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IAG.L - Q3 2015 International Consolidated Airlines Group SA Earnings Call

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PRESENTATION

Operator

Good day and welcome to the Q3 2015 earnings presentation. Today's conference is being recorded. At this time I would like to turn the conference over to Willie Walsh, Group Chief Executive Officer. Please go ahead sir.

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

Thank you and good morning. Thank you for joining us on our third -quarter results call. As usual, Enrique Dupuy has a presentation that he will take you through and then we'll give you an opportunity ask some questions. Enrique, over to you.

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

Thanks Willie. Good morning ladies and gentlemen. So Q3 results represent a strong set of figures for this central quarter of the year. We've been able to achieve an operating profit of EUR1.25b, which is EUR350m better than the figure that we reported last year. It includes EUR45m of positive operating profit coming from Aer Lingus since August 18 until the end of the quarter.

The basis of these improvements in our results have to do, on one side, with a significantly better performance on unit revenues compared with the one that we presented to you by the end of July on Q2. Unit revenues have been falling at constant currency terms and on a like-for-like basis, so excluding Aer Lingus, falling by 3.3%. And this, combined with a strong performance on the cost side in the respect ex-fuel unit cost reduction improvement, then has been 3.5%, again on a like-for-like basis and excluding the currency impact.

So currency impact has been relevant, both on the revenues side and on the cost side. Of course it has to do with the strength of the dollar and the strength of the sterling, which are the two very significant currencies in our operations.

So in terms of total unit revenues the reported figure in terms of improvement against last year has been 4.8% and in total unit cost it has been just 1%. And this again shows the significant contribution of savings in constant currency terms on our fuel bill. So unit fuel cost in constant dollar terms have been falling by nearly 20%.

The results have been achieved under the frame of a capacity increase of 5.3% pre Aer Lingus integration -- including Aer Lingus it has been a quasi-10% -- with an RPK demand growth, of 12.1%.

So if we go to the next page, page number 3, we'll be showing how the EUR350m figure of operating profit improvement has been made from. So, as I mentioned, there is EUR45m of contribution, operating profit contribution, coming from Aer Lingus. And there is a significant positive net impact of foreign exchange -- again, it's dollar plus sterling strength -- of EUR76m. So the core improvement is around EUR229m, which is basically sitting upon passenger revenue improvements. The combination of volume and price will be making nearly up to EUR100m of improvement. We are going to be focusing on the qualities of this revenue improvement in unit revenue terms in following slides.

Of course mention also fuel cost savings. Price effect, as I mentioned before, of fuel cost savings is very significant. It's in the range of EUR335m. Also very relevant improvements that we've been able to achieve on a sustained basis on ex-fuel costs, and they have to do with the three basic lines of costs, employee costs, supplier costs and ownership costs, and this is also an area where I'm going to be expanding in the following slides.

So if jump to page number 4 -- 5, sorry, we get a more concrete explanation of how our ex-fuel unit costs have been improvement for this quarter. Taking away a small Aer Lingus impact in terms of contribution and ForEx increase in our unit costs base -- and this is again dollar and sterling related, which is 8.7 percentage points, nearly 9% of currency impact -- the underlying net move in our unit non-fuel costs is minus 3.5%.

And this has to do with our unit employee costs. We see again Iberia showing very significant, I would say, [green] (corrected by company after the call) bars on the chart, improvements, again in terms of productivity and cost per employee. We see British Airways with a minor increase, which is temporary and has to do basically with training costs that are attached to introduction of new fleets, in this case basically the 787-9 fleet. And the performance in Vueling, that's even still been negative is better than better quarters. We are already rolling gradually on top of the big one-off increases in Vueling in salaries because of a last year new bargaining contract.

If we get into the supplier cost arena, we see also significant improvements across the board. Handling and catering have been benefiting from new negotiations with suppliers on a Group basis. As we've been repeating, we have now a unit-wide procurement team which is revising and negotiating most of our supplier contracts. In this case handling and catering contracts have been the beneficiaries.

More or less a similar landing fee structure, with slight inflation in terms of price and mix. Engineering improvements, which have to do also with negotiations with engine manufacturers and other suppliers, bringing some significant savings and probably there will be more to come in this area. Together with selling and IT costs, which also are showing improvements in GDS costs. Also outsourcing of IT contracts and other initiatives that are fructifying through these quarters.

Again on the ownership side of the costs, we have been able to achieve improvements on the depreciation side. This is coming from impairments and grounding of old fleet that we did through the last quarters and that have reduced the base of our depreciable assets. Together with a constant unit lease cost for the Group and this especially significant because, as you well know, we are in the middle of renewal and introduction of new generation aircraft in our fleet base.

So coming then to slide 6, we're showing here on a graph that I think you're familiar with already how we would be seeing the reduction on our unit fuel costs because of our hedging unwinding and the reference market prices that we're considering today as spot market prices.

So, as a matter of an example, we would be saying that either fuel prices would be remaining for the next quarter where they are today, our reduction of unit fuel cost in terms of dollar base would be in the range of 22% and, taking into account strengthening of the dollar, in euro terms it would be around 13.3%. So the chart will be showing something that we are going to be seeing into the next quarters and through year 2016, which is a significant reduction on our unit fuel cost base that will be coming.

If we then move to page number 8, we're here showing, again on a graph that you well know, the evolution of our capacity growth and the allocation of the capacity growth that we're foreseeing on the three companies. We have also a first reference to Aer Lingus.

So what we show here is the Group growth in terms of ASKs was 5.3% in Q3 against last year's Q3. And it will be coming down, it will be coming down in Q4 to a rate of 4.1%. This has to do basically with capacity adjustments that we have been foreseeing in some markets, as we have been quite vocal about that through the last, I would say, weeks and months. So the 4.1% will represent for British Airways, for example, an increase of just 1.2%, combined with greater capacity increases in both Iberia and Vueling, which are more on the range of 10% to 12%. And that will be making for a full-year capacity increase of 5%, out of which British Airways will be growing around 2%, Iberia 10% and Vueling 14%.

We will be seeing for year 2016 similar growth pattern as we have seen in year 2015.

Coming then to how we're implementing these growth patterns in the different airlines, so page 9, you're also probably familiar with this slide and it shows the nature of the growth changes. So basically for this quarter the nature of the growth is very much related to restoring routes that we were operating, in the case of Iberia, and some new routes that have been opened.

So worth to mention in the case of Iberia, restoring well-known routes as Havana or Gatwick, and opening new routes as Cali and Medellin. In the case of British Airways, the main driver is Kuala Lumpur which is a route that will be maturing through the following quarters. In the case of Aer Lingus, it would be Washington and here are some additional routes to be coming through year 2016; we'll be talking about them soon. In the case of Vueling, it's reinforcing their presence and growing their network out of Barcelona, Sevilla and Rome.

So maybe coming then to page number 11, and here is where we're going to be expanding a little bit on unit revenue recent trends and how we see a little bit of the future. As you remember, we are showing these two circles, on the left hand side capacity growth, on the right hand side unit revenue performance.

So worth to note that North America been adjusting capacity by 1.7%, unit revenues being stabilized now with a small decrease of 1.8%. As you well know, this is a market where we have a significant presence and we are comfortable with the level of stabilization that it's getting after a period of volatile movement through Q2 that we commented by the end of July.

On the short-haul, short-haul important capacity increases and we're satisfied with the response in terms of unit revenues. There are decreases. The decreases that we're achieving both in domestic and Europe are modest. And you have to bear in mind that the capacity increase, it's been implemented in a very efficient way. So remember for Iberia and Vueling we're using low-cost tools, very efficient, both Iberia Express and Vueling. In the case of British Airways, it's basically been done through the densification of our short-haul fleet so it will be driving down our short-haul unit cost in a significant way.

So I think we're satisfied with North America performance, but also with short-haul, both domestic and Europe.

In the case of Asia Pacific, significant growth, of course having to do very much of it with Kuala Lumpur, reduction in unit revenues, but also very much related to the maturing of this new route, which is a long one, and then because of the length of it, it has a lower unit revenue than average. There are other routes in which performance has been strong. We will be mentioning Japan routes, maybe also Shanghai and Hong Kong. So as a global approach to Asia Pacific we're also, I would say, satisfied with its performance.

Africa, Middle East and South-Asia, it's still suffering because of basically impact of oil weakness in oil routes and oil corporates, and that's something that's happening even through reduction of capacity that we're implementing. We are changing the size of their aircraft that we are using in India and this is, again, improving unit revenues, focusing on direct traffic and introducing new generation 787s to that market and that's proving to be very successful.

Finally, Latin America. Latin America, as you well know, has some dark spots. Basically they refer to Brazil, also Venezuela. But there are also some other bright spots that have to do with Central America, Mexico, and in this last quarter by the way, Argentina. So it's a blend of different countries. We are concerned with Brazil. We are cutting capacity there. We will be cutting capacity there. But the rest of the countries show also some bright interesting spots into the future.

Getting then to page 12 very briefly, nothing very much to add here in terms of what we have already said. So long-haul performance, as we said, slightly negative, but I would say, as we were planning. Short-haul it's also in terms of unit revenues negative in terms of Iberia, British Airways. Interestingly enough, Vueling performance in the short- and medium-haul, which is their basic network, as you know, has been positive, achieving unit revenue increases for the summer quarter which is encouraging.

The non-passenger weakness has to do with something that we've been referring to you in these last months and quarters, which is the cargo weakness that we are experiencing. So cargo weakness has been there through Q3. We have a certain sense that maybe it is bottoming. It's still I would say early to say and we'll track and monitor this market closely toward the year end.

So page 13 shows, as we've been referring in the past also, the performance of the three main companies. We'll tell more about Aer Lingus in our capital markets day, in their local currency. So British Airways is expressed in sterling, Iberia euros, Vueling euros. The figures are not adjusted by currency movements so it's basically as they are shown.

So starting with British Airways, a strong performance, as you see, in terms of operating margin, both absolute terms and also unit terms, an increase of 3.8 percentage points in the operating profit margin, reaching 19% on a lease-adjusted basis. So we are satisfied on this, I would say, summer performance of British Airways, which is based on a strong performance in terms of CASK. It's a 2.9% improvement on ex-fuel basis and on an aggregated basis it's minus 8.6%, which is a very strong performance and that clearly more than offsets the reduction in RASK in sterling terms.

For Iberia, the performance has also been better than last year, so it's nearly 1 percentage point of improvement, getting to 16% on a lease-adjusted basis. Operating profit margin, it's been done on a capacity increase of 11% so it shows the way Iberia has been able to grow nearly 11% and at the same time create value through operating profit improvement.

The RASK of course in euro terms is positive and this is showing the very positive impact of the euro on the revenue side. The CASK is showing slightly negative ex-fuel and total CASK, but again you have to understand this is due to the strong impact of the dollar in some of the basic cost lines of the company. So stripping off the strength of the dollar impact, CASK and CASK ex-fuel will be clearly on negative terms on a unit basis in respect of last year. And the basic demonstrator of this positive performance is the last figure we are showing for Iberia, employee cost per ASK coming down by 7.6% on a year-to-year basis.

So, for Vueling. For Vueling also positive performance, a lease-adjusted margin 25%. Of course you know they are a very seasonal performer, Vueling, very much related to summer season and leisure traffic. But 25% is a very, very strong margin figure, at the top of the range of the sector, and it's been done again on a growth pattern of nearly 14%. Again to mention, as I said before, RASK for Vueling has been 2.5% up on last year's figure. And there's no dollar influence, positive influence here, it's just, I would say, the underlying base unit revenue performance. So good figures again for Vueling.

And as you're going to see in the next chart, page 14, Vueling is still the top performer in terms of a ROIC figure for the last four quarters. So it's 13.6%, clearly about the target lower limit that we have set for our companies which, as you know, is 12%. The rest of the companies show improvements against last year's figures, both in an operating margin trend and also in the ROIC level. So for British Airways it's now very, very close to the 12% target, 11.4%. For Iberia there's still some more improvements to come, it's 7.5%. And for the Group it's nearly 11%, so showing an operating margin trend improvement of 3.2 percentage points against last year, which is a very interesting achievement.

So a very quick snapshot of our balance sheet summary composition and our basic leverage figures. What we're seeing on the September figures is significant cash improvement again for the Group, EUR1.7b. Part of it is due to the integration of Aer Lingus of course. Our balance sheet net debt, which has been coming down even after the integration of Aer Lingus' balance sheet. And adjusted gearing and adjusted net debt to EBITDAR showing in both cases improvements against December 2014. And again, sorry to repeat the issue and the case, it's after the integration of Aer Lingus, a company for which we have paid EUR1.4b.

So very strong, I would say, and solid financial position for the Group.

Finally, just repeat the guidance that we've been publishing for the full year 2015 accounts. The trading outlook that we are foreseeing for the full year will allow us to mention a bracket of operating profit figures between EUR2.25b and EUR2.3b. Remember our previous message was a EUR2.2b-plus operating profit for the full year.

And again remind you about the dividend statement that we published yesterday for the full year. It's very much consistent with what we said in our previous statements. For the full year we expect to pay out 25% of our underlying profit after tax in dividends and plan to announce a proposal for a final dividend for year 2015 just after the closing of the full-year results. And it will be included in a proposal that will be submitted to the shareholders' assembly in the month of June. You know the first interim tranche of our year 2015 dividend will be EUR0.10 per share.

So basically that's my presentation and we're happy to hear from you your questions and comments.

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

Okay. Thank you Enrique. I'll hand back to the operator to manage the questions session now. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Neil Glynn, Credit Suisse.

Neil Glynn - *Credit Suisse - Analyst*

Good morning. Three questions from me please. The first one on price control, I'm just interested in how your experience with yield management in the current fuel price environment shapes your approach to 2016, as I would guess summer pricing declines have been slightly greater than you might have at first anticipated.

The second question, with respect to the transatlantic, revenues seem to be down about 3.5% at constant currency in the quarter, putting together your capacity reduction as well as the pricing decline, which obviously frames that markets development, for you at least, in quite poor fashion. But how do you think about growth returning and what is really going on there from your perspective?

And then the third question. You mentioned Iberia is cutting capacity in Brazil, but with Iberia's leaner cost base and the reinvigorated brand, does the market's challenges actually provide an attractive window to accelerate market share gains that have been lost? Thank you.

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

Okay. Thank you for those questions. No, the summer actually pricing was fine.

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

Pretty much aligned with our expectations.

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

Yes. We saw, Q3 was very much in line with what we had expected when we produced our financial plan in November/December of last year. I think, as we stated before, Q2 was the bit that surprised us, but Q3 is fine and we expect Q4 to be in line with our expectations.

Transatlantic, I still think the transatlantic is great, to be honest with you. There was a bit of heavy capacity in the second half of the second quarter through Q3. We see it in Q4 and Q1. And that's down to realigning the Virgin network, which was anticipated. But in the main we're comfortable with that and that will flow through, as I said, probably into the early part of the second quarter of next year. But looking beyond that we see very little additional capacity coming on the transatlantic to impact on our markets. So we see the transatlantic performance actually to be quite a good environment for us and we expect that to be the case in 2016.

And with relating to Iberia, we're not in the business of artificial market share gains. We've been very clear that we will only put capacity into markets where we believe that that capacity growth is profitable and sustainable. We believe that there is more capacity to come out of Latin-America from some of our competitors who quite foolishly -- I said this at the time -- put capacity in when we withdrew. The capacity they placed in that market was loss-making because we know what our cost base and we know their cost base was higher than ours, and definitely not sustainable.

So we're very clear with Iberia that the game they're in is one of sustainable growth, sustainable profitable growth. And we're in it for the long term so these short-term movements we think are artificial and we discourage that activity within the Group. So we'll continue to act in a disciplined manner, pursuing growth opportunities where we believe that that growth will be profitable and sustainable for us.

Operator

Oliver Sleath, Barclays.

Oliver Sleath - *Barclays - Analyst*

Yes, good morning everybody. Thank you. Three questions as well please. Firstly, just to pick up on the Virgin realignment that you mentioned Willie. I know, obviously earlier in the year Virgin dropped some of their Asia routes, so moving on to the Atlantic, and now running into the winter we've lost Little Red as well under the domestic. So I just wondered if you're seeing any benefit on those routes or are some of them just a bit offset by some patchy demand in some of the markets.

A second question just on unit costs. The performance there obviously continues to be really strong. I think in the first nine months you're averaging about minus 4% or so on ex-fuel CASK and that's probably better than many of us has expected at the start of the year. Are you being surprised by the amount of costs you're able to take out, and therefore for the future we should expect no change to trends, or is there a sense of timing here and it means that the phasing in the future might be a little bit lower, i.e. a bit more front-end-loaded on savings?

And then the third question is just on demand and your thoughts on the general demand environment. It feels like we've got a very strong intra-Europe leisure consumer and then somewhat more patchy in long haul. I know we don't have a crystal ball, but does it feel to you more like the European consumer is particularly outperforming at the moment or the global markets are under-delivering? And in your financial planning what assumptions are you making about the economy going forward? Thank you.

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

Okay. Thank you. Yes, we definitely saw some benefit from the Virgin network realignment. Enrique mentioned Japan being strong for us now and where Virgin have withdrawn it definitely has helped. In other cases where they're realigned it reflects weakness in the market. So, for example, Little Red, the disappearance of Little Red. Aberdeen was weak. They weren't operating there but Scotland has been weak and as a result of that we haven't really noticed any particular difference there.

And, as we've highlighted previously, the issues that we see impacting on demand globally are most obvious in oil-related markets. So we've highlighted Houston in the US, Nigeria, Lagos and Abuja, Rwanda in Africa, and then of course Aberdeen in Scotland. And that trend has continued, but as we've expected to see.

I think on unit costs, yes, we're pleased. We're not surprised; we're pleased. There is more to come. I think an area of focus that we've mentioned to some of you will continue to be in supplier costs. We've a major IT transformation program going on that will deliver significant savings which will come through the business in 2016 and 2017. So there is more to be delivered and we'll give you some guidance in relation to that at capital markets day next week, but we're clear that there is a lot more that we can do. The major restructuring at Iberia is work-in-progress, and I think it's important to point that out, that Iberia is still going through that restructuring, implementing the plans that they have and there is more that they can and more that they will do.

And the demand, yes, the demand in Europe was strong, particularly in the third quarter. And I think what we experienced in all of the airlines in the Group, and I would include Aer Lingus in the, since the August 18 but certainly the commentary that Stephen has given us before that, suggests that the peak summer third quarter demand around Europe was very buoyant, probably stronger than we had expected. We were, as you know, disappointed with US consumer behavior in the second quarter. I think third quarter behavior is more in line with what we'd expected.

And we're looking at an environment in 2016, which we'll talk about in much greater detail next year, which supports, as Enrique said there, capacity plans that are similar to what we've had in 2015. And just to remind you, when we announced these headline capacity growths, so we said going into 2015 our capacity would grow at 5.5% and you can see now we're talking about 5%. So we will always look to make tactical adjustments to the capacity as we go through the year and you should expect a similar pattern to continue in 2016.

But the general environment, as I said, is very strong. The performance on the network, you know we focus a lot on the currency-adjusted RASK, but the actual RASK has been very strong and the performance under transatlantic in particular was very strong with RASK of over -- it was about 12% I think. So currency definitely is having a big impact on our results this year and is probably more volatile than we had expected. We would expect that to wash through into 2016.

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

Yes, a subject, an issue that you need to consider when you were mentioning our short-haul performance has to do with where we are positioned in Europe. So remember our basic hubs and operational centers are Madrid, Barcelona, growth of 3.5% maybe through the summer. UK, Heathrow area growth of somewhere in the range of 2% or 2.5%, doubling. So our positioning in terms of long-haul operations and point of sales in Europe is probably stronger than the average.

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

Okay. Thank you.

Oliver Sleath - *Barclays - Analyst*

Thanks. That's very helpful, thank you.

Operator

Mark Fortescue, Jefferies.

Mark Fortescue - *Jefferies - Analyst*

Morning. My questions have been answered actually. Thank you.

Operator

Alexia Dogani, Goldman Sachs.

Alexia Dogani - *Goldman Sachs - Analyst*

Hi. Good morning. I just had two questions please. Just firstly, on the Iberia margin performance, can you talk a little bit why the rate of improvement on the margin has slowed from the second quarter even though capacity growth was very similar? Can you just talk us through what happened exactly there and if it's a comparative, a yearly comparative issue?

And then just secondly, I think when you start to look at 2015 obviously you've just said that your unit fuel costs will be down 24%. Then we are starting to lap the big drop in the oil price, the big moves in currency. And so when you look at those parameters do you expect that unit revenues should be -- will continue to be impacted by that drop in the fuel price or is it more driven by underlying demand?

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

Okay. Thank you. On Iberia, as I said, what you have to remember about Iberia is it is going through a process of restructuring, and we are giving them flexibility to adjust their network and try different things. I think during 2015 our view is, and this is the view that the Iberia team gives, is they put probably too much additional capacity on the short-haul and you'll see that being rebalanced next year.

So the view that we've taken is they've got a very effective cost base. We are giving them scope to try some different things, reestablish their position in certain markets. As I said, the guideline is that they should only pursue growth where that growth is sustainable and profitable and, if it isn't, reverse out of it. And that's another feature of Iberia is the flexibility that they will have going forward, which is clearly much greater than they've had historically. And that will enable them to adjust to market conditions and demand.

Enrique?

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

Yes, and there is a temporal type of impact that you will see in page 13 through the figures, which has to do with a slower pace of unwinding of the hedges in Iberia, which makes that their fuel cost advantage in Q3 -- has been and will be temporary -- has been not as significant as for the case of Vueling and British Airways. That's probably something that's going to be improving gradually through Q3 and into year 2016.

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

And looking at 2016, the oil price environment is exactly as you said. I think we've probably more to benefit from the unwinding of our hedges than some of our competitors. But we take the general view that RASK will decline in 2016 and that's our planning assumption. So we are comfortable in an environment where we'll see some RASK decline because we are comfortable that we can continue to adjust our ex-fuel unit costs. But we'll give you greater visibility on this next week at the capital markets day. But in general we are looking at an environment in 2016 from a profitability point of view that will be significantly better than 2015.

Alexia Dogani - *Goldman Sachs - Analyst*

Great. Thank you very much.

Operator

Andrew Lobbenberg, HSBC

Andrew Lobbenberg - *HSBC - Analyst*

Morning guys. Couple on slots please. How have we integrated the Little Red returning slots and how happy are you with their deployment?

And is there anyone -- we've heard some noise out of Michael, but do you expect anyone to grab the Gatwick slots from the context of the competition policy remedies for Aer Lingus?

And then just on the North Atlantic, you talk with some confidence for 2016, but north of the US there looks to be a right old bun fight heading on the Canada/Europe market. Is that of any concern? I appreciate it's a great deal smaller than the US, but does that create any concern?

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

Thank you, Andrew. On the Little Red, yes, we've had -- the slots have reverted to us and, as you know, we are required to use them or lose them. So what we're doing is we've increased some domestic capacity but we are looking at tactical cancellations across the network to operate within the 80/20 rule so as to minimize the overall increase in capacity. And in fact we should be able to through the fourth quarter maintain it flat versus what we had planned to do.

Going into 2016, obviously we have nine additional daily slots that we need to utilize. We'll apply the same sort of criteria next year, but it will slightly increase the BA short-haul capacity beyond what we had. But it's not additional capacity in the market because it's just replacing capacity that was there operating out of Heathrow anyway, as you know.

And, yes, we do expect somebody to take up the Gatwick slots. We believe there has been interest expressed by a number of operators. So our assumption has been that somebody will be successful in acquiring those.

And, yes, you're right Canada has seen some significant increases with WestJet and Rouge. It is a much smaller part of our network. We are comfortable with the capacity that we have there. And again we have the advantage of being able to adjust capacity using gauge, where we see some -- if its oversupply in terms of capacity. But our network is pretty robust there and we don't expect to see any major impact to our performance on Canada, but it is an area that we are looking at and it will be interesting to see how that plays out during 2016. But its overall effect on us I would say at best is going to be marginal.

Andrew Lobbenberg - *HSBC - Analyst*

Fair enough.

Operator

Andrew Light, Citi

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Andrew Light - *Citigroup - Analyst*

Hi. Good morning. Your premium traffic in September slowed quite considerably down to plus 1.9% I think against a run rate of almost 8.7% in the prior two months, and obviously a significant mix deterioration. Is that a sign of a slowing trend in premium and corporate traffic?

And as you grow capacity 5% next year, do you think the premium traffic can keep up with that rate? Thank you.

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

Thanks Andrew. I think you've got to remember that in September last year, so there is a base effect here we had the Air France strike and I think there was a bit of Lufthansa disruption as well. So we are still seeing premium demand grow. Surprisingly it is still growing on the short-haul, which I think is an indication of underlying strength in the markets that we operate in.

And the general environment for both a business, a leisure, premium leisure point of view, continues to be fine. So we are very comfortable with what we've seen through this year, which has actually been stronger than what we had expected. But, as was said, the September figure impacted by a base year effect because of the strikes in Air France last year, which would have benefited us.

Andrew Light - *Citigroup - Analyst*

So that mean a disproportionate impact on premium traffic as opposed to non-premium?

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

There was benefit last year in all three of the airlines as a result of the [termination] Air France. But, yes, we had probably a disproportionate benefit on the premium. There's some issues there that I won't disclose actually, maybe at a later stage, and that relates to our relationship with Air France, but we might be able to talk about that at a later point, but the general environment I would say its fine actually.

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

And October.

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

Yes, October looks fine. So we are not seeing any trends there that would cause us concern, in fact quite the opposite. I saw some comments yesterday about momentum in September. We thought third quarter actually was good and our results reflect that, and what we are seeing in the fourth quarter is fine. So I think some of our competitors may have been targeting an internal audience rather than an external audience when they made those comments yesterday.

But in general the trends that we are seeing in the third quarter were very much in line with what we'd expected to see, and fourth quarter is in line with what we expect. So that's given us the confidence to move into 2016 with the plans that we have, which we'll disclose to you next week.

Andrew Light - *Citigroup - Analyst*

Great. Thank you very much.

Operator

Damian Brewer, Royal Bank of Canada.

Damian Brewer - *RBC Capital Markets - Analyst*

Yes, good morning. A couple of questions from me. First of all, given the emphasis on it in the US network airlines last week, could you talk a little bit more about the completion factor and how much of the schedule was actually operated in Q3, not so much in terms of punctuality, but just schedule reliability?

And then the second question would be on the Atlantic JBA. Could you tell us about any changes or developments in that within Q3, and how the contribution from that has shaped in Q3 this year versus last? Thank you.

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

Okay. Completion factor, I don't have the exact figure in front of me, but from memory it was about 99.3%, 99.4%, which is in line with what we'd expect. And we did have some tactical cancellations which we highlight. We do that from -- well, we do it throughout the year where we see opportunity to take a bit of capacity out and that impacts on the completion factor. So a tactical cancellation in our completion factor figures shows as a cancelled flight rather than -- we don't adjust the schedule and then report it. So if you like, compared to what we would have planned in our mind to operate, completion factor would have been higher than that 99.3%.

And sorry, I missed the start of your second question, so can you repeat that for me please?

Damian Brewer - *RBC Capital Markets - Analyst*

Yes, could you just give us an update on whether there had been any changes with the Atlantic JBA with American and the IAG Airlines, and whether there's any change in the contribution from that towards the IAG Airlines?

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

There has not been any change in that the trends in terms of contribution continues as we've seen through the year. So the overall performance of the transatlantic, as I said, remains very strong. I think it's probably fair to say BA is performing stronger than the other airlines within the JBA on the transatlantic, which does have a slight impact on the transfer payment structures that we have. But the trending has been the same going through Q3 as we saw in Q2 and Q1, and we would expect that to be the same in Q4 as well.

And just to reinforce the view on the transatlantic, the Aer Lingus story on the transatlantic is a really positive story. Transatlantic underlying demand remains very strong and very healthy and you'll see some evidence of that next week when we get Stephen Kavanagh to give you a presentation on Aer Lingus. But obviously their performance has given us the confidence to support the launch of three new transatlantic routes from Dublin to Los Angeles, Dublin to Newark and Dublin to Hartford, Connecticut which will start in 2016 with Aer Lingus. And you'll see some information, as I said, next week that will give you a better understanding of our view of the transatlantic. Thank you.

Damian Brewer - *RBC Capital Markets - Analyst*

Okay. Thank you. Can I ask one cheeky follow on then? It looks like Virgin are pulling out their 747s out of Heathrow from next February. And if my math is right, as you reconfigure some of your own 747 fleet, you're taking net seats out. At this early stage what does your Atlantic seat growth look like for next year? Is it up or could it even be flat or down?

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

Well, we think the general market, looking at everything we see at the moment, is that the transatlantic capacity is going to be flat, possibly slightly down next year, but it's probably going to be flat. And as you know we are adding premium capacity with the High J, or Super High J configuration as we call it. That's already operating already to New York, so we'll be taking some non-premium capacity out. We do have one new British Airways transatlantic route to San Jose. So the like-for-like capacity I think will be flat or down, but the San Jose obviously is new capacity.

Damian Brewer - *RBC Capital Markets - Analyst*

Okay. Thank you very much.

Operator

Edward Stanford, Lazarus.

Edward Stanford - *Lazarus Partnership - Analyst*

Good morning everyone. Two questions. Just perhaps if I might pick up on what Willie said about competitors talking about severe pricing weakness emerging in the current situation, could you just confirm your view that that's not something that you're seeing in your markets?

And secondly, just looking at the quite, still quite strong capacity growth in Latin America, how should we think about that going forward into the winter season, particularly given the constant currency RASK is still, while it's getting better, it's still weakening? Thank you.

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

In relation to what we say and what our competitors say, I think we're probably much more realistic in terms of outlook. So as we talked about going into 2015 we always said that we saw 2015 being a year of unit revenue decline, and I've said the same for 2016. I think maybe some of our competitors felt that they might -- maybe they were over optimistic in terms of what they would achieve.

So what I'm saying is that what we are seeing in the third quarter and -- what we saw in the third quarter and what we are seeing in the fourth quarter is very much in line with what we had expected to see in Q3 and Q4 when we produced our financial plan for the year, which was in November/December of last year. I don't know what they did, but I think their outlook is definitely more pessimistic than us. And I apologize for being boring and delivering on what we said we would deliver rather than surprising you, but we are going to try and continue to be as accurate as possible in giving you guidance as we go through the year and looking forward into next year.

And Latin America, yes, I anticipate there will be more capacity adjustments to come through, not just maybe some additional changes that we'll make but some additional changes that our competitors will make. BA is adjusting capacity, reducing the number of flights into Sao Paulo. We are doing the same with Iberia. I would expect pretty much everybody operating between Brazil and Europe to do the same, and we probably haven't seen the full scale of the capacity adjustments that are likely to take place in that market.

But, as Enrique said, while Brazil is a dark spot, there are some bright spots in the Latam region as well and overall we remain very comfortable with the capacity that we would have. But if we can adjust further then we will. And that's the approach we've always taken, to look where possible at capacity adjustments as we go through.

And again coming back to Iberia, Iberia has that flexibility now to move quickly. And it's something that's really encouraged us is the speed at which Iberia will respond to market conditions, switching capacity from one market to the other in a way that maybe they haven't done as well historically. So again we are comfortable with the capacity that we have and comfortable with the planned capacity that we have for 2016.

Edward Stanford - *Lazarus Partnership - Analyst*

Thank you very much.

Operator

James Hollins, Nomura.

James Hollins - *Nomura - Analyst*

Hi. Two from me please. The first one is if I look at slide 13 the Iberia staff cost performance clearly puts them at the top of the table at IAG right now. Clearly you've highlighted some one-off impact at BA, but would we and should we be expecting actually a fundamental cost program on staff costs at BA and Vueling into next year or is it just about incremental change coming at those?

And then secondly, on capacity, as we look at it now, clearly you guide to 5%. Is that as per (inaudible) by airline as well, so BA, Iberia, Vueling up 2%, 10% and 14%.

And related to that, is the BA up-gauge on the short-haul complete now or there still some way to go? Thank you.

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

The performance of Iberia is Premier League without question, Champion's League maybe, so they are really delivering on all of the promises they made.

I think the other two operating companies, and we'll talk about Aer Lingus again in the future, have scope for adjustment and they will do that. But I wouldn't call it fundamental; I think it's going to be just part of the day job and business as usual. So we do have some planned initiatives in terms of adjustments that will come through in 2016. I talked about the transformation of our IT. That will impact BA more than other parts of the Group. So you'll see the effect of that coming through in 2016 and 2017. And there will be other initiatives.

But the story in BA is very simple. We see opportunity to grow which will create some frontline recruitment. That is complex because of the number of aircraft fleets we have in BA, which drives training requirements as the yield capacity, the new aircraft come online. But frontline growth will be supported by continuing adjustment to the back office activities.

And Vueling is just digesting a deal with the pilots that we had talked about previously, and you should expect Vueling to get back to their normal trends as we go into 2016.

Operator

Jarrod Castle, UBS.

Jarrod Castle - *UBS - Analyst*

Thank you. Just a number of questions. You've mentioned obviously the Group capacity. You haven't said that much about Aer Lingus at this stage except obviously they'll be speaking next week, Friday, and the three new routes to launch from Dublin on long-haul. But can you give any idea in terms of are you happy with the way things are progressing so far?

And also if you can give an idea now or maybe it's something for Friday just in terms of capacity expectations for Aer Lingus next year.

And then just also looking at other revenues and maybe the loyalty program, in Q3 it looks like other revenues are flat. I'm not sure if the loyalty program goes into that line or in passenger revenues, but can you just talk about obviously the changes you've made to the loyalty program, how that's progressing, and then also what's going on in the other revenue line? Thanks.

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

Okay. Sorry, I should have said in relation to the last question as well, yes, the headline capacity of around 5% will be, the pattern with the individual operating companies will be similar in 2016 to 2015, but again we'll give you the details of that.

Aer Lingus adds about I think 8% ASKs to the Group. They are looking at additional transatlantic capacity. The three new routes that we announced would add about 17% on a full-year basis to our capacity. So they will be growing at a slightly faster pace than, certainly faster than BA and probably in line with Iberia, the trends that you've seen there. But again we'll give you more specific detail on that.

And in relation to the loyalty program, the loyalty program is split between the operating companies and other revenues. We will give a presentation on that next week. As we've said I think to most if not all of you, we will account for Avios separately from next year. So you'll have much greater visibility in relation to Avios through 2016 because, as you know, we've structured Avios as a standalone subsidiary within the Group. And we've decided now to account for that separately and give you visibility in relation to that, and you will start getting that as we go through 2016. But we'll talk a bit more about that next week.

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

Yes, the other revenue line is basically dampened down because of a reduction in cargo revenues. So other concepts of revenues, cargo handling and maintenance for Iberia, or the British Airways holiday programs, are performing efficiently and growing.

Jarrod Castle - *UBS - Analyst*

Okay. Thanks very much.

Operator

Anand Date, Deutsche Bank.

Anand Date - *Deutsche Bank - Analyst*

Hello. Good morning. I just had two questions too. The thing about cash flow, it looks like over the nine months I think, stripping out Aer Lingus, you're up about EUR900m. Could you just give us a number for the CapEx year to date as well?

And if we just roll forward the interim you announced yesterday, is it fair that's going to be about EUR400m outflow, so that's how we should be thinking about the cash progression, and then next year if you're saying there is going to be a significant step-up in profitability, that excess cash should probably grow quite significantly?

And then just on American and US Airlines, they moved to the joint reservation system in mid-October, which seems to have gone quite well. Have you seen anything from that or should we expect anything from that? Thank you.

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

Okay. Thanks for that. Yes, in relation to the -- we are just pulling out the CapEx figure here so you can hear all the papers being rustled. And just to remind you, we will update on CapEx for the plans going forward next Friday. The outflow in relation to the dividend is, yes, in or around what you've said there. As we said, it will be 25% of the underlying profit after tax and I think most of your modeling would be able to get you to a figure that would be close to that EUR400m.

Going forward, it's probably best to leave this one to next week because it will be part of the presentation that Enrique gives you as usual in terms of CapEx, and cashflow on the balance sheet. I'll ask you to wait until next Friday.

On AA US, yes, their move to single reservation went well. We haven't seen any impact of that. I think to be fair one of the things that we would comment on is that they were clearly quite rightly very focused on their integration and getting that done as quickly as possible. And therefore they prioritized those integration issues ahead maybe of some other aspects of the business that might benefit us more so.

We understand their reasons for doing that and we support their reasons for doing that because it clearly is better in the longer term. So we are comfortable with what it is they've done, but that integration to a single res platform didn't have any real impact as yet. And we're unclear as to whether it a major issue for us going forward, other than I think they'll now have the opportunity to focus on some other issues.

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

Yes, very briefly and before consulting with my detailed figures, as you see, since the beginning of the year the cash increase that we have been achieving is worth EUR1.8b. So approximately 50% of that has to do with cash being integrated from Aer Lingus and the other half has been cash internally generated by the Group through this first nine months.

And this is of course a result of the free cash flow being generated, so basically our gross margins minus the CapEx that we have been paying for the nine first months of the year. So it shows our ability to generate free cash flow even on years as we are going to be -- some years as we are going to be seeing where we are going through renewal, intense renewal of our fleet. And that has been one of the basis that management and Board has been taking into account to decide to launch our dividend policy and to start it with this first payment before the end of this year.

We will give you a full picture next week on our capital markets day, where you will see the evolution of this cash position through the years to come.

Anand Date - *Deutsche Bank - Analyst*

Okay. Thank you. Thank you.

Operator

Alexia Dogani, Goldman Sachs.

Alexia Dogani - *Goldman Sachs - Analyst*

Sorry, I had two quick follow up's. Just on the unit revenue outlook, having appreciated your comments on 2016 that it's still going to be negative, the US carriers have publicly said that they want to work towards flat unit revenues. Do you think this is something that you want to try to achieve or are you happy to be taking basically the margin of gross unit revenues versus gross unit cost in the context of the fuel cost reduction?

And then just secondly, would you be willing to make a comment on the GDS changes we are seeing in the market and whether you've seen any benefit from Lufthansa's addition of the charge on the GDS? Thanks

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

On the unit revenue, I noted what the US carriers were saying and I think a lot of their comments relates to the domestic market where their unit revenue, from memory, has declined significantly through this year.

In terms of what we're looking to do, we're looking to capture as much of the fuel benefits we possibly can, recognizing that there will be certain routes and certain markets where competition will not enable us to do that. So we are not setting out to, if you like, give away that benefit. We're trying to capture that benefit but we need to be realistic.

And it's therefore our assessment that having gone through a route-by-route analysis that the net effect of that will continue to be a unit revenue decline. That's what we anticipate for 2016. It's what we anticipated in 2015. It's not driving our approach to unit cost. We'd be doing that anyway. So even if we were seeing unit revenue increases we'd been looking to continue to improve our unit cost performance.

So our view is that there is scope for us to continue to improve the cost base of our business and that applies to all of the operating companies. And therefore we will pursue those cost initiatives in a very structured and disciplined way, and we'll do that in a strong revenue environment and we'll do that in a weak revenue environment.

On the Lufthansa changes to GDS fees, I would comment that we have not seen any material change. So we are not noticing any change in behavior. I'm not sure the degree of detail. I didn't get a chance to see all of the Lufthansa comments that they gave yesterday in relation to that.

I said publicly that I think it's been a good and a brave initiative by Lufthansa to do that, and most in the industry would want to see them succeed. But at this point, as I said, we have not noticed in any of our operating companies any trends that would suggest that there are people booking away from Lufthansa as a result of the changes that they've implemented. But I think you'd get a better sense of that by talking to Lufthansa directly in terms of the trends that they have noticed. But we are not seeing anything.

Alexia Dogani - *Goldman Sachs - Analyst*

Thank you.

Operator

Mark Simpson, Goodbody.

Mark Simpson - *Goodbody Stockbrokers - Analyst*

Yes, hi. I've got four questions. Sorry, I apologize for that. First off, I'm wondering if you can give us the out-run RASK. You gave that to us in the Q2 release in terms of by region. It's useful information and that would be good to have if you have that to hand.

Also thinking about regional changes, I wonder if you could tell us about BA looking into Q4. It's obviously only a 1.2% capacity growth being forecast, but can you give us a feel, any sense by region, how that's going to play out?

On two other things, fuel, I'd just note that the slide 6 this quarter and the same page number for last quarter, the guidance has changed for the Q4 2015. And what I mean by that is that the blended fuel price given last quarter for Q4 2015 was circa $670 per metric tonne. This time around it's just over $700 per metric tonne. Is that a reflection of bringing Aer Lingus into the mix and Aer Lingus' fuel price performance, there's scope for improvement, or I wonder if you could explain that differential?

And then finally, Willie, you said earlier Q4 yield in line with expectation at the group level. I'm wondering if you could tell us what expectation means.

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

I could tell you but I won't.

So the outturn, yes, we showed two charts last time round. We showed the happy chart which had lots of green on it with the outturn. It was so happy this time round that we thought we shouldn't show it to you because -- no, it's very good. I'll call it out so you can have it. North Atlantic was plus 12.2%, domestic plus 1.2%, Europe plus 2.7%, Asia Pac plus 7.5%, Africa Middle East plus 8.9% and Latin America plus 6.7%. That gives you plus 6.9% overall RASK improvement.

So it's very much what we had said last time round, that currency's have a big impact and when we look at it in constant currency terms you clearly get a very different picture to what you see when we look at it in outturn. And I think the actual performance is pretty good, but the currency movements that we've seen on both the revenue and the cost side have been significant this year. We don't at this stage see that having as significant an impact next year.

On BA, in fact Keith has just -- Keith is here so he's given me a quick note here so I'll give you the main headlines. Some capacity reduction in Newark. Capacity reduction on Sao Paulo as we've mentioned. Miami goes in -- changes to an A380. So they are the main changes there on the North and South Atlantic. And then we had two route cancellations, Entebbe and Almaty. And the rest of it then, it's pretty routine.

Yes, the fuel, it's Aer Lingus. As you said, they had some hedges which again will unwind so they'll see benefit from that in 2016. So their hedging unwinding will have a good impact for them. And Q4, as I said, in line with our expectations, but we don't give you what our expectations are. But you'll see that when we report, so when we report our Q4 figures I'll tell you that they were exactly in line with our expectations.

Mark Simpson - *Goodbody Stockbrokers - Analyst*

Fair enough. All right. Thanks for that.

Operator

As there are no further questions in the queue I would like to turn the call back to Mr. Walsh for any additional or closing remarks.

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

Well, thank you. Again I apologize. This Q3 call is always probably a frustrating one for you given that it's followed by our capital markets day and a lot of the issues that I'm sure you will be interested in them from the questions you've asked today will be addressed specifically in the presentation that we give you next Friday. So we look forward to seeing most if not all of you next Friday at capital markets day. Thank you very much.

Operator

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