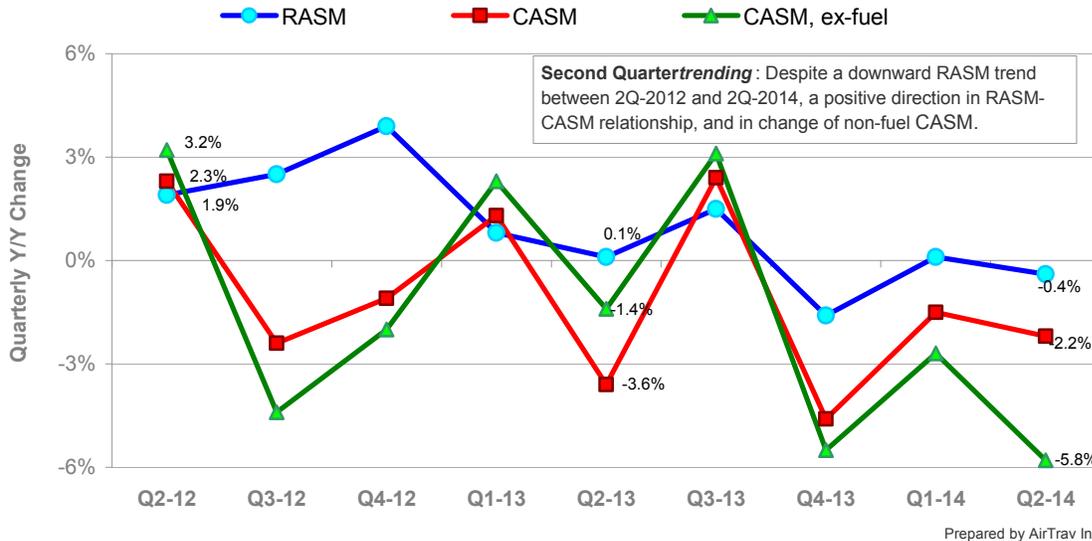




AirTrav Research Flash – Air Canada Second Quarter 2014
 Unit financial trending and seat densification efforts

May 13, 2014

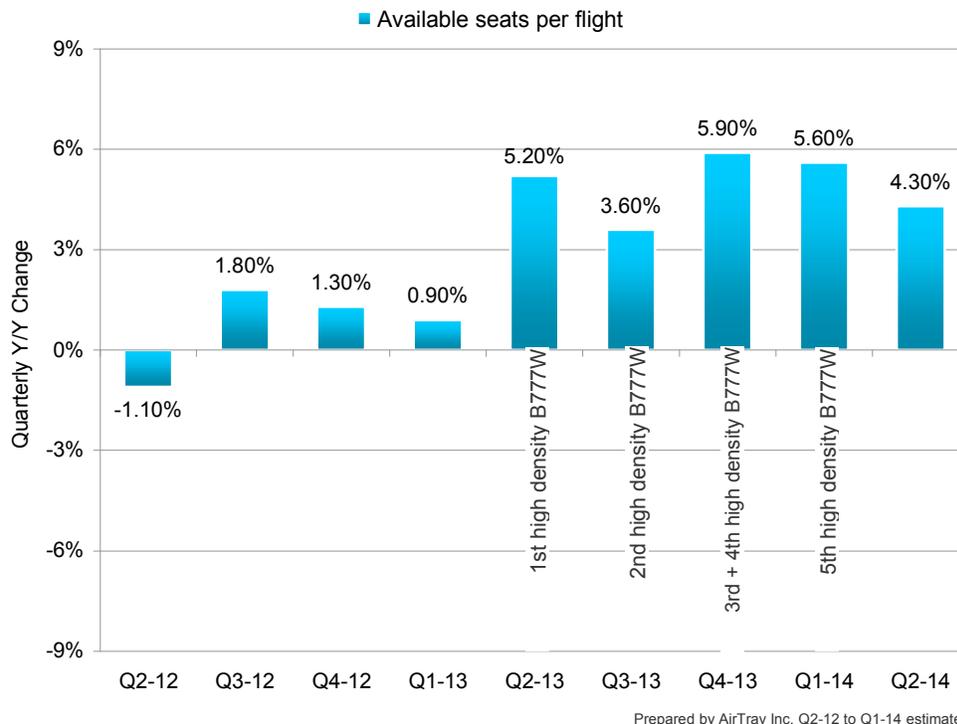
9QTA trending of key unit financials (TSX: AC.A, AC.B)



The text box in the graph says it all. Despite a downward trend in RASM (which, though not shown here, essentially mirrors a downward trend in Yields), CASM and ex-fuel CASM in particular have been falling at rates faster than RASM. As a result, Operating Income has been improving.

Seat densification efforts – quarterly trending of average seats per flight

9QTA Densification Trending (TSX: AC.A, AC.B)





There are several reasons why the average available seats per flight (note, this is per flight, not per aircraft) can rise. For example, the mix of deployed aircraft in the fleet affects this average. That said, we believe that Air Canada's introduction of a three-class, high-density Boeing 777-300ER (ICAO code: "B77W") is having a favourable impact on Air Canada. As noted in the above chart, the airline's average number of seats per flight has been increasing at between 3.6 percent and 5.9 percent since the first quarter in which a higher density B77W was introduced (2Q-2013).

The transfer of Embraer 175 aircraft from Air Canada mainline to Sky Regional would not impact the above graph, as Air Canada reports on total flights operated and total seats dispatched across all mainline and AC Express flights.

Note that Air Canada only commenced reporting of "dispatched seats" in 2Q-2014. In prior quarters, AirTrav has estimated dispatched seats, and thus seats per flight, based on other reported data.

In its First Quarter 2014 analyst call this past May, Air Canada announced that it would be re-configuring the remainder of its B777 fleet in a three-class, "higher" density configuration (not yet confirmed if all aircraft will have a ten-abreast economy class and simply a tighter seat pitch due to new slim-back seats).

Also, the gradual replacement of Air Canada's B767-300ER fleet (between 191 and 211 seats per aircraft) with B787-8 Dreamliner aircraft (251 seats per aircraft) will add to the rising densification and related benefits. Even the transfer of B767-300ER from mainline to low-cost sister company Rouge is adding to the densification drive since the Rouge configured aircraft have an average of 272 seats onboard.

Aircraft densification will have an increasingly favourable effect on Air Canada's unit costs and revenues. Not only will there be more available seat capacity over which to spread costs (the focus of most analysts' reports), but incremental revenue creating capacity will be substantial.

For example, on the B777W example alone, the current higher density 349-seat version has 109 more seats than the 289 seat lower-density version. At Air Canada's recent load factors on trans-oceanic routes, this should deliver approximately 92 more passengers per flight. While there are some incremental costs, such as slightly higher fuel consumption and catering due to the higher passenger loads, the net benefit of revenues in excess of costs is significant.