

# MONTHLY TRAFFIC ANALYSIS

## SEPTEMBER 2008

### KEY POINTS

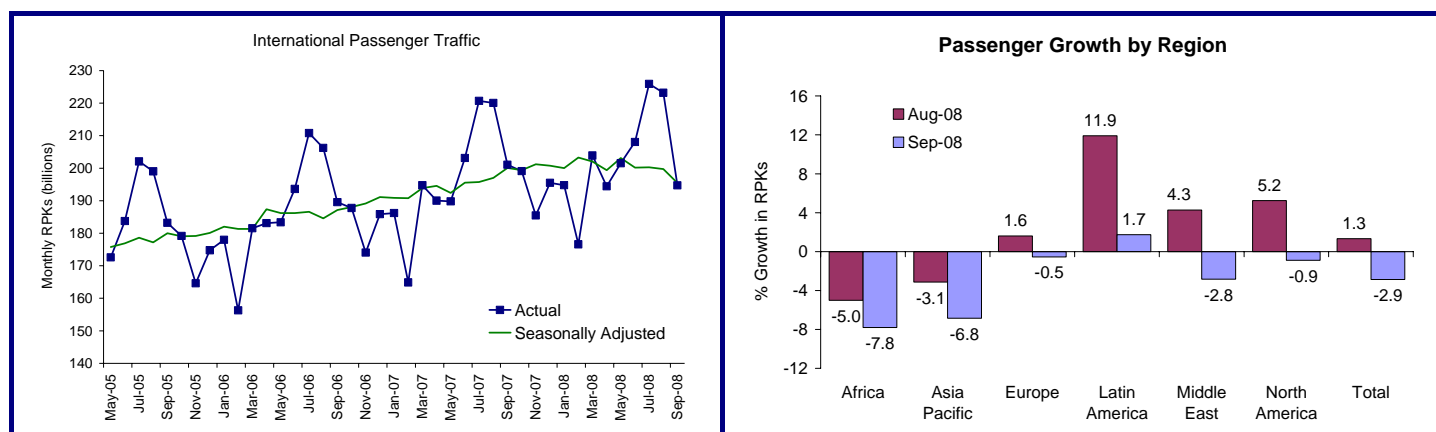
- International airlines traffic markets deteriorated very significantly in September, indicating a decline towards recession in the world's major economies even before the latest financial sector turmoil.
- Passenger traffic had been slowing sharply in July and August, after near-trend growth of 5.4% in the first half of this year. In August traffic grew by just 1.3%. However, data for September show traffic is now shrinking, with a decline of 2.9% over a year earlier.
- Weakness had been concentrated in Asia-Pacific, and this region weakened further in September. However, the widespread declines now also seen in Europe and N America indicate that air travel worldwide is now suffering from the intensifying economic downturn being experienced in many major economies around the world.
- Air freight weakened before passenger markets and fell even more in September to a level 7.7% lower than a year earlier. As with passenger markets weakness is now widespread, reflecting a sharp downturn in world trade. In the year to September air freight volumes are now only 0.1% higher than they were in 2007.
- Airlines reacted to the July fuel price spike by cutting capacity plans and there was a sharp slowdown in capacity in September. However, this was insufficient to keep pace with the unexpected collapse in demand. Load factors fell 3% points as a result. Although fuel prices have now halved since their July peak, hedging is delaying the full benefit of lower fuel costs. Meanwhile the scale of declines being seen in demand, on a \$500 billion revenue base, could easily swamp the benefits of lower fuel costs, potentially worsening the \$5.2 billion industry losses we forecast in early September.

	Sep 2008 vs. Sep 2007					YTD 2008 vs. YTD 2007				
	RPK Growth	ASK Growth	PLF	FTK Growth	ATK Growth	RPK Growth	ASK Growth	PLF	FTK Growth	ATK Growth
<b>Africa</b>	-7.8%	-4.7%	70.3	1.5%	-8.7%	-2.8%	-2.7%	69.9	-5.7%	-5.8%
<b>Asia/Pacific</b>	-6.8%	-1.1%	71.8	-10.6%	-4.9%	1.2%	3.3%	74.6	-2.3%	-0.5%
<b>Europe</b>	-0.5%	3.2%	77.3	-6.8%	1.1%	2.5%	4.6%	76.7	1.2%	3.7%
<b>Latin America</b>	1.7%	-0.8%	73.5	-14.6%	0.6%	12.2%	9.9%	74.7	-12.0%	7.5%
<b>Middle East</b>	-2.8%	4.2%	69.5	5.0%	5.6%	7.6%	9.1%	75.4	9.9%	9.9%
<b>North America</b>	-0.9%	0.6%	79.0	-6.0%	0.7%	4.9%	5.7%	80.6	3.0%	5.2%
<b>Industry</b>	-2.9%	1.1%	74.8	-7.7%	-0.9%	3.3%	4.8%	76.3	0.1%	3.0%

### INTERNATIONAL PASSENGER TRAFFIC IS NOW SHRINKING

- September marked a very sharp downturn in passenger traffic across all markets. It seems that many economies were moving into recession even before the latest turmoil in the financial sector. International air passenger markets in total shrank 2.9% in September, compared to a year earlier. This follows growth of 1.3% in August and near-trend growth of 5.4% in the first half of this year.
- Until September the sharpest declines in air travel had come from domestic markets, not international. ATA data shows the large US domestic market was down 6% in August. In Europe AEA airlines saw their domestic traffic shrink 7.9% in the 12 months to August, and then a further 10.4% decline in September. The domestic market in India was reportedly down 18% in September. The only good news was evidence of a rebound in domestic passenger traffic in China in September, following the restrictions associated with the Olympics in earlier months. Overall global air travel must have been shrinking in September.

- ↗ International traffic carried by Asia-Pacific airlines had led the decline since July and there was a further sharp decline in this region with passenger-kilometres flown down 6.8%. Economic growth did slow in China during the third quarter with 9% GDP growth, down from 10.1% in the second quarter. However, in most developed travel markets this would generate slower rather than declining air travel; but international air travel is still shrinking in China. The Indian economy seems to have slowed more precipitously than China, with barely 1% growth in industrial output in August, following growth of 5-8% during earlier months. Moreover, the largest regional travel markets are still associated with Japan and there industrial production shrank 5% in August after earlier growth in the region of 2-3%. It is now becoming clear that there has been a sharp downturn in world trade, which has disproportionately damaged air travel (and air freight) in the region.
- ↗ European airlines saw the traffic they carried on international markets decline for the first time since the SARS outbreak in 2003. International passenger kilometres flown were down 0.5% in September, on top of a steep decline in domestic traffic. European economies have weakened significantly in recent months. The UK is now thought to be in recession together with parts of southern Europe, with GDP falling, while the previously robust economies of Germany and France have seen declining industrial output and sharp declines in business and consumer confidence. Intra-European international travel will have made up much of the decline seen by European airlines. However, traffic on long-haul markets to Asia and N America also declined in September, according to AEA data. The economic weakness now driving travel markets downwards is widespread.
- ↗ Perhaps the most striking change in trend has been for the North American airlines, who were steadily increasing international traffic at a rate of around 5% through to August. This changed abruptly in September with a 0.9% decline in their international traffic. ATA data had showed that Pacific markets were in decline, reflecting the weakness in Asia already discussed. However, traffic across the Atlantic and to the previously strong South American economies had been remarkably strong. We do not have this market detail so far but it would seem that spreading economic weakness in September is leading to more widespread travel market damage.
- ↗ Another striking change was the 2.8% decline in passenger traffic carried by Middle Eastern airlines, which until recently had been growing steadily in double figures for a number of years in response to substantial investment in capacity and new services. The oil producing economies in the region remain very strong and investment in tourism facilities continues. However, much of the traffic carried by the Middle Eastern airlines is 6<sup>th</sup> freedom traffic carried, for example, between Europe and Asia over Middle Eastern hubs. As a result the airlines in this region are just as exposed to the economic slowdown now intensifying and spreading. African airlines continued to see traffic and market share shrink during September. The only region to see any growth was Latin America, but growth of 1.7% was very different to the 11.9% expansion seen just the previous month.

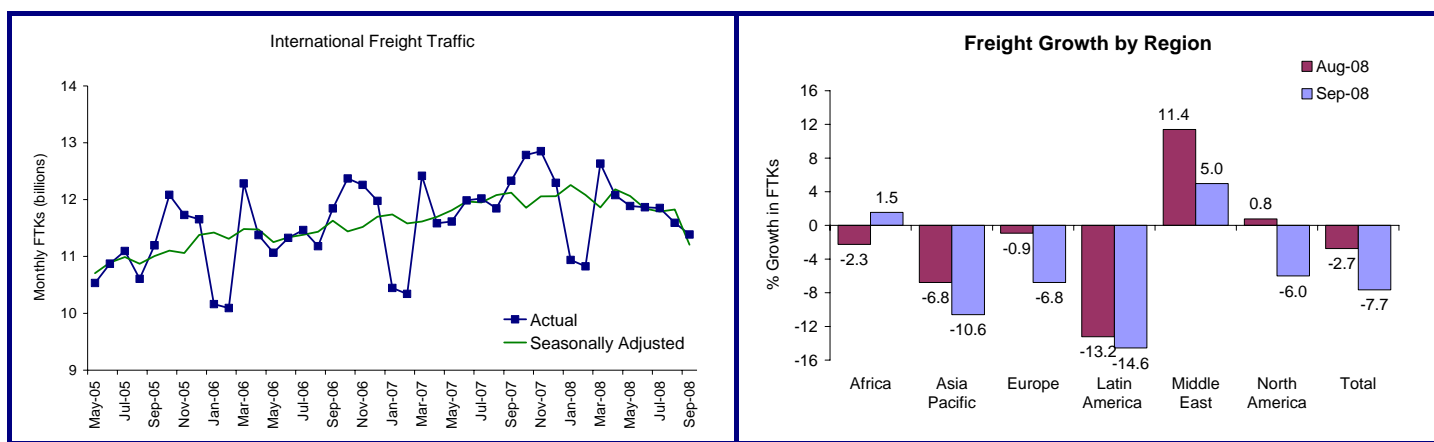


## SHRINKAGE IN FREIGHT VOLUMES HITS NEW LOWS

- ↗ Air freight tonne kilometres flown fell dramatically from a decline of 2.7% in August to a level 7.7% lower than 12 months earlier. The chart below shows that the level of air freight volumes, after adjusting for seasonality (much less than for passenger travel), was down 5% month-on-month. In other words air freight volumes were declining at an annualised rate of almost 50% in September. There is often sampling error and other noise in

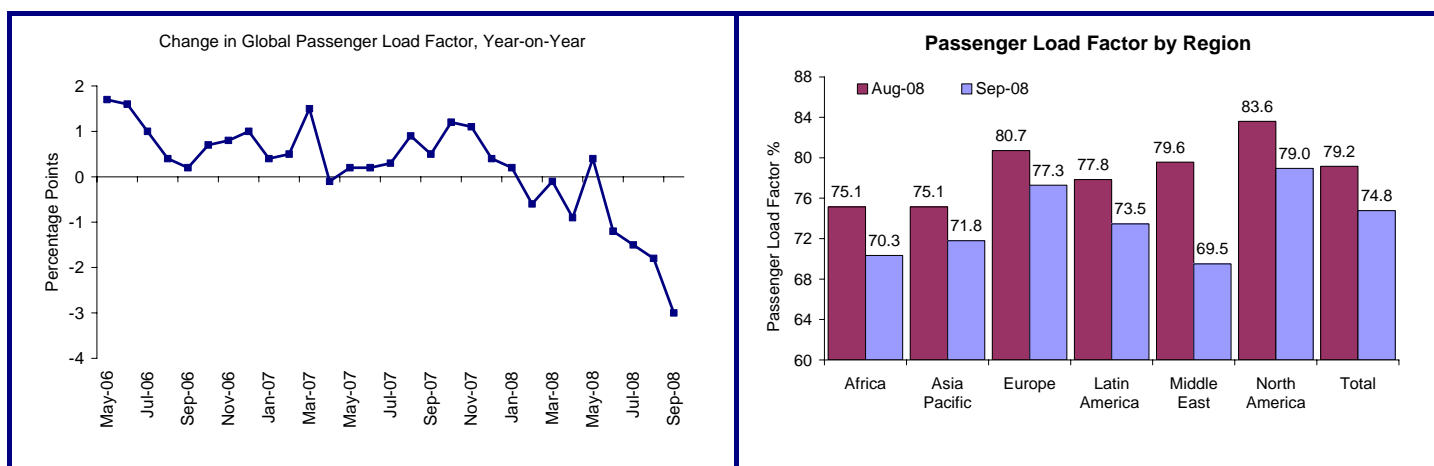
these month to month movements, but even so the speed of the decline in air freight is alarming and clearly points to a significant weakening in world trade in Q3.

- These latest declines mean that in the year to September air freight volumes are now no higher than they were last year. It is almost inevitable that total 2008 air freight volumes will be lower than they were last year. The air freight industry is already entering recession.
- All of the large regions are now facing declining air freight volumes. As with the passenger markets, the most recent weakness has been led by Asia-Pacific which had not been expected given regional economic growth. However, the economic data for India and Japan point to a sharp downturn in goods exports, which are what sustains air freight markets. Asia-Pacific airlines saw air freight volumes fall over 10% in September. But there were big changes for airlines in Europe and N America, where air freight had been more or less flat in August. Airlines in both regions saw freight volumes decline by more than 6%, reflecting the intensification of the economic downturn in these regions and the long-haul markets they serve.



## LOAD FACTORS DOWN AS FALLING DEMAND OUTPACES CAPACITY CUTS

- From the industry's perspective the most worrying aspect of September's market developments was that demand fell away much more rapidly than airlines were able to adjust capacity. Capacity (ASKs) grew just 1.1% in September, in spite of new aircraft deliveries of just under 100, which is a sharp slowdown from the 5-7% growth of earlier in the year. These actions from airlines, originally motivated by the July spike in fuel prices, have so far been insufficient to keep pace with the fall in demand. Load factors have fallen very significantly as a result, down 3% points in September. The decline was largest for Middle Eastern airlines with a 5% point fall, followed by Asia-Pacific airlines with a 4.4% decline and then European airlines who load factors fell 2.9%.
- Spot fuel prices are now almost exactly 50% lower than their July spike but hedging is delaying the benefit from lower fuel costs. Meanwhile the sort of traffic declines now being experienced on a \$500 billion revenue base could easily swamp lower fuel costs, causing industry losses to exceed the \$5.2 billion anticipated for 2008 in our early September forecast.



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