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Free Hobby Executive Summary



The Southwest Effect

- The “Southwest Effect” is alive and well. History shows that lower pricing drives demand. (*Free Hobby Report, p 2, Moody’s, p 1 & 4*)
- Low Fare stimulation creates a bigger passenger pie for all. (*Free Hobby Report, p 9 & 10*)
- Monopoly fares at IAH are significantly higher than fares in markets that compete with Southwest at Hobby. (*Campbell-Hill Traffic Forecast, p 3 & 4, Free Hobby Report, p 5, 6 & 7*)
- Houston travelers will save approximately \$255 million per year due to lower fares. (*Campbell-Hill Traffic Forecast, p 8*)
- Campbell-Hill projects that 2 million additional passengers will be created by Southwest’s international service at Hobby – 1.95 million at Hobby and 50,000 at IAH. This is comprised of 1.4 million increased local travelers and .6 million new connecting passengers. (*Campbell-Hill Traffic Forecast, p 7 & 8*)
- Conservative fare assumptions drive this conclusion. Both Hobby and IAH projected increases are in addition to normal growth, and are driven by competitive pricing. (*Campbell-Hill Traffic Forecast, p 7*)

Missed Opportunities

- Value minded passengers are already flying out of Hobby to international destinations. They do this by flying to other hubs such as DFW and Atlanta in their quest for value. (*Free Hobby Report, p 12*)
- Low fare passengers are presently lost to other Cities. These lost passengers will be reclaimed, thereby increasing Houston’s competitive position. (*Campbell-Hill Traffic Forecast, p 7, Table 5*)
- A market exists – Miami and Ft. Lauderdale - that is similar to the Hobby/IAH proposal and sheds light on what will happen in Houston with lower fares and competition. While Spirit Airlines has grown at Ft. Lauderdale, American Airlines has also grown at Miami. (*The Boyd Report, p 5*)

Outdated Arguments

- United Airlines retained William Swelbar to predict the consequences of competition. Mr. Swelbar has predicted traffic shifts and loss of service at IAH. Mr. Swelbar made similar predictions in 2005 concerning Dallas Love Field as part of an analysis of the Wright Amendment impacts to DFW and American Airlines. Despite his dire assessment, American Airlines increased or maintained service to 15 of 18 markets Mr. Swelbar predicted would shrink. American matched fares, and Dallas traffic grew significantly. (*Wright Amendment testimony to Congress*)

Costs are Covered

- Houston taxpayers will not be at risk. An existing Use and Lease Agreement covers operations and capital improvements at Hobby Airport. This agreement anticipates expansion, as does the Hobby Master Plan.

**TRAFFIC FORECAST AND FARE SAVINGS FROM
HOUSTON HOBBY – LATIN AMERICA/CARIBBEAN
LOW-FARE SERVICE**

Prepared for:



Prepared by:



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HIGHLIGHTS

- United's monopoly position at IAH in most of its international and domestic markets has caused airfares to be significantly higher than in markets where it competes with Southwest at Hobby.
- Southwest's projected Latin America/Caribbean service will generate 2.0 million more Houston passengers in 2020 - 1.95 million at Hobby and 50,000 at Intercontinental. Local Houston residents and visitors will account for 1.17 million of Hobby's new passengers and 780,000 will be connecting at Houston to or from other cities.
- Campbell-Hill's forecast, using conservative assumptions, of 2.0 million additional Houston passengers due to Southwest's new service and competition at HOU is 27% higher than the HAS forecast of 1.57 million passengers. Campbell-Hill's analysis was conducted completely independent of the HAS study.
- IAH will gain approximately 50,000 additional passengers in 2020 over and above expected growth, due to the increased traffic that will be stimulated by lower international airfares at both Houston airports.
- Travelers in Houston international markets will receive approximately \$255 million per year in fare savings as a direct result of Southwest's new service - \$84 million for Hobby passengers and \$171 million for IAH passengers.
- Passengers travelling to and from points outside Houston but connecting at Hobby and IAH will obtain an additional \$54 million in annual fare savings.
- Lower fares inspired by Southwest will divert traffic from other U.S. connecting gateways to both Hobby and IAH, thereby making Houston more competitive for flow traffic to Latin America and the Caribbean.

INTRODUCTION

The Campbell-Hill Aviation Group (“Campbell-Hill”)¹ has been retained by Southwest Airlines to analyze market responses and consumer benefits that would flow from Southwest’s projected expansion at Houston Hobby Airport into Latin America and Caribbean markets. This analysis includes detailed traffic forecasts for both 2017 and 2020, including projections for Houston Hobby (HOU), Houston Intercontinental (IAH), as well as connecting passengers originating or terminating at points outside Houston that will use one of the Houston airports as the gateway to their final destination. For the sake of brevity only the 2020 results are shown in the main body of this report, although forecast data for both 2017 and 2020 are presented in Appendix A. The analytical methodology and significant assumptions are described in Appendix B.

Campbell-Hill selected the new international markets likely to be served based on its industry expertise and after consultation with Southwest. Designation of daily frequency and aircraft type was determined by Campbell-Hill for the purpose of this study.

The Campbell-Hill analysis was conducted completely independent of the recent HAS study.² Campbell-Hill’s passenger forecasts utilize a different methodology and different analytical assumptions than HAS. However, Campbell-Hill’s analysis incorporates widely accepted sources of input data and methodology the firm has utilized in numerous studies. In brief, Campbell-Hill’s traffic forecasts are a little higher than the HAS estimates, and by comparison the HAS results are conservative. Campbell-Hill has extended the analysis to estimate the annual fare savings by Houston residents and visitors who use both airports. Connecting passenger volumes and fare savings by all passengers are included in the Campbell-Hill analysis as well.

¹ Campbell-Hill was formed in 1993 to serve airline and airport clients along with other enterprises and government agencies with interests in commercial aviation. Several of our senior staff have substantial operating experience at U.S. airlines including Delta, US Airways, United, Northwest, AirTran and Midway Airlines. Campbell-Hill serves many airports in their efforts to obtain additional domestic and international air service. These clients include Austin, San Diego, Portland, Or., Milwaukee, Pittsburgh, Hartford, Baltimore-Washington International, West Palm Beach and Richmond. Campbell-Hill prepared the 2003 Economic Impact Study for the Houston Airport System and is very familiar with HAS economic studies.

² Prepared by InterVISTAS and GRA, published March 26, 2012.

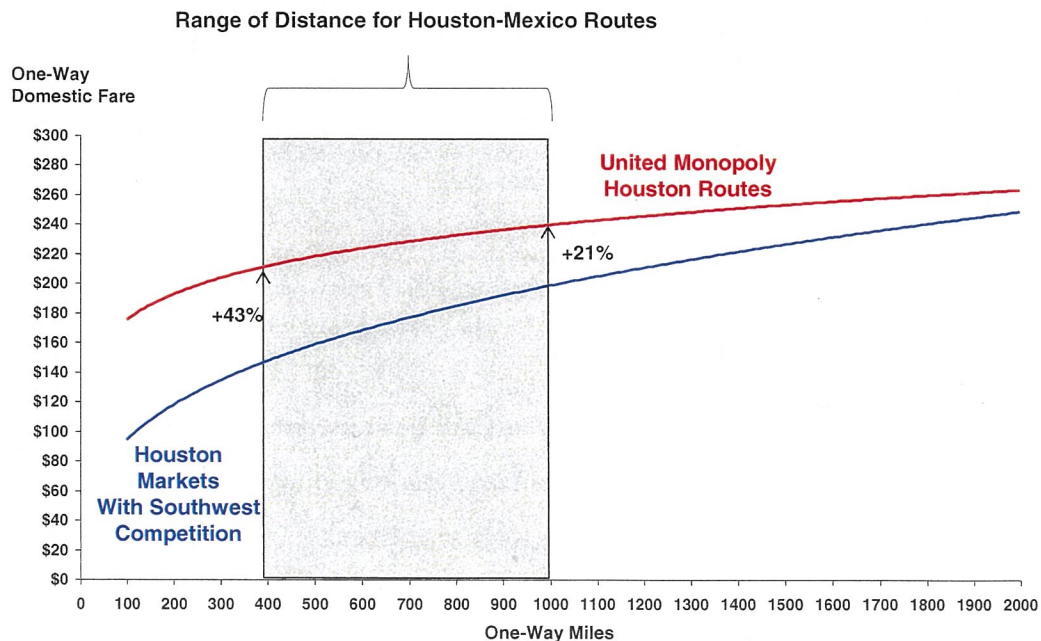
FINDINGS AND CONCLUSIONS

Framework of Competition

United heavily dominates domestic air service at IAH. Currently it provides 90% of all domestic flights and 88% of the seat capacity³. At Hobby, Southwest serves 34 domestic nonstop markets in competition with United at IAH. The disciplining effect Southwest has on United's pricing is clear and obvious. Chart 1 shows that United's Houston fares in markets where it does not compete with Southwest are significantly higher than in markets where it does compete with Southwest. The presence of Southwest in head-to-head competition with United drives down United's fares significantly.

Chart 1

Southwest's Presence Reduces One-Way Domestic Fares By Over \$50 In Domestic Markets with Distances Comparable to Houston-Mexico Markets



Note: Fared passengers only. Excludes all taxes and government charges.

Includes all Houston domestic markets with 600 or more one-way flights for 12 months ended September, 2011.

Source: U.S. DOT, O&D Survey and Schedule data, 12 months ended September, 2011, via Diio, LLC.

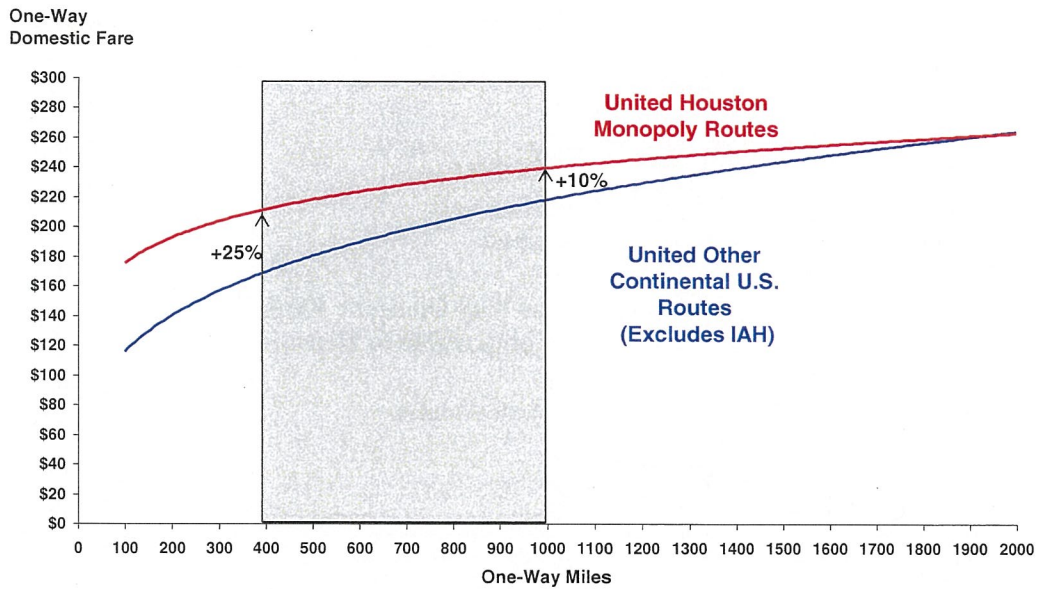
It is also important to note that United's fares in domestic monopoly routes at IAH are significantly higher than the fares it charges in the rest of the U.S. The fare disparity is

³ Based on June, 2012 published schedules.

particularly acute for markets under 1,000 miles (Chart 2) – for example charging an average of 25% more in markets of 400 miles distance.

Chart 2

United Charges Higher Domestic Fares in Houston Monopoly Markets Than Its Typical Fares from Other U.S. Airports



Note: Fared passengers only. Excludes all taxes and government charges.

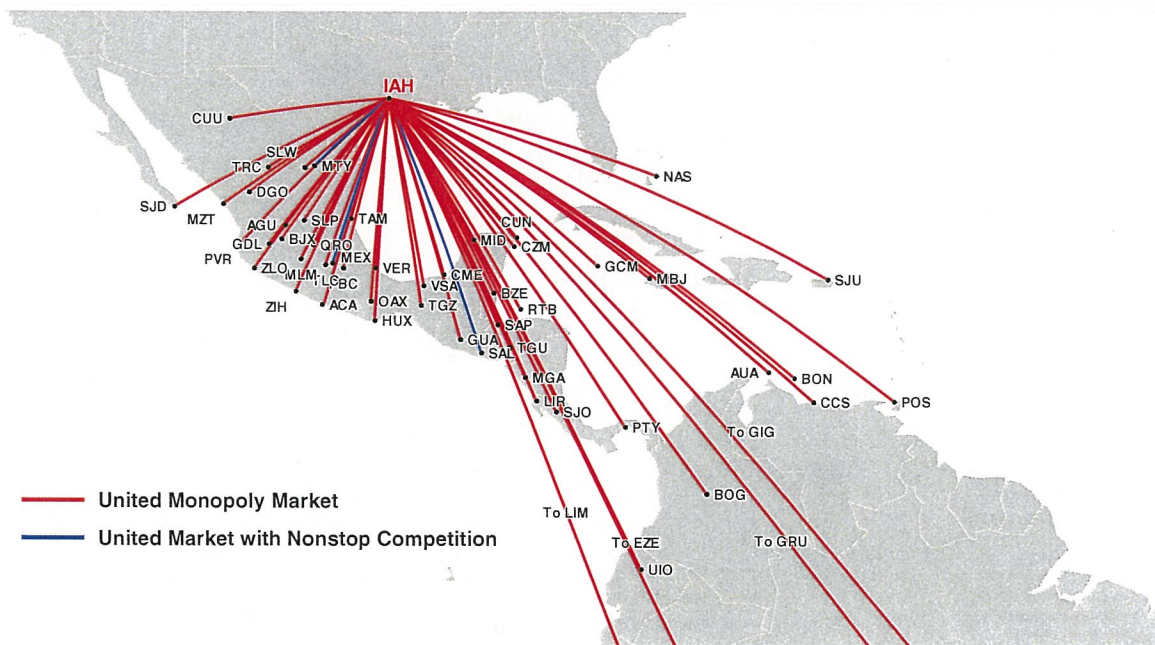
Includes all Houston domestic markets with 600 or more one-way flights for 12 months ended September, 2011.

Source: U.S. DOT, O&D Survey and Schedule data, 12 months ended September, 2011, via Diio, LLC.

United serves 54 Houston – Latin America/Caribbean markets and 51 of them are United monopolies (Chart 3). United’s average fares in these markets are typically very high, given the lack of any nonstop competition by either US or foreign airlines.

Chart 3

51 of 54 Latin America and Caribbean Markets Served by United from Houston Are Monopolies

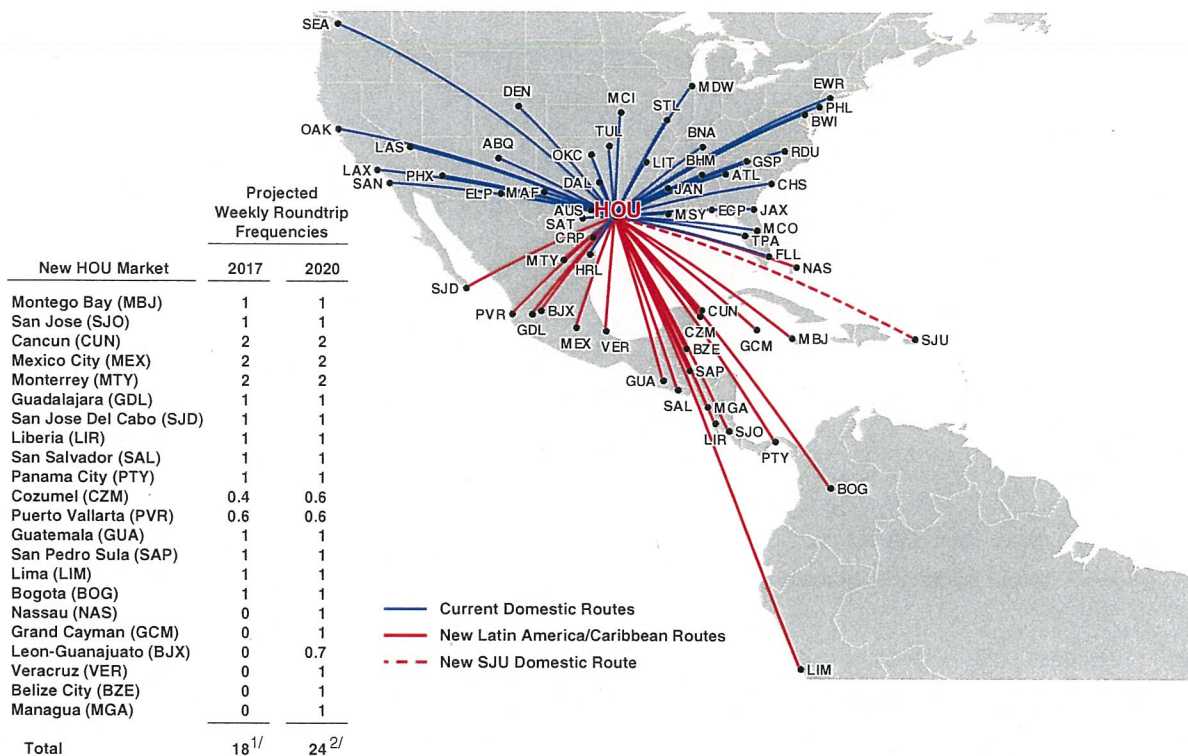


Source: OAG Schedule Data, June 2012, via Diio, LLC.

Southwest plans to begin service from Houston Hobby to Latin America/Caribbean destinations in 2015. Campbell-Hill understands that to support this expansion at Hobby Southwest will make its own investment in the required infrastructure (gates and related facilities). The Southwest pattern of service will build toward a developed profile by 2020 at which time it is expected that Southwest will serve approximately 22 nonstop markets with 25 round trips per day (Chart 4).

Chart 4

Projected Southwest Airlines New Hobby – Latin America/Caribbean Markets



1/ 19 peak day departures.

2/ 25 peak day departures.

Southwest’s low-fare high-quality service will cause United’s and other competitors’ fares to decline significantly, thereby stimulating new passenger travel to/from Houston. It will also divert connecting passengers (e.g. Kansas City-Cancun) to Houston from other U.S. gateways like Dallas, Los Angeles and Miami.

The fundamental issue to be decided by the City of Houston is whether or not it wants to allow competition to United’s international service. To help enlighten this issue Campbell-Hill (1) forecast traffic at both Houston airports in all the relevant Southwest Latin America/Caribbean markets,⁴ (2) derived the impacts on IAH and, (3) estimated the annual fare savings for passengers at both airports.

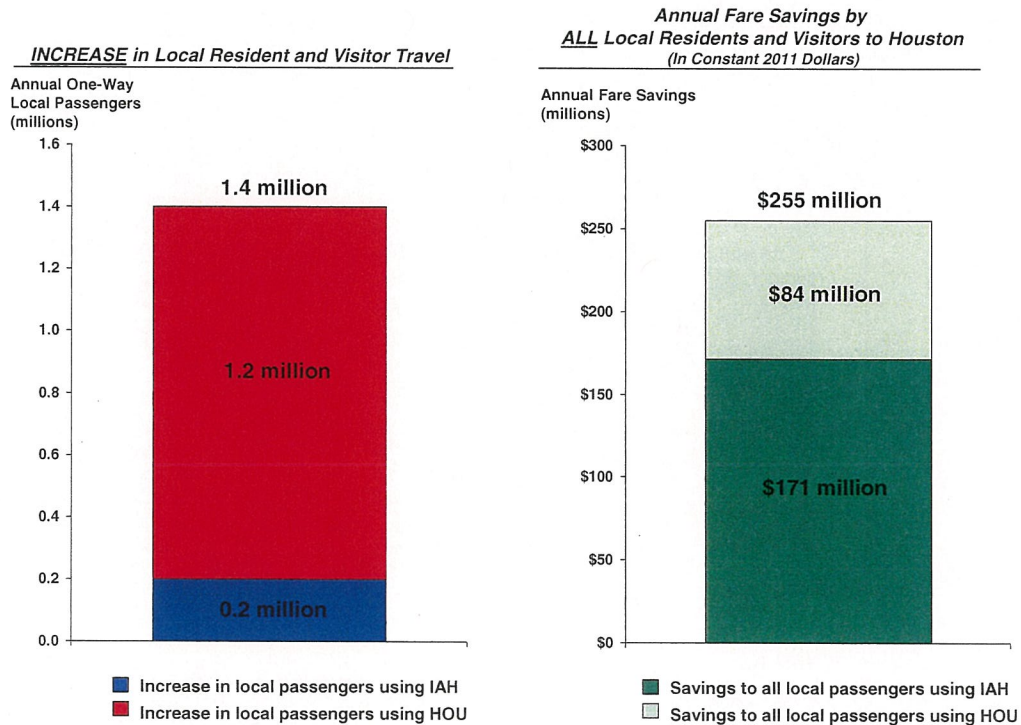
⁴ All traffic forecasts were prepared by Campbell-Hill at the individual city-pair level and then aggregated for purposes of this written report.

Forecast Results and Fare Savings

For the year 2020 (full schedule development) Southwest's international service at Hobby will generate 1.4 million additional local passengers⁵ in the 22 new Southwest markets. HOU will handle 1.2 million and IAH will experience a net increase in local traffic of 0.2 million passengers. This incremental traffic is over and above the volume of passengers that Houston could expect with normal growth, and without Southwest in the markets (Chart 5).

Chart 5

Increased Local Houston Passenger Traffic and Fare Savings in 2020 Due to Southwest's HOU – Latin America/Caribbean Service



Southwest's low fares⁶ will cause United and other IAH carriers to reduce their fares in response. For purposes of this analysis, Campbell-Hill has conservatively assumed that

⁵ Houston residents plus visitors to Houston from one of the Latin America/Caribbean cities to be served by Southwest. Visitors spend time in Houston and then return home. They are not passengers who merely "connect" at a Houston airport.

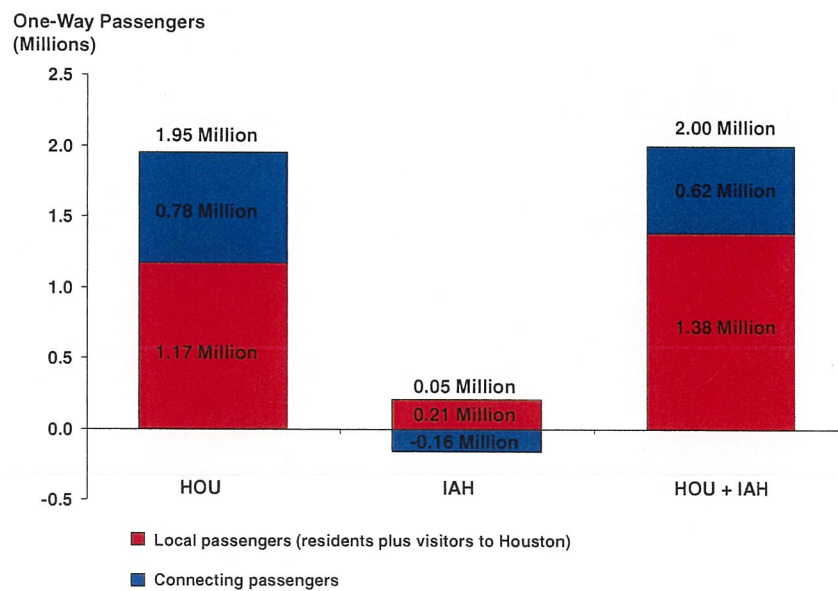
⁶ Campbell-Hill estimated Southwest fares by constructing Southwest's HOU fare curve and adding an assumed \$15 per passenger to account for higher expected costs in these international markets.

competitors will not reduce all their fares to Southwest’s level, but only partially match Southwest.⁷ Under that assumption Campbell-Hill estimates that local Houston passengers using IAH in 2020 will save \$171 million and those using HOU will save \$84 million. The total savings for all Houston passengers will be \$255 million (Chart 5).⁸

In addition to generating more *local* passengers at Houston’s airports, Southwest’s international service will produce over 600,000 net additional *connecting* passengers at the two airports.⁹ Consequently, the total increase in 2020 passengers at the Houston airports will be 2.0 million – 1.95 million at Hobby and 50,000 at IAH (Chart 6).

Chart 6

The Houston Airports Will Gain 2.0 Million Additional Passengers in 2020 as a Result of Southwest’s Latin America/Caribbean Service



⁷ Campbell-Hill determined the relationship between Houston domestic fares where other carriers compete with Southwest, and the fares in markets where they do not compete with Southwest. This relationship allows Campbell-Hill to construct the “market” fare after Southwest’s entry in the relevant new markets.

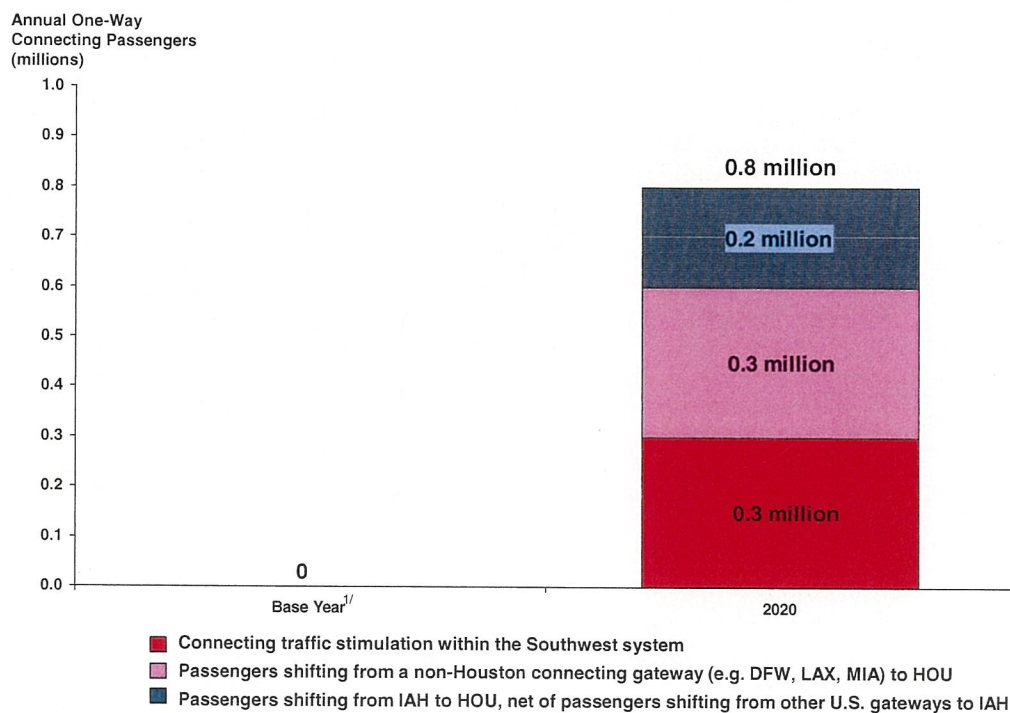
⁸ All dollar amounts for future fare savings are expressed in 2011 constant dollars throughout this study.

⁹ 781,000 additional connecting passengers at HOU, less 164,000 shifted from IAH.

Southwest's service and fares will also make Houston more competitive with other U.S. gateways to Latin America and the Caribbean. Because of Southwest's new service and the fare reductions it will spawn, Campbell-Hill forecasts that Hobby will gain approximately 781,000 new connecting passengers traveling to and from other cities (Chart 7).

Chart 7

Southwest's New Service Will Make Houston More Competitive With Other U.S. Gateways and Generate Nearly 800,000 Connecting Passengers at Hobby by 2020

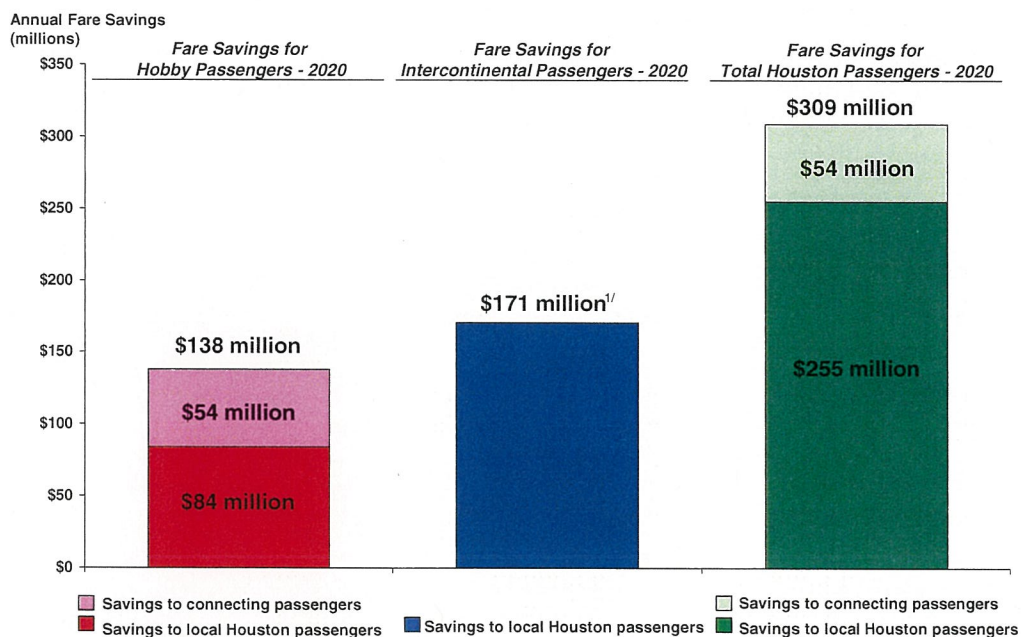


^{1/} 12 months ended September 2011

In addition, connecting passengers using the Houston airports will obtain \$54 million in fare savings in 2020 (Chart 8).

Chart 8

Fare Savings by All Passengers Using the Houston Airports Will Exceed \$300 Million From the Projected Southwest Latin America/Caribbean Service (In Constant 2011 Dollars)



1/ It is conservatively assumed that other airlines do not reduce their fares in connecting markets in response to Southwest. Consequently, we do not forecast fare savings for passengers connecting at IAH.

Diversion From IAH

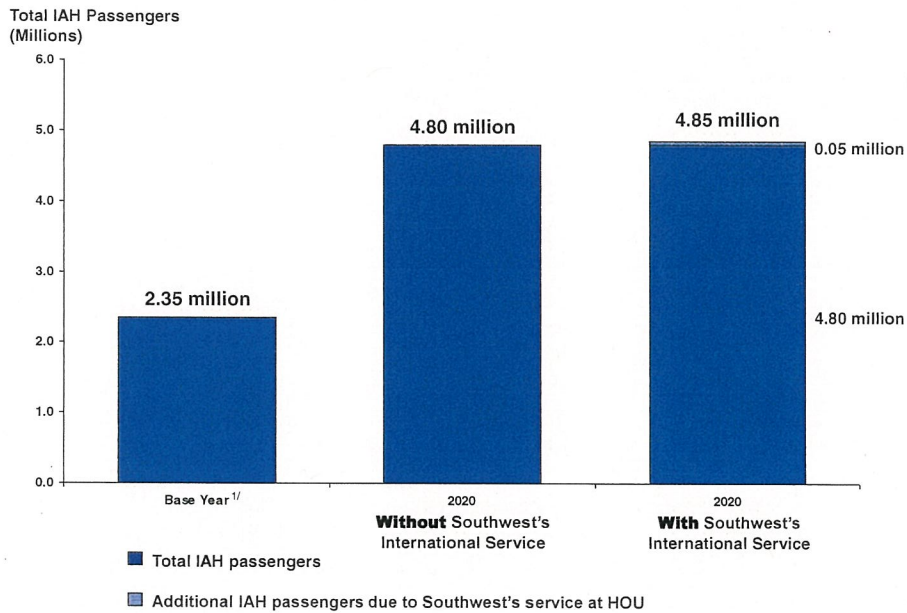
In the base year¹⁰ IAH handled 2.4 million passengers to/from the 22 Latin America/Caribbean cities that Southwest is expected to serve. Campbell-Hill projects this volume of traffic to increase to 4.8 million passengers in 2020 under status quo conditions, without new service by Southwest. However, Southwest’s new service and lower fares will cause competing carriers to reduce their fares, and both HOU and IAH will experience an increase in passengers as a result. The vast majority of the new passengers will use Hobby, but

¹⁰ 12 months ended September, 2011.

on balance IAH will gain approximately 50,000 more passengers in the year 2020 because of Southwest's initiative (Chart 9). IAH will suffer no net diversion as a result of Southwest's Latin America/Caribbean services.

Chart 9

IAH Passengers in 2020 Will Be 50,000 Greater as a Result of Southwest's Latin America/Caribbean Service



1/ 12 Months ended September 2011.

It is very clear that if United competes with Southwest's fares in international Houston markets, as it does in 34 domestic Houston markets, it will increase its total Latin America/Caribbean traffic; it will suffer no net diversion; and it will not need to eliminate any of its IAH domestic service.

**Forecast Passengers and Fare Savings In the Relevant
Southwest Latin America/Caribbean Markets**

	HOU			IAH			Total Houston		
	Base Year ¹	2017	2020	Base Year ¹	2017	2020	Base Year ¹	2017	2020
1. Total Passengers									
Local	0	902,862	1,168,588	1,166,403	1,893,580	2,591,930	1,166,403	2,796,442	3,760,518
Connecting	0	597,805	780,999	1,186,207	1,772,958	2,256,973	1,186,207	2,370,763	3,037,972
Total	0	1,500,667	1,949,587	2,352,610	3,666,538	4,848,903	2,352,610	5,167,205	6,798,490

2. Fare Savings (Millions of Constant 2011 Dollars)

Local									
Current and Growth Passengers		\$34	\$51		\$82	\$118		\$116	\$169
Newly Generated Passengers		\$24	\$33		\$35	\$53		\$59	\$86
Total Local		\$58	\$84		\$117	\$171		\$175	\$255
Connecting									
Current and Growth Passengers		\$28	\$38		\$0	\$0		\$28	\$38
Newly Generated Passengers		\$12	\$16		\$0	\$0		\$12	\$16
Total Connecting		\$40	\$54		\$0	\$0		\$40	\$54
Total									
Current and Growth Passengers		\$62	\$89		\$82	\$118		\$144	\$207
Newly Generated Passengers		\$36	\$49		\$35	\$53		\$71	\$102
Total		\$98	\$138		\$117	\$171		\$215	\$309

3. HOU Connecting Passenger Sources

Passengers within Southwest's System	215,462	291,301
Passengers Shifting from Non-Houston Gateways	257,701	325,674
Passengers Shifting from IAH to HOU	124,642	164,024
	597,805	780,999

4. IAH Stimulation, Growth and Diversion

	2017	2020
Local		
Growth	699,115	1,211,301
Stimulation	28,062	214,226
Total	727,177	1,425,527
Connecting		
Without Southwest	711,393	1,234,790
Less: Diversion to Southwest	124,642	164,024
Total	586,751	1,070,766
Total	1,313,928	2,496,293

1/ 12 Months ended September 2011.

Analytical Methodology

The traffic forecasts and fare savings estimates associated with Southwest's projected new international services at Hobby are based on publicly available government statistics and standard forecasting techniques for aviation analysis. The Campbell-Hill forecasting model combines current year passenger and fare data, historical traffic growth trends, and projected fare changes derived from patterns in domestic Houston markets with competitive Southwest services. The following sections describe the methodology and significant assumptions.

1. Selection of New International Markets

Campbell-Hill selected 22 Latin American and Caribbean markets as most likely for Southwest entry based on the Firm's knowledge of the airline industry as well as discussion with Southwest Airlines. Campbell-Hill assumed that Southwest's service in most of the markets would be one roundtrip per day. Exceptions are CUN, MEX, and MTY with two roundtrips per day, and CZM, PVR, and BJX with less than daily service.¹¹ Campbell-Hill assumed that Southwest would utilize the 175-seat B737-800 for both daily services in the HOU-CUN and HOU-MEX markets. All other schedules were assumed to use the 137-seat B737-700.

2. Local Market Traffic Forecasts

2a. Base Year¹² Local Houston Traffic and Fares

The number of passengers¹³ traveling between Houston (IAH and HOU combined) and the 22 Latin America/Caribbean markets¹⁴ was determined by aggregating the most recent U.S. Department of Transportation O&D Survey data (YE 2011 Q3¹⁵) with U.S. DOT T-100 data to arrive at total market sizes including both U.S. and foreign flag carriers.

Forecast traffic for CY 2017 and CY 2020 was based on CY 2003 to YE 2011 Q3 compound annual growth rates (CAGR) for each of the 22 markets. The annual growth rate was

¹¹ The markets selected for less than daily departures were those with low projected overall load factors after an initial model run using one daily departure.

¹² 12 months ending September, 2011.

¹³ For purposes of this study, Campbell-Hill has excluded wherever possible frequent flier redemptions and pass riders in order to reflect only revenue passengers.

¹⁴ TLC was combined with MEX as part of the Mexico City market.

¹⁵ Unless otherwise specified, "current," or "base year" market statistics are based on the 12 months ending September 30, 2011. The passenger data used in this report has been compiled by Diio, LLC in its Diio Mi product.

constrained to 10% per year for large markets and 20% per year for small markets (those without nonstop service in 2003). On average, the constrained historical growth rate used to prepare the forecast was approximately 9% per year.

Current average fare levels were estimated from the DOT O&D Survey data for U.S.-flag passengers¹⁶. It was assumed for purposes of the forecast that the average fares of foreign flag carriers were the same as those for U.S. carriers.

2b. Service Stimulation for Local Traffic

The addition of new non-stop service in the 22 markets will stimulate new local traffic quite apart from fare changes. The new service levels (with Southwest flights) were compared to existing service levels using a standard DOT “quality of service index” (QSI) formula:

$$\text{Stimulation} = ((\text{With WN QSI}/\text{Current QSI})/(0.3741 + 0.5561(\text{With WN QSI}/\text{Current QSI}))/1.075$$

The service stimulation model was applied to the forecast Houston local traffic. On average, traffic was stimulated from 8% to 27%, depending on the individual market. The average service stimulation was 13%.

2c. Price Stimulation and Forecast Fare Savings

The introduction of lower Southwest fares into these international markets will influence other carriers’ fare decisions, cause a reduction in overall fares, and stimulate new passenger traffic. The projected average market fare for each of the 22 new local markets, giving effect to Southwest’s lower fares, was based on a yield curve derived for UA/CO non-stop domestic Houston routes with significant Southwest competition.¹⁷ The fare amount was derived from the yield curve which relates yield to nonstop distance. Campbell-Hill added \$15 to each one-way fare to account for potential higher costs in foreign countries in which Southwest would initially have a small operational footprint.

¹⁶ The fares examined for this study have been adjusted by Diiio, LLC to exclude government taxes and fees. U.S. DOT does not permit the disclosure of international fares on a market-level.

¹⁷ Competitive markets were defined as UA/CO non-stop markets in which Southwest also had over 300 roundtrip departures for YE 2011 Q3 at Hobby.

The Campbell-Hill analysis estimates that the entry of Southwest will reduce the average one-way Houston fare to the combined 22 international markets from \$273 to \$202 – an average decline of 26%. The calculation of fare stimulation, as a result of lower fares, assumed an elasticity of -1.2¹⁸, constraining the fare-stimulated traffic growth to a maximum of 150% for any market.¹⁹ Fare stimulation averaged 58% for the combined Houston markets.

The distribution of traffic impacts between HOU and IAH was based on assumptions for Southwest traffic levels and the expected response of competing carriers. Southwest's traffic levels were initially assumed using an 80% load factor, with 60.9% of the onboard traffic expected to be local passengers (based on Southwest's current mix at HOU). Southwest's local traffic for each market was capped at a maximum of 67% of the total market after stimulation (with residual traffic remaining at IAH).

Fare savings were calculated using the FAA's "consumer benefit" methodology. Fare savings for projected existing passengers (i.e., passengers that would travel even without the new Southwest service) are calculated based on the difference between the current fare and the projected market fare with Southwest service. Fare savings for new or stimulated traffic were calculated using half of the fare differences, consistent with FAA's methodology.²⁰

3. Connecting Market Forecasts

3a. Baseline Flow Traffic and Fares

An initial set of connecting markets included all airports²¹ served non-stop by Southwest to/from HOU, combined with each of the 22 markets. Circuitous markets for which Houston airports account for less than 1% of all current traffic were eliminated from this initial list. The flow traffic available for diversion to HOU was limited to connecting passengers which totaled

¹⁸ This is the composite elasticity for business and leisure travel recommended by the FAA. See "FAA Airport Benefit-Cost Analysis Guidance", Office of Aviation Policy and Planning, Federal Aviation Administration, December 15, 1999.

¹⁹ Fare stimulation was calculated using the arc elasticity formula:

$$E_p(-1.2) = [(Q2-Q1)/((Q1+Q2)/2)] / [(P2-P1)/((P1+P2)/2)],$$

where Q1 = passengers before WN service, Q2 = Passengers after WN service,

P1=Fare Before WN service, P2 = Fare After WN service

²⁰ The FAA's "consumer surplus" methodology assumes all existing passengers would benefit by the full amount of average fare savings, while stimulated passengers would benefit in a range between 0% and 100% of the net change in fares, or an average of 50%. See, "FAA Airport Benefit-Cost Analysis Guidance", Office of Aviation Policy and Planning, Federal Aviation Administration, December 15, 1999.

²¹ Markets were limited to the Southwest airport markets and excluded traffic via other airports in multi-airport metropolitan areas (e.g., ORD in Chicago).

3.7 million in the base period. This includes 1.2 million passengers currently connecting at IAH.²² Average fares for the connecting passengers in each market were used as the baseline market fares.

Forecast traffic for CY 2017 and CY 2020 was based on the CY 2003 to YE 2011 Q3 compound annual growth rates for each of the connecting markets, assuming a maximum annual growth rate of 20% per year. Growth averaged 9% per year for all of the markets combined. While new connecting options via HOU would have some traffic impacts, no service stimulation was incorporated for flow traffic.

3b. Price Stimulation and Forecast Fare Savings

Campbell-Hill's predicted one-way fares for the new Southwest services were based on the current yield curve for Southwest's domestic connecting markets, plus \$15 to allow for potentially higher foreign operating costs. The predicted one-way average fare for connecting traffic available for diversion to HOU is \$203, which is 27% less than the current \$277 average fare for the same passengers. Campbell-Hill conservatively assumed that other carriers would not reduce their *connecting* fare levels in response to Southwest.

After fare stimulation is applied, (using the price elasticity coefficient of -1.2), the growth in connecting market traffic over HOU was 291,000 new passengers.

Southwest's total flow traffic for each market combines all of the stimulated traffic (which is assumed to move via the new Southwest flights) with traffic diverted from current gateways. Any diversion traffic was subtracted from the IAH flow traffic in proportion to IAH's current share of flow traffic for each market (164,000 passengers were diverted from IAH). However, as explained in our report, IAH will not suffer a net diversion of traffic because stimulation from low fare service from Southwest will outweigh the diversion of connecting passengers. In fact, on balance IAH will have 50,000 more passengers in the year 2020 because of Southwest's effect of lowering Houston fares.

Fare savings for projected existing passengers are calculated based on the difference between the current average fare and the projected Southwest fare, as applied to all of

²² Nonstop traffic (including foreign flag) was assumed to be unaffected by the new Southwest service and was excluded from the (1) traffic levels available for diversion, and (2) average fare calculations.

Southwest's diversion traffic. Fare savings for all new or stimulated traffic via both Houston airports was calculated using half of the derived fare differences, as explained earlier.

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Southwest Effect is Alive and Well

Destination	Southwest Start Service	Total Houston Market			UA in IAH	
		% Chg Passengers	% Chg Avg Fare	% Chg Passengers	% Chg Avg Fare	
Denver, CO	July, 2006	34	-22	+19	-20	
Panama City, FL*	January, 2010	121	-28	N/A	N/A	
Charleston, SC	March, 2011	53	-18	-2	-15	
Greenville, SC	March, 2011	139	-22	21	-13	
Newark, NJ	June, 2011	38	-8	17	-4	
Above Destinations Combined	After One Year of Southwest Service →	+41%	-15%	+18%	-16%	

*UA/CO has not served Panama City, FL from either PFN nor ECP

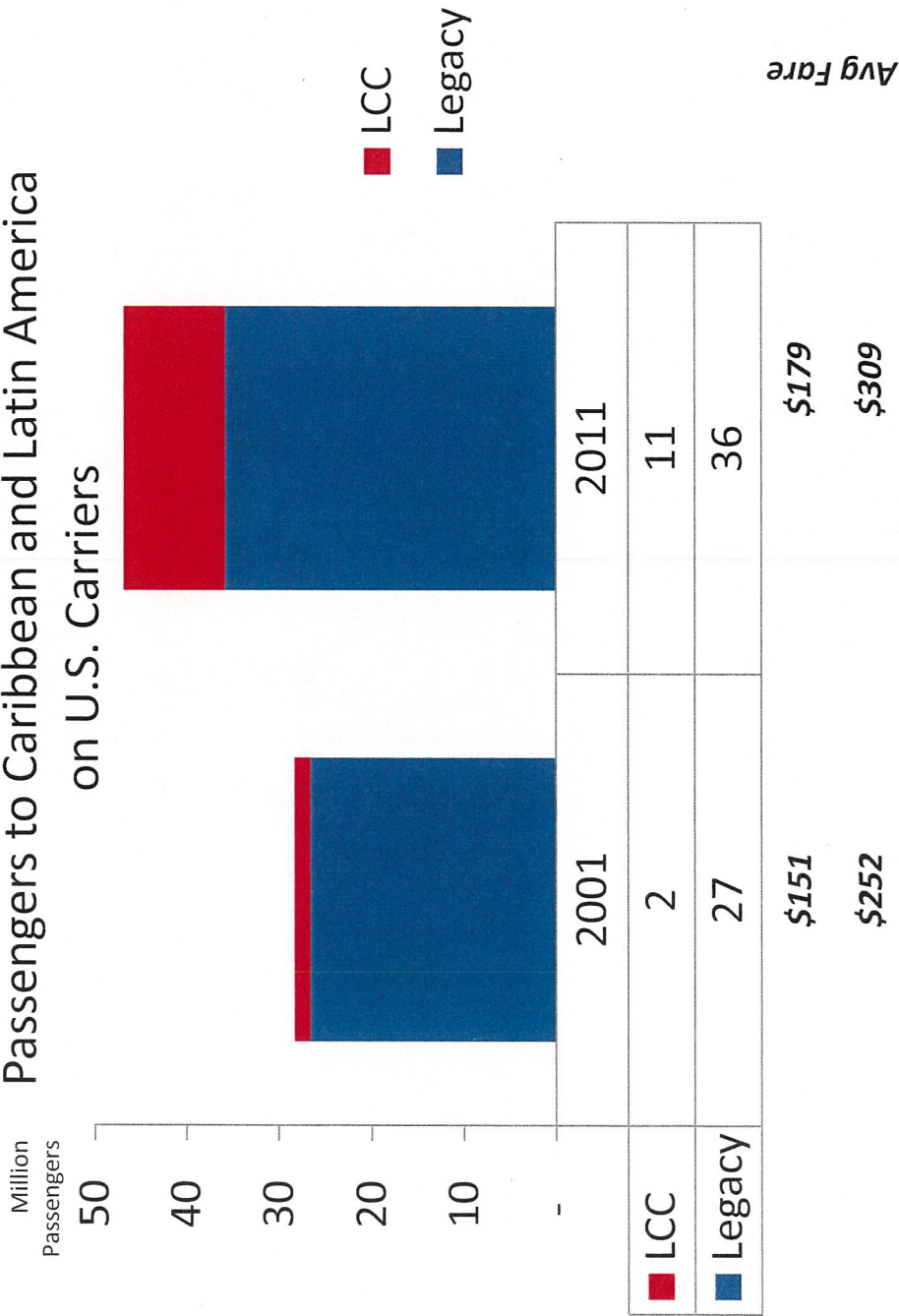


FREE HOBBY



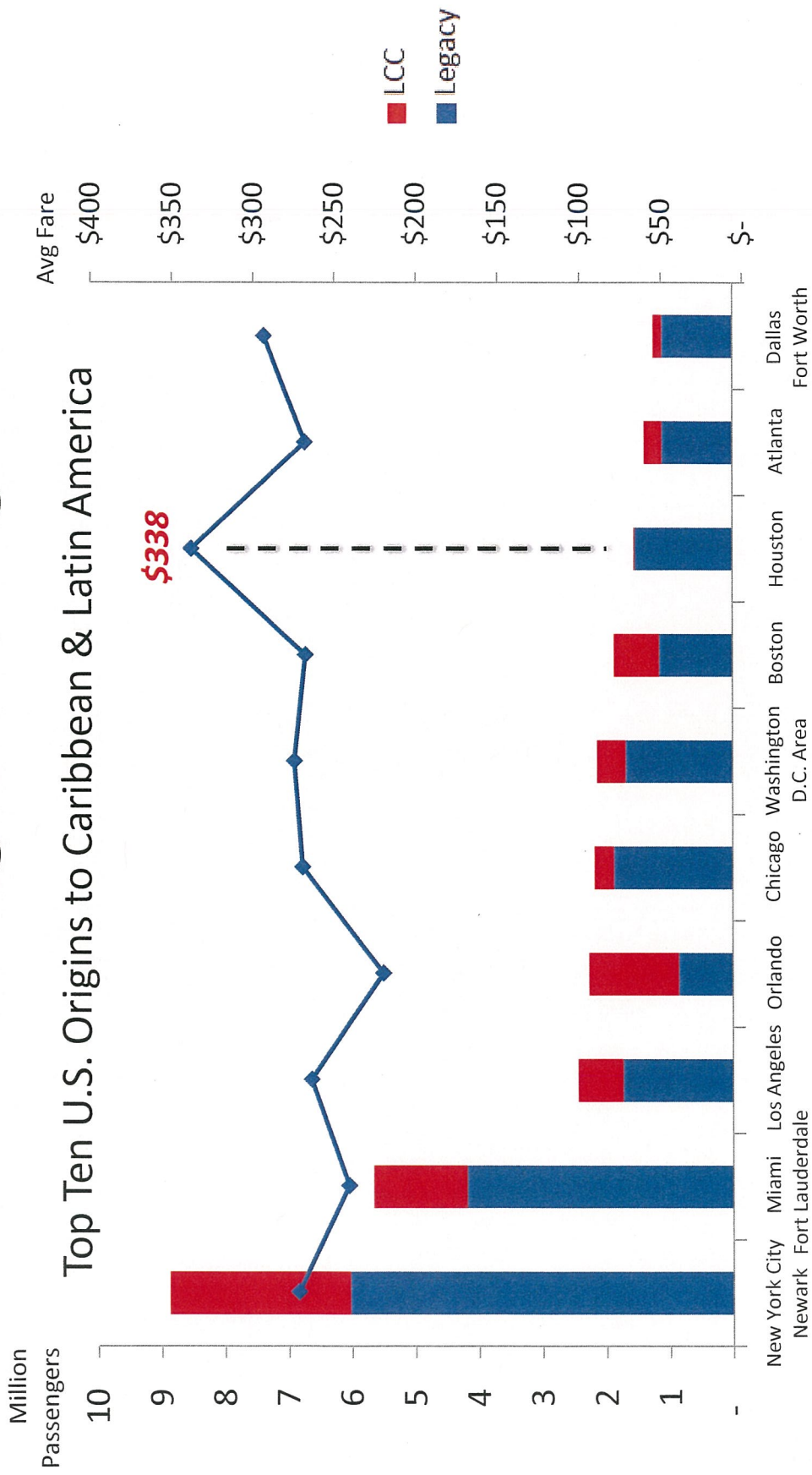
U.S. Air Travel has Grown Due to Lower Fares

Passengers to Caribbean and Latin America on U.S. Carriers



FREE HOBBY

Houston has Highest Average Fare



FREE HOBBY



United Houston Fare Premiums Over Southwest

Direct Competition: Southwest Nonstop Markets vs United Nonstop Markets

Houston Market	Mileage	Southwest Fare	Southwest Fare with Bag/Chg Fees	United Fare	United Fare with Bag/Chg Fees	United Fare Premium over Southwest	United Fare Premium with Bag/Chg Fees over Southwest
Dallas Love	239	\$ 127	\$ 128	\$ 125	\$ 140	-2%	10%
New Orleans	303	\$ 130	\$ 130	\$ 146	\$ 161	12%	23%
Chicago	937	\$ 160	\$ 160	\$ 202	\$ 217	26%	35%
Las Vegas	1235	\$ 148	\$ 149	\$ 186	\$ 201	25%	35%
Los Angeles	1390	\$ 172	\$ 173	\$ 233	\$ 248	35%	44%
Denver	883	\$ 121	\$ 121	\$ 164	\$ 179	36%	48%
Harlingen	276	\$ 83	\$ 83	\$ 119	\$ 134	44%	62%
Baltimore	1246	\$ 180	\$ 180	\$ 205	\$ 220	14%	22%
St. Louis	687	\$ 166	\$ 166	\$ 197	\$ 212	19%	28%
Orlando	848	\$ 174	\$ 174	\$ 180	\$ 195	4%	12%
Oklahoma City	419	\$ 144	\$ 144	\$ 224	\$ 239	56%	66%
Tulsa	453	\$ 150	\$ 151	\$ 220	\$ 235	46%	56%
Nashville	670	\$ 172	\$ 172	\$ 200	\$ 215	16%	25%
Phoenix	1020	\$ 169	\$ 169	\$ 183	\$ 198	8%	17%
San Diego	1312	\$ 170	\$ 171	\$ 209	\$ 224	23%	31%
Midland/Odessa	441	\$ 142	\$ 142	\$ 170	\$ 185	20%	30%
El Paso	677	\$ 164	\$ 164	\$ 197	\$ 212	20%	29%
Albuquerque	759	\$ 158	\$ 159	\$ 192	\$ 207	21%	31%
Tampa	781	\$ 177	\$ 177	\$ 185	\$ 200	5%	13%
San Antonio	192	\$ 122	\$ 123	\$ 131	\$ 146	7%	19%
Ft. Lauderdale	957	\$ 166	\$ 166	\$ 180	\$ 195	9%	18%
Newark	1411	\$ 167	\$ 167	\$ 277	\$ 292	66%	75%
Austin	148	\$ 122	\$ 122	\$ 120	\$ 135	-1%	11%
Philadelphia	1335	\$ 168	\$ 168	\$ 200	\$ 215	19%	28%
Jackson	359	\$ 106	\$ 106	\$ 127	\$ 142	20%	34%
Little Rock	393	\$ 111	\$ 111	\$ 149	\$ 164	35%	48%
Birmingham	570	\$ 162	\$ 162	\$ 198	\$ 213	22%	31%
Corpus Christi	187	\$ 119	\$ 120	\$ 152	\$ 167	27%	39%
Greenville, SC	845	\$ 148	\$ 149	\$ 223	\$ 238	50%	60%
Jacksonville	816	\$ 176	\$ 176	\$ 211	\$ 226	20%	28%
Charleston, SC	928	\$ 149	\$ 149	\$ 197	\$ 212	33%	42%
Total for Group		\$ 146	\$ 146	\$ 195	\$ 210	34%	44%

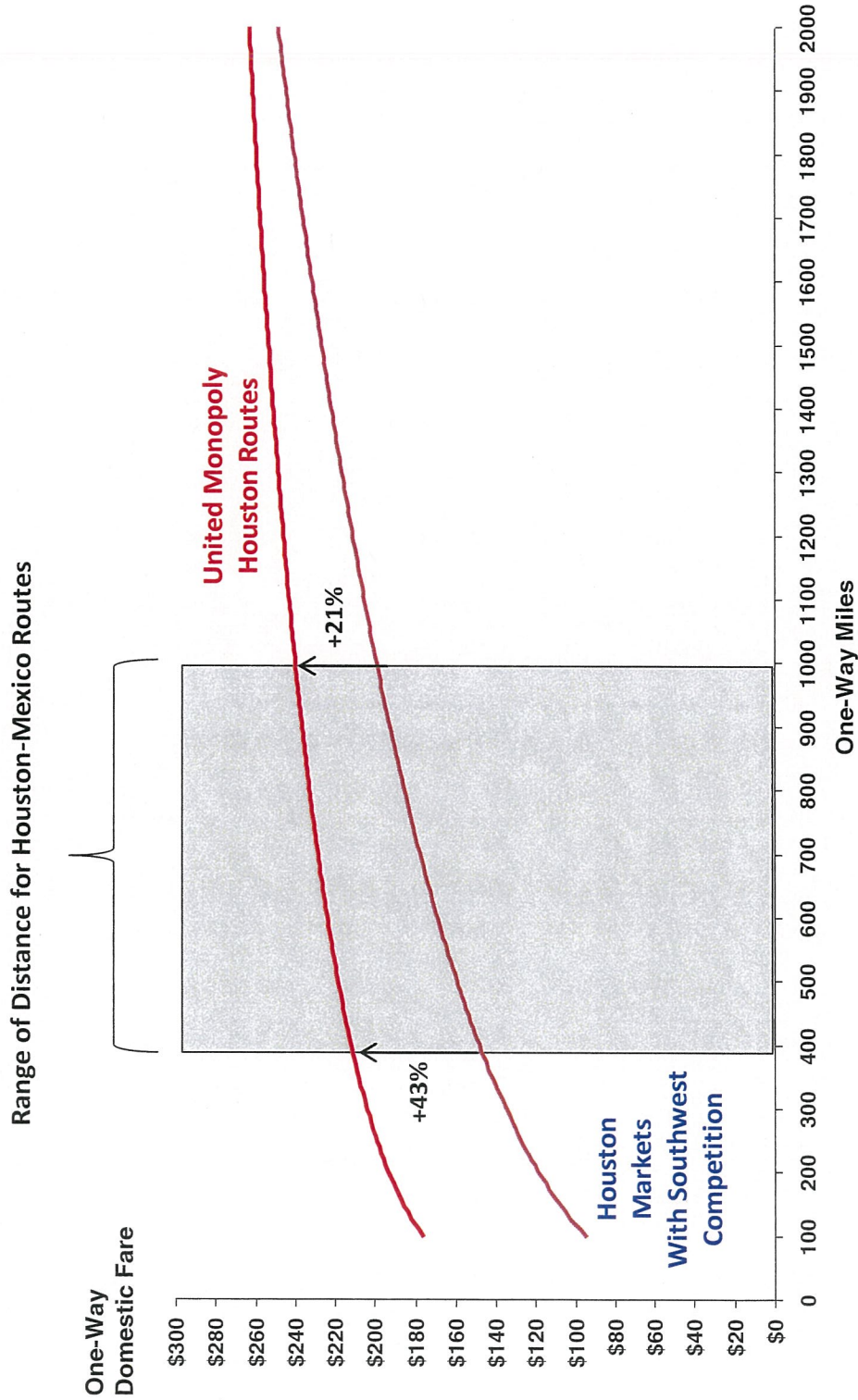


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*DOT survey data for YE4Q11. Total Group fare for Southwest is total Southwest revenue in this group divided by total Southwest Passengers. Total Group fare for United is total United revenue in this group divided by total United Passengers. Bag/Chg Fees are 35 cents per pax for SWA and \$15 per pax for UAL (Form-41 YE3Q11).

Southwest's Presence Reduces One-Way Domestic Fares By Over \$50 In Domestic Markets with Distances Comparable to Mexico Routes

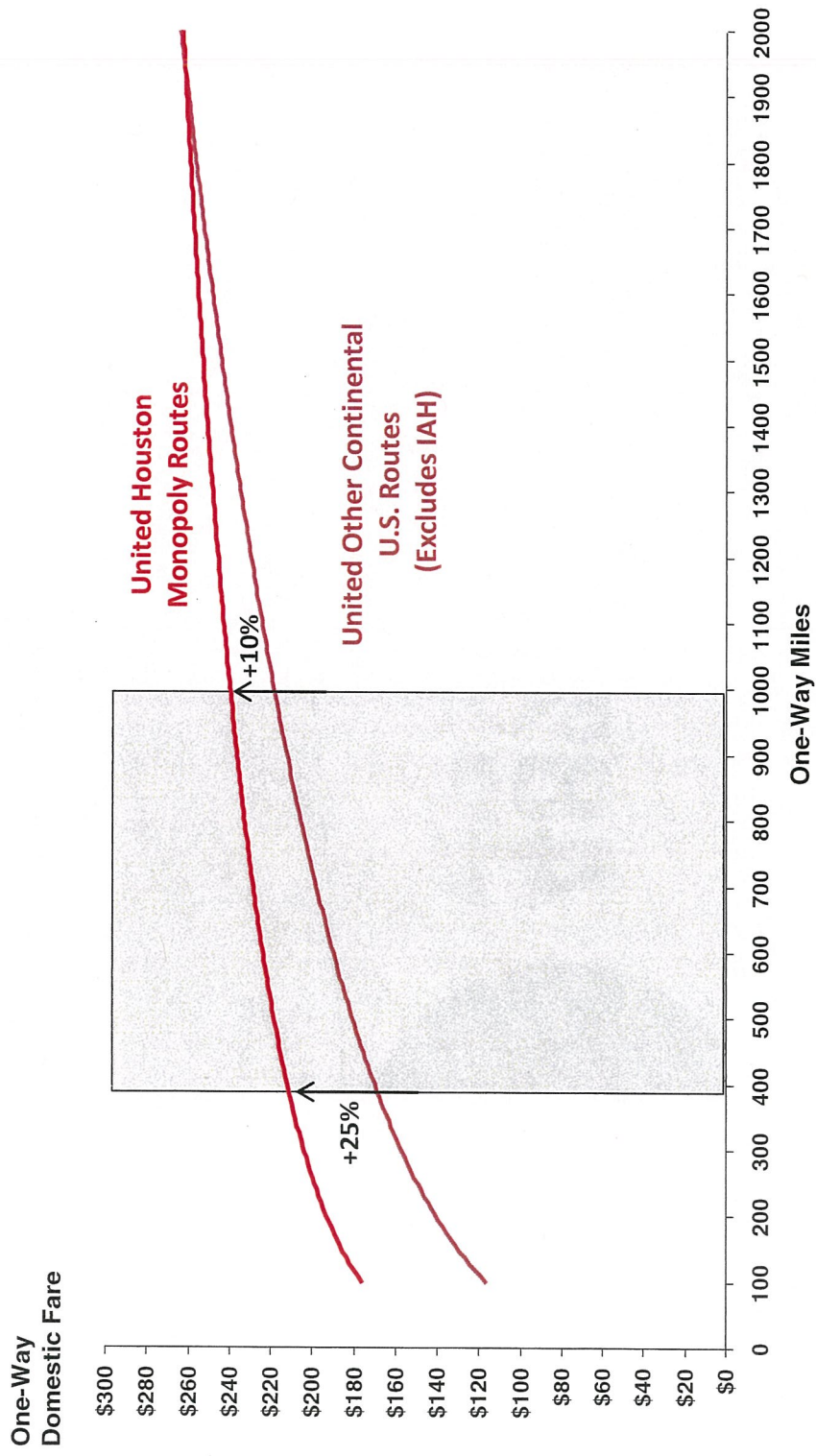


Note: Fared passengers only. Excludes all taxes and government charges. Includes all Houston domestic markets with 600 or more one-way flights for YE Q3 2011.

Source: U.S. DOT, O&D Survey and Schedule data, 12 months ended September, 2011, via Diio, LLC.

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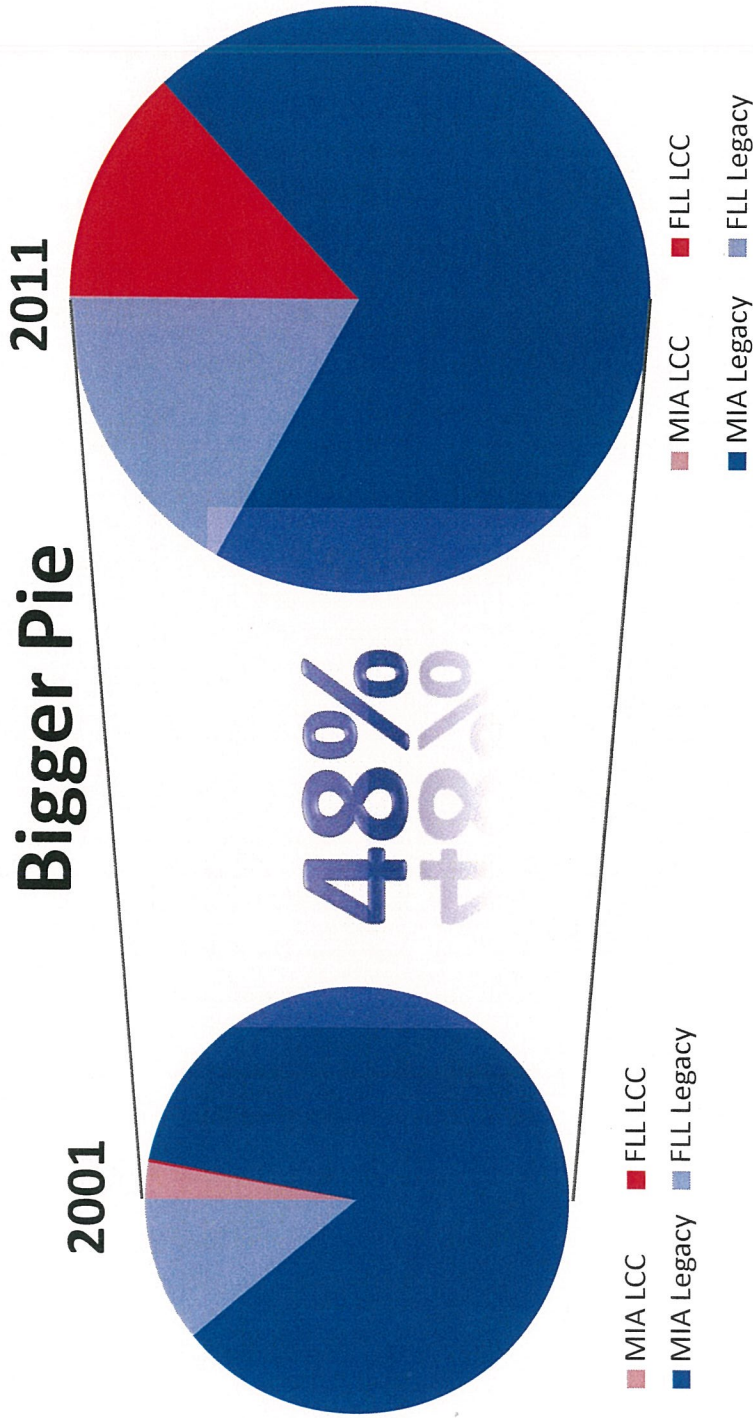
United Charges Higher Domestic Fares in Houston Monopoly Markets Than Its Typical Fares from Other U.S. Airports



Note: Fared passengers only. Excludes all taxes and government charges. Includes domestic markets with 600 or more one-way flights for YE Q3 2011.

Source: U.S. DOT, O&D Survey and Schedule data, 12 months ended September, 2011, via Diio, LLC.

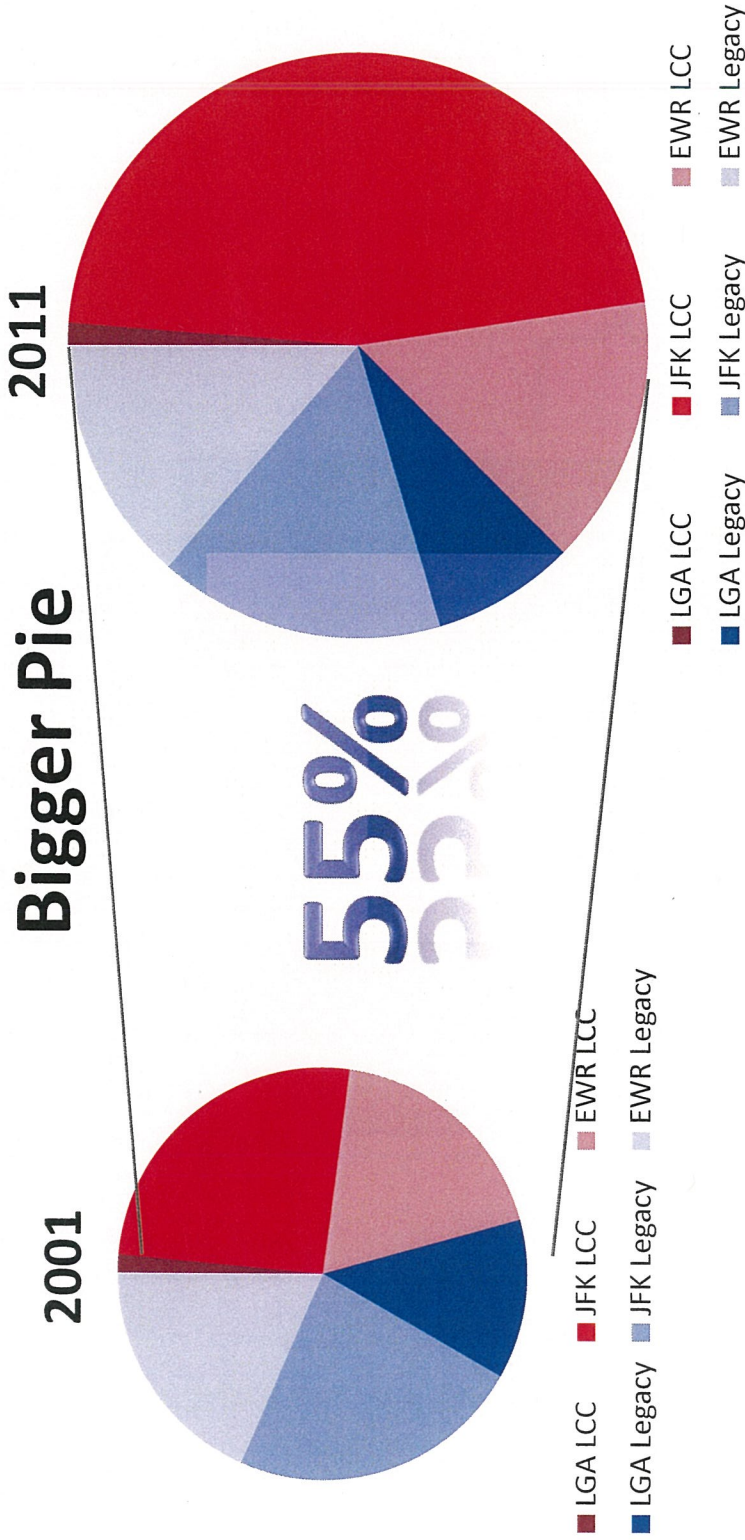
Competition in Miami/Ft. Lauderdale Created a Bigger Pie



Miami and Fort Lauderdale Airports 10 year Passenger Growth

2011 vs. 2001	MIA	FLL	Total
% Growth	17%	293%	48%

Competition in New York Created a Bigger Pie



New York City Airports 10 year Passenger Growth

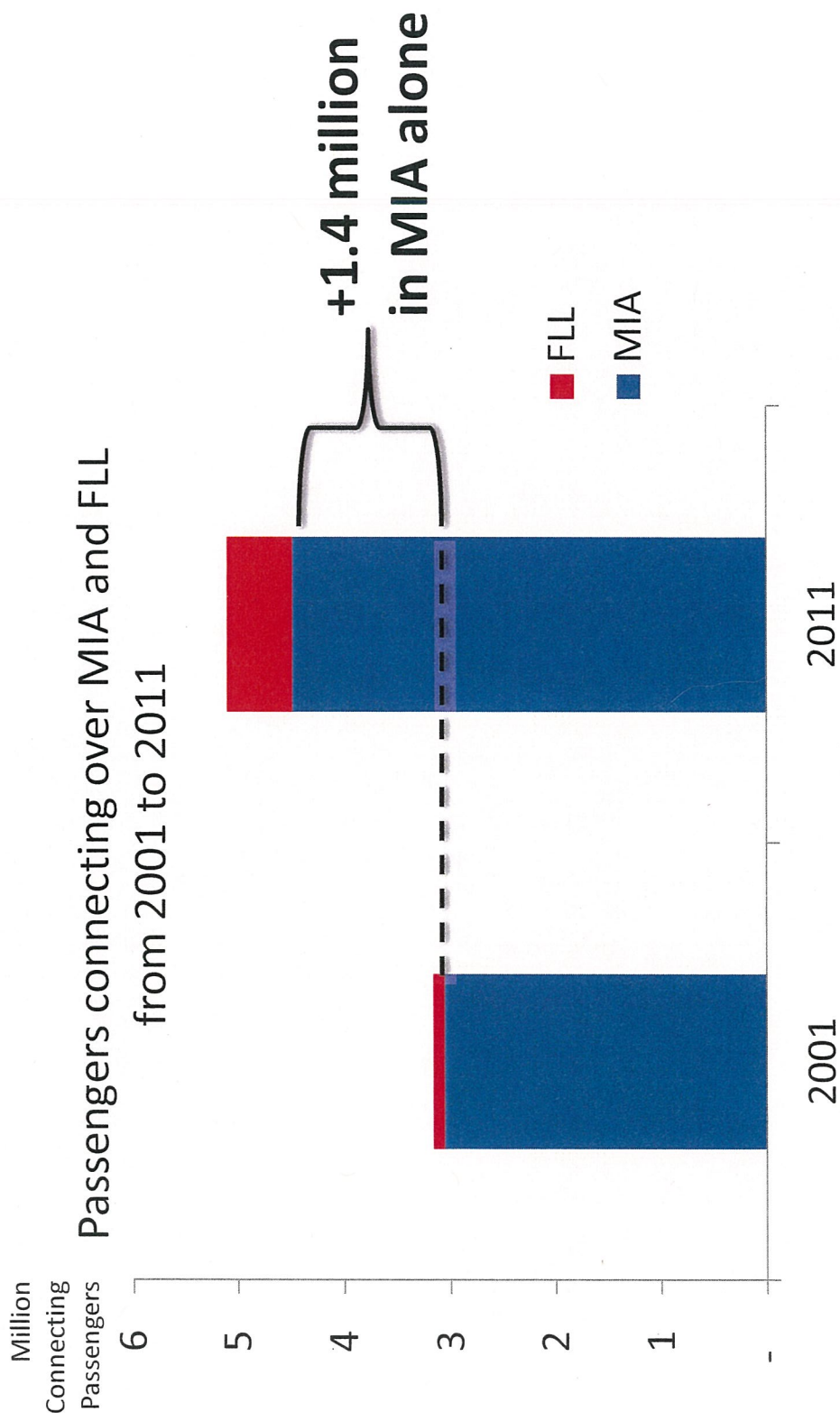
2011 vs. 2001	LGA	JFK	EWR	Total
% Growth	3%	98%	19%	55%



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The Connecting Passenger Pie Gets Bigger Also







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Houston Loses Flyers to Other Hubs

The Effect of Low Fares

Competitor Airport	2011 Hobby Originating Int'l Passengers	Average Fare
Connecting to Caribbean and Latin American Destinations	15,861 	\$326
Flying to ATL from Hobby	10,873 	\$305
Flying to DFW from Hobby	3,395 	\$379
IAH		\$503



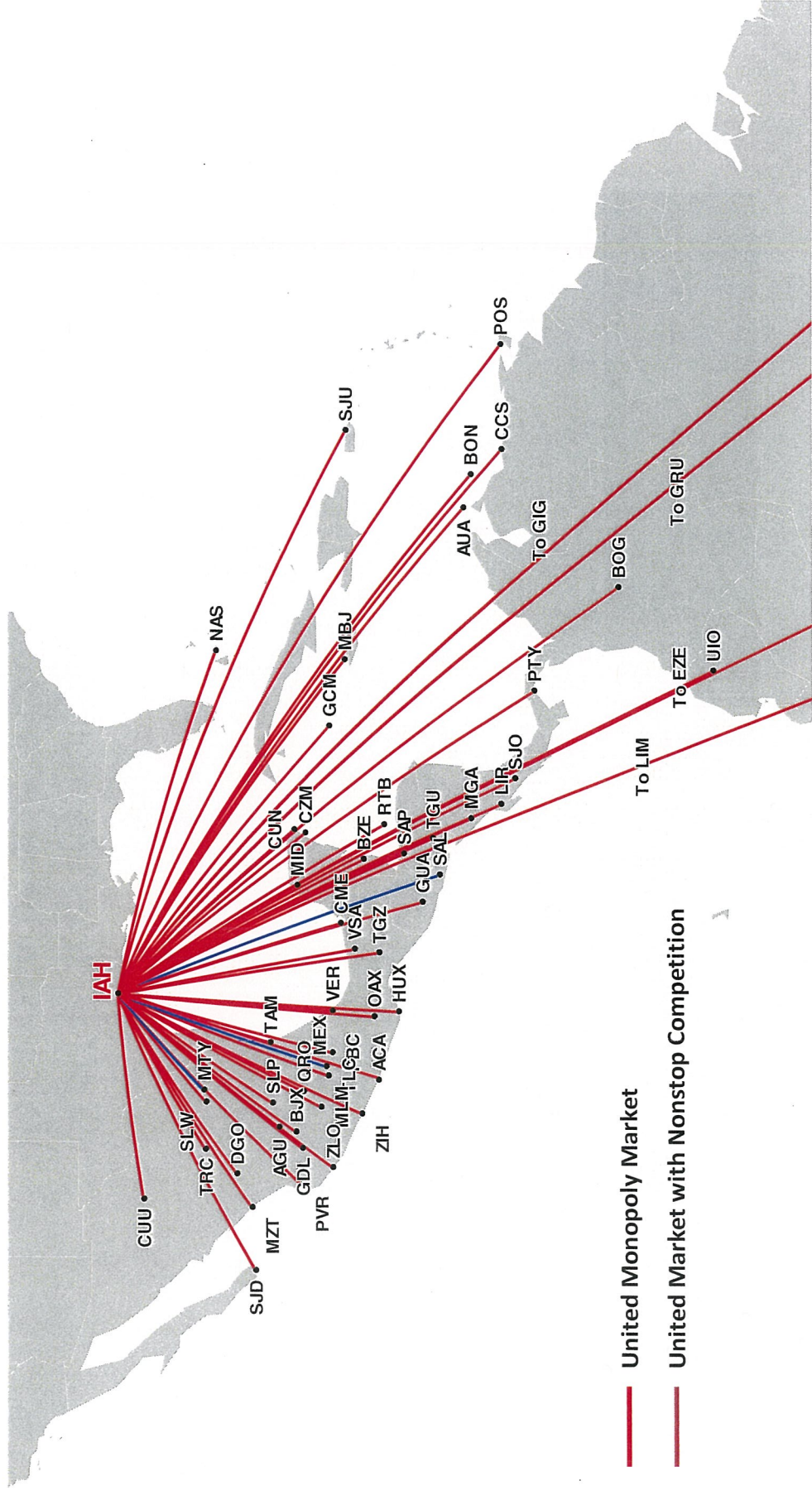
Lack of low fares and multiple carriers makes Houston uncompetitive to other airports.



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Fifty-One of Fifty Four-Latin America and Caribbean Markets Served by United from Houston Are Monopoly Routes



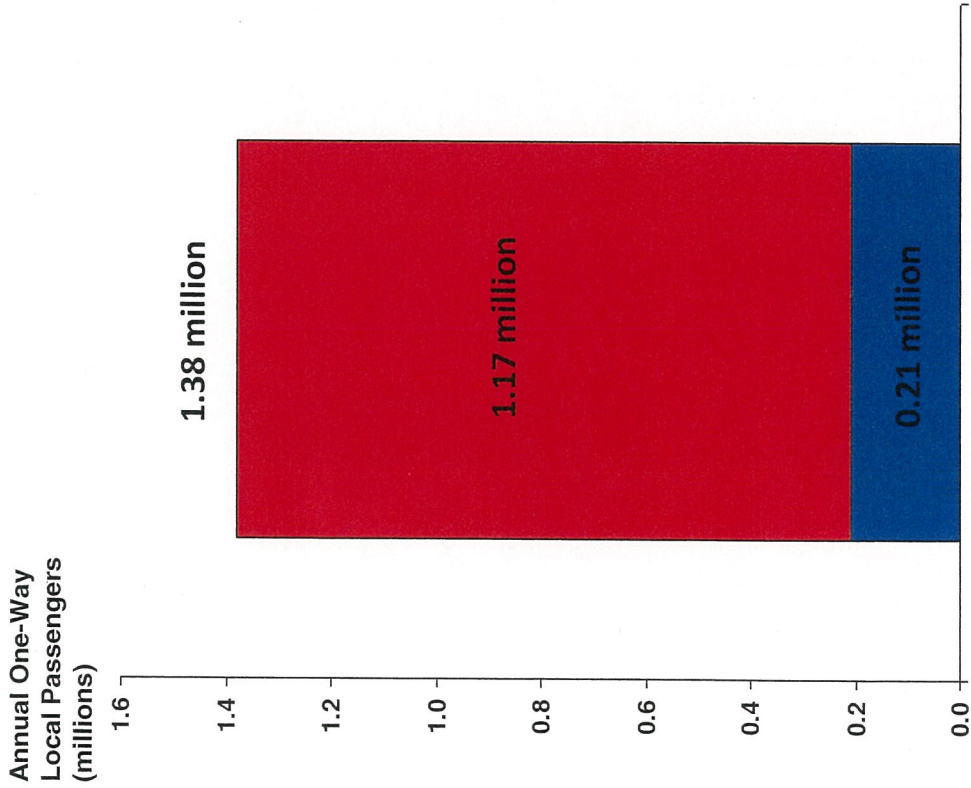
- United Monopoly Market
- United Market with Nonstop Competition

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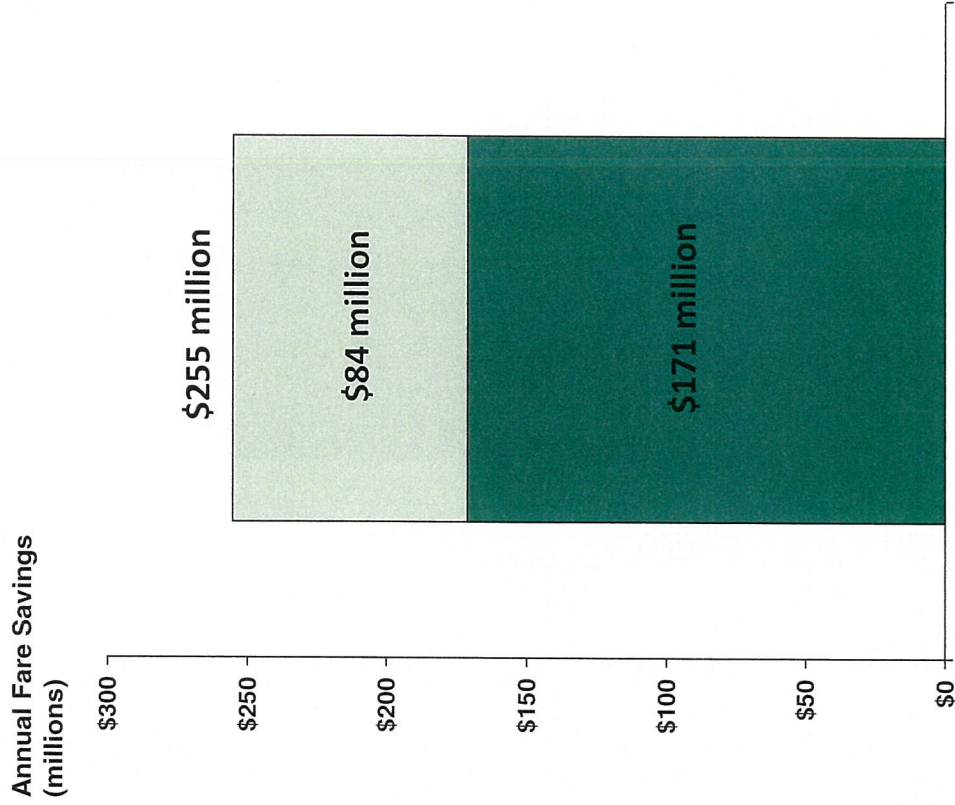
Source OAG Schedule data, June 2012, via Diao, LLC.

Increased Local Houston Passenger Traffic and Fare Savings in 2020 Due to Southwest's HOU – Latin America/Caribbean Service

INCREASE in Local Resident and Visitor Travel



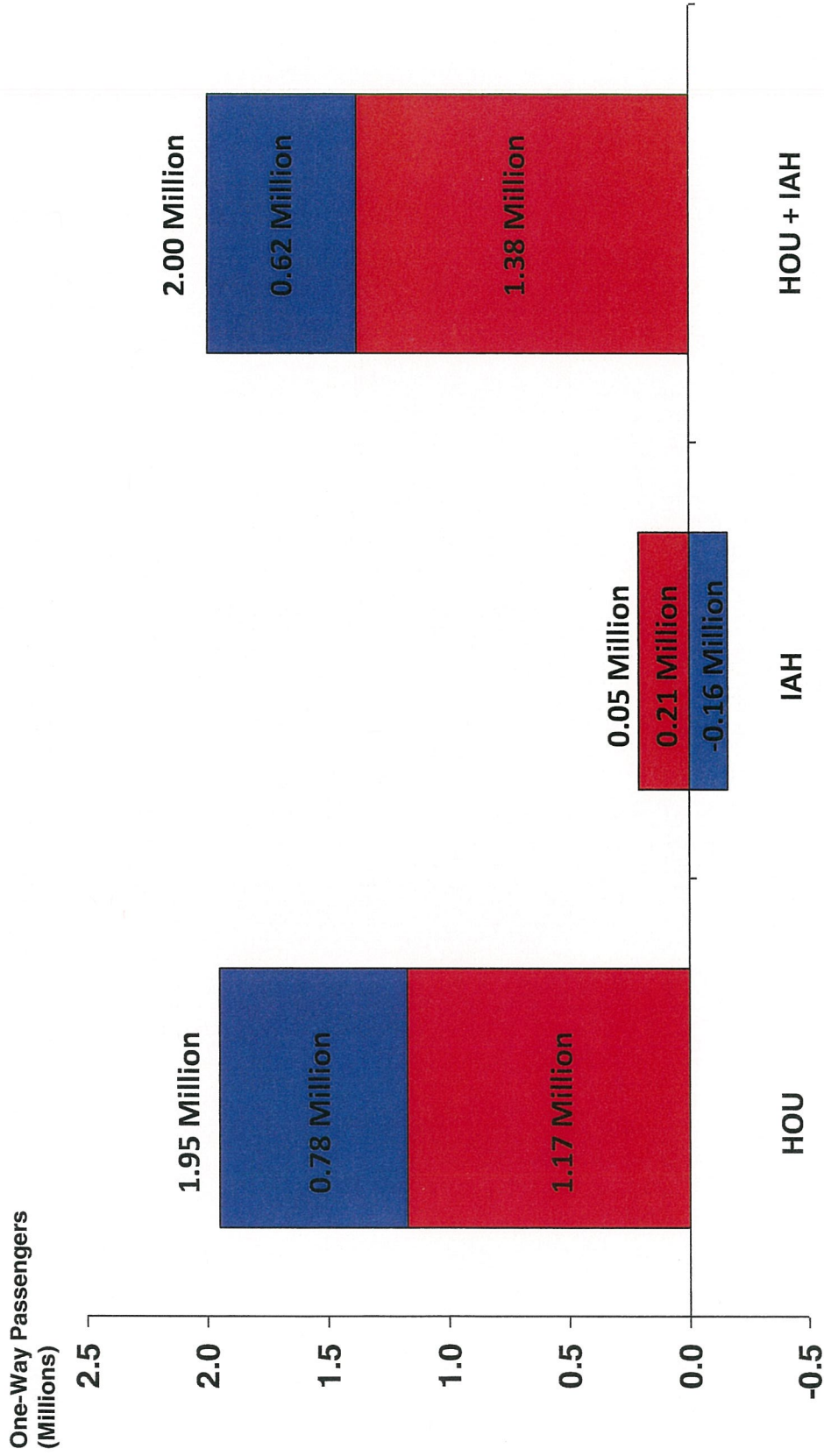
Annual Fare Savings by ALL Local Residents and Visitors to Houston
(In Constant 2011 Dollars)



■ Increase in local passengers using IAH
■ Increase in local passengers using HOU

■ Savings to all local passengers using IAH
■ Savings to all local passengers using HOU

The Houston Airports Will Handle 2.0 Million Additional Passengers in 2020 as a Result of Southwest's Latin America/Caribbean Service



■ Local passengers (residents plus visitors to Houston)

■ Connecting passengers

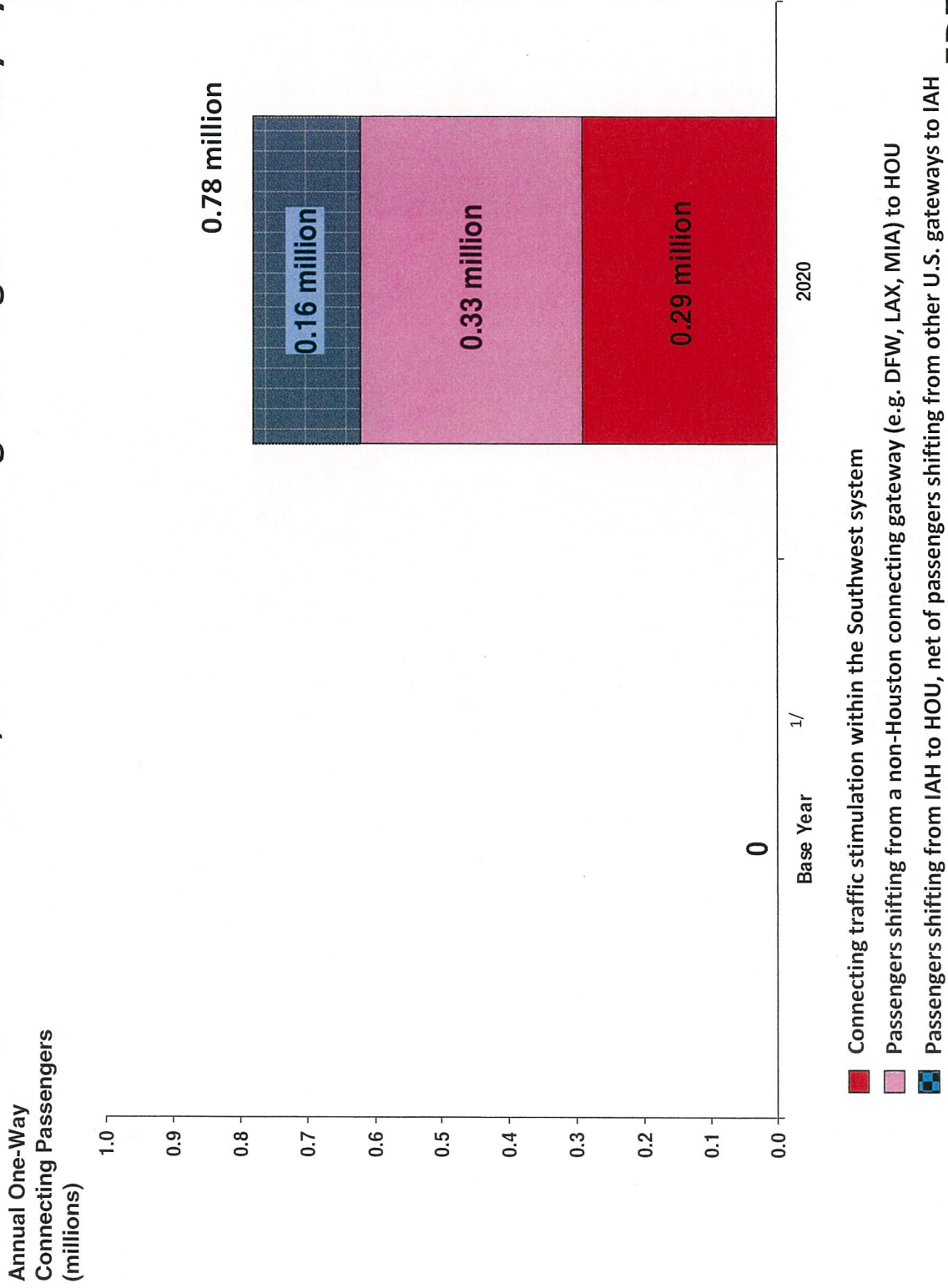
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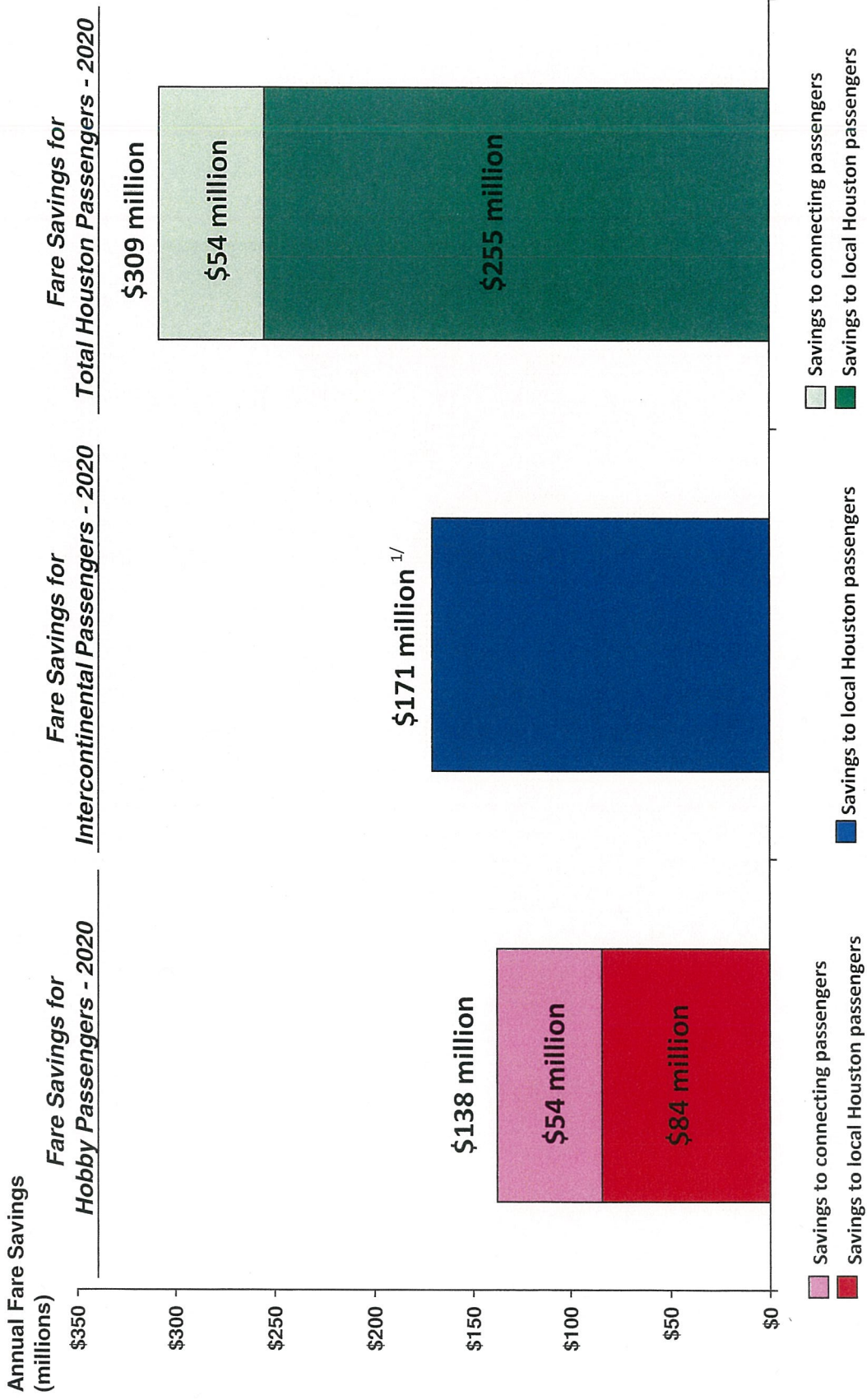
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Southwest Will Make Houston More Competitive With Other U.S. Gateways and Generate Almost 800,000 Connecting Passengers at Hobby by 2020



Fare Savings by All Passengers Using the Houston Airports Will Exceed \$300 Million With the Projected Southwest Latin America/Caribbean Service

(In Constant 2011 Dollars)



Our roots in the Houston community are over 40 years strong



We proactively invest in meaningful and mutually beneficial long-term relationships by providing community organizations with time, talent, and resources across the Greater Houston Area.



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Houston Community Investment

Houston is among a few of Southwest's 73 cities that receive the highest percentage of our charitable giving budget.

From 2011 through first quarter of 2012, we gave charitable donations including tickets, volunteer hours and cash donations equaling nearly \$1.3 million.

Employees dedicated time toward community projects where they contributed 9,788 volunteer hours in the Houston region.



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April 26, 2012

Statement of Dr. Brian M. Campbell
Chairman, Campbell-Hill Aviation Group, LLC

William Swelbar has been retained by United Airlines to rebut the proposition that Southwest's proposed international service at Hobby Airport will bring significant economic benefits to Houston and its air passengers, and to raise the specter of severe service cutbacks at Intercontinental Airport in response. In a similar case in 2005, American Airlines hired Mr. Swelbar¹ to support its position against Repeal of the Wright Amendment, which restricted air service at Dallas Love Field (DAL). As expected, Mr. Swelbar testified that Repeal would severely hurt American Airlines, DFW Airport, and the economy of North Texas. However, Mr. Swelbar painted such catastrophic consequences of Repeal, based on unrealistic counter-evidentiary assumptions, that his findings had no credibility and his report was disregarded in Congress' final legislative solution providing for Repeal.

Judging from the three-page commentary issued by Mr. Swelbar on April 2, 2012 he appears headed down the same path in the Houston case of making baseless and exaggerated claims in support of an airline that is trying to prevent competition to its monopoly position. Consequently, a brief review of his failed predictions in the Wright Amendment matter is appropriate. On behalf of American Airlines, Mr. Swelbar predicted that Repeal would not stimulate new traffic and service for the benefit of both Dallas airports as proponents claimed, but instead would only shift air service from DFW to Love Field, causing a major loss of passengers and commerce at DFW. Specifically, Mr. Swelbar predicted that the following changes would occur:

1. DFW carriers would shift flights to DAL as follows:
 - American – 45 daily departures
 - AirTran – 34 daily departures
 - Other airlines – 33 daily departures

¹ With the firm Eclat at the time.

2. American would not lower its fares to meet Southwest's low fares in new DAL markets.
3. American would reduce service in nonstop markets connecting Dallas with 18 other Texas cities, 10 of which were monopoly American markets (not served by Southwest).

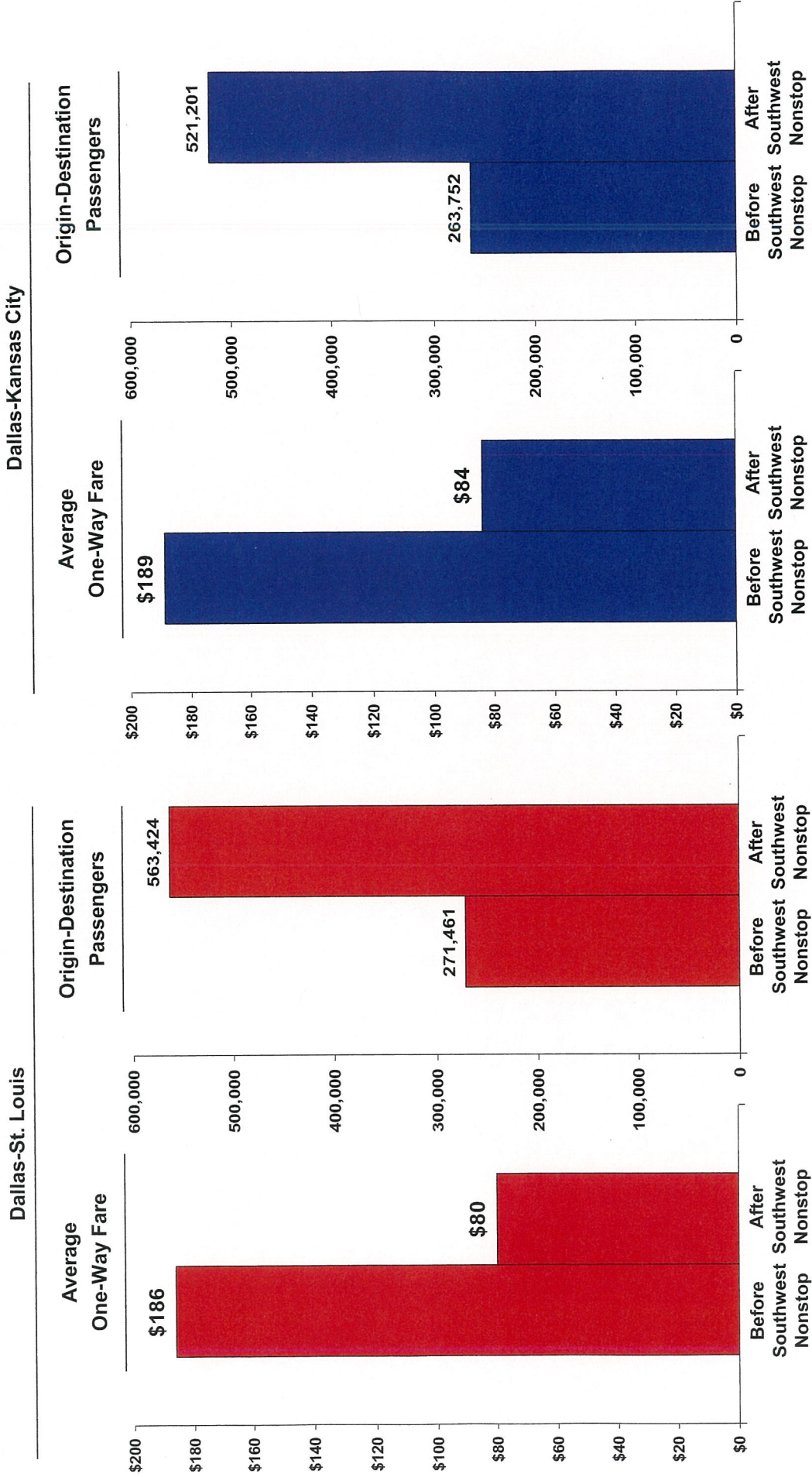
In fact, none of these dire predictions materialized. In late 2005 the Wright Amendment was repealed for service between Missouri and Dallas Love Field (DAL). Mr. Swelbar's theory argued that American would shift flights from DFW to DAL to compete with Southwest's new DAL flights to St. Louis (STL) and Kansas City (MCI), but would not reduce fares. But American shifted only a few flights to DAL for approximately two years; it reduced its fares aggressively at both DAL and DFW to compete with Southwest's STL and MCI flights; and then it abandoned its DAL service, but continued to offer lower fares competitive with Southwest after it returned all its service to DFW. No other DFW carriers shifted flights to DAL in response to Southwest's new DAL service.

Contrary to Mr. Swelbar's predictions, repeal of the Wright Amendment in these two markets triggered aggressive price competition that benefitted passengers at both DFW and DAL. The beneficial impacts may be seen clearly in Exhibit 1. Average fares at DAL and DFW combined dropped by 57% between Dallas and St. Louis and by 56% between Dallas and Kansas City within a year after Southwest inaugurated DAL service. At the same time, total annual passengers in these markets at DFW and DAL combined doubled, increasing by 292,000 in the STL market, and by 257,000 in the MCI market.

Mr. Swelbar's forecast that American would reduce frequencies in multiple Texas markets was also incorrect. Exhibit 2 lists the 18 Dallas intra-state markets identified for service reduction by Mr. Swelbar. Base year frequencies for Mr. Swelbar's October, 2005 study are shown in the first column, and the actual daily schedules in June, 2008 are shown in the next column. Only three of the markets had a reduction in frequencies; the other 15 received the same or greater frequencies by American. In fact, for all 18 DFW routes combined, America's service levels were higher in 2008 by 17%.

In sum, Mr. Swelbar's entire report in the Wright Amendment case was designed as a political scare tactic and it did not work. He appears headed down the same road with the same failed theories for defending United's high-fare monopoly position at Houston Intercontinental.

Markets that Were Formerly Restricted by the Wright Amendment Grew Significantly When Opened to Southwest's Competition from DAL (DFW and Love Field Combined)



Note: Before Period = 12 months ended September, 2005. After Period = calendar year 2006. Includes Fared passengers only and excludes all taxes and fees. Source: DOT, Origin-Destination Passenger Survey, via Diio LLC.

American Airlines Increased or Maintained Its Service Levels in 15 of 18 Intra-Texas Markets that Mr. Swelbar Predicted would Lose Service

<u>Daily Departures to DFW</u>		
	October 2005 Study	June 2008
Amarillo, TX, US	6	8
Austin, TX, US	14	15
Corpus Christi, TX, US	5	7
El Paso, TX, US	7	8
Houston-Hobby, TX, US	7	6
Lubbock, TX, US	6	9
Midland/Odessa, TX, US	5	7
San Antonio, TX, US	13	15
Texas - Southwest Markets	63	75
Abilene, TX, US	6	8
College Station, TX, US	6	3
Killeen, TX, US	6	12
Laredo, TX, US	4	4
Longview, TX, US	3	3
McAllen, TX, US	3	4
San Angelo, TX, US	5	5
Tyler, TX, US	7	5
Waco, TX, US	6	7
Wichita Falls, TX, US	6	7
Texas - Non-Southwest Markets	51	58
Texas	114	133

An Independent Strategic Review

Potential Effects Of International Service At Houston Hobby Airport

Prepared For

Southwest Airlines

Prepared By



Note: This report is prepared for the exclusive use of The data and information herein are from sources deemed reliable but not guaranteed. Any conclusions or recommendations herein are not to be construed in any way as investment or financial advice.

Data Relied Upon: The majority of the data used in this document are as of the full year ending 2Q 2011, analyzed by Aviation DataMiner™.

Issued: April, 2012



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Project Overview

Southwest Airlines has announced its intention to implement international flights from Houston Hobby Airport, proposing a new five-gate, FIS facility to be constructed at a reported cost of up to \$100 million.

The Houston Airport System has claimed that the project will increase passenger traffic through Houston by 1.5 million passengers annually, and create 10,000 new jobs.

United Airlines claims the Southwest plan will "spilt" the international traffic base in Houston, to the detriment of the consumer and to the carrier's future plans for expansion at Houston Intercontinental.

The objectives of this project are as follow:

- An independent review of current international traffic at IAH, including local and flow passengers
- An independent review of the potential effects on the market of Southwest establishing service to points in other countries from Houston Hobby
- A review of effects of international expansion at other points, and the effects on incumbent carriers and traffic flows.

In this project, no reference or reliance is placed on any outside "studies" accomplished by other entities, including the Houston Airport System.

The only issue under consideration in this document is whether the Southwest plan will "split" international traffic at Houston to the material detriment of the UA IAH hub.

Executive Summary

In this project, Boyd Group International reviewed the logical scope of a Southwest international operation at Hobby, and related it to the current international operations at IAH.

Based on the fact that the structure of the Southwest fleet limits the scope and reach of any international flying from HOU, markets in Mexico, near-Central America and the Caribbean will be the carrier's initial targets.

In this project, a review was made of the markets in that region which today generate over 20,000 local annual Houston O&D passengers. These would logically be the first markets that Southwest would consider in an operation at Houston Hobby.

Overall Findings

The general conclusions are straightforward and unambiguous.

- The Southwest plan will not harm IAH nor United Airlines;
- The Southwest plan will tend to stimulate traffic to and through Houston, thereby strengthening the Houston Airport System;
- The Southwest plan represents a measured and prudent increase in international capacity at Houston. With only five planned gates, operated with 737 airliners, any contentions that Southwest will flood the Houston international market with excess seats simply are not valid;
- The Southwest plan is positive for not only Houston, but it adds an additional Caribbean gateway for as many as three dozen US cities

Furthermore, an extensive review was accomplished of a near-mirror situation in South Florida, where FLL and MIA represent a very similar set of circumstances to the HOU/IAH situation. There, the existing American Airlines hub was "attacked" over the last few years by massive increases in low-fare service by Spirit to key AA-served destinations in Central America and the Caribbean.

The similarities are compelling. FLL and MIA are actually a few miles closer together than are IAH and HOU. American, like United at IAH, is a hubbing carrier. Spirit, as with Southwest at HOU is a low-frills, low-fare carrier.

But the additional capacity and frequency brought by the expansion of Spirit has not harmed American. In fact, American has been able to maintain higher traffic and load factors at MIA, while Spirit has correspondingly flourished at FLL.

Based on current O&D traffic levels, it is apparent that Southwest intends to invest substantial resources into making Hobby another gateway to Central America.

However, the traffic that will be generated from just five gates with narrow-body 737 airliners is no way a threat to the 2.8 million annual international passengers now using IAH.

Boyd Group International submits that the unique nature of the WN-proposed international operation at HOU will be consistent with the experience in South Florida: both airports, both airlines, and consumers across the nation will benefit.

Key summary findings are:

Southwest's International Operations Will Be Stimulative

The claim that Southwest's intent to operate international flights at HOU will materially divert traffic from IAH is not sustainable in the light of the type of operations and the route system that the WN model will generate.

The "international" operations that Southwest, with a fleet of 737s and a single-class product, can establish at Houston Hobby do not even approach the scope of international access at IAH.

The "target market region" for a WN/737 international operation is without question focused on the Caribbean and Central America region. While Southwest has provided no specific route or market planning information, the current IAH patterns of service to key destinations in the Caribbean and Central America very clearly indicate the types of destinations that Southwest can add at Houston Hobby.

Strong business/industrial destinations such as Monterrey, Chihuahua, Saltillo, etc., offer little initial potential for Southwest. The focus, clearly, will be on leisure markets. Since these markets tend to be stimulative, catastrophic diversion of traffic from IAH, as some may be predicting, is highly unlikely. In fact, experience elsewhere in the nation would indicate that in terms of net enplanements, the Southwest concept will bring additional traffic to the Houston Airport System.

United Has A Near Monopoly On Caribbean Destinations

A point not made clear in much of the media coverage is that many of the destinations to which Southwest is likely to fly are currently single-carrier markets from IAH.

To virtually all major leisure destinations in the target region, United currently has, for all intents and purposes, a lock on local traffic from Houston. Other than Liberia, Costa Rica (LIR), where United has 93% of the traffic, all other markets that generate over 20,000 O&D are captured at 95% or higher by United.

This, as a starting point, indicates that Southwest entry into these leisure destinations would bring new competition, and – in light of high current

With only five gates, the Southwest international operation will be highly focused, and not a blanket "threat to traffic levels at IAH.

United load factors to many destinations – additional local and connecting traffic.

The Scope of Southwest International Operations: Limited

The potential scope of the potential international service operated by Southwest at Hobby is miniscule compared to that offered at IAH. The Southwest fleet represents clear parameters on what service can be offered, and the five gates planned do not represent an untoward level of new international capacity for Houston.

Fleet & Unit Capacity Constrictions

Southwest does not, and has no plans to, operate any airliners larger than the 175-seat 737-800s now entering its fleet. This not only defines the potential reach of any WN international operations, but also the actual daily/weekly seats that can be put into the international skies from a facility of just five gates. Conclusion: the Southwest plan is measured, rational, and conservative.

The Competitive Battleground Is The US, Not Houston

The reality is that the proposed Southwest operation will essentially be another US gateway to the Caribbean and Central America.

This is the role of the current United service, where in the “target area markets” of over 20,000 IAH annual O&D, the local traffic IAH by itself would equate to just a 19.2.0% load factor, yet United’s powerful connecting operations feeds sufficient traffic to achieve average load factors of almost 80%¹

This means, without question, that the target customers of the proposed Southwest operation include high percentages of passengers generated from other points on the WN system.

This is positive not only for Houston, but also for each of the 34 airports that Southwest serves nonstop from HOU.

While the Southwest system still has significant point-to-point flying, it also relies increasingly on “flow” traffic – passengers connecting, and that includes Hobby. Today, approximately 36.1% of WN’s passengers at IAH are not local passengers, but are connecting to and from other points on the Southwest system. The international operations of Southwest will be

Southwest obviously is planning the HOU international service to generate additional flow traffic on domestic routes into Houston.

The contention that the WN service will weaken flights at IAH is simply not true. Experience elsewhere in the nation shows no such dynamic.

In fact, in Southeast Florida, where Spirit has added massive new Caribbean capacity at FLL, the effect on American’s traffic at MIA has been stimulative.

¹ Data provided in a table in the following section.

consistent with this, and will result in net-new passengers generated at points elsewhere in the nation, not just Houston.²

In fact, when analyzing United's top IAH-Central American markets of over 20,000 local Houston O&D, more than 80% of the passengers are connecting at IAH, from other United Airlines destinations.

What this points to, clearly, is that the proposed Southwest operation will flow traffic from cities on the WN route map across the nation. It is competing with all air carriers to these points, over multiple gateways, and not just with United at Houston.

The conclusion here is that Southwest will enhance the Houston Airport System by establishing Hobby as a wider gateway for the nation to the Caribbean and near-Central America.

The Southwest Concept Is Reasonable And Conservative

With a plan for only five gates, combined with the limited-gauge fleet operated, the Southwest plan is not one that can flood the Houston market with excess seats.

Throughput is also an issue. International flights cannot follow a "fast turn" approach. Customs, immigration, additional security and other procedures naturally increase the time to get a flight out, as well as to process it back in.

Therefore, Southwest cannot achieve the estimated 9 turns per-gate, per-day that is estimated at their operation at Dallas/Love. Boyd Group International would estimate that a five-gate system could likely generate approximately 5 turns per day per gate.

Experience In Other Regions

There are no substantive data from elsewhere in the nation where the entry of additional international capacity – particularly to Caribbean and Near-Latin destinations, as is the logical Southwest plan – has resulted in cannibalization of traffic.

Therefore the contention that existing traffic will be simply "split" – i.e., drawn to HOU and reducing passengers at IAH – is not supportable.

² Data is for the year ending 3Q 2011, analyzed by Aviation DataMiner™

Comparative Scope – HOU/WN v IAH/UA

It is necessary to clarify the players in the analysis.

- On one hand we have Southwest, which intends to put a five-gate international operation at HOU by 2015.
- On the other hand, we have United, which has a massive connecting hub operation at IAH. United claims that the WN plan could torpedo UA international expansion at IAH.

This is not a dispute regarding Houston, per se.

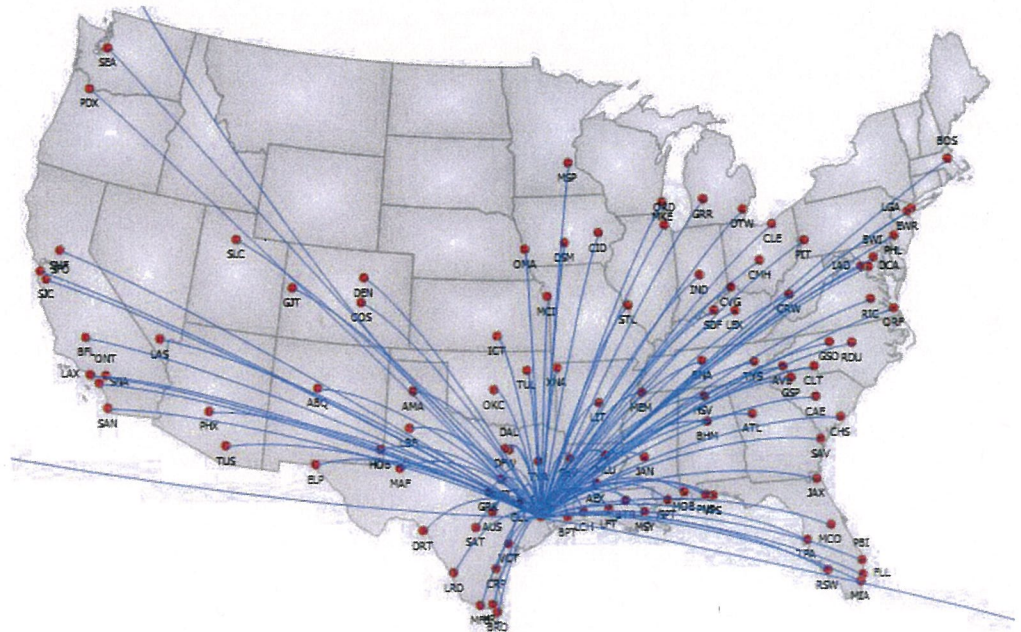
It is a matter of United v Southwest.

This is aside from input, studies, research, or other data from other entities.

Therefore, the crux of the controversy is not the overall effects on "international" traffic at IAH, but more parochially, effects of the WN plan on the United hub at IAH, which is a critical part of the Houston infrastructure. Therefore, the analysis focuses on United and Southwest.

United IAH Hub Operation

United at IAH has an operation comprising an average of approximately 604 daily departures, with approximately 56,900 daily seats.³



United today serves approximately 64 international destinations from Houston Intercontinental. Of the total United passenger traffic at IAH, over 60% is connecting traffic.

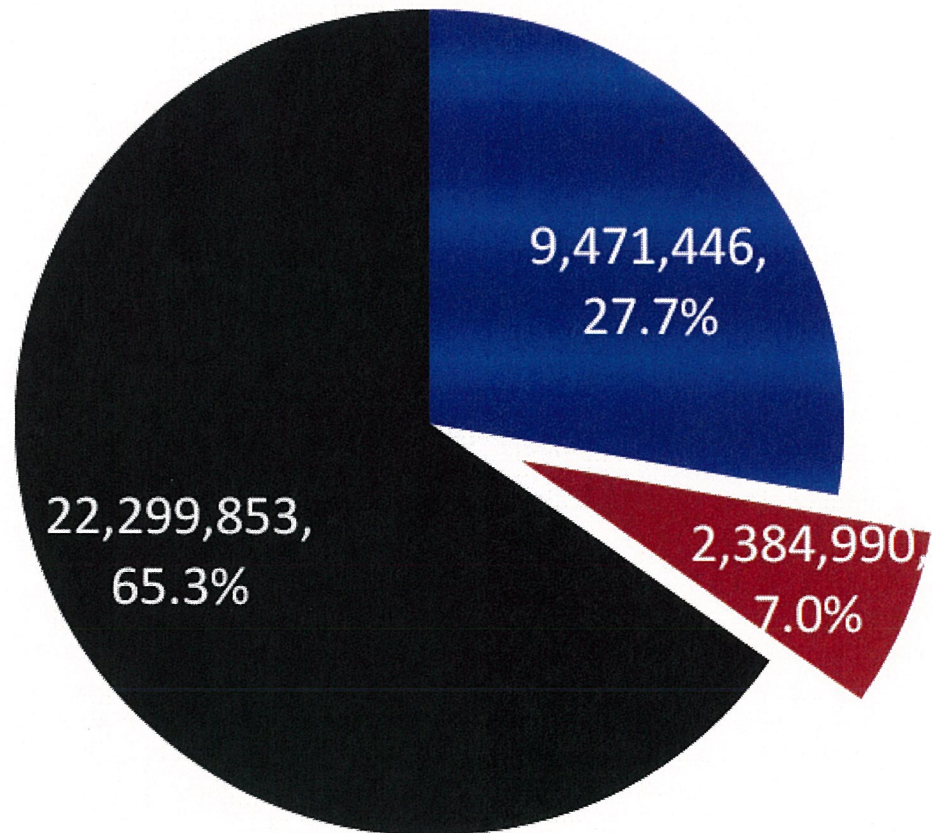
In fact, 35% of the passengers are local Houston O&D, and of the approximately 34 million passengers that are enplaning, deplaning and going

³ Based on schedules filed by United for April, 2012.

through the United operation only 2.4 million are local O&D international passengers.⁴

Traffic Mix - United/Houston Intercontinental

■ Domestic O&D ■ Intl O&D ■ Flow



Pertinent to this analysis is the international component, which some claim will be materially and negatively affected by a Southwest international operation at HOU. Such an assertion is at variance with the facts.

We need to analyze this based on the realities of what a Southwest hub operation will actually represent. First, the UA/IAH hub encompasses over five dozen international destinations, most of which cannot be physically operated by the Southwest 737 fleet at Hobby.

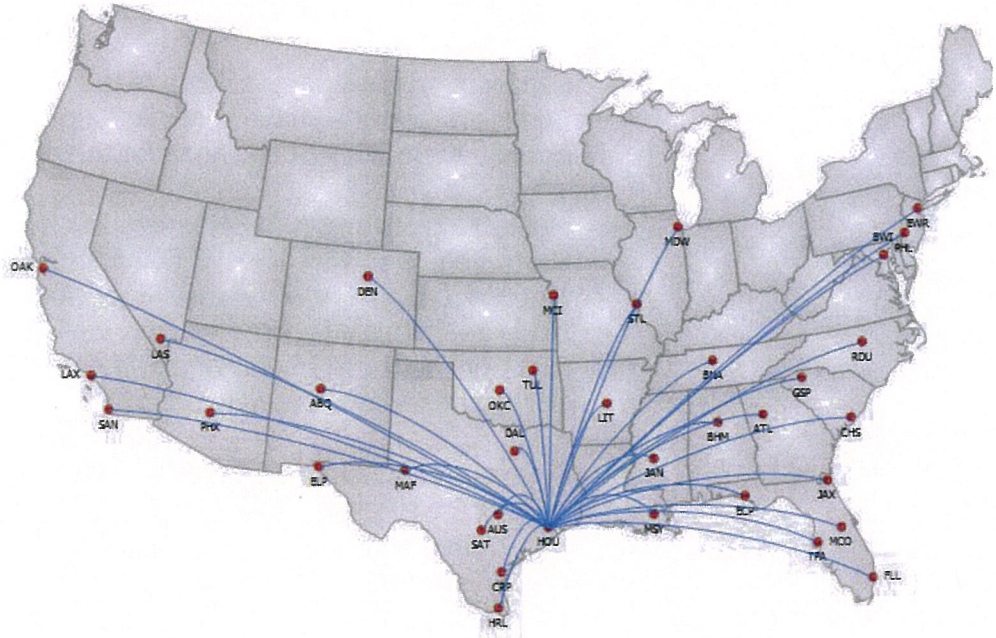
For example, the key markets such as London, Paris, Tokyo, etc. are not threatened by the Southwest service. That rules out any "splitting" of traffic to key markets in Europe, Asia, and deep Latin America.

⁴ Source: T-100 and reported O&D for full year ending 2Q 2011, analyzed by Aviation DataMiner™

Second, the Southwest model and competitive realities rule out many other potential points that represent strong revenue flows for United at IAH. These include business markets in Northern Mexico, which would require massive amounts of feed traffic – and are of a size that major carriers rely on RJs.

Domestic Feed – An Important Component In Building HOU

One of the first metrics to consider is the comparative reach of the Southwest operation at Hobby v that of United at Intercontinental.



Southwest has a Hobby an average schedule of approximately 130 daily departures, to 34 nonstop destinations, 14 of which are served with less than three flights per day. This is a fraction of United's 604 average daily departures at IAH.⁵

From that metric alone, the additional departures afforded by five FIS gates at Hobby do not represent the threat of weakening or diluting the international traffic base at IAH.

Initial Target Area: Central America & Caribbean

Southwest has made it clear that the 737-800 will be its largest aircraft, at 175 seats. However, the majority of its fleet for the foreseeable future – well beyond 2015, when the HOU facility is envisioned to open – will be the smaller 143-seat 737-700.

⁵ Based on flight schedules filed for month of April 2012.

Therefore, we have, right from the start, two metrics that will shape the scope of the WN operation. The first is unit capacity, where the average seats per departure will likely be in the 148-150 range. The second is the set of operational limitations – range v revenue v payload – of the 737 fleet.

We can cull down the range of markets where the Southwest operation will prosper by reviewing where the airline simply cannot fly from HOU:

- Obviously, nonstops to Europe, Asia, and Deep Latin America are not possible with the 737, nor does Southwest indicate it will ever acquire a fleet-type to fly such routes.
- Canadian markets are a *non sequitur* to this analysis. The major Canadian airports have pre-clearance, and therefore WN could operate them without the need for the planned FIS facility.
- Markets in near-South America, such as Bogota, Caracas, and Maracaibo, are well over 2,000 miles (3,200 km) from Houston. Furthermore, these very specific business markets, which, as with those in Northern Mexico, are now well served by major carriers who focus on business travel, and which have front cabins to generate significant revenue premiums.
- Several Caribbean destinations would appear to be attractive, but most are well over 2,000 miles. Grand Cayman and Nassau may be possibilities, but these, too face strong competition from other East Coast Gateways.

The markets reviewed on the following pages are intended as examples. They are markets that, based on independent professional analyses by Boyd Group International, would fit the initial Southwest operational template. To be sure, there are likely others.

However, with a fleet of 737s, and with the leisure-focused product of Southwest, these would be typical of the market objectives of the carrier's Houston plan.

Typical Initial Southwest International Markets

It is important to define "international" in the context of the Southwest 737 fleet and its product model:

Primarily leisure-focused markets within a roughly 1,500 mile (2,400 km) radius of Houston.

The typical markets that would focus upon represent less than 12% of United's total international revenues.

As a practical matter, however, with only five gates and only a 737 fleet, Southwest would operate a relatively limited schedule to such points.

When we pull the data for Houston for such markets, the immediate candidates for Southwest are obvious:

Market	UA Local Psg'r Capture	TTL On Board	% of On Board As Flow Pax	CO LCL Market Share	Net Rev.	Ticket Yield	On Board Load Factor	Local Pax Load Factor	United Capacity
Mexico City	182,588	511,568	64.3%	66.8%	\$43,722,439	32.49¢	72.5%	25.9%	705,601
Cancun	131,941	574,741	77.0%	98.1%	\$26,010,165	25.53¢	82.4%	18.9%	697,501
Los Cabos	45,671	167,192	72.7%	95.8%	\$10,987,848	28.12¢	77.3%	21.1%	216,290
San Jose, CR	43,874	309,565	85.8%	96.3%	\$12,896,719	21.26¢	83.9%	11.9%	368,969
Guadalajara	39,382	231,464	83.0%	99.0%	\$11,228,097	35.95¢	81.7%	13.9%	283,310
Cozumel	31,300	112,231	72.1%	97.7%	\$5,822,959	23.37¢	77.4%	21.6%	145,001
Puerta Vallarta	29,135	135,078	78.4%	98.3%	\$5,941,133	24.01¢	81.3%	17.5%	166,148
Panama City	25,659	202,801	87.3%	96.3%	\$9,449,467	24.06¢	79.6%	10.1%	254,775
Liberia CR	20,680	131,183	84.2%	93.9%	\$5,897,032	22.76¢	77.6%	12.2%	169,050
Grand Cayman	18,471	49,508	62.7%	84.9%	\$4,725,202	27.65¢	73.8%	27.5%	67,084
Montego Bay	17,192	46,729	63.2%	62.8%	\$4,232,666	19.45¢	86.5%	31.8%	54,022
Villahermosa	16,000	30,131	46.9%	99.2%	\$5,885,579	43.65¢	76.3%	40.5%	39,490
Nassau	15,190	21,258	28.5%	58.5%	\$3,920,165	25.14¢	84.6%	60.5%	25,128
Totals	617,084	2,523,449	75.5%		\$150,719,470		79.0%	19.3%	3,192,369
Pct of UA / IAH Intl Traffic	27.0%				11.6%				

In this analysis, we included markets where current local United O&D is at 15,000 annual passengers or above. These markets – including Mexico City – represent 27.0% of United's international O&D at IAH. However, these markets only represent 11.2% of United's total international local O&D revenues at IAH.⁶

These markets are felt to be the most likely to be considered by Southwest. It must be kept in mind that the limited gate capacity proposed will not accommodate any high level of frequencies to any specific set of markets.

This points to two main conclusions.

First, the scope of a Southwest international operation represents a specific and very tightly-defined scope. This is hardly a "threat" to United's international traffic at IAH, certainly from the perspective of the revenues at risk, and the markets that WN can serve.

Second – and important to the Houston economy – based on the current size of these markets, Southwest certainly intends to build and stimulate traffic, likely by a combination of fare and capacity approaches. This will

⁶ Source: Aviation DataMiner™

benefit Houston by increasing the flow traffic from Southwest's US domestic system.

It can also be expected that at some point Southwest would likely consider HOU-Toluca service, to connect with partner Volaris. While the levels of actual connectivity would be difficult to forecast based on that carrier's future growth plans at TLC, it has the potential of opening Houston to additional markets that it does not have today, and making it a stronger gateway for passenger traffic to the US from Mexico.

The United Houston Monopoly In Key Markets

In ten of the markets outlined, United has over 90% of the local Houston O&D. This is **not** meant to be in any way a pejorative observation regarding United. It is simply the outcome of Continental (now United) investing in a connecting hub operation at Intercontinental.

The Southwest investment in expansion at Hobby will enhance competition in the region, as well as flow additional passengers over HOU.

Potential Southwest Expansion Is Stimulative

In regard to the potential for this new gate capacity to “split” and balkanize traffic between the two airports, a hard look at reality indicates that such fears are entirely unfounded.

The five-gate facility that Southwest is proposing will likely allow Southwest to operate between 25 and 30 (at most) net new daily international departures from Hobby – i.e., between 50 and 60 total operations. *It is entirely inaccurate to claim that this level of flight activity would be a threat to the economic underpinning of the United operation at Houston Intercontinental.*

The math is compelling. An international operation by its nature cannot be a “ten-minute-turn” affair, or even a 30-minute turn. Both outbound and inbound flights require much more extensive documentation, preparation, passenger processing, security procedures, etc. than do domestic flights.

	Depts	Avg Seats/Flt	Total Seats
IAH Current	638	98	62,652
HOU Current	160	128	20,457
Current Total	798	104	83,109
WN Likely	30	148	4,440
Pct Increase	3.8%		5.3%

For this reason, it is logical that Southwest will require more time to process flights at these gates. The estimated 9 daily flights per gate that can be achieved at locations such as Dallas/Love will likely be reduced to more like 5 daily turns per gate.

The proposed facility will not engender anywhere near sufficient net-new seats to affect the traffic patterns at IAH.

Assuming a mix of 737-700/800s with an average per-departure seat capacity of 148 (estimated), Boyd Group International projects the new FIS at Hobby to increase departures, compared to the total at both airports) by less than 4%. This simply is not sufficient to torpedo any of United’s plans for expansion at IAH.⁷

⁷ Source: Snapshot schedule for single-day departures at both airports, based on Aviation DataMiner analysis of Innovata schedules filed as of April 11, 2011.

Experience At Other Airports

The claim is being made in some circles that the additional Southwest capacity at HOU will cannibalize IAH to the point that United's operations will be adversely affected.

Aside from the data above, which very clearly refute such claims, we have a near-identical example to review.

Spirit Airlines FLL Growth and Impact on American's MIA Hub

The expansion of Spirit Airlines Latin American capacity at Fort Lauderdale International Airport and its effect on American Airlines' Miami International Airport Latin American hub performance is an excellent barometer for what can be expected in Houston should Southwest Airlines establish an international terminal at HOU.

Overall, it is clear that the expansion of Spirit Airlines' Latin American air service at FLL has *not* negatively impacted the performance of American's Latin American gateway at MIA. A review of key metrics follows below.⁸

Capacity Comparison to Key Caribbean/Latin Destinations

Being just 30 minutes apart, it would be logical to assume that a wider international operation at FLL by Spirit would have a detrimental impact on the American hub at MIA. Many of the same Caribbean, Mexican, and Central American destinations are served by both Spirit and American at their respective South Florida hubs. However, this is not the case, as the data clearly illustrate at FLL and MIA.

A year-by-year review of seat capacity to key Caribbean/Latin destinations that have had both American MIA and Spirit FLL air service since 2006 is illuminating:

Available Seats by Year - American MIA

Market	2006	2007	2008	2009	2010	2011	Total
CUN	426,273	416,380	444,023	443,309	428,562	506,008	2,664,555
KIN	365,604	322,658	322,318	345,213	342,178	334,119	2,032,090
MBJ	363,972	346,982	365,183	382,666	369,202	351,532	2,179,537
NAS	456,912	451,312	497,478	483,932	403,005	328,397	2,621,036
SDQ	598,051	635,597	596,554	561,708	538,215	511,713	3,441,838
SJU	1,224,500	1,352,092	1,161,125	990,637	948,927	971,256	6,648,537
STT	235,465	284,068	270,338	273,066	270,874	309,834	1,643,645
TOTAL	3,670,777	3,809,089	3,657,019	3,480,531	3,300,963	3,312,859	21,231,238

⁸ Note that the travel distance between MIA and FLL is less than that between HOU and IAH.

While the capacity has been adjusted in specific markets by American, it certainly is not finding itself chased out of the region due to the corresponding expansion by Spirit at FLL.

Available Seats YOY % Change - American MIA

Market	2006	2007	2008	2009	2010	2011
CUN	-	-2.3%	6.6%	-0.2%	-3.3%	18.1%
KIN	-	-11.7%	-0.1%	7.1%	-0.9%	-2.4%
MBJ	-	-4.7%	5.2%	4.8%	-3.5%	-4.8%
NAS	-	-1.2%	10.2%	-2.7%	-16.7%	-18.5%
SDQ	-	6.3%	-6.1%	-5.8%	-4.2%	-4.9%
SJU	-	10.4%	-14.1%	-14.7%	-4.2%	2.4%
STT	-	20.6%	-4.8%	1.0%	-0.8%	14.4%
TOTAL	-	3.8%	-4.0%	-4.8%	-5.2%	0.4%

Since 2006, American's available seat capacity between MIA and popular Caribbean/Latin destinations has been relatively stable. The 2011 capacity levels are approximately 10% lower than 2006. This is an industry trend among network carriers, and not specific to American or MIA.

AA's capacity has remained steady, while Spirit has added an enormous number of additional seats in these same markets:

Available Seats by Year - Spirit FLL

Market	2006	2007	2008	2009	2010	2011	Total
CUN	100,793	164,292	193,095	126,562	128,537	188,688	901,967
KIN	108,136	176,396	111,467	83,665	84,100	65,458	629,222
MBJ	105,460	141,564	118,124	88,741	95,811	97,440	647,140
NAS	195,276	260,316	189,204	182,990	188,355	170,008	1,186,149
SDQ	153,374	230,892	203,613	172,405	178,640	137,422	1,076,346
SJU	167,910	295,062	313,640	392,641	377,958	344,147	1,891,358
STT	78,274	102,906	86,404	86,130	91,205	91,495	536,414
TOTAL	909,223	1,371,428	1,215,547	1,133,134	1,144,606	1,094,658	6,868,596

Available Seats YOY % Change - Spirit FLL

Market	2006	2007	2008	2009	2010	2011
CUN	-	63.0%	17.5%	-34.5%	1.6%	46.8%
KIN	-	63.1%	-36.8%	-24.9%	0.5%	-22.2%
MBJ	-	34.2%	-16.6%	-24.9%	8.0%	1.7%
NAS	-	33.3%	-27.3%	-3.3%	2.9%	-9.7%
SDQ	-	50.5%	-11.8%	-15.3%	3.6%	-23.1%
SJU	-	75.7%	6.3%	25.2%	-3.7%	-8.9%
STT	-	31.5%	-16.0%	-0.3%	5.9%	0.3%
TOTAL	-	351.4%	-84.7%	-78.0%	18.7%	-15.1%

Within the seven key markets outlined above, Spirit's 2011 capacity levels are approximately 20% higher than 2006 (909,223 v 1,094,658). While this is a large increase, it is critical to evaluate the performance of the flights to truly comprehend the impact this amount of capacity has had on American's MIA operation.

Traffic Comparison to Key Caribbean/Latin Destinations

The amount of additional capacity added by Spirit at FLL is much higher than what Southwest can achieve with their five-gate HOU operation.

But the indications in the FLL/MIA market are indisputable when passenger and load factor data are compared for the last several years. The Spirit growth at FLL has done nothing to harm American's Latin operations from MIA. The traffic that Spirit has gained is net new traffic due to market stimulation, and not dilutive to American at MIA. *There are no indications or market factors that would point to this situation being different in the HOU/IAH marketplace.*

American's passengers for the seven key Caribbean/Latin destinations below have increased between 2006 and 2011 by approximately 9%. Load Factors have increased by 15 percentage points, from 70% in 2006 to 85% in 2011.

On the other hand, Spirit has also enjoyed success in these respective markets since 2006. With an increase of approximately 20% in available seats came an increase in passengers flown of 19%.

Point: there is strong stimulative dynamics in play in Caribbean and Central American markets. The evidence proves that South Florida can accommodate both Spirit and American nonstop flights to Caribbean/Latin destinations. The same is true for the situation at Houston – the WN service will be additive and stimulative to the market. It is not a zero-sum passenger game.

Furthermore, the specific markets being compared are very likely to be similar to first markets entered by Southwest at HOU, further supporting the fact that a market such as Houston can successfully handle nonstop flights by separate airlines at separate airports within the region.

Passengers by Year - American MIA

Market	2006	2007	2008	2009	2010	2011	Total
CUN	295,858	331,198	349,816	325,856	367,285	434,826	2,104,839
KIN	237,206	241,060	248,073	272,239	259,161	275,181	1,532,920
MBJ	267,033	258,270	276,089	307,260	279,430	292,405	1,680,487
NAS	339,909	342,889	356,861	350,586	306,054	254,888	1,951,187
SDQ	421,022	447,355	456,625	454,957	446,042	430,262	2,656,263
SJU	855,763	1,050,518	964,256	863,591	853,518	866,496	5,454,142
STT	169,155	221,167	228,439	232,058	232,174	273,723	1,356,716
TOTAL	2,585,946	2,892,457	2,880,159	2,806,547	2,743,664	2,827,781	16,736,554

Passengers YOY % Change - American MIA

Market	2006	2007	2008	2009	2010	2011
CUN	-	11.9%	5.6%	-6.8%	12.7%	18.4%
KIN	-	1.6%	2.9%	9.7%	-4.8%	6.2%
MBJ	-	-3.3%	6.9%	11.3%	-9.1%	4.6%
NAS	-	0.9%	4.1%	-1.8%	-12.7%	-16.7%
SDQ	-	6.3%	2.1%	-0.4%	-2.0%	-3.5%
SJU	-	22.8%	-8.2%	-10.4%	-1.2%	1.5%
STT	-	30.7%	3.3%	1.6%	0.0%	17.9%
TOTAL	-	70.9%	16.7%	3.2%	-16.9%	28.4%

Load Factors by Year - American MIA

Market	2006	2007	2008	2009	2010	2011	Total
CUN	69.4%	79.5%	78.8%	73.5%	85.7%	85.9%	79.0%
KIN	64.9%	74.7%	77.0%	78.9%	75.7%	82.4%	75.4%
MBJ	73.4%	74.4%	75.6%	80.3%	75.7%	83.2%	77.1%
NAS	74.4%	76.0%	71.7%	72.4%	75.9%	77.6%	74.4%
SDQ	70.4%	70.4%	76.5%	81.0%	82.9%	84.1%	77.2%
SJU	69.9%	77.7%	83.0%	87.2%	89.9%	89.2%	82.0%
STT	71.8%	77.9%	84.5%	85.0%	85.7%	88.3%	82.5%
TOTAL	70.4%	75.9%	78.8%	80.6%	83.1%	85.4%	78.8%

Passengers by Year - Spirit FLL

Market	2006	2007	2008	2009	2010	2011	Total
CUN	78,000	127,337	152,604	80,755	105,481	148,775	692,952
KIN	86,485	134,558	92,530	59,828	55,324	48,836	477,561
MBJ	87,151	106,750	96,959	68,492	67,949	78,897	506,198
NAS	157,862	195,173	145,130	123,262	115,770	119,738	856,935
SDQ	124,778	176,486	153,437	123,892	126,261	109,449	814,303
SJU	148,361	233,214	265,045	313,411	318,398	298,342	1,576,771
STT	64,628	84,440	70,745	67,760	77,728	81,513	446,814
TOTAL	747,265	1,057,958	976,450	837,400	866,911	885,550	5,371,534

Passengers YOY % Change - Spirit FLL

Market	2006	2007	2008	2009	2010	2011
CUN	-	63.3%	19.8%	-47.1%	30.6%	41.0%
KIN	-	55.6%	-31.2%	-35.3%	-7.5%	-11.7%
MBJ	-	22.5%	-9.2%	-29.4%	-0.8%	16.1%
NAS	-	23.6%	-25.6%	-15.1%	-6.1%	3.4%
SDQ	-	41.4%	-13.1%	-19.3%	1.9%	-13.3%
SJU	-	57.2%	13.6%	18.2%	1.6%	-6.3%
STT	-	30.7%	-16.2%	-4.2%	14.7%	4.9%
TOTAL	-	294.3%	-61.8%	-132.1%	34.4%	34.1%

Load Factors by Year - Spirit FLL

Market	2006	2007	2008	2009	2010	2011	Total
CUN	77.4%	77.5%	79.0%	63.8%	82.1%	78.8%	76.8%
KIN	80.0%	76.3%	83.0%	71.5%	65.8%	74.6%	75.9%
MBJ	82.6%	75.4%	82.1%	77.2%	70.9%	81.0%	78.2%
NAS	80.8%	75.0%	76.7%	67.4%	61.5%	70.4%	72.2%
SDQ	81.4%	76.4%	75.4%	71.9%	70.7%	79.6%	75.7%
SJU	88.4%	79.0%	84.5%	79.8%	84.2%	86.7%	83.4%
STT	82.6%	82.1%	81.9%	78.7%	85.2%	89.1%	83.3%
TOTAL	82.2%	77.1%	80.3%	73.9%	75.7%	80.9%	78.2%

Comparison of AA MIA and NK FLL Overall Latin Capacity and LF

Comparing the seven key markets where American and Spirit both had nonstop operations to since 2006 is a solid proxy for the Houston situation. It is also helpful to look at overall Latin capacity and performance for both American and Spirit in South Florida. Latin includes Caribbean, Mexican, and Central/South American nonstops.

Spirit's FLL Latin Capacity, Passengers, and LF by Year

	2006	2007	2008	2009	2010	2011	Total
Passengers	868,781	1,486,321	1,581,805	1,376,421	1,414,556	1,534,632	8,262,516
Seats	1,094,001	1,962,938	2,069,694	1,896,753	1,832,049	1,874,043	10,729,478
Load Factor	79.4%	75.7%	76.4%	72.6%	77.2%	81.9%	77.0%

Spirit's FLL Latin Capacity, Passengers, and LF YOY Change

	2006	2007	2008	2009	2010	2011
Passengers	-	71.1%	6.4%	-13.0%	2.8%	8.5%
Seats	-	79.4%	5.4%	-8.4%	-3.4%	2.3%
Load Factor	-	-3.7	0.7	-3.9	4.6	4.7

American's MIA Latin Capacity, Passengers, and LF by Year

	2006	2007	2008	2009	2010	2011	Total
Passengers	8,713,761	9,585,338	9,884,544	9,363,414	9,619,144	9,909,027	57,075,228
Seats	12,128,271	12,719,880	12,856,097	12,052,530	12,291,127	12,397,145	74,445,050
Load Factor	71.8%	75.4%	76.9%	77.7%	78.3%	79.9%	76.7%

American's MIA Latin Capacity, Passengers, and LF YOY Change

	2006	2007	2008	2009	2010	2011
Passengers	-	10.0%	3.1%	-5.3%	2.7%	3.0%
Seats	-	4.9%	1.1%	-6.3%	2.0%	0.9%
Load Factor	-	3.5	1.5	0.8	0.6	1.7

Spirit Expansion Has Not “Split” International Traffic

The comparison of total capacity reveals that while Spirit has expanded its overall operations at FLL to the point where they now account for 20% of total FLL capacity, American’s capacity share at MIA has been consistent over the last five years.

American accounts for approximately 69% of total capacity offered at MIA on an annual basis, and this has not changed with the expansion of Spirit at FLL. Again, this is evidence that Houston can also support a growing Southwest operation at HOU while United continues to thrive at IAH.

American Share of MIA Total Seat Capacity

	2007	2008	2009	2010	2011
MIA Total	41,874,460	43,309,904	41,470,024	43,078,526	45,536,132
AA Total at MIA	28,813,994	29,658,900	28,510,640	30,027,974	31,052,730
AA % of Total	68.8%	68.5%	68.7%	69.7%	68.2%

Spirit Share of FLL Total Seat Capacity

	2007	2008	2009	2010	2011
FLL Total	28,977,790	28,714,970	26,190,398	27,004,056	27,720,208
NK Total at FLL	4,610,378	5,724,678	5,273,158	5,562,202	5,448,242
NK % of Total	15.9%	19.9%	20.1%	20.6%	19.7%

The FLL/MIA example is very close to the HOU/IAH situation. From this experience, there is no foundation to the allegation that the Southwest plan will be detrimental to IAH.

Appendix

International Trends At Key Airports

Miami International Airport (MIA)						
Load Factor 5-Year Trend						
Region	2007	2008	2009	2010	2011	5-Yr. Chg. 2011 v 2007
Asia	74.8%	74.2%	71.4%	66.0%	68.5%	(6.3)
Australia & Oceania						n/m
Canada	76.7%	72.2%	74.6%	79.6%	78.5%	1.8
Caribbean	70.1%	72.1%	76.2%	74.4%	78.2%	8.1
Central America	69.9%	68.1%	75.0%	75.7%	72.8%	2.9
Europe	82.9%	83.9%	82.5%	83.3%	82.9%	0.0
Mexico	67.6%	72.2%	68.4%	76.7%	76.9%	9.2
Middle East & North Africa	84.8%	81.6%		14.3%		n/m
South America	77.0%	76.6%	71.0%	78.0%	82.3%	5.2
Sub-Saharan Africa	66.7%	69.7%	68.1%	64.0%	65.5%	(1.2)
USA	80.2%	80.5%	81.9%	81.4%	80.3%	0.1
MIA Total	77.4%	77.6%	78.1%	79.3%	79.6%	2.3

Year-Ending September 30

Source: Aviation DataMiner © - RITA BTS T100 Traffic

Houston Intercontinental Airport (IAH)						
Load Factor 5-Year Trend						
Region	2007	2008	2009	2010	2011	5-Yr. Chg. 2011 v 2007
Asia	79.4%	80.3%	78.0%	81.9%	80.6%	1.2
Australia & Oceania			62.2%			n/m
Canada	71.4%	72.5%	67.9%	74.8%	74.4%	3.0
Caribbean	75.6%	79.8%	74.6%	72.6%	73.2%	(2.4)
Central America	75.5%	73.1%	74.8%	73.7%	75.8%	0.3
Europe	73.9%	71.2%	71.2%	74.8%	74.1%	0.2
Mexico	73.9%	76.8%	75.8%	80.2%	74.8%	0.9
Middle East & North Africa		81.2%	71.0%	72.0%	65.9%	n/m
South America	78.8%	79.1%	76.6%	78.6%	77.6%	(1.2)
Sub-Saharan Africa	65.1%	85.3%	76.4%	74.5%	75.5%	10.4
USA	79.7%	79.6%	79.7%	80.9%	79.6%	(0.0)
IAH Total	78.7%	78.7%	78.6%	80.0%	78.5%	(0.2)

Year-Ending September 30

Source: Aviation DataMiner © - RITA BTS T100 Traffic

Newark Liberty International Airport (EWR)						
Load Factor 5-Year Trend						
Region	2007	2008	2009	2010	2011	5-Yr. Chg. 2011 v 2007
Asia	80.0%	77.4%	75.7%	85.5%	83.1%	3.1
Australia & Oceania						n/m
Canada	70.6%	67.3%	62.2%	68.4%	67.5%	(3.1)
Caribbean	83.2%	84.3%	87.7%	85.5%	85.6%	2.4
Central America	81.4%	81.4%	86.1%	85.4%	83.9%	2.5
Europe	78.9%	77.0%	75.9%	83.1%	80.4%	1.5
Mexico	82.1%	85.8%	82.7%	84.1%	80.5%	(1.5)
Middle East & North Africa	86.7%	85.4%	83.1%	85.4%	84.8%	(1.9)
South America	77.5%	80.8%	83.0%	81.3%	77.9%	0.4
Sub-Saharan Africa	78.4%	77.2%	76.8%	71.9%	73.1%	(5.3)
USA	79.5%	78.1%	76.4%	78.4%	77.4%	(2.1)
EWR Total	79.3%	77.9%	76.2%	79.3%	78.0%	(1.4)

Year-Ending September 30

Source: Aviation DataMiner © - RITA BTS T100 Traffic

Fort Lauderdale-Hollywood International Airport (FLL)						
Load Factor 5-Year Trend						
Region	2007	2008	2009	2010	2011	5-Yr. Chg. 2011 v 2007
Asia	51.2%	48.8%			66.5%	15.3
Australia & Oceania						n/m
Canada	79.3%	83.7%	85.2%	85.7%	86.1%	6.8
Caribbean	68.4%	67.7%	68.3%	66.9%	74.9%	6.4
Central America	78.8%	74.7%	73.5%	80.8%	81.9%	3.1
Europe	76.6%	66.9%	76.2%	81.5%	85.1%	8.5
Mexico	67.4%	80.5%	64.4%	79.5%	78.6%	11.2
Middle East & North Africa						n/m
South America	72.7%	69.8%	73.2%	73.3%	80.7%	8.1
Sub-Saharan Africa	55.8%	65.0%				n/m
USA	78.5%	79.1%	80.4%	81.2%	82.1%	3.6
FLL Total	77.5%	78.1%	79.2%	80.0%	81.6%	4.2

Year-Ending September 30

Source: Aviation DataMiner © - RITA BTS T100 Traffic

Chicago O'Hare International Airport (ORD)						
Load Factor 5-Year Trend						
Region	2007	2008	2009	2010	2011	5-Yr. Chg. 2011 v 2007
Asia	79.4%	80.3%	78.0%	81.9%	80.6%	1.2
Australia & Oceania			62.2%			n/m
Canada	71.4%	72.5%	67.9%	74.8%	74.4%	3.0
Caribbean	75.6%	79.8%	74.6%	72.6%	73.2%	(2.4)
Central America	75.5%	73.1%	74.8%	73.7%	75.8%	0.3
Europe	73.9%	71.2%	71.2%	74.8%	74.1%	0.2
Mexico	73.9%	76.8%	75.8%	80.2%	74.8%	0.9
Middle East & North Africa		81.2%	71.0%	72.0%	65.9%	n/m
South America	78.8%	79.1%	76.6%	78.6%	77.6%	(1.2)
Sub-Saharan Africa	65.1%	85.3%	76.4%	74.5%	75.5%	10.4
USA	79.7%	79.6%	79.7%	80.9%	79.6%	(0.0)
ORD Total	78.7%	78.7%	78.6%	80.0%	78.5%	(0.2)

Year-Ending September 30

Source: Aviation DataMiner © - RITA BTS T100 Traffic

MOODY'S

INVESTORS SERVICE

SPECIAL COMMENT

Southwest meets the Southeast

Unexpected Credit Benefits of Airline Competition for U.S. Southeast Regional Airports

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Executive Summary

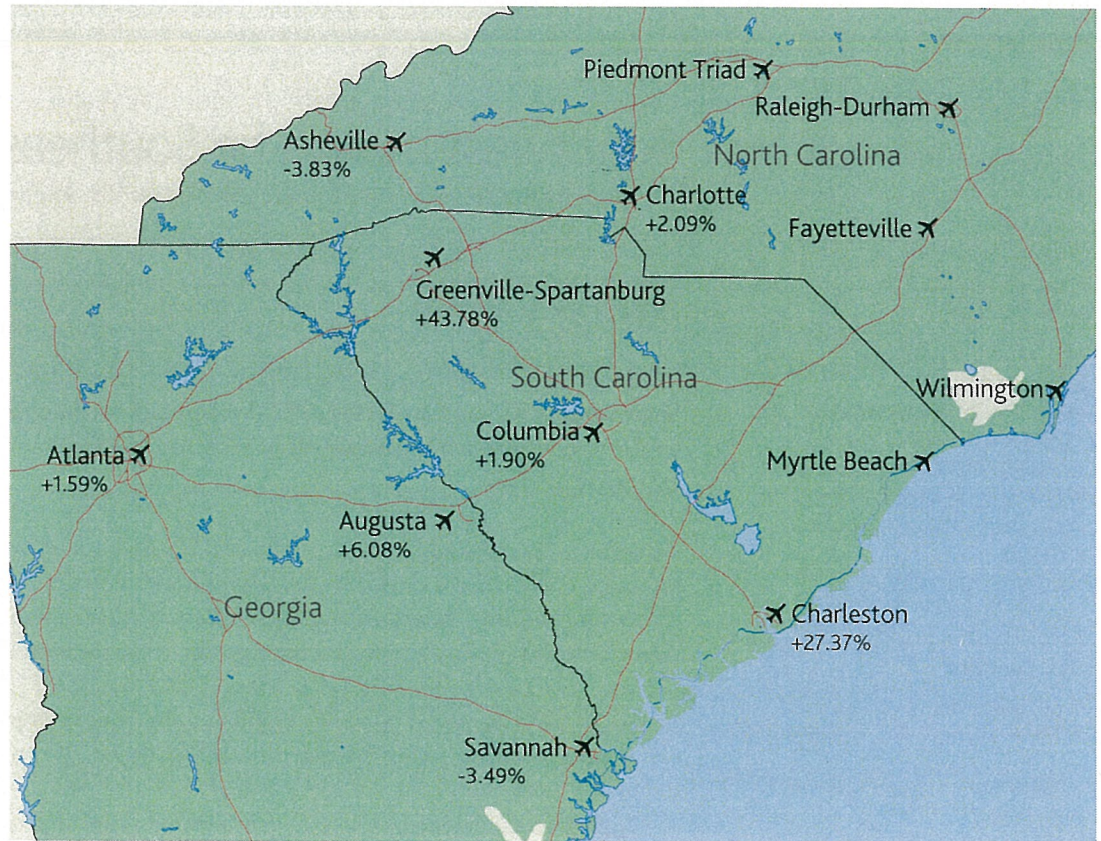
In March 2011, Southwest Airlines (Baa3, stable) began daily service to both Greenville-Spartanburg, SC and Charleston, SC. Average airfares dropped immediately, while enplanements increased substantially at each airport. The improved performance at the two airports is dramatic.

To counter Southwest's entrance, Delta and US Airways reduced their regional airfares. The increased enplanement caused by the additional competition is above the levels seen at other competing airports. Increased enplanements will improve non-airline revenues at regional airports, which Moody's views as credit positive for Southeast airports.

In this Special Comment, Moody's highlights the positive impacts of new airline competition on local/regional airports in the Southeast. Key observations include:

- » Increased enplanement levels do not increase airline derived revenue, as residual rate-making agreements calculate airline revenues on a cost recovery basis. It does however result in lower costs per enplanement, which could further decrease airfares and propel enplanements higher.
- » Airports with hybrid or compensatory rate-making structures will likely see increased non-airline revenues, such as concessions, parking, or rental car revenues, providing additional cash flow. This additional cash will support credit through increased liquidity levels or reduced debt to complete capital improvement projects.

FIGURE 1
Enplanement growth, rolling 12 months through Feb. 2012



Source: Respective airport websites.

Southeast Region Traditionally Underserved by Low-Fare Airlines

The Georgia/South Carolina/North Carolina commercial airport market is largely defined by two major large hub airports (Atlanta – Hartsfield Jackson International Airport, A1, positive and Charlotte International Airport, Aa2, stable) and several small regional airports. Atlanta serves as Delta's (B2 CFR, stable) main hub for the United States and Charlotte serves as US Airways' (B2, stable) main east coast hub. Due to the presence of these hubs, market share at most of the regional airports is dominated by Delta and US Airways. The combined market share of Delta and US Airways was greater than 58% at all of the fourteen largest airports in the region, with the exception of Raleigh-Durham International Airport (Aa3, stable) and Myrtle Beach (Horry County Airport Enterprise, A3, stable). Equally important, only Atlanta, Asheville Regional Airport (NR), and Raleigh-Durham had service from low-cost carriers.

The lack of low cost carriers and limited competition among the legacy carriers historically resulted in average airfares well above national averages at the Southeast regional airports. Only RDU and neighboring Piedmont Triad Airport (A3, stable) had airfares below the national average. These airports are located in the northern portions of North Carolina and were not easily reachable by travelers in Georgia, South Carolina or the southern portions of North Carolina. The other regional airports experienced average fares 26.7% higher and 20.1% higher than national averages in 2009 and 2010, respectively. Airfares at the two regional hubs were also above average.

TABLE 1

Regional Airfare Comparison, \$ per Ticket

	Q1-09	Q2-09	Q3-09	Q4-09	Q1-10	Q2-10	Q3-10	Q4-10
National Average	\$314	\$302	\$307	\$320	\$328	\$341	\$340	\$335
Hubs ¹	\$337	\$306	\$305	\$333	\$360	\$350	\$337	\$331
	7.4%	1.3%	-0.7%	4.1%	9.7%	2.7%	-0.7%	-1.2%
Airports with Low-Cost Competition ²	\$273	\$270	\$275	\$285	\$307	\$328	\$315	\$313
	-13.1%	-10.5%	-10.5%	-10.9%	-6.6%	-3.7%	-7.2%	-6.4%
Other Regional Airports ³	\$398	\$380	\$382	\$403	\$418	\$407	\$388	\$400
	26.7%	25.9%	24.4%	26.0%	27.3%	19.5%	14.3%	19.6%

Notes:

1 – Includes Atlanta-Hartsfield Jackson International Airport (ATL) and Charlotte International Airport (CLT)

2 – Includes Raleigh-Durham International Airport (RDU) and Piedmont Triad International Airport (PTI)

3 – Includes Asheville Regional Airport (AVL), Augusta Regional Airport (AGS), Charleston County International Airport (CHS), Columbia Metropolitan Airport (CAE), Fayetteville, NC Regional Airport (FAY), Greenville-Spartanburg International Airport (GSP), Myrtle Beach International Airport (MYR), Savannah-Hilton Head International Airport (SAV), and Wilmington, NC International Airport (ILM)

Source: Bureau of Transportation Statistics

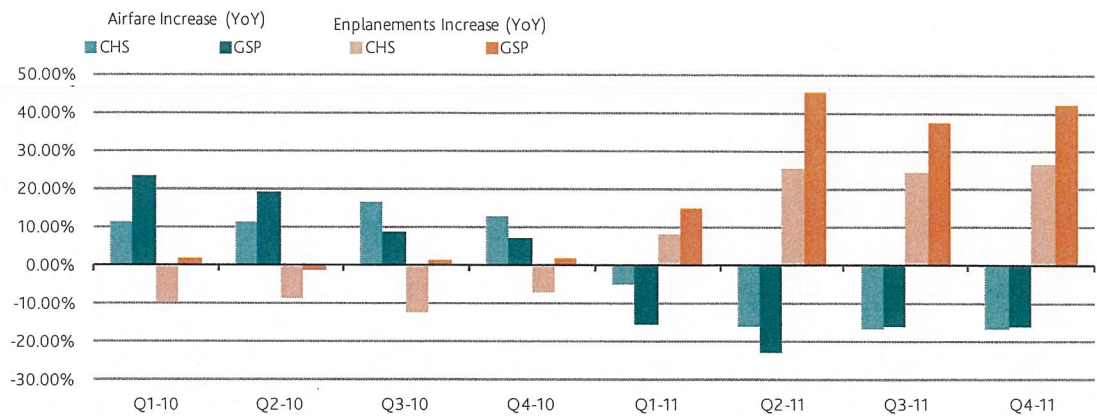
In the second half of 2010, both Delta and US Air began to lower fares at their respective hubs. Lower fares and the larger number of direct flights into Charlotte drew traffic away from neighboring regional airports, including Columbia Metropolitan Airport (Richland-Lexington Airport District, Baa1, stable), Greenville-Spartanburg International Airport (Greenville-Spartanburg Airport District, A2, stable) and Fayetteville Regional Airport (NR). Meanwhile, Savannah-Hilton Head International Airport (A1, stable) saw the departure of AirTran airlines in 2010, which resulted in higher average airfares at Savannah as well as nearby Charleston County International Airport (A1, stable). These higher fares resulted in lower enplanements.

Southwest Meets the Southeast

In March 2011, Southwest began a daily service to both Greenville-Spartanburg and Charleston. Average airfares dropped immediately, while enplanements increased substantially at each airport. When compared to national averages for airfares and enplanement levels, the growth at these airports was dramatic.

FIGURE 2

Airfare and enplanement growth at airports with Southwest service versus national averages



Note: Increases are versus national averages for the respective quarters.

Source: Bureau of Transportation Statistics.

The immediate impact on neighboring airports was predictable. Asheville saw declines through the end of 2011. Columbia continued to see enplanement declines through the summer of 2011. Savannah saw increased enplanement declines as travelers moved to Charleston, as well as the loss of Allegiant. By Q3 2011, even Charlotte began to see enplanement declines.

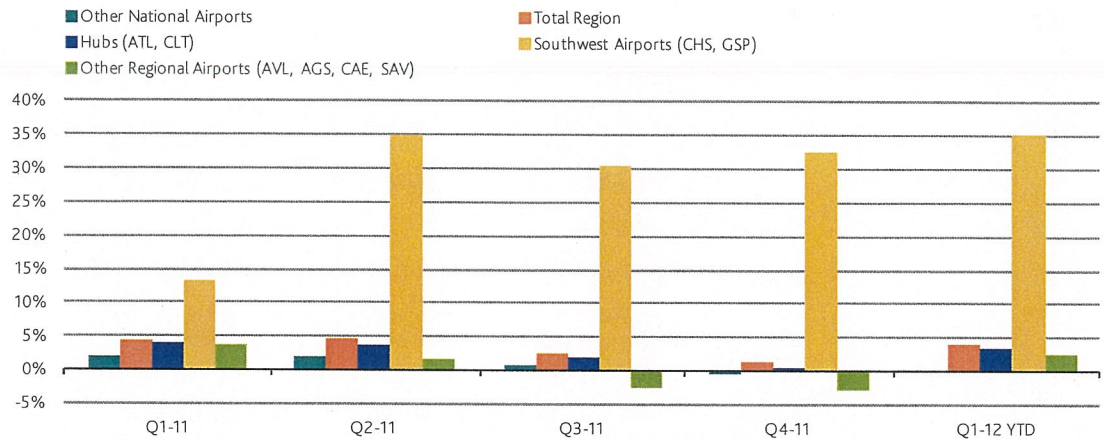
However, beginning in early fall, signs of unexpected travel patterns began to appear. Augusta Regional Airport (Baa2, stable) continued to see enplanement growth and Columbia began to see significant enplanement increases for the first time in nearly 5 years. By the fourth quarter of 2011 average fares at the airports closest to and including the Southwest airports (Asheville, Augusta, Columbia, and Savannah) had fallen to only 115% of national average fares, from 130% in the second quarter of 2010. This confirms anecdotal evidence from regional airports that Delta and US Airways have reduced fares not only on competing routes at Greenville-Spartanburg and Charleston, but within the region as a whole.

Laws of Price Elasticity Hold, Lower Fares Increase Demand for Travel

The study region has shown total domestic enplanement growth above that seen by other US airports. Although Savannah continues to lose enplanements, all other regional airports are showing enplanement growth year-to-date in 2012¹. From an airside revenue perspective, the increase in enplanements will reduce cost per enplanement, which will serve to further reduce fares (controlling for fuel cost) and could serve to further stimulate market demand. However, the most significant positive development for airport revenues will come from cost centers outside of most airline use agreements, such as concessions, parking, and customer facility charge revenues. Concession, parking, and car rental revenues derived from increased usage levels will largely go to the airports under the hybrid and compensatory airline agreements seen at most of the regional airports. Moody's views the growth of non-airline revenues as credit positive because it diversifies the revenue stream and provides non-restricted cash that airports can use for added liquidity or cash funded capital improvements. We recognize that ultimately growth in non-airline revenues is correlated to enplanement growth however increasing diversity of revenues is comparatively credit positive.

¹ The Bureau of Transportation Statistics has not released any aggregate level national data for enplanements. Increases shown are based on individual airports self-reported enplanement levels.

FIGURE 3
Enplanement increases (YoY)



Source: 2011 Enplanements: Bureau of Transportation Statistics; 2012 Enplanements: Respective airport websites

Regional dynamics may shift even further throughout 2012 as Southwest continues to operationally integrate with AirTran, and if a proposed US Airways/American Airlines (AMR, WR) merger is completed. For the first time, Southwest will have a presence in Atlanta. Southwest currently provides service to 40 cities that are not currently served by AirTran. It is still not clear how Southwest will choose to utilize its Atlanta gates, but if the past year is any guide, lower fares from airline competition will grow the market for travel in the Southeast to the benefit of all airports.

Moody's Related Research

Outlook:

- » [US Airports: Trends Indicate Another Difficult Year Ahead, January 2012 \(138859\)](#)

Special Comments:

- » [American Airlines Takeover Would Bring Turbulence to US Airport, January 2012 \(139335\)](#)
- » [US Airport Medians for FY2010, November 2011 \(137061\)](#)

Rating Methodology:

- » [Airports with Unregulated Rate Setting, July 2011 \(133793\)](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

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