



# IATA ECONOMIC BRIEFING

**JUNE 2007**

## AIRLINE FUEL AND LABOUR COST SHARE

- For the first time ever, **fuel replaced labour as the largest single cost item for the global airline industry in 2006**. Based on a sample of the financial reports of 45 major global (passenger) airlines, fuel accounted for 25.5% of total operating costs in 2006, up from 22.5% in 2005. By contrast, labour (including pension) expenses fell from 24.2% in 2005 to 23.3% in 2006.
- The rise in the share of fuel costs reflects the sharp increase in fuel prices faced by airlines. The **share of fuel costs was 12-13% between 2001 and 2003 but has since almost doubled** as the average price of jet fuel per barrel has risen from US\$34.7 in 2003 to US\$81.9 in 2006. The rise in the fuel price reflects a sharp increase in the price of crude oil over the period, but also reflects a widening in the refinery margin between crude oil and jet fuel due largely to capacity constraints at refineries. The widening of the refinery margin alone added an extra US\$14.7 billion to the industry's fuel cost in 2006.
- Airlines have responded to high fuel costs and severe financial pressures since 2001 by improving their efficiency of fuel use and by achieving large productivity and efficiency gains in non-fuel cost items. In particular, labour productivity (in terms of employees per available tonne kilometre) has improved by 56% over the period. As a result, **labour's share of total operating costs has fallen from 28.3% in 2001 to 23.3% in 2006**. Airlines have also achieved significant cost efficiencies in other areas such as distribution that have reduced the share of "other" costs (i.e. excluding payments to labour, fuel and capital) from 46.4% in 2001 to 41.7% in 2006.

## REGIONAL DIFFERENCES IN FUEL AND LABOUR COST SHARES

- There are significant regional differences between the shares of fuel and labour costs within total operating costs (see Table 1). In 2006, **labour's share of airline operating costs was 25-26% in North America and Europe but only 17.2% in Asia Pacific**, reflecting the relatively lower wage costs in that region. However, with relatively lower labour costs, fuel accounts for a much higher proportion of total costs (30.2%) in Asia Pacific than elsewhere.

**Table 1: Percentage Share of Airline Operating Costs, by Region of Airline Registration**

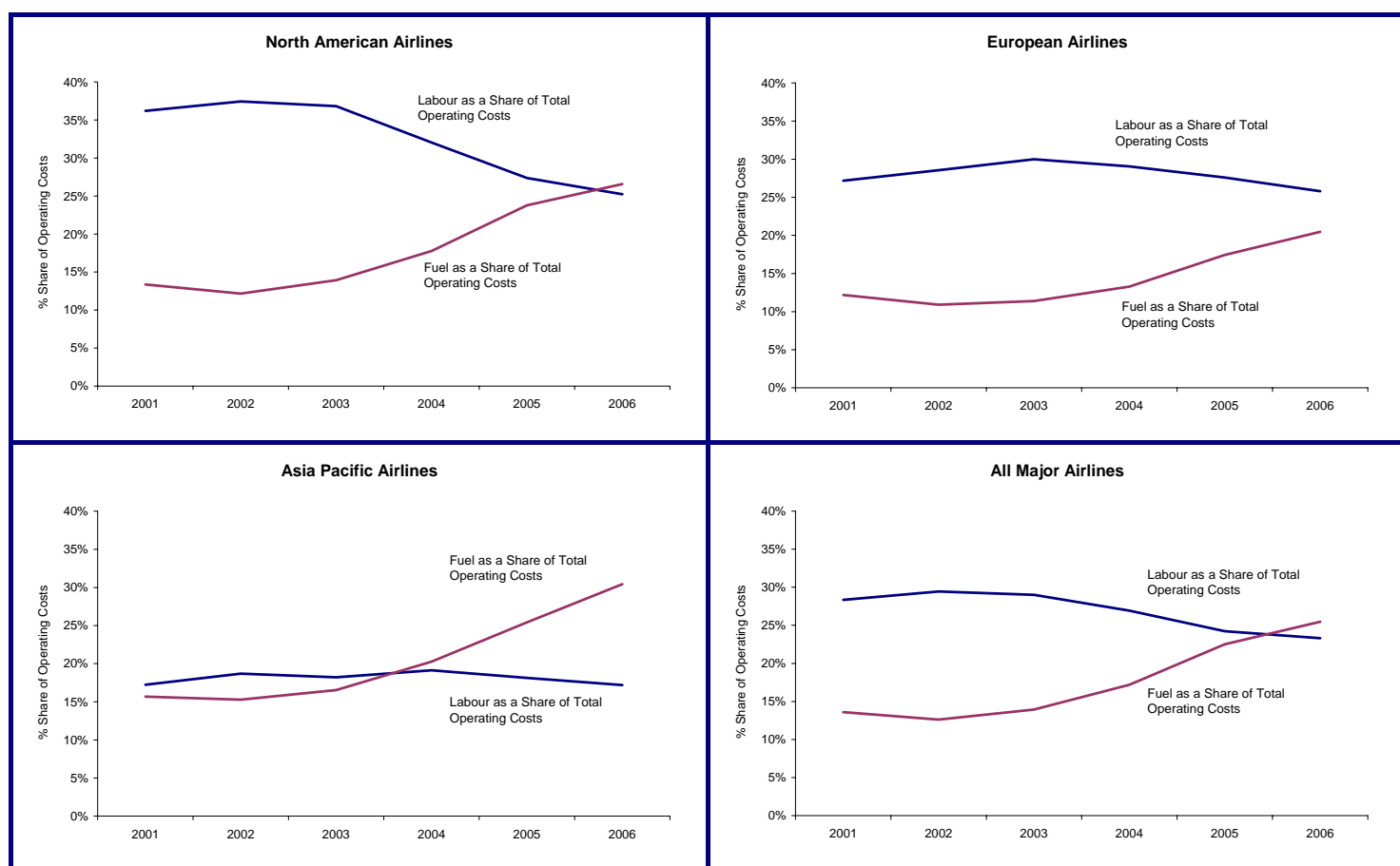
	North America		Europe		Asia Pacific		All Major Airlines	
	2001	2006	2001	2006	2001	2006	2001	2006
Labour	36.2%	25.2%	27.2%	25.8%	17.2%	17.2%	28.3%	23.3%
Fuel	13.4%	26.6%	12.2%	20.5%	15.7%	30.4%	13.6%	25.5%
Aircraft Rentals	5.5%	3.7%	2.9%	3.1%	6.3%	2.4%	5.0%	3.5%
Depreciation and Amortisation	6.0%	4.9%	7.1%	6.7%	7.4%	7.3%	6.7%	6.0%
Other	38.9%	39.6%	50.6%	43.9%	53.4%	42.7%	46.4%	41.7%

Source: Company Reports

- The large scale restructuring of North American airlines since 2001 – in some cases involving a period under Chapter 11 bankruptcy protection – has enabled them to achieve significant improvements in labour productivity and reductions in total labour costs. **Labour's share of total operating costs for North American airlines has fallen sharply from 36.2% in 2001 to 25.2% in 2006**. This reflects a sharp rise in the share of fuel costs over the same period, but also reflects much lower labour costs (including lower pension liabilities as a result of Chapter 11).

- **For European airlines, labour still accounted for a higher proportion of operating costs than fuel in 2006**, even though the gap has narrowed significantly since 2001 (see Figure 1). This partly reflects the greater commercial flexibility for European airlines to undertake financial hedging of their fuel costs that has provided some protection from the sharp rise in fuel costs. However, it is also likely to partly reflect the more diversified nature of some European airlines (e.g. Lufthansa), where more labour-intensive activities such as ground-handling and maintenance are included within the parent company's financial accounts.
- **With relatively low labour costs (in developing economies rather than in Japan, Australia and New Zealand), fuel has accounted for a higher share of costs than labour for Asia Pacific airlines since 2004**. As such, on a proportionate basis, Asia Pacific airlines have been more exposed to higher fuel costs than airlines in North America and Europe. Fuel accounted for 30.4% of operating costs for Asia Pacific airlines in 2006 and was as high as almost 40% for some airlines based in countries such as China.

Figure 1: Labour and Fuel Cost Shares, by Region of Airline Registration



## OUTLOOK

- IATA's June 2007 Financial Forecast (see: [www.iata.org/economics](http://www.iata.org/economics)) expects that fuel prices will soften slightly but remain very high over the next two years, with an average price per barrel of jet fuel of US\$80.0 in 2007 and US\$75.0 in 2008. At a global level, **fuel's share of total operating costs is expected to increase slightly further to 26.1% in 2007 before falling back to 24.7% in 2008**. The decline in 2008 reflects a combination of lower fuel prices, greater efficiencies in fuel use and cost pressure elsewhere as the industry expands to meet ongoing demand growth. The share of labour costs is likely to rise slightly (though remain much lower than in 2001) as more employees are needed to meet growth and as wage pressure increases, especially if labour skill shortages appear in some areas.