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IAG.L - Q3 2013 International Consolidated Airlines Group SA Earnings Conference Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the IAG Q3 results conference call. At this time, I would like to turn the conference over to Willie Walsh. Please go ahead.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Thank you; and good morning, everyone. Thank you for joining us for our Q3 results presentation. We've got a slightly different style of presentation for you this morning, so I'll hand straight over to Enrique Dupuy, who will take you through the results and the information in relation to Q3 and the nine months.

Thank you.

Enrique Dupuy - *International Consolidated Airlines Group SA - CFO*

Thank you, Willie. Good morning, everybody. As Willie has said, we are bringing today a strong set of results for IAG through this third quarter of a year. We're also bringing a change on our regular format with the aim of trying to explain to you better the way we are achieving these improvements in terms of performance and contributions to our operating profit through the different, I would say, areas and facts that really are making this happen.

So getting to the first financial summary, of course, we need to highlight the operating profit of the quarter which has been EUR690 million. This is, as you know, EUR420 million above last year third quarter results. And it has a lot to do with the second box passenger unit revenue increase, which it's on a like-for-like basis reaching 7.4%. So this is pre-Vueling and at constant foreign exchange terms.

If we include Vueling in the figure, it changes slightly and gets it down to 6.7%. If we get to actual ForEx rates, then we can really acknowledge about the impact of weaker revenues that we are selling tickets on, and the actual figure will be coming to 1.2%.

In terms of traffic and capacity, the Group again on a pre-Vueling, on a like-for-like (inaudible) basis, has reduced its capacity by 3.6%. But including Vueling, and taking into account this is the peak season for Vueling, the reported level of capacity increase has been 9%. And in terms of demand -- 9.1% in terms of capacity; 9% in terms of demand. So load factors are holding and they are holding at the three companies' level.

So on the cost side. On the cost side, in terms of ex-fuel unit costs, we have been near to a flat type of performance; negative in just 0.6%. And this is again before Vueling at constant currency terms against last year. Of course, if we embed the weakness of the currencies in which we're operating, especially sterling, it will be coming down to 9%. Including Vueling, which is also a bit of a disturbance because of the different business model, the plus 0.6% becomes minus 4.3%.

If we include fuel, this unit cost basis will become 0.5% negative on a like-for-like basis, and then minus 5% including Vueling, nearly minus 10% including the positive ForEx impact.

Talking finally about this combined currency impact, it has had a drag, a negative impact on our revenue base, about EUR290 million; and another one on our cost base, about EUR250 million. So the net-net negative contribution to our result this quarter has been around EUR42 million of a drag.

So we are now getting to this new format, the new charts. We call it a little bit of a Albert Hall type of scheme, a parliament type of chart. And it tries to show how the different facts will be effecting on a proportionate basis to our net contribution change through the quarter.

For example, we are stating that passenger revenues has a very significant impact in terms of heat, size; cargo of course is lower. And on the cost side, we have to mention again fuel has been very important on relative terms, and ex-fuel cost is the same.

So how we are measuring the relative performance of each of these areas, we're using this step-up and the step-down type of model. So if we get to positive contributions, we'll be using the blue steps. So blue steps will be becoming a positive contribution, first step up to 4%; then maybe in the second step up to 7%; on the third step up 10%.

So all this blue is going to represent positive contributions to the final result. And the other way round, the negative will be expressed coming down on the steps into the red zone to 1% to minus 7%, and then minus 10%.

A very simple example is fuel cost price. Fuel cost price has been coming down, so it represents a positive contribution. That's why it's blue. It represents a positive contribution between 4% and 7%.

So this is how we are going to be showing some of the contributions that have helped us to create this improvement through Q3.

Just as a reminder, again, we are going to try to strip off the ForEx impact on all of these charts, so reminding you that the global net on the quarter is negative and it's EUR42 million.

So let's get to the operating profit performance and the changes in terms of contributions that we have been achieving through this third quarter. So as we said, that positive contribution against last year's figures is EUR420 million. If we add the EUR42 million negative, it will be more about

EUR462 million. And if we just strip off Vueling, which is EUR139 million, that's how we get to the EUR323 million like-for-like figure in terms of difference in contribution one year against the other one.

And let's see where this improvement is coming from. Of course, passenger revenues, we have been insisting on this concept, and in terms of passenger revenues, price and mix. This is why we say that you need improvement in passenger revenues, and the like to like is [7.4%] (corrected by company after the call). In terms of contribution it's EUR310 million and it's about in the range of 7% to 10% improvement.

Of course, in volume, because we have been reducing our capacity, and this again is Iberia plus British Airways, minus 3.6%. It's about less contribution, it's negative. It's coming down into the red. It's coming down at the range of a little bit less than 4% negative.

So that's how we are building the passenger revenue net contribution. It's EUR310 million. Very positive in price and mix. And of course, less volume, minus EUR158 million.

So we'll go quickly through the rest of the factors that are explained in Q3.

If we continue and finish on the revenue side, we have a modest other revenues with a positive impact of EUR1 million; and as we have been saying, a weak cargo business with a negative contribution against last year's figures of EUR28 million.

Let's go to the cost side and then we get fuel. Fuel has a double improvement. One is because of low expense, low volume, low capacity. That is about EUR60 million.

And the other one is because of lower price, and this is about EUR43 million. So fuel has been helping us in this quarter in absolute contribution terms by EUR103 million.

And then let's go quickly through the ex-fuel. So ex-fuel, again, because of lower capacity, has a significant positive improvement. So less costs by EUR113 million.

And then there are more type of unit and other type of reasons behind the ex-fuel cost. In terms of employment, apart from the reduction in capacity, there is this mix of productivity and wages that is creating an additional positive of EUR18 million for the Group.

In terms of suppliers and ownership, it's slightly negative. We are going to get deeper on this concept in a further slide. So we have to say that the savings in terms of volume are in this case offset by inflation and other factors. So we are going to go a little bit more in detail on this ex-fuel type of impact.

We are coming then to this chart where basically the aim is to explain to you what is behind the negative 0.6% non-fuel unit cost performance. It's small. It's just I would say reaching negative. It's negative and it's in some way hitting our cost base by 0.6%.

What's behind it? Well, it's not the employee unit costs. The employee unit costs have been improving both in British Airways and in Iberia.

In British Airways, the story is more about productivity improvements. In Iberia it's both productivity improvements, but especially the impact of salary reductions on the mediation plan.

In terms of productivity in Iberia, we still have a lot more to do through Q4 and year 2014.

So let's get to the supplier unit cost side. We see the handling/catering type of suppliers. We have some positive savings having to do with the different scheme of sectors that we're applying in terms of reduction in capacity that we've been applying in Iberia, reducing sectors that we were operating last year and in the more recent quarters.

So there is a sector benefit there, about 3%, 4%, both in handling and catering; and there is a price, a unit price type of deterioration, which has to do with inflation in some of our handling and catering contracts, improvement on our catering services for premium travelers. And something that is not related to ASKs we have to mention, which is the cost that we allocate to our British Airways holiday program. So that's a different business. It's not related to ASKs. But as a fact, we are allocating these costs to this handling/catering segment.

So if we get to landing fees, again, there is a story which is positive about sectors. We are improving and reducing the sectors that we fly. There is a negative one about inflation.

So landing fees are increasing, especially in Heathrow Airport, and also in Malaga and in the rest of Spain. That's bad news, and that's something that we are trying to fight.

The rest of the supplier side, costs are all neutral or positive. So engineering is basically neutral. Selling is positive. We have to recall here the significant effort being made on last year on these selling and marketing costs through the Summer Olympics.

And then we have others, costs improving, and that's basically overheads improvement. It has to do a lot with what is being done in Iberia and also in British Airways in terms of overhead reductions.

In ownership, there is mixed type of -- quite neutral as a whole performance between retiring old fleets, which were owned, so depreciation being lowered, and new aircraft being operated under new lease contracts, as for example the A330 Iberia fleet, which is pushing slightly that account upwards. But as a whole, ownership is more or less equilibrated.

Let's then go to fuel, and the fuel, we're again using a different chart, but we think it's going to be more helpful for us and for you. These bars show for the different quarters, first at the top of the bar the price including hedging that we had last year. So for example, the first bar showed that last year after hedging, we had $1,020 kerosene price per tonne.

At the end, the lower side of the bar, shows where we are going to be this year, or where we expect that we will be this year if the unhedged portion remains at actual level. So actual levels are actually below $962 today, more in the range of $950, but it's going to serve us.

So there is still in the fourth quarter a bit of tailwind in terms of fuel. If nothing adverse happens, we could be getting to this minus [4%] (corrected by company after the call) in terms of unit terms. This is [before] volume. And you have to remember, unit terms coming down.

And it will make the same exercise for the following quarters. It will be minus 2% beginning of 2014, and again another minus 2% by the second quarter, minus 1% the third quarter of next year. So a slightly type of better environment in fuel than last year; little bit of a tailwind there.

For next year as a whole, what we see about the next 12 months is a minus 3% against the last-year figure, and considering that we are covered at 65% level.

So let's get a little bit as in following locations a little bit into the capacity-type of figures. Q3, as you've seen there, as you can see in the chart, is about a net minus 2.1% -- sorry, Q1 of this year, it has been minus 2.1%.

The second quarter was positive in 4.2%. Here, of course, we are including already Vueling growth, because the Iberia contribution was still negative at 3.7%. And the British Airways contribution was more or less flat. So second quarter we are already seeing the impact of Vueling in our capacity figures.

And then the third quarter is a little bit of the same. We are seeing Iberia still dragging down the capacity figures by 4.3%; British Airways slightly pushing them up by 0.7%. So as a whole, this is getting to minus 3.6% like for like before Vueling; then 12.7% Vueling, which means as a whole 9%/9.1% capacity increase.

And the fourth quarter, which is very much the same, so it's again 9.1%. And then Iberia reduction will represent a very similar figure. British Airways will be contributing more in terms of growth, about 4%, and the rest remaining will be 9.2% due to Vueling.

So as a whole, the figures for the full year 2013 will be shown for IAG, including Vueling, this 5.2%, out of which the Vueling contribution will be 7.6%, the British Airways contribution just 1.5%, and the Iberia contribution a negative nearly 4%.

How we are driving this capacity changes? So in the case of Iberia, it's simple. I'll go through it quickly. As you know, we are not opening new routes. We're of course canceling some routes, and these routes that have been canceled against last year represent about minus 10% in terms of capacity.

There has been also some frequency adjustment in terms of lowering the number of frequencies that we operate in existing routes, and this is about minus 5%. And there's no meaningful difference in capacity size of our fleet. So that's how we build up the minus 15% reduction in the case of the fourth quarter year 2013.

For British Airways, it's a little bit more complex. So there are new routes; we've been announcing them. It's about Chengdu, it's about Colombo, some other leisure destinations, but these two are the main ones. There have been some cancellations, Dar es Salaam and some other minor routes in the domestic.

There has been frequency change, and that represents the big chunk of growth that we're envisaging for the next quarter. It's 4.2%, so it's growing on existing and well-known routes. It's about a safe growth pattern. And then there is a little bit of aircraft size, and this is basically related to the introduction, gradual introduction in the fourth quarter of the A380 aircraft.

So coming to how all these capacity changes are affecting our network, we have this global chart here where we see the major changes.

The Americas; first with the Americas. North America, nothing very significantly happening there in terms of capacity in this last quarter, so 0.7% up. And Latin America affected by the reduction of Iberia. It's about minus 11%, so down.

Domestic and Europe; domestic is also affected by the Iberia reduction in Madrid. And also on the case of British Airways, there has been a reduction in the domestic size of the network, which has been transferred partially to Europe. So we are seeing Europe, which is more or less balanced, with an Iberia reduction which is more or less offset by a British Airways growth.

And then finally, we have to mention the Asia capacity expansion, and this is basically about the Seoul route on a year-to-year exercise of comparison. And a little bit of our kangaroo route, about our Sydney route, that is creating the plus 3.1% in Asia Pacific.

Africa and Middle East, you know because of the troubles that we have been suffering there, we have been applying a reduction in the range of 6%.

So all these capacity adjustments and moves, and growths in some cases, how they have been translated into unit revenue performance? And we have two charts for unit revenue performance.

The first one is actual, so it's suffering the currency weakness on these accounts. And the following page will be on a like-for-like basis. In both cases, we are not considering Vueling; we're trying to focus on the like-for-like unit revenue performance. So after this revenue weakness that I've been mentioning, we see North America still up 2.3%.

The weaknesses; these are Europe figures, and as you know, the weakness then in the North America area [which we] -- about our sterling sales, and also at a minor extent on our dollar sales. So even after that weakness, we have positive 2.3% improvement.

In Latin America, weakness of sterling/dollar have been basically offsetting a little bit of a strength in the local currencies and the euro sales, so it's a type of zero net effective.

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If we get to domestic and Europe, we get positive figures, both in the domestic network and also in Europe. In Europe, it's 4.6%, so it's significant. It's significant, and part of these sales are done in sterling. So if you recall this figure and you see the like-for-like one in the next page, you're going to see the difference.

Asia Pacific and Africa/Middle East, of course, suffering from some very weak currencies there, [that's] the yen and the rupee, are turning into modest negative territory.

Coming then to the like for like, and here is where we see, I would say, the significant improvement. Here is how we get the split of the 7.4% that we are mentioning.

And the split of the 7.4% unit revenue like-for-like figure is based on North America, up 9% nearly; Latin America up 5% nearly; Europe up 10%. The domestic network's rebounding, even in Spain, to a positive territory; both Asia Pacific and Africa/Middle East, above 7%.

So these unit revenue increases, how they're shown in terms of our revenue, passenger revenue and other revenue outlook. We get to the following page. We again strip capacity, we again strip currency, and we strip Vueling. We want to get to the contribution in terms of unit revenues of the different sectors.

And here, we get the long haul, the long haul both in premium; and this is even more surprising, in non-premium. Non-premium getting to the higher step in terms of 7% to 10% improvement, very significant in the long haul. And the premium very consistent growth in terms of unit revenues with prior quarters.

And then the short haul again. British Airways very high and Iberia on the positive territory, as I was telling you.

Cargo weaker, of course, weaker in terms of volumes, and not so weaker in terms of yields. We're probably getting a better performance in terms of yields than some of our competitors. And others has a mix of different impacts but, for example, British Airways revenues is allocated here showing this moderate improvement.

So getting a little more in detail into the performance by our different brands. So we know about the British Airways performance, a very strong operating result. And here we're talking in sterling terms of GBP407 million, operating margin of nearly 13%. And this is not the end of the story. I think we are aiming to higher figures in the following years.

In terms of where we're getting these improvements on the case of British Airways is unit revenues, is a flattish performance in terms of costs. For example, it's employee costs being down in terms of per ASK by 0.7%. And this is basically, as I told you, because of productivity.

Iberia. Iberia improving again from a meager EUR1 million to EUR74 million; so EUR73 million up. And this on a huge capacity reduction, 15%, on a sector length increase.

On a positive figure in terms of return -- of revenues per ASK, and this is one of the signs that we are in some way keeping positive on the Iberia story, and we hope we'll be able to improve it. And of course, significant positive performance in terms of CASK, which is basically related to lowering the employee cost per ASK by 7.2%.

And this is, of course, having two [plays] on the balance. On one side is salaries going down by around 14%, and then there is this other one about the redundancy program lagging the capacity reduction. So these types of compensation impacts will get lower and lower through the following quarters. We'll be getting closer and closer to a minus 14%.

Vueling. This is a little bit of a shocking story, I would say, because we are seeing there capacity increases of 22%. We are seeing load factor improvements at the same time. We are seeing unit revenue increases of nearly 9%, and we are seeing CASK ex-fuel and after fuel, being reduced. And a substantial improvement in employee cost per ASK, which in the case of Vueling has to do with growth and mix of employees. So there's a benefit of juniorship through growth in the mix of employment.

So a little bit on the balance sheet. Not big changes on IAG balance sheet but some impacts that's worth to be mentioned. So in terms of adjusted equity, the main two changes, because it's an improvement of EUR500 million, had to do with the conversion of the British Airways old, we will say, the British Airways old convertible, GBP350 million, and the positive contribution of the positive results for the quarter; for the whole nine months in this case.

What we are seeing in terms of cash improvement between the end of last year and this year is a figure that could be getting near EUR800 million. And this is basically related to the acquisition of Vueling, which is bringing about EUR590 million of their cash into our balance sheet. And the rest is a net improvement, in the case of British Airways, with a slight reduction of EUR100 million in the case of Iberia for the first nine months. What we can tell in this respect is second half Iberia cash will become neutral.

On aircraft leases, this is basically the adding of Vueling operating leases into the combined accounts of the Group. So as a whole, the adjusted net debt has experienced a reduction, even through the acquisition of Vueling, and even through the program of deliveries of new aircraft that we have been going through. And as such, adjusted gearing has been improving from 51% and down to the 49% that we are having by the end of September.

A couple of messages around the outlook. There is this first page that we have been using in the past. No big changes there on the underlying trends in the markets that we are operating. So non-premium, both short haul and long haul, we would be labeling it as stable, the same as premium, and I just referred to the weakness that we are now for some quarters experiencing on our cargo operations.

What we have to say consistently with this chart and with this no underlying change is, again, that there have been some exceptional circumstances that have been affecting Q3 figures that probably we are not going to be repeating. And I want to remind you again about the Olympics for British Airways, and I would remind you again about this exceptional performance of Vueling through the summer season. That had to do with being in the right place in the right time and having the ability of taking the benefit of this position.

So finally, a bit of a guidance for the whole of the year. We are guiding to an operating profit of full-year 2013, pre-exceptionals, of around EUR640 million (sic - see Press Release, "EUR740 million"). We're seeing ex-fuel unit costs down as a whole for the Group. We are sticking to the fuel bill of EUR6 billion, including Vueling all around.

Just a small caveat here. This is referred to $1,000 per tonne kerosene as a base, and $1.3 per EUR1. We know -- yes, EUR740 million. I'm sorry. I'm told that I have said EUR640 million. No, it's EUR740 million, as you see in the screen. Very sorry if I said EUR640 million.

So coming back to the fuel bill, it's probably -- could be a little bit better than the EUR6.0 billion. And capacity growth is 5.2% up, as we have explained in previous charts.

So I'll leave you now the floor for your questions and I will try to answer any doubt that you have.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). Stephen Furlong, Davy.

Stephen Furlong - *Davy - Analyst*

I was just wondering, on page 20 where you talk about the different markets, back in August in short haul, you classified non-premium as stable/strong. So I'm just wondering if you're seeing slight weakness there where you just [called] -- I know you're saying the market's stable.

And secondly just on cargo. I know you say it's been weak for some time. Some commentators are pointing maybe there's a little bit of a peak season. Or do you think there's conflicting signals there that there's just continuing structural issues with cargo?

And just finally, just -- might just talk about with the deliveries coming, where do you see broadly capacity growing in 2014?

Thank you.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Okay, thanks. In relation in to Q3, clearly, the -- sorry, the short haul non-premium, as Enrique said, I think Vueling had a particularly strong performance benefiting from the real peak that we witnessed in Barcelona.

I think one of the things that we're probably seeing in the short-haul market is a greater divergence between the peak and off-peak, and I think that's supported by things like Ryanair taking some of the aircraft out of the non-peak. But the underlying performance on short haul non-premium, we would continue to describe as stable and the environment as generally being positive for us.

In relation to cargo, I think cargo, it is a structural issue. What we're seeing at the moment is a number of operators who have dedicated cargo aircraft reducing the number of cargo aircraft they have. But that's been more than offset by the increase in capacity being made available on passenger aircraft. So as we've seen growth in passenger aircraft, and particularly growth in areas like the Middle East, you're seeing a lot of additional cargo capacity coming online.

And I think the other structural change is without question more goods are being moved by ship, by sea, than traditionally by air. So what we see as a structural change.

And clearly, the opportunity for us is to look at the network, but we have flexibility in terms our dedicated cargo aircraft. The freighters are, as you know, on a lease basis. So that gives us flexibility if we choose to use it to reduce our overall cargo capacity.

And in relation to 2014 capacity, we're going to update you in relation to that next week at the Capital Markets Day, so we'll give you a very good flavor of where we see 2014 next Friday.

Stephen Furlong - *Davy - Analyst*

Look forward to it, Willie. Thank you.

Operator

Jarrod Castle, UBS.

Jarrod Castle - *UBS - Analyst*

Three, if I may, just on Iberia, first of all. Can you just give an update in terms of the number of staff who've now left the Company and if there's any more to leave? And also, I guess, any conversations; how they're progressing with the unions or if there's going to be any further productivity gains there.

Secondly, you mentioned a little bit about the short-haul environment. It looks like you've got some pretty decent domestic and European pricing for the last quarter. Can you say anything in terms of any changes you're seeing in quarter 4? Obviously, it's a weaker quarter, but any changes there.

And then just lastly, there were some comments last week from Lufthansa in terms of reviewing its depreciation policy. They are very conservative as it currently stands, but they might be becoming even more conservative just given what they view in terms of realizable value on fleet disposals. Is there any kind of review process on any of those policies?

Thanks.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Okay. I'll ask Enrique to deal with the depreciation question in a moment. In relation to Iberia, [Luis] gave you a presentation at Q2 where he showed the planned headcount reduction through to the end of December. That remains on track, so we expect 2,375 people to have left by the end of the year, which is slightly ahead of where the mediator had planned it. So the progress is positive there and we're pleased with the way Iberia is moving forward.

But we do have to obviously caution people by saying that there's still a lot of work to do and get to a position where we would be confident about investing in Iberia, and particularly investing in new aircraft, which would generate in itself further significant improvement and costs with the reduction in fuel burn. We would need to see more changes to the work practices and improvements in productivity.

But we're doing well so far and Luis has made a huge difference, and the headcount reduction plan is on track in line with the chart that he showed you at half year.

In terms of short haul, I think what we witnessed in Vueling, in particularly, was a particularly strong peak season. And the challenge for the short haul business, and particularly the likes of Vueling, is to be able to manage peak opportunities, because, without question, there are significant opportunities still available during the peak season. But to be able to deal with the lower demand environment in the off-peak, because clearly, we could add a lot of capacity in the peak, but we'd then have to deal with that additional capacity in terms of aircraft and crew in the off-peak.

So if we can get a more variable cost structure, which Vueling to be fair has done extremely well on, then I think there's even further opportunities for us going forward in the peak.

The off-peak demand; we don't see much growth in the off-peak demand, so it remains a -- very much a seasonal activity in short haul. And I think that's exactly what Ryanair and easyJet are seeing. And Ryanair in particular have highlighted the weaker demand in the fourth quarter and the first quarter.

So as they've grown their fleet in the peak, they have more capacity to deal with in the off-peak. And given Ryanair's flexible cost base, they're able to achieve that by just grounding aircraft.

So the real opportunity in the short-haul market is for airlines that are very efficient in dealing with their costs and have as much variable costs in their overall costs base as possible.

In relation to depreciation, Enrique?

Enrique Dupuy - *International Consolidated Airlines Group SA - CFO*

Yes. The answer is yes. We revisit our policies from time to time and this is the case; we are doing it now and we are doing it because of a couple of issues.

On one side, it's about we have more certainty on the final replacement of some of our fleets, especially the 747 fleet, so we are now adjusting our final depreciation of these fleets to the final substitution dates.

The second one is on the new aircraft. And on the new aircraft, what we are basically revising, and [I don't know] if we're going to change it or not finally, is about the residual value level. It's not about the period of depreciation; it's about the residual value levels. And that's something that we'll probably have a complete opinion by the beginning of last year.

In the case of the residual value levels, and because we're using periods of above 20 years or around 20 years, it's going to have a modest impact.

Jarrod Castle - *UBS - Analyst*

Okay. Thank you very much.

Operator

Neil Glynn, Credit Suisse.

Neil Glynn - *Credit Suisse - Analyst*

If I could first ask on the long haul, non-premium performance. You've obviously highlighted the strength of that. I presume that's mostly coming from BA, but could I ask is that heavily driven by transfer traffic, or is point-to-point contributing equally?

Second of all on the winter. Even though Iberia's LatAm business should be benefiting from the capacity cuts, I guess the winter will be a good test of the greater level of resilience at Iberia. Can Iberia avoid losing money in the fourth quarter?

And then finally, Enrique, if you could comment on net debt, what your operating target suggests for net debt by year end, because I presume net debt will rise again in the fourth quarter.

Thank you.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Yes. The main strength in the long haul, non-premium is as you've identified. It's in the BA network. But it's principally point to point, which as we've spoken about before, demonstrates the strength of the London market. So when we look at the UK, more and more we just look at the London economy because it's a better indicator of BA's performance. And London has clearly performed, the London economy has performed more strongly than the UK economy overall.

So we continue to see good demand on a point-to-point basis. We always have the flexibility, and we've demonstrated this in the past, to switch capacity if we need to onto the transfer market. But the point-to-point market was the area of strength for us.

In relation to Iberia, it's very early days. Iberia's coming from a -- of significant losses to a position where it will be more competitive with a better cost base, but by no means where it needs to get to. And that's why we've talked about the need for further productivity improvements.

So the mediator's report, which we signed up to, was a good first step, and that's the way we've described it. It certainly has stemmed the losses in the cash outflow, which was our first priority.

We've got more work to do to implement the mediator's report, so there's that first step to be achieved first, and then to engage in further improvements in productivity.

We're not going to give a running commentary in relation to what Luis and his team are doing, but he has fully engaged with the trade unions and with the Iberia employees. And I think he deserves great credit for the impact that he has had in Iberia in the short time he's been there as CEO.

And, Enrique, net debt?

Enrique Dupuy - *International Consolidated Airlines Group SA - CFO*

Yes. The net debt, not a lot of variances, so we may be seeing a little bit of an increase to a range of EUR5.3 billion to EUR5.4 billion.

You have to remember that three companies -- maybe Iberia would be neutral, but I think that three companies may be creating cash through their operations on the third quarter -- on the fourth quarter, sorry. So it's about the balance between that cash being created through the operations and the CapEx [effort] that we expect for the quarter, which is not huge. So I would say something between EUR5.3 billion/EUR5.4 billion would be Russia.

Neil Glynn - *Credit Suisse - Analyst*

Many thanks.

Operator

Alexia Dogani, Goldman Sachs.

Alexia Dogani - *Goldman Sachs & Co - Analyst*

I also had three questions, please. Just firstly, I'm quite keen to get your view on how you're looking at capacity across North Atlantic in the winter season; and notwithstanding I guess the changes in terms of the aircraft size, whether you view the growth as supportive of the current demand environment.

Then secondly, just in terms of the BMI slot transformation, can you talk to us about how far down this process are you, or whether the full substitution, if you like, will happen in 2014?

And then just finally on the short-haul network, I'm just quite keen to understand the excluding Vueling performance. And if you can remind us what you have been doing in the BA short-haul network to improve the asset there and the initiatives you're taken there and the impact they're having.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Okay. We're very comfortable with the Q4 transatlantic capacity. I think we've got good visibility now in terms of what other carriers are doing. We believe that the capacity that we're adding and that is being added through the joint business very much meets the demands that we see in that market.

So what we're doing is absolutely appropriate given what we have performed, how we've done so far, and what we see as demand in the market. And we're comfortable with what other carriers are doing on the transatlantic as well.

So that's specifically in relation to Q4 where there's good visibility, and I think that will [toll] through going through into the Q1, so covering off the full winter period.

BMI; what we talked about in BMI was over time moving some of the short-haul slots into long haul, but that was dependent on the arrival of new long-haul aircraft. We're really only at the start of that process. So it will be a process through 2014 and 2015 and we'll give you an update in relation to that next week at the Capital Markets Day.

And the BA short-haul network making very good progress is the way I would describe it; significant improvement in the performance of Gatwick, where we've seen a big increase in seat factors, strong demand from the customers in relation to the hand baggage only fares, which has been very successful.

But Gatwick has improved its performance very significantly with an improvement in cost and an improvement in revenue. And the Heathrow operation continues to move in the right direction as well.

So I think what we have in the Group is a very, very efficient low-cost carrier in Vueling. They increased capacity in the quarter by 22% and so RPKs increased by over 27%.

And you'll have seen in the traffic stats that we reported this morning, that trend has continued in October with ASKs up 22.3% and RPKs up 27.6%. So the success in short haul comes from having good costs, and we're getting better at that with BA; we're getting better at that with Iberia as well. And, clearly, we have a very efficient low-cost operator in terms of Vueling.

Alexia Dogani - *Goldman Sachs & Co - Analyst*

Okay. Thank you very much.

Operator

James Hollins, Investec.

James Hollins - *Investec Bank (UK) plc - Analyst*

The standard three from me as well. The first one's on Q3 Europe. You had flat capacity. Yields are up north of 10% constant currency. I was just wondering, obviously, a decent performance, whether you've seen particular areas of strength there, or is it simply the case that a lot of Iberia capacity's come out to improve the overall yield?

The second one, I imagine you'll tell me to sod off and be patient, but just pushing you on capacity for full year 2014, I was wondering if in the absence of any direct guidance you could say whether Q3/Q4 capacity trends act as a decent guide; i.e., if you strip Seoul out, BA up a few percentage points, Iberia down 15%, Vueling up about 20%.

And the final one is just looking further out. You're looking at a margin, I guess, around close to 4% in full-year 2013. Is there anywhere -- or what sort of target do you have on a two-year basis? And I think historically, you gave a EUR1.6 billion EBIT guidance for full-year 2015. Could you update us on where that is with Vueling or whether again I have to be patient 'til next week and you might come out with a new guidance target then?

Thanks.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Be patient, be patient, be patient (laughter). No. Certainly, in relation to year 2015 targets, we will update you at the Capital Markets Day next week.

And I know this is frustrating for you. It's a little bit frustrating for us. We do still have a bit of work to do between now and next Friday, so we will update you in relation to all of those issues on Friday.

In relation to capacity, just to say the Iberia capacity, 15% reduction took place in 2013 versus 2012. So you're not going to see a further 15% reduction in 2014 versus 2013. So we're not planning on adding any capacity in Iberia. There may well be some minor capacity adjustments but --

So you should look at Iberia in effect being flat versus 2013. Vueling will be growth versus 2013. And BA, given the things like the A380s and the 787s, you're going to see some growth.

So we'll give you the figures next Friday, but it will be some modest growth in BA, principally flat in Iberia, and continuing good growth in Vueling. And all of that, we believe, absolutely appropriate given the market segments that each of the airlines are operating in.

James Hollins - *Investec Bank (UK) plc - Analyst*

Okay. Thanks. And just on the European strength --

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Europe, sorry. Yes. Europe was a combination of factors. A very strong performance for Vueling. We're seeing the benefit of capacity reduction in Iberia, plus the improved commercial performance of Iberia.

So we're seeing a -- it's a combination of both capacity reduction and some commercial improvement, and that's behind the turnaround and the performance in Iberia.

And BA had, as I said earlier, a good Gatwick performance and good position at Heathrow. So Vueling I would highlight as the star performer in the third quarter, which demonstrates how efficient they are.

They were able to move very quickly to exploit some growth opportunities given where they -- when they were able to see the retrenching activity by some of the major European carriers. So a very good performance by Vueling, a good performance by BA, and a good performance by Iberia in the quarter.

James Hollins - *Investec Bank (UK) plc - Analyst*

Okay. Great. Sorry to take more time, but given that I've eked out of your that you'll be flat Iberia next year, just on that, if we were sitting here six months ago, would you have probably assumed that would be flat as well? Or is Iberia actually performing slightly better than you'd expected? Or have you taken out more capacity this year than maybe you'd expected? Or am I wrong to assume you might have thought it was down in 2014 six months ago?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

We're actually very comfortable that we took the right decisions in Iberia. We haven't seen anything that indicates to us that we either took too much capacity or too little capacity out. So it's performing very much in line with what we had expected with probably slightly better performance in unit revenue.

But when I look at the overall financial results, if you remember, we had targeted a higher cost reduction in the year. So some of the shortfall in cost reduction has been offset by an improvement in unit revenue. But we're absolutely comfortable that we called the capacity right, and haven't seen any reason to make adjustments to that.

James Hollins - *Investec Bank (UK) plc - Analyst*

Okay. That's the lot from me. Thanks very much.

Operator

Andrew Evans, Nomura.

Andrew Evans - *Nomura - Analyst*

Just one from my side. Looking at your contribution map at the start of the presentation, which actually I like quite a lot, we can see the bulk of the operating profit improvement is coming from the price side. Can you just explain why you're going to switch across from price to volume in 2014 when historically this isn't something which has been particularly good for the airlines?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Yes. It's a very subtle change. We're not signaling a major change in direction. And as you know, we do switch -- even within month to month, we can change the focus of the revenue management.

So it's all designed to maximize the revenue, and you can maximize revenue by pursuing yield or by pursuing volume, or a combination and a mix of those. And we do things differently month to month, as I said.

But I think some of this reflects the fact that we are starting some new routes, and we believe that those new routes are absolutely right and long term of strategic importance, particularly to BA. And certainly, probably the situation with Vueling is similar to that.

So we are adding capacity where we believe the capacity is right. We're taking capacity out where we think routes have been underperforming. So we've taken Dar es Salaam, we've cancelled that route.

So it's adding capacity where it's long-term sustainable growth for the business and will be profitable in the long term, and this we believe is absolutely right for us.

So we can't stand still, but where we're at in capacity we believe it's right, and the A380 does automatically bring a bit of additional capacity. But as we've highlighted to you previously, that gives us opportunities in terms of adding capacity where it exists without having to add frequency. So A380 works on routes where there's good demand but where frequency isn't important.

So it's a subtle change. It's not a major change in direction. It's not a big swing. But we felt that we should highlight it given that there is some capacity coming on line. But the capacity we're adding we believe is absolutely right for the demand environment that we see today and for the route development that we have identified.

Andrew Evans - *Nomura - Analyst*

Okay. Thank you very much.

Operator

Damian Brewer, RBC.

Damian Brewer - *RBC Capital Markets - Analyst*

Two questions, please. First of all, in terms of the Q3 performance, can you give us an update on how much the Atlantic and also the Asian joint ventures contributed to the improvement? And secondly in that regard, just it looks like there's a slight shift in the amount of BA and American flying occurring over this winter.

Is that simply to allow American to bring its product up to something that can sell in the market, or is there something else more strategic in that?

And then the second question area. Looking at the mature parts of your network, leaving aside those long-term strategic new routes, how much of the network presently covers its cost of capital? And are there more routes like obviously Dar es Salaam, Lusaka that's going and Havana that's gone from Iberia, to be taken out of the network to improve the mix of return on capital in the business?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

In relation to the joint businesses, we don't give a breakdown. But I would say the joint business with JAL is at a very early stage, so we're not -- we wouldn't have recorded any benefit at all from that at this point.

The joint business with American continues to perform well, and as you've seen, one of the advantages of the joint business is that we can switch capacity, not just within our own network, but with our partners as well.

So we're switching capacity where we believe we have the right aircraft and the right timing to suit the demand. We're adding Boston and I think Miami as well. So it's much more efficient for us to be able to do that together with a partner than to do it in isolation.

And in relation to our route network, as you know, we don't give you a breakdown of profitability or contribution on a route-by-route basis, but with the BA long-haul network, it is a pretty solid network. And as we've previously indicated, the problem we've faced at BA in a static slot environment, to expand into what we believe are strategically important markets for the future, it would have had to come at the expense of profitable routes today.

And that's why I've highlighted the benefit and the importance of acquiring the BMI slot, because that allows us to continue to operate a network into North America, for example, which clearly has been a strong performer for us, and indeed, add some capacity in North America while at the same time adding capacity to new growth markets in Asia.

So there's always some work to do and changes by season to season, but I would describe our long-haul network, the mature network, as being a pretty solid performer, and hence the reason we're adding new capacity to new destinations where we believe we can deliver long-term sustainable profitability in excess of our cost of capital in the long term.

Damian Brewer - *RBC Capital Markets - Analyst*

Okay, great. So it sounds like it's just the growth that will drive the improvement and the returns in the long term.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

It's growth and you're always looking to improve the existing performance of your network. And that's why we've continued to highlight the need for further cost efficiencies. So we're always searching for areas of cost improvement within the airline.

Damian Brewer - *RBC Capital Markets - Analyst*

Thank you very much.

Operator

Oliver Sleath, Barclays.

Oliver Sleath - *Barclays - Analyst*

Just three questions, please, firstly, on Iberia's revenue performance. I think you mentioned recently, Willie, that that was a little way perhaps behind where you'd been expecting. You were looking at putting some improvements for the yield management system in place. So it would be good if you could update us on that. It sounds like it might have improved recently anyway.

Secondly, could you just give us an update on the new aircraft introductions; how the 787 and A380 are performing now they've been in service for a few months?

And then finally just on Vueling and perhaps growth plans there. And apologies if I should wait for next for this. I see Vueling's announced a base in Brussels for next summer. I just wondered if you could perhaps give us some more color on other markets that look promising for Vueling, perhaps Germany, and any others you might highlight.

Thank you.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Okay. In relation to Iberia, yes, what I'd said in relation to Iberia was our original plan assumed no growth in unit revenue, but that within IAG, we felt instinctively that if you take 15% capacity out, you should be able to improve your unit revenue performance. We are now seeing that trend.

So the unit revenue performance has been improving from Q2 into Q3, but there's still a lot of work that Iberia needs to do. But we're seeing the benefit of some changes to the revenue management system and the focus that we have put on that. And we believe that there is more available to Iberia through their improved commercial activities, including revenue management. And hopefully, we'll see that improve as we go into 2014 and we can give you some flavor of that next year.

Keith Williams is here, so I'm going to pass over to Keith in relation to the A380 and 787.

Keith Williams - *International Consolidated Airlines Group SA - Board Member and CEO of British Airways*

Yes. So we've got A380, 787s, and don't forget we've got some 777-300s coming in all at the same time. And one of the things it's allowing us to do is to recover from in fact the engineering works that we were doing on the older aircraft last year, which is why you're seeing some of the capacity increase.

In terms of the A380, very, very pleased with the A380; now got three deliveries going very well to Los Angeles and Hong Kong. Next aircraft is due to deliver in early January.

The 787 is actually going well. We've now got four 787s. The reliability is good and the fuel efficiency is delivering up to what we expected. 777-300s, we're still taking delivery of the last of those, two in the last few months; got another three to deliver there.

So if you look out over the next three/four years, I think we've got 51 aircraft coming in in total, if you include the short haul. So the program's going well to date. The engineering guys are obviously busy, but it's going well.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

And in relation to Vueling, Alex is always looking for opportunities, and you should expect to see more of this in the future. But Alex will give an update in terms of the Vueling strategy going forward. But Brussels is one of the markets that he believes will be strong for him, given what's happening in Belgium, and there are definitely opportunities in other parts of Europe. So don't be surprised if you see further Vueling bases being announced in the months ahead.

Oliver Sleath - *Barclays - Analyst*

Okay. Thank you. That's all very clear. Thanks.

Operator

Andrew Lobbenberg, HSBC.

Andrew Lobbenberg - *HSBC Global Research - Analyst*

Just a simple one, I guess. Could you talk us through the logic of the Board changes that were announced yesterday?

And second question, could you just say to what extent you see the growth plans of Air Europa as a challenge to Iberia?

And then thirdly, Qatar and LatAm are in oneworld, but we haven't seen you commit to much detailed partnership with them. When should we expect further updates on the scale of your collaboration with these new oneworld partners?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Yes, the Board changes I see as a very sensible development of our governance structure. The structure we put in place obviously reflected the merger of BA and Iberia.

One of the challenges we always had for ourselves was to ensure that the structure was scalable. Clearly, with the addition of Vueling, it identified that we can't keep adding OpCo CEOs to the main Board, and OpCo Chairmen to the main Board.

So we felt that we're at a point in our evolvement where we could just rationalize the Board. So Martin Broughton and Antonio Vazquez stand down as non-executive chairmen of the operating companies. They remain in their position of Chairman and Deputy Chairman within IAG.

It also clarifies and simplifies the reporting structure internally in that Keith and Luis and Alex all report directly to me. But because in the case of BA and Iberia there was also an operating company chairman, there was this additional reporting line through to the Chairman which was felt to be superfluous.

So we've just rationalized the structure and made it more simple, and we believe it will further develop the governance within the organization. I don't see it as being a big change.

Just in terms of Keith and Luis coming off the main Board, they clearly will still attend Board meetings, but not as members of the Board. And again, that was principally because we couldn't keep adding all the OpCo CEOs, so we didn't have scope to add Luis -- I'm sorry, to add Alex. But we also felt that a smaller main Board was more appropriate as well. So I'm pleased with the changes that we're -- we have announced, and they'll take effect from the beginning of January.

In relation to Air Europa, Air Europa has a more efficient cost base than Iberia. We have to acknowledge that. It's one of the reasons why we've said Iberia needs to continue to improve. The good news is that with the changes that we're implementing, and further changes that Luis is negotiating, Iberia will have a much better cost base than Air Europa, which will allow Iberia to recover lost ground.

So we're very clear; if we have competitors that are better than us, we're not going to compete with them where we know that they can beat us. So I would describe what we've done in Iberia as a tactical retreat to enable us to restructure ourselves with a view to engaging in a more competitive growth environment if we can get the right cost base in the future.

So I wish Air Europa well, but they need to recognize that we're going to be coming at them when we've restructured our business, and that will be an opportunity for us.

Qatar and LatAm, we have agreed some co-chairing with Qatar. As you know, we're one of a small group of oneworld carriers that actually fly to Doha today, but we do it over Bahrain. So we'll be code-sharing with Qatar on a number of destinations in India and some African destinations. That's the start of the co-operation with Qatar.

LatAm, we've actually got a deep relationship with LatAm through Iberia, and that will strengthen going forward. So there's ongoing discussions with LatAm. Our ambition is to establish an immunized joint venture with LatAm similar to the one we have with American on the North Atlantic.

So the relationship with LatAm I would describe as very good. It's principally an Iberia LAN relationship, and we're now extending that to bring in TAM and BA and to strengthen what has been traditionally a strong relationship between Iberia and LAN.

Andrew Lobbenberg - *HSBC Global Research - Analyst*

Lovely. Look forward to hearing more next week. Thanks.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Okay. Thanks, Andrew.

Operator

Suzanne Todd, Morgan Stanley.

Suzanne Todd - *Morgan Stanley - Analyst*

Just one question. BA has seen labor cost benefits from better productivity, and you're also aiming to reach agreement on productivity changes at Iberia. Can you give us just some more concrete examples of the changes you've made at BA? And is that the model you intend to bring into Iberia as well?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

We look at what's appropriate for each of the operating companies. It doesn't necessarily mean the same thing. BA has had significant benefit from the introduction of mixed fleet and cabin crew, where as you know, we've negotiated new terms and conditions that are -- I would describe them as market terms and conditions, and that addressed the cost differential that existed between BA and some of our competitors. So they're clearly getting a big benefit from that.

They've negotiated improvements in productivity at Gatwick. We've outsourced some activity that we used to do internally where we felt that outsourcing was a more appropriate way of improving productivity. We've had very good cooperation from all of our workgroups in BA. And what we're seeing now is with the growth that BA is embarking upon, the productivity agreements that we negotiated, we're being able to exploit them better.

The other thing we should highlight is that there was a dis-benefit associated with the introduction of the 787 and A380 because we had to train up, particularly pilots, in advance of them being productive. So as we start taking deliveries of these aircraft, we get an improvement in productivity because pilots who were not flying productively on the line but in training start becoming productive.

So productivity benefit will continue to accrue as we expand the long-haul network with the delivery of new aircraft that Keith spoke about.

Suzanne Todd - *Morgan Stanley - Analyst*

Very helpful. Thank you.

Operator

Tim Marshall, Redburn.

Tim Marshall - *Redburn Partners - Analyst*

The BA margins in the September quarter were similar to what you did in September 2007 where you [estimated] a 10% margin for the full year. I just wonder if there's anything particularly seasonally different between the business now and then, or perhaps you could compare the way that the business is performing now compared to back then when you did the 10% margin.

Then just on US Airways American, can you just --? If that does now go through, what the incremental benefits of US Airways coming in might be.

And then finally, if my memory serves me right, the integration costs for the synergies this year was around about EUR90 million, and that falls quite a bit as we go into next year. Just whether that's still the case or not.

Thank you.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Tim, I recognize that we haven't given much of an update in relation to synergies, so I think it would be useful for us update you on the synergy program next week at the Capital Markets Day, because you're right, there have been big changes in what we had previously shown you and what we've actually delivered. So Andrew has taken a note of that and we can update our performance and the synergies.

I would say that we're pleased we're still making good progress on synergies, and we are clearly looking to see if there are opportunities for new and additional synergies beyond the ones that we have previously identified.

The BA performance is interesting because we've got fewer ASKs in this quarter than we had in that peak quarter. Fuel is clearly very different. So the revenue performance has improved. BA has a better cost performance.

But I think there's still more to come from BA. And that's what we've always said that the benefit of the restructuring that BA has done becomes most apparent when we're able to get back into a growth environment for British Airways, which will happen with the delivery of the long-haul aircraft and the expansion of the long-haul network.

But, yes, I think the BA performance in the quarter has certainly been a positive development for us. I think to their credit, they've remained focused on their controllable costs, and that's something that we're very focused on here at IAG, ensuring that all parts of the Group do everything they can to maintain control of their non-fuel costs. And as you know, that's an area where we believe we have opportunity with Vueling pursuing growth, a little bit of growth in BA. And ultimately, when Iberia gets its cost base right, we can pursue growth in Iberia as well.

So I think there's more to come. I described this quarter as a very positive development for us, but there's still much more work that we need to do. And obviously, the external environment in 2013, particularly in the fourth quarter, I think is going to be slightly different to the fourth quarter that we witnessed at the peak in BA.

On US, AA, to be honest, I don't think there is anything we can say at this stage, Tim. We're optimistic that agreement can be reached. We were pleased to see the parties engage in mediation. I think that was a positive development. And we remain optimistic that the merger will be approved. We haven't done a lot of work with them.

As you know, we are able to talk to American, but on the issue of the merger between AA and US, they have been very focused on preparing for the litigation in the first case, and now involved in the mediation. So to be honest, we've left them alone because we were keen that they focus on that with a view to getting approval.

So if I'm honest, I haven't had any discussion with my counterparts in AA on the potential opportunities while they've focused on dealing with the scheduled court case with the DOJ.

So we'll give you an update if we can next week if there has been any development. Hopefully, there will through the mediation. But it's -- as I said before, I don't see any benefit accruing to us in 2014. It's likely to be something that will come through in 2015 and beyond. So we're not targeting anything at this point in 2014 in terms of additional benefit.

Tim Marshall - *Redburn Partners - Analyst*

Great. Thanks a lot.

Operator

Andrew Light, Citigroup.

Andrew Light - *Citigroup - Analyst*

Three questions. First of all, can you comment on the performance of your new routes you've introduced this year, I think like Seoul, Chengdu and Leeds, for example?

Secondly, can you remember the negative impact of Hurricane Sandy in the fourth quarter last year?

And then thirdly, on premium traffic, which has been quite resilient and quite strong, particularly in October, are there any particular corporate sectors which stand out as doing well?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Leeds, I haven't looked at Leeds recently. I looked at their results, their football results, which have been up and down (laughter). I'm hoping our route performs better than the team.

Chengdu, we're pleased about. Chengdu and Seoul have been good. I went out to Chengdu on the inaugural flight and I was surprised to see the return flight from Chengdu was full. And I came back on the second flight which was full. And that to us is very good because we always thought that the challenge for us is selling in China rather than in the UK. So we're very pleased with the performance of Chengdu.

It's very early days yet, but Seoul is performing well for us. So the new long-haul routes that we've identified, we're very pleased with the performance.

I can't remember Sandy, but I'm sure we'll have something to talk about in the fourth quarter. We normally have a hurricane or something. But we'll see if we can find an answer for you. But I can't remember offhand what the impact of that was.

Premium, as I said before, I think we benefit from a strong London performance. The London economy has been doing well. There aren't any particular [stars] or areas of particular strength in terms of the corporate performance. It's pretty much across the board. We haven't seen any areas that have indicated stress either. So I would describe it as just continuing good performance in the long-haul premium market.

And the corporate market has continued to grow, in fact. No evidence of any concern with any of the corporate that we keep an eye out.

Andrew Light - *Citigroup - Analyst*

Great. Thanks very much.

Operator

Donal O'Neill, Goodbody.

Donal O'Neill - *Goodbody Stockbrokers - Analyst*

First question just a point of clarification, if possible. Could you give us a view on what the reduction in non-fuel unit costs will be for the full year? You've said it will be down, but a number would be helpful.

Second question; can you give us any sense of what you think the proposed price reductions, or potentially proposed price reductions from [AINA] might mean for you guys, or your potential growth strategy there in Spain?

And lastly, I wonder if you could give us a view on what impact you think our friends in Norwegian might have on the long-haul market ex London, maybe not necessarily on yourselves, but on the market in general. That will be great.

Thank you.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

I can't give you an exact figure, but we're talking about a slight reduction in non-fuel unit cost.

The AINA price reductions really won't have a lot of impact, certainly for Iberia. There might be some benefit for Vueling, particularly if they identify some domestic markets from Barcelona. So it could be some opportunity for Vueling. But we're not pursuing growth in Iberia until we have the cost base addressed. So if I'm honest, we don't really see that impacting on our performance in 2014.

On Norwegian, it's a very, very small additional capacity on the transatlantic. I think they're doing, if you take New York, three flights a week against 30 flights a day at Heathrow, so it's not that significant. And as I pointed out to people, BA has widespread availability at GBP220 where Norwegian is pricing often well in excess of that.

So at GBP149, I hope they sell all their seats at GBP149, because they'll lose a hell of a lot of money, given that APD in the period next year would be GBP69, and fuel, which they have to pay for, so they're not going to make any money selling at GBP149.

Plus, as you know, GBP149 is the basic fare. If you want to check in or if you want to have a cup of water, I think you've got to pay extra money.

So I don't see it being a game changer at all, to be honest. I'm probably sounding overly cynical towards them, but I think it's being hyped up in the media more than it deserves. And we're not doing anything, we're not changing anything in relation to pricing or our capacity to reflect what Norwegian is doing.

Donal O'Neill - *Goodbody Stockbrokers - Analyst*

Thanks. I might just ask one follow-on question on long haul out of London. Have you seen any tangible change in behavior from Virgin Atlantic as a result of the tie-up with Delta?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

[They withdrew] from Accra, which didn't surprise me, and the thing that did surprise us was they handed the slot back into the slot pool, and that was an unusual thing for them to do. But I suspect that reflects a new rational approach where to operate that slot through this winter period they would have lost money.

So that's the only obvious thing that I have noticed, which I think is a significant change of direction. But as I said before, every speech that Richard Anderson makes, he talks about return on invested capital, everywhere, every day. Everyone within his organization talks about return on invested capital. And that to me is the rational language that I like to hear and the rational language that we need to hear. And as a result of that, I've held my view that the merger of Virgin and Delta remains overall a positive development for us and for the industry.

Donal O'Neill - *Goodbody Stockbrokers - Analyst*

That's great. Thank you very much.

Operator

Robin Byde, Cantor Fitzgerald

Robin Byde - *Cantor Fitzgerald - Analyst*

Just one from me on potential dividends. Your free cash is improving, the balance sheet is stronger. Are you anywhere close to recommending a dividend, or am I just two years too early with my question (laughter)?

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Yes and yes. No, clearly, we've publicly stated that in everything we do now, and all the plans that we make and all of the investments that we approve, we're factoring in a dividend payment.

So when we're looking at any CapEx proposal, associated with that is a return that would enable us to pay a dividend. But we've not had the discussion, the formal discussion about a dividend policy, other than the Board yet again has reaffirmed that it is the intention of the Board to introduce a dividend payment at the appropriate time.

But we're not at that stage yet, and we clearly have work to do, particularly in relation to Iberia. But it is the stated objective of the IAG Board to introduce a dividend payment, and everything we're doing is -- AIG at a management level is driven towards getting us into that position.

Robin Byde - *Cantor Fitzgerald - Analyst*

Okay. Thank you.

Operator

Geoffrey Collyer, Deutsche Bank.

Unidentified Participant

Well, it's actually Anand. A couple of quick ones. Can you talk about what you see as your main focus now? I think a bit earlier in the year, it felt like you were happy with where Iberia was going. Actually now, you're looking a bit more at -- looking closely at what BA was up to. So I was just wondering if you could just update on that.

And particularly given the strong performance, do you think -- your comments that you want to achieve high watermark margins in 2015, do you feel more confident about that and should we be thinking about perhaps a little bit better?

Keith, could you just go through on the A380 just in a bit more detail what you're seeing on unit yields and unit costs on those routes where you're introducing it?

And also, should we be thinking about it as a like-for-like plane replacement? Or do you think you'll be taking out two planes when you put it on the transatlantic and replacing both of them with one A380?

And then just lastly on Vueling, do you think it makes sense to create a new hub for it at Madrid, or how do you see that?

Thank you.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Okay. I'll deal with it in reverse order. I don't think Keith will give you the answer, but I'll (inaudible) (laughter). No, I don't think Vueling needs to create a hub at Madrid. It's got plenty of other opportunities that are more attractive to it than Madrid is at the moment. And we're not putting any pressure on Vueling to change its approach.

So they've identified several opportunities that rank well ahead of them establishing an increased presence; they do have a presence in Madrid, but an increased presence at Madrid.

And looking at Keith, he's looking pretty stubborn. I don't think Keith --?

Keith Williams - *International Consolidated Airlines Group SA - Board Member and CEO of British Airways*

We're really very, very pleased with the performance of the A380 on both Los Angeles and Hong Kong.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Okay. And our focus -- to be fair, although we're pleased with the performance of Iberia, as I've said quite clearly, it's a good start, but there's a hell of a lot of work to do.

We're delighted with the impact that Luis and the new management team has made. It's great to see they've been able to deliver an operating profit in the quarter, but there's a lot of work that they need to do. And we're not going to remove the focus on Iberia because the work that needs to be done there is -- remains quite significant.

We've continued to be very much focused on cost control across the Group. I'm pleased -- with the addition of Vueling and the addition of Alex to my management team, it reinforces what has been a strong culture within IAG about non-fuel unit costs. But having Alex identify some of the things that they've done I think has been of benefit to others within the IAG Group.

So BA has challenges still, but is making good progress. And as I said, great credit to the team there for their focus on their non-fuel unit costs. We want to make sure that that focus continues through the rest of this year and obviously in the future as well.

So for us, we remain very focused on Iberia because we've got a lot of work to do there. We're very focused on the improving performance of Iberia -- British Airways, and we're really impressed with what Vueling has been able to do and excited about the opportunities that Vueling has for the future.

And what we need to do now is make sure that at IAG, we're presenting them with as much support, which was evident in the fleet order that they made. But if we can help to further improve their cost base, it's got an unbeatable formula in terms of very efficient costs, great flexibility, great speed of reaction to market opportunities, and a product that is superior and continues to improve and to innovate against its principle low-cost competitors.

So there's plenty for us to do. The one thing that we're not doing at the moment is looking at any additional M&A activity because we just don't see anything that's of interest or attractive to us at the moment. But we do remain open to the possibility if the right possibility comes along.

Unidentified Participant

Thanks for that.

Willie Walsh - *International Consolidated Airlines Group SA - CEO*

Thank you. And I think that's it, so can I just finish by thanking everybody? And we look forward to seeing you all next Friday.

And I apologize for those of you who asked questions in relation to answers that will be given next Friday, but I'm sure you'll understand we're putting together a comprehensive presentation for you which will give you greater visibility in terms of our views on 2014 and this 2015 target that we have identified.

Thank you very much, everyone.

Operator

Thank you. That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.