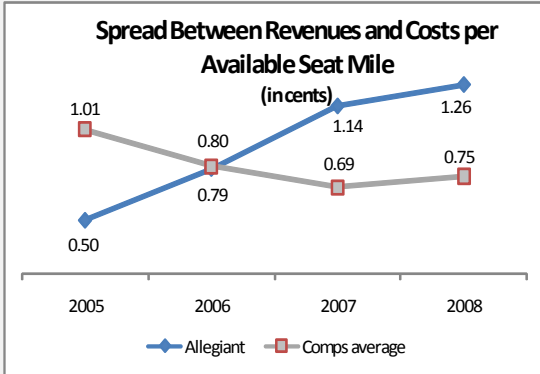




Recommendation: **BUY**

A Persistent Focus on Profitability



Company: Allegiant Travel Co.
 Ticker: NASDAQ: ALGT
 Headquarters: Las Vegas, Nevada

Price Target: \$ 49.00
 Current Price (3/8/09): \$ 33.44
 52 Week Range: \$ 15.89 - 49.06

	Comps	ALGT
Market Cap (\$M):	2,000.7	698.9
Debt to Equity (YE2008):	184.3	22.4
Oper. Margin %(ttm):	8.3	12.0
Price/Sales (2010):	0.5	1.1
Price/Earnings (2010):	4.7	14.4
Cash per Share (YE2008):	7.60	9.13
Load Factor %(FY2008):	79.2	87.0

	Comps	ALGT
ROA %(ttm):	4.3	6.5
ROE %(ttm):	14.1	10.5
ROIC %(ttm):	10.9	9.2

Comparables: Hawaiian Holdings, Republic Airways, Ryanair Holdings, and SkyWest

We place a **BUY** on Allegiant shares.

INVESTMENT THESIS

- Allegiant's continued growth and outperformance in a down market provides solid evidence that it has developed a durable competitive advantage in a niche market. The company has beat analyst expectations by more than 30% the past two quarters, growing net income by 40.6% CAGR since 2005.
- Allegiant will continue to see robust growth. The company has almost quadrupled its ancillary revenue to \$115 million from \$31 million over the past two years. In addition, management believes Allegiant can expand from 57 small cities to 100 cities in North America while maintaining its competitive advantage in each market.
- Competitors continue to drop service in key markets, unable to sustain profitability at Allegiant's low fares. In 2007 Allegiant faced head-to-head competition on nine routes in the U.S. In 2008, competition remained on only two routes.¹ This dearth of competition provides Allegiant with a degree of pricing flexibility, allowing for margin expansion in the near term.
- We predict Allegiant's average fuel cost per gallon will be lower than \$2.10 through 2010, significantly below the company's full-year 2008 average of \$2.98. This will push operating and net margins higher.

COMPANY OVERVIEW

Allegiant Travel Co. (Allegiant) is a leisure travel company, which provides air transportation between small cities in the U.S. and leisure destinations such as Las Vegas, Phoenix, Orlando, Tampa/St. Petersburg and Ft. Lauderdale. As of Feb. 1, 2009, Allegiant provided nonstop scheduled air service from 57 small cities primarily to the leisure destinations above.²

Allegiant's revenue consists of three segments: scheduled service revenue, fixed fee contract revenue and ancillary revenue. Scheduled service revenue is the core business among the three segments and accounted for 66% of total revenue in FY2008. Ancillary revenue, which includes hotel and rental car booking fees and in-flight charges, has increased 260% since 2005, and continues to help drive top-line growth.

¹ Allegiant, "Management Presentation," Nov. 2008. Accessed on 3/8/09. www.allegiantair.com

² Allegiant 2008 10-K. Page 2. Accessed on 3/7/2009.

COMPETITIVE ADVANTAGES

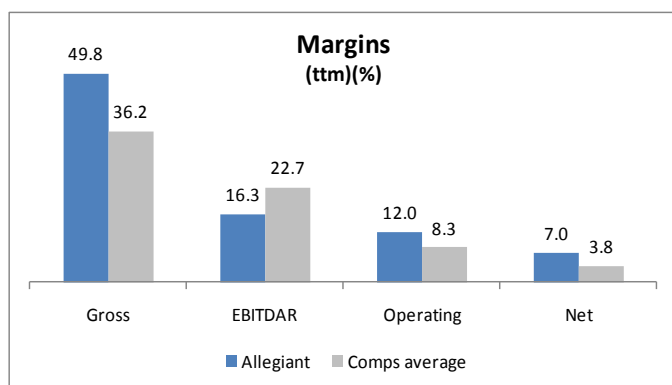
Allegiant has developed a cost-driven strategy. It focuses mainly on underserved small cities where there is little competition for passengers. The company offers nonstop flights only, provides no free food or drinks, and does not employ frequent flyer or other loyalty programs. Furthermore, Allegiant uses MD-80 aircraft instead of newer aircraft like the Airbus A320 or Boeing 737. These measures ensure that the company minimizes its operating costs, making its low fares feasible.

Allegiant has a strong balance sheet with \$190.8 million of cash and equivalents and \$64.6 million in total debt. This gives the company much more flexibility in implementing its strategy in the event of further economic deterioration, and frees the company from default risk.

INDUSTRY ANALYSIS

Allegiant has become an elite company in the regional airline industry due to its continued growth and superior execution over the past four years.

While many airlines are losing money (and lots of it), Allegiant has found a niche by avoiding direct competition at small airports. As a result, the company's gross, operating and net margins are approximately 33% higher than its peers.³



To achieve such superior margins Allegiant has been able to keep its planes fuller than competitors, as evidenced by its load factor of 87% in 2008. The comparable average in 2008 was 79%. The load factor is the percentage of occupied seats an airline has on each flight.

	Load factor (in %)			
	2005	2006	2007	2008
Allegiant	77.4	78.4	81.3	87.0
Comps average	78.9	80.1	80.5	79.2
Hawaiian	87.6	86.4	87.4	82.7
Republic	68.8	72.6	74.5	74.3
Ryanair	84.0	83.0	82.0	82.0
Skywest	75.0	78.3	77.9	77.7

The high load factor is somewhat attributable to decreasing competition from competitors going bust and the fact that Allegiant uses a smaller aircraft, the MD-80. Allegiant's higher than average load factor in 2008 was notable considering the faltering economy and the company's exposure to leisure destinations.

High fuel prices adversely impacted the entire industry in 2008. The average cost of fuel per gallon was \$2.87 for Allegiant and its comparables. Prices have dropped substantially in the last few months, which should improve profitability industry-wide. Allegiant reported an average cost of fuel per gallon of \$1.65 in December.⁴

IMPACT OF THE CURRENT ECONOMY

Allegiant's leisure-centric business model does place it at a higher risk of underperformance due to the poor economy than competitors. The exposure to Las Vegas, in particular, is cause for concern since the city has been one of the hardest hit by the current recession, and the airline flies the most routes (39) to the city. However, management has said the casinos are the ones in trouble, not Allegiant.⁵ In fact, with room prices down 40% in Las Vegas, management believes the discounts could have a stimulative effect on travel to Las Vegas in certain key markets.⁵ Even with the economic headwind, Allegiant has shown no signs of distress, posting a 90.2% load factor in February, a year-over-year increase of 3.8%.⁶

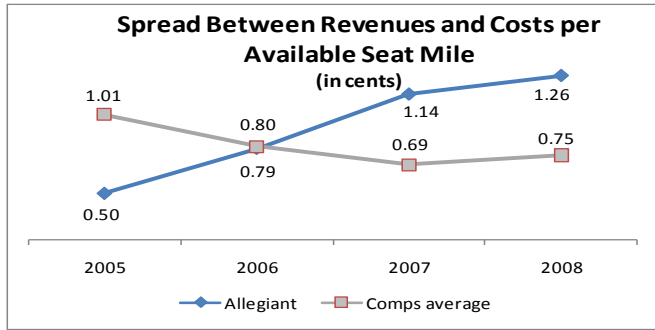
Allegiant has increased its revenue per available seat mile (RASM) almost 70% since 2005, while the peer average RASM fell slightly. In addition to the increased revenue, Allegiant has been able to control costs, which has led to a growing spread between its RASM and cost per available seat mile (CASM). The spread increased 150% from 2005 to 2008, bolstering Allegiant's profitability.

⁴ Allegiant press release, "Forth Quarter and Full Year 2008 Results." Accessed on 3/8/09. www.allegiantair.com

⁵ Allegiant, "Management Presentation," Feb. 2009. Accessed on 3/8/09. www.allegiantair.com

⁶ Thompson One. "February 2009 Traffic Report." Accessed on 3/8/09. www.thompsononeim.com

³ Thompson One data. Financial information was obtained from Thompson. Accessed on 3/8/09. www.thompsononeim.com



Allegiant's fleet primarily consists of the older and larger MD-80 aircraft. Using the gas-guzzling MD-80 makes Allegiant more sensitive to fuel prices compared to competitors' smaller, more fuel-efficient aircraft. Although not expected, any signs of increasing fuel prices should be watched carefully as the increased cost would shrink the company's margins disproportionately relative to peers.

VALUATION

We performed two valuation techniques to arrive at a target price for Allegiant's shares: discounted cash flows (DCF) and relative multiples. The results of these techniques yielded drastically different intrinsic values per share, depending on the method employed. The target prices ranged from 32% undervalued to 208% overvalued.

DCF: Key Assumptions			
Cost of Debt	8.0%	Perpetuity Rate	2.0%
Cost of Equity	9.4%	Tax Rate	36.0%
WACC	8.7%	Market Return	10.0%

According to our DCF assumptions, including future growth and profit margins for Allegiant, the company's cash flows should exceed \$50 million through 2011.

FREE CASH FLOWS					
	2007	2008	2009E	2010E	2011E
EBITDA	60.1	79.3	87.7	105.6	113.1
Less: Cash taxes	19.2	19.8	22.9	27.9	29.9
Less: Capex	42.1	43.1	25.0	30.0	35.0
Less: Inc. in NWC	(22.8)	(10.4)	(11.8)	(12.6)	(14.0)
Free Cash Flow	21.6	26.8	51.6	60.4	62.2

We arrived at two target prices with our DCF model – one using a 2% perpetuity rate and another using an EV/EBITDAR exit multiple. The exit multiple, an average of our comparables' 2011 EV/EBITDAR multiples, was 4.8. The perpetuity model generated a target price of \$49.30, nearly 50% higher than the current share price of \$33.44.

The exit multiple model produced a target price of \$35.67, about 7% higher than the current price.

To understand the influence that our estimated WACC and perpetuity rate exert on Allegiant's target price, we performed a sensitivity analysis on the two variables. In all scenarios, however, Allegiant's shares were undervalued.

Target Price: Sensitivity Analysis				
		Perpetuity Rate		
		0%	1%	3%
WACC	10%	36.46	39.19	46.99
	9%	39.76	43.24	53.67
	8%	43.88	48.44	63.01

In addition to our DCF analysis, we completed three relative valuations using the following multiples: 2010 EV/EBITDAR, 2010 Price/Earnings, and 2010 Price/Sales. For comparables we averaged forward multiples for Hawaiian Airlines, Republic Airways, Ryanair, and SkyWest. The results of those models, along with our DCF results, are listed in the table below.

Valuation Summary			
Model	Key Variable	Target Price	Prem./(discount)
DCF: Perpetuity	2% growth	49.30	-32%
DCF: Exit Multiple	4.8x 2011 EV/EBITDAR	34.78	-4%
2010 EV/EBITDAR	4.9x EV/EBITDAR	18.43	81%
2010 P/E	4.7x P/E	10.95	205%
2010 P/S	0.5x P/S	16.06	108%

Because Allegiant generally outperforms its comparables in terms of margins and returns, its multiples are significantly higher than those of other airlines. Therefore, we believe relative valuations provide less insight into Allegiant's true value. As such, we based our target price exclusively on our DCF model.

CONCLUSION

Allegiant will continue to prosper despite the tough economy. With fuel prices much lower and competitors dropping service in Allegiant's markets, the company should experience modest margin expansion. Continued growth in routes and in the number of cities served should provide profitable growth in the next three years. Although we place a BUY on Allegiant's shares with a price target of \$39, we do not believe the APM class should purchase shares of Allegiant. With more than 6% of the APM portfolio invested in Ryanair, we believe the portfolio is sufficiently exposed to the airline industry and recommend the class not increase its exposure.