Industry report

Barcelona, 2009

IMPORTANTÉ: este informe es sólo una herramienta para entender mejor el entorno competitivo del transporte aéreo en la época del caso. No hace falta “estudiárselo”, basta con leerlo y entenderlo.
Industry overview for the last 40 years

- Impact of liberalization in the European market
- Competitive strategies of European airlines
- Impact of financial crisis in the European market
- Spanair’s competitive framework
<table>
<thead>
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<tbody>
<tr>
<td><strong>US facts</strong></td>
<td><strong>Europe facts</strong></td>
<td><strong>Global facts</strong></td>
</tr>
</tbody>
</table>
| **US airline industry deregulation (1978)** | | Beginning of wide body era (Early 70’s)  
Boeing, MD and Lockheed inaugurated wide body service, representing a big boost for airlines. Airbus began producing Europe’s most commercially successful line of airliners (1972) |
| Congress passed the Airline Deregulation Act in 1978, easing the entry of new companies into the business and giving them freedom to set their own fares and fly whatever domestic routes they chose.  
Deregulation of the industry was followed quickly by new entrants, lower fares and the opening of new routes and services to scores of cities. | | |
| **US dominated again by major airlines (early 80’s)** | | |
| Major US airlines dominate again their routes through aggressive pricing and additional capacity offering. Only America West Airlines remained a significant “new entrant” survivor.  
Explosive growth in US demand for air travel, as a result of deregulated environment. | | |
# Airline industry overview (1985-2000)

<table>
<thead>
<tr>
<th>1985-90</th>
<th>1990-95</th>
<th>1995-00</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>US facts</strong></td>
<td><strong>Europe facts</strong></td>
<td><strong>Global facts</strong></td>
</tr>
<tr>
<td>The economic recession, together with the Gulf War from 1991, caused the industry to experience the first drop in passenger numbers in a decade. By the end of the three-year period 1989-1992, it had lost about US$10 billion. Large airlines like Pan American and Eastern disappeared; others, such as TWA and Continental Airlines, sought shelter from bankruptcy by going into the protection of Chapter 11 bankruptcy.</td>
<td>Lufthansa (Germany), Air France (France), Iberia (Spain), British Airways (UK), Alitalia (Italy), KLM (Netherlands), SAS (Scandinavia), Austrian (Austria), TAP (Portugal), Olympic (Greece), LOT (Poland), Czech Airlines (Czechoslovakia), Sabena (Belgium), Swissair (Switzerland), Malev (Hungary).</td>
<td>The number of international passengers dropped for the first time. The financial difficulties were exacerbated by airlines over-ordering aircraft in the boom years of the late 1980s, leading to significant excess capacity in the market. IATA’s member airlines suffered cumulative net losses of US$20.4bn in the years from 1990 to 1994.</td>
</tr>
</tbody>
</table>

| **US-Canada open skies (1995)** | **European airline industry deregulation (93)** |  |
| The bilateral “Open Skies” agreement between US and Canada authorized any US or Canadian airline to offer transborder services without restriction in terms of fares, flight frequencies or aircraft types. The capacity of scheduled airline services between the two countries experienced strong growth starting in 1995, with a sharp increase of 25% the first year alone. **New LCC style (Late 90’s)** | The 1992 package that created the Single European Aviation Market did away with bilateral agreements for services within the EU. Community air carriers were permitted to exercise traffic rights on routes anywhere within the EU, with some cabotage restrictions. European de-regulation was rapidly followed by new entrants and a significant increase in competition. **Emerging of European LCCs (Early 90’s)** | Emerging of a new style of low cost airline, headed by Southwest Airlines, JetBlue, AirTran Airways, Skybus Airlines…, representing a serious challenge to the US legacy carriers. |

| **Legacy carriers privatization (Late 90's)** |  |  |
| Beginning of the privatization process of traditional European legacy carriers, combined with some other corporate operations (merger and acquisitions). |  |  |

**European final stage of deregulation (1997)** Liberalization of freestanding cabotage.
# Airline industry overview (2000-2009)

<table>
<thead>
<tr>
<th>Year</th>
<th>US facts</th>
<th>Europe facts</th>
<th>Global facts</th>
</tr>
</thead>
</table>
| 2000-05 | | Emerging of Continental LCCs (Early 00’s)  
The low-cost business model extended to the continent. New low-cost entrants headed by Germany (Air Berlin, Germanwings...) | 11-S (2001)  
September 11th terrorist attacks led to a dramatic downfall in worldwide air traffic, specially affecting to US traffic (which afterwards underwent a slowly recovery), where several airlines went to bankruptcy.  
SARS + Irak War (2003)  
Global epidemic SARS (severe acute respiratory syndrome) temporarily steered passengers away from flying to certain regions of the world. Thus SARS, together with the Irak War significantly impacted on international traffic, which decreased by more than 20%. |
The European Commission adopted proposals for a Single European Sky (SES), to create a Community regulator for air traffic management within the EU, Norway and Switzerland. | Single European Sky revision (2008)  
Final agreement on SES II (Single European Sky revision).  
Global financial crisis (2009)  
Global financial crisis extended to air transport, impacting with special virulence on this sector. Air traffic downfall (global RPK fall by -6.0% from 2008), significant global losses (global net losses of US$11 billion in 2009), capacity cuts (global ASKs fell by -3.6% from 2008) and airlines collapse. |
Industry overview for the last 40 years

**Impact of liberalization in the European market**

- Competitive strategies of European airlines
- Impact of financial crisis in the European market
- Spanair’s competitive framework
The **1992 package** that created the **Single European Aviation Market** did away with **bilaterals for services within the EU from 1993 on**. Its main provisions were:

- **Community air carriers** were permitted to exercise **traffic rights on routes anywhere within the EU**

- Several **safeguards** were provided:
  - **To protect routes where a public service obligation existed**, particularly in routes operated by small aircrafts
  - **Provision to enable** a Member State **to refuse/limit access for congestion/environmental reasons**
  - **To deal with excessively low or excessively high fares** (1)

- **Capacity limitations** were made **illegal**

- **Community carriers** were “**free to set airfares**”

NOTA: los bilaterales hacen referencia a los acuerdos entre Estados que regulan quién y a qué aeropuerto puede volar una compañía de otro Estado. Es decir, dos países acuerdan de forma normalmente simétrica autorizar vuelos y frecuencias a sus respectivas compañías. No se puede volar a otro país libremente si no hay un acuerdo bilateral. Eso es lo que se abolió en Europa, pero sigue vigente en gran parte del resto del mundo

(1) It has never been used
In October 2001, the European Commission adopted proposals for a Single European Sky (SES), to create a Community regulator for air traffic management within the EU, Norway and Switzerland. The Community regulator aimed to merge upper European airspace, organize this airspace uniformly, with air traffic control areas based on operational efficiency, and integrate civil and military air traffic management.

In June 2008 a revision of the SES regulations was adopted (SES-II), with focus on four areas:

- The existing Single Sky legislation was sharpened to deal with **performance and environmental challenges**
- The **SES ATM Research (SESAR) programme** was to provide the future technology
- The **competence of the European Aviation Safety Agency (EASA)** was extended (1)
- The ‘**action plan for airport capacity, efficiency and safety**’ was implemented

(1) To aerodromes, air traffic management and navigation services
The air transport liberalization in Europe brought several consequences

1. Proliferation of new entrants, emergence of Low Cost Carriers
2. Increase in capacity and densification of routes
3. Passenger stimulus
4. Decrease in yields
5. Pressure on costs to improve competitiveness
6. Airline profitability falls
New 176 airlines have been launched since the liberalization process in Europe.

The removal of competency entry barriers has brought the appearance of new airlines, which has increased competition and pressure over yields and costs.

Source: AEA, OAG
Among these new airlines LCCs are the ones who have most modified the competitive scenario in Europe

LCC European market share and traffic evolution

LCCs capacity share 2009 (seats available)

Source: Eurocontrol (2007)

Source: OAG (2009)
After the UK, Spain has Europe’s highest low cost offer, with a market share of 46% in European routes.

The LCC seats offer in Spain rose to 31.6 million in the 2009 Summer Season, which meant a penetration of 46% in the Spanish-Europe market.
In 2009, Spain generated 18% of the low-cost Intra-European seats offer.

Country of origin of Available Seats Within Europe (Millions; Apr’09-Oct’09)

<table>
<thead>
<tr>
<th>Country</th>
<th>Low-Cost Available Seats</th>
</tr>
</thead>
<tbody>
<tr>
<td>Others</td>
<td>24.1%</td>
</tr>
<tr>
<td>Italy</td>
<td>5.4%</td>
</tr>
<tr>
<td>France</td>
<td>12.5%</td>
</tr>
<tr>
<td>Germany</td>
<td>16.0%</td>
</tr>
<tr>
<td>Spain</td>
<td>17.7%</td>
</tr>
<tr>
<td>UK</td>
<td>24.3%</td>
</tr>
</tbody>
</table>

Ranking of low-cost departures Within Europe at European airports

<table>
<thead>
<tr>
<th>Ranking 2009</th>
<th>Airport</th>
<th>LCC available seats (million Apr-Oct 09)</th>
<th>LCC market share</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>London Stansted Apt</td>
<td>6.96</td>
<td>96%</td>
</tr>
<tr>
<td>2</td>
<td>Palma de Mallorca</td>
<td>6.43</td>
<td>74%</td>
</tr>
<tr>
<td>3</td>
<td>London Gatwick Apt</td>
<td>6.32</td>
<td>66%</td>
</tr>
<tr>
<td>4</td>
<td>Barcelona Apt</td>
<td>4.74</td>
<td>43%</td>
</tr>
<tr>
<td>5</td>
<td>Dublin</td>
<td>4.07</td>
<td>54%</td>
</tr>
<tr>
<td>6</td>
<td>London Luton Apt</td>
<td>3.60</td>
<td>100%</td>
</tr>
<tr>
<td>7</td>
<td>Manchester International Apt</td>
<td>3.54</td>
<td>66%</td>
</tr>
<tr>
<td>8</td>
<td>Cologne/Bonn K.A. Apt</td>
<td>3.30</td>
<td>82%</td>
</tr>
<tr>
<td>9</td>
<td>Dusseldorf International Airp.</td>
<td>3.25</td>
<td>46%</td>
</tr>
<tr>
<td>10</td>
<td>Malaga</td>
<td>3.07</td>
<td>67%</td>
</tr>
<tr>
<td>11</td>
<td>Berlon Tegel Apt</td>
<td>2.98</td>
<td>51%</td>
</tr>
<tr>
<td>12</td>
<td>Munich International Airp.</td>
<td>2.83</td>
<td>23%</td>
</tr>
<tr>
<td>13</td>
<td>Madrid Barajas Apt</td>
<td>2.78</td>
<td>17%</td>
</tr>
<tr>
<td>14</td>
<td>Alicante</td>
<td>2.67</td>
<td>76%</td>
</tr>
<tr>
<td>15</td>
<td>Brussels Airp.</td>
<td>2.67</td>
<td>46%</td>
</tr>
</tbody>
</table>

Source: OAG Apr’09 – Oct’09

3 Spanish airports among the Top-10: PMI, BCN and AGP
This has increased competitive pressure dramatically in the high density routes...

### Air transport liberalization in the EU: Key Indicators

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Pre-Liberalization (1992)</th>
<th>Current</th>
<th>Variation</th>
<th>Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td># EU domestic city pair routes</td>
<td>813</td>
<td>1.139</td>
<td>40%</td>
<td>+326</td>
</tr>
<tr>
<td># EU domestic routes with more than 1 carrier</td>
<td>106 (13.0%)</td>
<td>334 (29.3%)</td>
<td>215%</td>
<td>+218</td>
</tr>
<tr>
<td># Intra-EU (int'l.) city pair routes</td>
<td>692</td>
<td>3.072</td>
<td>344%</td>
<td>+2.380</td>
</tr>
<tr>
<td># Intra-EU (int'l.) routes with more than 2 carriers</td>
<td>61 (8.8%)</td>
<td>906 (29.5%)</td>
<td>1.385%</td>
<td>+845</td>
</tr>
</tbody>
</table>

#### Intra-EU routes with more than 5 carriers

- Rome-Milan: 8
- Bari-Milan: 7
- Paris-Marseille: 7
- Paris-Rome: 7
- Cagliari-Milan: 6
- Dusseldorf-Palma Mallorca: 6
- Faro-London: 6
- Las Palmas-Tenerife: 6
- London-Malaga: 6
- London-Palma Mallorca: 6
- Milan-Naples: 6
- Milan-Palermo: 6
- Palermo-Rome: 6

*Source: OAG apr-09*

*Note: Not considered airlines with code shares*

- **Great increase in the number of routes operated**, both at domestic and intra-EU levels
- **Moreover, huge increase in the number of carriers operating each route**
  - Domestic routes operated by more than 1 carrier increase from 13% in 1992 to 29% in 2009 (16 p.p.)
  - International Intra-EU routes operated by more than 2 carriers increase from 9% in 1992 to 29% in 2009 (20 p.p.)
stimulating passenger demand, mainly driven by LCCs...

- The liberalization in Europe in 1993 allowed any airline registered in any European Union (EU) member state to serve any city-pair inside the EU.
- Since then the industry has been radically shaken up by LCCs, expanding their operations, opening up new routes with new destinations and greatly fostering demand with their low prices.
- In fact, the creation of the Single European Aviation Market led to a traffic CAGR 95-04 that almost doubled the CAGR 90-94.

Intra Europe Air traffic growth
(Millions of Passengers)

- CAGR 90-95 3.5%
- CAGR 95-07 5.5%
- CAGR 95-07 27.0%

Source: European Airline Industry, ALG estimations
...and reducing yields by 30% in Europe

- **US domestic Yield**: decrease of 50% from liberalization (1978) to 2006 (CAGR -2.4%)
- **Intra-European Yield**: decrease of 30% from liberalization (early 90’s) to 2006 (CAGR -2.5%)
...and cost reduction has become key to compete with LCCs for passenger volumes and lower fares

<table>
<thead>
<tr>
<th>CASK ex-fuel 2004-08 evolution (sample of carriers)</th>
</tr>
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<tbody>
<tr>
<td>TAP</td>
</tr>
<tr>
<td>-16,5%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Iberia case – Evolution of CASK ex-fuel (c€/ASK) vs. Short haul production share</th>
</tr>
</thead>
<tbody>
<tr>
<td>c€/ASK</td>
</tr>
<tr>
<td>2004</td>
</tr>
<tr>
<td>6.47</td>
</tr>
</tbody>
</table>

Source: Annual Reports of selected companies

Source: Iberia Annual Report

- Main traditional carriers have significantly reduced their CASK over the last five years
- Iberia, which showed a downfall in CASK of -9.7% between 2004-08, has combined this initiative with a progressive retreat from the short haul market (-8.5 p.p. in the same period)
These market dynamics have led the airline sector to show losses most years on the current decade...

Global commercial airline profitability

<table>
<thead>
<tr>
<th>System-wide global commercial airlines</th>
<th>Operating profits, US$ billion</th>
<th>Net profits, US$ billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Global</td>
<td>19.7</td>
<td>-3.8</td>
</tr>
<tr>
<td>North America</td>
<td>9.3</td>
<td>-2.3</td>
</tr>
<tr>
<td>Europe</td>
<td>6.4</td>
<td>3.3</td>
</tr>
<tr>
<td>Asia-Pacific</td>
<td>3.5</td>
<td>-5.5</td>
</tr>
<tr>
<td>Middle East</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Latin America</td>
<td>0.4</td>
<td>0.5</td>
</tr>
<tr>
<td>Africa</td>
<td>0.1</td>
<td>0.2</td>
</tr>
</tbody>
</table>

Source: ICAO data to 2007-08, IATA 2009-10 forecast
- Industry overview for the last 40 years
- Impact of liberalization in the European market
- **Competitive strategies of European airlines**
- Impact of financial crisis in the European market
- Spanair’s competitive framework
Based on their market orientation, airlines are classified into four groups.

<table>
<thead>
<tr>
<th>Type of network</th>
<th>Domestic</th>
<th>European</th>
<th>Long haul</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scheduled</td>
<td></td>
<td></td>
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<tr>
<td>Full Service Network Carriers (FSNC)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Low-Cost Carriers (LCC)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-scheduled</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Regionals</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Charters</td>
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<tr>
<td>Chartered</td>
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</tr>
</tbody>
</table>

### Distribution of EU air transport by carrier type

(Number of seats available, weekly; share)

<table>
<thead>
<tr>
<th>Carrier Type</th>
<th>Seats 2007</th>
<th>Seats 2008</th>
<th>Share 2007</th>
<th>Share 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Full service network carrier</td>
<td>9,933,291</td>
<td>9,832,574</td>
<td>(60%)</td>
<td>(58%)</td>
</tr>
<tr>
<td>Low cost carrier</td>
<td>5,069,098</td>
<td>5,775,406</td>
<td>(31%)</td>
<td>(34%)</td>
</tr>
<tr>
<td>Charter / holiday carrier</td>
<td>1,046,138</td>
<td>787,884</td>
<td>(6%)</td>
<td>(5%)</td>
</tr>
<tr>
<td>Regional carrier</td>
<td>569,418</td>
<td>543,343</td>
<td>(3%)</td>
<td>(3%)</td>
</tr>
</tbody>
</table>

Source: OAG 2008
Full Service Network Carriers

- **Scheduled airlines** focused on providing **high value services**, with **several different classes**
- Typically, **international operating companies** with a **network-oriented system** (one or more hubs) dominating one geographical area or market
- **Sector composed of both traditional carriers and new entrants**, founded after liberalization or coming from charter services
- **High business diversification** in main FSNCs (AF-KLM, Lufthansa, Iberia...): **maintenance, handling, cargo**...
FSNC are continuously working on cost reduction, in order to get closer to an LCC cost structure

--- Main initiatives implemented by traditional carriers ---

- **Cabin densification**, allowing airlines to increase their available seats per flight
- **Convergence to unified fleets**, with a unique aircraft model both for short-medium haul and long haul, providing the airlines with relevant advantages:
  - Increase in **crew productivity**
  - Increase in **aircraft utilization**
  - More efficient **maintenance model**
- **Concentration of operations in no more than 1-2 bases**, increasing crew productivity and aircraft utilization, as well as reducing overheads
- **Increase of austerity regarding salary policies**
- **Strict cost control**
- **Focus on core markets** (mainly long haul), leaving the non-core ones or transferring them to subsidiaries

“**Air France-KLM** has not ruled out the possibility of removing Business class from some medium-haul routes “

*Centre for Asia Pacific Aviation 12th Oct 09*

“**Iberia** studies whether to charge for baggage”

*Reuters, 7th Oct 09*

”**British Airways** ditch first class in new long-haul planes as age of austerity bites“

*Guardian, 22nd May 09*

“**Air France-KLM** will charge 50 euros for a second check-in bag“

*Europa Press, 20th Oct 09*
Low-Cost Carriers

- **Scheduled airlines offering low prices** for the majority of flights
- **Very simple business model; no frills**
- Operation mainly based on **Point-to-Point routes of short-medium haul**, with focus on:
  - High density routes
  - Secondary markets, where competition is lower
- **Low cost structure and high load factors**
- **Sector basically composed of fully private new entrants**, founded after liberalization

**Top 20 LCCs in Europe in terms of seats in Summer Season 2009**

(Total seats capacity, millions)

Source: OAG Apr-Oct 2009
### Low-Cost Carriers

LCCs take advantage of their simpler business model and lower service level...

<table>
<thead>
<tr>
<th>LCC</th>
<th>FSNC</th>
</tr>
</thead>
</table>
| **Network** | **Point-to-Point in high-density high-yield routes**, with specific focus on long haul  
• Regarding secondary routes, focus in **connectivity** aimed to feed long haul |
| **Product** | **Multiple classes**  
• **Seating** assignment  
• **All-inclusive product** |
| **Commercial** | **Targeted** at both **business and tourists**  
• Several distribution channels; higher relevance of indirect sales (GDS, travel agencies)  
• Medium marketing investment  
• Extended brand: price and service |
| **Operational** | **Medium-intensive aircraft usage** (1)  
• Primary airports  
• Several aircraft models  
• Less efficient turnaround time  
• Integration of non-core activities (handling, maintenance) |

- **Focus on Point-to-Point operations**, both in high-density and secondary routes
- **One class**  
• **No seating** assignment  
• **Strong ancillary revenues**: baggage, first in boarding, buy-on-board...
- **Target** customer: **tourist**, increasing pressure for business pax  
• **Distribution** highly concentrated on **direct sales**, especially **online channel**  
• Intensive marketing investment; aggressive advertising campaigns  
• **One brand**: lowest price
- **Highly intensive aircraft usage**  
• Mostly secondary airports  
• Unified fleet  
• Turnaround time: 25 minutes  
• Outsourcing of operational non-core activities

(1) Regarding long haul, utilization decreases due to network and programme constraints
Low-Cost Carriers

Full Network Carriers vs. Low-Cost Carriers current cost structure

2008 CASK excluding fuel of European airlines
(€/ASK)

Full Service Network Carriers

Low-Cost Carriers

Source: Airlines 2008 Annual Reports
- Industry overview for the last 40 years
- Impact of liberalization in the European market
- Competitive strategies of European airlines
- **Impact of financial crisis in the European market**
- Spanair’s competitive framework
Air transport demand is suffering a significant fall (passenger traffic is expected to decrease by 6.5% in 2009), especially affecting short-medium haul routes.

Traffic fall has been followed by decrease in capacity, which seems to be not enough:

- Available seats have decreased in 2009 by 3.6%
- ASKs have decreased at a lower level (2.5%), as short haul routes have been cut the most

The over-capacity has led to a general decrease in yields.

In this context, and in spite of the decrease in jet fuel prices, most European airlines show significantly negative results in 2009.

LCCs are the airlines managing this situation the best, thanks to their lower decrease in traffic, as well as to their lower costs structure.

Thus, airlines need additional funds in order to overcome the crisis; the great difficulty in finding equity is leading them to basically raise funds through debt (In 2009 up to August, European airlines raised more than US$5 billion in funds, over 90% corresponding to debt)
European traffic has decreased the most on the intra-European routes in 2009

- Intra-European routes have been especially affected by the traffic fall, decreasing by 9.2% in terms of passengers
- Almost all the markets show a greater decrease in passengers than in RPKs, which means that traffic downfall affects the shortest routes the most
...and has specially affected to premium segments

Passenger travelling in business classes in European short haul routes have shifted to Economy Classes in spite of the fares decrease
And even though in 2009 jet fuel reached its lowest price in recent years,...

**Crude oil and jet fuel price evolution (US$/barrel)**

- **Jet fuel price**
- **Oil price**
- **Futures curve early Sep 2009**

*Source: Platts, Bloomberg*

**AEA airlines fuel cost evolution (€ billion)**

- 2005: 13.3
- 2006: 16.9
- 2007: 17.4
- 2008: 22.9
- 2009: 19.4

*Source: AEA*

**Fuel cost weight for AEA airlines (€ billion)**

- **Fuel & Oil**: 27.9%
- **External costs excl. fuel & oil**: 36.2%
- **Internal costs**: 35.9%

*Source: AEA*
...most airlines are performing worse in 2009 than in 2008, especially FSNCs

FSNC’s 2009 YTD results are significantly worse than 2008 ones

Source: Annual Results
Note: results correspond exclusively to the airline business of each company (e.g. not maintenance business units)
(1) 2009 Vueling results correspond to Vueling + Clickair, as merger finalized on jul-09
- Industry overview for the last 40 years
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  - Spanish market outlook: Domestic market
Competition in the Spanish domestic market has increased in the past years. The entry of new competitors and the growing stimulation of low fares by LCCs in the domestic market have led to increasing competitive pressure, while demand is decreasing due to market conditions.
The positive trend of domestic market in the past years caused capacity to increase far above demand until 2008

- **The regular traffic offering in the Spanish domestic market** has grown in around 7,800 million ASK since 2005 (26%)
- **The offering of seats** has increased by 23% in past 3 years, showing *higher growth than passenger demand* (9%), which has resulted in a *fall of load factor*
  - 11 million new seats were offered from 2005 to 2008, while demand increased by only 3 million passengers
- **LCC strategy** is focussed on the achievement of high load factors by means of aggressive tariffs. Therefore, *reduction of load factor is affecting mainly Full Service Network Carriers*

**Evolution of regular domestic traffic parameters in Spain (2005 – 2008)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Flights ('000)</th>
<th>ASK (million)</th>
<th>Seats (million)</th>
<th>Passengers (million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>375</td>
<td>30,455</td>
<td>48,3</td>
<td>36,9</td>
</tr>
<tr>
<td>2008</td>
<td>496</td>
<td>38,252</td>
<td>59,3</td>
<td>40,1</td>
</tr>
</tbody>
</table>

Source: OAG, Aena
In addition, air traffic in peninsular routes is being highly affected by the high speed train

- The expansion of the AVE high speed train is threatening intrapeninsular air traffic
- The AVE expansion will imply a significant change in air transport demand, which will have a higher impact on the traffics with origin/destination Madrid
- The new demand scenario strengthens the focus on routes meant to enhance mainland connections to the islands
  - Air traffic between Barcelona and Madrid decreased more than 2.5 million passengers since 2007, due to the inauguration of the high speed railway between both cities
  - The AVE Madrid-Málaga caused air traffic to fall by 27.8% in 2008 (more than 400,000 passengers) in this route
  - In the coming 5 years new AVE lines will be opened between Madrid and Bilbao, La Coruña, Valencia and Alicante, with the AVE to Valencia being the closest to opening

<table>
<thead>
<tr>
<th>Route</th>
<th>Opening</th>
<th>Train time</th>
<th>Block Hours</th>
</tr>
</thead>
<tbody>
<tr>
<td>Madrid-Málaga</td>
<td>Dec 2007</td>
<td>2h</td>
<td>1:05</td>
</tr>
<tr>
<td>Barcelona-Madrid</td>
<td>Feb 2008</td>
<td>2h35m</td>
<td>1:15</td>
</tr>
<tr>
<td>Madrid-Valencia</td>
<td>2nd half 2010</td>
<td>1h25m-1h35m</td>
<td>1:00</td>
</tr>
<tr>
<td>Madrid-Alicante</td>
<td>2012</td>
<td>1h40m-1h50m</td>
<td>1:05</td>
</tr>
<tr>
<td>Madrid-Bilbao</td>
<td>2013</td>
<td>2h 10m</td>
<td>1:00</td>
</tr>
<tr>
<td>Madrid-La Coruña</td>
<td>2013</td>
<td>2h 50m</td>
<td>1:10</td>
</tr>
</tbody>
</table>
▪ Industry overview for the last 40 years
▪ Impact of liberalization in the European market
▪ Competitive strategies of European airlines
▪ Impact of financial crisis in the European market
▪ **Spanair’s competitive framework**
  - Spanish market outlook: European market
LCCs clearly dominate the European market and are causing FSNC traffic to decrease

**Spain – Europe traffic evolution 2001-2008 (Million pax)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>LCC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>41,3</td>
<td>12,8</td>
</tr>
<tr>
<td>2002</td>
<td>42</td>
<td>14,5</td>
</tr>
<tr>
<td>2003</td>
<td>49,5</td>
<td>19,6</td>
</tr>
<tr>
<td>2004</td>
<td>56,1</td>
<td>26,1</td>
</tr>
<tr>
<td>2005</td>
<td>64,6</td>
<td>33,8</td>
</tr>
<tr>
<td>2006</td>
<td>70,3</td>
<td>38,5</td>
</tr>
<tr>
<td>2007</td>
<td>80,5</td>
<td>51</td>
</tr>
<tr>
<td>2008</td>
<td>81,2</td>
<td>55,5</td>
</tr>
<tr>
<td>2009E</td>
<td>76</td>
<td>52,8</td>
</tr>
</tbody>
</table>

**Spain – Europe regular traffic evolution 2005-2008 (Million pax)**

<table>
<thead>
<tr>
<th>Year</th>
<th>FSNC</th>
<th>Others FSNC</th>
<th>LCC</th>
<th>Others LCC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>47.7%</td>
<td>52.3%</td>
<td>20.2%</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>31.7%</td>
<td>68.3%</td>
<td>19.9%</td>
<td></td>
</tr>
</tbody>
</table>

**Passenger increase 04-09**

- FSNC: -6.8%
- LCC: 19.9%
- Rest of airlines: 26.7%

Source: Aena

LCCs have captured all of the traffic growth between Spain and the European market, even though they are also suffering.
International routes show the reduction of economy passengers and premium passengers and fares: case of MAD-FRA

**MAD-FRA Share Evolution by Class in Pax (2006-2009)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Business+First Class</th>
<th>Full economy</th>
<th>Discount economy+others</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>78%</td>
<td>15%</td>
<td>7%</td>
</tr>
<tr>
<td>2009</td>
<td>87%</td>
<td>7%</td>
<td>5%</td>
</tr>
</tbody>
</table>

Source: IATA Paxis  
Note: 2009 has been considered as the period Jun'08-Jun'09

**MAD-FRA Share Evolution by Class in Revenues (2006-2009)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Business+First Class</th>
<th>Full economy</th>
<th>Discount economy+others</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>51%</td>
<td>31%</td>
<td>19%</td>
</tr>
<tr>
<td>2009</td>
<td>56%</td>
<td>28%</td>
<td>17%</td>
</tr>
</tbody>
</table>

Source: IATA Paxis  
Note: 2009 has been considered as the period Jun'08-Jun'09

**MAD-FRA Fare Evolution by Class (€, 2006-2009)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Business+First Class</th>
<th>Full economy</th>
<th>Discount economy+others</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>668</td>
<td>223</td>
<td>107</td>
</tr>
<tr>
<td>2009</td>
<td>522</td>
<td>208</td>
<td>67</td>
</tr>
</tbody>
</table>

Source: IATA Paxis  
Note: 2009 has been considered as the period Jun'08-Jun'09

Note: route operated by Iberia, Lufthansa, Spanair and LAN Chile
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- **Spanair’s competitive framework**
  - Competition in Barcelona
Barcelona airport traffic increased at a rate higher than 10% until 2007 but is suffering current financial turmoil since 2008.

Source: Aena

(1) 2009E: January – October 2009 Actual + November – December Expected

Note: YTD traffic is decreasing in Barcelona 11.4%
The main markets served from Barcelona airport are domestic and EU.

Source: Aena

(1) YTD: January – October 2009
...which is causing that majority of long haul traffics have to be derived through other hubs

Barcelona is lacking the presence of an airline deploying a connectivity strategy to distribute long haul passengers through its medium haul network

Note: GDP estimation from metropolitan area population and regional GDP
Besides, in the past years the market has been fragmented and there is not a dominating airline.

Barcelona is one of the few major airports in Europe that does not have a first-choice airline.