

## **Operator**

Good morning and welcome to the American Airlines Group third quarter 2017 earnings call. Today's conference call is being recorded. At this time, all lines are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session.

And now, I would like to turn the conference over to your moderator, Managing Director of Investor Relations, Mr. Dan Cravens. Please go ahead.

## **Daniel E. Cravens - American Airlines Group, Inc.**

Good morning, everyone, and welcome to the American Airlines Group third quarter 2017 earnings conference call. Joining us in the room today is Doug Parker, our Chairman and CEO; Robert Isom, the President; and Derek Kerr, our Chief Financial Officer. Also in the room for our Q&A session is Elise Eberwein, our EVP of People and Communications; Maya Leibman, Chief Information Officer; Steve Johnson, our EVP of Corporate Affairs; and Don Casey, our Senior Vice President of Revenue Management.

We're going to start the call today with Doug, and he will provide an overview of our third quarter financial results. Derek will then walk us through the details on the quarter and provide some additional information on our guidance for the remainder of the year. Robert will then follow with commentary on the operational performance and revenue environment. And then after we hear from those comments, we will open the call for analyst questions and lastly questions from the media.

Before we begin, we must state that today's call does contain forward-looking statements, including statements concerning future revenues and costs, forecasts of capacity, traffic, load factor, fleet plans and fuel prices. These statements represent our predictions and expectations as to future events, but numerous risks and uncertainties could cause actual results to differ from those projected. Information about some of these risk and uncertainties can be found in our earnings press release issued this morning, and as well as our Form 10-Q for the quarter ended September 30, 2017.

In addition, we will be discussing certain non-GAAP financial measures this morning such as pre-tax profit and CASM, excluding unusual items. A reconciliation to those numbers to the GAAP financial measures is included in the earnings release and that can be found on our website at [aa.com](http://aa.com).

A webcast of this will also be archived on the website. The information that we're giving you on the call is as of today's date and we undertake no obligation to update the information subsequently. So thanks again for joining us this morning.

At this point, I'll turn the call over to our Chairman and CEO, Doug Parker.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Dan. Thanks, everybody, for being on. It's not possible to talk about the third quarter without beginning with the hurricanes and what our team did in regard to those events. We're always proud of our team, but particularly so this quarter. They rallied around each other, they rallied around our customers, just showed incredible care and concern and made a huge difference and it's times like this that the people of American shine and they certainly did in the third quarter and we're so proud of them and appreciative and I should also note, as proud as we are as the people of American, this is not a time for all of our competitive juices to get too strong.

Our industry did a great job in this regard and we're proud of everyone in the industry for what they all did including our competitors. We made a big difference, we continue to make a big difference and we're proud of that and extremely thankful and appreciative of our team.

We had an investor day not too long ago, just last month, Investor and Media Day. It was very productive and helpful. Thank you for all – thanks to all of you who attended. During that Investor Day, we laid out some themes that are important to us. We talked about how we are playing for the long game, how we are running our own show, focused on American and not defining ourselves on others, looking to make long-term decisions and not be overly focused on near-term metrics. Those themes continue, of course, we're not going to go through them in great detail, but you will hear them running through all of our comments throughout this call.

We also laid out four long-term strategic objectives consistent with those themes. Those are to build a world-class product, to drive efficiencies, to make culture a competitive advantage, and to think forward and lean forward. We are, again, those are themes you'll hear us continue to bring up because we like the framework and we're excited about the message.

So with that said, I'll turn it over to Derek to give you some details on the numbers and then Robert will give more details as well.

**Derek J. Kerr - American Airlines, Inc.**

Good. Thanks, Doug, and good morning, everybody. And before I begin, I'd also like to thank our more than 120,000 team members. The third quarter brought more than its fair share of weather and operational challenges and our team delivered. Robert and I were both in Miami shortly after Hurricane Irma and witnessed firsthand how our team came together to take care of

our passengers and each other. The teamwork demonstrated by everyone at American made us all proud.

As Doug mentioned, we filed our earnings press release and 10-Q this morning and in that release, our third quarter 2017 GAAP net profit was \$624 million, or \$1.28 per share. This compares to our third quarter 2016 GAAP net profit of \$737 million or \$1.40 per diluted share. Excluding special items, we reported a net profit of \$692 million in the third quarter 2017 versus our third quarter 2016 net profit of \$933 million. Our diluted earnings per share, excluding special items, was \$1.42 per share versus \$1.76 in the third quarter of 2016.

Our GAAP third quarter 2017 pre-tax profit was \$1 billion. Excluding net special items, our third quarter pre-tax profit was \$1.1 billion, resulting in a pre-tax margin of 10.2%.

Looking at revenue, our total third quarter operating revenues were up 2.7% year over year to \$10.9 billion. Passenger revenues were \$9.4 billion, up 2.5% on a yield improvement of 1.6%. Cargo revenues were up 17% to \$200 million, due primarily to higher volume. Our other revenues were \$1.3 billion, up 2.2% year over year, due primarily to higher baggage and frequent flyer revenue.

Total GAAP operating expenses for the third quarter were \$9.6 billion, up 5.3% versus the same period last year. This increase was due primarily to a 13.3% increase in consolidated fuel expense and higher salaries and benefits expense as a result of the mid-contract base-pay increase given to our pilots and flight attendants earlier this year, as well as rate increases for our maintenance and fleet service team members that became effective mid-third quarter last year.

Third quarter consolidated ASMs, cost per ASM, was \$0.132, up 3.6% year over year. Excluding fuel and special items, our consolidated CASM was \$0.1043, up 4.5% year over year due primarily to the salary and benefit increases I mentioned earlier. We ended the third quarter with approximately \$8.3 billion in total available liquidity comprised of cash and investments of \$5.8 billion and \$2.5 billion in undrawn revolver capacity. The company also has a restricted cash position of \$393 million.

Since our last call, our Treasury team has been very busy. They completed another set of efficient financing transactions, including the 2017-2 EETC, AA- and A-tranches, as well as the 2016-3 and 2017-2 EETC B-tranches at very favorable coupon rates for junior subordinated EETC tranches. In addition, the team refinanced and extended the revolving credit facility,

upsizing it to \$2.5 billion in the process and closed on 5 mortgage transactions and 11 sale-leaseback transactions.

During the quarter, the company returned \$411 million to its shareholders including quarterly dividend payments totaling \$49 million and a repurchase of \$362 million of common stock or 7.7 million shares. Our share count has dropped by 37% from \$756 million at merger close in December 2013 to 480 million shares as of September 30.

In addition to our earnings release, we also filed our investor update this morning. Consistent with our previous guidance, in the fourth quarter of 2017, we expect our system ASM growth to be up approximately 2%, domestic up 0.5%, and international up 5%. For the full year, we continue to expect consolidated system capacity to be up approximately 1%, driven by increasing gauge, about 2.4%; stage length, about 1.5%, offset by 2.7% fewer departures. We expect full year domestic consolidated capacity to be approximately flat year over year and international capacity to be up 4%, primarily driven by the impact of the 777-200 retrofit program, which was completed during the third quarter and year-over-year impact of new destinations across the Pacific.

We expect our fourth quarter consolidated CASM, excluding fuel and special items, to be up approximately 4.5%, with mainline up 5% and regional up 2%. As we stated in our recent investor day, and consistent with our fourth quarter, we anticipate our unit cost growth rates to continue to trend lower and we expect 2018 full-year nonfuel CASM to increase, excluding the impact of any new labor deals, by approximately 2%.

We are forecasting a material increase in fuels in the fourth quarter. And based on the forward curve as of October 13, 2017, we expect consolidated fuel prices to be up approximately 16% year over year to between \$1.81 to \$1.86 per gallon on a consolidated basis. Using the midpoints of the cost guidance we provided in the TRASM guidance Robert will talk about a minute, we expect our fourth quarter 2017 pre-tax margin, excluding special items, to be between 4.5% and 6.5%.

As we continue with our fleet renewal program for the full year of 2017, we still expect gross aircraft CapEx to total \$4.1 billion, which includes the delivery of 57 mainline aircraft and 16 regional aircraft. In addition, we expect us to invest \$1.65 billion in non-aircraft CapEx for integration work and projects to improve our products and operations, a slight increase from previous guidance as we invest heavily in the installation of Premium Economy, narrow-body retrofit programs, updates to our clubs and other initiatives to improve the airline for our team members and customers.

On previous earnings calls, I provided estimates for our 2018 pension contributions as the airline relief legislation ends for us. While our minimum requirement contribution for 2018 are estimated to be only \$62 million, we now expect to contribute approximately \$780 million in order to maintain an 80% funded status on all of our plans.

We will continue to take a measured approach to matching our plan capacity levels with anticipated levels of demand. We are still in the process of developing our operating plan for 2018, so our formal capacity guidance will come when we report fourth quarter earnings. But on a schedule-over-schedule basis, we currently expect system capacity to be up approximately 2.5% in 2018 on a flat fleet count. We also expect domestic and international capacity to grow at similar levels of approximately 2.5%.

At our recent Investor Day, we also talked about the opportunities provided by our Project One Airline initiative to drive efficiencies. We've identified \$1 billion in cost savings that we expect to implement by 2021, driven principally by increased use of technology, changes to process and procedures and further eliminating post-merger redundancies. We are just getting started on these initiatives and will incorporate approximately \$200 million of savings in our 2018 plan. I look forward to updating you on our progress on future calls.

So in conclusion, despite the challenges resulting from the three hurricanes, our team has produced another excellent quarter. I would like to thank all of our team members for continuing to take care of our customers and as important, each other.

With that, I will turn the call over to Robert.

**Robert D. Isom - American Airlines Group, Inc.**

Thanks, Derek. Good morning to everyone, and thanks for joining us.

Before I begin my remarks about the third quarter, I'd also like to begin by thanking our more than 120,000 team members for all that they have done during a very challenging quarter. The tragic hurricanes in late August and September caused severe damage and disruption as Hurricanes Harvey, Irma and Maria made landfall in the U.S. and Caribbean. American canceled more than 8,000 flights due to the hurricanes and at the peak of the storm activity canceled all flights at nearly 30 stations. We estimate that these storms reduced pre-tax earnings by \$75 million.

In particular, I'd like to recognize our team members who endured the hurricanes at our hub in Miami and other airports in Florida, Puerto Rico, and the Caribbean, as well as those in Mexico City who endured a devastating

earthquake. You all have demonstrated courage, leadership, and compassion under extremely trying conditions. Not only did you help our airline get back online, but also and more important, you were all there for each other and for our customers. So a sincere thank you goes out to all of you from your teammates from around the system. You made us all very proud to be part of the American team.

As we discussed at Investor Day a few weeks ago, we have identified \$3.9 billion in revenue and cost initiatives that we expect to realize over the next few years. While I won't rehash all of that in detail today, and if it isn't already obvious, we are very excited about the opportunities ahead of us. We're already on our way with a full launch of Basic Economy across our domestic system on September 5. Our careful planning and measured rollout over the summer has resulted in a very successful launch with no disruption.

Performance has been in line with expectations, with about 50% of customers who received a basic offer choosing to buy up to the main cabin product. Although the rollout was too late to have a material impact on the third quarter of 2017, we do expect this to add revenue momentum to the fourth quarter 2017.

In addition, our Premium Economy product continues to gain traction with an average upsell of approximately \$400 each way over the coach cabin. Customer adoption of this highly differentiated product has been strong. As expected, the majority of Premium Economy customers are leisure customers looking for an affordable way to enhance their international flight experience. Premium Economy is now installed on 27 of our wide-body aircraft. And by year end, we expect that number to grow to 63, and by year-end 2018 to over 100 wide-body aircraft.

Operationally, our performance this summer showed significant improvement versus the summer of 2016. Summer on-time departures improved by 3.9 percentage points and arrivals by 3.2 percentage points, bouncing back from a difficult summer of 2016.

In addition, our baggage performance continues to be a focus for our team. This has been a bright spot, as the year-over-year mishandled bag rate has improved each month in 2017. When we do mishandled bags, we're working to minimize inconvenience for customers with the introduction of the new customer bag notification tool, which went live in July of this summer. This tool sends bag notifications to customers and allows them to set up free delivery for delayed bags or advises them to pick up early arriving bags at specific baggage claim locations. The early results are encouraging, as nearly 20% of customers notified of early or delayed bags are using customer bag notification to set up a bag delivery.

Turning to revenue, the demand environment remains robust. And despite the operational challenges and difficult year-over-year comparisons, we were pleased with our performance in the third quarter. Our third quarter PRASM was up 0.9% and our third quarter TRASM was up 1.1%, marking the fourth consecutive quarter of positive unit revenue growth for American. Our investments in people, product, and new corporate sales initiatives are beginning to pay off. And when combined with our new revenue management tools, changes to our AAdvantage program, and our new mobile platform, the results are even more encouraging.

In domestic, our consolidated PRASM was up 0.1%. We are very pleased with this outcome, as we faced hurricane impacts to our hub in Miami and had very difficult year-over-year comps due to beneficial pricing actions in the third quarter of 2016. On a year-over-two-year basis, our performance in the domestic market was materially better than our legacy counterparts.

Our Latin American performance overall was very strong, with PRASM up 8.3%. Positive Latin PRASM was driven by strong performance in all entities, consistent with what we saw in the second quarter. This is a great outcome as we have faced difficult conditions due to Hurricanes Irma and Maria.

Atlantic PRASM was up 2.6% year over year. Premium cabin pricing and yield management initiatives, improved share performance with travel management companies, and easing comps from past terror events continue to contribute to 2017 year-over-year PRASM performance.

The United Kingdom is showing the largest PRASM improvement on a year-over-year basis due to improved premium cabin performance. However, the overall environment remains challenged, as low-price carriers grow substantially, resulting in weaker pricing environment for coach travel.

Across the Pacific, PRASM was down 1.6% year over year. Japan, Australia, New Zealand, and Hong Kong were positive, but this was offset by softness in China and Korea.

Third quarter cargo revenue improved 17% year over year on strong volume growth, continuing a positive trend that we've seen since the latter half of 2016.

As we look to the fourth quarter, we expect our year-over-year TRASM to be up 2.5% to 4.5%, an improvement from our third quarter 2017 performance, as our revenue initiatives will continue to deliver top line benefits.

Regionally, our domestic PRASM is expected to be positive for the fifth consecutive quarter, helped by our launch of Basic Economy. Atlantic

performance is expected to be in line with the third quarter, with Pacific improving as we lap the growth of new routes from last year, and we expect the Latin entity to be modestly positive.

And to wrap up my comments and as we covered at our Investor Day, American has a privileged set of assets, our hubs and gateways in the U.S., and a world-class set of partners that extend our network even farther. A hub-and-spoke business model allows us to serve an incredibly broad spectrum of customers, getting them to the places they want to fly with the amenities that they value.

Our strategy investments and the investments that we've made and are making in our fleet, product and especially our team are working, as evidenced by our customer satisfaction metrics and our unit revenue performance versus the industry over the past five quarters and expected outperformance for a sixth quarter to close out 2017. And best of all, there's a lot more to come. And we're excited to deliver all that value for our customers, team members, and shareholders.

And with that, I'd like to turn the call back over to Doug.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Robert.

And before we open up to questions, I want to address an issue that's come up this week, which is the travel advisory from the NAACP. First, that announcement was obviously a disappointment to our team. That's because we at American Airlines pride ourselves on inclusiveness and diversity. What we do as an organization is connect people. We like to say we fly over borders and walls and stereotypes and divisiveness to bring people together. And our team members do that safely and professionally every day. And as a result, we make this world a smaller and more inclusive place.

Once we got past the disappointment, we realized this is a great opportunity. Yes, we're proud of our commitment to equality and diversity and the significant impact we make in that regard around the globe. But discrimination, exclusion, and unconscious biases are enormous problems that no one's mastered. And we would never suggest that we have it all figured out. What we know is we want to keep learning and we want to get even better. We want to be leaders for all of U.S. industry in equality, inclusion, and diversity because we actually think we can make a difference in the world if we do that. And organizations like the NAACP can help us, so we welcome the opportunity to work with them. Indeed, we're excited about it and enthusiastic to sit down and listen and learn together.



We've reached out and expect to begin working together in the very near term. That's good news for the people of American, for our customers, and our shareholders. We look forward to what lies ahead as a result of this effort, and we will keep you apprised as our work develops.

So with that said, Chris, we are ready for questions.

## **Question-and-Answer Session**

### **Operator**

Certainly. And our first question comes from Michael Linenberg. Please go ahead.

### **Michael J. Linenberg - Deutsche Bank Securities, Inc.**

Hey, I guess two questions here. Derek, I think you threw initially or maybe Robert, the capacity growth for next year, the 2.5% on a flat fleet count. Is that – I guess is that all gauge, or is there like a departure or stage length element in there as well?

### **Derek J. Kerr - American Airlines, Inc.**

Mostly gauge, probably 2 points of it gauge and the rest departures.

### **Michael J. Linenberg - Deutsche Bank Securities, Inc.**

Okay, that's helpful. And then probably to Don now, or Robert. Robert, you actually talked about domestic being strong again or positive again for, I guess, the fifth consecutive quarter on the backs of the success or early success that you're seeing with Basic Economy. Whether you or Don can just talk about that rollout. I guess we're six weeks into it, some of the pluses and minuses, any modifications or changes that you've had to implement since the rollout, that would be great. Thanks.

### **Robert D. Isom - American Airlines Group, Inc.**

I can start. It's been a smooth rollout. As you know, we took a measured approach with test markets, really made sure that our team out in the field was aware and could handle, and educated on the product, and so far, so good. We don't see a lot of changes and our expectation is to hit the targets that we've talked about. Don?

### **Donald B. Casey - American Airlines, Inc.**

Yes, I'd have to say that we introduced a million new fares into the marketplace, right, so that always takes a bit of time to stabilize. But I think

we're at a point right now where we're at a stable situation. I think we're probably not quite where the whole industry is probably going to end up from a pricing perspective. But we're kind of happy with where we are right now.

**Michael J. Linenberg - Deutsche Bank Securities, Inc.**

Great, thank you.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Michael.

**Operator**

And our next question comes from Brandon Oglenski. Please go ahead.

**Brandon Oglenski - Barclays Capital, Inc.**

Hey. Good morning, everyone and thanks for taking my question. So maybe this one's for Doug or Robert, but at the Investor Day, I think you guys highlighted to everyone that you've had a lot of internal focus the last couple of years, just bringing U.S. Airways and American together. As you look into 2018 and maybe some of those initiatives come off, what are the big priorities that you guys want to focus on, on improving the experience moving forward?

**Operator**

And pardon the interruption, Brandon. It looks like the speakers' line has just dropped. I'm going to go ahead and leave the queue as is. I'm going to reintroduce music until the speakers are reintroduced, so pause just a moment.

[Technical Difficulty] (25:07-27:03)

**Operator**

All right. Brandon, your line is back open. Please restart your question.

**Brandon Oglenski - Barclays Capital, Inc.**

Hey, everyone. I didn't know my question was that bad and gotten involuntarily denied here.

**William Douglas Parker - American Airlines Group, Inc.**

Brandon, we never even heard you. We actually just thought – once we had given our script and Linenberg asked his question, we were done. But apparently, some other people had more. Sorry, we don't know what happened. But anyway, we're back.

**Brandon Oglenski - Barclays Capital, Inc.**

I'm looking for some denied compensation on this one. But – listen, guys, my question was really, you talked about all the effort you guys have had internally the last couple years, merging U.S. Airways, American Airlines, and as you look into 2018, I think a lot of those initiatives really trail off. So what becomes more of an internal focus for you guys in 2018 as you can redeploy some people and assets and capital into more productive uses?

**Robert D. Isom - American Airlines Group, Inc.**

Yeah, I'll start. Look, our game plan is to really make sure that we make best use of what we've invested in so far. Yes, there's a lot more to come, but we take a look at our aircraft, our fleet, and the opportunity for utilization and deploying aircraft where we think it makes the most sense. And so that all plays into the One Airline initiative as well, where we think that we can grow revenues. We think that we can better utilize our aircraft, facilitate low-cost growth and then ultimately deliver more value overall.

So it fits very well, but really the focus is, if you take a look at what we've laid out so far, is to first deliver on what we've laid out, we've got a couple of things that are still important in terms of integration, and those are: making sure that we get a contract between our mechanics and our fleet service employees and then also making sure that we deliver on getting our flight attendants on one system and really fully integrate them. And then it's really at that point in time, it's a merged airline, able to focus on what we do best, and that's delivering value for our customers.

**Brandon Oglenski - Barclays Capital, Inc.**

I appreciate that, Robert, and I guess as we – you guys have attributed a lot of your revenue outperformance this year too to some of the changes you've made, I would say in your revenue management system. Should we be thinking next year, though, you don't have that level of outperformance on the industry and so you're going to look much more like the average industry participant? Or are there still levers that you're pulling on the revenue side?

**Robert D. Isom - American Airlines Group, Inc.**

Well, you saw from our Investor Day that we have a set of initiatives that are laid out. And it deals with everything from revenue management, and Don can speak a little bit about a new optimizer that just came online here recently, to all of our sales efforts and getting back out and really aggressive on that front, to making sure that we're flying and deploying aircraft where they can be best utilized. So we see that all of the initiatives that we laid out is playing out over the next few years and continue to advantage American, and in many cases, uniquely so, because many of these items are, in ways, catch-up. Some of the biggest initiatives that we laid out during Investor Day, everybody's aware of Basic Economy, of course, but Premium Economy is just in its infancy. And if you take a look at where we're headed overall, I feel really confident that we're going to be continuing to outperform.

**Brandon Oglenski - Barclays Capital, Inc.**

Thank you.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Brandon.

**Operator**

And our next question comes from Hunter Keay. Please go ahead.

**William Douglas Parker - American Airlines Group, Inc.**

Hunter Keay?

**Hunter K. Keay - Wolfe Research LLC**

Yes. Hello, Doug Parker, how are you doing? So the 2018 capacity growth, it's about a point higher than I was expecting, which it's my own bad modeling, I guess, but I suppose that makes the CASM ex-guide look that much less good than I thought, or less okay or acceptable. So given that type of capacity growth, and I guess this sort of dovetails a little bit with what Brandon just asked you, but do you still feel like you can grow RASM faster than CASM next year and expect to – effectively grow margins?

**William Douglas Parker - American Airlines Group, Inc.**

Hunter, again, I'll take a shot and the guys can fill in, I guess. First off, we always talk about CASM ex-fuel, of course. So you've got to make your own fuel forecast, but right now, it appears to be up. But if you're talking about...

**Hunter K. Keay - Wolfe Research LLC**

I'm sorry. CASM ex-fuel, Doug. CASM ex-fuel, thank you.

**William Douglas Parker - American Airlines Group, Inc.**

Yes, so can RASM grow faster than our – what we have now for our CASM ex-fuel guidance? Again, we're not giving a RASM forecast, but that's certainly been the trend of late and – anyway, Don, what do you want to say about that?

**Donald B. Casey - American Airlines, Inc.**

Yes, we had, as we kind of finished the third quarter, four consecutive quarters where our performance was materially better than the rest of the industry. And so as we kind of lap that, we still are going to have, in the third quarter, the fourth quarter, revenue that's kind of a bit better than the rest of the industry. And so that, I think, just speaks to the fact that we have a long list of initiatives, right, that are layering on top of one another that continue to drive better unit revenue year over year.

**William Douglas Parker - American Airlines Group, Inc.**

Yes, and, Hunter, I'll say this. Demand continues to look strong. All the initiatives that we've talked about are – those aren't things that we hope to get done. They're largely done. They're just kicking in. So we feel very good about that. So I'm happy to tell you – look, I would be disappointed if our RASM next year didn't exceed our CASM ex-fuel.

**Hunter K. Keay - Wolfe Research LLC**

Okay. Okay. And then on the cash flow, it looks like 2018 is going to be a pretty solid free cash flow for you guys given a few factors, even with the pension contribution. Derek, you said you're comfortable with the leverage levels and you guys are probably not focused on paying a 2.5%, 3% dividend. So is it safe to pencil in a pretty sizable uptick in the buyback relative to 2017, holding all else equal on margin assumptions and everything like that?

**William Douglas Parker - American Airlines Group, Inc.**

Hunter, again, make no assumptions. We can tell you what we can tell you, which is we think a minimum cash balance of \$7 billion -

**Derek J. Kerr - American Airlines, Inc.**

Liquidity.

**William Douglas Parker - American Airlines Group, Inc.**

Liquidity, I'm sorry, at American, which is awfully high relative to others, anyway, is the right number for us just because of the higher leverage. We think it's a better way to protect ourselves against downturns or any unforeseen circumstances than being less levered. So that's a number we look at as you do your forecast to the extent you see us generating cash levels substantially higher than that. We've always been of the view that once we've invested in our team, once we've invested in the airline, once we've paid down low-cost debt and invested in projects within the airline that can create returns for our shareholders, that the right thing to do is return it to our shareholders. So that would be a rational expectation of where the cash goes. What the actual cash flows are, again, not numbers that we're projecting, but you're welcome to.

**Hunter K. Keay - Wolfe Research LLC**

Okay. Thank you, Doug.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Hunter.

**Operator**

And our next question comes from Jack Atkins. Please go ahead.

**Jack Atkins - Stephens, Inc.**

Hey, guys. Good morning. Thanks for the time. Just to go back to Hunter's first question there on CASM, ex. Derek, could you maybe sort of outline a couple of the items that are maybe driving a little bit greater CASM, ex inflation, in 2018 than – and I guess who would've thought sort of before you provided that guidance? Just trying to think about some of the puts that are offsetting the efficiency gains that you outlined at the analyst day?

**Derek J. Kerr - American Airlines, Inc.**

Yes, I mean, there's four things that we believe will be higher next year. I mean, depreciation, of course, because we have the aircraft that are coming in and we have to – the CapEx that we've had year over year is the depreciation. Our rents and landing fees, I think from that perspective, we project to be from a CASM perspective a little bit up next year. Maintenance has a little bit of headwinds in there. And then, of course, salaries and benefits is the other one. But those four are the areas that we're focused on and that we know will be there next year, but we believe will hopefully offset most of those higher expenses to hit the 2% CASM that we talked about at the analyst day.

**Jack Atkins - Stephens, Inc.**

Okay. That's helpful. And then just, Doug, I guess for my follow-up question, maybe just a broader question for you. But certainly when you take the items that you guys outlined at the end of September at the analyst day together, it paints, I think, a very optimistic and very rosy outlook for the business as you sort of move forward here, and I think that's being reflected in the stock, starting to be reflected in the stock here. But I guess as you look out to 2018, things are setting out to be quite favorable for you guys, it seems like.

And I guess as you look at the business, what are some of the risks perhaps that you see out there that it could derail the story to some degree? Just trying to think through the risks that could show up next year in what otherwise would be a fairly positive environment for you guys?

**William Douglas Parker - American Airlines Group, Inc.**

Yes. Look, Jack, first off, we're bullish. So it's a fair question, of course, there are always risks. But I want to start out by saying, you're right; we're bullish. We feel really good about where American is. We feel good about the transformation that's taking place in the industry, the kind of risks that you would look at are the kind of things that could always happen in our business, economic downturn, well, the industry has dramatically transformed and stronger than it ever has been and I believe permanently transformed, we're still a cyclical business.

So if there's any sort of economic downturn, that would provide, that would pose some risk to the revenue performance. We're big consumers of fuel and so fuel spikes could have an impact. Again, I would argue spikes are one thing, but it's just increases given where we are, I think what you'd see is fares rise to levels to offset much of the fuel price increase.

So, look, I'm not going to be able to give you anything that's dramatically different than you would find and read in some of these risk factors. Because the real issue is we feel – we're really bullish. We feel really good about where American is, we feel good about where the industry is.

**Jack Atkins - Stephens, Inc.**

Okay. Great. Thanks again for the time.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Jack.

## **Operator**

And our next question comes from Helane Becker. Please go ahead.

### **Helane Becker - Cowen & Co. LLC**

Thanks very much. Hi, everybody, thank you very much for the time, Doug. So, I just have two questions. One is at Investor Day, you spent a lot of time talking about kind of focusing on the longer term in the outlook kind of beyond maybe 2017 and maybe even beyond 2018. And then on this call, you spend all your time talking about 2017 and 2018.

So I'm just kind of wondering if you can maybe talk about the longer term and tell us what you're thinking about with respect to maybe, I mean, I know you're not going to talk about pricing, but just in terms of where you see American in, say, 2019-2021 timeframe?

### **William Douglas Parker - American Airlines Group, Inc.**

Thanks, Helene. And I would love to do that, but I'm conscious of everyone's time. We tried really well to do that during the earnings call. What I'll tell you is, we know who we are. We are a global hub-and-spoke airline with, as Robert said, a set of privileged assets that allow us to do, to provide service to customers that we think is incomparable or certainly hard for others to replicate. And we know there is a good bit of upside in our ability to do that. What you should expect from us over time is an airline that has world-class products.

We know full well that we have to compete for all customers. But first and foremost, we want to make sure that we have an airline that is the airline of choice for business customers, for premium customers. And we're doing – everything we're working on now is designed to make sure we have a product in place to do that, not the least of which is a significant investment in our fleet, investment in satellite Wi-Fi across all the aircraft, and investment in our clubs, all this work that has just begun in the last couple of years and has the airline already in a much better place today than it was a couple years ago and we'll have it even better in the next couple of years.

We're going to work to make culture a competitive advantage. That as much as anything is where we think the upside is. We have an airline that, because of its history, still has our team members not as engaged and excited as we'd like them to be. And once we have leaders in place that our team knows care about them, that provide the tools to do their jobs the way they know how to do it, that lets them, that appreciates what they do, that helps them understand that what they do is incredibly important, and that they make a difference, so that they go home at the end of the day feeling



fulfilled. We know that will have a huge, that won't just be a better airline, that will be an airline that people want to fly and that's a competitive advantage. That's clearly not where we are now, but that's where we're moving.

We're going to continue to drive efficiencies, as Derek showed in our presentation. That includes a lot of work that just happens once we get integrated, but even more so a significant amount of work under the leadership of Maya and the IT team to make sure that we are at the leading edge of technology for our customers and for our team. And we're going to do all that with the mindset of thinking forward and leaning forward, a team that will be making sure that we come out of this past of short-term thinking and have a mindset throughout the organization that is always looking forward and thinking forward, something that we feel pretty good about, but we know we can do even better and we expect to be leaders in that arena.

### **Helane Becker - Cowen & Co. LLC**

So that's a great answer and I really appreciate it. I just have one follow-on question, and that's when you guys talk about the impact of the Middle Eastern airlines on your business, do you think that as your product improves, their relevance in our market dissipates?

### **William Douglas Parker - American Airlines Group, Inc.**

Look, the issue with the Middle East carriers is not about their product. That's a symptom of the problem. When you're subsidized and you don't care about making profits, you certainly can put in place a product that's uneconomic because the flying itself is uneconomic. But no, the answer to the Middle East carrier issue is not for us to have a product that competes with them. The answer to the Middle East carrier issue is for them not to be subsidized and for us not to have to compete against countries and for our country to step up and do what it needs to do and make sure that we aren't forced to do that.

One of the biggest threats, if not the biggest threat to everything I just said about the long-term viability of our business is the U.S. government not stepping up and making sure that those two countries aren't allowed to continue to subsidize flying and to jeopardize U.S. aviation jobs. We can compete against anybody as long as the playing field is close to fair. What we can't do is compete against oil-rich countries that don't care about making profits and that seem to have a different objective of trying to help their countries through having an aviation practice that doesn't make any money but brings people in and out of their countries.

So look, the good news on this is we've had productive conversations with the administration, myself as well as the CEOs of American – CEOs of United and Delta met with some secretaries this quarter and were encouraged by the reception. There's still work to do, of course, but are hopeful because this is as easy as it gets in terms of being able to create a case that shows that American jobs are at stake because of policies of other countries, and we should enforce ours.

So anyway, that's not a product issue, that's a subsidization issue and a really, really important one that we're screaming from the mountain tops about and people are beginning to listen, so we feel good about it.

**Helene Becker - Cowen & Co. LLC**

Great, thank you.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Helene.

**Operator**

And our next question comes from Jamie Baker. Please go ahead.

**William Douglas Parker - American Airlines Group, Inc.**

Hey, Jamie.

**Jamie N. Baker - JPMorgan Securities LLC**

Hey. I was expecting to be introduced as Jacques or Jaime or something. We're pleased with the fourth quarter guide, Doug. I hope you saw the mea culpa this morning in terms of the PRASM component. Well done, Don, that's for you too, but I still need to ask about margins. The gap to Delta is widening. Look, I know there's seasonality in the business, but the fourth quarter guide looks to be one of the widest gaps ever post-merger, and that's even with the profit-sharing change at Delta and an otherwise unimpressive ex-fuel cost guide from Delta.

So my question is when you decided to revisit the union economics mid-contract, you were pretty insistent or confident that you'd see a return on that investment. I'm not seeing it. And maybe I'm just looking in the wrong place, Doug. Maybe the goodwill that you thought to generate is just, I don't know, taking a longer time to filter through to better passenger service. I don't know, any thoughts on that?

**William Douglas Parker - American Airlines Group, Inc.**

I got a lot. So first off, on the mid-contract adjustment, I'm absolutely positive it was the right thing to do. We told you at that time you're not going to see it. If all you want to do is look at a spreadsheet, you should just raise your costs from what your estimate was. We also told you that if we didn't do it, you should have lowered your revenues in the future because we can't go do all the things I just said we're going to do in the future and ask our team to work for less than their peers at other airlines. We're not going to do that. So yes, we're going to sign contracts and when we sign them, they're going to be at those levels. And no, we don't expect that anytime someone else signs another contract that we need to match it.

But when we get into a situation like we did with our Boston flight attendants, where the contract we had put in place with that same mindset and the same objectives, because of just some unforeseen competitive circumstances, has them in a position where they're going to be well below their peers at other airlines for an extended period of time. We think the right thing to do is to correct that, and you should expect to see us do it in the future if it happens again. I don't expect it will happen again, but if it does, you should expect us to do the same thing because it's the right thing to do for our team.

We can't go make our culture a competitive advantage by asking our team to work for less than their peers do at other airlines. So that was absolutely the right decision and we feel extremely good about it and always will.

As to relative margin performance, I will reiterate again that we at American are focused on running our own game and don't spend a lot of time focusing on what others are doing. We certainly don't define – aren't going to define our success relative to others. But having said that, I'll entertain the comparison right now because I know it's important to you all.

What I know is this: The trend itself, which I know you know because you can see it in the numbers, is a cost trend, not a revenue trend, and the cost trend is due to what I just said. We had to get our, primarily due to what I said. We had a cost advantage in labor and we didn't think that was right and we don't think it's right, so we had to close it. So that's the trend. That is not a trend I would expect you would see continue going forward, but that's what's driving the trend in relative margins versus Delta.

On the absolute basis, look, margins by region come and go, margins by hub come and go, but what I can tell you right now is Delta has an airline that flies over 40% of their flights in and out of Atlanta, which is a really, really good hub. And if American flew 40% of its flights in and out of Charlotte, we would have a margin advantage there in the business because Charlotte's a really, really good hub. But we don't, so be it.

It's not about mismanagement or anything close to it. It's about the networks that are currently in place at the airlines. but given that advantage, they also have that – they have that advantage, by the way, in valuation. So look, we look at where we are, we know who we are, we know what we have, and we know there's enormous upside for our shareholders if we go execute against the plan we've laid out. And like I say, we're not going to define ourselves against what others are doing.

The other key point I would make here is, they did their large merger some six, seven years ahead of American and we are closing fast. So a lot of the upsides that Robert talked about and he rightfully said we're playing catch-up, we're not playing catch-up because we were asleep, we're playing catch-up because we did our merger in 2013 and they did theirs in 2007 or 2008.

So all those things will lead, I think, to the trend not being an issue and the absolute number, like I say, sometimes some of us will be in better conditions relative to others given where our networks are at any certain point in time and what region of the country we fly in, what the competitive dynamics are. But the valuations will fluctuate accordingly.

#### **Jamie N. Baker - JPMorgan Securities LLC**

Okay. And second, and it's a bit of a modeling question, I think it's where Hunter was going. But flown versus flown capacity looks like it's going to be up at least 3% next year, ex-fuel TRASM up 2%, given where the fuel curve is. You're going to need something like 5% TRASM if you want to hit that \$5 billion pre-tax state you're in. You just said that you'd be disappointed if TRASM doesn't exceed CASM, which is good. But I guess the question is whether you'd be disappointed if TRASM isn't more than twice the rise in CASM. I mean, you've got to admit for 2018 to be one of those mid-cycle, \$5 billion pre-tax years, we really need to stretch our models at this point. Should we just let go of that target for another year?

#### **William Douglas Parker - American Airlines Group, Inc.**

Look, the target is, again, one that we have said consistently is one that we believe over time will average. What we say is, good years on average – that's what we believe, that's how we set our short-term incentive compensation for our executives is if we have an airline that makes \$5 billion pre-tax, the incentive payments are 100%. If we don't, they're less than that. And if they're below \$3 billion, there's none. We've set that in place because we believe that's what the long-term earnings power of this airline is. And we certainly believe that.

We have not said, and not saying today, that that means every year, you should go expect we're going to be at that number. I'm not saying we're not,

either. I'm just making clear that we didn't ever mean to suggest that every single year will be that. What we said is we will be in a range of 3%, 5%, or 7%. So 2016 is not going to be one of those years, that's now clear. 2017, I'm sorry. 16 months. 16 months, that's really clear. So – as was 2015. 2017 wasn't. I don't know if 2018's going to be or not. But we'll see.

Again, that's something for you all to do your best to try and figure out based on the information we provide and the big missing piece of information that we don't provide is what we think our full-year 2018 RASM's going to be. But you can make your own guesses as best as we can. But what I can tell you is we feel really good about the industry dynamics. We feel particularly good about American's ability to do even better than the industry based upon all the initiatives that Robert and Don have laid out.

**Jamie N. Baker - JPMorgan Securities LLC**

Okay. Thanks so much for the time, gentlemen.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Jamie.

**Operator**

And our next question comes from Kevin Crissey. Please go ahead.

**Kevin Crissey - Citigroup Global Markets, Inc.**

Hey. Thank you for the time. Can you – I'm going to have two quick ones. Can you talk about the progress on corporate sales?

**Donald B. Casey - American Airlines, Inc.**

Sure, okay. This is Don. Yes, we've made good progress, this is now the third quarter in a row where we've seen improved performance in our share and share gap. And in this quarter, we also saw an improvement in average ticket value. And as we put more resources into our sales organization, we've also focused on getting more small to medium-size companies with a corporate deal with American. And this year, we've added 16,000 small to medium corporate accounts since January, that's up an increase in total small to medium corporate accounts of 50%. So we're very pleased with the progress we've made on that front.

**Robert D. Isom - American Airlines Group, Inc.**

Don, I'd just add a couple of other quick points. And one is that the team that we're bringing on, that's something that is in progress, but we'll have

over 130 new people out in the field by 2018. New distribution capability, really allowing all of our customers to be able to access all of our products, was launched back in June of 2017, will continue to have a positive impact. And then one of the areas that we hadn't spent a lot of time in terms of focus areas of the group's business is something that we've been getting back into and seeing some good progress there, too. So again, the sales team, under Allison Taylor's leadership, is really doing what we had hoped.

**Kevin Crissey - Citigroup Global Markets, Inc.**

Thank you. The second question, maybe for Don. When you're, and I assume it was you along with the team, setting the RASM target for the quarter, as I recall and looking at the data as well, the year last year closed quite well and I think close-in bookings did well, particularly in December and the close-in environment isn't as strong this year. Can you just talk about when you were setting that range, how you thought about that situation?

**Donald B. Casey - American Airlines, Inc.**

Again, we've set the range based on where we are, our current held position, as well as all of the initiatives that we have in place that are going to continue into the fourth quarter. As far as kind of the close-in yield situation, we saw kind of our close-in PRASM of the domestic business be off just like 2% in July and August, but rebounded quite strongly in September. We think a lot of that has to do with Basic Economy and Basic Economy appears to be doing exactly what we wanted to do. And we think that's going to help us actually drive near-term yields positive as we go through the fourth quarter.

**Kevin Crissey - Citigroup Global Markets, Inc.**

Thank you.

**Operator**

And our next question comes from Duane Pfennigwerth. Please go ahead.

**Duane Pfennigwerth - Evercore Group LLC**

Hey. Thanks. I'm not sure if anybody's already asked this, but can you talk about your revenue outlook by region underlying your healthy 4Q outlook?

**Robert D. Isom - American Airlines Group, Inc.**

It was covered in my opening comments.

**Duane Pfennigwerth - Evercore Group LLC**

My apologies.

**William Douglas Parker - American Airlines Group, Inc.**

He wasn't on then.

**Robert D. Isom - American Airlines Group, Inc.**

Yes.

**William Douglas Parker - American Airlines Group, Inc.**

You got it, Don? Go ahead.

**Donald B. Casey - American Airlines, Inc.**

Yes, I'll cover it. So domestic, we're seeing – as we look forward, we're seeing, actually, yields up, so we're seeing good yield performance in the domestic business. So we're expecting that to hold up as we go through the fourth quarter. Atlantic, we expect to be pretty similar to what we saw in the third quarter where we see pretty aggressive pricing in the coach cabin related to growth of low-cost carriers, but that's being offset by strength in the premium cabin, and we think Premium Economy is going to really help us as we move forward.

Pacific, we're actually expecting to be better in the fourth quarter. This is tied to lapping some of the capacity increases we had last year with new routes as well as improved share performance we're seeing in specialty channels to Asia and the response to the premium product that we put in the marketplace. We didn't have full lie-flat product in the Pacific until February of this year. And we're seeing very good response to the quality of our premium product.

And the Latin is the one market where there's been kind of the greatest amount of uncertainty. The impact of the hurricane in the Caribbean, although we're seeing right, it appears so far that that demand is holding up. Some questions around the travel warning to Mexico, which we've seen a bit of softness in Mexico. And we're seeing some capacity creep into Brazil. So probably the greatest uncertainty we see right now is in the Latin entity, but we still expect them to be positive year over year.

**Duane Pfennigwerth - Evercore Group LLC**

That's very helpful. Sorry to make you repeat that. And then did you put any numbers to Basic Economy contribution in the third quarter and what you expect in the fourth quarter? Thanks for taking the questions.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Duane.

**Donald B. Casey - American Airlines, Inc.**

We didn't, Duane.

**Duane Pfennigwerth - Evercore Group LLC**

Okay, thank you.

**Operator**

And our next question comes from David Vernon. Please go ahead.

**J. David Scott Vernon - Sanford C. Bernstein & Co. LLC**

Hey. Good morning, guys, and thanks for taking the question. So, Doug, I wanted to ask you like a longer-term question about industry dynamics. And I think a lot of investors look at changes in supply and demand and think that's going to be sort of the outright change in yield for the industry and for each carrier. Are you seeing any greater ability the last couple years to manage your yields independent of what might be happening in supply and demand on a route-by-route basis? Obviously, capacity is going to matter, but is it mattering a little bit less? And if you could talk little bit about what might be changing there, that would be great.

**William Douglas Parker - American Airlines Group, Inc.**

Sure, although at the end there, it sounded like a short-term question on the longer-term issue. Let me do the longer-term issue and I'll let Don talk about whether on the yield, if we're seeing yield be able to manage irrespective of capacity. Anyway, I have my own views, but I'll let Don answer it better.

On the longer-term issue, anyway, I'll give you – again, we can only – all we know about is American's capacity plans and where we think we have growth. I do happen to believe that what you're seeing in our industry is, in terms of the capacity increases, is entirely consistent with what we believe is where the industry is headed, which is in the final stages of a maturation process, where you're seeing hub-and-spoke carriers filling out only in their hubs and you see some attempts from ultra-low-cost carriers and other



carriers to find markets which they may or may not be able to do, largely point-to-point and they find trouble as they move into hubs.

So that doesn't feel to me like any sort of major trend, but rather a, like I say, kind of a – the end, really, of getting this industry to where I think we've been going for a long time, which is an intensely competitive business with three large hub-and-spoke airlines that do extremely well, doing what we do, and then some point-to-point carriers that can find markets where they don't, where what they do makes sense. And that, like I say, intensely competitive, but not continually evolving, so at any rate, with that said, Don, on this yields-versus-capacity question?

**Donald B. Casey - American Airlines, Inc.**

I think we have a number of initiatives that are part of our portfolio that have been rolling out that are all designed around increasing yields. So Basic Economy, all right, that increases yields, because while we were matching the fares before, now 50% of the people that were buying these fares before are not going to be paying more than they paid.

So that's the increased yields. Premium Economy, which we're going to roll out in the wide-body is again increasing yields. This is really a leisure product. And we're seeing people buy up from economy into the Premium Economy cabin. That's going to increase yields. We now have the leading product – business class product among U.S. carriers in the long haul and we're seeing tremendous demand which is allowing us to actually sell up through the fare ladder into the premium cabin. That increases yields.

All the initiatives we have in the sales organization side is getting a better share and we're seeing it today in our high-value channels. All of that increases share or increases our yield premium. And on the RM side, we've made a number of changes both in terms of our infrastructure and to our business process, which is all designed around selling out more effectively, which will increase our yields. And we have a host of initiatives coming in the AAdvantage program later in 2018 and 2019, which are going to attract more high-yield customers which is going to increase yields. So I think we got a big portfolio of initiatives that are all designed around increasing yields.

**William Douglas Parker - American Airlines Group, Inc.**

And, Don, just to add one more and that's just around all the work that we're doing with the ancillary products as well.

**Donald B. Casey - American Airlines, Inc.**

Yes.

**J. David Scott Vernon - Sanford C. Bernstein & Co. LLC**

Appreciate the color. Maybe just as a quick follow-up, could you help us understand where you see the distribution model evolving over the next couple years? How many customers are buying directly from you today versus the GDS and how do you expect that to change over the next, I don't know, maybe five years or so?

**William Douglas Parker - American Airlines Group, Inc.**

We've launched our own NDC initiative which we did in – just past summer. This is a long-term initiative, right? This is not going to be a kind of knife edge. Our goal here is to be able to offer more products and services to both our corporations and our travel agency partners, that's through our NDC product, it's not to replace GDS. But it's going to process, it's going to roll out over many, many years.

**J. David Scott Vernon - Sanford C. Bernstein & Co. LLC**

And do you...

**Derek J. Kerr - American Airlines, Inc.**

We lost you, David.

**William Douglas Parker - American Airlines Group, Inc.**

David, you cut out.

**Operator**

It looks like the line cut. I apologize. Our next question comes from Dan McKenzie.

**William Douglas Parker - American Airlines Group, Inc.**

Hey, Dan.

**Operator**

Please go ahead.

**Daniel J. McKenzie - The Buckingham Research Group, Inc.**

Hey. Good morning. Thanks, guys. Don, with respect to the full launch of Basic Economy across the system, does that mean it's available on 100% of

the domestic flights or only where you face the ULCC competition? That's first. And then I'm wondering if you could just help us frame the revenue exposure, is that, say 10% or 3% of the revenue base that's facing some of this intense pricing competition? I'm just trying to get a sense of the base exposure today because the revenue guide is, of course, pretty encouraging.

**Donald B. Casey - American Airlines, Inc.**

Sure. Well, when we rolled out Basic Economy, we rolled it out to the entire D48, and so we have it in all markets, broadly across the entire domestic system.

**William Douglas Parker - American Airlines Group, Inc.**

Exposure.

**Donald B. Casey - American Airlines, Inc.**

Oh, our exposure to ULCC price. If you take a look at our total revenue pot, so that's all revenue from all sources and look at the amount of revenue that we currently sell at ULCC fare levels, this is before the basic launch, it was about 3%. And so of the 3% that we sold at basic, or sold at ULCC levels, about half of that now is selling up into a main cabin fare. So it's probably about a 1.5% of our total system revenue, all revenue, total revenue, that's – we're currently selling at ULCC price level.

**Daniel J. McKenzie - The Buckingham Research Group, Inc.**

Very helpful. And then second, Derek, if I can just kind of go back to Hunter's question and help us to get a little smarter about forecasting stock buybacks, how do we think about aircraft financing for orders that remain aircraft orders? Obviously, aircraft CapEx slows down a lot, but there's still a chunk of change going into new aircraft, so 50% financed or bought in cash? Just anything...

**Derek J. Kerr - American Airlines, Inc.**

I think as we look at – we're all done financing everything in 2017 and we also have financed a few aircraft into 2018, so our aircraft CapEx for 2018 is about \$1.2 billion. I would assume that we finance 70% of that, 70% to 75% of that instead of full up. We may do some sale-leasebacks depending on where the market is and do it all, but I think for modeling purposes, I would use 75% to do that.

**Daniel J. McKenzie - The Buckingham Research Group, Inc.**

Perfect. Thanks, Derek.

**Derek J. Kerr - American Airlines, Inc.**

And just one other thing I just wanted to correct from Mike's earlier question on capacity, when we talked about 2018 capacity, I had it backwards. I apologize, but departures will be up about 2% where gauge is up about 0.5%. So that's the 2.5% on a flat fleet. I just wanted to correct that from an earlier question.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, Derek. Hey. We hate to cut people off that have questions, but we have a hard stop in about 20 minutes and we need to get to the media. We've got a couple of analysts lined up, it looks like. So we're just going to do speed answers on those and get to the media if that's okay.

**Operator**

All right. And our next question comes from Joseph DeNardi. Please go ahead.

**William Douglas Parker - American Airlines Group, Inc.**

Joseph, how are you?

**Joseph William DeNardi - Stifel, Nicolaus & Co., Inc.**

Great. So, Derek, if I back out the ancillary revenue that will be put into passenger revenue starting next year with the rev-rec changes, about 90% of other revenue next year will be the loyalty revenue that goes through other. So is there a plan to either rename or break out that line next year? Why would you continue to call it other when that's not really what it will be?

**Derek J. Kerr - American Airlines, Inc.**

I think it's 80% is what the number will be when we get done with it. But we have disclosed a fair amount of it. We already have disclosed what the number is in that line, so you will know what that number is where we have it. If we have one line that says that and one that's other, that's the other 20%. We haven't thought about that in the next year, but I think that number that is in that line has already been disclosed and will continue to be disclosed.

**Joseph William DeNardi - Stifel, Nicolaus & Co., Inc.**

Yes, just buried a little in the 10-Q. So, Doug, it would seem like maybe one of the unintended benefits from disclosures is to your labor groups, the stability that the marketing company speaks to, why they're part of a more

sustainable organization than in the past. So has that been a consideration as you think about providing more disclosures and transparency? It feels like you guys are trying to find reasons not to disclose and not really looking at some of the benefits. So what do you think there?

**William Douglas Parker - American Airlines Group, Inc.**

Look, we're not trying to find reasons not to disclose, Joseph. We told you in the past, we have confidentiality issues that make it hard. We try to be pretty transparent about it. But nonetheless, we don't have any issues in communicating with our team members as is. There's nothing about our relationship with our team members that makes us think gosh, we wish they understood better how strong this company was. I think they get it. Indeed, they're a big part of why that's the case. So I'm not compelled by that.

But nonetheless, we hear you on disclosure and transparency. Look, the long and the short of this, Joseph, is at the end of the day, that's just yet another revenue channel for us. And it's a place that we collect dollars even though they come through a credit card company because people use them, and we use that to give people seats that we could sell otherwise. And we don't generally disclose profitability by revenue channel. And indeed, it's really, we can talk about the revenues, it's really hard to talk about the profitability because what you're really talking is the opportunity cost of an unsold seat.

So nonetheless, we'll keep working through this with you. I know it's important to you. We certainly agree it's a key part of our business, and our team gets that completely because they're a big part of the business, as is that program. Who's next?

**Operator**

And our next question comes from Darryl Genovesi. Please go ahead.

**William Douglas Parker - American Airlines Group, Inc.**

Hey, Darryl.

**Darryl Genovesi - UBS Securities LLC**

Hi, guys. Thanks for the time. So you guys, along with many of your peers, have highlighted some unexpected cost items creeping in your business lately, things like accelerating airport cost inflation, rising CPA costs, healthcare, shortening useful lives. There's been a long list from airline to airline. But if I were to generalize, I can come up with explanations for a lot of these. You've got tighter labor supply, tighter airport capacity, an R&D cycle at Boeing, Airbus, and oil's taken a reasonable bounce. I suppose these

are all things that we could highlight as items that also restrain supply growth and afford you and the industry overall some pricing power.

That being said, can you see any stabilizing factors on the horizon? For instance, have higher wage rates yet resulted in an increase in entry-level labor supply? Are growth investments in airports accelerating, anything like that? Overall, I guess what I'm asking is whether these items are, whether or not first of all, you think they're real supply constraints, and then secondly, whether you think any of them are going away.

**William Douglas Parker - American Airlines Group, Inc.**

Go ahead, Robert.

**Robert D. Isom - American Airlines Group, Inc.**

No, I'll just start with, look, our greatest competitive advantage is our hubs and our gateways. And at the end of the day, the more that we're able to execute our business model and be able to provide connections and serving the broadest market possible, that is something that we think is a sustainable advantage and something that is unique to American and other large network carriers, and it's going to be where we put our time and attention.

**William Douglas Parker - American Airlines Group, Inc.**

And, Darrell, on the trends question, I'd just add again. And I'm not trying to actually reinforce the view that we think there are enormous cost issues here, but certainly, as Derek said, there are some areas like airport. What's happening is the industry has been consistently under-invested in for a really long period of time because we weren't profitable. And airports require profitable airlines in order to go invest. The good news is we have that now and that's what's happening. You're seeing huge capital improvements throughout the industry in airports. But yes, that won't continue. Over time once those investments are made and that's in the cost structure, I don't think you'd see that continue.

As it relates to the labor costs, as we said, we had a lot of catch-up to do. Once everyone is on an equal basis, we certainly are not seeing at our existing and now raised pay rates any sort of issue in terms of attracting and retaining great people. And I imagine that's the case at our competitors. So I wouldn't expect you'd see once everyone gets on a fairly level basis, certainly not the levels you've seen in terms of wage inflation going forward either. So there is a good bit of catch-up that had to happen from what was once a horribly inefficient industry to one that is now investing for the long

term in its people and its airports. But once those investments are made, you shouldn't expect to see it continue.

**Darryl Genovesi - UBS Securities LLC**

Okay, thank you.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks. All right, we can go to the media.

**Operator**

All right, and our first question comes from Mary Schlangenstein. Please go ahead.

**Mary Schlangenstein - Bloomberg LP**

That was close. Hey, I wanted to ask you guys, JetBlue said on their call this week that they don't see tourism to Puerto Rico recovering until the end of 2018. I wanted to see if you have the same view there or if you see a – and they're talking about 100% recovery, if you see that maybe on a shorter timeframe.

**Robert D. Isom - American Airlines Group, Inc.**

Mary, we just don't know.

**Mary Schlangenstein - Bloomberg LP**

Okay.

**William Douglas Parker - American Airlines Group, Inc.**

Anything else, Mary?

**Operator**

And our next question comes from David Koenig. These go ahead.

**David Koenig - The Associated Press**

Thanks for doing this. I'm sorry if this came up during the analyst session. I didn't catch all of it. But, Doug, what do you make of the NAACP travel advisory? Did they tell you that it was coming, and are you worried it will hurt sales? Will people book away?

**William Douglas Parker - American Airlines Group, Inc.**

Hey, David. So you weren't on at the start, I guess. I did address that already. Anyway, what we think is we think it's a great opportunity. We know that we work very hard to make sure that we have a diverse and open environment and organization that we pride ourselves in those things. We also know we can always get better. So while the initial reaction was certain disappointment because when you look at that and think how can that be true of us, but once you get past that and think, well, this is a fantastic opportunity because we want to get better. We always want to get better. And what we think is business can lead the way in things like this.

It's an important issue for our country and our world and divisiveness seems to be getting worse, not better. It's things that we always, within business, you don't, we can be leaders in this regard, because our employees are a diverse group of people, our customers are a diverse group of people, so we always end up being leaders in areas like this. But we can also be leaders in making it better. So if the NAACP wants to talk to us and wants to help us get better, we're excited about that. So we've already reached out. We're going to work together to get better. And we appreciate their input and we're excited about it.

**David Koenig - The Associated Press**

Any worry about the impact on bookings?

**William Douglas Parker - American Airlines Group, Inc.**

I don't know. We haven't seen anything, but again, that is not the point. The work we're doing has nothing to do as to whether or not – it's not about whether or not it has a financial impact on our company. We're going to do it because it's the right thing to make our company stronger and that we care about. So this isn't about whether or not people fly us. We got – people are flying us and that's not the issue. It's about being a stronger company and providing leadership, so we're excited about that.

**David Koenig - The Associated Press**

Thanks.

**William Douglas Parker - American Airlines Group, Inc.**

Thanks, David.

**Operator**

And our next question comes from Edward Russell. Please go ahead.

**Edward Russell - Flightglobal**



Hi. Yes. Derek, I wanted ask about the 5 loans and the 11 sale-leasebacks you mentioned in the third quarter. Are those under the certain aircraft financings and the 10-Q that was released this morning?

**Derek J. Kerr - American Airlines, Inc.**

Yes, they are.

**Edward Russell - Flightglobal**

Okay. And in terms of those aircraft, I mean what kind of aircraft were those 16 transactions involving?

**Derek J. Kerr - American Airlines, Inc.**

Mostly narrowbody aircraft. I think all of the MAXes were part of those. Some of those were refinancing of Embraer 175's also.

**Edward Russell - Flightglobal**

Okay. So the MAXes will be arriving through the end of the year?

**Derek J. Kerr - American Airlines, Inc.**

Yes.

**Edward Russell - Flightglobal**

Okay. Got it. Thank you very much.

**Operator**

And your next question comes from John Biers. Please go ahead.

**John Biers - Agence France-Presse**

Hi, thanks very much for taking my question, John Biers from Agence France-Presse. I also have a question on the NAACP. One of the examples they pointed to was of a passenger who experienced discriminatory conduct and responded and was removed from the plane. I wondered what is your policy in this kind of example where a passenger is abused by another passenger? Now are you seeing more instances of this kind of conduct on your flights right now?

**William Douglas Parker - American Airlines Group, Inc.**

Okay, well, first off, we'll separate your question from the issue with the NAACP because I don't want to conflate those two issues. If you're asking

just are we seeing an increase of customer issues on aircraft, not to my knowledge. I mean, we have those from time to time, but our team does a really nice job of de-escalating issues and our objective is to make sure we provide a product that makes all of our customers feel welcome and we'll continue to do that.

But we certainly have, we don't see any significant trends one way or another. These are very rare events when they happen, we transport 500,000 people a day at American Airlines. And sometimes we do have issues with customers and that's our responsibility, just as much the other 500,000 people, so we take responsibility for them. But there is no major trend going on in that regard, but that doesn't mean they're not important.

Anybody else?

**Operator**

It appears we have no more questions at this time.

**William Douglas Parker - American Airlines Group, Inc.**

All right. Thank you all very much for your time. We really appreciate it. Any further questions from analysts, give Dan a call; media can contract Corporate Communications. We appreciate your time. Thanks.