

Air France-KLM profits climb in 'challenging' market

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A favourable comparison point meant a boost in quarterly profits at Air France-KLM, but rising fuel costs threaten to erode earnings

Air France-KLM reported a solid increase in profits Wednesday as more people flew on its network, but growth was held back by higher fuel prices that will put more pressure on the group to find ways to hold down

costs.

The French-Dutch airline said operating profits reached 400 million euros (\$446 million) in the second quarter, up 15.6 percent from a year earlier—when a series of strikes at Air France forced flight cancellations over several months.

The protests by pilots and other staff, which shaved 260 million euros off operating profits in the period last year, ended after the company agreed to lift wages for the first time in several years.

Like other airlines, Air France-KLM is scrambling to keep a lid on costs in the fiercely competitive air travel market, particularly in Europe where low-cost rivals have made significant inroads.

Chief Finance Officer Frederic Gagey acknowledged to journalists in a conference call that the improved earnings "is very much thanks to the end of last year's strike".

Soaring jet fuel costs limited the positive impact, however, and the airline warned its overall fuel bill for 2019 would jump by 550 million euros compared to last year's.

That prospect has prompted CEO Ben Smith, a Canadian who took over as the airline's first non-French leader last year, to pursue a vast fleet renewal programme to reduce its reliance on older, less efficient jets.

On Tuesday, it announced a huge order to buy 60 new A220s from Airbus for its short and medium-haul routes, and said it would stop flying its 10 mammoth A380 superjumbos by 2022 because they were no longer economically viable on long-haul routes.

In a statement, Smith confirmed the group would meet its full-year

target of reducing costs by up to 1 percent, while passenger traffic is expected to continue growing from last year.

"We continue to implement our strategic vision focused on reducing costs and making our group more robust in the very competitive marketplace in Europe," Smith said.

Profitability gap

By airline, Air France's operating profit soared to 143 million euros in the quarter, up from just 13 million euros last year, for an operating margin of 3.3 percent.

At KLM, the higher fuel costs trimmed operating profit to 258 million euros, down 70 million euros from the quarter last year, but its operating margin managed to remain higher, at 8.9 percent.

The profitability gap between the two carriers has long been a source of tension between the group's French and Dutch executives and shareholders.

Those frictions burst into the open this year when the Dutch government unexpectedly lifted its stake in the airline to 14 percent, just shy of the 14.3 percent held by the French state.

The move was prompted by doubts over the alliance's growth strategy, and worries that Dutch interests were being neglected and that Air France pilots and crews were resisting the hard choices needed to streamline operations.

The dispute ended only after executives agreed in March to form a working committee to examine ways to improve the alliance's management.

Low-cost ambitions

Also on Wednesday, Air France secured pilots' backing for a plan to expand its Transavia low-cost subsidiary, a subject that for years has met fierce resistance from its French employees.

Weeks of strikes in 2014 by pilots fearing they would lose pay and benefits if transferred to the no-frills carrier had forced management to agree to limit the number of Transavia's French planes to fewer than 40.

That ceiling will be abolished under the new accord, allowing Transavia to increase its French fleet of 38 Boeing 737s, compared with the 42 operated on the Dutch side.

The unit posted record operating profit last year of 139 million euros with flights serving around 100 destinations in Europe and North Africa.

"The company will be able to accelerate its offensive in the highly competitive low-cost market, departing from Orly and regional French stations," Air France-KLM said.

Investors cheered the results, with shares jumping 8.6 percent in afternoon trading in Paris, far outpacing a flat performance for the benchmark CAC-40 index.

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