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Book Reviews

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BOOK REVIEWS

THE AIR LINES. A Pamphlet issued by Stern, Wampler & Co. Inc. Chicago: 1940. Pp. 14.

HANDBOOK OF THE AIR TRANSPORT INDUSTRY. Issued by J. S. Bache & Co. New York: 1940. Pp. 48.

One of the major market phenomena of the last few years has been the failure of air transport stocks to keep pace market-wise with the mounting enthusiasm manifested by the public at large in the industry. Though at one time the stocks of air transport holding companies were a subject of speculative buying, largely a result of trading by insiders, there has been no sustained trading since the enforced reorganization of companies as operating units subsequent to the 1934 Congressional inquiry into airmail contracts.

Laggardness of the investing public may be contrasted with the sharpened interest of the general public in air transportation—an interest which is exhibited in the form of growing passenger revenue and the use of aeroplane as a means of travel by those to whom the mere idea would have been abhorrent a short time back, by the rising volume of written communications dispatched through the skyways by means of the air mail service, and by the as yet meager and tentative but nonetheless unmistakable beginnings of air express on an important scale.

The reason for this laggardness in the markets is not far to seek. It is to be found in the fact that it is only the exceptional investor who can afford to buy for the long pull, foregoing income now, in the prospect of a profit arising from a capital appreciation over the years as the industry begins to find itself and to get over its growing pains. To the ordinary security buyer, present income is vital, and longer range consideration, however valid, must yield to it. To this investor, therefore, air transport stocks have not been an attractive medium of investment because, in common with all struggling infant industries, dividend distributions by air line companies have been characterized by both modesty in amount and infrequency or total absence of occurrence. Further, the speculative traders who, in contrast to the average investor, like to get in and out of the market fast and who are interested in price rises rather than dividends, find little of interest for they recognize the lack of speculative possibility in the industry. And whatever confidence may exist in the future of the industry as an industry, it is still too early to forecast with reasonable infallibility the individual companies which will be the leaders a few years hence.

The two studies here under review are in essence a species of sales literature supplied by two brokerage houses to their clients for the purpose of affording a background of information and analysis which will enable those clients to make—or perhaps not to make—investments in the air transport industry with a fair degree of intelligence and appreciation of the rewards and dangers involved. They are fully in the tradition of the true investment counsellor inasmuch as there is in neither any effort to

paint an altogether roseate picture of the future of commercial aviation, but, rather, the blemishes which mar that prospect in actuality are faithfully recorded. The rays of hope which shine through the hazards are enumerated and evaluated with a temperateness and a continual undertone of caution which serve to indicate how inappropriate is the application of the term "sales literature" to these pamphlets.

The one prepared by Bache & Co. is lengthier but this is mainly due to the fact that it, unlike the Stern, Wampler study, considers separately in some detail the situation of twelve of the leading companies, and supplies as well an excellent two-page map of the United States showing all of the officially scheduled airways. These individual company studies describe the territory and routes of the particular line, its pending applications before the Civil Aeronautics Board for new and additional routes, its equipment, and its financial condition, the latter including its current capitalization in tabular form; and this is followed by an analysis of the line's operations in which are discussed such relevant matters as the comparative sources of revenue, special factors affecting the operating ratio, and a tentative estimate of per share earnings, all followed by a number of the principal operating statistics, also in tabular form.

Both of the pamphlets have examined, from the viewpoint of the industry generally, a number of things which bear importantly upon the rate and certainty of growth of the industry as a whole, and, indeed, the Stern, Wampler booklet is confined in its scope to considerations of this character. The picture which emerges from each is basically the same, namely, that of an industry which is forging ahead with breath-taking speed insofar as relative increases in volume of business are concerned, but which is not yet at all ready to begin regular and sustained earnings distributions to its owners. Passenger revenues particularly, which seem destined to be far and away the most important for the lines, are now to be nearly doubling themselves of late—and this will probably continue although these studies were issued at a time when the industry was riding the crest of a remarkably long safety record period which has since been brought to an unfortunate end. Mail revenues, although life-savers now for many lines and once the first in importance for all, have definitely taken second rank as a source of income. Air express is still in its barest infancy and is now furnished at almost prohibitive rates, but may one day yield a large and lucrative income. The conclusion seems to be amply justified that, with respect to the single factor of business volume alone, the air transport industry is on the threshold of even greater gains than those that have been made and are now being made.

The seeds of the greatest threats to the industry at present appear to lie within the great National Defense effort which is in progress and which really did not get under way in earnest until after these studies were written. In the Bache & Co. pamphlet the view is expressed that this national program will benefit the air lines in a variety of ways although it is recognized that there may be some immediate difficulties with such things as labor supply. This optimism is premised on the view that because of the "obvious importance of the air lines themselves . . . it is indicated that every effort will be expended to maintain their orderly operation." Since this entirely reasonable supposition was first expressed,

however, the public prints have carried intimations to the effect that some persons highly placed are not so convinced that commercial aviation should not be sacrificed to certain conceptions of military necessity. The vigor and force with which these intimations were publicly attacked by spokesmen for the industry may perhaps succeed in scotching the possibility of injury from this quarter, but at present it continues to be a threat of a serious nature.

A second harm generated by the defense program is contained in the peculiarly crushing effect on the air line companies of the tax measures devised to finance it. The Excess Profits Tax embodied in the Second Revenue Act of 1940 provides two alternative bases for the computation of the tax—earnings in excess of those realized in a prior average earnings period, or earnings in excess of a certain proportion of the company's invested capital. Since many of the air transport companies have been in existence for several years but have only lately realized, or are just on the verge of realizing, net income, it is plain that the first alternative will cut heavily into earnings available for corporate purposes after taxes, as will also the second because the companies operate on a relatively low degree of capital investment. The injury that will be wreaked by taxation of this sort will follow from the industry's inability to help finance itself from earnings as well as from the consequent inability, because of inadequate earnings for dividends, to attract equity capital from outside. Capital for the expansion and improvement of equipment and facilities being the major need of the industry, the National Defense program, because of its staggering expense, was bound to be a source of danger. The particular manner in which the expense is to be met has magnified the danger for the air transport industry, which not even the exemption contained in the statute for income derived from air mail payments wholly removes.

A survey of the respective capitalizations of the various individual companies does, however, disclose an extremely healthy condition with respect to certain aspects of the capital-raising problem. Paradoxically enough, the industry may well congratulate itself that it has presented to the investment world such a speculative and hazardous prospect, because this has operated to prevent the companies from financing publicly on any sizeable scale other than the sale of common stock. Of the twelve companies examined in the Bache & Co. report, not one has any long-term funded debt, only two have any preferred stock outstanding, and seven are capitalized solely with common stock. The capitalizations of the remainder include relatively negligible amounts of short-term bank loans or equipment obligations. The contrast of this over-all capital picture with that of such an established and non-speculative business as the furnishing of electricity and gas, where complex capital structures and excessive debt financing have finally come to hang around the neck of that industry like a millstone, is striking as well as illuminating. Apparently a business succumbs to the financiers only when it has become stodgily respectable from an investment point of view. It is true, of course, that the relatively small fixed plant and properties owned by an air line do not look in the direction of much borrowing on a long-term secured basis, but this is perhaps just as well. The experiences of the

depression period have demonstrated the desirability of equity financing as causing merely a cessation of dividends in times of stress instead of a decline into the dark recesses of the bankruptcy court precipitated by a failure to meet accruing interest charges. From this danger the various air transport companies appear to be reasonably immune. The current capital needs of the companies, these studies plainly show, flow mainly from the necessity of keeping abreast of aeronautical advance by the purchase of new transport equipment. Fortunately the recent introduction into this field of the equipment trust device, which has been so successfully utilized in the case of railroads, has gone far towards solving or at least alleviating this particular fund-raising problem. Its use may be expected to increase.

The immediate legal problems confronting the individual companies revolve around the prosecution of applications to the Civil Aeronautics Board for new routes. The Bache & Co. study shows a veritable deluge of these requests and spells out in some detail the conflicting nature and competitive consequences thereof. The point is properly made that the ultimate disposition of these will have a vital effect upon the fortunes of the companies involved, and that, accordingly, investment in a particular line must be made subject to the realization that an unhappy run of luck in connection with these applications may render that investment less desirable than another might have been. But this goes only to the matter of single companies; the future of the industry as a whole is not jeopardized from this quarter for the reason that the new routes will be forthcoming and someone will be flying them. Thus, a rational diversification of investment should serve as an effective counter-irritant and reduce this peril to a minimum. Again from the lawyer's standpoint, the number and importance of these applications to the Board—as well as other matters over which the Board has jurisdiction—converts practice before the Board into one of the newer and more significant segments of the expanding area of administrative law. The air lawyer is now an administrative lawyer.

In sum, these two detailed and intelligent considerations of a young industry so obviously a foundation-stone of future national development come at an opportune time and perform a real service. The air transport business seemingly has come through its worst years and there are unmistakable signs that its ceiling is beginning to lift. The prospective investor, peering through the overcast which remains, stands in need of all the assistance which can possibly be given him, and the industry stands equally in need of his substantial participation. The function of the honest broker in seeking to bring together those who can become mutually advantageous to each other has been well discharged by the two houses sponsoring these studies. That the cautious optimism which they generally express as to the attractiveness of air transport investment was not unfounded is evidenced by the fact that present market quotations show the air lines to be holding the levels existing six months ago when these reports were issued, despite the subsequent termination of the record safety period and the enhanced threat from the defense program.

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WIN YOUR WINGS. Book Two. By Colonel Roscoe Turner, world famous pilot, President of the Turner Aeronautical Corporation and Turner School of Aeronautics, and by Jean H. Dubuque of the Civil Aeronautics Authority. Chicago, Frederick J. Drake & Co. Pp. 426. Price: \$3.50.

In (1940) 11 Journal of Air Law 368, I reviewed Book One of the present work. In regard to Book Two I can only repeat what I priorly stated in recommending Book One. The pilot student who has completed the primary field training and has studied the theory as presented in Book One, finds in Book Two detailed and exhaustive advanced aviation instruction in order to prepare him for a commercial pilot's certificate or for a flight instructor's rating. The first five lessons offer a thorough and impressive description of advanced and aerobatic maneuvers, modern aircraft instruments, principles of aircraft engines, airplane structure, and radio and instrument navigation. The clear and skilful diction together with excellent diagrams, tables, and photos make it easy not only for the student, but also for the layman to obtain a clear understanding of the intricacies of the modern technique. Lesson Six is named "Winged Commerce". What the authors say here about the selection of a flying school, the organization of airlines and aircraft manufacturing companies, contributing industries, and the United States Government Service will be of special interest. Lesson Eight, named "Your Career in Aviation", gives excellent hints how to apply for a position in aviation, and describes the possibilities of, and the approach to Army and Navy Flight Training and to Aircorps Flying Schools. A carefully selected index concludes this most valuable work.

The two volumes of "Win Your Wings" will certainly become one of the standard books for the training of students pilots. The experienced pilot likewise will gladly return to this thorough and reliable source of information for the high art of flying.

Fritz G. Lorenz