brazilian airline unveiled a new restructuring plan that extended the deadline for repaying debts - which possibly includes those owed to ILFC.

Boeing Capital Corporation (BCC)

BCC has refocused to purely support its parent company's aircraft sales, in effect becoming a "lender of last resort" to new aircraft customers that cannot otherwise finance their purchases (see *Aviation Strategy*, November 2004).

BCC is based in Renton, Washington, and also has offices in Sweden, Ireland, Belgium and Hong Kong. Although BCC includes a Space & Defence division, 95% of BCC's assets are aircraft, which have a current value of $9.2bn. In its 10-Q filing for July-September 2005 BCC states that "while lease rates for aircraft are increasing, values for various aircraft types serving as collateral in BCC's portfolio generally have not increased". And in its third quarter 2005 report Boeing Corporation noticeably says that "the industry's aggregated financial health remains under the shadow of the US network carriers".

Since its refocussing, BCC is reticent about revealing just how many aircraft it has in its portfolio, but the number is believed to have been reduced to around the 500 mark (compared with more than 550 aircraft as of a year ago). However, of its $9.2bn worth of aircraft assets, 717s account for $2.5bn - which given that Boeing is halting production of the 717 in 2006 due to "lack of overall market demand" is a dangerous exposure. All BCC says on the matter is that "should the 717 aircraft suffer a decline in value and market acceptance, such impacts could result in a material adverse effect". The BCC portfolio is also believed to include a number of 757s and MD-11s, again models that have potential for significant falls in valuation.

To make matters worse, "a substantial portion of BCC's portfolio is concentrated among US commercial airline customers". As at the end of September 2005, Chapter 11-protected United was BCC's second largest customer by value, with some 20 aircraft worth $1.1bn (12% of BCC's total portfolio by value).

BCC's exposure to other Chapter 11 or financially troubled airlines includes ATA (where it had placed 12 757s, eight of which are being returned to BCC by early 2006), Varig (where BCC's exposure is nine aircraft worth $323m), Delta ($112m of exposure), and Northwest ($484m). Significantly, in the 3Q 2005 period (July-September 2005), BCC recognised $32m of expenses due to "the deterioration in the credit worthiness of BCC's airline customers, airline bankruptcy filings and the continued decline in the commercial aircraft … asset values".

On the other hand, in the entire 1Q-3Q period BCC also reduced its provision for losses by $26m due to the emergence of Hawaiian from bankruptcy, although BCC also stated that this was partially offset by a decline in the value of the 717s leased to the airline.

Nevertheless, in the third quarter of 2005 BCC paid a $58m dividend to its parent, Boeing, and it has returned a total of $923m over the January 2004-September 2005 period. In the nine months to September 30 2005, BCC reported revenues of $728m, 1% down on the same period in 2004, and a pre-tax profit of $192m, compared with a $148m pre-tax profit in January-September 2004.

Entirely separate to BCC, in June 2005 Boeing created a new leasing and asset management group that is tasked with specifically targeted at drumming up more business with aircraft leasing companies, reportedly to include allowing customers to trade in Airbus aircraft as part of deals for new Boeing equipment.

CIT Aerospace

US-based CIT Aerospace has a fleet of 325 aircraft, with an average age of six years and worth €5.8bn. 208 of these are commercial and 117 are regional aircraft, and they are leased to more than 120 airlines worldwide, with 85% of these outside the US.

A lessening of dependence on the US market was the rationale behind the announcement in August that the lessor was launching CIT Aerospace International, responsible for the European and Asian markets, and to be based in Dublin in order to take advantage of the generous Irish taxation regime for aircraft leasing. Currently 40% of CIT's customers are based in Europe. 46 aircraft worth $1.5bn were transferred from CIT Aerospace to this new international division, and the aim is for this to at least triple by 2008, with the Dublin arm accounting for more than half of the entire CIT portfolio.

CIT targets 10% revenue growth each year, and although analysts speculate it may bid for AWAS, the lessor insists it will achieve its target by organic growth only. However, CIT's lack of interest in AWAS may be more to do with the age of that lessor's fleet, as CIT is trying to reduce the average age of its own portfolio. Jeff Peek, CIT Group CEO, says: "We like to have young aircraft and the average age of the AWAS fleet is almost double ours."

CIT's fleet age is falling as in October the lessor began to sell a number of "older vintage, out-of-production aircraft". Additionally, 57 aircraft are on order. In August CIT ordered 24 A320 family aircraft and five A350s, with a list price of $2.2bn. The A320s will be delivered in 2007 and 2008, and the A350s in 2012 and 2013. CIT has options for further Airbus aircraft, and the lessor is also looking at acquiring aircraft in the 70-90 seat capacity market, with Embraer 170/190s believed to be among the leading contenders.

Along with the fleet-regeneration, CIT Aerospace is also taking over the remnants of the CIT Group's corporate aircraft portfolio (worth around €0.5bn), following the July sale by the CIT Group of leases and loans worth almost €1bn on 380 corporate aircraft (business jets, turboprops and helicopters) to GE Commercial Finance.

Pegasus Aviation

San Francisco-based Pegasus Aviation was launched in 1988 and traditionally focussed on older aircraft, but following an investment of $250m by Oaktree Capital Management and the raising of other finance, the lessor has changed strategy. Earlier this year it ordered six 737-800s, for delivery in 2006-2008, of which four have already been placed with Transaero. Further orders are likely with both Boeing and Airbus as Pegasus further expands its portfolio, which currently stands at 250 aircraft worth $4.6bn. After acquiring younger aircraft valued at £2.5bn over the last two years, the average age of its fleet now stands at just over four years.

Although it has no offices outside of the US, up to a fifth of Pegasus's fleet is with Asia-Pacific clients (it has more than 20 aircraft in China alone), which Pegasus says makes it among the top four lessors in the region.

AerCap

AerCap was previously called debis AirFinance until the lessor was bought from DaimlerChrysler and a consortium of four German banks by New York-based Cerberus Capital Management in July this year for an undisclosed sum. Cerberus also owns 9.2% of Air Canada, acquired in 2004 when the carrier was reorganised.

Schiphol-based AerCap has offices in Ireland and the US, and has a fleet of 238 aircraft, currently placed with 85 clients in 46 countries. At acquisition debis owned 126 aircraft, with another 107 aircraft managed for third parties.

Following the change of owner, AerCap is believed to be analysing the doubling of its fleet within the next two years. 10 A319s, eight A320s and four A321s are currently on order, and in late November Airbus announced that AerCap had signed an LoI to buy 70 A320 aircraft. Negotiations for new orders are believed to be taking place with Boeing, and the lessor is also interested in acquiring used aircraft from other companies. The lessor is looking for a "diversified portfolio" (the current fleet includes MD-80s, Dornier 328s and F100s) although the A320 family and 737NGs are likely to be the focus for orders over the next year. Prior to the change of ownership, in June debis agreed a deal to sell to Avianca the 10 Fokker 50s that it was leasing to the Colombian airline.

GATX Air

GATX Air own 160 aircraft, all of which were placed with approximately 60 customers as at the end of 3Q 2005. The San Francisco-based lessor also manages 60 aircraft for third parties, and has offices in the US, Japan, Singapore France and the UK. However, GATX Air says that although "lease rates on certain aircraft types continue to recover …. as highlighted by the recent concurrent bankruptcy filings by two major US carriers and continued high jet fuel prices, the air market remains volatile".

No aircraft are scheduled for delivery this year, and it has just four outstanding orders, for A320s (although two of these were placed in September this year). In the first three-quarters of 2005 GATX Air achieved a net profit of $10.1m, compared with $9.6m in the same period of 2004. For the whole of 2004 GATX Air reported a net profit of $10m, compared with $2m in 2003. And in April GATX Air partnered with German bank NSH Nordbank to launch an aircraft investment company called Alster & Thames Partners.

Aviation Capital Group

A year ago California-based ACG owned or managed 100 aircraft, but in June it bought Seattle-based Boullioun Aviation Services from WestLB for a reported €2.7bn. The acquisition added more than 120 aircraft (and orders for 11 Airbus aircraft) to ACG's portfolio, which now comprises 220 aircraft and has a value of more than $5bn. ACG claims this makes it one of the top five global lessors, although our table (page 6) shows it is in equal seventh place according to fleet size.

In 2004 ACG recorded revenue of €137m, 33% up on 2003, but this will rise considerably in 2005 following the Boullioun acquisition. ACG - a subsidiary of US insurance giant Pacific LifeCorp - also has offices in the UK and Chile, and it is making a push into the Chinese market through a new Beijing office. Already ACG has 19 aircraft on contract with Chinese airlines, which compares with 24 aircraft placed with US carriers.

RBS Aviation Capital

RBS Aviation Capital was launched by the Royal Bank of Scotland in 2001, but is undergoing a major expansion aimed at turning it into one of the industry's top lessors.

It owns 161 aircraft, placed with more than 100 customers worldwide. These comprise 37 A319s, 20 A320s, three A321s, two A330s, 78 737s, one 777, four CRJs, four Dash 8-300s and 12 ERJ-145s. RBS has increased its fleet by more than 40% in just a year, and its portfolio will increase further following orders placed in July for 20 737-800s, five A319s and 15 A320s, all for delivery between 2006 and 2008.

The RBS fleet has an average age of three years, which the company claims is the youngest of any fleet lessor. RBS is headquartered in Dublin and has offices in the UK, Hong Kong, China and the US.

AWAS

Seattle-based AWAS has 114 employees and offices in the US, the UK, Singapore and Australia. Its fleet of 155 aircraft are currently placed with 76 customers around the globe. However, a year ago AWAS had 176 aircraft on its books, but this has reduced by 12% in just a year. The bulk of this reduction in portfolio came in January 2005 after AWAS sold 12 737-300s, four MD-83s and two Fokker

F27s to undisclosed buyers. The aircraft had an average age of 17 years and were indicative of AWAS's fleet, which even after this disposal has an average age of around 10 or 11 years, and still greater than most of its competitors. The portfolio currently comprises 10 A300s, nine A320s, two A321s, one A330, one A340, 39 737-300s, eight 737-400s, 12 737-500s, four 737-700s, 20 757s, 26 767s, two 747s, one 777, 17 MD-80s and three Fokker 70s.

Morgan Stanley bought AWAS (then called Ansett Worldwide Aviation Services) in 2000 from the TNT Post Group and New Corporation, but its performance since then is unclear. The bank says it will write down the value of AWAS and make an "after tax non-cash accounting charge" of $1bn in the third quarter of 2005 in preparation for its sale, although the relatively old fleet may be inhibit interest from the larger lessors, which have younger portfolios. AWAS is more likely to attract interest from private equity players, although despite the write-down, in order to secure a sale Morgan Stanley may yet have to drop the $2.6bn price tag it currently values the portfolio at.

Pembroke

Pembroke is owned 50% by GATX Capital and 50% by Rolls-Royce and currently owns a fleet of 27 aircraft, with another 114 managed on behalf of clients (compared with 29 owned and 119 managed a year earlier). It is a narrowbody specialist, with 737s and A320 family aircraft making up two-thirds of its total portfolio. Launched in 1993, Dublin-based Pembroke has around 30 customers around the world.

Babcock & Brown

Babcock and Brown operates a portfolio of 144 aircraft, with an average age of just under eight years and with a total value of worth US$3.8bn. The majority of the fleet are narrowbodies, which "have a more liquid market as compared to wider bodied aircraft". As at 30 June 2005 Babcock's fleet was 98% utilised, with aircraft on lease to 52 airlines. Babcock & Brown listed on the Australian Stock Exchange in late 2004, and according to its annual report for last year the aircraft leasing business was "a major contributor to the operating lease group result".

ORIX Aviation

Dublin-based ORIX Aviation is owned by a Japanese financial company and has a fleet of 80 aircraft (compared with 68 a year ago), which with engines is worth more than $3bn. ORIX specialises in narrowbody aircraft, which it says are "relatively versatile and easy to lease". The portfolio comprises 46 A320 family aircraft, two A330s, five A340s, 15 737s, two 747s, two 767s, one 777 and seven ATR72s.

Singapore Aircraft Leasing Enterprise (SALE)

SALE is an Asian leasing specialist based in Singapore, although it also has offices in the UK and US. It currently has a portfolio of 59 owned aircraft (with another eight managed for clients), with assets totalling more than US$2.6bn.

A year ago SALE had 14 aircraft on order - all from Airbus - but in the last 12 months it has doubled its order book as the leasing market has picked up. In May SALE placed a firm order for 20 737-800s, although these are convertible to 737-700 or 737-900X variants. The first aircraft will arrive in the fourth quarter of 2006, with deliveries due to be completed by 2009, and 20 further aircraft are on option. According to Robert Martin, CEO of SALE, the order was placed as a "logical diversification of the SALE portfolio", which currently comprises 42 Airbus aircraft and 17 Boeing aircraft. It owns just 10 737s at present, most of which were acquired through sale and leaseback deals with airlines. In particular the 737s will enable SALE to offer a better choice of narrowbodies to the raft of LCCs launching or planning to launch in Asia.

The company also has outstanding orders for eight A320s, all of which will be delivered by the end of the second quarter of 2006.

Earlier this year SALE considered ordering Embraer 190 regional jets, but reportedly decided against this after not being able to get the discount it wanted.

In order to pay the deposits required for the Boeing order, in the summer SALE issued US$47m worth of bonds in the Singapore market, the latest of approximately US$4bn of funding the company has raised since it was founded in 1993. SALE is currently owned by Singapore Airlines (35.5%), WestLB (35.5%), Temasek Holdings (14.5%) and by the Government of Singapore Investment Corporation (14.5%) - and although WestLB sold Boullioun this year, claiming it was not part of core operations, its holding in SALE is believed to be more longer-term.

Guggenheim Aviation Partners (GAP)

GAP was launched by US-based Guggenheim Capital in 2003 with just $50m, but has quickly built up a fleet of 20 aircraft, 15 of which are 747-400s. Its portfolio is placed with customers, other than two 747-400 Combis, which are scheduled to be converted to Boeing Converted Freighters (BCFs).

GAP has ordered 17 aircraft over the last year. In July Guggenheim ordered six 747-400ER freighters, at a list price of $1.4bn and for delivery in 2006 to 2008. Four of these have been contracted to Martinair, for delivery from 2007, and the other two are going to Iceland-based Bluebird Cargo. This order followed the purchase of five 747-400s in October 2004 for conversion into BCFs. And this October GAP bought six 737-400s, three 757s and a 767-300 from an undisclosed seller, and all but one of these aircraft (a 757) had been placed with airlines within a few weeks.

Oasis

After reporting pre-tax profits of $3m in 2004 (double those in 2003 but based on a 12% drop in revenue), Abu Dhabi-based Oasis International Leasing has been raising further funding this year in order to finance an expansion of its regional leasing business. In July it added $220m to the $190m it had already raised since it was launched in 1997 by the Abu Dhabi investment company, BAe and the Gulf Investment Corporation.

Oasis has a portfolio of 20 aircraft - one A319, six A320s, one A321, four 737s, two 777s, two CRJ-100s and four Emb-120s - that are placed largely with Middle Eastern or North American customers. The latest fund-raising is being used to fund Oasis's largest ever contract: a $1bn deal for eight A330-200s for delivery to Middle Eastern airline Etihad Airways in 2006-2007.

Other lessors

Other lessors include Munich-based Bavaria International Aircraft Leasing - originally started as a charter airline back in 1958 and currently owned by German corporate group Schorghuber. Bavaria currently operates a fleet of 30 aircraft (although four are currently unplaced), all of which are A320s, 737s or 717s. In January 2005 Bavaria ordered six 737-700s worth around $330m at list prices, with six further aircraft on option. The aircraft will be delivered by 2007.

US-based Q Aviation has a fleet of 54 aircraft and opened an office in Singapore this year, while Dublin-based Aergo Capital has a fleet of 36 aircraft, all of which are older model 737s or MD-82s. BCI Aircraft Leasing has a fleet of 78 aircraft, most of which are old generation 737s, while at the Dubai Air Show in November Airbus announced an order worth $2.9bn for 12 A350s, plus six options, from Kuwait-based lessor Alafco, which specialises in Sharia-based leasing and currently has a portfolio of 11 aircraft.

Sunrock Aircraft Corporation, a subsidiary of Nissho Iwai Corporation, has a fleet of 18 exclusively Boeing aircraft and has two 737s on order, while Hong-Kong-based new entrant LCAL (Low-Cost Aircraft Leasing) placed an order for six 787-8s at the Dubai air show in November.

US Airways/America West: "Full-service, low-cost, low-fare"?

US Airways and America West closed a merger transaction on September 27 that pulled US Airways out of Chapter 11 bankruptcy and created an AWA-managed nationwide carrier described as the "first full-service, low-cost, low-fare airline". The deal was notable for its speedy completion, for raising a staggering $1.7bn in new equity investment and partner support and for its initial unenthusiastic reception by Wall Street analysts. How did the airlines manage to persuade savvy investors to part with their money, given the difficult industry environment and dismal history of large airline mergers in the US? How will they meet the challenge of labour integration? Is the new US Airways a likely long-term survivor?

Under the "reverse merger" type transaction, which took only four months to complete since it was announced on May 19, America West Holdings (the acquirer) became a wholly owned subsidiary of US Airways Group and will give up its name. The reorganized company began trading on the New York Stock Exchange (NYSE) on September 27 under the symbol "LCC".

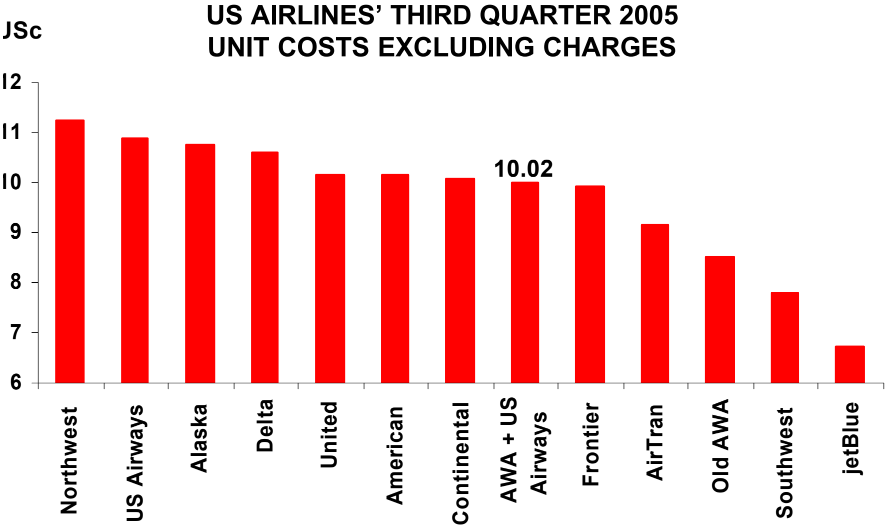
US Airways and America West plan to fly on separate operating certificates for up to two years, with their own maintenance and training regimes, while employee seniority and labour contracts are sorted out. However, the airlines are already codesharing, have combined their FFPs and airport clubs and expect to have combined operations at most of their 38 common-use airports by year-end. The plan is to roll out completely new branding and eliminate the AWA name in the first quarter and have a single web site by April. Combining reservations systems is likely to take until early 2007.

The deal offered a lot to AWA. Its shareholders received the largest single stake in the new entity (37%); the rest was divided between outside investors who provided financing (52%) and US Airways' unsecured creditors (12%). AWA also received the largest number of board positions: six out of 13, with US Airways designating four directors and outside investors taking up three positions. AWA's chairman/CEO, Doug Parker, took over at the helm of the new US Airways, whose management team is made up of roughly two-thirds AWA and one-third US Airways executives. The reorganised company is based at AWA's headquarters in Tempe, Arizona.

In supporting the deal, AWA's controlling shareholder TPG Partners and the company's board were swayed by the argument that the merger would enhance AWA's long-term strategic position. Even though AWA was already a low-cost carrier - it had always had low costs and since 2001 had also transitioned to an LCC-style simple low-fare structure - its geographically limited, leisure oriented network posed a hurdle to long-term survival as a stand-alone entity. The deal with US Airways offered something AWA had coveted for years: access to the higher-yield East Coast.

US Airways' general shareholders received nothing in the transaction, having seen their shares wiped out in Chapter 11. While secured creditors recovered 100% of their claims, unsecured creditors recovered only 3-17%. Special deals were negotiated with the ATSB, GE Capital and Airbus. Retirement Systems of Alabama (RSE), which financed US Airways' first Chapter 11 reorganization in 2002-2003, lost its entire $240m investment, though the merger facilitated a graceful exit for RSE's chairman David Bronner. US Airways' CEO/president Bruce Lakefield, who worked closely with Doug Parker to push the merger through, is serving as vice-chairman/board director of the new entity.

For US Airways, the deal provided a new lease on life. Although the airline did reduce debt and improve liquidity in Chapter 11, even succeeding in substantially reducing labour costs and lining up new equity fund-



Source: Calyon, December 8 2005

ing, it was struggling to come up with an acceptable business plan in the high fuel cost environment. Many in the industry had expected US Airways to liquidate in its second stay in bankruptcy protection.

This was probably the key to getting the merger approved on the US Airways side - it was the airline's last chance. Nevertheless, it was a major accomplishment that the parties managed to persuade everyone that the deal was worth doing.

Industry experts have attributed the success of the transaction to the fact that the airlines had a clear plan, that they acted quickly and that they avoided labour trouble at the outset.

Parker's vision, proven track record and presentation skills must have also played a part. Aged 43, he has been described as "smart, energetic and eager". He has presented the new entity very effectively as a new type of "hybrid LCC", an airline of the future that will be copied by others. This airline has all of the prerequisites for survival: a strong cash position, a robust business plan, a low cost structure and a strong network. As Parker bragged at Wing's Club in September: "No-one has been able to come up with this amount of capital, cost structure and route network" and that "this airline has staying power".

As Parker has frequently pointed out, two things happened that were critical to getting the merger completed and which will also help make the new entity successful. The first was Chapter 11, which enabled US Airways to get the right cost structure and eliminate key differentials with AWA. Second, the substantial additional financings, equity investments and partner support were vitally important, giving US Airways strong cash reserves.

Chapter 11 was the key

US Airways ended up in Chapter 11 again in September 2004 largely because during its first reorganisation it had failed to sufficiently anticipate the growth of LCC competition in its markets. Consequently, in its second Chapter 11 the airline focused on and succeeded in reducing its high legacy labour costs to effectively LCC levels. This was done by renegotiating union contracts, to obtain further concessions, and by terminating defined benefit pension plans for the flight attendants and machinists in January 2005 (following the termination of the pilots' plan in the first Chapter 11). Overall, the two Chapter 11 visits reduced labour, pension and benefit costs by around $2bn annually.

The labour cost savings were in addition to cost savings achieved in Chapter 11 through cutting overheads, including reducing management payroll, by renegotiating various contractual obligations and by rationalising the fleet.

Chapter 11 transformed US Airways into an attractive - or at least lower-risk - merger target for AWA. While removing aircraft and capacity made possible to avoid duplication and permitted synergies, having similar labour costs will help smooth workforce integration. As Parker explained in a recent presentation, "the bankruptcy process allows things to happen that will be friendly to consolidation.

The history of the airlines' dealings, outlined in prospectuses and SEC filings, illustrate how important Chapter 11 was in paving the way for the merger. US Airways and America West first held discussions and undertook due diligence in February-July 2004, but those talks concluded that "a number of issues, particularly related to labour, pension and benefit costs, made a merger impracticable". The talks were revived five months later "in anticipation of US Airways' success in significantly reducing its labour costs", following its second Chapter 11 filing.

The airlines also noted in December 2004 that the bankruptcy gave US Airways "greater flexibility to combine its network with AWA's network in a more efficient and cost-effective manner" and that the improved liquidity would also help a potential combination. Negotiations on a merger resumed in earnest in January 2005, resulting in the May 19 agreement.

The new US Airways will obviously not have unit costs rivaling those of JetBlue, Southwest and AirTran. Analysts such as Merrill Lynch's Mike Linenberg and JPMorgan's Jamie Baker have estimated that its CASM will be in the middle of the pack - lower than those of most legacy carriers but higher than most LCCs'.

New funding and partner support

The merger was possible only thanks to substantial new investment and financial assistance from a multitude of parties in the context of the Chapter 11 reorganisation. After attracting $867m in new equity financing and another $830m in partner support, US Airways had an ample $2.6bn in cash (of which $1.7bn was unrestricted) at the end of October. This was about 25% of annualised revenues - at the high end of the industry range, with only Southwest, JetBlue and AirTran having better cash positions. The reserves should enable US Airways to avoid a cash crisis even if fuel prices stay high through 2006.

However, as the credit rating agencies have pointed out, US Airways remains highly leveraged, with a debt load of about $3.5bn, or over $9bn including operating leases. The lease-adjusted debt-to-capital ratio of 95% is in line with legacy ratios but much higher than the mid-70s typical for LCCs (or Southwest's 40%). On the positive side, total leverage will fall modestly as the leased fleet shrinks further, but debt maturities will still be significant in 2007-2009.

In summary, US Airways benefited from the following new equity investments, partner support and other transactions in connection with the Chapter 11 exit and the completion of the merger:

• New equity funding
The total of $867m in new equity, which is the largest amount of new equity ever raised by a US airline, far exceeded the $375m stipulated by the merger agreement. The funds came from four established investment firms (Wellington, PAR, Tudor and Peninsula) and two airline partners (ACE and Air Wisconsin), as well as a September public share offering that raised $180m.

• Convertible debt offering
In late September US Airways also raised $139m in net proceeds from a private placement of senior convertible notes due in 2020.

• Payments from credit card partner
Under a new agreement signed in August, AWA's credit card partner Juniper Bank made a $130m bonus payment and pre-purchased another $325m worth of miles from US Airways, in return for becoming the exclusive co-branded credit card provider for the merged entity.

•Loans from Airbus
Airbus provided US Airways two loans totaling $250m, in addition to rescheduling deliveries and promising additional backstop financing for A350s.

• Sale/leaseback transactions
US Airways received $125m in additional support, primarily from aircraft lessors, in the form of sale/leaseback transactions involving various Airbus aircraft.

• Agreement with GE Capital
Under a complex deal, GE Capital agreed to retire US Airways' bridge loan facility, buy and lease back 21 aircraft and engines, allow $28m new borrowings, restructure 59 leases to market rates, provide financing for current and growth aircraft and waive certain penalties. In return, US Airways paid GE $125m in

cash, accepted certain modified leases and returned early 51 aircraft and engines.

• Asset sales to Republic
US Airways raised $100m from the sale of Embraer RJs and airport slots to Republic Airways, its regional partner. Republic purchased or assumed the leases of 28 E170s and will continue to operate them for US Airways.

• Restructuring of ATSB loan guarantees
The ATSB has been highly accommodating to US Airways, allowing the airline to continue using the cash collateral that secured the government-guaranteed loan while in Chapter 11 and in July promptly approving the merger transaction. In September new terms were negotiated for US Airways' and AWA's ATSB-backed loans, which at that time totaled $832m. The loans were kept separate, with different repayment schedules and interest rates, but new requirements were introduced about using proceeds from asset sales to pay down the debt. Subsequently, in late October, the loans were sold to fixed-income investors, meaning that the ATSB no longer has an interest in US Airways' debt.

• Deal with the PBGC
The Pension Benefit Guaranty Corporation (PBGC), which has been trustee for US Airways' three terminated defined benefit pension plans since February 2005, reached a settlement with US Airways on its claims that totaled $2.7bn. Under the deal, the PBGC received $13.5m in cash, a $10m unsecured promissory note and an ownership stake in the reorganised carrier. The latter amounts to 4.9m shares, representing 70% of the common stock allocated to unsecured creditors.

KEY FIGURES

	US Airways	America West
Passengers (2004, 000s)	42,400	21,119
Pax Load factor	75.1%	77.4%
Revenue (2004, $m)	5,482	2,327
Net result	-611	-87.6
Yield/RPM (US cents)	12.5	7.7
Cost/ASM (US cents)	10.8	7.8
Pay/employee ($)	79,240	51,503
Av. Aircraft utilisation (hrs per day)	9.4	10.9
Av. stage length (miles)	782	1,053

Source: The Airlne Monitor, December 2005

A "hybrid LCC"?

The US Airways/AWA combination is not really aiming for anything new with its "hybrid" legacy/LCC product and market strategy, because LCCs in the US have moved further and further away from the traditional Southwest model. For example, many LCCs now use both point-to-point and hub models, operate to both secondary and primary airports, operate more than one aircraft type, have FFPs and in many cases provide a higher quality and better service than the legacy carriers. However, the new US Airways is clearly a few notches closer to the legacy type than existing LCCs.

The new entity offers a combination of premium amenities not available on other LCCs, including a global FFP, airport clubs, assigned seating, first class cabin and the hourly US Airways Shuttle between Boston, New York and Washington. The aim is to provide "excellent value" with a "competitive, simplified pricing structure", essentially replicating the fare structure that AWA put in place in March 2002. Merrill Lynch's Linenberg suggested that the brand could be characterised as "business casual".

US Airways will stand apart from other LCCs because of its scale - it will be the fifth largest domestic airline, with a truly nationwide network - and because of its international franchise. The airline offers on-line service to 44 destinations in Europe, the Caribbean, Mexico and Canada, plus nearly 800 destinations in 139 countries through the Star Alliance. The airline will continue to operate hubs in Charlotte, Phoenix and Philadelphia, with secondary hubs or focus cities in Las Vegas, Pittsburgh, Boston, New York LaGuardia and Washington Reagan National. Two wholly owned subsidiaries operating as US Airways Express will continue to feed into the hubs.

The airline expects all of that to differentiate its service from other LCCs, allow it to strengthen customer loyalty and attract new traffic. It may succeed, but it is worth bearing in mind that, as Southwest and JetBlue have demonstrated, real success in the marketplace for LCCs is the result of hard-to-replicate factors such as great leadership, strong corporate culture and high employee morale.

Parker is highly regarded both in the industry and on Wall Street, having led AWA's transformation since 2001. The key tenets of his management philosophy seem exemplary - diligent cost control, an analytical approach to revenue management, operational integrity and employee focus. However, he will have the enormously challenging task of combining two very different corporate cultures and implementing the merger without adverse effects on employee morale.

Merger synergies

In early December US Airways estimated that it would incur about $300m in one-time costs related to the merger over two years, including information systems, severance, training, aircraft painting and configuration and other transition expenses. About $90m of the total will have been spent by year-end, with the remainder to be spent mainly in 2006.

However, those costs would be handsomely offset by the merger synergies, which the airline predicts will build up to $600m annually by 2007. This figure has been criticised as over-optimistic, given all the uncertainty in the competitive environment; however, the sharper than expected capacity cuts by competitors on the East Coast in 2006 have, for the moment at least, made that figure look more achievable.

The $600m annual synergy total would be made up of $250m cost savings, $175m cost savings or revenue enhancements resulting from fleet and route restructuring and $175m revenue synergies. The cost savings, which look likely to be achieved in full, include a reduction in the administrative overhead, insourcing of information technology and combining facilities. US Airways has eliminated 31% of management positions at director-level and above and will close the old Crystal City headquarters by April.

US AIRWAYS/AMERICA WEST MERGER: ANTICIPATED TRANSITION COSTS AND SYNERGIES ($m)

	2005	2006	2007
Transition costs* (total $300m)	(90)	(210)	0
Ramp-up of synergies			
Route	0	175	175
Revenue	22	132	175
Cost	18	186	250
Total	40	493	600
TOTAL BENEFIT (COST)	**(50)**	**284**	**600**

Note: * = Transition costs include information systems, severance, training, aircraft configuration and marketing.
***Source**: US Airways*

The $175m fleet/route-related synergies will come from right-sizing the total fleet, eliminating unprofitable flying, down-gauging aircraft to better meet demand and adding Hawaii service. Specifically, US Airways is parking 60-plus mainline aircraft in the near-term, rejecting expensive leases and replacing more 737 flying with 70-seat and 90-seat RJs.

Hawaii is a strong, relatively high-yield leisure market that has proved attractive to many airlines in recent years, including the Southwest/ATA codeshare alliance. US Airways introduced the first phase of its Hawaii expansion in mid-December: daily 757-200 flights linking Phoenix with Honolulu and Kahului. A second phase, introducing service from Las Vegas and more destinations and frequencies from Phoenix, will follow in March.

The $175m revenue synergies are envisaged through enhanced city presence, improved connectivity and better asset utilisation. This is the most questionable category, because it essentially assumes a market share shift from competitors. Then again, the East and West route networks are so nicely complementary that one would expect there to be revenue benefits through improved connectivity.

Much will depend on who the future competitors are. Merrill Lynch's Linenberg made the point in a recent research note that while Independence Air's shrinkage at Washington-Dulles and possible liquidation in early 2006 is obviously a major positive for US Airways, it could quickly turn into a negative if, say, JetBlue started to build a position at Dulles. Linenberg said that his 2007 forecast gave US Airways credit for only half of the targeted $175m revenue synergies.

The integration challenge

US Airways' biggest challenge over the next two years will be labour integration - the stumbling block in many past airline mergers. Seniority issues, always tough to resolve, pose a particular hurdle for these airlines because old-established US Airways has a much more senior workforce than 22-year-old America West, and America West is the acquirer.

There are two mitigating factors. First, two of the key groups - the pilots and the flight attendants - are represented by the same unions, which have established procedures for integrating seniority lists. Second, some of the contracts and wage levels are apparently fairly similar. In JPMorgan analyst Jamie Baker's estimates, mechanics' wage rates are nearly identical, while pilots' wage rates are within about $10 per hour of each.

However, US Airways' management has conceded in recent speeches that addressing issues of pilot seniority has been a difficult task. There are no obvious solutions.

On the positive side, the two airlines reached a transition agreement with their respective ALPA-represented pilot groups in mid-September that will govern merger-related aspects of their relationships until there is a single collective bargaining agreement. Negotiations on a combined contract kicked off in mid-November, with the somewhat ominous message coming from the pilot groups that they had mapped out a strategy and it involved getting their fair share of the rewards arising from the merger synergies.

US Airways has also reached transition agreements with several of its smaller unions, most recently with the communications Workers of America (CWA) and the Teamsters, which represent passenger service employees.

The management is counting on the workers bearing in mind that the merger means lasting job security for a large number of employees. Morale among the old US Airways workforce, which earlier this year was at an all-time low after repeated concessions, pension plan terminations, job losses and liquidation fears, has evidently improved in recent months.

Labour integration may be further complicated by the two companies' vastly different cultures, with US Airways having a typical staid, businesslike East Coast culture and AWA a more relaxed West Coast, Southwest-style fun culture. Among various measures, the merged entity has appointed a "VP of culture".

Aside from the labour issues, the integration of systems, processes and facilities are all challenging tasks. If not expertly executed, they can lead to higher costs or customer service problems.

THE COMBINED FLEET

	US AIRWAYS		AMERICA WEST	
	In fleet	On order	In fleet	On order
A318				15
A319	57		34	8
A320	24	6	57	10
A321	28	13		
A330	9	10		
A350		20		
737-300	60		35	
737-400	43			
757-200	31		13	
767-200	10			
Total	262	49	139	33

Growth and financial prospects

To its credit, US Airways has not only removed 59 aircraft or 15% of its fleet through the merger but has chosen not to grow over the next couple of years, preferring instead to focus all of its efforts on integration. This is admirable and likely to pay off financially, though the company's share price may suffer.

As a plus point, all of the 59 aircraft being removed are apparently leaving North America, which means that US Airways will have contributed meaningfully to the industry capacity reduction.

US Airways expects to operate a 361-strong mainline fleet in 2006 - 198 A319/320/321s, 100 737s, 44 757s, ten 767s and nine A330s - plus 241 RJs and 112 turboprops. This compares with 411 mainline aircraft operated by the two airlines at the end of June.

Although the merged airline is taking a few AWA-ordered A320s by February, the A320s and A330-200s that the old US Airways had on order will now not arrive until 2009-2010. To rationalise international flying, the airline will begin transitioning to an all-A350 fleet in 2011; a firm order for 20 A350s was signed at the end of November. On the regional front, US Airways already operates 38 90-seat RJs and plans to grow that fleet while shrinking its 50-seat fleet.

The company recently reiterated its original early-summer projection that it will be profitable in 2006 excluding one-time merger-related costs. Wall Street analysts, who generally did not agree with that 2-3 months ago, now accept it more. The current consensus estimate is a loss of 6 cents per share - effectively a breakeven - before one-time items in 2006, with the forecasts ranging from a loss of $2 to a profit of $2.80.

Somewhat confusingly, the current profit forecast was made when the crude oil price was only about $47 a barrel. By September, when oil had surged to the high-60s, the forecast looked out of date, even though US Airways insisted that the revenue environment had improved enough to compensate. In the past couple of months, as the industry capacity cuts have gathered pace, unit revenues have surged and oil prices have moderated, the original forecast again looks realistic.

US Airways has recorded double-digit RASM growth in recent months, well exceeding the industry average. The consensus now is that it is uniquely well positioned to benefit from competitors' capacity cuts in the East Coast. In the longer term, however, there remains considerable uncertainty. Could Southwest and JetBlue make serious trouble in US Airways' markets? And what will be Virgin America's impact in the West?

By Heini Nuutinen
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Cathay Pacific: Reduce costs, retain revenues, build Hong Kong hub

Cathay Pacific's strategy has three main planks, first to reduce its cost base, second to preserve its revenue premium, and third to build the Hong Kong hub. Its strategic direction is buoyed up by a complex range of subsidiaries and cross-holdings in aerospace-related companies that provide strong secondary revenue streams to and through Cathay Pacific.

Unit cost targets

Reporting a year on year 239% improvement in net profits of HK$4.4bn (US$565m) on a HK$39.1bn turnover, Cathay has set itself a target of reducing unit costs per ATK from the 2004 year end level of HK$2.07 to HK$1.80 by 2007. This target was affirmed in the interim results presentation which was made in August 2005 for the first half of the year despite actual costs/ATK rising to HK$2.19 largely because of the increase in fuel costs. Tony Tyler, Cathay's Chief Operating Officer, downgraded the hopes of reaching a cost base of HK$1.80 as now a "goal rather than a target".

Historically Cathay has covered about one third of its fuel buying forward for a six-month period, using a model developed by

Morgan Stanley. Since the spike in oil prices Cathay has abandoned this strategy and chosen not to hedge at all. Cathay has recently decided to take a new approach to fuel hedging. This has involved the airline taking out a series of collar and caps options to cover once again about a third of their fuel requirement, giving the airline a more defensive position which should ensure some protection on any major spikes in the fuel price.

With fuel accounting for some 30% of total costs, Cathay is redoubling its efforts to make cost savings elsewhere. The next largest cost case is personnel. Growing the airline assists here as new staff are recruited at lower than average salaries. A major initiative is streamlining the airline's supply base. A special task force has been set up to ensure that all new contracts with suppliers lead to a "continuous improvement" in the airline's cost base.

Fleet

On December 14, Cathay placed a firm order for 12 777-300ERs and is also leasing four 777-300ERs and three A330-300s from ILFC in a decision that has been six years in the making. Tyler says that the six-year delay has benefited Cathay as there have been significant advances in both planes' in service development. This delay especially benefits Cathay, which has to operate its aircraft at the limit of their payload range due to Hong Kong's geographical position.

The airline would appear to be a natural customer for the A380, especially as many of its nearest competitors have ordered the aircraft, notably Singapore Airlines, Malaysian, China Southern and Qantas. Cathay chose to model the impact of adding an additional A340 frequency versus putting an A380 on a given route. Larger financial benefit was gained from the additional A340 frequency and this has been borne out at London Heathrow where Cathay has just been awarded a new slot which will allow it to offer four daily services. With this frequency Cathay feels comfortable that its offer will be superior to a potential Virgin Atlantic A380 operation on the route.

Cathay will assess the merits of the A380 versus the 747Adv, but it has appeared to rule out being a launch customer again for a new type after having experienced problems in the past with both Boeing and Airbus introductions. Cathay was the lead operator of the Rolls powered 747-400 and the Trent powered A330.

Route development

Cathay is presently trying to obtain passenger rights to fly to Shanghai and wants to increase frequency on its Hong Kong - Beijing service from its current level of three flights per day.

Increased access to Chinese markets requires "patience". Cathay is working with Dragonair and Air China to drive this process forward. A long-term shareholder in Dragonair, Cathay has recently purchased a 10% stake in Air China at a cost of US$400m. Cathay's action was a significant factor in helping make the Air China IPO a success. Air China and Cathay now codeshare and participate in each others' FFPs.

Cathay intends that Hong Kong's home carriers, itself and Dragonair, will continue to play a vital role in maintaining Hong Kong as the regional hub and gateway to China. Hong Kong is likely to remain for the foreseeable future the hub with the most connecting opportunities to China and Cathay is determined to ensure the airport keeps ahead of its nearest competitor at Guangzhou.

The carrier's busiest route is Hong Kong - Taipei, on which Cathay offers 16 daily flights. The absence of any direct flights between China and Taiwan means that car-

CATHAY PACIFIC'S FLEET

A/C family	Fleet	Orders
777	17	13
747	35	0
A330	26	3
A340	18	0
Total	**96**	**16**

riers such as Cathay, Dragonair and Air Macau provide the air link between the two countries. Although there is no immediate prospect of direct flights being permitted, it would appear that the current political climate would suggest that they may be allowed to in the not too distant future.

Cathay acknowledges this would impact the airline, but believes that it will still be an important player in the market given that a total of 48 Chinese cities are served out of Hong Kong and this could not be replicated from Taiwan. Also Cathay contends that a Sino - Taiwanese agreement would be a major boost to economic growth in the region and significantly stimulate traffic growth. Hong Kong and the US have been in protracted talks about "open skies" for many years and the talks are ongoing. Cathay has taken a consistent line, it has no problem with progressive liberalisation but considers the US line unfair. Cathay sees little use for any beyond-US traffic rights it receives. However if US carriers were to receive fifth freedom rights beyond Hong Kong these could be damaging to Cathay's business, particularly concerning is the action that cargo operators such as Fedex and UPS could take.

Cargo accounts for about one third of Cathay's revenues. Tyler says that "very few" of Cathay's flights would be profitable without the contribution of cargo. With Fedex and UPS primarily making their money from carrying small packets, Cathay is concerned that these carriers, who are making aggressive inroads into the South East Asian area, could price the carriage of general cargo at much lower rates.

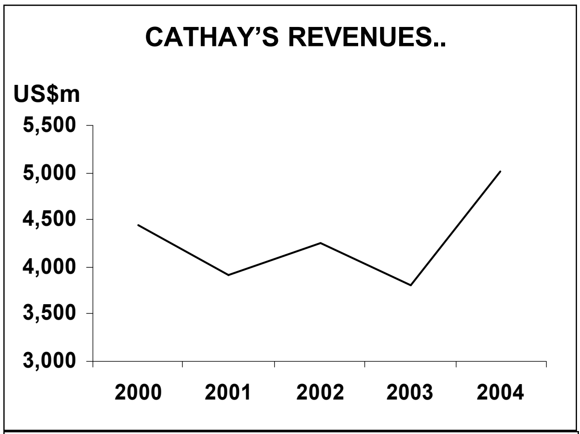
Alliances

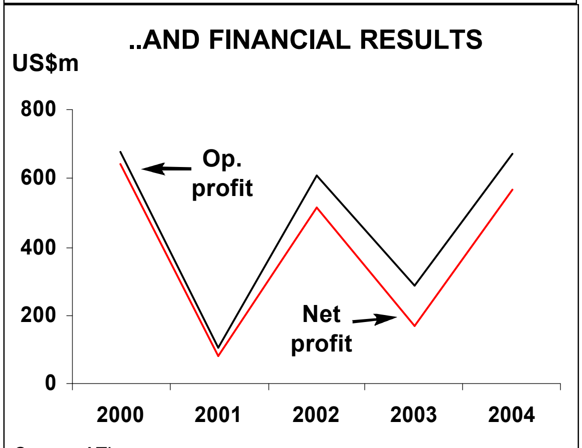
Cathay is a founder member of the oneworld strategic alliance. Tyler describes oneworld as an "alliance of successful airlines", driven for the benefit of the participating airlines, suggesting that some other alliances are driven more for the benefit of the alliance itself.

The oneworld alliance has grown this year with the announcement of new members Royal Jordanian, Malev and JAL. Although oneworld members have indulged in some joint purchasing in order to save costs, Tyler says the vast majority of the benefits are derived from increased revenue. Although Cathay and BA compete aggressively with each other the codeshare feeds (from/to Europe and Asia) they provide each other is very valuable.

Through a series of straight rate and prorate agreements Cathay takes many BA passengers on to Taipei for "not very much" but in turns pays BA not very much for the European passengers it feeds onto Cathay flights at Heathrow. These agreements allow Cathay to compete effectively for European traffic with Air France and Lufthansa. And with an annual passenger load factor of 77.3%, Cathay has the capacity to take some low yield traffic.

The co-operation with BA stops short of the sort of Joint Service Agreement (JSA) that BA has with Qantas on the kangaroo





Source: ATI

route. It has been considered, but Cathay regards the regulatory price it would have to pay for such an agreement, for example a loss of slots at Heathrow, would be too high. Indeed, because Hong Kong is a designated stop on the kangaroo route, Cathay would probably have to include Qantas in such an agreement adding to the complexity.

With Cathay owning minority stakes in both Dragonair (17.8%) and Air China (10%) there is always speculation that the airlines may consolidate at some time in the future. Cathay has no plans to increase the size of the stakes it already holds in either carrier. Tyler says that Cathay has no plans to invest in any carrier although if ownership and control would be available then a review of this stance may occur. It may well be the result of a successful outcome in the EU - US open skies talks that may be the catalyst to such a change taking place.

Secondary revenue streams

Cathay is unusual in the amount of stakes it holds in non-airline businesses. The primary business of Cathay Pacific Catering Services (CPCS), wholly-owned by Cathay, is flight kitchens at Hong Kong airport. CX Catering also has smaller kitchens in Canada, Cebu in the Philippines, Vietnam and Taipei in Taiwan.

HAECO is a separately listed company on the Hong Kong stock exchange in which Cathay retains a 27% stake. Cathay's major shareholder, the Swire Group hold a 59.9% stake in HAECO giving the two effective control.

HAECO is Asia's largest aeronautical engineering company in terms of capability. It performs major airframe checks on 747s, 777s and the A320, A330 and A340 aircraft and provides line and base maintenance at Hong Kong airport, and performs component overhauls at a cheaper external site.

The business is very successful, producing profits of HK$451m (US$58m) on turnover of HK$2153m (US$277m) in 2004. Major checks are performed in 14 days compared to a 21-day wait for a comparable check at some US-based maintenance bases.

The success and reputation of HAECO (which was founded in 1950) has led to a couple of offshoots. A joint venture founded in 1997 between HAECO (45%), Rolls-Royce (45%) and SIAEC (SIA Engineering Company - 10%) called HAESL provides aero engine repair and overhaul services based in Hong Kong's New Territories. Tyler describes HAESL as "the best managed joint-venture business in China".

TAECO (Taikoo Xiamen Aircraft Engineering Co.) in which Cathay holds a 9% stake, but also has exposure through HAECO's 54.5% stake, has been set up in Xiamen which offers labour rates well below those in Hong Kong. The company has just opened a fourth hangar and now can simultaneously accommodate eight widebodies and three narrowbodies. TAECO has won a contract from Boeing to perform 747 freighter conversions. Boeing has committed to converting 34 747-400s into Special Freighters and options exist on a further 29 aircraft. The first 747SF of six ordered in January 2004 was delivered to Cathay on December 19, which marks the first time that Boeing has completed an aircraft certification outside the USA. The aircraft will be added to Cathay's current cargo fleet of 13 747-200/400Fs.

Cathay's other major shareholdings are in Air Hong Kong in which it holds a 60% stake and holds a 53% stake in the CRS provider, Abacus. Cathay has had approaches to sell off its FFP, Asia Miles, but has no intention to sell the business.

Distribution

Another unusual feature of Cathay is its strategy towards distribution. Tyler says that Cathay's online internet sales are in the "low single digit figures". Instead Cathay relies on the "very efficient" Hong Kong travel agency businesses for most of its sales. Many tickets are sold on a net fares basis with travel agents putting on their own mark-up. Cathay is unconcerned with its low level of internet sales, and is convinced that if it alienated the travel agents then it would lose revenue. Some distressed inventory is sold via the internet, "fare 48" being fares available for a two-day period.

LCC competition

Although Cathay is a primarily long-haul carrier it is not immune from competition from LCCs. On one of its trunk routes, Hong Kong-Singapore, JetStar Asia operate a double daily service. In the past fares on this route would be sold at around HK$ 2,500, today Cathay has to offer fares at HK $900. This is having a knock-on effect in other markets. With low fares available in the Singapore market, Cathay feels obliged to offer lower fares elsewhere, for example to Bangkok where fares are as low as HK$ 1,800.

On the Hong Kong-Singapore route, Cathay is relying on its ability to carry a large share of business traffic, 30 tonnes of cargo and the offer of some low fares to keep a lid on LCC capacity.

		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	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
	Oct-Dec 04	656	714	-58	-45	-8.8%	-6.9%	8,774	6,399	72.9%	3,998	9,433
	Year 2004	**2,724**	**2,804**	**-80**	**-15**	**-2.9%**	**-0.6%**	**35,849**	**26,121**	**72.9%**	**16,295**	**9,968**
	Jan-Mar 05	643	723	-81	-80	-12.6%	-12.4%	8,642	6,271	72.6%	3,851	9,219
	Apr-Jun 05	756	747	9	17	1.2%	2.2%	8,920	6,947	77.9%	4,232	9,144
American	Jul-Sep 04	4,762	4,789	-27	-214	-0.6%	-4.5%	71,638	55,777	77.9%		93,300
	Oct-Dec 04	4,541	4,896	-355	-387	-7.8%	-8.5%	69,049	51,325	74.3%		90,700
	Year 2004	**18,645**	**18,789**	**-144**	**-761**	**-0.8%**	**-4.1%**	**280,042**	**209,473**	**74.8%**		**90,700**
	Jan-Mar 05	4,750	4,727	23	-162	0.5%	-3.4%	68,965	52,024	75.4%		88,500
	Apr-Jun 05	5,309	5,080	229	58	4.3%	1.1%	72,447	57,605	79.5%		88,500
	Jul-Sep 05	5,485	5,446	39	-153	0.7%	-2.8%	73,405	59,584	81.2%		88,500
America West	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
	Oct-Dec 04	579	602	-24	-50	-4.1%	-8.6%	12,236	9,471	77.4%	5,336	11,845
	Year 2004	**2,339**	**2,357**	**-18**	**-90**	**-0.8%**	**-3.8%**	**48,525**	**37,550**	**77.4%**	**21,132**	**11,904**
	Jan-Mar 05	723	673	50	34	6.9%	4.7%	11,749	9,126	77.7%	5,172	11,869
	Apr-Jun 05	833	803	30	14	3.6%	1.7%	12,480	10,277	82.3%	5,752	12,200
	Jul-Sep 05	846	904	-58	-71	-6.9%	-8.4%	12,673	10,192	80.4%	5,802	12,179
Continental	Jul-Sep 04	2,564	2,540	24	-16	0.9%	-0.6%	35,371	28,843	81.5%	11,182	
	Oct-Dec 04	2,397	2,558	-161	-206	-6.7%	-8.6%	37,962	29,350	77.3%	14,253	
	Year 2004	**9,744**	**9,973**	**-229**	**-363**	**-2.4%**	**-3.7%**	**95,082**	**73,151**	**76.9%**	**56,482**	**38,255**
	Jan-Mar 05	2,505	2,676	-171	-184	-6.8%	-7.3%	37,955	29,148	76.8%	14,122	
	Apr-Jun 05	2,857	2,738	119	100	4.2%	3.5%	36,138	29,041	80.4%	11,465	
	Jul-Sep 05	3,001	2,892	109	61	3.6%	2.0%	37,450	31,185	81.7%	11,642	
Delta	Jul-Sep 04	3,871	4,294	-423	-646	-10.9%	-16.7%	63,031	48,952	77.7%	28,247	69,700
	Oct-Dec 04	3,641	5,897	-2,256	-2,206	-62.0%	-60.6%	61,384	45,237	73.7%	27,794	69,150
	Year 2004	**15,002**	**18,310**	**-3,308**	**-5,198**	**-22.1%**	**-34.6%**	**244,097**	**182,351**	**74.7%**	**110,000**	**69,150**
	Jan-Mar 05	3,647	4,604	-957	-1,071	-26.2%	-29.4%	60,955	45,344	74.4%	29,230	66,500
	Apr-Jun 05	4,185	4,314	-120	-382	-2.9%	-9.1%	65,136	50,957	78.2%	31,582	65,300
	Jul-Sep 05	4,216	4,456	-240	-1,130	-5.7%	-26.8%	66,054	52,323	79.2%	30,870	58,000
Northwest	Jul-Sep 04	3,052	2,973	79	-38	2.6%	-1.2%	38,324	31,774	82.9%	14,800	38,178
	Oct-Dec 04	2,753	3,177	-424	-412	-15.4%	-15.0%	36,964	29,107	78.7%	13,775	
	Year 2004	**11,279**	**11,784**	**-505**	**-848**	**-4.5%**	**-7.5%**	**147,055**	**117,981**	**80.2%**	**55,374**	**39,342**
	Jan-Mar 05	2,798	3,090	-292	-450	-10.4%	-16.1%	36,636	29,238	79.8%	13,502	39,105
	Apr-Jun 05	3,195	3,375	-180	-217	-5.6%	-6.8%	38,256	32,218	84.2%	15,145	38,348
	Jul-Sep 05	3,378	3,545	-167	-469	-4.9%	-13.9%	38,881	32,889	84.6%	14,984	33,755
Southwest	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
	Oct-Dec 04	1,655	1,535	120	56	7.3%	3.4%	32,540	21,140	65.0%	17,709	31,011
	Year 2004	**6,530**	**5,976**	**554**	**313**	**8.5%**	**4.8%**	**123,693**	**85,966**	**69.5%**	**70,903**	**31,011**
	Jan-Mar 05	1,663	1,557	106	76	6.4%	4.6%	32,559	21,304	65.4%	17,474	30,974
	Apr-Jun 05	1,944	1,667	277	159	14.2%	8.2%	34,341	24,912	72.5%	20,098	31,366
	Jul-Sep 05	1,989	1,716	273	227	13.7%	11.4%	35,170	26,336	74.9%	20,638	31,382
United	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
	Oct-Dec 04	3,988	4,481	-493	-664	-12.4%	-16.6%	58,033	44,824	77.2%	17,143	57,500
	Year 2004	**16,391**	**17,168**	**-777**	**-1,644**	**-4.7%**	**-10.0%**	**233,929**	**185,388**	**79.2%**	**70,914**	**58,900**
	Jan-Mar 05	**3,915**	4,165	-250	-1,070	-6.4%	-27.3%	55,133	43,103	78.2%	15,667	56,300
	Apr-Jun 05	4,423	4,375	48	-1,430	1.1%	-32.3%	56,538	47,156	83.4%	17,150	55,600
	Jul-Sep 05	4,655	4,490	165	-1,172	3.5%	-25.2%	58,123	48,771	83.9%	17,448	54,600
US Airways	Apr-Jun 04	1,957	1,874	83	34	4.2%	1.7%	24,991	19,336	77.4%	25,953	26,880
	Jul-Sep 04	1,799	1,976	-177	-232	-9.8%	-12.9%	25,462	19,382	76.1%	14,274	26,835
	Oct-Dec 04	1,660	1,802	-142	-236	-8.6%	-14.2%	24,514	17,622	71.9%	14,097	24,628
	Year 2004	**7,117**	**7,495**	**-378**	**-611**	**-5.3%**	**-8.6%**	**98,735**	**72,559**	**73.5%**	**55,954**	**24,628**
	Jan-Mar 05	1,628	1,829	-201	-191	-12.3%	-11.7%	24,976	17,779	71.2%	14,068	23,696
	Apr-Jun 05	1,945	1,904	41	-62	2.1%	-3.2%	26,547	20,165	76.0%	15,826	21,396
	Jul-Sep 05	926	997	-71	-87	-7.7%	-9.4%	21,281	16,503	77.5%	10,109	
JetBlue	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
	Oct-Dec 04	334	322	12	2	3.6%	0.6%	8,200	6,802	82.9%	3,179	6,413
	Year 2004	**1,266**	**1,153**	**113**	**47**	**8.9%**	**3.7%**	**30,434**	**25,315**	**83.2%**	**11,783**	**6,413**
	Jan-Mar 05	374	349	26	7	7.0%	1.9%	8,318	7,136	85.8%	3,400	6,797
	Apr-Jun 05	430	390	39	12	9.1%	2.8%	9,408	8,247	87.7%	3,695	7,284
	Jul-Sep 05	453	439	14	3	3.1%	0.7%	10,190	8,825	86.6%	3,782	7,452

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/												
KLM Group	Apr-Jun 04	5,394	5,205	189	115	3.5%	2.1%	48,944	38,025	77.7%		
YE 31/03	Jul-Sep 04	6,328	5,964	364	248	5.8%	3.9%	57,668	46,767	81.1%		
	Oct-Dec 04	6,628	5,745	883	83	13.3%	1.3%	54,144	42,042	77.6%	15,934	
	Year 2004/05	**24,641**	**21,744**	**641**	**453**	**2.6%**	**1.8%**	**214,606**	**168,998**	**78.7%**	**64,075**	**102,077**
	Apr-Jun 05	6,257	5,982	275	135	4.4%	2.2%	57,936	46,041	79.5%	17,948	101,886
BA												
YE 31/03	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
	Oct-Dec 04	3,801	3,589	212	94	5.6%	2.5%	35,723	25,999	72.8%	8,428	45,888
	Jan-Mar 05	3,549	3,474	96	17	2.7%	0.5%	35,677	26,062	73.0%	8,178	45,914
	Year 2004/05	**14,681**	**13,666**	**1,015**	**472**	**6.9%**	**3.2%**	**144,189**	**107,892**	**74.8%**	**35,717**	**46,065**
	Apr-Jun 05	3,716	3,398	318	162	8.6%	4.4%	36,706	27,768	75.6%	9,177	46,079
	Jul-Sep 05	3,887	3,427	460	301	11.8%	7.7%	37,452	29,812	79.6%	9,767	46,144
Iberia												
YE 31/12	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
	Oct-Dec 04	1,660	1,605	55	74	3.3%	4.5%	15,700	11,398	72.6%	6,329	24,783
	Year 2004	**6,466**	**6,212**	**254**	**252**	**3.9%**	**3.9%**	**61,058**	**45,924**	**75.2%**	**26,692**	**24,993**
	Jan-Mar 05	1,531	1,571	-40	-21	-2.6%	-1.4%	15,261	11,421	74.8%	6,181	24,044
	Apr-Jun 05	1,466	1,392	74	54	5.0%	3.7%	15,843	11,939	75.4%	7,242	24,435
	Jul-Sep 05	2,384	1,910	475	449	19.9%	18.8%	16,659	13,619	81.8%	7,656	25,069
Lufthansa												
YE 31/12	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
	Year 2004	**25,655**	**24,285**	**1370**	**551**	**5.3%**	**2.1%**	**140,648**	**104,064**	**74.0%**	**50,300**	**90,763**
	Jan-Mar 05	5,041	5,079	-38	-150	-0.8%	-3.0%	32,477	23,793	73.3%	11,190	89,939
	Apr-Jun 05	5,487	5,138	349	140	6.4%	2.6%	37,700	28,178	74.7%	13,583	90,373
	Jul-Sep 05	5,798	5,411	387	501	6.7%	8.6%	38,967	30,466	78.2%	14,203	91,433
SAS												
YE 31/12	**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	
	Oct-Dec 04	2,271	2,293	-22	-96	-1.0%	-4.2%	12,667	7,649	60.4%	7,645	32,600
	Year 2004	**8,830**	**8,967**	**-137**	**-283**	**-1.6%**	**-3.2%**	**43,077**	**28,576**	**64.0%**	**32,354**	**32,481**
	Jan-Mar 05	1,842	1,990	-148	-137	-8.0%	-7.4%	12,465	7,342	58.9%	7,299	31,797
	Apr-Jun 05	2,046	1,925	121	64	5.9%	3.1%	13,810	9,259	67.0%	9,357	32,285
	Jul-Sep 05	2,140	2,036	104	68	4.9%	3.2%	13,599	9,838	72.3%	9,325	
Ryanair												
YE 31/03	**Year 2002/03**	**910**	**625**	**285**	**259**	**31.3%**	**28.5%**	**14,072**		**84.0%**	**15,740**	**1,900**
	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%**	**22,524**		**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
	Oct-Dec 04	402	335	68	47	16.9%	11.7%			84.0%	6,900	2,671
	Year 2004/05	**1,727**	**1,301**	**426**	**345**	**24.7%**	**20.0%**	**28,665**		**84.0%**	**27,593**	
	Apr-Jun 05	488	392	96	84	19.7%	17.2%			83.4%	8,500	2,764
	Jul-Sep 05	652	409	244	208	37.4%	31.9%				9,500	2,987
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**	**3,727**
	Oct-Mar 05	1,039	1,116	-77	-41	-7.4%	-3.9%	14,526	12,150	83.8%	13,500	

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

		Group revenue US$m	Group costs US$m	Group op. profit US$m	Group net profit US$m	Operating margin	Net margin	Total ASK m	Total RPK m	Load factor	Total pax. 000s	Group employees
ANA												
YE 31/03	**Year 2001/02**	**9,714**	**9,529**	**185**	**-76**	**1.9%**	**-0.8%**	**87,908**	**57,904**	**64.7%**	**49,306**	**29095**
	Year 2002/03	**10,116**	**10,137**	**-22**	**-235**	**-0.2%**	**-2.3%**	**88,539**	**59,107**	**66.7%**	**50,916**	**28,907**
	Year 2003/04	**11,529**	**11,204**	**325**	**234**	**2.8%**	**2.0%**	**87,772**	**55,807**	**63.6%**	**44,800**	**28,870**
	Year 2004/05	**12,024**	**11,301**	**723**	**251**	**6.0%**	**2.1%**	**85,838**	**55,807**	**65.0%**		**29,098**
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	
	Year 2004	**5,024**	**4,350**	**674**	**581**	**13.4%**	**11.6%**	**74,062**	**57,283**	**77.3%**	**13,664**	**15,054**
	Jan-Jun 05	3,074	2,799	275	225	8.9%	7.3%	39,535		78.1%	7,333	15,400
JAL												
YE 31/03	**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**	
	Year 2003/04	**18,398**	**19,042**	**-644**	**-844**	**-3.5%**	**-4.6%**	**145,900**	**93,847**	**64.3%**	**58,241**	
	Year 2004/05	**19,905**	**19,381**	**524**	**281**	**2.6%**	**1.4%**		**102,354**	**67.4%**	**59,448**	
Korean Air												
YE 31/12	**Year 2001**	**4,309**	**4,468**	**-159**	**-448**	**-3.7%**	**-10.4%**	**55,802**	**38,452**	**68.9%**	**21,638**	**15,127**
	Year 2002	**5,047**	**4,679**	**368**	**366**	**7.3%**	**7.3%**	**58,310**	**41,818**	**71.7%**	**22,160**	**15,309**
	Year 2003	**5,172**	**4,911**	**261**	**-202**	**5.0%**	**-3.9%**	**59,074**	**40,507**	**68.6%**	**21,811**	**15,352**
	Year 2004	**6,332**	**5,994**	**338**	**414**	**5.3%**	**6.5%**	**64,533**	**45,879**	**71.1%**	**21,280**	**14,994**
Malaysian												
YE 31/03	**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**
	Year 2003/04	**2,308**	**2,258**	**50**	**121**	**2.2%**	**5.2%**	**55,692**	**37,659**	**67.6%**	**15,375**	**20,789**
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**
	Jul-Dec 04	5,017	4,493	524	358	10.4%	7.1%	57,402	43,907	76.5%	16,548	35,310
	Year 2004/05	**9,524**	**8,679**	**845**	**575**	**8.9%**	**6.0%**	**114,003**	**86,986**	**76.3%**	**32,660**	
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**

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 - MONTH END

	Old narrowbodies	Old widebodies	Total old	New narrowbodies	New widebodies	Total new	Total
Dec-1999	243	134	377	101	53	154	531
Dec-2000	302	172	474	160	42	202	676
Dec-2001	368	188	556	291	101	392	948
Dec-2002	366	144	510	273	102	375	885
Dec-2003	275	117	392	274	131	405	797
Dec-2004	185	56	241	194	48	242	483
Oct-2005	149	53	202	251	46	297	499

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	321	177	498	1,815	325	2,140	2,638
Sep-2005	35	11	46	142	20	162	208

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 %
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
2004	220.6	144.2	65.4	224.0	182.9	81.6	153.6	119.9	78.0	535.2	428.7	80.1	795.7	600.7	75.5
Oct-05	27.0	18.8	69.4	20.0	16.1	80.4	14.8	12.2	82.6	48.8	39.7	81.3	72.1	56.0	77.5
Ann. chng	3.8%	6.5%	1.7	2.9%	2.3%	-0.5	8.8%	10.8%	1.5	6.1%	6.3%	0.1	4.9%	6.0%	0.8
Jan-Oct 05	260.9	177.4	68.0	192.5	159.9	83.0	139.2	111.5	80.1	470.6	383.4	81.5	696.6	539.5	77.4
Ann. Change	3.0%	5.3%	1.5	1.0%	2.0%	0.8	9.1%	11.6%	1.8	5.1%	6.4%	1.0	4.4%	6.3%	1.4

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 %
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
2004	1,014.5	763.6	75.3	164.2	134.4	81.8	105.1	87.6	83.4	96.4	68.0	70.5	365.6	289.8	79.3
Oct 05	81.7	62.5	76.5	15.6	12.3	78.6	9.8	8.0	81.4	7.4	5.1	69.2	32.8	25.4	77.3
Ann. Change	-4.0%	-2.0%	1.6	5.6%	1.9%	-2.8	7.9%	7.0%	-0.7	3.4%	7.7%	2.8	5.7%	4.6%	-0.8
Jan-Octt 05	842.5	659.2	78.3	148.2	123.3	82.6	97.6	80.5	82.5	87.3	63.9	73.2	333.1	266.7	80.1
Ann. Change	-0.6%	3.0%	2.7	7.1%	7.6%	0.4	12.7%	10.3%	-1.8	10.0%	13.8%	2.5	9.5%	9.9%	0.3

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	21 Nov	LCAL	6 x 787-8	4Q 2009 onwards	
	06 Dec	Royal Air Maroc	4 x 787	2H 2008 onwards	
	13 Dec	El Al	2 x 777-200ER	2007	
	13 Dec	Qantas	45 x 787	2008 onwards	plus 20 options and 50 purchase rights
Airbus	20 Nov	Jazeera Airways	6 x A320		CFM56-5
	29 Nov	US Airways Group	20 x A350	2011-2014	
	06 Dec	Philippine A/L	9 x A320		plus 5 options
	12 Dec	Aegean Airlines	8 x A320		plus 12 options/ IAE V2500
	13 Dec	UPS	10 x A380F	2009-2012	
Embraer					
Bombardier	08 Dec	Lufthansa	12 x CRJ900		

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