

Easyjet Q3 Results 24 July 2013

Speaker key

OP	Operator
CM	Carolyn McCall
CK	Chris Kennedy
DO	Donal O'Neill
SF	Steven Furlong
NG	Neil Glynn
TM	Tim Marshall
AL	Andrew Light
JC	Jarrold Castle
AD	Annad Date
AN	Andrew Lobbenberg

OP Good morning, ladies and gentlemen, and welcome to the Easyjet Q3 results conference call, hosted by Carolyn McCall and Chris Kennedy. My name is Andrea and I'll be your coordinator for today's conference. For the duration of the call you will be on listen-only. However, at the end of the call you will have the opportunity to ask questions. If at any time you need assistance, please press * 0 on your telephone keypad and you will be connected to an operator.

I'm now handing you over to Carolyn McCall and Chris Kennedy to begin today's conference. Please go ahead.

CM Thank you. Good morning, everybody. Thanks for joining us to discuss our IMS for the third quarter of 2012/13. In the room, as you've heard, are Chris and myself, obviously; also Will, Rachel and Tom, who you all know as well. You'll have been sent the slides along with the statement and the slides are available also on our corporate website. I intend to keep the presentation quite short this morning to give time for any questions that you may have.

If you look at slide two, the performance in the quarter has exceeded our expectations, largely due to continued benign capacity environment for Easyjet. Competitive capacity was down 1.2% on our routes with notable reductions in Italy and in Switzerland. I'll go through the performance now in a bit more detail.

If we look at slide three, revenue continued its strong performance and we've seen that this year we've benefitted from the introduction of allocated seating, improvements to CRM and also we've improved our mobile offering and we have optimised further the revenue management system.

We would not expect such a large increase in revenue in the next financial year from these factors. Q3 revenue per seat grew by 6.1% on a constant currency basis and by 6.7% on a reported basis to £61.44. Load factors were 88.2% in the quarter, a decline of 0.9 percentage points, a reflection of the timing of Easter which fell on 31st March, a week earlier than in 2012. Our capacity grew by 3.6% in the quarter. Selective capacity growth

was focused on markets with the potential to generate the greatest returns, such as the new French regional bases and new network points like Moscow.

Easyjet's average sector length increased by 0.7% and this was driven by longer routes such as the Manchester-Moscow and the Gatwick-Moscow, routes to Sharm from the UK and Milan and increased frequency on the Luton-Tel Aviv and we've also added Manchester-Tel Aviv.

Turning to slide four, the strong revenue performance, as I said, was largely driven by seat revenue which grew on a per-seat basis to £60.38, an increase of 6.1% at constant currency. Seat revenue benefitted from continued competitive retrenchment with competitors' capacity, as I mentioned, declining 1.2% or 0.5 million seats, a one-off step change from the reallocation of capacity from the Madrid base, and allocated seating which drove approximately one percentage point of the underlying RPS increase.

I mentioned that we continue to derive improvements in our digital platform, our mobile platform. What I mean by that is that we are rolling out mobile boarding passes. That's progressing well. It's now live in 50 airports with over 250,000 passes downloaded since launch. In April our iPad Inspire Me app launched and our new and innovative flight tracker with live updates is now available through our mobile app. It's a key part of our commitment to keep customers informed when they're on the move.

Other initiatives include Easyjet's new online check-in process, integrating our cars and hotel partners into the mobile home page, and also developing a Chinese-language web home page.

In the quarter Easyjet made progress on the business traveller initiative, including improvements to Travel Port's [?] Galileo booking system, which we had been, waiting for, and further details with European public sector bodies including the German Government.

In the quarter business passengers increased by 4.2% compared to Easyjet's overall passenger growth of 2.6%. Easyjet's made steady progress on the business passenger side, as I said, but I'd like to remind you it is a long-term strategy and it will take time to deliver. Non-seat revenue per seat at constant currency in the quarter rose 9.4%, driven by the improved in-flight offer and the benefits from new partners' product such as hotels.

Turning to slide five on cost, I just want to spend a little bit of time on this as this is an area of significant focus for us, as you would expect. As expected, there was significant year on year airport cost inflation in the quarter, which was partially offset by Easyjet Lean savings. Airport costs contributed almost 4% of the 4.5% constant currency cost increase. Around 0.5% of the constant currency increase was driven by the combination of increased de-icing costs well into April and May of the year and significant disruption in the quarter from the French ATC strike in June. Overall, total disruption costs increased £6 million year on year in the quarter.

The French ATC strike in June led to 521 direct cancellations. It's estimated that a further 40 sectors were cancelled due to crewing and displaced aircraft. The French ATC strike was significant for us not only because of its impact in France but also because 63% of Easyjet flights fly through French airspace.

In the quarter Easyjet cancelled 746 flights compared to 425 in the same quarter last year. Easyjet now has an improved capability to manage disruption and recover performance, as evidenced by our industry-leading on-time performance at 88.9% in the quarter. As you are aware, inflationary cost pressures are partially offset by Easyjet Lean savings. We remain on track to deliver £135 million's worth of cumulative savings by the end of this financial year. In particular, improvements have been made to ground handling contracts and other initiatives such as lightweight seats.

Now I'm just going to hand over to Chris.

CK Thank you, Carolyn. Turning to slide six and moving on to the detail of our hedging positions for fuel, US dollar and Euro, all the positions are within broad policy. We've now got 85% of our remaining 2013 fuel requirement hedged at \$974 per tonne and 67% of 2014 at 984 per tonne. We continue to pursue the policy of using hedging to smooth the impact on cashflows of changes of fuel and foreign exchange rates.

Taking into account the hedges currently in place, a \$10 movement in the fuel price impacts PBT by \$800,000. A 1c movement in the dollar rate impacts by £500,000 and a 1c movement in the Euro by £200,000.

Looking forward, forward bookings are in line with prior year with 73% of H2 seats sold. And now I'll hand you back to Carolyn.

CM Cheers, Chris. We're on slide eight now. You'll have seen our outlook in the RNF. With 73% of the summer seats now booked, revenue per seat at constant currency for the second half is performing better than expectations set out at the time of the half-year results. It's now expected to increase by up to 6% compared to the second half of the prior year. ASDI [?], ie, seats flown in the second half of the financial year is expected to grow by 3.3% year on year, assuming no further significant disruption.

Costs ex fuel at constant currency are performing in line with management expectations and are anticipated to increase by 4% per seat in the second half of the year, again assuming no significant disruption. It is estimated that at current exchange rates and with fuel at \$985 per metric tonne, Easyjet's fuel bill for the second half of the financial year will be around £900 favourable year on year. Using current rates it's estimated that year on year exchange rate movements, including those related to fuel, will have an adverse impact of around £10 million in the second half of the financial year.

Easyjet is performing strongly, driven by a combination of management initiatives and a benign capacity environment for Easyjet in 2013. Therefore the board expects that pre-tax profits for the year ended 30th September 2013 to be between £450 million and £480 million, assuming no further significant disruption.

So to conclude, Easyjet continued its strong performance in the quarter driven by initiatives such as allocated seating, improvements to mobile and to the revenue management system and a benign capacity environment for Easyjet. We have also benefitted from the one-off reallocation of capacity away from the Madrid base.

It is clear that we remain a structural winner in European short-haul aviation and we remain well positioned to deliver returns and profitable growth for our shareholders. Thank you for listening to all of that and now over to you for questions.

OP Ladies and gentlemen, if you would like to ask a question please press * 1 on your telephone keypad. If you change your mind and wish to withdraw your question please press * 1 again. You will be advised when to ask a question.

The first question comes from the line of Don O'Neill from Goodbody [?]. Please go ahead.

DO Hi, guys, good morning and congratulations on a very good set of results. My first question's in relation to the net cash position, which was very, very strong. Obviously some of that's reflected from the strength of bookings and pricing, I guess, but also in terms of the sale and leasebacks. Could you quantify what proportion of the contribution was from sale and leasebacks?

And my second question is, in terms of the capacity focus in Q3, should we expect a similar capacity focus in Q4 or will there be any further reallocations across the network? That's it, thanks very much.

CM I'll get Chris to take the cash question.

CK Yes, Donal. I don't have the – because we've done sale and leasebacks over the course of the year and we've done the 12 A320s and the 12 A319s so that's built up over the course of the year. What I can say is that the bookings reflect where we are at the moment so you've got the [unclear] in there and in terms of the net cash position, clearly we're going to have the pre-delivery payment on the new fleet deal going out in Q4 as well.

CM And on the capacity side really there's nothing as big as the Madrid reallocation of capacity because we had eight aircraft in Madrid which we've taken out and we reallocated all of that. That really kicked in in this quarter so there's nothing as substantive as that in terms of reallocation of capacity but we are constantly looking at where our capacity's working hard and driving returns and where it's not doing that. So that's a constant and continual process but it's not of the scale of Madrid.

DO Thanks. I just need one more question, if I can, on allocated seating. Can you tell us, is the vast majority of allocated seating booked at the time of booking or is it booked just before the flights, close to the flight time?

CM We'll give you far more detail on allocated seating at the full-year and it's hard to see because there is a difference between the summer and the rest of the year in terms of allocated seating trends, in terms of what you've just said, when people book. So let us come back to you on that because I don't want to say something that'll only apply to July and August.

DO Sure, no problem. Thanks very much.

OP The next question comes from the line of Steven Furlong from Davey [?] Research. Please go ahead.

SF Hi, Carolyn, Chris.

CM Hi, Steven.

SF Picking up something on allocated seating, not on timing but I know the focus maybe in 013 was on ensuring efficient roll-out across the network. Are you just surprised maybe that the revenue kickers have become early? I know there was a focus maybe on yield managing perhaps in 2014. Do you think it's more potentially a 2013 event?

And then just a final question is the back end of the summer. I was just wondering, do you think it's a bit harder comp with the post-Olympics, certainly in and out of the London market and from last year maybe with the weather as well? Just might make some comments.

CM Yes. Let's be clear on the 2013/2014 thing. If you're talking financial year then...

SF Yes.

CM Yes, in terms of 2013/14 financial year, so starting October, we will start yield managing. We will not do that before the new financial year because we want at least a whole summer and, as much as possible, a year's data so that we can actually see what the trends are in allocated seating because that's the way we'll maximise that yield as best as possible. So we will start, towards the end of this year and certainly into 2014, yield managing allocated seating.

On the harder comps, you're absolutely right, the September comps are going to be very, very tough indeed because just remember last year there was obviously the Olympics in July and everyone said, no, well, the Euro – everyone across Europe stayed put. So September was very, very strong last year so, yes, harder comps and the weather is, I think, a particularly UK phenomenon actually, is what we are seeing, in that when the weather was bad and we had that very helpful forecaster who said that the summers were going to be bad for the next ten years, there's no question we saw a real increase in our bookings; it was very good when the weather was bad.

Conversely, with a heatwave you see a flattening out of the curve but the bookings are buoyant so you've just got a balancing effect with the weather in the UK and we've taken that into account in the guidance we've given you.

SF Very helpful, thank you.

CK Steven, also just to remember, that really strong September then ran into October as well so October will be a hard comp as well.

SF Got it. Thanks, Chris, thanks, Carolyn.

CM Okay.

OP The next question comes from the line of Neil Glynn from Credit Suisse. Please go ahead.

NG Good morning, Carolyn and Chris. If I could ask first of all a question on labour, you've referenced within the IMS the lifestyle deal in Italy and also the UK pilot agreement. Are there significant stepping stones that we can think about over the next six months or so in terms of additional labour deals to be done hopefully?

And then a second question just on non-seat initiatives. Obviously we'd seen a near-10% growth in, I think, unit non-seat revenues. Can you give us some kind of understanding in terms of where you are relative to where you'd like to be? I appreciate it's clearly a continually evolving process but you've obviously mentioned a hotel deal and in-flight improvements in the third quarter.

CM Okay. On our pilot deals and cabin crew deals, yes, I would say we're making steady progress with all of them. The UK deal was not a pay deal; we're still negotiating that now. What it was was the new mentoring [?] contract deal but yes, after two years of negotiations we've come to a conclusion on that so that was very good news.

I think what we are doing is talking about lifestyle in every single market that we operate for pilots because it's something that our pilots want and it's something that helps us with the inflationary cost increases of our crew cost base. So we are working on that but there's nothing particular to report on that as an exceptional item that might be coming up in the course of the next six months.

CK And then, Neil, on the non-seat, definitely hotels are performing well now. We're fully integrated with bookings.com and the work that Peter Duffy and team have done on the booking process is definitely helping with conversion so in answer to your question, we're exactly where we want to be. We should finish the year about flat year on year so we're finally... I think for a long time people have been asking, when are we going to offset the insurance decline? And I think this is the year where we offset it and then you'll be able to see some modest growth in that in future years.

NG Great. Could I just round back on the labour side? Is it possible to give us an understanding as to what proportion of pilot contracts are currently lifestyle deals, if you will?

CM Yes, very small. It's only Italy where we have a lifestyle deal.

NG Great, thank you.

OP The next question comes from the line of Tim Marshall from Redburn. Please go ahead.

TM Morning, everybody. I just have one question which is about the FX impact. It was negative 35 million in the first half of the year and you're saying it's going to be negative ten million in the second half. My understanding is that that reverses next year. Can you just help me understand a little bit how that progresses into FY14 with the strength of the Euro?

CK Tim, I think there are two factors at work, you've got Euro and dollar. Part of the adverse this year is dollar and clearly that is going to increase next year if dollar stays where it is because it's been very benign at the 160 level for most of this year. On the Euro, it really depends what happens to Euro next year so if Euro is flat then substantially there will be a benefit on the Euro for next year. But as you know the reason we... In terms of that 35 in the first half, that was the year on year impact so you've got two factors at play.

Remember that last fiscal year the Euro was strong and then weak so we had a real tailwind in FY12 and then we had a headwind in FY13 because it went from weak to strong. So you

can't expect the full reversal next year because part of that 35 is a year on year impact and actually it all depends on how the Euro moves next year because this is assuming that – all of your modelling will be if it stays flat the entire year. Who knows actually, with fluctuations within the year?

TM I was tempted to ask what the weather forecast is for the next couple of weeks but instead of that perhaps I'll ask; just clarify that your guidance is taking into account that the heatwave's going to continue to have downward pressure on short-term bookings. Is that fair?

CM It's a range precisely for that reason, because we have no idea what the weather's going to do and nor do you so none of us have a clue whether this is going to remain or not, which is why we've put a range of guidance in which we feel confident we will deliver.

TM Perfect. Thanks very much.

OP The next question comes from the line of Andrew Light from Citigroup. Please go ahead.

AL Hi, good morning. A couple of questions; first of all, are you seeing much of an impact from Norwegian's new base at Gatwick since April and also, I think, in three Spanish locations as well? And secondly, I'm just wondering the performance of your relatively new routes to Russia and Tel Aviv; are they any different from the rest of the network, do you see those areas as a good opportunity for future growth given – or rather, despite bilateral restrictions?

CM On Norwegian, no, we're seeing no impact in our trading at all from the Norwegian stuff. Obviously we monitor it very closely; we're keeping a very beady eye on it but at the moment, no impact on our pricing or bookings. Moscow/Tel Aviv; both really doing well; Gatwick-Moscow doing very well; all our Tel Avivs are doing well. So I think you will see us, because of the open skies agreement now with Israel, you will see us connecting much more of our network with Tel Aviv and that will be a priority for us because we know that that is a good, strong route for us.

I think on the Moscow I would say that's much longer-term, the bilaterals are more difficult and so at the moment we have no intention of expanding Moscow to anywhere else in the network, we just consolidate what we're doing.

AL Great, thanks very much.

OP The next question comes from the line of Jarrod Castle from UBS. Please go ahead.

JC Good morning, three if I may. Firstly, just on Easyjet Lean, I think at the half-year you had delivered 125 million. You're guiding for 135 for year end. Can you say where you are in terms of the nine-month and also if at some point maybe we could expect the 190 million target to maybe go a little bit higher?

Secondly, do you have any comments in terms of what you're seeing on calendarised Q4 capacity? Clearly Ryanair's bringing in quite a lot. There are some indications that maybe some of the flags are reacting to that, etc. Are you seeing anything which makes you feel that maybe some of the short-haul discipline is not there?

And then just lastly on the constant currency per seat guidance, you're talking about H2 up 6%. You obviously did better than that in Q3. Is the caution related to September or potentially could we see more than 6% based on what you're currently seeing? Thanks.

CK On Lean, Jarrod, yes, we've got the 135 for the year and I think what I'd like to emphasise...

CM I don't know where you got the 125 from Jarrod

CK Yes, but for me, Lean is a continual programme so the 190; that's at a point in time. We will continue to deliver savings every year, that's the purpose of the programme so right now we're putting the plans together for 16, 17 and 18 so that we can deliver those double-digit millions of savings each year. So we'll just keep going, innovating and doing what we can to drive out waste.

CM Can I just build on that just a sec, Jarrod because the 190 million was not something that we've – we need to talk to you offline about that because I'm not quite sure where that's come from. So as Chris said, it's embedded in everything we do, it's a unit cost programme reduction. We don't set targets like big pots of money because what we found when we got here is that although we were achieving targets like 90 million, 100 million, 120, whatever it was, actually unit costs were going up.

So what we try very hard to do is not put targets like 190 million out there internally. We actually say we want to see unit cost reductions, ie, from inflation so we target unit cost rather than one great big pot of money. Now, of course, that cumulatively makes a big pot of money, £135 being the example of that. Do you see what I mean?

JC Sure, thanks.

CM Chris, do you want to go here? I'll talk about the calendarised capacity in Q4. I'm not sure it is entirely about ill-discipline suddenly coming back into the market. I think what is happening is that Ryanair have made statements about binning [?] less through the winter and expecting to grow 5% over winter and about two to 3% over summer. Of course, then you've got Norwegian's expansion plans, basically. I still think you're seeing quite a lot of capacity restriction and containment around the flags so just as an example, we would see Alitalia has come out of Malpensa and that is not going to go back in, we don't see that reversing in anyway.

So capacity in H2 as a whole for Italy in terms of our competitors; mainly Alitalia's down 11% in H2. Switzerland is down 6.5% so I think you've got an offset from the flags where they are restructuring and they are retrenching and I don't see that really reversing. Does that make sense?

JC Yes.

CM I think there will be less – if you had to ask me today, it's hard to know what is going to happen exactly next year but I would say that the capacity environment will not be quite as benign for us as it has been this year. This year has been an unusually benign capacity environment for Easyjet, which we have taken full advantage of. I think next year, because

of the Ryanair and the Norwegians and the Wellings [?] all in expansion mode, it's going to be a tougher capacity environment for us, if that makes sense.

JC Sure, thanks.

CK And then on the outlook for the year and for H2, the guidance is up to 6% so 6% is right at the top end of where we think it might be. That is all down to those really tough September comps. As Carolyn said, we saw a big wave of late bookings from the middle of August all the way through to the end of September and late bookings obviously are very valuable to us because they tend to be high-priced. So that's why we've got that big range, because those comps really are very tough for Q4.

JC Okay, thanks very much.

OP The next question comes from the line of Anna Date [?] from Deutsche Bank. Please go ahead.

AD Hi, morning, everyone. I've got three general questions, if possible. The first one is, you've been talking about the open skies that are there with Israel. Do you see any other open skies opportunities potentially coming up that would be of most interest to you or is there anywhere that you would particularly see as a good market that you would like to open up?

The second question is, I know, Carolyn, you were talking about businesspeople being the medium-term driver. Do you think there's anything more you can do to get businesspeople to fly Easyjet, can you speed up that process in any way, do you think?

And then lastly – I know this has been asked before but is there a fair spread to your flag competitors that you would like to maintain? For example, if BA is charging 100 between a city pair, do you see any elasticity developing at, say, 80 or is it 90? I'm trying to think, theoretically, is there a fair ceiling above which people become a bit indifferent? Thanks.

CM On open skies, I think some of the bigger ones have already materialised for us. There are always some outliers that we would be interested in; Tunisia is a good example of that. But I don't think there's anything material out there on a bilateral or an open skies agreement that we would be targeting right now.

On the business passenger, actually I genuinely don't think we can accelerate that by spending a bit more money or investing in any other way. We've taken a decision not to go full GDF. That is the right decision for Easyjet because we have other priorities from an IT point of view and also because from a commercial model point of view it is a different model. Therefore we are partial GDF and we are reliant on Amadeus, Travel Port and Savour [?] to provide technology that makes us easy to use. Amadeus is coming in in July. Its soft launching and it'll be live launched in September. You heard what I said about Travel Port.

So we are now putting the last piece of that jigsaw in place. Actually the really big thing now for us is to change the mindset of people in both travel management companies and in corporates. That's the big heave-ho, that's where we have to put the effort. It's all about getting them to change the way they think about business travel and that takes time. That is not going to be something we can just achieve by putting a bit of money into it and turning it around in six months.

So that's why I say, this is a long and quite bumpy road because it's cultural change but it's doable and we're making good progress.

CK Then on your question about the fair spread, our pricing model is very different so we adopt a dynamic pricing model so periodically the legacies will try a pricing strategy like 100 destinations for £100 or Swiss doing their 50-franc fares or Air France doing their no-bag fare. But they are on a limited number of routes and for a limited period of time. The legacies come on and then they'll pull off again and move their offer somewhere else.

So by having dynamic pricing we naturally always maintain what the consumer is saying is the right fare because we're constantly reacting our pricing to the elasticity at any point in the booking curve. So in answer to your question, the algorithm is dealing with all of these limited offers on a daily, hourly...

AD Ad hoc basis, almost.

CK It's not ad hoc, it's continuous, and it's absolutely continuous.

CM Continual pricing, effectively.

AD Sorry, Carolyn, just one more thing, on the businessperson; I think this has been brought up before but have you ever looked at potentially leasing lounges at airports or anything like that?

CM That wouldn't be very cost-efficient for us so again, anything that adds cost to this would not really be in our...

AD You're just not interested.

CM In our thinking. We're looking at innovative ways of doing that, however. I won't mention what we're doing but we have some innovative ways of [inaudible] that and I hope soon that we will be able to talk about what that is.

AD Okay, lovely. Thanks, guys.

OP Your next question comes from the line of Andrew Lovenberg [?] from HSBC. Please go ahead.

AN Hi, Carolyn, hi, Chris. I'm tempted to wonder how the sales of suntan lotion are going on board and whether there's good money there. But otherwise, I wondered if you could comment on the prospective merger in the handling market between Service Air and Swiss Port [?]. I know Menzies is your main handler but you're very reliant on outsourced handling and so the effectiveness and competitiveness of that sector is important for you.

Could you comment on the launch of Linate Fumincino because you commented on Rome and Tel Aviv so I just wondered how that was going? And then are you any further along planning for your new portfolio of slots at Gatwick and when do they get redeployed and into the market?

CM We welcome the merger between Swiss Port and Service Air. I think it's a highly fragmented industry, as you know, ground handling and from our point of view that consolidation is really good because we deal with both of them currently and it means that we are able to affect and influence what goes on in terms of the training and the customer side and all of that; it's just far easier dealing with one than two and that should drive efficiency so I think it's good news for us.

On the Linate Siomettino, Andrew; far too early to call, it's very, very early days. It was never going to be an easy route for us given that Alitalia have as many frequencies as they have. That's their route, it's been their monopoly. We need to increase our saliency in Italy on the business travel side as much as anything else. Again, we're making good progress on that. It's just very early days so that's that.

On the slots at Gatwick, I'll let Chris talk about this but just remember, it still has to go through shareholder approval before we start getting – we expect it to go through but it's July that it'll go through Flybe's shareholders and we're optimistic about that.

CK Yes, Andrew. We haven't got the slots because the Flybe shareholders need to approve. They will obviously fly them this summer and into next winter and then we'll start scheduling for next summer, which isn't on sale yet. So, as you'd expect, in anticipation of getting them we're doing a fair amount of planning on where we can use them and obviously we did that before we came up with a price for them.

So it'll be the summer schedule when you'll start to see that. I think the only one we have confirmed is that we will fly Inverness if we get the slots.

Perfect, thanks.

CM Okay.

OP We currently have no further questions in the queue so as a reminder, please press * 1 on your keypad to ask a question.

Just a final reminder, please press * 1 on your keypad to ask a question.

There are no further questions so I will hand you back to Carolyn and Chris to close today's conference.

CM Thanks very much, everyone, for listening and for your questions and have a good rest of the summer. Bye for now.

OP Thank you for joining today's conference call. You may now replace your handsets.