Money makes the world go round

With a sharp jump in the US economy, airlines have experienced improvements in traffic volumes and consequently yields. Combined with tight cost controls, most airlines in the US have managed to increase margins between unit revenue and cost and have reported impressive results for the third quarter. Forecasts are that this will continue for most into the fourth quarter and 2004.

A turnaround in the fortunes of major US carriers seems to be under way, after most reported third quarter operating profits and improvements in traffic, passenger yields and unit revenues. The main factor has been an improvement in yields, a result of the fast recovering US economy. Only a minority of airlines have reported operating losses.

The leading carriers with improved performance are JetBlue, AirTran, Frontier, America West and Alaska. Virtually all US majors are now expected to make operating profits in 2004, while some will show a profit for 2003.

AirTran

AirTran experienced the third highest increase in revenues and traffic of all major US carriers, and has one of the highest margins between unit revenue and cost. AirTran's revenue traffic, in revenue passenger miles (RPMs) rose by 33.9% over the year and revenues climbed 29.8% to $238 million. Capacity, in available seat-miles (ASMs) only rose by 21.3% and costs by 20.2%. These large rises in traffic and revenue over capacity and costs increased load factor to 73.4% saw unit revenue increase by 7.0% to 9.13 cents. Unit costs in cents per available seat-mile (CASM) are 8.11, leaving a 1.0 cent margin, one of the highest of all US airlines *(see table, page 5)*.

Alaska Airlines

Alaska generated an operating profit of $79 million in the three months to 30 September *(see table, page 5)* on a turnover of $702 million. This represents a 11.2% operating margin.

Revenues were 13.1% up on the year, while costs increased by just 4.8%. RPMs were up 12.3%, resulting in a load factor of 72.5%.

Alaska had 1.3% higher passenger yields, resulting in a 3.0% increase in unit revenues per available seat-mile (RASM) of 10.1 cents, compared to a unit CASM 9.24 cents. CASM, excluding fuel and extraordinary items, was 7.8 cents. Alaska has a programme to reduce CASM (excluding fuel) to 7.25 cents.

American Airlines

American Airlines, which was suffering particularly badly in the first quarter of 2003 with an operating loss of $1.32 billion, generated an operating margin of $185 million in the three months to 30 September. This is 3.6% of turnover *(see table, page 5)*.

American did not experience a high revenue increase, but managed to cut costs by 24% over the year. This reduction compares to a 6.3% reduction in capacity and only 1.1% lower traffic. The cost reduction is attributed to a simplified fleet structure and 'de-peaking' on various hub operations, which have increased aircraft utilisation and allowed American to reduce its aircraft fleet.

The airline has managed an increase in passenger yields, of 2.5%. This has led to a 8.0% increase in RASM to 9.78 cents; the first rise achieved by American since the first quarter of 2001. This compares a CASM of 9.49 cents, down by 8.0% from 10.37 cents a year before.

American has so far reduced its labour bill by $1.4 billion our of a targeted annual reduction of $2 billion.

America West

America West has lead the industry out of recession since 11 September 2001, starting with a simplified fare system that has saw improvements in RASM.

Revenues were up 13.8% on the year to $592 million, while costs were down by 3.3% to $542 million, resulting in an operating profit of $50 million; 8.5% of turnover *(see table, page 5)*.

America West has gained from an increase of 5.2% in RPMs and 7.3% in passenger yield, and a decrease of 1.2% in ASMs over the year. Overall this resulted in an increase in RASM of 15.4% to 8.24 cents, while unit CASM was down by 2.3% to 7.57 cents. Cost reductions have also been aided by a 33% fall in fare commissions; part of the carrier's simplified fare structure.

America West has also revised its plans for 2004 and will now have a 9.0% increase in ASMs, on the basis of a forecast 10% rise in revenues and 8.0% increase in traffic.

Continental

Continental has also shown a strong recovery, with its second consecutive quarterly operating profit (after recording an operating loss of $224 million in the first quarter) and its first net profit in two years. Like all other US majors, Continental has gained from higher traffic and passenger yields.

Continental has a large international network and has been one major to suffer the effects of the SARS crisis in the Asia Pacific. Traffic began to recover in the third quarter with an overall increase of 3.2% over the previous year. Revenues climbed faster, with an 8.6% increase. Costs, in contrast, only increased by 2.8%, and ASMs were actually 2.3% lower. This all led to an improved operating profit margin of $174 million, which is equal to an impressive 7.4% of revenue, and is the highest of all network carriers for the quarter. Moreover, Continental is expected to make an operating profit of $209 million for 2003, although a lower result of $174 million is forecast for 2004.

Unit RASM for the whole network rose 6.6% over the year to a network average of 9.81 cents, indicating an overall market recovery, but also for trans-Pacific traffic. The highest gain in unit revenues were 6.9% for the domestic US market, 5.7% for the Latin American sector and 2.2% for the transatlantic. Unit revenues were still 5.5% lower on the year for the trans-Pacific, but was still an improvement over the second quarter.

Unit CASM was 9.01 cents, making a respectable margin of 0.80 cents.

Delta Airlines

Although Delta has also experienced higher unit revenues, its traffic was down 5.7% over the year, leading to an operating loss of $81 million. Delta is one of the few US majors to suffer a fall in traffic for the third quarter. Delta also, however, managed to reduce ASMs by 9.4%, leading to an improved load factor. This contributed to better unit revenues and prevented a larger loss.

Unit RASM was up 8% to 9.98 cents, while unit CASM was down slightly at 10.23 cents, generating a negative difference of 0.25 cents. Unit revenues were up on all sectors of its network except for the trans-Pacific, which is still recovering from the SARS outbreak.

Delta's main problem is a high CASM, and is among the highest of all US majors. Moreover, no reduction in CASM is expected for 2004. A better operating performance and smaller loss are forecast because of improved traffic and revenues. Delta, however, has a long-term objective to reduce CASM by 15% to 8.5 cents.

US AIRLINE OPERATING RESULTS THIRD QUARTER 30 SEPTEMBER 2003

Airline	AirTran	Alaska	American	America West	Continental	Delta
Load factor-%	73.4	72.5	73.4	79.8	80.0	78.0
Revenues ($m)	238	702	4,605	592	2,365	3,443
Costs ($m)	211	623	4,440	542	2,191	3,524
Operating profit ($M)	27	79	185.0	50.0	174.0	(81.0)
RASM	9.13	10.10	9.78	8.24	9.81	9.98
CASM	8.11	9.24	9.49	7.57	9.01	10.23
Margin: C/ASM	1.02	0.86	0.39	0.67	0.80	(0.25)

Airline	Frontier	JetBlue	Northwest	Southwest	Westjet
Load factor-%	76.6	87.7	81.4	70.5	76.4
Revenues ($m)	165.8	273.6	2,556	1,553	253.9
Costs ($m)	143.5	219.7	2,410	1,368	200.6
Operating profit ($M)	22.3	53.8	146.0	185.0	53.2
RASM	9.63	7.38	9.83	8.53	13.4
CASM	8.34	5.93	9.13	7.51	10.6
Margin: C/ASM	1.29	1.45	0.70	1.02	2.8

Source: Merrill Lynch

Frontier

Frontier achieved one of the most impressive results of all US carriers in the third quarter. It had the second highest gain in revenues: a jump of 38.9% to $165.8 million. This was in hand with a 4.28% increase in RPMs. This outpaced increases of 15.7% in operating costs and 10.4% in ASMs, allowing a large increase in operating margin from a negative result of -3.9% of revenue in the third quarter in 2002 to a positive margin of 13.5% in 2003: equal to $22.3 million.

Frontier managed a large jump in traffic compared to capacity, increasing load factor by 17.4 percentage points and unit revenue by 25.9%. Average yield, however, fell 4%.

The increase in load factor was the main factor that widened the gap between RASM and CASM to 1.30 cents. Frontier, however, also allowed unit cost to increase by about 5%.

JetBlue

JetBlue continues to be the star of the show, with a 72.1% increase in RPMs of and a 65.5% gain in revenues to $273.6 million. These increases outpaced rises in capacity and costs of 66.3% and 53.9%. This led to increased load factor and improved profit performance, despite suffering 4.1% lower yields.

JetBlue generated an operating profit of $53.8 million; a margin of 19.7% of revenue. JetBlue has also managed to reduce unit cost by 7.5% to 5.93 cents, and generated a margin of 1.45 cents; one of the highest of all US airlines.

Further high rates of growth are expected in 2004, and the carrier is forecast to maintain the lowest unit cost of all US carriers at 6.14 cents.

Northwest

Northwest made its first real operating profit for several years, with an operating margin of $146 million, equal to 5.7% of turnover. Like most other carriers, Northwest has seen yields and unit revenues increase, although it has had to deal with a 4.1% fall in traffic as a consequence of the SARS outbreak the spring. This led to a small fall in revenues during the quarter, with the 2.0% increase in yields offsetting the lower passenger numbers.

Northwest also cut back capacity and reduced costs by 5.7%, allowing a healthy operating profit. Unit yields rose to 11.14 cents, bringing RASM up 4.6% to 9.83 cents. This compares to a CASM of 9.13 cents, leaving a margin of 0.70 cents.

Northwest has been successful in reducing unit costs by 5.7%, and is negotiating with labour unions to achieve further reductions in costs over the coming years. Performance is forecast to be an operating loss of $309 million in 2003, while an operating profit of about $283 million is expected in 2004.

Southwest

Southwest delivered an impressive result. Revenues were up 11.6%, in part due to a 7.7% increase in traffic and 4% rise in yields. Southwest also doubled the gap between RASM and CASM by 0.52 cents to 1.02 cents, mainly due to higher load factors and yields.

RPMs climbed 7.7%, and capacity rose by 3.4%. Southwest overall generated an operating profit of $185 million; a margin of 11.9%. This compares to an operating margin of 6.6% for the same period a year ago.

Westjet

Canadian carrier Westjet turned out an impressive quarter, despite a fall in load factor and 11% drop in yield. RPMs jumped 39% and revenues 25%. Despite the fall in yield, CASM increased by 21.5%, more slowly than the rise in revenue, which allowed it to maintain the a margin of about 2.8 cents per ASM.

The fall in load factor saw unit revenues drop by 14.1%, but this was matched by a reduction in unit costs of 16.5%. This improvement in cost efficiency was mainly due to an increase in size of operations and achievement of economies of scale. AC