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“Mr Chairman and members of the Senate Transportation committee, it’s an honor to be here today, so thank you. As background, I have been helping investors analyze the airline industry for 10 years and my firm does not seek investment banking business from the airlines.

As has been widely reported and recognized, the US airline industry, with the exception of low cost carriers, has been a financial failure. We’ve seen serial bankruptcies in successive decades. And if there is one point I want to leave with you, it’s this: Despite that fact that the industry is structured as a monopolistic oligopoly, it hasn’t behaved as one, and there are a number of reasons for why this behavior won’t change looking ahead.

The second key point I want to leave with you today is “Cost Disequilibrium,” which ties to my first point. As long as there are low cost carriers with a 20-30% cost advantage, they are going to try and undercut legacy carrier pricing and take market share. And I don’t see this changing over my horizon. Or to put it differently, the day we no longer have a competitive industry is the day every airline has the same cost structure. However, low cost carriers, which today enjoy widespread brand acceptance, have been able to sustain sizeable cost advantages and through discounting, drive a shakeout among the legacy carriers, a phenomenon that will continue for the next several years.

The third point I want to leave you with is that the industry is on the financial mend, but it remains vulnerable to another spike in crude or another economic downturn. My outlook assumes average ticket prices rise 12% this year and 5% next year, which positions the industry to finally begin reporting modest profits. My forecast will naturally fluctuate based on the macro backdrop.

So what are factors that have caused the industry to suffer so much? Industry fragmentation is one key reason. If looking at capacity, the top 4 airlines in 2000 controlled 66% of industry capacity. That rose to 70% in 2005 and remains the case today. After the the announced United and Continental merger, the top 4 airlines would control 81%.

But perhaps the easiest way to think about the industry’s poor health is to think of it in terms of the real estate crisis. People that couldn’t afford to buy houses could. In the case of the airline industry, airlines having a “junk” credit rating can nonetheless, very easily, go out and buy new planes, which over the past 32 years, has led to brutal competition.

Separately, the macro backdrop has hit the industry hard. The reality is, fleet and personnel plans made years ago could not have possibly anticipated the demand shock following the calamity of 9/11; a super spike in crude to \$147; the recent financial meltdown; or worldwide health pandemics. Just as the tech bubble, the telecom bubble,

the real estate bubble, and even the commodities bubble have burst, there has been a capacity bubble in the US Airline industry which today, is beginning to deflate as a consequence macro backdrop volatility. The industry has been undergoing a painful transformation over the past 32 years and I'd say that today, we're probably in the 7<sup>th</sup> inning.

Some may wonder if deregulation 32 years ago was a mistake. Of course it wasn't, with too many benefits to cite. Recall that deregulation in the US has led to deregulation globally. Boeing, Airbus, all of their suppliers naturally; the banks; aircraft leasing companies; the gaming & lodging industry; and Travel Management Companies have all been very big winners.

So what does the future look like? The industry is not growing today, but there are orders for planes for delivery in 2012 and 2013, and the additional capacity will impact average ticket prices further out. Meanwhile, low cost carriers will continue to undercut on pricing and take market share. And separately, as long as management teams make promises to labor they can't keep, we'll continue to see Ch. 11 filings. I predict we'll see another Ch. 11 filing sometime in the next 5 years.

But there is one wild card here, and that's very volatile fuel prices which represent the No. 1 threat to the financial health of the industry. The debate on speculative trading in commodities is not whether it exists, but how best to remedy it. Unfortunately, the airline industry is a highly levered, high-fixed cost business that is reeling from 30% of its costs getting whipsawed by 50% in any given year. And the threat of another super spike has curtailed plane orders by many legacy carriers. Said differently, speculative trading is perverting capital spending and investment plans and as a result, is ultimately perverting economic growth.

I'll conclude by saying that there are a lot of factors that have and continue to impact the financial health of the industry. Demand is coming back and finances are improving, but there remain a number of structural challenges in place that will continue to make the recovery a slow process.

Mr Chairman and members of the Commerce Committee, thanks again for the opportunity to be here."