June 2024

Global Outlook for Air Transport

Deep Change

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This semi-annual report takes a broad look at developments in the airline industry, the context in which it is operating, and the challenges it is facing.

Main takeaways

- The year 2024 is unusually challenging, notably because 4.2 billion persons, a majority of the world's population, will go to the polls in as many as 70 countries – an unprecedented occurrence. Many of the elections will take place in a polarized setting and many will be less than free. Policies could change significantly, and weaken our global capacity to address systemic problems, and to deliver economic growth and improved welfare for all.

- This will likely take place against a backdrop of still very tight labor markets, in turn contributing to prices being sticky and inflation taking longer to drop within central banks' target range. Policy interest rates will therefore not fall as rapidly or by as much as many might expect in 2024. Higher for longer policy interest rates in the US will keep the appreciating bias in the US dollar against most other currencies – a feature that is of course growth-dampening for most countries and which adds costs to all USD-denominated debt and invoices for non-USD based businesses. For airlines, this of course adds to the already high oil price by pushing up the local currency price of fuel.

- Thanks to solid and persistent demand for air transportation, our industry can now turn the page on the Covid-pandemic. Traffic has caught up with 2019 levels, and profitability has returned to the industry. To be sure, this is a laudable feat. While the trend is will in all probability stay positive regarding both growth in activity and profitability, the pace of improvement is likely to slow. A key variable to watch is unemployment which could challenge the trend were it to begin to rise. In the interim, gains will also be capped by capacity constraints pertaining to labor and aircraft.

- The airline industry matched 2019 levels of Revenue Passenger Kilometers (RPKs) as of February 2024. This year, we expect 11.6% growth in total RPKs and an increase of 10.4% in the number of global passengers. Asia Pacific will lead the growth among the regions, contributing to more than half of the global net gain in passenger numbers by 2043. The different air transportation needs across the regions and the industry's ability to respond to them will continue to drive change across the global network, change that was set in motion already by the Covid-pandemic and by geopolitical developments. Traffic numbers are back at 2019 levels, but the nature of the connectivity provided is changing.

- Air cargo of course faces all the challenges common to the industry as a whole, but it is uniquely exposed to trends in manufactured goods trade and to all the related policies. There is a global increase in steps taken by countries to restrict international trade by different types of measures, including raising tariffs. Despite this difficult context, 2024 has seen growth in trade accelerate from a difficult 2023. Cyclical indicators point to further improvements in the second half of this year, helped by booming e-commerce and disruptions in maritime shipping, both of which favor air cargo. Global air cargo traffic is expected to grow by 5% in 2024.

- Thanks to the anticipated growth in passenger and cargo traffic, the industry's revenue should increase by 10% and nearly reach the evocative USD 1 trillion mark. The top-line development will benefit not only from the traffic volumes but also from higher passenger yields. Cargo, on the other hand, will see a decline in revenue as the expected drop in cargo yields will outweigh the increase in Cargo Tonne Kilometers (CTK). The bottom line is projected to generate a net profit of USD 30.5 billion in 2024, with a 3.1% net profit margin and a 6.0% operating margin.

- With such slim margins, the industry's profitability is still fragile, leaving meagre buffers with which to absorb the rising costs of climate change and decarbonization, and the many other potential sources of additional costs or threats to activity. Moreover, compressed margins in a context of generalized cost increases will impede the strengthening of balance sheets that still carry excess debt since the Covid pandemic.

- Airlines are committed to deliver net-zero CO2 emissions in air transportation by 2050. Addressing aviation's energy transition could not only bring about emissions-free air transportation but create win-win situations across the air transport industry and the transportation sector, across entire countries, regions, and the global economy, and this of epic proportions. Providing access to sustainable, abundant, and cheap energy for all will transform every human activity. Airlines cannot achieve this on their own because no industry or country can. Together though, it is for sure, definitely, 100% do-able.

1. Deep Change

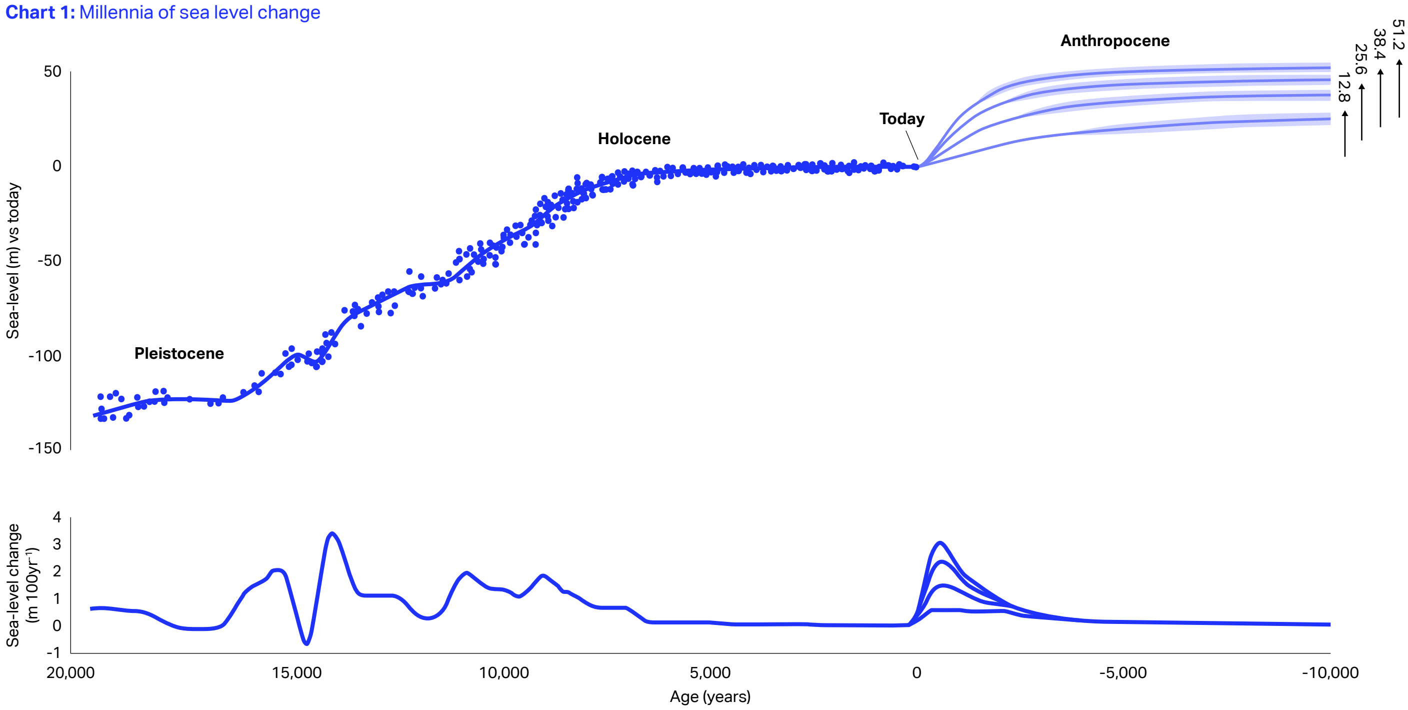
Heraclitus, the ancient Greek philosopher (born around 540 BC), famously proclaimed, "There is nothing permanent except change". It ought to surprise us little then that change is still upon us. The difference a few thousand years make is that the pace of change seems to be accelerating, and that the change to come could prove to be unusually profound.

Climate change

For the past 6,500 years, average sea levels were so stable that they came to be taken as a constant, as far as human endeavors were concerned (Chart 1). This stability coincided with and enabled the emergence of our civilization. Since around 1900, the average sea level has risen by 20 cm (about 7.87 in), according to NASA[1], and half of this rise has occurred since 1993. This climate fact alone tells a compelling story about the deep change our global economy will face going forward.

Weaning the global economy off its dependence on fossil fuels must be everybody's most overarching priority. While undoubtedly an unprecedented challenge, the world has experienced energy transitions several times over. The unusual aspects of the current situation are the ubiquitousness of fossil fuels, involved in nearly all human activities, and the speed with which replacement renewable energies need to be developed. The good news is that such technologies exist, and that financing appears feasible in the absolute. The part that has yet to deliver on its necessary and cataclysmic role is that played by our political leaders. There is a lack of will, determination, focus, and coordination, as countries' attention turns to seemingly more immediate threats.

Chart 1: Millennia of sea level change



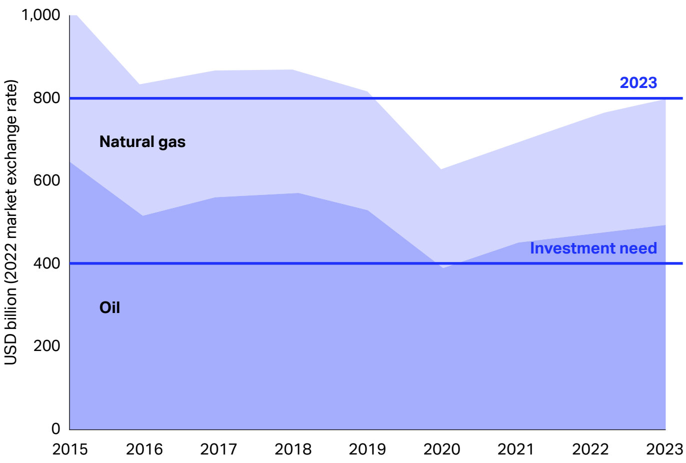
Source: Real Climate

1 NASA Sea Level Change Portal

The oil and gas industry and renewable energy

The oil and gas industry contributes a mere 1% to global investments in renewable energies (Chart 3). Over 60% of this amount comes from only four companies, leaving many thousands of companies in the sector completely absent from taking any part in the energy transition, according to the International Energy Agency (IEA). The IEA also calculates that current investments in the oil and gas industry are twice as high as the amount needed to safeguard the production that will still be required in a net-zero CO_2 emissions world in 2050. This equates to an overinvestment in the industry of USD 400 billion per year which could be redirected to renewable energies and sustainable aviation fuels given the appropriate policy framework (Chart 2).

Chart 2: Investment in oil and natural gas, USD billion



Source: International Energy Agency, "The Oil and Gas Industry in Net Zero Transition", December 2023

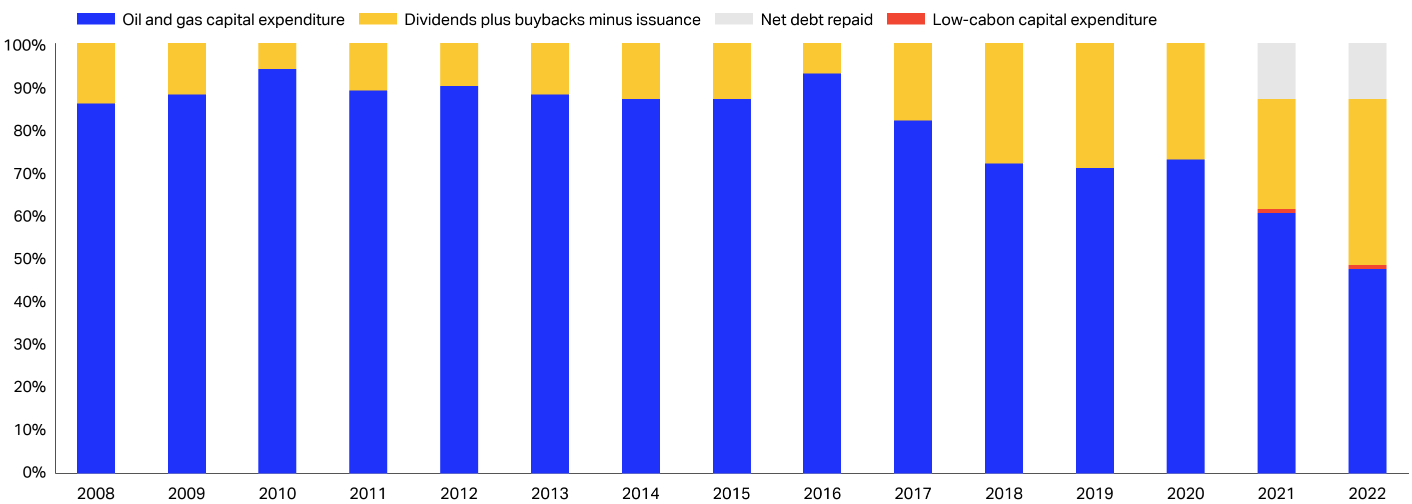
Geopolitics

Wars in Europe and in the Middle East caused all brakes on oil drilling to be lifted. The US, for instance, allowed oil and gas exploration on federal lands again in 2022 after the invasion of Ukraine. 2024 will be a record year in terms of oil production, and the US has become the world's record oil producer [2]. Energy security is at the top of political agendas.

At a time when radical cooperation is required on a global scale, multilateralism is faltering, and the post-WW II institutions are losing influence. A more organic and "self-organized" way of running the world can be seen in the role played by the G20 in global affairs since the group's creation in 1999, and in the emergence of the Paris Agreement in 2015. Many factors have of course contributed to curtailing such global collaboration, including the UK's decision to leave the European Union in 2016, the trade wars of the first Trump administration in the US, and the Covid pandemic, all of which promoted more inward-looking economic policies.

With a majority of the world's population, over 4 billion people, in around 70 countries, representing 60% of global Gross Domestic Product (GDP), being called to vote in national elections as well as in the regional elections to the bodies of the European Union, there is every reason to expect an inward focus also in 2024. As these elections take place in an unusually polarized climate, with strongmen on the rise and political freedoms under pressure, election results can produce starkly different policies. While policy volatility tends to be a break on economic growth and welfare gains at the best of times, it is particularly harmful when there is an exceptional need for global policy coordination to address global challenges that no country can solve on its own.

Chart 3: Distribution of cash spending by the oil and gas industry, % of total, 2008-2022



Source: International Energy Agency, "World Energy Investment 2023", May 2023

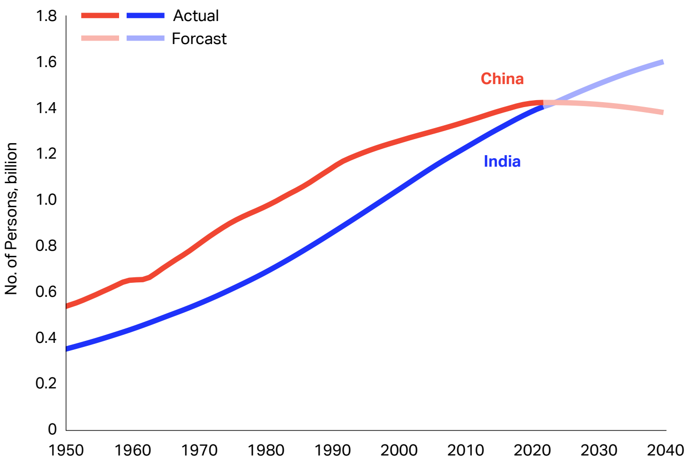
Superpower

Changing demographics and economic heft are also influencing geopolitics. China's population was surpassed by India's in 2023, according to the United Nations[3]. Last year China's population fell by 2 million to 1.40 billion, and India's rose to 1.42 billion (Chart 4). India could become the world's third-largest economy already by 2030, reports S&P Global Ratings, behind the US and China.

It is unlikely that India will follow the same path as China and become the manufacturing hub of the world. The world is now truly a service economy with 67% of global GDP being generated thanks to this sector[4], and India can be expected to continue to excel in this domain thanks to its young and tech savvy workforce. Its economy's full potential will only be realized, however, if a reform agenda can dominate religious and cultural agendas.

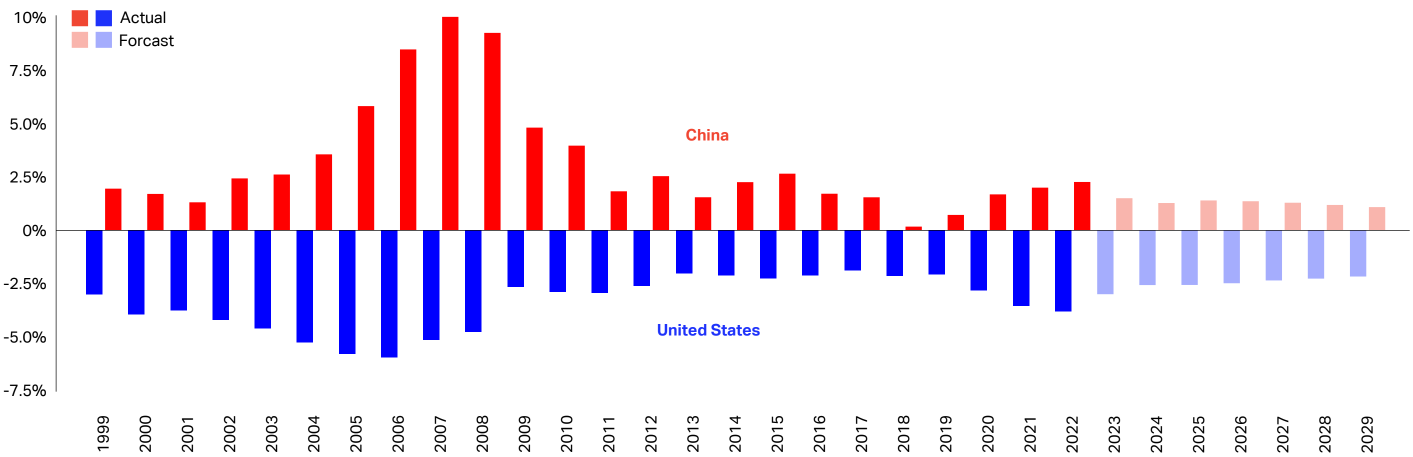
Similar remarks could be made regarding China, where a reform agenda is needed to adapt to the shrinking population, lower demand for housing and construction, and the end of unlimited cheap labor to manufacture the country's exports. China's current account balance showed a surplus of 10% of GDP in 2007. In 2024, it might be as low as 1% and it is expected to continue to decline going forward, possibly turning negative. This is in and of itself not a sign of economic decline – the US' current account has been in deficit since 1970 with only a handful of exceptions (Chart 5). The US has, however, always depended on the kindness of strangers, as Tennessee Williams might have said. Without access to foreign countries' excess savings, the US cannot finance its structural overconsumption, and China's ability to play this important role in the global financial system is waning.

Chart 4: Total population of China and India, billion



Source: UN World Population Prospects, 2022

Chart 5: Current account balance, % of GDP



Source: IMF World Economic Outlook, April 2024

3 https://www.un.org/en/desa/india-overtake-china-world-most-populous-country-april-2023-united-nations-projects#:~:text=24%20April%202023%20%2D%20China%20will,the%20population%20of%20mainland%20China

4 WTO, 2021 data