

IATA ECONOMIC BRIEFING

PREMIUM TRAFFIC

AUGUST 2006

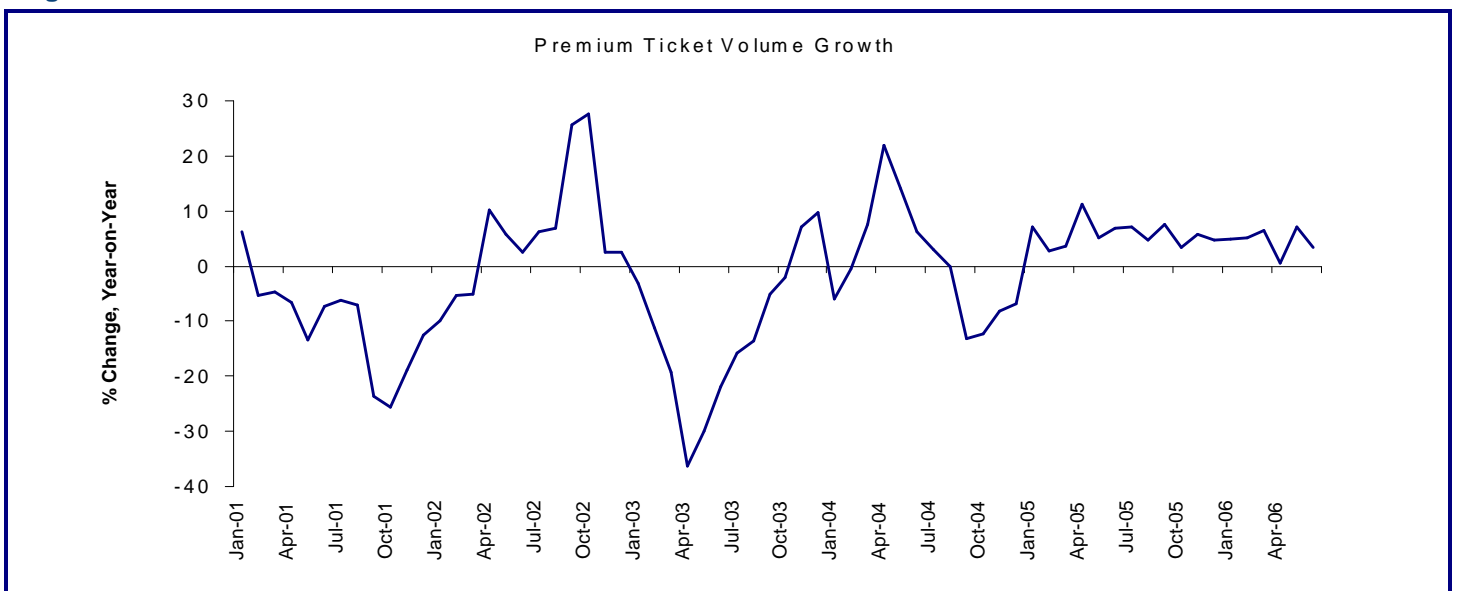
KEY POINTS

- Premium traffic (i.e. first or business class passengers) is a key source of revenue and profitability for airlines. The sustained period of growth in premium traffic over the last 18 months has been a key factor behind the recent strong revenue environment that has enabled the airline industry to improve operating profitability even though fuel costs have risen significantly.
- Premium traffic accounts for around 11% of total international traffic, with a higher share 14-15% on the major long-haul routes. Premium traffic volumes are highly concentrated, with five route areas accounting for 72% of all premium traffic, though faster growth on smaller routes in the Middle East and Asia, combined with structural changes in Europe, have seen this level of concentration fall from 82% for the top 5 routes in 2000.
- There has been a structural change in premium traffic within Europe, driven by strong competition on short-haul routes from “no-frills” airlines. By contrast, premium traffic on the major long-haul routes is linked more closely to the economic cycle, and has grown at a faster rate than total traffic on these routes since 2003.
- Premium traffic growth may be temporarily impacted by several factors, but the longer-term risk to premium traffic is primarily from a slowdown in the global economy. The key is whether higher economic growth in other regions can help to offset the impact of any US slowdown and support further growth of premium traffic into 2007 and beyond.

PREMIUM TRAFFIC GROWTH

- A premium traffic monitor has been developed from IATA's monthly Origin and Destination data collection. This monitor provides up-to-date information on premium traffic growth, both in aggregate and by route area.
- The monitor shows a period of strong and sustained growth over the last 18 months, with an average rate of growth of 5.6% since January 2005. By contrast, airlines faced a highly volatile and overall declining premium market between 2001 and 2004. The sustained growth in high-yield premium traffic has been very important for improved airline financial performance over the last year.

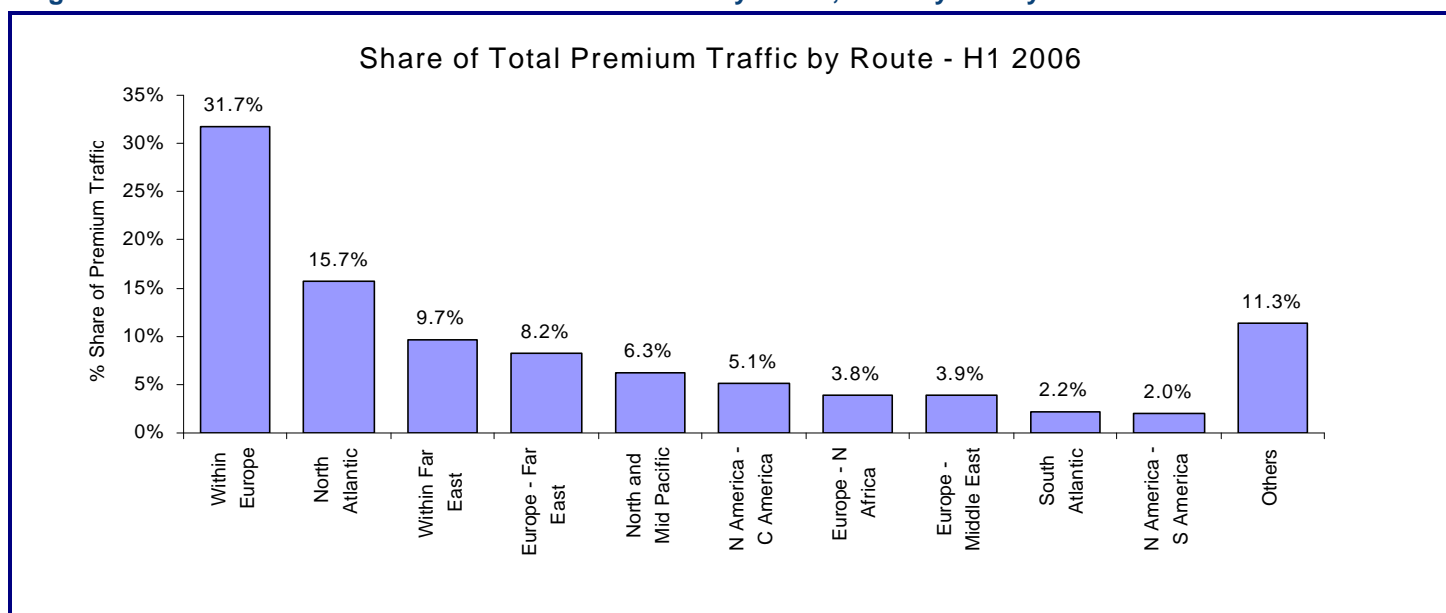
Figure 1: Premium Traffic Monitor



PREMIUM TRAFFIC BY ROUTE

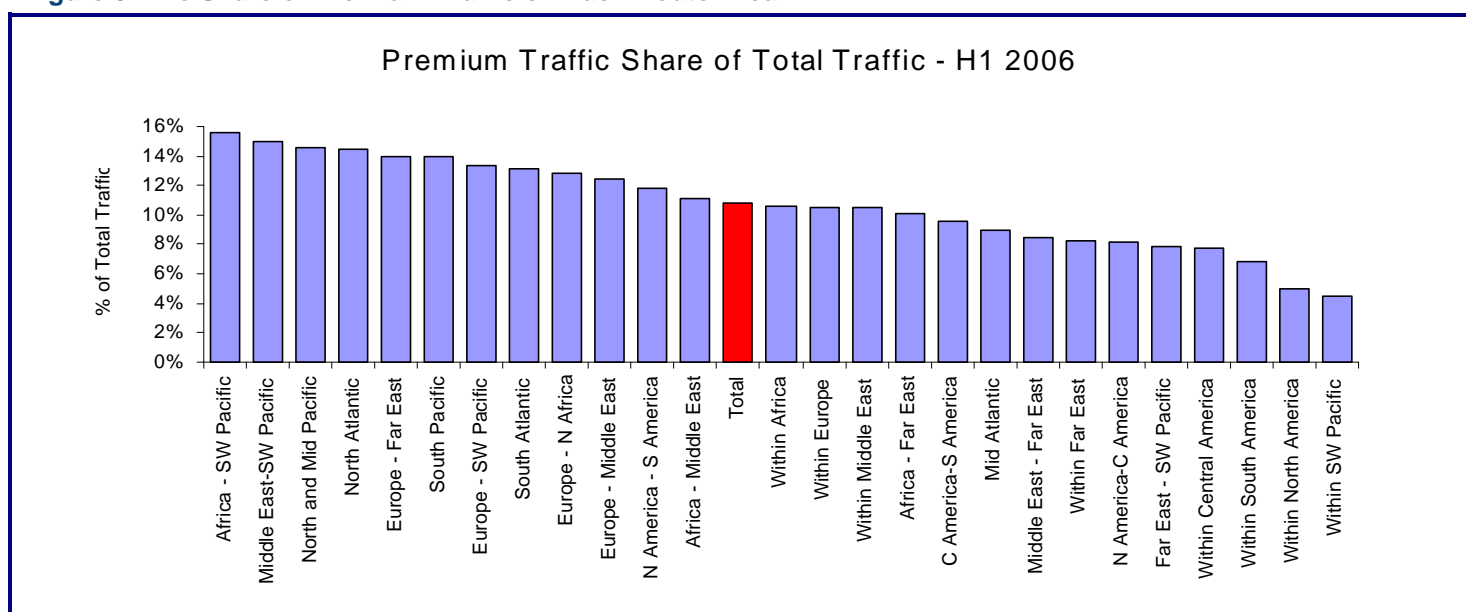
- International premium traffic is relatively concentrated, with routes within Europe accounting for just under a third of all premium traffic and the top 5 major route areas accounting for 72% of all premium traffic (see Figure 2). However, structural changes and fast-growing premium traffic on smaller Middle Eastern and Asian routes has seen the level of concentration fall in recent years. In 2000, routes within Europe accounted for 50% of all premium traffic and the top 5 route areas accounted for 82% of total premium traffic.

Figure 2: The Distribution of Premium Traffic Volumes by Route, January to May 2006



- On average, premium traffic accounted for 11% of total traffic in the first half of 2006 (see Figure 3). However, as expected, premium traffic typically accounts for a higher proportion of total traffic on long-haul routes than on short-haul routes. For example, premium traffic's share is 14-15% on Transpacific, North Atlantic and Europe to Far East routes compared to just 5% on US-Canada routes.

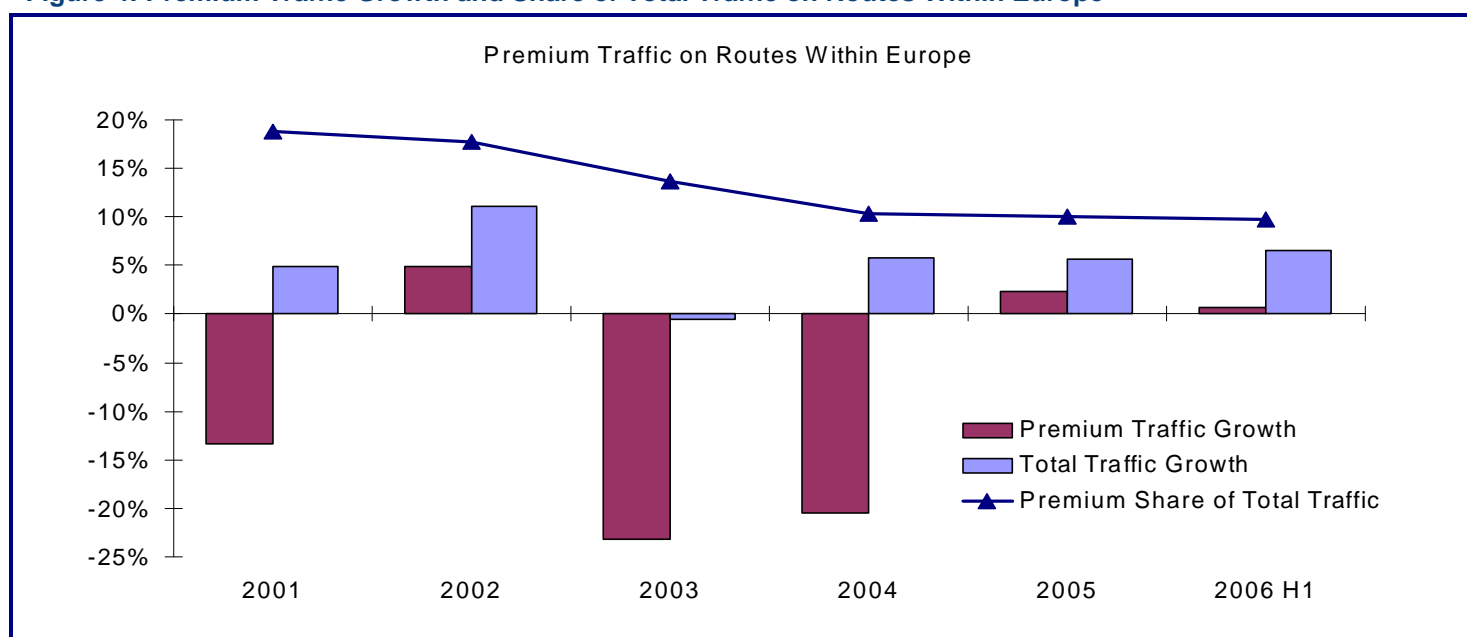
Figure 3: The Share of Premium Traffic on Each Route Area.



PREMIUM TRAFFIC WITHIN EUROPE

- Intra-European routes still account for nearly a third of international premium class passengers, but the structure and level of this traffic has changed significantly since 2000. Premium traffic volumes fell significantly between 2000 and 2004, with premium as a share of total traffic within Europe falling from 22% in 2000 to 10% in 2005 (see Figure 4). Premium traffic volumes have stabilised since 2005, but continue to grow at a much lower rate than economy-class traffic, at a time when the economic cycle in the Eurozone economies is moving into an upturn.

Figure 4: Premium Traffic Growth and Share of Total Traffic on Routes Within Europe

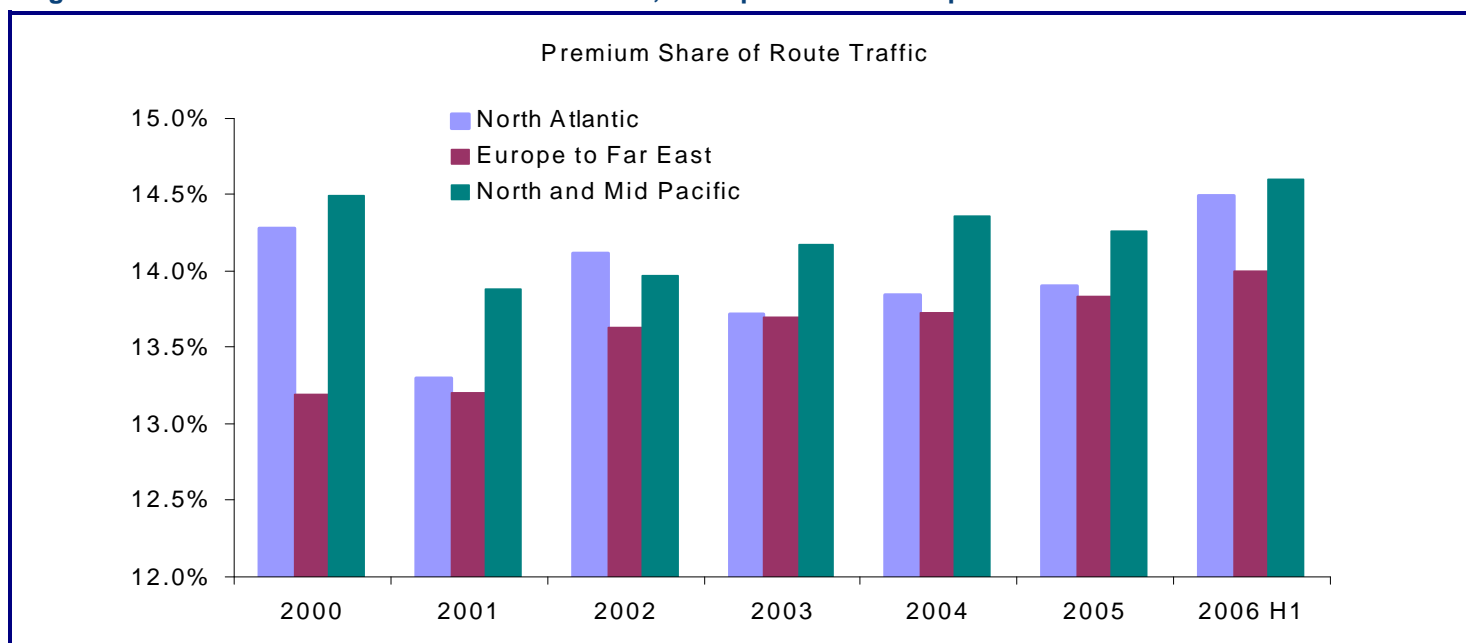


- The changes in premium traffic growth within Europe are structural as well as cyclical. The sharp fall in traffic between 2001 and 2004 will have been influenced by low European economic growth, but is also likely to reflect stronger competition on short-haul routes from “no-frills” airlines. On the demand side, constraints on corporate travel budgets have increased the attractiveness of economy class or “no-frills” airlines for short-haul business travel. On the supply side, efforts to reduce costs have seen some airlines remove the business class cabin from some short-haul routes (e.g. BA Connect).
- Nevertheless, network airlines can still attract profitable premium class traffic on short-haul routes by offering a higher-quality, efficient service. IATA’s recent report on [Airline Cost Performance](#) shows that though airlines such as Ryanair retain a significant cost-gap over the network airlines on intra-European routes, the higher quality service provided by network airlines continues to attract a revenue premium. There are still many competitive advantages in a high quality, efficiently delivered network model.

PREMIUM TRAFFIC ON OTHER ROUTES

- The structural changes seen within Europe have not been witnessed on the three main long-haul routes; North Atlantic, North and Mid Pacific and Europe to the Far East. Indeed, premium traffic has grown faster than total traffic on all of three of these routes since 2003, increasing the share of premium traffic on each route (see Figure 5).
- Premium traffic on these long-haul routes appears to be more driven by economic influences. Premium traffic on Europe to the Far East has increased strongly as trade and investment has increased between the regions in recent years. North Atlantic and Transpacific traffic fell in 2001 following the US economic slowdown and the September 11th attacks, but has since been boosted by strong growth in the US economy.
- The strong premium traffic growth on these major routes has been a major factor supporting the current strong revenue environment. This can be seen in significantly improved operating profitability for the airline industry in Q2 2006, even with current high oil prices.

Figure 5: Premium Traffic Share on North Atlantic, Transpacific and Europe to Far East Routes



- Premium traffic growth may be temporarily impacted by several factors, for example the conflict in Lebanon and by the security alert at UK airports. However, the longer-term risk to premium traffic is primarily from a slowdown in the global economy. US economic growth slowed in Q2 2006, which may be the signal of a period of slower growth for the US. The key is whether higher economic growth in Europe, the Middle East and Asia can help to offset the impact of any US slowdown and support further growth of premium traffic into 2007 and beyond.
- Indeed, strong economic growth in the Middle East and Asia is already feeding through into strong growth in premium traffic on some of the smaller routes to and from these regions (see Appendix). In particular, demand on routes to and from the Middle East has been boosted by higher oil-related incomes and new capacity in the region.

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APPENDIX: PREMIUM TRAFFIC GROWTH BY ROUTE

	Share of total Premium Traffic	Premium Traffic Growth	
		2005	H1 2006
Africa – Middle East	0.8%	19.0%	23.7%
Africa – SW Pacific	0.0%	2.4%	8.2%
C America – S America	0.3%	19.7%	-6.9%
Europe – Far East	8.2%	10.3%	11.2%
Europe – Middle East	3.9%	15.3%	11.4%
Europe – SW Pacific	0.2%	9.8%	-1.9%
Africa – Far East	0.2%	13.1%	13.0%
Within Africa	0.4%	2.1%	5.8%
Within Central America	0.2%	27.2%	17.1%
Within Far East	9.7%	5.5%	5.6%
Within Middle East	1.6%	11.0%	13.6%
Within N America	1.3%	-3.3%	-4.6%
Within SW Pacific	0.3%	7.7%	5.8%
Within South America	0.8%	3.9%	-5.7%
Mid Atlantic	1.1%	5.5%	4.9%
Middle East – Far East	1.8%	13.9%	14.3%
Middle East – SW Pacific	0.4%	44.3%	26.3%
North Atlantic	15.7%	5.3%	2.2%
N America – C America	5.1%	11.4%	13.1%
Europe – N Africa	3.8%	3.1%	6.0%
N America – S America	2.0%	4.8%	3.2%
Far East – SW Pacific	1.5%	10.8%	3.9%
North & Mid Pacific	6.3%	6.7%	4.5%
South Pacific	0.5%	15.4%	2.4%
South Atlantic	2.2%	9.2%	8.1%
Within Europe	31.7%	2.4%	0.6%
Total International	100.0%	5.9%	4.5%