

Towards a worse-than-expected year-end for air transport

## I Letter from the Director Air France-KLM

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### *Monday's Press Review*

#### > Towards a worse-than-expected year-end for air transport

(source Le Journal de l'Aviation) September 29 - Presenting the air transport balance sheet for the month of August, the **IATA in turn confirmed the slowdown that hit the industry** when the number of Covid-19 cases resumed its rise. The airline association is now "less optimistic" **about traffic for the remainder of the year. It considers that in December it will no longer be down 55% compared to the same period in 2019 (forecast for July) but down 68%.** "Our long-term forecast is unchanged, our concerns are focused on the coming weeks and months," said Brian Pearce, IATA Chief Economist.

(...) As in recent months, the **signs of recovery are mainly in domestic markets**, with very wide variations between countries. **The Russian market**, stimulated in particular by strong tariff cuts, **has returned to its 2019 level and the Chinese market continues to grow**, while **the Australian market is stagnating at -90% and the United States and Japan remain weak (-70%).**

However, (...) "the improvement more or less stopped in September", regrets Brian Pearce. He notes that during the last six weeks - which corresponds to the resumption of the epidemic and the re-establishment

in scattered order of travel restrictions - there has been no improvement in the domestic sectors and that a decline had begun where international traffic had been able to take off again. At the same time, **while business confidence seems to have returned, consumer confidence remains at an all-time low**. Thus, bookings for the fourth quarter (...) are 76% to 81% lower in the fourth quarter compared to last year (instead of 66% to 73% in the third quarter). IATA recognizes that there is a growing phenomenon of last-minute bookings but is concerned about a survey it conducted among passengers, which indicates that half of them will not fly this year.

**Cargo activity continues to improve** (demand gained 1.8 points compared to August) **but remains severely hampered by the lack of capacity** caused by the immobilization of the passenger fleet (bunkers usually carry 50% of air freight). (...) On the other hand, **the sector risks losing market share** as the peak season begins in the coming weeks.

***My comment:** At the beginning of the health crisis, the airlines drew up action plans based on a gradual upturn in activity.*

*Most of them have benefited from financial support from their supervisory authorities, contributions of funds from their shareholders in the form of loans or capital increases. As this was not enough, they had to reduce their workforce, resort to short-time working or even modify the terms of their employees' remuneration.*

*The resurgence of the epidemic has thwarted these action plans. New support measures have been introduced, including the Long-Term Partial Duration Business (APLD) in France. This measure is currently being negotiated within Air France.*

*It is to be feared that this will not be enough to stem the decline in activity. New workforce reduction measures have been announced in the United States. Airline shareholders could be approached again.*

### **> Air France saw its revenues drop by 70% in August, says its CEO**

(source Reuters) September 30 - **Air France** suffered a 70% loss of revenue in August and filled only about 30% of its aircraft on intercontinental flights, said its CEO Anne Rigail in an interview with Corriere della Sera published Wednesday.

The airline, which belongs to the Franco-Dutch group Air France-KLM (PA:AIRF), **continues to burn about 10 million euros of cash per**

day "but is working to limit its losses," Anne Rigail added.

"In August, we flew at 70% of last year's capacity on domestic routes, at 55% on medium-haul (especially Italy, Greece, Spain and Portugal), while due to the various restrictions in the countries, the intercontinental segment did not exceed 30%. All this **with** lower load factors and a **70% decline in revenues**," Anne Rigail said in the interview.

"Before the summer, we expected a gradual recovery to reach 70% of business by December. But **in September, we noticed that tourist bookings had fallen and we did not see any recovery in business class traffic**.

Anne Rigail, who has formed a new transatlantic alliance with Delta Airlines and Virgin Atlantic, has also invited Alitalia, which is in the process of being renationalized, to join this new group.

"Alitalia is a long-standing partner and we are inviting them to join the joint venture as an associate member. I want to maintain a strong relationship with the company," says Anne Rigail, while ruling out any investment in Alitalia.

***My comment:** At the recent session of the Air France Central Social and Economic Committee, Anne Rigail presented the evolution of the company's economic situation to Air France's elected personnel representatives.*

*On this occasion, it made a point of specifying that recourse to the Long Term Partial Activity (LTA) will be necessary but not sufficient to compensate for the new losses.*

**> In the inevitable next round of support for KLM, it becomes really difficult (Avec l'inévitable prochain cycle de soutien à KLM, cela devient vraiment difficile).**

(source FD) October 2 - **A few hours before the deadline, KLM submitted the requested recovery plan to the Ministry of Finance on Thursday evening.** The pilots' union was the last of eight unions to accept a wage cut. If the proposal (...) is approved by Minister Hoekstra and the House of Representatives, KLM will receive 3.4 billion euros in state-guaranteed loans to survive.

However, the next hurdle already appears (...). KLM wants to get more money.

**A team of arithmeticians and lawyers has been working for several weeks at the airline's headquarters on the following mission: how much money KLM needs to get in order to increase its capital.** We

are working with three to five economic scenarios, ranging from a short and severe recession to a deep recession. This is partly a guess, because nobody knows how often the virus will paralyze the company. Initially, **May next year was set as the target date for a share issue not only for KLM, but for the whole of Air France-KLM.** With the second wave in full swing and a lockdown imminent, **it may well be necessary to do so earlier.** Once the calculations have been made, the question remains as to what amount is acceptable to the Meeting, and under what conditions. The loans and the recovery plan have been "relatively easy," according to one person involved, subject to anonymity. Now it's getting really difficult.

It's this political dimension that complicates things, especially since this time it's not about loans but about venture capital. **At KLM, there are fears that support for the company will be part of the electoral battle that will erupt in the coming months.** It is expected that the parties will certainly impose additional conditions on an injection of capital with public funds (...)

**The minister can make an impression by strengthening KLM's position in the Franco-Dutch aviation combination.** This is a response to the nationalist sentiment in the House of Representatives, where the PVV, among others, has called for an investigation into a KLM demerger. Safeguarding KLM's position was also the main reason why the Minister took a significant stake in Air France-KLM in early 2018.

**However, Hoekstra will need the cooperation of the French government to achieve this.** (...) In vain, Hoekstra tried to negotiate a veto right for the auditor who, on behalf of the Dutch state, will ensure that the billions in loans will exclusively benefit KLM. The attempt to obtain an additional seat for the Netherlands on the board of directors of the parent company Air France-KLM also failed. What Hoekstra has obtained is a guarantee from the French that no route in the network will be moved from Schiphol airport to Charles de Gaulle airport for the next five years.

Hoekstra can of course threaten not to participate in a share issue. But this will not put pressure on Paris. The minister has repeatedly stated that the survival of KLM is of vital importance for the Dutch economy. So if the French participate in a share issue, Hoekstra cannot be left behind. Otherwise, there is a threat of enormous dilution of Dutch interests (...).

As the problems of Air France and KLM become more and more important because of Covid-19, Mr. Smith will have more arguments to integrate or center the activities of both companies at the head office in Paris. With this in mind, **Hoekstra can try to secure the current**

situation. So do not strengthen KLM's position, but prevent its position from weakening. The only question is how to make it look like a victory in the political arena in The Hague.

*My comment: Dutch Finance Minister Hoekstra is preparing public opinion in his country for a recapitalization of Air France-KLM.*

*In the run-up to the legislative elections, the subject will be the subject of heated debate.*

### > **British Airways gives up laying off its employees to rehire them at a lower price, ...but lowers their salary.**

(source La Tribune) October 1 - **No "fire and rehire" at British Airways.** Strongly criticized in the United Kingdom, the British airline company has decided not to fire the commercial flight and ground personnel it intended to keep and then rehire them on lower-cost contracts. **Although legal in Britain, this procedure caused an outcry across the Channel, with extremely severe criticism from a large part of the political class.** In June, members of the House of Commons Transport Committee called British Airways "a national disgrace for trying to take advantage of the pandemic to reduce the working conditions of its staff. More than 30,000 people were affected by the "fire and hire". **After having decided to lower their salaries by 20%, the pilots were not concerned by this measure.** As a reminder, British also cut 12,000 jobs.

To lower its wage bill, the airline preferred to play the card of negotiation.

(...) **An agreement was reached with the unions of commercial flight crew (PNC) to lower the remuneration of flight attendants by 15% on average** (basic salary, meal allowances...), except for the lowest salaries which will keep their remuneration. **In comparison, the "fire and rehire" project provided for a 20% reduction in base salary.** However, the cuts in the various allowances that accompany the pay of seamen resulted in an even greater reduction in pay. For some cabin crew, the reduction could be as much as 40%.

Even so, even in the agreement, **some categories of cabin crew will leave many more feathers than others. These are the principal pursers. And more precisely the oldest ones, who joined the company before 2011 (from that date, the cabin crew were hired with lower salaries).** With the drop in activity, many of them will lose their rank and return to that of hostesses or stewards, leading to a drop in pay of around 30 to 35%. When activity returns, they will be able to return to their position as head purser with the accompanying salary,

which has been cut by 15%.

Former contracts should see their compensation frozen until the end of their careers, while cabin crew hired after 2011 will continue to benefit from an annual increase. While maintaining three different contracts within the cabin crew population, **the company will now mix the different cabin crew on board aircraft, regardless of the type of contract. A small revolution. Until now, they were separated to avoid the tensions linked to differences in treatment.** In addition, each cabin crew will be able to fly both medium- and long-haul flights. **While management has been able to reach agreement with the NCPs, it has not yet found common ground with the ground staff unions.**

### > **Ryanair could order up to 200 B737 MAX!**

(source Boursier) October 2 - Ryanair's traffic started to decline again in September. 5.1 million people traveled with Europe's leading low-cost airline last month, a 64% drop over a year. The Irish group, which operated 53% of its program compared to 'normal', saw its load factor reach 71% over the period. In addition,

**'The Independent' echoes a strange rumor this morning.** According to the British online daily, **Ryanair could order between 150 and 200 Boeing 737 MAX aircraft by the end of the year.** The site, which does not cite its sources, states that such an agreement would amount to 15.9 billion euros at list price. The order would consist of a mix of MAX 200 and MAX 10. **Ryanair is used to taking advantage of industry crises to purchase new aircraft in order to benefit from better purchasing conditions.**

***My comment:** Ryanair is not just an airline.*

*An important part of its activity consists in buying large volumes of aircraft in times of crisis with substantial discounts. When the activity starts again, Ryanair resells little by little the planes it doesn't use. The profit it then makes is substantial.*

### > **TAP Air Portugal recorded a loss of 582 million euros in the first half of the year.**

(source AFP) September 28 - **TAP Air Portugal suffered losses of 582 million euros in the first half of 2020 due to the Covid-19 pandemic,** which paralyzed global air transport, the airline announced Monday evening.

**TAP, which has** to present a restructuring plan by December to receive

public aid of up to 1.2 billion euros, **saw its passenger numbers fall by 62% to 3 million passengers** compared to 4.9 million passengers in the first six months of 2019 (...)

**In June, the European Commission authorized the Portuguese state to rescue TAP with a loan of up to 1.2 billion euros, which will be accompanied by a restructuring plan.**

In order to help the company, the Socialist government had to reach an agreement to allow the State to increase its participation in the capital of TAP from 50 to 72.5%, by buying half of the private consortium Atlantic Gateway, which belonged to the American businessman David Neeleman, for 55 million euros.

The Portuguese Humberto Pedrosa, former partner of Mr. Neeleman and owner of the road and rail transport group Barraqueiro, retains 22.5% of the capital while the employees keep their 5% stake.

### > **Latam at 26% of its operational capacity in October**

(source AFP) September 29 - **Latam, the largest airline in Latin America**, shaken by the Covid-19 pandemic, announced on Tuesday **that in October it would reach at best 26% of its operational capacity** with 440 flights per week.

(...) The Chilean-Brazilian airline, whose U.S. bankruptcy court approved in mid-September a 2.45 billion dollar rescue plan, is betting on the resumption of international air traffic on October 1 in Peru, one of the airline's most important hubs in Latin America, to increase by 40% the number of flights operated compared to September. (...)

) Latam, which recorded a 75.9 percent drop in revenue in the second quarter, has gradually revived its international routes since June, but **the crisis has forced the company to cut 12,600 jobs.** (...) Following the approval of the rescue plan, **the company must now present a reorganization plan to be approved by the bankruptcy court.**

### > **FAA chief satisfied with his own Boeing 737 MAX aircraft**

(source La Tribune) October 1 - U.S. Civil Aviation Authority (FAA) Director Steve Dickson said he was satisfied with the B737 MAX he flew on a two-hour test flight on Wednesday. This is an important step in the process of recertifying the aircraft, which has been grounded since March 2019 for safety reasons. The aircraft could return to service by the end of the year.

(...) **Steve Dickson said he was pleased with the performance of the aircraft he flew after undergoing the new pilot training**

recommended by a panel of representatives from various aviation regulatory agencies, first online and then in a simulator.

(...) But, he immediately added, "**we are not yet at the end of the process**" of re-certifying the aircraft. To resume service, the modifications made to the aircraft must be certified, especially those concerning the MCAS stall-proof software, which was the subject of both accidents.

Once the B737 MAX has been given the green light to resume flights, airlines will then be required to perform the requested modifications on the aircraft they operate and provide the required training. **Dickson did not want to get ahead of schedule**, but last week Patrick Ky, director of the European Aviation Safety Agency (EASA), said he could give his technical clearance "in November", which could lead to the 737 MAX returning to service "by the end of the year".

***My comment:** The health crisis has put the progress of the Boeing B737 Max compliance work on the back burner into the background. Initial tests appear to be satisfactory.*

*Yet, according to the site [embarque\\_developpez.com](http://embarque_developpez.com), voices are being raised in Great Britain to question the new version of the MCAS (the system responsible for the crashes of two B737 Max).*

*"In the event of a problem, one of the procedures is to disable the airline's automatic trim system, which is activated by the MCAS when the software turns on, and to ask both pilots to use an emergency manual trim wheel instead of the aircraft's powerful electric motors.*

*However, the British Airline Pilots' Association (BALPA) is questioning this emergency procedure. The British trade association said in its comments: "Requiring both crew members to turn the trim wheel simultaneously in a non-standard scenario is extremely undesirable and goes against all philosophies of having one pilot fly the aircraft and another perform the QRH [quick reference manual: reading the emergency checklist]. No flight control system should require both pilots to use it at any time, let alone in an emergency.*

*The results of the MCAS tests will be examined with the utmost attention.*

**> Covid-19: Roissy airport prepares for vaccine arrival**

(source RTL) October 1 - **The first coronavirus vaccines are expected to be available in the first half of 2021.** But at the same time, **airlines and logisticians are already organizing their transportation. At Roissy Charles de Gaulle airport,** all the players in the industry have already started to meet with this in mind.

**At the Air France KLM cargo terminal, suppliers of containers for pharmaceutical products are getting organized.** Vaccines have to be kept in a cold room.

"This is perhaps the most sensitive product to be transported at the moment," says Patrick Van de Weghe, sales manager for France at Envirotainer, one of the companies that manufacture the containers. The containers can have an autonomy of about 1000 hours, between 2 and 8 degrees maximum. And they are already being used, for example, to send influenza vaccines around the world.

Real-time monitoring is carried out in the cargo control center, with temperature curves and systematic readings. But these more than 6,000 containers may not be enough if a vaccine is actually launched. So companies are trying to anticipate needs. "You have to have the right container in the right place at the right time," says Patrick Van de Weghe.

In the cargo area of the airport, three other suppliers of pharmaceutical containers are also organizing to ensure that as many refrigerated containers as possible will be available next year.

**Air France KLM ensures that it works "with all the laboratories".**

But transporting vaccines has a cost: just to rent a container of about 30,000 doses, it costs between 5 and 10,000 euros. A relatively small amount when you know that a shipment can be worth several million euros.

(...) As soon as a vaccine release date is announced, the supply chain should start moving to import, export, or transit the precious goods.

***My comment:** At Roissy Charles de Gaulle as at Schiphol, the Air France-KLM group is preparing to be in a position to deliver the Covid-19 vaccine as soon as it is ready.*

## ***End of the press review***

### **> My comment on the evolution of the Air France-KLM share price**

**The Air France-KLM share is at 2.997 euros at the close of trading on Monday 5 October. It was up very slightly (+0.66%) over one week, after three consecutive weeks of sharp decline.**

Before the coronavirus epidemic, the Air France-KLM share was at 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 down \$1 to \$41.** 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**

**Director Air France-KLM representing employee shareholders PNC and PS.**

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