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INVESTMENT RESEARCH

HAWAIIAN HOLDINGS INC. | HA

"Ripping the Wave of Transformation"

RECOMMENDATION: *Strong Buy*

Hawaiian Holdings Inc. | Nasdaq: HA

We believe shares of Hawaiian Holdings Inc. ("HA" or "Hawaiian") are grossly undervalued, reflecting a deep misunderstanding of the company's economics. In 2010, HA began investing heavily in growth, implementing a capex program to build additional capacity primarily in support of new international routes. Being that initiating services on routes involves start-up costs, and that from the time service is initiated they take 3 years to reach optimal profitability (i.e., to mature), HA's GAAP margins were negatively impacted; put another way, from 2010 – 2013, when HA was expanding most aggressively, its GAAP financials both understated and obscured its economic potential. With the capex program approaching completion, HA is at an inflection point: As capex decelerates and new routes mature, we expect Hawaiian's GAAP financials to begin reflecting its economic potential. We expect margins to rise in 2014 and free cash flow to turn positive in 2015, opening the door for capital returns to shareholders. In 2016 *alone*, we project the company will generate free cash flow equating to 35% of its current fully diluted market capitalization. Meanwhile, Wall Street analysts and investors appear to be missing the forest for the trees in assuming continued deterioration or the status quo into the future – that HA's current financials represent its future – and use this as justification for valuing it at a depressed multiple. ***We believe Hawaiian stock has an intrinsic value today of $20 per share, >97% above current trading levels. The significant disconnect presented by HA's valuation is sweetened by several near and intermediate-term catalysts we believe will drive share price toward intrinsic value:***

Catalyst Overview

Key Data

Conclusion:		**Strong Buy**
Current Price:	$	10.20
Price Target:	$	20.10
% Upside:		**97%**
Basic Shares o/s		52.4
Dilution, Convert/Hedges		2.7
Dilutive Options & RSUs		1.0
Fully Diluted Shares		56.1
Market Capitalization	$	572.13
Add: Total Debt	$	730.00
Less: Unrestricted Cash	-$	423.00
Enterprise Value	$	879.13
Add: Aircraft Rent @ 7x	$	759.74
Adjusted Enterprise Value	$	1,638.87

Fiscal Year Ended December 31,
$ in millions

Street Consensus*	**2013A**	**2014E**	**2015E**
Sales	$ 2,156	$2,341	$ 2,491
EBITDA	$ 217	$ 254	$ 305
% Margin	*10.1%*	*10.9%*	*12.2%*
EBITDAR	$ 325	$ 351	$ 374
% Margin	*15.1%*	*15.0%*	*15.0%*
EPS	0.88	1.14	1.20

Valuation	**2013A**	**2014E**	**2015E**
EV/Sales	0.4x	0.4x	0.4x
EV/EBITDA	4.1x	3.5x	2.9x
Adj EV/EBITDAR	5.0x	4.7x	4.4x
P/EPS	11.6x	8.9x	8.5x

*Source: CapitalIQ
Note: Prescience estimates diverge from consensus; we believe they understate HA's economic prospects

- **Margins Set to Rise as Growth Slows in 2014, GAAP Financials to Begin Reflecting HA's Potential:** With exception to initiating service to Beijing, HA is pausing new route initiations in 2014. By Q4, only 8% – 10% of HA's routes will be <1 year old. We expect this to translate into improved unit revenues and margin expansion; our assumptions are supported by management expectations.
- **Significant Free Cash Flow Generation on the Horizon:** HA will begin generating FCF when its capex program ends in 2016, opening the door for capital returns to shareholders. In 2016 *alone*, we estimate HA will generate FCF of ~$200m, equating to **~35% of its current market cap.** By simply taking its 2016E net debt/EBITDAR up to the peer average, it would in theory be able to implement share repurchases totaling $500m, equating to **~90% of HA's current market cap!** Even if the company desired to maintain a more conservative balance sheet such that net debt to EBITDA was contained to 1x, it could still initiate a repurchase or dividend program to return ~$200mm over the next 2 years and does not jeopardize its capex plan. While shareholder capital returns of such size may be overly ambitious, we believe that even a modest program of $50mm in 2014 is easily affordable and would be well-received by the market.
- **Management Appears Open to Returning Capital to Shareholders, for the First Time in Years:** Indications from the most recent earnings call suggest that in light of HA exiting a period of heavy investment, management is at least giving thought to the potential of shareholder capital returns – for the first time in years.
- **Prominent Activist/Stock Picker to Join HA's Board this Month:** When HA's February 2014 board meeting takes place, Zac Hirzel, an investor activist with an outstanding track record as a stock picker, will assume his role on HA's board. Being that he has become HA's largest shareholder, with a 10.8% stake, he is likely to be influential; no other board member has a shareholding of any significance, with the exception of HA's CEO, who has a 2.3% stake. Hirzel's involvement reestablishes the linkage between boardroom decision-making and shareholder interests, a bond founded on shared incentives. David Einhorn's fund of funds manager, Greenlight Masters, is an investor in Hirzel's funds, and according to their recent shareholder letter, "Hirzel envisions a number of ways to create shareholder value (at Hawaiian)."
- **Dramatically Undervalued, Heavily Shorted, and Just Plain Unloved:** HA is the most underappreciated among equity in the airline sector: HA is cheaper than every single domestic carrier on every relevant trailing and forward metric, and is one of the cheapest airline equities in the world. HA is among the most highly shorted equities of all airlines. Its share price performance has lagged that of the majority of its peers. Lastly, even the sell-side cannot manage to like HA equity; 5 of 8 analysts rate HA equity at either Neutral (3) or Sell (2).

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Introduction

Hawaiian Holdings Inc, parent company of Hawaiian Airlines, is in the business of transporting people and cargo to, from, and between the Hawaiian Islands. The company classifies its route networks based on the 3 geographic markets served: 1.) Neighbor Islands – includes routes between the Hawaiian Islands; 2.) North America – routes between Hawaii and North America, and 3.) International – routes between Hawaii and the Pacific Rim.

Hawaiian is the largest airline based in Hawaii and the eleventh largest US domestic airline. Compared to other airlines, however, HA's business model is differentiated by its simplicity: While most airlines are network or point-to-point carriers, HA is a destination carrier. It operates with the single mission of making the Hawaii experience possible.

HA has also built a strong brand, leading all U.S. carriers in on-time departures and arrivals for each of the past eleven years (2004 – October, 2013) as reported by the U.S. Department of Transportation; it is consistently ranked among the top domestic carriers by travel publications and consumer rating agencies. [1,2,3]

But, as discussed later in this report, what separates HA most from its airline peers is the sustainable competitive advantage it enjoys in having its infrastructural assets concentrated to a single location. It is one of the lowest cost carriers in the world, enabling it to defensibly generate economic profits and relatively high returns on invested capital.

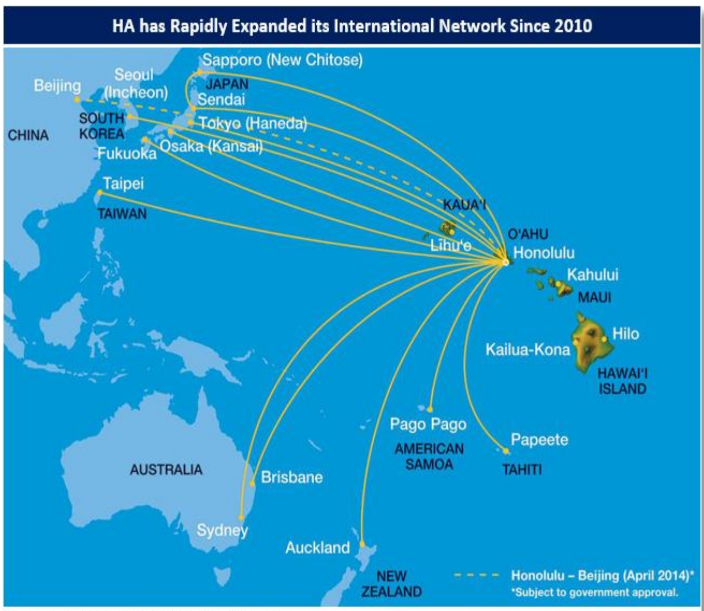
On this basis, since 2010 it has been investing heavily in growth, implementing a capex program to build additional capacity primarily in support of new international routes. Being that initiating services on routes involves start-up costs, and that from the time service is initiated they take 3 years to reach optimal profitability (i.e., to mature), HA's GAAP margins were negatively impacted over the past several years; put another way, from 2010 – 2013, when HA was expanding most aggressively, its GAAP financials both understated and obscured its economic potential.

With the capex program approaching completion, we believe HA is now at an inflection point. As capex decelerates and new routes mature, we expect Hawaiian's margins to rise toward steady-state and for the company to become free cash flow positive, opening the door for capital returns to shareholders.

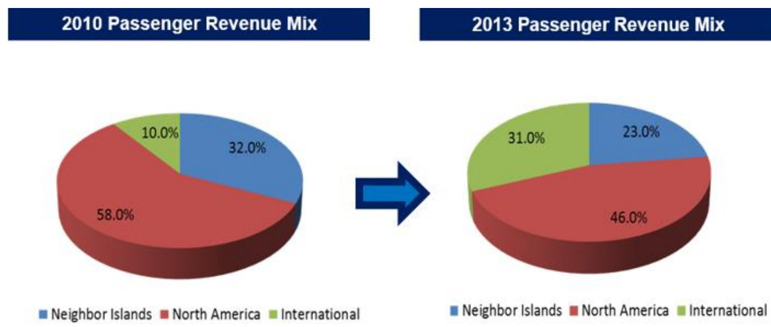
[1] http://www.dot.gov/airconsumer/air-travel-consumer-reports
[2] http://investor.hawaiianairlines.com/phoenix.zhtml?c=82818&p=irol-newsArticle&ID=1837231&highlight
[3] http://www.harrisinteractive.com/NewsRoom/HarrisPolls/tabid/447/mid/1508/articleId/1194/ctl/ReadCustom%20Default/Default.aspx

Transformative Growth Plan Approaches Completion

In 2010, Hawaiian embarked on a multi-year, transformative growth strategy. The initiatives include growing revenue, decreasing costs, expanding existing markets, and initiating service on new international routes to gain exposure to high-growth markets in the Pacific Rim, primarily countries in Asia.[4] In just three years, HA has added 10 new international routes to six countries and substantially diversified its revenues. It now serves more international than US mainland destinations.



*Source: Hawaiian Airlines Investor Day Presentation (10/29/2013)

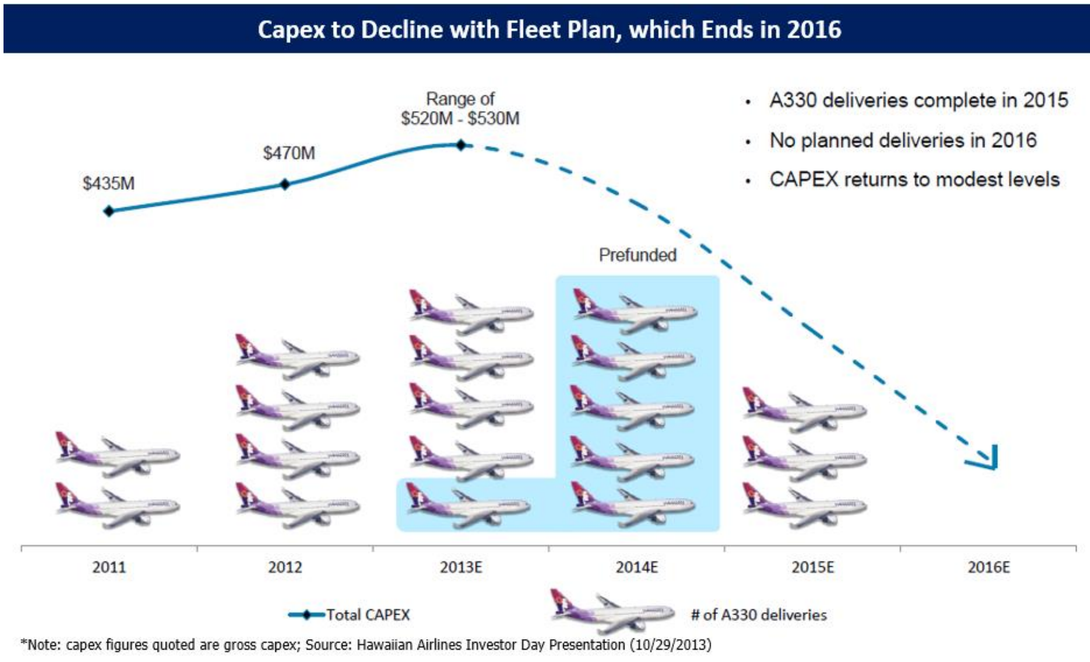


Significant Free Cash Flow Generation on the Horizon

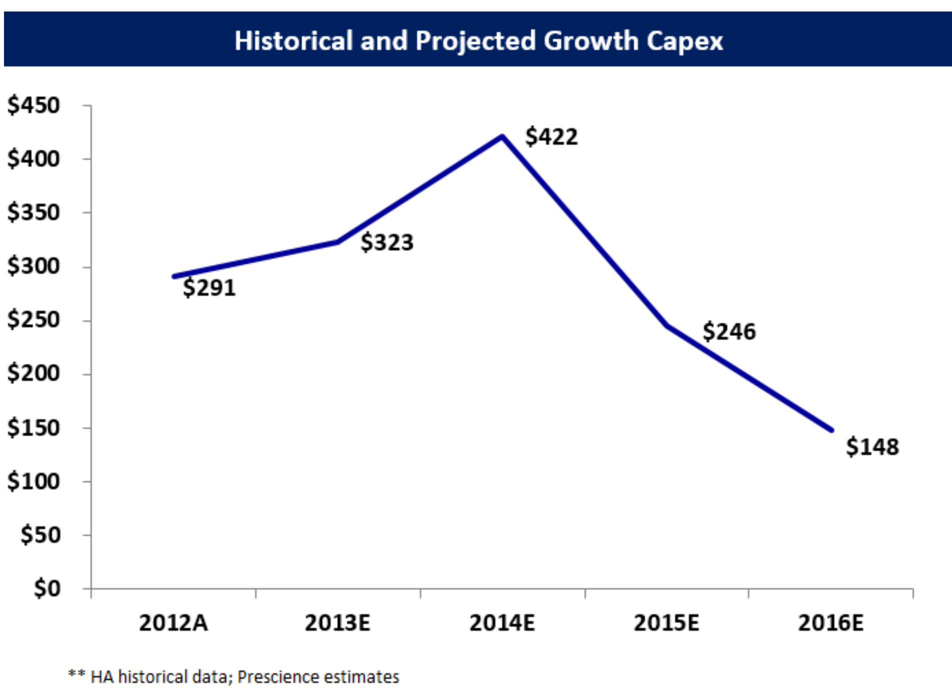
HA's international route expansion necessitated the purchase of Airbus A330s to replace 767s, which neither had the range or the underlying economics to make the flights to Asia work. By 2016, the capex program for purchasing the necessary aircrafts will be complete, at which time we expect Hawaiian to begin generating significant free cash flow, opening the door for capital returns to shareholders.

Hawaiian is expected to complete the acquisition of 13 new Airbus A330's originally ordered in 2010. In 2014 the company will take delivery of five A330s, all prefunded. The company has arranged debt financing through a $445m EETC (Enhanced Equipment Trust Certificate) facility, a common financing structure for securitizing aircraft leases. In 2015, HA will take delivery of three more A330s. We assume that the 2015 deliveries will be funded with 70% debt financing and expect Hawaiian to be able to secure another $172m in debt financing. In 2016, we do not model any debt financing and assume growth capex of $148m is funded by our 2016E cash flow from operations of $369m.

[4] http://investor.hawaiianairlines.com/phoenix.zhtml?c=82818&p=irol-newsArticle&ID=1400360&highlight=



The chart that follows demonstrates HA's historical and expected net growth capex. (Note that capex in the chart displayed above is gross capex.) We estimate that between 2014 and 2016, net growth capex (gross capex less debt financing) will total $815m. As shown, the capex starts to decline sharply as the number of planes purchased declines.



<u>In 2016 *alone*</u>, we project the company will generate free cash flow of ~$200m, equating to <u>35% of its current market capitalization.</u> It is worth noting that there is significant committed capex in 2017, but financing aircraft purchases at the historical average of 70% debt should mean that the company will still have plenty of cash to complete these purchases since the capex net of debt would be approximately $160mm (or less than ½ of estimated EBITDA for that year).

On our projections, HA will have a 2016 cash balance of ~$820m versus debt of ~ $1.1B, resulting in a gearing of ~2.3x net debt to EBITDAR. The average net debt to EBITDAR of airlines is 3x, meaning that at that point, HA could pay out up to $500mm before having its net debt to EBITDAR ratio equate to the peer average. **In other words, in 2016 HA should have the capability to return cash to shareholders in the form of share repurchases or dividends in an amount <u>equating to ~90% of its current market cap!</u>** Even if the company desired to maintain a more conservative balance sheet such that net debt to EBITDA was contained to 1x, it could still initiate a repurchase or dividend program to return ~$200mm over the next 2 years without jeopardizing its capex plan.

While shareholder capital returns of such size may be overly ambitious, we believe that even a modest program of $50mm in 2014 is easily affordable and would likely be well-received by the market.

This is not to say that we think Hawaiian should stop growing its fleet or number of routes, but to point out the *potential* for returning cash, which is deserving or due consideration by investors.

Management Appears Open to Capital Returns – For the First Time in Years

Investors may note that HA has had the capability of repurchasing shares or paying dividends for some time. While this is true, the company was exposed to significant risks as it navigated its capex program. It was firmly committed to plane purchases and had to think about the potentialities of a seizure in debt markets or route underperformance, necessitating the prioritization of balance sheet liquidity. For years, management has responded to incessant shareholder and analyst questions about the potential for buybacks with the same answer:

> *"We're clearly mindful (of the) headlines about macroeconomic (uncertainty). Although we have seen none of that in our market places, we wanted to make sure that in the event that there is a dip that really, everybody has been expecting for the last 4 years, come about that we have a cash cushion …At the same time … we are mindful that in the next probably 1.5 years, 2 years, we've got quite a load of additional aircraft coming on. We've got some aircraft leaving the fleet too. So I think those are some of the things that influence our thinking… We're not looking around to buy back stock or to do anything dramatic, because as Mark said, we're growing…"*
>
> – HA CFO Scott Topping on the 10/23/12 call
>
> *"We're very mindful of our balance sheet as we continue to execute our growth plans. We feel a buffer is important as we enter into new markets, buy new airplanes and take the risks of our growth strategy. And to guard against surprises, we keep a high level of liquidity."*
>
> – HA CFO Scott Topping on the 9/6/12 call

The company is now substantially de-risked. Management has been clear that HA is at the tail end of its capex program, and debt financing is already in place for all but two of the A330s to be purchased prior to 2016.

When asked about a buyback on HA's Q4'2013 earnings call, management deviated from the response shareholders have come to expect, potentially giving a subtle indication that for the first time in years, they are open to the idea of returning capital to shareholders.

> *"We are now in a period of much slower growth and it is absolutely the case that we've got to improve our maturities markets and so on. All of which will -- should improve our return on invested capital. What it does to our cash balance and how we're going to manage that is obviously something -- it'd be inappropriate for me to speculate about on this call. But we do recognize that we're coming out of a period of heavy investment and should be into a period of generating some free cash flow."*
>
> – HA CEO Mark Dunkerly on the 1/28/14 call

Our notion is supported by the company's recent willingness to appoint an activist investor to its board.

Prominent Activist Investor Appointed to Board of Directors

This month, when Hawaiian's February board meeting takes place, Zac Hirzel, an investor activist with an outstanding track record as a stock picker, will assume his role on HA's board. Through the funds he manages, he has become HA's largest shareholder, owning 10.8% of the company. His close involvement is of clear benefit to shareholders and increases the likelihood of the implementation of share repurchases and/or a dividend.

Hirzel's track record is reflected upon in David Einhorn's fund of funds' ("Greenlight Masters") year-end 2013 letter to investors. Greenlight Masters is invested in Hirzel's funds. The letter states that Hirzel's long investments have returned in excess of 25% gross annually, and it directly references his investment in HA:

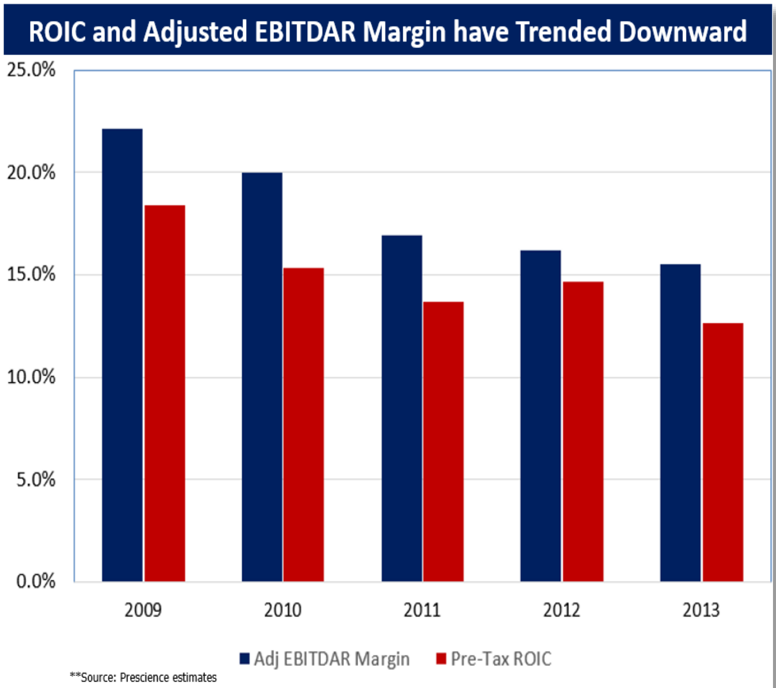
> *"Hirzel… filed its first 13D on Hawaiian Airlines (HA) last year, where Hirzel envisions a number of ways to create shareholder value."*
>
> – Greenlight Masters 2013 Year End Letter to Investors (1/21/2014)

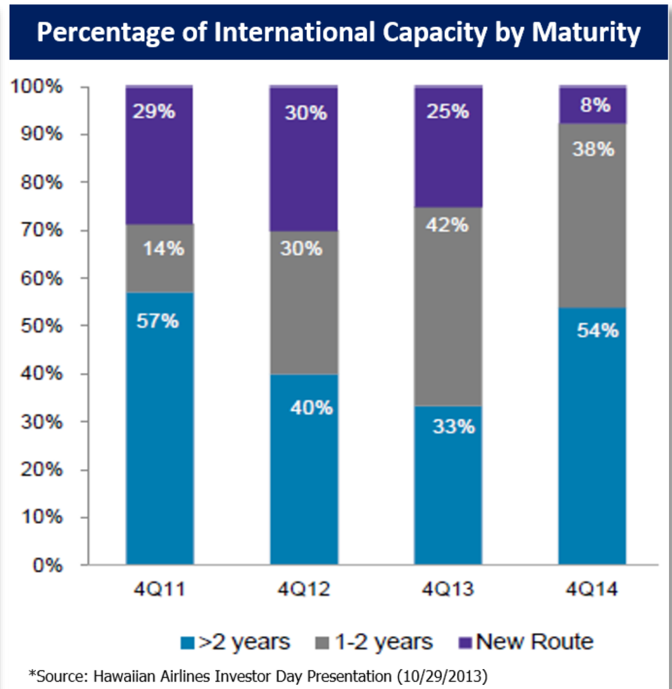
With the exception of CEO Mark Dunkerly, who owns 2.4% of HA's stock, Hirzel is the only significant shareholder on the board. No other member holds a substantive stake in the company. Having credibility lent by his track record for successful investing and the size of his holdings, Hirzel's ideas for creating shareholder are unlikely to go ignored.

Margins Set to Rise in 2014; Strong Results to Command Investor Reassessment

HA's margins and ROIC have trended downward as HA's invested in growth, we believe playing a large role in investors' loss of faith in the company. This is because new routes are less profitable, generally maturing over a 3 year period. With the exception of initiating service to Beijing, HA is pausing its route initiation program in 2014 to focus on the maturation of new routes established over the prior 3 years. We expect this to translate into improved RASMs and that the company will report higher margins and ROIC in 2014, which the sell-side appears to have overlooked.

Per the graphic below at right, in Q4'13, a full 2/3 of HA's international capacity was either in the <1 year or 1 – 2 year category. As the company slows its growth this year, this will quickly change. By the fourth quarter of 2014, only 8% – 10% of HA's routes will be in the <1 year old bucket.





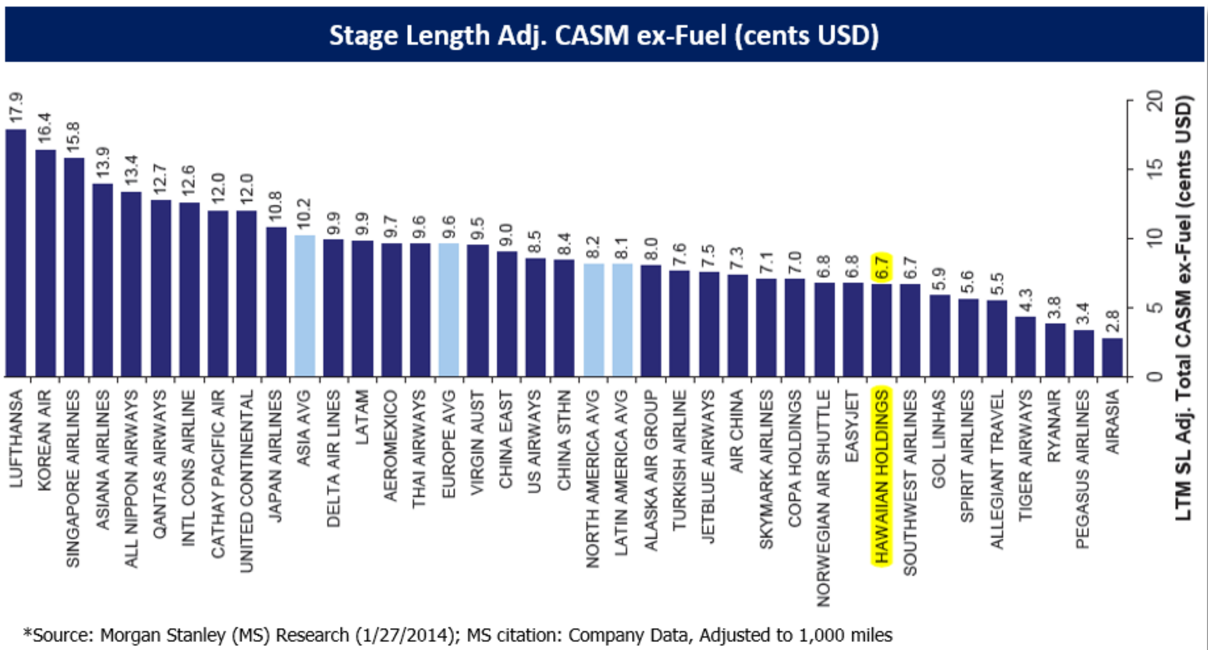
Our assumptions are supported by management's expectations:

> *"The past 3 years have been a period of rapid expansion at Hawaiian. We remain solidly profitable, adjusted for non-routine items, while launching service to 10 new cities. We're now entering a different phase in our evolution. Capacity will start to slow, and there will be fewer new route launches. Our efforts are going towards maturing the ones we have so recently started…*
>
> *… our returns are expected to improve. And there's a very good case for that. And to understand it, what I'd like to do is describe this inflection point, give you some insight into it. We recognize that the fleet plan is what is driving the growth to more moderate levels. We understand that investment is falling. There are certain other costs that when you move from this period of rapid growth to a period of moderating growth, those costs tend to fall away, in some cases, and there are inefficiencies with rapid growth. We're going to expect that.*
>
> *As Peter laid out, we have momentum around our unit revenues as these fairly large clutch of new routes in the international business are coming to maturity… So that's the tailwind. If you wrap all of this in good cost control, we have all of the elements here that should point to a higher return on investment."*
>
> – Management on the 10/22/13 call
>
> *"We think that there'll be expanding margins – which, if there are not if we don't see big sort of environmental effects out there in the markets in which we compete – within our ambition for 2014…*
>
> *…we see cost control and we see optimism on the revenue line that would logically lead to that conclusion (increasing margins in 2014)."*
>
> – Management on the 1/21/14 call

An Airline Able to Sustainably Compound Shareholder Wealth

We believe HA enjoys a defensible competitive advantage, insulating its ability to produce sustainable economic profits. Because HA is a destination carrier, its primary infrastructural assets are concentrated to one market, as are the fixed costs associated with them. We estimate these costs – which relate to infrastructure for aircraft maintenance, terminals, gates and runways, and management and overhead expenses – to make up ~50% of HA's expense structure. Hawaiian is the beneficiary of economies of concentration; no other airline approaches its level of concentration of fixed costs in Hawaii. As it adds more routes and its volumes grow, these costs are leveraged, resulting in declining unit costs which lends the company more flexibility than any other airline in setting ticket prices to and from Hawaii.

Based on its advantages, Hawaiian is positioned as <u>the lowest cost airline</u> flying to/from Hawaii and one of the lowest cost airlines in the United States. It is also one of the lowest cost airlines <u>in the world</u>.



Its cost advantages have enabled it to be a dominant force amongst its peers.

> ***"We attract the highest fares on costs which are equal to or lower than those of any of our main competitors."***
>
> HA CEO Mark Dunkerley, Q3'12 Earnings Call

HA is the #1 carrier flying between Hawaii and North America with a seat share of ~26%. HA commands a ~55% seat share in and out of Honolulu International airport, with no other carrier's seat share exceeding 10%.[5]

The fortitude of Hawaiian's competitive position is a function of the symbiotic interchange between its Neighbor Island and North America routes. Management has effectively built a time-tested moat that insulate the near-monopoly it enjoys on inter-island travel; its dominance in this market is absolute, with its seat share exceeding 88%![6]

HA's Crown Jewel – A Defensible Near-Monopoly on Inter-Island Travel

*Source: Hawaiian Airlines Investor Day Presentation (10/29/2013)

Because of the absence of highways, trains, and boat service between the islands, HA's network performs the essential function of connecting Hawaii's major population centers. It is effectively the highway system in the state of Hawaii, evidenced by the disproportionate amount of traffic on these routes relative to what would be expected for a state with a population of 1.3 million. Demand is relatively inelastic and when met with Hawaiian's monopoly on supply, the recipe makes for economic profits.

Hawaiian's North America routes (primarily to the West Coast), on the other hand, are some of the most fiercely competitive in the US. Prices on the routes are highly subject to momentary changes in capacity, but given prices are already slashed to the bone, they are somewhat stable. Our research indicates that taken as a whole, Hawaiian flies them at cost, which would mean other airlines are taking losses. We believe Hawaiian flies these routes to insulate its profitable inter-island network, effectively keeping competing airlines from establishing a foothold in Hawaii; furthermore, Hawaiian's West Coast routes pull a high number of passengers into its inter-island network.

Hawaiian's capex program builds on this foundation, adding incrementally profitable routes in less competitive markets that also feed its Neighbor Island segment.

[5] http://www.transtats.bts.gov/carriers.asp?pn=1
[6] http://www.sec.gov/Archives/edgar/data/1172222/000110465913041108/a13-10922_4fwp.htm

China Offers Potential for Long Term Growth

One of the biggest opportunities for further growth is China. HA commenced ticket sales for its first flight between mainland China and Honolulu on November 26th, 2013, with the route expected to begin service out of Beijing on April 16th, 2014.[7]

Based on our analysis, this route could result in significant future growth opportunities. Until this month (January, 2014) there were no direct flights from Beijing to Hawaii. Yet, despite this, some 130,000 Chinese visited Hawaii last year, up 20% from a year earlier, according to the Hawaii Tourism Authority.[8] More broadly, there were only 3 flights *per week* between the PRC and Hawaii, operated by China Eastern and coming out of Shanghai. In contrast, there are 18 flights *daily* between Japan and Hawaii.

Air China commenced a Beijing to Hawaii route on January 14, 2014. According to a Wall Street Journal article, Air China officials say they see plenty of demand for the new route. He Zhigang, managing director of Air China's marketing department, *"We are really optimistic about the flights and we believe the load factor can reach more than 80% this year."*[9]

According to HA CEO Mark Dunkerley (via USA China Daily), "Hawaiian Airlines is interested in going to many cities in China, and its network will expand if traffic from Beijing is encouraging… If those encouraging numbers emerge, however, the first thing the carrier will do is add more flights onto the Beijing-Honolulu route."

We also believe that HA will be a choice carrier as we believe it offers a premium product to both Air China and China Eastern. HA consistently wins awards for service, quality and on time performance.[10] Recent initiatives include providing all passengers with iPad minis to offer movies, games and other entertainment.[11]

Dramatically Undervalued, Heavily Shorted, and Just Plain Unloved

HA's valuation appears completely dislodged from the strength of its business. HA stock is cheaper than every single domestic airline **on every relevant trailing and forward metric** and is one of the cheapest in the world.

[7] http://investor.hawaiianairlines.com/phoenix.zhtml?c=82818&p=irol-newsArticle&ID=1880374&highlight=
[8] http://blogs.wsj.com/chinarealtime/2014/01/22/chinese-tourists-say-aloha-to-hawaii/
[9] Ibid.
[10] http://www.hawaiianairlines.com/aboutus/pages/awards-and-recognition.aspx
[11] http://investor.hawaiianairlines.com/phoenix.zhtml?c=82818&p=irol-newsArticle&ID=1850533&highlight=

Hawaiian is One of the Most Undervalued Airlines in the World

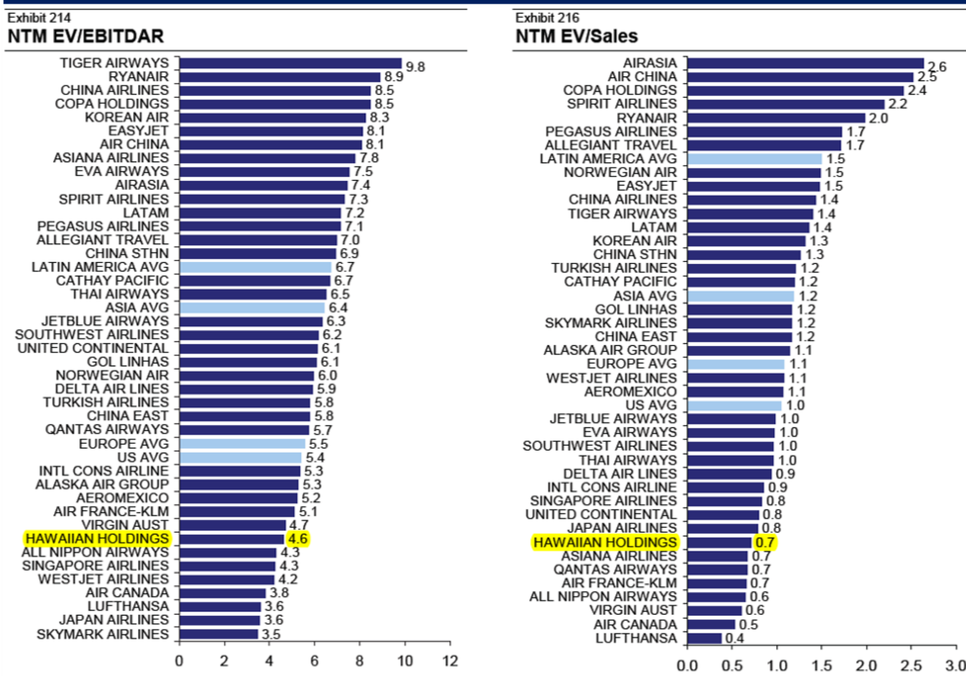
	Adj EV/EBITDAR			Adj EV/Sales			P/E Ratio		
	2013	2014	2015	2013	2014	2015	2013	2014	2015
US Carriers									
Alaska Air Group	5.9x	5.3x	5.1x	1.2x	1.1x	1.1x	15.1x	12.7x	11.7x
Delta Airlines	7.0x	5.9x	5.5x	1.0x	0.9x	0.9x	10.4x	12.5x	10.9x
United Continental	7.3x	6.2x	5.4x	0.8x	0.8x	0.8x	17.1x	11.1x	8.8x
Allegiant Travel	8.2x	7.0x	6.3x	1.9x	1.7x	1.6x	21.9x	17.2x	14.8x
Jetblue Airways	7.1x	6.4x	5.6x	1.1x	1.0x	0.9x	18.2x	13.7x	11.3x
Southwest Airlines	6.5x	6.2x	5.8x	1.0x	1.0x	0.9x	19.0x	16.5x	14.6x
Spirit Airlines	8.6x	7.4x	5.2x	2.5x	2.2x	1.8x	21.2x	17.1x	14.3x
Max	**8.6x**	**7.4x**	**6.3x**	**2.5x**	**2.2x**	**1.8x**	**21.9x**	**17.2x**	**14.8x**
Average	**7.0x**	**6.1x**	**5.6x**	**1.3x**	**1.2x**	**1.1x**	**16.9x**	**13.7x**	**11.9x**
Min	**5.9x**	**5.3x**	**5.1x**	**0.8x**	**0.8x**	**0.8x**	**10.4x**	**11.1x**	**8.8x**
Hawaiian Airlines	**5.1x**	**4.7x**	**4.5x**	**0.7x**	**0.7x**	**0.7x**	**12.4x**	**8.8x**	**8.5x**
Asian / Pacific Carriers									
Air China	8.6x	8.1x	7.5x	2.7x	2.5x	2.4x	16.1x	13.4x	10.4x
Cathay Pacific Air	8.1x	6.7x	6.1x	1.3x	1.2x	1.1x	24.9x	13.2x	10.0x
China East Airline	6.9x	5.8x	5.4x	1.3x	1.2x	1.1x	9.9x	8.8x	7.5x
China Sthn Airline	7.6x	7.0x	6.4x	1.4x	1.3x	1.2x	11.4x	9.5x	8.7x
China Airlines	9.6x	8.5x	8.5x	1.5x	1.4x	1.4x	41.8x	18.5x	12.2x
EVA Airways	8.2x	7.5x	7.6x	1.0x	1.0x	1.0x	21.1x	17.4x	19.3x
Asiana Airlines	12.6x	7.9x	6.8x	0.7x	0.7x	0.6x	-	26.3x	10.2x
Korean Air	10.0x	8.3x	7.8x	1.4x	1.3x	1.2x	-	24.7x	11.1x
Sinagapore Airlines	4.5x	4.3x	4.0x	0.8x	0.8x	0.8x	29.7x	22.3x	16.5x
Tiger Airways Airasia	9.1x	10.0x	8.0x	1.3x	1.4x	1.3x	-	-	-
AirAsia	8.1x	7.5x	6.8x	2.9x	2.7x	2.4x	9.7x	8.2x	7.2x
Thai Airways	8.4x	6.6x	5.9x	1.0x	1.0x	0.9x	-	19.2x	8.1x
Qantas Airways	4.3x	5.8x	4.7x	0.7x	0.7x	0.6x	37.4x	-	-
Virgin Aust	5.3x	4.7x	4.1x	0.7x	0.6x	0.6x	-	-	46.2x
Japan Airlines	3.2x	3.6x	3.5x	0.8x	0.8x	0.8x	5.7x	6.9x	6.8x
All Nippon Airways	3.7x	4.3x	3.9x	0.7x	0.7x	0.6x	19.0x	39.6x	22.5x
Skymark Airlines	4.6x	3.4x	3.6x	1.1x	1.2x	1.1x	7.1x	4.9x	5.9x
Max	**12.6x**	**10.0x**	**8.5x**	**2.9x**	**2.7x**	**2.4x**	**41.8x**	**39.6x**	**46.2x**
Average	**7.2x**	**6.5x**	**5.9x**	**1.2x**	**1.2x**	**1.1x**	**19.5x**	**16.6x**	**13.5x**
Min	**3.2x**	**3.4x**	**3.5x**	**0.7x**	**0.6x**	**0.6x**	**5.7x**	**4.9x**	**5.9x**
Hawaiian Airlines	**5.1x**	**4.7x**	**4.5x**	**0.7x**	**0.7x**	**0.7x**	**12.4x**	**8.8x**	**8.5x**

*Morgan Stanley ("MS") estimates as of 1/27/14; MS definitions:

Adj. EV = Mkt Cap + Adj. Net Debt, where b/s metrics are a wavg of annual data to target the most recent prd

Adj. Net Debt includes capitalized operating leases, based on the 7x convention

HA is *the* Cheapest Domestic Airline and One of the Cheapest in the World



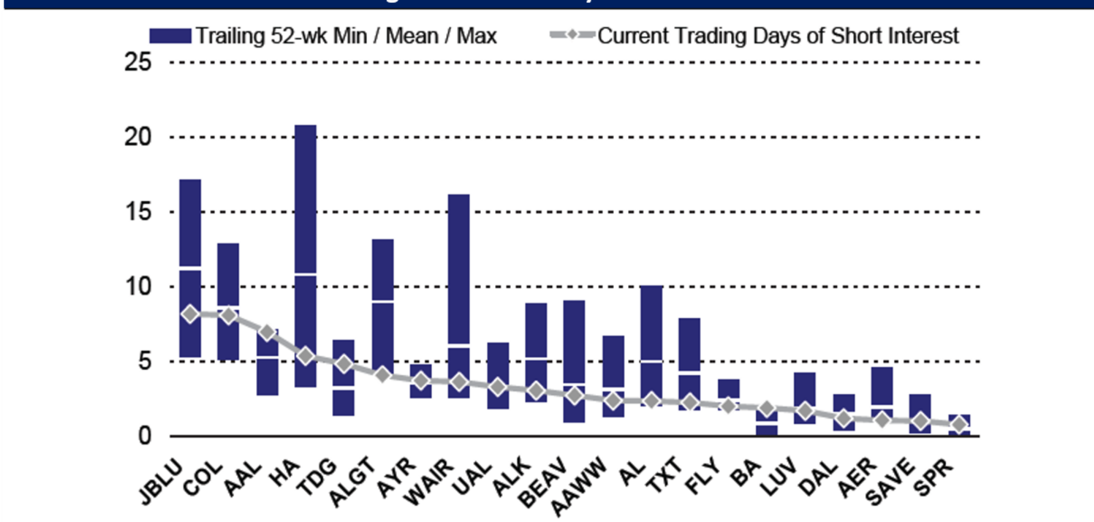
Source: Company Data, Morgan Stanley Research

Source: Company Data, Morgan Stanley Research

**Source of Charts: Morgan Stanley Research – Airlines/A&D; *Co-Pilot: Mid-EPS Update: Stronger For Longer & Aftermarket Surprises*. Jan 27, 2014

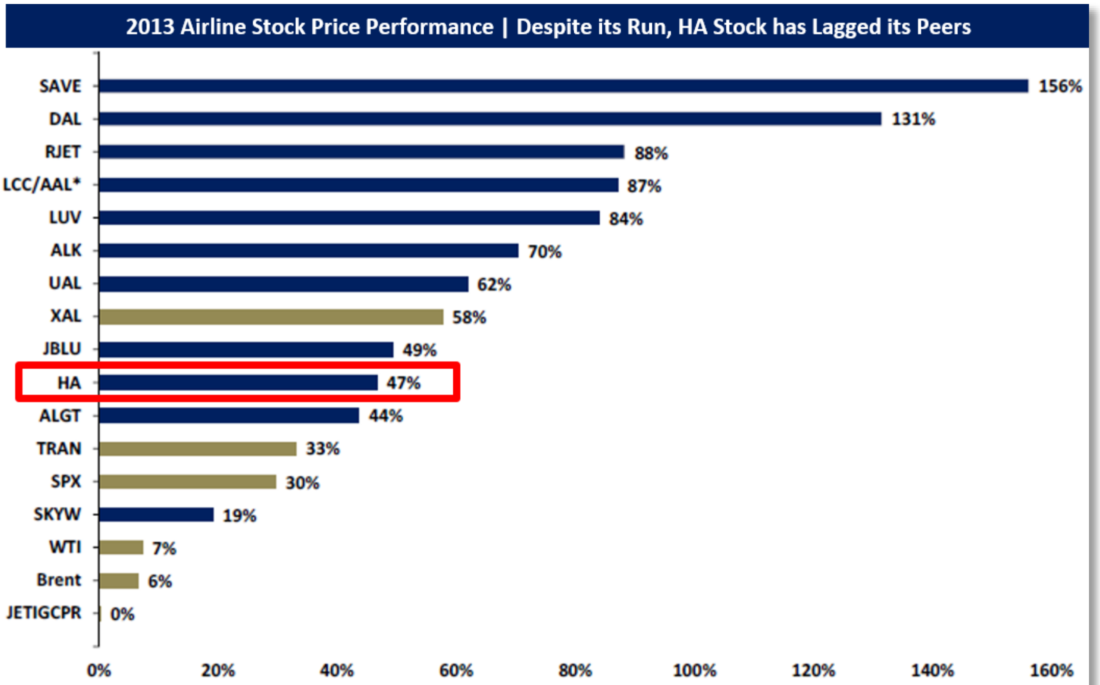
Its stock is the 4th most highly shorted of all domestic carriers' and its shares have lagged airline peers in price performance.

HA Stock is Among the Most Heavily Shorted in the Airline Sector



Source: Morgan Stanley Research, Thomson Reuters; *Short Interest Days outstanding is calculated as the current Short Interest Shares Outstanding / the Avg Daily Volume over the last month; *Note: JBLU, and UAL all have convertible debt outstanding which can increase the level of short interest

**Source of Chart: Morgan Stanley Research – Airlines/A&D; *Co-Pilot: Mid-EPS Update: Stronger For Longer & Aftermarket Surprises*. Jan 27, 2014



Note 1: return performance does not include dividends.
Note 2: LCC shares converted to AAL shares on a one-for-one basis, effective on merger close (December 9, 2013).
Source: Deutsche Bank Airline Research.
**Source of Chart: Deutsche Bank Markets Research – Airlines Industry Outlook 2014: *Airlines Becoming an "Investable" Sector.* Jan 9, 2014

Even sell-side analysts have a hard time liking the equity, with 6 of the 9 who cover it having it at either Neutral (3) or Sell (3). We believe market participants are missing the forest for the trees. Having been lulled to sleep in the midst of HA's multi-year capex program, they assume the current financials represent the company's future, and value it in accordance with its current, depressed multiple. As a group, they inherently assume there will be no multiple expansion, which of course will take place when its economics are reflected by its financials – i.e., when it's too late. To our knowledge, every sell-side analyst that covers the company makes projections that span only the next 2 years, through 2015. Their models give no consideration to 2016, when HA's routes will by and large have matured, and HA is likely to reap peak reward from the hundreds of millions of dollars of capital it invested toward growth.

Valuation

In 2016, HA will have completed its transformative capex program and the majority its new routes will have matured. As such, we base our valuation on its 2016E financials, which are more reflective of the steady-state economics of its business.

Hawaiian trades at 3.4x our 2016E adjusted EBITDAR of $683m. With airlines typically trading at 5x - 7x forward Adjusted EV/EBITDAR, HA is severely under-appreciated. The current valuation fails to reflect the attractiveness of its steady-state economics and defensibility its competitive position.

At 5x our 2016 EBITDAR estimate, Hawaiian stock has an intrinsic value today of $20 per share, >97% above current trading levels. With several near and intermediate-term catalysts likely to drive the convergence of stock price to intrinsic worth, at current levels HA equity represents a uniquely compelling opportunity.

Valuation	
$ in mm except per share amounts	
Share Price	$10.20
Fully Diluted Shares o/s(1)	70.1
Equity Market Cap	$ 715
Add: Total Debt	$ 1,078
Less: Excess Cash(2)	$ (388)
Enterprise Value	**$ 1,405**
Add: Aircraft Rent @ 7x	1,318.0
Adjusted Enterprise Value	**2,723.2**
2016 EBITDAR Multiple	**5.0 x**
Share Price	**$20.10**
% Upside	**97.1%**

(1) adjusts for dilution from convertible note, hedges, & warrants
(2) assumes cash necessary for working capital purposes @15% of revenue
*Note: valuation incorporates 2016 estimates for EBITDAR & cap structure

Our valuation gives HA credit only for its 2016E excess cash balance, based on the assumption that cash in the amount of 15% of revenue is necessary for working capital purposes.[12] On the other hand, Wall Street airline analysts' valuation computations, by convention, give companies the benefit of their entire cash balances. **If we were to value HA on this basis, our estimate of intrinsic value increases to $26.25, for upside of >155% from the current market price.**

Pro Forma Operating Metrics

Our base case assumes ASM growth in line with management guidance. Specifically, we assume 5.5% 2014E ASM growth, which is at the midpoint of the most recently guided range (4%-7%). From 2015 through 2016 ASM growth decelerates as international routes mature. Our conservative assumptions include a constant load factor and modest yield growth.

Fuel Prices as a Macro Tailwind

In addition, we model a slight increase in fuel expense in 2014 to 318 cents/gallon, and flat-line our fuel expense estimate for 2015 and 2016 at 320 cents in accordance with Wall Street consensus estimates. Economists are forecasting US and global GDP growth of 2.8% and 3.6%.[13] While historically GDP growth has driven both increasing demand for air travel and rising jet fuel prices, increased global oil supply from US shale production has weighed on prices and disrupted this relationship. We have already seen the effects of this in 2013, with increased travel demand resulting in many airlines reporting significant growth in net income and net margins. We note that HA does hedge its fuel price risk, but on a rolling basis, resulting in some uncertainty as to what realized fuel cost will be.

[12] http://phx.corporate-ir.net/External.File?item=UGFyZW50SUQ9MjA4MjM3fENoaWxkSUQ9LTF8VHlwZT0z&t=1
[13] Source: Goldman Sachs

Key Forecast Drivers			
$ in mm except per share amounts	2014E	2015E	2016E
Selected			
ASM Growth	*5.5%*	*4.5%*	*4.0%*
Capex	471.5	265.6	167.8
Load Factor (%)	*80.0%*	*80.0%*	*80.0%*
Yield (¢)	15.1	16.0	17.0
Fuel Price (¢/gal)	318.0	320.0	320.0

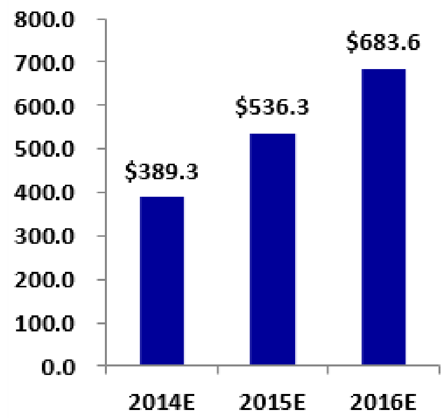
Income Statement			
$ in mm except per share amounts	2014E	2015E	2016E
Passenger	2,135.5	2,364.6	2,612.9
Other	229.0	246.2	264.7
Other Growth	7.5%	7.5%	7.5%
Total Revenue	**2,364.6**	**2,610.9**	**2,877.6**
Salaries & Benefits	458.7	438.6	489.2
% Revenue	*19.4%*	*16.8%*	*17.0%*
Aircraft Fuel	747.7	774.4	799.2
Cost/ASM (¢)	4.23	4.19	4.16
Aircraft Maintenance	226.3	236.5	245.9
Cost/ASM (¢)	1.28	1.28	1.28
Aircraft Rentals	111.4	181.0	188.3
Cost/ASM (¢)	0.63	0.98	0.98
Rentals & Landing Fees	83.1	145.9	151.8
Cost/ASM (¢)	0.47	0.79	0.79
Commissions	139.5	154.0	169.8
% Revenue	*5.9%*	*5.9%*	*5.9%*
Aircraft & Passenger Servicing	125.5	131.2	136.4
Cost/ASM (¢)	0.71	0.71	0.71
D&A	100.8	145.9	151.8
Cost/ASM (¢)	0.57	0.79	0.79
Other Airline	194.5	194.0	201.7
Cost/ASM (¢)	1.10	1.05	1.05
Total Operating Expenses	**2,187.4**	**2,401.6**	**2,534.1**
Adjusted Operating Income	**177.2**	**209.3**	**343.5**
Adj EBITDA	**278.0**	**355.2**	**495.3**
EBITDA Margin	*11.8%*	*13.6%*	*17.2%*
Adj EBITDAR	**389.3**	**536.3**	**683.6**
EBITDAR Margin	*16.5%*	*20.5%*	*23.8%*
Interest Expense	(49.9)	(60.7)	(60.5)
Interest Rate	*5.5%*	*5.5%*	*5.5%*
Interest Income	4.7	5.9	7.4
Interest Rate	*1.0%*	*1.0%*	*1.0%*
Total Other Income	**(45.1)**	**(54.7)**	**(53.1)**
Pretax Income	**132.1**	**154.5**	**290.4**
Income Tax (benefit)	52.8	61.8	116.2
Tax Rate	*40.0%*	*40.0%*	*40.0%*
Net Income	**79.2**	**92.7**	**174.3**
Shareholder Information			
Diluted Shares Outstanding	61.2	64.4	70.1
Diluted Earnings Per Share	$1.29	$1.44	$2.48

PRESCIENCE

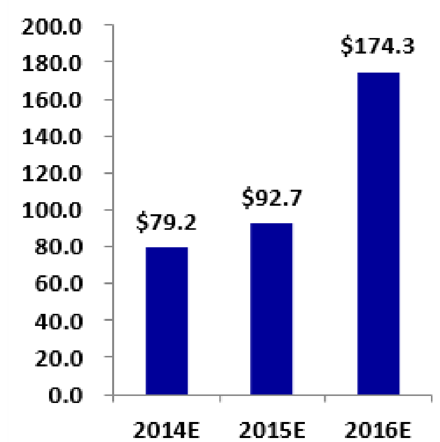
Operating Metrics			
$ in mm except per share amounts	2014E	2015E	2016E
RPMs	14,142.4	14,778.8	15,370.0
ASMs	17,678.0	18,473.5	19,212.5
ASM Growth	*5.5%*	*4.5%*	*4.0%*
Load Factor (%)	*80.0%*	*80.0%*	*80.0%*
Yield (¢)	15.10	16.00	17.00
Yield Growth	*6.2%*	*6.0%*	*6.3%*
RASM (¢)	13.38	14.13	14.98
RASM Growth	*4.0%*	*5.7%*	*6.0%*
PRASM	12.08	12.80	13.60
PRASM Growth	*4.2%*	*6.0%*	*6.3%*
CASM (¢)	12.37	13.00	13.19
CASM Growth	*2.5%*	*5.1%*	*1.5%*
CASM ex-Fuel (¢)	8.14	8.81	9.03
CASM ex-Fuel (¢) Growth	*3.1%*	*8.2%*	*2.5%*
Fuel Price (¢/gal)	318.0	320.0	320.0
Fuel Gallons (mm)	235.1	242.0	249.8
Fuel Gallons per ASM	0.0133	0.0131	0.0130

Free Cash Flow			
$ in mm except per share amounts	2014E	2015E	2016E
Cash Flow from Operations			
Net Income	79.2	92.7	174.3
D&A	100.8	145.9	151.8
Δ Operating Working Capital	18.9	20.9	23.0
Δ Other Operating Cashflows	20.0	20.0	20.0
Adjusted Cash Flow from Operations	**218.9**	**279.6**	**369.1**
Less: Growth Capex	421.5	245.6	147.8
Less: Non-Aircraft Related Capex	50.0	20.0	20.0
Free Cash Flow	**(252.6)**	**14.0**	**201.2**
Debt Issuance / (Discr. Repayment)	368.4	171.9	0.0
Required Debt & Lease Payments	(15.0)	(46.5)	(45.0)
Net Change in Cash	**100.9**	**139.4**	**156.2**

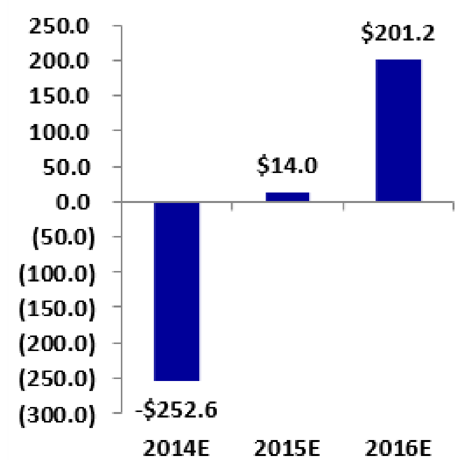
EBITDAR



Net Income



Free Cash Flow



Appendix A – Airline Glossary

ASM - Available Seat Miles – one airplane seat flying one mile, ASM is a measure of capacity which is calculated by multiplying the total number of seats available for transporting passengers by the total number of miles flown during a reporting period.

CASM – (Operating) Cost per Available Seat Mile - the amount of operating cost incurred per available seat mile during a reporting period. Also referred to as unit cost.

CASM Ex-Fuel – the amount of operating cost incurred per available seat mile during a reporting period, excluding aircraft fuel expense.

EBITDAR – a measure of the airline's cash pre-tax earnings. EBITDAR is calculated by adding pretax income plus net interest expense plus depreciation and amortization plus rental expense.

Enterprise Value – calculated by adding market value of equity plus preferred equity at liquidation value plus minority interest plus long-term debt plus capital leases plus operating leases (capitalized at 7x) and subtracting out cash and marketable securities.

Passenger Load Factor – a measure of aircraft utilization which is calculated by dividing RPMs by ASMs for a reporting period.

Passenger Mile Yield - amount of passenger revenue earned per revenue passenger mile during a reporting period.

Passenger Revenue per ASM - The amount of passenger revenue earned per ASM during a reporting period. Passenger RASM is also referred to as 'Passenger Unit Revenue'.

RASM – (Operating) Revenue per Available Seat Mile - The amount of operating revenue earned per available seat mile during a reporting period, also referred to as unit revenue.

RPM – Revenue Passenger Mile - One revenue-paying passenger transported one mile. RPMs are calculated by multiplying the number of revenue passengers by the number of miles they are flown for the reporting period.

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