



June 22, 2017

## RBC Flight Deck

### You are free to move around the cabin

**Traffic growth remains healthy.** Heading into the seasonally largest third quarter for the Canadian airlines, general traffic trends remain quite healthy. And we note both Air Canada and WestJet pointing to a strong forward booking curve at our conference in Toronto on May 17 ([highlights](#)). What continues to be interesting to note is the ability for the North American carriers to manage capacity, largely matching traffic demand on a monthly basis. For the month of May, WestJet reported traffic growth at 4.8% Y/Y (vs. our 6%), on capacity growth at 5.9% (vs. our 6%). While Air Canada no longer provides monthly traffic stats, the peer group reported 5.2% traffic growth in May – exceeding the average capacity growth of 5%.

**Fare increases holding in.** Despite three consecutive weeks in April of fare increases for Air Canada as compiled by the RBC Fare Survey (and a similar set-up for WestJet), higher fares are holding in. For the first two months in Q2/17, the RBC Fare Survey tracked fare price declines of -0.8% Y/Y for Air Canada. After adjusting down by -350bp to account for stage length changes, it points towards a yield decline of -4.3%, which compares to our current Q2/17 yield estimate at -3%. For WestJet, the RBC Fare Survey is showing fare prices are up +2.7% Y/Y. After adjusting down by 50bp to account for stage length changes, it implies a yield of +2.2% Y/Y, as compared to our current Q2/17 yield estimate at +1.2%.

**Spicing things up.** Bombardier was able to lock in a nice 50 Q400 turboprop order from Spicejet in Paris, which we had on our Bombardier New Order Heat Map. The value of the order at list is \$1.7B and adds roughly 2 years of production capacity for the aircraft. And while Bombardier failed to secure a CSeries order, interest is clearly growing with the plane garnering positive reviews following a year into commercial service. The key is that the airlines that are flying the CSeries are putting the plane on new routes, which we think could force the competition into seeking to provide a matching service through their own CSeries orders.

#### In This Edition...

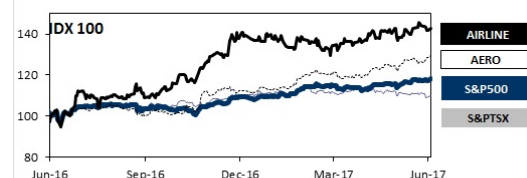
- **RBC Fare Tracker (p. 2):** Seeing positive fare growth, as per the RBC Fare Survey.
- **The Load Factor (p. 3):** Traffic demand remains robust.
- **The Bombardier New Order Heat Map (p. 4):** Bombardier lands Q400 order from SpiceJet.

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INDEX	1-M (%)	YTD (%)	1-YR (%)	TREND
S&PTSX	(1.0)	0.1	10.1	▼
S&P 500	2.8	9.4	18.3	Δ
AMEX Airline	3.4	4.5	42.9	Δ
AMEX Aerospace	4.5	16.8	29.8	Δ



COMMODITIES	1-M (%)	YTD (%)	1-YR (%)	TREND
WTI	(8.7)	(21.2)	(9.4)	▼
Jet Fuel	(11.4)	(16.2)	(4.8)	▼
CAD/USD	(2.1)	(1.6)	3.3	▼

AEROSPACE				
Bombardier	18.6	15.9	28.3	Δ
Boeing	10.1	27.8	53.3	Δ
EADS	4.1	22.2	51.1	Δ
Embraer	4.0	0.8	(7.6)	Δ
General Dynamics	4.4	18.5	47.2	Δ
Textron	3.6	(0.8)	25.9	Δ
United Technologies	0.7	11.3	20.6	Δ

N.A. MAINLINE				
Air Canada	3.0	27.6	88.7	Δ
AMR	9.1	5.6	68.1	Δ
Delta	8.2	6.0	37.2	Δ
United	(0.2)	6.8	82.6	▼

N.A. REGIONAL				
Alaska	6.0	1.0	49.6	Δ
Allegiant	1.3	(13.2)	0.4	Δ
Chorus Aviation	(2.4)	0.0	21.5	▼
JetBlue	7.3	1.9	40.1	Δ
SkyWest	6.7	0.8	48.3	Δ
Southwest	5.0	22.2	53.3	Δ
WestJet	0.5	(2.4)	7.0	Δ

INTL. AIRLINES				
Lufthansa	14.9	52.6	66.5	Δ
Air France/KLM	19.9	115.5	79.4	Δ
BA/Iberia	0.1	35.3	26.2	Δ
Cathay Pacific	6.7	(23.3)	(20.0)	Δ
Air China	8.7	56.2	53.1	Δ
China Eastern	0.0	24.5	11.9	Δ
China Southern	17.1	59.6	50.6	Δ
Singapore Airlines	0.1	3.3	(5.4)	Δ
Qantas	13.4	65.5	88.7	Δ

Source: Bloomberg

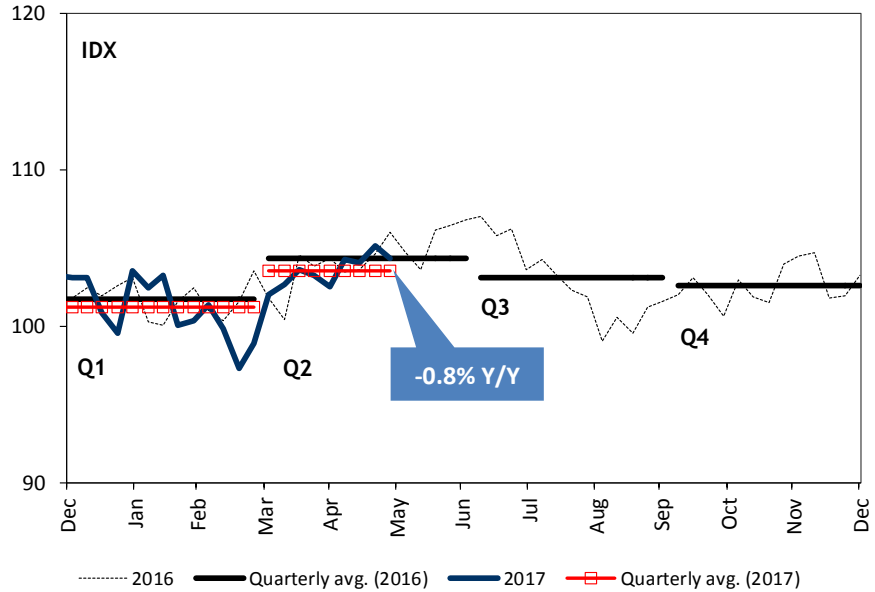


### RBC Fare Survey

We present below the results of our RBC Fare Tracker. This proprietary algorithm provides investors a unique snapshot of Air Canada and WestJet’s ticket pricing strategies ... and a window into yield growth trends *before* they are announced.

#### Air Canada

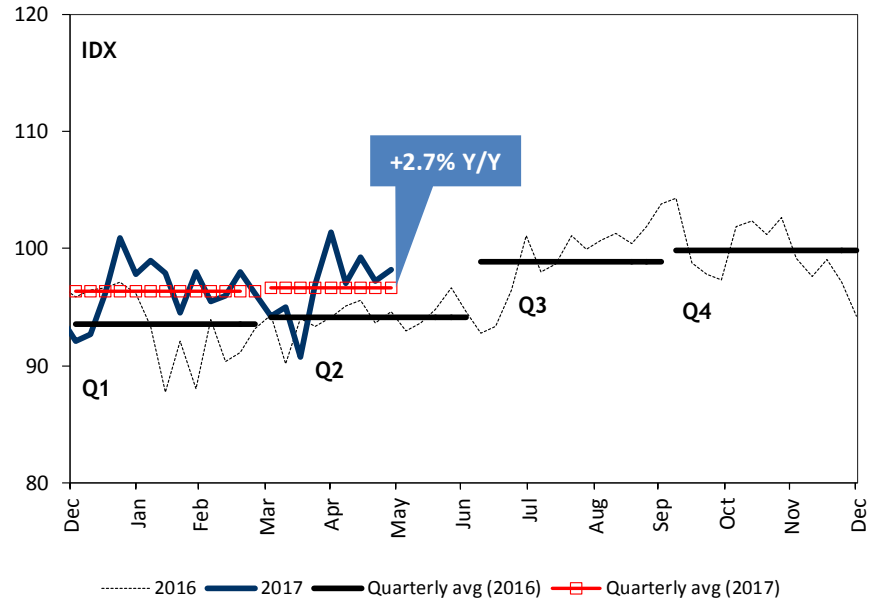
Following three consecutive weeks in April of higher fare prices, the increase has slowed, but remains stable at higher levels as tracked by the RBC Fare Survey. For the first two months in Q2/17, the RBC Fare Survey tracked fare price declines of -0.8% Y/Y for Air Canada. After adjusting by 350bp to account for stage length changes, it points towards a yield decline of -4.3%, which compares to our current Q2/17 yield estimate at -3%.



Source: RBC Capital Markets estimates, Company websites

#### WestJet

For WestJet, the RBC Fare Survey did pick-up a rebasing of fares higher in mid-April, which appears to have largely stuck into May. For the first two months in Q2/17, the RBC Fare Survey is showing fare prices are up +2.7% Y/Y for WestJet. After adjusting down by 50bp to account for stage length changes, it implies a yield of +2.2% Y/Y, as compared to our current Q2/17 yield estimate at +1.2%.



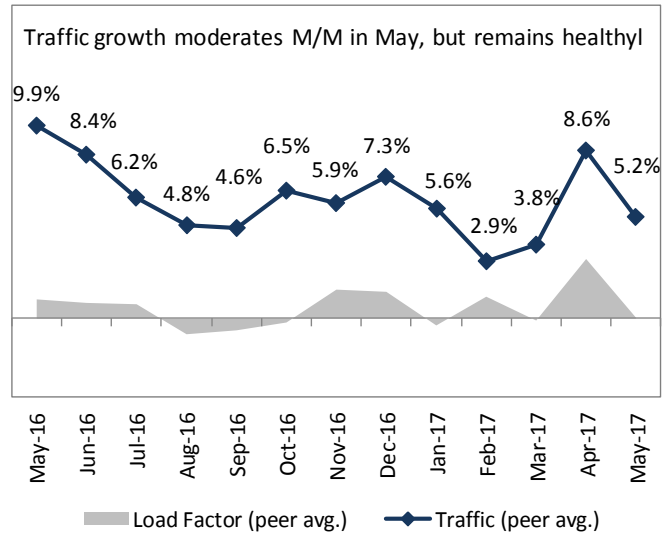
Source: RBC Capital Markets estimates, Company websites



## The Load Factor

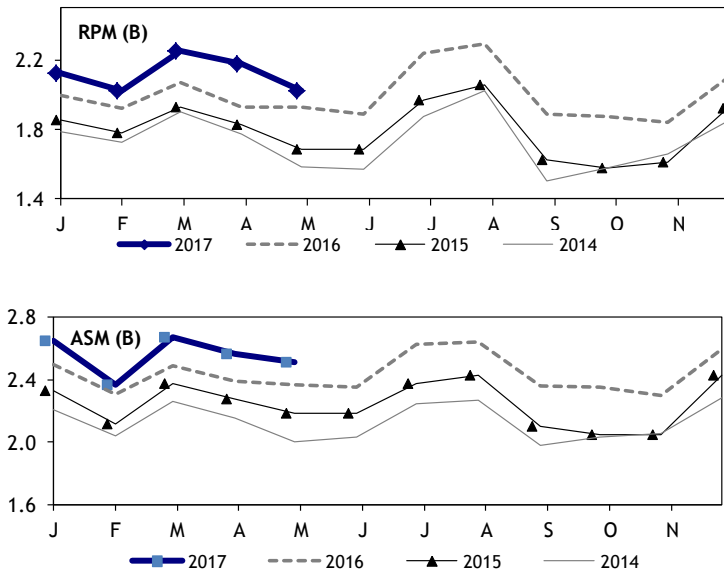
### Industry trends

On average, the peer group reported 5.2% traffic growth in May – exceeding the average capacity growth of 5% and leading to higher load factors. We continue to see good capacity management across the peer group, with most carriers effectively matching capacity to traffic demand.



### WestJet

For the month of May, WestJet reported traffic growth at 4.8% Y/Y (vs. our 6%), on capacity growth at 5.9% Y/Y (vs. our 6%), leading to a system load factor at 80.6% (down -80bp Y/Y). While planes were less full in May, it follows the 12.8% Y/Y traffic growth WJA reported in April, with the moderation in traffic growth month-to-month potentially a timing related impact. And we note, WestJet did implement several fare price increases in late March (as per the RBC Fare Survey). The key question is whether the current fare rate can be sustained in light of sustained domestic capacity additions (management guiding to 7.5%-8.5% in 2017), and potential competitive pressures from new ULCC in Canada.












	May			Year to date		
	2017	2016	Δ	2017	2016	Δ
RPMs (B)	2.023	1.931	+4.8%	10.594	9.848	+7.6%
ASMs (B)	2.511	2.371	+5.9%	12.779	12.060	+6.0%
Load Factor	80.6%	81.4%	-0.8 pts	82.9%	81.7%	1.2 pts

Source: RBC Capital Markets estimates, Company websites

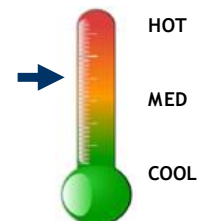
## Bombardier New Order Heat Map

We outline order campaigns in which we believe Bombardier Aerospace (BA) is participating. The bigger the heat, the bigger the potential impact on the BBD shares, in our view.

CUSTOMER	TYPE	SIZE / VALUE	TIMING / COMMENTS	HEAT
<b>Qatar Investment Authority</b>	<b>Commercial:</b> C-Series	100 potential (~\$8B)	QIA and Qatar Air plan to submit a joint application to set up a new Indian carrier according to Bloomberg. Indicated 100 planes needed for the new venture and interest in the C-Series.	
<b>Multiple airlines</b>	<b>Commercial:</b> C-Series	Potentially 50+ (~\$3.4B)	With eight airlines with C-series' order commitments (at 200+ aircraft), BBD could announce several conversions to firm orders.	
<b>Chinese Airlines</b>	<b>Commercial:</b> C-Series	+20 potential order size (+\$1.4B)	BBD flew in the CS300 to Air Show China last month, which generated good interest. With two conditional orders, which includes CDB Leasing (five CS100s and ten CS300s) and Zhejiang Loong Airlines (LOI signed for 20 CS100s) we continue to look for these orders to convert, and potentially new ones in the region.	
<b>Latin American Airlines</b>	<b>Commercial:</b> C-Series	Uncertain	Bombardier is set to take the C-Series on a Latin American tour later this year. The plane is set to stop in every country from Mexico to Argentina – according to Bombardier executives.	
<b>JetBlue</b>	<b>Commercial:</b> C-Series	Uncertain	Following the Delta win, JetBlue has resumed talks with Bombardier. The C-Series may substitute E-190s for short-haul, high-frequency routes out of Boston.	
<b>AtlasJet</b>	<b>Commercial:</b> C-Series	LOI signed for 10 CS300 + 5 options	The LOI was signed November 2011. We expect this order to firm once in-flight data is compiled.	
<b>SpiceJet (WON)</b>	<b>Regional:</b> Q400	Up to 50	The carrier is looking to buy 50 additional regional jets and is in talks with Bombardier, ATR and Embraer about placing a large aircraft.	
<b>CityJet</b>	<b>Commercial:</b> C-Series	Uncertain	CityJet chose to take 15 Superjets over 12-year leases. A C-Series order is still possible, but timing has likely been pushed out.	
<b>Delta Air Lines</b>	<b>Regional:</b> CRJ900	Potentially 50+ (~\$2.3B)	Recent Union negotiations failed to secure scope-clause changes for 100-seat jets to be flown by regional airliners. Next opportunity will be in 2018.	

### OVERALL HEAT GAUGE

We are maintaining the heat at more elevated levels. With the C-Series now on revenue generating flights, and as performance and dispatch reliability numbers come in, we are seeing a pick-up in interest in the C-Series. While the Paris Air Show in June will be good test, and while order announcements cannot be timed, we will be looking for indications of the broader interest in the aircraft at the air show.





## Air Buzz

As part of RBC Flight Deck, we highlight news with implications relevant to the regional jet and Canadian aerospace industry, in particular as related to Bombardier and CAE.

### Bombardier

#### Narrow-bodies

- **No dumping allowed.** The U.S. International Trade Commission is opening an investigation into commercial aircraft imports from Canada, following dumping allegations by Boeing against Bombardier for their sale of C series jets to Delta Airlines. Boeing argued that Bombardier unfairly aided by the Canadian government financially, resulting in excess market supply and delivery of jets at costs below production, \$19.6MM sale price compared to a \$33.2MM production cost. Canadian Prime Minister Justin Trudeau defended the government's financial aid to the company, highlighting the importance of upholding Canadian competitiveness. (Flight Global, April 28)
- **Pension plans getting active.** The Canada Pension Plan Investment Board (CPPIB), Ontario Teachers' Pension Plan (OTPP), Caisse de dépôt et placement du Québec, and British Columbia Investment Management Corp. voiced their opposition for re-electing Pierre Beaudoin, Bombardier's Executive Chairman. Bombardier's senior executive pay raises worth \$32MM raised concerns among investors and government officials given the company's receipt of \$1.37B of government financial aid. On May 11, Beaudoin stepped down from his Executive Chairman role—instead continuing to lead as Chairman of the Board of Directors. (Sources: Globe and Mail, May 11)
- **MRO service, more sales.** Bombardier opened a new 8,500 square meter maintenance, repair and overhaul (MRO) facility in Tianjin, China. It will offer hangar space, offices, as well as back shop areas. This is a part of Bombardier's strategy to serve a larger segment of Asia's aerospace industry. The facility strives to strengthen Bombardier's customer support network in China, with support from more Field Service Representatives, Customer Support Account Managers, and four Authorized Service facilities. (Source: Bombardier, April 7)

#### Regional jets

- **RJ rumble in Paris.** The battle between Airbus and Boeing tends to attract most of the attention, but the regional jet arena is arguably more competitive, as new manufacturers try to take share from Bombardier and Embraer. While Mitsubishi (MRJ), Comac (ARJ), and Sukhoi (SRJ) took over 30% of the regional jet orders the past three major air shows, only ATR was able to register an order in Paris for 2 ATR72 turboprops outside of Bombardier and Embraer. Bombardier did not register a CRJ order, but came away with orders for 59 Q400 turboprops valued at \$1.9B at list. While Embraer continued to lead the pack on the regional jet side, racking up 8 orders for its current generation ERJ and another 30 for its second generation E2 regional jet. However, there continues to be a gap in the production skyline for Embraer between the E1 and E2, and although the 8 E1 orders are helpful, there still remains a significant production gap that will need to be filled. (Company reports, June 20).

#### Business jets

- **End of litigation a Triumph.** Bombardier and Triumph agreed to resolve all outstanding commercial dispute and pending litigation related to the wing components for the Global 7000 program. Terms of the settlement were not released, but relations between the manufacturers are back to business as usual, accordingly to company press releases. (Sources: Bombardier; Triumph, May 24)



## CAE

### Civil

- **IATA revised 2017 industry profitability outlook** – forecasting higher revenue and profits: At the IATA AGM in June, IATA released their revised 2017 outlook, pointing to higher revenue and profits reflecting increased passenger and cargo demand. Highlights include:
  - **Top and bottom line growth in the industry:** Airlines are expected to report ~\$743BN in revenue (up from previous forecast of \$736BN) and ~\$31.4BN in profit (up from previous forecast of \$29.8BN). Growth in revenue is supported by increased demand for cargo and passenger businesses, partly offset by rising fuel, labor and maintenance expenses pressuring margins. The industry is expected to retain a net profit of \$7.69 per passenger (vs. \$9.13 in 2016 and \$10.08 in 2015).
  - **Strong passenger and cargo demand:** IATA forecasts passenger demand to grow by 7.4% in 2017, similar to growth rates posted in 2016. The increase will translate into an additional 275 million passengers, bringing the total number of flyers to 4.1 billion, marking the largest absolute passenger number increase ever recorded. Cargo demand is expected to grow by 7.5% in 2017, more than double the 3.6% rate realized in 2016, with total cargo carried expected to reach 58.2MM tonnes.
  - **Fuel, labor and supply costs offset top line growth:** IATA estimates that revenue increases realized will be partially offset by increasing fuel and labor costs. At ~\$54/barrel for the year, IATA estimates the industry's total fuel bill will reach \$129BN. Unit labor costs is forecasted to increase by almost 3%, offsetting some of the sector's productivity gains. (IATA, Jun 5, 2017)

### Military

- **Canada announces plans to increase defense budget by 73% over the next decade:** The Defense Minister announced that Canada's military spending would jump by ~73% by 2026/2027 to C\$32.7BN, up from C\$18.9BN in 2016/2017, with larger increases in outer years. The increased spending is unveiled as part of a new 20-year defense policy, and would take total defense expenditures from 1.2% of GDP now to ~1.4% of GDP by 2024/2025. Plans for the new budget include the purchase of 88 advanced fighter jets to replace its aging fleet of 77 CF-18 planes, and could imply higher demand for military pilot training in the coming years. (Reuters, Jun 7, 2017)



## The Landing Strip

### MAKS

**When:** July 13-20

**Where:** Moscow, Russia

**What:** The International Aviation and Space Salon MAKS holds one of the world's largest aviation forums. The main objective of MAKS is to demonstrate the achievements of Russian high tech and receptiveness of the domestic Russian market to joint projects with foreign partner.

**The Buzz:** MAKS provides a comprehensive insight into the priorities and achievements of the Russian aerospace industry. Some prototypes of aircrafts and combat systems as well as experimental units that for one reason or another cannot be shown abroad, are demonstrate exclusively at MAKS. Experts believe that Sukhoi could launch a stretched version of its SuperJet at this year's MAKS, which would take its seat capacity up from 100 and inot the CS300 seating capacity towards 120+ seats.



Appendix 1: Airline Comparables

	Symbol	21-Jun-17 Price	EV/EBITDAR				EV/Sales				EBITDAR Margin				2018 FCF yield	Net Debt to EBITDAR	
			2015	2016	2017E	2018E	2015	2016	2017E	2018E	2015	2016	2017E	2018E			
<b>Discount Airlines</b>																	
WestJet	WJA-CA	C\$	\$22.71	4.9x	5.1x	5.5x	5.0x	1.2x	1.2x	1.1x	1.0x	25%	24%	20%	21%	3.4%	1.9x
Southwest	LUV-US	US\$	\$61.03	7.3x	7.0x	7.1x	6.2x	2.0x	1.9x	1.8x	1.7x	27%	27%	26%	28%	7.2%	0.3x
JetBlue	JBLU-US	US\$	\$22.54	5.5x	4.8x	5.3x	4.8x	1.5x	1.5x	1.4x	1.3x	28%	31%	26%	26%	9.2%	1.1x
<b>Discount Average</b>				<b>5.9x</b>	<b>5.7x</b>	<b>6.0x</b>	<b>5.3x</b>	<b>1.6x</b>	<b>1.5x</b>	<b>1.4x</b>	<b>1.3x</b>	<b>27%</b>	<b>27%</b>	<b>24%</b>	<b>25%</b>	<b>6.6%</b>	<b>0.7x</b>
<b>Mainline Airlines</b>																	
Air Canada	AC-CA	C\$	\$17.11	4.7x	4.3x	4.7x	3.9x	0.9x	0.8x	0.8x	0.7x	18%	19%	17%	19%	10.5%	2.3x
Delta Air Lines	DAL-US	US\$	\$52.27	5.4x	5.2x	5.4x	5.1x	1.1x	1.2x	1.1x	1.1x	21%	22%	21%	22%	12.0%	0.9x
United Continental	UAL-US	US\$	\$77.59	4.7x	4.5x	5.0x	4.7x	1.0x	1.0x	1.0x	0.9x	21%	23%	20%	20%	11.2%	1.7x
American Airlines	AAL-US	US\$	\$48.43	5.0x	4.9x	5.5x	5.3x	1.1x	1.1x	1.1x	1.0x	22%	23%	20%	20%	12.6%	2.5x
<b>Mainline Average</b>				<b>5.0x</b>	<b>4.7x</b>	<b>5.1x</b>	<b>4.6x</b>	<b>1.0x</b>	<b>1.0x</b>	<b>1.0x</b>	<b>1.0x</b>	<b>21%</b>	<b>22%</b>	<b>19%</b>	<b>20%</b>	<b>11.6%</b>	<b>1.7x</b>
<b>Regional Airlines</b>																	
Chorus Aviation	CHR-CA	C\$	\$7.44	7.6x	7.3x	6.7x	6.3x	1.5x	1.9x	1.8x	1.8x	20%	25%	27%	28%	13.4%	4.0x
SkyWest Inc.	SKYW-US	US\$	\$36.35	5.6x	5.7x	5.2x	5.9x	2.0x	2.0x	2.0x	2.0x	36%	35%	38%	33%	17.5%	4.1x
<b>Regional Average</b>				<b>6.6x</b>	<b>6.5x</b>	<b>6.0x</b>	<b>6.1x</b>	<b>1.8x</b>	<b>1.9x</b>	<b>1.9x</b>	<b>1.9x</b>	<b>28%</b>	<b>30%</b>	<b>32%</b>	<b>31%</b>	<b>15.5%</b>	<b>4.1x</b>
<b>Airline Average</b>				<b>5.6x</b>	<b>5.4x</b>	<b>5.6x</b>	<b>5.2x</b>	<b>1.4x</b>	<b>1.4x</b>	<b>1.3x</b>	<b>1.3x</b>	<b>24%</b>	<b>25%</b>	<b>24%</b>	<b>24%</b>	<b>10.8%</b>	<b>2.1x</b>

Sources: Company reports, FactSet, and RBC Capital Markets estimates for Air Canada, Chorus Aviation, and WestJet. Priced at the close on June 21, 2017



Appendix 2: Aerospace Comparables

Company	Exch: Ticker	21-Jun Price	CY EPS <sup>(1)</sup>				CY PER				CY EV/EBITDA <sup>(1)</sup>				Mkt Cap B	
			2015	2016	2017E	2018E	2015	2016	2017E	2018E	2015	2016	2017E	2018E		
<b>Aerospace</b>																
Boeing**	NYSE:BA	US\$	\$199.17	\$7.72	\$7.24	\$9.37	\$10.26	23.7x	25.3x	19.6x	17.9x	11.9x	14.6x	10.1x	9.5x	\$120.2
Embraer*	NYSE: ERJ	US\$	\$18.81	\$1.48	\$1.58	\$1.43	\$1.47	13.7x	12.8x	14.2x	13.8x	6.1x	5.5x	5.6x	5.4x	\$3.5
General Dynamics**	NYSE: GD	US\$	\$203.89	\$9.08	\$8.64	\$9.80	\$10.54	21.5x	22.6x	20.0x	18.6x	13.0x	14.5x	12.9x	12.2x	\$61.5
Textron	NYSE: TXT	US\$	\$46.19	\$2.50	\$2.62	\$2.52	\$2.99	19.2x	18.4x	19.0x	16.1x	10.3x	10.3x	10.4x	9.1x	\$12.4
<b>Average</b>								<b>19.5x</b>	<b>19.8x</b>	<b>18.2x</b>	<b>16.6x</b>	<b>10.3x</b>	<b>11.2x</b>	<b>9.7x</b>	<b>9.0x</b>	
<b>Transportation &amp; Conglomerates</b>																
Siemens	XE: SIE	EUR	124.45	6.17	6.93	8.10	8.65	20.2x	18.0x	15.4x	14.4x	14.6x	13.0x	11.2x	10.5x	\$105.8
General Electric	NYSE: GE	US\$	\$27.78	\$1.31	\$1.49	\$1.63	\$1.89	21.2x	18.6x	17.0x	14.7x	16.6x	18.2x	16.1x	15.0x	\$241.9
United Technologies	NYSE: UTX	US\$	\$121.75	\$6.30	\$6.61	\$6.58	\$7.05	19.3x	18.4x	18.5x	17.3x	10.3x	10.8x	10.7x	10.4x	\$97.5
<b>Average</b>								<b>20.2x</b>	<b>18.3x</b>	<b>17.0x</b>	<b>15.5x</b>	<b>13.8x</b>	<b>14.0x</b>	<b>12.7x</b>	<b>11.9x</b>	
Aerospace Multiples								19.5x	19.8x	18.2x	16.6x	10.3x	11.2x	9.7x	9.0x	
Transportation Multiples (ex. GE, UTX)								20.2x	18.0x	15.4x	14.4x	14.6x	13.0x	11.2x	10.5x	
<b>Average</b>								<b>19.9x</b>	<b>18.9x</b>	<b>16.8x</b>	<b>15.5x</b>	<b>12.5x</b>	<b>12.1x</b>	<b>10.4x</b>	<b>9.7x</b>	
<b>Bombardier</b>	<b>TSX: BBD.B</b>	<b>C\$</b>	<b>\$2.48</b>	<b>\$0.16</b>	<b>-\$0.15</b>	<b>-\$0.03</b>	<b>\$0.11</b>	<b>11.5x</b>	<b>nmf</b>	<b>nmf</b>	<b>17.1x</b>	<b>10.5x</b>	<b>13.0x</b>	<b>11.0x</b>	<b>7.3x</b>	<b>\$5.5</b>

\* Covered by RBC Dominion Securities, Industrials analyst Derek Spronck

\*\* Covered by RBC Capital Markets, LLC Aerospace and Defense analyst Matthew McConnell

(1) Peer group consensus EPS and EBITDA estimates sourced from FactSet

Sources: Company reports, FactSet, and RBC Capital Markets estimates. Priced at the close on June 21, 2017



## Companies mentioned

Air Canada (TSX: AC CN; C\$17.11; Top Pick; Speculative Risk)  
 Bombardier Inc. (TSX: BBD.B.TO; C\$2.47; Outperform; Speculative Risk)  
 CAE Inc. (TSX: CAE.TO; C\$22.29; Sector Perform)  
 Chorus Aviation Inc. (TSX: CHR.TO; C\$7.44; Outperform)  
 Embraer S.A. (NYSE: ERJ; \$18.81; Sector Perform)  
 WestJet Airlines Ltd. (TSX: WJA.TO; C\$22.71; Sector Perform)

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