

What we were . . .

What We've Done . . .

What We're Facing . . .



Based on a summary of the first 12 months of Hughes Air Corp. management presented by Irving T. Tague, vice president and general manager of Hughes Airwest to the Civil Aeronautics Board, July 16, 1971.

INTRODUCTION

This obviously is not the happiest time in the airline industry's history.

We do not plan to try and show that everything is rosy at Hughes Airwest; that all the problems have been solved since the present management took over.

We will attempt to show how far we have come, what has been done, what the effect has been, and what the major problems facing Hughes Airwest appear to be.

We can see some possible solu-

tions. We're facing manageable, not unmanageable, problems.

Two years ago Hughes Airwest was on the brink of disaster. We now feel that Hughes Airwest is a well operated airline that is making progress and providing good service.

Hughes Airwest, like other airlines, is facing severe economic pressures.

Employee productivity is the key to increased total revenue for the airline.

The merger between Pacific Airlines, West Coast Airlines and Bonanza Air Lines took effect on July 1, 1968.

In 1968 expenses were \$65.2 million. Revenues, or money brought into the company, were only \$62.1 million.

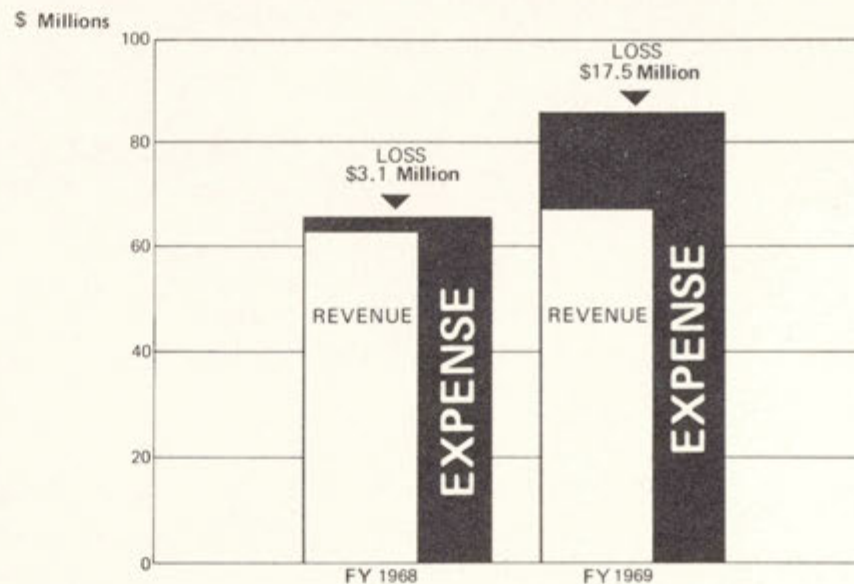
In 1969 our expenses were up to \$85.5 million with revenues of only \$68 million.

Like any company, there are many costs over and above a payroll to keep us in operation.

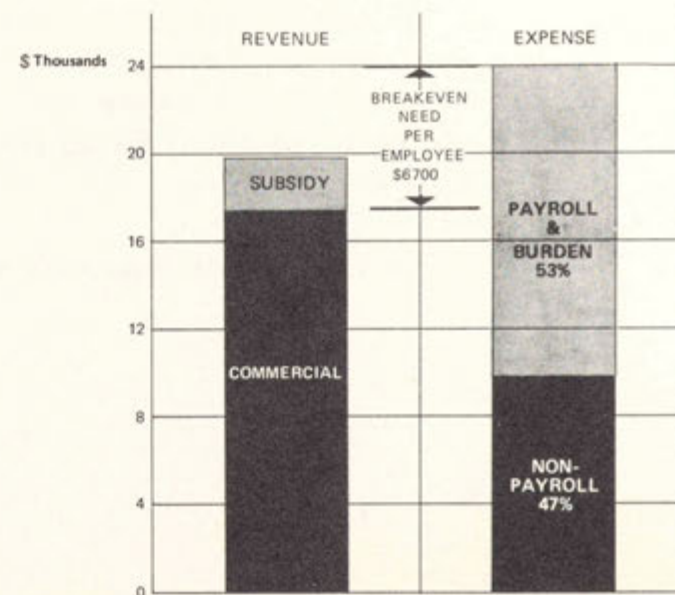
If we were to take all costs and all revenues and divide the sum by the number of employees, this is what it would look like for Hughes Airwest.

In 1969 we took in \$19,800 per employee, while we spent \$24,000 per employee. Thus we needed to earn \$4,200 per employee just to break even — but didn't. The \$4,200 gap includes subsidy. Without it, the difference would have been \$6,700 per employee.

OPERATING REVENUE AND EXPENSE 1968 - 69



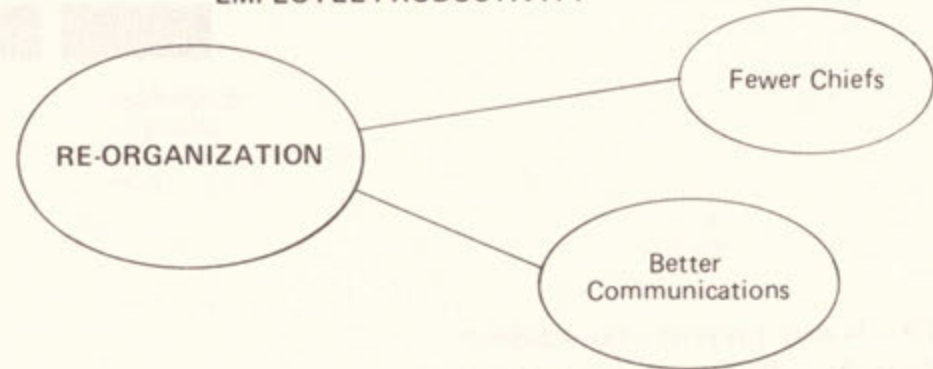
OPERATING REVENUE AND EXPENSE PER EMPLOYEE 1969



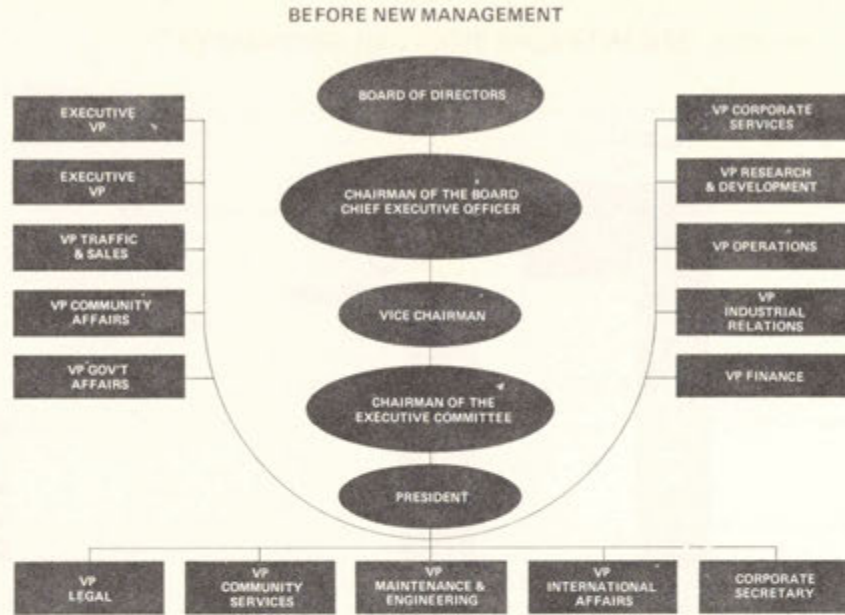
Hughes Airwest took control in April, 1970. With an enormous job ahead of us we had to map our plan of action: Our goal was to *increase employee productivity*.

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MANAGEMENT TO INCREASE EMPLOYEE PRODUCTIVITY

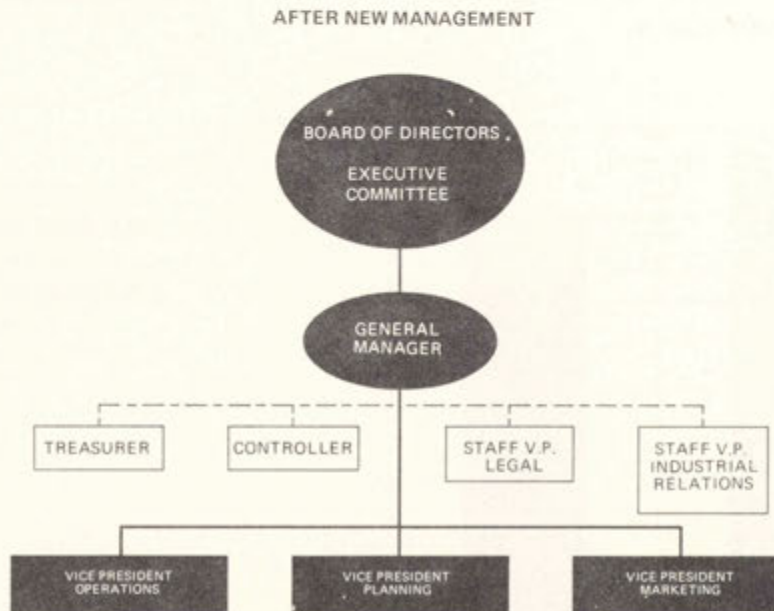


Before the takeover by Hughes Air Corp., the airline's organizational chart showed too many chiefs: 14 vice presidents, 8 assistant vice presidents (not shown) and 5 "chief executive officers," including a corporate secretary.



This is our present organizational chart. It calls for three operating vice presidents, one of which has yet to be filled.

It's a streamlined organizational chart and the end result is improved management communications.



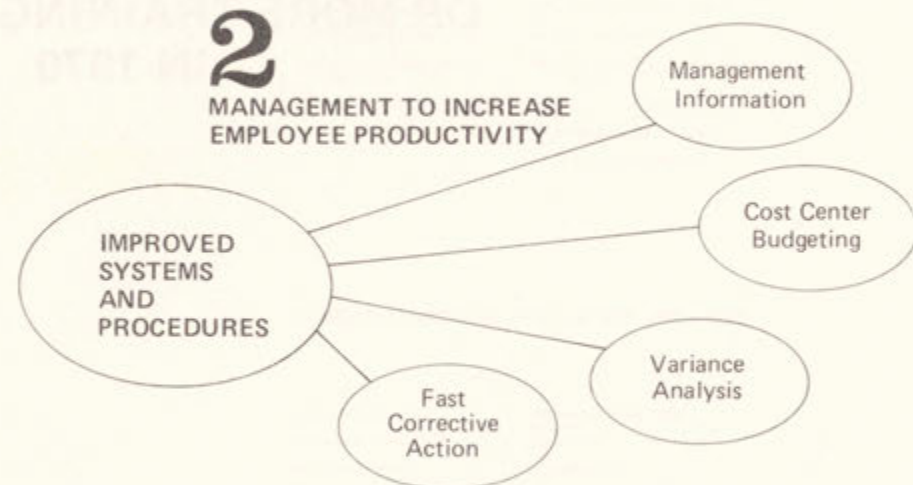
A number of steps had to be taken to increase employee productivity.

By reorganization we increased management information.

Another means to increase management information is budgeting. We now have a profit-and-loss statement, showing what we've earned and spent each month, by the 10th working day of the following month.

Budgeting, coupled with the financial studies (such as the profit-and-loss statement), gives management the ability to pinpoint where we are financially and, more important, to see where we are losing money.

Thus we can react and take fast corrective action.



SYSTEMWIDE TRAINING

APPROXIMATELY 3000 EMPLOYEES
(OUT OF 3530) ATTENDED ONE
OR MORE TRAINING COURSES
IN 1970

Training played an important role in our reorganization. We trained and retrained all Hughes Airwest employees who have contact with the public.

All airlines have continuous training of their flight and maintenance crews as well as new personnel. This chart shows the courses in the Air West training program when Hughes Air Corp. took over in April, 1970.

We added 36 new courses over and above the existing training program.

We have, in effect, completely retrained our supervisors, hostesses, reservationists, salesmen, and station agents.

TRAINING COURSES IN EFFECT APRIL 1970

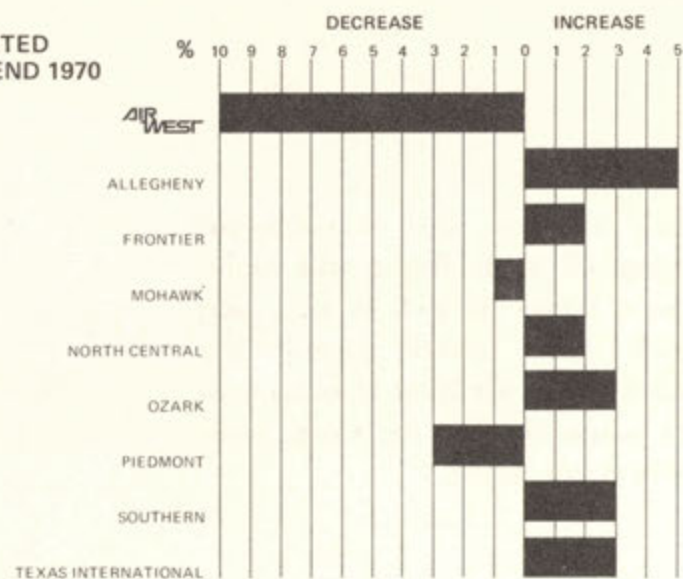
Initial Ramp Agent	F-27 Recurrent/Freon System
Initial Station Agent	F-27 Recurrent/Winter Operations
Initial Operations Agent	F-27 Recurrent/Pneumatics
Initial Reservations Agent	Initial Inspection
Supervision Basic	Basic Indoctrination - Maintenance
Initial Hostess	F-27 Maintenance Home Study
Recurrent Hostess	DC-9 Initial Maintenance
Weight and Balance	DC-9 Initial Electrical (R & E)
F-27 Initial Maintenance	DC-9 Initial Run-Up, Taxi and Trim
F-27 Initial Electrical (R & E)	DC-9 Initial FD-108 Integrated Flight (R & E)
F-27 Initial Run-Up, Taxi and Interconnect	DC-9 Recurrent/Electrical (R & E)
F-27 Recurrent/Propeller	DC-9 Recurrent/APU
F-27 Recurrent/Flight Controls and Rigging	DC-9 Recurrent/Air Conditioning System
F-27 Recurrent/Electrical (R & E)	DC-9 Recurrent/Hydraulic System
	DC-9 Recurrent/Electrical System
	DC-9 Maintenance Home Study

TRAINING COURSES STARTED AFTER APRIL 1970

Supervision Intermediate	Maintenance Posing Course
Supervision Advanced	Initial Supply
Management Development	Recurrent/Supply
Creative Management	Catering
Hostess Regualification	Air Freight
Hostess Standards	Air Freight Procedures for Supervisors
Effective Listening	Ticketing, Basic
Data Processing	Ticketing, Recurrent
F-27 Initial Avionics (R & E)	Tariff, Basic
F-27 Recurrent/AC Deicing Generator System	Tariff, Intermediate
F-27 Recurrent/Avionics (R & E)	PNR Computer Training (All Station Personnel)
F-27 Home Study	Mexico Station Special Training
DC-9 Initial Avionics (R & E)	Orientation Training for Sales Representatives (New York, Chicago, Miami)
DC-9 Initial Radar (R & E)	Technical Assistance Training for Air Vietnam Personnel
DC-9 Initial DME (R & E)	Travel Agency Training
DC-9 Initial Radio Altimeter (R & E)	Reservation Home Study
DC-9 Recurrent/Pneumatic ITCAN	Station Home Study
DC-9 Recurrent/Avionics (R & E)	
Basic Electrical Maintenance (Shop)	

In order to save money, we grounded or disposed of 10 airplanes that were uneconomical to operate.

NUMBER OF AIRCRAFT OPERATED BEGINNING AND END 1970

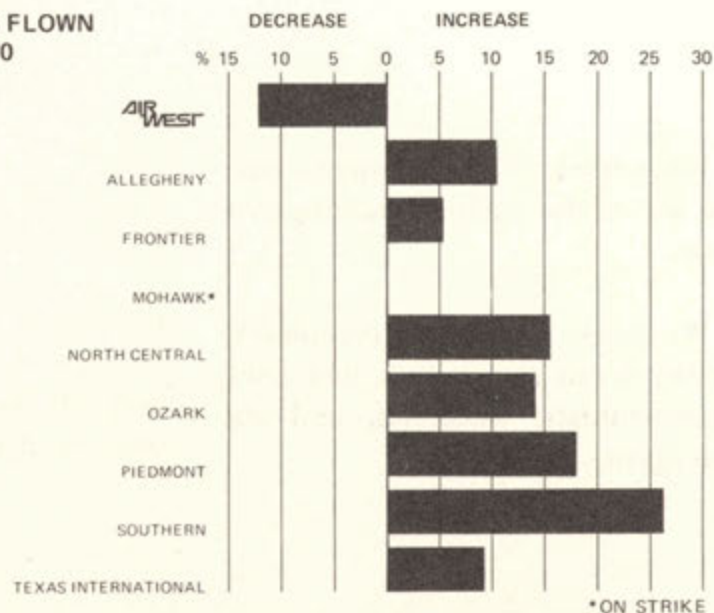


While other airlines were increasing their miles flown, we were decreasing ours.

We reduced shorthaul trips that were costly and non-productive.

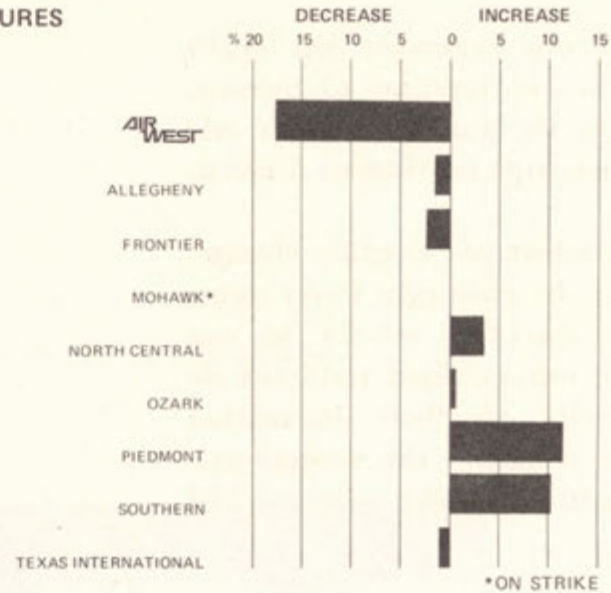
We did this by rescheduling the airline and cutting the number of aircraft miles flown... thus decreasing our revenue miles flown.

REVENUE MILES FLOWN 1969 - 1970



AIRCRAFT DEPARTURES
1969 - 1970

The result was that we were able to reduce our departures around 17 per cent.

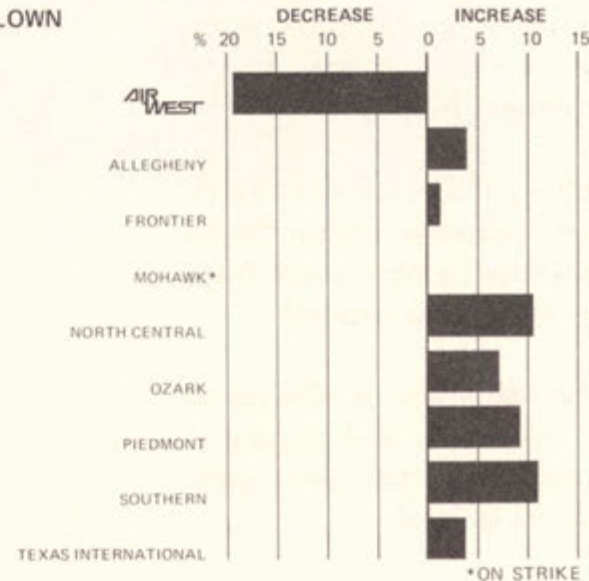


REVENUE HOURS FLOWN
1969 - 1970

It costs us money to be in the air. Fuel and personnel expenses alone are high.

By (1) cutting our airplane miles, (2) grounding our older, more expensive airplanes and (3) reducing our departures, we reduced our time in the air.

Thus we cut our revenue hours flown.



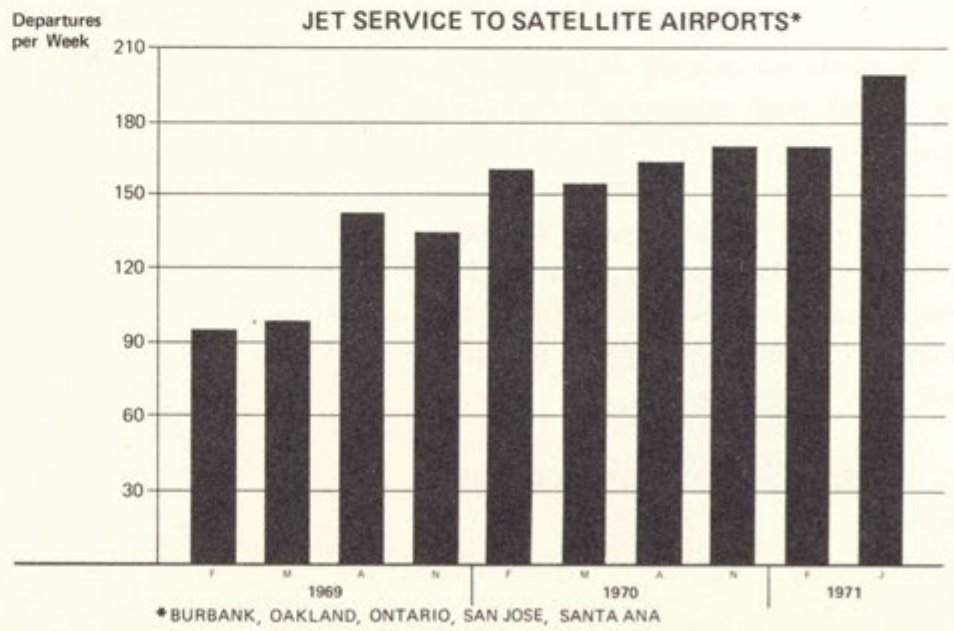
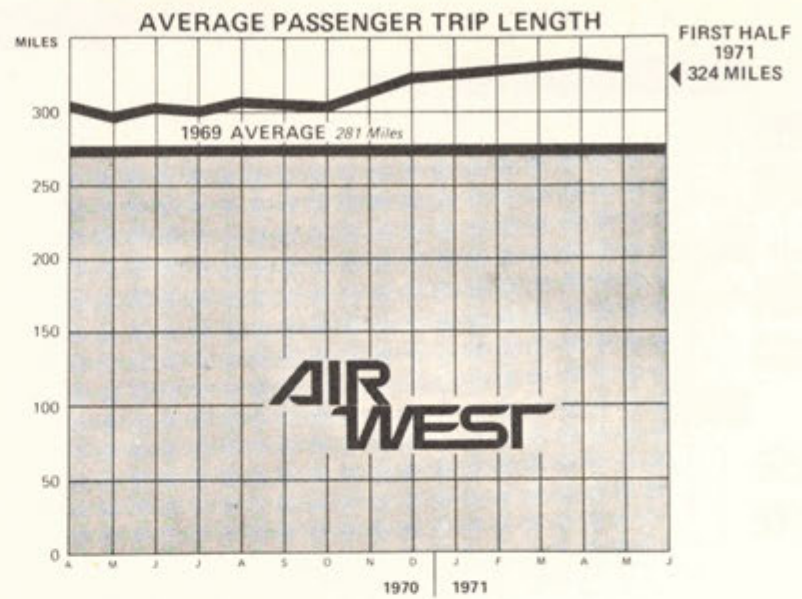
When our passenger trip length increases, our revenue, or income, increases. We want passengers taking longer trips on Hughes Airwest.

As a result of schedule changes that give the passenger fewer stops, better connecting service to our own and other airlines and more direct service to their destination city, we increased the average passenger trip from 281 miles to 324 miles.

A concentration of flights into large, metropolitan airports keep our planes in the air longer due to air traffic congestion.

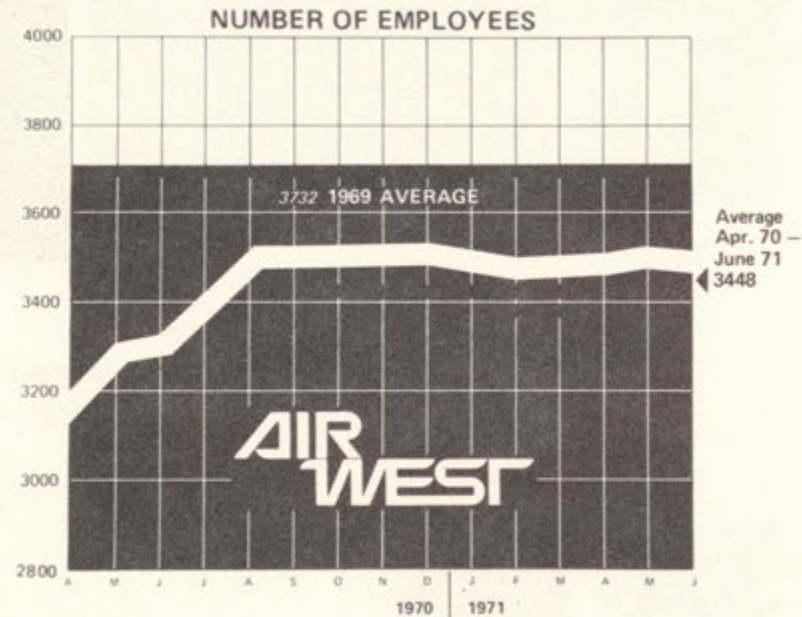
We added jet operations to satellite airports (airports within 60 to 90 minutes driving time away from a major metropolitan airport).

Thus better service is offered to suburban customers and money is saved through less time spent waiting to take off or land.



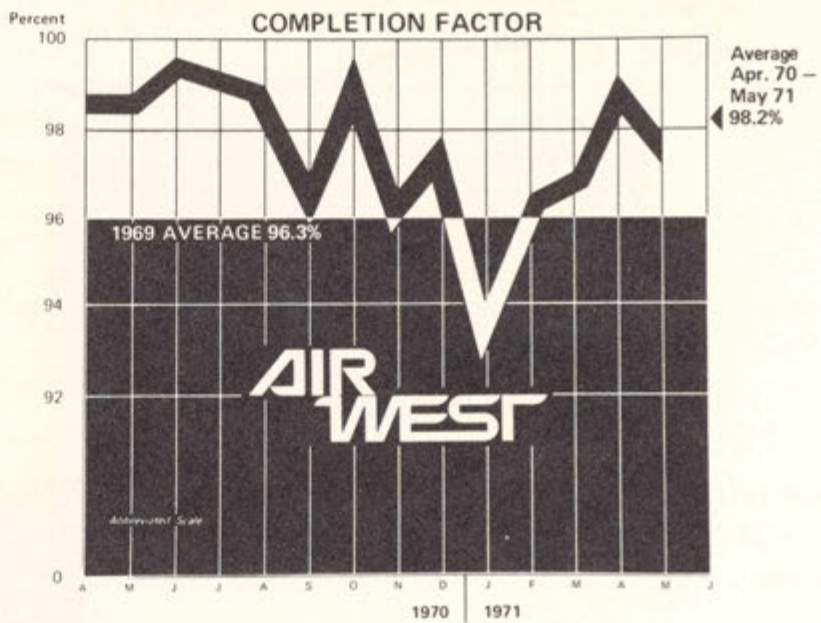
We had to reduce the number of employees because the airline was losing money.

We went down from 3,700 employees in 1969 to 3,200 employees currently.



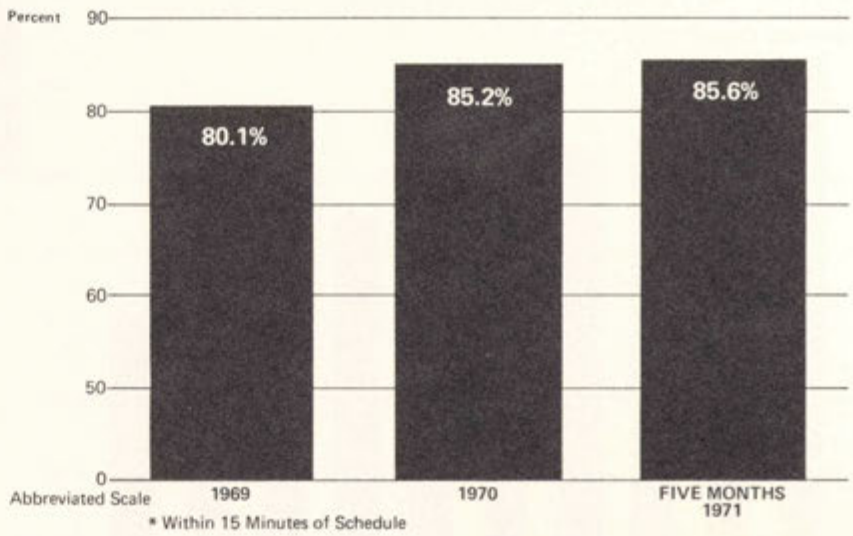
With all these changes came improvements.

Our airplanes completed more trips. Our completion factor went up from 96 per cent to more than 98 per cent.

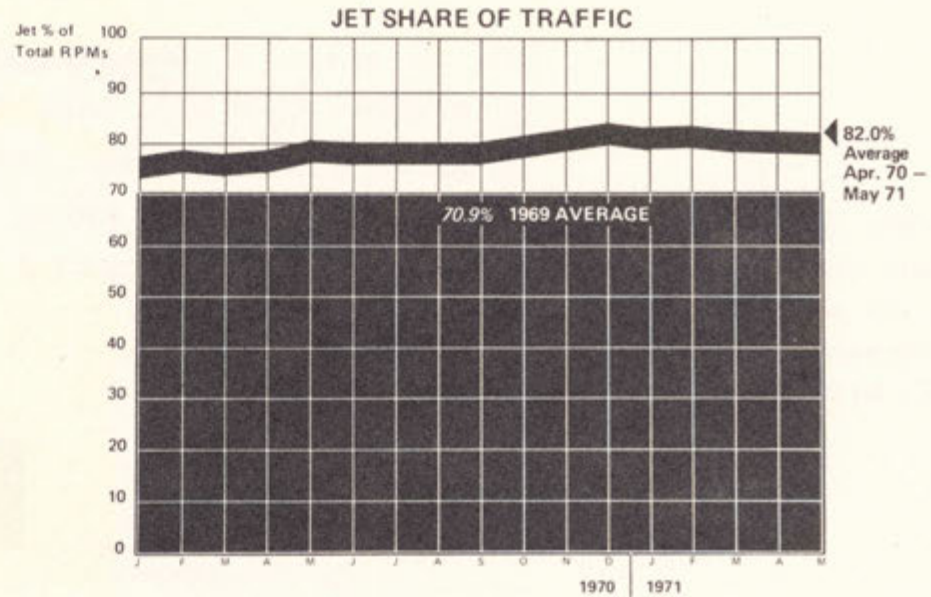


Our airplanes were on-time. We are now operating at 85 per cent on-time. This 85 per cent is an average for our entire system of 72 airport stations.

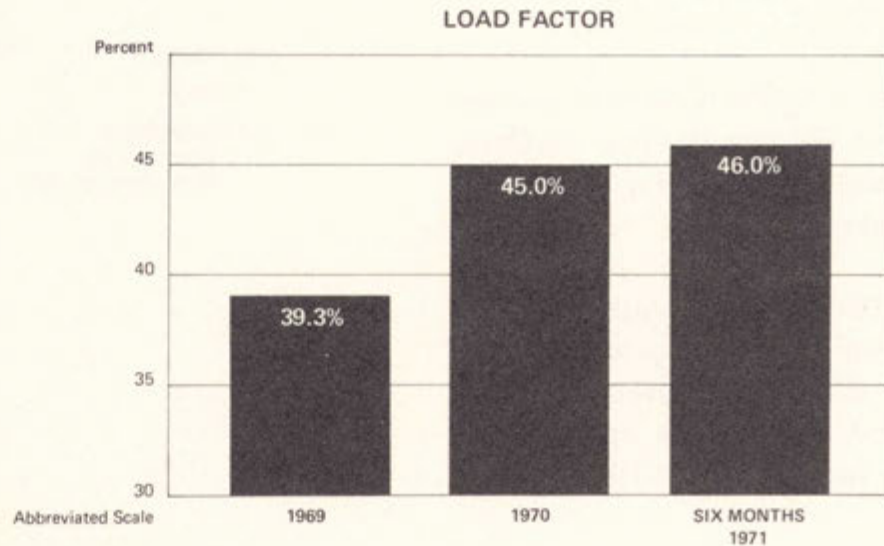
ON TIME PERFORMANCE



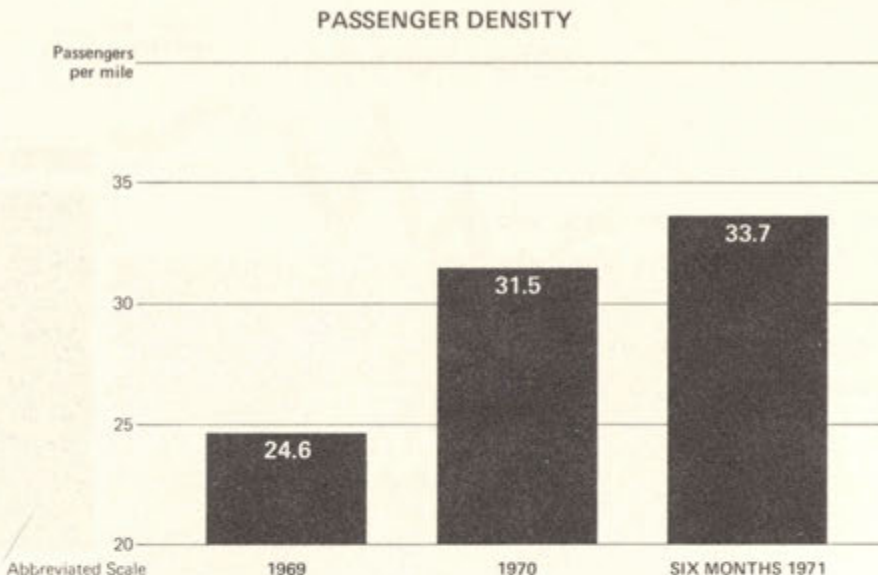
More of our passengers are receiving the jet service they desire. More than 82 per cent of our income from passenger traffic, or revenue passenger miles, is on jets.



Our load factor has improved. We've been filling our planes.

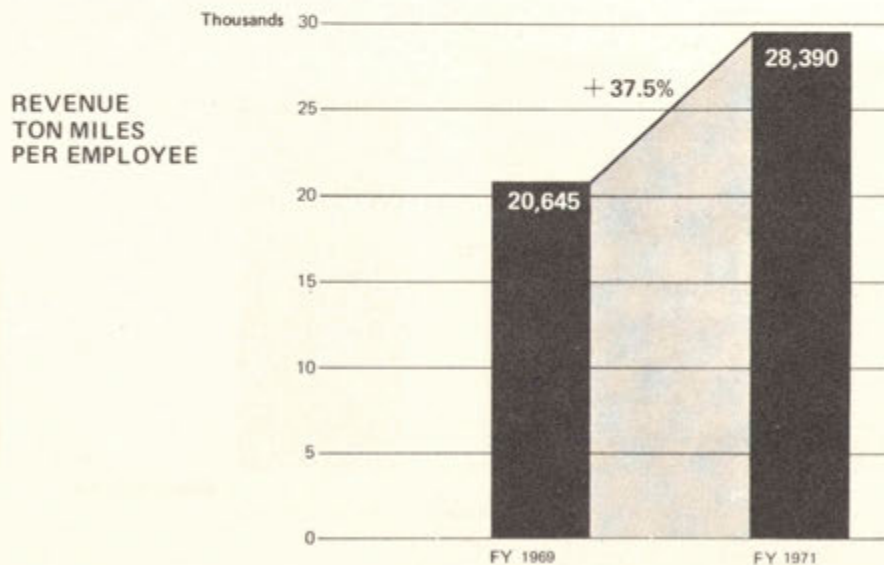


More indicative, our passenger density (average number of passengers per mile) has improved from 24.6 passengers for every plane mile we fly to the current 33.7.



Improving the quality of our service and holding the line on flying hours and the number of employees has paid off.

In 1971 our revenue ton miles per employee (or percentage of planes filled with revenue passengers and cargo) was up 37.5 per cent in two years over 1969.

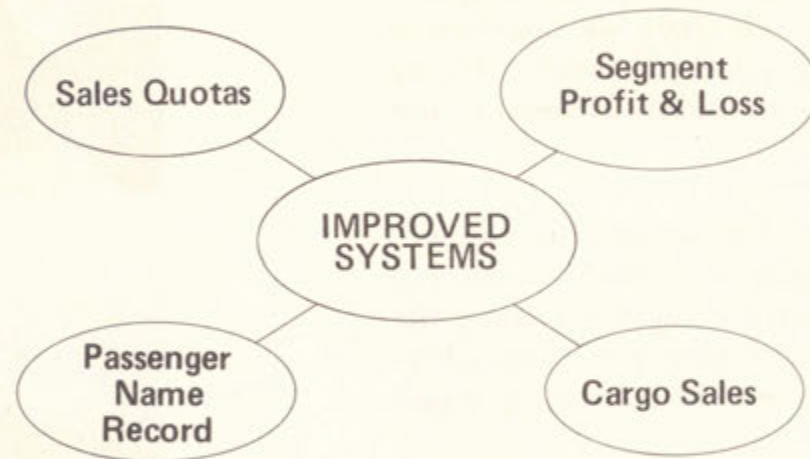


We've explained a few of the changes we made and the results of these changes. Still more had to be done and is being done to improve our financial situation.

Sales quotas have been established, implemented and are regularly checked.

We also have financial reports for each segment, or flight, in our system. This is called a segment profit-and-loss statement.

We have been working on our cargo sales. Our ton miles are up 25 per cent over last year.



Our old reservations system was inadequate. We were faced with doing something about it right after the April, 1970 takeover.

We chose the Mutual Computer Services subsidiary of Continental Airlines, joining in time sharing with Continental, Piedmont and Ozark.

Using this system, the cost per passenger is 14 cents. If we had put in our own computer system, the cost would have been somewhere between 50 and 60 cents per passenger.

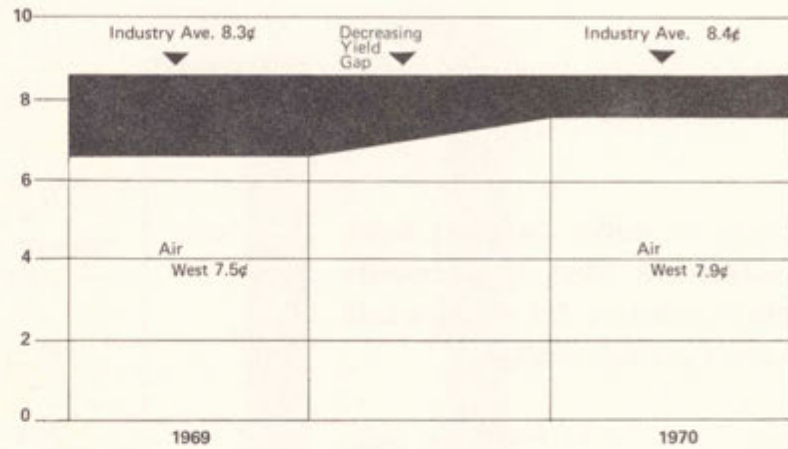
This new system makes it possible for us to implement new marketing surveys using information about the passenger that is received from the computers.



One of our major problems was yield, or how much we receive per revenue passenger mile.

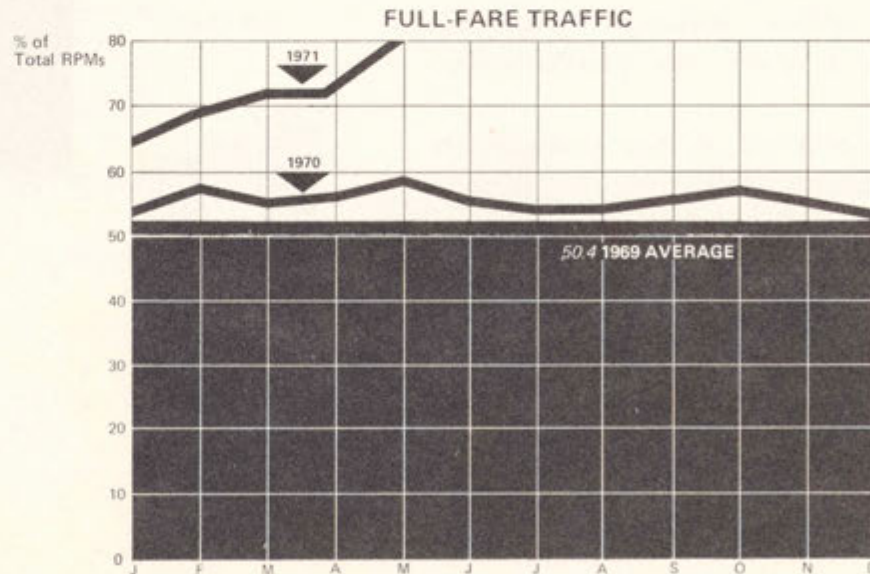
We had a yield gap. In other words, our yield was not up to average with the rest of the airline industry. If Hughes Airwest yields in 1970 had been at the local service industry average, Hughes Airwest revenues would have been \$5 million higher. This amount would have accounted for three-fourths of our total operating loss in 1970.

COMPARISON OF YIELD PER PASSENGER MILE



The yield problem is two-fold: We had too many discounts and too small a share of full fare traffic. We discontinued several discount fares, such as the Discover America Fare, in an attempt to get full fare passengers.

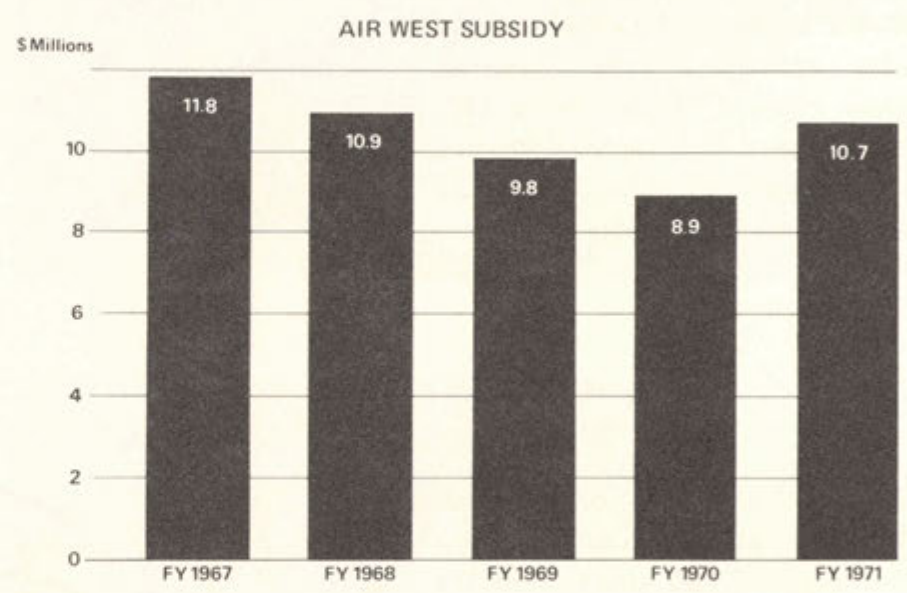
Now our full fare traffic is more than 80 per cent.



Subsidy is dollar funding from the government that supplements the airline industry for monies lost due to unprofitable routes.

From Fiscal Year 1968 on, subsidy for Hughes Airwest, as well as for the other regionals, had dropped sharply – faster than we could offset inflation with increased revenue and productivity.

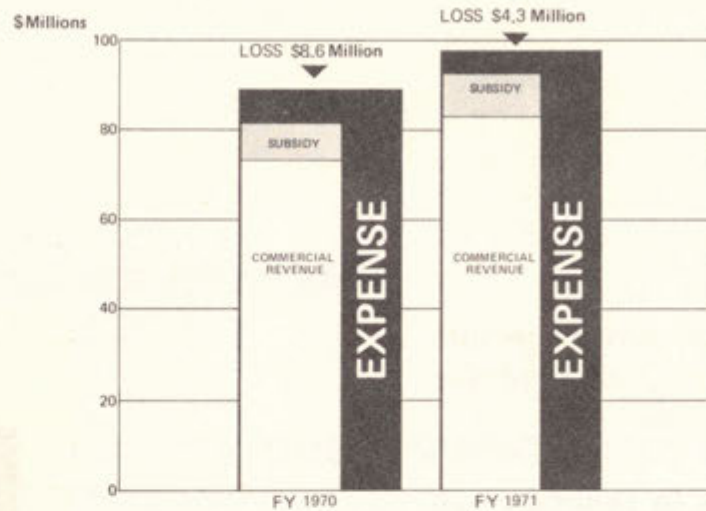
The reversal of that decrease in total subsidy dollars for Fiscal Year 1971 has helped.



Here's where we are now.

In Fiscal Year 1970 and 1971 commercial revenues, or income from operating our aircraft, have gone up.

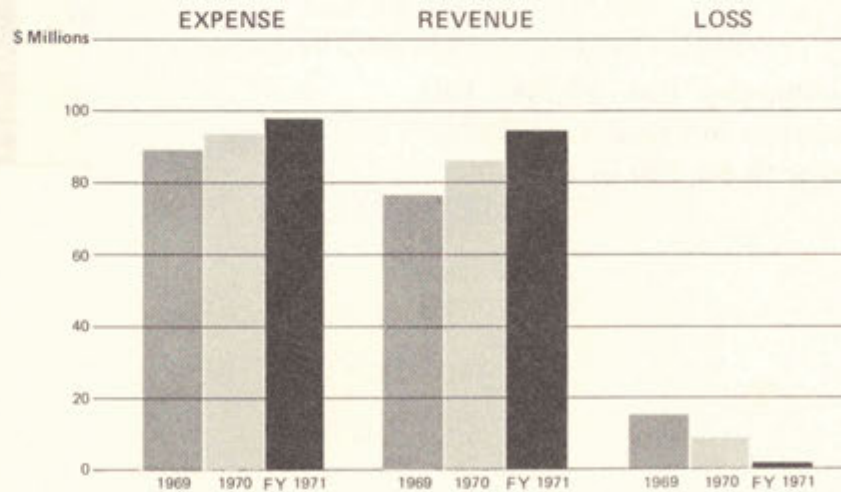
OPERATING REVENUE AND EXPENSE 1970-71



In Fiscal Year 1971 our expenses have gone up.

Our revenue has increased.

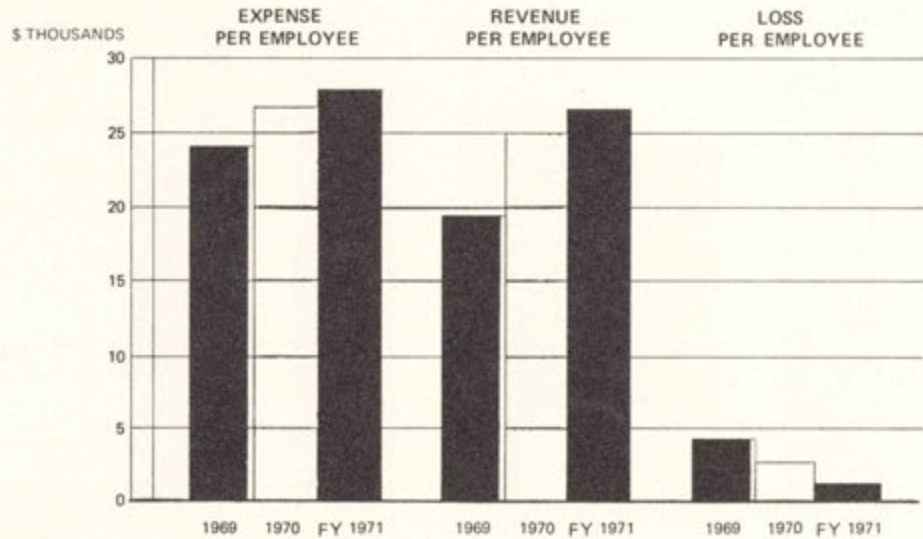
But our losses have decreased substantially. Our operating loss was cut in half, from \$8.6 million to \$4.3 million. (This is based on a Civil Aeronautics Board Fiscal Year which is June to June. Thus June 1969 to June 1970, and June 1970 to June 1971.)



The expense and revenue picture for each employee, or employee productivity, changed.

While expenses to maintain each employee went up, revenue to support that employee went up even more.

The company lost \$1,300 for each employee in Fiscal Year 1971, compared with \$6,700 in 1969.



MAJOR PROBLEMS

The remaining gap is going to be difficult to close.

There are five major reasons, as we see it, for the gap.

They are (1) uneconomic cities, (2) rising costs, (3) constraints on California operations, (4) what we call the aerospace recession and (5) route integration.

We'll explain these further.

UNECONOMIC CITIES

RISING COSTS

**CONSTRAINTS ON
CALIFORNIA OPERATIONS**

AEROSPACE RECESSION

ROUTE INTEGRATION

Uneconomic cities. . .

Other airlines are worrying about stops that do not enplane (board) 30 or even 20 passengers a day. Twenty-seven of our cities generate less than 30 passengers a day. Our problem is that we have too many points that do not even board 10 passengers a day.

We are still paying for crews, maintenance, and ground personnel for these low-productivity points.

Other regional carriers serve an average of eight cities that enplane less than 10 passengers a day.

Hughes Airwest serves 19 cities enplaning less than 10 passengers a day.

Up to 10, or maybe 12, of these 19 cities are within some 60 to 90 minutes driving time of another major airport.

It has been extremely difficult for us to find suitable, financially responsible third-level carriers (or carriers operating smaller airplanes) willing to serve these small cities.

AIR WEST LOW-TRAFFIC CITIES

1970 Enplanements Per Day	Number of Cities*
Less than 10	19
10-20	4
20-30	<u>4</u>
Total	27

*Total Air West System, Excluding Canada and Mexico.

**AIR WEST SERVES MORE THAN
TWICE AS MANY LOW TRAFFIC CITIES*
AS THE AVERAGE LOCAL SERVICE CARRIER**

Served by Local Service Carrier	83
Served by Air West	<u>19</u>
Served by Other Locals	64
Average Other Locals	8

*NO. OF CITIES
WHICH AVERAGE
LESS THAN 10
ENPLANEMENTS
DAILY

Our second economic problem is rising costs.

Our new wage contracts average more than 10 per cent in initial increases, with further raises to follow.

ALPA — Air Line Pilots Association

ALPA — Hostess division

ALEA — Air Line Employees Association

IAM — International Association of Mechanics

AMFA — Aircraft Mechanics Fraternal Association

ALDA — Air Line Dispatchers Association

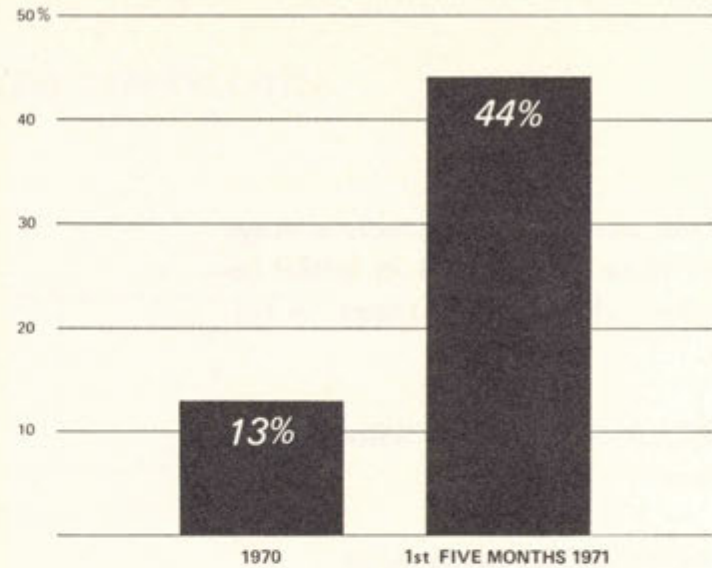
STATUS OF LABOR AGREEMENTS

	INITIAL INCREASE	STATUS JULY, 1971	EXPIRATION DATE
ALPA Pilots	10% %	✓	April 1972
ALPA Hostesses	11 %	✓	October 1972
ALEA Station, Clerical	11 %	✓	February 1973
IAM Storekeepers	12 %	✓	July 1973
AMFA Mechanics	—	In Negotiation	March 1971
ALDA Dispatchers	—	Negotiation Due	October 1971

Fixed costs are rising. One example is our landing fee picture.

Landing fees were up 13 per cent in 1970. In the first five months of 1971 landing fees are up 44 per cent and they will continue to rise.

Cost of Landing Fees
(% Increase over 1969)

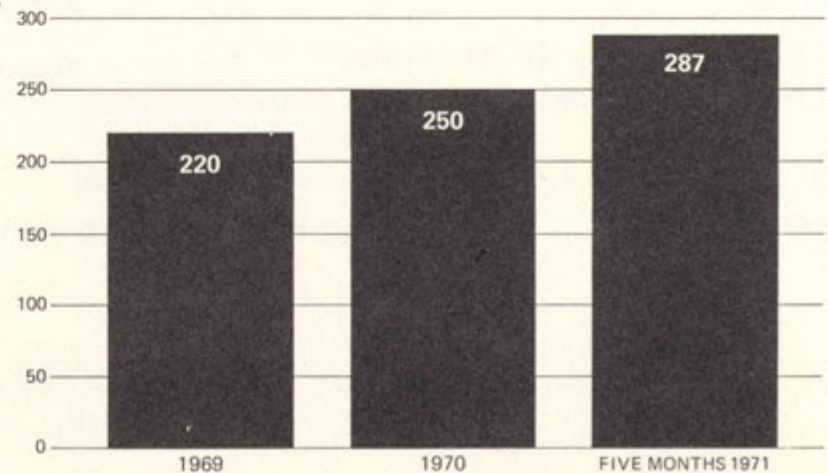


Wages and increased landing fees particularly hit our smaller aircraft, the F27s.

Their block hour costs, or cost per hour in the air, are escalating. In 1969 it cost \$220 per airborne hour to operate an F-27. It cost \$287 per block hour for the first five months of 1971.

F-27 OPERATING COSTS

Dollars per Block Hour



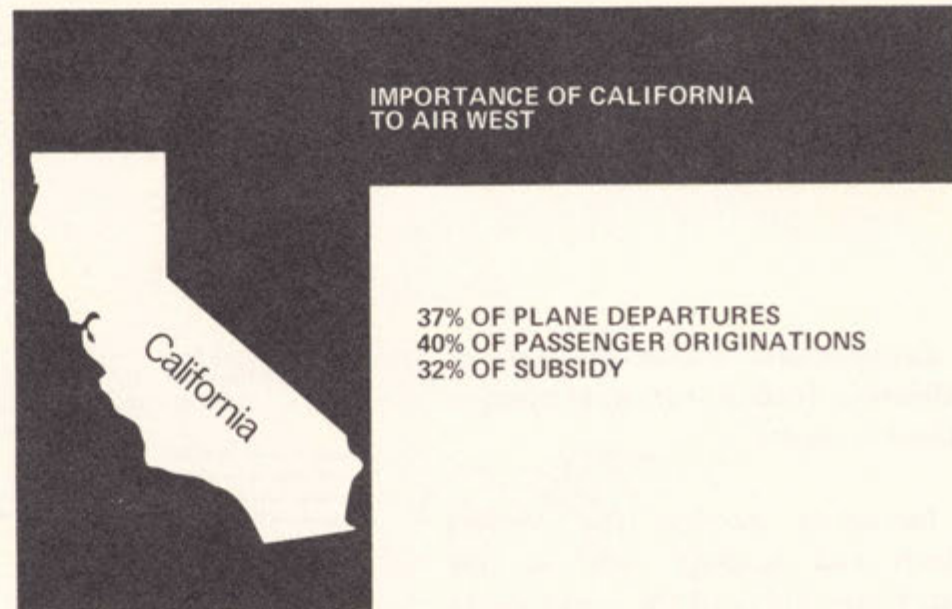
Constraints on California operations.

California is a very important part of our system, but the state presents some serious and unique problems.

First, California fares are lower than local service carrier fares in other states. There is always a time lag involved in getting California fare changes moved upward.

As a case in point, the fare increases approved by the Civil Aeronautics Board to become effective May 7, 1971, are not yet effective in California. This is because this fare increase has to be approved by the California Public Utilities Commission. (As of September 30, 1971, it was still pending before the PUC.)

As pointed out, California is important in our system and since the increased fare is not effective in California it costs Hughes Airwest \$1,700 a day in lost revenue.



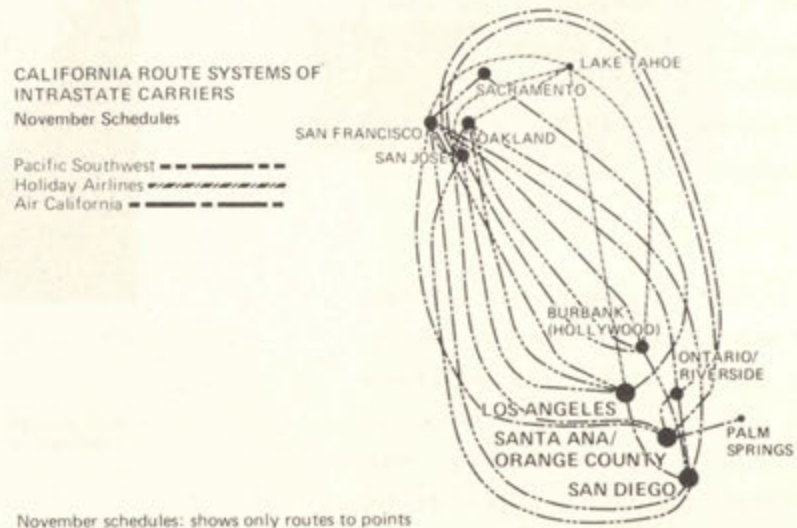
CALIFORNIA FARE LAG
("PHASE 7" FARES ONLY)

Revenue Loss Per Day	\$ 1,700
x Days Lag May 7—Oct. 1	<u>x146</u>
= Total Revenue Loss	\$248,200

Competition within the state of California (called intrastate competition) is severe.

Intrastate carriers (or carriers which can operate only in one state) have many of the same routes in California as Hughes Airwest.

This chart shows the duplication of routes by California intrastate carriers and Hughes Airwest.



This chart shows applications by intrastate carriers for new routes within the state of California.

The dotted lines indicate applications for routes over and above their present route structure.

For example, new applications to Fresno, Stockton and Eureka are duplications of Hughes Airwest's routes. We feel these routes being sought by intrastate carriers would divert some \$1.6 million annually from Hughes Airwest.

Since intrastate carriers need only apply to the California Public Utilities Commission (and not to the Civil Aeronautics Board) for new routes, Hughes Airwest has asked the Public Utilities Commission NOT to grant these routes to the intrastate carriers.

Our main reason for opposition is that it would not be profitable for two carriers to serve the same route.

ROUTE APPLICATIONS OF CALIFORNIA
INTRASTATE CARRIERS
(AS OF JANUARY, 1971)

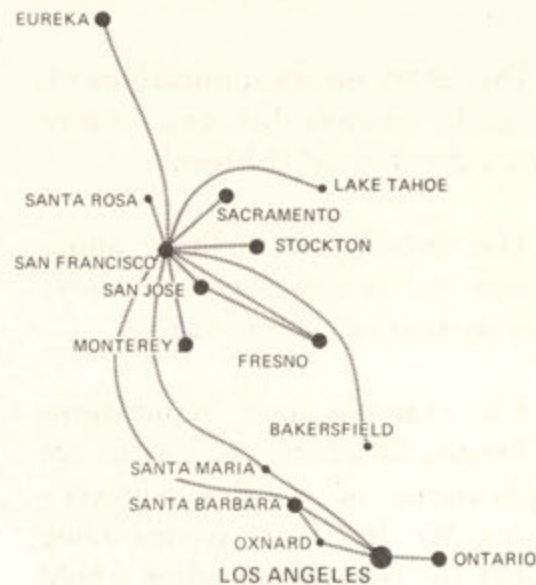
PACIFIC SOUTHWEST
AIR NEVADA
HOLIDAY AIRLINES - - - - -
AIR CALIFORNIA ······



Air taxis, or shorthaul carriers, are serious competition in many California markets. These "commuter carriers" carry more than 1.5 million passengers per year in California.

This chart shows California air taxi markets competing with Hughes Airwest.

CALIFORNIA AIR TAXI MARKETS*



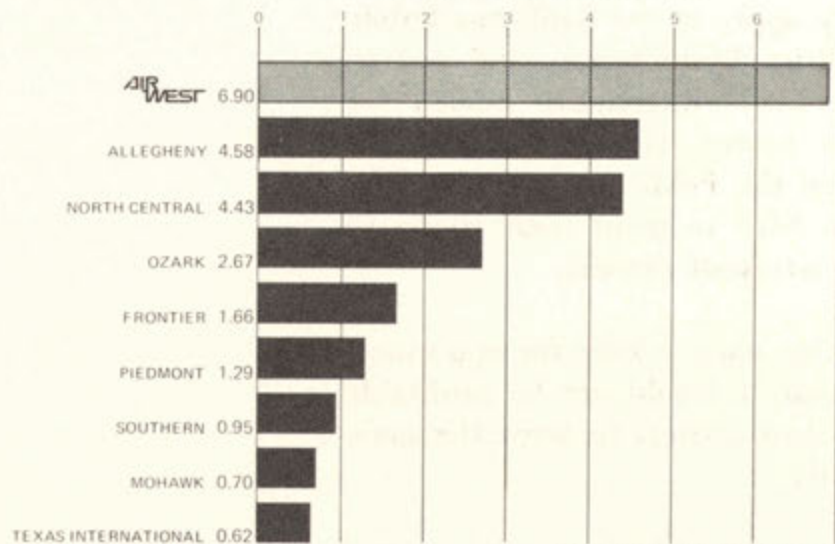
COMPETITIVE WITH AIR WEST

Hughes Airwest is more affected by air taxi competition on our routes than any other regional carrier.

This chart gives comparative figures for nine regional carriers, indicating the percentage of air taxi passengers in their markets.

AIR TAXI COMPETITION* 1969

COMMUTER PASSENGERS AS A PERCENT OF TOTAL LOCAL-SERVICE PASSENGERS



*Markets in which both carriers averaged a minimum of five passengers per day.

Aerospace recession. . .

We operate in four of the top 10 unemployment areas in the nation.

The statistics on the chart are for March, 1971. In July, 1971, Seattle's unemployment figures were in excess of 15 per cent.

This affects the travel business. People are uncertain and cautious. They are waiting. To point this out, personal savings in California have risen 38 per cent in the last year. People simply are not spending money.

Other leading Hughes Airwest markets also are hurting because of unemployment. Even our smaller cities, which have less than a half-million work force, are well above the national average for unemployment.

UNEMPLOYMENT
IN MAJOR MARKETS

Air West Cities Include Four
of the Top Ten Unemployment
Areas*

	CITY	% UNEMPLOYMENT
1	Seattle	13.2
2	Detroit	8.2
3	Anaheim	7.8
4	Los Angeles	7.7
5	Paterson (N.J.)	7.0
6	Buffalo	6.9
7	Newark	6.5
8	St. Louis	6.3
9	San Francisco—Oakland	6.2
10	Kansas City	6.1
	Ave. 26 Largest Labor Areas	5.7

*MARCH, 1971 - CITIES WITH OVER
500,000 IN LABOR FORCE

UNEMPLOYMENT—OTHER LEADING AIR WEST MARKETS

	%
Fresno	9.2
Sacramento	7.2
San Bernardino, Riverside, Ontario	7.3
San Diego	7.1
Spokane	9.4
Tacoma	11.0

MARCH, 1971

Route integration. . .

Route integration is one of our major problems. From a certificated route standpoint we are still three separate airlines.

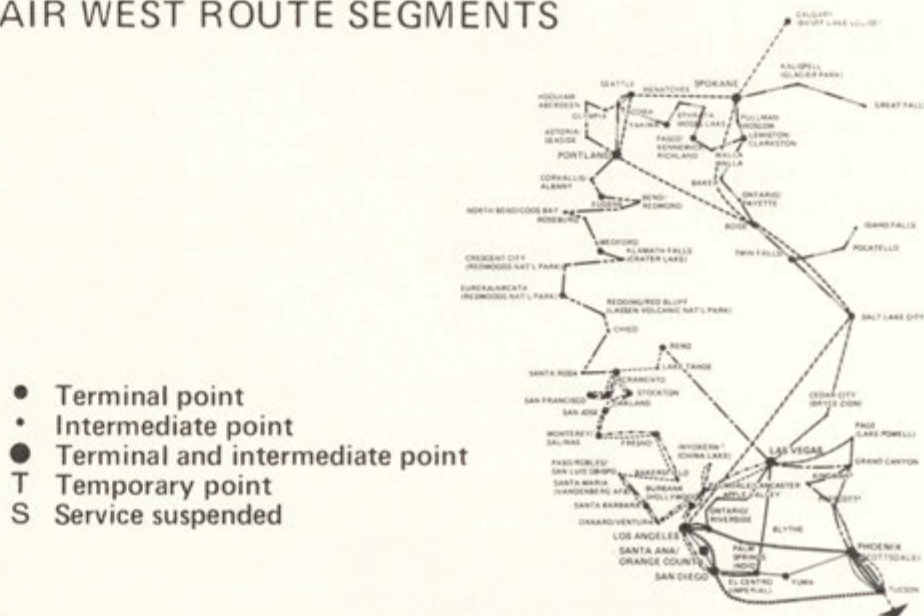
For example, when the three airlines merged in April, 1968, they brought with them three separate and different route systems that connected at different cities.

As a case in point, West Coast Airlines flew from Eugene to San Francisco. Pacific Airlines flew from Los Angeles to San Francisco.

Hughes Airwest still stops at San Francisco when flying from Los Angeles to Eugene. Legally eliminating this required stop at San Francisco would be called route integration.

Without route integration, we still have 15 separate segments (13 domestic and 2 trans-border) all of which require mandatory stops and some of which are unnecessary and costly.

AIR WEST ROUTE SEGMENTS



Every regional carrier has received a Subpart M Award.

Usually, when a carrier wishes to delete a stop or change a route it applies to the Civil Aeronautics Board which will consider the action in a hearing.

A subpart M, however, is an action to delete a stop awarded by the Civil Aeronautics Board without hearings.

Neither Hughes Airwest, nor its predecessor airlines have ever had a Subpart M before.

AIR WEST AND ITS PREDECESSOR COMPANIES HAVE NEVER RECEIVED A SUBPART M AWARD

CARRIER	NUMBER OF SUBPART M AWARDS
Mohawk	14
Allegheny	5
Frontier	5
Ozark	4
North Central	3
Texas Int'l	3
Piedmont	1
Southern	1
AIR WEST*	None

*And predecessors

SUBPART M BENEFITS
1. Reduced Operating Expenses
2. Increased Yields on Existing Traffic
3. End-to-End Traffic Stimulation
4. Beyond Flows

A Subpart M provides four benefits:

- 1) It reduces operating expenses (by deleting costly stops).
- 2) It decreases the per mile cost to the passenger and increases the average ticket value by generating more distance traffic and larger fares.
- 3) It provides end-to-end traffic stimulation (longer passenger trips).
- 4) It adds a considerable amount to beyond flows (traffic beyond the route in question).

Here is a hypothetical example of what a Subpart M would produce for us: a 28 per cent saving on our costs by changing a one-stop to a non-stop.

Hypothetically, we could then eliminate some 24 per cent of the miles flown.

Our departures would be cut in half.

Our flying time would go from one hour and forty-seven minutes to one hour and four minutes. This is a 41 per cent reduction in block hours.

By being able to operate at a 28 per cent cost reduction we would be able to give a lower fare to the passenger and increase our average ticket price at the same time.

HYPOTHETICAL SUBPART M AWARD -

	SHORTEST ONE STOP		NON-STOP		SAVINGS	
	Per Trip	Round Trips Per Yr.	Per Trip	Round Trips Per Yr.	Per Trip	Round Trips Per Yr.
Distance in Miles	600	438,000	458	334,000	142	24%
No. of Departures	2	1460	1	730	1	50%
Block Hours	1:47	1325	1:04	779	0:43	41%

It looks as if we will be unable to close the gap between expenses and revenues ourselves during the next 12 months.

If we allow for new wage contracts and the escalations built into the old contracts, we feel the operating expenses will be in the area of \$105.4 million in Fiscal Year 1972.

If the most recent 12 months' traffic is carried at current yields, if our cargo gains continue as strong as they have been for the last year, and if our Class Rate V subsidy remains where it is today, our annual revenues will be \$102 million.

In addition, there are \$2.4 million in non-operating expenses, making a net loss of \$5.8 million after subsidy.

REVENUES AND EXPENSES (\$000,000)

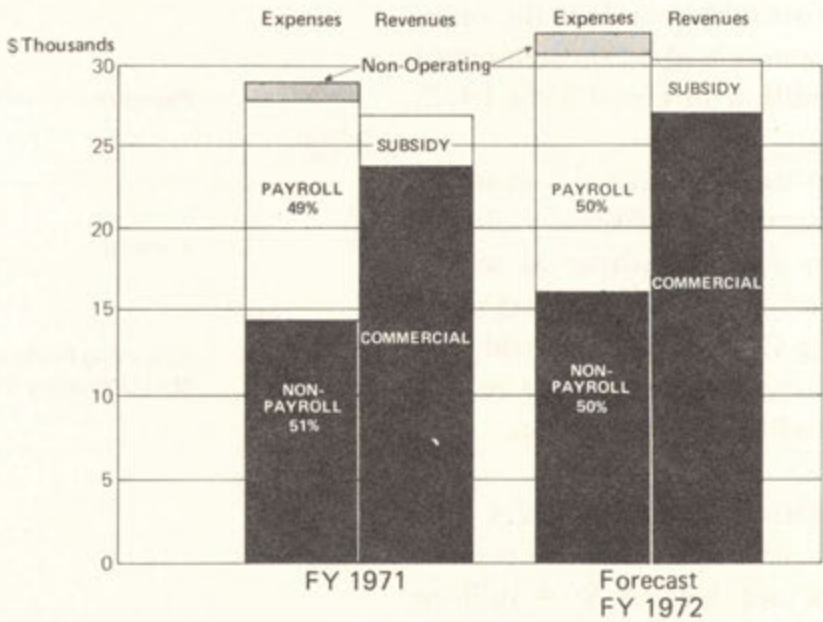
		FY 1971	Forecast FY 1972
Revenues	Commercial	82.8	91.3
	Subsidy	10.7	10.7
	TOTAL	<u>93.5</u>	<u>102.0</u>
Expenses	Payroll	47.0	53.0
	Non-Payroll	50.8	52.4
	TOTAL	<u>97.8</u>	<u>105.4</u>
Operating Profit (Loss)		<u>(4.3)</u>	<u>(3.4)</u>
Non-Operating Expenses		2.7	2.4
Net Profit (Loss)		<u>(7.0)</u>	<u>(5.8)</u>

We could keep these expenses from reaching \$105 million by:

- 1) Eliminating some of the points that do not board 10 passengers a day.
- 2) Realigning our route structure to eliminate non-productive departures.
- 3) Arranging route transfers and joint servicing (sharing facilities with other airlines).
- 4) Obtaining Subpart Ms to allow fewer mandatory stops.

Without such changes, we cannot catch up with the \$2,700 per employee increase in operating expense this coming year.

REVENUES AND EXPENSES PER EMPLOYEE



This presentation is based on hard economic factors traditionally used to determine the financial status of a company.

However, economic statistics do not reflect the human element, an *immeasurable* factor that determines the quality and depth of any company.

In this respect, Hughes Airwest has the people who already have demonstrated the skill, professionalism and pride needed to develop their airline as one of the best in the industry.

We must become profitable for several reasons. The first is that we cannot afford not to be. But more important, a profitable airline will provide us with opportunity, security and future of interest to every employee.

The years 1970 and 1971 were periods of stabilization and over-all product improvement. Now we must reach out to our customers and tell them about our product.

This is why 1972 will be the year to concentrate the whole company on marketing its products and services.

This important program will include:

A new image for Hughes Airwest, which will involve new hostess and agent uniforms, new corporate colors, a new insignia (or mark), and a new logo (or type style for the company name).

Under current development are new sales quotas, automatic ticketing at certain stations, new scheduling and an improved reservation system.

There are many more phases of the program – all directed at emphasizing the 1972 coordinated marketing effort.

Even though economic conditions in the Western region are at a low point, we expect an upswing in 1972 within the territory we serve.

That, coupled with our new marketing program and our desire to implement our goals, can assure success – not only for Hughes Airwest and its employees but also for the many communities it serves.

Prepared by:
Hughes Airwest
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