A man in a dark suit stands with his back to the camera, looking out over a large airplane hangar. In the background, a large white commercial airplane with a blue and white tail is visible. The hangar has a high ceiling with a complex steel structure and large windows. The overall scene is brightly lit, suggesting a clear day.

# Flight plans are needed, despite the clear skies

Ludovic Subran – Chief Economist  
and Director of Research

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Manager

Bruno Goutard – Sector Analyst

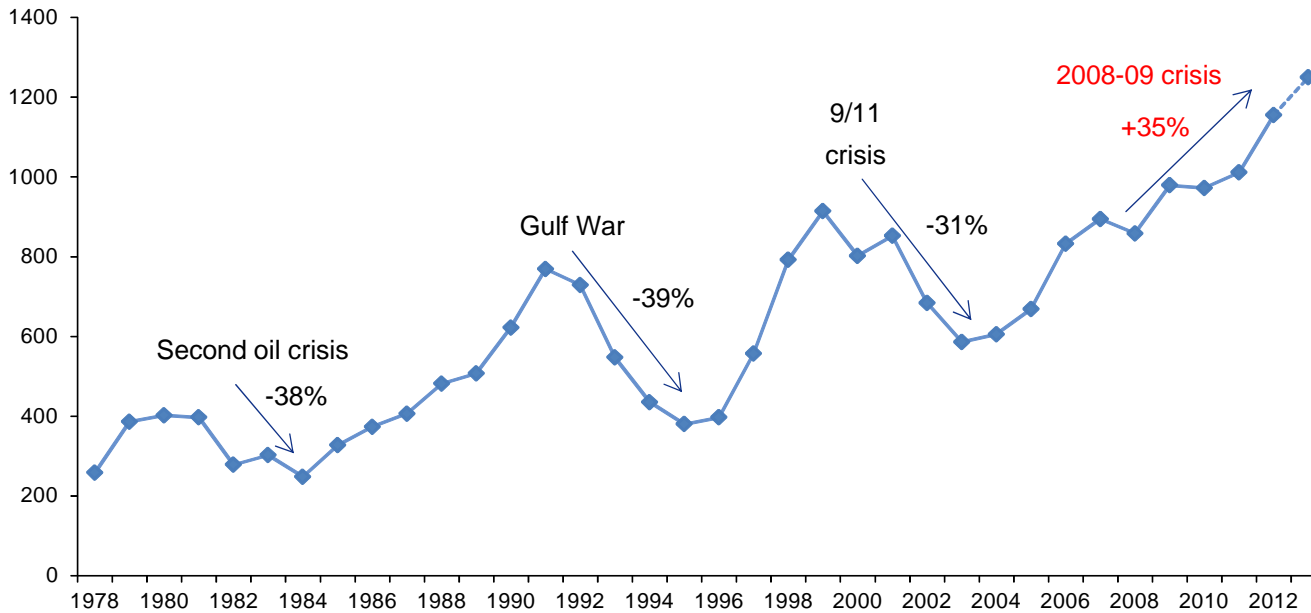
Paris, December 13, 2012

1

- 1 The aeronautics industry will remain strong in 2013**
- 2 Airlines will continue to revise their flight plans in 2013**
- 3 In 2013, the sector faces risks due to financial costs and the role of leasing**
- 4 Conclusion**

# Deliveries of commercial aircraft reached record levels in 2012. To be continued in 2013?

## Annual deliveries of commercial aircraft (100+ seats)



- In 2012, 1,155 aircraft (e) were delivered (+14%)
- This growth was driven by the almost universal rise in production

Sources: manufacturers. Forecasts: Euler Hermes

(e): estimates

**▶ Further sharp rise in deliveries in 2013 (+10%)**

## Return to more "normal" levels in 2012, after an exceptional year 2011

### Aerospace manufacturers activity indicators (units)

	2009	2010	2011	2012 (e)	2013 (p)
Deliveries	979	972	1011	1155	1270
Net orders	413	1104	2224	1700	1200
Order books	6850	7000	8200	8700	8600

(e): estimates / (p): forecasts

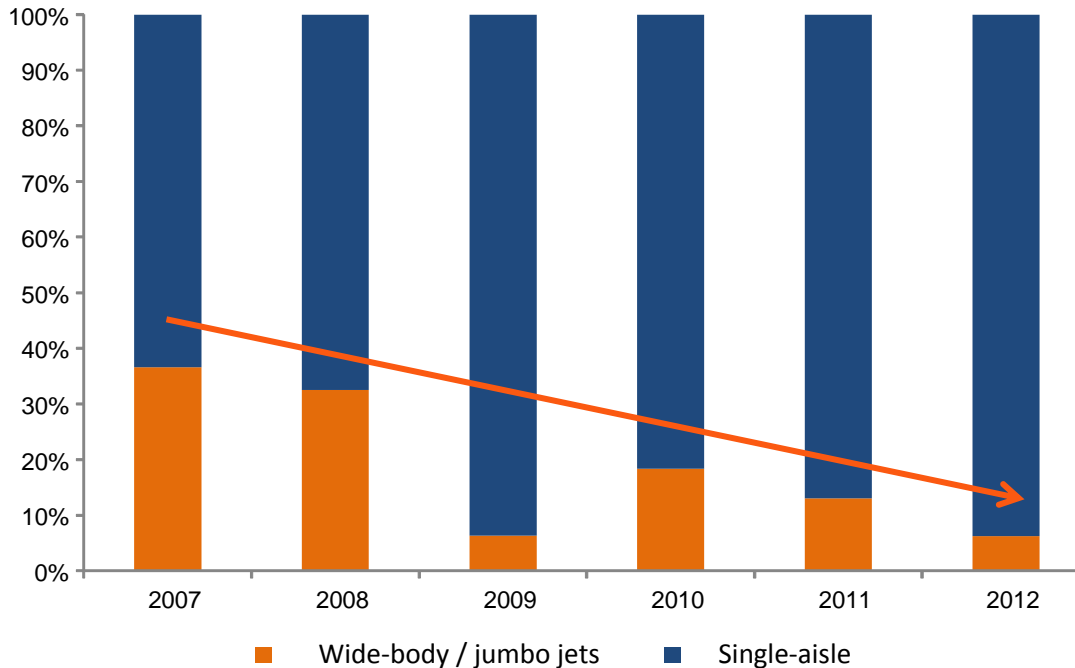
Sources: manufacturers. Forecasts: Euler Hermes

- 25% drop in net orders in 2012
- The B737Max took over from the successful A320Neo, with almost one half of total net orders in 2012
- Current order books represent 7-8 years of production

▶ Healthy order books offer visibility into industry's future

# Total orders of long-haul aircraft and jumbo jets declined 75% between 2008-2012

## Breakdown of net annual orders of aircraft manufacturers\*



- Decline due in particular to manufacturing problems encountered by new programs (A380, A350, B787, B747-8)
- A mix of single-aisle / long-haul and jumbo jets that could harm revenue in the long term: e.g., in terms of value, one A380 = four A320Neos\*\*

\*At October 31, 2012

Sources: manufacturers, Euler Hermes

\*\*Catalog price

Long-haul aircraft and jumbo jets have crossed a commercial desert, but this has not called the consistency of their order books into question

# Airbus continues to improve its profitability; Boeing maintains high profitability

## Operational profitability of manufacturers (as a % of revenue)

	2009	2010	2011	2012 (e)	2013 (p)
Airbus Commercial	+1.5%	+1.1%	+1.7%	+3.3%	+4.0%
Boeing Commercial Airplanes	-1.7%	+9.4%	+9.7%	+9.5%	+9.5%

(e): estimates / (p): forecasts

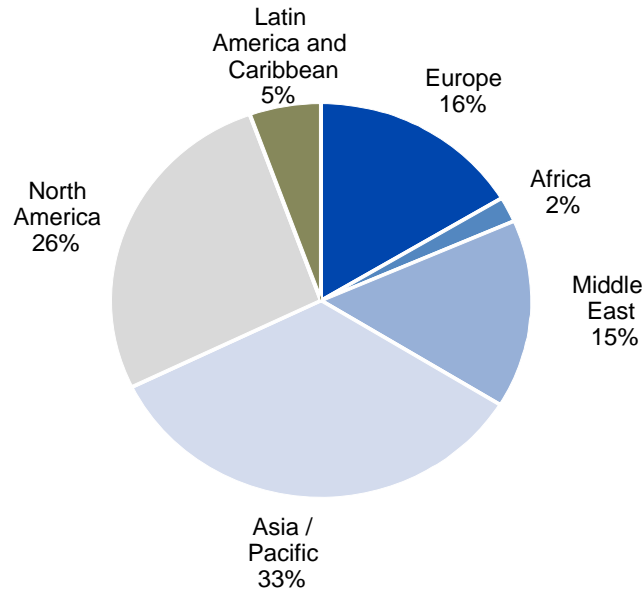
Sources: manufacturers. Forecasts: Euler Hermes

- Airbus's profitability has benefited from a rise in output, but is still affected by the A380 (micro cracks) and the A350 (capital outlay)
- Boeing continues to spread the excess costs of the B787 development across the duration of the program

▶ A rise in profitability in 2013, but still under "industrial" pressure

# Three good reasons to remain confident...

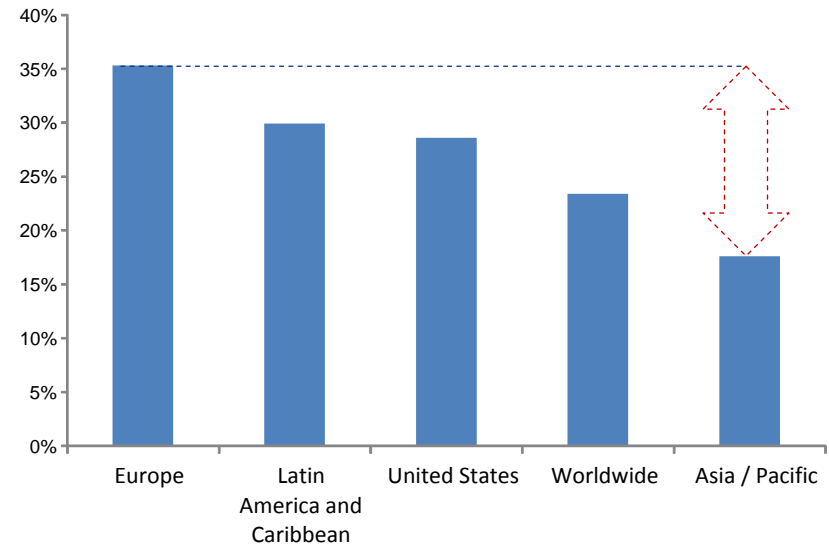
## Diversified order books\*



\*in value at Sep. 30, 2012 / 3% of orders are of undetermined origin

Sources: manufacturers

## Potential of low-cost segment in Asia\*



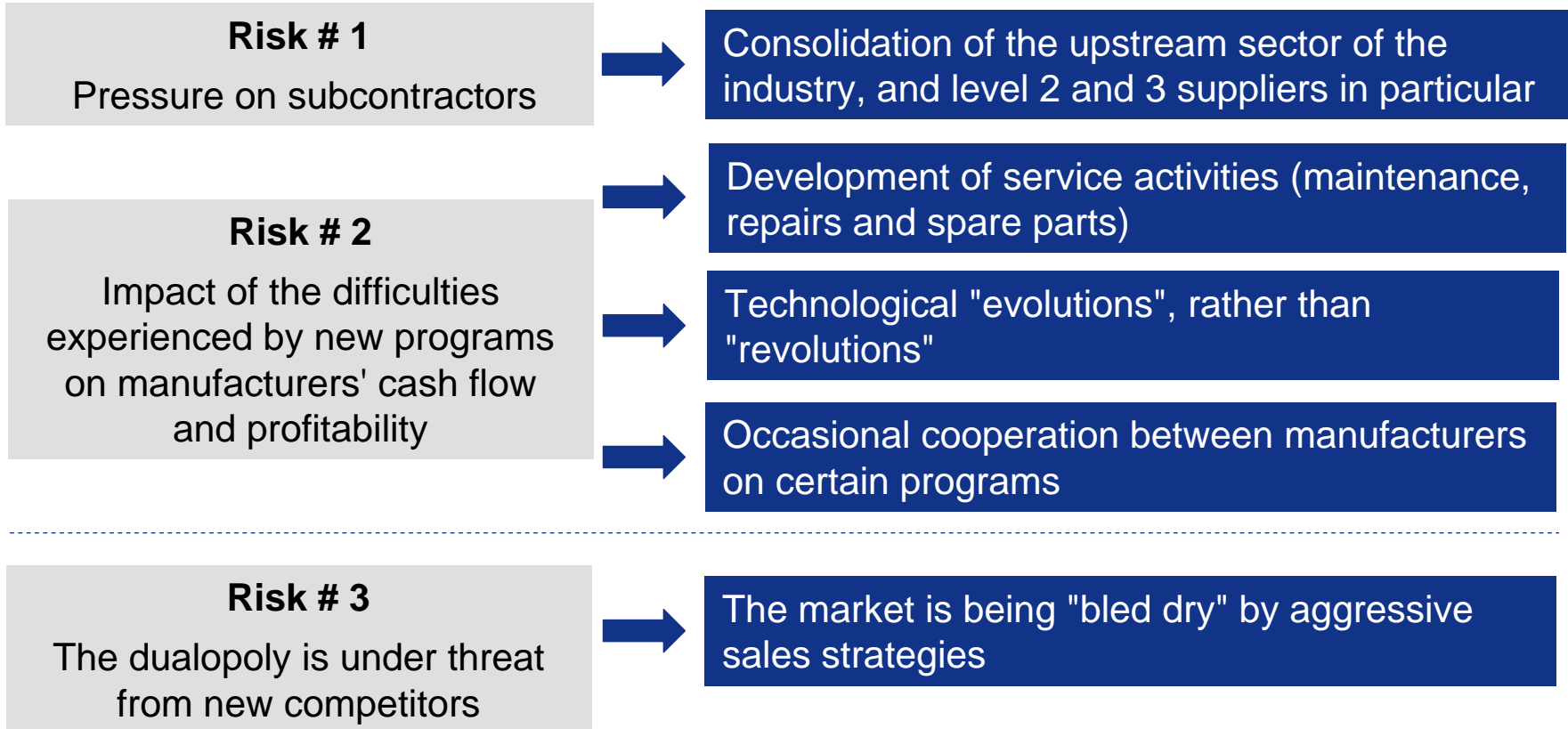
\*in 2010, in regional market share

Sources: CAPA, Deutsche Bank

## ▶ Fleet renewal: another source of growth emerges

## ... Despite three major risks for aircraft manufacturers

### Structural adjustments expected over the next years



► **An industry that is adapting, despite its success**

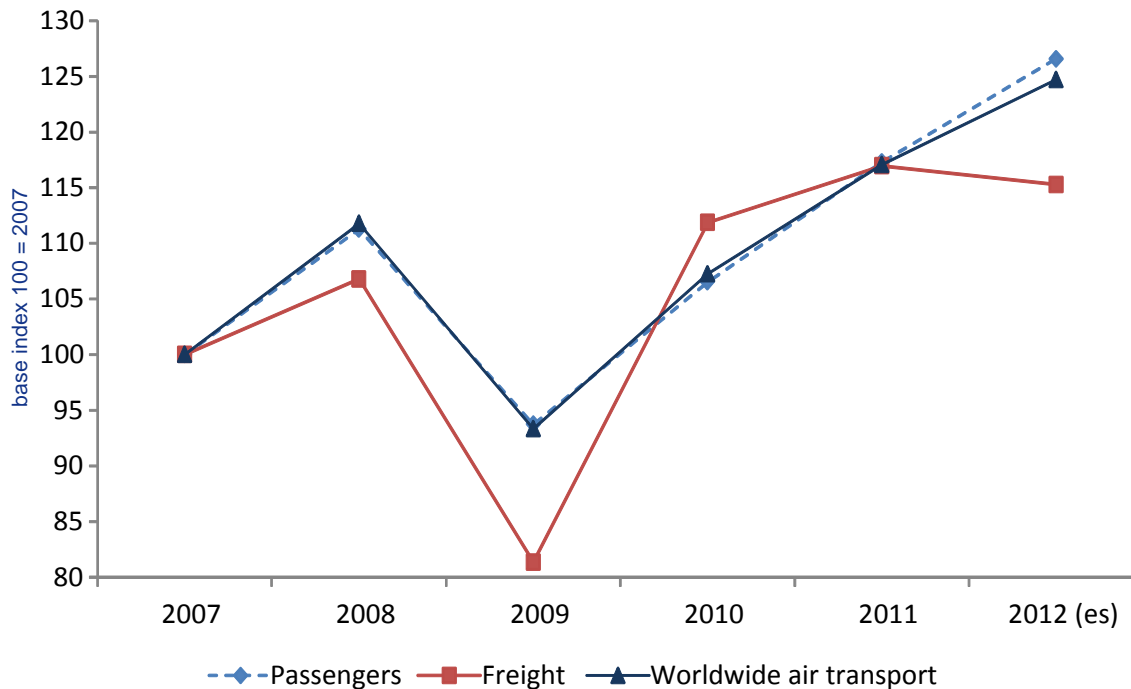


# 2

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# Worldwide air travel revenue up 6.4% in 2012

## Worldwide air travel revenue index



- According to IATA, the sector's revenue of \$636Bn (€491Bn) outstripped its pre-crisis peak
- In 2012, global passenger business revenue continued to grow by about 7.9%, to \$505Bn\* (€390Bn), while revenue from cargo dropped by about 2.0%, to \$68Bn\* (€53Bn)

(e): estimates

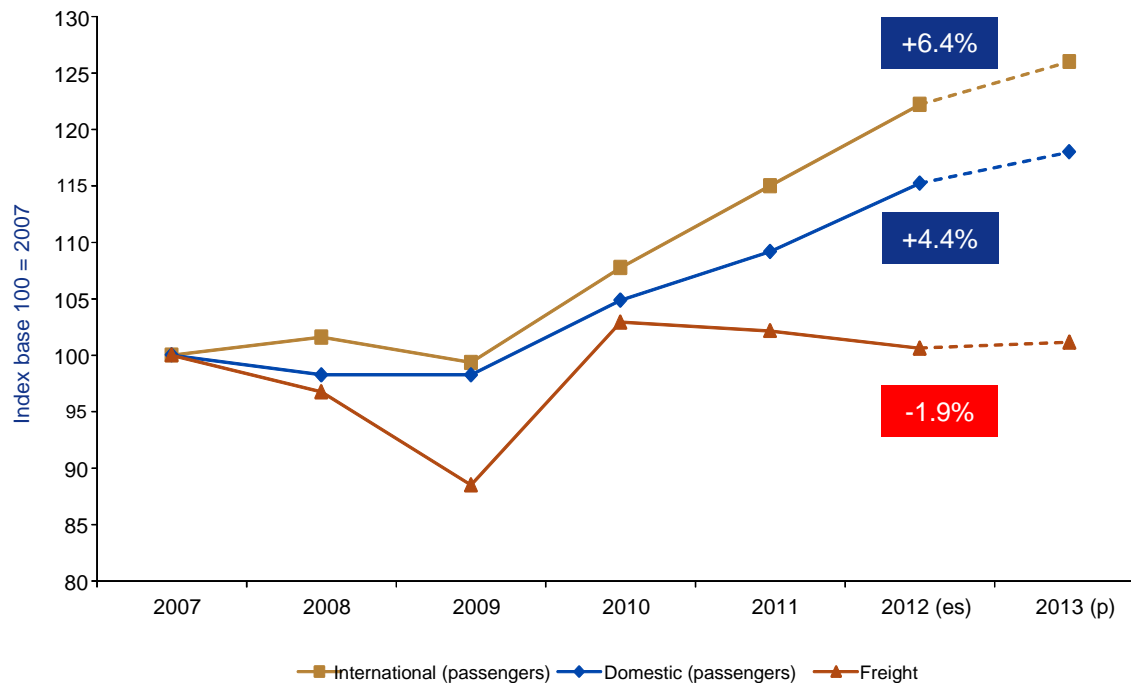
Sources: IATA, Euler Hermes

\*The sector's associated services accounted for about \$63Bn in 2012

## The diverging stories of cargo and passenger activities

# A clear contrast between the rise in passenger traffic and the slump in cargo traffic in 2012

## Worldwide passenger (international and domestic) and cargo traffic



- In 2012, the economic slowdown in Europe impacted two major cargo routes: Europe – Far East and North Atlantic
- In 2013, the uncertainty in Europe will affect global passenger traffic growth
- In 2013, cargo traffic will benefit from the recovery in international trade

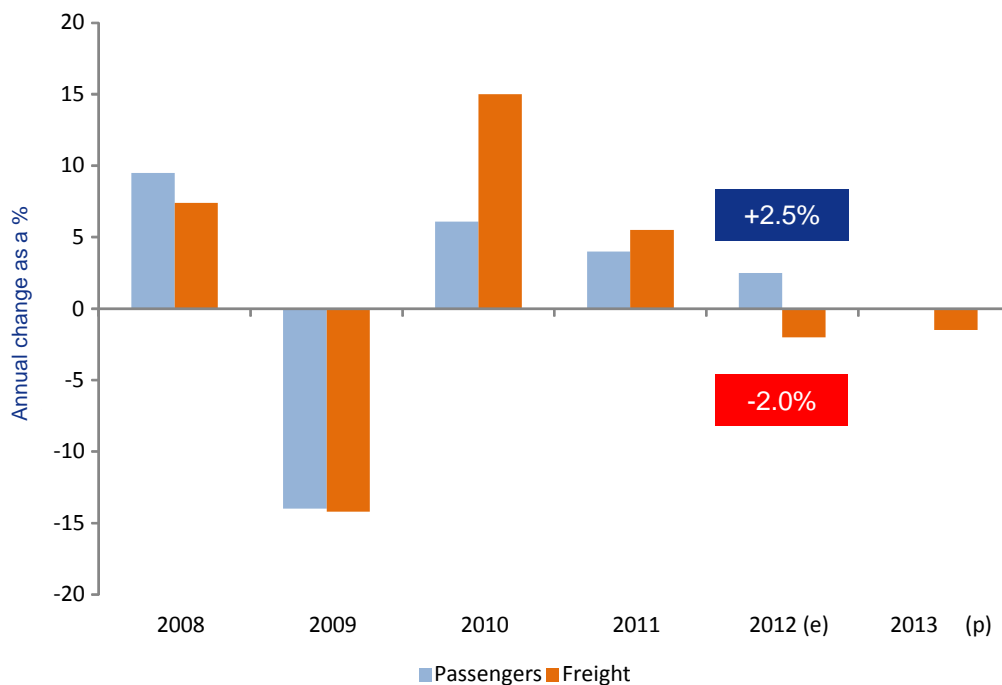
(e): estimates / (p): forecasts

Sources: IATA, Euler Hermes

The gap between passenger traffic (a drop in growth to 4.5%) and cargo traffic (stabilization after two years of erosion) to be bridged in 2013

## In 2012, for the first time in 11 years, prices in the passenger and cargo segments were de-linked

### Worldwide prices in the passenger and cargo segments



- In 2012, the cargo segment was hit by the rigid drop in its capacity, due to the slump in traffic
- In 2013, prices in the passenger segment will be hit by the massive introduction of extra capacity, while growth in traffic is expected to slow down

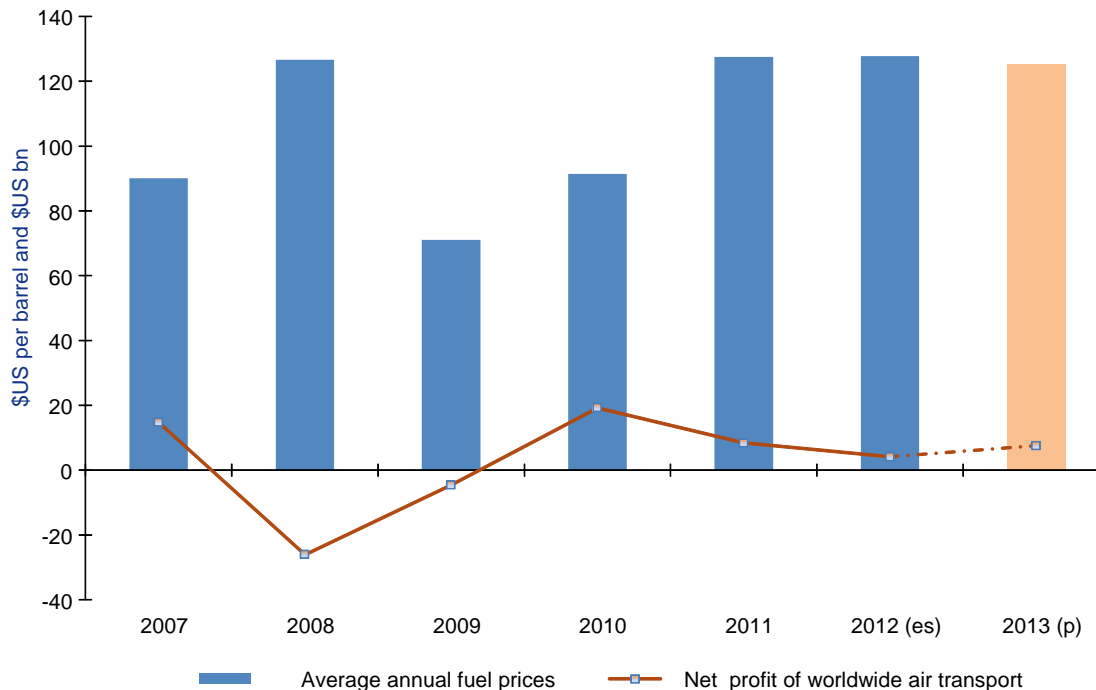
(e): estimates / (p): forecasts

Sources: IATA, Euler Hermes

**In 2013, prices in the cargo sector are expected to drop by a further 1.5% while prices in the passenger sector will stagnate**

## Fuel prices, a key profitability component of air transport, had a negative impact again in 2012

### Average annual price of fuel and net profit of worldwide air transport



(e): estimates / (p): forecasts

Source: IATA, Euler Hermes

- Fuel accounts for about 1/3 of operating costs
- Since the first "shock" in 2008, the industry has tried to adapt to fuel prices that have become structurally high (e.g., retiring aircraft that consume the most fuel)
- As long as fuel prices remain at current levels, the global profitability of the sector hits a "glass ceiling"

**In 2013, limited growth of the sector's net profitability**

# Conventional air transport is still regional, despite the fact that it symbolizes globalization

## Consolidation and scope of activity of local players differ according to region



## United States: Sound profitability in 2012, the "Made in the US" model is in good health

### Indicators of legacy US airlines activity

Passengers	First half 2012 / First half 2011	2011 / 2010
Traffic	+1%	+1%
Prices	+6%	+8%
Capacity	0%	+1%

- Continuation of a strategy to keep capacity under strict control
- Slight erosion of the "pricing lever" in the first half of 2012, due to a less favorable domestic environment
- Recovery of AMR, pending the final stage of US air transport consolidation

Source: Euler Hermes sample (American Airlines, Delta Air Lines, United Airlines and US Airways)

	2011	2012(e)	2013(p)
Average net profitability* of American legacy air transport	-1.0%	+2.2%**	+3.5%

\*Net profitability = net result / revenue \*\* excluding AMR restructuring charges

(e): estimates / (p): forecasts

### ▶ Increased profitability of American air transport in 2013

## Europe: Still restructuring after a year in the red (2012)

### Indicators of legacy European airlines activity

Passengers	First half 2012 / First half 2011	2011 / 2010
Traffic	+4%	+7%
Prices	+4%	+2%
Capacity	+2%	+8%

- Premium transatlantic passenger traffic remains weak
- Operators are focusing more on controlling capacity in a degraded environment and, therefore, inclined to strengthen their "pricing power"
- Significant restructuring

Source: Euler Hermes sample (Air France – KLM, IAG and Lufthansa)

	2011	2012(e)	2013(p)
Average net profitability* of European legacy air transport	+0.4%	-0.5%	+0.5%

\*Net profitability = net result / revenue

(e): estimates / (p): forecasts

▶ The first benefits of restructuring may be felt in 2013



## Middle East: Continues to expand

### Indicators of legacy Middle East airlines activity

Passengers	2011 / 2010
Traffic	+10%
Prices	+8%
Capacity	+10%

Source: Euler Hermes sample (Emirates)

- In 2012, Middle Eastern airlines continued to expand, with a two-digit increase in capacity
- Fuel prices significantly impacted their profitability (proportion of fuel in their operating costs: 40%)

	2011	2012(e)	2013(p)
Average net profitability* of Middle Eastern legacy air transport	+2.5%	+4.0%	+4.0%

\*Net profitability = net result / revenue

(e): estimates / (p): forecasts

▶ Stabilization of Middle Eastern airlines' profitability expected in 2013

## China: Profitability burdened by high fuel prices and increased competition in 2012

### Indicators of legacy Chinese airlines activity

Passengers	First half 2012 / First half 2011	2011 / 2010
Traffic	+7%	+12%
Prices	+2%	+7%
Capacity	+8%	+10%

Source: Euler Hermes sample (Air China, China Eastern Airlines and China Southern Airlines)

- The industry continues to benefit from growth in the Chinese market (9.7% at end of Sep. 2012)
- Indications of pressure on prices due to the aggressive expansion in supply
- Fuel accounts for 38% of operating costs

	2011	2012(e)	2013(p)
Average net profitability* of Chinese legacy air transport	+6.3%	+4.5%	+4.7%

\*Net profitability = net result / revenue

(e): estimates / (p): forecasts

**Growth of Chinese airlines will remain highly profitable in 2013**

## Asia (excluding China): 50% drop in profitability of conventional Asian airlines, under heavy pressure in 2012

### Indicators of legacy Asian airlines activity

Passengers	First half 2012 / first half 2011	2011 / 2010
Traffic	+8%	+5%
Prices	+1%	+6%
Capacity	+7%	+7%

- Protecting market share impacted prices on a market that remains strong, but is faced with increasing competition from local low-cost operators
- Premium passenger traffic is less lucrative
- Cargo activity in Asia: traffic down by 7%, prices down by 3% in the first half of 2012

Source: Euler Hermes sample (ANA, Cathay Pacific, Korean Airlines and Singapore Airlines)

	2011	2012(e)	2013(p)
Average net profitability* of Asian legacy air transport	4.0%	2.0%	3.0%

\*Net profitability = net result / revenue

(e): estimates / (p): forecasts

### ▶ Stronger profitability of Asian airlines in 2013

# Strategic movements: the start of a new era?

## An end to taboos in 2012

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- New alliances or code sharing with Gulf airlines
- Introduction or strengthening of low-cost subsidiaries/offers

## Potential capital movements in 2013

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- Certain companies on the market are still looking for buyers (e.g., TAP, SAS, LOT)
- Finalization of the consolidation between AMR and US Airways?
- And what about IAG?
- Europe discreetly approaches the US regulators. The start of negotiations for transatlantic rapprochement?

 2013: the first steps toward truly global air transport?

# 3

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## Airlines still exposed to heavy debts...

### The ability of airlines to cope with their debt

MLT debt / operational cash flow ratio*	2010	2011
United States	7.1	4.7**
Europe	7.1	7.0
Asia (excluding China)	3.0	3.7
China	3.4	4.1

\* MLT: medium-long term / in years of operational cash flow

\*\* excluding American Airlines

Source: Euler Hermes samples

- Even the "best-behaved pupils" have a mediocre MLT debt / operational cash ratio (reference point: 3.0)
- Becoming worse for European operators, while American peers are recovering

▶ All players need to find alternative sources of funding

## ... and the means of obtaining public support that remains crucial in order to finance deliveries in 2012

### Funding of commercial and regional aircraft deliveries (% of the total)

	2011	2012(e)
Export credit agencies	30%	30%
Commercial banks	25%	21%
Leasers	10%	7%
Financial markets	5%	10%
Cash	25%	25%
Other	5%	7%

- Airlines are still highly dependent on external sources to finance their aircraft
- Trend towards diversifying sources of funding
- Public export guarantees will become more costly, due to the new OECD procedures passed in 2011

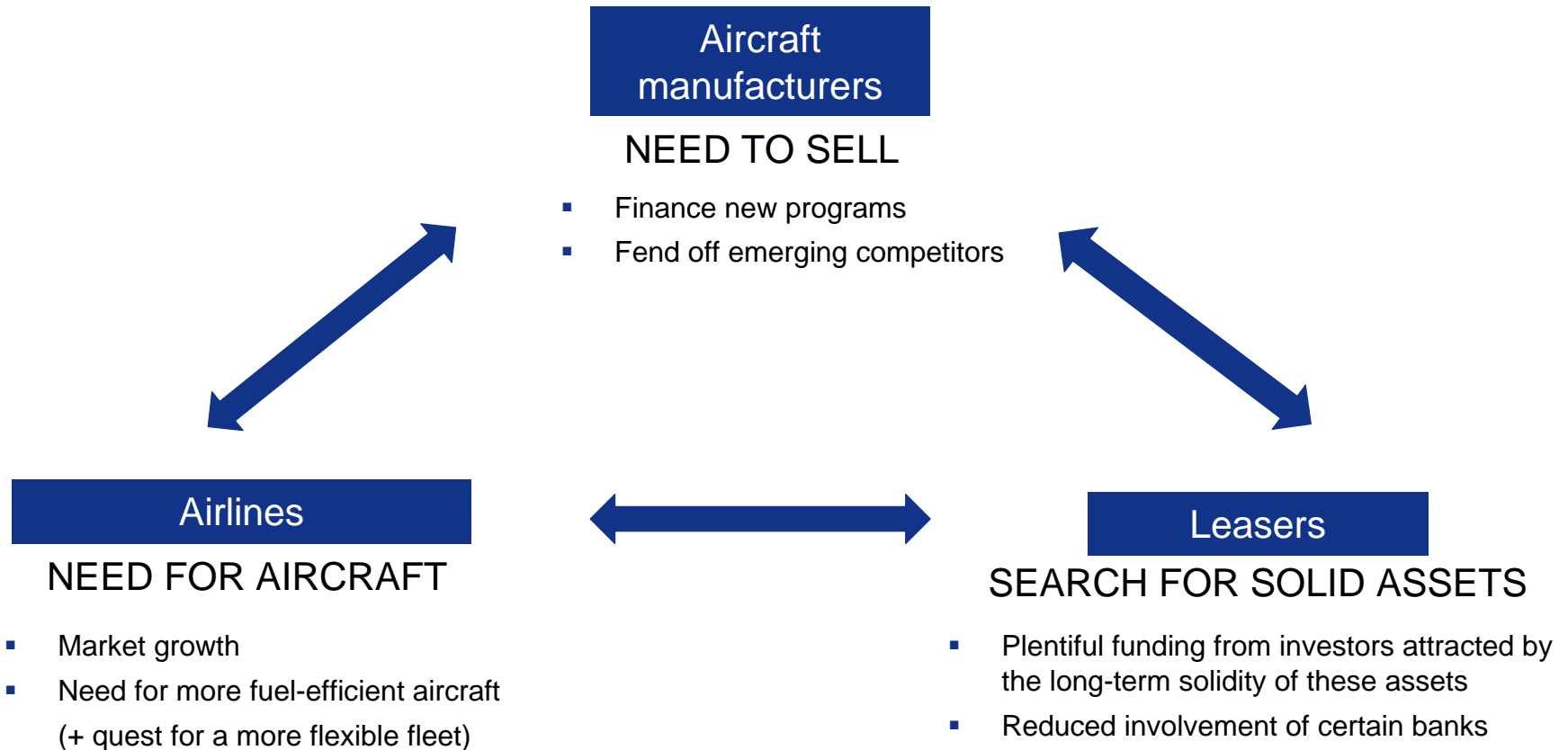
(e): estimates

Sources: Boeing Capital Corporation

### ► Structural increase in the cost of financing aircraft

# A "win-win-win" cycle

Leasers contributed to 46% of deals announced in 2011





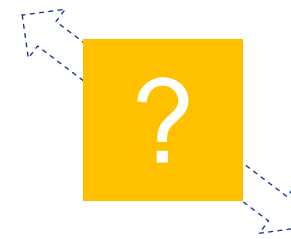
... but at a high risk

## Risks and uncertainty affecting this virtuous circle

Aircraft  
manufacturers

### INDUSTRIAL PROBLEMS

- Disruption of delivery schedules



Airlines

### DROP IN PROFITABILITY

- Reduced solvency that prevents certain airlines from honoring their commitments



Leasing

### DESTABILIZATION OF THE MODEL

- Aftermarket affected by the lack of funds
- Profitability damaged by downward pressure on leasing rates and/or faster depreciation of large fleets of conventional single-aisle aircraft

# Conclusion

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## Conclusion

- **The aerospace industry will continue to grow in 2013 by 10%**, driven by renewed progress in output
- The healthy state of order books provides the industry with **a clear visibility of the years ahead**, but does not completely do away with the **industrial risks** inherent in new programs **and the current pressure on subcontractors**
- **The European conventional air transport sector could break even in 2013**, while remaining a long way behind its American and Asian competitors
- In addition to the intense restructuring efforts launched in Europe in 2012, **2013 could see the first steps towards a future global “consolidation” of the aerospace sector**
- **The increased costs of financing aircraft and the uncertainty that may affect lessees** are risks for both the front end and the back end of the industry

A man in a dark suit stands with his back to the camera, looking out over a large aircraft hangar. The hangar is filled with various aircraft, including a large white and blue airplane with a prominent tail fin. The structure of the hangar is visible, with a high ceiling and large windows. The scene is brightly lit, suggesting a well-maintained facility.

# Thank you

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