US majors make further financial progress

The first financial results for the fourth quarter of 2003 illustrate the progress some of the troubled majors have made since late 2001. Despite high fuel prices, respectable margins are being made.

Continental

Continental made one of the largest operating profits of any US carrier in the third quarter of 2003, and continued its success with an operating profit of $16 million in the fourth quarter. The $238 million profit from the second quarter cancelled out its loss of $224 million in the first quarter, and overall Continental generated an annual operating profit of $204 million.

This compares to an annual revenue of $8.87 billion, so a profit performance of 2.3%. Continental's traffic, in terms of revenue passenger miles (RPMs), was little changed in 2003 over 2002, while its capacity in available seat-miles (ASMs) was down 2.2%, resulting in a load factor increase to 75.5%.

While traffic was virtually unchanged, revenues increased by 5.6% because of higher passenger loads. Set against this was a 2.1% reduction in yields, which combined with higher traffic volumes increased unit revenues overall by 3.5% to 8.66 cents per ASM.

While capacity was slightly lower, total operating expenses were little changed from 2002. Continental, like many other US carriers, has had to deal with high fuel prices for the past two years. Average fuel cost was 87 cents per gallon. This is 20-25 cents higher than fuel prices of earlier years, and probably accounted for $300 million in extra costs over the year.

Continental has managed to reduce its other costs, and given flat traffic volumes and high fuel costs of 2003, the airline has turned in an impressive result.

The outlook for 2004 is for an equally slim margin, but with a traffic growth of 6.5% and an in-line capacity increase. Revenues and operating costs are both forecast to increase by 7.3%, and result in an operating profit of $217 million; equal to 2.3% of revenue.

This on the assumption that load factor will be maintained, but that fuel price will rise another eight cents of so to 95, a high fuel cost compared to the past 25 years. Continental expects passenger yields to fall about 1% in an environment that continues to be challenging, thus underlining the need for high load factors. Unit revenue is expected to be 9.55 cents per ASM, actually lower than the majority of large US carriers, and only higher than airlines such as jetBlue, Southwest and America West.

Expectations are for an operating loss of about $38 million in the first quarter, but profits in the following three quarters. While Continental has coped with challenging yields, its main cost problem has been high fuel prices, which are expected to peak in 2004 and decline again in 2005.

ExpressJet

Continental's regional subsidiary Expressjet continues to report impressive results; the last quarter showing an operating profit of $46.6 million, equal to 13.7% of revenue. Operating profit for the year was $182 million; 13.9% on revenues of $1.311 billion. ExpressJet is one of the highest performing airlines in the US.

ExpressJet has had the advantage of high traffic growth, RPMs increasing by 46.0% over the year, while capacity increased less by 35.5%. This has raised load factors to 68.5%, one of the highest of North American regional carriers.

ExpressJet also has high passenger yields; with unit costs averaging 15.57 cents over the year against a unit cost of 13.44 cents. This resulted in its impressive profit margin.

ExpressJet has gained cost efficiencies through an all-jet and single-type fleet. It also has the advantage of a fixed fuel price contract from Continental Airlines of 66 cents per Gallon. The airline has no exposure to rising fuel prices, and this benefit comes from its contractual flying agreement with Continental. Continental thus pays the balance of ExpressJet's fuel

Continental's traffic volumes were unchanged from 2002 to 2003 and yields declined slightly, but it nevertheless managed to increase load factors by reducing capacity. Overall, it managed an operating profit of 2.3% of revenue for the year.

American made impressive progress in 2003, with a reduction in annual costs of almost $2 billion while revenue remained level. The majority of this can be attributed to the reorganisation of its operation, de-peaking of hub and spoke schedules and fleet reduction. This cost reduction is against a backdrop of high fuel prices.

bill, effectively subsidising the regional partner.

ExpressJet is forecasting strong growth for 2004. RPMs are expected to rise by about 30%, while capacity will be increased less by 24%; resulting in a load factor of 71.2%.

Revenues are expected to increase by 28.9%, while yields are forecast to fall slightly, resulting in an overall reduction in unit revenues to 14.8 cents. Units costs should also fall slightly, resulting in a similar margin between unit revenue and cost to that of 2003.

American Airlines

American's restructuring plans appear to be achieving results. It made an operating profit of $111 million, after special items were excluded, from a revenue of $4.39 billion, a margin of 2.3%. This compares to an operating profit of $165 million, equal to 3.6% of revenue, in the third quarter.

American made good progress in 2003, with revenues hardly changed from 2002 but costs reduced by almost $ 2billion or 11%, widening the gap between unit revenue and cost. Its first quarter result of 2003 was a loss of $869 million, which was only partially offset by a combined operating profit of $363 million for remainder of the year. American, however, had to absorb the cost of special items in the fourth quarter, resulting in annual loss of $844 million. This would have been a loss of $506 million.

American's main achievements have been its reduction in capacity while maintaining its traffic volumes, leading to an increase in load factor of 2.1 percentage points to 72.8%. Despite the challenging environment of the US economy and increased competition, American managed to maintain passenger yield in 2003, with the result of improved unit revenues up at 9.64 cents per ASM.

This was against an even more impressive result of a 10.11% lower unit costs, especially when a 15.2% higher fuel price (at 87.5 cents) is taken into consideration. This clearly underlines that American's strategy of reorganising its operating schedule, de-peaking its hub and spoke system and reducing its fleet are clearly working. The full benefits of this should be realised in 2004, when restructuring costs and special items are removed. Revenues are forecast to increase by 8.3% in 2004, while traffic is expected to rise by a smaller level of 6.2%. Capacity will increase at the same rate, so while load factors will not change a small increase in yield can be expected.

While revenue, traffic and capacity are all expected to increase, a small reduction in costs is still expected, widening the gap between unit revenues and costs, with a result of an annual operating profit of $787 million.

Unit cost for 2004 is forecast to be 9.28 cents, compared to 10.11 cents in 2003 and 10.70 cents in 2002. This is despite a high fuel price of about 90 cents during 2004.

Tu-204 progresses

On December 21st 2003, Russia's deputy prime minister, Boris Alyoshin and Dr. Ibrahim Kamel, Chairman of Sirocco Aerospace International, announced in Ulyanovsk that Sirocco Aerospace had secured funding of $105 million to complete the manufacture of five Tu204-120Cs ordered by two Chinese airlines, scheduled for delivery between August 2004 and early 2005.

The major portion of the funding has come from the EBRD ($50 million), with the balance coming from a group of French and Egyptian banks.

Sirocco regards this as a normal part of its financing arrangements for any order it receives.

The loans will also cover completion of the European JAR25 certification programme.

So far, three of the four sections of the JAR25 programme have been completed. The fourth section requires for two flight tests to be flown on an aircraft fitted with an English language cockpit, and the first Chinese aircraft will be used for this after its rollout in April 2004. The modifications specified by the JAA team are now being implemented by Aviastar, the production factory, and will be included on all new aircraft.

Sirocco will also complete the Russian/CIS certification of the Rolls-Royce RB211-535E4-powered version and the Chinese certification work.

With airline consolidation continuing in China, the first aircraft will be delivered to Air China Cargo, which will receive a total of three, and China Eastern Cargo will take the other two. These airlines will compare the Tu-204's operation against Boeings and Airbuses, which will mean support services will have to be of a comparable standard. AC