

How legacy airlines lost so much since 9/11

August 31, 2009

How the Legacy Airlines Lost So Much Altitude Since 9/11:

After losing over \$5 billion last year, the airline industry is now on course to lose a similar amount for 2009. This projected loss comes after the airlines will spend over \$13 billion less for fuel compared to 2008.

Losing money for the old legacy carriers is nothing new. But this year, even low cost Southwest (LUV), after 35 consecutive years of profits, is expected to lose money. Of significance for how serious the revenue problems are for the industry, Southwest's load factor will be the highest in the airline's history.

If you've taken a flight or read a newspaper lately, you're probably aware the airline industry has serious problems from customer service to record financial losses.

Before jumping to conclusions and attributing blame, let's do a review of what has – really- occurred to the industry.

While this article focuses on the largest legacy carriers, over the past two decades over a hundred smaller airlines went out of business or have struggled to stay alive.

The following considers the 6 largest legacy carriers and their mergers/acquisitions before and after the September 11, 2001 tragedy.

These airlines –American (AMR), Delta (DAL), Northwest, United (UAUA), Continental (CAL) and USAir (LCC)- currently carry 58% of the US market share or approximately 65% after accounting for regional carrier affiliates.

Since 9/11, United, Delta, USAir (twice) and Northwest all filed bankruptcy. American and Continental reorganized outside of bankruptcy.

For the 8 years leading up to 2001 (1993-2000) the airlines noted above had cumulative net profits of \$17.1 billion.

The same airlines had a cumulative net loss of \$38.5 billion in the following 8 years (2001-2008). Note: Amounts exclude reorganization and goodwill write downs. See Chart 1.

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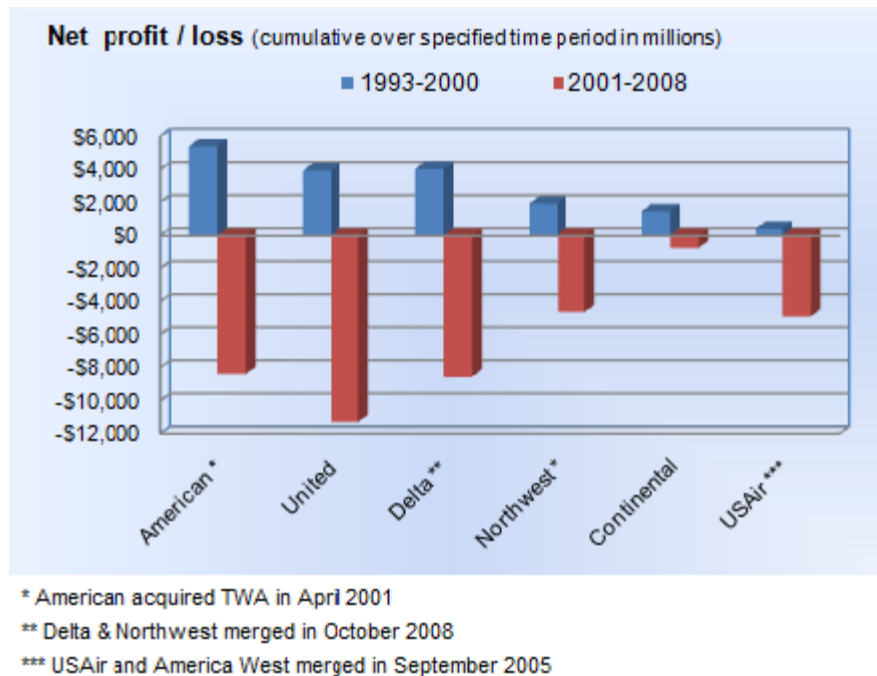


Chart 1

While many billions of debt and employee pension obligations were abrogated through the bankruptcies and reorganizations; Cumulative long term debt and capital leases are still 15% higher than they were just prior to 9/11. Note: Data includes impact from acquisitions and mergers. See Chart 2.

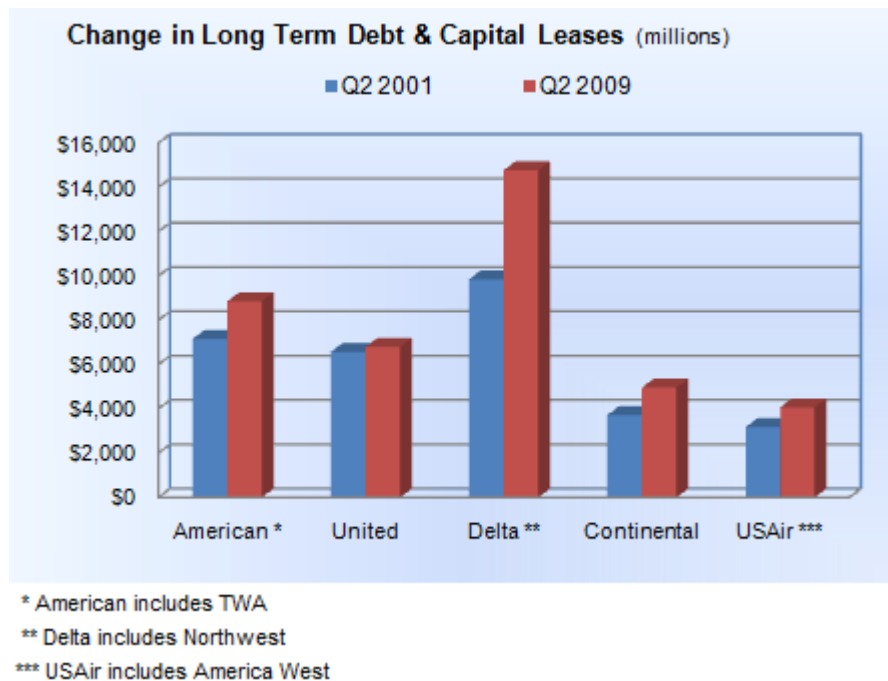


Chart 2

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One of the most recognized losses to the airline industry and investors has been the large drop in market cap (share price x shares outstanding). This loss of shareholder value affects each airlines borrowing power and increases the cost for financing.

Over the past 8 years and not accounting for tremendous losses through the bankruptcy process, cumulative market cap for the airlines noted above dropped by over 52% going from \$21.8 billion in the 2nd quarter of 2001 to \$11.4 billion in the most recent 2nd quarter of which Delta alone claims half of the current market cap. Note: Change in market cap does not reconcile significant stock value losses from bankruptcy. See Chart 3.

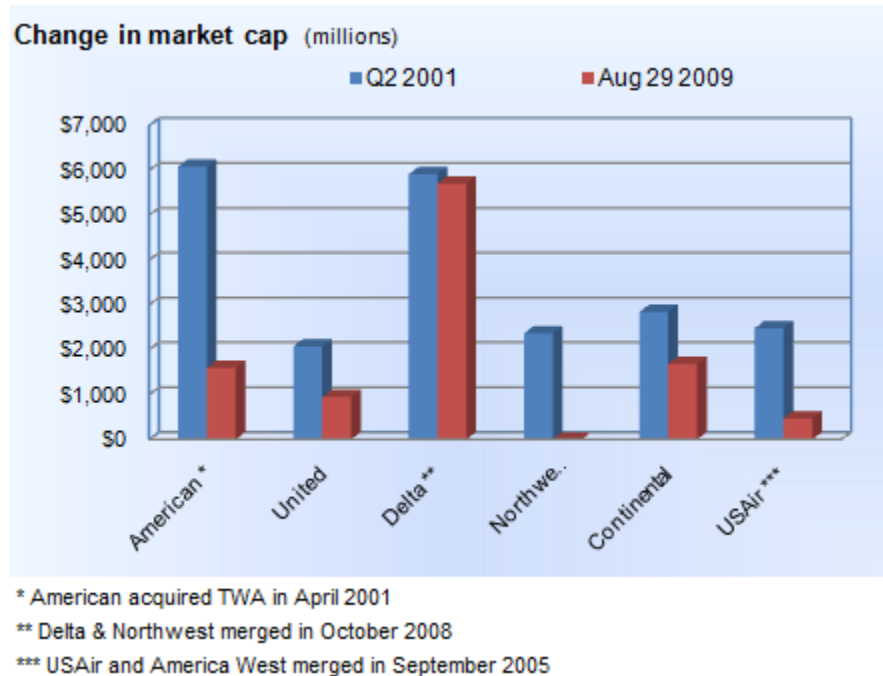


Chart 3

As we approach the 8th anniversary of the 9/11 tragedy, here are some startling statistics showing what has –really– occurred since then to the legacy carriers that were once recognized as the best airlines in the world.

Comparing year 2008 to 2000 for the 6 remaining legacy airlines:

- Total Operating Revenue decreased by \$2.3 billion falling from \$89.2 billion to \$86.9 billion.
- Fuel cost skyrocketed from \$11.3 billion to \$36 billion (+218%).
- The fuel cost for the average one way passenger fare increased by 402% going from \$23 to \$93.
- Capacity as measured by available seat miles (ASM's) decreased by 14.3%.

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- Employee wage/salary expense decreased by 33.5%.
- The average one-way passenger fare increased by 22% going from \$162 to \$198. This increase was below the 25% CPI inflation over the same time period. Note: This is revenue to the airlines and does not include taxes, airport fees, security charges etc. that airlines are required to collect but do not keep.
- While the average air fare increased by \$36, the labor wage cost for the average air fare decreased by 36% to \$41.
- Since 9/11, over 155,000 jobs for just the airlines noted above have been lost falling from 428,000 to 272,000 (-36%) total employees.
- The average passenger ratio to airline employee increased from 1,139 passengers per employee to 1,413. In other words, the reservation or ticket agent, flight attendant etc., on average, now resolve issues and provide customer service to over 24% more customers than 8 years ago.
- As employees worked more for less, the average revenue generated per employee increased by an astounding 53% as it went from \$209,000 per employee to over \$319,000.
- While 155,000 jobs were lost and the average revenue per employee increased by over \$110,000; general management wages/salaries as reported on DOT41 forms, increased by 44% as it climbed from \$243 million to \$350 million.

The airline industry is vital to our economy and national defense. It is not going to go away.

When discussions and questions revolve around why is customer service and morale so bad in the airline industry? It seems like a rather easy question to answer after you understand what has actually occurred in the last few years.

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