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Are Airline Stocks Taking Off Again?

Securities of the airlines, the most phenomenal transportation development of mankind, are attracting shrewd bargain hunters. Equities in this severely deflated group, selling at approximately 25% of their 1945-6 highs, appear to be in a long term buying range and recently have shown independent strength marketwise.

Admittedly the outstanding flop of the postwar period from the standpoint of profits and market action of securities, the air transport industry has achieved tremendous growth and now seems to be on the road to profitable operations. Many problems are still to be overcome and the outlook for some airlines is better than for others, but the indications of improvement throughout the industry are striking.

Recent actions by the Civil Aeronautics Board have indicated a realization that unbridled competition is no more desirable in the air transport field than in public utilities. Recent decisions on mail pay justify the expectation that a sound mail pay policy is evolving. Substantial retroactive mail payments have been granted to Braniff, Chicago & Southern and Delta, transforming their previous deficits into black figures. Continental was an earlier beneficiary of this policy. Not only have these airlines received substantial cash payments for retroactive pay, but the CAB has restored their mail pay to a plane-mile basis, with a sliding scale which increases rates when traffic declines. Mid-Continent, a consistent earner, is scheduled to receive an adjustment in mail pay in the immediate future. Within the last few days, National has been granted a large temporary rate increase on a plane-mile basis, and retroactive pay for 1945. Western and Capital are expected to receive increases soon. The mail case of the Big Five (American, Eastern, Northwest, TWA, and United) has not been finally decided, although in April, 1948, small retroactive payments were authorized, and ton-mile rates were increased to approximately 64 cents. The final decision may be rendered very soon, and the expectation is that the Big Five will receive considerable increases, which may largely reduce or eliminate any 1948 deficits.

The rates of air mail pay are still far below the 1935-39 average whereas all other mail pay is higher. Any carrier of mail adhering to the required schedules must operate regardless of daily or seasonal traffic demand and must be compensated therefor. Mail pay is a necessity to the railroads as well as to the airlines, and a considerable number of trains would not be running if the railway mail contracts were eliminated. Nevertheless, there has been a steady decrease in the dependence of the airlines upon Government aid, despite rising costs of doing business. For instance, Chicago & Southern is today earning a fair profit with a mail rate which is 33% less than the rate prevailing in 1941 when it was just breaking even. This 33% decrease in dependence on Government aid has been accomplished despite a 62% increase in operating costs and use of what is really pre-war equipment. "None of the airlines has yet had a chance to demonstrate the possibility of post-war equipment or to profit by advances in all-weather flying," according to Carleton Putnam, President of Chicago & Southern Airlines.

There are signs that the airlines are adjusting their operations to produce profits from presently available traffic. American has cut costs and reduced its break-even point, in terms of passenger load factor, to around 55% for the active traffic months. As a result, earnings for October were around \$800,000, comparing favorably with September, a normally better month. Eastern, earning more this year than last, is an outstanding example of economical operation. TWA has substantially reduced costs by its recently developed system of budget control, and United's consolidation of services, operations, and maintenance is extremely efficient. The development of passenger, express, and cargo traffic is now on a hard-headed basis, and the gaining figures are eloquent testimony to the ability of the industry to attract customers. Fare differentials seem to be on the way to amicable adjustment.

Both the CAB and the airlines are to blame for the uneconomic and overexpanded route structure. Solution of the route problem by mergers, sales of routes, and consolidations of routes has the indicated approval of the CAB. Rumors of mergers have involved Delta, National, Capital, Braniff, and Northeast. United already has purchased one route from Western Airlines and seems a likely buyer of others.

The public demand for adequate air transportation and its role in military power raises the problem of attaining a healthy industry above party lines. The War Department has repeatedly shown its support of the airlines, and soon may give further help by diverting to the airlines part of the transportation of military personnel which hitherto has been the exclusive peacetime privilege of the railroads. Instigated by the President, the RFC report, shortly to be released, may provide a pattern for financing the industry. Incidentally, at least part of the delays in air mail pay decisions, etc., by the CAB may be charged to the unwillingness of the last Congress to confirm Presidential appointees to the CAB, some of whom were eminently qualified.

Unlike most industries, because of losses over recent years which may be carried forward as a tax offset, the airlines are in a measure protected against tax increases.

We maintain active markets in the following airlines securities in which we have a position:

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| AMERICAN OVERSEAS | CONTINENTAL |
| | DELTA |
| CHICAGO & SOUTHERN | MID-CONTINENT |

It is our opinion that the stocks of most of the airline companies offer attractive speculative possibilities for capital gain. These low priced issues should also provide attractive mediums for tax-switch replacements.

Dec. 3, 1948.

The information given above has been derived from sources we consider reliable, but is not to be construed as representations made by us, nor is the above to be regarded as a prospectus offering securities for sale.