

# **Remarks for Calin Rovinescu**

**President and Chief Executive Air Canada**

**Vancouver Board of Trade, Nov. 20, 2014**

## INTRODUCTION

Good afternoon and thank you Craig for that kind introduction.

It is always a pleasure to visit Vancouver. As many of you likely know our first flight ever, when our company was called Trans-Canada Air Lines, took off from Vancouver in 1937, in the days when the city airport was little more than a muddy field. Here is where it all began.

Seventy-seven years later, Vancouver retains a central role in our story. Today, I wish to discuss how your city is a cornerstone for

Air Canada's global strategy and how everyone will share in our success.

## AIR CANADA OVERVIEW

First, I would like to give you a quick overview on our company and what we have been up to.

Curiously, people are always amazed when they hear of the scale and scope of our "little" company. We have approximately 27,000 employees and in B.C. alone we have more than 6,000/ counting those employed by our regional partners, many of whom are active in local communities.

Including these regional carriers, we have more than 1,500 daily flights worldwide. On average an Air Canada aircraft takes off somewhere every minute of every day of the year.

We fly to 180 destinations on five continents.

To support this network, each day we coordinate the flying of 360 aircraft – more aircraft than are operated by the Canadian air force, according to Wikipedia.

Last year, we carried more than 35 million people – the equivalent of every man, woman and child in Canada – and we had operating revenue in excess of \$12 billion.

Overall, we are among the top 20 largest airlines in the world, while Canada is only about 38th in terms of its population among the world's countries.

By any measure, we are complex company.

While it is therefore a formidable challenge to keep everyone and everything moving in the right direction, the good news is that

progress is being made as was recently shown by our record third quarter results, the best ever in our company's history.

On the measures most closely-watched by financial analysts we reported very solid quarterly results. Adjusted net income was up 25 per cent from a year ago and our system passenger revenues grew almost 10 per cent to nearly \$3.5 billion.

But revenue coming in is only half the story. Costs are an equally important part of our equation especially given that such a large portion of our costs are fixed. We managed to reduce our unit costs by 2.9 per cent from a year ago, and are well on the path to meeting our five-year 15% CASM reduction target we promised the financial community and our shareholders in 2012.

## CORPORATE PRIORITIES

Taken together, I am very pleased by these results and I want to publicly thank our employees for their hard work to help us achieve this important transformation. As most of you know, Air Canada, and indeed the airline industry as a whole, with its notorious cyclical nature, has faced financial challenges throughout its history. However, in recent years we have undertaken a very focused fundamental transformation to make our company sustainably profitable over this cycle by pursuing a relatively straightforward set of corporate priorities.

The first of these was to create a solid foundation by focusing on cost control and revenue growth. Apart from the record earnings of the past two quarters and the CASM reductions, perhaps the clearest sign of progress is our level of cash on hand – we closed the 3<sup>rd</sup> Quarter at \$2.8B of liquidity.

Along with strong results and a surplus restored pension plan, by using innovative financing tools to reduce our cost of capital and

delivering on our various initiatives, we have shifted the paradigm in the investment community. This was reflected not only in a recent Moody's upgrade of our corporate debt, but also in a strong stock performance. Air Canada shares have risen seven-fold over the last two years and we were the top performing stock on the TSX in 2013.

Another priority is customer engagement. Air Canada has been named the Best Airline North America by the highly-respected Skytrax Awards, our industry's Academy Awards, for five consecutive years.

We are also the only network carrier in North America to earn a Four Star rating from Skytrax. And moreover, in the annual Ipsos Reid Canadian business travel study, Air Canada was rated the preferred carrier of 83 per cent of Canadian frequent business travellers for 2014, a 14 percentage point improvement over the last six years, so our footprint in the business market is still deepening.

Key to engagement is offering customers the newest and best product and yesterday we showcased our new Boeing 787 Dreamliner for our Vancouver-based customers. By yearend we will have six of these latest technology aircraft in our fleet and this winter four of them will be stationed in Vancouver to serve routes to Asia. We are purchasing 37 Dreamliners and when our 737 order and 777 aircraft purchases are added, this represents nearly \$9B of capital spending over the next several years.

Closely connected to customer engagement is employee culture change. Air travel is to some extent a commodity but one way airlines can differentiate themselves is through service, and great service requires motivated employees. We have been intensely focused on this priority. The conclusion last month of an unprecedented 10-year labour agreement with our 3,000 pilots is a very clear indicator of the changing culture at Air Canada.

More recently, we were named one of Canada's Top 100

Employers from an initial list of 80,000 firms, based on factors such as benefits, working conditions, and training.

This brings me to our final priority, and one of particular relevance to this audience, and that is international expansion.

Perched as it is on the shore of the Pacific, Vancouver has throughout its history been an outward looking jumping off point and a welcoming destination for global travellers and global trade.

You occupy the threshold, not only of Canada, but also North America.

As such, Vancouver is ideally situated to be an aviation hub and we are intent on building our presence here to seize on this opportunity by expanding internationally. Let me give you a great example of the international opportunities that exist.

We already operate up to 28 flights per week to Beijing and Shanghai, of which 14 are from Vancouver. Our Star Alliance partner Air China operates up to 11 flights per week between Vancouver and Beijing. Clearly China is a big market for us but it holds even more promise in the future.

Just ten days ago I signed a memorandum of understanding in Beijing with Air China which sets out the main principles for a comprehensive joint venture and enhanced partnership. The joint venture will generate additional service, more options which stimulate growth and pricing benefits for passengers travelling between the two countries. We signed the MOU during an official visit to China by Prime Minister Harper and also in the presence of Premier Li prior to a meeting of APEC member nations. Over the past five years the Canada-China air travel market has grown on average by almost 11 per cent annually. This trend is expected to remain strong and will of course represent enormous opportunities for Vancouver.

Connecting traffic is the lifeblood of the modern airline industry.

In our globalized world, traffic flows around the world but increasingly it connects only at a limited number of key global hubs. The challenge for a network airline is to capture this traffic along with locally-originating traffic to fill its planes and expand its frequencies and destinations.

The potential is enormous. To give you one important example, despite our over \$13B of revenue, we calculate we currently carry only about 0.3 per cent of U.S. originating traffic that flies on foreign carriers to international destinations. We estimate that if we could grow this share to a reasonable 1.5 per cent – for example by convincing someone from San Francisco to connect through Vancouver rather than Los Angeles to travel to China – that incremental traffic would translate into an incremental \$400 million in revenue.

Already, we are seeing significant growth. In the first nine months of 2014, such connecting traffic through Vancouver was up 25.1 per cent.

Other airlines and airports have done this successfully - the best example being Amsterdam's Schiphol Airport. Holland is a country of only about 16 million people yet 52 million customers travel through Schiphol each year. All this traffic means increased business for the airport and more choice for travellers because airlines can sustain routes from Amsterdam that local traffic alone could not support. And while foreign carriers flying to Amsterdam certainly contribute to the airport, they cannot be a replacement for the powerful hub the home carrier has created.

## VANCOUVER: AN AIR CANADA HUB

So what are the keys to building a successful hub?

The first, which I have already touched on, is location. It is necessary to be at a crossroads where people and goods naturally converge. As a Pacific gateway, Vancouver is starting from an advantageous position. Great geography.

Second, you need a strong network carrier with sizeable operations, an appetite for international growth and an expansive route network to give customers choice.

Air Canada fills this role in Vancouver where we are very heavily invested. We are 2.5 times larger than our nearest competitor at Vancouver International Airport. We operate more than 1,100 flights a week – or more than 53,000 departures a year – to 46

destinations this winter. We account for 47 per cent of the flights from Vancouver International Airport. So we are offering lots of connectivity and, for local customers, a wide selection of non-stop routings.

Next, good infrastructure and a reasonable fees and charges methodology is imperative to encourage carriers to invest the billions of dollars in aircraft we are investing and in launching our international routes. Vancouver International Airport clearly satisfies this infrastructure requirement, having been named Best Airport in North America for five straight years by Skytrax.

The airport has been working with us to continue delivering a high level of customer experience through a number of key initiatives and important pilot projects. For example later next year there will be refreshed and expanded gate areas to better accommodate our B787 and B777 aircraft bound for overseas.

And YVR has also shown leadership by investing heavily in a very important aspect of the customer experience that is often taken for granted – unless it stops working – and that is the baggage sorting system.

As we grow at the airport, it is critical that the capacity of the system keeps pace with our customers' needs. Our ability to move the 30,000-plus checked bags that we handle each day will be enhanced by a state-of-the-art, fast conveyance and baggage tracking system.

I would also like to acknowledge the YVRAA for its leadership on many other fronts including in setting airport charges at levels that make growth viable. In return, over that last four years, our growth in passenger volume has contributed over \$100 million incremental dollars of revenue to the airport. This gives us the confidence to invest further in Vancouver.

Infrastructure includes supportive policy as well. The B.C. Government showed strong forward thinking by removing the fuel tax on international flights. The payback to B.C. is increased economic activity worth a multiple of the initial tax reduction. It also provides quality employment for British Columbians.

The B.C Government's approach to the fuel tax issue should serve as a great lesson for other less forward-thinking provinces in terms of what is needed in real "stimulus" initiatives.

Finally, locally-originating traffic is also important for hub airports. While we tend to talk about Vancouver, this also includes our network within BC and the Yukon. In recent years we have increased flying by deploying larger, Q-400 aircraft throughout B.C. and added capacity to markets such as Fort St. John and Terrace.

Our regional flight schedule connects communities in B.C. to every corner of the world – a skier from Sydney Australia can be in Kelowna with one quick connection in Vancouver. Cargo shipments from Prince George can be in local markets in China within 24 hours.

With Air Canada Express, everyone is globally connected through Air Canada or its partners. In this vein, I like to recount the story of Steve Jobs, who insisted that the iPod interface be designed to be easy, so that users could get to wherever they wanted in three clicks. Well, we want our customers to get wherever they want in two clicks, or should I say, two flights (or less).

### AIR CANADA IN VANCOUVER

Western Canada is increasingly a priority for us and we have located Kevin Howlett, Senior Vice President – Regional Markets, one of our most senior officers and a B.C. resident in Vancouver

to connect with local community and industry partners. Some of you may know Kevin from his days as an executive at Canadian Airlines. He has been tireless in his travels to most local communities in the West, and in B.C. in particular. We recognize that we need to be on the ground to hear firsthand about the business community's needs and how we can work together.

But creating a hub is not an end in itself. Hub airports are highly prized because of the economic spin-off benefits they bring. I see it every day and it is heartening to see that others in business and academia do likewise. Professor Tae Hoon Oum from the UBC Saunderson School of Business has correctly observed that airports today are “multi-modal, multi-functional enterprises generating significant commercial development within and well beyond their boundaries.” And we of course like this for the non-aeronautical revenue it brings to airports which in turn helps to reduce the fees charged to airlines

We ourselves employ 4,100 in the Vancouver region and we have an annual payroll of nearly \$300 million so we are putting our money where our mouth is in B.C. Additionally, nearly 8,500 retirees live in the community, spending their hard-earned pension cheques. This makes Air Canada the fifth largest private sector employer in Metro Vancouver and a significant contributor to the local economy,

We also spend nearly \$1 billion in other expenditures in B.C. That includes \$34 million on food and beverage supplies – which is a fair amount of B.C. wine and millions more on everything from crew hotels, office supplies, ground transport to advertising. We proudly hosted in 2012 all of the CEOs of the 27-member Star Alliance at a global strategy conference here in Vancouver and by popular demand we are again hosting international executives from

Star Alliance in Vancouver next spring. We simply love to show off this city and everything it has to offer.

## CARGO

Apart from moving tourists, business people and others who come to work and spend money here, we have a robust cargo business. In the first nine months of 2014 we have seen an increase of 13 per cent in total kilos shipped from Vancouver.

To give you some examples, the cherry season in BC was much better in 2014 than 2013, and as a result we had very large increase in demand into the Brussels market. It was also the first full season in which B.C. fruit was permitted to move by air into mainland China, so we saw a significant jump in shipments to Beijing and Shanghai.

The B.C. waters have had an excellent salmon season, and we have moved a great deal of wild BC salmon into Paris. In fact, most weekends over the past couple of months we typically moved 20-35 tons of Pacific salmon from Vancouver to Paris.

Through network and connecting traffic, as well as by using direct lift into Europe, we have seen significant cargo gains from this market, including shipments into Paris up 30 per cent, to London up 100 per cent, and Brussels up more than 400 per cent. And, within Canada, our increased domestic wide-body service has spurred domestic cargo growth to Toronto and Montreal.

### AIR CANADA GROWTH

The economy is not at a bad place in Canada with moderate growth being sustained, but Air Canada's capacity additions have outpaced GDP growth by several multiples.

Between 2009 and 2013, as the global economy recovered, Air Canada grew capacity by 7.8 per cent in the Vancouver market.

But now as we are on a more solid footing from a financial point of view, we have accelerated this expansion and increased capacity a further 7.7 per cent from January to September of this year alone.

Next year, we plan to expand overall capacity here by nearly 10 per cent, making Vancouver our fastest growing hub in 2015 based on incremental capacity

In 2014, Air Canada added significant seat capacity to each of the domestic, international and transborder markets. This resulted in a substantial increase of 480,000 seats year-over-year in enplaned passenger traffic for the first nine months of the year. We anticipate we will produce over 600,000 additional passengers in YVR by the end of the year. That's 10 B.C. Place Stadiums full to the rafters.

Growth in the international market has been particularly strong with a double-digit, year-over-year percentage increase. To put this in perspective, our growth this year is the hypothetical equivalent of adding 12 new start-up international carriers operating three-times weekly, year-round B767 flights in Vancouver.

This translates into more jobs, more tourism, more infrastructure facilities and further highlights the differentiated economic value and advantages of having a strong hub carrier with an expansive network.

In addition, as I mentioned, we are also assigning our newest aircraft, the Boeing 787 Dreamliner to the Vancouver market, representing a very important statement in terms of a capital commitment – in fact nearly \$1B.

In October we began operating it to Shanghai. Next month it will begin Tokyo-Narita. In February we will add Beijing. And in March it will start flying to Seoul.

These new aircraft offer the latest in customer comfort and will keep us competitive in the Asian market where we are up against some of the best airlines in the world. As well, the cargo capacity of the 787 is greater than that of the 767, which again should benefit B.C. businesses.

## ROUGE

We of course work with many B.C. businesses as suppliers and partners. One such business we are helping is Fleuvog shoes. This is because we made B.C.- based Fleuvogs part of the uniform for the crew of Air Canada rouge, our new leisure carrier launched in mid-2013.

When looking at our performance over the past decade in leisure markets, the reality is that these routes, from a financial perspective, were marginal at best or money-losing at worst.

Rouge offers an attractive leisure product yet operates at up to 30 per cent lower cost than Air Canada mainline to yield sustainable profits at leisure-market ticket prices and offering a superior leisure product, with access to our loyalty programs and other advantages. We plan to solidify our presence in these markets and grow rouge over the coming years which, incidentally, is already supporting more than 100 jobs in Vancouver.

Rouge is an essential component of Air Canada's Vancouver growth. It is increasing the capacity on Vancouver-Las Vegas by 160 per cent and on Vancouver-San Francisco by 41 per cent this winter. Year-round, non-stop rouge service from Vancouver to Honolulu, which incidentally, starts tomorrow, and Maui, beginning in early December, will result in a 61 per cent capacity increase on Vancouver-Hawaii routes.

In addition to Hawaii, Las Vegas and San Francisco, Air Canada rouge flies non-stop to other of the more popular U.S. vacation destinations from Vancouver, including Los Angeles and Anchorage. Non-stop service to Puerto Vallarta started earlier in November and, here's the scoop, new routes will launch to Phoenix and Palm Springs in December. Next May rouge will launch its first trans-Pacific route with seasonal service between Vancouver and Osaka to tap into the Japanese inbound tourism market.

## CONCLUSION

By way of a conclusion then, I want to reiterate that Air Canada's strong growth in Vancouver is a trend that we see continuing. Our partnership is intertwined and very deep with your airport, your business community and your tourism industry. After growing more than seven per cent in 2014, we intend to make your airport the fastest growing hub in our entire network next year.

And while such growth is beneficial to travellers, giving them more options of flight times, destinations and routings, it is also beneficial to your community. This is because a modern hub airport that is progressive and forward-thinking, combined with a large, international network carrier, can together make for a powerful economic dynamo. We have seen this in many places around the world and it is happening now in your community.

British Columbia is a great place to do business. We are appreciative of the many strong partners and advocates we have in your community. We also thank our Vancouver and B.C. customers for their ongoing loyalty to Air Canada.

Together, we are realizing our goal of transforming Air Canada into a leading international carrier, a global champion for Canada and for Vancouver and British Columbia. And as our newest marketing strategy suggests... “Your World Awaits...”

Thank you