

Air France is only halfway there



I Letter from the Director Air France-KLM

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Monday's Press Review

> Air France is only halfway there

(source Les Echos) August 28 - Once again, **Air France** has **demonstrated that it is never as quick to reform as in times of crisis**. In three months, Benjamin Smith managed to obtain 10.4 billion euros in loans in France and the Netherlands, and to have two voluntary departure plans validated - one for 368 pilot positions and the other for 1,700 flight attendant positions - as well as an unprecedented restructuring of the domestic network. He convinced Air France's unions to accept a 40% reduction in the regional Hop subsidiary, as well as the transfer of part of Air France's business at Orly to its low-cost subsidiary Transavia France. Ben Smith has also made good progress in fleet optimization, taking out all A380s and A340s at Air France, as well as Boeing 747s at KLM, while confirming the replacement of Air France's A319s by A220s as of 2021.

However, while Air France and KLM are protected from default thanks to government loans, the return to break-even in 2023, with a target margin of 7%, and a return of supply to pre-crisis levels in 2024, still seem very optimistic.

In terms of cost reduction, discussions have yet to be finalized for the voluntary departure plan for Air France ground staff, for 3,640 positions, as well as the 1,000 job cuts at Hop. In

the event of failure or an insufficient number of candidates for departure, layoffs would be imposed. Never before seen.

On the Dutch side, KLM's management has yet to accept some 3,500 job cuts, as well as wage cuts of 10% to 22%. In addition, while Air France has been very proactive in reopening 80% of its network in July (150 destinations), with the aim of increasing to 85% and 170 destinations in September, the **average load factor did not exceed 56% in July compared with the usual 90%**. And **the decline in revenue, which was greater than the decline in supply, was 67% on short-haul, 76% on medium-haul and 85% on long-haul** (for an 80% lower supply) (...).

And far from improving, **the level of bookings is expected to fall sharply in September and October, due to a sharp decline in business customers**. Nevertheless, the Group remains optimistic, with plans to recover to 65% of its capacity in the fourth quarter (compared to 55% for Lufthansa and 46% for IAG), 80% in 2021 and 100% in 2022. But a more pessimistic assumption, evoked internally, would be 60% in 2021 (...).

My comment: *From the very beginning of the crisis, the airlines indicated that they had two objectives:*

- . surviving the paralysis of air traffic,*
- . keeping their backs to the ground while waiting for a return to normal,*

Most had sufficient cash to last a few months without traffic (4 to 12 months). On the other hand, none could survive if the recovery did not come quickly.

When the extent of the crisis became known, the companies found themselves obliged to ask for the support of their shareholders and their supervisory states. Their requests were assessed on the basis of a reasonable recovery scenario.

This so-called reasonable scenario appears more and more to be an optimistic scenario. While it is difficult to affirm that the date of return to a pre-crisis level of activity will be 2023, 2024 or 2025, it appears certain that recovery will be slower than expected by 2022.

Will airlines need more restructuring, more financial support? The answer is largely up to the scientists. The development of a treatment, or even a vaccine, will depend on the airlines' ability to get by without further support.

> **WizzAir in Transavia: interest in Lelystad Airport (WizzAir and Transavia interested in Lelystad Airport)**

(source DFT translated with DeepL) August 29 - Amsterdam - **WizzAir and Transavia are still interested in flying from Lelystad Airport** (...).

On Friday, Schiphol CEO Dick Benschop said that "parts of the market" are still interested in the controversial polder airport, although air traffic is largely paralyzed due to the Covid-19 crisis. At Schiphol airport, half of the number of flight movements prior to the corona pandemic are recorded (...).

According to the CEO of Schiphol, there is still a shortage of landing slots, because current users of Schiphol have so-called historic rights. These are largely linked to the KLM group, Schiphol's largest customer. The cabinet is expected to make a decision before the elections, according to Benschop (...).

"There **will come a time when Schiphol will be saturated again**, so it's good that there is still extra capacity available, but that won't happen for a few years," says Van der Heijden. **At Lelystad Airport, a maximum of 68 flights per day can be handled, which is about as many as Schiphol can handle in one hour.**

The idea would be to transfer all vacation traffic from Schiphol Airport to Lelystad Airport, thus freeing up slots for connections with other economic centers in the world (...).

The Lower House passed a motion that the airport should only be used as an overflow for Schiphol and not for new users.

***My comment:** The Dutch government, supported by members of parliament, wants the slots available at Lelystad to be reserved for companies already operating at Schiphol.*

The European Commission opposes it in the name of free competition. It believes that the new slots must be distributed fairly between the companies operating at Schiphol and new companies.

Local residents, for their part, do not accept that the opening of Lelystad could allow an increase in traffic, which would lead to an increase in noise and environmental pollution.

The opening of Lelystad, a small airport near Amsterdam, has already been postponed several times. In the run-up to the March 2021 elections, it is likely that the political parties will refuse to take a stand.

> Virgin Atlantic's restructuring plan validated by its creditors

(source AFP) Aug. 29 - **Virgin Atlantic's restructuring plan has been approved by its creditors**, the British airline announced Tuesday, which has been hard hit by the air transport crisis linked to the pandemic of the new coronavirus (...).

The next step is a hearing in the High Court on September 2 to approve the restructuring plan, the company said, saying it was "confident that the plan represents the best possible outcome for Virgin Atlantic and all its creditors". A procedural hearing will follow on September 3 in the United States to ensure recognition of the restructuring plan in that country.

The company had reached an agreement in principle in July to raise 1.2 billion pounds of private funds to avoid bankruptcy.

Billionaire Richard Branson, founder of the company and majority shareholder with 51% of the capital, is to contribute 200 million pounds. The other shareholder, the American company Delta Airlines, which holds 49%, is also supposed to participate in the rescue.

During a hearing before a London court in August, **Virgin Atlantic's lawyer explained that the company could run out of money by the end of September if the recapitalization plan is not validated, given the collapse of air traffic (...).**

> American Airlines: 40,000 fewer employees in the space of 6 months?

(source Boursier com) 26 August - (...) In March, American companies received 25 billion dollars from the federal government to ensure the payment of salaries and to preserve jobs until the end of September, with the hope that demand will pick up in the meantime. While traffic has picked up somewhat, it is still far from returning to pre-crisis levels.

Including voluntary departures and unpaid leaves, American Airlines' workforce could drop to 100,000 in October from 140,000 before the crisis. "In short, American's crew will be at least 40,000 fewer employees on October 1 than when the outbreak began," Managing Director Doug Parker and President Robert Isom said in a memo to employees. "Today is the most difficult message we've had to share so far - the announcement of involuntary staff reductions effective October 1.

According to them, the **only way to avoid forced departures is to extend the plan to support salary funding.** "The only problem with the legislation is that when it was passed in March, it was assumed that by September 30, the virus would be under control and

demand for air travel would have returned... This is obviously not the case".

Based on current demand, the group expects for the fourth quarter less than 50% of its usual

flight supply, and only a quarter for international flights, the two executives said.

American Airlines, of course, is not the only carrier to ask for an extension of federal assistance, while several companies have also warned of massive job cuts. Delta Airlines plans to lay off 1,941 pilots unless it reaches a cost-cutting agreement with the unions, while United Airlines has warned that 36,000 employees could lose their jobs.

My comment: US airlines are in a worrisome situation.

The resumption of domestic traffic in the United States is slower than expected, due to a management of the epidemic that is risky to say the least: the United States is by far the country most affected by the coronavirus (more than 180,000 deaths) ahead of Brazil (120,000 deaths).

> **China: air transport limits losses thanks to the domestic market**

(source AFP) August 29 - **Chinese airlines reported lower overall losses in the second quarter than in the first**, thanks to the ongoing recovery in their huge domestic market, where Covid-19 has been virtually eradicated (...). The epidemic has slowed significantly in recent months on Chinese soil, with zero new deaths since mid-May. A situation that has allowed the gradual resumption of tourism and business travel.

China Southern Airlines, the country's largest airline in terms of passenger numbers, posted losses of 2.9 billion yuan (355 million euros) over the April-June period, compared with 5.3 billion yuan in January-March (...).

For its part, the emblematic flag carrier Air China reported losses of 9.4 billion yuan for the first half of the year -- slightly less in the second quarter (4.6 billion) than in the first quarter (4.8 billion) (...). China

Eastern Airlines, China's second-largest airline in terms of passengers, recorded greater losses in the April-June period (4.6 billion yuan) than in January-March (3.9 billion yuan).

This was mainly the result of a more aggressive pricing policy, which brought travelers back, but at the cost of lower margins. A dozen Chinese airlines have launched unlimited flight packages to boost business (...).

In the second week of August, air ticket bookings reached 98% of last year's levels in the same period, notes the tourism analysis firm ForwardKeys.

"This is the first time since the beginning of the Covid-19 outbreak that a significant segment of the aviation market anywhere in the world is returning to its pre-pandemic level," commented Olivier Ponti, Vice President of ForwardKeys.

***My comment:** Traffic is picking up in China, but with a low price level. We'll have to wait for the third quarter results to assess the quality of this recovery.*

> **Emirates** airline got \$2 billion injection from Dubai government

(source Reuters translated with DeepL) August 31 - **The Emirates airline company has received 7.3 billion dirhams (\$2 billion) from the Dubai government** as it faces a cash shortfall caused by the COVID-19 pandemic, according to a prospectus for a possible bond issue seen by Reuters (...).

No such injection has been publicly announced by the government or the airline (...). The Ministry of Finance declined to comment. The Dubai state media office and the airline did not respond immediately to Reuters' requests for comment.

In May, **Emirates** said it planned to raise funds to manage the impact of the pandemic. It **raised 4.4 billion dirhams (\$1.2 billion)** in the **first quarter**.

This month it asked cabin crew to take voluntary unpaid leave, and sources said a layoff process that began in July is continuing, with more staff being laid off this month.

***My comment:** European, Chinese, Indian or American airlines have a domestic market that could partially offset the decline in international activity.*

This is not the case for Gulf airlines (Emirates, Qatar Airways, Etihad Airlines). Already unprofitable or even loss-making before the crisis, they will need substantial aid to get out of it.

> **Ryanair** denounces the rescue of its Portuguese competitor TAP, the court in charge of the case.

(source Capital) August 27 - **Ryanair "has filed an appeal against the European Commission's decision" to authorize the Portuguese socialist government's plan,** a spokesman for the company told AFP.

After receiving the approval from Brussels, Lisbon announced last month an agreement to renationalize TAP, which, like the entire airline sector, has been hit hard by the health crisis. The Portuguese state will increase its stake from 50 to 72.5% after the purchase for 55 million euros of half the share of the private consortium Atlantic Gateway, which was controlled by the American businessman David Neeleman. **This rescue plan provides for aid of up to €1.2 billion. It will be accompanied by a restructuring of the airline, including a reduction in routes and the number of aircraft, in order to ensure its long-term viability (...).**

The European Commission also gave the green light last week to public aid of €290 million to support the airline Brussels Airlines, a subsidiary of the German Lufthansa group. But **for Ryanair, the pandemic must not lead to distortion of competition rules.**

"In a context of liberalization of the air market (...) a government cannot decide to support only the country's companies," explained Juliusz Komorek, Ryanair's legal director, to the Portuguese daily Publico. Ryanair also contests the government aid granted to other companies such as the Scandinavian company SAS, Air France and Lufthansa.

***My comment:** TAP Air Portugal was in trouble before the health crisis. Its medium-haul activity was strongly loss-making, its long-haul activity was concentrated on Brazil (one of the countries most exposed to Covid-19).*

The rescue plan accepted by the European Commission will lead the Portuguese airline to reduce its fleet. It is likely that this reduction will mainly affect the medium-haul fleet. If this is the case, Ryanair's complaint would be unfounded.

> Norwegian will not get through the winter without new financial support

(source Les Echos) August 28 - Norwegian will not get through the crisis without additional financial aid from Norway. This is the unambiguous warning issued by the CEO of the low-cost airline, Jacob Schram, on the occasion of the publication of bright red half-yearly results on Friday. "We are grateful for the loan guarantee provided by the Norwegian government. However, in the current market conditions, this will not be enough to get us through this prolonged crisis," he said at an online press conference.

Norwegian, which posted a loss of NOK 4.8 billion (EUR 455 million) in the first half of the year, still had nearly NOK 5 billion (EUR 480 million) in cash at the end of the half year. But according to its managers, the

company burns "between 300 and 400 million Norwegian kroner per month" (28 to 37 million euros). It **would have enough to continue its activity at least until the end of the year, but would not be able to last more than six months under current conditions, and thus reach the 2021 summer season without a new financial oxygen tank.**

In March, Norwegian was rescued from bankruptcy by an Oslo-guaranteed loan of 3 billion kroner (about 280 million euros), as well as by the conversion of part of its 4.3 billion dollar debt into new shares. At the same time, the company embarked on a drastic restructuring plan, which included refocusing on the medium-haul network, laying off 90% of its employees, selling its aircraft and canceling all outstanding orders with Boeing. The group had also closed its subsidiaries in Sweden and Denmark.

As a result, Norwegian was able to resume some of its flights in July, with 20 Boeing 737s instead of the previous 100. **However,** not everything went according to plan. **Sweden refused to guarantee an additional loan, judging the risk of default too high.**

Discussions with Boeing for the cancellation of an order for 92 B737 MAX and five B787s ended without agreement and the company had to initiate legal proceedings, these executives said. **Aircraft resales have not been as rapid and numerous as hoped.**

Above all, the resurgence of the coronavirus pandemic in Europe broke the recovery of traffic. "When Spain turned green, bookings flooded in overnight, but when Spain turned red, they collapsed," said the company boss. Hence the impossibility of making forecasts for Norwegian, which plans to "stay with 20 or 30 planes" all winter, waiting to see more clearly.

***My comment:** Norwegian was in great difficulty before the crisis. Its strong exposure to the Europe-US market limits its prospects for recovery.*

> Hungary's low-cost Wizz Air makes progress in the wake of the crisis

(source Les Echos) August 24 - Daring, a lot of opportunism and expense management to make a Harpagon proud: this seems to be the recipe for the anti-crisis remedy according to Wizz Air. While its main competitors, including Ryanair, are having to lower their hopes for recovery, **the Hungarian low-cost airline has already recovered 70% of its pre-crisis business** and plans to return to 80% this winter. Based

in Budapest, it has even inaugurated 200 new routes and nine new bases in Europe in the last four months, including the latest at London-Gatwick airport, home of EasyJet. **Wizz Air has redeployed part of its fleet to the most favorable destinations, while its employees have not been spared layoffs and salary cuts.**

Wizz Air seems to have left to be among the main winners of the crisis. In its latest analysis note, Citi Research ranks it at the top of its favorites in Europe, alongside Ryanair. According to its analysis, **the Hungarian airline**, which has already managed to become the leading airline in Central Europe, **is best placed to increase its market share, taking advantage of the decline of its competitors.** This is notably the case in London-Luton and London-Gatwick, where Wizz Air is significantly increasing its offer, while EasyJet's offer is declining. Taking advantage of the crisis to gain ground is also the ambition declared by **its founding Chairman, Jozsef Varadi.** At the presentation of the quarterly results at the end of July, he maintained the expansion plan, which calls for increasing the fleet from 121 Airbus A320 and A321 aircraft to 201 in 2024 and 275 in 2027. Wizz Air is thus one of the very few airlines to have not cancelled or postponed any orders.

The CEO **also confirmed the launch on October 1 of a particularly daring project: the opening of a base in Abu Dhabi.** A first for a European low-cost company! From the capital of the United Arab Emirates, Wizz Air plans to serve 11 cities in ten countries, including five in Central Europe, with Airbus A321s.

As with Ryanair, however, there is a flip side to the coin. If **Wizz Air has succeeded in generating traffic of 40 million passengers to destinations in Central Europe that are** little or not served by traditional airlines, it is **thanks to a cost management without any hesitation. With a holding company in Jersey and a boss living in Geneva, the Hungarian company is also one of the last in Europe without a union.**

This explains in part the speed with which **it was able to lay off a thousand out of 4,500 crew members in the spring, impose an average 14% pay cut** and relocate some 20 aircraft and their crews to new destinations. Wizz Air was also not exemplary in terms of reimbursing cancelled flights. And it is also usually the only one to charge for baggage in the cabin. All these characteristics are less likely to be the case in Western Europe.

My comment: According to the author of this article, who is generally well informed, Wizz Air would do worse than Ryanair socially.

> EASA Plans Test Flights on Boeing 737 MAX

(source: Le Journal de l'Aviation) August 28 - After Transport Canada, **EASA also reached an agreement with the FAA and Boeing to conduct test flights on the 737 MAX. The European agency deemed that the process of correcting the aircraft's defects was sufficiently advanced** for it to consider scheduling these flights, a prerequisite for the modified aircraft to be certified in Europe. They will begin on September 7.

However, due to the health crisis and restrictions on traffic between Europe and the U.S., the test flights will have to take place in Vancouver. Prior to that, as of September 1, simulator tests will be conducted in London (Gatwick). Then the Joint Operations Evaluation Board (JOEB) will meet in Gatwick during the week of September 14.

The re-certification process is still underway in the U.S., with test flights with FAA inspectors having taken place in early summer. **However, FAA requests to update the flight control and alerting software, revise certain pilot procedures and modify certain wiring, have again forced Boeing to extend its 737 MAX return-to-service target from the third quarter to the fourth quarter of 2020.**

This EASA announcement comes the week that Transport Canada conducted its own test flights with the aircraft, this time from Boeing's Seattle facility.

My comment: *Two years.*

It's been nearly two years since Boeing began modifying its 737 Max to compensate for the malfunctions it discovered. How much longer will it take to apply the fixes to the 800 aircraft already built?

> The great breakdown of business travel

(source Le Figaro) August 29 - From the very beginning of the Covid-19 epidemic in February, **most companies took "travel ban" measures, forbidding their employees to travel.** For health reasons, for financial reasons as well: cutting the travel budget is a major source of savings, before moving on to the stage of staff cuts. As the pandemic is persistent, **these travel bans are often extended until the end of the year. And the cutbacks could last even longer.** During containment, companies have discovered new and effective ways to operate remotely, both internally and with their customers. What was supposed to be only temporary is now shaping up to be a profound change in work

habits....

Reductions in travel spending are having a cascading effect on whole swathes of the economy. **They undermine airlines, cabs, hotels and restaurants.** Not to mention trade show organizers. As the world's leading tourist destination, France logically plays a big role in business tourism: **after the United States and Germany, France is the largest organizer of international congresses,** according to the International Congress and Convention Association (ICCA). Paris is even the leader in the ranking of cities, ahead of Lisbon. Business tourism accounts for more than 25% of France's tourism revenues, or more than 43 billion euros," says Caroline Leboucher, CEO of Atout France. Business travelers are the most expensive tourists. And they come all year round". This year, the shortfall is colossal: 15 billion between May and August, according to the French Union of Event Professions (Unimev). **The expected recovery in the fall will not take place.** Because of the quarantines imposed by Great Britain and Germany; because of the limit of 5000 participants in the rallies imposed by the authorities. **"Two of the main business tourism regions, Île-de-France and Paca, are classified in the red zone,"** adds Caroline Leboucher. It will take several years before they return to 2019 levels. Moody's analysts are talking about 2023, at best. "On a global scale, the resumption of business travel will take time, they warn. They will remain limited as companies protect the health and safety of their employees, try to cut costs, and rely on teleconferencing. »

At a standstill, thousands of companies are struggling to survive, clinging to encouraging signs (...). Above all, **the need for human contact has not disappeared. Experience shows that the chances of a transaction are higher in a face-to-face meeting than in front of a screen (...).**

***My comment:** The weak recovery in business travel is a source of concern for most traditional airlines, but also for some low-cost companies. For example, in France, EasyJet carries proportionally as many businessmen as Air France.*

Hotels are even more affected by the decline in business travel than airlines: 70% of their customers are professionals on the move.

End of the press review

> My comment on the evolution of the Air France-KLM

share price

The Air France-KLM share was at 3.787 euros at the close of Monday, August 31. It is down slightly by -0.42% over one week.

Before the coronavirus epidemic, the Air France-KLM share price was 9.93 euros.

The average (the consensus) of analysts for AF-KLM shares is 3.24 euros. The highest target price is 5 euros, the lowest is 1 euro. You can find on my blog the details of the analysts' consensus. I no longer take into account the opinions of analysts prior to the beginning of the health crisis.

The barrel of Brent oil (North Sea) is up \$1 to \$46. For the last two months, it has varied very little. At the beginning of the coronavirus epidemic, it was at \$69.

This indicative information in no way constitutes an incitement to sell or a solicitation to buy Air France-KLM shares.

You can react to this press review or provide me with any information or thoughts that will help me better carry out my duties as a director of the Air France-KLM group.

You can ask me, by return, any question related to the Air France-KLM group or to employee shareholding...

See you soon.

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| François Robardet

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