The forecasts in this document are forecasts of aviation demand, driven by models built on forecasts of economic activity. There are many assumptions in both the economic forecasts and in the FAA models that could impact the degree to which these forecasts are realized. This year’s forecast is driven, at least in the short-term, by a number of factors including the strength of the economic recovery and any impact resulting from the U.S. government fiscal situation. Also, as numerous incidents in the past few years (like the attempted bombing of a Northwest airliner on Christmas Day 2009, the discovery of multiple devices on cargo flights out of Europe in October 2010) remind us, terrorism remains among the greatest risks to aviation growth. Any terrorist incident aimed at aviation would have an immediate and significant impact on the demand for aviation services that would be greater than its impact on overall economic activity.

Although oil prices remained high for most of 2014, the recent volatility reminds us there is still considerable uncertainty as to the future direction of oil prices. The FAA’s baseline forecast (derived from economic assumptions in IHS Global Insight’s December 2014 U.S. macro forecast and 30-Year Focus released during the fourth quarter of 2014) calls for a sharp decrease in oil prices in 2015 to $60.50/bbl. Over the next six years (2015-21), the price of oil increases an average of 10.8% a year, to $112/barrel. After 2021, price increases moderate to average 2.7 percent a year for the remainder of the forecast period, reaching $162/barrel by the end of the forecast period in 2035. Some forecasters are calling for a more gradual rebound in the price of oil. In January 2015, the World Bank released its latest commodity price forecast. The forecast calls for oil prices to fall to $53/bbl in 2015, then rising to about $74 in 2020, and only exceeding $100/bbl in 2025. The International Monetary Fund (IMF) also sees oil price increasing at a more moderate rate than the FAA’s base forecast, as its January 2015 forecast called for oil prices increasing from $51/bbl in 2015 to only $68.5/bbl by 2020. Over the long run, lower oil prices give consumers an impetus for additional spending, including air travel, and should enhance industry profitability. However lower oil prices could delay orders for new aircraft as carriers focus on maintaining and increasing cash balances and weigh the savings from new aircraft vs the costs of operating an older fleet.

The baseline forecast assumes that global economic growth will accelerate, over the next few years, but weakness in certain areas may threaten the strength and sustainability of the expansion. The baseline forecast assumes that growth in the emerging market economies will be significantly higher than in the other large economies, in particular the U.S., Japan and the European Union. While economic growth appears to be picking up in the U.S., there are concerns about the strength of demand in Japan and in the European Union as these areas continue to be constrained by structural economic problems and institutional constraints. In addition, many countries in the European Union are still grappling with the impacts of fiscal austerity policies, aimed at reducing government spending and debt, implemented during the past four years which have prolonged the regional downturn. Furthermore the steps that were taken to resuscitate the global economy may prove to be excessive, since the resulting surge in liquidity growth may cause asset bubbles and exacerbate existing global imbalances. The
current forecasts assume strong passenger growth for travel between the United States and other world regions. Any slowing of worldwide economic activity could seriously inhibit the growth in global passenger demand.

With the merger of American Airlines and US Airways completed, the outlook for further consolidation via mergers and acquisitions (M&A) appears to be rather limited. Based on FY 2014 data, the Big 3 (American, Delta, and United) plus Southwest accounted for almost 77% of the U.S. airline industry capacity and traffic. Of the network carriers, only Alaska remains independent, although it does have code share agreements with both American and Delta. In the low cost carrier sector, the merger between Southwest and AirTran achieved full integration of the fleet and a single ticketing system during 2014. Aside from Southwest and AirTran, there appears to be little scope for further consolidation as there are significant obstacles. In particular the financial situation of many low cost carriers limits the possibilities of additional merger activity. For many low cost carriers, the sheer size of merger transactions or the amount of financial risk associated with a merger makes further merger activity unlikely. However, U.S. airlines are continuing to explore other options including global alliances. Many of the major carriers in the U.S. are members of global alliances that operate with some measure of anti-trust immunity from the U.S. DOT. While anti-trust immunity may provide flexibility for airline operators across borders, it may create an anti-competitive environment in the marketplace. These market consolidating vehicles, particularly the anti-trust immunity provisions, may invite increased regulatory scrutiny. If such oversights are launched in the future, this will complicate the evolving structure of the airline industry and may impact demand via new regulations.

The forecast assumes the addition of sizable numbers of large regional jets (70 to 90 seats) into the fleet of regional carriers. However, the regional carriers’ future is closely linked to those of the larger network carriers. As demand continues to slowly recover, financial pressures on regional operators have increased. Furthermore, as consolidation has occurred among the network carriers, many regional carriers have found themselves either saddled with excess capacity or lack of sufficient capacity, or lack of feed traffic. The network carriers continue to make adjustments to the size and breadth of their networks, without providing opportunities for regional carriers to backfill the loss of the mainline service. Delta is well along in its plans to reduce its small (read 50 seat) regional jet fleet and plans to retire another 50 to bring its total to just 125, down from almost 500 at the end of 2009. United is adding 85 Embraer 175’s to its partners’ regional fleet and reducing the number of small regional jets flown by its partners to 242 by the end of 2015 from an estimated 380 at the end of 2012. Meanwhile the new American Airways is planning to reduce its small regional jet fleet by 21 aircraft in 2015. While these actions may provide some opportunities for well positioned regional carriers, the overall impact of consolidation so far has been to reduce opportunities for regional flying substantially.

After suffering through a significant downturn in 2009-10, business and corporate aviation have seen a partial recovery during the past four years, with promising increases in aircraft deliveries in 2014. The pace of the recovery in business and corporate aviation is largely based upon the future prospects of economic growth and corporate profits. Future uncertainty in these leading indicators could pose a risk to the forecast, but the risk is not limited to these factors. Public perception of business and corporate aviation, potential environmental regulations and taxes, along with increased security measures placed on business jets, will
place downward pressure on the forecast. On the other hand, while corporate profits are currently high, perceived economic and political uncertainties are causing companies to postpone their purchase of new business aircraft. Translation of this pent-up demand into sales of business jets in the near future can create an upward impact on the forecast. The impact of fuel price decline on business aircraft demand is also uncertain. While a positive effect on corporate profits will increase the demand, revenue losses resulted from low fuel prices may move the demand in the other direction.

Other factors, such as new and more efficient product offerings and increased competition from new entrant manufacturers, serve to broaden the potential of the industry. Estimates show that a record number of new business jets are delivered overseas and, with the potential easing of regulations on the use of airspace in foreign countries, the scenario for business jet manufacturers looks all the more promising. Raising the level of security restrictions, and the subsequent travel hassles placed on airline passengers, could make corporate jet travel look increasingly appealing.

Not only is the volume of aircraft operating at most large hubs expected to increase over the next 20 years, but the mix of aircraft is changing for this same period. The expected increases in the numbers of regional jets and business jets will increase the impact on the national airspace system and make the FAA’s job more challenging. This change in the mix of aircraft will impact workload strictly due to the increasing demand for aviation services projected over the forecast period.

Although overall activity at FAA and contract towers fell in 2014, activity at 10 of the Core 30 airports increased in 2014 and delays remained at historically high levels at many U.S. airports. As demand recovers and workload increases, congestion and delays could become a critical limit to growth over the forecast period. FAA’s forecasts of both demand and operations are unconstrained in that they assume that there will be sufficient infrastructure to handle the projected levels of activity. Should the infrastructure be inadequate and result in even more congestion and delays, it is likely that the forecasts of both demand and operations would not be achieved.

There are concerns that aviation’s impact on the environment could potentially restrict the ability of the aviation sector to grow to meet national economic and mobility needs. Airport expansion or new construction is often a contentious issue because of noise, air quality, and water quality concerns. There is also an ongoing effort to address the climate impacts of aviation. Aviation currently accounts for two to three percent of global carbon emissions, but this percentage is expected to increase with the growth in operations unless mitigated with new technologies and standards, renewable fuels, operational improvements and potentially as a gap filler, market based measures. While certain measures to address climate impacts can result in reduced costs, such as increased fuel efficiency, other measures, such as market instruments could pose additional constraints on growth. Energy concerns are also rising, driven by spikes in fuel prices, supply and security issues, and concerns about fossil fuel emissions contributing to global climate change. Lack of progress in improving the environmental and energy outlook for the future fleet may result in more access restrictions or operating limitations on the fleet in service which in turn may depress growth. By contrast, breakthroughs in quieter, cleaner aircraft technologies and renewable fuels could reduce environmental and energy constraints on the forecast, and enable sustainable growth.