

PROSPECTS FOR U.S. MAJOR AIRLINES — 1995 THROUGH 1999

*Edmund S. Greenslet
ESG Aviation Services*

I was reminded recently of a story that Robert Benchley told on himself. He was a drama critic in the 1920s; and when he reviewed Abie's Irish Rose, he said it was a flop and would close in weeks. Years later, after setting Broadway records for longevity, it finally did end its run. At that Time Benchley wrote another column saying: "See, I told you it would close!" See, I told you the airlines would make money! The only problem is that I said this three years ago. However, in this forecasting business it is better to be early than late, and most of the reasons cited then are the forces driving the earnings recovery now. The job today is to consider how durable this recovery is likely to be and what is the most probable outlook for the U.S. airline industry over the rest of the decade.

In the 1992 case for an extended period of positive earnings, I pointed out that the most critical relationship characterizing rising or falling operating earnings was the relative percentage change in yield and unit costs. History tells us it is not the size of the change in these two factors that is important; it is just the relationship between them that counts. In quarters when the yield rises more (or falls less) than unit costs, operating earnings increase; and vice versa. The direction of the change in earnings does not correlate well with rising or falling load factors or with the rate of traffic growth. Only the yield/unit cost relationship seems to count.

Since 1979 there have been 66 quarters of operating results. In 35 of them earnings were up, and in 31 they declined. (Table 1) If that surprises you, given all the

TABLE 1 HISTORY OF OPERATING INCOME AND CHANGE IN KEY VARIABLES

Year	Quarter	Operating Income (000)		Quarterly RPM % change	ASM % change	Spread I: RPM % - ASM %	Quarterly		Spread II: Yield % - Cost %	Total Spread (I plus II)
		Quarter	Trailing 12 Quarter				Yield % change	ASM cost % change		
1978	Fourth	72,055	1,160,054	16.2	11.2	5.0	(3.1)	1.2	(4.3)	0.7
1979	First	(18,250)	1,048,676	18.0	13.1	4.9	(0.4)	2.1	(2.5)	2.4
	Second	184,266	855,525	11.9	2.7	9.2	0.5	12.9	(12.4)	(3.2)
	Third	86,554	324,625	12.3	13.9	(1.6)	5.6	15.2	(9.6)	(11.2)
1980	Fourth	(231,325)	21,245	7.2	7.6	(0.4)	15.9	20.3	(4.4)	(4.8)
	First	(324,852)	(285,357)	0.0	5.4	(5.4)	27.6	25.0	2.6	(2.8)
	Second	(167,989)	(637,612)	(1.5)	13.2	(14.7)	26.5	16.9	9.6	(5.1)
	Third	180,464	(343,702)	(8.3)	(2.5)	(5.8)	27.6	18.7	8.9	3.1
1981	Fourth	(21,223)	(333,600)	(7.7)	(6.7)	(1.0)	23.7	18.0	5.7	4.7
	First	(156,632)	(165,380)	(10.0)	(6.8)	(3.2)	22.2	14.1	8.1	4.9
	Second	116,696	119,303	(2.8)	(2.6)	(0.2)	16.5	11.6	4.9	4.7
	Third	92,480	31,321	(5.2)	(5.1)	(0.1)	10.4	11.6	(1.2)	(1.3)
1982	Fourth	(480,992)	(428,448)	(1.3)	(0.2)	(1.1)	2.4	7.6	(5.2)	(6.3)
	First	(563,977)	(835,793)	4.5	0.2	4.3	(7.0)	3.1	(10.1)	(5.8)
	Second	126,146	(826,343)	1.7	(0.7)	2.4	(4.4)	(2.0)	(2.4)	0.0
	Third	290,880	(627,943)	2.1	4.3	(2.2)	(1.2)	(5.4)	4.2	2.0
1983	Fourth	(504,467)	(651,418)	4.1	3.7	0.4	(4.5)	(4.2)	(0.3)	0.1
	First	(621,298)	(708,739)	10.4	2.8	7.6	(8.6)	(2.0)	(6.6)	1.0
	Second	76,318	(758,567)	6.4	5.7	0.7	(2.1)	(1.4)	(0.7)	0.0
	Third	528,380	(521,067)	6.9	5.3	1.6	1.4	(0.1)	1.5	3.1
1984	Fourth	247,793	231,193	6.7	5.3	1.4	6.1	(2.9)	9.0	10.4
	First	127,586	980,077	(0.3)	9.8	(10.1)	17.3	(3.0)	20.3	10.2
	Second	758,663	1,662,422	7.2	7.0	0.2	7.1	0.0	7.1	7.3
	Third	846,586	1,980,628	8.7	7.7	1.0	(0.8)	(2.5)	1.7	2.7
	Fourth	335,487	2,068,322	10.2	9.9	0.3	(2.8)	(3.4)	0.6	0.9

TABLE 1 HISTORY OF OPERATING INCOME AND CHANGE IN KEY VARIABLES (continued)

		Shaded Periods = Improving Earnings			Outlined Periods = Declining Earnings					
Year	Quarter	Operating Income (000)		Quarterly		RPM % Less ASM %	Spread I:		Spread II:	
		Quarter	Trailing 12 Months	RPM % change	ASM % change		Yield % change	ASM cost % change	Yield % Less Cost %	
1985	First	93,192	2,033,928	13.2	5.7	7.5	(6.2)	0.6	(6.8)	0.7
	Second	710,286	1,985,551	13.7	5.5	8.2	(6.5)	1.6	(8.1)	0.1
	Third	640,872	1,779,837	11.4	9.9	1.5	(5.1)	(1.3)	(3.8)	(2.3)
	Fourth	(229,796)	1,214,554	7.2	9.5	(2.3)	(3.8)	0.8	(4.6)	(6.9)
1986	First	(621,060)	500,302	8.8	10.1	(1.3)	(7.7)	(1.0)	(6.7)	(8.0)
	Second	193,353	(16,631)	4.0	14.4	(10.4)	(7.4)	(10.7)	3.3	(7.1)
	Third	972,293	314,790	10.4	8.5	1.9	(7.5)	(8.7)	1.2	3.1
	Fourth	373,993	918,579	10.5	7.6	2.9	(7.1)	(10.4)	3.3	6.2
1987	First	30,013	1,569,652	11.0	9.1	1.9	(1.8)	(6.8)	5.0	6.9
	Second	872,214	2,248,513	14.5	6.6	7.9	0.8	1.4	(0.6)	7.4
	Third	961,595	2,237,815	9.4	5.3	4.1	4.4	8.5	(4.1)	0.0
	Fourth	(28,379)	1,835,443	6.7	5.3	1.4	7.3	11.0	(3.7)	(2.3)
1988	First	99,473	1,904,903	5.0	5.9	(0.9)	9.1	6.0	3.1	2.2
	Second	964,244	1,996,933	2.1	3.3	(1.2)	10.3	8.0	2.3	1.1
	Third	1,201,156	2,236,494	4.4	3.5	0.9	4.9	4.3	0.6	1.5
	Fourth	350,653	2,615,526	6.9	4.3	2.6	2.7	1.6	1.1	3.7
1989	First	173,171	2,689,224	0.7	0.8	(0.1)	10.6	9.5	1.1	1.0
	Second	953,780	2,678,760	1.0	(0.7)	1.7	6.0	8.7	(2.7)	(1.0)
	Third	666,593	2,144,197	2.6	0.9	1.7	1.5	8.2	(6.7)	(5.0)
	Fourth	(489,131)	1,304,413	4.3	2.9	1.4	0.3	8.9	(8.6)	(7.2)
1990	First	(642,867)	488,375	8.2	6.8	1.4	(1.7)	5.4	(7.1)	(5.7)
	Second	649,837	184,432	7.7	10.1	(2.4)	1.2	1.4	(0.2)	(2.6)
	Third	98,248	(383,913)	7.1	8.8	(1.7)	3.5	6.0	(2.5)	(4.2)
	Fourth	(2,389,374)	(2,284,156)	3.6	5.7	(2.1)	5.8	16.2	(10.4)	(12.5)
1991	First	(1,509,345)	(3,150,634)	(7.9)	(4.1)	(3.8)	3.7	7.8	(4.1)	(7.9)
	Second	(35,224)	(3,835,695)	(2.1)	(3.7)	1.6	(1.6)	6.2	(7.8)	(6.2)
	Third	205,363	(3,728,580)	(0.4)	(1.1)	0.7	0.8	0.5	0.3	1.0
	Fourth	(1,045,906)	(2,385,112)	0.9	(1.4)	2.3	(0.1)	(6.4)	6.3	8.6
1992	First	(453,250)	(1,329,017)	9.1	6.9	2.2	3.6	(4.2)	7.8	10.0
	Second	(615,104)	(1,908,897)	4.7	6.0	(1.3)	(2.1)	(0.2)	(1.9)	(3.2)
	Third	(158,369)	(2,272,629)	10.4	4.3	6.1	(7.6)	1.0	(8.6)	(2.5)
	Fourth	(1,257,562)	(2,484,285)	3.1	4.2	(1.1)	(2.0)	(1.2)	(0.8)	(1.9)
1993	First	(377,583)	(2,408,618)	4.5	2.8	1.7	(1.2)	0.9	(2.1)	(0.4)
	Second	488,554	(1,304,960)	3.0	2.2	0.8	6.5	0.1	6.4	7.2
	Third	1,089,784	(36,807)	(5.5)	0.3	(5.8)	12.7	(1.2)	13.9	8.1
	Fourth	(269,568)	931,187	2.9	(0.6)	3.5	2.6	0.4	2.2	5.7
1994	First	(49,147)	1,259,623	1.8	(2.6)	4.4	(3.1)	0.6	(3.7)	0.7
	Second	624,018	1,395,087	3.1	(1.4)	4.5	(2.8)	1.9	(4.7)	(0.2)
	Third	1,367,979	1,673,282	4.5	(0.6)	5.1	(4.3)	(1.1)	(3.2)	1.9
	Fourth	(229,406)	1,713,444	6.4	2.4	4.0	(5.3)	(1.9)	(3.4)	0.6
1995	First	336,109	2,098,700	5.6	3.7	1.9	(3.6)	(4.6)	1.0	2.9
	Second	1,865,877	3,340,559	4.0	1.7	2.3	1.7	(3.9)	5.6	7.9
	Third									
	Fourth									

negative words about airline profitability in recent years, it may also come as a surprise to know that 40 of those 66 quarters were profitable, while 26 had an operating

loss. Of course, nine of those loss quarters came between the fourth quarter of 1990 and the first quarter of 1993, and several of them were by far the worst the

industry has ever had. Recent events always tend to stand out in our minds more than distant ones, particularly when those events were as traumatic as the early 1990s were for the airlines. This fact is part of the cure, as the industry is unlikely to soon forget this time of troubles. After all, it took 20 years and a world war for the depression generation to get over the 1930s.

Returning to the key relationship between yield and unit costs, in only four of those 31 quarters when earnings fell did the yield improve relative to unit costs; and three of them were in the quarter immediately preceding an earnings upturn. On the other side, prior to 1994, the change in yield was worse than the change in unit costs in five of the 35 periods when earnings increased. Four of these events came in the quarter immediately preceding an earnings decline. This is the record that drives the conclusion that this relationship is the most significant indicator of airline earnings. Then came 1994. In all four quarters of last year the yield to unit cost relationship was negative yet operating earnings increased in all of them.

What happened? I suggest last year was a unique exception to the established pattern that was caused by an unprecedented decline in capacity at a time when traffic was rising. Never before has this happened, and never before has the positive gap between the percentage change in traffic and that of capacity been so large for so long. This overcame the unfavorable yield/unit cost relationship, allowing earnings to rise. It was unlikely that the traffic/capacity condition could continue at this pace, as the load factor increased three points in 1994 to 66.5 percent, and it has not. In the first half of 1995 the traffic/capacity gap was half that of 1994, and in July it disappeared entirely. However, the yield to unit cost relationship again became positive, and in the second quarter this was the main energy source for the reported 60-percent rise in trailing twelve month earnings. I submit that from here on this will again be the key determinant of earnings.

What is the five-year outlook? Table 2 is a projection of airline economic factors through 1999. The yield to unit cost relationship is judged likely to remain favorable through 1996. 1997 will be the cusp year when the balance turns negative; but, as usual in past cycles, the margin is so small that the earnings momentum will remain positive. 1998 and 1999 will be negative, with earnings falling. This decline is projected to continue, perhaps leading to a loss in 2000.

A number of things were considered in reaching these conclusion, but none were more important than the obvious change in management philosophy toward the business. This can be summed up by noting that cost reduction, not market share, is now the dominant

objective of most airline managements. It may be impossible to overstate the significance of this shift in thinking, which is a direct product of the financial black hole that most companies have been drawn into. Airlines have always paid lip service to cost control, but those who follow the industry have always known that the airlines did not have their hearts in it. The eyes of airline managers began to sparkle only when they talked about fleet plans, the new markets they planned to enter, and the new hubs they were establishing.

Throughout the 1980s the defense of the established carriers against low-fare startups such as People Express was built around growth and a pricing strategy based on an unwillingness to surrender market share at any service point. The only effective cost reduction effort in those years came through the "B-scale" wage plan that depended on rapid growth to work. Today all this has changed. Another wave of startups fills the landscape, but the establishment is more inclined to ignore than confront them. It remains to be seen whether this strategy will work in the long run, but the near-term effect should be positive.

The strategy of the 1990s is to concentrate on marketing strengths, which for most airlines is moving large numbers of passengers with complex itineraries through megahubs, and for the first time truly working hard to reduce the cost of doing this. The final plank in this platform is a pricing strategy based less on what fare the latest startup offers than on the value of the service provided. The key to this change is management emphasis on unit revenue, usually expressed as revenue per available seat mile, or RASM. This focus on unit revenue tends to lead to more optimum fleet utilization, which means fewer airplanes, higher load factors, and a serious effort to reduce costs.

Sayings these things does not imply a belief that the basic economics of the airline business have changed. Air transportation is still very like a commodity service that is an intermediate rather than an end product in the eyes of the consumer. Within the limitations implied by this, however, the industry is exploring the narrow window that exists due to the fact that air transport is not a pure commodity. There is some room to differentiate prices (or as some put it, to achieve a revenue premium), and airline managers seem determined to find out just how wide that window might be. Certainly it has its limits, but until now there has been no true will among airline managers to probe the outer limit of the envelope.

Such a will is crucial to a sustained profit recovery. Clearly it will take the trauma of the 1990-1992 depression and its lingering aftereffects, which added two more years of losses and will keep the balance

TABLE 2 MAJOR AIRLINES — FIVE-YEAR EARNINGS MODEL

Airlin	1989	1990	1991	1992	1993	1994	1995E	1996E	1997E	1998E	1999E
Revenue											
Passenger	\$50,979.6	\$55,557.7	\$54,554.3	\$56,928.4	\$60,499.4	\$60,473.2	\$63,533.9	\$67,779.3	\$72,357.2	\$76,682.9	\$80,787.0
Other	5,108.4	5,565.9	5,793.6	5,914.4	6,517.0	6,888.3	6,864.6	7,330.0	7,830.0	8,280.0	8,730.0
Total	56,088.0	61,123.6	60,347.9	62,842.8	67,016.4	67,361.5	70,398.5	75,109.3	80,187.2	84,962.9	89,517.0
Pct. Change	6.7	9.0	(1.3)	4.1	6.6	0.5	4.5	6.7	6.8	6.0	5.4
Expenses (\$ mil.)	54,783.5	63,407.8	62,733.1	65,327.1	66,122.9	65,647.8	65,340.1	68,234.2	72,612.6	78,232.8	84,435.9
Pct. Change	9.9	15.7	(1.1)	4.1	1.2	(0.7)	(0.5)	4.4	6.4	7.7	7.9
Operating Income (000)	1,304,413	(2,284,156)	(2,385,139)	(2,484,285)	893,578	1,713,484	5,058,336	6,875,046	7,574,645	6,730,057	5,081,082
Operating Ratio %	97.7	103.7	104.0	104.0	98.7	97.5	92.8	90.8	90.6	92.1	94.3
Oper. Inc.-Total (000)	1,417,524	(2,231,357)	(2,404,109)	(2,566,065)	1,051,854	1,850,518	5,353,335	7,075,046	7,774,645	6,930,057	5,281,082
Non-Oper. Inc.& (Exp.)	(472,237)	(2,768,903)	(416,706)	(2,219,202)	(2,448,595)	(2,626,359)	(1,994,558)	(2,070,000)	(2,035,000)	(1,963,000)	(1,857,000)
Pretax Income	945,287	(5,000,260)	(2,820,815)	(4,785,267)	(1,396,741)	(775,841)	3,358,777	5,005,046	5,739,645	4,967,057	3,424,082
Tax Rate %	95.7	3.5	16.9	26.1	6.7	(50.4)	43.1	38.7	37.5	37.9	39.4
Taxes	904,258	(174,829)	(477,730)	(1,249,352)	(94,024)	391,059	1,447,432	1,938,974	2,153,985	1,883,905	1,349,969
Net Income (000)	41,029	(4,825,431)	(2,343,085)	(3,535,915)	(1,302,717)	(1,166,900)	1,911,345	3,066,072	3,585,659	3,083,152	2,074,114
Net Profit Margin	0.07%	(7.89%)	(3.88%)	(5.63%)	(1.94%)	(1.73%)	2.72%	4.08%	4.47%	3.63%	2.32%
Traffic: RPMs (mil.)	413,631.2	441,000.7	431,127.7	460,813.8	464,595.3	483,240.6	496,934.9	520,898.7	547,474.6	569,300.2	588,078.6
Pct. Change	2.2	6.6	(2.2)	6.9	0.8	4.0	2.8	4.8	5.1	4.0	3.3
Capacity: ASMs (mil.)	652,774.0	704,126.6	686,243.4	722,838.7	731,126.0	727,098.1	739,267.3	764,862.5	800,039.2	840,933.3	882,096.7
Pct. Change	1.0	7.9	(2.5)	5.3	1.1	(0.6)	1.7	3.5	4.6	5.1	4.9
Load Factor %	63.4	62.6	62.8	63.8	63.5	66.5	67.2	68.1	68.4	67.7	66.7
Yield per RPM - (%)	12.32	12.60	12.65	12.55	13.02	12.51	12.79	13.01	13.22	13.47	13.74
Pct. Change	4.4	2.3	0.4	(2.3)	5.4	(3.9)	2.2	1.8	1.6	1.9	2.0
Cost per ASM - (%)	8.39	9.01	9.14	9.04	9.04	9.03	8.84	8.92	9.08	9.30	9.57
Pct. Change	8.8	7.4	1.4	(1.1)	0.1	(0.2)	(2.1)	0.9	1.7	2.5	2.9
Profit Equation - Percent Change in:											
Yield	4.4	2.3	0.4	(2.3)	5.4	(3.9)	2.2	1.8	1.6	1.9	2.0
RPMs	2.2	6.6	(2.2)	6.9	0.8	4.0	2.8	4.8	5.1	4.0	3.3
Revenue	6.6	8.9	(1.8)	4.5	6.2	0.1	5.0	6.6	6.7	5.9	5.3
Cost / ASM	8.8	7.4	1.4	(1.1)	0.1	(0.2)	(2.1)	0.9	1.7	2.5	2.9
ASMs	1.0	7.9	(2.5)	5.3	1.1	(0.6)	1.7	3.5	4.6	5.1	4.9
Expenses	9.8	15.3	(1.1)	4.2	1.2	(0.7)	(0.4)	4.4	6.3	7.6	7.8
Spread	(3.2)	(6.4)	(0.7)	0.3	5.0	0.8	5.4	2.2	0.3	(1.7)	(2.5)

Company Results & Forecast - Airline Operating Income (millions)

American	\$730.8	\$68.0	\$17.5	(\$77.2)	\$563.5	\$911.6	\$1,368.3	\$1,646.8	\$1,755.3	\$1,546.2	\$1,132.9
Amer. West	48.1	(31.6)	(104.7)	(74.8)	121.1	146.4	161.0	182.4	197.9	171.8	120.8
Continental	161.0	(241.8)	(269.1)	(194.5)	(46.2)	(86.3)	212.0	329.2	394.7	365.7	276.8
Delta	676.6	(235.1)	(266.4)	(825.5)	(274.9)	(215.1)	1,005.4	1,437.5	1,563.6	1,387.3	1,044.2
Northwest	290.1	(141.7)	(60.1)	(308.8)	330.8	876.5	927.4	1,002.8	993.6	885.6	755.7
Southwest	97.6	81.6	62.0	181.8	281.2	289.9	291.2	389.9	484.2	502.7	443.2
Trans World	24.3	(162.2)	(348.4)	(369.5)	(248.3)	(217.4)	56.3	210.2	262.1	251.4	202.7
United	456.9	(54.3)	(490.6)	(440.2)	295.2	513.0	948.0	1,379.4	1,477.9	1,260.8	918.9
USAir	2.7	(543.2)	(202.1)	(375.5)	(128.7)	(505.1)	88.5	296.9	445.3	358.5	185.9

sheets weak for several years to come, to achieve this fundamental change in management objectives. But that is history. The real question is how long will these objectives dominate policy. No one can know, but it will probably be several years. I remain skeptical enough to believe that, in time, the siren of expansion and market share may become too attractive to resist. In the meantime, should the airlines' resolve weaken too soon, they need only look at their balance sheets to gain renewed courage.

The best will in the world cannot prevent problems from interrupting a positive earnings trend. Many problems may arise in the next several years.

RECESSION

Rarely are we so close to the last one that we do not worry about the next, and so it is today. My response to the question of when is to say that, if a recession occurs in 1996 or 1997, it would probably cause only a modest dip in earnings but no return to the condition of 1990. Why? Because the industry is already being managed in a recession mode. Recessions reduce traffic; and it is almost certain that, in its present state, the industry would quickly cut capacity and lay employees off at the early signs of softness in the market.

Do not forget that it was not the recession of 1990 that caused the industry's massive financial problems. They were more a product of the unbridled expansion going on at that time, together with the disaster of the Gulf War in terms of both increased fuel prices and traffic losses. Actually, an early recession might be welcome. It would cause little real pain and clear the way for a more extended string of good earning years that could stretch into the beginning of the next century. The model I use indicates a recession in 2000, by which time the damage it could do might be much greater.

FUEL PRICES

This is more a political than an economic factor. All we know is that fuel prices have doubled three times in the last 20 years, and it would be foolish to think it cannot happen again. No such increase is in the model I use; but, if it occurred, the greatest damage would be to those airlines with the oldest fleets.

Related to this is the 4.3 cents per gallon tax scheduled to become effective on October 1, 1995. My assumption is that it will be put in place, although strong efforts are being made to postpone it for another three years (This tax increase did go into effect on October 1,

1995 ed.). I also believe it will be largely passed through to the consumer and that its negative effect on costs and earnings will be hard to detect after the fact. The tax represents about a 7-percent increase in fuel price. Since fuel is presently about 11 percent of total operating cost, the result is expected to be a 0.8-percent rise in total expenses. Most analysts agree that a yield increase of this amount will have no negative elastic effect on traffic. It is unlikely that the point can be tested because yields are expected to be up as much more than 1 percent for the rest of 1995 and into early 1996, and these large yield gains will slow traffic growth. Indeed, they already have.

LABOR

Barring a recession, it seems almost certain that 1996 and 1997 will be difficult years in labor negotiations. The airlines will be profitable, but airline management will still be in a stringent cost-control mode. On the other hand, counting the three major employee groups (pilots, flight attendants, and mechanics) at the 10 largest carriers, there are 30 possible labor contracts, 19 of which have expired or will expire between now and 1997. (Some of the other 11 are not unionized groups.) This has all the characteristics of a classic case of employees saying they have suffered enough and it is time to share the fruits of prosperity. Employee groups are likely to be more successful than management would like; and the resulting rise in costs is one reason for projecting that earnings will decline from 1998 on.

NEW LOW-FARE AIRLINES

We are seeing a new wave of startup carriers; but if "startup" is interpreted in its broadest possible sense, startups are less of a factor now than seemed likely just a year ago. Continental Lite was essentially a startup, as was United Express. When those two began operation, it looked as if low-fare domestic service could very soon capture more than a third of the market. If others were driven to copy the formula, it was thought that low-fare carriers might reach a 50-percent market share. This did not happen. Continental Lite folded, and of the truly new carriers only Valujet so far appears to be a real success. Most of the other startups occupy very small niches, and for many their long-term prospects may ultimately depend on linking up with a large airline, as Reno has done with American.

If these airlines do not make a real impact on the business in the next two years, it is unlikely they will do

so at all. Making an impact means causing the large airlines to alter their pricing strategy which, as observed earlier, is largely to ignore rather than match startups' fares. The reason for the two-year window is that by 1997 or 1998 the supply of available aircraft of any type will be sharply reduced and the tightening of noise rules will significantly increase the capital cost of any old airplanes that might be available.

Although Southwest Airlines is obviously not a startup, some mention must be made of the effect that it may have on the air travel market. Southwest's traffic is expected to grow at about four times the industry rate and in the process move from about 6 percent of the domestic market last year to about 10 percent in 1999. There are two things to remember about Southwest, however. One, Southwest will grow, but never at a rate faster than it feels it can comfortably manage. Two, the airline likes to be very profitable. Do not look for Southwest to grow 50 percent in one year, and do not expect them to eat industrywide cost increases such as the proposed fuel tax. In other words, Southwest is prudently managed and not inclined to do dumb things. Its strategy may be different, and the execution usually better, but its objectives are really no different from those of the major carriers. This is why, at least over the five-year period projected here, a wary coexistence is possible between Southwest and the large carriers, with each following the strategy deemed best for itself.

replay of the Luddite complaint that new technology will destroy our jobs and businesses. The fact that it has never worked out this way does not matter. The same fears arise with each technological innovation. The question is not relevant to the five-year forecast presented here. However, it should be pointed out that much of the same kind of new technology will be used by the airlines to reduce distribution costs, and this *could* have an impact on the near-term prospects. The reduction in travel-agent commissions will be noticeable this year; and the next step must be to simplify, if not eliminate, the ticketing process to reduce costs for both airlines and travel agents.

Others can certainly come up with additional difficulties the airlines might face in the next few years, but in the end it is not the problems that matter, but how industry management responds to them. More often than not the largest problem for major carriers has been themselves. Thus, we end where we began. The key to success is keeping a favorable relationship between the change in yield and the change in unit cost. The key to sustaining that relationship through 1996 (if not 1997) is the will of management in the several airlines to do what is necessary to achieve it. The trial by fire over the past five years has transformed management policies in a way that sets the stage for some very positive earning years. The only real issue is whether early success will erode the will of managers to hold the course they have established.

TELECONFERENCING

In recent years few subjects have received more illumination, with less light, than this one. It is really a