

December 2008



Dear Fellow Airplane Obsessors,

This is **not another letter about Eclipse**. Honestly, I have no desire to continue kicking that dead horse. Besides, it's Christmas. Let's play nice. But as I reflect back on Eclipse's inevitable collapse, I've never seen a better example of the enormous rift between two kinds of aviation people. There are basically two groups. One loves planes and the culture of planes. Perhaps they are pilots, hobbyists, or engineers, a broad and ecumenical group. Let's call them "**romantics**." Then there are folks who have jobs like mine. This group, call them "**analysts**," care about exactly one thing: **return on investment**. Neither group is right. In fact, there is no right or wrong. The two groups just see the world through different lenses.

The difference between the two groups explains a lot about where the industry has come from, and where it is headed. Romantics love **new technology, new transportation options, national and regional prestige, and giving people jobs**. If a plane looks like it will do any of these things, romantics want it to happen. Analysts, by contrast, don't want to know about any of this. They only want to know if a plane will **make money** for the industrial and financial players in this business. The rest is anecdotal stuff, only interesting as a side benefit if it accompanies profitability.

The world is increasingly run by analysts, and by the dictates of the market. Analysts are there to provide needed discipline. Eclipse and DayJet, however, got off the ground largely because of romantics. The utopian vision of small high-tech jets transforming the world and taking people where they wanted to go produced record levels of support from romantics (for a superb view of this ideal, see James Fallows' *Free Flight: From Airline Hell To A New Age Of Travel*). But in the end the analysts were right. As the two businesses failed they destroyed considerable value (around \$2 billion, but more if you look at the Eclipse suppliers that have to write off their investments). Jobs were lost. Lives were disrupted. If the romantics prevailed this unpleasant story would happen more often.

The **A380** is an even better example. From a romantic's perspective, this plane has it all — national pride, cool technology, grandeur, utopianism, even a **delightful children's book** handed out at air shows. But there was no business case. In fact, Airbus never even provided a *pro forma* business case. Airbus, like the romantics, avoided all carnal knowledge with a P+L sheet. The consequences are painfully obvious. The A380 is something Airbus needs to recover from. The painful restructuring of Power8 is one result. Worse, thanks to heavy spending on the A380 the timetable for the far more important A350XWB is under serious pressure, which will only get worse in the coming jetliner deliveries downturn.

So...hooray for us analysts, right? **Nope**. Far from it. Analysts face **an uncomfortable truth**. Most of the great achievements in aviation would never have happened if analysts were completely in charge. **Concorde. Comet**. Possibly even the **747** (fathered by great romantics like Juan Trippe). The analysts' mandate is to prevent misinvestment and promote profitable enterprises. That rules out an awful lot of good things.

The first time this hit me was on an A380 demo flight a few years ago. As an analyst, the very sight of the plane somehow signified financial waste, misplaced nationalism, and reckless imprudence. But entering the plane, it was hard not to be impressed. As Oscar Wilde said, **nothing succeeds like ex-**

cess. This was one beautiful interior. The flight itself reminded me of how grand travel can be (and I was back in cattle class). If analysts were completely in charge, this impressive machine wouldn't have been built.

Don't get me wrong. I still think the A380 was a bad idea. But that way of thinking is tough to reconcile with my fondness for aircraft. All of my historical favorites — the curious but intriguing **Tri-dent**, the impossibly beautiful **Caravelle**, the technically advanced **L-1011** — had one thing in common. They cost people a lot of money and left a trail of write-offs and layoffs in their wake. If we analysts had been in charge a history buff like me would have a bookshelf lined with about ten books, each describing a bland and homogenous series of money making commodity jets.

The damage done by analysts is even clearer on the military side of the business. Many great fighters wouldn't have happened if analysts were in charge. When Robert McNamara took charge at DoD in 1961, one of his highest priorities was to halt the proliferation of combat aircraft programs and replace them all with the **TFX** (later the F-111), the first major program created by (and arguably for) analysts. Fighter pilots, the ultimate romantics, have been pushing for a return to "pure" fighters ever since. You can see this played out today as the quintessential analyst's aircraft, the **F-35**, displaces the quintessential romantic's aircraft, the **F-22**. And if some hardcore analysts had their way, the F-22 budget would be diverted straight to UAVs. If that happened, you would hear the sound of romantic hearts breaking everywhere.

Boeing's 787 fiasco is the most recent example of how analysts can do as much harm as good. The discipline of the market ensured that Boeing, unlike Airbus with its A380, made only smart product launch decisions. The 787 came with a brilliant business plan that guaranteed strong sales, strong pricing, and strong profits. That pleased analysts. But the same discipline induced Boeing to do something shortsighted with their in-house engineering capabilities. Analysts loved the idea of outsourcing enormous volumes of design work to industrial partners, offloading costs and risk. But **neglecting tribal knowledge to provide better investment leverage and returns** was, in retrospect, a really bad idea. (By the way, if you think the fourth 787 schedule is any more believable than the first, please send me \$1,000 and **I'll triple your money in a week**. You can trust me, too.)

I'm not abandoning my viewpoint and position as an analyst (although I am a closet romantic). But it would be great to reconcile the analyst and romantic viewpoints, and find a balance. Returning to the vile subject that began this letter — Eclipse — I think about the jobless workers who find themselves looking for employment in the midst of an economic crisis, and how that could have been prevented if analysts were in charge. But **Warren Buffett**, the ultimate analyst, the *echt*-analyst, once joked that airlines been such bad investments that someone should have saved the world a lot of money and **shot down Orville and Wilbur Wright** before they pioneered manned flight. You know what? If that kind of analytical thinking had prevailed, I would not have my job...**as an analyst**.

December aircraft updates include a new World Aircraft Overview, the F/A-18, AH-64, Su-27/30, Falcon, A.109, B-2, E-8 JSTARS, E-3/E-737 AWACS, and the Mitsubishi Regional Jet. I'll be on vacation until January 12th. If you need anything logistical, please contact Tim Storey at tstorey@tealgroup.com. Have a great new year. Or any kind of new year that isn't 2008.

Yours, Until I Retire And Become A Romantic,
Richard Aboulafia