

U.S. Airline Industry Headed Toward 'Catastrophe' at Current Oil Prices

2008-06-17

Several Airlines Likely to Fail, Affordable, Frequent Air Travel and Jobs at Risk

At current oil prices, several large and small U.S. airlines will default on their obligations to creditors beginning at the end of 2008 and early 2009, according to a study issued today by AirlineForecasts, LLC and the Business Travel Coalition. The study shows that \$130/barrel oil prices will increase yearly airline costs by \$30 billion, while airlines will be able to generate only \$4 billion in fare increases and incremental fees. The implication of this alarming trend is that several large and small airlines will ultimately end up in bankruptcy, and of those, some will be forced to liquidate.

For a full copy of the study, go to <http://tinyurl.com/6qhh99>

"If oil prices stay anywhere near \$130/barrel, all major legacy airlines will be in default on various debt covenants by the end of 2008 or early 2009," the study conducted by AirlineForecasts for BTC states. "U.S. commercial aviation is in full blown crisis and heading toward a catastrophe."

"Airlines are the primary source of inter-city transportation, critical to national and local economic development, the flow of human capital, movement of just-in-time parts for manufacturing, perishable food and other goods critical to our economy," the study says. "With airlines gravely threatened, so is our economic well-being."

Findings:

The top 10 U.S. airlines will spend almost \$25 billion in higher fuel costs this year over last year when jet fuel averaged \$2.11 per gallon. Fuel hedge benefits could offset \$5 to \$6 billion of the increased fuel costs.

Earnings for the group, when one-time reorganization charges are removed, were less than \$4 billion in 2007, the only year of profitability this decade. The group could lose as much as \$9 billion over the next 12 months if the current range of oil prices holds.

Industry fares will have to increase at least 20% -- across the board and on average -- just to cover the dramatic gap-up in fuel costs from 2007. This is not possible given the level of uneconomic seat capacity in the system today.

The upshot of higher fares is less traffic, and given a reasonable estimate of price elasticity, the industry will eventually be forced to shrink its seat capacity by 15% to 20%. However, there is no guarantee that a transition to a smaller, more expensive (for the consumer) airline industry would be successful and sustainable.

Airlines have the ability to raise some cash, and moreover, suppliers such as aircraft manufacturers, leasing companies and travel management companies will have an incentive to support large airlines that provide a stream of value. Nevertheless, without a swift reduction in the price of fuel, the industry is headed toward a massive failure that will result in more bankruptcies, including liquidations.

"The U.S. airlines, and those who depend on them, are watching with growing alarm as their cash reserves fall precipitously toward zero as the price of oil, already at unsustainable levels, continuously spikes into uncharted territory," the study says. "These airlines have never faced a darker future."

"Brand name legacy carriers that we and American communities from coast to coast have depended upon for decades to provide us with affordable, frequent air service are running out of cash, and therefore, toward a date with bankruptcy and liquidation," the report warns.

"Airlines can attempt to radically shrink the industry," the study states. "But given the competitive situation they face, it's highly unlikely that they will have the ability to reduce capacity to levels that will allow all of them to survive. Instead, absent direct policy intervention, the likelihood is several airlines will fail."

"Stabilizing this ailing industry must become a national policy priority," the report states. "Many Members of Congress, federal regulatory officials, state legislators and Governors have yet to fully appreciate the devastating impact an oil-crippled airline industry will wreak on our culture and our national and local economies."

This article comes from Travel Industry Wire

<http://www.travelindustrywire.com>

The URL for this story is:

<http://www.travelindustrywire.com/article33093.html>

© 1998 - 2008 Travel Industry Wire and the author.

Advertisement



THE KNOWLAND GROUP
www.KnowlandGroup.com
See What All the Buzz is About...