

US Airways could become a mosaic of carriers as the airline seeks money, partners for post-bankruptcy world

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By Dan Fitzpatrick, Pittsburgh Post-Gazette

Odds are good that US Airways will make it out of bankruptcy again this summer, defying predictions of its imminent demise.

But if it survives, US Airways will likely do so with a new set of owners. The Arlington, Va.-based airline expects to land as many as two "substantial" investors and another \$100 million to \$275 million beyond the contribution of regional carrier Air Wisconsin Airlines, which recently agreed to put up \$125 million in exchange for an air services partnership and a nearly 25 percent stake in a newly restructured US Airways.

A post-bankruptcy US Airways also could be a merger candidate and part of a larger alliance that expands its route network to more parts of the United States. Even as the airline focuses on its East Coast and the Caribbean strongholds, talk of consolidation within the battered airline industry is heating up, with some arguing that the financial problems of many may mitigate antitrust concerns in Washington, D.C. -- the same concerns that nixed a proposed United Airlines-US Airways merger in 2001.

Air Line Pilots Association President Duane Woerth pressed that point with reporters last week, saying that many large carriers would like to combine operations but remain fearful of the U.S. Justice Department.

Arguing that mergers would alleviate the industry problem of too many seats and perhaps stop future bankruptcies, Woerth urged the lawmakers to allow failing carriers to merge without barriers.

His comments echoed a similar call made by former Delta Air Lines chief executive officer Leo Mullin in July 2003. Other executives, including former Continental Airlines chairman Gordon Bethune and former US Airways CEO David Siegel, have predicted industry consolidation is inevitable and that, ultimately, the number of major domestic carriers in the country could be reduced to three.

However the industry shakes out, a restructured US Airways could make for an affordable if not attractive partner for another airline and a decent bet for well-heeled investors. In recent bankruptcy documents, the airline valued itself at \$250 million before any new equity investments and as high as \$650 million if it is able to lure an additional \$400 million from outside investors.

For an investor with "discretionary income," it may be tempting to take a gamble on US Airways, said airline analyst Bill Warlick, of Fitch Ratings in Chicago. But, he adds, the

temptation to buy an airline also brings with it enormous risks, given the industry's history of bankruptcies, failures and red ink.

While it may be easy to buy into the industry, it can be "very hard to get out" -- and very costly, too, he said. Still, "there always seem to be investors out there, despite the airline industry's poor overall performance, who are willing to take the bet," said Kevin Mitchell of advocacy group Business Travel Coalition.

Spokesman David Castelveter would only say that US Airways is talking to a number of "parties" interested in some type of investment but declined to provide details.

Following is a closer look at some potential investors or partners that observers believe could play a part in US Airways' future:

#### United Airlines

The industry's No. 2 carrier has been mired in bankruptcy the last two years but CEO Glenn Tilton got people talking on Feb. 17 when he said industry consolidation was inevitable and it would be best for United to participate in a merger. "Tilton put a for-sale sign up," said local airline analyst Bill Lauer.

United and US Airways tried to join operations in 2000, but antitrust regulators opposed the deal, leading to its collapse just a month before 9/11. A union between the two still "is the most compelling" of potential combinations, but given their weakened state, the pair may need a third-party investor to act as deal maker, Lauer said. One possibility, he said, was Texas Pacific Group, the San Francisco investment firm that bid for US Airways in 2003 but lost to an Alabama state pension fund.

Justification for a merger would not be increased market reach, as was the case made by the two carriers in 2000, but the opportunity to lower costs further. Such a deal would allow the combined company to compete more effectively against superefficient Southwest Airlines or JetBlue Airways, the only airlines to post consistent profits recently.

"I think developments along this line are likely," Mitchell said. "I think United is a good candidate."

#### America West Airlines

The Phoenix-based carrier is No. 8 in the industry, one spot behind US Airways. It is strong in the West, prompting some to speculate that it could be a good match for US Airways' stronghold in the East.

America West Airlines CEO Doug Parker fed the rumor mill when he said in early February that he would "look aggressively" to purchase a rival carrier and that he wanted to add new routes on the East Coast.

He appears, however, to have his eye on airlines smaller than US Airways, saying that the number of low-cost carriers in the United States would shrink from seven or eight to two or three, and he expects America West to be one of the survivors. A spokesman later said that the comments were not specific to any particular airline.

One link between America West and US Airways is John Luth, CEO of New York consultancy Seabury Group, a specialist in aircraft finance and airline restructurings. Luth helped US Airways through its first bankruptcy, and he is doing the same in its second, making at least \$15 million in fees for his firm.

Luth also was a close adviser to America West in the days after 9/11, when the airline nearly collapsed. Luth helped the airline restructure its debts and win financing backed by the federal government. Some believe Luth's dealmaking could still bring America West and US Airways together. A Seabury spokeswoman could not be reached for comment.

Richard Branson

The British entrepreneur and operator of Virgin Atlantic is trying to launch a new U.S. carrier, Virgin America.

Delayed by a search for investors in the United States, the airline may not start its San Francisco-based operations until 2006. Branson's company has looked at US Airways before, and some believe he could do so again.

Observers said Branson could be seeking airline assets; he may want to act as an equity investor; or he may want to purchase a spare operating certificate from US Airways, which might make it easier for him to get his U.S. operation off the ground. A Virgin spokeswoman in London did not respond to a set of questions for this article.

David Bronner and the Retirement Systems of Alabama

A big question among airline observers is whether Bronner, who runs the \$25 billion Alabama state pension fund that bailed US Airways out of its first bankruptcy, is willing to bet more of the fund's money on an airline that lost \$611 million last year and has predicted privately that it could lose another \$280 million in 2005.

The fund, after pouring \$240 million into the airline in 2003, became the airline's majority owner and appointed most board seats, installing Bronner as chairman. Bronner said last year that he would not put any more money in if US Airways filed for bankruptcy again, but some observers believe he could change his mind.

Bronner told Bloomberg News in December that he would consider spending more money to help US Airways acquire new planes if its reorganization plan looked like the smaller, more efficient JetBlue Airways. That plan is due to be filed by March 15.

Bronner has written off his investment in US Airways but still was able to earn \$2.4 billion for his pension fund last year. The normally loquacious Bronner has not been available for comment in recent weeks.

#### Air Wisconsin Airlines

The Appleton, Wis.-based carrier has positioned itself as a major player in US Airways' future with a \$125 million loan that could turn into equity if US Airways makes it out of bankruptcy.

As part of its agreement, Air Wisconsin will be able to appoint three board seats and place 70 of its regional jets within the US Airways network, flying under the US Airways Express banner and taking fees from US Airways.

The deal is an insurance policy for the regional carrier, which may lose its feeder business with United Airlines this year.

#### Mesa Air, Chautauqua Airlines and other regional carriers

Some observers believe that US Airways, in its search for more investors, will look to its other affiliate carriers -- some of which are independent and some of which it owns -- that carry US Airways passengers to smaller cities and receive fees in return.

Lauer, the local analyst, believes that US Airways could sell the carriers it owns -- PSA Airlines or Piedmont Airlines -- to raise cash. Or, it could ask other regional carriers with feeder contracts, such as Mesa or Chautauqua, to invest in US Airways as Air Wisconsin did and receive guaranteed service in return.

"In the quest for exit financing," Lauer said, US Airways "has zoned in on this whole area of the regional contracts." Chief executives at Phoenix-based Mesa and Indianapolis-based Chautauqua could not be reached for comment.