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ALK - Q3 2012 Alaska Air Group, Inc. Earnings Conference Call

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OVERVIEW:

Co. reported 3Q12 revenues of nearly $1.3b, GAAP profit of $163.4m and adjusted net income of $150.3m or $2.09 per share.

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PRESENTATION

Operator

Good morning, my name is Jonathan and I will be your conference operator today. At this time, I would like to welcome everyone to the Alaska Air Group third-quarter 2012 earnings conference call. Today's call is being recorded, and will be accessible for future playback at www.alaskaair.com. All lines have been placed on mute to prevent any background noise. After the speaker's remarks, there will be a question-and-answer session, for analysts and journalists.

(Operator Instructions)

I would now like to turn the call over to Alaska Air Group's Managing Director of Investor Relations, Chris Berry.

Chris Berry - *Alaska Air Group Inc - Managing Director of Investor Relations*

Thanks Jonathan, and good morning everybody. Thank you so much for joining us for Alaska Air Group's third-quarter 2012 earnings call. Today our CEO, Brad Tilden; and our CFO, Brandon Pedersen, will share their thoughts on our third-quarter financial results, our operations, and our outlook for the remainder of this year. Several members of our senior management team are also here to help answer your questions.

Our discussion today will include forward-looking statements regarding future expectations which may differ significantly from actual results. Information on risk factors that could affect our business can be found in our SEC filings available on our website. We will refer often to certain non-GAAP financial measures such as adjusted earnings or unit cost excluding fuel. We have provided reconciliation between the most directly comparable GAAP and non-GAAP measures in our earnings release.

This morning, Alaska Air Group reported a third quarter GAAP profit of $163.4 million. Excluding the impact of mark-to-market adjustments related to our fuel hedge portfolio, Air Group reported a record adjusted net income of $150.3 million or $2.09 per share. This result is basically in line with the First Call consensus, and exceeds last year's adjusted net income of $131.1 million or $1.79 per share.

Additional information about our unit cost expectations, capacity plans, future fuel hedge positions, capital expenditures and other items can be found in our investor update, included in our form 8K issued this morning, and available on our website at alaskaair.com. With that I'll turn the call over to Brad.

Brad Tilden - *Alaska Air Group Inc - CEO*

Thanks Chris, and good morning everyone. As Chris said, Alaska Air Group reported an adjusted net profit of $150.3 million this quarter, versus $131.1 million last year. Our revenues increased 6.2% to nearly $1.3 billion on the strength of our low fares and the preference for our products. This is the highest quarterly profit in our history, and it is the fourteenth consecutive quarterly profit that we have reported. Our people are working together better than ever, and to the employees listening today, I want to thank you and your colleagues for everything you did to make these results possible.

Our pretax profit margin was 19.2% this quarter versus 17.7% last year. We believe this margin leads the domestic industry. Seasonally, this is our strongest quarter, our pretax margin for the last 12 months is 11.5%. On a year-to-date basis, we produced $289 million of adjusted net income, and for the last 12 months that figure is $327 million. These strong earnings are driving our return on invested capital which is 12.7% for the last 12 months. And they're also enabling us to improve our balance sheet, reward our shareholders and reinvest in our business.

You have probably seen that on September 26, we announced a $250 million share buyback program. The size is roughly 10% of our current market cap, and is significantly larger than anything we've done before. The program comes on the heels of six programs since 2007, five of which have been fully executed, and which together have amounted to $312 million of share repurchases, and a net reduction in shares outstanding of 13%. Given what many of you have said about our valuation, we think share repurchases have been, and will continue to be, an excellent use of capital that will materially benefit our long-term investors.

We also just announced an order for 50 Boeing 737s, including the new 737 MAX. The new order provides for mainline fleet replacement over the next 10 years. With options, we will have the ability to flex up, if economic conditions warrant, and if we are achieving our ROIC objectives. Over the last several years we have seen the material advantage that comes from having modern, fuel-efficient aircraft that are bought at the right prices, and we're extremely pleased that we secured airplanes to continue this pattern well into the future.

The reason we are able to make commitments like the share buyback and the aircraft order is because of our earnings and our strong balance sheet. Looking at the changes in our balance sheet since 2004, which might be viewed as the peak of the post- 911 industry crisis, our equity has increased from $665 million to $1.4 billion; our debt and lease obligations have declined from $2.3 billion to $1.7 billion; and we've moved from 78% of our capital structure being represented by debt to 54% today.

In those same eight years our revenues have increased from $2.7 billion to over $4.5 billion and we have added 93 737-800s and Q400s to our fleet, 36 of which are owned free and clear.

Turning to our growth, we have several new markets starting in the fourth quarter including San Diego/Orlando, Bellingham/Maui, Portland/Kauai, and Anchorage/Kona. Our growth over the past few years has been successful and has been accretive to earnings. We believe that we can continue to modestly grow our network in a way that is consistent with our return goals, and in a way that gives our customers even more choice when flying Alaska.

On the labor front we recently signed a six-year agreement with our Alaska ramp services and stores agents. And, I'll note that at that point, six years was the longest term for a labor deal that we have ever had. This follows agreements reached in the past couple of years with Alaska technicians and Horizon pilots. Each of these contracts provides for pay raises, productivity improvements, and continued alignment around financial goals throughout our incentive plan.

And just yesterday, Horizon reached a tentative agreement to extend our deal with our pilots again to six years. This deal is mutually beneficial to both the Company and our pilots. And both sides worked hard to craft an agreement that should be funded through productivity gains. Voting will commence in November and will conclude by mid-December.

Elsewhere, our teams are working hard for equitable long-term agreements with flight attendants at both Alaska and Horizon. And we also recently started early discussions with our pilots at Alaska. I am optimistic that we can reach deals that follow our guiding principles and that provide long-term assurance for everyone involved.

I can tell you that every one of us here is focused on running an excellent business that is sustainable, and that provides good results for all of its stakeholders over the long run. I don't need to remind any of you that this is the airline industry, and this sort of long-term success and balanced, consistent execution has evaded most airlines. But we believe we have a solid plan and employees who know what is at stake and who are committed to our success.

One of the things we spent a lot of energy on over the 12 months, is a program we call Flight Path that is attended in small groups by every one of our 13,000 employees. In these full-day sessions, the rest of the leadership team and I listen to our employees and talk with them about the industry, the threats, our plan, and what we need to do together to keep our company thriving. The response from our people has been good, and I believe we have a strongly aligned team that is ready to take advantage of the opportunities and deal with the challenges that come our way.

I want to end with a thank you to all of the employees at Alaska and Horizon for a record summer performance. They were able to handle more customers than ever before, and still managed to run two of the most on-time airlines in the country, with very high customer satisfaction ratings. And when they weren't at work, our folks were involved in 67 community events, demonstrating our commitment to local areas across our route network. My hat is off to all of them for their incredibly hard work, and for their contribution to the success of this company. With that I'll turn the call over to Brandon.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Thanks Brad, and hello, everyone. Air Group's third-quarter adjusted net profit increased by nearly 15%, up from $131 million last year to a record $150 million this year. This represents an after-tax 12.7% return on invested capital for the last 12, months which was up from 12% at September 30th last year. This will almost certainly mark the third year in a row that we have exceeded our 10% after-tax ROIC goals. With a cost of capital estimated to be between 7% and 8%, the investments we are making to the business are creating significant value for our owners.

As recently as 2009, our ROIC was just 6%. The improvement that we have seen over the last three years is not by accident. Our track record of financial performance can be attributed to matching capacity with demand, while expanding our networks, offering low fares, reducing costs by controlling overhead and improving productivity, having industry-leading operational performance, flying single fleets of fuel-efficient aircraft at both airlines. And because our people are working together to deliver an engaging travel experience that keeps her customers coming back.

Because of these and other factors, we have improved profit and we have reduced the amount of capital invested in the business. On a pretax basis, our adjusted profit grew by nearly $33 million to $244 million. The improvement was driven by a $74 million increase in operating revenues and a $14 million improvement in nonoperating expenses. These gains were partially offset by a $33 million increase in adjusted non-fuel operating costs, and a $22 million increase in economic fuel costs.

Pretax margin expanded by 150 basis points to 19.2%, the second quarter in a row of margin improvement. We know that others in our industry focus on operating margin, but we believe looking at pretax margin is important, because it fully considers the effect of aircraft financing decisions, and the amount of leverage in a business.

For example, net non-operating expenses were only $4 million this quarter compared to $17 million in the third quarter of 2009. With much of that improvement coming from lower interest expense, because we have much less debt now than we did three years ago. Passenger revenues were higher on a 6.8% increase in capacity with flat unit revenues.

Mainline PRASM was up 1.2%, which compares favorably to the A4A domestic average of 0.3% for the quarter. Our industry comps are even more favorable when adjusting for our 4% increase in stage length. As we move into the fourth quarter and for the first half of next year, PRASM will again be affected by longer stage lengths.

We would once again characterize the demand environment as stable. Both leisure and business traffic seem to be holding up, despite continuing concerns at the macro level. As we look to the fourth quarter, advanced book load factors are up about 2.5 points for October, 1 point for November, and December is currently down 0.5 point.

Turning to cost, our adjusted non fuel operating expenses increased by 5.3% on the 6.8% increase in capacity. This resulted in a 1.5% decline in our consolidated non fuel CASM, which was consistent with our latest guidance and represents the best unit cost performance we have reported this year. There are a few notable changes in the P&L that I would like to mention.

First, we saw a 12% increase in maintenance cost, largely due to a high number of engine removals at Horizon. Second, contracted services increased by 9% because of handling costs at the new cities we fly to. Third, the food and beverage costs increased by 15% because of the growth of buy onboard sales, as well as investments we're making to improve the cabin experience. And finally, variable incentive pay is up because we're exceeding our PBP plan goals more than we were at this time last year.

Looking to the fourth quarter, we expect consolidated unit costs to decline about 2.5% on a 7.5% increase in capacity, bringing full year CASM ex fuel to be between $0.0845 and $0.085, which will represent a 1% decline. Full-year mainline costs are expected to be down slightly as well to $0.0755 to $0.076.

On the fuel side, economic fuel costs were up 6.5%, basically in line with the 6.3% increase in consumption. Although the economic price per gallon was the same in the third quarter this year as last, the month of September tells a very different story, where the economic price per gallon was higher than the quarterly average by nearly $0.20 at $3.43 a gallon, and in line with prices we're seeing today.

Most investors are aware of our simple, proven hedging program designed to protect our balance sheet from spikes in crude oil. We really view it like it is an insurance policy. You might recall that late last year we began purchasing 10% out of the money options, as a means to reduce our premium cost and self insure a bit more given the strength of our balance sheet.

More recently, we started buying options that are up to 20% out of the money, depending on forward crude prices. We'll see the benefit of this dynamic approach in the form of lower premiums in two to three years, as those hedges mature. There is a table in our investor update that provides current hedge protection levels.

Looking to next year, we are in the middle of the 2013 budget season and our divisional leaders are working diligently to build budgets that leverage capacity growth and to further unit cost reductions. The higher gauge 900ERs that will begin to enter our fleet next month; and customer facing initiatives, such as self-serve bag tagging at the kiosks; and our new booking functionality offered on our mobile site, will help us keep costs in check.

We are, however, facing significant cost pressures in several areas. First, because of the decline in the discount rates, pension expense will increase, perhaps up to $15 million based on what we were seeing today. Medical costs continue to grow, and we are planning to increase IT spend again this year to fund required infrastructure projects, and innovation activities such as the mobile and self-service investments that I just mentioned.

Finally, there is some uncertainty with airport costs, principally at Sea-Tac as we come up on the expiration of our lease there. Although we are not ready to give preliminary 2013 cost guidance just yet, let me assure you that even with these cost pressures, we are mindful of the need to make our costs more competitive and maintain our track record of unit cost reductions.

Turning to capacity, we expect consolidated capacity to grow about 7% to 8% in 2013. The Alaska fleet will grow by a net of seven aircraft over the next 15 months as we take delivery of 13 737-900ERs starting next month, and retire six aircraft in the fourth quarter of 2013. An advantage we have is that the majority of our airplanes are owned versus leased, giving us a great deal of flexibility to adjust our fleet growth. An example of this flexibility is our recent decision to dispose of three additional 737-700 aircraft next year, bringing our planned retirements to the six aircraft I just mentioned compared to three originally planned.

Moving to our balance sheet, we ended the quarter with $1.2 billion in cash and short-term investments. During the first nine months of this year, we have generated $635 million of operating cash flow, compared to $609 million last year. Capital spending was $340 million, resulting in roughly $295 million of free cash flow. We have paid off $240 million of long-term debt, including $102 million of debt prepayments, improving our debt-to-cap ratio to 54%, and taking net balance sheet debt to zero, in fact slightly net cash.

We've also purchased approximately 1.5 million shares of our common stock for $52 million so far this year. Brad mentioned our recent Boeing deal. With this order, our planned capital expenditures for 2012 increased $30 million to $500 million because of the initial predelivery deposits. Firm CapEx in 2013 increased by only $40 million, and is now expected to be $420 million and firm CapEx in 2014 increased by $135 million to $370 million.

We have options that, if exercised, would increase those amounts, but we'd only do so if we felt confident we could meet our return objectives. Our treasury team, which also handles fleet transactions, has been very busy lately and I want to thank them all.

Besides the new repurchase program, the Boeing order, and debt prepayments, they recently completed the extension of one of our two credit lines out to August 2015 with lower fees. We are pleased that the hard work of the last decade is paying off in many ways, including solid financial returns that are exceeding the cost of capital; strong cash flows; and material balance sheet improvement.

We're often asked why improvements in returns, cash flow and our balance sheet are not better reflected in our multiples. Of course, we don't know the answer to that question. But, what I can say is that we are very focused on running the business in a way that benefits are long-term owners, by sustaining a level of performance that meets our return goals. And now, I will turn the call back over to Brad to kick off the Q&A.

Brad Tilden - *Alaska Air Group Inc - CEO*

Thanks Brandon, and Operator, at this time, we're ready for our questions from analysts.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Hunter Keay, Wolfe Trahan

Hunter Keay - *Wolfe Trahan - Analyst*

Thank you very much. Good morning everybody. So I have to ask you about fuel hedging, I apologize. I asked a similar question to UAL about an hour ago, and I'm only asking because you're guided at $3.46 a gallon in the fourth quarter. And, Brandon, I appreciate the color and the movement of buying more out of the money hedges. But the results that you guys that have produced over the last couple of years have been unbelievable, and your balance sheet is pristine, you have unencumbered assets. If there is one airline, again, maybe outside of Southwest that probably has an excuse not to hedge fuel, it is you. And I look at US Airways paying less for fuel than anybody, in something like four of the last eight quarters.

At what point, do you look at that and you say you know what, this is not a fluke, this is a real thing, and even if there is a crisis in policy and framing in the context of you describing the hedge book as insurance, even if there is a crisis, we have the balance sheet and we have the assets to withstand it no matter what happens? So let me ask you a question? At what point did you -- (laughter) Yes, let me ask you a question, the classic sell-side rhetoric, when does US Airways not no-hedge policy stop being a fluke?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

When oil prices run up.

Hunter Keay - *Wolfe Trahan - Analyst*

I hear you, but oil prices just did go up in September in they paid less for fuel than anybody in the quarter.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Hunter, it's Brandon. I get the question and I am going to let Mark Eliasen, our Treasurer answer it. What I will say, is that we have a strategy that we really believe in, it's a long-term strategy. In terms of comparison to other airlines you do get into apples to oranges comparisons because of where people put taxes and in to plane fees. But I think what you're really getting at, is does the strategy make sense? And Mark maybe you have some comments on that?

Mark Eliasen - *Alaska Air Group Inc - Treasurer*

Yes, Hunter, this is Mark Eliasen. I appreciate what you are saying and you make a lot of good points. We are always evaluating our program as you well know. And we may do some things that change. But for now our program has served as very well. Again, I respect what you are saying, but we really don't know where fuel prices are going, and we're not going to try to figure it out, and our program does protect us against spikes.

Hunter Keay - *Wolfe Trahan - Analyst*

Okay.

Brad Tilden - *Alaska Air Group Inc - CEO*

Hunter knows this, but for others, you have gone from basically hedging at the money, co-buying at the money call-offs just a couple years ago to 20% of the money is the practice.

Hunter Keay - *Wolfe Trahan - Analyst*

I appreciate the progress, no doubt about it, so I think it's trending in our directions. There's even an argument be made that if you just actually sold the entire hedge book right now, how much that is actually worth, like Southwest had an opportunity do back in '08. That's another question. But, let me ask you another question relating to bag fees. How do you guys quantify the lower bag fee structure that you have relative to peers? How do you measure the fact that your customers are booking away from other airlines and onto Alaska? How do know that they remember that they paid $5 to $8 less per bag a week after the took the trip? How do you measure that?

Joe Sprague - *Alaska Air Group Inc - VP, Marketing*

Hey Hunter, this is Joe Sprague from Marketing. It's a good question and definitely something that we pay a lot of attention to. We actually are doing more customer research right now, I think, than we have probably ever done in our history, and customer perceptions and behavior around bag fees is definitely something we look at within that research. So that is partly how we know. And just to elaborate a little further on that, our bag fees on a per passenger basis are down this year. I think we're seeing an ongoing change in customer behavior, just generally when it comes to checking bags. But we do feel good about where our bag fees are today. It's not to say we would not ever consider making some adjustments, but right now there's a lot to be said for the simplicity, where we have each of the first three bags set at $20. And we do talk about that with customers and we make sure that they are aware that, that is what the fees are in that there is that simplicity.

We still have the industry's only baggage service guarantee. So, we promote the fact that customers are getting something of direct value in exchange for their bag fees. And it is interesting, the new DOT customer passenger protection regulations that came out with respect to bag fees, we are not sure that they are accomplishing exactly what they were intended. But it has brought a lot of visibility to bag fees that consumers are probably paying more attention to the actual fees, maybe than they have in the past.

Typically the customers are looking at this, and in our case, we have a lot of leisure travelers, as you know, a lot of families traveling with small kids and what not, and in those cases, just a basic example, a family of four traveling together, what they would pay for checking two bags each with Alaska Airlines versus any of the other airlines charging bag fees, could be $80 to $100 or more per family traveling. And we think that they do realize that and that's a meaningful number for them.

Hunter Keay - *Wolfe Trahan - Analyst*

Yes, if they check three bags, they pay more on Southwest than they would on Alaska, by the way. Shame on anyone for checking three bags. All right, well thanks, I appreciate the time.

Brad Tilden - *Alaska Air Group Inc - CEO*

Hunter, this is Brad. I might just want to acknowledge that this is a good question. I think Joe outlined our current thinking. We think the customers notice. And as you look at JD Power results and all that, we do think fees do affect their preference for airlines. The flip side is that we get that we -- and I think Alaska has been a leader in this notion to provide the appropriate returns to investors. We get that it is an important source of revenue that has helped the industry. So I think we have articulated our thinking about this today, but we acknowledge that it is a good question. It is something that you wrestle with every quarter and you think about all the time. Anyway, I just wanted to acknowledge that it is a good question for us to think about.

Hunter Keay - *Wolfe Trahan - Analyst*

No, thank you Brad, I appreciate that color.

Operator

Michael Linenberg, Deutsche Bank

Michael Linenberg - *Deutsche Bank - Analyst*

I just two questions, my first on some of the competitive capacity. I was going to ask you how your Bellingham-Maui is booking up? And then, knowing that there is another competitor starting service in that market? And then I was also wondering how Bellingham to Honolulu is doing

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since you have another competitor starting up in that market? Those are potential negative markets. Then, in some of the positives are some of the capacity cutbacks that we are seeing from competition in your markets. If you can just talk about that.

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

Thanks Michael, this is Andrew. (multiple speakers) Yes, hi. Just on the Bellingham, and I might touch on Hawaii in general because I'm pretty sure I'm going to get the question. But the Bellingham-Maui is seasonal, and it is booking up within our expectations, and the same with the Honolulu. Competitive-wise you are right. I think many of the airlines have been very disciplined, especially as we move into the first quarter of 2013, people are getting more surgical with discipline which is [being] right. One of the things, I think, Mark Dunkerley did an excellent job, a little bit describing the environment of Hawaii this summer, and the seat capacity. And he shared that the Bay Area was up 25%, and Southern California were up 15%. Both Alaska and Hawaiian added seats to those markets, we added over 100% capacity to the Bay Area, San Jose opened to be all four markets.

People talk about the fiscal cliff, I learned the hard way about the Hawaii-California cliff in September. (laughter) Jokes aside, we are learning and we are adjusting, and what I can assure you is that going forward as we learn Hawaii better, we will be making adjustments and refinements. Overall, capacity to Hawaii will continue to grow at about 40% next quarter -- in the fourth quarter. But what I will say is that we have essentially seen all the capacity come back from a low [here] in ATA. We've talked internally about pushing the envelope for Hawaii, while still maintaining a good strong business. I think we're at the corner of the envelope looking down at the stamp right now, but that's to say we will do a little bit more. But I think you'll see the growth subside, and us get smarter about our revenue management and capacity discipline, especially for the seasonality going forward.

Michael Linenberg - *Deutsche Bank - Analyst*

Okay good. And then some of the other markets, like some of the moves by Virgin and Southwest in your markets?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

Yes. So, as is probably obvious to some folks, basically San Francisco network, for lack of a better word, is completely covered now by Virgin. They have launched on top of us in every market. So we are seeing some challenges there. Same with Portland to the Bay Area. San Francisco's up 40% in seats. They're abating going forward, but those are pretty much some of the hotspots that we're seeing. But on the plus side, we are seeing some rationalization of capacity in the Pacific Northwest, especially in some of our feeder markets. So overall, net net, we see competition somewhat, the capacity again, somewhat neutral going into the fourth and the first quarter.

Michael Linenberg - *Deutsche Bank - Analyst*

Okay good. And then just my next question, to Brandon, you talked about higher pension expense. With some of the legislation and I think it was the Transportation Bill back in July, there was a modification to the discount rate. And I'm not sure if you guys benefit from that or not? Because you're -- I believe you are also a beneficiary of the Pension Protection Act of '06 and one may supersede the other? So is there anything in that bill that would benefit you from a pension expense or even a contribution basis?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Mike, it's Brandon. I want to apologize, I will not be able to come up with nearly as humorous of analogy as Andrew has been able to put forth on this one. I think you are confusing funding with GAAP expense. From a GAAP expense perspective we don't get any relief, if you will, from any sort of bill that's floating around in Congress, that's a funding thing. On the GAAP side what I was talking about is movement in the discount rate down to what GAAP says you're supposed to use, which, as I said, would put our pension expense up maybe -- maybe up to $15 million next year. Now, having said that, on the funding side, we actually have no required funding this year or next. And so it really doesn't help us in that regard. We choose to fund, but we have no required funding.

Michael Linenberg - *Deutsche Bank - Analyst*

Okay that's helpful. Thank you.

Operator

Helane Becker, Dahlman Rose

Helane Becker - *Dahlman Rose & Co. - Analyst*

Thanks very much, Operator. Thanks for the question guys and the time. Just on a couple of things. One is with respect to your maintenance costs. I was surprised that they were up 12% in the quarter? I don't think we were thinking it would be that high? Is there something in there?

George Newman - *Alaska Air Group Inc - Controller*

Actually, the maintenance costs are split between our two divisions. Alaska is up probably about $1 million, and original operation is just one that is contributing to it. Most of it is attributable to engine repairs, and I will let Glenn expand further on that.

Glenn Johnson - *Horizon Air Industries, Inc. - President*

Thanks [George], hi Helane this is Glenn. So we are actually in a heavy point in engine maintenance cycle. So this year we had 14 engine events in the quarter versus seven last year. What I would also say is that we had some issues with the engine work that was done by Pratt where the life of some previous repair work that they had done did not meet the expectations that we had. So that affected 5 of that increase of 7 year-over-year. We're expecting to see that same kind of trend through the fourth quarter of this year. And we're also working with Pratt to determine what we can do in terms of mitigating the cost that we were not expecting due to that deficiency in the earlier work.

Helane Becker - *Dahlman Rose & Co. - Analyst*

Oh, okay. So the same level of increase for the fourth quarter?

Glenn Johnson - *Horizon Air Industries, Inc. - President*

I'm expecting to see an increase in the volume, again, in the fourth quarter.

Helane Becker - *Dahlman Rose & Co. - Analyst*

Got you. Okay. And then my other question is just with respect to some of the new service like Portland-Washington, Seattle-San Antonio that you talk about in the press release comments. Did you say how those have booked up and how the success has been on those?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

Hi Helane, it's Andrew. I was just reflecting on this morning that we started 17 new markets in the 12 months ended September. And so what I would say, although we don't state specifics, is that many of these markets are booking up certainly on the volume side, where we would like to see them. Right now they are healthy with sale fares and promotional fares going into the Fall season. So we are going to be watching those closely. In general, normally markets take one to two years. What I will tell you, is that there is nothing that we have seen that gives us cause for major concern on these new markets. So overall we feel pretty good, but we will be working them hard with Joe and his marketing team, to promote those markets going forward.

Helane Becker - *Dahlman Rose & Co. - Analyst*

Okay. And then just my last question. Did you say that you were going to slow the number of new cities that you are opening now going forward? I thought I heard you say something about growth for next year and I missed that, sorry.

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

That's okay, I was probably referring to Hawaii growth and how that is going to become much slower. What I will tell you is, Helane, I think given the aircraft deliveries we're looking at about 7% to 8% growth next year. In the next three weeks, we will be announcing three new markets for 2013 for the mainline business. And from where I sit today, that will be it for new markets in 2013.

Helane Becker - *Dahlman Rose & Co. - Analyst*

Okay thank you.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Helane, this is Brandon, just some more color on that. You might have been referring to the comment I made about slowing down the fleet growth. We have made the decision recently to get rid of three additional 737-700s late in the year, next year. Just because we want to be prudent with the fleet.

Helane Becker - *Dahlman Rose & Co. - Analyst*

Okay. That's very helpful, thank you.

Chris Berry - *Alaska Air Group Inc - Managing Director of Investor Relations*

Thanks.

Operator

John Godyn, Morgan Stanley

John Godyn - *Morgan Stanley - Analyst*

Thanks a lot for taking my question. I just wanted first to ask a question about your thoughts behind the fleet order that you placed? We have seen a number of airlines be very opportunistic about taking advantage of what seems to be almost rock-bottom pricing for some older used aircraft. Relative to those types of opportunities, what made timing of the new aircraft order so attractive?

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Brandon Pedersen - *Alaska Air Group Inc - CFO*

John, I will start and then maybe Mark can jump in here a little bit. Brad made the comment in his section that we have really benefited in a material way from having a fleet of really efficient aircraft, larger-sized aircraft, and for us, that is kind of the mindset that we have. We know that there's great deals out there on used airplanes, but that has not really been successful for us. We prefer to go the other direction.

As we looked at the timing of the fleet order, it is important to know and to keep in mind, that of the 75 firms now that we have on the books, about two-thirds of that book, are largely -- or are replacements, and the other third allow a really modest amount of growth over the next ten years or so. In then the final thing that we were really thinking about was, getting in line for the MAX. The MAX is going to be an awesome airplane. It's going to have 13% better fuel efficiency. And what we didn't want to do is put ourselves at a competitive disadvantage position by not being appropriately timed on that. Mark, you want to add to that?

Mark Eliasen - *Alaska Air Group Inc - Treasurer*

I was just going to add that our partnership with Boeing is very strong and we're happy and pleased that they gave us early slots in the MAX that we can give both the Dash 8 and the Dash 9 early in the cycle. Like Brandon said, we're really impressed with the fuel savings that that will bring us.

Brad Tilden - *Alaska Air Group Inc - CEO*

From the way we look at the economics, it's not like you have to pay something to have new airplanes, as we look at a 15 or 20 year-old airplane and look at those airplanes on a cost-per-block-hour or cost-per-seat basis, they are normally very, very pricey for both maintenance costs and fuel costs. So, we look at the analyses that our teams run, the new airplanes make sense, they pay for themselves. As Brandon said, you have the chance to up-gauge as well and bigger airplanes are working better for us.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Yes, for sure, especially if you think about the 900ERs that come in the next five years or so. The NPV on that decision is great, because what you do is, you take an airplane that has 181 seats, low maintenance cost, great fuel efficiency, and you use it to take out a 400 that has high maintenance costs, bad fuel efficiency, or a 700 that, frankly, an airplane that is just too small for what we want to do that.

John Godyn - *Morgan Stanley - Analyst*

Okay that's helpful. And is it fair to say that just given the size of the order, we're unlikely to see another order for a number of years? Are we taken care of for a while now?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

The way I would answer that is, when we were thinking about the way to structure this order, what we really wanted to do was position the Alaska book to allow for replacement, and potential growth to the extent we saw market opportunities. This is a very, very dynamic business, lots of changes. What I will say is we are really happy with how we have positioned the order now. But I can't say over the long-term whether or not we wouldn't need more airplanes if there were some big change in the industry that caused us to want do more than we are doing. But just to reiterate, for now, and based on what we see, our order book positions Alaska for exactly what we want to do over the long term.

John Godyn - *Morgan Stanley - Analyst*

Okay that's helpful. And can I just ask a question about the advanced book factors that are out there? And, I know that's not the only moving part, and you guys have put up very good PRASM numbers even when we've seen some volatility in advanced book factor. But I couldn't help but notice how much it was revised down, and then the fact that it is negative in December? Which caught my eye. Can you just talk to maybe what is going on there? And in particular, to the extent you have any visibility, how are the holidays booking up?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

John, this is Andrew. As we look forward, and look at October is up 2.5 points, November 1 point, and December down just 0.5 point, that feels right to me personally. We've often seen further out. Especially when you have a lot of holidays in the December period, the holidays are actually, both Christmas and Thanksgiving, are all booking up solidly and normal. The one thing to also remember is our trip length is going to be up 4.3%, also in the fourth quarter. But overall, other than as I shared earlier, recovering a little bit from, I'll just say lack of understanding of the seasonality of Hawaii and California, so we're going to bring that in a little bit more, so I think some of these you will see improved. But overall we feel pretty solid about the fourth quarter.

John Godyn - *Morgan Stanley - Analyst*

Okay, great. Thanks a lot guys.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

John, it's Brandon. I want to come back and just add one more thing about the fleet. What I was really focused on was the mainline fleet, and how our order with Boeing positioned us for the future. The other thing that we are thinking about, and we've talked about this internally with our employees, is we're looking at whether or not it makes sense to have Q400s up in the state of Alaska at some point. This is really, really early in the planning stage, but to the extent that we did something like that, we may see a need for more Q400s.

John Godyn - *Morgan Stanley - Analyst*

Okay, thanks for the clarification.

Operator

Ray Neidl, Maxim Group.

Ray Neidl - *Maxim Group - Analyst*

Yes, with your big cash reserves and strong profitability, have you ever thought about buying another airline and showing them how to do it right? Only kidding.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Kidding, that's good right. (laughter)

Ray Neidl - *Maxim Group - Analyst*

It might be worthwhile for the industry though. No, I just want to clarify a couple of things about what is happening in the great direction in your ROIC, and the debt-to-capitalization ratios? Do you have any new target levels that you are shooting for now in those two areas, as use of your cash?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

In terms of targets, no, we don't really have target levels necessarily. I will take each one of those individually. ROIC, we have long since said that our goal is to generate a 10% return on invested capital over the business cycle. We have had a couple of really strong years, we're at a 12.7% ROIC number on a rolling 12 basis now. And we will certainly finish this year, 2012, with a really strong number. But we are sticking by our long held goal on ROIC.

In terms of debt-to-cap, we are really, really proud of what we have been able to do with the balance sheet over the last couple of years; three, four maybe; and bring debt-to-cap down to 54%. I noted in my remarks that we had prepayments of roughly $100 million so far this year. We would likely not prepay any more debt. We're feeling good about our capital structure. Just if you look at normal maturities next year, we have $160 million-ish of current maturities, and then you take that and you assume there's going to be some increase in equity if we have profitability again next year, which all signs are pointing to us having. That would bring our debt-to-cap down into something that started with a 4.

People would say, is that too low? And, I don't know that there is ever an amount that is too low in this industry. I think the history of this industry has been that there's been way too much debt. We don't necessarily have a target, but boy I'll tell you, as we realistically look at our capital structure, I just don't see it getting down into the 30%s. We would probably want to do something a little bit different, tweak our strategy at tiny bit. But I don't see anything, any issues with having a capital structure that has a debt weighting in the 40%-something range.

Ray Neidl - *Maxim Group - Analyst*

Okay, that's interesting. Also talking about the Q400 that you were mentioning a little while ago, maybe bringing up to Alaska or whatever. That leads to my question with Horizon. At this point, you've got it pretty well fixed the way that you wanted, maybe there is a little bit more work to do there? Now are you looking at other tasks for maybe Horizon, other parts of the country? You did mention Alaska, I assume that Horizon, if you were going to use the Q400 up there, it would be Horizon flying this? Are there any other opportunities, separate from Alaska Airlines, where you can move that type of model or that product?

Brad Tilden - *Alaska Air Group Inc - CEO*

Hi Ray, it's Brad. The first thing, I'm going to ask Glenn to really answer the question, but the first I want to say, to Glenn and to the Horizon employees, that they have done a fantastic job of improving that Company's performance. If you look at the cost structure and the move to the single fleet, lots of back office overhead they pulled out, the branding stuff which I think is really their Alaska-branded airplanes or Alaska with a small Horizon. I think the operation is really, really cleaned up, and if you look at the returns that Company is producing, they've come a long way in a couple of years. And, so I think a huge compliment goes to Glenn and his leadership team, and all the folks at Horizon. And then Glenn, you could talk more about that, and talk about further opportunities for Horizon.

Glenn Johnson - *Horizon Air Industries, Inc. - President*

Sure, thanks Brad. Hey, Ray, this is Glenn. The first thing I would say is, like Brad, I want to extend my thanks and compliments to the whole Horizon team. They are the ones that got this thing turned around. At the same time, I would like to say that we're never done. We've got cost pressures still on, in particular our maintenance costs, that we are working very hard internally and with Bombardier, so those things are still on our sites in terms of improvement.

In terms of future opportunities, as Brandon said, we are starting a very preliminary look at how the Q400 might be a good fit in the state of Alaska. Beyond that, we are a typical CPA carrier now. So we look to our friends at Alaska to determine what opportunities they can best use the Q400s to feed the growing fleet size as well as the growing gauge at Alaska. And I'm personally very enthusiastic about those opportunities, both in the Pacific Northwest network, as Alaska gets bigger airplanes that Brandon was talking about, and then potentially more in the state of California. I would say, you've seen us do some things intra-California. And I personally believe the Q400 is a great airplane for that kind of stage length, just like it will be in the state of Alaska.

Ray Neidl - *Maxim Group - Analyst*

Okay, great and congratulations on the quarter guys.

Operator

Glenn Engel, BofA Merrill Lynch

Glenn Engel - *BofA Merrill Lynch - Analyst*

Good morning or afternoon. Question on the regional operation. If I look at the regional, the RASM there was down about 4%, so why is the regional lagging the mainline so much?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

Firstly, we had very tough comps, unit revenues were up 15% last year in Q3 as we shrunk ASMs, and restructured the fleet. But just bluntly, the major reason for the reduction in unit revenue was competitive capacity in the summer. Southern California had some big increases. California to Portland, we have ten flights a day. And as I said seats were up 60% between Portland and San Francisco. We see those competitive pressures abating a little bit going forward, but that is the main reason for those negative unit revenues.

Glenn Engel - *BofA Merrill Lynch - Analyst*

And can you talk about the transcon opportunities? When you're looking at the 7% growth, what region of the country now starts looking most attractive if Hawaiian is starting to fill out? And how is that opportunity doing?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

So as I mentioned earlier, essentially we have got all of the new markets going in for 2013. We're going to announce three more here shortly which I can't comment on right now. But you're going to see very few new markets going into 2013, outside of the new ones that we have already done recently.

Glenn Engel - *BofA Merrill Lynch - Analyst*

Finally I have noticed that you have been cutting the Alaskan capacity quite a bit? What is driving that?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

I believe we were flat in the third quarter, but historically we had too many seats in the market, to be quite honest. And we have been shoring that up. We look at Alaska week by week by week. So we're just getting the stage right in that market.

Operator

Savi Syth, Raymond James

Savi Syth - *Raymond James - Analyst*

Good morning guys. Just one additional question on Hawaii? How is the ancillary revenue trends in Hawaii?

Joe Sprague - *Alaska Air Group Inc - VP, Marketing*

Yes Savi, this is Joe. Ancillary overall is about flat in absolute dollars year-over-year, down a little bit on a per passenger basis, but the big contributor there is, as we have all ready talked about, is the bag fees. But maybe specific to your question, Hawaii does a couple of things that are really nice for us from an ancillary standpoint. One area where we have really strong performance for the last several months, is with our buy on board food and beverage program. We do especially well with that on our flights to Hawaii. We try and plus up the product a little bit there to make it for a great customer experience, but we get some additional revenue benefit as well. And then, over time, we're trying to build up more of our car and hotel business. It is not where we want it today, but over time we think we can grow that a lot higher. And Hawaii will be a key part of that. And, in fact, as it pertains to our current hotel business, Hawaii actually is up nicely year-over-year.

Savi Syth - *Raymond James - Analyst*

What's the gating factor in building up the hotel and car business?

Joe Sprague - *Alaska Air Group Inc - VP, Marketing*

I'm sorry, Savi. One more time?

Savi Syth - *Raymond James - Analyst*

What's the gating factor, or what will you need to see for that component to start increasing?

Brad Tilden - *Alaska Air Group Inc - CEO*

Savi, it's Brad. I think the first thing I think we would say is, I think there is enormous opportunity in places like Hawaii for us to sell cars and hotels over alaskaair.com. I think it's customer preference and awareness and getting critical mass, and the right relationships with the hotels. So I think it is all of that stuff. And I think, with a lot of these things, if you maybe contrast it with other technology moves, you see little moves to get from 0% to 1% to 2% to 3% to 4%, and then you start moving bigger. And I don't know if we can say right here what the gating factor is, but I would just say that I think over time there is an enormous potential there. Because I think customers trust us. They like the Alaska Airlines experience and I think alaskaair.com is a trusted place to buy airline tickets, and it will also be a good place for cars and hotels.

Savi Syth - *Raymond James - Analyst*

Understood, so great. And just one quick last follow-up question on the booking trends. I think in the past you mentioned, just because of the selling patterns that you should see book load factors narrow as we get closer to the date. Is that still the case? Or has something changed there?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

Savi, this is Andrew. I don't see any major changes in our booking patterns, except as I shared earlier, we've got some work to do on how we've been selling Hawaii, especially California. And you're going to see us make some adjustments there, and maybe sell more a little earlier and build our way up there. But other than that, nothing significant.

Savi Syth - *Raymond James - Analyst*

All right, great. Thanks guys.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Thank you.

Operator

David Fintzen, Barclays

David Fintzen - *Barclays Capital - Analyst*

Hello everyone. Just a couple of quick ones, maybe one for Andrew. You talked about being a little bit more tactical in Hawaii, and I think you mentioned California in terms of seasonal capacity. Are there good counter seasonal markets to shift into? Or should we be thinking in terms of a bit less aircraft utilization?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

I think overall, between the summer in California, and the winter in the Pacific Northwest, we have opportunities to offset each other. We have opportunities to leverage our feed network in the Pacific Northwest to help out California. So I think what you are finding is just a tweaking of our Hawaii network on some of the weakest days. Nothing majorly material.

David Fintzen - *Barclays Capital - Analyst*

Okay, okay, that's helpful. Then on the 7% to 8% ASM growth, that I think Brandon mentioned for next year, how much of that is upgauging? Is that what 2 points, 3 points or is that less?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Hey David, it's Brandon. I don't have that handy. Andrew, do you know off the top of your head?

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Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

The smaller portion of -- (multiple speakers)

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Yes, I don't know the answer to that off the top of my head. What I do know is that we have got 15 900ERs coming in, 6 going out, or excuse me, 13 coming in, 6 going out. So that's basically seven net aircraft. They are bigger and our stage length is going to continue to grow as well. But I don't know the split.

David Fintzen - *Barclays Capital - Analyst*

Okay. All right, appreciate that, thanks.

Operator

Steve O'Hara, Sidoti Company

Steve O'Hara - *Sidoti & Company - Analyst*

Could you just go to the buyback? I mean, in terms of the amount, looking at the consensus estimates that are out there. It looks like you guys are going to generate, you should generate, based on the estimates at least, a lot of free cash flow, based on the CapEx guidance you have so far. Your debt repayments are going down, I think in the next two years. So I mean, it seems like maybe the $250 million seems a little small or maybe the timeframe seems a little long? But can you just talk about that a little bit?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Sure. This is Brandon. I obviously can't and won't comment about first call and guidance, and your assertion that the cash flow is going to be big. What I can tell you is that generating free cash flow is certainly a goal of this Company. And in terms of the $250 million being small, I'd push back a tiny bit and say it is 10% of our market cap. And if you look at the history of what we have done, we have done a series of $50 million authorizations for, I think there's four of them in a row. And what we really wanted to do with $250 million authorization, that is again 10% of our market cap, is demonstrate our confidence in our plan and our cash flow. So I don't know that I have a lot more to add other than that.

Steve O'Hara - *Sidoti & Company - Analyst*

Okay. In terms of what you guys have done to the balance sheet over the last couple of years, it seems like you could easily do a lot more.

Brad Tilden - *Alaska Air Group Inc - CEO*

Steve, it's Brad. I think another thing we might say about it is, is it's something that you continually look at. And Brandon, I can't remember but we -- our grid -- we increased our repurchase rate by 71% a few months ago, I can't remember the month when we did that, at current stock prices. But it's something that, we've just announced this $250 million, now we get into 2013 see how things are looking at. You continue to evaluate it is you go.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Yes, the other thing I would add is, that a balanced approach has worked well for us as I said. We probably won't do any more prepayments necessarily, but we've had a cash balance of roughly $1.1 billion to $1.2 billion for quite a while now. And we have always found good uses for that cash that are investor friendly.

Steve O'Hara - *Sidoti & Company - Analyst*

Okay. And then second, just going to Delta's buy of the Trainer facility, just curious what your opinion of that, as maybe an option for Alaska on a smaller scale? And, is this something that the industry could do on a JV, or a co-op basis to help save on fuel costs?

Mark Eliasen - *Alaska Air Group Inc - Treasurer*

Hi Steve, this is Mark Eliasen. I would just say that we understand why Delta did that, we're all frustrated with fuel costs. As far as our immediate plans, those are creative ideas that you threw out there. But we really don't have anything in the works right now, other than to continue to watch fuel and do our best through our hedging program to protect ourselves from spikes in that fuel cost.

Steve O'Hara - *Sidoti & Company - Analyst*

Okay. And then lastly, what is your ancillary revenue per passenger? And, then, I think Allegiant has done a pretty good job of cutting their credit card fees by moving to debit cards. Is this something you could do for -- in cabin? Would that help at all? Or is that something that you guys have on your radar?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Yes, in terms of ancillaries, our ancillary fee per passenger right now is about $11.80, on a year-to-date basis. In terms of opportunities, I think Joe spent a few minutes earlier talking about the ancillary opportunities that we have. Turning to the debit card thing, we have seen a significant decline in credit card costs because of the Durbin Amendment, and how that has brought credit card costs down. In terms of moving to debit cards in the cabin, we do accept both debit and credit. Joe, do you want to add to that?

Joe Sprague - *Alaska Air Group Inc - VP, Marketing*

No, just that we think we have some opportunities with our overall credit card agreement. It is important financial vehicle for us and we think we can enhance on that even further.

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

This is Andrew. I might pile on here real quick. We talked a lot about ancillary, but, one thing folks should be aware of, is we are doing a lot of work to get more revenue onto our aircraft. For instance, we only have one fare. Say Seattle-San Francisco, we only have one fare. We only have one class to sell, in the first class, of the deepest, of the lowest to the highest of the highest peak, peak season. We're going to add more booking classes. We have a leg-based revenue management system. We're hoping by 2014 to have an O&D system that will significantly improve our revenue performance. We sell upgrades at the gate, we need to get that electronic and more variable. So we have a bunch of things in the works, to Brandon's IT comments, that we think are going to help bring more revenue in as we continue to grow the airline.

Steve O'Hara - *Sidoti & Company - Analyst*

Okay. Thank you very much.

Operator

Duane Pfennigwerth, Evercore Partners

Duane Pfennigwerth - *Evercore Partners - Analyst*

Hey guys, good morning. Just a couple of little items, most of this stuff has been well hashed here. On the CapEx guidance through 2015, appreciate that's a long-term plan, you've got some footnotes around incremental deposits, around options. How should we be thinking about how you think about whether or not you're going to exercise those options and timing? So, for next year, what do you need to see to decide if you're going to pull the trigger on that incremental $100 million of CapEx?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Well, Duane it's Brandon, hi. What we need to see is a plan that gives us confidence that those incremental airplanes are going to be able to meet our return targets.

Duane Pfennigwerth - *Evercore Partners - Analyst*

So when would you know that? Is it middle of next year, and you say yes, we're going to hit 12% ROIC again? So let's do it? Or how do you think about that?

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Yes. It's really more of where these airplanes are going to go, and what we think the MPV looks like. One of the difficulties in this business is you have to put down deposits on airplanes a fairly long period before you actually get the asset. And then it is a 20-year asset that you have to use profitably. And, so there is a great deal of uncertainty obviously. But as we talk about it internally, as we look at the fleet plan, as we look at our list of market opportunities, as we look at the direction we are going on our cost structure, again, it would all come down to whether or not we have a high degree of confidence that we can deploy those aircraft in a way that meets our return targets.

Duane Pfennigwerth - *Evercore Partners - Analyst*

Okay, consistent good answer. What is the value of your unencumbered assets as they stand today? And along those lines, if you had to raise something against them, what do you think you could raise?

Mark Eliasen - *Alaska Air Group Inc - Treasurer*

Hey, Duane, this is Mark. I would say that we have got, as we've mentioned, 40 unencumbered aircraft. It is a little speculative to say how much we could raise. We talk to banks and creditors all the time, and they would be anxious to lend against especially our 737-800s. So it is in the several hundred million dollar range, if we needed to. But right now, we don't see that need.

Duane Pfennigwerth - *Evercore Partners - Analyst*

Okay. Thank you.

Operator

Kevin Crissey, UBS

Kevin Crissey - *UBS - Analyst*

You got it covered by this point. Thanks guys.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Thanks Kevin.

Operator

Hunter Keay, Wolfe Trahan

Hunter Keay - *Wolfe Trahan - Analyst*

Hey, sorry, thanks for taking my follow-up. Andrew, I just want to hear your opinion, on one particular market, and that's San Diego-Orlando. I believe that it is historically a lower yield market on an O&D basis. I'm curious to know, A -- why you think that specific market can work? And B -- more broadly, just tell my what you think about when you decide to open up a market like that, that does not touch Seattle?

Andrew Harrison - *Alaska Air Group Inc - VP, Planning and Revenue Management*

In short, number one, you are very spot on as it relates to a lower yielding market. But I would say is that firstly we look for is we still have a good presence in Southern California. San Diego-Orlando, we have experience with Orlando. It is one of the largest demanded markets that has not got direct service today, largest O&Ds out of San Diego. So there's no head-to-head competition, it has very high demand, and our [aero plan] that we are using there is around utilization. We're actually getting some utilization play there. But to your point, it's a test market, I mean it's outside of our core, and we will be working that hard with the marketing group. But that is a little bit how we think about it.

Hunter Keay - *Wolfe Trahan - Analyst*

Perfect. Thank you.

Brandon Pedersen - *Alaska Air Group Inc - CFO*

Thanks Hunter.

Operator

There are no further questions at this time. We will turn the call over back to Mr. Tilden.

Brad Tilden - *Alaska Air Group Inc - CEO*

All righty, well thanks everybody for joining us today. We're looking forward to chatting with you again next quarter. Thanks.

Operator

Thank you for participating in today's conference call. This call will be available for replay beginning at 12.00 PM Eastern Standard Time today through 11.59 PM Eastern Standard Time on November 25, 2012. The conference ID number for the replay is 94985179. The number to dial for the replay is 1-800-585-8367 or 1-404-537-3406. Also, the call will be accessible for future playback at www.alaskaair.com. Thank you. You may now disconnect.