BUSINESS

Airline Shares Drop on Capacity Expansion Plans

Investors don't like go-go capacity expansion because they fear it will spark accelerated growth by other carriers

United outlined on Tuesday plans to add routes and beef up domestic hubs. PHOTO: TIM FADEK/BLOOMBERG NEWS

By Susan Carey

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Airline shares tumbled on Wednesday as investors fretted that United Continental Holdings Inc.'s expansion plans threatened profit margins and could spark a price war if other carriers follow suit.

United shares plunged more than 11% a day after the No. 3 U.S. airline outlined plans to add routes and beef up domestic hubs. Shares of four airlines due to report earnings on Thursday, American Airlines Group Inc., Southwest Airlines Co. Alaska Air Group Inc. and JetBlue Airways Corp. , all slipped as well, as did shares in Delta Air Lines Inc. and Spirit Airlines Inc.

"There's no way to sugarcoat the capacity additions," JPMorgan Chase analyst Jamie Baker said of United's plans to add as much domestic capacity by 2020 as discounter Spirit operates today overall. "Couldn't United have bolstered its hubs by severing one?"

Evercore Analyst Duane Pfennigwerth said United failed to convince investors that the capacity boost will generate enough passenger and revenue growth to reverse six quarters of declining profit margins. "Investors are still expected to take it on faith," he said.

Investors don't like go-go capacity expansion because they fear it will spark accelerated growth by other carriers, which can result in more seats than demand and lead to price wars. "United's capacity outlook is likely to be met with aggressive competitive responses," said Cowen & Co. analyst Helane Becker.

American, the biggest U.S. carrier, added just 1% to its capacity in 2017 compared with the prior year, but its shares tumbled 6% on Wednesday. Shares of Southwest, Alaska Air and JetBlue all fell a day before their earnings reports, though investors don't expect any of them to expand capacity as aggressively as United.

Delta, the first carrier to report fourth-quarter results, said it expects to add 3% to its capacity in the current quarter. Its shares fell 5.2% Wednesday.

United President Scott Kirby on Tuesday stressed the need to boost its network and catch up with rivals after shrinking service over the past five years. He said United in particular needs to bolster its midcontinent hubs in Chicago, Houston and Denver, where profit margins are 10 points lower than at American and Delta hubs. “We’re not trying to reinvent the wheel here,” he said. “In fact, this is a well-worn playbook.”

In a statement Wednesday, United said it is “very confident in the strategy we set out, which we believe will drive sustainably higher margins and profits. We are fully focused on executing our plans in 2018 and beyond.”

The share turmoil recalled a 12% one-day decline in October when United irritated investors by offering little clarity on its progress in efforts to cut costs and raise revenue. The Chicago-based company disclosed better-than-expected fourth-quarter results on Tuesday.

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