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IAG.L - Q3 2014 International Consolidated Airlines Group SA Earnings Call

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PRESENTATION

Operator

Good day, and welcome to the Q3 2014 results presentation of International Airlines Group. At this time, I would like to turn the conference over to Mr. Willie Walsh, CEO. Please go ahead, sir.

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

Good morning, everyone, from London. Thank you for joining us for our third-quarter results presentation. As usual, I'll hand over to Enrique Dupuy to take you through the presentation, and when Enrique is finished we'll be happy to take your questions. Enrique?

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

Thank you, Willie. Good morning, everybody. We are presenting today another good set of results this time for Q3, for the summer holiday quarter. If you go through the summary page, we have been achieving an operating profit at a Group level of EUR900m, and this is above last year figures, by EUR210m.

Through the following slides, we would explain how, adjusting the ForEx element, this EUR210m will be turning into EUR236m. So this positive improvement in reference to last-year results has to do a lot with the combination of unit revenue performance and unit cost performance.

Unit revenue performance in actual terms has been slightly positive, 0.4%. When we get into constant ForEx terms, we have achieved a marginal reduction of 0.9%. And we'll go through the different segments and geographical areas of our network to explain how we've been performing in each of them.

It's -- as you probably agree with me, the reduction in ex-fuel unit costs, 4.5% at constant currency terms, is very impressive. And it's again following a consistent row of ex-fuel cost -- ex-fuel unit cost reductions that we've been achieving on the previous quarters. Taking into account that the fuel has again been a tailwind for the Group in the last quarter, total unit cost in constant terms have been reduced by 5.7%. And this on a capacity increase of 9%, which you will see has very much to do with Vueling growing 28% and Iberia plus British Airways growing about 6.5% in the quarter.

So if we turn to the following page, we will be seeing how this EUR210m -- at EUR236m of improvement at constant currency terms are split between the different contributors. So in terms of passenger revenues, we see a very significant contribution coming from growth, more than EUR400m, with a slight dilution coming from price and mix. Non-passenger revenues brings a slightly negative contribution, and it's more -- most of it related to accounting issues, so having to do with Vueling consolidation and eliminations across the group.

When we get into the cost side, ex-fuel costs have been improving significantly. And we are going to concentrate on the issues behind, both in terms of employee, labor costs, and also supplier costs, with of course a negative impact of growth.

In the case of fuel, as you will see, the negative increase, having to do with the growth that we have been producing, has been quasi offset by the price reduction that net of hedges we have been able to achieve in the these quarters.

Ownership costs, even through the renewal of the fleets that we are undergoing, have had a marginal negative impact on our basic Q3 operating profit.

So getting a little more into the non-fuel unit cost evolution, what we see is employee unit costs have been driven down very significantly. And of course, it has to do with Iberia implementing their Mediator plan and achieving very significant improvements in terms of productivity. So the redundancy program in Iberia is following its path, even it's accelerating the initial, I would say, schedule that we had.

But again, British Airways is improving its employee unit costs, and this is good news. It has to do with what we've been explaining about the model of efficient growth that we are implementing in British Airways.

Vueling has had a marginal deterioration. And this is basically related to the expansion, international expansion, and the opening of new bases, especially in Italy, with initial one-off costs.

On the supplier side, on the supplier side is basically good news, so on the handling and catering arena. And the good news are coming from the price and the mix element. Of course, Vueling is bringing its better averages to the Group, but also Iberia and British Airways have been able to improve their contractual costs through supplier negotiations.

In the case of landing fees, it's more or less neutral in terms of stage length and slightly negative because we are suffering a bit of inflation on some of our destinations and operations.

When we talk about engineering, the picture looks very positive, and this having to do with supplier renegotiation as well. It's also about getting through these first deliveries of 787s and the A380s that now we'll be leaving behind. And significant improvements also on Iberia in terms of engineering costs, again, having to do with the introduction of a new and more reliable fleet, the A330s.

Ownership costs show a couple of two-folded developments. On one side, as you can understand, depreciation is increased because of two things, on one side, new fleet coming into British Airways, basically, on an ownership basis. The other one, as you will remember, is a change in the depreciation scheme for the 747 fleet.

On the lease side, it's basically improvements coming from Iberia renegotiating its own contracts and also freighter -- cargo freighters discontinuation.

So as a whole, it's been a very robust and structural improvement that you see is getting on a like-for-like basis, constant currency, to 4.5% for the Group.

If we talk now a little bit about fuel, of course in the pattern of a reduction in fuel costs that we are forecasting, you have to take into account two considerations. On one side, it is our hedging profile, and we are showing how we have been hedging our consumption for the following quarters.

On the other side is the counterbalance of the dollar strength, that it's limiting our savings in euro-expressed terms. Remember that the strengthening of the dollar has its -- at the other side of the equation, has a very positive impact on our revenue base, as the revenue that we have denominated are strictly linked to dollars.

So as a whole, what we see is fuel costs will be coming down in IAG Group through the following quarters. We are sticking, for the year, to a EUR6b figure of total bills for fuel.

And we again would like to remind you that in this chart that we are showing, the changes and improvements are basically related to market fuel prices, kerosene prices specifically. Our hedge profile, our dollar estimates on hedges profile, are not included the expected improvement in our unit cost because of our new fleet and our improvement in procedures. And that's having a very significant impact through this year already.

On the capacity trend, we are bringing again this chart that you know well about that shows how capacity has been growing for the Group in the last quarters. So if we concentrate in Q3, where you can see capacity has been up 9% for the whole Group. If we take into consideration only British Airways and Iberia, that would be 6.5%, so downsizing on a fine-tuning exercise the previous figures that we have shown to you.

If we get into quarter-four expectations and projections, as we already told you, as we told you before, we are expecting the whole Group capacity growth to be reduced to 6%. And then when we talk about British Airways and Iberia, the figures will be showing just a 4.1% growth for the next quarter.

So basically, what we now will be forecasting for the Group on a full-year 2014 basis, we'll be making 7.1%, including Vueling on a pro-forma basis, so full-year basis again for Vueling, and 5.2% for British Airways and IAG.

Let's see how this capacity - thank you very much. Willie has brought for me a little bit of water because my voice is not perfect today.

So this is how we see the capacity growth that we are expecting into Q4 on our different operating companies. As I think we anticipated to you in the past, British Airways capacity is coming down into the 3% level, and it's going to have to do very much with a couple of areas of increase. On one side, it's going to be about new routes, just 1.2 percentage points allocated to new routes. And it's going to be also about increase in aircraft gauge. So as you know, this has to do very much with a year-on-year impact of the introduction of the 380s and the 787s and the substitution of 767s and other bigger aircraft.

So as a whole, this mix will be increasing our average size in our aircraft, in the case of British Airways by 1.7%. So these two and the limit of additional frequencies are the ones to define the 3.4% we are regarding for next year.

In the case of Iberia, the pattern is of higher capacity growth. This is basically because Iberia is restoring some routes that they are -- they were operating before. They know very well about the traffic and the customer profile on these routes. On the long haul, it's about Montevideo and Santa Domingo. In the short and medium haul, it's about feeding routes, basically it's Istanbul, it's Amsterdam and it's Stockholm.

So as you see, this exercise of growth in Iberia is very strictly related to the recovery of profitability that we are seeing on their operations. In a chart that is going to be coming next, we will show how profitability in Iberia on the third quarter has been improving to reach, I would say, best in class in the Group. So this is very good news.

For the case of Vueling, as you well know, Vueling is our growth tool and Vueling has been growing above 25% in Q3. And basically, it's having to do with opening of new routes. As you know, basically, Italy is going to be, it has been, it will be a very preferred market for Vueling expansion and it basically will be accounting for most of the new routes that have been opening, a little bit of domestic additional markets and European markets being -- receiving more frequencies through the - this last quarter as well.

So let's get now a little bit in capacity and the RASK chart. And this one is one you well know now. It's related to how we've been growing in the different regions and the RASK type of achievements that we've been able to produce in these same regions.

So the first one I would like to mention because I think it represents a very positive achievement in this Q3 -- sorry. It is the performances in North American market, so a very significant level of growth, 7.1%. But at the same time, even if it's marginal, a positive improvement in unit revenues, so 0.6%.

And this again demonstrates that this market is behaving strongly, is being managed in a very rational way. And we at IAG have, with our partners in the US, a very significant leadership position, which is enabling us to produce this combination of high growth and increasing unit revenues.

Let's talk now about domestic and Europe because here of course we're integrating for the first time Vueling figures, so 100% of this domestic improvement that you are seeing increase in terms of RASK is related to Vueling. And about more 0.5% of the European capacity increase that you are seeing there is again having to do with Vueling expansion.

So here, unit revenues have been coming down, but of course, as you will see, Vueling is very able to produce positive margins and positive operating profits at those level of unit revenues. And then that's something that we are going to show again.

Another one it's worth to mention is Latin America. We've been growing in Latin America and unit revenues in this area have been disappointing. And probably you've been hearing more about this -- the reasons behind. They have been about the impact, negative impact of the football cup, especially in the month of July. And then negative performance, why not to say, in three specific areas, which are Brazil, Argentina and Venezuela. The rest of the company -- or the countries have been more or less on a flat or minus performance.

And then finally, Asia and Middle East, Asia Pacific and Asia Middle East, which have been benefiting from significant growth. But at the same time, we've been able to keep unit revenues with just, I would say, marginal drops, and that's producing positive contributions at the operating profit level for the Group.

So as a whole, probably this is the last quarter you are going to be seeing this level of growth, especially in the long-haul market. And we are happy with the unit revenue performance that we have been able to achieve in the different areas, maybe with a little bit of disappointment on the Latin American market.

If we get then to this next chart, which has to do with the different products and segments that we are operating; on the long haul, both premium and non-premium, and for different reasons, political instability and I suppose critical conflicts in some areas, have been also, in some way, loading down our performance, especially in the premium side. We are seeing slightly negative impacts, both in long-haul premium and long-haul non-premium.

In short haul, it's very interesting to note how British Airway's performance has been neutral. Iberia has been slightly negative. And of course, as we said, Vueling has been more negative, very much having to do with the expansion in some areas, as Italy, Brussels and others.

The non-passenger is really about revenues that are not so much related to ASKs, so the negatives here are not strictly a negative impact. It's about cargo being affected by the discontinuation of the freighters. It's about maintenance revenues and handling third-party revenues following different patterns to the growth in ASKs that we have been producing.

So getting then to the following page, which is about the financial performance per brand. We -- is that working? Okay. Yes. Now it is working. So here we are showing on our different operating companies, our three brands, what has been happening in these last quarters.

So for the case of British Airways, lease-adjusted margin has been reaching 15.2% at operating result level, which is 2 percentage points above last year. So a positive improvement and some very specific matters that we are proud about; employee cost per ASK, so been reduced by 3.6%; CASK as a whole has been reduced by 7.2%; revenues improving by 1.5%. So as a whole, the performance for British Airways has been improving significantly from last year.

If we get into Iberia, I will make this correction that it has to do with a very high percentage of operating leases that they are using. The operating margin for the summer season in Iberia would be reaching, on an adjusted level, again 15.2%. And this is extremely encouraging.

So you have to bear in mind, you have to take into account that Iberia has a more pronounced seasonal pattern than British Airways. So of course the truthfully for Iberia it's not about the average, but it's again very encouraging to acknowledge how Iberia has been already able to improve the margins in the summer season. And the why, and the argument behind, because employee costs, as you see, per ASK have been reduced in Iberia by 10.3 percentages, a very impressive figure.

So as a whole, you can see lease-adjusted margin in the case of Iberia is improving 7 percentage points above last-year figures. And it is justifying the recovery of these routes that we were mentioning before and they will be justifying the recovery of more routes in the future, and the recovery of market share in the Europe-to-Latin-America market.

In the case of Vueling, basically, lease-adjusted markets have reached 23%, that it's a high end of the range type of margin. It is below last-year figure, of course, but when you consider the reduction in the margin you have to take into account the increase in ASKs that they have been producing on this quarter, 28%. So a reduction in margin of 4 percentage points, a retained operating margin of 23% on a 28% capacity growth, we think it is a very significant achievement.

So let's finish with our balance sheet main figures. Adjusted equity has been improving through the first nine months of the year, basically because of retained earnings. Gross debt has been also increased because of the financing of the new fleet. But as you see, cash and cash equivalents have been increasing faster, so by nearly EUR1.4b, reaching EUR5b by the end of September.

So on balance sheet, net debt has been reduced to EUR1.91m -- EUR1,000m, sorry. And then the in balance sheet, balance sheet gearing has been decreased to 14%.

Of course, we have to take into consideration operating leases. As you well know, we use an 8-times multiplier, so we'll be getting to an equivalent notional operating lease debt of EUR4.4b, to produce a total equivalent adjusted net debt of EUR5.5b, which is lower than the one that we kept at the beginning of the year. And that's why our adjusted gearing has been improving by 4 percentage points and getting to 46%. Remember, our medium-term guidance is about 50%.

So finalizing with current trading and our outlook. This is becoming a little bit of a boring chart. We have this sense of stabilization. Our main markets, our main segments, what we can say today is they remain stable. What we will be seeing is probably, even a better balance through Q4 and next year of capacity and demand in our main strategic markets.

As still a little bit of an anecdote, we are showing you a slight improvement of cargo yields and cargo unit revenues on some markets. And this is a trend that we are still cautious about and that we will -- it will have to consolidate through the following quarters before we consider it as a new trend.

So the guidance for the full year 2014 has been improved slightly. Now we are saying that our full-year profits will be exceeding, improving the ones in the base, so the EUR770m of last year, by a range between EUR550m and EUR600m.

We are keeping our fuel bill scenario for the full year, and this is because the level of hedging and the impact of a stronger dollar, to EUR6b.

And we are fine-tuning our level of growth for the full year at the 9.3% on a reported level. That will be 7.1% on a pro-forma level.

So this is basically my presentation, and I'll give you back the word for your questions or your doubts.

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

Okay. Thanks, Enrique. You can take a break now.

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

Thank you.

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

And hand over now to the operator to start taking your questions. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Stephen Furlong, Davy Research.

Stephen Furlong - *Davy Research - Analyst*

Morning, gentlemen. I just -- just one or two quick questions. Just -- could you just comment on the fuel price movement? And I was just trying to understand whether you still see some correlation between that and the revenue, how you play that, lower fuel prices, in terms of fuel surcharges and things like that and that dynamic.

And the second thing, maybe just -- you might just talk about the cargo market a little bit and why maybe you think it might be improving. Is it because of maybe freighter capacity has been taken out or demand is improving a bit?

And maybe you just -- might just touch on, finally, the competitive dynamics at the new bases of Vueling in Rome and Brussels. Thank you.

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

Thanks, Stephen. The fuel impact in the third quarter was minimal, as you know, because of our hedge positions. So as Enrique said, we had a relatively strong hedge position going into the quarter, as we do going into the fourth quarter.

In relation to fuel surcharges, we keep that under review on an active basis and we'll continue to do that. But when we're looking at pricing, obviously it's the blend of the various functions of pricing. And I would describe the environment as being reasonably stable given what we're seeing, but to reinforce again that, going into 2014, we always believe that the profitability this year will be driven much more by our cost performance than our unit revenue performance. And I think we're really demonstrating the benefit of discipline in relation to cost compared to some of our major competitors, and that will clearly continue to be a focus as we go through the final parts of this year and into next year.

Cargo, I think best described as improving demand. Capacity, although the freighters are coming out, we're still seeing capacity growing through belly hold. So the general capacity environment is probably still growing slightly, but clearly the removal of freighters is improving the general situation. But for us, it's been a big benefit, so taking the freighters out of our operation has been very positive.

What's been particularly positive is the arrangements we have with Qatar because we've been able to replace capacity on key market flows where we're seeing growth, and that is out of Asia, through the arrangement we have with Qatar Airways. So I think we see the general cargo environment improving. The cargo guys are optimistic. I wouldn't describe them as being bullish, but they're optimistic about the rest of this year. And clearly, going into next year, our situation is improved as a result of the changes that we've made, removing the freighters from our operation.

And Vueling's competitive environment, particularly in the new bases, is exactly as you would expect. It is competitive, which is what we thought it would be. But Alex is pleased with the way their presence in those markets is developing. It's very much in line with what he had expected to see. We remain confident about Vueling's ability to compete. And that's enhanced by what we see as continual retrenchment by the so-called legacy airlines, which is leaving good space available to grow where people have a competitive cost base.

So we're doing well, and what gives us good confidence about our ability to compete is when we look at our EBITDAR margins, which are operating above those of EasyJet. So it's a competitive environment, but I would say generally it's in line with what we had expected to see.

Stephen Furlong - *Davy Research - Analyst*

Great, Willie. Thank you.

Operator

Jarrod Castle, UBS.

Jarrod Castle - *UBS - Analyst*

Good morning, gentlemen. Three questions if I may, please. Just one thing about the result so far from the flag carriers is both for Air France and Lufthansa we saw, over the quarter, material changes in the pension deficits. So I know your next actual review, if I'm not mistaken, is March 15, but just from an accounting perspective, just on slide 15, has that taken into account any changes in pension regarding changes in discount rate assumptions? If you can just talk about that situation from an accounting perspective.

Secondly, just looking at your fuel hedging, 74%, is that normal that you actually -- so much hedged at this stage of the year? I would have been expecting a number which would be slightly lower. Is there any change I guess in hedging policy at the moment going on?

And then just lastly, just on Iberia, you did touch on it a little bit in terms of the redundancies. Do you care to put any numbers in terms of people putting up their hands and people leaving Iberia? Thank you.

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

Okay. I'll ask Enrique to deal with the pension issues and then I'll come back to the fuel hedging and Iberia.

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

Yes. On the pension issues, we basically re-evaluate our variables and our position in balance sheet and profit-and-loss account on a yearly basis. So that's something that we will be doing by the end of the year.

In that sense, what we have been acknowledging through the last quarters is a consistent reduction of our pension fund deficit in actuarial terms. Of course, we'll go through the formal revision by the end of the first quarter next year. So that's what we can tell you about. We will make this formal evaluation on our full-year accounts.

Maybe the sterling-denominated corporate bonds have been more stable as well in terms of our yields than the Central European ones, so we don't anticipate major changes.

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

In relation to our fuel hedging, we've not had any change in policy. One of the issues that we are considering is whether we start looking to hedge out into the third year. We don't normally do that, but that is something that we have looked at. So it is absolutely within the structures that we have disclosed and operated, so we've not changed our policy at all and we will continue to apply fuel hedging structurally in the way we have done so because we believe that's the sensible thing to do.

On Iberia, really pleased with the performance there. The restructuring is showing very good returns. There's still more work to do. The first stage of that, which will be, if you remember, the mediator's plan. We're well through that and have accelerated the implementation of that. The next stage, which is voluntary redundancy, we're getting good appetite. There's a good appetite for the redundancy under the program. It's a bit early to give you any details, but it's something that we'll -- we can talk about at Capital Markets Day next week.

But so far, we're pleased with what we're seeing, particularly in the areas of higher-cost employees, where there is good appetite for the redundancy program that we've put in place. And that will, as we described earlier this year, show improving labor unit costs going forwards, which will clearly position Iberia very well to not just recover some of the lost ground as a result of the capacity reductions during the restructuring, but look at some new growth opportunities for Iberia.

So really pleased with the performance there. I think the team has done extremely well. They're clear in terms of what they need to do and very determined and committed to deliver.

Jarrod Castle - *UBS - Analyst*

Okay. Thanks very much.

Operator

Credit Suisse, Neil Glynn.

Neil Glynn - *Credit Suisse - Analyst*

Oh good morning, if I could ask three questions also please. The first on transatlantic revenue, the revenue piece seemed to be up about 8% in the third quarter, combining pricing and capacity, but I was interested to understand how much do you attribute that to share gains in premium and also economy classes and what do you see as the drivers of those gains? I'm sure you've done a lot of work to understand your performance relative to peers, who obviously clearly have been a little bit behind.

The second question on Vueling, obviously Enrique mentioned comfort with Vueling's performance, but when you grow to that extent I'd expect something a little bit better than flat ex-fuel unit costs. So can you confirm are there additional costs of starting up in the new bases, marketing spend, etc., in there and what do you see as the underlying ex-fuel cost performance at Vueling?

And then thirdly, obviously very impressive from Iberia in the third quarter; it seems to be cost driven per the numbers, but to what extent can you see new commercial initiatives showing up in these numbers at this point?

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

Okay, the transatlantic, yes, we monitor very carefully our market share, particularly in the premium -- more so in the premium than in the non-premium, and we continue to gain market share from competitors. It's a strong market, we have always said that the transatlantic with the GDP growth that we're seeing at forecasts in the US and in London supports the additional capacity that we've put in there, because the market continues to grow well and capacity is, I think, very disciplined. So we're pleased with the performance but there have been small gains in premium market share. If we look we -- I would describe them as more significant gains last year, but we continue to make progress with our premium market share and that's something we keep under review.

Vueling, the Vueling performance I think is good, in the circumstances. You're right to highlight there are costs associated with the stage of the expansion that they're doing because this is more about going into new markets rather than growing in their traditional Barcelona hub, which clearly has some costs associated with it. They will continue to improve as we develop our presence there, so Enrique said we were comfortable about it -- we are comfortable about it; it's very much in line with what we had expected to see. There are some adjustments that Alex will be making, but in the main I think they've done a good job. They're very focused on areas where they can see some opportunity to reduce cost in the year ahead and we're very confident about their ability to continue to grow with the capacity that they've demonstrated so far; so good performance by Iberia.

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

There's a specific area in FHS cost base -- sorry, in Vueling cost base that is going to be improving and of course it has to do with the new A320 contract that is going to represent deliveries of new aircraft for the next four to five years. So, as you know, the way Vueling has been expanding has been basically through the introduction of second hand aircraft and this has created a real complication in the sense of extending leases, looking for new aircraft in the marketplace, etc., etc.; also we're delevering old craft. So, that's going to be becoming better and better in the next three to four years, because the impact of the new stable fleet is going to be extremely beneficial.

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

And in Iberia, yes, we are beginning to see some improvement in underlying commercial performance. The brand positioning is very strong now in Spain. The rebranding that they've done, which was very, very cost effective, has been very successful and we have a new team operating in the commercial and revenue management department and they're beginning to make a difference, so I think that does represent some opportunity for us. But the opportunity, the main opportunity continues to be on cost and that's why we will continue to focus our attention on cost while having a clear look at the revenue opportunity as well, but I think there is going to be a mixture of both of those for Iberia going forward.

Neil Glynn - *Credit Suisse - Analyst*

Thank you and get better soon, Enrique.

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

Thank you.

Operator

Oliver Sleath, Barclays.

Oliver Sleath - *Barclays - Analyst*

Yes, good morning, Willie, good morning, Enrique; three questions please. First of all, just on competitor development and looking east, actually, I noticed that this winter both Qatar and Etihad, I think, A380s into Heathrow and there's quite a lot of scheduled growth by the Middle East carriers into London. Are you expecting any impact at all on that on South East Asia and India, or can you work with Qatar and some of the extra capacity they're putting in?

My second question is on BA on-time performance; I know that was a little bit weaker than you may have liked earlier in the year, I'm interested to know how that's been trending through Q3?

And my final question is on fuel. I wonder, do you see a risk in a lower fuel price environment that some of the weaker, unhedged airlines actually get a bit of a lifeline, if you like, and legacy retrenchments don't happen as quickly as may be anticipated? Thank you.

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

Okay, on -- yes, the A380s coming into Heathrow are what we'd expected, so we haven't seen any change and continue to look for opportunities to work with Qatar. We have a strong network into India where we serve five cities directly; in fact we're increasing our capacity there. We will also look at changing aircraft so we're moving more 787s into India, which actually we believe will be the right aircraft for us. So, overall, we're relaxed about the capacity development that we're seeing into Asia over the Middle East hubs. I think that will become more of an issue for our European competitors rather than us, because these guys have been in Heathrow, as I've argued before, for some considerable time so the addition of A380s was anticipated by us.

The Indian market will be best served by us by 787s, we see that as being the perfect aircraft, because it supports the point-to-point market better out of London and means we have less seats that we need to fill on a transfer basis and, as you know, transfer traffic is always at a yield discount to the point-to-point. Sorry when I said increased capacity, I should have said increased frequency, so we're going to daily services in Chennai, where we previously didn't, but with 787s rather than 777s and we see that as being positive for us into India.

BA's on-time performance has been improving in the third quarter, there is still more that they can do and will do and they've got a clear focus on this. So it's pleasing to see that they're looking to Iberia to understand how Iberia has improved their performance and we've had some people from BA talking to the Iberia people more to learn from the changes that Iberia have made. So there is some opportunity there, but I'm pleased to say that we have seen an improvement in the third quarter.

And on fuel, not really concerned about the reduction that we've seen, fuel is still in or around $85, $86 a barrel. Some unhedged carriers will get a little bit of benefit from that, but structurally fuel is about a third of the cost base, they're still going to have to do a hell of a lot more if they're going to survive in the short to medium term. So it might have the very, very small benefit for them relative to people who have hedged, but we see that as being insignificant in the overall scale of things.

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

I see the fuel hedge or not hedge advantage as a temporary one. On the other side, what's happening is this combination of low fuel cost but strong dollar will make the fuel bill in euros not coming down as quickly as people could imaging. But, at the same time, will provide airlines having a strong stream of dollar related revenues on a clear advantage with the companies that don't have them. So that's going to create a different competitive landscape in the next years if it keeps as it is.

Oliver Sleath - *Barclays - Analyst*

Great, thank you, that's very clear. Thanks.

Operator

Damian Brewer, RBC.

Damian Brewer - *RBC - Analyst*

Hello, good morning; the first question I've got is about flexibility, Willie, I know you mentioned it at the Q2 results presentation, could you tell us a little bit more about how that's worked in Q3, in particular improving Gatwick performance?

What's happening with densification of short-haul aircraft at Heathrow?

How you're thinking about the potential return of the BMI remedy slots?

What's happening with pilot flexibility?

And, finally, whether there is anything clever you can do with remaining lifetime on near-to-retirement aircraft, particularly the 747s at BA?

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

Yes, a lot of questions in one there, but flexibility we believe is absolutely key and we're fortunate in that we have what I would describe as structural flexibility that, if you like, Vueling has where they can upscale and downscale very quickly. So the fleet is structured in a way that we can release aircraft that are leased and we're all the time ensuring that we have capacity to take aircraft out of the fleet very quickly and they have flexibility within their labor contracts. So Vueling is in a perfect position to be able to adjust capacity up or down on a very, very short timeframe.

In BA you're quite right, the advantage we have there is the 747, where we can take 747s out of operation quickly. We've got 46 in the fleet at the moment and we will continue to wind that down. From memory, 17 of those aircraft are 16 years or less and the rest are 16 years plus and some of them are getting close to even 25 years. So we've got, I think, great flexibility within BA to adjust capacity down by taking 747s out and to adjust our recruitment. We're recruiting pilots so we can slow down the recruitment process.

So BA has what I would describe as good flexibility and Iberia's in a very similar position with the A340s, we've got great flexibility there. And, as we're going through labor restructuring, obviously that's a key issue for us going forward. I think at the moment we're very well positioned to be able to adjust downward the capacity if we were to see reason to do that, and that's clearly something we keep a very close eye on, but we will continue to ensure that we have good flexibility within the business.

The densification of seating on the A319s and A320s at Heathrow is making progress. Good, I have to be honest, good consumer reaction, I describe consumer reaction in that most people don't notice any difference and, where people have noticed a difference, actually they have been generally positive. You will always get some people who will be aware of what it is we're doing and make some negative comments, but when we look across the customer base, the reaction has been actually positive.

Gatwick continues to make very good progress; we're seeing excellent load factors at Gatwick, so we're clearly making progress there. Still work for us to do, but that's been one of the bright spots in the BA performance, relative to where it is and relative to where it needs to be there's still work to do, but they're ahead of target in terms of the progress that we needed to see.

The remedy slots at this stage we're making plans to utilize the slots on the assumption that they will come back to us, but clearly they may not come back to us if somebody else steps in. We're not aware of anybody expressing interest in those slots at this stage, but if they do come back to us we have a plan in place to utilize them, bearing in mind that we have to continue to make them available on a remedy basis of somebody does step in.

And overall, I think we're seeing a good performance by all three companies. The star performer in the quarter has to be Iberia, but the performance there was to be anticipated on the back of the restructuring that we're doing. But it's great to see the underlying financial performance of Iberia being as strong as it is and that will give everybody there great confidence going forward.

Oliver Sleath - *Barclays - Analyst*

Great, thank you.

Operator

Juan Ros, BBVA Bank.

Juan Ros - *BBVA Bank - Analyst*

Hello, good morning, I have one question regarding the charge or the revaluation of the cash you have hijacked in Venezuela. I was wondering if you have -- you can provide us maybe a timeline of when can we expect the cash in and where would be the full amount or the restated amount; maybe you will get local currency or bonds or whatever? Thank you.

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

No, I don't think we can add anything to what we've added already. This is something that is in the process of negotiation with the Venezuelan government and it would be inappropriate for me to say anything at this stage.

Juan Ros - *BBVA Bank - Analyst*

All right.

Operator

Donal O'Neill, Redburn.

Donal O'Neill - *Redburn Partners - Analyst*

Hi chaps, good morning, I'll ask two questions if I can. First one, the Delta Virgin partnership I guess is realigning their growth plan a little bit more towards the North Atlantic into the first half of next year and I'm just wondering, how does that make you think about your pricing versus load factor strategy on those competing routes, I guess, particularly on JFK into the first half of next year?

And second question, can you give us an indication about how Iberia Express performed through the quarter and what part of the contribution was that to Iberia's very good performance? Thanks.

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

Thanks, we see no reason to change our position in relation to our competition with Delta, it's exactly as we had anticipated, they're doing what we thought they would do and our strategy is developed and we don't see any reason to change it at the moment. So, as I said, the transatlantic continues to show good underlying growth and our performance on the transatlantic is a strong part of the business at the moment.

We don't break out the Iberia Express performance, but clearly Iberia Express is positive, the cost base there is very effective. It's a fantastic vehicle for us because it's given us an opportunity, as Enrique mentioned, in terms of the capacity growth in Iberia. Clearly an element of that on the short-haul comes from Iberia Express because they can get back into market and we have the ability to grow the Iberia Express fleet. So it's performing very well, but we don't break it out in terms of performance in the quarter.

Donal O'Neill - *Redburn Partners - Analyst*

Okay, that's great. Thank you very much.

Operator

Andrew Light, Citigroup.

Andrew Light - *Citigroup - Analyst*

Hello, good morning, three questions. First of all, on capacity for next year, can you give us an idea of what you plan by airline in terms of ASKs?

Secondly, was there any significant windfall from the strikes at Air France and Lufthansa in the quarter and would you expect that to continue into the fourth quarter?

And thirdly, are you still on track to book a gain on the Amadeus disposals, of which I think you've made 30 so far?

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

Yes, we'll talk about capacity for next year next week at the Capital Markets Day. We did see a benefit in the quarter, in the third quarter from Air France and Lufthansa, principally from Air France and we saw that with all three companies, somewhere in the order of EUR40m.

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

Yes, 40 contribution.

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

In the third quarter and yes, we will get a small benefit in the fourth quarter. Most of it came in the third quarter and, as I said, it was principally benefiting from Air France rather than Lufthansa.

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

Yes. And yes, you are right; the capital gains that we expect to be achieving through the Amadeus divestment will be reaching the EUR85m figure. But as you know, we have to do it on a type of gradual basis so as not to disturb the market and the way their prices are formed every day. So the bulk of the figure will be achieved on Q4 and just a minor additional figure will be coming on the first quarter of next year.

Andrew Light - *Citigroup - Analyst*

Okay, thank you very much for that.

Operator

James Hollins, Nomura.

James Hollins, Hi, morning, three quick ones for me. The first one is following from Neil's question on transatlantic, are you seeing any noticeable benefit from US Airways coming into the joint agreement? I think they've now been in for a full quarter in Q3.

The second one was are you able to quantify or provide some detail on the unit fuel benefit from the more efficient and new aircraft coming into the fleet, or are they still so negligible it's really just down to the fuel price itself?

And the third one is just can you give us some full-year tax guidance? I think there's the recognition of Iberia tax assets coming in Q4? Any sort of guidance would be helpful, thank you.

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

Okay, we are beginning to see some of the benefit from US Airways, but probably best described as we see it ramping up now so it's still early days in relation to US coming in to the joint business, but yes there was some positive as a result of that.

In terms of fuel performance and new aircraft, it's about 2% or 3%, which is -- it's performing -- those aircraft are performing in line with the expectations and we're very pleased to see that we're getting some benefit from, particularly in Iberia and we highlighted this previously from a good operating performance. So that's also adding to the underlying fuel unit costs performance that we see.

And on the tax there are a lot of moving parts there from now to the end of the year. We have potential recovery of tax paid; we have the new Spanish law on tax being approved or not by the end of the year, so that's one that we'll give you much more details by the end of the year, if you don't mind.

James Hollins - *Nomura - Analyst*

Okay, thanks.

Operator

Andrew Lobbenberg, HSBC.

Andrew Lobbenberg - *HSBC - Analyst*

Morning, guys, can I ask about Iberia's growth plans into the fourth quarter? The logic of growing it is absolutely straightforward, but when Enrique discussed the different regional performance, in terms of unit revenue terms, it was Latin America which was one that stood out as being slightly weak. So to what extent might we be concerned about the impact on unit revenues from Iberia pushing forward on the throttle?

Second question, on Vueling and its labor costs, I didn't know Italians were that expensive, or maybe it's the Belgians, but that's a strong increase in unit labor cost at Vueling, how long might we expect that headwind to continue or how rapidly can Alex do something to put that into the reserve? Because, as Neil said earlier, you sort of expect unit costs to be going the other way with such strong growth.

And then just finally, do you want to comment a little bit about London City where you're continuing to grow and I guess that's trading nicely, but do you want to give us a bit of chat about that?

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

Okay, in Iberia we're very closely monitoring what Iberia does in terms of capacity. It is about recovering markets where, based on their previous performance, we know that there's good commercial demand and we know that with the new cost base that they have that they can be profitable in those markets and we're also, where there are competitors, we're targeting competitors where we think they're particularly weak in those markets. So strategically we believe that what Iberia is doing is absolutely right.

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

And then to the impact of the restored new routes, which have been restored early summer, it's a year-on-year impact just so there are not new routes coming into Q4, it's the year-on-year impact of the opening that Iberia decided earlier in the year.

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

In Vueling, the labor costs are driven by training and also some additional hotel costs associated with the way they're doing the growth in markets outside of Barcelona. So it's not the underlying cost of the employees, it's skewed by the amount of training that Vueling is undertaking at the moment, so we would expect some of these issues to flatten out as we go forward. They will have some continuing training costs as they go through the rest of this year and into next year preparing for the summer.

But some of this is just a bit -- biting off (technical difficulty) themselves in the right position and, once they get up to full speed, you'll see the underlying cost performance of Vueling improving plus, as Enrique said, there is also some cost improvements coming down the line in the aircraft and aircraft ownership costs.

And on London City, London City's actually -- we're really pleased with the way London City is going. We've got about 44% market share there. The Embraer aircraft is the perfect aircraft for London City. We are seeing some competitors grow, but we believe that our cost structure, our brand, everything to do with the BA position, the network that we have there, gives us confidence that we'll be strong in London City. So we're looking at London City carefully to see what's happening there, but we're pleased with the performance of our London City operation.

Andrew Lobbenberg - *HSBC - Analyst*

Okay, lovely, thanks.

Operator

Robin Byde, Cantor Fitzgerald.

Robin Byde - *Cantor Fitzgerald - Analyst*

Morning guys, just one from me actually. Just on ancillary revenues at BA, I think last year you set out fairly ambitious targets; that was at your Capital Markets Day last November, I think that was to grow ancillary revenues by about 40% between 2013 and 2015. So can I just get a quick update on progress there please? Thanks.

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

Yes, that's mainly through BA Holidays and it's progressing very, very well; so we actually had a review of it within IAG a couple of weeks ago and were very encouraged by what we've seen so far and the plan that BA had communicated is well on target, it's ahead of target in fact, and that's something that we see as an opportunity. It's generating very significant revenues, but interestingly we also see it now presenting an opportunity for Iberia.

So we're looking at leveraging the BA Holidays position to take advantage of the success that they've had there and extend that to Iberia and that's something we can talk about. In fact, we may at some point -- I don't think we'll have scope to get it into the presentation next week, at Capital Markets, but we'll try and get a presentation on BA Holidays for you so you can understand what we're doing there.

One particular area of great success is on the Caribbean out of Gatwick, so I think we've taken a lot of share from the main competitor in that market and that's something that's very encouraging at the moment. But as I said, I don't think we'll have time nest week to go into it in great detail, but we will for a future presentation get the team of BA Holidays to give you a presentation on what it is they're doing.

Robin Byde - *Cantor Fitzgerald - Analyst*

Oh great, thanks very much, thank you.

Operator

And from Deutsche Bank we've got Anand Date.

Anand Date - *Deutsche Bank - Analyst*

Hello, morning, everyone, it's just two intercontinental questions. I think LAN and TAM this week were saying that they want to ramp up their advertising and clearly be trying to improve, I think, their brand awareness in Europe. Do you think about that as a competitor being more aggressive, basically, to Iberia or is it a partner taking share in South America, which should therefore be positive for you?

And then just secondly, if we're starting to expect more US Airways feed on the transatlantic at the Oneworld hubs on the East Coast, do you have the ability to send more bookings or grow your bookings share on the US side versus the UK side? So I think that's something you've talked about in terms of FX on euro/sterling, is that something you can do as well on dollar/sterling?

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

Yes, the thing we need to say about Latam is that in some areas we have a joint business with them, so between Iberia and LAN there are markets where we have an immunized joint venture. Where we don't have an immunized joint venture, clearly we are competitors, but we are in discussions and have been in discussions with them about developing joint ventures. So it's a situation where in some markets we're partners and in some markets we're competitors, but we don't see any particular threat in terms of what Latam is doing. Longer term, we would hope to engage with Latam and develop a joint venture on the South Atlantic similar to the joint adventures we have on the North Atlantic.

And with US Airways, yes, there's always that opportunity and it is something we look at and you're right, we have talked about this previously in terms of where in the past we saw a strong euro switching point of sale more to that to take advantage of the currency benefit and we look at that in the context of the transatlantic business. But what I say about the transatlantic is demand is very strong at both ends of the routes, so we're not being overly picky where we take the customer, because they're all contributing handsomely to our performance on the transatlantic.

Anand Date - *Deutsche Bank - Analyst*

Okay, thank you.

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

I think you should be keeping some questions for next week, no?

Operator

[Martin Dreyer], Meridian Investment Management.

Martin Dreyer - *Meridian Investment Management - Analyst*

Hello, thank you for taking my call, maybe I could ask you to comment a little bit on the allegations you did to look e-Dreams Odigeo. Thank you.

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

Yes, we were absolutely clear in terms of what we did, we have been in discussions with them for some considerable time, we told them that if they didn't make the changes to bring themselves into line with consumer legislation that we would take the action. So if they believe we've done something wrong, I'm sure they will take steps, but we're absolutely clear that what we did was right and we will defend ourselves if they do choose to take any action against us. But it can't have been a surprise because we were absolutely upfront and we did what we said we would do and that is what we will continue to do, so I have no issue at all with the action we have taken.

Martin Dreyer - *Meridian Investment Management - Analyst*

Okay, maybe you could specify exactly what your allegations are?

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

No, I'm not making any allegations and I said what I would be prepared to say at this stage. We're not making any new allegations, if they want to do something we're happy to defend ourselves, but we're absolutely clear that what we did was right and appropriate and we gave sufficient notice at all stages, so we're extremely comfortable with the actions that we have taken.

Martin Dreyer - *Meridian Investment Management - Analyst*

And to what extent did they not respect --

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

You'll have to talk to them, you'll have to talk to them, it's not an issue for us, we're moving on and if they want to do something fine, but it's a completely non-issue as far as we're concerned.

Martin Dreyer - *Meridian Investment Management - Analyst*

Okay, thank you, all the best.

Operator

Mark Simpson, Goodbody.

Mark Simpson - *Goodbody - Analyst*

Yes, hi, good morning; two questions. I wonder if we could just touch on the Asia Pacific market a little bit more. We obviously saw quite a positive move in RASK and I'm wondering if that's a turning point in those markets or whether the improvement won't last into next year?

And then, just on the short-haul Europe, I'm wondering if we can just touch on the BA short-haul, if there's anything you can tell us in terms of how you're managing costs, what's happening on the pricing for BA's operations in that marketplace.

On BA short-haul it's continuing to make the changes that they need to make, so densification of the aircraft, addressing the core structures within BA, improving the operational performance. So they've got a long list of initiatives. They're working through those initiatives and they're making steady progress and there is still more opportunity there. So BA is clear in terms of what it needs to do and we're very clear with BA in terms of what will happen if it doesn't make the progress that it needs to make, but at this point it's well on track to achieve the financial performance that we have agreed with them in terms of their short-haul. And on Asia Pac?

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

Yes, on Asia Pac well we don't have any reason to understand that the positive trends that we have been going through are going to change. So where we had a positive improvement and contributions were basically places as Singapore, Bangkok has improved significantly; also improved performance in Beijing. So yes, even Chengdu, even our new route in Chengdu has experienced better performance through the last quarter. Again to mention Tokyo, which has been also -- yes.

Mark Simpson - *Goodbody - Analyst*

Are you saying that improvement is being driven in part by outward bound from those markets?

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

I think both. I think London originated market has also been powerful. The combination of fleet that we are operating has also helped a lot, I guess, so new fleet A380, 787s, the combination of these new fleets has been very well received by our customer base.

Mark Simpson - *Goodbody - Analyst*

And going forward, the delta changes to the network will improve as they reduce their presence in Asia into London?

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

(multiple speakers).

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

Yes, it should continue to be positive for us.

Mark Simpson - *Goodbody - Analyst*

Yes, great, okay, thank you.

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

I think we've probably come to an end, I don't know if there are any more questions, but I've been given the time and we need to draw to a close. Can I just finish by saying I think it's a very good performance in the quarter, clearly we're very, very pleased with the performance of Iberia and goods received, that the difficult restructuring is paying off there. There is more work to do there, but we're making excellent progress and we look forward to talking to all of you next week at Capital Markets Day and hopefully you'll have a lot more questions to ask us then.

But thank you for joining the call and look forward to talking to you next week.

Operator

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