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US Airways Group, Inc. Q2 2010 Earnings Call Transcript

Executives

Dan Craven - Director, IR

Doug Parker - Chairman and CEO

Derek Kerr - Executive Vice President and Chief Financial Officer

Scott Kirby - President

Analysts

Gary Chase - Barclays Capital

Michael Linenberg - Deutsche Bank

Jamie Baker - JPMorgan

Hunter Keay - Stifel Nicolaus

Bill Greene - Morgan Stanley

Kevin Crissey - UBS

Helane Becker - Dahlman Rose

Glenn Engel - Bank of America

Justine Fisher - Goldman Sachs

Dan McKenzie - Hudson Securities

Bill Mastoris - Gleacher & Company

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Doug Cameron - Dow Jones

Ted Reed - TheStreet.com

US Airways Group, Inc. (LCC) Q2 2010 Earnings Call July 22, 2010 1:30 pm ET

Operator

Good day and welcome to the US Airways second quarter 2010 earnings conference call. This call is being recorded at this time for opening remarks and introductions I would like to turn the call over to Mr. Dan Cravens, Director of Investor Relations. Please go ahead, sir.

Dan Cravens

Thank you and hello and thanks for joining us today for our second quarter 2010 earnings conference call. In the room with us today is Doug Parker, our Chairman and CEO; Scott Kirby, President; Robert Isom, our Chief Operating Officer; Derek Kerr, our Chief Financial Officer; Steve Johnson, our EVP of Corporate; and Elise Eberwein, our Head of People and Communications.

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As we usually do, we are going to start with Doug. He will provide an overview of our second quarter financial results. Derek will then walk us through the details on the quarter, including our cost and liquidity. Scott will then follow with commentary on revenue environment and our operational performance during the quarter. And then after we hear from those comments, we will open the call for analyst questions and lastly questions from the media.

But before we begin, we must state today's call does contain forward-looking statements, including statements concerning future revenues and fuel prices. These statements represent our predictions and expectations as to future events, but numerous risk and uncertainties could cause actual results to differ materially from those projected. Information about some of these risk and uncertainties can be found in our earnings press release issued this morning, our Form 10-Q for the quarter ended June 30th, and our 2009 Form-10K.

In addition, we will be discussing certain non-GAAP financial measures this morning such as net loss and CASM, excluding unusual items. A reconciliation of those numbers to the GAAP financial measures is included in the earnings release and that can also be found on our website at www.usairways.com under the Company Information/Investor Relations section. A webcast of this call is also available on our website and will be archived for one month. The information that we are giving you on the call this morning is as of today's date and we undertake no obligation to update the information subsequently.

At this point, we'll turn the call over to Doug and thanks for joining us.

Doug Parker

Thanks Dan. Thank you all for being on. As you all know by now we reported net profit this morning of $279 million. Excluding special charges is brought under $265 million and that compares very nicely to a loss excluding special charges of $95 million in the second quarter of 2009. This is a big deal for us, it's the first profit excluding charges since the third quarter of 2007 US Airways, as the second highest since our merger in 2005.

And importantly we are not just doing better than we've been doing. We are doing better than our peers of a major hub-and-spoke peers that we reported so far. We have the highest pretax margins and the highest EBITDA margins and we expect that will be true to everyone than reporting. And that by the way despite at least some of them including a significant out of period, yes they have refunded normal earnings that we put in special earnings which has about as their corresponding something a little more than that one half point of the margin differentials that you see now as you look at our earnings versus others.

Return on earnings and improvement and our performance is a result of a lot of hard work in the past few years. We have reduced our capacity and focused on flying on airs of competitive strength. We've got both our operating and our capital spending in check. We changed our business model to be a more profitable all across pricing model, and we've run a fantastic operation. I am extremely pleased that we were recognized by the Department of Transportation last month as being number one in each of on-time performance, baggage handling and fewest customer complaints. That's quite a feet and is a enormous turnaround from just couple of years ago and I want to apologize and thank all of our 31,000 hardworking team members who made that happen.

So you combine all that with an improving economic environment and you get these kinds of results on profits and industry leading margin. So, it feels very good, we have been sending our team over the past couple of years they are on the right track. We've been telling them keep doing what you are doing and we will indeed return to profitability, we just keep doing, what we are doing is down this track. Thankfully they had faith in the argument and we've gotten where we are today.

Having said that we are not done, one profitable quarter does not necessarily mean a long-term sustainable business model. We have lot of work ahead of us to make certain we get better the plan that we just got. But there is an enormous step in the right direction and we are extremely pleased. As in the near term outlook we expect to report a profit of over third quarter and the full year 2010.

So, that said I'll turn it over to Derek, who will give you a lot more detail on the earnings number himself as Scott will talk more about the revenue environment. Derek?

Derek Kerr

Thanks Doug, we just filed our second quarter 10-Q this morning and in that Q as Doug said we reported a net profit of $279 million or $1.41 per diluted share, this compares to a net profit of $58 million or $0.42 per share a year ago. When you exclude the special items, the company's net profit for the second quarter was $265 million or $1.34 per diluted share versus a net loss a year ago excluding special items of $95 million or $0.77 per share. Today's result produced in industry leading pretax margin of 8.4% and an EBITDA margin of 18.7% which we believe is the right way to look at operating margin in our business.

During the second quarter the company recognized $10 million of operating net special credits consisting of $17 million

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refund of Aviation Security Infrastructure Fees paid to the TSA during 2005 to 2009.

As Doug noted, from what we have seen we believe that other airlines have taken this credit above the line through operations thereby increasing operating income. As this credit is out of period, we believe it is better recognized as a special item. That said our cost performance is even better relative to few other airlines than reported.

For the quarter, full capacity Mainline and express was $22.1 billion ASMs, up approximately 0.4% from 2009. ASMs came in slightly higher year-over-year due to our higher completion factor, 99.4% Mainline and total 98.9% as we continue to run a great operation. Our Mainline capacity for the quarter was $18.4 billion ASMs, up 0.7% from the year ago and express capacity was $3.6 billion ASMs, down 1.3% from 2009.

We did continue to reduce our fleet in the second quarter. We reduced the Embraer 190 fleet by two aircrafts. We are now at that 10 and we are to stay at 10 on the Embraer 190, ended the quarter at 345 Mainline aircraft. For the remainder of the year for 2010, we still plan to retire six aircraft and we are maintaining our previous ASM guidance.

Mainline ASMs are projected to be $71.5 billion this year, which is up approximately 1% versus 2009. Domestic Mainline is still expected to be down 1% to 2%, while international is up due to the increase in Latin America flying with the resumption of Mexico service that was reduced due to H1N1 in 2009 and the introduction of our new service to Rio de Janeiro.

ASMs for the third and fourth quarter are $19.0 billion in the third quarter and $17.5 billion in the fourth quarter. Total operating revenues for the quarter were $3.2 billion, up 19.3% from the same period in 2009 and a 0.4% increase in total ASMs. Total revenue per available seat mile was $0.1437, up 18.9% versus last year. During the quarter, other operating revenues were up $59 million or 22% due to the increase in a la carte revenues. We are on track to achieve more than 500 million in annual a la carte revenue for 2010.

Cargo revenues were up 82% year-over-year or $17 million driven by an increase in international freight volume as a result of the recovering economic environment. Total passenger revenue increased 18% to $0.127 in 2010 versus second quarter of 2009 with Mainline up 17.3% and Express up 20.9%. For the same period, combined yields increased 18.6% and our combined load factor was 82.9%, a slight decrease versus 2009.

These improvements in passenger RASM and yield were driven by an improving economy resulting in greater demand for business travel, and Scott will go into more detail after I am done. The airlines operating expenses for second quarter were $2.8 billion, up 10.4% compared to a year ago due mainly to 38.7% increase in Mainline and fuel and Express fuel expenses. Mainline cost for ASM excluding special items was $0.1152, up only 2.1% year-over-year despite the increased cost of fuel.

Our team members have done an outstanding job of producing industry leading operational results. As Doug said, it maybe ranked first among the five largest in three important operational DOT measures after being first in on-time performance in April. For this performance, we include $9 million in operational incentive pay during the quarter for our team members. These payments to employees for operational excellence are an addition to employee profit sharing for which $18 million was accrued during the quarter based on our year-to-date profit. There is a welcome change in our business condition where we can reward our employees for our financial success.

On the cost side, the outstanding operational performance achieved by our team members continues to contribute to our cost discipline, excluding fuel, special items in profit sharing, our Mainline cost per ASM decreased year-over-year by 0.7% to a little over $0.08. Express operating cost per ASM, ex special items in fuel was $0.1305 for the quarter, up 3.3% versus 2009 on a 1.3% decrease in ASMs.

Our Mainline fuel price including taxes for the second quarter of 2010 was $2.23 per gallon versus $2.07 per gallon in the second quarter of 2009, an increase of 7.8%. Last year's second quarter did include $0.49 in realized hedge losses. We continue to monitor opportunities to hedge our exposure to fuel cost. However, given the continued volatility of fuel prices, we haven't entered into any new hedges this year at all. For the full year, we are forecasting Mainline fuel price in the range of $2.19 to $2.24 that is based on the July 14 forward curve and slightly higher than our previous guidance. Our forecast breaks down by quarter as is follows, $2.16 to $2.21 in the third quarter and $2.24 to $2.29 in the fourth quarter.

We have maintained our full year cost guidance with a slight shift between quarters due mainly to the maintenance cost timing. For the full year our CASM ex fuel on profit sharing guidance has Mainline flat versus 2009. This breaks down by quarters. The third should be a approximately flat, the fourth quarter would be flat to down 2%, Express CASM forecast to be up 3% to 5% in 2010. We ended the quarter with $2.5 billion of total cash and investments of which $2.05 billion was unrestricted, an increase of $451 million since the end of the first quarter. This is the company's highest quarter ending total and there is a cash balance since the second quarter 2008. Total cash at June 30th, did include $59 million of auction rate securities at fair market value currently reflected out on nine current assets on our balance sheet.

Restricted cash for the quarter decreased by $36 million mainly due to return of credit card holdback because of the company's improved outlook. We also believe that as of June 30th, we have met the quarterly financial requirements under our

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Visa Mastercard processing agreement which we estimate will further reduce our current holdback by approximately $50 million and that will happen in the month of August. During the quarter, the company generated $540 million of positive cash flow from operations and $520 million of positive free cash flow to find its operating cash flow less capital expenditures.

We also had debt payments of $105 million which included a prepayment of debt received as part of our liquidity initiative that was originally scheduled for the fourth quarter. Looking at the CapEx, we have reviewed our capital plan and reduced spending by $20 million under that plan in 2010 primarily due to the FAA decision which is putting a propose slot swap transaction on hold. Our second quarter non-aircraft CapEx was $19 million, we forecast total net CapEx to be $212 million in 2010. This includes non-aircraft CapEx of $130 million and net aircraft CapEx of $82 million.

So in summary we are extremely pleased to report our first quarterly profit excluding special items since the third quarter 2007. All the hard work our team members have completed over the last three years has led to these improved results. I would like to thank all of our 31,000 team members for all they have done to position us for a profitable third quarter and full year 2010.

With that I will turn it over to Scott.

Scott Kirby

Thanks Derek. So I will take a minute to talk briefly about our operational results and then turn to the revenue environment. As Doug and Derek both said, we are extremely proud of our team and continue to run a spread of operations in the second quarter, capped off by winning the Triple Crown amongst network carriers, it was the number one on-time performance, number one in lowest complaints and number one in lowest mishandled bags in the month of May.

Turning to the revenue environment, during the second quarter our total RASM increased 19% among the best year-over-year performance of any of the network carriers particularly to adjust prior mix of domestic and in fact we have no Pacific fly as compared to the rest of the industry. Of course last year at least hopefully, so comparing only to the comps for 2009 can be a little misleading. Compared to 2008, our 2Q RASM was still down 2% though of course 2Q and 3Q of 2008 represent the all time high for airline revenues as the economy was strong and the airline responded to high fuel prices with aggressive price increases.

I will give you a few more statistics in a minute, but we will preview them with a consistency. All of our revenue metrics went up dramatically year-over-year but still down slightly from their peak in 2008, and we aren't seeing either acceleration or deceleration from here. For some regional color, transatlantic RASM was up 37% and domestic was up 17% though versus 2008 both transatlantic and domestic were down 3%.

We expect the transatlantic market to continue to dramatically outperform domestic on a year-over-year basis going forward. As we've seen throughout 2010, the quarter's improvement was driven largely by improving business demand. During the quarter, our book corporate revenue is up 42%, though still down 2% compared to 2008. In June, for the first time this year corporate revenues were actually up slightly versus 2008, consistent with improving corporate revenue, our business oriented markets significantly outperformed leisure markets. For a couple of examples; Delta RASM was up 24% and our La Guardia RASM was up 36%, and these markets are almost exclusively business demand.

On other hand leisure was relatively less strong on a year-over-year basis with quarter RASM up only 6%, Caribbean up 1%, and Hawaii market up 2%. While business markets are much stronger on a year-over-year basis, it's once again due to the dramatic drop off that we saw in 2009.

If you compare these same markets on a two year basis, the year over two year performance is almost identical. For having overwhelmed with your year-on-year or two year statistic shift, I'll turn the revenue outlook going forward. As most of you know the comp starts get much more difficult on year-over-year basis. We spend lot of time and energy trying to understand revenue trends compared to 2009, 2008, and even back to 2007, and our simple conclusion is while there is some month-to-month volatility in ours and other airlines monthly RASM, by-and-large what we have experienced is a revenue recovery that's been good but is essentially flat line since March and April.

There is recovery in a couple of percent below the peak pricing and revenue environment of 2008 and 2% better than what we thought was a really good revenue environment in 2007. From the macro economic perspective, this built us like a tepid recovery and one, it isn't getting rapidly better but certainly is in double dipping or getting any worse. While that's not what we would like to see for the country at large, a test of recovery is also leading to moderate fuel prices.

As a result year sale in the industry are producing near record profit despite the fact that we have a weak recovery underway. For some specific forecast, our CASM with the comps really being a tough on a year-over-year basis going forward. The following forecast assumed that the revenue environment remains status quo, that is, no improvement and no worsening. We currently expect July passenger RASM to be up about 16% year-over-year. The comps gets harder in August and September and we still have a lot of revenue left to book. So our best estimate is that RASM will be up slightly less than in July based simply on the fact the comps get more difficult. For the full quarter, we currently expect passenger RASM to be up about 15%.

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So to conclude, the employees of US Airways continue to run a truly fantastic operation, and we continue to be encouraged with the revenue environment. Despite what feels like a tepid recovery, it means we still haven't yet reached the peak in revenue environment of 2008. US Airways is still producing near record financial results. So, we are well positioned even in this environment with upside if the economy strengthens. With that I'll turn it back to Doug.

Doug Parker

Thanks Derek, thank you Scott. And we are ready to take questions.

Question-and-Answer Session

Operator

Thank you. (Operator Instructions) Now we will take our first question from Gary Chase with Barclays Capital.

Gary Chase - Barclays Capital

I wanted to ask you two questions, Scott, first that, I just want to clarify that's a full quarter passenger RASM you are expecting at plus 15?

Scott Kirby

Correct.

Gary Chase - Barclays Capital

Okay. That wouldn't imply very much deceleration in September. I'm just kind of curious for your thought process on that. I know for sure that the year over two comps get quite a bit harder in September because of all the capacity reductions that developed in a way, and at least my perception was we had a lot of acceleration as you moved through both the August and September last year. So, I just wondered if you can flush out a little bit more about how that September is going to look.

Scott Kirby

Okay, well, we don't have a lot of revenue booked yet, but what we do looks very good for the month of September. Do expect that the council get kind of sequentially a little worse, and so July will be the best month, August will be the second and September will be the weakest of the three. But September is also benefiting from the fact that it's more business oriented. So, while the comps start to get more difficult in September, it also is going to have a more business orientation. So that's going to help. It's a forecast at this point and we feel reasonably good about it. But some uncertainty about what will happen with September, but the new event, we think the fourth quarter will be up about 15%. And I view that really as not really acceleration or deceleration to be at about 15%. Again, there is a lot of volatility in the kind of month to month numbers and with differences between what's happening with corporate versus leisure, then comparing all the way back to '08 and '07, which '08 also had a lot of strange things going on with fuel prices going up. So we really think that 15% forecast is mostly a continuation of the trends that we are currently seeing today and at least bookings that we have and current book yields that we have are supportive of that forecast as well.

Gary Chase - Barclays Capital

There can't be too much variance if you got plus 16 in July and 15 for the quarter, so it must not be much in the way --

Scott Kirby

We aren't expecting a lot of variance.

Gary Chase - Barclays Capital

And then, the other thing I wanted to ask is just on the non-ticket revenue and I obviously understand that there has been a lot of build in that, but if you think sequentially and you look at it relative to passenger revenue, I would say that's a cross in a number of carriers. It doesn't look like it's has been spooling the way you might have expected with the bags, these changing the way they have. Any thoughts on what's going on there, is that just as we move more towards business mix or kind of moving away from the customer that tends to pay those fees or are we kind of budding up against on the elasticity there.

Scott Kirby

I think, and then I have to go through the analysis of how you come to the original permit, because our numbers have been virtually spot on what we forecast from the beginning and it's ramped up as we expected and that really does mean shift in mix or shift in behavior. Our numbers have been right on until, from our data and I have to go do it with the expose to see how you

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reach that conclusion. [Our day], I would not have reached the same conclusion that you use as a permit to the question, because it has seemed consistent with what we expected.

Gary Chase - Barclays Capital

I'm just looking at other revenue that hasn't really built much more than normal between the first and second quarter now possibly…

Scott Kirby

Nothing has really changed between the first and second quarter.

Doug Parker

These weren't changed between first and second quarter.

Gary Chase - Barclays Capital

Okay. So, do you think we'll see an uptick with that as we move forward or?

Scott Kirby

Well, I think some new ancillary change. I think we are running basically run rate revenues. It very based on load factor and is very based on seasonality of mix of leisure verses business traffic as you pointed out, but we are basically a run rate until we do something new.

Operator

We'll take our next question from Michael Linenberg with Deutsche Bank.

Michael Linenberg - Deutsche Bank

Couple of questions. I guess the first thing Derek on the holdback, the $15 million, which is you said you will see that in August. Where are you then on the holdback? What is left and how quickly can that reverse? I mean so you have met obviously some sort of financial metric, can that very quickly work in reverse or is it over a longer time frame? How should we think about that and maybe some potential upside in additional holdbacks being released?

Derek Kerr

Okay, the calculation is a fixed charge coverage ratio and unrestricted cash to revenues. Those are the two calculated numbers. We were at a 25% holdback, it will take us down to 15% holdback, I would add $50 million as a 10% reduction. So we probably have about another 150 holdback so the possibility of going down to Tier 1 would depend on that fixed charge coverage in unrestricted cash calculation. So if the environment continues to go over fix charge obviously we will continue to go up and cash will go up and we will be fine and try to take it down to Tier 1 over the next 12 months.

Michael Linenberg - Deutsche Bank

Okay.

[Multiple Speakers]

Michael Linenberg - Deutsche Bank

Tier 1 we'll get a zero percent holdback?

Derek Kerr

What's that excuse me?

Michael Linenberg - Deutsche Bank

Tier 1 would be in zero percent holdback?

Derek Kerr

Correct.

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Michael Linenberg - Deutsche Bank

Okay, great. And then my second question, now that you are going down the path with this appeal process on the slots and the gates. Can you give us a sense of the potential timing, how long it will take to play out or is that something that just you can't determine? Is there anything that prevents you from still at least potentially leasing more slots from others at DC and potentially leasing the slots that you currently own at LaGuardia to others and so sort of moving ultimately in the direction that you wanted to get to in one big transaction maybe at least moving toward that direction through a bunch of different transactions, baby steps here, what prevents you from doing that?

Derek Kerr

First question we think it will be taking about 12 months and we are hopefully that will be successful in that appeal and I can get the deal done. There are some restrictions in doing it in terms of leases, some in our debt agreement that limit the number of flights we can lease. So by-and-large we could do a lot of it as you mentioned by leasing, it's a matter of well and deciding if we want to, Delta I think is taking the position now and reasonably that this is a long-term investment we are trying to make in New York and if they got do it in a series of short-term leases with no certainty about what's going to happen in long-term, that's not in investment if they want to make.

So I doubt you will see us in Delta, it starts to do a lot of it through leasing transaction just because it requires both of us to make big investment and if you don't have some certainty that you are going to have time for those investments to pay back we probably won't be doing it.

Michael Linenberg - Deutsche Bank

Okay, as I recall I think there was a financial impact of running LaGuardia operation and so I guess that you still incur that, maybe it's less though either with the backdrop of a better economy I guess.

Derek Kerr

We still to be clear would like to get the deal done. It's the right long-term strategic position, we can create more benefits for us with DC slots and more for consumers because they have a bigger network there and the reverse is also true. Delta can do more with our slots in New York because they have a bigger presence in New York. But in the near term that benefit is financially less just because LaGuardia has recovered so much. LaGuardia rises up 36%, so the near term of financial benefits are less than it would be, it's still the right long-term strategic move in the right allocation of assets so overtime hopefully we can find a way still if we get something like that done but probably northing in the near term.

Michael Linenberg - Deutsche Bank

Okay, very good and great job this quarter.

Operator

And we'll take our next question from Jamie Baker with JPMorgan.

Jamie Baker - JPMorgan

Some follow-up actually to Mike's question, Scott on the slots swap, so there is no exclusivity agreement that you have with Delta presently, is that correct?

Scott Kirby

We have a commitment on the deal that runs through I think August of next year, so effectively we are exclusive through August of next year.

Jamie Baker - JPMorgan

Okay, all right and I know you don't like [airlines], typically you don't like to break out profitability by hub but if you exclude the shuttle, is there anyway that you can help quantify what sort of an earnings drag, LaGuardia actually represent? For example if your pilots did accept that $120 million offer that I believe is still technically on the table, correct me if I'm wrong. Could finding a LaGuardia solution potentially offset maybe half of that amount?

Scott Kirby

LaGuardia is actually, modestly profitable in this revenue environment. It is the least profitable of any of our operation, so it's the lowest margin and it's modestly profitable in this revenue environment.

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Jamie Baker - JPMorgan

That's exclusive of the shuttle?

Scott Kirby

Correct, excluding the shuttle and excluding the hub flying, it's all regional capacity in the right quarter and we are going to find non-hub, non-shuttle, is slightly above breakeven. And its still again as I said to Mike, the right strategic answer and DCA is our highest margin market. So, we would be swapping our lowest margin for highest margin. So, there is still upside and plus the international benefits. So, we absolutely still would like to get that deal done. But as I also said to Mike, the near-term financial benefits are less than they otherwise would have been because it already has recovered so much.

Jamie Baker - JPMorgan

Sure, all right. Well that's helpful. And a second question I guess to Doug, as you are no doubt aware, investors continue to fret the sort of profit production we are now witnessing, the free cash flow generation that we are seeing. It's ultimately going to coke somebody off the wagon and they will go on to some sort of growth bench for lack of better term. I happen to have my own views on that topic, but I am curious if that is also a pressing concern for you and the management team there, and feel free to name names in the industry if there is any particular airline that you think might possibly go rogue from a growth perspective?

Doug Parker

Thanks, Jamie. I am not going to do that. I will assure you it won't be us. Anyway, the short answer is, yeah, we surely are concerned. Anybody who has been following this business for the last number of years as you and I have can't help to have that concern. For reasons that define logic, every now and then when people start to make money in this business they seem to think that it makes sense to go add more airplanes as if that will allow them to make even more money, the result is it because this all will loose money. And airlines also tend to do things they like to cost strategic fines, which is just fly loss making fine in times like this, and so that's starting to go on right now. It is a concern.

I am hopeful that rationality will prevail. We are encouraged by the fact that at least this time you hear not as many people or see as many people acting like that, encouraged by the fact that the five largest airlines are now run by, I guess probably four airlines we run now by what two ex-CFOs and two ex-lawyers, people who used to care more about returns than they care about flying men all around and being the world's biggest airline. So that's encouraging, but that doesn't mean it's not going to happen again. So, I don't know, it's not going to be us.

Operator

And we will take our next question from Hunter Keay with Stifel Nicolaus.

Hunter Keay - Stifel Nicolaus

I'm not sure if you guys heard the United call yesterday, but they have some interesting commentary on the international bag fees, and I realize that some fees are harder to lead on than others, others are probably better to follow, most of them really for that matter. But is that one that maybe you consider leading or do you prefer to wait and see what others do before you jumped on board?

Doug Parker

Yes, we can't talk about that, I would just note though, we did see the comment and the comment that was made is that only 40% of the bags are being charged for. That does not mean that is just the international bags, lead flyers are the biggest bags that are flying for free.

Hunter Keay - Stifel Nicolaus

Right, yes, absolutely. Okay, great.

Doug Parker

I was wanting to point out, you see now that the comment, it's not about charging, it's not so much about charging for international. Most of the bags are flying for free air flown by frequent flyers.

Hunter Keay - Stifel Nicolaus

And also another one on this slot swap transaction. I wondered if you have a sense of sort of who is pushing back on that at

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DOT. Is it your sense that these are sort of courier guys that typically evaluate this or is it coming from maybe the political appointee level? Do you have any sense there at all?

Doug Parker

We do not.

Operator

(Operator Instructions) We'll now take a question from Bill Greene with Morgan Stanley.

Bill Greene - Morgan Stanley

I just wanted to ask, Doug, when you look at your labor situation after the merger and you compare it to say the merger situation that Delta between, in fact they have gotten collective bargaining agreements in the single contract you have not, and I'm just curious what you think about the pros and cons of those differences. Is there actually a net negative for not having it? Is it the net positive because you haven't had to offer the $120 million or how do you think about how these have played out?

Doug Parker

Well, first off, the reality is that we have the more of our employees on joint contracts as Delta does. What you say is true about the pilots and flight attendants for us, Delta it has every other work group working on one set of our contracts and one not. So, we have done a nice job. We've had an issue with our pilots that has resulted in; there has really been a seniority integration dispute that's been going on for a very longtime, it continues to this day. But that's the only thing that has kept us from getting a joint contract, and that if you couldn't have been resolved partner or merger, I assure you that if it was not resolved five years later, it wouldn't have been resolved by partner or merger.

So, we had a different situation. We have the situation with two sets of products that are very different in their seniority profile and they are having trouble between the two of them coming to a resolution of how to integrate. So now it's gotten tied up in court. But that's an issue. Now having said that, so I don't view the way either of us went about it as peculiarly in different way. They were able to get something out of their products before hand, because they are in the same situation we did. What it's meant for our airline is it makes it more difficult for management and because we spend a lot of our time, working with an airline does not fully integrated but is working with employees that are fully integrated and trying very hard to make that work, we do it. So, for our customers you see the operating results we've done because our pilots while they have disputes between the two groups are exceptionally professional and go find the airplanes doing exceptionally well.

The dispute will resolved at some point, we get to a joint contract at some point it is not there yet. So, we like to have it done. We don't need this as a big cost saving measure as Mike suggest and something that we are actually happy about. We'd like to have it done, we want to have it done four years it's not done yet. We will get it done one day. But it's a bigger situation then others have to deal with.

Bill Greene - Morgan Stanley

Okay. On that sort of different topic costs, little bit of better than expected cost performance in the quarter, you've had some good revenue performance in the overall results are obviously positive. So, when we look forward how sustainable are these trends have you sort of taken out all the structural cost that you can and so from here on now we are going to start to see cost pressures creep up if the revenue environment sort of flat lines as you suggested after few months?

Doug Parker

Yeah. Bill, I think though I think from a cost perspective we still have some productivity, things that we are working on within the operations we've done a great job over the last year and a half, two years keeping the cost down I think there is still some opportunities from the productivity standpoint as revenue grows up those costs have increased in certain areas just due to revenue driven, so we've been able to offset that as we go forward. So I don't see anything as we look forward into unless 2011 any big issues from a cost perspective that are going to drive our cost up next year and I do see a lot of opportunities from an operation standpoint to be even more efficient as we put new systems out in place at the airports and with the people that we have out there.

And we have a lot of those risk items that we haven't quite and got to yet just as we did the merger and got ourselves out of bankruptcy back in five years ago. So we are still working on systems like that. And we still have the ability to produce some productivity benefits with our people.

Robert Isom

This is Robert Isom, the Chief Operating Officer. I will just add a couple of points. One of the good things about our

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operational turnaround is that we've had a quite a lot of catch up in terms of technology investment and efficiencies that we gained out at the airport in daily operations.

And the good news is as Derek mentioned, we haven't exhaust that list. We have more catching up to do and it will bring operational benefit to the company, probably not huge dollars but certainly the kind of dollars that will keep our cost in check.

Operator

We will take our next question from Kevin Crissey with UBS

Kevin Crissey - UBS

Thanks so much for the comprehensive particularly the revenue outlook, it's most useful and certainly something I spend a lot of my time on. I am trying to kind of reconcile Delta's implied quarterly RASM guidance against your 15%, now I think there is probably some conservatism in there but I am trying to assess like is there something unique about the Southeast or something you would make them have more difficulty because I would think of anything given the international strength and exposure to Asia that they would be meaningfully higher. Their comparisons don't look that dramatically different than yours. So I'm trying to understand whether there is weakness in the Southeast and maybe you could tell me how to [Charlotte]. I can't reconcile the two numbers, 13% for them or 15% for you.

Scott Kirby

Well, it's partly a comment on their numbers, we certainly don't see weakness in the Southeast, we see the opposite actually. So, I don't think that yet, maybe they are conservative, maybe we are too aggressive. There is a slightly different capacity situation, Delta has more capacity on a year-over-year basis in the back half of the year then we do. So that's going to affect their RASM numbers, but other than that I don't really have any good theories.

Kevin Crissey - UBS

Do you have any exposure to ITA at all?

Scott Kirby

We do, we use ITA to a large degree.

Kevin Crissey - UBS

Can you give us your thoughts on the Google?

Scott Kirby

We are still talking to ITA, we don't have any explicit internship and although and although we would like assurances from ITA, we've had a fantastic relationship, we were the first airline and it certainly worked with ITA in a big way. Years ago we had a fantastic relationship with them and have done a lot. It really has been a true partnership and we want to make sure that as they become Google, it stays that way and so we just want reassurance in that regard or [by the ratios] in that regard before the transaction closes.

Kevin Crissey - UBS

With regard to what having access to the software at similar prices, can you tell me what kind of assurance?

Scott Kirby

I don't know for sure what that will mean, but it will mean contractually keeping the relationship as it is today, not changing the business model and keeping the relationship as it is today, and a partnership that's expanded and that is not all just what's written within the four corners of the contract, but the partnership always been things that are mutually beneficial for both us, and we just want to maintain the working relationship that we have with ITA today, and so we would be working with them for some reassurance that that's going to stay the same.

Operator

Our next question comes from Helane Becker with Dahlman Rose.

Helane Becker - Dahlman Rose

So I just have two questions; one, I think at one point Doug you had talked about your fuel philosophy and really not hedging

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and I thought I heard some of kind of the little shift in philosophy there and may be wanting to put on some hedges. So I wondered if you could just talk about that. And my other question is unrelated, a year or so ago you did an equity raise when the stock was under $5 and now that the stock is more than double that, is that something you would consider coming back to the market to deleverage the balance sheet a little bit? Thanks.

Doug Parker

First on the hedges, I don't think we certainly need to imply or said that we are changing philosophies regarded to hedges. So, anyway, the philosophy is, of course we haven't entered into a hedge since August of 2008, and because we saw what happened back in 2008. So, we are not going into it all again. Our theory, our view on this apparently is different than others. But it's at least strongly felt by us and remains strongly felt, it could change. But there right now hedging is not in the interest of our shareholders. We see written from time to time, two things, neither which I really want, we've done a really smart thing by not hedging, but again indeed that our earnings are better because we didn't hedge, we shouldn't take credit for that. I mean we didn't know the fuel price; we certainly did not hedge because we thought fuel prices are going to fall. That is speculation that we don't enter into either.

So that's point one, point two, though is another view that's written that those who have hedged because they have even though they are paying more for their fuel now have more certainty in their earning and have protected themselves from disaster let's say. That I think is option two, our view is the largest potential disaster, not saying it's happened, but I think we need to be most concerned about. Is indeed a double debt, that results in revenues going down and results in oil prices going down just like we saw at the end of 2008, the first step. And in that scenario pretty good airlines that have entered into costless collars, what you will see is they will have to pay higher prices for their oil, they have to pay in advance and their revenues will go down. That's the most likely disaster in our view, much more likely than what people seemed to assume will happen which is everything else stays equal and oil prices somehow go up, that clearly can happen somehow. But I would clearly as to whether in that scenario, there are other things going on that result in the airline ministry being in a different situation anyway. So anyway, that's what we think. We believe right now there is a natural hedge in place, and it has certainly has been the case, at least for the last year and half and that natural hedge is the economy, and if the economy gets stronger, oil prices may go up but that's okay because we are hedging our revenues. If it gets a lot weaker, those who've locked in fuel prices are going to have a scenario that's going to be difficult to manage, and we don't want to be in that position again.

Like I said on equity, you're right we did write equity back when it was $4 or $5, we also did it because we didn't have much cash, and we did it not to delever, but to survive, that is not the situation anymore. As we noted, we have more cash today than we've in two years, our earnings are higher than they have been in three years. We feel very good about the prospects; we don't see any need to out raising additional cash at this point.

Operator

Our next question comes from Glenn Engel with Bank of America

Glenn Engel - Bank of America

First question is can you do me a favor on the second quarter on breakout RASM by region Atlantic, Latin and domestic?

Scott Kirby

We gave Atlantic was up 37 and domestic was up 17, I don't off the top of my head remember what Latin is, Latin is small for us.

Glenn Engel - Bank of America

And two, can you talk about the Star Alliance in terms of one with Continental joining it, are you seeing any incremental contributions?

Scott Kirby

We aren't really seeing much incremental yet with Continental joining Star, but we haven't done much integration with Continental. We do have some benefits. We are sharing clubs and other things. But the bigger benefits co-chair and potential participation in JV are things that we hope are on the horizon but aren't in place yet.

Glenn Engel - Bank of America

And finally, can you talk about, is it easy to as you continue to repurchase, kind of regenerate free cash flow is it easy to buyback that? What that makes sense to buyback first?

Derek Kerr

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All right at this point in time Glen we don't plan on buying it back; we are going to build cash over time. We will be opportunistic in it, this morning we did pay down some debt that we raised in the liquidity initiatives we paid that early. So we are looking opportunistically doing some of that but as of right now its going to be building cash through earnings.

Glenn Engel - Bank of America

And why is that since holding cash flow expenses? Is there a desired cash level you might get to?

Scott Kirby

There is a desire to have a higher level of cash than we have today given the volatility of this industry given what we saw in both 2008 and 2009. I would add to Derek's point one future debt that we are all going to have to deal with the near term is convertible which is [puttable] to us in September. So, those are best known and outstanding and is effectively actually today. So, we will deal with that one way or another.

Glenn Engel - Bank of America

As a percent of revenue do you have a cash target?

Doug Parker

Not expressly going, there is no specific target. Our desire is to have enough that we can feel extremely good about you might have in the future and that means both an absolute number that means a relative number to others and we've made a lot of progress against the others but still versus most of our competitors were at the lower end. So, we are going to keep building cash.

Operator

Our next question comes from Justine Fisher with Goldman Sachs.

Justine Fisher - Goldman Sachs

All of my questions have been asked and answered, thank you.

Operator

(Operator Instructions) And we've got the next question from Dan McKenzie with Hudson Securities.

Dan McKenzie - Hudson Securities

I appreciate the business leisure demand commentary but I'm hoping you can help us slice that a little bit more in particular the mix today versus where that was in 2007 and 2008. And that is as we look ahead at this next cycle so looking past this upcoming quarter of course, how should investors think about the incremental headwind for revenue recovery looking ahead and then related to that how material the average ticket prices is a shift by US Airways to more international flying?

Doug Parker

As first compared to 2007 and 2008 business in leisure trend are almost identical and very little difference between that. So what happened was their dramatic difference versus last year only because business fell off much more than leisure did in 2009. And to your point about is there headroom I think the answer is yes. Just to us it seems like what has been a fairly week recovery to-date. We have revenue that's still a couple of percent below the peak in 2008 in terms of RASM and if you are more below the 2008 peak in terms of total revenue production, I mean total revenue production is below you are aware every industry that is we are in 2007. All that is consisted with other data and indicative to me of a week recovery that has a recovery to strength or even becomes the model recovery has upside for airline revenues but by March we are now back to slightly below into our revenue where we were in 2007 and 2008 and the mix of business and leisure is now very similar to those years. 2009 really were the anomaly was. After your average ticket values, there is a number and I really tracked and expressively but these are a little much more at yield than the average ticket value but clearly with the greater mix in international flying and in longer states so I think that's the result. I'm sure the average ticket value is going up and the yield is a good pattern of metric to look at.

Dan McKenzie - Hudson Securities

Okay, good enough. Thanks that will do for me.

Operator

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We'll take our next question from Bill Mastoris with Gleacher & Company.

Bill Mastoris - Gleacher & Company

Derek, what are your Tier 1 requirements on your credit card processing agreement with this fixed charge coverage on unrestricted cash level that require to achieve that?

Derek Kerr

We are not allowed to talk about that as part of our contract.

Bill Mastoris - Gleacher & Company

Okay, I guess secondly with the prospect for a full year profit and he building of cash, I would think that would probably at least trigger or motivate on the renegotiation of that credit card processing agreement. Is that on the cards?

Derek Kerr

I would say that wouldn't trigger a renegotiation of that.

Bill Mastoris - Gleacher & Company

Okay, thank you.

Operator

And our next question comes from Dawn Gilbertson with Arizona Republic.

Dawn Gilbertson - Arizona Republic

I have a few follow-up questions, Scott we were just talking about the potential upside if the recovery becomes moderate or strengthened, at what point if any does a [tethered] recovery and become a problem for you guys?

Scott Kirby

Well, the point as I made on this call I think is, even in the temporary recovery as I have as a moderating influence on fuel prices, so I think more than likely does it become a problem because this revenue environment combined with this fuel environment needs to near record results. If it improves that's upside.

Dawn Gilbertson - Arizona Republic

Another question, can you explain on the furloughs, I know you made a point in your release to say, this is not growth per se or maybe that was in your employee communication, but what's the thinking behind recalling the 300 pilots and flight attendants?

Doug Parker

We need them. Even though we haven't grown much, we don't expect to grow much. There is natural attrition overtime and we haven't added any project for flight attendants in sometime, so this is just natural attrition. I mean, again, just a little inside based on, we also have peaks and valleys in our business and we are complicated, but you know we made it through. We made it through a summer peak and we about head into a trough and we hit the next peak grounding more people because of attrition.

Dawn Gilbertson - Arizona Republic

And I think during the downturn though, you were seeing as much attrition which is why you had to do some of those recalls correct?

Doug Parker

Anyway, we have seen the rate of attrition slowing from where it had been.

Dawn Gilbertson - Arizona Republic

And now it's more normal?

Doug Parker

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No, it's still, it's lower than it was back when the economy was much stronger. But it does exist.

Dawn Gilbertson - Arizona Republic

Doug or somebody on the pilot front, from a management perspective, from the company's perspective is anything going on right now in terms of pilot talks, any efforts you are making at all to try push forward the seniority integration. Are you guys doing anything at the moment?

Scott Kirby

We are doing a lot. We are involved in mediated negotiations with our pilots and continue to meet on a regular basis with pilots, and hopefully we will make progress. And so, from the company's perspective that's principally where we are involved and we are following what's going on with the Addington case and the various appeals on the Addington case, but the company is committed to [unique] deal done and to the negotiation progress which was done in the media is ongoing.

Dawn Gilbertson - Arizona Republic

Any timetable, I know we ask this question every quarter it seems for the past five years, any timetable on likely resolution of this in terms of getting a contract?

Doug Parker

It's extremely hard to project on this because of the seniority issue. We do its [consent] with mediated negotiations that should help as well. But frankly, I mean those talks, what are going on in their productive. I think both parties realized that as long as this issue blooms, we can't get anything done anyway, so they don't go to same place they would have otherwise.

Dawn Gilbertson - Arizona Republic

Okay, that's about it, okay. Doug, did the approved results in your pretty bullish outlook cool your interest at all in a merger?

Doug Parker

Where we've always been done which is we think consolidation make sense in the business, but it doesn't have to happen for us. These results prove that. We have a standalone airline that is producing better margins than any of our peers. So we don't have to do something, but we think it makes sense overtime. We think we are happy to see United and Continental progressing. We think that's good for our industry. So, our interest in consolidation was always, what if you that if it happens in the industry, that's great, if it happens and it includes us, well, that would only be better because we actually chose to participate. So we thought it was even better, but we never had to and we still don't have to.

Dawn Gilbertson - Arizona Republic

Okay. And last question if I may. Scott, can you give any update on the talks with Mesa about extending their agreement?

Doug Parker

We are making good progress with them. I hope to have something to announce soon.

Dawn Gilbertson - Arizona Republic

Soon did you say?

Doug Parker

Soon.

Operator

(Operator Instructions) Our next question comes from Josh Freed with Associated Press.

Josh Freed - Associated Press

Just a quick follow-up on labor, is there any chance at all of finalizing your flight attendant situation before the pilot situation is done or is there something that sort of dictates that pilots have to be done for us there?

Doug Parker

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There is not, Josh, its good question. We for the longest time, were tied up with their flights attendants because often times flight attendant contracts follow pilot contracts because their work roles are so tied together and we had some issues with on the old US Airways in particular, the flight attendants skate with the pilots throughout their trip and that wasn't a case with the old America-wise. So we had to get through that, we have gotten through that which is great news. So now, there doesn't appear to be scheduling issues that tie the flight attendants to the pilots. So, that allows us to break through and hopefully get something done soon or maybe get something going with the pilots. Still to be completed, but we have seen some nice progress in the last few months in our flight attendant negotiations and we are hopeful that we can get something done there.

Josh Freed - Associated Press

Okay. Are those talks happening pretty regularly then? Are there new ones coming up soon?

Doug Parker

There is. Yes.

Josh Freed - Associated Press

Okay. And my other question was whether there is any change with your aircrafts delivery schedule. I remember a while back you had pushed a few back, does that all stand sort of status quo or is there anything new to be said about when you are taking aircraft?

Doug Parker

No, that's status quo. We'll take deliveries in the back half of 2011. We're at 12 deliveries in the back half of 2011. To replace existing planes, but the schedule is still the same.

Operator

Our next question comes from Mary Jane Credeur with Bloomberg News.

Mary Jane Credeur - Bloomberg News

Can you talk a little bit more about the impact of the United, say Apollo deal on the double slot swap, might there be another round trip from Philadelphia some cash, some other consideration in there?

Derek Kerr

Well we are excited and happy to have gotten the deal done with United to at least one of their spots and I appreciate to our standalone partner and she always wanted to benefit in an alliance for the airlines and also for our consumers we will now look at for the US Airways flying to Sao Paulo as well will that have any impact on our Delta deal. We did this deal and if get the best deal done and when the appeal some how that will be a high class issue and that will be with another flight to Brazil.

Mary Jane Credeur - Bloomberg News

And did you guys allude to JV to start a bit ago if I've heard correctly and if so I am assuming any kind of JV action would happen within Star?

Scott Kirby

We are not in the JV and don't have any announcement about being in the JV and I think its no secret that we would ultimately like to be in JV and Alliance and our preferences for that to be in Star which is the largest, the most integrated and having pretty clear and the best alliance in the world.

Mary Jane Credeur - Bloomberg News

And I assume that there are active talks underway about that?

Scott Kirby

No comment.

Mary Jane Credeur - Bloomberg News

Okay fair enough.

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Operator

We will take the next question from Doug Cameron with Dow Jones.

Doug Cameron - Dow Jones

Anyways three things one on house keeping, sorry I was juggling, who was talking about ITA?

Scott Kirby

That was me Scott.

Doug Cameron - Dow Jones

Okay thanks Scott, back on your warm relations with your alliance partner United, its likely that you would have very opposite wishes with regard to that the potential listing of the rig and perimeter rule. I don't expect you to dive on such differences but differences but what would you guys want from, if the perimeter rule is lifted. How do you would want it changed?

[Multiple Speakers]

Doug Parker

I'd really. Doug we would like to see the perimeter rule lifted in its entirety and we think it's our [cake rule] or all it makes no sense whatsoever. Having said that that appear to be cortically feasible. So for really three reasons, we've heard three reasons why the perimeter rule augment to keep perimeter rule in place. One is noise by people near in the airport, two is small communities insight the perimeter concern that, if you take a constrain resource and now you can fly to more place as you will take a new flight to large airports at the expense of small communities; and then point three of the Delta's argument which is the extremely archaic piece of the argument which is Delta's airport somehow needs to be propped up, and you are able to flatside the perimeter, then Delta's will somehow be hampering that. That clearly makes no sense.

Doug Cameron - Dow Jones

I'm sure the United folks say exactly on that last point.

Scott Kirby

I'm not sure who says it but it's been said.

Doug Parker

So nonetheless that point makes no sense, Delta's is on 25% bigger than DC now that rule was made in 1967. So was this next point three, point two we've addressed was legislation, registered and are boxed in an instant that says airlines would be able to fly outside that we would able to convert slots inside the perimeter to fly outside the perimeter, so long as they reduced flying to a major hub, a DOT defined term. So for example, US Airways would need to reduce a flight to Atlanta to add a flight to Los Angeles. So, no new noise, no reduction in service to smart communities. So we are only left with the Dallas argument which Doug says, speeches are best. So, that's where we are…

Doug Cameron - Dow Jones

The bottomline, Doug, do you support the conversion approach?

Doug Parker

Of course.

Doug Cameron - Dow Jones

Yes, okay.

Doug Parker

We definitely support it. We think it's been compromised down frankly, Doug, to a level that it is a lot less than we would have liked which is often the case in these things, and things that require an active Congress usually get compromised and diluted down to a level this much as we like, but it's a big step forward and we can get this done, we will keep fighting now for years to come.

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Doug Cameron - Dow Jones

One another quick small question, the respect of one world approvals in CD open up some Heathrow slots, [pretty rubbishy] ones from the European side, Miami and Dallas or guess you could look at Boston as more flexible on the DOT side. Have you got any interest in applying for any of these additional Heathrow slots or leases they are technically?

Scott Kirby

Well, at least our initial read is that you have to fly to Dallas or Miami.

Doug Cameron - Dow Jones

Or Boston?

Scott Kirby

Yes, but since you are competing, those are markets where we could effectively compete with American BA. We would love to able to get to fly and fly to Charlotte and we could then create competitive benefits for customers.

Doug Cameron - Dow Jones

Which you can with the US one, because at least two deadly slots for any US city?

Doug Parker

Yes, I think those are in cards of 2013 and may begin. Our initial read is at least in the near term, we are frankly wondering who can even apply for these slots?

Doug Cameron - Dow Jones

Exactly, I mean the commissions say they have been waiting outside the door, but it's difficult to find anyone waiting outside the door and it doesn't sound like you are in that queue?

Scott Kirby

We are not. I mean our desire is to get one and be able to fly to one of our hubs, which we think will create significant competitive benefit, but it appears to us that at least currently that we are not going to be able to do that.

Operator

And our next question comes from Ted Reed with TheStreet.com]

Ted Reed - TheStreet.com

I have a couple of things, about the pilot with the recent court decisions and I read them, they say that [Nikeli Award] need not be in our future contract. So, given that and given fact the appeal has been turned down, if you agree with that interpretation, isn't the door kind of open now, much more than ever before to negotiate a pilot contract?

Doug Parker

Yeah, we are not going to comment on that, Ted.

Ted Reed - TheStreet.com

All right, well, I will go to my next question then. This is about the slot deal. As I read the slot deal, you and Delta announced something it would turn down then you came in sort of with a good package on the table that would benefit everybody with low cost carriers in the mix and that was turned down. Why do you think they didn't proceed and negotiate and create an environment where there were low cost carriers at these airports? What do you think their motivation was not to negotiate further, but simply to say no?

Doug Parker

Ted, look, we had a similar question on this before, when someone asked where we thought this is going to arrive, we didn't comment then so, I hate to keep you in no comments. I will say the following, our view is DOT is trying very hard to do what they think is best for the flying public. We just differ on what that is. They are not trying to do the wrong thing for certain. Their apparent view is that they can make a thing even better for consumers by having us, get something, the result was good

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enough for us and then even have some additional low cost flying in there. We don't think that's the case. Get additional flying, we just fly in the same markets we already fly to. And so we have a disagreement on that point as to what's best and we know what's best for US Airways. So, we just didn't like all the waking up with this. There are bad people trying to do the wrong things, leaning close to it. They are good hard working people trying to do their jobs and do what's best for the flying public. We just disagree with their solution and we obviously don't have to accept it. So, we are not.

Operator

And that concludes our question-and-answer session for today. I would like to turn the call back over to Mr. Parker for any additional or closing remarks.

Doug Parker

Thank you all very much for your time and thanks again to our employees who did a fantastic job getting this airline back to profitability. More to come. Thanks.

Operator

And that does conclude today's call. Thank you all for your participation.

Continue to Q&A »

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