
AURIGNY GROUP ANNUAL REPORT

2017



JUNE 13, 2018



Corporate Details

The Aurigny Group of Companies ('Aurigny')

The Aurigny Group of companies comprises:

- ┐ Cabernet Ltd - holding company (not trading)
- ┐ Aurigny Air Services Ltd – airline
- ┐ Anglo Normandy Aero Engineering Ltd – aircraft engineers

The Board of Directors of

Aurigny Air Services Ltd and Anglo Normandy Aero Engineering Ltd:

- ┐ Andrew Haining (Chairman)
- ┐ Mark Darby (CEO)
- ┐ Malcolm Coupar (Commercial Director)
- ┐ Chris Simpson (Finance Director) (appointed 28.9.17)
- ┐ John-Paul Williams (Technical Director) (appointed 6.6.18)
- ┐ Chris Holliday (Non-Executive Director)
- ┐ Meriel Lenfestey (Non-Executive Director)
- ┐ John Le Poidevin (Non-Executive Director) (appointed 1.1.17)

P. O'Donovan resigned on 28.9.17

M. Richards resigned on 31.3.17

Registered Office for all Group companies:

Aurigny Air Services Ltd,
La Planque Lane,
Forest,
Guernsey,
Channel Islands,
GY8 0DT



Chairman's Statement

Andrew Haining

2017 – a year of progress and milestones

I am pleased to be able to present the 2017 Annual Report for the Aurigny Group, marking a year in which our business made important progress in a number of key areas.

While 2017 was a year filled with its fair share of challenges, as you would expect in regional aviation, it was also a year where key decisions were made to improve the performance of the airline, both financially and in the service we offer customers.

Undoubtedly, one of the biggest and most difficult decisions of 2017 was the decision to end the London City route but, it must be remembered, there were several reasons behind this move, not least the need to improve the financial performance of the airline.

Elsewhere on our London network, we were able to make an important and positive investment at London Gatwick, the lifeline link for the island, where we launched our own dedicated team of staff. With improved customer service and operational performance, I have no doubt this was not only the right decision for Aurigny as an airline, it was also the right decision for Guernsey and for the economic prosperity of the island.

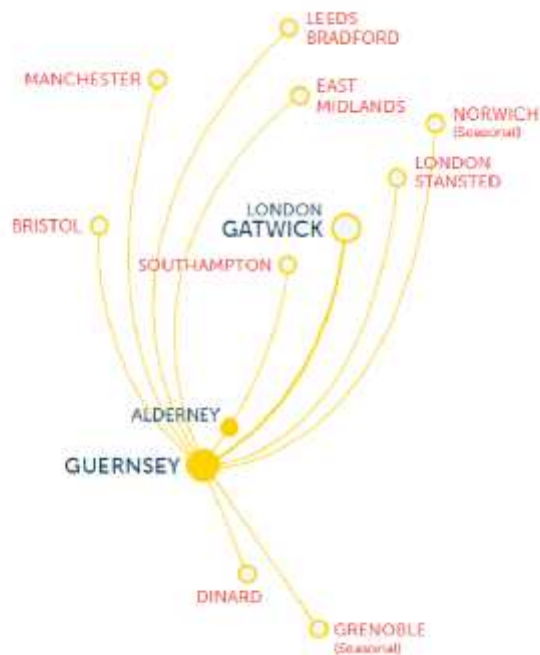
Across our network as a whole, the Company once again recorded stable passenger numbers in difficult market conditions and we continue to be Guernsey and Alderney Airports' number one customer. If you take together the amount we contribute to the Airports and the amount our staff pay in local employment taxes, Aurigny contributes an estimated £9m+ to the States' exchequer each year, making us a significant net contributor to the islands. Looking forward, we are far from complacent and remain focussed on improving the services we provide our customers, as well as our overall finances.

In financial terms, our revenue for the year was in line with the prior period at £44.68m (2016 - £44.68m) and this generated positive EBITDA* of £0.82m (2016 - £0.73m). Our overall reported loss for the year was £5.19m (2016 - £5.18m) but was almost £2m better than we anticipated. We expect this position to improve following our withdrawal from the London City route in the last quarter of 2017.

We also have plenty of reasons for optimism and celebration in the years ahead, not least with our 50th anniversary in 2018. It was on 1st March 1968 when we saw the inaugural flight take place between Alderney and Guernsey and in that year Aurigny flew 30,000 passengers on its inter-Island routes, 11,000 of them between Alderney and Guernsey.

Since then our network and passenger numbers have grown considerably and in 2017 we flew 540,000 passengers on 13 routes using our fleet of 9 aircraft.

Aurigny Route Network Map



Aurigny has now carried close to 16 million passengers over the last 50 years, quite a feat for an airline with such modest beginnings.

Our Strategy

As we look to the future, we are pleased that the main outcome of the States Strategic Review of Aurigny, published in 2017, was that it clarified and reconfirmed the overriding strategic goals of the airline: to be an economic enabler providing safe and reliable operations and a break-even financial position on our Guernsey operations.

We also note the intention to launch a Public Service Obligation (PSO) process for the Alderney services and look forward to the publication of the tender document. In particular, this is anticipated to set out the arrangements that prospective operators will be expected to put in place. Aurigny operates under the terms of its Memorandum of Understanding with the States of Alderney and States of Guernsey, and we have committed to submit a bid for retention of this service as part of the PSO process. Of course, maintaining resilient service year-round at high frequency comes with a cost attached which current passenger demand, coupled with fares limits prescribed in our MoUs, results in losses. In the meantime, we have a service to maintain which requires not only aircraft but most importantly skilled professionals - pilots, engineers, ground and office-based staff. We trust, therefore, that the process can be handled as swiftly and as sensitively as possible. Obviously, we hope that we will win the tender as well.

When looking at the market as a whole, one of our biggest challenges will always remain the fact that we operate in a sub-scale market for air services. The reality is that the islands' population is static; as a consequence, the local air market is relatively inelastic and additional demand is very difficult to stimulate. Despite this, concerted efforts are being made to boost inbound passenger sales and numbers, including the recent change to our new website and fares structure. In 2017, Aurigny continued to have relatively strong and stable 64% market share locally, a figure that has not fluctuated for a number of years.

Our commitment to our community

We recognise that, through States ownership, we are owned by the people living and working in the Bailiwick. We know that we are serving communities where connections between the islands, to London and to other large UK population centres are an essential part of life. Everything we do is for our communities in the islands; we value our role and responsibilities within those communities.

Lifeline routes

Our route network continues to be developed around the need to serve lifeline routes, including the London Gatwick and Alderney services.

Gatwick investment

In 2017 we added extra flights to the winter season to provide even more choice and frequency at peak times. Two extra flights were added to the Saturday schedule on the lifeline route, giving our customers the choice of six return flights every Saturday and bringing our weekly service in the winter to a record 42 return flights.

Aurigny also took the important decision to launch its own ground handling operations at London Gatwick. This important investment, made towards the end of 2017, has not only helped to improve our customer service and communication, it has directly resulted in improved punctuality and performance on the lifeline route. Importantly, it means that we have our own team of staff at Gatwick at all times to help our customers, provide support during disruption and ensure customers are looked after from start to finish.

Alderney Service

Proud to have served Alderney for 50 years, we understand the importance of the lifeline service that we provide to the Island community. 2017 was also a milestone for other reasons. The last of our Trislander aircraft, G-BEVT, retired from service and we moved to an all Dornier fleet.

In addition to our own investment, improvements to the facilities and infrastructure at Alderney Airport are essential for the service we provide. We very much look forward to the proposed runway repairs, which will see the width being restored and will improve our crosswind landing performance in Alderney. Adverse weather continues to challenge our operational performance on the inter-island route. However, despite this we continue to keep our punctuality and on-time performance in line with the rest of the network.

Elsewhere on our Network

2017 saw the continuation of our Leeds-Bradford and Norwich summer services, as well as our other year-round services to London Gatwick and Stansted, Manchester, East Midlands and Bristol. We also serve Dinard in France throughout the year and have a winter Grenoble service.

Our people

As an airline, we continue to invest in our workforce and recognise their importance to us and our customers.

We appreciate the dedication and pride they have in their important roles at Aurigny, and their continued commitment in helping to get passengers where they need to be, each and every day. We are also incredibly proud as an employer of the length of service given to us by so many of our staff. This shows just how much they value working for Aurigny and how dedicated they are to their roles. Daily airline operations are incredibly complex and rarely without their challenges, so it is vital that we have a committed team of staff who can make everything work, particularly at times of disruption. We would like to thank all our staff, across all our locations, for helping us to achieve and deliver to our customers throughout 2017.

Conclusion

Looking ahead, we have much to celebrate and look forward to in 2018, as we mark our 50th anniversary. As always, the community in both Guernsey and Alderney will be at the heart of these celebrations, and we hope we can bring people of all ages together to help us mark 50 memorable, varied and rewarding years.

Another reason for celebration is our recent success at two prestigious industry awards. Aurigny was voted best short haul airline by Which? Magazine and ranked third best short haul airline by readers of the Daily Telegraph in 2017.

This represents our highest ever placing in these awards. Importantly, they were both based on the positive feedback of the people who matter most, our customers. We hope to build on this success in 2018. To do so, we must continue to invest in our staff, fleet and the services we offer customers.

*EBITDA is a commonly used industry standard term and represents Earnings before interest, taxation, depreciation and amortisation



Chief Executive's Report

Mark Darby

Safety in our operations is the number one priority for everyone at Aurigny. We have put in place a Safety Management System with robust checks and balances throughout our organisation designed to identify risk trends and, where added risk is being introduced to our business, enabling management to take mitigating action. The UK Civil Aviation Authority, our regulator, follow the standards set by EASA – the European Aviation Safety Agency. They undertake regular audits, notify management of their findings and follow up on open actions. We also invested in the new role of Technical Director during the year and I am delighted to have been able to welcome John-Paul Williams to the team; he is responsible for all aspects of our maintenance and engineering.

Listening to our passengers, we know that they value being able to travel at convenient times to airports which fit their travel plans so we have designed our timetable to offer the best possible balance of frequency of service to the most popular destinations. We also listened to customer feedback and increased the long-standing baggage size on our Guernsey operations, taking into account the restrictions imposed by the make-up of our fleet.

London is a lifeline destination. We serve the London market 7 times daily – 6 flight rotations to Gatwick and 1 to Stansted – with departures spread across the day so whether your journey is on business and you need a day return, or for more leisurely purposes, you will find a departure that meets your needs.

The link between Alderney and Guernsey is another lifeline: we fly at least 4 times daily and we ensure that we have the capacity to put on additional services at peak times. We provide flights on behalf of the hospital in Alderney when it is necessary to transfer residents to Guernsey for medical treatment; in 2017 we flew 70 such services. Alongside this lifeline service, we also connect Alderney with Southampton 3 times daily.

During 2017 we have continued to invest in our business.

-) At Gatwick Airport we have invested in improvements to our customer experience by employing our own team of Aurigny staff dedicated to our flights and our customers. The feedback has been very positive. We now handle our flights in most airports and I would like to applaud the service that they provide to you, our customers..
-) With around 80% of our bookings coming directly through our website, we took the decision to invest in an essential upgrading and throughout 2017 we were working on our new website. Now launched, not only has this improved functionality but has also given the site a contemporary makeover and improved compatibility with different devices and browsers. Just as importantly it has allowed us to introduce a new fares structure, with new lower-priced hand baggage only fares now available. These new fares, introduced in April 2018, offer more choice and flexibility to passengers, giving them fare more control over their travel plans. It also brings us in line with the rest of the industry, ensuring we are just as competitive when potential visitors compare us to other airlines and destinations.

-) We continue to invest in and maintain back up aircraft and crew in our fleets to enable us to recover as swiftly and smoothly as possible from weather-related disruption
-) Finally, in August 2018 we look forward to taking delivery of a brand-new Dornier 228NG aircraft for our Alderney operations, replacing a 'Classic' Dornier.

Operational Review

Our fleet

During 2017 we operated a fleet of 8 aircraft plus an additional Dornier 228 on loan from RUAG, the manufacturer of the type.

Aircraft	Reg'n	Owned/ leased	Age	Fleet Average Age
Embraer 195	G-NSEY	owned	4 yrs	4 yrs
ATR72-500	G-COBO	owned	9 yrs	11.5 years
ATR72-500	G-VZON	owned	9 yrs	
ATR72-500	G-LERE	leased	9 yrs	
ATR42-500	G-HUET	leased	19 yrs	
Dornier 228NG	G-OAUR	owned	3 yrs	22 yrs
Dornier 228	G-LGIS	owned	30 yrs	
Dornier 228	G-SAYE	owned	33 yrs	
Average age of our fleet - 14.5 years				

Aurigny's fleet has an average age of 14.5 years. Easyjet, acknowledged as a lead player in the short-haul market, has a fleet with average age of 7.7 years. Ryanair's fleet of 300 aircraft has an average of 5.5 years. Flybe has a fleet of 75 aircraft with average age of 9.6 years. Leading airlines have policies of fleet renewal for good reason: they are seeking to exert control over maintenance costs and avoid declines in reliability which come with ageing aircraft. Aurigny's Directors keep our fleet requirements under review and are actively evaluating renewal of the ATR fleet. We had been expecting the delivery of a second Dornier 228NG aircraft in 2017 which would have brought down the age of the Dornier fleet and reduced reliance on the old 'Classic' Dorniers. Unfortunately, this delivery was delayed by the manufacturer, but we look forward to this new aircraft entering our fleet in mid-2018 at which time the primary fleet age will reduce significantly.

Weather factors – new technology

In 2017 Guernsey airport experienced 47 days where fog conditions reduced visibility below our landing minima, given the landing systems installed at the airport today. Alderney airport experiences even more days with foggy conditions. When the disruption due to fog is taken with other meteorological conditions it will be no surprise that we suffered more than 60 days of disruption including knock-on effects. We continue to work hard to minimise the disruption to our services which the challenges of operating in these extreme weather conditions brings. We maintain back-up aircraft in our fleets and standby crews to fly them, enabling us to recover as swiftly and smoothly as possible from weather related delays. Of course, this high level of resilience

comes at a cost, which airlines flying in other less challenging places don't have to bear. Add to that the costs of looking after passengers who are delayed, and it adds up to a significant sum. Looking forward, aircraft installed technology solutions – enhanced vision systems - are becoming available which have the capacity to change things for the better for Guernsey. Aurigny has the inhouse skills, experience and capability to capitalise on these opportunities as they become available on new aircraft; we are in discussion with aircraft manufacturers and hope to be able to report positively on developments in our fleet in 2018. Significantly, enhanced vision systems are installed on board aircraft therefore it is airlines, and not airports, which make the investment.

Future investment in new aircraft will ensure we have a fleet that is fit for purpose for future operations and will reduce the significant risk and unpredictability of maintenance costs that are associated with older aircraft.

Our staff

At the end of December 2017, the Aurigny Group of companies employed 313 people (full-time equivalents) across 4 locations: Alderney, Guernsey, Gatwick/UK and Southampton, demonstrating our commitment as a significant employer within the islands and our investment in our Gatwick ground operations staff.

	Alderney	Guernsey	Gatwick & UK	Southampton	Total
Pilots	5	53			58
Cabin crew		39			39
Engineers		22			22
Ground staff	16	91	25	8	140
Administration	2	46	6		54
Total	23	251	31	8	313

As we celebrate our 50th year servicing the islands' community, I would like to give my considerable appreciation and thanks to all of our staff who have helped put airline safety and customer service at the heart of our organisation throughout the year.

Finance Director's Report

Chris Simpson

Our financial performance

We have changed the presentation of our financial results for 2017 to fit in with best practice in the airline industry and make our numbers easier to understand.

Revenues

Total revenues were static year-on-year at £44.68m (2016 - £44.68m). Within that, passenger revenues were £41.59m (2016 - £41.98m), a decline of £0.39m mostly due to the closure of the London City route in Q4. Other revenues increased by a similar amount mostly due to increased charter flights we performed for other airlines.

Costs and Profits

Our overall operating costs improved slightly during the year to generate an EBITDA* of £824,000 (2016 - £726,000). This is the profit measure that the Board uses to assess operational performance as it highlights the underlying performance of our business before charges for: non-cash depreciation on our aircraft fleet; interest on our loans to finance our aircraft fleet; and overdraft interest which we are charged by the States of Guernsey and our bank.

With hedging in place, many of our operating costs are relatively stable and predictable. Hedging is integral to an airline's risk mitigation because it eliminates uncertainty over cash flows and enables management to plan better. The Board has put in place our Hedging policy covering jet fuel procurement and US dollar exposures which currently extend towards the middle of 2019 and which are renewed on a rolling forward basis.

The biggest financial and operational risk that we cannot control, and can lead to volatility in our numbers, is unplanned fleet maintenance. As the average life of the fleet continues to age, there will be both expensive scheduled maintenance checks at certain key lifetime dates to be planned for, and also an increased risk of unplanned fleet maintenance issues, which is one of the drivers for the fleet review outlined in the Chief Executive's report.

Loss for the year was £5.19m, in line with the loss in the previous year, but ahead of the forecast loss that we expected at the mid-way point in 2017.

Our business segments

We view our business in two operating segments: our Guernsey network operated by the Embraer jet and ATR72s and our Alderney network operated by Dornier 228s.

90% of our passengers flew on our core Guernsey operations, representing 91% of our passenger revenues and generating a positive EBITDA contribution of £3.1m, but a loss of £1.9m in 2017.

We are committed to the provision of the lifeline Alderney service: this is underscored by the fact that in 2017 approximately 40% of our flights were flown on the Alderney network whereas it represents

only 10% of our overall passengers and 9% of our passenger revenue, generating a negative EBITDA contribution of £2.3m and a loss of £3.3million in 2017.

2017 Results	Guernsey Network	Alderney Network	All Routes
Passengers flown	489,115	54,918	544,033
	£000s	£000s	£000s
Passenger Revenue	37,800	3,794	41,594
EBITDA Profit/(Loss)	3,107	(2,283)	824

Table showing 2017 results in our key business segments – Alderney and Guernsey networks

Approximately 80% of our fixed assets are employed in our Guernsey operations, with the remaining 20% used on the Alderney network.

Cash flows

We generated a positive cash flow from operations of £608,321 (2016 - £937,901) and invested a further £2.1m in the purchase of tangible fixed assets in the year (2016 - £3.1m).

Our year end net cash position had improved to £1.7m at 31 December, compared to a net overdraft position of £0.4m at the end of 2016.

Balance sheet

The most significant number in our balance sheet continues to be our investment in the aircraft fleet and at 31 December the net book value of our tangible fixed assets stood at £40.8m (2016 - £42.9m). This change represents £2.1m of fixed asset additions, less depreciation of £4.2m in the year.

These assets and our underlying operations are financed primarily through bank loans to finance aircraft of £9.6m (2016 - £10.8m) and amounts due to the shareholder of £32.9m (2016 - £26.1m) which includes loans to finance aircraft and a temporary overdraft facility.

Strategic risks

The Board groups our strategic risks into 4 headline areas:

Safety – encapsulating the fact that safety is core to our overall mission and reflecting on the risks associated with the occurrence of a safety related event and the Safety Management System we have in place to mitigate and navigate these risks.

Operational – reflecting the high level of service provision we aim for against a background of variable weather conditions and the prevalence of fog in the islands and the risks associated with aircraft unavailability, which we mitigate through the provision of back-up aircraft and stand-by flight crews.

Financial – representing the unpredictable movements in the price of Jet fuel and US dollar exchange rates, mitigated by an effective hedging strategy to manage the unpredictability.

Reputational – understanding that we are a state-owned airline servicing the islands' community and that we have an obligation to meet the needs of that community, our commitment to high levels of customer service and our risk mitigation plans that are put in place to ensure that we can deliver on that commitment.

*EBITDA is a commonly used industry standard term and represents Earnings before interest, taxation, depreciation and amortisation

