Qantas Airways Ltd
Half-Year Results, 16 February 2012
Introduction by Alan Joyce, Qantas CEO

Let me begin with the context in which we deliver our half-year results today.

Competitive realities

Australian companies like Qantas confront three competitive realities.

First, is the ongoing reshaping of global finances.

The painful economic restructuring in Europe is far from over.

We are seeing job losses in the financial sector, including in Australia.

We are continuing to see a significant credit squeeze that is affecting the borrowing costs of Australian banks.

Second, is the rebalancing of global economic weight to Asia, and particularly China.

Australia's resources sector is a prime beneficiary of this shift and the Qantas Group is also benefiting, both in Australia and Asia.

Asia will continue to offer significant growth opportunities for Australian companies including Qantas.

Third, and largely due to the two previous factors, we confront a profound transition in the Australian economy.

With our dollar likely to stay at a sustained high value for the foreseeable future, Australia has become a very high cost economy in which to do business.

Many companies, including our own, are grappling with this.

These factors will not go away and are likely to magnify.

At Qantas we know we must continue to adapt if we are to prosper and enhance long term shareholder value.

Last week Minister for Finance, Penny Wong, said that, "We are living through a global economic realignment…we know that change cannot be avoided."

At Qantas we share the Government's view.

That’s why we are confronting the new global realities upfront.

We are making the right decisions to restore, retain and increase our efficiency and competitiveness and enhance long term shareholder value.

Results

Let me now turn to the half year results.

For the six months ending 31 December 2011, the Qantas Group delivered an underlying profit before tax (PBT) of $202 million.

This compares to an underlying PBT of $417 million for the first half in the previous year.

Statutory PBT was $58 million, down from $322 million.

The result highlights the unique challenges we faced during the period, with a $194 million negative impact due to industrial action and jet fuel costs up by $444 million.

It also demonstrates our resilience as a business, with most parts of the Group delivering high-quality and even record performances.

The Group’s yield performance was up 4% - despite the industrial action.

Unit costs, excluding fuel, were down 3%.

Qantas and Jetstar performed strongly during the period.

We remain focused on maintaining our 65% market share which we believe is optimal for the business.

With Qantas Domestic, corporate travel revenue achieved double digit growth.

We signed 45 new accounts, renewed 160 and two were not renewed.

We continue to invest in the renewal of the B737 fleet, and in the product and service upgrades that will ensure we retain our leading market position.

Qantas domestic customers, for example, have been the first in the world to experience Q-Streaming, our trial of inflight WIFI technology.

QantasLink goes from strength to strength.

It was named 2012 Regional Airline of the Year by Air Transport World.

It continues to contribute to, and benefit from, the resources boom, with rapid growth into the key regional centres in Western Australia and Queensland, the expansion of Network Aviation for the fly-in-fly-out market, and three large corporate contracts.

Jetstar achieved a record underlying EBIT (Earnings Before Interest and Tax) of $147 million.

It continued to grow capacity here and overseas; continued to achieve unit cost improvements; is strongly placed for growth in leisure travel in the Asia-Pacific; and Jetstar Japan is now on track to commence operations in early July, months ahead of schedule.

Frequent Flyer also achieved a record result, increasing its EBIT to $119 million up from a normalised EBIT of $107 million last year.

Billings growth was up by 16 per cent compared to the prior period, and membership grew 11 per cent to 8.3 million, reflecting the increasing range of opportunities to earn and redeem points, including the new partnership with Optus. Frequent Flyer remains central to retaining and strengthening our customer relationships.

The damaging industrial action we faced last year is over, and industrial action on that scale is unlikely for the foreseeable future.

Our decision to ground the fleet was made necessary because our customers were being massively disrupted by the unions and the ongoing campaigns by unions were damaging our brand.

It was impossible to deliver our schedule and the business community was starting to leave Qantas.

But after we brought the dispute to a head we saw a rapid positive response in forward bookings, and an upswell of support from customers.

If we had done nothing our brand would have been in trouble.

The action we took, though difficult, was necessary.

Our customer research shows that our brand has rebounded strongly and fast, with a prompt return of forward bookings, underpinned by domestic leadership in on-time performance for every month of 2011 that was not affected by industrial action.

Looking forward, while the global economic situation remains volatile, we remain cautiously optimistic about the demand environment, both domestically and in the Asia-Pacific region.

Capital expenditure and cash balance

Our management of capital has always been defined by discipline, timing and flexibility.

Our position is strong.

Qantas remains one of only two global airlines with an investment grade credit rating with both ratings agencies.

We have significant cash reserves of $3.3 billion.

We have access to a broad geographic spread of funding sources, and a $300 million undrawn standby debt facility.

The majority of our 2012 Group funding requirements are in place.

Today I announce targeted reductions in capital expenditure.

We will reduce projected capex from $2.5 to $2.3 billion for full year 2012, and from a projected $2.8 billion down to $2.3 billion for financial year 2013, with further cuts to be identified for that year.

Our savings will come from a range of initiatives including: reductions in non-aircraft capex, deferral of B787-8 aircraft due to manufacturer delays, reductions in capacity growth requirements in the domestic market in financial year 2013 (bringing capacity growth in line with our long term demand estimate of five per cent), and utilisation of a capital-lite model for any premium airline investment in Asia.

As a leading aircraft buyer, the Qantas Group has strong relationships with aircraft manufacturers and a high degree of flexibility in our order book.

Any further capex savings will come from orderly changes to our fleet arrangements – with the cancellation, delay, or restructuring of purchase arrangements for our fleet.

An outcome of these capex decisions is the prospect of positive free cash flow earlier than anticipated.

Qantas International five year plan

Qantas International remains a weakness and a key focus.

The reality is that even the strengths of the rest of our business will not be able to compensate for this issue over the long term.

We face high competitor capacity growth into Australia.

While we have a strong outbound travel market, the inbound market is flat and in particular there is a softening of demand for travel out of the UK and Europe.

The challenges are structural and ongoing which is why last year we developed our five year plan for building a better and stronger Qantas.

It is now being implemented and in some areas accelerated.

Our **Gateway Strategy** continues with the popular services to Dallas increasing to daily from July.

We have received Anti Trust Immunity clearance for our Joint Business Agreement with American Airlines which will bring commercial benefits to both parties.

Santiago will replace Buenos Aires next month, opening many doors in a booming South America.

Unprofitable flying between Bangkok/Hong Kong and London will be eliminated in March via our strengthened partnership with British Airways.

Today I announce that we will also be withdrawing services from the Singapore-Mumbai and Auckland-Los Angeles routes in May.

We will replace our B747 Sydney services to Bangkok with A330 aircraft from June.

And on the Sydney-Auckland route, A330s will be replaced with B737-800 aircraft.

We are adding wide body A330 aircraft to Melbourne-Perth and allocating A330s on certain services between Sydney and Perth in place of B747s.

With these network changes and with a critical mass of 12 A380s in our fleet, we will be retiring two B747s in addition to the four that are due to retire in April this year.

This accelerates our plan to simplify and modernise our fleet.

We continue innovating to be **Best for Global Travellers.**

Two B747s have been upgraded to A380 product standards, with seven to follow soon.

We have commenced award-winning A380 services to Hong Kong.

We are expanding and improving our international lounges.

In response to a rebound in the Japan market we will be moving to daily B747 Japan services, up from six per week.

We will offer increased premium service from Los Angeles to New York with our upgraded B747 aircraft.

We have once again won a raft of global awards for our Cellar in the Sky.

The Qantas Group plans for **Growing with Asia** continue to evolve.

We are making excellent progress with our three Jetstar-franchise Asian airlines based in Singapore, Japan and Vietnam.

We continue to evaluate the options for establishing a premium airline in Asia.

Mindful of global economic uncertainty, and consistent with our focus on conserving capital however, the focus is on a capital-lite model.

The fourth pillar of our five year plan is to ensure a **Strong and Viable Business.**

Everything we do is about delivering a sustainable business model: a stronger, better and more resilient Qantas Group.

And that requires us to make some tough decisions.

Tough decisions today will ensure we don't need to make harsher ones later.

A more competitive maintenance operation

Today I announce a range of initiatives to increase the efficiency and productivity of our engineering and maintenance operations.

Qantas has an outstanding track record in aircraft maintenance, and our commitment to setting a global standard for safety and quality in airline maintenance will never change.

No other airline has a major heavy maintenance base in Australia.

We employ over 5,500 people in aircraft maintenance, professional engineering and support roles.

We spend $1.4 billion on engineering and maintenance every year.

We invest in the future with over 7000 apprentices having coming up through our programs since 1927, and 343 apprentices in training today.

With this massive commitment comes a responsibility to ensure that our engineering and maintenance operations are globally competitive and sustainable for the long term.

Today Qantas Engineering services costs are at least 30 per cent higher than those of our competitors.

And we have the ability to change.

The combination of older fleet retirements; the advent of new-generation, high-tech fleet; our new technology maintenance system; and a modernised regulatory regime means we can take significant steps to achieve greater efficiency.

1) Consultative review of heavy maintenance

Today I announce a consultative review of our heavy maintenance.

Our current heavy maintenance facilities are individually, and collectively, sub-optimal in scale.

With aircraft retirements, there is simply not enough heavy maintenance work to justify the three facilities in Melbourne, Brisbane and Avalon.

Doing nothing is not an option.

Preserving the status quo in the short term would only risk the business over the long term.

We have no plan to move operations offshore but we need to consolidate our activities in Australia.

That is why we will undertake a pre-decision consultation process with the relevant unions on the future of the heavy maintenance footprint.

We'll be consulting with the AMWU, AWU, ALAEA and other relevant unions over the next two months about options to address our heavy maintenance challenges.

Our objective will be to ensure that any decision takes into account the views of all stakeholders.

But we will be acting in the best interests of the business and our people over the long term.

We will not be propping up the past at the expense of the future.

2) Consolidation of maintenance tasks

The second area of focus is to consolidate a range of maintenance tasks for greater efficiency.

The Qantas Airlines Aircraft Airworthiness Group consists of professional engineers in Sydney, Brisbane and Melbourne who translate regulatory requirements into our program of maintenance and undertake a variety of administrative, planning and fleet support functions.

Apart from roles specifically related to ports in Melbourne and Brisbane, the remainder will be consolidated in Sydney.

This will ensure efficiency, consistency and an Aircraft Airworthiness Group that is similar in proportion to our peer airlines around the world.

Qantas currently has two Maintenance Operations Centres: one in Melbourne looking after B737 aircraft only; the other in Sydney looking after all other Qantas aircraft types (B747, B767, A330, A380).

We will consolidate our Maintenance Operations Centre into our home base in Sydney where it will be better placed to coordinate with the daily operational oversight of our Sydney Integrated Operations Centre.

This will drive consistency of process across all fleet types, both international and domestic.

Our Engineering Supply Chain can also be made far more efficient.

It is currently too fragmented and requires a total restructure of its operations.

A first step will be to consolidate our Commodities Management Group from Melbourne into Sydney.

We will be undertaking a further review of opportunities relating to warehouse optimisation and organisation design, with an outcome expected by the end of March.

3) Doing line maintenance more efficiently

The third area of focus is doing daily line maintenance tasks more efficiently.

Last year I spoke about the need for our Qantas aircraft maintenance processes to accord with new technologies and new regulations.

We don't maintain cars the way we used to; nor should we maintain aircraft like we did even ten years ago.

So Qantas Engineering is now proceeding with what is known as Maintenance on Demand for new generation aircraft across our line maintenance operations.

We will be consulting on the impact of this decision with the relevant stakeholders.

Maintenance on Demand means that our well qualified engineers will not be conducting aircraft checks that are not required.

This will bring our practice into line with both the manufacturers' guidelines and Civil Aviation Safety Authority regulations.

It will allow our engineers to be assigned to aircraft that require attention.

Strengthening catering

Now a few words about our catering business.

Our aim is to develop a sustainable business model for catering that continues to deliver a premium standard.

With the redevelopment of Adelaide Airport, the Qantas QCatering lease will expire in twelve months and the existing premises will be demolished.

We have reviewed the business case and decided against a costly reinvestment.

We will now consult with our employees on future options for catering in Adelaide.

We will certainly be focusing our investment in our catering facilities in Sydney, Brisbane, Melbourne and Perth.

Our state-of-the-art Brisbane facility is under construction and will open later this year.

In preparation for the move we are updating our processes and propose to partner with a greater number of local specialist food suppliers.

As part of our catering review Qantas is also exploring potential sale opportunities for Cairns, and the riverside catering centre in Sydney.

Airport ground operations

And finally our airports rostering and workforce planning team, currently dispersed around individual airports, will be largely consolidated in Sydney.

Impact on positions and care for affected employees

Let me turn now to the effect of these decisions on our people.

We anticipate there will be 500 positions affected by the immediate changes that we have announced today.

But let me clarify that there will be NO jobs going offshore.

Not one.

The jobs that are going have become structurally redundant.

The various reviews I have announced will need to be worked through their consultation processes, but they are also likely to have implications for jobs in due course.

Our objective is to minimise compulsory redundancies, so we will be considering a range of options including: voluntary redundancy or redeployment; using annual and long service leave where appropriate; or leave without pay to give people experience in other areas of the industry, including other airlines.

Conclusion

The results I have announced today show the resilience of the Qantas Group and our readiness for the future.

Overall our business is strong, we are exerting financial discipline, and we are well placed to handle this complex economic and competitive environment.

But as I said at the outset, the highly competitive markets and tough global economy in which we operate mean that we must change.

We need to be ready to take tough decisions, and we must become more flexible and productive.

Minister for Workplace Relations, Bill Shorten has rightly urged Qantas to think about the long- term in relation to jobs.

It is precisely because we are thinking about the long term jobs and the long term value of this company, that we are taking some hard decisions today.

Everything we do is about the long term success of the Qantas Group, and building shareholder value.

And our outlook is extremely positive.

The majority of our businesses are performing very strongly.

The new measures I have announced will move us structurally towards a more sustainable enterprise for the future.

Our aim is to secure our long term future as a modern and innovative Australian company employing tens of thousands of Australians in sustainable jobs now and in the future.

Today is another step along that path.