

**SPEECH BY ANTONIO VAZQUEZ,**

**CHAIRMAN INTERNATIONAL AIRLINES GROUP**

**Annual General Meeting,**

**Thursday June 20, 2013**

**CHAIRMAN'S SPEECH**

Ladies and gentlemen,

I would like to begin by extending you all a warm welcome to this, our second annual shareholders' meeting.

As forecast, and as you are all aware, 2012 was a very challenging year for the global economy and the aviation industry in general. As with many of our competitors, these conditions inevitably affected our results during the year. Consequently, as our CEO Willie Walsh will explain later on, posting operating losses before non-recurring items of €23 million and revenues of €18 billion is encouraging news for the future in an extremely complex environment such as the present.

These results we are announcing today are largely due to the benefits that were envisaged when Iberia and British Airways merged continuing to bear fruit, and to the growing synergies in cost reductions and revenues stemming from the integration of our operations. Our CEO will be providing the details in due course, but in 2012, synergies totalling €313 million were generated, easily exceeding the initial target of €225 million for the year. This is undoubtedly a major achievement and evidence of the good progress of the merger between Iberia and British Airways.

There is no doubt that IAG made considerable progress during our second full year of operations. Our Group expanded with the addition of Vueling, a great airline whose integration is very welcome indeed and will be even more beneficial in the future. Vueling has a huge amount to offer IAG thanks to its leading position in Barcelona, European growth strategy, and low cost structure.

Another milestone during the year was the integration by British Airways of the former airline bmi, which was completed ahead of schedule. This deal has opened up interesting possibilities to expand operations through new long-haul routes to high-growth markets in Asia, as well as new short-haul destinations.

These takeovers form a part of IAG's objective of becoming a leading international airline, as we said when IAG was first created.

We have continued to make progress in this second year of our existence to reach this goal. In 2012, the IAG Group generated consolidated revenues of €18.12 billion, operating a fleet of 377 aircraft that carried 55 million passengers to over 200 destinations.

We know we are facing serious challenges, but we will not back down from achieving our principal objective: to take centre stage in the process of consolidating and transforming the global airline business.

## **COMPLEX ENVIRONMENT**

Although 2012 data show that several economies performed better than expected, and the general outlook for this year is much brighter, uncertainty has put the brakes on corporate investment, and when companies do not invest, demand for flights is directly affected.

In addition to an environment of significant economic uncertainty, especially in the eurozone, we have the fact that the airline business is extremely complex. Recently, IATA, the International Air Transport Association, said that the challenge of keeping revenues ahead of costs remains monumental, and that many carriers are struggling every day to survive.

By way of example, IATA's Director General said that on average, airlines will earn about \$4 per passenger carried – less than the cost of a sandwich in most places.

There is no doubt that the airline industry is undergoing a process of profound transformation. According to IATA data, the number of new airlines has dropped sharply since the end of the nineties, from around 120 per annum to only 20 in 2012. Many companies launched in more prosperous times have disappeared, while barriers to entry are now higher for new carriers. When this is added to the fact that financing has become more scarce and expensive and investors more prudent, we find ourselves in an environment that is substantially different from that of just a few years ago.

Furthermore, prospects for global economic growth have deteriorated since last March because the recession in Europe has turned out to be worse than expected, as I referred to previously. The result has been that the partial beneficial effect of lower fuel prices has been partly offset by weak economic growth, which has in turn resulted in only a moderate boost to the industry's earnings.

However, I would still like to mention the fact that while oil prices have fallen and it is expected that they will settle at an average of \$108 per barrel this year, this level is close to double that of 2006. Our fuel bill has risen by around €1 billion per annum in recent years, accounting for over a third of our total costs. This figure puts the impact on the industry into perspective.

## **IBERIA**

With regard to Iberia, during the past year we have pushed forward in resolving Iberia's critical financial situation, announcing an exhaustive transformation plan for it to return to profit. This is the first step and there is still much more to be done. Although change is always difficult, we must continue to work and to strive towards making permanent structural changes that will allow the company not just to survive, but to grow in the future.

Iberia has been posting operating losses since 2008, i.e. for three years prior to the merger. In the first quarter of this year, it lost €202 million, on top of the €351 million in losses incurred in 2012.

It costs Iberia twice as much to carry each short-haul passenger than it does for the airlines with which it competes every day. Why is this? For one simple reason: its cost structure is significantly higher than that of its competitors, while its productivity is lower.

This situation requires the company to make widespread changes to its flights to compete efficiently. The challenge is to become a competitive and profitable business, capable of growing in the future. I repeat that there is only one path that can be taken to reach this goal: to restructure in order to adapt to the new environment and be able to compete under similar conditions to those of our direct rivals.

70% of passengers on long-haul flights come from connecting flights or are making transfers. We therefore need an efficient and profitable short- and medium-haul network extending out from Barajas, which feeds operations connecting Spain with the rest of the world. Otherwise these routes will not break even, and therefore it will not be possible to sustain intercontinental flights. Such a situation would not only be detrimental to IAG, but also Madrid and the Spanish economy.

We can achieve this. Iberia occupies a privileged geographical position for routes to and from Latin America. Its network is strategically important to IAG, and we have always seen Barajas Airport as a natural gateway to this market. We want to protect this position for the future, and therefore reiterate the urgent need to restructure. This adjustment strategy is not all that different from the steps taken by other Spanish public and private enterprises in recent times to rebuild the foundations for competitiveness in order to take advantage of the future growth of the economy.

Likewise, a company that does not make a profit is a company that has very limited capacity to invest, and without investment there is no growth. Therefore we are confident that all those who form part of Iberia, and in particular our union representatives, will understand that it is essential and beneficial for the company to change the way we operate, because only by transforming Iberia can we ensure its future.

We are committed and determined to make the company once again profitable, competitive and capable of contributing to Spain's economic recovery.

## **OTHER CHALLENGES**

Unfortunately, the aviation industry does not only face challenges of competitiveness and profitability. In addition to the day-to-day battle to drive down costs and boost revenues to survive in a global economy, other serious challenges lie ahead in the

mid-to long-term. I would now like to mention a phenomenon that has critically distorted competition.

Along with the other traditional European carriers, IAG strives each day for its component companies to reach a competitive cost base. We have taken very difficult measures, but remain committed to doing all that is necessary to ensure the Group's financial viability.

Nonetheless, our task has been made harder still in the past by state support used to keep European airlines considered to be flag-carriers afloat, some of which are either too small or have failed to restructure successfully on several occasions.

This funding is often provided for political reasons, and there is a long list of instances in the airline industry, although it should also be acknowledged that the European Commission has acted appropriately in certain cases by taking a hard line.

According to available information, our estimates are that since 2011, at least €800 million in state subsidies has been pumped into 10 European airlines. This is exactly what the aviation sector does not need to become efficient.

The European airline industry needs to consolidate and rationalise if it is to retain its competitive edge. This would benefit passengers, the airlines and regional economies.

## **CONSOLIDATION**

On-going consolidation remains key to the sector. Mergers are likely to remain of a regional nature, especially in Latin America, North America, Europe and Asia, and we will not see cross-regional mergers while the restrictions on foreign investment continue across most of the world.

Meanwhile, global alliances and joint ventures are driving up competitiveness and offering significant benefits to passengers.

We are very happy with the continuing progress of **oneworld**, which last year welcomed Malaysia Airlines and will soon include Qatar Airways and SriLankan Airlines.

Meanwhile, the LATAM Group has announced its decision to remain in the alliance, reinforcing its leadership in South America.

In the North Atlantic, our joint venture with American Airlines continues to bear fruit, and in 2012 we launched a new joint venture with Japan Airlines. The merger of American Airlines and US Airways is also excellent news as it will further bolster our transatlantic business and the **oneworld** alliance.

## **CORPORATE GOVERNANCE**

Let me now turn to the robust corporate governance structure we have created, enabling us to comply with our numerous regulatory duties, while at the same time preserving the flexibility needed to meet the challenges of our industry.

Our governance system once again showed itself to be robust in 2012. Despite market headwinds, we have achieved a perfect balance between the daily operations of our carriers and the Group's global strategic direction.

The boards of IAG, British Airways and Iberia work in perfect harmony, guided by a clear set of corporate responsibility principles and a coherent vision of the opportunities and challenges we will encounter.

Our current board is composed of people with magnificent professional abilities. We have brought together a group of highly-qualified professionals who bring ample international experience not only from Iberia and British Airways, but also from other business areas and the public sector. This year we have been joined by Manuel Lagares, in representation of Bankia, and as from today, by Alberto Terol, if you approve his appointment. Both have broad experience in the financial and business worlds. We are confident that their skills and experience will be – and in fact already are – a valuable contribution to the board.

I would like to take this opportunity to thank all my colleagues for their support and dedication. It has been a particular pleasure for me to have worked closely with the Deputy Chairman, Sir Martin Broughton, who, as I speak, is meeting many of our shareholders at the London Heathrow Marriott Hotel. I send my warm greetings to all of them from sunny Madrid.

## **SOCIAL RESPONSIBILITY**

I could not close my speech without mentioning a subject I believe to be of paramount importance. I am referring to the role we perform in society.

Many believed that five years of severe recession would inevitably cause companies to shy away from their commitments to corporate social responsibility. However, I am very proud to say that this has not been the case with IAG. Corporate social responsibility remains a very important priority for us.

Both Iberia and British Airways continue to perform an extraordinary job of supporting the communities in which we operate and to which we fly. While both companies have their own programmes – such as Iberia's pioneering work with disabled children in Spain or British Airways' Flying Start programme in conjunction with Comic Relief – we are increasingly coordinating our corporate social responsibility policies and procedures to maximise their impact.

## **CONCLUSION**

And to wind up now, I would like to emphasize that the challenges faced by the airline sector revolve around competitiveness and profitability.

Carriers must change with the times. This involves not only becoming more efficient from a cost perspective, but also driving up profit margins.

We face serious threats that also represent huge opportunities. As we said in our first shareholders' meeting: innovation, entrepreneurship and determination are what define us.

In general, we should all be satisfied with the progress made during IAG's second year, and I would like to thank the entire team for this tremendous effort during what has been a difficult period.

Our firm commitment to you, the shareholders, is to develop IAG in a profitable and sustainable manner. We will therefore continue to focus on improving profitability, not just through achieving synergies, but also by transforming business models to the extent necessary in order to improve and fly ever higher.

Thank you