REVIEW OF 2010

The grim operating environment faced by the carriers at the start of the global recession has revolutionized how they operate today. A view held by some industry professionals is that recent carrier initiatives will provide traction towards profitability, even during periods of uncertainty. One recent initiative by the passenger carriers is a shift in focus from increasing market share to one of boosting shareholder return on investment. Evidence of this initiative is three straight years of capacity reductions which have landed 2010[2] domestic capacity levels 6.4 percent lower than those posted one decade earlier. Another relatively new tactic by the carriers is generating revenue for services beyond the core purchase of an airplane seat. For example, air carriers are charging fees for services that used to be included in airfare (e.g. meal service), as well as for services that were not previously available (e.g. premium boarding and fare lock fees). The impact from these recent initiatives gives reason for optimism. After posting net losses for eight consecutive quarters, the industry (passenger and cargo carriers combined) posted profits in three out of four quarters of FY 2010.

Demand for air travel in 2010 grew slowly following a dismal 2009 that was marked by fading consumer confidence, tightening credit, surging unemployment, and eroding corporate travel budgets. In 2010 system revenue passenger miles (RPMs) increased 2.2 percent as enplanements increased 1.2 percent. Commercial air carrier domestic enplanements were up 0.7 percent while international enplanements were up 5.2 percent. The system-wide load factor pushed through the 80 percent barrier for the first time to 81.8 percent (up 2.1 points from 2009). Domestic enplanement market share continued to rise for low-cost and regional carriers in 2010 while network and “other” carrier share decreased. Enplanement market share for the network carriers shrank 1.8 points to 45.9 percent while market share for “other” carriers shrank 0.1 points to 1.3 percent. Low cost carrier[3] share rose 0.9 points to 27.4 percent and regional carrier market share rose 1.1 points to 25.4 percent.

Capacity restraint by the carriers as passenger demand returned helped system wide real yield to increase by 3.2 percent in 2010. Data for FY 2010 show that the reporting passenger carriers had a combined operating profit of $7.4 billion (compared to a $0.2 billion operating loss posted for FY 2009). The network carriers reported combined operating profits of $5.0 billion and the low cost carriers reported combined operating profits of $1.6 billion, with five out of the six network carriers and seven of the nine low cost carriers posting profits. Net profits for U.S. commercial air carriers (cargo and passenger) for the year totaled $3.0 billion, with the network, cargo, low cost and “other” carrier groups each posting net profits of $1.5, $1.3, $0.6, and $0.2 billion, respectively. The only carrier group to post a net loss for 2010 was the regionals ($0.6 billion).

The market for general aviation products and services declined sharply in the first three quarters of CY 2010. U.S. manufacturer shipments declined for the third year in a row, down an estimated 20.9 percent, while worldwide billings are estimated to have declined 5.4 percent compared to 2009. Piston and turbine aircraft shipments by U.S. manufacturers fell an estimated 6.7 percent and 35.4 percent, respectively. The decline in shipments and billings seen in the turbine fleet are a direct reflection of the downturn in the U.S.

2 All stated years and quarters for U.S. economic and U.S. air carrier traffic and financial data and forecasts are on a fiscal year (FY) basis (October 1 through September 30). All stated years and quarters for international economic and world traffic and financial data are on a calendar year (CY) basis, unless otherwise stated.

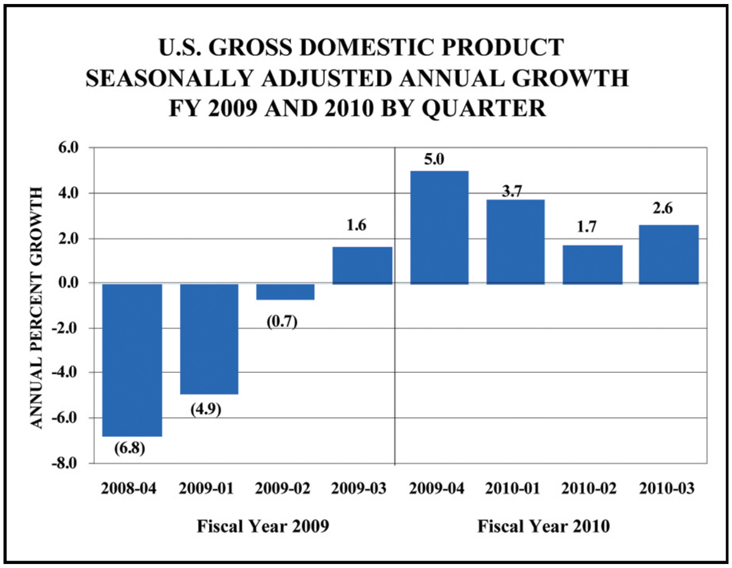
3 Allegiant Air, AirTran Airways, Frontier Airlines, JetBlue Airways, Southwest Airlines, Spirit Airlines, Sun Country Airlines, USA3000, and Virgin America Airlines.

and world economy. Along with the fall in shipments and billings, general aviation activity at FAA and contract tower airports fell 5.1 percent in 2010.

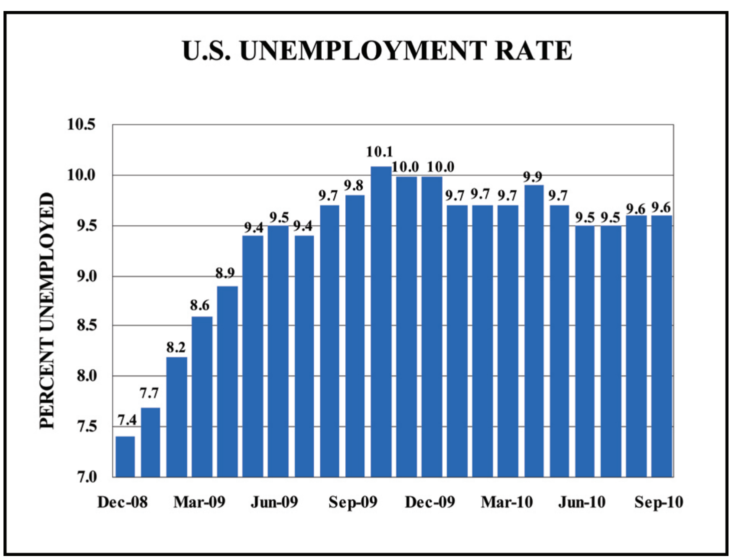
Total operations at FAA and contract towers fell 3.2 percent to their lowest levels since 1982 as activity declined in all user categories with the exception of military. Although the overall number of flights fell, FAA's workload didn't. As the fleet mix changes with increasing numbers of regional and business jets in the nation's skies, and as carriers consolidate operations in their large hubs, the complexity of activity in the airspace continues to grow, increasing our workload.

U.S. ECONOMIC ACTIVITY

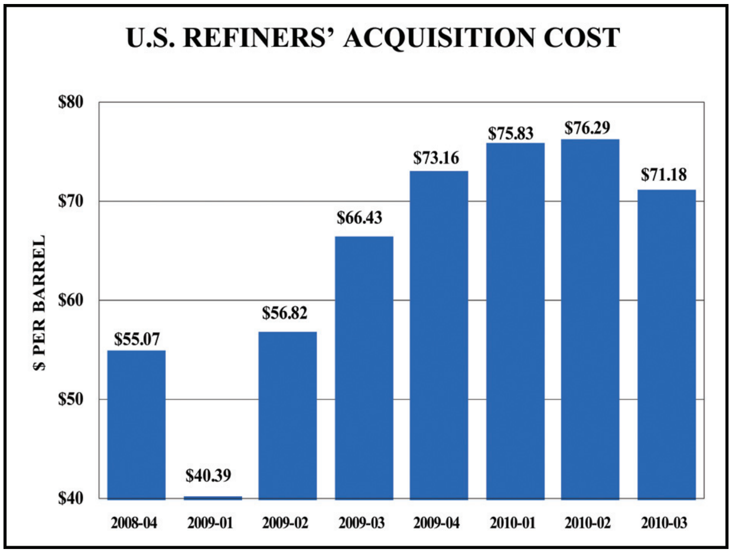
To help revive the economy from the worst recession in the post war era, lawmakers enacted the American Recovery and Reinvestment Act (ARRA) in February 2009. The bill included a combination of individual tax cuts, investment incentives, aid to people directly hurt by the recession, state fiscal relief, and direct government investment spending which was expected to have a total fiscal impact of $817 billion between 2009 and 2019 (with half of the stimulus projected to occur during 2010). The results from enactment of this bill are encouraging. After four consecutive quarters of contraction, the economy grew for the first time during the fourth quarter of FY 2009 (up 1.6 percent) and 2.2 percent for all of FY 2010.



One repercussion to the economy resulting from the recession was to the nation's unemployment rate. When the recession began in December 2007 the unemployment rate was 5.0 percent. Unemployment climbed throughout 2008, intensified during 2009, and reached its pinnacle during the first month of FY 2010 (10.1 percent). The unemployment rate for all of FY 2010 averaged 9.7 percent. All told, from the beginning of the recession through the end of FY 2010 approximately 7.6 million jobs were lost.



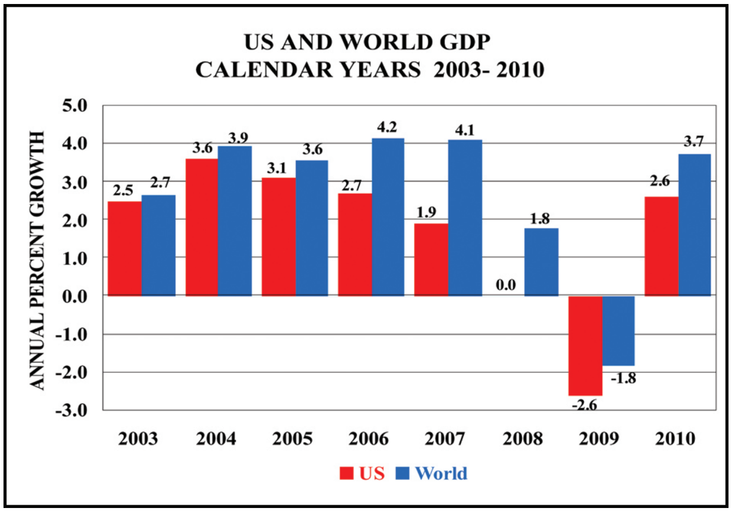
Oil prices, as measured by the U.S. Refiners' Acquisition Cost, increased 35.5 percent from FY 2009 to average $74.11 in FY 2010. The fuel price volatility that plagued 2008 and 2009 diminished in 2010, with prices in 2010 falling within a narrower band (between $72.08 and $80.83 per barrel) versus prices in 2009 (between $37.67 and $74.22 per barrel).



After declining 0.3 percent in 2009 (the first decline since 1955), consumer prices increased in 2010. The combination of growing demand and higher energy prices drove the consumer price index (CPI) up a modest 1.7 percent in FY 2010.

WORLD ECONOMIC ACTIVITY

In 2010, the U.S. and world economies grew 2.6 and 3.7 percent, respectively, after posting their worst performance since the Great Depression in 2009. The advanced economies (U.S., Western Europe, Japan, Australia, New Zealand, and Canada) expanded 2.4 percent. All world regions saw their economies grow, but data coming out at the end of the year suggest that the recovery in Europe is continuing to lag that of other world regions.



In CY 2010, GDP in Canada expanded at a faster pace (up 2.9 percent) than the U.S. (up 2.6 percent). The combined economies of the Asian and Far East nations grew 6.5 percent in 2010, up from 1.7 percent a year earlier. This region includes the world's second largest economy, Japan (up 2.7 percent), and the world's most vibrant economy, China (up 10.2 percent). The combined economies of Europe are rebounding more slowly, with Western Europe up 1.6 percent and the combined economies of Central Europe and the former Soviet Union up 3.4 percent. GDP in Latin America expanded by 4.7 percent with Brazil up 7.3 percent and Mexico up 4.8 percent.

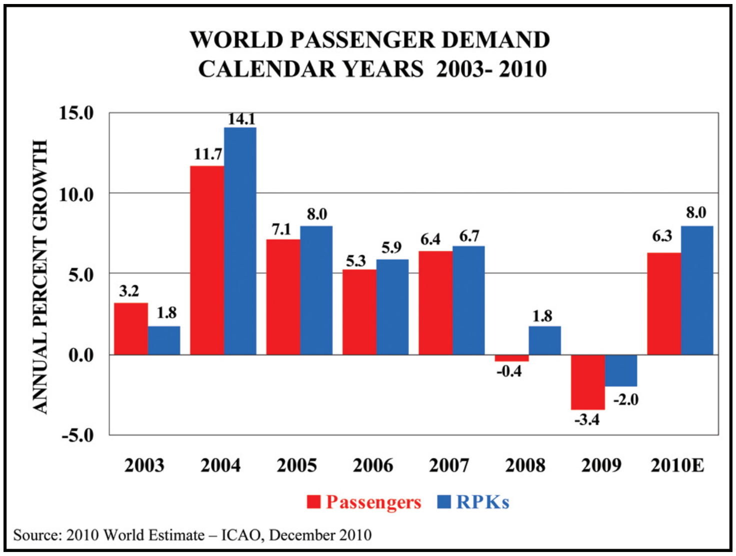
COMMERCIAL AVIATION

Commercial aviation rebounded in 2010 despite rising jet fuel prices. Coming off of two years of losses, the U.S. industry posted a net profit in 2010, with a similar outcome predicted for foreign carriers. With none of the world regions in recession during the year, global industry net profits for calendar year 2010 are expected to be \$15.1 billion.[4] Profits are expected for all global regions as revenues rebound and airlines better manage their capacity.

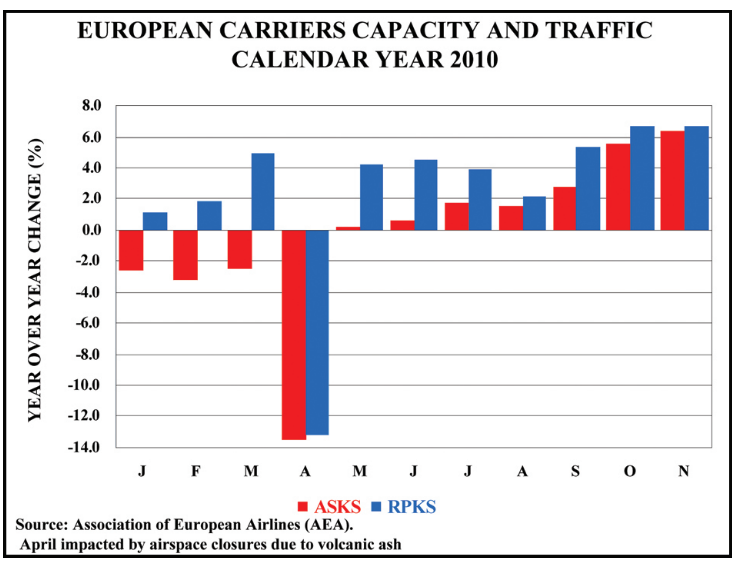
4 IATA Financial Forecast, December 2010.

World Travel Demand

Based on data compiled by the International Civil Aviation Organization (ICAO), world air carriers are expected to post a strong performance in CY 2010 as demand for air travel picks up from the depressed levels recorded during 2009. Although traffic results are not available for full year 2010, ICAO forecasts that worldwide RPKs will increase 8.0 percent after a decline of 2.0 percent in 2009.[5]

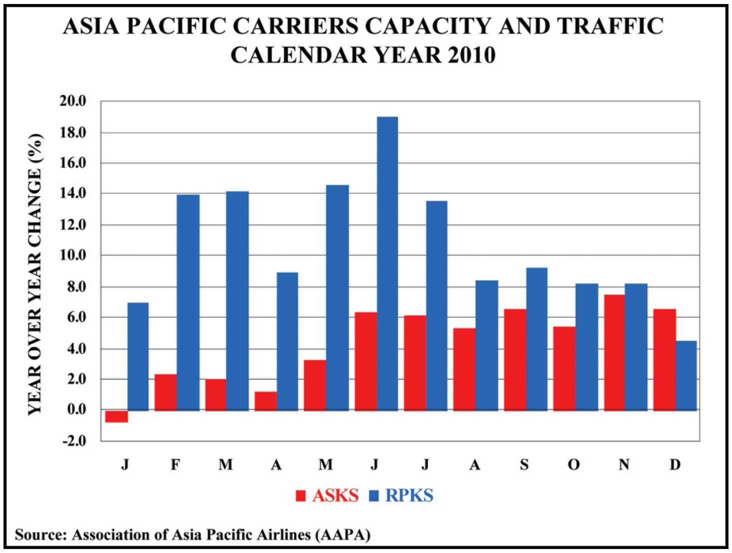


Statistics from the Association of European Airlines (AEA) available through November 2010 show passengers are up 2.8 percent over the same 2009 period. Data for the same eleven month period shows capacity, as measured by available seat kilometers (ASKs), to be down 0.2 percent and RPKs to be up 2.7 percent. Results for April 2010 were negatively impacted by airspace closures stemming from volcanic ash clouds.

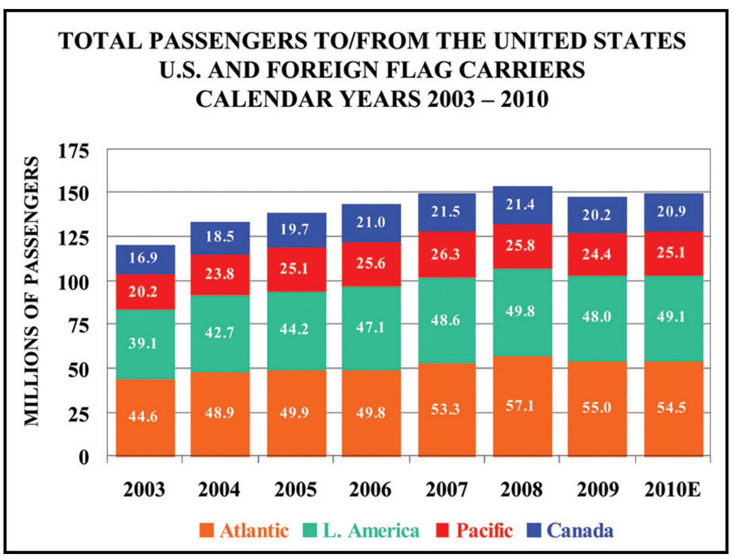


5 ICAO press release dated December 23, 2010.

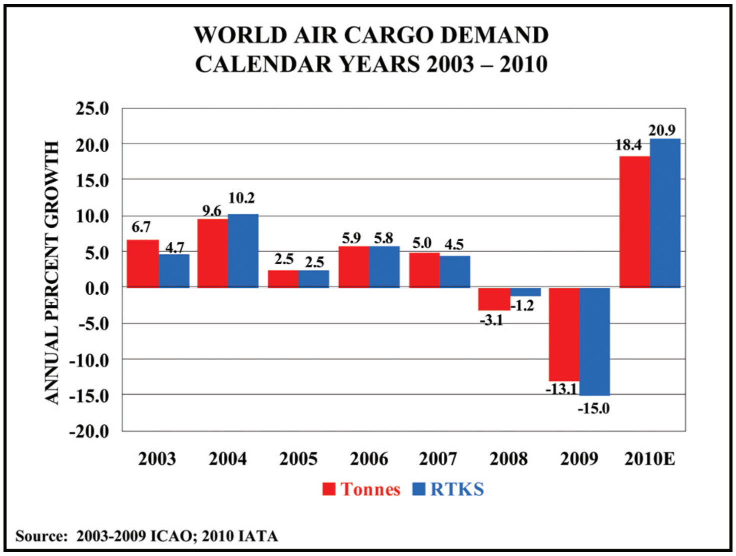
The Association of Asia Pacific Airlines (AAPA) reported an increase of 9.8 percent in international RPKs on a 4.1 percent increase in international ASKs for the calendar year of 2010. International passengers were up 13.0 percent during the same period.



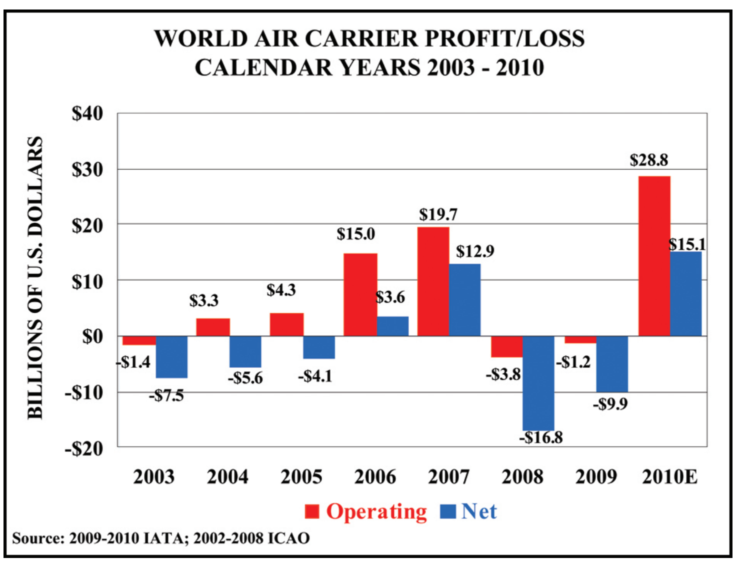
In CY 2010, U.S. and foreign flag carriers will transport an estimated 149.6 million passengers between the United States and the rest of the world, a 1.4 percent increase from 2009. Year-over-year growth increased in the Transborder, Pacific and Latin markets (up 3.4 percent, 2.9 percent and 2.3 percent, respectively). Passengers decreased in the Atlantic market (down 0.9 percent) due to repercussions from the debt crisis in Europe, which is slowing the recovery of that region's economy, and from airspace closures during the Spring of 2010 stemming from the eruption of volcano Eyjafjallajökull.



Worldwide air cargo demand resumed in 2010 as world trade volumes picked up from the global economic downturn of 2009.[6] According to IATA, worldwide freight ton kilometers were up 21.9 percent for the first 11 months of 2010 compared to a 12.7 percent drop for the same period in 2009. AEA and AAPA member carriers FTK's were up 8.9 percent and 26.3 percent, respectively, for the eleven months ending November 2010.



The International Air Transport Association (IATA) reports world air carriers (including U.S. airlines) are expected to register an operating profit of $28.8 billion for 2010. IATA estimates global airline industry net profits to be $15.1 billion for the same period with all regions expected to be in the black. Based on financial data compiled by ICAO and IATA, between 2001 and 2009 world airlines produced cumulative operating profits of $14.5 billion (with four years out of nine posting gains) and net losses of $50.9 billion (with two years out of nine posting gains).[7]



6 IATA News Release, November 2010.

7 IATA Financial Forecast, December 2010.

U.S. TRAVEL DEMAND

By year end FY 2010, the U.S. commercial aviation industry consisted of 16 scheduled mainline air carriers that use large passenger jets (over 90 seats), 64 scheduled regional carriers that use smaller piston, turboprop, and regional jet aircraft (up to 90 seats) to provide connecting passengers to the larger carriers, 14 nonscheduled passenger carriers, and 26 all cargo carriers. Mainline and regional carriers provide domestic and international passenger service between the U.S. and foreign destinations, although regional carrier international service is confined to border markets in Canada, Mexico, and the Caribbean.

Shaping today's commercial air carrier industry are three distinct trends: (1) convergence of the network and low cost carrier business models; (2) industry consolidation and restructuring, and (3) the proliferation of ancillary revenues.

A sign that the business models for the low cost and network carriers groups are converging is the narrowing share of capacity flown between these two groups and the fares they charge. After losing market share in 2008, partially due to the cessation of operations by two low cost carriers in that year,[8] low cost carrier capacity share has been on the rise (up 0.9 points in 2009 and up 0.4 points in 2010). Since 2000, the share of capacity flown by the low cost carrier group has almost doubled, going from a 17.0 percent share in 2000 to a 31.6 percent share in 2010. Also narrowing is the gap in average domestic yield (a proxy for airfare) reported by the low cost and network carrier groups. In 2000, average domestic yield for the low cost carrier group was 12.4 cents versus 14.5 cents for the network carrier group. By 2010, low cost carrier yield had increased to 12.7 cents (up 2.4 percent from 2000) while network carrier yield dropped to 12.5 cents (down 13.8 percent from 2000).

Industry restructuring and consolidation continued in 2010. Operations at Northwest Airlines were folded into Delta Airlines, while operations at Midwest Airlines were folded into Frontier Airlines. For the regional carriers, Delta Airlines sold its subsidiaries, Compass and Mesaba, to Trans States and Pinnacle, respectively, and Arctic Circle Air merged with ERA Aviation. Announced during 2010 was the merger of Continental Airlines with United Airlines, the merger of Southwest Airlines with Air Tran, and the acquisition of ExpressJet by SkyWest Airlines. As a result of industry restructuring and consolidation, 53 fewer carriers reported traffic to the Bureau of Transportation Statistics in 2010 compared to 2000. Subsequently, 6.4 percent fewer domestic ASMs were flown and 1.0 percent fewer passengers were carried domestically in 2010 compared to ten years earlier.

The 6.4 percent reduction in domestic capacity since 2000 has not been shared equally between the mainline carriers and their regional counterparts. In 2010, the mainline carrier group provided 15.5 percent less capacity than it did in 2000 (and carried 16.1 percent fewer passengers). Conversely, capacity flown by the regional group increased 150 percent over the same ten year period (with passengers carried up 100 percent). The shift in capacity from the mainline carrier group to the regional carrier group emerged from several factors. One factor was the type of aircraft flown by the regional carriers, which has been transformed from one of predominantly turboprop and piston aircraft to that of 50-90 seat regional jets. The transformation of the fleet permitted the regional carriers to fly longer haul routes that were not previously accessible with smaller turboprop aircraft. Another factor leading to a shift in capacity was the external operating environment. As a result of the terror attacks of September 11 and the record breaking fuel prices of 2008 demand for air travel was reduced. To better match demand to capacity, the mainline carriers "shed" thin routes to their regional counterparts, which could provide lift at a lower cost.

8 American Trans Air and Skybus Airlines.

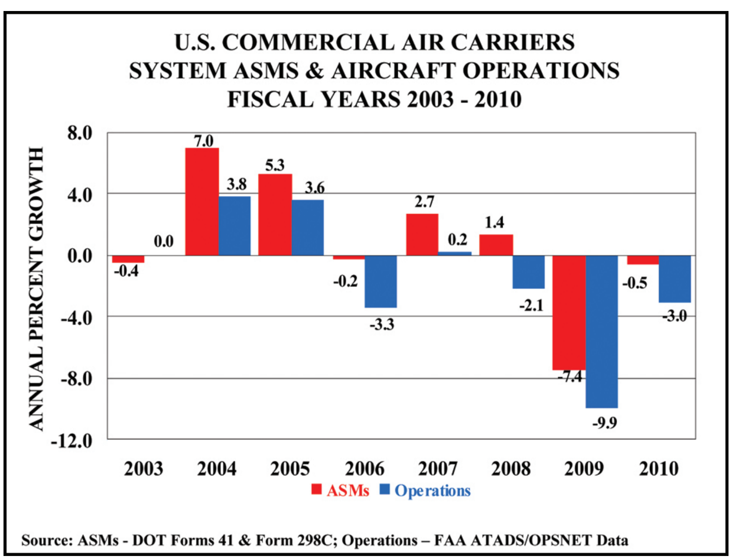
The most recent trend to take hold is that of ancillary revenues. Carriers generate ancillary revenues by selling products and services beyond that of an airplane ticket to customers. The industry will post a net profit for the first time since 2007, with ancillary revenues a contributing factor to the favorable outcome.

Commercial Air Carriers — Passengers

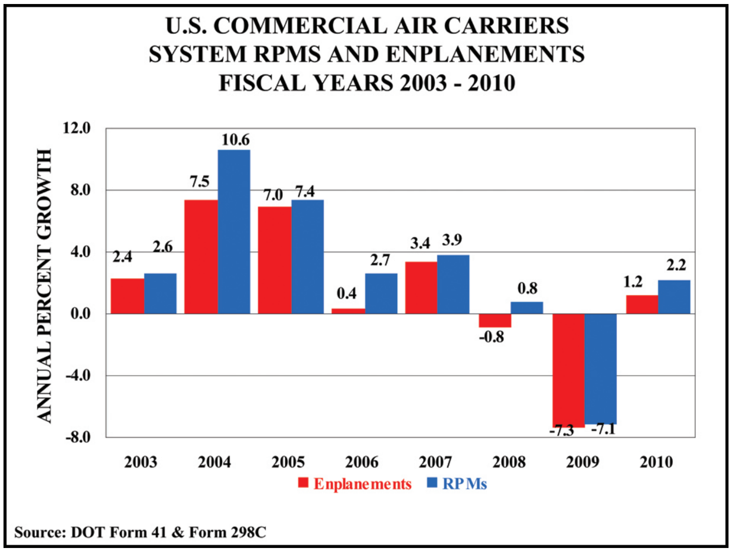
After a challenging 2009 which was impacted by the global economic meltdown and the H1N1 flu, U.S. commercial air carriers posted improvement to traffic results during 2010, with little change in capacity for the year. System (the sum of domestic plus international) capacity dropped 0.5 percent to 961.3 billion ASMs while RPMs increased 2.2 percent to 786.7 billion. During the same period system-wide passenger growth increased 1.2 percent. For the year, mainline carrier passenger growth was up 0.1 percent while passenger growth for the regional carriers was up 5.0 percent. In the domestic market mainline passengers fell for the seventh time in ten years during 2010 (down 0.7 percent) while mainline passengers in international markets posted strong growth (up 5.2 percent).

Even though the recession was officially over in June 2009,[9] carriers continued to face economic uncertainty in 2010 as corporate travel budgets remained strained and double-digit unemployment persisted. Capacity reductions instituted in 2009 to counter skyrocketing fuel prices and reduced demand for air travel continued into 2010. With fewer seats available to the travelling public, carriers were able to raise airfares as demand returned. Initially forecast to lose money for the year, U.S. carriers finished 2010 with a net profit.

System load factor and trip length climbed in 2010, as seats per aircraft mile fell. Load factor reached a record-breaking 81.8 percent, up 2.1 points from 2009. For the eighth consecutive year, trip length increased, up 11.0 miles to 1,104.0 miles. Seats per aircraft mile fell to 139.7 seats (down 0.3 seats per aircraft mile).

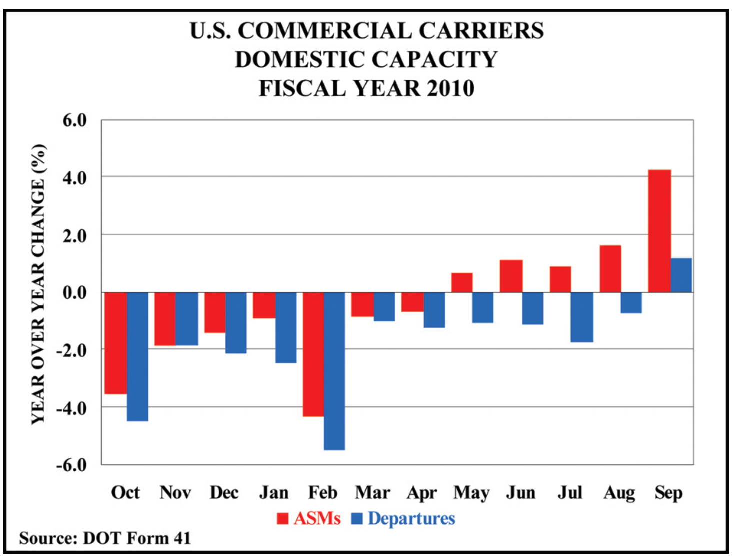


9 National Bureau of Economic Research.

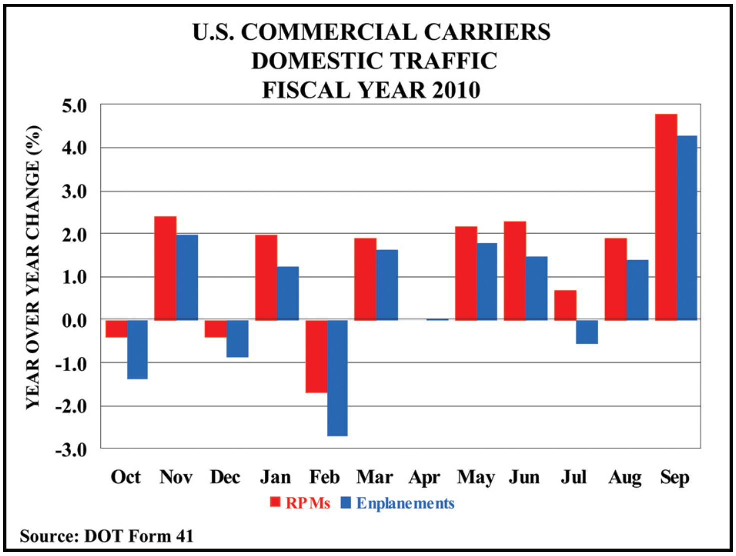


Domestic Passenger Markets

Domestic capacity (50 states, Puerto Rico, and the U.S. Virgin Islands) was down 0.4 percent in 2010 after coming off of a decline of 9.0 percent in 2009, the steepest decline recorded since deregulation of the industry in 1978. Departures decreased by 1.8 percent for the year after falling 8.6 percent in FY 2009. Year-over-year declines in capacity were posted for the first seven months of 2010 with the first quarter down 2.3 percent and the second quarter down 1.9 percent. Capacity grew 0.4 percent and 2.2 percent year-over-year in the third quarter and fourth quarter, respectively. Mainline carrier capacity was down 1.1 percent for the year, while regional carrier capacity was up 4.1 percent. At the end of 2010, domestic ASMs were 9.6 percent below pre-recession levels (2007) with departures 12.2 percent below.



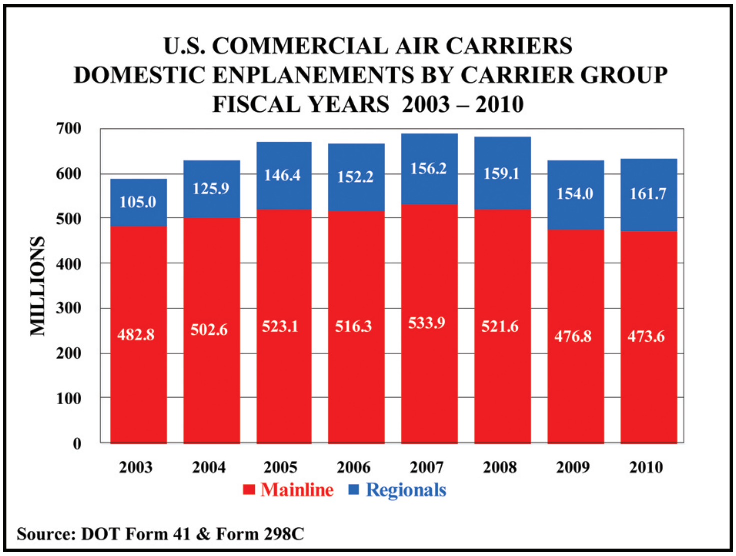
Domestic passenger enplanements and RPMs grew at a faster rate than ASMs in 2010. Between the first and second quarter, passenger growth went from negative (down 0.1 percent) to positive (up 0.2 percent). During the last half of the year growth accelerated, up 1.1 percent in the third quarter and up 1.5 percent in the fourth quarter. On a year-over-year basis, mainline carrier enplanements were down 0.7 percent for the year while the regional carrier enplanements increased 5.0 percent (rebounding from its first post-deregulation era decline in 2009).



Similar to passengers, domestic RPMs grew faster than ASMs with domestic RPMs up 1.3 percent in 2010. Growth accelerated during the year with the first quarter up 0.4 percent, the second quarter up 0.8 percent, and the last half of the year up 1.9 percent (with September posting year-over-year growth of 4.8 percent). For the year, mainline carrier RPM growth was up 0.5 percent, while regional carrier growth was up 6.7 percent.

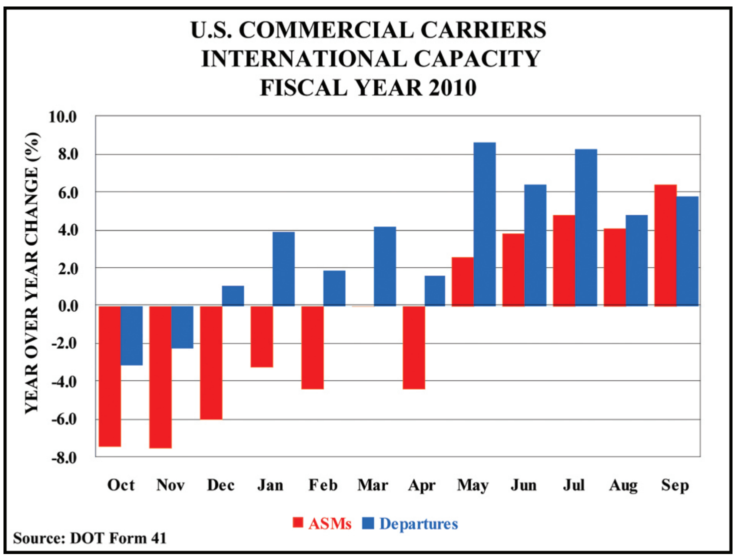
Domestic carrier load factor increased 1.3 points to 81.7 percent, with both the mainline and regional carriers groups posting record high loads. Mainline carrier load factor increased 1.3 points from 2009 to 82.7 percent, while regional carrier load factor increased 1.9 points to 76.2 percent.

Since 2000, total domestic capacity has decreased by 6.4 percent. Mainline carriers have reduced their domestic capacity by 15.5 percent with cutbacks by network carriers more than offsetting the growth of low-cost carriers. Making up some of the shortfall from network carrier capacity cuts during this time are the regional carriers. This segment of the industry has greatly expanded capacity (up 257 percent from 2000). During the same period, mainline carrier RPMs have decreased 1.9 percent, while enplanements have fallen 15.7 percent. In comparison, regional carrier RPMs and enplanements have increased 228.9 percent and 103.0 percent, respectively. As a result, mainline carrier domestic capacity share has fallen from 94.7 percent in 2000 to 85.5 percent in 2010, with their share of RPMs dropping from 95.6 percent to 86.5 percent during the same period. Regional carriers now fly 1 in every 4 passengers, up from 1 in every 8 in 2000.

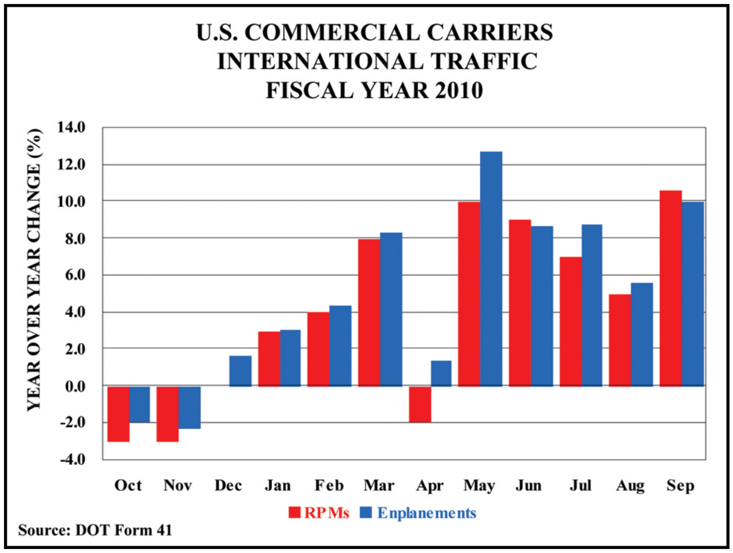


International Passenger Markets

U.S. carrier ASMs were down 0.7 percent but departures were up 3.6 percent in 2010 as Latin markets rebounded from a depressed 2009 due to H1N1. ASM growth in the first half of the year was down 4.7 percent year-over-year, but accelerated during the second half of the year to be up 2.9 percent. ASMs increased in the Latin and Pacific market, up 5.9 and 0.9 percent, respectively, but decreased 5.2 percent in the Atlantic market.



International RPMs were up 4.3 percent and passenger enplanements were up 5.2 percent in 2010, with the growth stronger in the latter half of the year (up 1.4 percent for the first half versus up 6.8 percent during the second half for RPMs; up 2.3 percent versus up 7.8 percent for enplanements). The Atlantic market posted a decline, with RPMs down 0.3 percent and enplanements down 1.0 percent. RPMs and enplanements increased 9.3 and 8.6 percent, respectively, in the Latin American market, while RPMs and enplanements increased 8.3 and 7.5 percent, respectively, in the Pacific market.



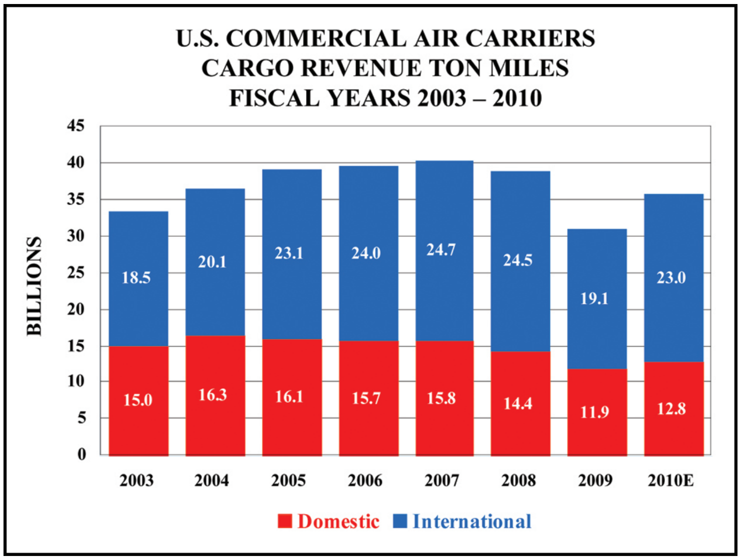
The international load factor surged 4.0 percentage points in 2010 to 82.1 percent, an all-time high. Load factor increased in all markets: in the Pacific market up 5.8 points to 84.1 percent; in the North Atlantic market up 4.1 points to a record high 82.9 percent; and in the Latin America market (up 2.5 points to 79.1 percent).

In 2010, 51.6 percent of the passengers flying abroad on U.S. flag carriers traveled to the Latin America market. The remaining 48.4 percent of international passengers was split between the Atlantic market (31.7 percent) and the Pacific market (16.7 percent).

Commercial Air Carriers—Cargo

Air cargo traffic contains both domestic and international revenue freight/express and mail. The demand for air cargo is a derived demand resulting from economic activity. Cargo moves in the bellies of passenger aircraft and in dedicated all-cargo aircraft on both scheduled and nonscheduled service. Cargo carriers face price competition from alternative shipping modes such as trucks, container ships, and rail cars.

U.S. air carriers flew 35.9 billion revenue ton miles (RTMs) in 2010, up 15.7 percent from 2009, with domestic cargo RTMs increasing by 8.0 percent (12.8 billion) and international RTMs increasing by 20.6 percent (23.0 billion). The strong growth in domestic and international RTMs reflects a rebound from the recession and the global financial crisis, although RTMS are still 11.4 percent below levels posted in 2007.



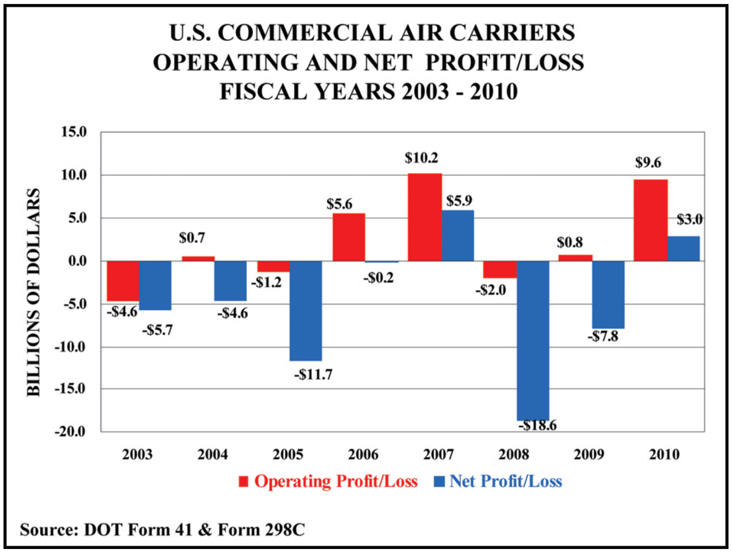
Air cargo RTMs flown by all-cargo carriers was 75.7 percent of total RTMs in 2010, with passenger carriers flying the rest, or 24.3 percent. Total RTMs flown by the all-cargo carriers increased 15.7 percent in 2010, from 23.5 billion to 27.1 billion. Total RTMs flown by passenger carriers were 8.7 billion in 2010, 16.0 percent higher than in 2009.

On August 3, 2007, “Recommendations of the 9/11 Commission Act of 2007” was signed into law. Section 1602 of this Act states that air cargo placed on passenger aircraft will receive the same level of screening as passenger-checked baggage. The legislation went into effect on August 1, 2010, and requires 100 percent inspection of cargo transported on passenger aircraft at the piece level. The legislation did not apply to cargo on U.S. bound passenger flights from overseas or on cargo-only aircraft. However, following the discovery of a bomb on an all-cargo plane bound for the U.S., the Air Cargo Security Act was introduced on November 16, 2010. The purpose of this Act is to expand the 100 percent cargo screening mandate of passenger aircraft to cargo only aircraft.

U.S. COMMERCIAL AIR CARRIERS 2010 FINANCIAL RESULTS

U.S. commercial air carriers posted a net profit of $3.0 billion during FY 2010 after reporting a net loss of $7.8 billion one year earlier.

Operating revenues (passenger and cargo) for FY 2010 were up 7.0 percent from FY 2009. The increase in revenue underscored the ability of passenger carriers to push through fare increases and to offer value-added services that leisure and business passengers were willing to buy. The increase in revenues for cargo carriers followed a rebound from the global financial crisis which strengthened demand for air cargo services.

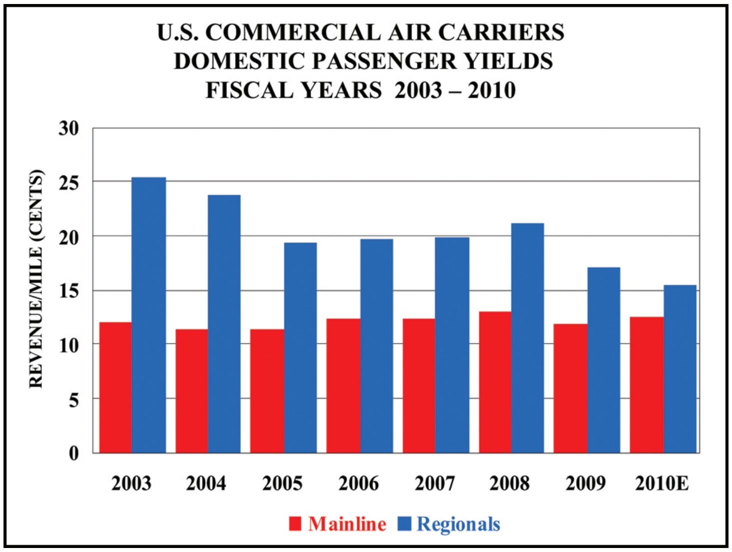


During the same period, operating expenses increased 1.6 percent. The slight increase in operating expenses during FY 2010 was driven by a 35.5 percent rise in the price of fuel for the year, as well as an increase in variables costs resulting from increased demand for passenger and cargo services.

In FY 2010, passenger carriers reported operating income of $7.4 billion and net profits of $1.7 billion, while air cargo carriers reported an operating profit of $2.1 billion and a net income of $1.3 billion. In the domestic market, passenger carriers generated an operating profit of $4.4 billion and a net profit of $0.06 billion. In the international market, this carrier group posted operating and net profits of $3.0 billion and $1.7 billion, respectively. Cargo carriers posted an operating profit of $0.7 billion and a net income of $0.4 billion in domestic markets. In international markets, the cargo carriers reported operating profits of $1.4 billion and net income of $0.9 billion.

The industry's financial boost is largely due to a turnaround in the performance of the network carriers. After two consecutive years (FY 2008-2009) of net losses totaling $27.3 billion, this carrier group finished FY 2010 with a net profit of $1.5 billion (and operating profits of $5.0). For the nine reporting low-cost carriers, operating profits totaled $1.6 billion and net income totaled $0.6 billion for the full year.

An upswing in leisure and business demand along with ongoing capacity discipline led to a rebound in mainline carrier passenger yield for the year. Domestic mainline carrier passenger yield increased 5.2 percent in 2010.



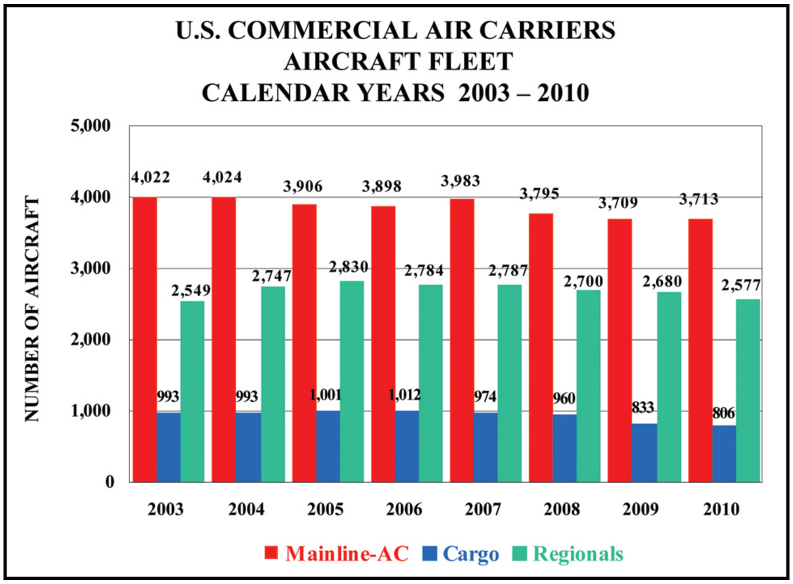
Of the reporting regional carriers, operating profits totaled $0.6 billion and net losses totaled $0.6 billion for FY 2010. During the same period, regional domestic yield fell 7.5 percent.[10] Reflecting the changing nature of the industry the network carriers are putting the squeeze on their regional partners by negotiating fee-for-departure contracts that shift more of the financial risk of contract flying to the regional carriers. Since 2000, regional yield is down 59.0 percent in real terms (compared to a drop of 29.7 percent in mainline yield for the same period). The drop in regional yield can be attributed to longer trip lengths (due to growing number of larger and faster regional jet aircraft entering the fleet) and rising load factors. All other things equal, an increase in either the trip length or the load factor results in drop in yield since passenger revenues are spread over a broader base of RPMs.

U.S. COMMERCIAL AIR CARRIERS
2010 AIRCRAFT FLEET

The commercial passenger carrier fleet is undergoing transformation. The mainline carriers are retiring older, less fuel efficient aircraft (e.g. 737-300/400/500 and MD-80) and replacing them with more technologically advanced 737-700/800/900 aircraft. The regional carriers are growing their fleet of 70 to 90 seat regional jet aircraft and reducing their fleet of 50-seat jet aircraft.

The total number of aircraft in the U.S. commercial fleet (including regional carriers) is estimated at 7,096 for 2010, a decrease of 126 aircraft from 2009. This includes 3,713 mainline air carrier passenger aircraft (over 90 seats), 806 mainline air carrier cargo aircraft, and 2,577 regional carrier aircraft (jets, turboprops, and pistons).

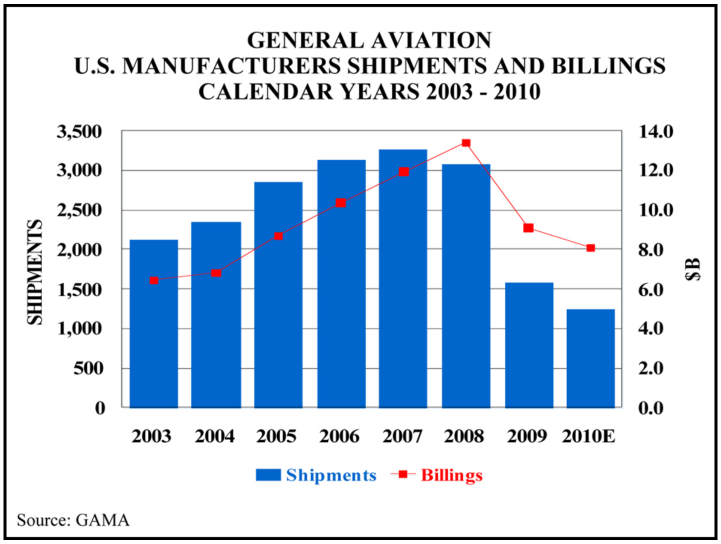
10 Yield is defined as passenger revenues divided by RPMs. Passenger revenues include payments received by regionals from mainline partners for contractual flying.



The mainline carriers' passenger jet fleet increased by 4 aircraft in 2010, the first increase in the size of the fleet since 2007, as low cost carriers added to their narrow body fleet while network carriers added a modest number of wide body aircraft. Despite the rise in the fleet in 2010, the mainline carrier fleet stands at 17.3 percent below (775 aircraft) the level it was in 2000. Since reaching a peak of 2,830 aircraft in 2005, the regional fleet has shrunk by 253 aircraft.

GENERAL AVIATION

Despite signs of economic recovery, the general aviation industry suffered through a difficult 2010. Based on figures released by the General Aviation Manufacturers Association (GAMA) through the 3rd quarter, U.S. manufacturers of general aviation aircraft delivered an estimated 1254 aircraft in CY 2010, 20.9 percent fewer than in CY 2009. This translates into a third consecutive year of decline in shipments. The turbine categories, turbojets and turboprops, were down an estimated 43.2 and 20.4 percent, respectively. Overall piston deliveries declined 6.7 percent, with single-engine down 10.7 percent while the much smaller multi-engine category rose 88.8 percent. Billings in CY 2010 are estimated to have totaled $8.1 billion, down 11.2 percent compared with 2009.



General aviation activity at FAA air traffic facilities posted mixed results in 2010. Operations at combined FAA and contract towers declined 5.1 percent in 2010, continuing a decade long trend. General aviation activity at consolidated traffic facilities (FAA TRACONs) fell 1.9 percent, while the number of general aviation aircraft handled at FAA en route centers rose by 3.4 percent.

The FAA uses estimates of fleet size, hours flown and utilization from the General Aviation and Part 135 Activity Survey (GA Survey) as baseline figures upon which assumed growth rates can be applied. This survey has been conducted annually since 1977. Beginning with the CY 2004 Survey there were significant improvements to the survey methodology. These improvements included conducting 100 percent samples for turboprops and turbojets, all rotorcraft, all aircraft in Alaska and all aircraft operating on-demand under Part 135. In addition, the sample design was revised to stratify by aircraft type (19 categories), FAA region (9 categories), and whether the aircraft was owned by an entity certified to fly Part 135 operations (2 categories). Furthermore, a large fleet reporting form was incorporated to allow owners/operators of multiple aircraft to report aggregate data for their entire fleet on a single form. In 2005 an additional aircraft category (light sport aircraft) was added. The result of these changes was the sample size nearly doubled. Between 2003 and 2005 large changes in both the number of aircraft (turbojets up by 22.8 percent, total rotorcraft up by 33.7 percent) and hours (single-engine piston down by 17.6 percent) in many categories occurred. The results of the 2009 Survey, the latest one available, are consistent with the results of past surveys since 2004. This reinforces our belief that methodological improvements have resulted in superior estimates relative to those in the past and they are used as the basis for our forecast.

Based on the latest FAA assumptions about fleet attrition and aircraft utilization along with GAMA aircraft shipment statistics, the active general aviation fleet is estimated to have increased 0.1 percent in 2010, to 224,172. With the increase in the active fleet, general aviation flight hours are estimated to have increased 1.2 percent in 2010 to 24.1 million.

Student pilots are important to general aviation and the aviation industry as a whole. Student pilot numbers had been in decline for many years but in 2010, the FAA issued a rule that increased the duration of validity for student pilot certificates for pilots under the age of 40 from 36 months to 60 months. As a result, according to statistics compiled by the FAA's Mike Monroney Aeronautical Center, the number of student pilots at the end of 2010 increased by 64.8 percent, or approximately 47,000 pilots, compared to calendar year end 2009. The impact of the new rule on the long term trends in student pilots has yet to be fully determined. The average age of a U.S. pilot in 2010 was 44.2 years old.

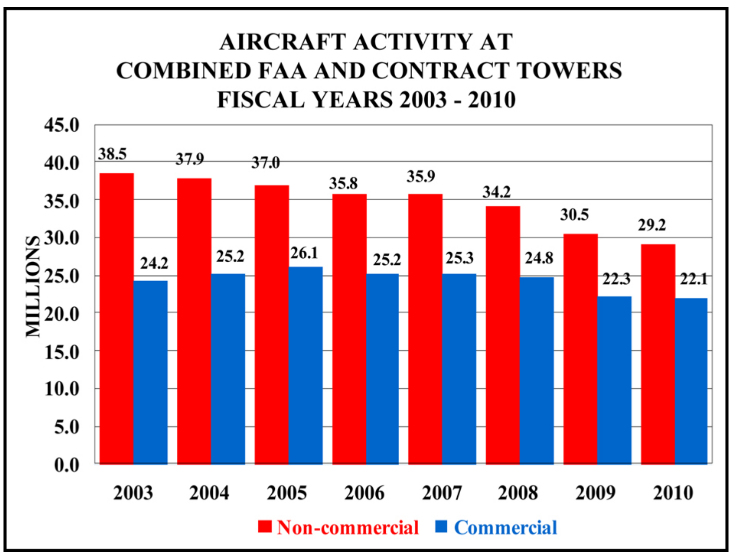
FAA WORKLOAD

In 2010, FAA facilities experienced their third straight year of decline in activity. Commercial air traffic activity fell during the first seven months of the year as carriers restrained capacity in response to weakened demand. The decline in noncommercial activity is attributed to a lackluster economy and rising fuel prices.

Total activity at combined FAA and contract tower airports was 51.2 million operations in 2010, down 3.2 percent from 2009 and 25.4 percent below the peak activity level recorded in 2000. Commercial activity (the sum of air carrier and commuter/air taxi) at combined FAA and contract towers fell by 1.3 percent in 2010. Air carrier operations were down 1.4 percent while commuter/air taxi operations declined 1.1 percent. Commercial operations in 2010 were 15.4 percent lower than their peak in 2005.

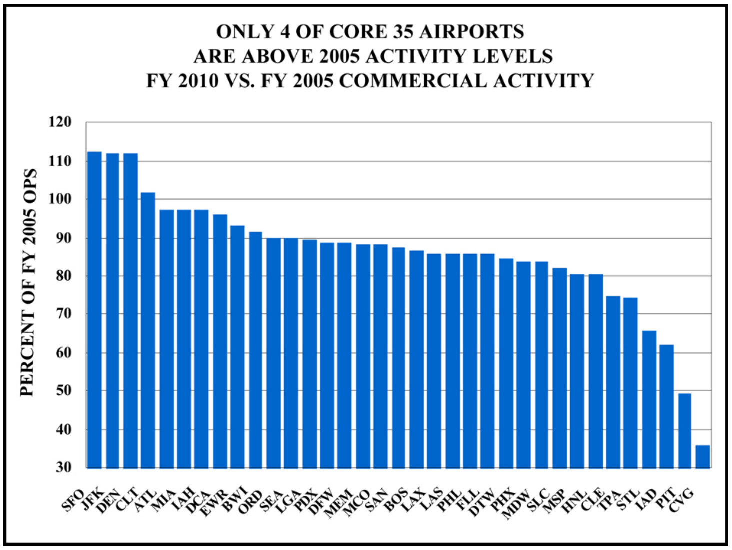
Non-commercial activity (the sum of general aviation and military) at combined FAA and contract towers fell by 4.6 percent in 2010, with general aviation activity (26.6 million) down 5.1 percent and military activity (2.6 million) up 0.9 percent. General aviation activity has declined in ten of the eleven years since 1999.

At the end of 2010, non-commercial aircraft activity was 31.8 percent below the activity in 2000.



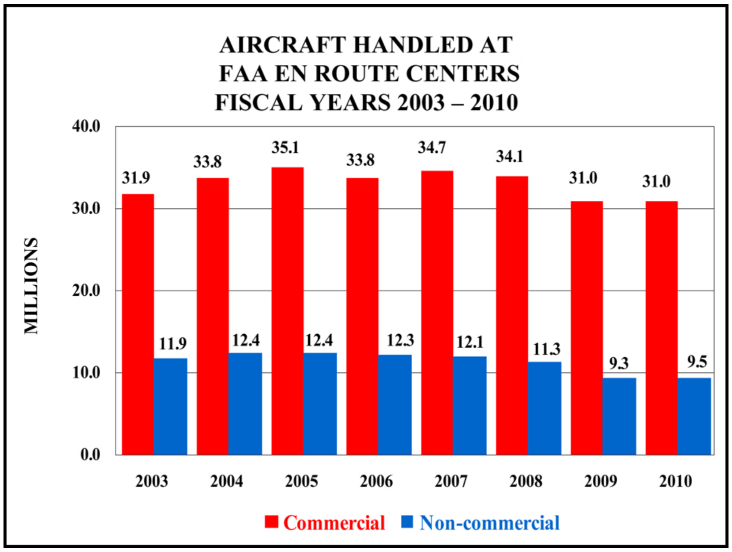
The FAA pays close attention to the trends occurring at the “Core 35” airports. These airports represent the top 35 airports in the country in terms of passenger activity (except PIT) and account for about 75 percent of commercial passengers. Commercial activity at the Core 35 airports peaked in 2005, but subsequent industry restructuring has resulted in a drop in combined commercial activity at these airports since. In 2010, commercial activity at the Core 35 airports fell by 1.0 percent from the previous year and was 12.9 percent below 2005 activity levels. Of the Core 35 airports, 21 recorded decreases in activity from 2009 with the largest declines occurring at Cincinnati (down 19.5 percent) and St. Louis (down 13.2 percent).

The largest increases in activity occurred at MIA (up 5.3 percent), and ORD (up 4.5 percent). Only 4 of the Core 35 airports exceeded 2005 peak activity levels during fiscal year 2010, unchanged from 2009, and down from 13 airports in 2008.



Since 2005 there has been a pronounced shift in demand which is reflected in the relative growth of commercial operations across the Core 35 airports. Commercial operations at San Francisco (up 12.5 percent), New York-Kennedy (up 12.2 percent), and Denver (up 12.1 percent), are up the greatest relative to their 2005 activity levels. Commercial operations at Cincinnati (down 64.1 percent), and Pittsburgh (down 50.5 percent) show the largest declines from 2005 levels. These activity level shifts reflect the impact of the restructuring of the airline industry. Delta's bankruptcy and subsequent merger with Northwest resulted in a consolidation of operations away from its Cincinnati hub, while the merger of US Airways and America West has led to a dramatic shrinking of US Airways' operations in Pittsburgh.

In 2010, total activity at FAA en route centers (40.5 million) increased 0.5 percent from the previous year. Commercial activity was relatively flat (down 0.02 percent), with air carrier operations down 0.3 percent and commuter/air taxi operations up 0.7 percent. Non-commercial activity was up 3.4 percent for the year as general aviation activity increased 3.4 percent and military activity decreased 0.4 percent. In 2010, air carrier operations were 10.6 percent below their 2000 activity levels and air taxi/commuter operations were 6.4 percent above activity levels for 2000. Operations for the general aviation and military user groups were 25.1 and 28.9 percent below their 2000 activity levels, respectively.


AIRCRAFT HANDLED AT
FAA EN ROUTE CENTERS
FISCAL YEARS 2003 – 2010
MILLIONS
40.0
30.0
20.0
10.0
0.0
31.9
33.8
35.1
33.8
34.7
34.1
31.0
31.0
11.9
12.4
12.4
12.3
12.1
11.3
9.3
9.5
2003
2004
2005
2006
2007
2008
2009
2010
Commercial
Non-commercial