Delta MEC Touch & Gos
A PRODUCT OF THE DELTA MEC COMMUNICATIONS COMMITTEE

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Delta's First Quarter Results

Executive Summary

- Delta reported a loss of $320 million excluding special items
- Revenue was up 13% year over year
- Fuel costs increased by $610 million
- Delta predicts a profit for the second quarter and for the full year
- A consolidated industry is rapidly adjusting to fuel price changes allowing the airline to thrive in a turbulent industry

The Bad

Delta lost $320 million for the quarter (excluding special items) primarily due to fuel costs, inclement weather and the Japan crises. The corporation's operating margin was negative 1.5%.

Fuel prices climbed rapidly in the first quarter and increased Delta's fuel costs by $610 million. Fuel costs are expected to remain relatively high, and Delta predicts fuel costs will come in at an additional $3 billion for the full year.

Delta estimated that they lost $140 million in the quarter due to the impact of the worse than expected winter weather, especially the ice storm in Atlanta and the earthquake/tsunami in Japan. Delta has acknowledged that it needs to improve its handling of severe weather events and has formed a study team to find better processes.

Delta increased capacity by 17% year-over-year in the transatlantic markets, while the industry increased capacity by 11%. This led to decreased yields and contributed $150 million to the loss. Delta plans to decrease transatlantic capacity by 4% year-over-year following Labor Day, and management announced they will park 20 mainline aircraft including an unspecified number of wide bodies to accommodate the capacity reduction.

The Good

The real story of the quarter is the reaction of a consolidated industry to the rise in fuel prices. In 2008, the last time fuel prices spiked, Delta estimated that the industry recovered about 30% of the increased costs with fare hikes within a few months of the fuel price increase. In this quarter, they estimate a recovery of about 70% of the price hike, and in many markets they were able to recover 100% of their costs. It is interesting to note that Delta led many of the fare hikes initiated throughout the industry.

Delta generated about $800 million in operating cash flow and sees strong bookings for the summer, which they predict will lead to double-digit yield growth. The company paid off $223 million in long-term debt and reduced its adjusted net debt (which includes long-term lease obligations less cash on hand) by $500 million. Interest payments were reduced by $35 million year-over-year due to a lower level of debt. Management continued to invest in the fleet with $274 million in additional aircraft and upgrades.

Delta expects to be profitable for the next quarter and for the full year, a dramatic change from the last time fuel prices increased this much in such a short period of time.

Big Picture Analysis

The pre-merger Delta and Northwest MECs supported the Delta/Northwest merger as part of a larger industry consolidation, in part because they believed that a consolidated industry would behave in a more economically rational manner. The fifteen years prior to this latest consolidation wave saw large spikes in industry profitability accompanied by unsupportable capacity increases, which led to even larger industry losses on the back end of the wave. That last cycle saw both Delta and Northwest enter bankruptcy, which in turn led to a massive degradation in our pay and career prospects.

The two MECs believed that a consolidated industry would more carefully control both the capacity and pricing of their product. This discipline would lead to an industry that could better weather economic shocks (terrorism, war, fuel price increases, etc.), shocks which seem to have become the new normal in our industry. As the industry was better able to consistently produce profits, our contracts and our careers should improve on the backbone of that success.

While it is too early to pop the champagne corks, the results from the past quarter and predictions for the year to come are early signs that the industry will indeed actually manage itself to produce profits rather than fighting for market share or engaging in cutthroat competition in an attempt to strangle the weakest competitor. Rather than reach for the panic button, Delta management was upbeat despite the disappointing quarter. The company predicts continued yearly profits following a strong summer season.

The Delta pilots charted a new course with this merger. We facilitated the merger to accelerate the benefits of the merged company while capturing a portion of those benefits to begin the rebuilding from the painful bankruptcy-related cuts.

Your MEC is meeting in Salt Lake City next week. A good portion of that meeting will focus on continuing to chart a path to significant contractual improvements, capturing value from what should be a more consistently profitable carrier in a more stable consolidated industry.

Revenue up 13%

Total fuel cost increased $610 mm

Negative 1.5% operating margin
(7,747 – 7,839) / 7,747

Interest expense continues to fall as debt is repaid

Invested $274 million in additional aircraft and upgrades

Paid off $223 million in long term debt

(in millions, except per share data)		2011
Operating Revenue:		
Passenger:		
Mainline	$	5,134
Regional carriers		1,441
Total passenger revenue		6,575
Cargo		250
Other		922
Total operating revenue		7,747
Operating Expense:		
Aircraft fuel and related taxes		2,166
Salaries and related costs		1,727
Contract carrier arrangements		1,300
Aircraft maintenance materials and outside repairs		485
Contracted services		425
Depreciation and amortization		376
Passenger commissions and other selling expenses		369
Landing fees and other rents		313
Passenger service		164
Aircraft rent		78
Restructuring and other items		7
Other		429
Total operating expense		7,839
Operating (Loss) Income		(92)
Other (Expense) Income:		
Interest expense, net		(221)

(in millions)		2011
Net cash provided by operating activities	$	788
Cash Flows From Investing Activities:		
Property and equipment additions:		
Flight equipment, including advance payments		(274)
Ground property and equipment, including technology		(66)
Purchase of short-term investments		(240)
Redemption of short-term investments		•
Other, net		4
Net cash used in investing activities		(576)
Cash Flows From Financing Activities:		
Payments on long-term debt and capital lease obligations		(460)
Proceeds from long-term obligations		245
Other, net		(8)
Net cash used in financing activities		(223)