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ALK - Q1 2020 Alaska Air Group Inc Earnings Call

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OVERVIEW:

Co. reported 1Q20 GAAP net loss of $232m.

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PRESENTATION

Operator

Good morning. My name is Chris, and I'll be your conference operator today. At this time, I'd like to welcome everyone to the Alaska Air Group first quarter earnings release conference call. Today's call is being recorded and will be accessible for future playback at alaskaair.com. (Operator Instructions)

I'd now like to turn the call over to Alaska Air Group's Director of Investor Relations, and Emily Halverson.

Emily Halverson - *Alaska Air Group, Inc. - IR*

Thank you, Chris. Good morning. And thank you for joining us for our first quarter 2020 earnings call. This morning, Alaska Air Group reported a first quarter GAAP net loss of $232 million. Excluding onetime costs and mark-to-market adjustments, Air Group reported an adjusted net loss of $102 million. Onetime costs incurred this quarter include approximately $160 million of asset impairment charges that were triggered as a result of the significant decline in demand for air travel and market conditions. These impairments included approximately $145 million of aircraft and aircraft-related parts as well as approximately $15 million of financial and intangible assets.

On today's call, Brad, Ben and Shane will be discussing the impact of COVID-19 on our business and sharing details about our response to the economic and health crisis. Several other members of our management team are also on the line to answer your questions during the Q&A portion of the call.

As a reminder, our comments today will include forward-looking statements regarding future performance, which may differ materially from our actual results. Information on risk factors that could affect our business, which were updated today, can be found in our SEC filings.

On today's call, we will refer to certain non-GAAP financial measures, such as adjusted earnings and unit costs, excluding fuel. And as usual, we've provided a reconciliation between the most directly comparable GAAP and non-GAAP measures in today's earnings release.

And now I'll turn the call over to Brad for his opening remarks.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Thanks, Emily. And good morning, everybody. Thanks to all of you for joining us for our first quarter call. This call comes at an unprecedented time for our industry. Many people have lost loved ones or at distance from their family and friends, and others have lost confidence in the future because of concerns about the economy or their own financial situation. People are justifiably fearful about the future.

In the face of one of the greatest challenges in the history of aviation, our people at Alaska and Horizon are doing extraordinary work to respond to these circumstances. Our pilots, flight attendants, customer service agents, ramp service agents, mechanics and others continue to come to work and be their best in an extremely difficult environment. They're caring for our guests with kindness, while delivering safe and remarkable service to those who are traveling. All of us on the leadership team are grateful for their dedication.

I also want to thank the very dedicated leaders at Alaska and Horizon, including folks around this table who are wholly focused on responding to these crises and preparing Alaska to sustain itself and grow stronger in a highly uncertain future.

Their commitment and their love for what they do and for this company give us all confidence that Alaska is going to come through this crisis stronger and better.

We would typically use our earnings call to discuss our performance for the quarter, to provide an update on our strategic efforts and to share guidance for the remainder of the year. But that does not make sense today. Instead, we'll be sharing with you what we know at this juncture, how we're thinking about future scenarios given the macro uncertainty and how we plan to bridge what is essentially an economic closure across our country to a future where Alaska is stronger and better and fully prosperous.

As Emily mentioned, we incurred an adjusted pretax loss of $102 million for the quarter. This was the result of a 14% decline in passenger revenue driven by the near complete loss in demand that we began to see in early March. This is our first quarterly loss in over a decade, and it is sobering to report. There is no doubt that our second quarter loss will be much higher. And there is very high uncertainty about the third and fourth quarters.

Safety has always been our top priority, and this crisis has caused us to review and improve our procedures. We've implemented several changes, including expanding and enhancing the cleaning of our aircraft, including the use of high-grade registered disinfectants and electrostatic sanitizing spray. We're requiring our flight attendants and CSAs to use masks. We're limiting load factors and seat availability. We've modified boarding procedures to encourage self-scanning of boarding passes and to encourage slower boarding to prevent crowding. And we've suspended or reduced most in-flight services.

Additionally, beginning next week, masks will be mandatory for our guests. These changes can be difficult at first for both guests and crews, but our teams have handled them with professionalism. We anticipate further changes to our policies and procedures in the future, and we will continue to be industry leaders with health and safety standards.

As we think about our industry and air travel more broadly, we're highly confident that people in the future will want to physically connect with one another and see other places. We're also very confident that they will value an airline that offers them safety, low fares and the type of personal hospitality you would see from a family member.

As you know, we have taken and are continuing to take aggressive action to preserve our financial position. Shane will detail all of this, but we've acted swiftly to build on our already strong fortress balance sheet and to make some very difficult decisions to manage our cash burn rate. We've gone from a monthly burn rate of $400 million 1 month ago to approximately $260 million today, and our commitment is to get to $200 million by June and to breakeven by year-end.

Just 2 weeks ago, we received $992 million in payroll support from the federal government. The program was the result of decisive bipartisan action on the part of our federal leaders, and we very much appreciate their efforts to provide direct support to airline employees. The passage of this bill demonstrates one of the bright spots that exist during this crisis, the opportunity for all sides to come together and work toward a common good. We are thankful for the efforts of the President and his administration, Congress, Secretaries Mnuchin and Chao and all -- and many others for their efforts in providing this vital support to help our industry and our economy weather this downturn.

While our full attention is focused on the situation at hand, we've always operated with our eyes on the horizon, and that focus continues today. We have been historically and are today financially conservative. We're proud to be the only pre- deregulation to not file for bankruptcy. Throughout history, our people have worked our way through challenge after challenge. And we've gained new skills and capabilities as we've gone along, and we've come away from these challenges better and stronger. We have every belief that will be the case this time, and we are fully focused on this outcome.

With that, I'll pass it to Ben.

Benito Minicucci - *Alaska Air Group, Inc. - President of Alaska Airlines Inc. & Director*

Thanks, Brad, and good morning, everyone. I want to begin by sharing a few of the facts we know. Our home base, Seattle, was among the first places in the country to be hit by the pandemic. Washington (inaudible) limit gatherings and closed schools.

California was the first to issue stay-at-home mandates. These communities and their leaders have shown great courage in handling the situation. While necessary, these actions had a significant negative impact on our business. With many of our largest hubs in these two states, we began to see signs of demand deterioration in late February. On March 11, we saw cancellations overwhelm gross new bookings for the first time ever. We have since experienced 56 days of net negative bookings.

The largest wave of cancellations appears to be behind us. However, daily cancellations do continue to modestly exceed gross new bookings. We are attentive to gradual improvements in our daily passenger counts, which remain 90% below normal levels. We are showing very modest week-over-week improvement.

In March, we reduced our capacity 12% versus prior year, primarily through closing cancellations and consolidating frequencies. Soon after, we cut April and May capacity by 80% and expect to cut June's flying similarly as well. The top near-term challenge we face is to reduce our current cash burn rate of $260 million to $200 million per month by June and to achieve our commitment for cash breakeven by year-end.

To do this, we will lean heavily into our competitive advantages. Because it is impossible to forecast a shape of the recovery with any certainty, we are planning potential courses of action for multiple recovery scenarios. There are several factors about our business model and our competitive advantage that I believe will benefit us in any recovery scenario.

First, we have built our business to have structurally lower costs than our competitors. Alaska has a history of managing a low overhead, high productivity operation, and this remains a guiding principle going forward.

Our CASMex fuel is 20% lower than legacy airlines, which enables us to compete more effectively with low fares. More than ever, we see a future where low fares and low costs matter, and we have resolved to strengthen our cost advantage as much as possible.

As Brad mentioned, we've received payroll support program funds from the federal government. These funds cover approximately 70% of our original budgeted payroll through September 30 and allow us to keep employees on the payroll, while the airline is operating at significantly reduced capacity. This relief affords us more time to be thoughtful about restructuring decisions and how we will shed costs. It also presents opportunities to redeploy management employees and crew whose work has slowed to utilize their time with purpose where possible. For example, many management employees have been redeployed to other divisions or to clean aircraft and on the crew side, we're taking advantage of this shortfall in demand to retrain Airbus pilots as Boeing pilots to avoid both opportunity costs and economic costs. Shane is going to share more detail on our cost-saving opportunities that we are planning for.

Second, we have strong hubs with some of the best customer loyalty in the industry. Even with passenger counts significantly down, the loyalty of our guests shines through. We welcome words of appreciation in person and over social media from travelers who have the need to travel, including medical personnel, loved ones going to meet and care for family members and employees or business owners whose work requires them to travel for essential reasons.

In fact, our guest-facing communications and positive sentiment across social media was recognized last week by the Airline Passenger Experience Association as the best in the U.S. airline industry.

And third, our network orientation and our fleet are well suited for the recovery ahead. It is likely that recovery will first bias towards domestic travel. Our limited international exposure and our fleet of narrow-body aircraft will be assets in this scenario. As you know, we began a full fleet analysis last year. These crisis have made it imperative that we take a fresh look at our long-term plans to ensure we select the best, most efficient aircraft for our future state. This will be another important aspect of our cost restructuring.

Finally, our employees are aligned in their commitment for the challenge ahead. Alaska has experience of being an underdog, and we are battle tested. Today, we face new challenges, and the gravity of those challenges is understood by our people. Each day of this crisis, I'm struck by the dedication I see throughout the organization. Our crews have worked together with leadership and experts to evolve our guest-facing health and safety policies. Our call center employees have supported thousands of guests with challenging transactions and issues. Our finance, legal, communications and government affairs teams have rallied for many long work weeks as we navigate changing business conditions. Thousands of employees across the company showed their support through letter writing to the U.S. treasury to help obtain industry support.

While the prospect of a smaller industry and a potentially smaller company is not something we would have wanted, we are realistic about the challenges ahead. We have more fight in us, and we will do what it takes to make Alaska emerge stronger.

As always, we're focused intently on controlling what we can control. Outside of our control but also important is understanding what will influence the demand recovery path. To name a few factors, travel restrictions and stay-at-home orders that are likely to be lifted at different times, unemployment and broader economic trends and evolving public sentiment about whether to travel and for what reasons will all be considerations. Our role is to have robust plans for any scenario we may encounter to communicate honestly with our people about those plans, and to execute against them to the best of our ability. We commit to doing that over the next several months, as things become clearer and to emerge from this crisis a stronger and better company. That means getting to 0 cash burn by December and setting up the conditions to control our destiny.

And with that, I'm going to pass it over to Shane.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Thanks, Ben, and good morning to everyone joining us. My comments will focus on why we are confident Alaska will bridge this period of no demand and continue forward as one of the industry's strongest performers.

An appropriate place to start that discussion is cash on hand and our remaining capacity to create additional liquidity should we need it. We began 2020 with $1.5 billion in cash and marketable securities, to which we added $400 million from existing lines of credit, $425 million from a 364-day term loan. And subsequent to the end of the quarter, we added an additional $50 million in secured financing. In April, we received $992 million for payroll support via the CARES Act. Together, that totals $3.35 billion. Today, we have approximately $2.9 billion of cash and marketable securities on hand, meaning we've burned about $467 million of cash from the beginning of the year.

Our cash burn rate is a critical figure that we are managing aggressively. And today, it is about $260 million per month. With demand at essentially 0, our $2.9 billion at this rate of burn would sustain us for 11.2 months. However, we intend to increase how long our cash will last. Our commitment, as Brad and Ben have both previously indicated, and as I will reiterate now, is to achieve $200 million cash burn by June and to reach cash breakeven by the end of the year. We know this will require significant work and hard decisions on cost removal and restructuring.

And while we are very focused on managing our cash burn, we also have multiple channels we can tap to add further liquidity to our current $2.9 billion, including more than $2 billion of high-quality unencumbered aircraft. Banks and investors we've spoken to have indicated interest in lending against these assets with reasonable terms. We have an additional $500 million of real estate and slot assets that we can borrow against. We have a very valuable loyalty program that could be tapped for liquidity, we have available to us as much as $1.128 billion in CARES Act loans. And although in the category of having no current plans to tap, we believe our equity would be a very high interest to investors as well.

This $7 billion to $8 billion of collateral and $1.1 billion of CARES Act loans, we believe represents well in excess of $4 billion of incremental liquidity potential. Taken together, our on-hand liquidity, our access to additional financing and our aggressive goals to reach cash breakeven results by the end of the year will ensure that we bridge this downturn and are prepared to rebuild our success during a recovery. The increased debt load that will result as we navigate this crisis is obviously not our ideal long-term setup. While we are first and foremost focused on ensuring the survival of Alaska, when the industry stabilizes, we will return our focus to repairing the balance sheet, just as we did post Virgin acquisition.

To discuss cash reduction and preservation efforts, I would share the following. We have rightsized our schedule commensurate with demand and have seen a very strong linear reduction in nonwage variable costs. We have reduced discretionary and overhead spend by nearly $50 million per month. We have deferred nearly $600 million of capital expenditures for 2020 bringing our planned CapEx to under $175 million, which includes no additional aircraft capital spending. We have suspended share repurchases and dividends, and we have reduced executive pay, reduced management hours by 10% and have over 5,000 employees who have opted to take unpaid leaves for, at least, the next 60 days. And we have also implemented extended payment terms and sought and in many cases achieved, payment relief from suppliers.

I'd like to elaborate on a couple of these items. First, as mentioned, we've dramatically cut capacity in Q2 and anticipate operating a reduced schedule for the balance of the year. As a rule of thumb, I view our nonwage variable costs to represent 50% of our cost structure. Most of our operational contracts do not have minimums and so scale almost perfectly, although I acknowledge under the current climate, this has been extraordinarily difficult on our suppliers.

Wage costs are our largest cost pool and tend to be less variable. Our frontline work groups all have minimums within their contract that ensure they receive a certain amount of pay. We have adjusted down to those minimums, which reduces payroll by about 10%. And in partnership with our union leaders, we have also entered into other agreements that allow and incentivize employees to take leaves, which as mentioned, represent over 5,000 people currently.

With these efforts, I expect payroll costs will be down 30% from plan for, at least, the next 60 days, and we expect our CARES Act payroll support funds to cover the vast majority of our payroll through September. To date, none of these changes are structural, and there remains significant work to be done to achieve any longer-term changes to wage costs.

Turning to aircraft, given the temporary grounding of a significant portion of our fleet, and our initial assumptions about demand over the next several quarters, we have determined that at least 12 mainline aircraft would be permanently parked, including 10 A319s that were among the smallest and least efficient aircraft we have and 2 leased A320s that had not yet been reconfigured to our new interior. The rest of the parked aircraft are being stored and maintained so they can reenter service. We will make decisions about when and how many of them do return to service in the future.

So we are working all the cost levers hard to drive towards our commitment of 0 cash burn by the end of the year. And to clarify, our cash burn rate does include the impact of refunds and cancellations and excludes the impact of CARES Act payroll support funding and additional financing. It does factor in all of the self-help I've just described.

Reaching our goal of $200 million cash burn by June and cash breakeven by the end of the year will require more work on our cost structure. But I believe we will get there. Our people attack tough goals like this with intensity and commitment. And I believe that all 23,000 of our people understand that if we can achieve a breakeven cash burn rate, our destiny is back squarely in our control, which means we are also in control of building towards a better future again.

And with that, let's go to your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question is from Savi Syth from Raymond James.

Savanthi Nipunika Syth - *Raymond James & Associates, Inc., Research Division - Airlines Analyst*

Just on the -- kind of getting to cash burn 0, breakeven by the end of the year. I wonder if you could elaborate a little bit more on that. And is that -- how much of that do you expect to come from the revenue side? And then on -- depending, I'm guessing on the kind of demand recovery, what kind of decisions, and how quickly could you scale to that?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. Savi, it's Shane. The way I want to talk about the cash breakeven is it's an objective that we have to get to. So we look at the recoveries, having the costs through 0, we've got to get there. We've put a marker out in front of us 8 months from today. We actually don't know the exact path to get there. We don't know exactly what revenue is going to be. But what we're thinking is, regardless of the revenue environment, we've got to make the decisions necessary to take the actions to get to cash breakeven. Obviously, we'll talk to you a lot more as we get through some of that decision-making process and have better clarity about what Q4 looks like. But we're not relying on any particular revenue outcome to get there.

On the scale question, I just want to make sure I understand. Are you thinking about if demand is better than we're thinking? Or I just want to make sure I understand the question.

Savanthi Nipunika Syth - *Raymond James & Associates, Inc., Research Division - Airlines Analyst*

Yes. I mean clearly, unless we have a V-shaped recovery, you have a lot of kind of difficult decisions in front of you. And just how quickly could you scale the operation to kind of a newer demand level? Is there kind of a reality on like how quickly you can scale that? Just, I'm guessing some of the biggest fixed costs, and how do you get it to kind of a new level of demand if we don't see a V-shape recovery?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes, yes. If you're talking about like sort of scaling down, I mean, I think we don't know exactly how long that's going to take. I think there's a part of our business, like I mentioned, 50% of which is variable, it just moves with the operation. We've been really happy to see those costs almost perfectly linear with capacity. The other 50% is payroll and a lot of just overhead and fixed costs. The overhead and fixed costs that we can make decisions on, those are tough, but we can act on that quickly. I think it's really when you talk about the size of the company and how many people we have, that's something that takes more time. That's something that we've got to go talk with our labor leaders about and sort of work through over the next several months. But the most important thing is we've got to know what size of the company we're aiming for. And we just don't know that as we sit here today.

Savanthi Nipunika Syth - *Raymond James & Associates, Inc., Research Division - Airlines Analyst*

That makes sense. And if I may just ask a clarifying question on the costs. Really helpful to have the kind of the cash burn side, but on the kind of the P&L standpoint, what do you expect costs to be in 2Q generally?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. We -- like unit cost, I don't think we're providing any guidance to, I think?

Savanthi Nipunika Syth - *Raymond James & Associates, Inc., Research Division - Airlines Analyst*

Just overall.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. Yes. I think, Savi, the 50% that's variable linear, I think you can calculate very closely just given our capacity. And then we're not really quantifying the other side of the business or revenue at this point. If we do, we'll be clear about that in an 8-K or something to make sure you guys know that.

Operator

The next question is from Mike Linenberg with Deutsche Bank.

Michael John Linenberg - *Deutsche Bank AG, Research Division - MD and Senior Company Research Analyst*

Just I guess 2 here. On the payroll support program, the $992 million, I believe you called out that you could potentially get something for McGee. I know that's small, but every dollar matters. And the $992 million that you got, it seemed like you got it in one installment. I know other carriers are getting it in two or maybe more installments. I'm curious why you were able to get all of it, and then I have a second question.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

This is Shane. The treasury gave us the option of taking it in a couple of installments or all at once. We looked at it closely. We didn't think there was a real difference. There's no -- it's not a different amount of money. There's no difference in terms, and so we decided to take it all at once. I think a couple of other carriers may have, and some have taken it in installments. But it was just a choice given to us, so we took it all at once.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

McGee.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Oh yes, sorry. McGee is in process, I believe from the payroll support grants there were well over 200, 250 applications. The focus was sort of the largest carriers to begin with. They're in that process. I think we expect to hear back from treasury sometime this week. I think their sort of qualified amount was around $40 million. That would be if they got 100% of what they applied for, nobody is getting 100%. So it's hard to know exactly what they'll get, but they are in line to still receive funding from the payroll support portion of the grant.

Michael John Linenberg - *Deutsche Bank AG, Research Division - MD and Senior Company Research Analyst*

Okay, great. And then just my second, just reading between the lines, training Airbus pilots to fly Boeing jets and putting Airbus planes on the ground. I guess it's probably safe to assume that the fleet decision is being made in real time. I guess the one issue is the A321neos. Did you have any additional on order that were expected to come in? Or have you taken all of the newer Airbuses? Just thoughts on that and maybe any additional color you can talk about the fleet decision because, again, it looks like it's being made in real time.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Mike, I might start and go to Ben. That was a good 3 question in 1 question. No more neo, no more A321s on order. We've taken the 10.

Michael John Linenberg - *Deutsche Bank AG, Research Division - MD and Senior Company Research Analyst*

Okay.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

And so that's the answer to that. I would -- and Ben can talk more about our thinking about fleet and sort of what we're doing. When -- and I just want to connect a couple of things. We are training 240 pilots off of the Airbus on to the Boeing. That is really a by-product of the fact that we determine these 12 aircraft aren't going to fly again. And if we do decide to backfill that capacity at some point, we expect that, that capacity would be backfilled by Boeings that we have on order today.

And so it just -- it was prudent to do that. We've got very limited flying. We have a full payroll. We have pilots that we have the opportunity to get into the training school house without costing us growth, so there's no opportunity cost. And it's not totally free, but it's close to free training at this point. So it just made a lot of sense to marry those two decisions up to park those 12 aircraft and train the pilots over. But Ben may have more to say on our future of fleet.

Benito Minicucci - *Alaska Air Group, Inc. - President of Alaska Airlines Inc. & Director*

Mike, as you can imagine, we're doing a lot of modeling with different fleet structures. And just to give you a sense of what's guiding us is, look, we have the 0 cash burn rate goal that we're aiming for. And also, we're going to restructure the company to have low cost. A dual fleet does have a higher cost for us. So that is a factor we're going to consider. The Airbus 321 is a great airplane. We like it a lot. But we're going to bring all these factors together. And we're going to look forward to the future. We're going to look how we're going to reconfigure this company for the best success. So a lot of things in play, and as the months play out, we'll get more clear on what our direction is.

Operator

The next question is from Joseph DeNardi with Stifel.

Joseph William DeNardi - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Airline Analyst*

Shane, just on the cash burn, like I'm assuming that the $200 million by June assumes kind of a similar revenue environment to what you're seeing now. What can you get that to by the end of the year if this revenue environment continues just so we can kind of think about things apples to apples?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. Thanks, Joe. It does essentially assume demand is similar to what we're seeing right now. Look, I'm not going to hypothesize about exactly where we would be if there was literally 0 demand at the end of the year. We are very focused on getting the cash breakeven. That's what we're sort of putting in motion. That's where we're forcing ourselves to look at different scenarios and make decisions. And it's just -- there's the range of potential outcomes in Q4 so wide, it doesn't make a lot of sense to hypothesize on where we'll end up, especially on the revenue side.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

And Joe, it's Brad. I might jump in. That's -- the way we got to that is that's what we believe is required for us to be able to control our future. It's like all of these airlines, we've got decent liquidity. Shane detailed, we've got good plans to raise liquidity, but that gets us to a finite number. And then you have a burn rate. And at some point, you do have to take control of your future if you want to control your future. And so that's our mentality, is we've got to -- if we can get to 0, if we can commit to a 0 cash burn rate by December, we're in control of our future in 2021 and beyond. And if there are opportunities that present themselves on the landscape, we can take advantage of those opportunities. We can mitigate the downside. So it's going to be painful. We believe it's going to be painful, but I -- there's just a lot of belief in the goodness of making a commitment like that and the good things that will come.

Another point I was going to -- you guys are asking good questions, Savi and Mike as well. But we do believe Alaska is configured to be a bit more agile than the average airline, if you look at us right now. Our fleet is all -- it's basically, on the Alaska side is all narrow bodies. As Mike pointed out, we're moving now 20 -- 19 or 20 Airbus airplanes to Boeing. So I think we're going to be a little bit more able to scale up or scale down depending on the demand that we see than some of our competitors. I think we also like the fact that we -- our business is more oriented towards leisure travelers, and our business is more oriented towards domestic travelers and narrow-body travelers.

So all of that stuff sort of informs us. We believe that if we can sort of sit here and say, oh, we don't know, blah, blah, blah. But we think that if we sort of define the future that we need to have, we think we can get there, and we think if we get there, we'll be in control, less bad -- fewer bad things will happen to our people, and we'll be in a better position to take advantage of opportunities that we see. So that's the more thinking around the goal.

Joseph William DeNardi - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Airline Analyst*

That's very helpful, Brad. Shane, you mentioned $2 billion of unencumbered aircraft, $500 million of real estate and then $7 billion to $8 billion of collateral. So does that imply that the loyalty program is kind of $5 billion-ish? Did that surprise you? And what do you think the kind of the -- is it safe to assume that, that would be the last line of liquidity that you'll look to access?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. Thanks, Joe. I think -- yes, I think the math is probably fair because you sort of added up the only asset I didn't put a price tag on. So fair enough. No, I think it's that we've known it's a valuable program for a long time. In terms of what our order of preference of raising money is, honestly, we're not in a position to share what that is right now. We're still working on what the best opportunities and options are for us. There's a number of different vehicles we could go down the path of tapping. Mileage Plan is one of those, and it's on the table, but it's -- there's no certainty about which one we'll do at this point.

Operator

The next question is from Jamie Baker with JP Morgan.

Jamie Nathaniel Baker - *JP Morgan Chase & Co, Research Division - U.S. Airline and Aircraft Leasing Equity Analyst*

Can you just sort of comment as to how the negotiations with treasury are going? When we might have some timing around the loan outcome?

And also as a follow-up to the previous question, did you specifically list loyalty as an asset on the loan application that you were willing to pledge?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. Jamie, it's Shane again. I would just -- I'd start by saying that the discussions with treasury and their advisers from the very beginning on the payroll support we ran through today have been very, very productive, super professional. It's a great group of people back there trying to do everything they can to support the country, support the economy, give it a way back in the future. And there's probably nobody working harder right now than that group of people back there.

On the loan side, it has been in a bit of a lull. We did talk last week with treasury's advisers. I think they're very intent on beginning to get more clarity on what these loan terms and conditions and collateral will look like in the coming weeks. So we anticipate a more active dialogue in the next 5 to 10 days. And yes, we did list the loyalty program, listed essentially most of our asset base, which was sort of expected to be listed just based on the way that they gave us the application.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

And those are all options of collateral, right, Shane?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Well...

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes, TBD on what we use.

Jamie Nathaniel Baker - *JP Morgan Chase & Co, Research Division - U.S. Airline and Aircraft Leasing Equity Analyst*

And then following in Mike's footsteps, I'll try to do only a two-part follow-up question. So on fleet, and I apologize if you mentioned this in response to this question, it was breaking up a little on my end. But have you reached the walkaway point in the MAX contract? And how should we be thinking about that as it relates to future CapEx?

And then second, in the release, you mentioned lease deferrals. Can you add any color on that as to the duration and when repayment is going to take place is -- I'm sure it's in your cash guide, but is that a net cash saving for the year? Or did you just shift lease payments from the second quarter to the fourth, for example?

Nathaniel Pieper - *Alaska Airlines, Inc. - SVP of Fleet, Finance and Alliances*

Jamie, it's Nat Pieper. Let's start first with the MAX question. So Boeing has been a terrific partner of ours for years and years. Our original order for the MAX, 32 airplanes, and Boeing's got a considerable amount of predelivery deposits on hand of ours. We're working with them and sorting through what the right scenario is for that. And I think that's part of the fleet discussions and analysis that we're having internally to figure out what's the most efficient fleet for Alaska moving forward.

Regarding the lease deferral discussions, we started those really in the second week of March and have had pretty good traction, very diverse lease base within Alaska and have been able to secure lease deferrals with all but two of our lessors and are appreciative of the partnership with them.

I would think of it, Jamie, as a 12-month process. So deferrals that we get eventually within that 12-month window, we're going to repay those amounts with the exception of discussions with each of those lessors, should the revenue environment continue to be super challenging. They understood from the beginning, we may have to come back and have a second bite.

Operator

The next question is from Helane Becker with Cowen.

Helane R. Becker - *Cowen and Company, LLC, Research Division - MD & Senior Research Analyst*

So here is one question for you. I think Horizon received money and so did SkyWest, and they are both providers to you. Have you gone to them and asked them for their -- the payroll support program cash that kind of directly attributes to your business?

Andrew R. Harrison - *Alaska Airlines, Inc. - Chief Revenue Officer, Chief Commercial Officer & Executive VP*

Helane, it's Andrew. Obviously, Horizon is a wholly owned subsidiary. So that money comes to Air Group. And I will tell you, SkyWest has been a fantastic partner along all of this. They've -- we've looked at our contract, and they've helped us through this financially. And we also -- the costs for labor that they incur to fly for us, those CARES funds are being flowed through to us in our contract.

Christopher Michael Berry - *Alaska Air Group, Inc. - VP of Finance & Controller*

And Helane, this is Chris Berry. I would say we're also having the same discussions with ground service providers and other contract folks out of the airports who have also received those CARES grant. So we're having those conversations with all of our vendors that have received some form of federal support.

Helane R. Becker - *Cowen and Company, LLC, Research Division - MD & Senior Research Analyst*

Right. Because otherwise, they'd kind of be double dipping.

Christopher Michael Berry - *Alaska Air Group, Inc. - VP of Finance & Controller*

Right.

Helane R. Becker - *Cowen and Company, LLC, Research Division - MD & Senior Research Analyst*

Right. And then my other question is, do you -- are you changing your operations at Paine Field to kind of focus back on SeaTac, given how low demand is? And the other part of that question is, Seattle was one of the first cities to experience the virus. And I'm just kind of wondering if as Seattle and the State of Washington and the State of Alaska have opened up a little bit, have you noticed any recovery in bookings?

Andrew R. Harrison - *Alaska Airlines, Inc. - Chief Revenue Officer, Chief Commercial Officer & Executive VP*

Helane, Andrew, again, just with respect to Paine Field, we've obviously materially reduced capacity just like everywhere else. We run 175 airplanes out of there, very low trip costs per se. We just keep the bare minimum service there, and that's where we're at right now. We have a lot of our folks who live up and around that area, and that they enjoy to travel out of there. So that's what we're doing there.

As you've heard on many of the analyst calls, we've reached the bottom. I mean, the bottom is the bottom, obviously. But I would say that, although extremely modest, we continue to see passengers carried every day on our network grow a little bit by little bit, day in and day out. But it won't be until there's a material change in the stay-at-home orders that we expect to see any material shift in that. So we're still heavily reduced demand as we sit here today.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Diana, do you want to talk about what's happening in our state, the other important geographies in terms of where we think shelter-in-place orders are and so forth?

Diana Rakow;VP Of External Relations

Sure. Helane, it's Diana Birkett Rakow. I lead external relations at Alaska. We have seen the curves out here flatten but like the rest of the United States, they haven't necessarily gone down and our leadership out in a lot of our West Coast states have worked together to have sort of this four-phase approach. That said, we haven't actually opened up significantly. Washington State is still in Phase 1. We've opened up construction and as of today, outdoor recreation and some other areas, but not significantly opened up in terms of the workplace or groups gathering.

And then in California, Governor Newsom just announced that Friday, we will move into Phase 2 of the four-phase approach, which means that some barber shops, retail will open, the sidewalk delivery, some manufacturing workplaces and again, construction. But we have a ways to go in terms of sort of truly opening up the economy. Every state is kind of going there -- taking their own approach. But the way that we think about it is both where -- what is the state of play in our hub, and what's the state of -- respectively, and what's the state of play sort of at the other end of that spoke?

And then just for Alaska and Hawaii, there's still some quarantine restrictions. So we're watching each of those states closely.

Operator

The next question is from Catherine O'Brien with Goldman Sachs.

Catherine Maureen O'Brien - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

So maybe just a couple more on your cash burn figure. Sorry to belabor this point, but -- so first is on that June -- month of June rate, what is your assumption on revenue? Are you assuming [receive less] refunds improve from where we're trending today? Or you're assuming no improvement there?

And then maybe just one more on that breakeven year-end cash burn figure. I just want to make sure I understand that, if demand was to remain at current levels, would you still -- would you be able to take actions to get that burn to breakeven? Or I realize there's many more questions and answers on recovery. But just thinking if you have -- just wondering if you do have the tools to get that breakeven, even if demand kind of stays down here?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Catie, it's Shane. Yes, on the June number, I would just say, we're assuming that it looks very similar to April and May, to be honest. So no real recovery. It would be great if we saw forward demand pick up and people start to book travel for later in the year, but we're not necessarily counting on that. On the what if, sort of, scenario, I'm not going to sort of go down that path very far, except to say that there's no scenario under which we're assuming we can't get to our target. And so it's incumbent on us to go after it as hard as we can and to get there, and we're not going to take that goal and commitment off of the table, certainly not as we're sitting here talking today. And so lots to be seen on where that may end up in terms of Q4 revenue, but our job is to go work the things that we can control and get ourselves to cash breakeven for all the reasons that Brad said.

Catherine Maureen O'Brien - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Okay. Great. Appreciate that. And then can you just walk -- I have one more, sorry. So can you walk us through how you're thinking about additional liquidity raises? So what type of demand recovery scenarios are you making contingency plans for in terms of those future potential liquidity raises?

And I guess what I'm really trying to get a sense of is how many months of liquidity are you comfortable with having on balance sheet, assuming that we don't see an improvement from current levels in demand over the medium term?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. Thanks, Catie. Yes, I think for us, and I think others who have gone before us have said that there's a real asymmetrical risk with -- should you get more cash onto the balance sheet, or should you not? And so our bias is more liquidity is not going to be something we regret. At the same time, I think what we're trying to also be very clear about is we don't want to burn through that cash. In a perfect world, we know we're going to burn through a lot over the next several months. We know we'll burn through a lot in 2020. We would like to get to an equilibrium as we get into 2021. And then hopefully, demand stabilizes, the industry stabilizes, and we don't have to sort of burn through anything else that we compile on the balance sheet. But our job #1 is to make sure we're here that we bridge this downturn and that we have an opportunity to take advantage of any potential opportunity on the other side.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Shane, all that burn, that's just -- that's -- if you raise the liquidity and get your burn under control, you pay the liquidity off, and you're in good shape. If you don't manage your burn, it's just debt.

That burden saddles the company, burdens the company for a -- Catie, my own thinking is I think we're going to be aggressive on the fundraising side. I just think that's the personality and the profile of Alaska Air Group. But we hope that we don't come out of this with like -- I don't want to say that number, but an enormous amount of debt on our -- it's going to be a high number. We just don't want it to be $6 billion, $7 billion of debt on our balance sheet. That would be a difficult thing for us to manage with. So that's why managing our burn rate is so important.

Operator

The next question is from Hunter Keay with Wolfe Research.

Michael James Maugeri - *Wolfe Research, LLC - Analyst*

This is actually Mike Maugeri on for Hunter. So I saw that you're beginning to operate some tag flights, which I assume is due to the DOT minimum service requirements. Can you just talk a little bit about what that's doing for your operation? And if that portends to how your network might look post COVID?

Andrew R. Harrison - *Alaska Airlines, Inc. - Chief Revenue Officer, Chief Commercial Officer & Executive VP*

Yes. Thanks. This is Andrew. We -- so really, we only ask for exemptions for a couple of cities. But the tag flights and also what we call loopers, where we sort of do a little bit of a circle, these are a very efficient way to serve multiple markets when there's low demand. And instead of flying two flights, we can fly on one single aircraft. The way the crews are working right now, we can easily fit our crew times within those trips. And of course, crews will stay over in the hotels, especially on the transcons and then come back. I think we launched about 11 markets this month, and we're going to be doing some more. But I think in this time, we are going to be looking at how can we serve our guests to give a maximum utility at the lowest cost and a win-win for everybody, and that's what we're going to be looking at.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Andrew, it's more based on our desire to take care of our customers than a order from the federal government?

Andrew R. Harrison - *Alaska Airlines, Inc. - Chief Revenue Officer, Chief Commercial Officer & Executive VP*

Absolutely. Yes.

Michael James Maugeri - *Wolfe Research, LLC - Analyst*

Got it. That makes sense. Then sort of, I guess, a follow-up to that, how do you think about serving

multiple airports in one metro area, again, in the post-COVID world, say it's Dallas with Love Field and DFW. Is it sort of worth the complexity there to sort of serve your customers?

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Yes. What I will say is we have spent an exorbitant amount of time -- as much time as Shane's been talking about on the financing and the business. We've spent a lot of time in our network and where everything is. And so we're also looking at many, many scenarios on how to build and raise our network back up to strength in the future. And that's what we're doing right now, and we have nothing more to really add as it relates to that.

Operator

Your next question is from Duane Pfennigwerth with Evercore ISI.

Duane Thomas Pfennigwerth - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Shane, I just wanted to say, I hope you're enjoying the nice easy start to your new role.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Appreciate it. Duane. I appreciate it.

Duane Thomas Pfennigwerth - *Evercore ISI Institutional Equities, Research Division - Senior MD*

For 2Q, you've given us your monthly cash burn. What is the amount of CapEx and debt service that's included in that? And how much of the payroll support are you excluding from that, that you expect to take here in the 2Q?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

I'll let Chris chat through the question on CapEx. But just to be clear, the way we're talking about cash burn, any money we raise and we would put the government grant money in loans in that bucket, we're just putting that into the cash and liquidity bucket. It's not part of our calculation. Our calculation is simply whatever revenue we're able to get in the door, less all of the cash that's going out of the door. And so it's pretty pure from that perspective. We're not offsetting any of the cash expense with grant money.

Christopher Michael Berry - *Alaska Air Group, Inc. - VP of Finance & Controller*

And Duane, this is Chris. So from a debt service standpoint, it's about $60 million a quarter. So -- and it's a little bit lumpy throughout the quarter, but it's just put in your model, $60 million per quarter for debt service. On the CapEx side, as we mentioned earlier, we've eliminated all the aircraft CapEx. What we have left is pretty minimal. And I don't have a number for you, but it's a relatively small number for a few projects that are still ongoing. I just don't have that number in front of me right now, but it's pretty small.

Duane Thomas Pfennigwerth - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Got it. And then your comments about having some concern about where debt goes and being able to pay it down on the other side really resonate, because this is after all, a bunch of equity analysts that are on the call here. What are the long-term implications for capital spending given that goal?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes. Duane, again, I -- it's a great question. It's -- and I want to be -- I'll just mention, you guys are asking awesome questions. We wish we had like more clarity and more answers. We were sort of intent on sharing whatever we know today and not really hypothesizing so much. And so that's in the category where it's really too early to tell. If we do our job right, we get the liquidity we need, we get down to the cash breakeven goal. We manage the business well. And then we are able to see a recovery at some point.

We'll be balanced in terms of managing growth opportunities and sort of getting back to baseline levels of capacity while we're also needing to go back and pay down debt. I would just reflect on our last earnings call, when I think Brad said for the 20th call in a row that we were very proud of our couple of year pay down of the Virgin debt that we had acquired, and we're certainly focused on getting back into that range of debt to cap.

There is some flexibility on the fleet side, we do have a lot of PDP money on deposit with Boeing. And we can take aircraft under some of that. And so there's an opportunity for us to -- without new cash going out the door, actually flex back up from whatever our new normal is out in the future, if that makes sense and is helpful.

Operator

The next question is from Darryl Genovesi with Vertical Research.

Darryl J. John Genovesi - *Vertical Research Partners, LLC - Principal*

Good numbers. I know it's early for this, but I wanted to ask a little bit more about how this is going to affect your long-term planning process. And I'm not sure if it's for Brad or Ben or Shane. But what we're going through now represents somewhat of a paradigm shift. Before now our downside scenario modeling efforts usually centered on a financial crisis like demand environment, so a 20% peak-to-trough decline, give or take. And what we're seeing right now is clearly much worse than that. So two questions. First is, I guess, one that would fall into the category of one that you know, what was the range of demand assumptions that have typically informed your long-term planning processes before now? In particular, what was the bare case assumption that you would sort of model around when you were trying to figure out how to size the airplane and whether to build an -- whether to buy an airplane or not?

And then secondly, and I guess this one kind of falls in the hypothesis category. But regardless of the timing and shape of the recovery, is 2020 now likely to represent the bare case that you'll model to going forward?

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Yes, good question. Darryl, yes, I think that we historically had similar sort of downside models that you're talking about. I think inherent in a lot of our planning and decision-making was, we wanted to have an ability to manage through crises that were of the size we had seen in the past, give or take, and to do so as comfortably as possible from a financial perspective, to be able to weather those and just make sure we were here to participate in the recovery, and nobody obviously had modeled something like we're going through today. And so it is creating more question about how we think about downside cases in the future.

But again, we're about 60 days-ish or something into this, and we're really now just pivoting our focus to managing the economics as we get into Q4 and into next year, we just haven't had a chance to really think through what we think a new normal pattern might look like and what downside cases might look like. We're certainly modeling a range of 2021 demand assumptions right now, all better than we see today, but certainly much lower than we saw in 2019.

Darryl J. John Genovesi - *Vertical Research Partners, LLC - Principal*

And then on the ATL, I continue to be surprised by how resilient these have been across the airlines that have reported so far. Can you provide some color perhaps on how the air traffic liability trended intra-quarter? And how much risk there is to the $1.1 billion balance in Q2?

Christopher Michael Berry - *Alaska Air Group, Inc. - VP of Finance & Controller*

Sure, Darryl, this is Chris. Yes. The ATL, if you look at ATL on our balance sheet, it's inclusive of normal, what you would consider traditional ATL, which is tickets that are there for future travel. And it also includes our voucher or credits, what we call e-wallet on our side, and that's where there is just a residual value or some sort of credit in that we're holding on to as a liability that has no future date assigned to it.

So what you saw in Q1 was really a -- especially March, a significant shift from that traditional ATL into credit or the vouchers. And so you didn't see ATL overall come down. So as we look at that, that certainly is something that we're looking at. We're trying to model right now how that rolls through. And it really totally is dependent on when demand comes back. We cannot model that with any sort of precision. But what we do know is we continue to see sort of refunds and cancels, as Andrew and others mentioned and others are seeing in the industry. And the majority of those are going into this e-wallet or this credit balance. And so as we look to the rest of the year and as demand starts to come back, then that's when you'll see that start shifting back over into traditional ATL as people book their tickets.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Cash inflows will lag revenues.

Christopher Michael Berry - *Alaska Air Group, Inc. - VP of Finance & Controller*

Correct. That's exactly right. But we don't have a lot of precision on that model yet simply because we don't know when demand is going to start coming back.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Sorry, I might just add, I think there's about $600 million of traditional ATL right now in our number. The refund -- cash refund to credit split has been 70% to credit or a little bit higher. So you can sort of infer the potential downside if we saw refund activity continue to be what it was over the first couple of months of the downturn here.

Operator

There are no further questions at this time. I'll turn the call to Mr. Tilden for any closing remarks.

Bradley D. Tilden - *Alaska Air Group, Inc. - Chairman, CEO & President*

Thanks very much for tuning in, everybody. We look forward to talking with you at the end of the second quarter. Thanks.

Shane R. Tackett - *Alaska Air Group, Inc. - CFO & EVP of finance*

Thanks, everyone.

Operator

Thank you for participating in today's conference call. This call will be available for future playback at alaskaair.com. You may now disconnect.