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Delta Air Lines, Inc. (DAL)

Bernstein Strategic Decisions Conference

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MANAGEMENT DISCUSSION SECTION

David Vernon

Analyst, Sanford C. Bernstein & Co. LLC

All right. Good morning, everyone. This is David Vernon with Bernstein, covering airlines and transports. Welcome to Day 2 of our 37th Annual Strategic Decisions Conference. We are delighted to be joined by Ed Bastian and Julie Stewart from Delta, CEO and IR, respectively. We are going to spend most of our time on Q&A. Ed's going to kick us off with some prepared remarks. Julie is going to build a little intro before that.

As we're going through the conversation, if you want to ask a question on your screen, you should see a button that says, ask a question that will go into the system. We'll be able to see here if we'll be able to add those points in the conversation.

With that, I will hand the mic and the podium over to Ed, and welcome everyone to the conference.

Julie Stewart

Vice President-Investor Relations, Delta Air Lines, Inc.

Thanks, Dave. I'll give a quick disclaimer here. We filed an updated 8-K this morning with investor presentation and updated June quarter outlook. Today's discussion contains forward-looking statements that represent our expectations about future events. All forward-looking statements involve risks that could cause actual results to differ materially from forward-looking statements, and those risks are described in Delta's SEC filings on ir.delta.com.

Over to you, Ed.

Edward Herman Bastian

Chief Executive Officer & Director, Delta Air Lines, Inc.

Well, thanks, Julie; and Dave, thanks for having us. Good to be with you. Hopefully, everyone is getting ready to enjoy summer. Certainly, that's what we're seeing in our business. The US consumer is leading the return of our

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air travel business, and I could not be happier with what we're seeing happening as our business really is into a full-fledged recovery mode. Hopefully, this also will be the last virtual conference that we need to do.

We started to do most of our conferences and investor meetings in person. I think that's going to be a sign of the times that we're getting back and reclaiming our lives. And when you think about all we've been through, it's only been 15 months, it seems a heck of a longer than 15 months; probably many more in human years than actual physical years. But getting people to return back to life, reclaim their experiences is what we're doing here at Delta. I could not be happier again with what I'm seeing with the recovery.

Our Memorial Day volumes were very strong. We ran a load factor domestically in the mid-80s and carried nearly 3 million customers over the seven-day Memorial Day period. It was a great start to the summer and our team ran a very, very solid operation. With better than expected results and demand in May and June, we've also updated our guidance which Julie mentioned is in the 8-K. We now expect to be at the top end of our revenue guidance, down roughly 50% to 2019, representing about – a little over $6 billion in revenue generation.

For us, that represents a double from revenue from just the first to the second quarter. First quarter revenues were in the $3 billion range, we're expecting a $6 billion range. So just massive volume starting to show up. As I mentioned earlier, it's being led by the US consumer. Domestic leisure is expected in June to be more than 100% recovered. In our digital, booking volumes are also more than 100% recovered to 2019 levels, which indicates that demand for travel is going to continue to accelerate from this point.

We're seeing nice improvement in yields. As you could appreciate, now that our load factors are up, Delta was the last airline to block the middle seats. We're blocking the middle seats right through the end of April. And we went from load factors that we were averaging in April to 50% up to the Memorial Day holiday, which was in excess of 80%. When you have that level of volume, you can appreciate there's some choppiness in the pricing environment in the very short term. But we're already seeing in the month of June, some nice improvements in yield as well as a 25-point load factor increase if we took the March month compared to where we expect to be in the June month.

The corporate travel is improving, still not where it needs to be by any means. But domestically, we're at about a 30% recovery level. But every week, it gets stronger and stronger. And anecdotally, from the many CEOs and business leaders I talked to, people are just – they're ready to go and they are starting to move. In large part, this is going to be initiated by the reopening of businesses. I'd expect over the course of the next few months, certainly by Labor Day, no later than, we're going to see corporate America open for business.

And as the businesses are reopening, corporate travelers are getting back to doing what they do which is driving their business, being out, making connections, and continuing to lead their businesses forward. For Delta, for example, we are fully open now this month of June. And many, many companies here in the southeast are already back to 2019 levels.

On the cash front, cash is also quite strong. We're seeing in the current month of May and June, revenues that are coming and cash revenues that are coming in roughly 25% higher than where we had originally forecast at the start of the quarter. June month daily cash sales system-wide are 60% recovered to the 2019 level, and we expect to be solidly cash positive in the June quarter even ahead of the $4 million per day that we saw in the month of March. So, on the cash front we're also doing well and our cash reserves are in good shape.

On the cost front, there have been some noise, some friction. Fuel, as everyone can appreciate, is starting to move and that's moved up over the course of the quarter. So, we've seen some pressure on fuel as well as RINS

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for our refinery at Monroe. And we expect to be also at the upper end of the guidance range on our non-fuel cost, primarily due to a decision we made last month to reward our employees for the great job they did as we won the J.D. Power Award for Best Airline in North America. We awarded all of our employees to positive space travel tickets anywhere they want to fly, and that unfortunately counts as a cost in our in our bookkeeping. And that's about a point to a point and a half of pressure in the quarter that we were not – we're happy to receive, but we weren't anticipating. So, absent that we're right in the midpoint of guidance on the quarter. So, I feel good where we are in cost.

And that all adds up to our June quarter coming in at expected pre-tax loss in the billion dollar range, but we do expect to be solidly profitable at the pre-tax level in the month of June. And we also expect to be profitable in the back half of this year. So, inflecting to profitability just 15 months through the worst crisis in this industry's history, I think is a pretty impressive statement about the resiliency of the business that we have created and the great work of our people. And we look forward to continuing to grow from here.

Very, very quickly and that I'm not going to go through the charts, but when you look at the strategies and the key areas that underpin our positioning in the recovery, it's probably best captured on slide number 5, very focused on leveraging our brand loyalty. The health of our brand has come through this crisis stronger than ever due to the great work of our people and how we took care of our customers. During the crisis, we're seeing that recognized in the highest ever Net Promoter Scores, customer satisfaction scores as well as the recent award of the J.D. Power Best Airline Award in North America. Interestingly, during the quarter, when the crisis began, people were concerned as to what that might mean to our premium strategy.

At Delta, we are a premium airline. We get paid for delivering premium product and premium service. And in a consumer-led, leisure-led recovery, it was unclear in many people's eyes how our strategy was going to hold up. And fortunately, this held up quite well. And we anticipated it was going to hold up well. People are paying for quality and they're paying for premium. And our premium products have outperformed our main cabin in both the yield and load factor improvements by 10 points. So, it's good to see that the product segmentation strategy and our ability to maintain the revenue premium to the industry continuing to click in and confirmed during the crisis, which we think again will only be stronger as we go with corporate starting to return back to the business.

And we're also monetizing that strength through our great partnership and loyalty program with American Express. Our American Express Co. brand, which is the most powerful card on the American Express platform, the spend level is already back. It's starting to exceed levels in 2019 already. So, customers are opting to use the Delta card. They believe travel is going to be an important part of their future experience. And while they may not be traveling at the present time as much, they're putting all their points into future travel. And that's great to see as well.

On the balance sheet, we are actively working on the restoration of our balance sheet. Since the end of the June quarter, we've reduced our financial obligations by nearly $11 billion through a combination of paying down debt as well as accelerating pension funding earlier this quarter. And we're in the process now of evaluating the additional opportunities for debt reduction and committed to getting back to investment-grade metrics over the short to medium term.

Importantly, on our pension plan, we have fully funded the pension plan with the – a last contribution that we're making this month of roughly $500 million. So $1.5 billion that we contributed within the quarter. And with that contribution, we are basically done and we don't expect to make any additional contributions period to the pension plan into perpetuity. So when you think about coming through the pandemic with a pension plan having been fully

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funded and retired, is another great sign of the good work our people did and the strength of the balance sheet coming through the crisis in maybe unexpected ways.

On the cost front, we're also continuing to focus very well on the efficiency of our business, streamlining our product offerings, streamlining our fleet. We've had a significant reduction in personnel. As you know many people opted to take early retirement, delayer the organization. We anticipate by the end of this year getting our non-fuel unit cost below 2019 levels, despite the fact that we'll probably be at about 15% less capacity than we were for the comparable quarter. So, that's for me is a pretty good testament to what we've done and the extent of sustaining power as we go forward to keep that cost efficiency in place.

So, Dave, I'm going to turn it over to you for questions. Are moats are – our competitive advantages had held up well throughout the crisis. Strength of our people, our culture is always number one. The operational efficiency of the airline. We – we're running the best airline in the skies, bar none. Our loyalty programs are strong. The balance sheet is starting to recover and our hub structure is in place with good international partners still by our side. And with – everything what we're seeing today importantly that we expect at the present time that we should be able to generate 2019 level of revenues no later than 2023 on a more efficient cost base, which positions us to generate potentially higher margins in 2023 as compared to 2019.

QUESTION AND ANSWER SECTION

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

That's a great intro at. Could you maybe help us understand as you have been managing through this obviously unprecedented crisis, what are the two or three things that have surprised you the most about the recovery in fare levels and consumer behavior as we've been coming out of this?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

Well, the strength of the premium product is certainly a surprise given that people were anticipating it was going to be a leisure led recovery with a lot of excess supply in the marketplace. The fact that we've blocked the middle seats right through the end of April and generated a considerable price premium to the market was one, we anticipated, but the strength of that I did not anticipate.

In the fourth quarter, which is the most recent quarter we have the government statistics from, Delta generated a 35% price premium over the competition and that is without our main traveler's flying, our big corporate travelers as well as our international travelers. So, even in a pandemic when pricing was very choppy and consumers were a very different demographic than we typically carry, people flocked at the Delta brand and paid a premium to be on Delta.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

And what does that tell you about sort of the normal assumption that most people have that the price of the seat is the most important thing when you're selecting an airline to fly? Is this the sign that maybe consumer behavior is changing a little bit in the market?

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Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

No question about it. The health of our brand has never been stronger. About 10 years ago, we set out on a path to de-commoditize. Our product from the industry, we realized that if we just stayed on the commodity path where pricing was the most important decision point in the consumer's eyes, we'd never make it. We could never generate the type of returns that we needed for our investors. And so, we focused on delivering a highly reliable product with the very best reliability. And we've done that over the last five years. And we're back this year fully to generating by far the best operational integrity and reliability in the sky, which is what customers deserve.

And we've added the products and the services that customers want alongside that operational reliability and the scale that we're bringing back to the skies as we start to reopen international. I think it's going – we're going to exit this crisis in a – even healthier standpoint on the commoditization or the de-commoditization of our business than where we were in 2019 alone. In 2019, we were generating a 20% premium domestically to the competition.

So, one of the things that consumers throughout our country are seeing is that their health and wellness have been something they've taken a bit for granted as people return back to public life, as people return back to travel. Those brands that have – are seen as being protective of and create the greatest wellness and ability to serve in the face of the crisis or the brands are going to get consumer power. And I think that's going to be even stronger when corporates come back.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, as you think about this notion of de-commoditization, what are the two or three things that Delta is doing uniquely to be able to kind of extract that premium? Is it the segmentation of the cabin? Is it – I mean, obviously, the quality of the service, the onboard experience is going to be a part of that. But could you talk a little bit about some of the things that make Delta able to uniquely execute on this opportunity?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

Well, it's the segmentation of the cabin, is certainly a big part of that. We have more premium product in the sky than any airline. We'll continue to put more and more of that on our fleet as we simplify our fleet or modernize and upgrade our fleet with all of our new airplanes coming in. And we did not stop taking planes during the crisis. We actually put more metal in the sky and we got rid of a lot of old metal. I think we shaved almost two years off our fleet age through this crisis. So, we're coming out as a much – in a more modern position and simplified position.

We are the number one airline to corporate America. We've won Business Travel News award for the last 10 years running. Corporate America appreciates the service, the reliability, the quality of the experience we're providing. And when you think about the decommoditization, a big part of that for us was going hard into the corporate space and showing the corporate travelers that we have their back and we are the preferred airline, without a doubt, in corporate America, and then candidly, it's not even close.

And the third part of that is the expansion of our international partnerships. The investments that we've made internationally are driving premium experiences back here in the US as we take international customers into the country and expect to return here over the course of the next year. And the partnerships that we've had while they've been stressed during the pandemic, they're actually in an even stronger place than they were pre-2019 as we've been through this crisis together with them.

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David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, I want to switch to business travel in one second, but one last question for you on sort of the domestically leisure traveler. What do you think is changed about the way other than maybe being willing to pay out more for a premium experience? What has changed about their sort of expectations for airlines around whether it's advanced purchase days or where they're going? What do you – are you seeing any sort of changes in the way consumers are interacting with Delta, are engaging with the airline? And do you think any of those changes will be permanent as we come out of the crisis?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

I think they will. One of the things that we've seen is the engagement with our digital tools, our Delta.com bookings. As I mentioned, we're already back and beyond 2019 booking volumes on Delta.com. Throughout the pandemic we saw over 50% of the transactions were being made directly by consumers with Delta as compared to going through the OTAs and in all the intermediaries who try to disintermediate us along the way, which allows us to create an even closer connection to our customers to be able to better serve them. And once those connections are made, then we don't we don't lose them. They just continue to develop and mature in a relationship moving forward, built a lot of new customers through this period.

SkyMiles, one of the things that customers love about Delta is the rewards we provide through the SkyMile program in our American Express partnership. We are already back to 2019 levels on acquisitions of new SkyMile members through the card program with Amex as well as just through natural means by people signing up to the program.

So, we actually created a whole new level of customer through the experience. People that did not have the previous opportunity to try Delta had that opportunity and loved the experience and paid a premium to be it. It's going to also allow us to get probably into another segment that we haven't focused as much on which is the small and mid-sized traveler. We've been very heavily focused on the large corporate customers, we are the airline of choice of corporate America. We also want to be the airline of choice in the mid-sized market for business as well. And we've had a lot of opportunity to get closer to that marketplace during the pandemic. That segment of business travel is actually a bit larger than the traditional and the classical large corporate travel segment. And it's also held up best through the pandemic.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, it feels like with fare levels where they are, we've kind of killed the lazy bear case with too many seats in the sky, never going to be able to get back to profitability. But one of the issues that still is out there and talking to investors is this fear of a business travel recovery, maybe never coming back to 2019 levels. Business travel changing forever kind of thing. How is your perspective on that debate changed as we've moved through the crisis? I think when we started out everybody was thinking, oh now, it's down 30% to 40% and now maybe it's down 10% to 15%. But from where you sit and talking to your corporate customers, how has your perspective on the nature of the business traveler recovery changed over the last sort of 10 to 12 months?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

Well, it certainly has improved as we've gotten closer to the recovery. I can appreciate at the beginning of the crisis people were very nervous about where the future travel was going, broadly, not just corporately. And as the

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vaccines have gotten people confident that they can carry on life as normal, as people understood and probably placed a much higher value on travel and not just business travel, travel in general when it was taken away from them over the last year. People are getting back to realizing how powerful travel and experience is a part of our life and whether it's in business or for personal reason, there's just so many reasons why people need to get out and connect.

On, again, specifically to your question, I've said all along that I expect the traditional corporate travel that we've carried, the business travel, to be reduced by 20% to 30%. And I hold true to that. But it's not doesn't mean the overall volume is going to be 20% to 30% lower. I think the lines actually will hold in just fine with where we were in 2019. I think the mix is going to change. The nature of the travel is going to change. These tools are going to be a complement to business travel going forward. They're not going to be a substitute for business travel.

I was with the CEO of a large ad agency a couple of weeks ago, came down to see me in Atlanta, and he said, one of the big obstacles to the traditional business travel [audio gap] (00:22:29-00:22:42) in the past has been when you get on the road, [indiscernible] (00:22:45) a bit challenged. Now, that everyone's used to video technology, you literally take your office with you when you get out on the road and you start to return and say you don't have any dead time, you can be as productive when you're on the road as you are in your office because people have found a way to be mobile.

Video technology makes you mobile, it doesn't make you immobile. It actually gives you freedom to move. So, that's just one of many ways we're going to see that technology is – complements what we do. Internationally, I think there will be some business trips that were, overnights to Europe that won't return, and they shouldn't return. Those are inefficient use of people's times. When people travel internationally, I think people are going to spend more time, getting back and actually investing in relationships. The world needs to get reconnected. And we've never felt as disconnected as a society as we are today. And one of the reasons is because people haven't been able to be with each other.

And my view and I'll go out on a limb here, Dave. I think starting July 1 forward, if you look at least on the domestic business travel side, I think the volumes of domestic travel July 1 for 12 months forward are actually going to be even higher than the domestic volume – travel volume for business that we saw in 2019 alone because there's such a demand, there's such a push to travel, and people are going to be out there. Our [ph] planes (00:24:16), it's amazing to me. We saw the jump from April to May and load factors I talked to you from 50% to 80% virtually overnight once people felt safe. And as business -those people all have jobs that are traveling.

And those companies once they finally reopen, which they're already in the process of accelerating the openings for many companies, they're going to be out, and encouraging people to get back out on the road to be with customers. And so, I think everyone's going to be leaning in the same direction to go and to reconnect and get their businesses going. I think there's going to be a lot of peer pressure. No one is going to be waiting for the government to say it's now, now is the right time to travel. Businesses are going to be making that decision and pushing their people out on the road. And I think there's going to be a renaissance of business travel in our country not just for the airlines, I think for the hotels and for the hospitality sector in general.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

As you think about that recovery, one of the things that we had been looking at prior to the crisis was eliminating some of the constraints through the GDS systems in the channel that would allow you to maybe extract an even better yield premium going forward through the business channel. You recently announced a partnership with

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Sabre, I think, to expand some of your distribution. Could you talk to investors about kind of what that's going to do for you from a – either upsell or a more premium product available kind of into the business channel?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.
A

Well, one of the things that traditional GDS relationships were based on was volume. And we've been after them for a long time that we're not focused on volume, we have no problem getting volume. We're focused on premium, and we're focused on fund value back to our consumers and the value of the experience.

And what we did with Sabre and I give Sean and the team there a lot of credit for stepping up with us and doing this. It allows them to create a real retail storefront with Delta where they can put on their site the Delta product, market it, and merchandise just as you would in retail. That's our goal. Very similar to what we're doing in Delta.com. And so, there's alignment and consumers are understanding the value they receive in the products and the services that they receive when they shop, Sabre on Delta as well for our corporate travelers as well.

So, there's been a [ph] lot changed (00:26:42) in our industry over time. And the quality of the experience, the products that we're putting out, the opportunity to upsell, the opportunity to segment and differentiate in the marketplace has never been better. And we need our travel partners to be able to generate and bring the technology with a retail mindset and be able to price accordingly similar to how we handle that on the Delta.com site.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC
Q

So, you mentioned earlier that your expectation would be some of this pull forward the direct relationships for leisure is a permanent pull forward. And with a change to Sabre – like if you were to think about just the business part of your distribution challenge, how much of the market have you enhanced with the ability to kind of offer the full suite of products from Delta? Like I'm trying to get a sense for how much more they need to be to go over the next couple of years as you think about rolling out similar [indiscernible] (00:27:38) with other general partners.

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.
A

Well, I think it's significant and for us it's aligning our objectives. I'm not going to put a number on that for you. It's internal we have a number and it's a significant number.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC
Q

Okay.

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.
A

But it's about aligning our objectives and getting us all moving in the same direction paying Sabre for bringing the customer that we want as compared to just volumes of the premium customer, and providing the incentive for them to invest in their channels to differentiate Delta and give us that retail experience that we're looking for.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC
Q

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Okay. If we talk about loyalty for a little bit. I think prior to the crisis at your Investor Day down in the Delta Museum, you guys had laid out a pretty ambitious plan to get the contribution from the card programs up to I think it was $7 billion over a couple of years. How has the crisis changed that expectation? Is it just push the number out? Or if we maybe found that loyalty is actually more valuable, there's more potential in there. Like how do we think about that expectation for the contribution for the loyalty programs kind of coming from where we are today over the next several years?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

I see no change to that, Dave. I think that $7 billion target is what we share together with American Express as well. We're working towards that. Obviously, we didn't know that we hit a major speed bump in the form of pandemic when we gave that forecast. But at the same time we have seen the – the pandemic has created the opportunity for differentiation in the eyes of the consumer like never before. And so loyalty is something that people have great place, greater value on it. People are again picking winners and losers through this crisis. And those that want to ensure that they're staying with the brand that is – aligns up with the value of the experience that they're looking for, there's no question that brand is Delta and the card that they're using is American Express.

I find it remarkable, honestly, that we are already beyond 2019 co-brand volume levels on the most important card in the entire Amex stack period, not just Delta, but period for American Express. We are their largest commercial partner. They are our largest commercial partner. And that's with travel which typically is a big part of the spend that goes on the card, still down 30% to 40%, you know, travel volumes and revenues.

So, people are putting – we hear a lot about all the discretionary income of the consumer in our country and the bank accounts that are growing in the consumer space. As people are spending, they're putting their home improvements on the Delta card. They're putting their furniture purchases on the Delta card. They're putting their small business expenses on the Delta card because they want to go on Delta as they get through. And they used it really as a source of optimism to get them through the pandemic, that they were looking forward to the experience they're going to have.

I can't explain anything else, but this brand and the strength of this partnership is even stronger now than it was in 2019. And that's a pretty remarkable accomplishment and achievement just in and of itself on top of everything else we've accomplished during the pandemic.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

Excellent. So, one thing I also wanted to get your perspective on. In the past when we've gone through periods of crisis, there has always been this view of opportunistic changes in the business and whether it's new entrants coming into the market, whether it's rationalization of capacity in certain corridors.

How do you think about the risks and the opportunities that are created by effectively resetting the domestic travel landscape from 2019 levels to 20% [ph] off and (00:31:48) now on the way back up? What kind of risks and opportunities are you seeing for Delta in the next couple years?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

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I think the next couple years on the domestic front, Dave, are going to look more akin to what we saw previous to 2019 – in 2019 prior than any radical change. Yes, there are some new entrants that have gotten a lot of publicity. We enjoy competition. It makes us better and makes us stronger. That's not something I worry about. In the least, I think it's good for our industry.

But the fact that the US government was as strong with its support of the industry through the CARES Act, kept the industry essentially intact through the heart of the crisis. Very different than almost any other country around the world. Most countries around the world either gave no support to their airline industry or gave it in the form of loans and taking capital in those businesses.

The majority of the support we've received in the US was in the form of a grant, to keep our people employed, to keep our people engaged, and to be able to stay in this company – in this country back up, as the virus was started to recede which is done just that, and you can see the effects of that. So, I think that the structure for the next year or two is going to look very similar to what people have seen. I think over time, change will happen; it's just going to be delayed. And I think that change over time is stronger and going to get stronger.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

What do you think about the opportunity for you in the international markets, given that the US airline industry is going to emerge a little bit ahead with a large domestic market? Does that give you a chance to maybe kind of reshape the international landscape as we move forward?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

Yeah. One of the things we talked a lot about pre-pandemic was the opportunity to improve our international margins and bring them in line with our domestic margins. In Delta, we generate our highest margins in the US in our domestic business. And particularly in Latin America, in Asia, our margins are significantly lower than they are in the US and even Europe, which is still a quite healthy margin; it's still below where it is in the US.

As capacity has been rationalized internationally as a lot of the low cost players, the carriers that were probably not as well capitalized and that were instable, going into the pandemic have gone away. And those business models have proven that they didn't stand up in the face of the pandemic. It's going to allow the strong carriers, the truly global carriers to be able to expand quicker and be able to grow faster and be able to take better productivity and better margins internationally forward over the next few years than where we've been previous.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

And do you think that that gap between domestic and international will fully close? Or how should we be thinking about that?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

I don't know that it'll fully close, but it'll certainly improve considerably. I could see international getting potentially higher than domestic. It's been there in the past. It's not unheard-of for international margins to be stronger than our domestic margins. But I believe, over the next several years it'll be more focused on closing the gap.

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David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. So, what are the downsides of the lack of support internationally for Delta has been, some of the markdowns you've had to take on the foreign equity investments in airlines? How do you think about that as a strategy coming out of this? I mean, obviously this is not – I'm not making a judgment about it, but it was a situation that I actually thought was very forward thinking strategy coming into it. Post-COVID, kind of hurts a little bit. How do you think about changing that elements of Delta's capital allocation going forward? Or do you think – have you thought about it at all?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

Yeah. I don't regret any of those decisions, and I think they're actually just going to be all the more beneficial to us going forward. We've been through this crisis together, whether it's the group at LATAM and Iquitos or AeroMéxico, or Virgin or Air France-KLM or Korean. We stood by our partners. We've been great partners through this difficult time. And so, the bonds that we forged are even tighter than they were pre-pandemic which is going to give us even greater opportunity long term to make those investments and those partnerships, all the more strategic and more lucrative.

While the accounting guides have required us to write down the investments because of the – going through the restructurings and the bankruptcies, the only thing that's really happened is the balance sheets of those companies have gotten a lot cleaner. And so, they're going to come out of this even stronger without the level of debt and without a lot of the inefficiency. They've gotten a lot younger. They've been able to streamline their fleets. They've been able to bring the cost of their product down a lot in their order books, in their fleets.

So while officially in the accounting records those marks have been taken, they're not off my personal accountability. I still expect to generate a return on the aggregate amount that we invested in those airlines which I know it's in the $4 billion to $5 billion range we've invested over the last decade, that's the level that I expect to generate solid double-digit returns over time.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. And on the cost side of the business, you mentioned you're going to expecting to be at or below CASM-Ex for 2019 levels at a lower level of capacity. Can you help us understand exactly kind of what that is? Is that gauge, is that just de-layering on the overhead? Like, how do we think about the contributors to that pretty remarkable achievement? I think anybody coming into this would have said, with capacities 15%, 20% lower, there's no way you're going to get down to a lower unit cost. What are those two or three things that are helping you kind of get to that level quicker?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

It's a lot, Dave. One of the big things is the continued up-gauge of the domestic system. As we've taken out a lot of the smaller planes, the MD-80s, the MD-90s, retired tremendous number of regional jets, and continue to modernize the fleet going forward. We've been able to upgauge, and every plane that we upgauge, that we bring to the domestic market. Let's say, you take out an MD-88 or an MD-90 and you put an Airbus 321neo in, you're bringing 25% more seats to the departure to the actual flight, find a better quality experience, a better quality for the customer, and a much more fuel efficient, a 25% lower fuel cost per flight as well. And so, it's a win all the ways around.

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And so, as we continue to upgauge and we still have – I'd say, we're in the mid innings of our upgauging strategy, that's been the single biggest source of productivity over the last number of years and will continue. In fact, through the crisis it's accelerated the upgauging that we're doing. Though we've also – tremendous simplification of our fleet, we've taken out four of our fleet families, as we've retired during the pandemic over 200 planes with another 200 to go in the next few years. We've accelerated those retirement dates. We've de-layered the organization. We actually exited through retirements 20% of the total workforce of the company as we went through. And so, it's given a lot of younger people opportunities to step up.

So, we have a younger team going forward and we're getting the [indiscernible] (00:39:55) benefits, all across the frontline as well as the management team. And we're getting ourselves set up for the future. And as we grow back to the 2019 revenue levels which I indicated that we should be at no later – maybe earlier than 2023, but no later than 2023. We don't need to bring back as many of the people, as many the cost profile and that's going to allow us to sustain that non-fuel cost opportunity that we've developed here this past year.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

And that ability to kind of maybe do more with less, is that enabled by technology or productivity programs? Like is this just, hey, we were in a crisis so we've de-layered and there's a potential tension for that cost to come back into the system? Or has there also been some sort of fundamental redesign to some of the work from those fundamental expansion of spans of control, how will you think about it from a managerial standpoint?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

It's much [audio gap] (00:40:51-00:41:04) the redesign. Well, we have the ability to reengineer, redesign many of our operating processes and cost structures from catering to rethinking how we cater planes, provision planes, what we have on planes to how we staff to the airport experience, how do we get greater leverage and efficiency out of that products?

So many, many things that in a pre-pandemic world that we're just running all out at peak velocity. When you have a chance to stop and rethink and reflect on how to do it better, how to do it smarter and how to do it simpler; and it's all underpinned by technology, it's underpinned by the simplification of the fleet into fleets that were sitting on the ground and the opportunity to come out of this a much more modern, simpler airline.

It's going to allow us to sustain that lower cost profile into the future. And listen, we expect to come out as a higher premium airline as a result of the pandemic with a lower cost profile. And that's what gives me optimism that the margins that we exited the pandemic are not only going to be back, but they're going to be better in the next couple of years than where we were.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

So, as we kind of get down that path of the revenue recovery, the margins coming in. As you're starting to think about the next three- to five-year investment plan, what are the priorities for you and for the board from a capital allocation standpoint going forward?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

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Well, it's interesting. We first order businesses to get our balance sheet fully restored and back to where we were to get our investment-grade metrics back. And I really do believe that we will be there over the next couple – two to three years. And as we get later in the year, we're going to start to give some concrete targets for the streets, so people know how they want to measure the balance sheet, what our goals are.

You think about the fact that we're not going to have pension obligations any longer going forward in terms of funding obligations on behalf of company. We've averaged over $1 billion a year of contributions into the plan over the last decade. Those contributions will no longer be required. We're done, as you look forward. When you think about that we bought back on average $2 billion to $3 billion of stock over the last number of years, we're not going to be buying back stock certainly over the next two to three years because the CARES Act limitations as well as the fact that we're going to prioritize, getting our debt pay down and the balance sheet restoration.

And the same thing is true for dividends over the next year or two, the restrictions of the CARES Act are going to enable us to take that capital. We put all that together. That's on the order of $4 billion to $5 billion of free capital that we've been spending in the business that we're going to target exclusively to get the balance sheet fully restored. So when you think about the pandemic, we generated – we grew our net debt by about $8 billion from the start of 2020 to where we sit now. And we're not going to be adding any more to the net debt.

I think it's very reasonable thinking the next couple of years that $8 billion is going to be fully paid back. And we'll be back at the investment-grade metrics that we were in a short two-year time span. In addition to that, we're certainly going to continue to invest in the modernization of our fleet. Continuing to upgauge the airline where Airbus has been a great partner working through this crisis. We're going to continue to grow with Airbus and grow the upgauge; and every plane that we put into system is immediately accretive to our operating margins as well as our cash flows.

When you think about technology, we've had a chance to sit back and think where our technology really matters. And what really matters for us is the connectivity to our customers. So whether it's improved WiFi performance, a better digital experience, it focus more and more on the connection of Delta with its customer taking the strong NPS and customer satisfaction scores and cementing that much further. And when you think about continuing to be the airline of choice to corporate America, those areas we're going to focus our CapEx in the next several years.

David Vernon
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. And as you think about – let's say, we get to a couple years from now, EBITDA margins are doing well, balance sheet's repaired. How do you think the business is going to think differently about taking risk, taking capacity on, thinking about balance sheet and quality metrics on a go-forward basis? I mean, is there going to be a permanent shift in the level of either unencumbered assets or financing that you're going to be thinking about – there you're going to need to have on hand as a result of this sort of once in a 100-year crisis?

Edward Herman Bastian
Chief Executive Officer & Director, Delta Air Lines, Inc.

A

Well, one of the things that we saw coming through the crisis is that we have a lot more resiliency than anyone would have thought. I hesitate to think anyone thought in 15 months that we'd be back to profitability, that we'd be back to positive cash generation, that we'd be talking about getting our investment-grade ratings back in a 15-month period. This is an industry that bounced [indiscernible] (00:46:35) crisis-to-crisis over time. And this may have been the final test of the resiliency of this industry, Dave, and certainly this company at Delta.

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One of the things is I talked to investors over the last number of years, people were thrilled with the progress that we've been making, whether it's consolidation or improvement in core business and the focus as an investable segment. But the nagging question in the back of people's minds, in the front of people's minds at times was, what's going to happen when you get the next big crisis? What's it going to look like? Well, I think we now know what that looks like and knock on wood, hopefully we don't encounter anything worse than that or that ever again in our lifetimes.

And as a result of that, the resiliency of this business has proven itself. What does that mean? We're going to carry even lower debt loads and even higher cash levels? Absolutely. Resiliency has shown us that we don't want to be maybe sitting as exposed as we were. And we'll be given those targets in latter part of this year when we give our targets, as we come through the crisis and restore investment-grade back to the company. But my hope is that we've tested a Delta at least, the proposition of our airlines investable. And I think the strong answer is, yes, they are investable.

And even in the worst crisis imaginable, we've proven ourselves. We've proven the value of what we bring to the society. We've proven the governments will be there for us if ever needed again, hopefully never again. And that customers have a desire to get back out on the road and reconnect like never before. Their technology can't possibly replicate. So, I think you're going to see when we all look back a year or two from now, and say, wow, that was the – this industry got through the fire in a way it never could have imagined and Delta specifically led the way.

David Vernon

Analyst, Sanford C. Bernstein & Co. LLC

Q

That's an excellent way. We're coming up here onto the end of our 50-minute allotted of time for Q&A. Is there anything else you'd like to leave investors with? I think that was a perfect drop-the-mic kind of moment for me, but if you'd like to leave us with any other parting thoughts?

Edward Herman Bastian

Chief Executive Officer & Director, Delta Air Lines, Inc.

I appreciate all the support we've received. We've received a lot of support to get through this with a lot of encouragement, and a lot of our investors, but also our customers on Delta. I appreciate you all. And we're going to be back stronger than ever. And I think that's true. I think a lot of people say that. We're showing that we're doing it. We're profitable in the month of June, we'll be profitable in the back half of this year, and we're well on our way back, climbing back to the top of the industry stack.

David Vernon

Analyst, Sanford C. Bernstein & Co. LLC

All right. Well, thank you very much. And thank you very much, Julie, for joining us. A great overview. Always great to talk to you. Hopefully, we will be able to do this again live next year.

Edward Herman Bastian

Chief Executive Officer & Director, Delta Air Lines, Inc.

Thank you, Dave.

Julie Stewart

Vice President-Investor Relations, Delta Air Lines, Inc.

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Thanks, Dave.

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