Media Release

QANTAS GROUP STRATEGY UPDATE

Key points:

- $2 billion cost reduction, including 5,000 jobs
- More than 50 aircraft to be deferred or sold
- $1 billion capital expenditure reduction
- Core investment in customer service to continue

SYDNEY, 27 February 2014: Qantas today announced detail of its $2 billion cost reduction program and capital expenditure review.

Qantas will take action to permanently reduce costs in all parts of the Qantas Group through to FY17, including fleet and network changes, productivity improvements, consolidation of business activities, new technology and procurement savings. More than 50 aircraft will be deferred or sold and the Group's workforce will be reduced by 5,000 full-time equivalent positions by FY17.

The Qantas Group's planned capital expenditure net of operating lease liability[1] will be reduced to $800 million in both FY15 and FY16, a total reduction of $1 billion.

Qantas has reached agreement on the return of its Brisbane Airport terminal lease, together with related assets, to the airport owner at a cash value of $112 million. The broader structural review of the Qantas Group portfolio continues and no final decisions have been made on other assets.

Chief Executive Officer Alan Joyce said Qantas would do everything in its control to overcome some of the toughest market conditions it had ever faced.

Market Conditions

"It's clear that the market Qantas operates in has changed, with structural economic shifts exacerbated by an uneven playing field in Australian aviation policy," Mr Joyce said.

"This situation is reflected in the financial result Qantas announces today, an Underlying PBT[1] loss of $252 million for the half-year. This is an unacceptable and unsustainable result. Comprehensive action is needed in response.

"Qantas' competitors have increased capacity to Australia by 46 per cent since 2009, more than double the world average, at a time of record fuel costs and economic volatility.

"We have met these challenges head on. Over the past four years, we have been carrying out the biggest transformation since Qantas was privatised – cutting comparable unit costs[1] by 19 per cent over four years, introducing new aircraft and technology on a large scale, modernising work practices and revitalising service. But this is not enough for the circumstances we now face.

[1] For definitions please see 'Qantas Group Financial Result' media release Attachment 1 – Review of Operations.

"The Australian domestic market has been distorted by current Australian aviation policy, which allows Virgin Australia to be majority-owned by three foreign government-backed airlines – yet retain access to Australian bilateral flying rights.

"Late last year, these three foreign-airline shareholders invested more than $300 million in Virgin Australia at a time when, as Virgin Australia reported to the ASX on 6 February, it was losing money. That capital injection has supported continued domestic capacity growth by Virgin Australia despite its growing losses.

"The Virgin Australia Group has increased capacity into the domestic market at more than twice the rate of the Qantas Group since July 2011. As a result of these combined capacity increases, the total domestic profit pool has been shrunk from more than $700 million in FY12 to less than $100 million in 1H14.

"We have been clear with the Australian Government about the uneven playing field and the measures we believe could address it. But our focus today is on the immediate steps that Qantas must take."

Immediate Priorities

"We must take actions that are unprecedented in scope and depth to strengthen the core of the Qantas Group business.

"To reach $2 billion in cost cuts over three years, we have to work our assets harder, become more productive, retire older aircraft, and make sure that our fleet and network are the right size. We must defer growth and cut back where we can, so that we can invest where we need to.

"We have already made tough decisions and nobody should doubt that there are more ahead.

"While the implementation and pace of delivery must change, the guiding principles of our strategy will not. Safety remains our first priority and we are committed to being the airlines of choice for customers in all our markets.

"Our long-term goal remains the transformation of the Qantas Group for profitable, sustainable growth.

"Over the next three years, we aim to secure our strong Group domestic position and maximise Qantas International's competitiveness.

"Qantas Loyalty will continue to access new markets and revenue streams, building on its success to date.

"When it comes to Jetstar in Asia, we need to take the right decisions in accord with current market circumstances and our balance sheet. In Singapore, growth has been suspended by the Jetstar Asia Board until such time as conditions improve.

"The over-arching focus in Asia continues to be profitably bedding down existing businesses and partnerships. Jetstar has been a pioneer Australian brand across Asia and we continue to see major opportunities for it in the world's fastest-growing aviation region."

Commitment to Customers

"Despite the tough decisions we have to make, we will keep delivering outstanding service for our customers," Mr Joyce said.

"Important customer investments will continue, such as the upgrade of our Airbus A330 fleet and the opening of new lounges in Hong Kong and Los Angeles, and the service that Qantas passengers receive will not be compromised. Thanks to the skill and commitment of our people, we have earned record customer advocacy, and we plan to keep it there."

Accelerated Qantas Transformation Program

Fleet and Network

After a detailed review of network and schedules, the Qantas Group will re-assign aircraft to better match demand, defer aircraft orders, dispose of aircraft, increase fleet utilisation and exit under-performing routes.

- Qantas Domestic will increase utilisation of narrow-body aircraft, allowing Airbus A330 aircraft in the domestic market to concentrate solely on East-West services and peak services on the Sydney-Melbourne-Brisbane triangle.
- A330-200s will be freed up to enter the Qantas International fleet as replacement aircraft, helping to accelerate the retirement of older Boeing 747 aircraft.
- All six of Qantas International's non-reconfigured B747s will be retired ahead of schedule, by the second half of FY16. Nine reconfigured B747s with A380-standard interiors will remain.
- Qantas' final two B737-400s have been retired this month and all B767s will be retired by the third quarter of FY15, resulting in cost and passenger benefits from fleet simplification.
- Qantas International's eight remaining A380 orders will be deferred, with an ongoing review of delivery dates to meet potential future requirements. Schedule changes will allow maximum use of Qantas' current 12 A380s.
- The final three of 14 Jetstar B787-8s on firm order will be deferred.
- Jetstar's A320 order book has been restructured.

In total, more than 50 aircraft will be deferred or sold.

By FY16, the Group's passenger fleet will have been simplified from 11 aircraft types to seven aircraft types, with an average age of eight years.

Over the next 12 months, Qantas will exit underperforming routes and make aircraft changes on certain routes to better match capacity to demand.

- Qantas International will withdraw from the Perth-Singapore route (first quarter FY15).
- Qantas' Brisbane-Singapore and Sydney-Singapore services will be operated by A330s, replacing B747s (first quarter FY15)
- Qantas services between Melbourne and London will be re-timed in November 2014 to reduce A380 ground time in Heathrow (second quarter FY15). There are no changes to overall capacity on London flights.
- The Melbourne-London service change frees up an A380 for additional flying, and Qantas will evaluate opportunities to use the aircraft on other routes.

Workforce Changes

Over the next three years, Qantas will reduce employee numbers across the Group by the equivalent of 5,000 full-time positions, through measures including:

- Reduction of management and non-operational roles by 1,500.
- Operational positions affected by fleet and network changes.
- Restructure of line maintenance operations.
- The closure of Avalon maintenance base, as previously announced.
- Restructure of catering facilities including the closure of Adelaide catering, as previously announced.

The wage freeze for executives implemented in December 2013 will continue and will be extended to all Qantas Group employees.

The wage freeze will be:

- Ongoing for executives.
- Immediate for open EBAs.
- Proposed for other EBA-covered staff.

This is in addition to the reduction of fees paid to the Qantas board and a reduction in the take home pay of the Qantas CEO by 36 per cent this financial year.

No pay rises or bonuses will be contemplated until Qantas is profitable again on a full-year Underlying PBT basis.

Mr Joyce said these were hard but necessary decisions to protect as many Qantas jobs as possible and build a strong business for the future.

“I regret the need for these wide-ranging job losses, but we will do everything we can to make the process easier for employees who leave the business,” Mr Joyce said.

“At the end of this transformation, Qantas will remain an employer of more than 27,000 people, the vast majority based in Australia – and we will be a better and more competitive company.”

Capital Expenditure and Financial Position

The Group’s planned capital expenditure net of operating lease liability in FY14 will be $1 billion.

Planned capital investment, including movements in operating lease liabilities, will be $800 million per year in FY15 and FY16 – a total reduction of $1 billion over the two years. Qantas will maintain flexibility to make further changes if needed.

Transformation through FY17 will be funded through the reprioritisation of capital, future free cash flow as benefits from the cost reduction program begin to flow, and asset sales. Qantas continues to target positive free cash flow[1] from FY15, with capital expenditure aligned to financial performance.

Qantas has total liquidity of $3 billion, comprising $2.4 billion in cash and $630 million in standby debt facilities, as at 31 December 2013.

Update on Structural Review

Qantas has reached agreement on the return of its Brisbane Airport terminal lease, together with related assets, to Brisbane Airport Corporation, with a cash value of $112 million to be recognised in the second half of FY14.

Qantas continues to work through the broader structural review of the Qantas Group portfolio launched in December 2013.

The review has identified a number of high-quality assets of significant value.

No final decisions have been made about other assets within the Group’s portfolio.

Qantas will update the market as and when required.

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