# Lower fuel costs deliver profit bonanza for US majors

**Lower fuel costs over the past year have further improved the impressive operating profit performance of the US majors. Average spot fuel price has fallen by 85 cents per US Gallon, generating annual pro-rata savings of $11 billion.**

Lower fuel costs and robust travel demand continue to positively impact the balance sheets of US airlines. Analysis shows that, compared to the same quarter in 2014, the six US major carriers (American, Alaska, Delta, jetBlue, Southwest and United) recorded a 49% higher operating profit in the first quarter of 2015.

These carriers posted their most profitable results since 2007 in the second quarter of 2015 (2Q 2015). Fuel costs have fallen by 30% since the same period last year.

Jet fuel prices closely follow the price of Brent crude oil. On average, a barrel of Brent crude oil was about 43% lower in 2Q 2015, as compared to the second quarter of 2014.

The average daily spot price for Brent crude oil during 2Q 2015 was $62 per barrel, compared to $109 per barrel during the second quarter of 2014. Brent crude has since continued to fall. It has been less than $50 per barrel in the third quarter of 2015.

On a daily basis, Brent crude oil prices fluctuated during Q2 2015 between a high of $66 per barrel to a low of $56 per barrel, and closed the quarter on 30 June 2015 at $60 per barrel.

While hedging can insure against soaring fuel costs, as it did for Southwest Airlines a decade ago, in recent months carriers, such as American Airlines, which did not hedge, have emerged as winners.

The six major US scheduled passenger airlines reported an operating profit of $7.53 billion in 2Q 2015, up from $5.09 billion in the same quarter of 2014, an increase of 48%. The collective operating margin for the six carriers during 2Q 2015 is 21.9%, a margin previously considered to be unattainable. Alaska Airlines recorded the highest operating margin, at 27.1%.

This is the highest margin since the carriers collected $5.9 billion in the same period in 2007.

The latest financial data show the airlines remain on a firm footing after first managing to make substantial cuts in non-fuel costs, and subsequently enjoying the bonanza of the drop in fuel prices.

Detailed analysis of each airline's fuel consumption and unit fuel costs shows that fuel consumption, and total size of operations in generated available seat-miles (ASMs), has changed by just a few per cent. Fuel consumption fell by 0.15% compared to the same quarter of 2014, while ASMs increased by 4.4%, showing an improvement in fuel efficiency of operations.

The 49% improvement in operating margins is due mainly to a reduction in fuel cost for the six airlines of $2.5 billion, a fall of more than 33%. The saving is equal to 1.07 cents per ASM.

The largest drop in fuel price was recorded by American Airlines, which paid 105 cents less per US Gallon (USG) compared to 2014. The average drop for the six airlines was 72 cents, with a relatively high fuel price drop of 87-94 cents per USG recorded by Alaska, jetBlue, Southwest and United. Delta had a smaller drop of just 43 cents per USG.

Despite the large fall in fuel costs, other non-fuel operating costs have dropped by almost $500 million, equal to a decline of 2.5%. The rise in ASMs by 4.4% indicates that airlines are still making good progress in reducing their non-fuel operating costs, and increasing productivity.

The fall in non-fuel costs almost matches the six major airlines' drop in revenues over the past year. Although ASMs have increased, traffic revenue passenger-miles (RPMs) have not gone up by the same proportion. This indicates that airlines have increased capacity to take advantage of low fuel prices. The rise in capacity is reflected by a drop in passenger yields that resulted in the lower revenues.

Total operating revenue for the six US major passenger airlines in 2Q 2015 was


*Alaska Airlines recorded the highest operating margin of 27.1% of the six major US carriers in 2Q 2015. It has persistently outperformed most other US carriers over the past 10 years.*

## US MAJORS 2Q 2015 FINANCIAL RESULTS

| Airline | American Airlines | Alaska Airlines | Delta Air Lines | jetBlue Airways | Southwest | United Airlines | TOTAL |
|---|---|---|---|---|---|---|---|
| Revenues - $m | 9,068 | 1,203 | 9,155 | 1,612 | 5,111 | 8,199 | 34,348 |
| Fuel costs - $m | 1,774 | 232 | 2,170 | 371 | 1,005 | 1,765 | 7,317 |
| Non-fuel costs - $m | 5,373 | 645 | 4,511 | 959 | 3,021 | 4,989 | 19,498 |
| Total costs - $m | 7,147 | 877 | 6,681 | 1,330 | 4,026 | 6,754 | 26,815 |
| Operating profit - $m | 1,921 | 326 | 2,474 | 282 | 1,085 | 1,445 | 7,533 |
| Operating margin | 21.2% | 27.1% | 27.0% | 17.5% | 21.2% | 17.6% | 21.9% |
| Fuel price - cents/USG | 189 | 211 | 247 | 213 | 204 | 212 | 214 |

Source: Airline Monitor

$34.35 billion. This compares to $34.91 billion for the same period in 2014.

The highest operating profit during 2Q 2015 in absolute dollars was recorded by American Airlines, at $1.92 billion, equal to an operating margin of 21.2%

The highest operating margin performance was 27.1%, recorded by Alaska. This was closely followed by Delta, with a 27.0% margin, despite seeing the smallest drop in fuel price.

The biggest operating profit increase was also reported by Delta. It generated an operating margin of $2.47 billion during the period, an improvement of $850 million over 2014. Despite growing capacity by almost 3 billion RPMs, it saved $261 million in fuel and $608 in non-fuel costs. Delta is the second-largest carrier in terms of ASMs. Its fleet comprises 800 aircraft with an average age of 16.9 years.

American Airlines has become both the largest major US and global carrier following its merger with US Airways in 2013. American Airlines generated nearly 62 billion ASMs in 2Q 2015, a small increase on 2014. Despite the growth of the airline's operation, its revenues declined. It was able to offset this through a small reduction in non-fuel costs and the large saving of $984 million it realised in fuel expenditure.

During the second quarter of 2014 American sold its portfolio of fuel hedging contracts that were scheduled to settle on or after 30 June 2014.

American has not entered into any contracts to hedge fuel consumption since 9 December 2013 and, as of 30 June 2015, has had no such contracts in place.

Assuming no future fuel consumption hedges, American will continue to be fully exposed to fluctuations in fuel prices. It has clearly managed to benefit from this over the past year.

American also announced a significant cost-containment measure in June, deferring delivery of 35 A320neo aircraft from 2017 and 2018 until after 2020. It still anticipates taking delivery of about 75 new aircraft in 2017 and 2018. American's fleet comprises 963 aircraft, with an average age of 12.4 years.

Alaska's active all-Boeing fleet comprises 140 aircraft with an average age of 9.5 years.

Alaska's record margin of 27.1% for 2Q 2015 came from an overall revenue of $1.20 billion and total costs of $877 million. It gained from a large drop in fuel costs, with the unit fuel price falling by 94 cents per USG and $78 million. This alone reduced total costs by 8.5%.

Alaska increased capacity by more than 11%, the largest rate of growth of the six US majors. In contrast, its non-fuel costs rose by 6.4%, indicating an improvement in overall efficiency. While its overall unit revenue per ASM fell by 1.13 cents, its unit cost fell faster by 1.58 cents per ASM. Alaska's already impressive operating performance of 21.9% in the second quarter of 2014 improved still further to 27.1% in the same period of 2015.

jetBlue Airways reported overall revenue of $1.61 billion for 2Q 2015, against $1.48 billion for the same quarter of 2014. The airline grew its operation by 7.4% over the year, the second-largest growth of the six US majors.

jetBlue's fuel expenses dropped from $483 million in the second quarter of last year to $371.0 million for 2Q 2015, a saving of $112 million. The airline consumed 8% more fuel compared with the same period of 2014, but its unit fuel cost was 87 cents per USG lower.

In 2Q 2015 jetBlue had hedges in place for about 19% of its fuel consumption, resulting in a realised fuel price of $2.13 per USG.

jetBlue recorded $30.0 million in losses on fuel hedges settling during 2Q 2015.

jetBlue has hedged 14% of its third quarter of 2015 projected fuel requirements, using a combination of jet fuel swaps and collars. It will pay spot rates for the remaining 86% of its fuel. jetBlue has also hedged 15% of projected fuel consumption for the last quarter of 2015. The jetBlue fleet of 209, mostly Airbus aircraft, includes 60 E-190s.

Low-cost carrier Southwest Airlines posted the same operating margin as American Airlines, at 21.2%. This was $1.08 billion on revenues of $5.11 billion and was a $309 million higher operating profit compared to the same 2014 period.

Southwest's unit fuel price was 88 cents per USG lower than in 2014, and it spent $365 million less for fuel compared to the same quarter in 2014.

For 2Q 2015, Southwest had no active 'economic' hedge in place for its estimated fuel consumption. The carrier previously had hedges in place that were subsequently offset.

Southwest operates an all-737 fleet of 670 aircraft with an average age of 11.7 years.

United Airlines posted reduced revenue of $8.20 billion for 2Q 2015, a fall of $194 million from the same quarter in 2014.

Total costs, however, dropped by $733 million from $7.49 billion in the second quarter of 2014 to $6.75 billion in 2Q 2015.

United's fuel bill was reduced by $709 million to $1.77 billion for 2Q 2015. This came from a combination of a 1.35% rise in consumption and an 89 cents per USG or 29.5% drop in unit fuel price. The airline also grew the size of its operation by 3.6%, but still managed to marginally reduce non-fuel costs.

United Continental Holdings, parent of United Airlines, closed out in January almost all of its remaining fuel hedges for the first quarter, as sinking oil prices were expected to result in hedge losses of close to $1 billion for 2015.

In July 2015, however, United Continental added new hedges against a rise in oil prices.

United operates a fleet of 709 aircraft with an average age of 13.4 years. AC