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## A4A Operational and Financial Review of 1H 2016

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Vice President & Chief Economist  
A4A Media Briefing  
August 17, 2016

# A4A Projects U.S. Airlines to Carry 15.6M Passengers Over Labor Day\* 2016: +4% Growth in Available Seats Will Exceed Growth in Passenger Volume

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## U.S. Airline Onboard Labor-Day Period Passengers (Millions)



- 
- Airlines will **carry 2.23M passengers/day** (up 81.5K)
  - Airlines will **offer 2.54M seats/day** (up 98.2K)
  - The Thursday (#2) and Friday (#1) preceding LD are typically the busiest days of the period

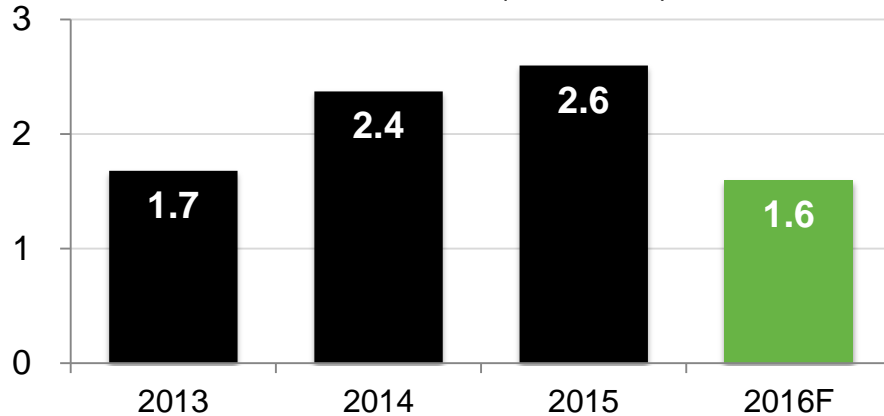
Source: A4A, Innovata (via Diio Mi) TSA and BTS T100 segment data, scheduled service on U.S. carriers only

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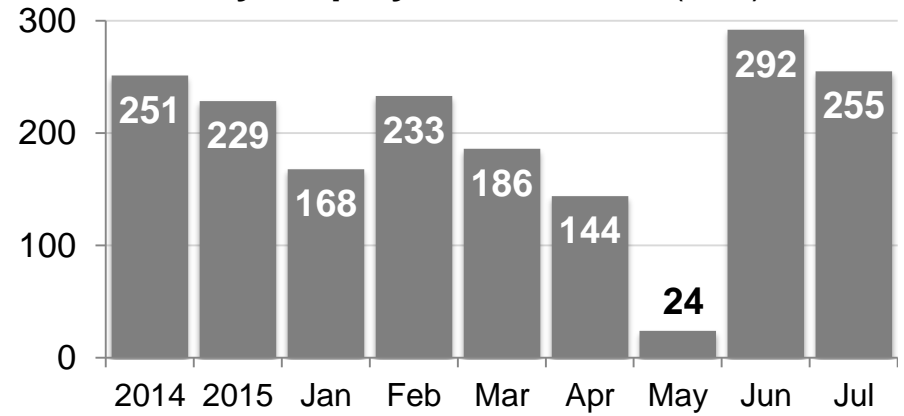


# U.S. Economy Still Expanding But Decelerating, Job Growth Volatile

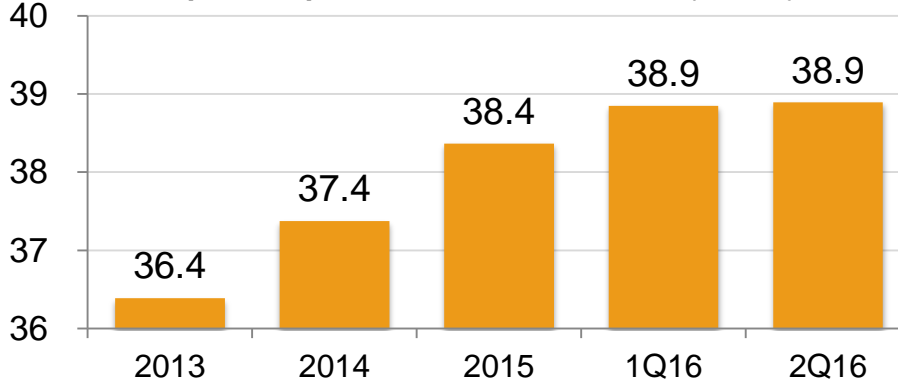
### Real GDP Growth Rate (% CAGR)



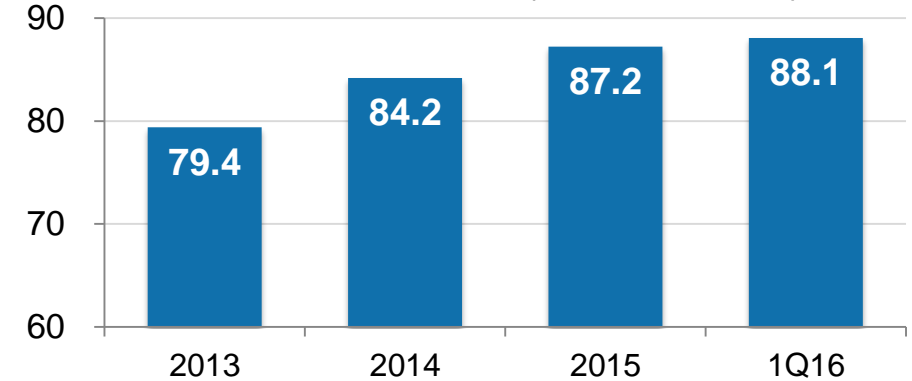
### Monthly Employment Growth (000)



### Real (\$2009) Personal Incomes (\$000)



### Household Net Worth (\$ Trillion, NSA)



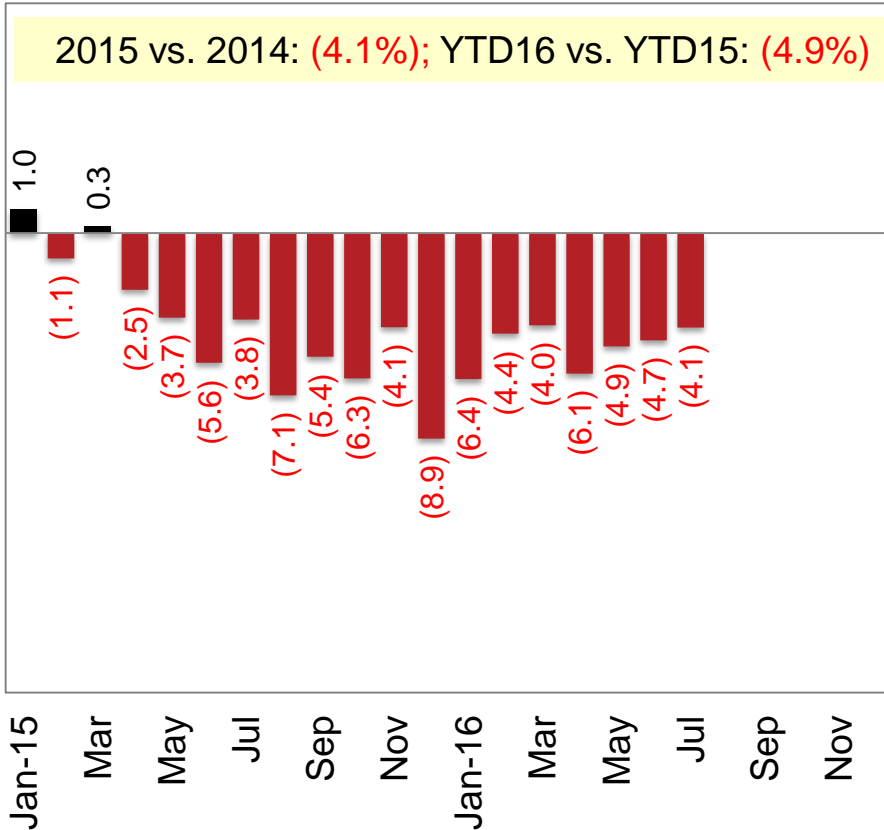
Sources: BEA, BLS, Federal Reserve and IHS Economics; U.S. GDP real annual average growth rate (%), U.S. nonfarm payroll employment growth (month-over-month, in 000s, seasonally adjusted), U.S. disposable personal income per capita (chained 2009 dollars, SAAR); U.S. household net worth in current dollars, not seasonally adjusted



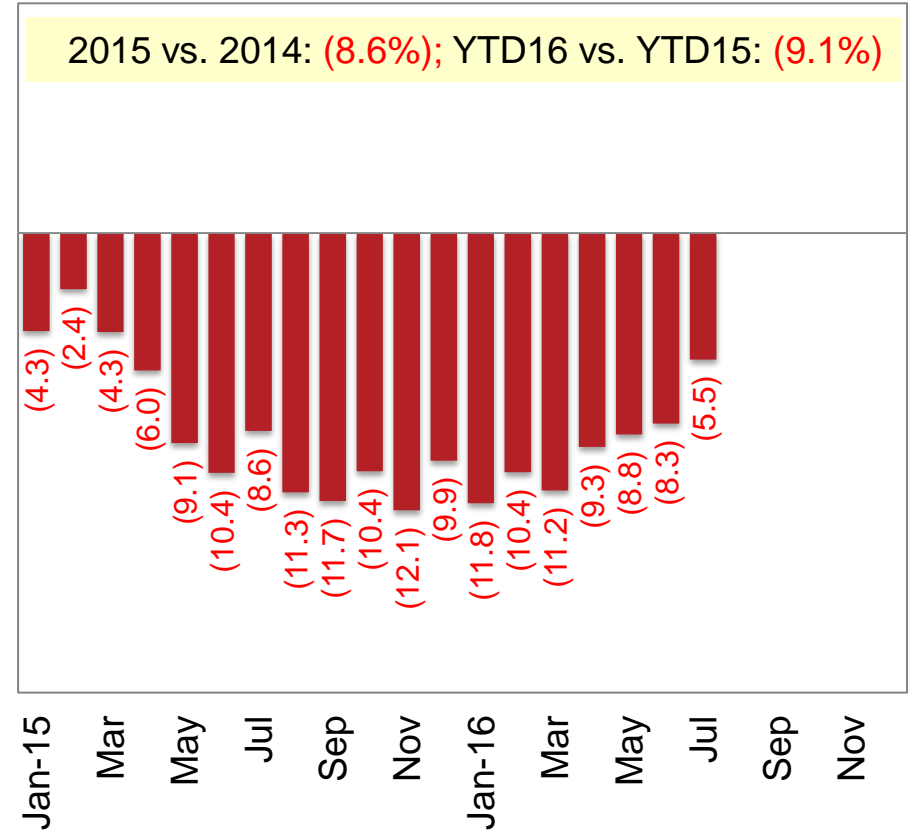
# Amid Competitive Pressures, U.S. Carrier Air Fares\* Continue to Fall in 2016

Systemwide, Fares\* Down 5.2% in 2015 and 5.9% Thus Far in 2016

## % Change YOY in Domestic Yield\*



## % Change YOY in International Yield\*



Source: A4A analysis of data from Alaska, American, Hawaiian, JetBlue, Southwest, United, Virgin America and regional affiliates

\* Fare per mile (cents per RPM)

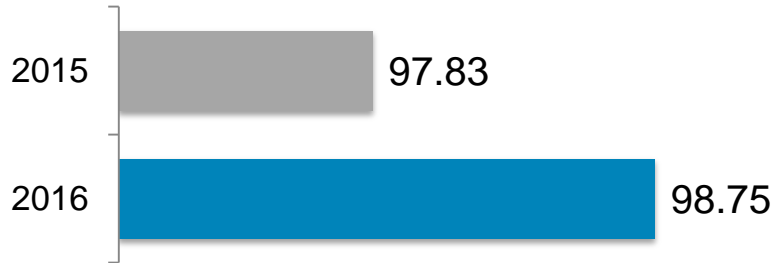


# U.S. Airlines Seeing Improvements in DOT Core-Four Operational Metrics in 2016

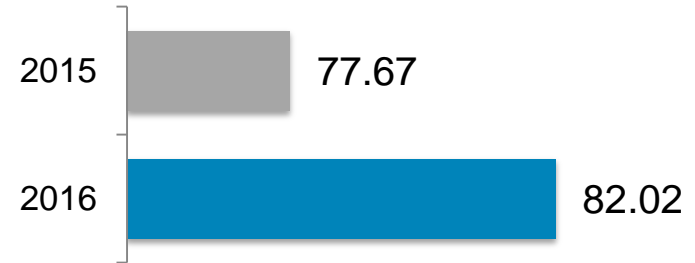
## Gains Driven by More Benign Weather and Investments in Systems, Procedures, Staffing

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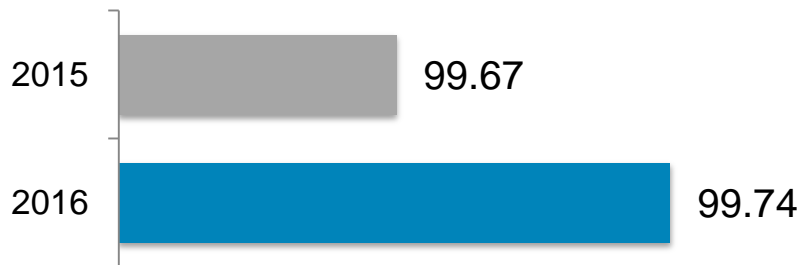
### Flight Completion Factor (%) – Jan-Jun



### On-Time Arrival Rate (%) – Jan-Jun



### Properly Handled Bag Rate (%) – Jan-Jun



### Oversales per 10,000 Customers – Jan-Jun



Sources: BTS and DOT *Air Travel Consumer Report* (<http://www.dot.gov/airconsumer/air-travel-consumer-reports>)

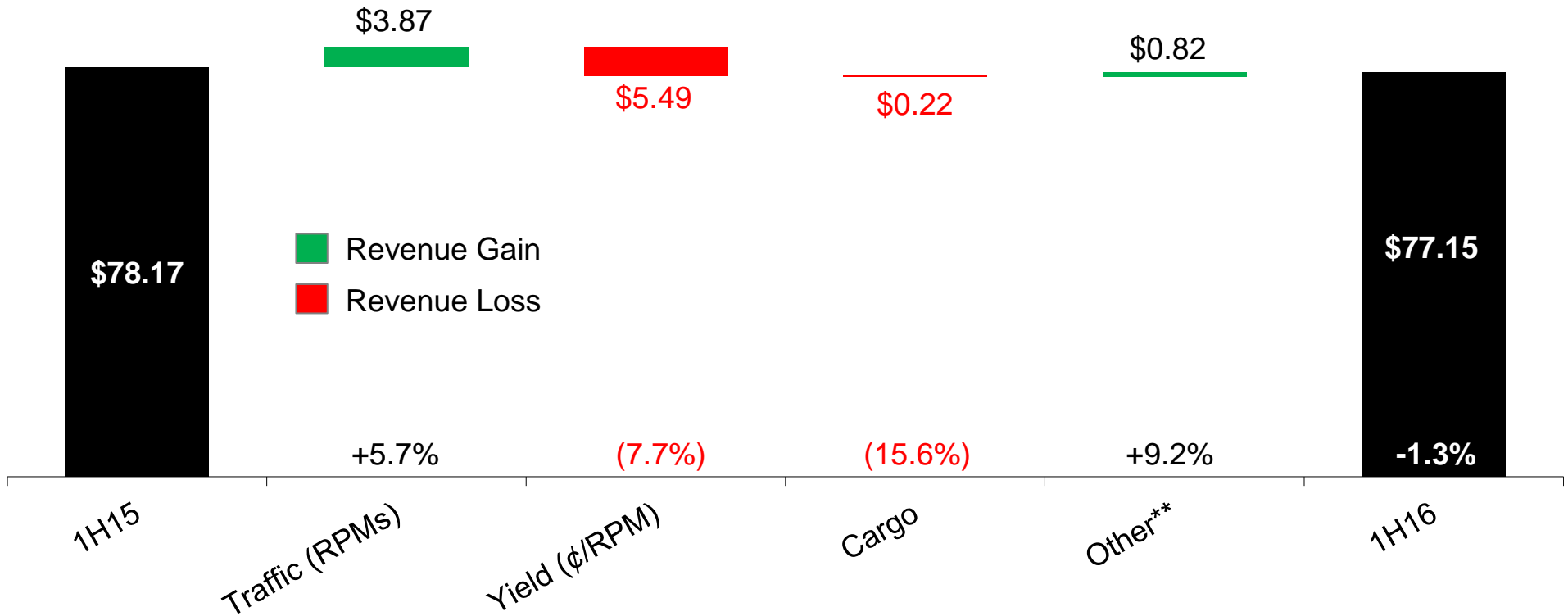
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# 1H16 Airline Operating Revenues\* Fell 1.3% on Lower Fares and Cargo

Passenger Revenue Fell 2.4% on 5.7% Higher Traffic and 7.7% Lower Yield (Fares/Mile)

## Operating Revenues\* (\$ Billions)



\* A4A analysis of reports by Alaska, Allegiant, American, Delta, Hawaiian, JetBlue, Southwest, Spirit, United and Virgin America

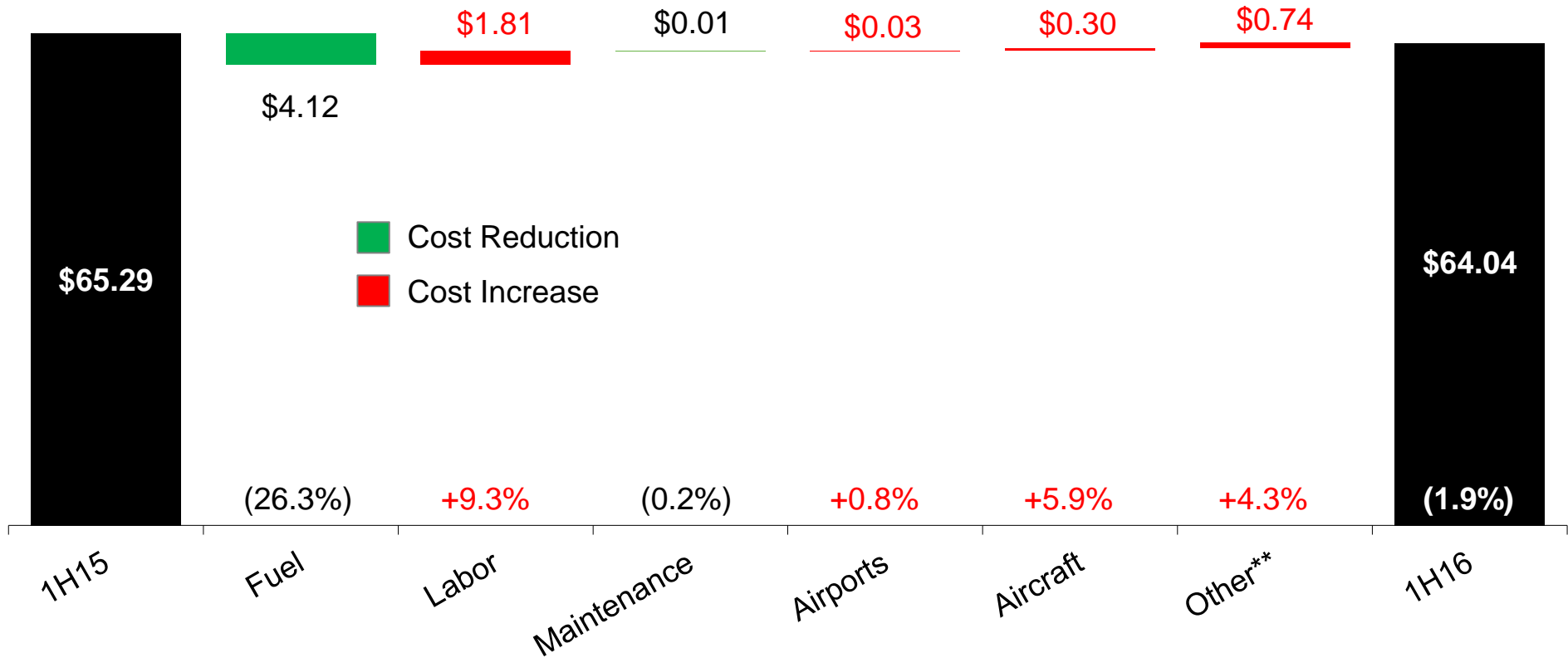
\*\* Sale of frequent flyer award miles to airline business partners, pet transportation, in-sourced aircraft and engine repair, flight simulator rentals, inflight sales, etc.



# 1H16 Airline Operating Expenses\* Fell 1.9% As Lower Fuel Offset Higher Labor

## Airlines Also Saw Increases in Airport and Aircraft Costs

### Operating Expenses\* (\$ Billions)



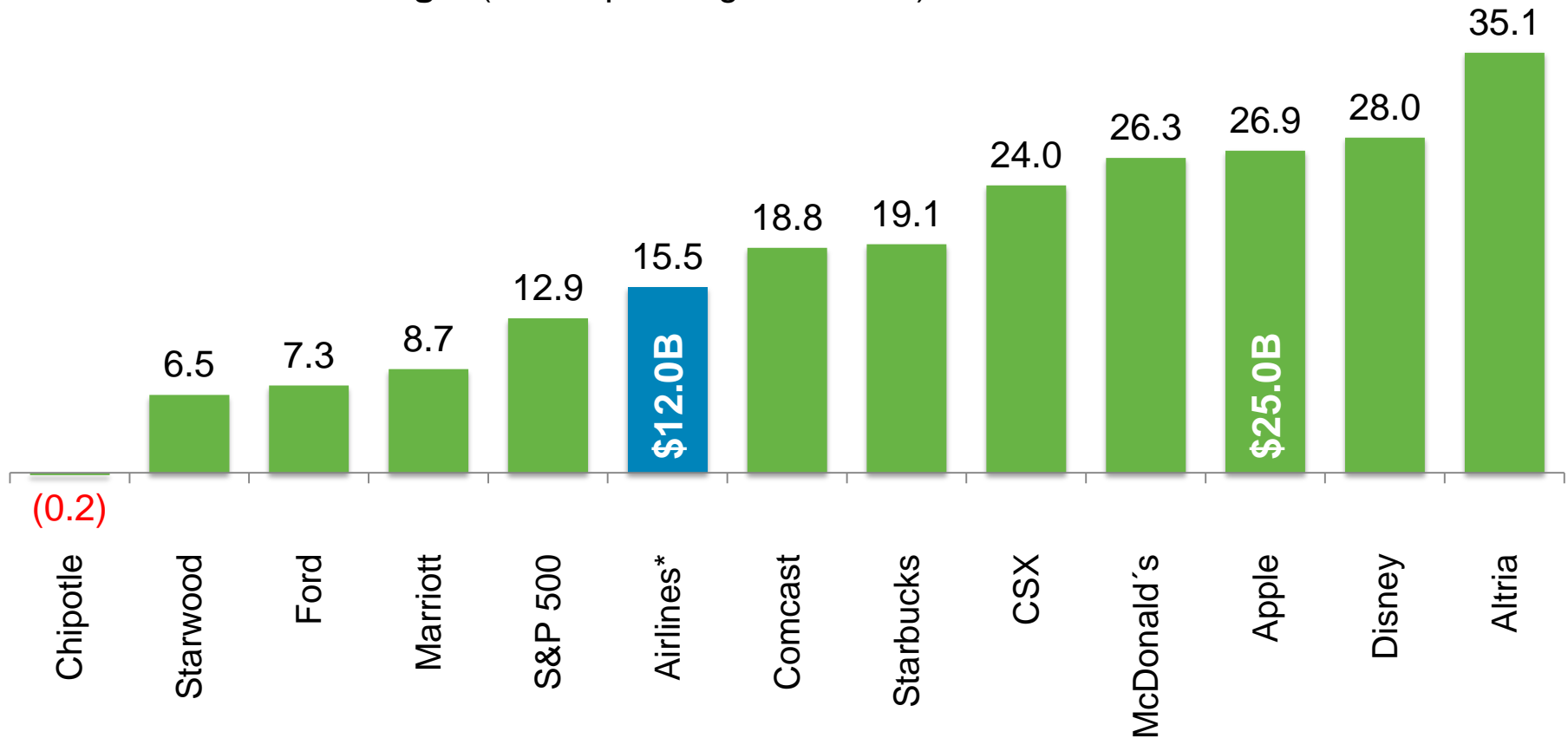
\* A4A analysis of reports by Alaska, Allegiant, American, Delta, Hawaiian, JetBlue, Southwest, Spirit, United and Virgin America

\*\* Professional fees, food/beverage, insurance, commissions, GDS fees, communications, advertising, utilities, office supplies, crew hotels, nonfuel payments to regionals



**In 1H16, U.S. Airlines\* Posted Respectable Margins, Averaging 15.5% Before Taxes**  
**U.S. Passenger Airline\* Profitability Was Substantially Below Starbucks/McDonald's/Apple**

**1H16 Pre-Tax Profit Margin (% of Operating Revenues)**



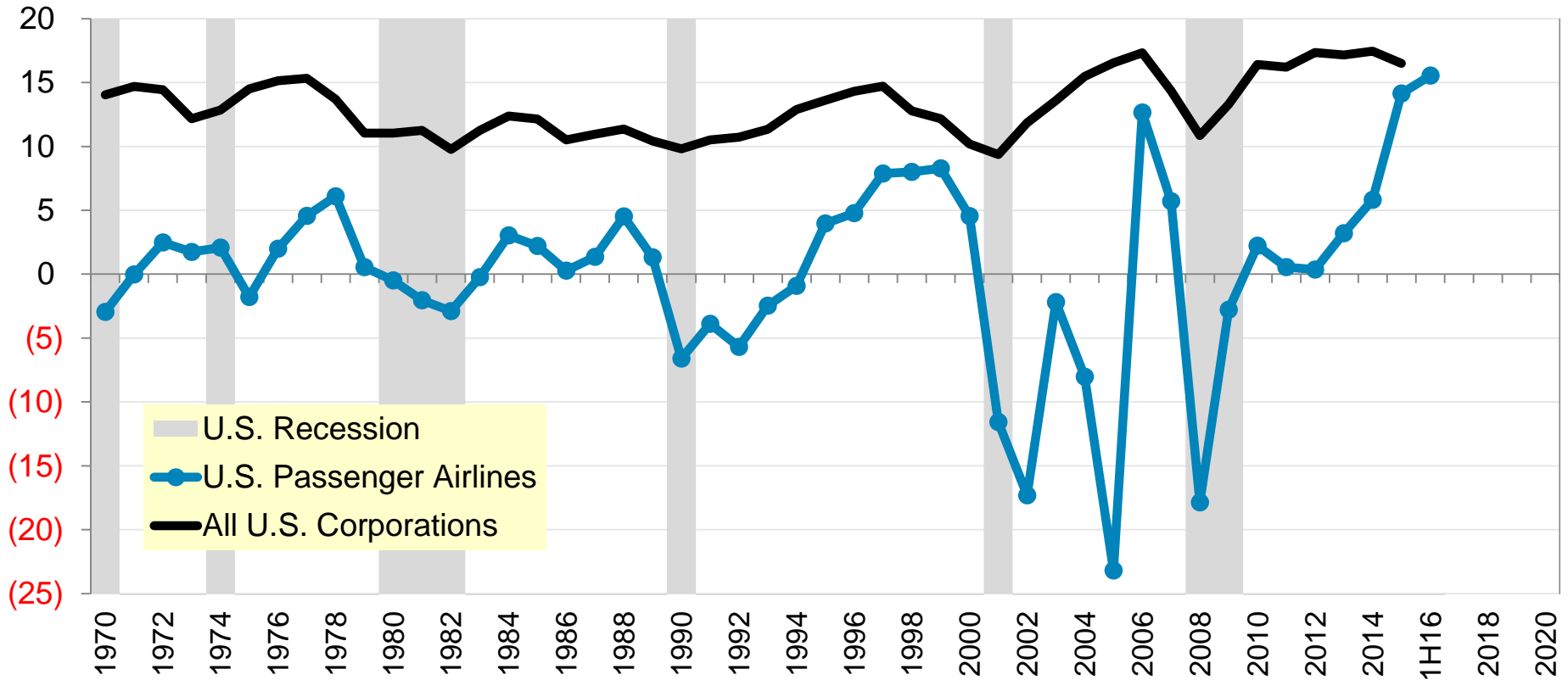
\* A4A analysis of reports by Alaska, Allegiant, American, Delta, Hawaiian, JetBlue, Southwest, Spirit, United and Virgin America





# Since the Great Recession,\* U.S. Airlines Have Been Closing the Gap to Average U.S. Corporate Profitability; 2015 Gap (14.1% vs. 16.5%) Was Narrowest on Record

## Pre-Tax Profit Margin (%)



Source: ATA Annual Reports (1970-1976), A4A Passenger Airline Cost Index (1977-present); Bureau of Economic Analysis NIPA Table 1.14

\* Dec-2007-Jun-2009



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# Airline Creditworthiness Remains Far From Stellar


Per S&P, Only Two U.S. Passenger Airlines Have Investment-Grade Credit

“Standard & Poor’s ratings express the agency’s opinion about the ability and willingness of an issuer...to meet its financial obligations in full and on time.”

## Investment Grade<sup>1</sup> (>= BBB-)

Johnson & Johnson, Microsoft		AAA
GE, ExxonMobil, USG		AA+
Google, Wal-Mart		AA
Toyota		AA-
UPS		A+
McDonald’s, PepsiCo, Target		A
BP, Amtrak, Starbucks		A-
Ryanair, eBay		BBB+
FedEx, Ford, Marriott, SWA, Starwood		BBB
ALK, Lufthansa, Qantas, WestJet		BBB-

## Speculative<sup>2</sup> Grade (< BBB-)

Delta, Turkish	BB+
British Airways	BB
ALGT, AAL, HA, JBLU, LATAM, UAL,	
Avis, Sabre	BB-
AC, Virgin Australia, Hertz	B+
SAS	B
Gol Linhas Aereas (GOL)	CCC
 Passenger Airline	

<sup>1</sup> Describes issuers with relatively high levels of creditworthiness and credit quality

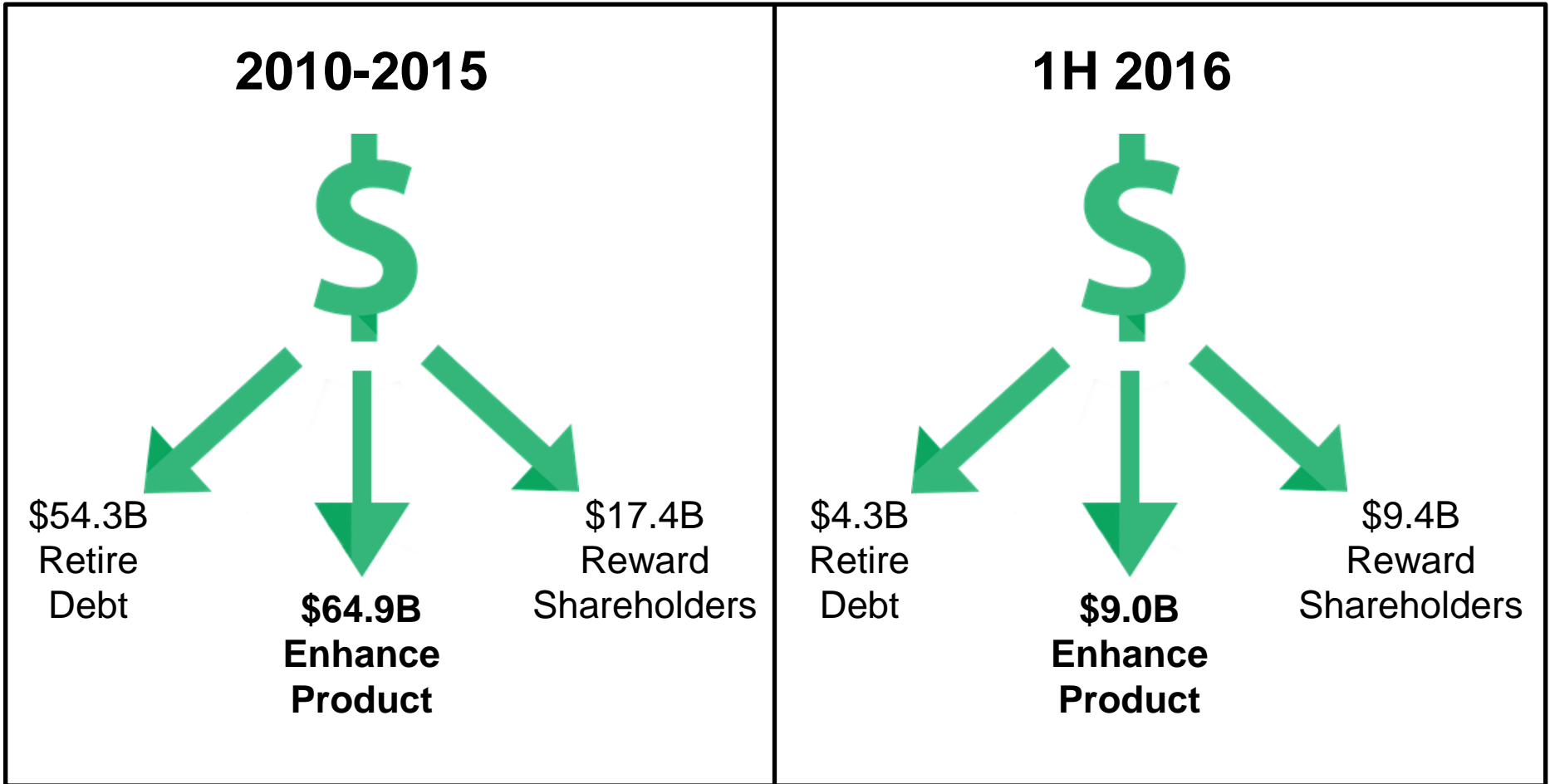
<sup>2</sup> Describes issuers with ability to repay but facing significant uncertainties, such as adverse business or financial circumstances that could affect credit risk

Source: Standard and Poor’s; “Guide to Credit Rating Essentials: What are credit ratings and how do they work?”



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**U.S. Airlines Are Putting More Than \$25 per Passenger\* Right Back Into the Product**  
 Primary Uses of Operating Cash from 2010-1H16 Included \$74B of Capital Reinvestment



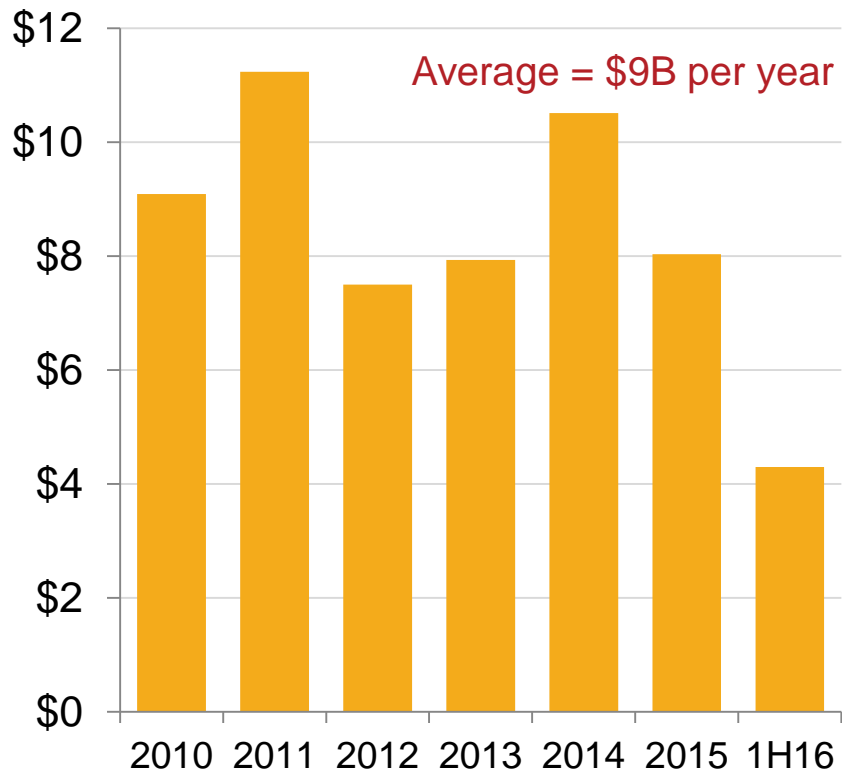
\* SEC filings of Alaska/Allegiant/American/Delta/Hawaiian/JetBlue/Southwest/Spirit/United/Virgin America; denominator is enplaned passengers



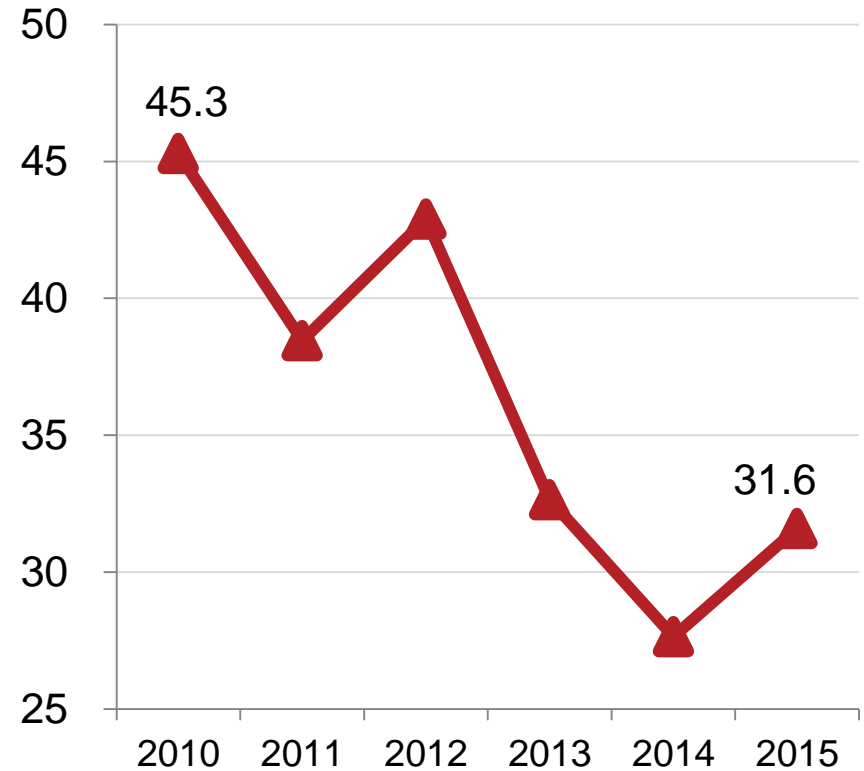
# Following Enormous Losses of 2001-2009, U.S. Airlines Have Retired \$58.6B in Debt

## Adjusted Net Debt Now Just 32% of Operating Revenues, Down from 45% in 2010

Payments on Debt\* (Billions)



Debt\*\* as % of Operating Revenues



Source: SEC filings of AAL/ALGT/AAL/DAL/HA/JBLU/LUV/SAVE/UAL/VA

\* Payments on long-term debt and capital lease obligations

\*\* Includes 7x annual aircraft rents (capitalized operating leases)



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# Improving Finances Enabling Significant Reinvestment in Customer Experience



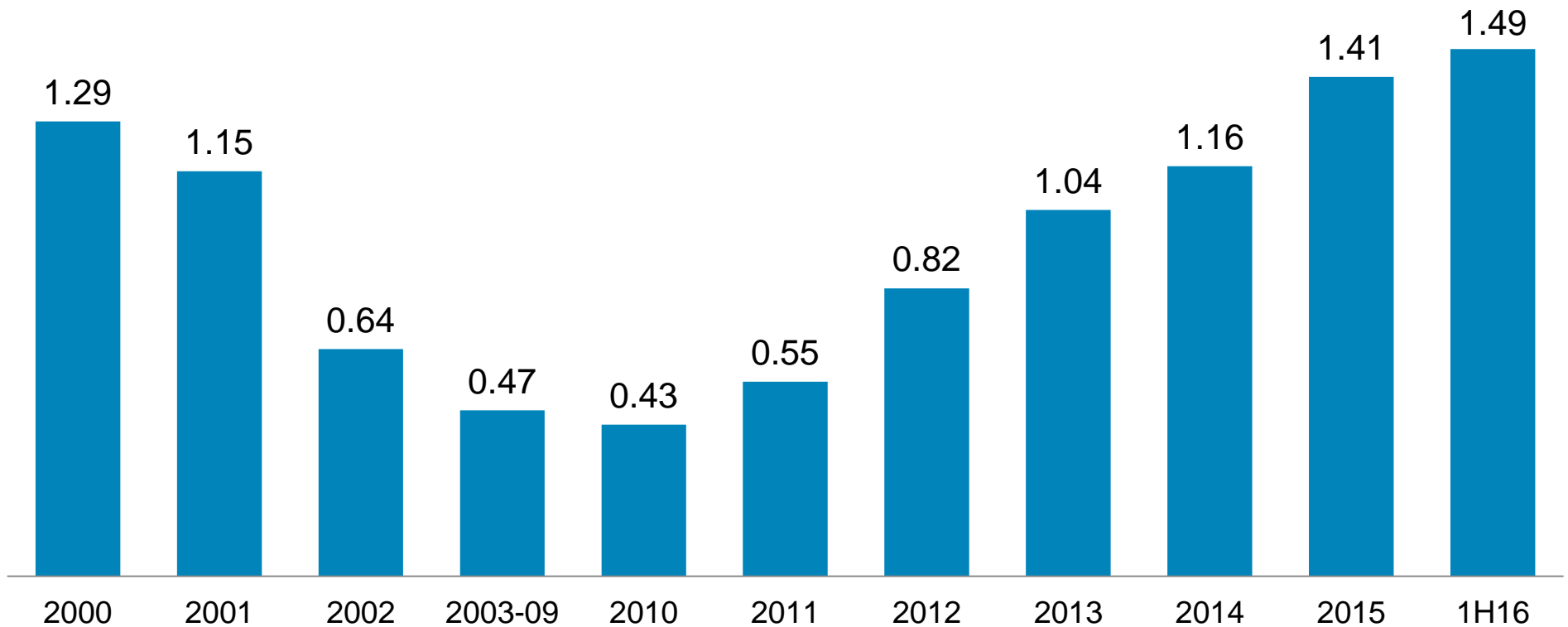
- » New or refurbished aircraft, larger overhead bins for luggage
- » Availability of lie-flat seating with AC power and USB, proliferation of Wi-Fi and inflight entertainment
- » Expanded route networks (scope and frequency) and schedules (seat growth)
- » Improved airport check-in areas, lounges, gate amenities, baggage systems, ground equipment
- » Continued development and roll-out of mobile technology and website/kiosk functionality
- » Increasing operational reliability (controlled for weather conditions)
- » Enhanced tools (computers, tablets, software) and training for customer-contact employees



# Improving Finances Enabling Significant Reinvestment in Customer Experience

1H 2016 Capital Outlays Averaged \$1.5B per Month, Exceeding 2015 Rate

## U.S. Passenger Airline\* Capital Expenditures (\$ Billions per Month)



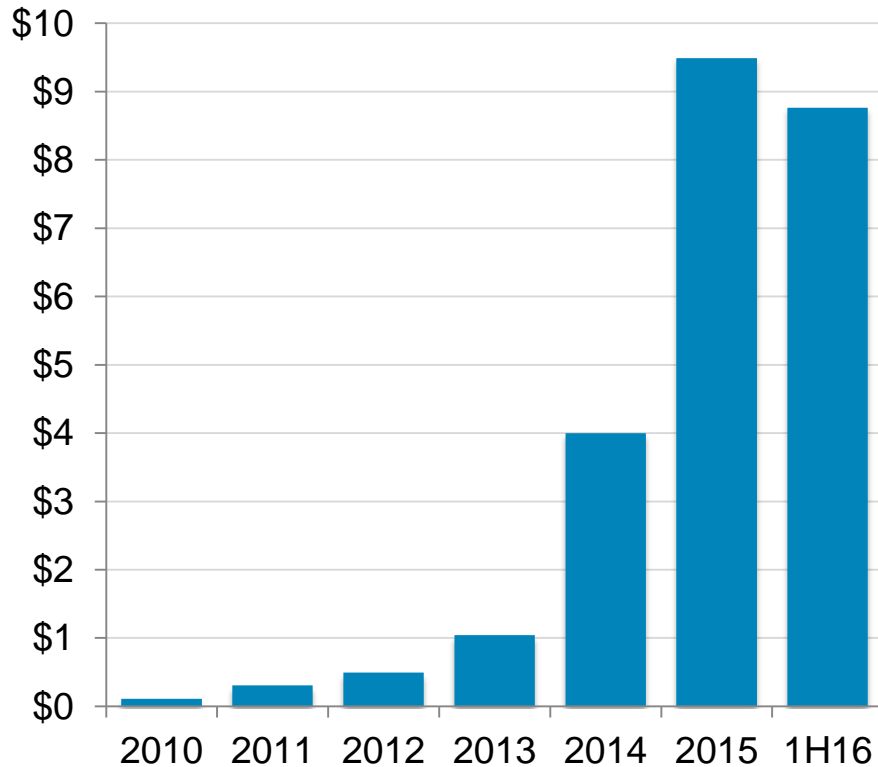
\* SEC filings of Alaska, Allegiant, American, Delta, Hawaiian, JetBlue, Southwest, Spirit, United and Virgin America



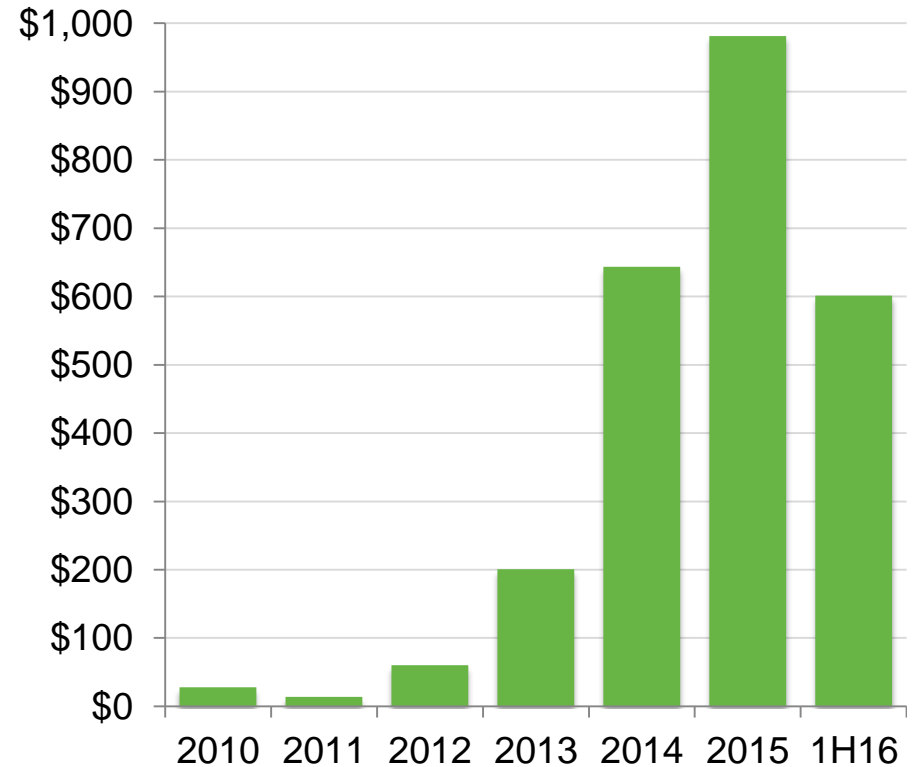
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# In 1H 2016, U.S. Airlines Continued Efforts to Retain and Lure New Equity Investors, Returning \$9.4B to Shareholders Via Stock Buybacks (\$8.8B) and Dividends (\$601M)

## Stock Repurchases (Billions)



## Dividends (Millions)



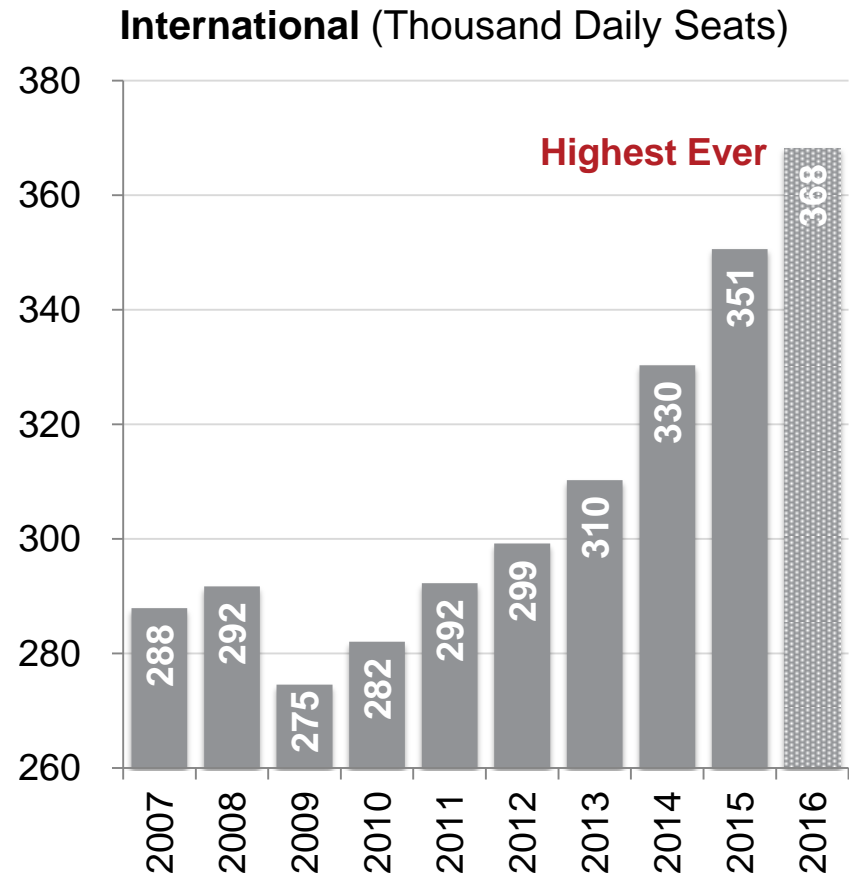
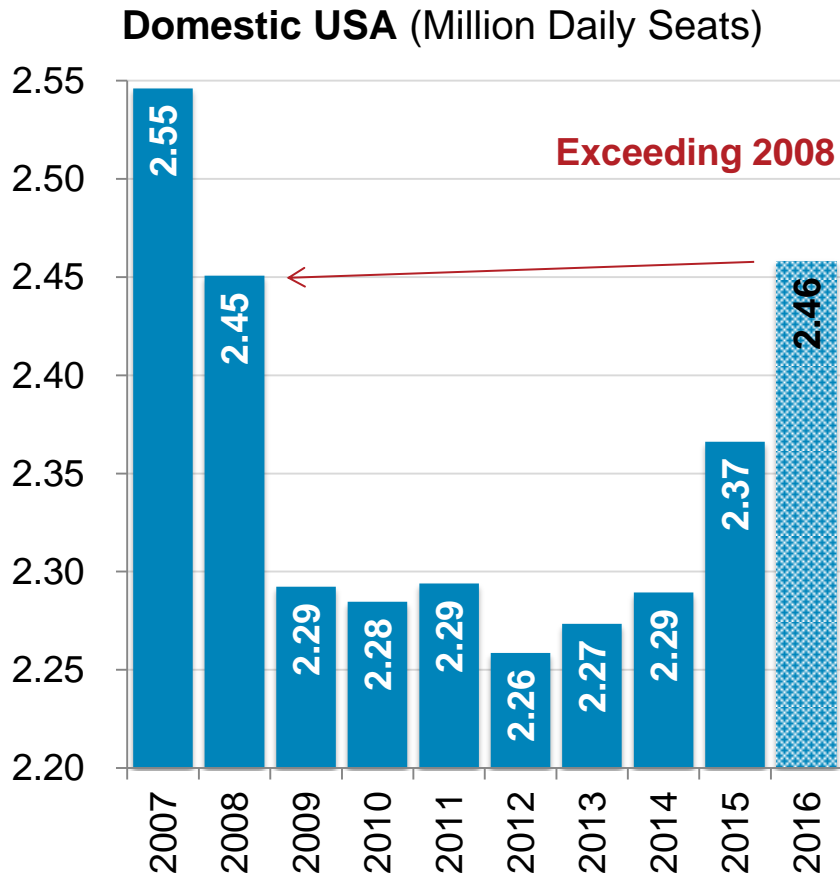
\* SEC filings of Alaska, Allegiant, American, Delta, Hawaiian, JetBlue, Southwest, Spirit, United and Virgin America



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# As Airlines Generate Normal Returns on Capital, Customers Are Seeing More Seats

## Domestic Supply at Highest Point in Eight Years; International Supply at All-Time High



Source: Innovata (via Diio Mi) published schedules as of Aug. 12, 2016, for all airlines providing scheduled passenger service from U.S. airports to all destinations

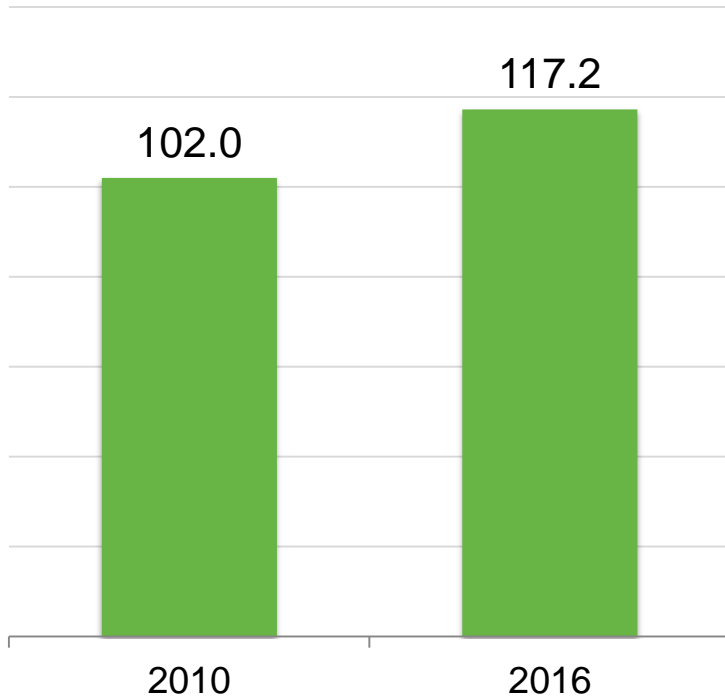




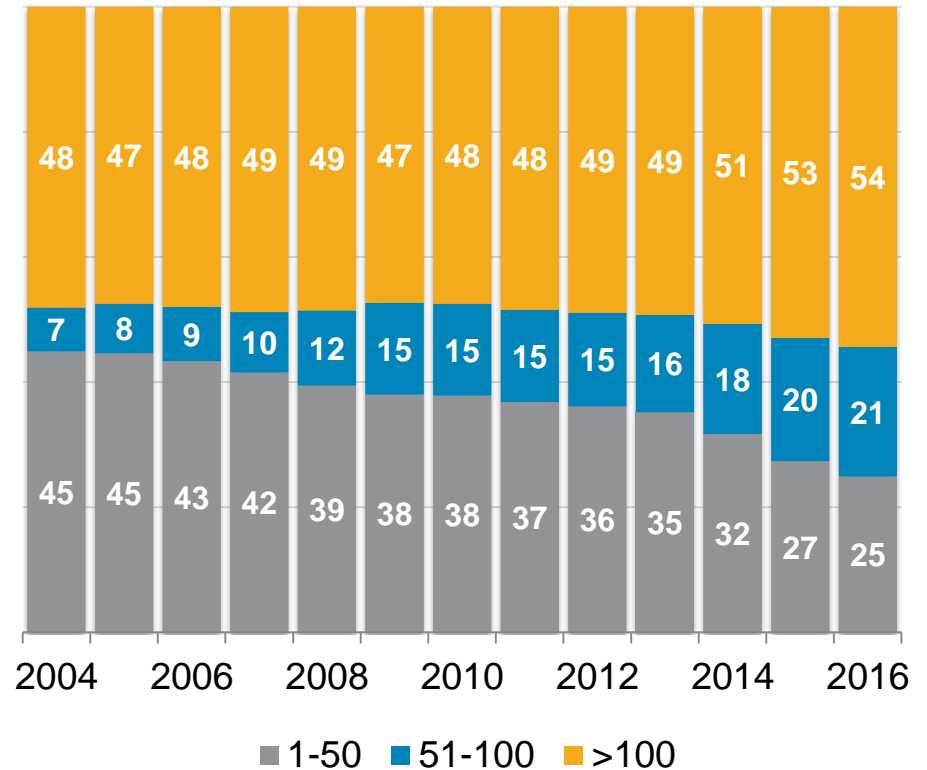
# In Addition to Expanding Schedules, Airlines Are Deploying Larger Aircraft

## Replacement of 50-Seaters With Larger Regional Jets Is Biggest Driver of 15% Jump

Seats per Sched. Domestic Departure



Share (%) of Departures by Aircraft Size



Source: Innovata (via Diio Mi) as of August 5, 2016

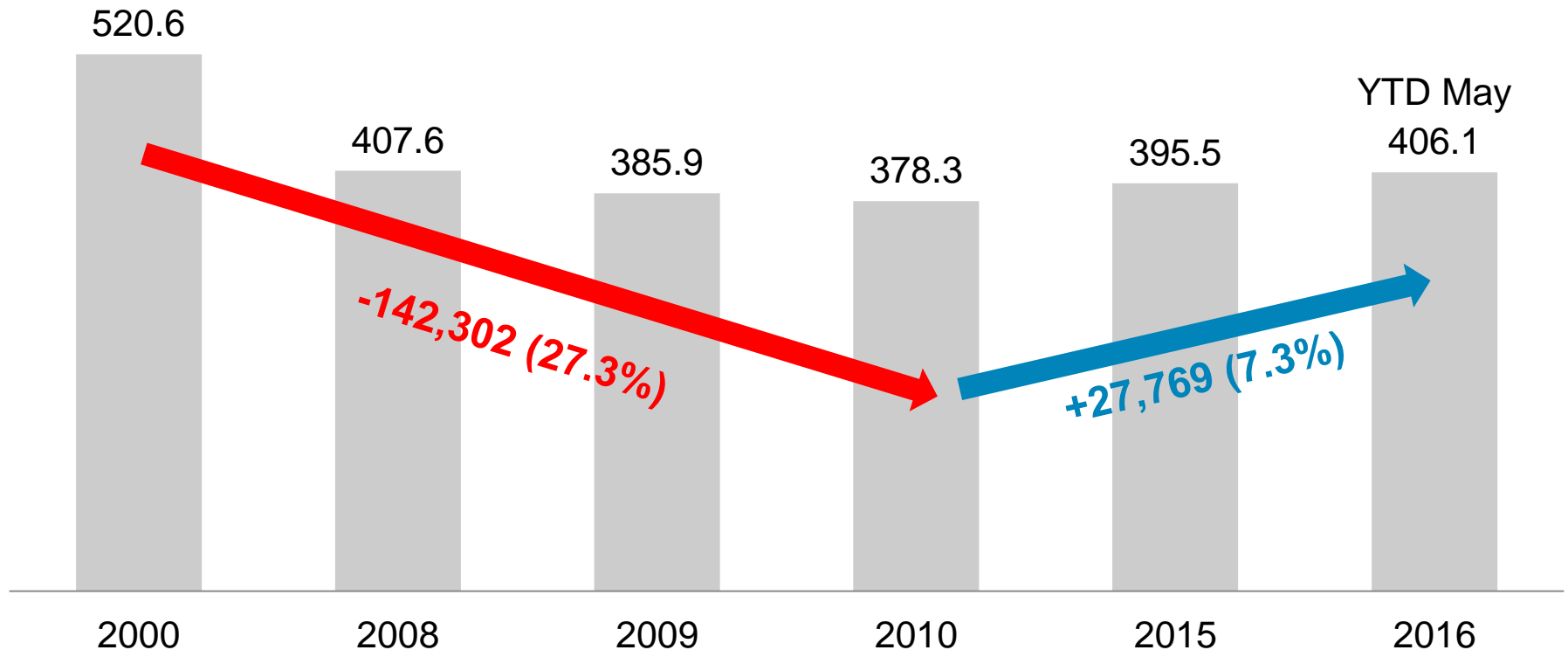


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# U.S. Airline Jobs Are Exceeding 400,000 for First Time Since 2008

May 2016 Was **31<sup>st</sup> Consecutive Month** of YOY Gains

## Employment at U.S. Passenger Airlines (Thousand FTEs)



Source: Bureau of Transportation Statistics for scheduled U.S. passenger airlines

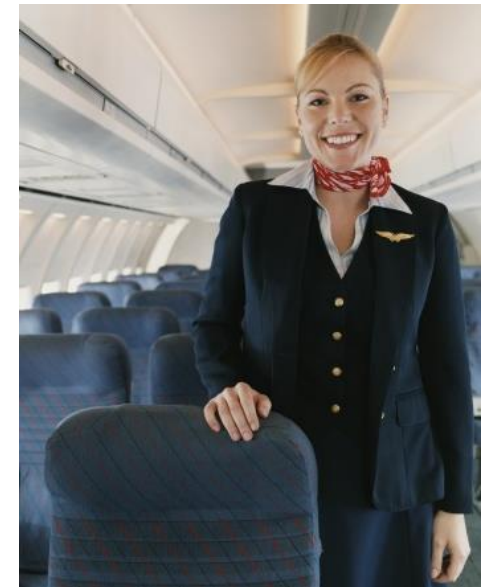
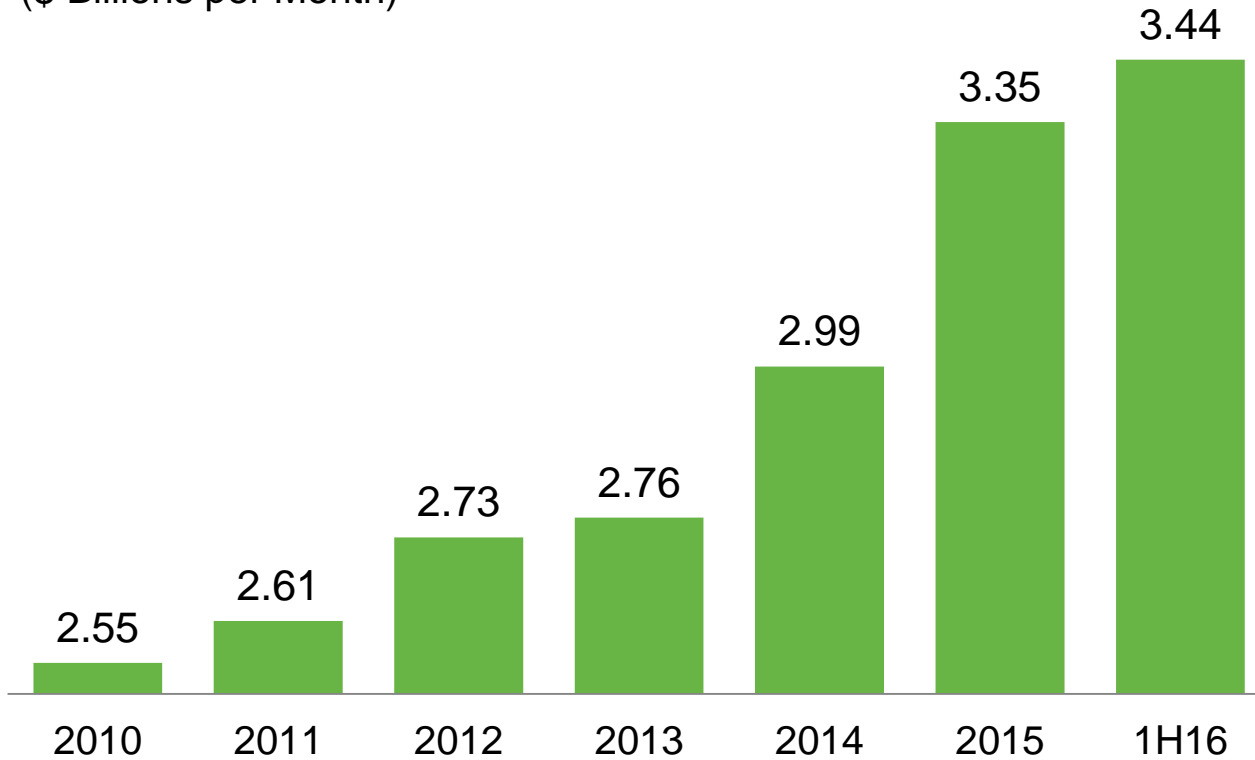


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# U.S. Airlines\* Continue to Pump More Wages and Benefits into the Economy

Airlines\* Spending **\$3.44 Billion per Month** on the Workforce – Up 35 Percent from 2010

**Total Employee Wages and Benefits\***  
(\$ Billions per Month)



\* SEC filings of Alaska, Allegiant, American, Delta, Hawaiian, JetBlue, Southwest, Spirit, United and Virgin America

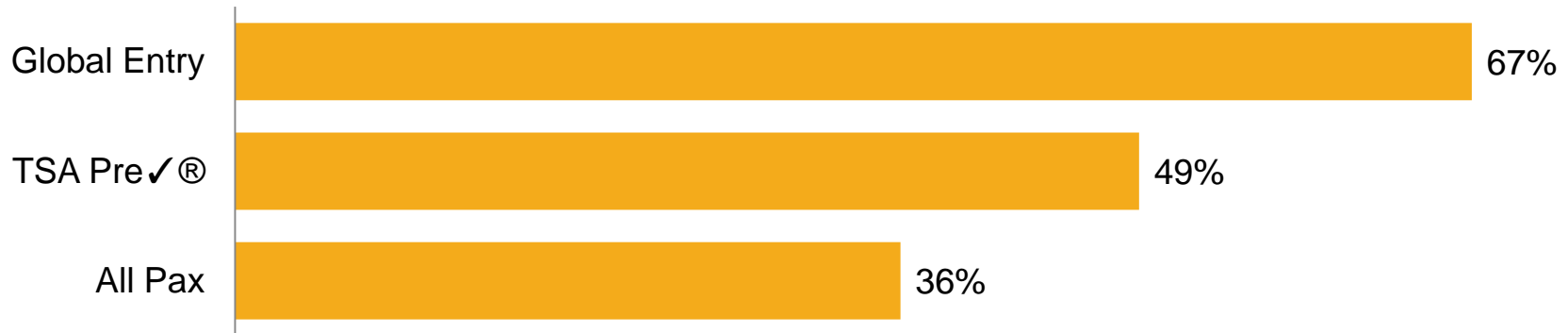


# Flyer Satisfaction Rises Markedly With Enrollment in Expedited Screening Programs

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- » April 2016: UMich-based American Customer Satisfaction Index® (ACSI) for U.S. airlines ties all-time high as “data show passengers are perceiving a better value for their money”
- » April 2016: Ipsos survey (see below) finds overall flyer satisfaction is 80 percent, with fraction who are “very satisfied” rising sharply with enrollment in TSA PreCheck and/or Global Entry
- » May 2016: J.D. Power reports that North American airline satisfaction climbs to 10-year high, as “we see satisfaction rising across all touch points of the passenger experience”

## % of 2015 Flyers Indicating “Very Satisfied” With Overall Air Travel Experience



Sources: <http://www.theacsi.org/news-and-resources/press-releases/press-2016/press-release-travel-2016>, <http://www.jdpower.com/press-releases/2016-north-america-airline-satisfaction-study>, <http://ipsos-na.com/news-polls/pressrelease.aspx?id=7208>

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## First Quarter 2016 Operational and Financial Recap: U.S. Passenger Airlines

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- » 1H 2016 saw continuation of consummate airline safety performance, as well as significant year-over-year improvements in operational reliability
- » Declining fares exceeded traffic gains to drive operating revenues lower, but reduced fuel costs more than offset increases in labor, airport, aircraft and other expenses to drive modestly improved profitability, with airlines realizing a pre-tax margin of 15.5%
  - Airline profitability continued to lag that of Starbucks, McDonald's and Apple
- » Among other uses beneficial to stakeholders, cash flow generated during this period allowed U.S. airlines to retire expensive debt; acquire new, larger aircraft; deploy more seats in the marketplace; boost staffing and wages; and reward investors
- » Sharp airfare declines and U.S. job growth are fueling record passenger volumes, including 4 percent projected growth for the seven-day Labor Day travel period
- » Market research affirms that participation in expedited screening programs markedly improves the air travel experience

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