

BLYTH FUND

Date: 11-14-00
Proposal: AMR Corp. (Holding Company of American Airlines) Watch List Proposal
Ticker: AMR
Current price: 32 3/16 (close 11-11-00)
Analyst: Ian Lopuch and Charles Najda
Profile: AMR Corporation is the holding company of American Airlines, Inc. (American). American is one of the largest scheduled passenger airlines in the world. At the end of 1999, American provided scheduled jet service to more than 169 destinations throughout North America, the Caribbean, Latin America, Europe and the Pacific. American also is one of the largest scheduled airfreight carriers in the world, providing a full range of freight and mail services to shippers throughout its system. In addition, AMR Eagle Holding Corporation (AMR Eagle), a wholly owned subsidiary of AMR, owns three regional airlines that operate as American Eagle: American Eagle Airlines, Inc., Executive Airlines, Inc., and Business Express Airlines, Inc. The American Eagle carriers provide connecting service from seven of American's high-traffic cities to smaller markets throughout the United States, Canada, the Bahamas and the Caribbean. (From *Yahoo! Finance*)

The Numbers:

Shares Outstanding:	150.7 bln	Market Cap:	\$4.85 bln
P/E (00)	5.46	PEG Ratio (5 years)	.557
EPS Growth (00)	6.35%	EPS Growth - 5 years	9.8%
P/book	.68	P/sales	.27
Operating Margins	8.1%	Net Margins	4.9%
Cash:	\$2.33 bln	Debt/Equity	0.84
EPS	\$5.92	EPS (01)	\$5.36
ROE	14.00%	ROA	3.79%
Dividend	N/A	Dividend Yield	N/A

Comparisons:	<ul style="list-style-type: none"> • American has an advantage over DAL (Delta Airlines) in a number of critical areas. These include: • American's net cash is 2.1bln, while Delta's is a lower 1.4bln. • American's total property and equipment assets total 18,047mln, while DAL's total 14,017mln. • American's long term debt stands at 3.7bln, while DAL's is higher at over 4.4bln. • Total current assets are again relatively higher for AMR. AMR 5,352mln. DAL 3,939mln. • Load factors for both airlines are about 70%; however, this figure does not take into account the possible effects of the More Room Through Coach program, which may buoy the load factor up. Delta has not announced a similar plan. • American's route structure is more diversified than Delta's. American has a strong presence throughout the US, while Delta is mainly concentrated on the east coast, and has a weak presence on the west coast. In fact, Delta barely participates in such lucrative routes as JFK to LAX, and DAL cannot fly to London's Heathrow Airport, which is one of American's top ten routes for revenue.
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Recent News:

- In 1981, American introduced the AADVANTAGE travel awards program. They were the first airline to create such a program, which builds customer loyalty. AMR also pioneered the creation of Supersaver last minute fares, which allow the airline to fill seats that otherwise would go empty.
- Six major oil companies have teamed up with some of the world's largest airlines to launch an online venture designed to help carriers better manage their jet fuel supplies. Companies backing the Jet-A.com project are Exxon Mobil, Shell, BP Amoco, Texaco. Airlines will reduce costs through the better management of their fuel needs, by cutting

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corporate red tape and making more efficient use of inventory.

- American's new b-to-b initiative to cut costs, the newly robust, Aircraft.com will target the spare parts and service needs of commercial airlines. Other airlines including British Airways, Air France, and Continental are also participating in the venture.
- Earlier this year, American Airlines and America Online joined forces to create a revolutionary new program - AOL AAdvantage Rewards. When people join AOL AAdvantage Rewards, they earn miles doing every day things, like shopping online for popular brand name products and services. The program with AOL expands the usefulness of AAdvantage miles, while also allowing people to earn "miles" while shopping through AOL merchants. AOL/AAdvantage allows AMR to build even more loyal customers. Likewise American earns money on the miles that its partners give to AAdvantage members.
- Moderate expansion of route system with potentially profitable routes such as: American Airlines will begin flying nonstop daily between San Jose International Airport and both Taipei, Taiwan, and Paris, France, on April 1, 2001. American is favored to win the right to serve China, from Chicago. Delta and United are competing for that same right.
- American Airlines' oneworld alliance is made up of eight members. Although the alliance is smaller than its rival staralliance, a recent survey in Conde Nast Traveler magazine found that 2 of the top four airlines in the world, Qantas and Cathay Pacific, belong to the oneworld alliance.
- American had been well hedged against rising fuel prices in 2000, offsetting nearly \$500 million in costs with financial risk instruments but still had spent \$350 million more on fuel than had been expected at the start of the year. This compares to a competitor such as USAirways, which did not hedge at all and reported losses in the most recent quarter.
- A federal appeals court recently rejected an effort by the union representing American Airline's 10,500 pilots to postpone paying a potentially bankrupting \$45.5 million fine to the airline. This gives the airline a bargaining chip in next year's contract talks with the pilots.
- American is streamlining its fleet with Boeing aircraft. These aircraft are purchased at substantial discounts, because American signed an agreement making Boeing its exclusive supplier for the next 20 years, in return for lower aircraft prices. American is also investing in large infrastructure projects such as a new 1.6 bln dollar terminal at JFK. A 300 mln dollar expansion of its terminal in Boston, a new 1 bln terminal in Miami, as well as new satellite commuter terminals in DFW and ORD.
- American completed the retrofitting of its MRC (more room throughout coach) program in its domestic aircraft. This program increases coach seat pitch about 3-4 inches. The program reduces the overall number of seats American has to sell, and attracts business travelers who will not pay first class fares, but want the best product for a coach fare. Likewise, American has announced an increase in international business class seat pitch from 50" to 60" in order to attract more full fare passengers. American also introduced the Flagship Suite, a first class seat that resembles a private pod. This product is of the same caliber as seats offered by Cathay Pacific, British Airways, and Singapore Airlines. In general, most major airlines are investing in upgraded premium classes in order to attract full fare customers.

Financial Analysis (10-Q From Quarter Ending 9/30/00):

- AMR is a cash-generating machine, much like Philip Morris (MO). Cash is up 100% when comparing the quarter ending September 30, 2000 to the same quarter in 1999.
- AMR is managing its liabilities well. Current liabilities are up 24.15% and long term debt is down 6.4%.
- Top line and bottom line growth is great for such an established company. Revenues are up 11.5% and earnings are up 12.19%. Earnings would be up even more if oil prices were lower. AMR paid 42% more on aircraft fuel.
- Net margins are up fractionally, coming in at 5.96% (versus 5.94%). This shows the strength of management, given the high fuel prices.
- Unfortunately receivables are up 31%, outpacing revenue growth. This is the only problem on an otherwise stellar balance sheet.

Financial

- The book value of AMR is \$47.07 and the price / book ratio is .68.

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Analysis (General):

- According to Yahoo Finance! AMR has \$15.49 per share in cash (2.33 bln dollars). Discounting cash, AMR is trading at a P/E of 3.06. These valuations are ridiculous even if AMR runs into problems and has trouble meeting analyst expectations of 9.8% earnings growth for the next 5 years.
- AMR is trading at 2.5 times operational cash flow of 1.74 bln.

Technical:

- AMR's chart is not particularly exciting. After dropping drastically, AMR has been consolidating for the last six or so months in a tight trading range. When stocks trade sideways, as AMR is, it is usually undergoing a phase of either institutional accumulation or distribution.
- The chart below includes the 20-day Bollinger bands. Bollinger bands basically form an envelope (or channel) around the activity of a stock. They are useful to tell when a stock is at the top or bottom of its trading range.

