

FINAL TRANSCRIPT

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the fourth quarter 2006 SAS AB earnings conference call.

[OPERATOR INSTRUCTIONS]

At this time, I'd like to turn the call over for your host for today, Mr. Sture Stolen, Head of Investor Relations. Please proceed, sir.

Sture Stolen - *SAS AB - Head, IR*

Yes. Thank you very much. Welcome, everyone, to this teleconference for the full year 2006 results. We have a presentation of about 15 -- think about 15 to 20 minutes. It's around 10 slides. Hopefully, you have found the slides on the internet. And after that, you're welcome to ask questions. So, with that, I will transfer to our CEO, Mats Jansson.

Mats Jansson - *SAS AB - President and CEO*

Hello, everybody. My name is Mats Jansson. And I'm sitting here together with my CFO, Gunilla Berg. And I'm going to start this conference going through some of the first slides and after that Gunilla going through the results more in detail for last year. And after that, I'm going to give my comments and my first reflection on the first period in this group.

But I start to work informally in November and December and formally from the first of January. And during this time, I've been in a learning curve, you can call it. I have met more than 2,000 employees and talked a little bit with them. I've also deep interviewed about 100 top managers in the group and traveling around and meet people out in the different stations and the subsidiaries in the whole group. So I have got some experience after those 39 first days in the company.

If you start with the first slide, which describes the growth in the market 2006, you can see the underlying growth is very good and GDP is very good. The business cycle is, more or less, on top for the moment. We have had very good growth in our different markets and different companies during '06. And the strongest traffic you can see in Spain and also in Norway and also in the Baltics. And we can also see strong growth in Finland. And overall, as a total, we have good growth in the group.

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If you take the next slide, you can see the figures overall for the whole group for '06. As you know, I was not related to the group last year formally, so this good sign or good figures is related to the former group management team and the employees. And we have said today in the press conference here in Sweden, that the fundamental crisis for the group is now over. And we have related the definition of crisis to the situation, which Swiss Air and KLM and so on was in for a couple of years ago. We go into a new period now and this augmentation is based on that you can now see better figures. The underlying results for last year was nearly SEK1.3 billion and the total profit was nearly SEK5 billion, including gain and also nonrecurring items.

The reason or the explanation of the good results is combination between the good business cycle and also the way the management team and the employees work in the company now. We steer the company in another way than before. We have a better cost control in the whole group and the growth is more now depending on the customer need or the customer demand than ever before. We have nowadays better control when we talk about the capacity and adjust the capacity of how the market is developing during the year. So, I feel a little bit confident in the way the group management team and the -- all the other management and then -- have been working out the last two, three years.

If you look at the next slide, you can see the present platform for the group of today. And later on, I'm going to describe a little bit about the strategy work for the following five years. We call this Strategy 2011. And one important point in that strategy is to define the current position and situation for the whole group. And if we start with the cost level, as you know, Gunilla and her colleagues have reduced the cost tremendous during the last years. The first program was about SEK14.5 billion. The next program, which is still working was on SEK2.5 billion. And we have almost gone through with those two programs.

But that means that the cost level is lower now, that we are more efficient than before. But we, still we have a disadvantage when we talk about the cost levels, which we have to eliminate the following years. Another piece of the platform is the business model. And there have been big changes also there. You remember when the group launched the one-way prices, which is a revolution in this industry. We are going to take the next step now when we talk about the commercial activities. I come back to that a little bit later on also. The business structure is also changed and has also been -- we can call it a tool in this improvement activities during those two years since we started the decentralization of the whole group. And I believe in this decentralization. I think it's necessary to have this type of model.

The last thing here is the more focus, as we say, on the core operation. And by the divestment of the Rezidor Hotels, we are, more or less, an airline company in three different parts in the value chain, as you know. One is airline part, one is the ground handling part and the third part is the technical services. But per definition, we are, more or less, an airline company nowadays after all the divestitures.

We have also said today that the result is a good sign, is a good step. But it's not -- enough level. It's a gap, we have said. The gap we have defined of about SEK3 billion. It's the preliminary simulation before we launch the strategy in May this year. So, the base is today SEK1.3 billion, we had to reach about SEK4 billion or SEK4.5 billion for the following years to cover all the investments we had to do in new aircrafts, in maintenance, in the markets, in the employees and so on. So, the whole -- the goal for us, the following years, the overall goal is to implement a strategy in different ways, which leads us to another cash flow and another result level than we ever have reached before. And let us come back to that later on. Gunilla, please.

Gunilla Berg - SAS AB - CFO

Good afternoon. Gunilla Berg speaking. If you look at the first slide, it shows the business result for the different business areas. As Mats said, we are pleased with the result development, but, of course, not with the actual level, since we are far away from the return target and Mats mentioned. This strongest result improvement in 2006 within Scandinavian Airlines with an improvement of SEK1.6 billion. The development in Q4 is stronger than previous quarter, due to the stronger deals and due more seasonal capacities adjustments. The result in Q4 for the individual branded airlines is better than last year and we are almost on the same level for the whole business areas for 2006.

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We have a rather large deviation -- negative deviation -- for our business area of aviation services and that's due to lower volumes and lower prices compared to last year. We have some nonrecurring items. In Q4, we made some write-downs after impairment test of small stakes in different small companies. And we have also, in quarter four, made a provision of about SEK50 million for the legal costs we expect, related to the SAS Cargo investigation.

If you look at next slide, we have four main result drivers for the improvement within the Scandinavian Airlines. The introduction of the business model has been very important for the result development, since that has increased campaign factors substantially and the possibility to seal the deal more optimal.

Of course, the group's business climate has had a positive impact on the result, especially since that has helped to reduce the overcapacity in different markets. The cost reduction, as Mats mentioned, is also an important result driver. And last, but not least, I think that the more flexible capacity focus, both reduction on some unprofitable destinations and what we call focus on round trip management, which is the more seasonal adjustments of the round trips during the day, week and the month.

If we look at the result for the different companies, we have impressive developments, especially in Denmark and in Sweden, improvement of about SEK800 million. The Danish company has been affected by the pilot strike as well as Braathens has been affected, both by the pilot strike and the cabin strike. We have, for the first time since '95 got a positive result for our intercontinental business, which we are very pleased with. We are doing some changes in the strategy for the intercontinental business, which Mats will come back to and we think that will improve the results further on.

If you look at next slide, we can see, for the subsidiaries in our two other business areas, we have a rather mixed picture. We have negative result for Blue1 and STS. And for Blue1, the main explanation for the lower results this year compared to last year is that we have phase-in costs for the three MD-90s we have introduced for the Europe expansion. We have also negative results in our SAS Technical Services and that's due to, as I mentioned, much more lower volumes in 2006 from that in 2005 and also lower prices. And we have some still result problem or profitability problems with the components -- [SF] component.

For Spanair, we have improved the result, good cabin factor improvement, better yield. Wideroe is a positive result, but a negative development compared to last year. And that's due to the cost development. And they have started now a cost program of SEK200 million. They have reduced the capacity by two aircraft and they have also done some other improvements on the concept. airBaltic -- good development in a rather competitive area. SGS is more about timing and lower volumes, lower prices and they are reducing the cost as fast as possible. So, Cargo -- good development.

If you look at next slide, [SAS] management we are almost through the SEK2.5 billion program. The SEK2.5 billion program is for the Scandinavian airline companies and ground services and technical services. So far, we are implementing 80% and we have about 500 left this year to implement. Okay. Thank you.

Mats Jansson - SAS AB - President and CEO

Okay. Let's go further on. You see on the next slide -- we see the description of my reflection during this first time and, as you see, on the first bullet, we need, as I say, a much clearer and distant concept and customer offering in the future. This is very important. And what I mean is that we have to have balance between cost reduction to reach the right cost level and to work with cost efficiency all the time and also have a very distinct and clear customer offer to consumers. And I'll come back to that a little bit later on also.

We haven't been enough clear and distinct in the past. A lot of good initiatives have been taken in this way and one new initiative I'm going to tell you a little bit later on. Now, this is necessary for the future to, every year, to be innovative and take initiative to create and launch more value added on for our business or frequent flyers and also for the lesser flyers. As I said before, we had to continue to rationalize and to fulfill the intention to eliminate the cost disadvantages we have today. And we look at our competitors, who is the -- what is the peer group in our different geographies in the Scandinavia, which is our main geography,

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and also in Europe and also on long-haul. And I think you have been discussing before the expected level of the cost gap and I'm not going to mention the exact level here today because we have to define it. But we have still much to reduce for the following years.

At the same time, we have to be running all the time enough efficient. What I mean, with that, it's another thing then to reach the right cost level is to work every day and have maximum operational excellence in our work. We need to grow, I say. And once again, it has to be a balance between cost reduction and also grow. All companies have to grow, especially this type of company, which is in the service business. But it's also important to realize and to understand in what position the SAS group are in for the moment. We can see positive signs, but we have, I think when we launched a new strategy, we have to close the gap even more to reach another level before we try to grow a little bit harder, before we try to take some market investment risks in our different companies.

So, cost gapping are reaching another cost level and try to make the commercial offer more aggressive. I think it will come in different sequences during this five-year period. We also have to make a clearer definition about the different roles after the decentralization in the group of two years ago. Between the parent company at headquarter and the different subsidiaries and also between the different subsidiaries, especially the airline subsidiaries. That's one important thing to look at when we do our strategy homework.

You can see on the right-hand side, the presentation or the call it the structure of the Strategy 2011. You can see some of the questions which we address, first of all, to ourselves, to the group management and also to the board. And in the next step also external. And the logic in this structure is to start to define and we have started our position today. And we know it quite well. We have also some very important discussions about what type of company should we become in the future. In what geography should we operate? Who are our main customers? And so on and so on. And when we have defined the business idea and the vision for the future, then it's going to have consequences on our whole company.

And after that, we try to answer the question about what should we have -- what kind of offer should we have to the customer? How should we behave and how should we be managed or steered in the company? And what is the need of the result or financial strength -- cash flow and financial strength in the company to fulfill the plans for the following years?

Let's go over to the next picture. As I have mentioned before, we've taken initiative now on the commercial side, especially in the SK subsidiaries in Scandinavia and also in long-haul. Let me say once again that our main customer is, on one hand, the frequent fliers, who most of all are related to business. And their share of the total volume is about 60%, something like that. And the rest 40% is also important part of the company. It comes from private customers. So, we try to work in both of those segments. And I have experience from other industries. And the -- one of the differences between the airline industry and this -- and other industries is that you can build on the same low-cost platform, two different concepts to attract the different consumers' needs. It's possible to do that. It's very difficult in other industries to do that.

And that's what we try to do in the future. So, what we are launching now in a couple of weeks is a two-class system in Scandinavia and very distinct three classes, some in the rest of Europe in the most frequent destinations. This is also in line with the new long-haul strategy to U.S. and also to Asia. That means that we upgrade everything from meals, environment in the aircraft, some way of -- so, we also upgrade the services for the cabin. We also reduced prices, especially in the extra class. And all those details together will strengthen our customer offer for the following years. Just one step more. The first step, as I said before, was to allow us, for example, the one-way price system.

I mentioned a little bit about the intercontinental operation and long-haul program and the new strategy on that. A lot of pieces in that program. One is that the -- we try to operate for the following years with a lower cost level. It's necessary -- necessary in all our subsidiaries and operations, as I said before. We also launched a new traffic program now. It's more demand driven. There's three pieces. One is the base or the bulk is every day destinations to U.S. and to Asia. And we have also added to that now two types of seasonal programs.

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And what we said today on the press conference was also to come with some -- one new destination. And so, we launched the destination from Stockholm to Bangkok, which start in November. We still work with 11 aircrafts in long-haul operation. We are going to do that during this period, as far as we know now. And as I said before, also in the intercont business we are more demand driven now than ever before.

The last slide before we take the Q&A is to sum up something of what I have been saying before. Starting point, as I said before, '06 result do sign a good step. We have more control over the company now than ever before, I must say. This market has grown. Business cycle is good. But also by own activities and own power, we have managed the company well. The people have managed the company well. The new business model, I mentioned it before. Good cost control, but not on the right level. Also, a focus on capacity activities to also steer the yield in another way than before. Be more professional in that way.

And we go from, as I said before, from the strong crisis situation to more normal situation into a - more of concept driven restructuring of the whole company. That's what we call Strategy 2011. And the overall goal is to fill the gap. The gap, as I said before, related to the level we reach '06 is about SEK3 billion, if we can reach those SEK4 billion, SEK4.5 billion in early -- in average each year. Then we can be more comfortable when we talk about future investments and also to give the shareholders return on their investments and so on and so on.

The outlook, you can see the slide, is more about the overall trends in the market, about the business cycle is still strong. And we believe it could be strong. Also, in the future, we should grow in that environment. Hopefully, we can take market shares in our group for this year, depending on the new commercial initiative and so on, hopefully. You can see also that we mentioned that in this S-11 or Strategy 11 program, which we'll announce in May, there could be some restructuring items, but we don't know exactly, but we would like to mention it now for you. And then, as you show it -- uncertainties about the strength of the future growth, as we said before, the fuel prices and also the effect of competitive situation in the group.

That was all from me and Gunilla. Please come with your questions.

QUESTIONS AND ANSWERS

Operator

Thank you, sir. [OPERATOR INSTRUCTIONS] Your first question comes from the line of Jacob Pedersen of Sydbank. Please proceed, sir.

Jacob Pedersen - Sydbank - Analyst

Good afternoon. I have a couple of questions. First of all, you state that the result effect from the SEK2.5 billion cost measures are SEK1 billion in 2006. What additional effect should we expect this year? That's my first question.

Mats Jansson - SAS AB - President and CEO

Do you know?

Gunilla Berg - SAS AB - CFO

I can answer that immediately. About SEK1 billion for 2007.

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Jacob Pedersen - Sydbank - Analyst

So, additionally, SEK1 billion.

Gunilla Berg - SAS AB - CFO

Yes. Compared to 2006.

Jacob Pedersen - Sydbank - Analyst

Yes. Okay. Also, I'd like to hear the reason that you now expect flat capacity in the Scandinavian Airlines business. At the end of the third quarter you guided for, I think, 1% to 2% growth.

Gunilla Berg - SAS AB - CFO

That -- the most reason for that is round-trip management. We do see some adjustments and especially in January, February, July and December, we do rather large seasonal adjustments. So, otherwise, it's like we had said then -- for the capacity increase in -- within Scandinavian Airlines, it's more about seats and there is no more aircraft. There's more seats in special aircraft.

Jacob Pedersen - Sydbank - Analyst

Okay. Okay, finally, I'd like to talk a bit of the dynamics impacting the earnings in the individually branded airlines in 2007.

Mats Jansson - SAS AB - President and CEO

What you mean with dynamic impact for 2007?

Jacob Pedersen - Sydbank - Analyst

Yes. When you look at 2007, which dynamics will impact the development of the -- on the earnings side of the individual branded business -- airlines, sorry.

Mats Jansson - SAS AB - President and CEO

First of all, I'll -- I must say that we don't give forecast now in our [inaudible]. And so, we're not going into now the different subsidiaries and now make a forecast for their possibilities to grow in top line or profit and so on. So, I can't give my comment on the different pieces in the group. But I, as I said before, I've been visiting the different pieces or subsidiaries in the group. And when we talk about Spain, Spain company we hold there as a very good company with a good market share and so on. It has good possibility for the future to grow. And also, the other subsidiaries in -- when we talk about the individually branded airlines.

And I think the same pattern, if I've taken overall explanation in all our subsidiaries, it's a combination with cost activities and also with the revenue activities or to strengthen up the commercial offer. And it depends on subsidiary, how we weigh those two things together. But that's my overall answer. Unfortunately, I can't go into the different companies and comment.

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Jacob Pedersen - Sydbank - Analyst

Okay. Thank you very much.

Operator

Your next question comes from the line of Andrew Lobbenberg of ABN. Please process, sir.

Andrew Lobbenberg - ABN AMRO - Analyst

Oh, hi, there.

Mats Jansson - SAS AB - President and CEO

Hi.

Andrew Lobbenberg - ABN AMRO - Analyst

Just to ask a question -- you spoke how you're doing quite a lot of inward gazing and thinking about what sort of company SAS should be. Does that include the possibility of major [circle] changes and disposals of the subsidiary companies or do you start from the standing point that you're working within the existing structure?

Mats Jansson - SAS AB - President and CEO

Yes, we look at everything now, almost everything. All the important things which you do when you start in strategy work, define all the different, you can call it tool in the toolbox. It's the same in all other companies also that they have different weight and different effects also. So, one part is to look at the whole portfolio. We are, as a family, for more or less, and company now which concentrate us on the core operation.

But when we look into the company, in this strategy process, we can see that we already split it up in geography. You have the Spanish operation. We have the operation in the Eastern. You have the main operation in Scandinavia. It's one thing to look into. How we work together. How is the brand strategy towards those nine subsidiaries? Do we take out the synergies? Should we take out the synergies and so on? And how are they linked to each other? That's one question. So, I only address the question. I don't give the answer as you heard.

The other thing is also to look at the company, which I said before, we work in three different parts in the value change, which is, from my background, very -- a little bit complicated. I'm used to working only one part or maybe two parts in the value chain. And so, we run the airline operation, the pure airline operation in one part of the company, in nine different subsidiaries. And then, we have the ground handling in another subsidiary. And then, we have also the technical services. We have also cargo. And so, we look into the whole portfolio.

And per definition, we are now -- we have a core operation in the group, but we also have to look into it more in detail in the final, which is the core, core, core operation and what consequences could it have on our growth for the future. So, that's what we are doing. It's not an answer. Only a description of the way we work in the process.

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Andrew Lobbenberg - ABN AMRO - Analyst

Okay. Lovely. Thanks. And if I may, just another question. If I just look at the traffic data for the subsidiary airlines in December and in January, they look lousy. Is there any trend we should be worried about or do you think they'll just miraculously bounce back in a week or so?

Gunilla Berg - SAS AB - CFO

If you look at the traffic figures in January, it's especially -- the companies Spanair, Blue1 and airBaltic, which has reduced the load factor. But as you can see, there is rather high [increase] in [ASK] and that's more or less a timing question. But we have decided about some reduction of the capacity in Spanair because we can see that the market maybe slows down a little from what we expected. So, this is -- we always try to calibrate the capacity. So, I don't think there is any -- to worry about. We calibrate all the time. So, if you look at Scandinavian Airlines, which is the major part of the group, we have increase in the cabin factor. And as you can see, the last month, we have a rather, rather strong yield. So, in total, we think, anyway, the development goes as we expect.

Andrew Lobbenberg - ABN AMRO - Analyst

Okay. Lovely. Thanks very much. See you guys tomorrow.

Mats Jansson - SAS AB - President and CEO

See you. Okay. Nice to meet you again.

Operator

There are no more questions at this time.

Mats Jansson - SAS AB - President and CEO

Okay.

Operator

I apologize, sir. We do have one final question that queued up.

Mats Jansson - SAS AB - President and CEO

That's okay.

Operator

It's from Michael Nielsen of Jyske Bank. Please proceed, sir.

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Michael Nielsen - Jyske Bank - Analyst

Thank you. Good afternoon. One question regarding you mentioned a cost disadvantage. Could you maybe indicate where you see some major possibilities to enhance efficiencies going forward having been in the companies for a couple of months?

Mats Jansson - SAS AB - President and CEO

As I said before, we have a cost disadvantage and I think the same pattern all over the world if you look at the network carrier. And when the whole market was deregulated and after a couple of years the full effect of the deregulation you could see with other players in the market, you can see the same trend. If you go to full retail and non full retail, it's absolutely the same pattern. And then, we can call it a big fire start in the market. And then, it's important to be consequently related to your mission or business idea. And SAS, the SAS group, very well reputed and the brand is very strong. And we are a network carrier, which is an advantage in the competition.

At the same time, as I said before, 40% of our passengers are private or in the lesser segment. So, in this new environment, in this new competition, you had to also to have a good program for them. That's why the group reduced the cost so much -- SEK14.5 billion and now 2.5. And some part on those reduction was invested in better prices to be more competitive in the market. So, when we now look at the cost disadvantage, we look in different pieces in the company from top to the bottom. From the headquarter administration and all overhead down to distribution.

Remember, when I mentioned before, one thing is the cost level, to change it by structural activities. Another way is to work more in the operational way to be more operational excellent in the daily business. So, those two pieces together to change the structure in different parts in the company. And maybe work in another way in our group that we could reach another cost level and another cost platform. And based on that, as I said before, we can also launch and develop the commercial offer in another way in the future.

And after that, Gunilla.

Gunilla Berg - SAS AB - CFO

Yes, just adding, when we are talking about a cost gap, we are comparing with the most efficient player in different markets. And the most efficient players must say is all the new players. If we compare with the traditional carrier, we are very competitive on the cost side. But we look at the new -- the most efficient player and we see that we still have the cost gap and we have to close it as much as possible.

Mats Jansson - SAS AB - President and CEO

Yes, I agree with that.

Michael Nielsen - Jyske Bank - Analyst

Okay. Thank you. You have -- regarding the aviation service and the cost pressure situation and so on, is -- could it still be in the cards to outsource or sell off these activities if they are not improve -- if they don't improve performance going forward?

Mats Jansson - SAS AB - President and CEO

I don't want to answer that concrete question. As I said before, I gave you all -- an overall description about the way we work with the strategy. And once again, we have divest all of the non-core operations. And now we have per definition core operations

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in our group. But we still have to look if it's maximum efficient to work with every part in the group. So, I -- let us work with it and come back in May with that.

Michael Nielsen - *Jyske Bank - Analyst*

Okay. Final question, you mentioned that you expect the yield to continue, whatsoever, continue a positive trend in the first half of '07. Could you shed some light on the level of improvement you are seeing out there or, for example, compared to 2006?

Gunilla Berg - *SAS AB - CFO*

What I said was that we have had the last month good improvement in the yield, especially for Scandinavian Airlines. But as we have said before a lot of times, we don't guide anything about the yield development.

Mats Jansson - *SAS AB - President and CEO*

Okay?

Michael Nielsen - *Jyske Bank - Analyst*

Okay. Thanks.

Mats Jansson - *SAS AB - President and CEO*

Thank you very much. Okay. Yes, thank you very much, everyone, and for those who are along tomorrow, we hope to see you there. Thank you.

Sture Stolen - *SAS AB - Head, IR*

Thank you. Bye-bye.

Gunilla Berg - *SAS AB - CFO*

Thank you. Bye.

Operator

This concludes today's presentation. You may now disconnect.

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