

Air France-KLM earns big profits, equity remains largely negative

## I Letter from the Director of Air France-KLM



### François Robardet

Representative of employees and former employees PS and PNC shareholders

N°885, November 7, 2022

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## Monday's Press Review

### > Air France-KLM finally makes a big profit, but the company's equity remains largely negative

(source Wansquare) November 2 - **Buoyed by the recovery in travel during the summer, the Air France-KLM group posted an operating profit of more than one billion euros in the third quarter.** However, the company is far from having finished paying off its debts, while demand for air transport could weaken again as early as next year.

Air France-KLM has survived Covid 19, but how will the company, 28.6% of which is controlled by the French state, fare in the coming recession? Kept afloat and recapitalized during the health crisis with French and Dutch government aid, bank loans guaranteed by the two states and capital increases, the company is back in

business and taking advantage of the travel recovery.

(...)

**All the indicators used by the industry point to the expansion of the Franco-Dutch company's business.**

(...)

**Everything would be fine in the best of worlds if the company's financial situation were completely cleaned up. A process underway but far from complete.** The carrier, which had benefited from a total of 4 billion euros of French state-guaranteed loans (PGE) at the height of the health crisis, had repaid 500 million euros by the end of 2021. Then at the end of June 2022, KLM fully repaid its revolving credit line ("RCF") and the direct loan from the Dutch state, for a total amount of €0.9 billion.

The group now wants to make an early partial repayment of the EMP in November for €1 billion of the remaining €3.5 billion outstanding, "in order to reduce its overall financial costs and its exposure to floating rates," it said. Going forward, no further prepayments of the EMP are expected between now and May 2024, and the profile of this bank loan is even expected to remain unchanged until May 2025.

But there **is one major problem that remains to be resolved. That of the negative equity on the company's balance sheet, with a deficit that still amounts to 2.8 billion euros at the end of September, compared to 3.2 billion euros at the end of June.** The company believes it will be able to restore its equity "thanks to the profits" it expects to generate "and quasi-equity projects", mentioning the possible issuance of hybrid bonds in 2022 and 2023. However, the economic situation could put a spanner in the works.

**Faced with weaker demand and rising costs next year, the company's still large equity deficit "is not a comfortable balance sheet position,"** Stifel warns. "Air France-KLM's structural weaknesses persist, with notably fragile cash generation," points out analyst firm Octo Finances. **The stock market is just as fearful: the Air France-KLM share fell on Friday 28 October by 13%, to 1.37 euros.**

***My comment:** Here is an article which illustrates the feeling of the investors towards the Air France-KLM group and which explains the important fall of the share price despite the announcement of good quarterly results.*

*If you want explanations about the equity of a company and how to bail them out when they are negative, I invite you to (re)read [my Flash n°84](#).*

*Note that Air France-KLM announced today that it has proceeded with the early repayment of 1 billion euros of the 3.5 billion euros outstanding loan guaranteed by the French State (the "PGE").*

## > **The new boss of Schiphol, Mr. Sondag, wants to do a "huge job" by focusing on the staff.**

(OTP source) Nov. 1 -- Ruud Sondag, **the new boss of Schiphol Airport, faces a monster job streamlining the airport's operational activities and solving staffing shortages.** In a welcome video to airport staff, Sondag talks about a "huge job" to "free up the energy" needed throughout the system to get the job done.

In his video, Sondag points out that **in recent years, Schiphol has somehow forgotten to make and keep the airport attractive to staff.** He has been to the airport a lot recently to get an idea of the situation. (...) "You notice it. There is some fatigue. I'm going to try to energize by supporting you," said Sondag, who promised to treat people "in a more sustainable way."

**"We outsourced activities. Then things stopped going well," Sondag said to sum up Schiphol's policy.** "We're really going to fix that."

The new boss, who took office Tuesday, says he is targeting not only Schiphol-employed staff, but also cleaners and handlers employed by Schiphol customers. "The direction I want to give is that **we have to act together.** But **at a fast pace,** with an eye and a heart for execution. Because **that's what our customers and airlines really count on,**" it reads. In the

meantime, **Schiphol has yet to launch the recruitment campaign for new security officers, in collaboration with security companies.** According to a spokesperson, this will start "very soon," but the spokesperson could not give a concrete start date. The lack of staff, especially in the field of security, has caused long queues in the departure halls of the airport in recent months.

(...)

***My comment:*** *If the translation of this article is correct, the statement made by the new CEO of Schiphol airport is clear: not everything has been done to bring the activity back to its 2019 level.*

*It is urgent to remedy this. KLM announced that since April 2022, the airport's problems had cost it 175 million euros.*

*The airport management had indicated its willingness to compensate KLM, which has still not been contracted.*

## > **Lufthansa and MSC back in the race to take over ITA Airways?**

(source Air & Cosmos) November 3 - On Monday, October 31, **the Italian government ended the period of exclusive negotiations with the Certares fund, to which Air France-KLM and Delta are backed. But it did not give any explanations on the next steps of the takeover file.**

Europe's leading air transport group Lufthansa remains interested in taking over the

Italian state-controlled airline ITA Airways, after Rome lifted an exclusive negotiation period with a consortium that includes Air France KLM on Monday. (...) **Lufthansa has always said it favored a complete privatization of the Italian company**, while the former government of Mario Draghi had chosen to retain a public participation

(...)

The previous government had announced in late August that it had selected the offer of Certares, associated with Air France-KLM and Delta Airlines, for the purchase of ITA Airways to open exclusive negotiations. This surprise announcement was a setback for the Italian-Swiss shipowner MSC and its ally Lufthansa, which had previously been considered favourites in the race to buy the successor to Alitalia and could now enter the fray again.

This new setback could be linked to the arrival in power in Italy of the Italian Brotherhood party, whose **leader Giorgia Meloni, elected President of the Italian Council, has repeatedly stated her opposition to the privatization of ITA Airways**. It should also be remembered that this election has certainly justified the extension by one month of the period of exclusive negotiations with the Certares fund, which was initially due to end at the end of September.

Air France-KLM has "taken note" of the Italian Ministry of Economy's announcement of the end of the exclusivity period **and added that it is "evaluating its options in the Italian air transport market and awaits further information from the Italian State"**.

(...)

Before being eliminated from the race, MSC and Lufthansa had proposed at the end of August to pay 850 million euros for 80% of ITA, leaving the Italian state with only a 20% share. **For Air France-KLM, this setback is yet another episode in its complicated relations with the Italian air transport sector. In 2009, the group had acquired a 25% share in the capital of Alitalia, the predecessor carrier of ITA Airways, but faced with growing difficulties, had gradually withdrawn from 2013.**

***My comment:*** Two proverbs, one Italian and one French, illustrate this saga:

*"Chi va piano, va sano, e va lontano" (in French "qui va doucement, va sainement et va longtemps").*

*"Patience and length of time are more important than strength and rage".*

*The continuation in the next episode...*

## > **LATAM officially exits its restructuring process**

(source Air & Cosmos) November 4 - **The LATAM Airlines group has just announced that it officially exited on November 4 from its restructuring**

**process, in which it had voluntarily entered at the end of May 2020 by filing**, a few days after the Colombian company Avianca, for **Chapter 11 of the U.S. bankruptcy law**, which corresponds to the French judicial reorganization process and which allows firms in difficulty to be protected from creditors.

The South American airline group has emerged from the process with more than \$2.2 billion in cash and about \$3.6 billion less debt than it had before entering Chapter 11 protection, equivalent to a 35% reduction in debt. In October, the group served 144 destinations in 22 countries, with subsidiaries operating in five domestic markets in the region: Brazil, Chile, Colombia, Ecuador, Peru and international routes in Latin America, to Europe, the United States, the Caribbean and soon to Africa, since LATAM Airlines will take over the Sao Paulo-Johannesburg route in mid-2023. **The group expects to close the year with a total of 85% of its capacity, compared to the level of capacity that was offered in 2019**, before the crisis.

It should also be noted that Delta Airlines is a 20% shareholder in the LATAM Airlines Group since the end of September 2019. Subsequently, Delta and LATAM Airlines have established a joint venture that allows passengers to access more than 300 destinations between the United States/Canada and South America (Brazil, Chile, Colombia, Paraguay, Peru, Uruguay).

Note that **LATAM Airlines left the Oneworld alliance in May 2020**, and that logically, **it would be an ideal candidate to join the SkyTeam alliance, gathered around Delta and Air France-KLM**.

On the fleet side, LATAM has signed agreements with Airbus to acquire until 2029 a total of 87 A320neo family aircraft, which are 20% more fuel efficient. On the cargo side, LATAM Cargo and its subsidiaries are in the midst of an expansion plan that will allow them to increase their respective fleets from a current total of 11 Boeing 767-300F aircraft in 2019 to a total of 20 Boeing 767-300F aircraft in 2024.

***My comment:*** *Within the Skyteam alliance, the two main representatives of the alliance are working to strengthen their presence in Latin America.*

*Air France-KLM Group has had an agreement with GOL since 2017, which focuses on routes between Europe and South America.*

*Delta Air Lines acquired a stake in LATAM in 2019, a prelude to the joint venture agreement between the two airlines on routes between North and South America.*

*Note that last February, American Airlines announced its intention to invest \$200 million in GOL. Its goal: to compete with the joint venture Delta - LATAM on routes between North and South America.*

*Note: I would like to take this opportunity to correct an error that some of you noticed in my letter #860. I had mixed up the nationalities of TAM and LAN!*

*The LATAM group was created in 2010 by the merger between TAM (Brazil) and LAN (Chile).*

### > **More delays for the Boeing 737 MAX 7 and 10**

(Air Journal source) Nov. 4 - Boeing now expects that certification of the 737 MAX 7 will not be granted until early next year, and the 737 MAX 10 not until late 2023 or early 2024.

**At its investor day on November 2, 2022**, the first in four years, **the American aircraft manufacturer had created a surprise by postponing the entry into service of a new aircraft to 2035 at the earliest, a virtual burial of the NMA**. But Boeing also mentioned its ongoing dispute with the FAA over the certification of its last two models of its family of single-engine planes. **Stan Deal, CEO of Boeing Commercial Airplanes (BCA), said he expects another certification deferral, for the 737-7 "early next year" and for the 737-10 "in late 2023 or early 2024."**

Instead of 2022 and the summer of 2023 respectively, as previously hoped.

Remember that **these certifications depend entirely on Congress passing a law allowing the December 31, 2022 deadline imposed for the certification of the two 737 MAXs "as is" to be overridden**. Otherwise, Boeing would be forced to install a new EICAS safety system, a complicated prospect for both the manufacturer and the airlines. Apart from increased costs and new postponements of deliveries, **the pilots themselves are divided on the subject (for the exemption at Southwest, against at American Airlines)**. Last July, Boeing CEO Dave Calhoun even threatened to abandon the MAX 10 program

(...)

According to the Seattle Times, defects were discovered at the Spirit AeroSystems supplier, which manufactures the 737 MAX fuselages in Wichita, Kansas. "At the last moment, our quality management system detected two defects in the fuselage," said Stan Deal, who wants to believe that by the end of the year he will be able to deliver about 30 737 MAXs per month.

**My comment:** *The end of 2022 deadline is approaching for Boeing and the 737 MAX versions 7 and 10.*

*In 2019, the U.S. Congress had deemed it unacceptable for both 737 MAXs to be certified without EICAS installed.*

*If Congress persists, Boeing will be in deep trouble. The cockpit of the B737 Max is small and there is no room to insert new equipment. Except to completely redesign the cockpit, but the cost would be prohibitive.*

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

### **> My comments on the Air France-KLM share price trend**

**Air France-KLM shares closed at 1.307 euros on Monday 7 November. It is down slightly this week by -1.883%.**

After rising 15% in two weeks, benefiting from positive announcements from US and European airlines, it has lost 13% in recent weeks after announcements of quarterly results below expectations.

Restrictions on operations at Schiphol (Amsterdam airport) and Air France's negative equity had more effect than the announcement of exceptional third quarter results.

**The average (consensus) analyst rating for AF-KLM shares is 1.53 euros.** The highest price target is 2.00 euros, the lowest 0.85 euros. I only take into account analysts' opinions after the May 2022 capital increase.

You can find the details of the analysts' consensus on my blog.

### **> My comment on the evolution of fuel prices**

**The gap between oil and jet fuel prices has never been wider.**

**The price of jet fuel in Europe is down this week by -\$8 to \$135 per barrel.** After peaking at \$182 in June 2022, it was down to \$132 in early August. It was at \$79 a little over a year ago.

**Brent crude oil (North Sea) is up slightly this week by +\$2 to \$95**

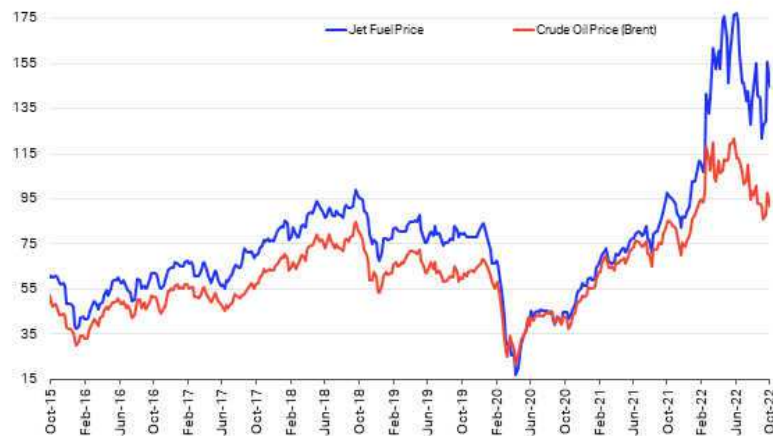
From mid-February to the end of July, it was yo-yoing between \$100 and \$120. Since then, it has oscillated between \$85 and \$99.

At the beginning of March, Brent reached \$132, close to its record of \$150 (in 2008).

Fears that the economy will be in recession by the end of 2022 led to a drop in fuel prices. Then the announcement by OPEC+ to reduce oil production brought prices back up.

**Since the beginning of the war in Ukraine, there is no longer any correlation between the price of a barrel of Brent oil and the price of a barrel of Jet Fuel.** This is very clear on the graph below, which covers the period June 2015 - October 2022.

Jet Fuel & Crude Oil Price (\$/barrel)



Source: S&P Global, Refinitiv Eikon

Jet fuel price per barrel by region (source IATA) as of November 4, 2022

**Fuel Price Analysis**

The jet fuel price for week of up 3.7% at \$144.3/bbl:

4 November 2022	Share in World Index	cts/gal	\$/bbl	\$/mt	Index Value 2000 = 100	vs. 1 week ago	vs. 1 month ago	vs. 1 yr ago
<b>Jet Fuel Price</b>	100%	343.63	144.33	1139.70	394.53	3.7%	-7.4%	52.9%
Asia & Oceania	22%	304.11	127.73	1009.04	364.95	0.8%	-2.3%	40.3%
Europe & CIS	28%	346.43	145.50	1148.00	392.02	7.4%	-3.4%	53.2%
Middle East & Africa	7%	314.83	132.23	1044.02	394.87	3.3%	-3.2%	44.8%
North America	39%	366.92	154.11	1217.43	409.69	2.8%	-12.7%	60.3%
Latin & Central America	4%	364.35	153.03	1208.91	423.91	3.6%	-6.1%	56.3%

**Good to know**

**> Advice for employees and former employees who are shareholders**

You will find on my [navigaction](#) site the modalities of access to the managers' sites.

To avoid forgetting to change your contact information each time you change your postal address, **I advise you to enter a personal e-mail address.** It will be used for all correspondence with the management organizations.

Keep all the documents related to your Air France-KLM shares in one place: all the letters you receive from the different managers, Natixis, Société Générale, your personal financial institution if you bought your shares through it.

**> Management of employee investment funds**



When you invest money in one of the Air France FCPE funds, you get shares in these funds. You do not hold shares directly.

It is the supervisory boards, which you elected in July 2021 for a five-year term, that manage the funds and make the decisions.

The Aeroactions, Majoractions and Concorde funds only hold Air France shares.

The Horizon Épargne Actions (HEA), Horizon Épargne Mixte (HEM) and Horizon Épargne Taux (HET) funds manage portfolios of various stocks.

***My comment:*** *If you would like more information on the management of the various Air France FCPEs, please consult [my website Navigation, section Air France-KLM employee shareholding](#).*

## **Details**

**This information is not intended to be a solicitation to sell or a solicitation to buy Air France-KLM shares.**

You can react to this press review or send me 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 relating to the Air France-KLM group or to employee share ownership...**

See you soon.

To find the last press reviews of Monday, it is [here](#)

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**| François Robardet**

**Director of Air France-KLM representing the employees and former employees shareholders of PNC and PS.**

**You can find me on my twitter account @FrRobardet**

**Alternate Nicolas Foretz, PNC**



When I was elected, I received the support of the CFDT and the UNPNC.

This press review deals with subjects related to the Air France-KLM shareholding.

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