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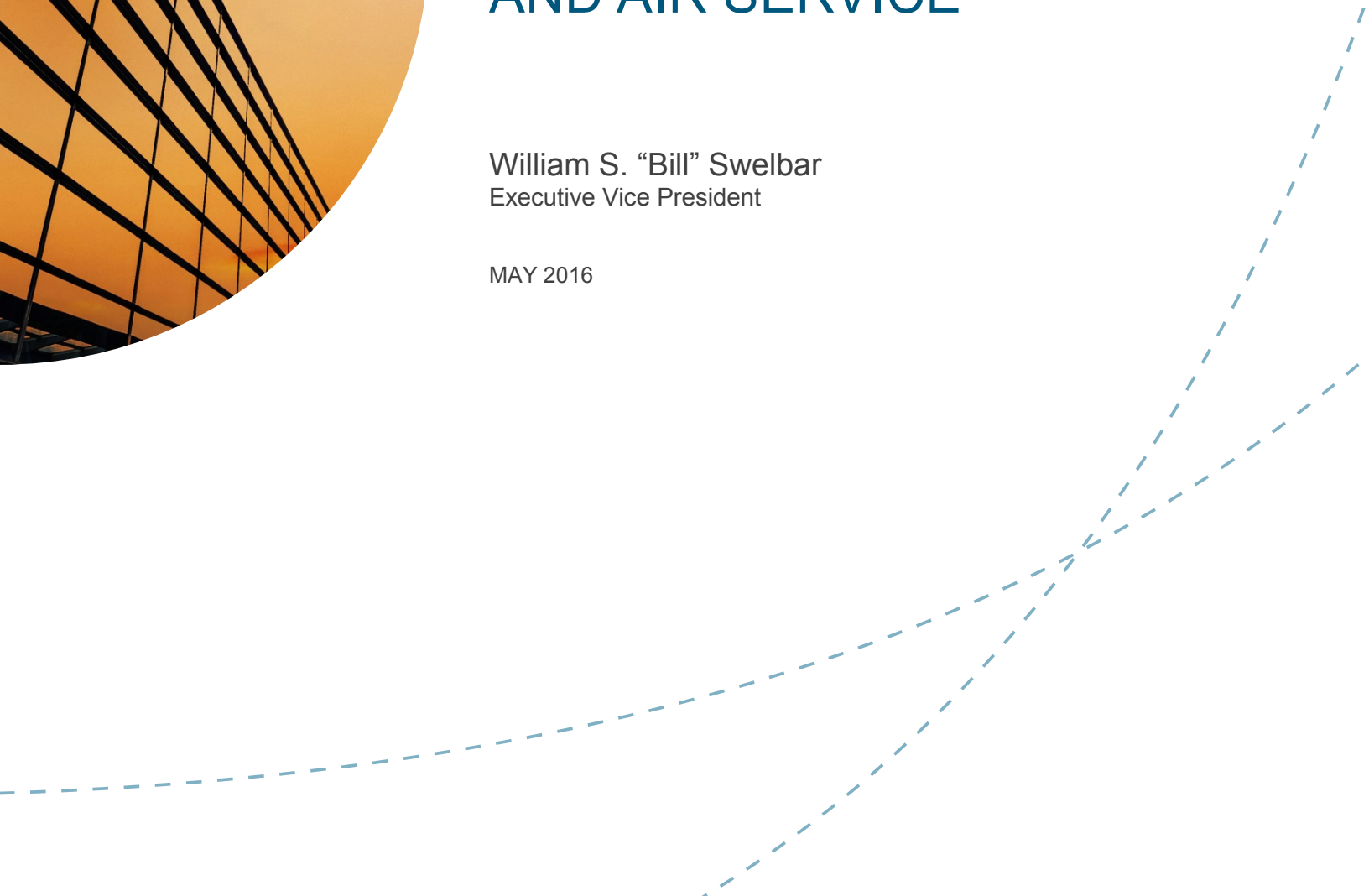
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An InterVISTAS White Paper

A “PEAK” AT THE U.S. ECONOMY AND AIR SERVICE

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Executive Vice President

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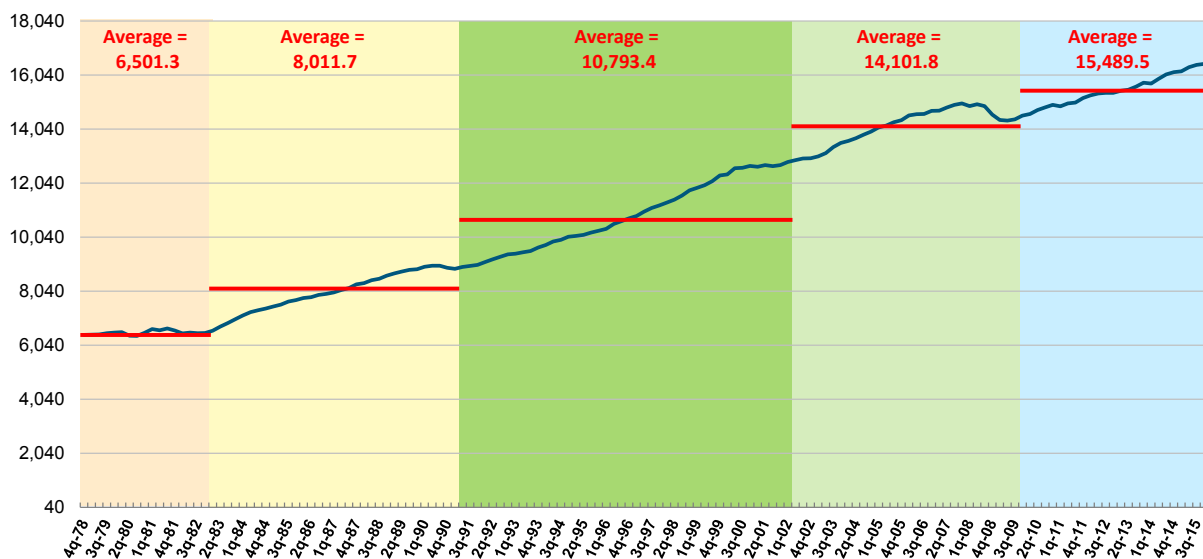
The official dates of business cycle beginnings and endings are determined by the National Bureau of Economic Research (NBER). Business cycles have four distinct phases: expansion, peak, contraction and trough. Between 1945 and 2009, there have been 11 distinct business cycles in the US with the average length of a cycle lasting about 69 months, or a little less than six years. The average expansion during this period has lasted roughly 58 months, while the average contraction has lasted only 11 months.

However, since the 1990s the length of the business cycles looks much different and the current cycle resembles those. The three business cycles from July 1990 to June 2009 had an average expansion phase of 95 months compared with the average recession length of 11 months over entire cycle. The current cycle began during the fourth quarter of 2009 and remains in an expansionary phase today. We are nearing the 80th month of the expansion and may very well have witnessed the peak.

History would suggest that the contraction period would begin sometime during the first half of 2017 which coincides by the way in a presidential election year or shortly thereafter much like the prior business cycle. The contraction of the economy would then run through 2017 and thus mark the end of this business cycle.

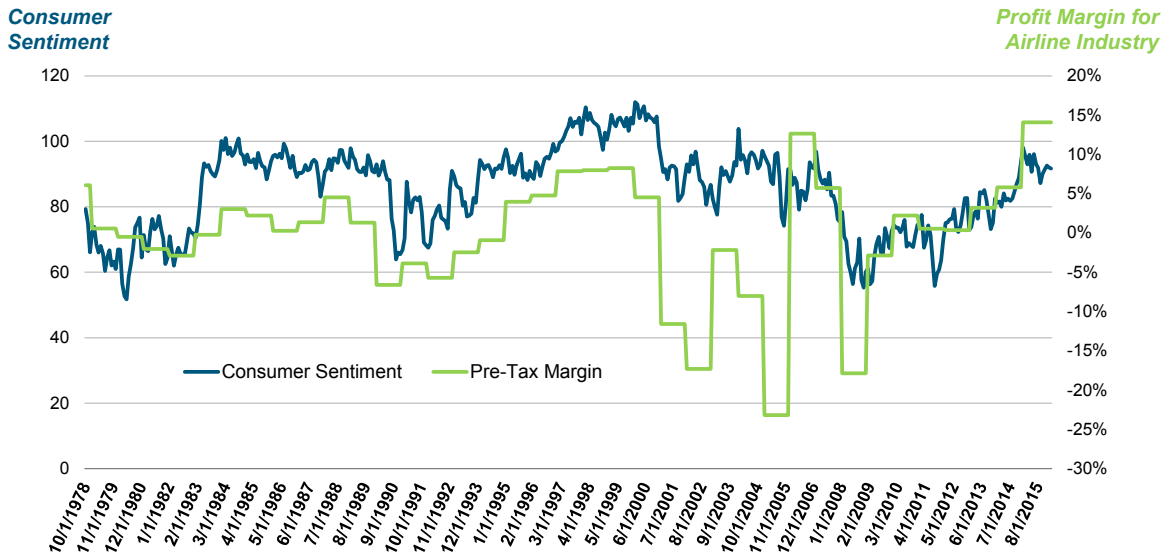
History seems to support the trajectory of the current business cycle. While still expansionary, the growth has occurred with macroeconomic crosswinds in place and geopolitical uncertainties in nearly every corner of the world present. Beginning in the second half of 2013, macroeconomic crosswinds turned into tailwinds as the expansion period marched toward a yet to be determined peak.

Slower Relative Real GDP Growth Defines This Cycle



In addition to Real Gross Domestic Product, two other indicators have demonstrated strong correlation with US airline industry health. They are the Institute for Supply Management's (ISM) manufacturing index which has been trending lower and the University of Michigan's Consumer Sentiment Survey which trended higher throughout 2015. As can be seen, the Consumer Sentiment Survey in 2015 correlates closely with the industry earning it highest margins during this business cycle.

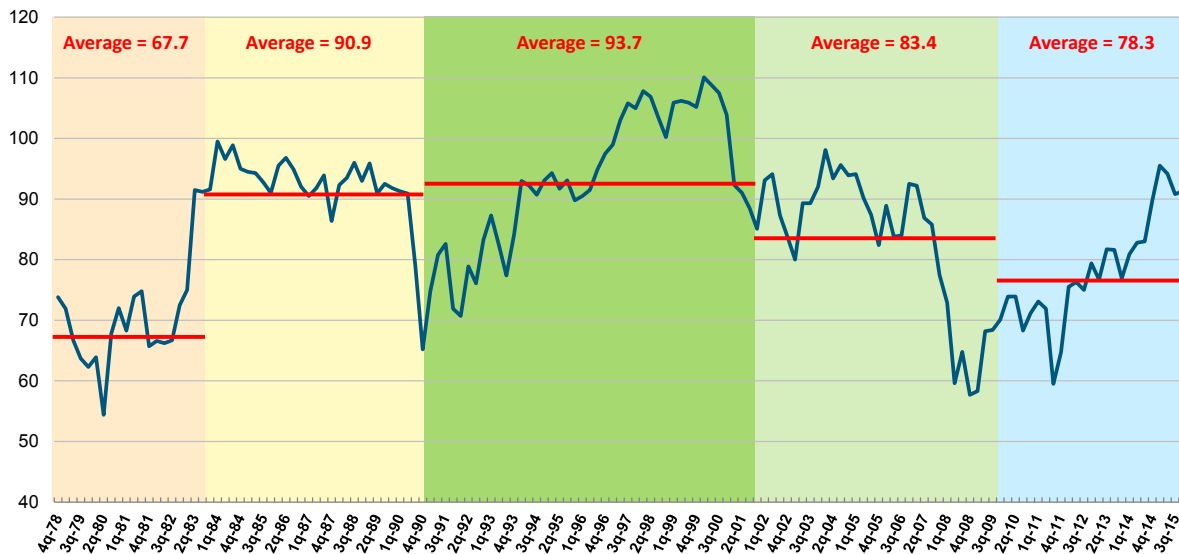
A Strong Directional Correlation Between Consumer Sentiment and Airline Profitability Exists



Source: University of Michigan

What is interesting to note is that during the expansionary period of the current cycle, the consumer has been less of a story than in the past and that is because macroeconomic indicators have not been as bullish, as home prices just now coming close to recapturing lost values and other commodity prices have been decreasing while growth in incomes persist.

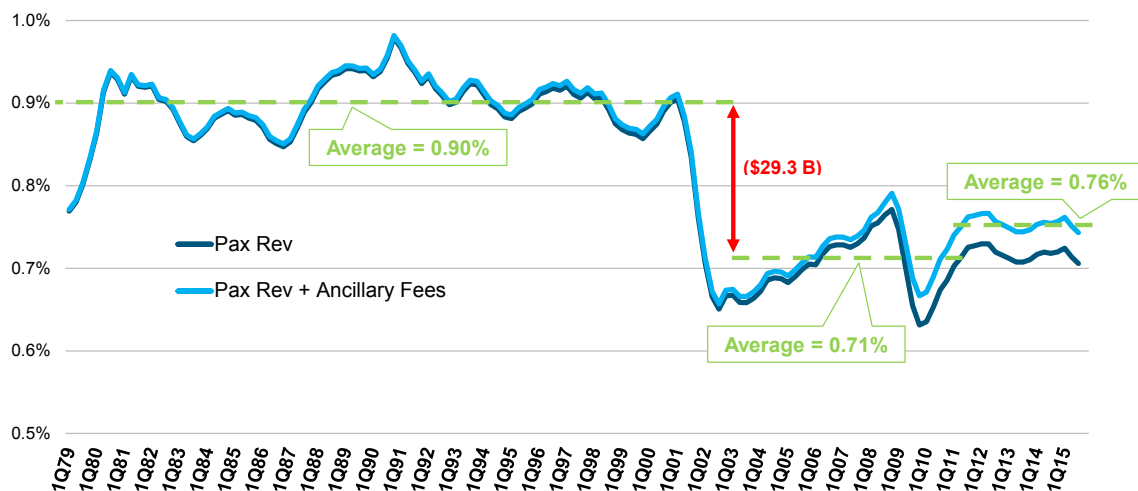
Consumer Confidence in This Business Cycle: Lower on average than that since the first business cycle



This is evident in the University of Michigan's Consumer Sentiment reading. In fourth quarter of 2013, the index measured 76.9, a decrease of nearly 5 points from the prior quarter. Importantly, consumers are not considered bullish until the index measures over 90. For the first time since July of 2007, the index achieved values in the 90's for all four quarters of 2015. This is yet another indicator that the economy is still in an expansionary mode but may be at or near its peak. Further, it is this indicator that suggests why mixed news about the macro economy are variegated.

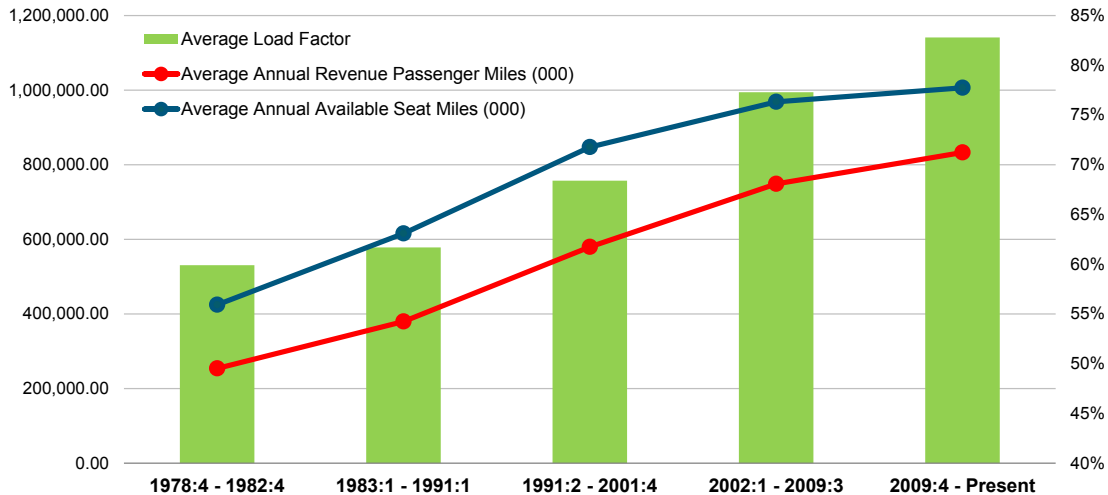
It used to be that the health of the US airline industry was inextricably tied to the health of the US economy. If one had a good real GDP forecast, forecasting US airline industry revenue was a pretty straight forward exercise. Historically, revenue equated to an average of .90 percent of Real GDP plus or minus four percent. That is no longer the case, with the internet as a ticket distribution vehicle, permitting price transparency shopping for the air travel consumer. In addition, the growth of the low cost and ultra-low cost carrier sector pushed prices down, and created vigorous price competition, forever changing the relationship of GDP and airline revenue beginning in the second half of 2000.

**Passenger Revenue and Ancillary Fees
as a Percent of Gross Domestic Product**



Like many things, this business cycle is harder to read based purely on macroeconomic indicators than at any time in the past. Unbundling and re-bundling the product in return for ancillary fees is part of the new revenue vernacular. Dated mindsets in commodity-emulating industries suggest that the only way to earn new revenue was to add supply in order to win a share of the newly created revenue. Now capacity discipline is the mantra leading to a profit-driven operating mentality for carriers of all ilk. The US airline industry looks very different in this business cycle than in any of the four that preceded it since deregulation. As growth in capacity has slowed over the past two business cycles, load factors has increased 15 points.

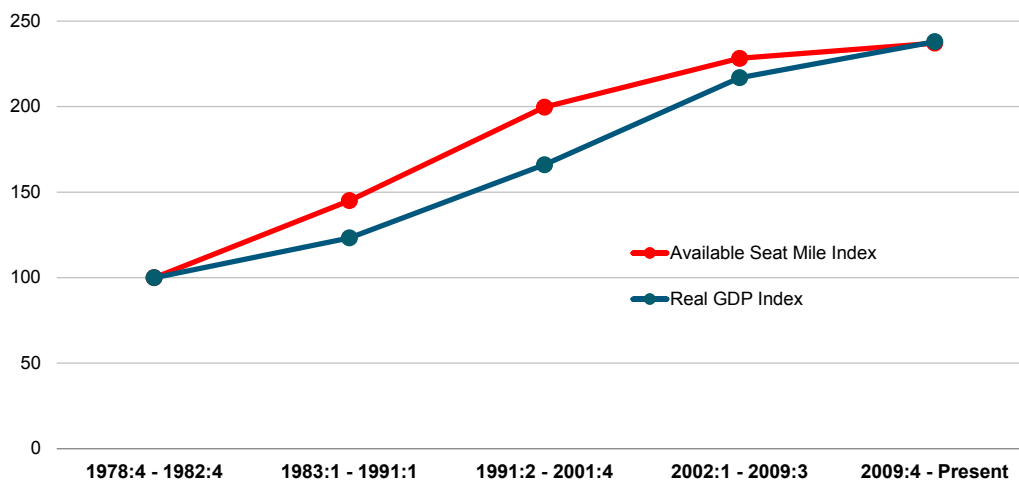
Capacity Growth Across the Business Cycles:
Load factors grow nearly 15 points over the past two cycles



Data Source: A4A Airline Cost Index Tables

Whereas in the past, growth in capacity has been faster than the growth rates in Real GDP, that is simply not the case in this business cycle. While we are seeing growth in excess of Real GDP in the nation's largest markets, the same cannot be said for the smaller markets who are still realizing modest decreases in frequencies and seats. Connectivity is being lost on the margin. The fact that capacity grew faster than the economy in the past was a major contributing influence to the industry performing poorly from a financial perspective.

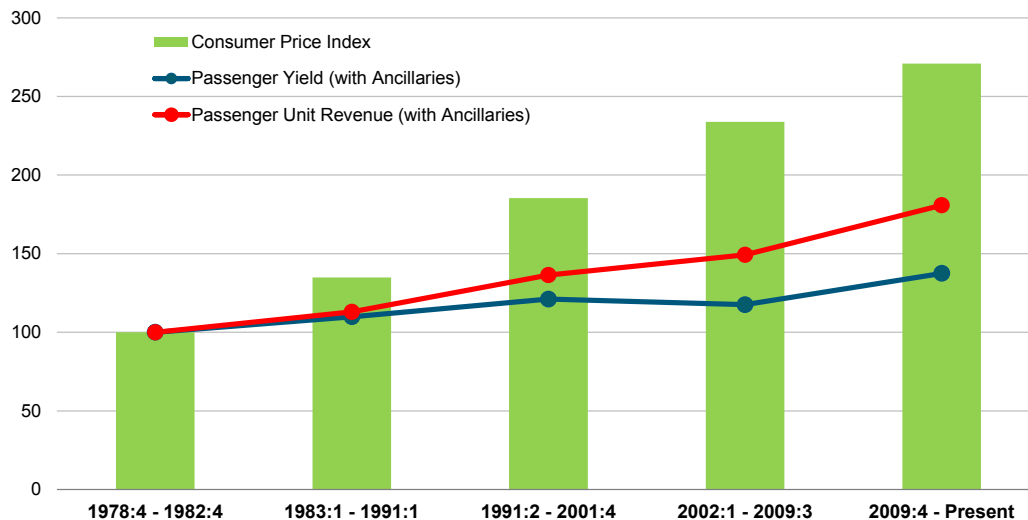
Capacity Growth Faster Than Real GDP:
Making sustainable profitability a difficult proposition



Notes: SAAR, 2009 Chained Dollars; Business cycle 1 = 100

As capacity grew faster than real GDP, unit revenue, whether in passenger revenue per revenue passenger mile (Yield) or per available seat mile (Unit Revenue) did not come close to keeping pace with inflation. The industry has done a good job of managing controllable costs relative to inflation, particularly labor costs. But rising labor costs in the past have been a good barometer that the industry is nearing a peak and that is certainly the case today.

Unit Revenue Does Not Keep Pace With Inflation:
Despite recent increases, a great consumer bargain remains

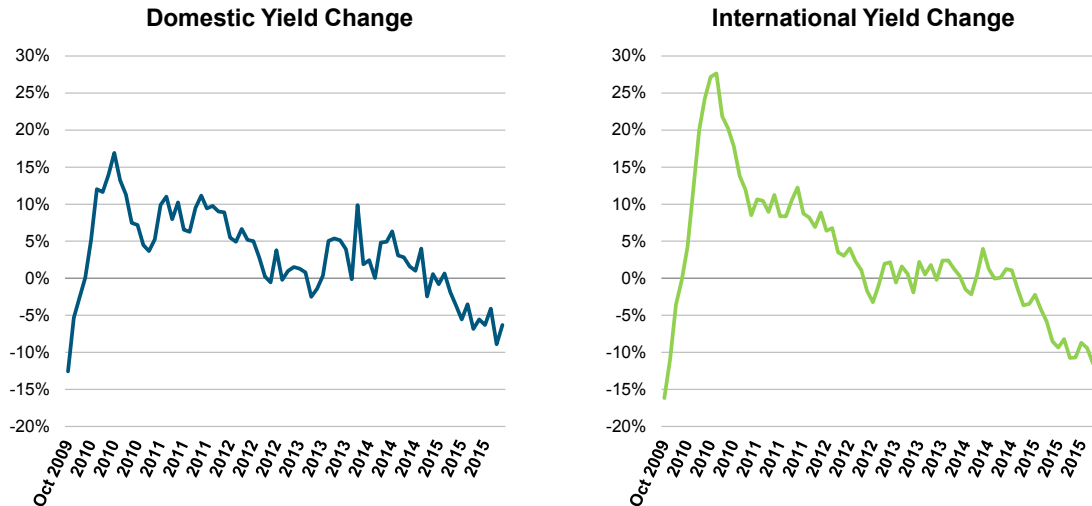


Note: SAAR, 2009 Chained Dollars; Business cycle 1 = 100

This was the rule and not the exception until the current cycle. Only in the current cycle did we see yield and unit revenues growing at significant rates. Through the first half of the current business cycle, domestic passenger yield increased year over year in 35 of the 38 months averaging 6.6% where data is available. During the second half of the current cycle domestic passenger yield increased in 22 of the 38 months averaging .2%, or at a rate 6.4 points slower than the first half. Truly a tale of two halves of the cycle is evident as domestic unit revenue has now declined year over year for the past 12 months. International trends look similar.

Over The Last 12 Months...

The consumer has realized lower prices from jet fuel price declines

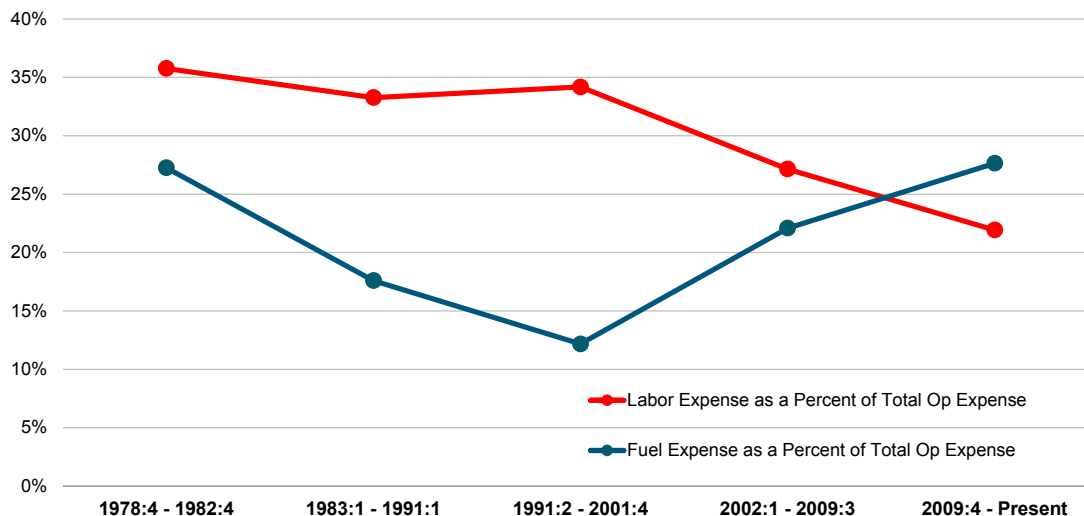


We have discussed certain catalysts that caused/forced the US airline industry to change its ways of doing business for fear they would end up in the graveyard like icons Eastern, Pan Am and TWA to name a few.

But no catalyst was more significant than the rapid rise in the price oil commencing in 2004 and culminating in a nearly \$148 price per barrel in July of 2008. For the most part, the price of oil was an irrelevant cost center during most the first four business cycles of a deregulated business. With little fluctuation in the cost of jet fuel, the industry would simply grow as this uncontrollable cost center was well under control averaging \$25 per barrel and a \$5 crack spread.

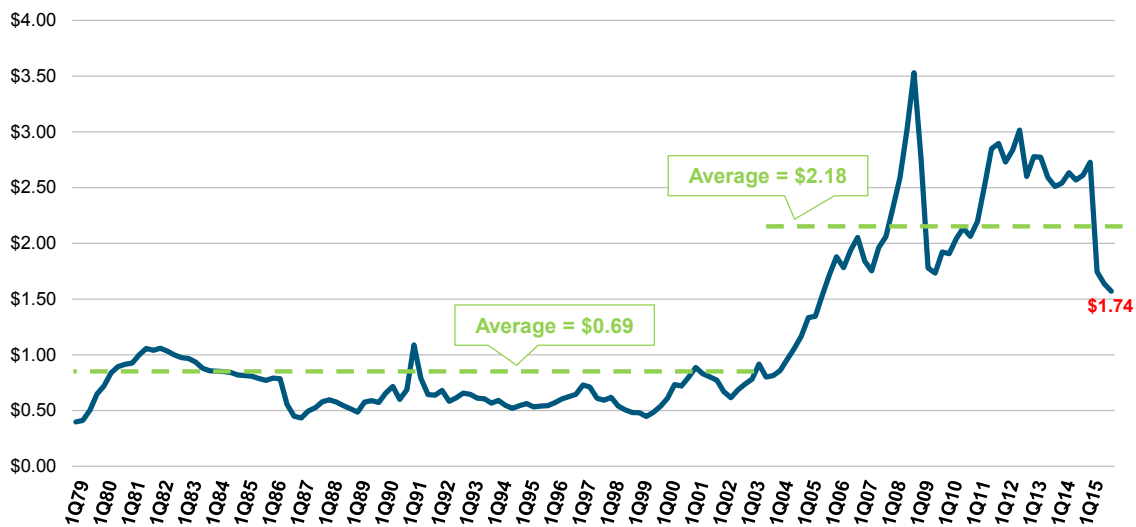
An Uncontrollable Cost:

Fuel was the catalyst the industry needed to change its game



Encouraging signs are on the horizon however. It is important to note that it has become less the absolute price of oil and more about the volatility that troubles the industry. Whereas volatility was the rule from 2004 through 2011, instability in the price of jet fuel moderated for two years then volatility again has become an issue albeit at a much lower price point. Moreover, virtually every futures forecast at the time suggested that the price of oil would remain at or \$100 per barrel or may even trend down modestly. There was even one long-time aviation observer that believed that the price of oil would drop to \$40 per barrel in 2017. While that seemed unrealistic just two years ago given the many geopolitical uncertainties in the world, it underscores the difficulty in predicting the price of jet fuel as an input cost.

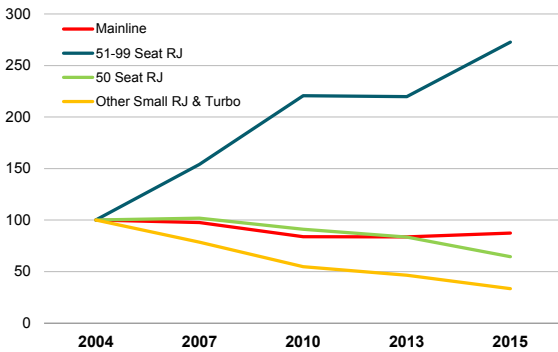
Fueling the Reinvestment
Yet today's jet fuel expense remains the industry's largest



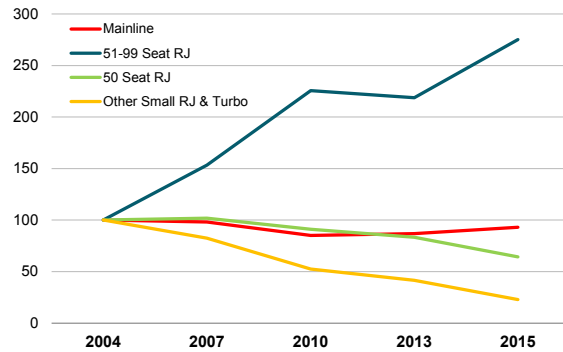
Certainly the escalation in the price of oil had a profound effect on the airline business and as a result, the airport business. The sector most impacted is the regional business where the simple rise in the price of oil made the 50-seat airframe uneconomic. But there is more to come in the regional sector and this will impact airports large and small. And with oil at \$40 per barrel, which in turn would make the 50-seat platform economic, this issue is even more prevalent.

A structural issue has presented itself with regard to the number of qualified pilots available to meet the demand for licensed airmen. That tempest is a combination of regulation and chronological age. 1500 hours is now required to get a license to fly commercially (can be less if hours are gained at a recognized university for example); new flight time/duty time regulations require that each airline have more pilots on hand to do the same amount of flying previously done; and the fact that the mainline airlines face a significant number of pilot retirements from now until 2024 which will also increase demand. All things point to a regional sector getting even smaller over the coming years as many markets will not be able to support a trend toward larger airframes, as well dealing with the structural issue, impacting pilot supply. Since 2010, the average seat size of an aircraft in the domestic market has increased 14%. The average size of a regional aircraft is now 53 seats, much greater than a decade ago.

51 Percent of 50-seat and Less Departures Cut Since 2000
Frequencies
2004 = 100.0

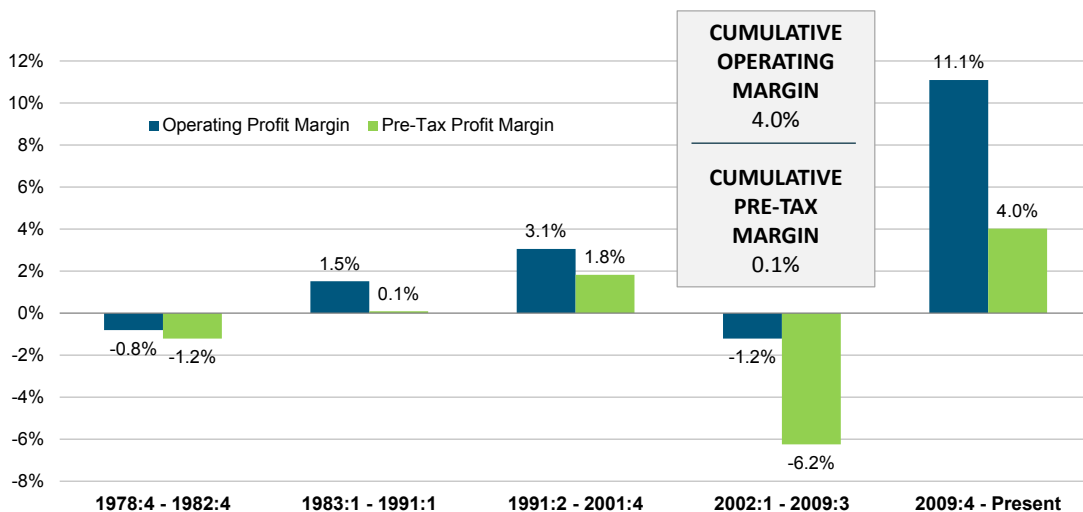


86 Million 50-seat and Less Seats Cut Since 2004
Departed Seats
2004 = 100.0



The bottom line also presents a very different result in this business cycle. Whereas the industry had lost a cumulative \$44 billion between the time the industry was deregulated and the first quarter of 2010, this cycle is much different. The magnitude of the losses was but one factor that caused the majority of industry to file for bankruptcy protection in order to restructure their operations. In 2015, pre-tax margins will approach 14 percent. Finally the industry is earning profit margins like US industry and the airline companies are actually earning profits and re-investing a portion of those profits back into the business. This is very different than cycles in the past where the industry was merely clinging for survival. No longer can it be said that the industry has lost money since it was deregulated. As of the fourth quarter of 2015, the industry has made back all of the historic losses and now shows a profit of \$200 million.

The Current Business Cycle Is Something Different:
The latest margins are on par with US industry

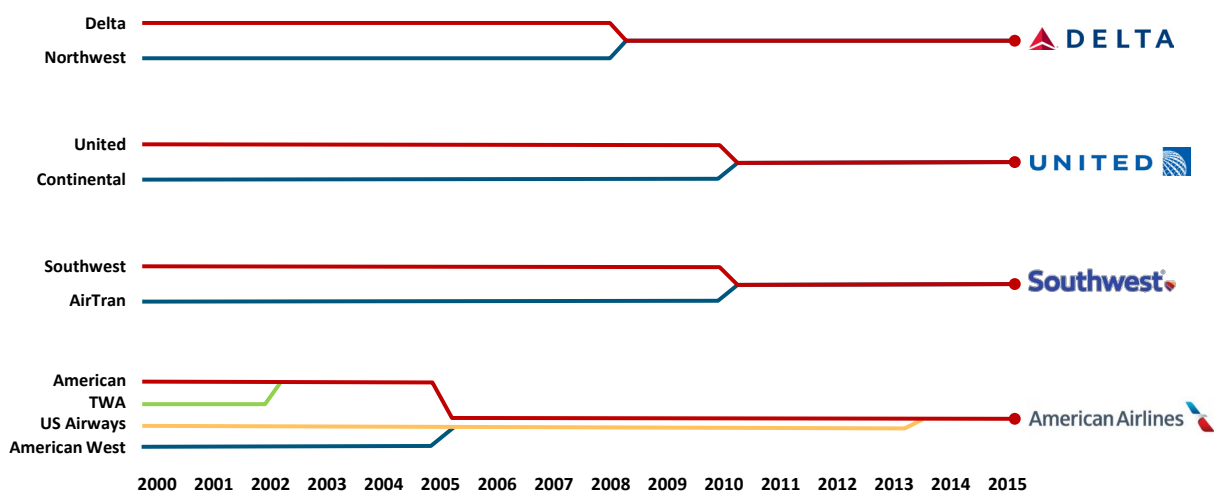


Data Source: A4A Airline Cost Index Tables

THE LANDSCAPE – ARE WE PEAKING AND ARE THE CHANGES LONG LASTING?

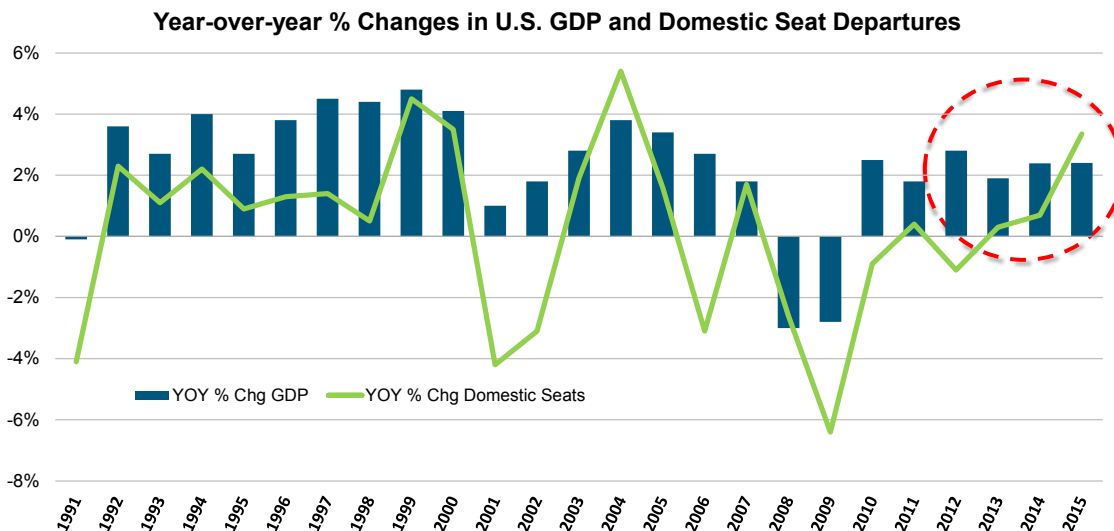
The concentration of the industry has certainly been an important factor in increasing the barriers to entry and the pricing environment in the US domestic marketplace. In addition to consolidation, the availability of capital (or lack of), high and volatile fuel prices, general lack of facilities in the nation's largest markets and simply a mature market have all worked to increase those barriers. And now a scarcity of qualified pilots presents itself. On the international side however, barriers to entry have been reduced as Open Skies Agreements create and present opportunities for international entry.

Today the Big 4 U.S. Airlines Hold 80% of the Domestic Market



Past airline management behaviors have been changed by the new guard. In the past, capital was merely recycled among and between industry stakeholders, with the exception being the shareholders. That is not the case today. In the past the industry competed away found economic gains, and efficiencies, largely in the name of low and lower air fares. That is not the case today. Yesterday's airline industry emulated other capital intensive, commodity-like industries by over-expanding during the up cycles and not removing inefficient capacity in the down cycles. This is certainly not the case today as the industry has actually been removing capacity and/or growing capacity at a slower rate than GDP during the expansionary phase of the current business cycle in the name of capacity discipline.

This Business Cycle Defines Capacity Discipline:
Domestic seat growth that is less than the growth in Real GDP



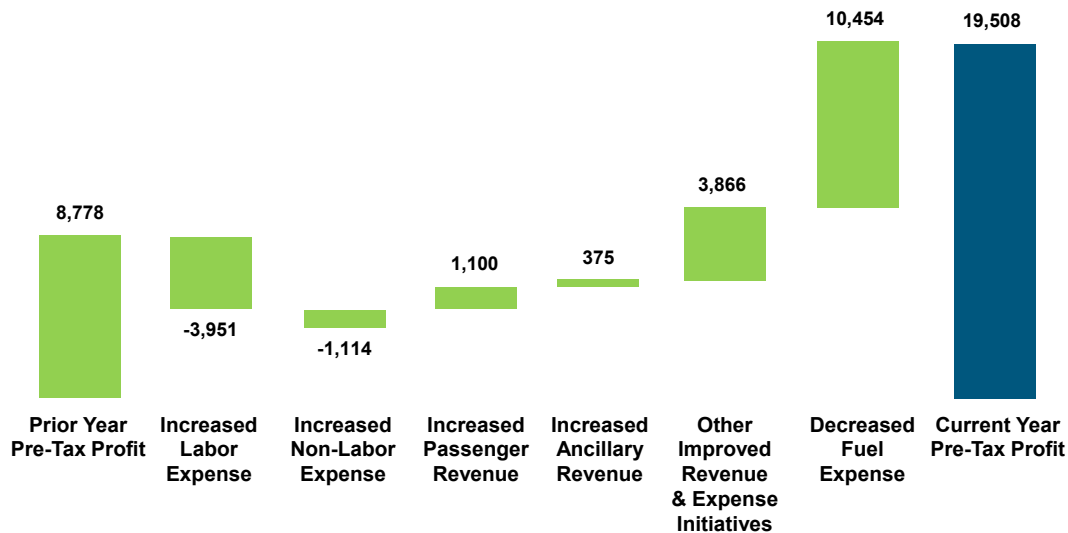
Source: US DOT T-100 database, via Diio online portal. BEA

Going forward, the number of dots on the airline map will be fewer. This will have some impact on airports of all sizes with the disproportionate impact being felt at the smaller markets. Given the mindset of current managements, profitability across the entire business cycle will remain the mantra and this cycle sets the bar very high. Prices to the air travel consumer will likely have to increase to maintain margins and will test the elasticity for an increasing number of flyers. Ultra-low cost carriers Spirit, Frontier and Allegiant will continue to find opportunities to grow by taking advantage of the cost spread they enjoy over the network carriers.

As costs at the network carriers creep up; and as the network carriers test the incremental consumer's price elasticity; and if fuel prices are to remain relatively low as compared with 2008 with little volatility; there may indeed be some new competition that finds its way into the US domestic market before 2020. The transatlantic market will look more and more like a domestic transcon market as lower cost carriers begin to put their toes into transoceanic waters.

History suggests that this business cycle will peak in 2016 or early 2017. This business cycle will end sometime in 2017 or early 2018 at the latest. Lower fuel prices will either bail out the incumbent network carriers or give capital sufficient comfort to fund start-ups again much like the last cycle which saw the low cost carriers grab 20 points of domestic market share. For the 12 months ending September 2015, the fuel savings versus the prior 12 months explained 97% of the pre-tax profit improvement. A scary proposition it seems is to realized improved profitability on fuel savings alone.

Fuel Explains 97% of the Year Current Profit Improvement
Balance sheets, shareholders and employees benefit



ARE WE PEAKING? HISTORY SUGGESTS YES.

Whether it be the macroeconomic indicators; or the fact that US companies have experience declines in profits for three consecutive quarters – the worst since the Great Recession; or the fact that labor rates are increasing at significant rates; or the fact that the industry has significant new aircraft on order; or the fact that merger and acquisition activity is likely to slow with another potential; or the fact that airlines are again growing capacity in at least the largest markets trying to increase revenue on volume over unit price; many indicators show eerily similar to points in the past when economic contraction begins. All of the above data points define cycle peaks not to mention that 2016 is a presidential election year.

The financial condition of the industry is light years better than past slowdowns as debt has been reduced and significant capital expenditures are being funded with improved profits and free cash flow. In every prior business cycle passenger load factors increased and this cycle is no different. In every other business cycle hub and spoke systems came and went and this cycle is no different. In at least the past three business cycles the LCCs/ULCCs became increasingly prevalent and this cycle is no different particularly as the ULCCs penetrate large metropolitan areas.

Where this cycle is different is that fares have trended up although the past 12 months have proven to be a most difficult pricing environment. And this cycle is different in that small community air service saw meaningful benefits primarily from the construction of hubs and spokes to airframes that could seat more and enhance competition by flying to points longer than the 400-mile limit of the turboprop aircraft.

To put things into perspective for those who suggest that the industry is gouging the consumer in the form of high and higher fares, it is important to understand that even today; base airfares alone produce only a modest operating profit per enplaned passenger. If not for ancillary revenue, what the passenger pays per enplanement does not pay the bills. Yes some costs like cargo are included but they are modest and do not change the story. The most recent 12-month period looks very different than the cycle in its entirety in

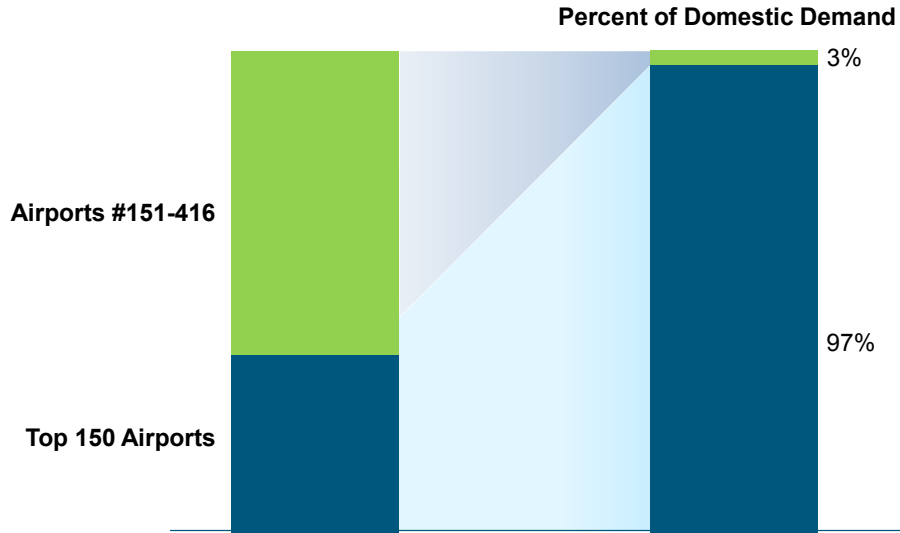
a number of ways like fuel per enplanement is down \$15 as compared to the cycle in total but labor rates are up \$10 per enplanement. It really does feel like the beginning of the end of this cycle.

Income Statement Based on Passenger and Ancillary Revenue ONLY
Revenue and expense metrics are per enplanement

	1978:4 - 1982:4	1983:1 - 1991:1	1991:2 - 2001:4	2002:1 - 2009:3	2009:4 - Present	12 Mos. Ending Sept. 2015
Quarters in Business Cycle	17	33	43	31	24	
Enplanements (000)	1,252,134	3,390,017	6,111,368	5,331,409	4,184,772	777.8
Passenger Revenue	\$ 92.48	\$ 108.68	\$ 130.45	\$ 134.89	\$ 167.45	162.97
Labor Expense	\$ 38.34	\$ 40.34	\$ 49.02	\$ 46.95	\$ 43.72	\$ 53.31
Fuel Expense	29.21	21.33	17.46	38.19	55.11	40.22
Commission Expense	6.02	10.78	11.15	2.31	1.98	1.64
Landing Fee Expense	1.83	2.19	2.93	3.56	3.84	3.67
All Other Expense	\$ 29.58	\$ 44.05	\$ 59.12	\$ 61.13	\$ 66.44	\$ 63.93
Total Operating Expense X TR	\$ 104.98	\$ 118.69	\$ 139.68	\$ 152.15	\$ 171.10	162.78
Total Operating Profit/Loss	\$ (12.50)	\$ (10.01)	\$ (9.23)	\$ (17.25)	\$ (3.65)	\$ 0.19
Ancillary Revenue	\$ 0.18	\$ 0.36	\$ 2.15	\$ 2.47	\$ 8.75	8.66
Op after Ancillary Revenue	\$ (12.32)	\$ (9.65)	\$ (7.07)	\$ (14.79)	\$ 5.10	\$ 8.85
Interest Expense /1	\$ 4.79	\$ 3.71	\$ 3.83	\$ 5.72	\$ 3.11	\$ 3.11
Pre-Tax after Ancillary Revenue	\$ (17.11)	\$ (13.36)	\$ (10.90)	\$ (20.51)	\$ 1.99	\$ 5.74

What about air service in a macroeconomic slowdown or even a recessionary period? If pilot supply is an issue, then forced retirements at age 65 do not change the calculus nor does the trend toward larger aircraft. The mainline carriers may slow down some deliveries however the demand for pilots just to stay the same size for the mainline carriers basically remains the same. The same pressure on the regional sector shows no signs of relief. Historically we have always seen some pulldown in capacity during recessionary periods and I am confident that the next one will be no different. The network carriers continue to make significant changes in frequencies and seats at small and non-hub airports. Those airports that are losing frequencies and seats in 2016 versus 2015 should feel some vulnerability as clearly they are underperforming markets relative to others on the respective networks. And then there is the 37:97 proposition.

A Hard Fact: The 37:97 Proposition
37 percent of mainland airports produce 97% of demand



Source: US DOT, DB1B database, YE3q 2015, via Diio online portal.

APPENDIX

	1978:4 - 1982:4	1983:1 - 1991:1	1991:2 - 2001:4	2002:1 - 2009:3	2009:4 - Present	12 Mos. Ending Sept. '15
Quarters in Business Cycle	17	33	43	31	24	4
Nominal Gross Domestic Product	2,981.4	4,835.1	8,319.0	13,122.6	16,316.6	17,809.8
Consumer Price Index	84.5	114.1	156.7	197.7	229.0	237.0
Real Gross Domestic Product	6,501.3	8,011.7	10,793.4	14,101.8	15,469.5	16,345.0
Consumer Confidence	67.7	90.9	93.7	83.4	78.3	93.0
Total Enplanements (000)	1,252,134	3,390,017	6,111,368	5,331,409	4,184,772	567,964
Total Revenue Passenger Miles (000)	1,080,596	3,134,033	6,234,878	5,804,170	4,996,789	889,596
Total Available Seat Miles (000)	1,803,746	5,078,606	9,110,513	7,506,932	6,037,407	1,067,066
Load Factor (Percent)	59.9%	61.7%	68.4%	77.3%	82.8%	83.4%
Regional Available Seat Miles (000)	72,880	39,678	165,290	569,357	554,380	90,125
Regional ASMs as pct. Of Total ASMs	4.0%	0.8%	1.8%	7.6%	9.2%	8.4%
Total Operating Seats	6,315,646	16,785,887	29,531,638	23,698,807	18,903,263	3,286,815
Passenger Yield (cents per RPM)	10.72	11.76	12.79	12.39	14.02	14.25
Passenger Yield with Ancillaries	10.74	11.79	13.00	12.62	14.76	15.01
Passenger Unit Revenue (cents per ASM)	6.42	7.25	8.75	9.58	11.61	11.88
Passenger Unit Revenue with Ancillaries	6.43	7.28	8.90	9.76	12.21	12.51
Cost per Available Seat Mile (x Trans Rel)	7.29	7.92	9.37	10.81	11.86	11.87
Cost per Available Seat Mile (xTR and Fuel)	5.26	6.50	8.20	8.09	8.04	8.93
Labor Cost per Available Seat Mile	2.66	2.69	3.29	3.33	3.03	3.89
Labor Cost per Operating Seat	30,401.67	32,583.73	40,575.77	42,246.48	38,714.89	50,465.93
Fuel Cost per Available Seat Mile	2.03	1.42	1.17	2.71	3.82	2.93
Fuel Cost per Operating Seat	23,165.01	17,228.58	14,450.22	34,366.72	48,799.37	38,068.54
Non-Labor Cost per Available Seat Mile	2.60	3.81	4.91	4.76	5.01	5.05
Total Operating Seats	6,315,646	16,785,887	29,531,638	23,698,807	18,903,263	3,286,815
Total Passenger Enplanements (000)	1,252,134	3,390,017	6,111,368	5,331,409	4,184,772	567,964
Average Full-Time Equivalents	333,020	380,662	476,335	424,896	384,568	391,711
Total Passenger Revenue (Millions)	115,792	368,424	797,247	719,158	700,748	126,760
Total Ancillary Revenue (Millions)	226	1,225	13,160	13,160	36,613	6,734
Total Operating Revenue (Millions)	133,150	417,332	904,026	910,941	938,528	169,464
Total Labor Expense (Millions)	\$48,001.55	\$136,737	\$299,567	\$250,298	\$182,959	\$41,468
-- as a percent of total Op Expense	35.8%	33.3%	34.2%	27.1%	21.9%	28.5%
Total Labor Expense per FTE	\$33,915.34	\$43,540.28	\$58,502.32	\$76,010.27	\$79,292.14	\$105,864
ASMs per FTE (000)	1,276	1,614	1,779	2,293	2,612	2,723
Total Fuel Expense (Millions)	\$6,575	\$72,299	\$106,685	\$203,613	\$230,617	\$31,281.1

	1978:4 - 1982:4	1983:1 - 1991:1	1991:2 - 2001:4	2002:1 - 2009:3	2009:4 - Present	12 Mos. Ending Sept. '15
-- as a percent of total Op Expense	27.2%	17.6%	12.2%	22.1%	27.6%	21.5%
Total Gallons of Fuel Consumed	43,655	106,279	171,569	124,694	94,750	16,410
Price per Gallon	\$0.84	\$0.68	\$0.62	\$1.63	\$2.43	\$1.91
Total Commissions Paid (Millions)	\$7,533	\$36,549	\$68,152	\$12,342	\$8,292	\$1,275
Percent of Passenger Revenue	6.5%	9.9%	8.5%	1.7%	1.2%	1.0%
Landing Fee Expense (Millions)	\$2,296	\$7,420	\$17,915	\$18,966	\$16,089	\$2,099
Transport Related Expense (Millions)	\$2,784	\$8,643	\$22,768	\$110,776	\$118,414	\$18,790
Total Operating Expense (Millions)	\$134,229	\$410,992	\$876,404	\$921,927	\$834,428	145,398.50
Total Operating Profit (Millions)	\$(1,078)	\$6,340	\$27,622	\$(10,986)	\$104,100	\$24,065
-- Operating Margin	-0.8%	1.5%	3.1%	-1.2%	11.1%	14.2%
Pre-Tax Profit (Millions)	\$(1,609)	\$389	\$16,528	\$(56,894)	\$37,701	\$19,508
-- Pre-Tax Profit Margin	-1.2%	0.1%	1.8%	-6.2%	4.0%	11.5%



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