

VANCOUVER BOARD OF TRADE

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Check against delivery

Speech to the Vancouver Board of Trade

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Thank you Larry for your kind introduction.

I always enjoy coming to Vancouver but it is particularly exciting right now with the energy of the 2010 Olympic Games still palpable in the air. I have been here three weeks in a row and I can sense the enthusiasm is carrying over to the Paralympic Games beginning Friday.

I caught Olympic fever when I came to Vancouver last July to unveil our B777 Olympic livery, the biggest billboard for Vancouver and the Olympics in the air. And on Day 44 of the Torch Relay I was fortunate enough to be runner Number 38 in Ottawa and bring the torch 300 meters closer to Vancouver. Even though I only ran with the flame that short distance, I will carry its memory for a lifetime.

I was astounded at the diversity of people who shared my section of the run that day. There was a woman in her 80s who dedicated her run to seniors everywhere; the child of first generation immigrants to Canada; the veteran athlete whose lifetime ambition was to carry the flame.

Contained in that microcosm were all the good things that the Games – and Canada itself – represent. And we all witnessed that same diversity in the throngs of passionate Canadians cheering our athletes at the Games and here in the streets of Vancouver.

Who could have guessed that the magnificent performance of our athletes could have brought such an outburst of unabashed patriotism from normally reserved Canadians of all origins. The excitement of that last Gold medal hockey game will be with us for a long time to be re-told by generations of fans. Here at Vancouver Airport, we incurred a flight delay for a reason Air Canada had not yet encountered in over 72 years of existence. Passengers glued to the airport departure gate TV screens during the third period simply could not be persuaded to board their flight for an on -time departure.

Taking our role as Official Carrier of the 2010 Games to heart, passengers on Air Canada aircraft throughout the world were kept abreast of the score on a real-time basis by flight crew via data link message received from our System Operations Control.

I congratulate Vancouver and everyone involved on the success of the Games for effectively delivering to Canada its 15th gold medal –in the form of an artistic, technically-accomplished and overall outstanding performance. All of Canada is very proud of your accomplishments.

Since I have been in Vancouver and through the airport so many times over the last weeks, I must publicly recognize the excellent work of Larry Berg and his team at the Vancouver Airport Authority. They certainly deserve podium standing for a flawless airport operation over the course of the Games.

The large number of passengers, the mountains of baggage – and the fact traffic levels fluctuated so much during the Games – made the airport's task a herculean one. Given this, the results are that much more impressive. So thank you Larry for your team's out-of-the box thinking, flexibility and creativity to overcoming the challenges.

As Canada's national flag carrier, we are well aware that there are very high expectations for our airline, especially during the Games. We planned for nearly a year to accommodate the rush of customers and the teams with their outsized equipment. The team working under our General Manager Airports for Western Canada, Mark Southern, who is here in the audience today, also deserves recognition for their extraordinary efforts. On March 1st Air Canada boarded 15,000 customers including Olympic athletes, VIPs, heads of state and European Royalty, media, and over 22,000 bags on 155 flights from Vancouver. All with near textbook perfection.

The Air Canada team had three check-in facilities in operation, including one each at the Whistler and Vancouver Athlete Villages, the newly-minted Sea Island Remote Terminal as well as the main terminal at YVR. Despite welcoming twice the number of passengers we normally see, the team checked in passengers and bags very quickly efficiently at both terminals with minimal wait times. We received great feedback from IOC members who travel to Olympic Games worldwide, telling us that their Vancouver airport departure was the best ever. All in all, the countless hours spent by our Olympic planning group with the Vancouver Airport team, VANOC and all operational groups paid off and we fully expect a similar success with the Paralympics.

Such challenges are a chance to excel and we wanted to seize the opportunity presented by the Games to showcase Air Canada's international operations, especially in Vancouver, as we are more focused than ever at making our operations here a success. And these Games were the perfect chance to celebrate everything that Air Canada, Vancouver and Canada are about – to show how efficiently we can connect Canada to the world through our magnificent Pacific hub.

I will talk about our opportunities in Vancouver more in a few minutes. First, though, I want to quickly recap recent events and update you on the Air Canada story.

The last two years have been difficult for our industry as a whole. Airlines are always the first affected by and the last to recover from economic downturns, especially an airline such as Air Canada, which caters to business travelers and premium traffic. The International Air Transport Association estimates that last year our industry collectively lost more than \$11 billion as traffic fell 3.5 per cent. Giovanni Bisignani, head of IATA, called 2009 the worst year ever for the industry in terms of lost traffic.

For its part, Air Canada did relatively well. Our revenue performance compared favourably with that of our North American peers, in fact, we outperformed most carriers in both yield and unit terms. Moreover, we managed capacity effectively. In 2009 we flew our planes 80.7 per cent full on average versus 75.6 per cent for the industry as a whole.

But at the start of last year we encountered a series of interconnected events that created a serious financial situation for our company that we are still feeling.

Most of you know the global airline industry suffered a severe whiplash as fuel soared to US\$147 a barrel (and at some points, jet fuel exceeded \$180 a barrel) and then fell back to US\$40 during 2008. While Air Canada was partially hedged, the fuel spike added some \$866 million in unexpected costs and severely weakened our balance sheet going into 2009. This overlapped with the onset of the very deep global recession that stubbornly persisted throughout 2009.

With the economic downturn, like other legacy carriers, we suffered significant losses in 2008 that carried over into 2009. Our cash position was severely depleted, putting us in danger of slipping below the covenants of our credit card processors and other lenders. The combination of a 40% drop in equity markets in 2008, coupled with historically low long-term government bond rates, created, at least on paper, a massive pension fund deficit which would have saddled us with unmanageable pension deficit funding payments. And layered on top of all this was the expiry of Air Canada's major collective agreements. We had a firm deadline for all of this to be resolved – in one way or another – by the end of July 2009 - and I was appointed CEO at the beginning of April – in fact on April Fool's Day.

During a media interview here in Vancouver last summer, I used the analogy of a Rubik's cube to describe our predicament. We were faced with multiple issues and none could be solved unless all were solved. We could not get additional funding without labour stability. We could not get labour stability without a pension solution. We could not get a pension solution without the funding. You get the picture.

Just as with a Rubik's cube we began working all sides of the problem at once. Early on we got lenders and credit card processors to relax their cash requirements, albeit conditional on some permanent funding coming in.

One-by-one we reached settlements and contract extensions with our unions on a cost neutral basis, again conditional on each other's arrangements, on certain savings from key suppliers, on funding and on a pension deal from the Government. We got suppliers and partners to rework and improve rates to be more market competitive or to extend their contracts. Based on the progress we made with Labour, the Government of Canada ratified a joint company-union agreement to reschedule our pension deficit payments, through a change to the pension funding regulations.

With these arrangements in place, we announced – on July 29, 2009, two days before the mandatory deadline - that we had raised more than \$1 billion from a diverse group that included our major shareholder, several key business partners and other lenders and stakeholders.

We had lived to fight another day – and in the process showed that Air Canada, this 72 year old former Crown Corporation, could be creative, could be nimble, could be flexible - when it needed to.

Meanwhile we were actively improving our customer offering, our services, products and our policies. We were re-engaging with both the customer and the travel trade, as well as our partners within Star Alliance.

The earliest indication that our rebound was real and starting to be understood by the investment community came in October when we announced an equity financing of \$260 million. Had someone suggested to me when I started in April that we might be in a position to raise equity by October, I would have sent them in for Olympian level drug testing.

This year, with our financial situation stabilized, we will focus on the real transformation that needs to occur so as to properly rebuild for the future. I am very proud of what we achieved last year but real progress can only be measured when the transformation is permanent. I would like to share four key elements of our transformation plan with you now that we have kicked it into gear.

The first element is our Cost Transformation Program (CTP) aimed at achieving \$500 million in annual cost and revenue improvements by 2011. We have already made significant progress toward this goal and surpassed our 2009 target by 40 per cent. Importantly, we are doing this without compromising the passenger experience. Transformation has to be about much more than cost reduction. It means technology. It means different processes. It means managers and front-line employees doing more different jobs with more empowerment. It means greater productivity. It means that despite being a big company, we will behave much more like a smaller entrepreneurial one.

A second element of our transformation is a renewed focus on the customer experience -- through a concerted re-engagement with our customers, our partners, the travel trade, and the other carriers of the Star Alliance.

A carrier such as Air Canada is highly dependent on premium traffic and this was the area most severely affected by the recession. While we have held our own with respect to such customers we will more aggressively play to our strengths.

Whether through our Maple Leaf Lounges, our Concierge Program, our In-Flight Entertainment Systems on the back of every seat or our international Executive First service, we will show why our product is industry-leading.

We have admitted straight up where certain irritants were getting in the way of progress and removed them. Without bureaucracy, without committees, without endless debate. We eliminated the call centre fee, increased the availability of Aeroplan reward seats, allowed small pets back in the cabin, improved our Super Elite members' access to revenue seats and reached out to the travel trade community to restore commissions on some of our lower fare categories.

We were also the first North American airline to introduce popular new IT services for customers in the form of Apple and Blackberry applications with automatic flight notification and rebooking tools.

These provide information in real-time, the way customers want to receive it. The underlying philosophy is that if we are easy to use, then we should be easy to choose.

And I am extremely pleased to see that others also recognize our industry leading products and services and the progress we have made. One clear indication is the series of prestigious awards we won in late 2009 from international magazines that cover our industry.

And this, despite the enormous challenges to our very survival that we faced last year. These awards are the Academy Awards of our industry and are based on extensive surveys of frequent travelers who fly many different carriers.

Business Traveler, a magazine with 500,000 readers and ten editions published globally, gave Air Canada more awards than any other carrier in the world last year. Its readers declared we have:

- the Best Flight Attendants in North America;
- the Best In-flight Services in North America;
- the Best Business Class among North American carriers;
- and that Air Canada is the Best North American Airline for International Travel.

A survey of 25,000 readers of the equally respected *Global Traveler* magazine found Air Canada to be the Best Airline in Canada and Best Airline in North America.

While I know we do not get it right 100% of the time, these surveys suggest that we do get it right *most* of the time. And for that I have to thank the great work of our incredible staff who go “above and beyond” and make the extraordinary effort on board, in the airport, on the phone, during both regular and irregular operations.

Thirdly, the transformation will require overcoming what I consider our greatest challenge: changing the culture at Air Canada. This must happen both in terms of how customers see us and how we behave as a company. This is the most important aspect of our transformation because a corporate culture provides the foundation and sets the tone for everything that you do.

Given the shackles of age and legacy, some think this transformation is not achievable. However, with the right drivers – both in terms of people and tools - Air Canada will absolutely become a more entrepreneurial and nimble company, a place where employees act as if they are owners. A place with a "Just Do It" culture, where things happen much more quickly without countless committees and white papers. A place where managers become leaders; where employees are ambassadors.

The fourth element entails building on our position as one of the world's leading international carriers. I always find it telling that Canada is 36th in terms of population among the world's countries yet Air Canada is the 13th largest airline in the world, punching well above its weight category. .

We therefore plan to take advantage of Canada's excellent geographic position, vast network underpinned by an array of bilateral authorities to fly to other countries and the relationships we have with other carriers, particularly those of the Star Alliance.

Our goal is to build an international powerhouse and to this end we have already announced new major international destinations for this summer – Brussels, Copenhagen, Athens and Barcelona.

As our Pacific hub, Vancouver is and should increasingly become a key cornerstone of this strategy. And this is an important message I want to leave you with.

Our hope is to expand our presence here in Vancouver to the mutual benefit of this city, this province and Air Canada. With more than 5,000 employees based in Vancouver, Air Canada currently spends over \$1.1 billion dollars on wages, benefits and other expenses annually in Vancouver. Our contribution to the BC economy generates over \$5 **billion** in incremental economic activity for the province. Our success is therefore your success.

Despite the lingering effects of the recession there are encouraging signs, particularly on Pacific routes. In February 2009, Air Canada's Pacific traffic fell more than 20 per cent from the prior year. This past February, traffic rebounded by 25 percent from the depressed 2009 levels and we are also seeing a pick up in cargo demand throughout our network. We are not yet spiking the football to declare victory – we have a long way to go before this recession is behind us, but we are finally seeing some green sprouts.

This summer we will operate **daily** service starting in June from Vancouver to Beijing and Shanghai, whereas last year we flew these routes only three and four times a week respectively. For Vancouver we plan to increase our total capacity, measured by what is referred to in the industry as Available Seat Miles, or ASMs by 3.3 per cent in July. On the Pacific alone, ASMs are to rise 26 per cent this summer. So we are betting significantly on the rebound of business and leisure traffic to and from Vancouver.

Moreover, there are two significant developments that promise to be of particular benefit to your city and British Columbia.

The first of these was the recent award of Approved Destination Status by China to Canada. This will make it easier for people from China's mainland to travel to Canada and allow Chinese tour companies to market our country as a travel destination. Located as Vancouver is on the Pacific Rim, there is no need for me to tell you how large the Chinese market is. And China and India have the fastest growing airline sectors within Asia. As well, the intra-Asian airline market is now bigger than the North American market. And with these developments, we will look to capture a greater share of the Asia to North America market.

A second development that will benefit Vancouver is our purchase of Boeing 787 aircraft. These will be game-changers in the sense they are mid-size aircraft with a 210-300 passenger capacity but have an incredible range of more than 7000 miles.

They will allow us to fly to secondary Asian cities that we cannot currently serve economically because not enough people fly there to justify using the larger aircraft. We have 37 firm orders for these “next generation” aircraft and they will start entering our fleet in three years.

Inevitably, when I talk about international expansion I have to deal head-on with attempts by foreign carriers such as Emirates Airlines to sway federal and provincial politicians and airport authorities into believing that somehow the economy will be dramatically enhanced and traffic will exponentially increase if they are allowed greater access to our markets, despite the fact that point to point traffic between the two relevant countries under the bilaterals is already more than adequately well served.

Emirates has waged an aggressive media and lobbying campaign in Canada on this issue. This state- owned and funded carrier complains that the Government of Canada does not allow Emirates to fly as much as it wants to Canada and limits the airline to several flights a week.

It is well known in the industry that Emirates is trying to push hard to divert as much global flow traffic via Dubai in order to deploy its massive fleet of wide body aircraft, including A380s it has purchased or has on order.

While the Canadian skies have been liberalized on a progressive basis over the years with our full support, some restrictions remain for good reasons. The bilateral agreement between Canada and the United Arab Emirates is a case in point. Simply put, the market between Canada and the UAE has not developed to the point where more capacity is warranted. Period. Full stop. There are already more airline seats being flown between Dubai and Canada than there are people to fill them. No adjustments to the Canada-UAE bilateral are warranted at this time and in our view it would be short-sighted on the Canadian Government's part to yield to the massive lobby effort underway by Emirates and the UAE.

Few Canadians actually travel to Dubai and fewer still residents of Dubai travel to Canada. Statistics show the number of people traveling daily to Dubai from Canada last year was barely enough to fill a mid-size, 213-seat Boeing 767 jet. So why then is Emirates flying an Airbus A380 with roughly 500 seats to Toronto? And why too is it intimating it wants to fly these behemoths to other cities, including Vancouver?

What Emirates wants to do is flood the Canadian market with capacity. Its strategy is to scoop up travelers going elsewhere in the world and funnel them through Dubai, further strengthening Dubai as a global flow hub. This would have the effect of severely damaging our hubs in Canada and our network in Europe and elsewhere.

Now, I'm sure you're thinking: "what is wrong with flooding the market with capacity? It gives me more travel options."

Well, at first blush it might. But the longer term impact is devastating and could have the effect of restricting or even marginalizing Vancouver as a hub. When an international carrier dumps seats into a market like Canada, it becomes harder for Canadian airlines to operate internationally. Ultimately, this translates into less economic activity, fewer jobs and fewer routes served.

In the case of Vancouver, Air Canada and other international airlines such as China Airlines, EVA Air, Korean Airlines, and Japan Airlines, all depend upon a certain amount of connection traffic beyond their respective hubs to make their point to point service profitable.

If Emirates, with virtually unlimited access to capital through its state ownership structure, operates here on an unrestricted basis and pours seats into a market where there is minimal point-to-point demand, it will sop up passengers from these other airlines damaging the direct service. This is not what the country- to- country Open Skies policy was intended for. This will undeniably impact the ability of other carriers, to augment the passenger loads on their flights, thereby threatening the viability of these direct services to Vancouver as a whole.

At the end of the day, sure, you will still be able to get to anywhere from Vancouver. But you will have to get there through Dubai.

The Emirates approach also hurts airports and the communities where they are located. Last month, with a lot of media hype and noise, Emirates unveiled a so-called economic impact study that purported to show that allowing it unfettered access to Canada would somehow generate massive economic benefits for Canada. However, this was based on the dubious assumption Emirates will magically find nearly 275,000 *more* passengers flying between Canada and Dubai. That kind of magic is the stuff of fairy tales. Those who understand airline traffic flows will see through this sort of subterfuge, no matter how many political and business junkets are organized to the UAE and no matter how much confusion is created around linking Open Skies with the UAE to military bases necessary for our country's operation in Afghanistan.

While its argument may be seductive, what Emirates' strategy will do is constrain the growth of Canadian airports by turning them from hubs into stubs at the end of a spoke that leads only to Emirates' hub in Dubai.

When you compare Vancouver to other cities, you quickly realize that this city and its airport have a great deal more room to grow. In 2008, Vancouver had a population of about 2.3 million and its airport had 17.8 million passengers. By contrast, Atlanta, with a population of 4.5 million, had 90.1 million passengers; Dallas-Fort Worth, with a population of 4.8 million, had 57.1 million passengers.

Of course factors such as geography and the passenger catchment area account for some of this discrepancy, but the fact remains, Vancouver has an opportunity to attract substantially more global flow traffic.

The best way to do this is with connecting traffic, where Vancouver is the hub- not where it is a stub. Foreign carriers such as Emirates will never ever bring hub connectivity to a Canadian airport whereas for our part, I believe we can connect a lot more U.S.-Asia traffic through Vancouver.

At present, we have about 34 per cent of the Canada-Asia market, so we are getting our share domestically. But of course, in North America the far, far larger market is between the U.S. and Asia, where our share is only one per cent. By winning only a couple of extra percentage points of market share on these routes we could connect a million more passengers through Vancouver's airport ensuring Vancouver's hub status. This is something we know we can do because of all the advantages I mentioned earlier. And *that* would be real economic growth for Vancouver. For the airport authority. For the Province. For Canada. Not fictional growth based on dubious traffic increase between Dubai and Canada. But real growth, adding to our already sizeable contribution to the economy of this province. Adding to our current direct spend of \$1.1 billion and \$5 billion in indirect contributions to this Province.

Competition for international traffic flows must exist on a level playing field that provides equal opportunities for all. Any trade agreement – and that is what an air bilateral agreement is – must be fair, balanced and mutually beneficial.

This is the basis of all trade. Anything less would be our equivalent of “Surrendering the Podium”.

Another necessary ingredient to be competitive is affordable infrastructure. At present, Canadian airlines are disadvantaged in this area due the number of government fees and charges that get added onto tickets. There is GST, provincial taxes, the recently hiked security charge, federal and often provincial fuel excise taxes, airport improvement fees and navigation charges.

The most outrageous of them all is federal airport rent, something no other industrialized country collects. Although Canada privatized its airports in 1992, Ottawa continues to collect more than \$300 million annually in rent for these facilities. Collecting this rent may help solve the federal deficit but it chokes economic development and is an anti-stimulus measure. Our industry has to stop being seen as a cash cow. That is too short-sighted a policy and the airline business is too fragile . Rather our industry should be one of the major catalysts for economic growth, especially post-recession.

So, to conclude. Despite the enormity of the challenges, we got through last year. We extended our collective agreements. We rescheduled our pension deficit payments. We raised nearly \$1.4 billion of capital. We were awarded the Best Airline in North America. As Official Airline of the Olympics, we helped VANOC, the Province of BC and Vancouver make the Games a huge success. We have increased our capacity from Vancouver dramatically year over year.

Provided we have the support and interest of the airport authority, and the various levels of government, especially Premier Campbell's Government, I am fully committed to further building and developing a vibrant and strong Pacific hub (rather than stub) in Vancouver, connecting passengers throughout Air Canada's global network.

Vancouver can absolutely become THE gateway capturing global flow by connecting the Asia-Pacific Region, North America, Europe and Latin America. This represents true economic opportunity for your airport, for your community for your province. I personally look forward to sharing many more years of success with the Vancouver business and trade communities – and building on each other's strengths.

It has been a pleasure to speak to you this afternoon. Thank you for your attention.-