



## Air transport creates large returns for national economies but returns for airlines are unsustainably weak

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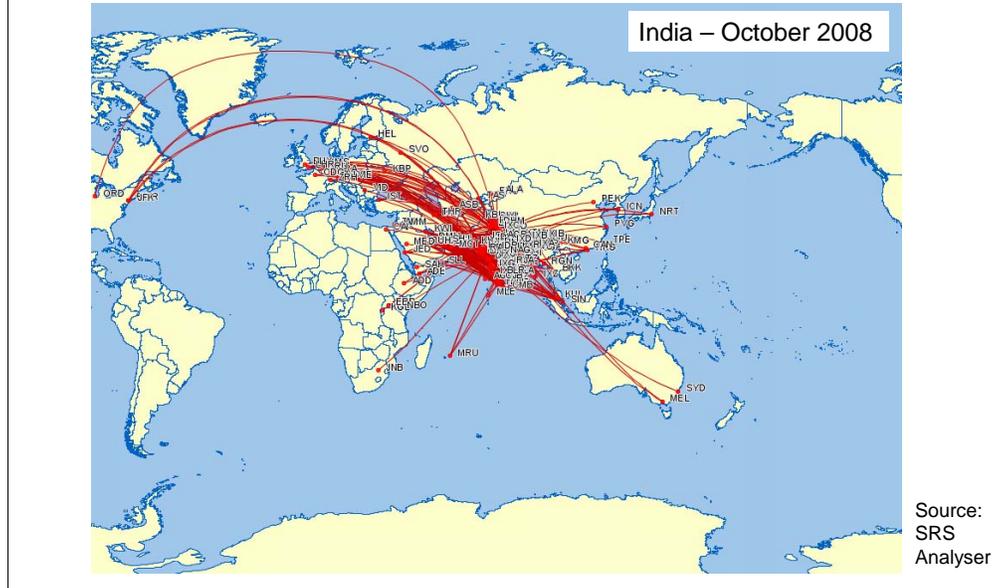
Theme – air transport brings large economic benefits to Asia-Pacific countries by providing an infrastructure that connects people and businesses to global markets and suppliers. However, returns to the airline industry that enables these economic benefits are unsustainably low.

## Air transport connectivity is a key infrastructure, enabling globalisation



This chart shows routes from India as of January 2000. The key to the economic benefits provided by air transport is this connectivity

## Expanded connectivity has facilitated trade and economic growth

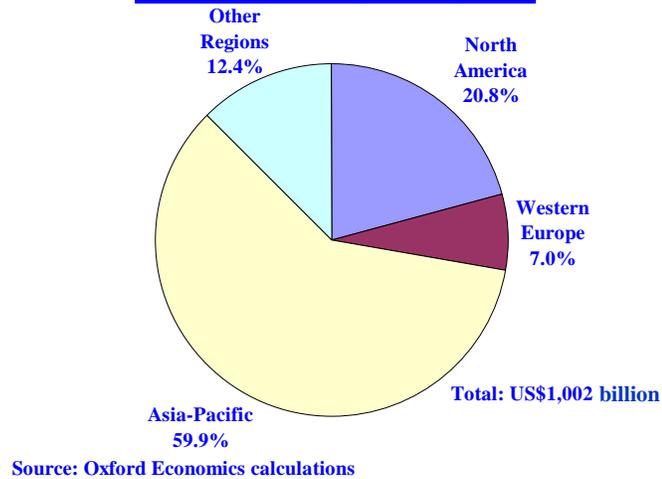


This chart shows India's route network today (October 2008)...new connections to N America, China, Australasia.

India's rapid economic growth in recent years, helped by outsourcing from N American and European companies and by globalisation generally has been facilitated by the expansion in the route network.

## Over \$1 trillion of A-P exports carried by air transport

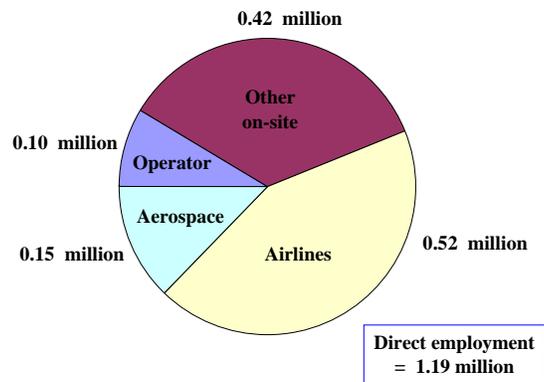
### Merchandise Exports by Air



Trade in high value low volume goods clearly been facilitated by air freight. Over \$1 trillion goods air freighted from Asia-Pacific.

## Direct employer of over 1 million jobs

### Asia-Pacific: Direct employment in the air transport industry

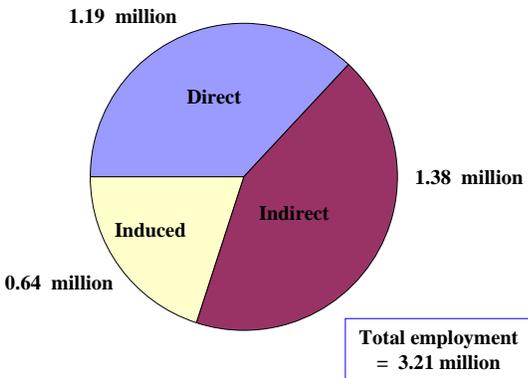


Source: ATAG/  
Oxford Economics

Air transports is also a major employer providing over 1 million jobs in the region

# Industry supports over 3.1 million jobs

**Asia-Pacific: Total employment in the air transport industry**

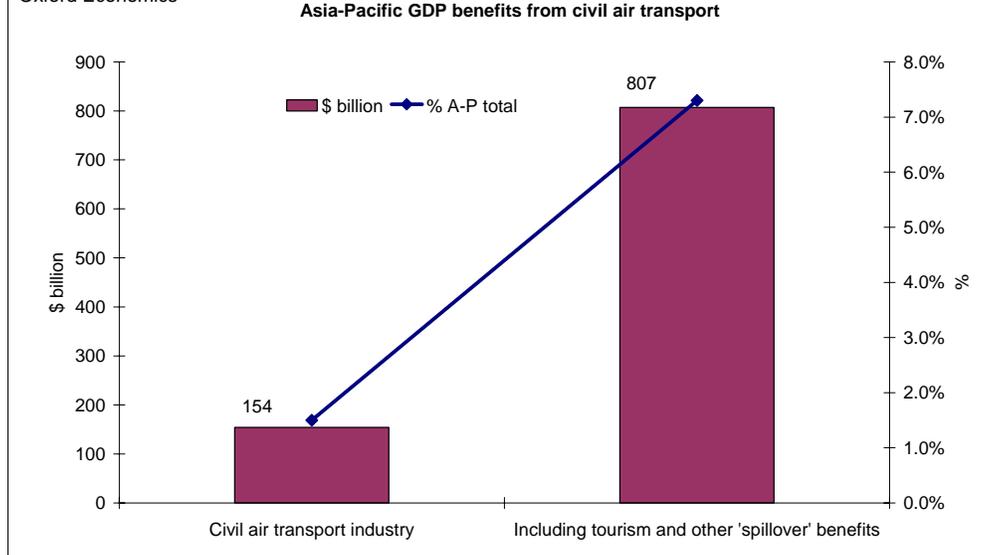


Source: ATAG/  
Oxford Economics

In total air transport supports over 3 million jobs in the region. 1m directly, another 1.3 million in suppliers and a further 0.6m in other industries through the spending of those employed in air transport

## Air transport supports over 7% of Asia-Pacific GDP

Source: ATAG/  
Oxford Economics



Air transport contributes \$154 billion or 1.4% to A-P GDP, through the value-added of airlines, airports etc and the multiplier effects through the economy of the spending of its employees.

If you include the GDP contribution of the tourism by air passengers and other spillover benefits to other industries then air transport supports over 7% of the regions GDP.

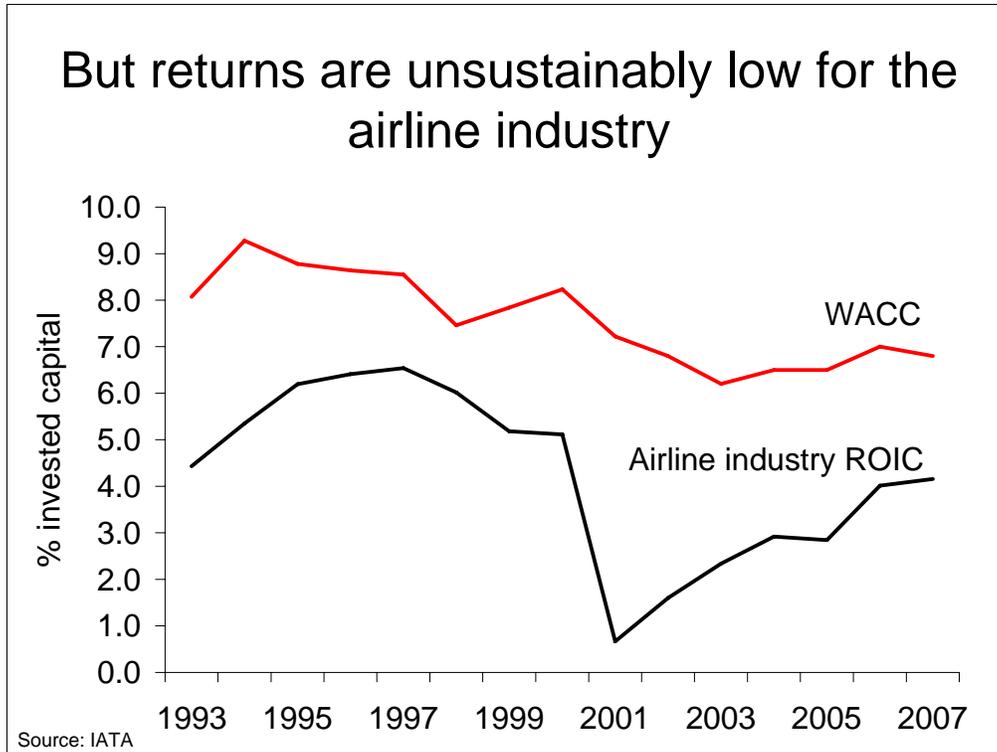
## Investment in air transport offers high rates of return for national economies – particularly developing nations

**Table 1: Economic Rates of Return from Aviation Investment**

	Kenya	Cambodia	Jordan	El Salvador	Jamaica
Investment (US\$ million)	409	786	360	802	191
Increase in national connectivity / GDP	59%	46%	55%	35%	28%
Impact on GDP (%)	0.42%	0.32%	0.39%	0.25%	0.20%
Annual Economic Rate of Return (%)	59%	19%	28%	16%	16%

Source: 'Aviation Economic Benefits' IATA Economics Briefing

As a result investment in air transport can deliver very high rates of economic return to nations – particularly developing nations. A recent study carried out for IATA showed that investment in developing countries air transport, like Cambodia, had produced annual economic rates of return (additional GDP) of 19%.

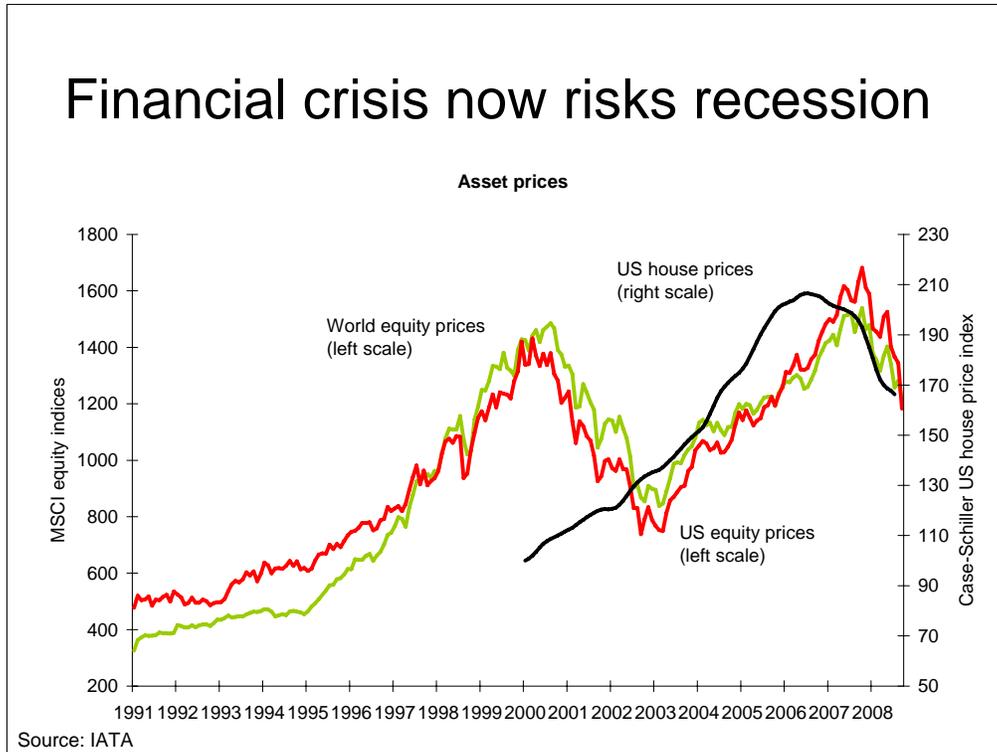


However, the returns to capital invested in the airlines that create these wider economic benefits are unsustainably low.

A competitive industry is expected to earn no more than its cost of capital (WACC – weight average cost of capital). An industry with market power over consumers earns more than its cost of capital. The fact that airlines have failed to even earn as much as their cost of capital shows first how competitive the industry is, and second that this is unsustainable.

To preserve and enhance the wider economic benefits from air transport, policy makers need to take measures (dereg O&C etc) to improve the financial performance of the industry.

# Financial crisis now risks recession

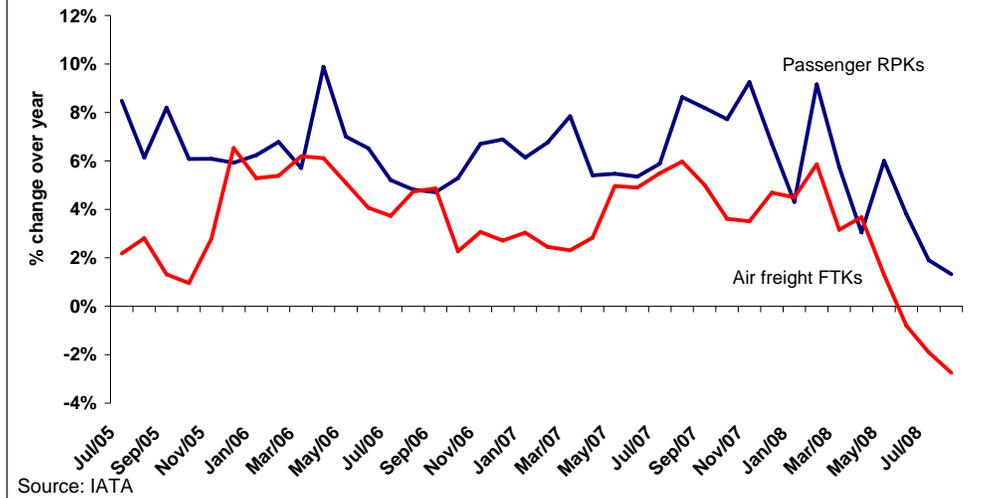


The current situation is highly dangerous and large falls in asset prices, the credit crunch etc risk recession and shrinking travel markets in 2009.

# Traffic volumes have already weakened very sharply

International passenger and freight tonne-kilometers

Source: IATA



International air traffic has already weakened sharply, reflecting economic conditions in the middle of this year. The impact of the most recent meltdown has yet to be felt in travel markets.

## Large drop in profitability in the first half of this year

Half year results		H1 2007		H1 2008	
		US \$ million			
Region	Nb Airlines	Op. profits	Net profits	Op. profits	Net profits
US*	10	3705	4756	-911	-2476
Europe	10	2392	2704	1791	-36
Asia - Pacific	6	1123	1939	1151	-207
Other	2	337	134	278	42
	28	7,557	9,533	2,310	-2,677

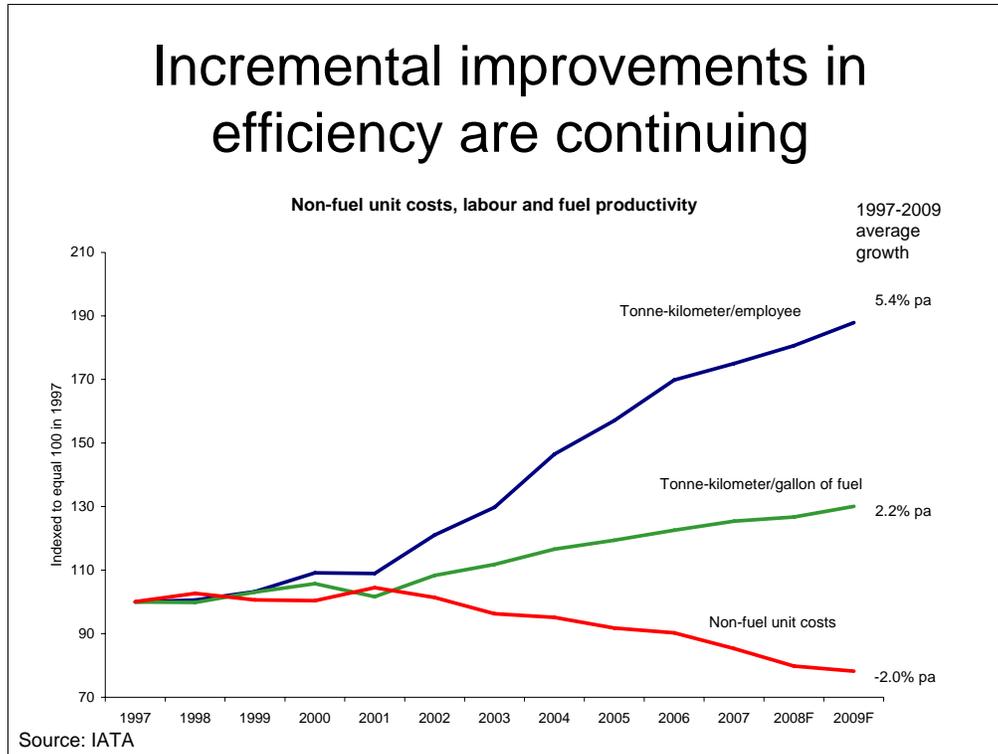
\* Excluding reorganisation costs

Source: IATA

The financial impact of the economic deterioration (partly high fuel costs in the first half of the year) has already been seen. During the first half of this year airlines lost \$2.6 billion. During the same period last year airlines made \$9.5 billion in profit.

Most of the losses have been for US airlines. However, performance for A-P airlines has deteriorated sharply with losses of \$207 million in 08H1 compared to profits of \$1.9 billion in 07H1.

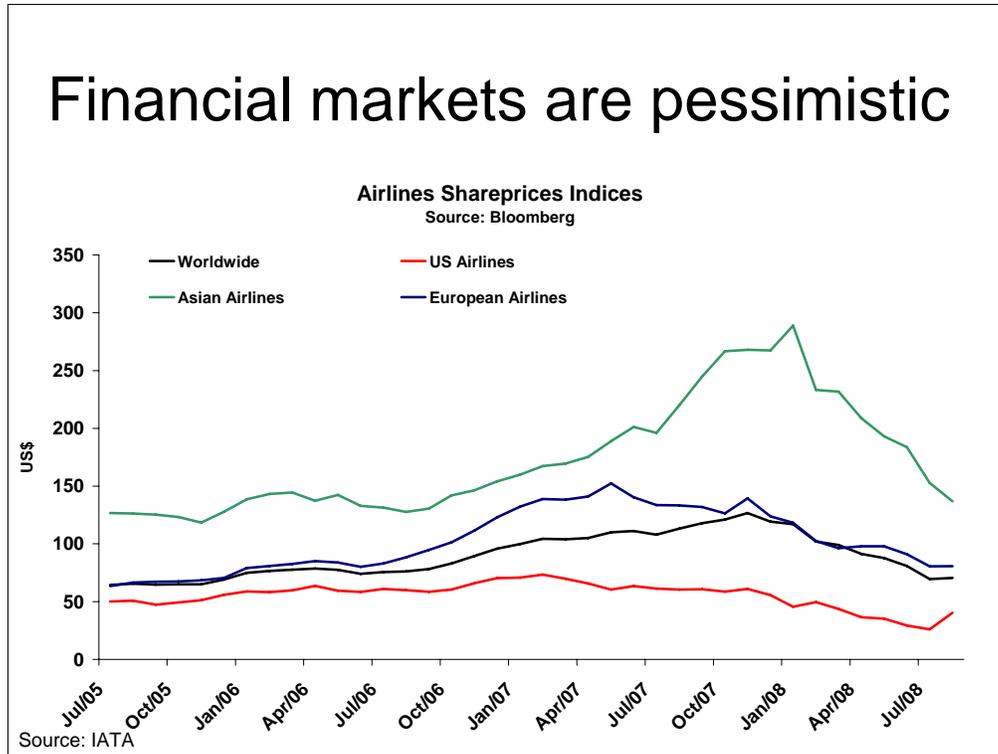
# Incremental improvements in efficiency are continuing



Airlines are no standing still. Efficiency improvements are continuing at an impressive pace.

However this incremental improvement is no match for the massive dislocation of demand that the industry is facing with the financial meltdown.

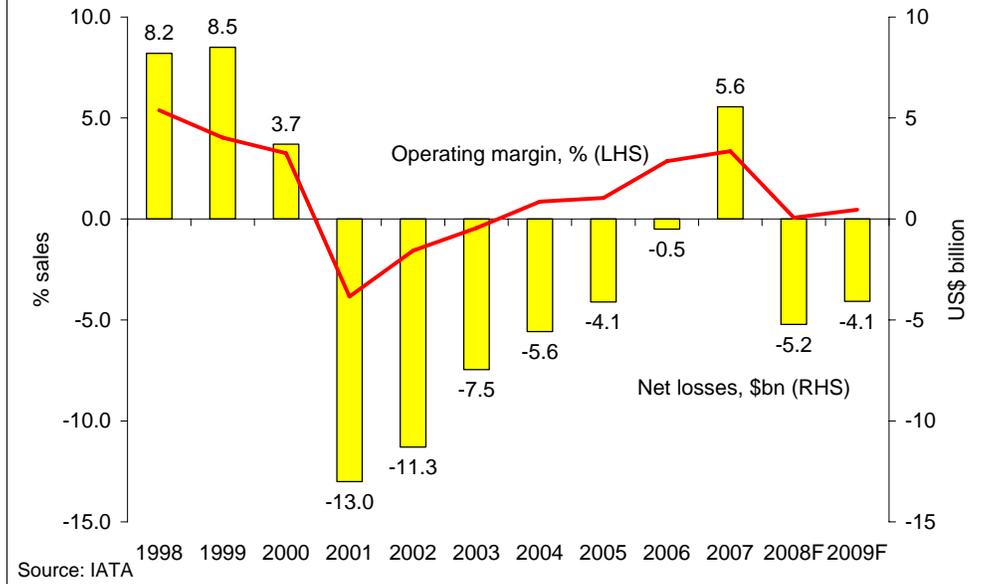
# Financial markets are pessimistic



Financial markets were pessimistic even before the latest meltdown (this shows share prices to the end of September).

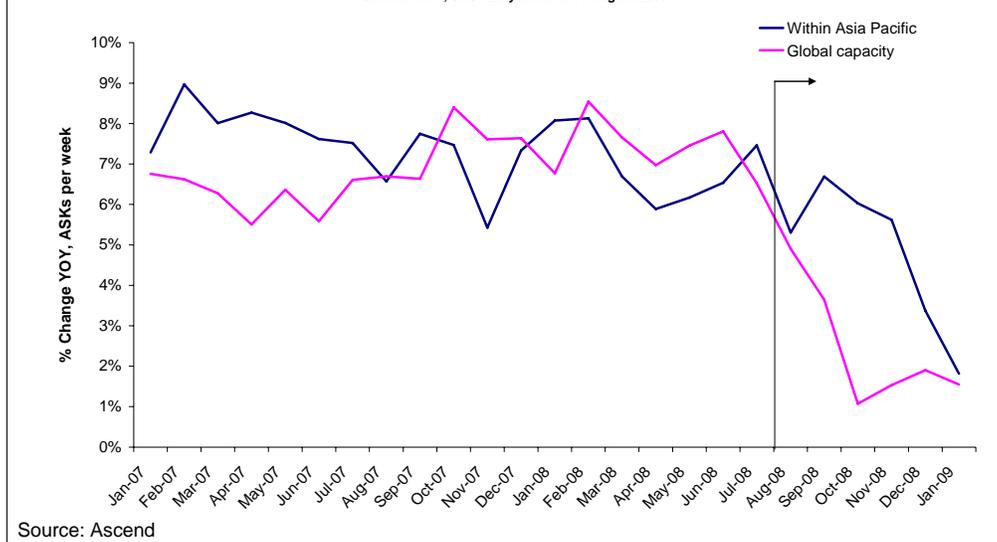
Share prices for A-P airlines have fallen 50% from their peak early last year.

## We forecast airline losses to continue into 2009



We see the industry losing \$5.2 billion this year. Fuel prices might be lower now and next year but the impact of recession or near recession on revenues will mean losses extending into 2009.

## Inevitably capacity growth will be cut - putting wider economic benefits at risk



Inevitably the only response of airlines is to cut capacity. These cuts are accentuated by the inability of the industry to consolidate across border and are certainly not as efficient as they would be if the industry had the commercial freedom of other global industries (don't mention banks!)

Cutting capacity may be the only response available for airlines to survive the current economic crisis. The problem is that it puts some of the wider economic benefits, that underpins A-P economic success, at risk.