Media Release

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QANTAS GROUP FINANCIAL RESULT

Key points:

- Underlying PBT[1] loss: $252 million
- Statutory Loss After Tax: $235 million
- Yield[1] excluding FX down 3%
- Revenue: $7.9 billion, down 4%
- Underlying fuel costs[1] excluding FX impact: $2.3 billion, up 3%
- Comparable unit costs[1] down 2%
- Liquidity: $3 billion

SYDNEY, 27 February 2014: Qantas today announced an Underlying PBT loss of $252 million and a Statutory Loss After Tax of $235 million for the six months ended 31 December 2013.

The underlying result is in line with guidance and reflects fundamental changes in the Australian aviation market, with a significant deterioration in earnings during the half.

Chief Executive Officer Alan Joyce said the result was unacceptable and comprehensive action would be taken in response.

“We are facing some of the toughest conditions Qantas has ever seen,” Mr Joyce said.

“Australia has been hit by a giant wave of international airline capacity, with a 46 per cent increase in competitor capacity since 2009 – more than double the global increase of 21 per cent over the same period.

“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 and 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.

“Qantas has been undertaking its biggest ever transformation over the past four years, cutting comparable unit costs by 19 per cent over four years, but this is not enough for the circumstances we face now.

“With structural economic changes being exacerbated by the uneven playing field in domestic aviation, we must now take actions that are unprecedented in scope and depth.

“We will accelerate our Qantas Transformation program to achieve $2 billion in cost reductions by FY17. Hard decisions will be necessary to overcome the challenges we face and build a stronger business.”

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[1] For definitions please see Attachment 1 – Review of Operations.

Summary of Results

Qantas Domestic

Qantas Domestic reported Underlying EBIT[1] of $57 million, down from $218 million in 1H13.

Competitor capacity growth in the domestic market continued to outpace Qantas Group capacity growth, as it has since FY12. At the same time, demand was lower than market growth, putting pressure on yields and passenger loads.

Overall, the total domestic profit pool has shrunk from more than $700 million in FY12 to less than $100 million in 1H14. During this period the Virgin Australia Group added 4.5 billion Available Seat Kilometres (ASKs), compared to 4.3 billion ASKs added by the Qantas Group.

A softening resources market, corporate account pricing pressure, and fuel and foreign exchange impacts also affected the Qantas Domestic result.

Despite the challenging market conditions, Qantas Domestic continues to deliver outstanding service, earning record customer advocacy. It was the most punctual major domestic airline in 12 out of 12 months during 2013, while its ongoing fleet renewal program helped reduce unit costs and improve the customer experience.

Qantas Domestic remains the airline of choice for business travellers, holding more than 80 per cent of the corporate market by revenue in the half.

Qantas International

Qantas International reported an Underlying EBIT loss of $262 million, compared with a loss of $91 million in 1H13.

The trend of intense competitor capacity growth in the Australian international market continued in the half. Total international market capacity growth for FY14 is expected to be 9 per cent, well above the global average, resulting in particularly strong yield pressure for Qantas' Asian and European markets.

Qantas International made continued progress in reducing comparable unit costs (by 4 per cent in the half) and maintained record customer advocacy.

However, the lower Australian dollar has meant higher fuel costs, with a significant impact on the long-haul sectors flown by Qantas International.

Jetstar

The Jetstar Group reported an Underlying EBIT loss of $16 million, down from an Underlying EBIT profit of $128 million in 1H13.

Competitive pressure on yields (especially in South East Asia), a $29 million share of associate losses, and fuel price and foreign exchange impacts were the main factors behind the result. Jetstar's domestic operations in Australia remained profitable.

The fundamentals of Jetstar's low-cost carrier model remain strong, with a 2 per cent improvement in unit costs[1] and increased ancillary revenue[1] during the half, and customer advocacy is at record levels. The introduction of the B787-8 into Jetstar's long-haul network is delivering cost and customer service benefits.

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Qantas Loyalty

Qantas Loyalty reported Underlying EBIT of $146 million, a record result[2], up from Underlying EBIT of $137 million in 1H13. The business continues to perform very strongly, with billings up 9 per cent in the half, three million awards redeemed and record customer advocacy. There are currently 9.8 million Qantas Frequent Flyer members[3], with a target of 10 million for the full year.

Qantas Loyalty's growth initiatives are exceeding expectations, with a positive customer response to both the new Qantas Cash member card and the AQUIRE small-to-medium enterprise loyalty platform.

Qantas Freight

Qantas Freight reported Underlying EBIT of $11 million, down from $22 million in 1H13, in the context of reduced capacity, consolidation and a weak global cargo market.

Financial Position and Capital Expenditure

Qantas has strong liquidity of $3 billion, comprising $2.4 billion in cash and $630 million in undrawn debt facilities, as at 31 December 2013. There are no major unsecured debt maturities until April 2015.

Approximately 30 per cent of the Qantas Group's passenger fleet is debt-free. The Group has added 31 new unencumbered aircraft since FY10, including seven added in the first half of FY14. Twenty mid-life aircraft become debt-free in FY14. The Group's average passenger fleet age is 7.6 years, the youngest in two decades.

Capital expenditure in FY14 is weighted to the first half, with $900 million invested in the six months to 31 December 2013 and a further $300 million planned for the second half.

Following the review launched in December, planned capital investment has been aligned with financial performance, with a total reduction of $1 billion over FY15 and FY16. Capital expenditure in FY15 and FY16 will be $800 million in each year, including movements in operating lease liabilities[1], while the Group maintains flexibility to make further changes if needed.

Outlook

The Group's 2H14 operating environment remains very challenging and volatile. Soft underlying domestic demand is continuing in the seasonally weaker half, with domestic and international yields and loads expected to remain depressed.

The Group's current operating expectations are as follows:

- Group capacity to increase by 3-3.5 per cent in 2H14 compared to 2H13.
- Group domestic capacity to increase by 3-4 per cent in 2H14 compared to 2H13, while maintaining flexibility.
- Underlying fuel costs expected to be approximately $4.6 billion in FY14.

No Group profit guidance can be provided at this time due to major transformation being undertaken by Qantas, the high degree of volatility and uncertainty in the competitive environment, global economic conditions, fuel prices and foreign exchange rates.

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[2] Qantas Loyalty record Underlying EBIT result compared to prior periods normalised for changes in accounting estimates of the fair value of points and breakage expectations effective 1 January 2009.
[3] As at February 2014.

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ATTACHMENT 1

REVIEW OF OPERATIONS

The Qantas Group reported an Underlying PBT[1] loss of $252 million for the half-year ended 31 December 2013. Statutory Loss Before Tax of $305 million and Statutory Loss After Tax of $235 million.

The operating environment during the half year was difficult, including:
- Capacity growth running ahead of demand in the Australian aviation market pressuring revenue
- Foreign Government owned or sponsored airline competition in all markets
- Fuel cost increase

Performance highlights include:
- Record result for Qantas Loyalty[2]
- Comparable unit cost improvement[3]

As a result of the deterioration in business performance and operating environment, Qantas has announced:
- An acceleration of the Qantas Transformation Program, targeting $2 billion in cost savings by financial year 2016/2017
- A reduction of 5,000 full time equivalent positions
- Significant changes to fleet plans and network
- A reduction in capital expenditure of $1 billion across financial years 2014/2015 and 2015/2016

Underlying PBT

The Qantas Group half-year Underlying PBT decreased to a loss of $252 million. The result was driven by revenue decline resulting from market growth running ahead of demand in both the domestic and international markets. Improvements in fuel efficiency and comparable unit cost[3] were offset by unfavourable fuel cost and foreign exchange movements. The first half 2012/2013 included the Boeing settlement[4] following the restructuring of the B787-8 deliveries.

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[1] Underlying Profit Before Tax (PBT) is the primary reporting measure used by the Qantas Group's chief operating decision-making bodies, being the Chief Executive Officer, Group Management Committee and the Board of Directors, for the purpose of assessing the performance of the Group. The primary reporting measure of the Qantas International, Qantas Domestic, Jetstar Group, Qantas Loyalty and Qantas Freight operating segments is Underlying EBIT as net finance costs are managed centrally. The primary reporting measure of the Corporate/Unallocated segment is Underlying PBT. Refer to page 15 for a reconciliation of Underlying PBT to Statutory (Loss)/Profit Before Tax.

[2] Qantas Loyalty record Underlying EBIT result compared to prior periods normalised for changes in accounting estimates of the fair value of points and breakage expectations effective 1 January 2009.

[3] Comparable unit cost is adjusted to aid comparability between reporting periods. Comparable unit cost is calculated as Underlying PBT less passenger revenue and fuel, adjusted for the impact of Boeing settlement (first half 2012/2013), changes in foreign exchange rates, B767-300 phased fleet retirement (first half 2013/2014), Share of net loss of investments accounted for using the equity method and movements in average sector length per ASK. Comparable unit cost is the primary measure of unit cost used by the Qantas Group adjusted to aid comparability between reporting periods.

[4] Boeing settlement of $125 million in first half of 2012/2013.

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REVIEW OF OPERATIONS (continued)

Group Underlying Income Statement Summary		December 2013	December 2012	Change	% Change
Net passenger revenue[5]	$M	6,786	7,042	(256)	(4)
Net freight revenue	$M	500	475	25	5
Other revenue[5]	$M	617	725	(108)	(15)
Revenue	$M	**7,903**	**8,242**	**(339)**	**(4)**
Operating expenses (excluding fuel and Share of net loss of investments accounted for using the equity method)[6]	$M	(4,771)	(4,754)	(17)	-
Share of net loss of investments accounted for using the equity method	$M	(26)	(16)	(10)	(63)
Fuel[6]	$M	(2,255)	(2,181)	(74)	(3)
Depreciation and amortisation	$M	(746)	(719)	(27)	(4)
Non-cancellable aircraft operating lease rentals	$M	(261)	(265)	4	2
Expenses	$M	**(8,059)**	**(7,935)**	**(124)**	**(2)**
Underlying EBIT[7]	$M	**(156)**	**307**	**(463)**	**>(100)**
Net finance costs[6]	$M	(96)	(87)	(9)	(10)
Underlying PBT	$M	**(252)**	**220**	**(472)**	**>(100)**

Operating statistics		December 2013	December 2012	Change	% Change
Available Seat Kilometres (ASK)[8]	M	71,844	71,374	470	1
Revenue Passenger Kilometres (RPK)[9]	M	56,393	57,095	(702)	(1)
Passengers Carried	‘000	25,094	24,701	393	2
Revenue Seat Factor[10]	%	78.5	80.0	(1.5)	(2)
Yield (excluding FX)[11]	c/RPK	10.10	10.43	(0.33)	(3)
Comparable Unit Cost[3]	c/ASK	5.04	5.13	0.09	2

5 Net passenger revenue has been adjusted in first half of 2013/2014 to include charter revenue previously reported as Other revenue. First half 2012/2013 net passenger revenue and other revenue has been reclassified accordingly. These items remain excluded from the calculation of yield.

6 Underlying operating expenses (excluding fuel and Share of net loss of investments accounted for using the equity method), fuel and net finance costs differ from equivalent statutory expenses due to items excluded from Underlying PBT, such as adjustments for impacts of AASB 139 which relate to other reporting periods and other items identified by Management. Refer to page 15 for a reconciliation of Underlying PBT to Statutory (Loss)/Profit Before Tax.

7 Underlying Earnings Before Net Finance Costs and Tax (EBIT) is the primary reporting measure for all segments except Corporate/Unallocated.

8 ASK – total number of seats available for passengers, multiplied by the number of kilometres flown.

9 RPK – total number of passengers carried, multiplied by the number of kilometres flown.

10 Revenue Seat factor – RPKs divided by ASKs. Also known as seat factor, load factor or load.

11 Yield (excluding FX) – Passenger revenue excluding foreign exchange, divided by RPKs.

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REVIEW OF OPERATIONS (continued)

Revenue fell four per cent driven by rapid capacity growth in all markets. International competitor capacity has increased 46 per cent into and out of Australia since 2009, more than double the world average at a time of sustained high fuel costs and economic volatility. Foreign airlines have continued to grow capacity aggressively in the Asia-Pacific attracted by the region's relative economic strength. Australian domestic market capacity has continued to grow ahead of demand, driven by competitor capacity growth ahead of the Qantas Group since July 2011. More recently, demand has been impacted by the resource sector slowdown, cautious business environment and low consumer confidence. These conditions have put considerable downward pressure on Group net passenger revenue resulting in three per cent yield decline and a two per cent revenue seat factor reduction during the half.

Net freight revenue increased following the acquisition and consolidation of Australian air Express from November 2012, offset by reductions in Qantas Freight capacity as a result of Qantas International network changes.

Other revenue continued to grow when adjusted for the one-off Boeing settlement in the first half of financial year 2012/2013[4]. Qantas Loyalty delivered continued growth in members and revenue to achieve another record result[2]. Jetstar further improved its ancillary revenues[12] per passenger, on top of four per cent growth in passenger numbers. Third party contract revenue was lower due to the sale of catering centres in the prior corresponding period.

Comparable unit cost[3] improved two per cent reflecting the delivery of Qantas Transformation benefits, successful growth in Qantas Loyalty and continuing cost control across the business.

Fuel costs increased three per cent on prior corresponding period to a record for any half-year period. This was driven by a nine per cent increase in Australian dollar fuel price offset by hedge gains and a three per cent fuel efficiency gain[13] resulting from fleet modernisation and reconfiguration initiatives.

The increase in net finance costs was driven by the increase in net debt.

Segment Performance Summary		December 2013	December 2012	Change	% Change
Qantas Domestic	$M	57	218	(161)	(74)
Qantas International	$M	(262)	(91)	(171)	>(100)
Qantas Loyalty	$M	146	137	9	7
Qantas Freight	$M	11	22	(11)	(50)
Qantas Brands Eliminations	$M	-	2	(2)	(100)
Qantas Brands	**$M**	**(48)**	**288**	**(336)**	**>(100)**
Jetstar Group	$M	(16)	128	(144)	>(100)
Corporate/Unallocated	$M	(92)	(108)	16	15
Eliminations	$M	-	(1)	1	100
Underlying EBIT	$M	**(156)**	**307**	**(463)**	**>(100)**
Net Finance Costs	$M	(96)	(87)	(9)	(10)
Underlying PBT	$M	**(252)**	**220**	**(472)**	**>(100)**

Qantas Domestic reported a half-year Underlying EBIT of $57 million with intense competition and market capacity growth impacting yield and revenue seat factor in addition to unfavourable Australian dollar fuel cost and foreign exchange.

Qantas International Underlying EBIT loss of $262 million for the half-year represents a $171 million reduction on the prior corresponding period. The reduction in Underlying EBIT was due to market capacity oversupply and unfavourable fuel cost and foreign exchange. International market capacity in and out of Australia increased by nine per cent[14] on prior corresponding period as a result of aggressive competitor growth largely from foreign government owned or sponsored airlines. The strength of the Qantas Emirates partnership partially offset revenue decline with codeshare bookings on the alliance double those under previous alliances.

[12] Ancillary revenue per passenger excludes management and branding fee revenue related to Consolidated Entities adjusted for customer mix.
[13] Fuel efficiency is measured as litres per ASK adjusted for movements in average sector length.
[14] BITRE data – November 2013.

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REVIEW OF OPERATIONS (continued)

Qantas Loyalty achieved a record[2] half-year Underlying EBIT of $146 million, a seven per cent improvement on prior corresponding period. Partner expansion and new growth initiatives have driven program membership up eight per cent, to 9.7 million members in December 2013.

Jetstar's half-year Underlying EBIT loss of $16 million reflects the impact of domestic competitive pressures and $29 million in start-up losses through its Jetstar-branded airlines through Asia.

Qantas Freight half-year Underlying EBIT of $11 million is down $11 million on prior corresponding period. This was driven by changes in the Qantas International network, increased market capacity and weaker market conditions. The result also reflects the sale of StarTrack in November 2012 and subsequent integration of Australian air Express into the Qantas Freight domestic business that is now complete.

Qantas' guiding strategic principles remain consistent

Qantas' guiding strategic principles are consistent with our objective to transform the Group's cost base and competitive position to deliver sustainable returns to shareholders:

- Safety is always our first priority
- The first choice for our customers in every market we serve
- Maintaining dual-brand strength in domestic market
- Reshaping Qantas International to remain competitive
- Maintaining the Jetstar opportunity in Asia
- Broadening Qantas Loyalty for strong, diversified earnings
- Driving efficiency and productivity

However, the Group must accelerate the pace of Transformation.

Qantas' priorities are to strengthen the core of our business and protect the sources of our long-term competitive advantage:

- The customer experience on the ground, in the air, and for Frequent Flyers;
- Qantas' domestic dual-brand strength

Qantas is accelerating our business Transformation to drive a recovery in earnings. This will be achieved through operational and structural initiatives while continuing to deliver superior customer product and services and continuing to work closely with our people. The immediate priorities are to:

- Accelerate cost reduction
- Right-size fleet and network
- Work existing assets harder
- Defer growth
- Align capital expenditure to financial performance
- Accelerate simplification

Earnings recovery through accelerating Qantas Transformation

Qantas is accelerating the delivery of strategic initiatives to enable it to remove the cost gap to its domestic competition and to obtain a competitive cost base compared to its international competitors.

Qantas Transformation initiatives delivered to date include:

- Comparable unit cost[3] reduction of 19 per cent over four years to end of financial year 2012/2013 through measures including:
  - Consolidation of engineering and catering facilities
  - 22 per cent improvement in labour efficiency[15] since 2008 across the Group
- Network optimisation
  - Development of strategic partnerships
  - Transferred European hub from Singapore to Dubai
  - Exited under-performing routes
  - Re-timing of the Asian network

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[15] Efficiency improvement is measured as average full-time equivalent employees per passenger.

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REVIEW OF OPERATIONS (continued)

- Fleet renewal and simplification
  - Reconfiguration of Boeing B747-400 and A380-800 aircraft
  - Retirement of B737-400 fleet
  - Retirement of the B767-300 fleet

To address its legacy cost base and work practices and offset the impact of inflation; the more than $500 million[16] increase in fuel price and foreign exchange movement and the reduction in the Group yields of 11 per cent[17], Qantas is targeting an earnings-led recovery through $2 billion in cost savings by financial year 2016/2017. To achieve this the Qantas Group will implement approximately 250 initiatives.

- Right-sizing fleet and network
  - Right Aircraft, Right Route – Qantas will exit underperforming routes and make aircraft changes on certain routes to better match capacity to demand through:
    - Withdrawing Qantas International from underperforming Perth-Singapore route in first quarter financial year 2014/2015
    - Operating all Sydney-Singapore and Brisbane-Singapore services with A330-300s in first quarter of financial year 2014/2015

  - Work existing assets harder – Increase aircraft utilisation through reduced turnaround times, schedule re-design and simplification of the Group's passenger fleet from 11 aircraft types to just seven by financial year 2015/2016 through:
    - Reduction in domestic wide-body aircraft with remaining aircraft focused on East-West and peak Sydney-Melbourne-Brisbane (Triangle) services
    - Free-up A330-200s to enter Qantas International as replacement aircraft
    - Retirement of all B767-300 aircraft by third quarter of financial year 2014/2015
    - Retirement of the six oldest B747-400 (not reconfigured) aircraft by second-half of financial year 2015/2016
    - Re-time services between Melbourne and London to reduce A380-800 ground time in Heathrow and improve revenue in second quarter of financial year 2014/2015

  - Deferring Growth – Qantas will revise its growth forecast to better align with immediate priorities and market demand resulting in:
    - Deferral of eight remaining A380-800 aircraft with ongoing review of delivery dates to meet potential future requirements
    - Deferral of the last three of 14 B787-8 orders
    - Restructure of the A320-200 order book
    - Suspend new growth for Jetstar in Asia and support existing businesses

- Productivity and Consolidation – To contain costs Qantas will create a step change in labour productivity and rationalise activities to achieve a reduction of 5,000 full-time equivalent positions across the Group, expecting to incur approximately $500 million in redundancy costs across financial years 2013/2014 and 2014/2015. This will be achieved through:
  - Operational positions affected by fleet and network changes
  - Reducing management and non-operational areas by approximately 1,500 full-time equivalent positions
  - Freezing wages until the Qantas Group makes a full-year underlying profit
    - Ongoing for executives
    - Immediate for open Enterprise Bargaining Agreements (EBAs)
    - Proposed for other EBA-covered staff
  - Restructure of line maintenance operations
  - Restructure of catering facilities, including the previously announced closure of the Adelaide catering centre
  - Efficiency gain in the engineering supply chain
  - Closure of Avalon maintenance base, as previously announced

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[16] Increase in Australian dollar fuel price and foreign exchange movements between financial year 2008/2009 and financial year 2012/2013.
[17] Yield[11] decline between financial year 2008/2009 and financial year 2012/2013 adjusted for sector length.

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REVIEW OF OPERATIONS (continued)

- Technology – Qantas will use new technology initiatives to enhance efficiency including:
  - Roll out of B787-8
  - Improve Freight supply chain and terminals
  - Rationalise its software applications

- Suppliers – Qantas will improve terms with key suppliers through:
  - Renegotiating commercial contracts across the Group
  - Improved vendor management

Unlocking value through a structural review

Since December 2013 Qantas has been working through a careful, methodical structural review process. Qantas will take the time necessary to make the right strategic decisions for the future. The review has confirmed Qantas has valuable and desirable assets in the portfolio:

- Brisbane airport terminal lease returned to Brisbane Airport Corporation together with related assets for $112 million to be recognised in the second half of 2013/2014
- Sydney and Melbourne terminal discussions continue

Qantas will take the time necessary to make the right strategic decisions for the future, and no final decisions have been made about other assets within the Group's portfolio.

Material Business Risks

The aviation industry is subject to a number of inherent risks. These include, but are not limited to, exposure to changes in economic conditions, significant aviation incidents, changes in government regulations, fuel and foreign exchange volatility and other exogenous events such as natural disasters, war or epidemic.

Qantas is subject to a number of specific business risks which may impact the achievement of the Group's strategy and financial prospects:

- **Competitive intensity** – Market capacity growth ahead of demand impacts industry profitability
  - Australia's liberal aviation policy settings coupled with the strength of the Australian economy relative to global economic weakness has attracted more offshore competitors to the Australian international aviation market, predominantly state-sponsored airlines. Qantas is responding by building key strategic partnerships and accelerating cost base reduction through Qantas Transformation. Qantas continues to leverage its considerable fleet flexibility to adjust capital expenditure in line with financial performance and appropriately manage its network.
  - The Australian domestic aviation market has attracted increased competition in recent years. The resulting intensity of competition as a result of continued capacity growth ahead of demand is being mitigated by maintaining the Qantas Group's market leading domestic position and executing Qantas Group's dual brand strategy. This strategy leverages Qantas Domestic (including QantasLink) to serve business and premium leisure customers and Jetstar to serve price sensitive customers. Qantas Domestic is focused on removing the cost base disadvantage to its competitor through its transformation initiatives and fleet renewal, while Jetstar is working to maintain its low-cost scale advantage and continually lower unit costs.

- **Jetstar-branded airlines in Asia** – The most recent Jetstar-branded airlines being established across Asia (Jetstar Japan and Jetstar Hong Kong) are in the start-up phase. The inherent risk associated with start-up operations, including obtaining necessary regulatory approvals, is being mitigated through strong local partners, leveraging their strength in each market, sharing risk through appropriate equity structures and appropriate contractual protection in relation to, inter alia, fleet procurement transactions.

- **Credit rating** – In the period Qantas' credit rating was downgraded to Ba2 negative watch and BB+ stable by Moody's and Standard and Poor's respectively. This may increase the price of new debt funding and/or reduce the Group's access to some sources of unsecured credit (including certain operational and working capital facilities) over time.

Qantas mitigates the potential impact of risk on the Group's financial prospects by maintaining a strong capital base to maintain creditor confidence, sustain future development of the business and maximise shareholder value. Qantas targets a capital structure consistent with an investment grade credit rating while maintaining adequate liquidity. The Group maintains access to a broad range of capital sources and the capacity to manage capital expenditure through a flexible fleet order book and processes to strategically prioritise investments and divest non-core assets.

The immediate priority to transform the cost base will result in credit metrics remaining outside the investment grade range for the immediate future. Qantas Transformation is to be funded through the reprioritisation of capital, asset sales and future free cash flow benefits from Qantas Transformation from financial year 2014/2015 onwards.

In addition, due to the size and complexity of the operations, Qantas is also exposed to a number of other risks that may impact the Group:

- **Industrial relations** – The risk of industrial action relating to Qantas' collective agreements with its employees is being mitigated through continuous stakeholder and employee engagement initiatives. The success of these programs is reflected through improving employee engagement scores.
- **Continuity of critical systems** – The Group's operations depend on the continuous functioning of a number of information technology and communication services. The Group has an extensive control and management framework to reduce the likelihood of outages, ensure early detection and to mitigate the impact.

Securing the future with financial discipline

- Maintaining a strong liquidity position
- Prudent capital management

Cash Flow Summary		December 2013	December 2012	Change	% Change
Cash generated from operations	$M	692	788	(96)	(12)
Other operating cash flows	$M	(111)	(8)	(103)	>(100)
Operating cash flows	$M	581	780	(199)	(26)
Investing cash flows	$M	(939)	(575)	(364)	(63)
Net free cash flow[18]	$M	**(358)**	**205**	**(563)**	**>(100)**
Financing cash flows	$M	(82)	(547)	465	85
Effect of foreign exchange on cash	$M	6	2	4	>100
Cash at period end	$M	**2,395**	**3,058**	**(663)**	**(22)**

The Group finished the period with a strong liquidity position of $3.0 billion[19]. Net free cash flow was negative in the period as a result of the operating result and the weighting of investing cash flows in the first half of the 2013/2014 financial year. Total financial year 2013/2014 investing cash flows are expected to be $1.2 billion.

The operating cash flows were favourable to prior corresponding period after allowing for one off receipts in the first half of 2012/2013 for Boeing Settlement and proceeds related to the sale of StarTrack and catering facilities. This was driven by a recovery in bookings which had temporarily declined pending regulatory approval of the transfer of our European Hub through Dubai announced in September 2012 and increased sales through our strategic partner airlines.

Seven new unencumbered A320-200 aircraft were added to the fleet.

The Group continues to retain significant flexibility in its financial position, funding strategies and fleet plan to ensure that it can respond to changing market conditions.

[18] Net free cash flow – Operating cash flows less investing cash flows. Net free cash flow is a measure of the amount of operating cash flows that are available (i.e. after investing activities) to fund reductions in net debt or payments to shareholders.

[19] Includes cash and cash equivalents and $630 million undrawn revolver facility at 31 December 2013.

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REVIEW OF OPERATIONS (continued)

Debt and Gearing Analysis		**December 2013**	**December 2012**	**Change**	**% Change**
Net on balance sheet debt[20]	$M	3,829	3,226	603	19
Net Debt including operating lease liabilities[21]	$M	5,334	4,847	487	10
Adjusted Equity[22]	$M	5,549	5,717	(168)	(3)
Gearing Ratio[23]		49:51	46:54	3 pts	7

Fleet

The Qantas Group remains committed to a fleet strategy that provides for long-term fleet flexibility, renewal and simplification. The fleet strategy is designed to support the strategic objectives of the Group's two flying brands, whilst retaining significant flexibility to respond to changes in market conditions.

At 31 December 2013, the Qantas Group fleet, including Jetstar Asia, Qantas Freight and Network Aviation, totalled 318 aircraft. During the first half of 2013/2014 the Group purchased 15 aircraft and leased 2 aircraft:

- Qantas – four B737-800s (owned), two Bombardier Q400s (owned) and two B717-200s (leased).
- Jetstar (including Jetstar Asia) – two B787-8s (owned) and seven A320-200s (owned).

The Group removed 11 aircraft from service during the first half of 2013/2014 including four lease returns. This included one B747-400, five B767-300s, three B737-400s and two EMB120s.

The Qantas Group's scheduled passenger fleet average age is now 7.6 years, the lowest average age since privatisation. The benefits of fleet investment include improved customer satisfaction, environmental outcomes, operational efficiencies and cost reductions.

With the fleet modernisation program nearing completion the low fleet age will enable planned capital expenditure net of operating lease liability[24], to be reduced by $1 billion over two years to $800 million in financial year 2014/2015 and $800 million in financial year 2015/2016.

[20] Net on balance sheet debt includes interest-bearing liabilities and the fair value of hedges related to debt less cash, cash equivalents and aircraft security deposits.

[21] Net Debt including operating lease liabilities includes net on balance sheet debt and off balance sheet aircraft operating lease liabilities[24].

[22] Adjusted Equity includes Equity adjusted to exclude hedge reserves.

[23] Gearing Ratio is net debt including operating lease liability to net debt including operating lease liability and adjusted equity. The gearing ratio is used by management to represent the Qantas Group's debt obligation including obligations under operating leases[24].

[24] Operating lease liability is the present value of minimum lease payments for aircraft operating leases which, in accordance with AASB 117: Leases, is not recognised on balance sheet. This operating lease liability has been calculated as the present value of future non-cancellable operating lease rentals of aircraft in service, using a discount rate of seven per cent applied in Standard and Poor's methodology.

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REVIEW OF OPERATIONS (continued)

Qantas Domestic

- Domestic market yields and revenue seat factor adversely impacted by market capacity growth running ahead of demand
- Comparable unit cost[3] improvement of one per cent
- Superior on-time performance
- Record levels of customer advocacy

		December 2013	December 2012	Change	% Change
Total Revenue and Other Income	$M	3,086	3,220	(134)	(4)
Revenue Seat Factor	%	74.9	76.9	(2.0)pts	(3)
Underlying EBIT	$M	57	218	(161)	(74)

Qantas Domestic Underlying EBIT of $57 million for the half-year ended 31 December 2013 was down from $218 million in the prior corresponding period.

The reduction in Underlying EBIT was largely driven by rapid domestic market capacity growth, unfavourable fuel cost and foreign exchange. Revenue has been further impacted by softening resource sector demand, particularly in the Western Australian and Queensland markets. This challenging competitive environment resulted in reduced revenue seat factor and weaker yields. However Qantas continues to be the clear choice for business travellers and has maintained over 80 per cent share of corporate market revenue.

Qantas Domestic's comparable unit cost[3] improved one per cent on prior corresponding period. Cost savings included transformation benefits following consolidation of the Qantas Heavy Maintenance Bases and completion of the fleet renewal.

Qantas Domestic recorded its best half-year of domestic customer advocacy since recording commenced in August 2008. Qantas Domestic was recognised through a number of industry awards:
- 'Best Domestic Airline'[25] four years running
- 'Best Economy'[26] noting that Qantas Domestic was the world's best by a wide margin
- 'Best Lounges'[26]

Qantas Domestic has achieved superior on time performance for the fifth year running[27] beating its main competitor in an unprecedented 12 out of 12 months in calendar year 2013.

Qantas Domestic continued to strengthen its customer proposition through improved lounge experiences by investing in new and expanded lounges in Melbourne, Perth, Tamworth and Coolangatta airports and continued investment in front-line team training.

Qantas Domestic continues to support the regional market position through QantasLink and Network Aviation services. QantasLink launched two-class B717-200 services on Canberra and Tasmania routes[28] and took delivery of two Bombardier Q400 aircraft and two B717-200 aircraft during the period. QantasLink relocated into the Qantas Sydney terminal creating a more seamless travel experience for Qantas customers through smoother connections and reduced check-in times. Qantas' Charter operations have increased market share 25 per cent since July 2012 to 30 per cent.

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[25] Australian Federation of Travel Agents National Industry Awards 2010-2013.
[26] AirlineRatings.com's Airline Excellence Awards, January 2014.
[27] BITRE data - January 2009 to December 2013.
[28] Tasmania Services commencing mid-April 2014.

REVIEW OF OPERATIONS (continued)

Qantas International

- International market yields and revenue seat factor adversely impacted by market capacity oversupply
- Comparable unit cost[3] improvement of four per cent
- Strengthening alliances through Emirates partnership and new codeshare agreements with China Southern
- Record customer advocacy among business flyers

		December 2013	December 2012	Change	% Change
Total Revenue and Other Income	$M	2,621	2,818	(197)	(7)
Revenue Seat Factor	%	80.8	82.7	(1.9) pts	(2)
Underlying EBIT	$M	(262)	(91)	(171)	>(100)

Qantas International Underlying EBIT loss of $262 million for the half-year represents a $171 million deterioration on the prior corresponding period.

The reduction in Underlying EBIT was due to lower revenues, unfavourable fuel cost and foreign exchange. Revenues reduced due to market capacity oversupply. International market capacity in and out of Australia increased by nine per cent[29] as a result of aggressive competitor behaviour largely from foreign government owned or sponsored airlines. The strength of the alliance with Emirates partially offset the revenue decline with codeshare bookings doubling compared to previous alliances.

Comparable unit cost improved four per cent reflecting ongoing benefits from the Transformation program, including the reduction in heavy maintenance, retirement of older B747-400 aircraft, improved fleet utilisation and improved fleet economics following A380-800 and B747-400 reconfigurations.

Continued investment in Qantas' international product and service offerings resulted in record advocacy levels amongst business flyers as business customers continue to take advantage of a broader network proposition through the Emirates alliance and product enhancements including the lounge offering, Business Sleeper Service, Select on Q-Eat and Chauffeur Drive.

Qantas International continued to strengthen its intra-Asia proposition, including announcing a new codeshare partnership with China Southern. Qantas International now has agreements with three major China-based carriers providing access to one of the world's largest and fastest growing economies.

[29] BITRE data - November 2013.

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REVIEW OF OPERATIONS (continued)

Jetstar

- Domestic business profitable every year since 2004
- Competitive environment impacting yields, in particular in South East Asia
- Low Cost Carrier (LCC) business fundamentals remain strong
  - Continued growth in ancillary revenue per passenger[12]
  - Unit cost[30] improvement
  - Successful introduction of the B787-8 Dreamliner
- Strong brand presence across Asia

		December 2013	December 2012	Change	% Change
Total Revenue and Other Income	$M	1,671	1,757	(86)	(5)
Seat Factor	%	78.5	79.0	(0.5) pts	(1)
Underlying EBIT	$M	(16)	128	(144)	>(100)

Jetstar Underlying EBIT for the half-year ended 31 December 2013 was a loss of $(16) million, down from $128 million profit in the prior corresponding period.

The decline in earnings was primarily driven by market capacity oversupply driving yield decline in South East Asia, market growth ahead of demand in the Australian domestic market and unfavourable fuel cost and foreign exchange.

Jetstar's LCC fundamentals remain strong. Jetstar Group improved unit cost[30] by two per cent and ancillary revenue per passenger[12] by one per cent compared to the prior corresponding period.

Jetstar has been profitable in the Australian domestic market every year since launch. Domestic seat factor increased by 0.5 points to 82.3 per cent as a result of five per cent passenger growth on capacity growth of four per cent.

Jetstar International successfully introduced the B787-8 Dreamliner into long-haul operations out of Australia during the period.

Jetstar Asia continues to provide a strategically important gateway to Asia, operating in a highly competitive market with LCC capacity up 34 per cent[31] putting significant downward pressure on yields. This was partially offset by unit cost improvement of two per cent[33] coupled with four per cent increase in ancillary revenue per passenger[12] compared to the prior corresponding period.

Japan continues to be a substantial opportunity for the Group, with Jetstar Japan in a strong competitive position. Jetstar Japan is the largest domestic LCC in Japan[32] with over three million passengers carried since launch, market leading On Time Performance and strong customer advocacy.

Jetstar Pacific continues to realise the benefits from the fleet renewal program, achieving a seven per cent unit cost[33] improvement compared to prior corresponding period. In addition commercial initiatives have enabled an eight per cent increase in ancillary revenue per passenger[12].

Jetstar Hong Kong's preparation for operational launch continues while seeking necessary regulatory approvals.

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[30] Unit cost - Jetstar Group unit cost is measured using controllable unit cost in line with industry benchmarks for low-cost carriers. Controllable unit cost is adjusted to aid comparability between reporting periods. Controllable unit cost is measured as total underlying expenses excluding fuel, carbon tax, Jetstar Asia and Share of net loss of investments accounted for using the equity method, adjusted for changes in foreign exchange rates and movements in average sector length per ASK.

[31] Diio Report published 9 January 2014.

[32] Based on fleet as at 31 December 2013 and domestic ASKs compared to Peach Aviation and AirAsia Japan/Vanilla Air.

[33] Unit cost - Unit cost is measured using controllable unit cost in line with industry benchmarks for low-cost carriers. Controllable unit cost is adjusted to aid comparability between reporting periods. Controllable unit cost is measured as total underlying expenses excluding fuel, adjusted for changes in foreign exchange rates and movements in average sector length per ASK.

REVIEW OF OPERATIONS (continued)

Qantas Loyalty

- Record[34] Underlying EBIT of $146 million, up seven per cent on the prior corresponding period
- Member growth of over 700,000 members in the period to 9.7 million members with approximately 2,000 members joining each day
- Billings[35] up nine per cent to $662 million
- New growth initiatives - Qantas Cash and AQUIRE
- Net promoter score at record high[36]

		December 2013	December 2012	Change	% Change
Members	M	9.7	9.0	0.7	8
Billings[35]	$M	662	607	55	9
Underlying EBIT	$M	146	137	9	7

Qantas Loyalty achieved another record[34] result with a seven per cent improvement in Underlying EBIT to $146 million for the half-year ended 31 December 2013. Underlying EBIT improved 10 per cent excluding Qantas Cash and AQUIRE start-up costs. This has been driven by strong billings growth, continuing member engagement and continued member growth to 9.7 million members, with more than 700,000 members added over the last 6 months[37].

Billings[35] increased by nine per cent to $662 million. Credit card billings were up by 10 per cent driven by promotional campaigns and new products.

Qantas Loyalty continues to grow with new growth initiatives Qantas Cash and AQUIRE exceeding expectations.

There have been over 200,000[38] card activations since the launch of Qantas Cash. In addition to faster, smarter check-in, boarding and lounge access, the prepaid multi-currency travel card gives members new ways to earn points and the ability to hold up to ten different currencies on one card.

Qantas Loyalty is launching AQUIRE in March 2014. Small to medium enterprise (SMEs) are showing strong interest in AQUIRE with over 25,000 SMEs pre-registered. This innovative business rewards program enables businesses to earn rewards on everyday business expenses and provides the flexibility to use rewards for multiple purposes including employee rewards and flight savings.

Qantas Loyalty added eight new partners during the period providing members with expanded opportunities to earn and redeem points including, Coral Sea Hotels, Kerzner International Resorts, Fresh Fragrances, Jumeirah Hotels & Resorts, Vendome, iSelect, Dimmi, and Qatar Airways.

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34 Qantas Loyalty record Underlying EBIT result compared to prior periods normalised for changes in accounting estimates of the fair value of points and breakage expectations effective 1 January 2009.
35 Billings represent point sales to partners.
36 Net promoter score is at its highest level since reporting started in 2008.
37 Members added in the last six months to 31 December 2013.
38 As at February 2014.

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REVIEW OF OPERATIONS (continued)

Qantas Freight

- Increased revenue in a competitive environment
- Integration of Australian air Express

		December 2013	December 2012	Change	% Change
Total Revenue and Other Income	$M	568	531	37	7
Revenue Load Factor[39]	%	53.9	55.9	(2) pts	(4)
Underlying EBIT	$M	11	22	(11)	(50)

Qantas Freight's Underlying EBIT was $11 million for the half-year ended 31 December 2013, down $11 million on prior corresponding period. This was driven by the sale of StarTrack and acquisition of Australian air Express during first half of financial year 2012/2013 together with an eight per cent reduction in international freight capacity and challenging air freight markets.

The integration of Australian air Express is now complete, delivering full run-rate synergy benefits from the second half of financial year 2013/2014 and creating Australia's leading independent air freight provider. The consolidation of Australian air Express contributed to the increase in revenue in the period.

Reconciliation of Underlying PBT to Statutory PBT

The half-year ended 31 December 2013 Statutory Loss Before Tax of $305 million is $453 million down on the prior corresponding period.

Underlying PBT

Underlying PBT is the primary reporting measure used by the Qantas Group's chief operating decision-making bodies, being the Chief Executive Officer, Group Management Committee and the Board of Directors, for the purpose of assessing the performance of the Group. The primary reporting measure of the Qantas International, Qantas Domestic, Jetstar Group, Qantas Loyalty and Qantas Freight operating segments is Underlying EBIT. The primary reporting measure of the Corporate/Unallocated segment is Underlying PBT as net finance costs are managed centrally.

Underlying PBT is derived by adjusting Statutory (Loss)/Profit Before Tax for the impacts of AASB 139 Financial Instruments: Recognition and Measurement (AASB 139) which relate to other reporting periods and identifying certain other items which are not included in Underlying PBT.

[39] Revenue Load Factor – Revenue Freight Tonne Kilometre (RFTK) over Available Freight Tonne Kilometre (AFTK).

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REVIEW OF OPERATIONS (continued)

Reconciliation of Underlying PBT to Statutory (Loss)/Profit Before Tax		December 2013	December 2012	Change	% Change
Underlying PBT	$M	**(252)**	**220**	**(472)**	**>(100)**
Items not included in Underlying PBT					
- AASB 139 mark-to-market movements relating to other reporting periods	$M	54	34	20	59
Items not included in Underlying PBT					
- Net impairment of property, plant and equipment	$M	(23)	(62)	39	63
- Redundancies and restructuring	$M	(59)	(68)	9	13
- Net profit on disposal of jointly controlled entity	$M	-	30	(30)	(100)
- B787-8 introduction costs	$M	(9)	-	(9)	(100)
- Other	$M	(16)	(6)	(10)	>(100)
Total items not included in Underlying PBT	**$M**	**(107)**	**(106)**	**(1)**	**(1)**
Statutory (Loss)/Profit Before Tax	**$M**	**(305)**	**148**	**(453)**	**>(100)**

AASB 139 mark-to-market movements relating to other reporting periods

All derivative transactions undertaken by the Qantas Group represent economic hedges of underlying risk and exposures. The Qantas Group does not enter into speculative derivative transactions. Notwithstanding this, AASB 139 requires certain mark-to-market movements in derivatives which are classified as 'ineffective' to be recognised immediately in the Consolidated Income Statement. The recognition of derivative valuation movements in reporting periods which differ from the designated transaction causes volatility in statutory profit that does not reflect the hedging nature of these derivatives.

Underlying PBT reports all hedge derivative gains and losses in the same reporting period as the underlying transaction by adjusting the reporting period's statutory profit for derivative mark-to-market movements that relate to underlying exposures in other reporting periods.

All derivative mark-to-market movements which have been excluded from Underlying PBT will be recognised through Underlying PBT in future periods when the underlying transaction occurs.

Other items not included in Underlying PBT

Items which are identified by Management and reported to the chief operating decision-making bodies as not representing the underlying performance of the business are not included in Underlying PBT. The determination of these items is made after consideration of their nature and materiality and is applied consistently from period to period.

Items not included in Underlying PBT primarily result from major transformational/restructuring initiatives, transactions involving investments and impairments of assets outside the ordinary course of business.

Items not included in Underlying PBT in the first half of the 2013/2014 year were driven by the Qantas Transformation. Costs include aircraft impairment due to early retirement following strategic network changes, further consolidation of engineering and catering facilities and the integration of Australian air Express.