Yale *School of Management*

135 Prospect Street, New Haven, CT 06511

JetBlue Airways

October 9, 2002

Time Frame

12 Months

Recommendation

SELL

Recommendations:
Buy: >20% Undervalued
Hold: Fair Market Value
Sell: >20% Overvalued

"If you want to become a millionaire, start with a billion dollars and launch a new airline…"

- Richard Branson, founder of Virgin Atlantic Airways

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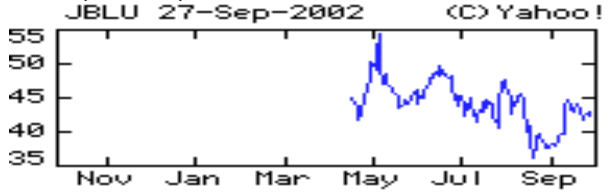
% Returns Over the Last 12 Months

(Prices are as October 7, 2002)

Airline Index (^XAL):	**(59.80)%**
S&P 500:	**(26.70)%**
JetBlue (JBLU):	**(20.73)%**
JBLU Current Price:	**$35.75**
JBLU Target Price:	**$29.44**
Projected (Short) Return:	**17.65%**



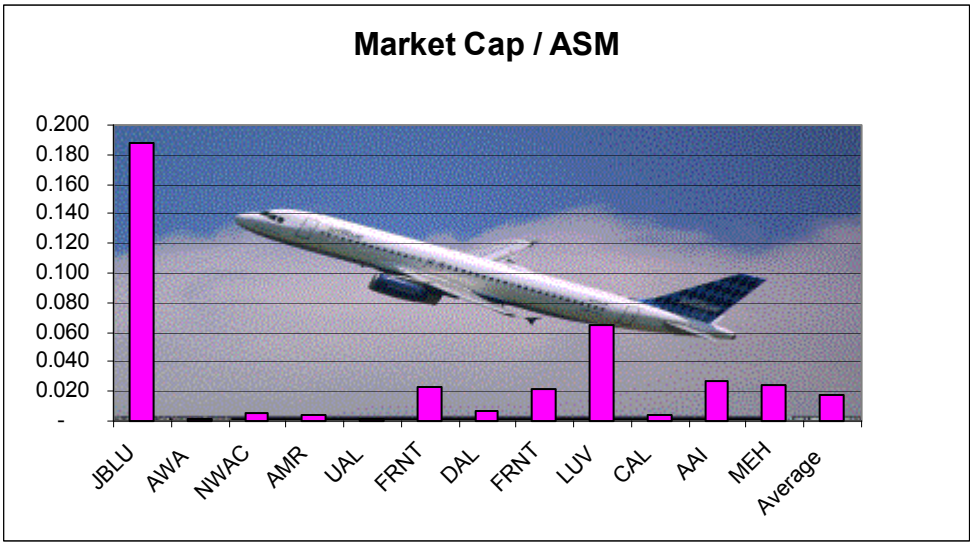
RECOMMENDATION: SELL

- **Short-lived, well-funded track record is unsustainable in current economic climate.**
- **Threat to cost structures within airline industry due to potential invasion of Iraq and resultant oil price increases.**
- **Immediate shorting opportunity due to overvaluation as compared to the industry (JetBlue P/E ratio is higher than the industry average by 18%) valuation ratios. Height of financial performance is already reflected in the JBLU's stock price, and we are bearish about future financial prospects.**
- **Inherent company risks include high leverage, dependence on JFK hub as key revenue driver and IPO-lock-up expiration in the near term.**

Historical Context

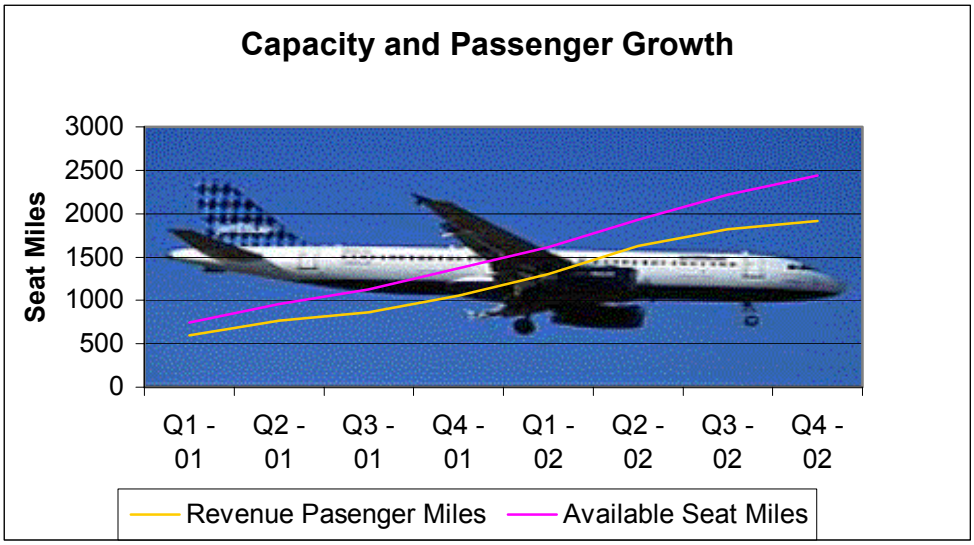
- JetBlue is the best-capitalized airline in start-up history. It has a short but impressive track record – with a fleet size of only 31, it has a market capitalization of $1.5 billion, currently ranked fifth in the airline industry. JetBlue's growth is primarily attributed to a strong and well-funded management team and a differentiated strategy claim.
  - The management team has an extensive leadership track record with successful carriers, such as Southwest Airlines.
  - JetBlue's business strategy is to be a low-fare, low-cost passenger airline that provides high-quality customer service primarily on point-to-point routes. The company focuses on underserved markets and large metropolitan areas that have high average fares, by maintaining a geographically diversified flight schedule that includes both short haul and long haul routes.[1]

- Since JetBlue has a much higher Market Cap-to-ASM (Available Seat Miles) ratio compared to its competitors, it indicates a potential for overvaluation. In fact, their Market Cap-to-ASM ratio is more than twice that of Southwest (LUV).



[1] Multex Market Guide

- JetBlue is an aggressive start-up, which began service in February 2000, and has grown steadily since its inception. Duplicating Southwest's simplicity, high aircraft utilization and low fares, JetBlue offers comfortable, affordable and convenient point-to-point air travel with some unique amenities (for example, leather seats and live-feed TV monitors). It has relied primarily on word of mouth advertising to execute its strategy. In contrast with most upstart discount carriers, JetBlue operates a fleet of 31 brand new, highly fuel-efficient Airbus A320 aircraft and employs a non-unionized FAA certified workforce (pilots, technicians, dispatchers).[2]



- JetBlue's pricing strategy provides widely available low fares that are designed to stimulate demand, and the airline had demonstrated its ability to increase passenger traffic in the markets it serves. For example, according to the U.S. Department of Transportation (DOT), in the fourth quarter of 1999, before JetBlue introduced its service, the average number of daily passengers flying between Buffalo and all three New York City metropolitan airports was 584. For the fourth quarter of 2000, after JetBlue began servicing Buffalo, the average number of daily passengers flying in that market increased by 75% to 1,020 of whom 441, or 43%, flew JetBlue. Prior to JetBlue's entry, competitor unrestricted roundtrip fares from New York City to Buffalo, Rochester, and Syracuse ranged from $500 to $800.[3] JetBlue charged an unrestricted roundtrip fare of $158, slightly above current $119 fares, but well below major carrier pricing. State and local leaders eagerly lobbied the DOT for peak hour flight waivers so that JetBlue would service the voters in their districts. Every politician wanted to be viewed as the person who helped reduce fares between New York City and Upstate New York. The New York State Administration worked closely with JetBlue to help them succeed in providing low-cost accessible air service that was deemed "long overdue" for so many New Yorkers.

- In September, 2002 JetBlue acquired LiveTV technology from Harris Corp for approximately $81 million. This acquisition gives them control over its proprietary technology, which enables a direct in-flight 24-channel satellite television service. This was a defensive move more than strategic since LiveTV was likely to discontinue operations, and JetBlue could not afford to lose a significant part of its differentiation strategy.[4] In the future it is possible that they could lease this technology to other airlines, however it is unlikely that they will want to sell a major sources of competitive advantage. According to management JetBlue expects no impact on future earnings due to this transaction.[5]

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[2] JetBlue IPO Prospectus
[3] Goldwasser, Amy. Something Stylish, Something Blue. Business 2.0. February 2001
[4] Morgan Stanley, Company Update, September 10, 2002
[5] Morgan Stanley, Company Update, September 10, 2002

Business Strategy

Overview. Founder David Neeleman sought to "bring humanity back to air travel" but also have "high quality airline service at affordable fares." JetBlue's strategy is to create an improved "travel experience" by using new airplanes with leather seats, an uncommon amount of legroom, and free satellite TV at every seat. In addition, by leveraging technology to reduce "paper" work and employee headcount, JetBlue can offer first-rate personal service, and competitive pricing at low costs (less than $0.06 per available seat mile).

- **Convenience and Quality of "Travel Experience"**. JetBlue strives to be truly customer friendly, with computer terminals that can be rotated to show the customer what the agent is looking at, giving a $159 voucher whenever a flight is delayed for more than four hours for reasons other than weather or traffic, and giving a $25 voucher for misplaced bags. However, in an effort to contain costs and deliver on its reliable service promise, JetBlue does not sell tickets to coordinate with other airlines, nor would they transfer a passenger's bags to another airline[6]. Therefore, by focusing on being the low cost differentiated competitor on major routes, they can avoid the costs associated with running a feeder airline[7].

- **"No-Frills" Service and Simple, Affordable Pricing**. The airline has created a single class of service with fares averaging 65% less than those of the competition. To accomplish this, all seats are assigned, all travel is ticket less (use of internet ticket sales in Q2 2002 amounted to 61% of revenues, which compares favorably to the industry average of 50%), there are no discount seats, and all fares are one-way (with no Saturday night stay required). JetBlue's low cost structure offers simplified, everyday low fares to its customers. JetBlue offers 14-day, 7-day, and 3-day purchase fares and a "walk-up" fare in each market. Most JetBlue fares are non-refundable. JetBlue's fares increase as the number of days prior to travel decreases, with the highest "walk-up" fare charges at approximately twice the amount of the lowest 14-day advance purchase fare. Based on the Company's research, JetBlue's advance purchase fares are often 30-40% below those of existing markets prior to JetBlue's entry; while JetBlue's "walk-up" fares are generally 60-70% below major U.S. airlines' unrestricted "full coach" fares[8].

- **Extensive Metropolis Service.** As of December 31, 2001, JetBlue operated 102 flights per day, including 50 daily flights between JFK and Florida, 24 daily flights between JFK and upstate New York and 18 daily flights between JFK and the western United States. On August 28, 2001, JetBlue began service at its new West Coast base of operations, Long Beach Municipal Airport, which serves the Los Angeles area.

  Initially, JetBlue went against conventional wisdom by selecting JFK as its home base of operations. Neeleman's logic was three-fold: First, JFK is located in the middle of a huge population center, with 19 million people living within a 60-mile radius. Second, JFK, widely thought of as an old, rundown, busy, international airport, had capacity to add domestic flight routes out of its existing terminals. Since plenty of start-up airlines had failed in the past, there was adequate space for JetBlue. Although new space didn't have to be constructed, waivers (slot exemptions) needed to be obtained for flights during peak hours. Neeleman's business plan was to fly to several under-served cities in New York State. **Currently, JetBlue accounts for 27% of JFK's domestic traffic, which constitutes close to 90% of the airline's capacity and revenue base[9].**

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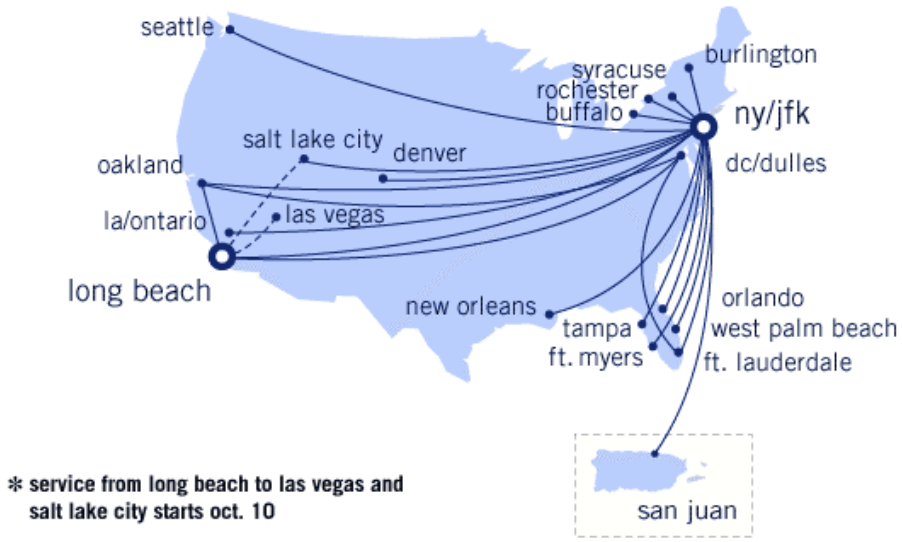
[6] Multex Market Guide
[7] Deutsche Bank, Coverage Initiated with a Hold Rating, September 9, 2002
[8] Deutsche Bank, Coverage Initiated with a Hold Rating, September 9, 2002
[9] Deutsche Bank, Coverage Initiated with a Hold Rating, September 9, 2002

Even with strong public support, the JFK headquarters was not without risk. For example, the DOT granted JetBlue 75 daily takeoffs and landing slot exemptions at JFK in 1999 after vigorous lobbying by political leaders and David Neeleman**. JetBlue has made a down payment of approximately $25,000 per slot and the slots cannot be sold, given, or traded to anyone else. If the Company does not use all of its slot exemptions by February 2003, the DOT has the right to take them back[10].** In addition, JetBlue operates out of Terminal 6 at JFK under an annual one-year permit from the Port Authority of New York and New Jersey. With 30 days notice, either party could cancel the current permit. As of December 31, 2001, JetBlue was working with the Port Authority to negotiate a long-term lease but has not yet come to a resolution.

JetBlue serves over 20 destinations, most of which are metropolitan:



Source: IPO Prospectus

[10] JetBlue IPO Prospectus

- **Low Cost Structure**. JetBlue has one of the most modern aircraft fleets in service. They operate one type of aircraft with one type of engine - the A320 - because it offers high fuel efficiency and allows for better spare parts inventory management and lower pilot retraining costs. In addition, the young age of their fleet helps them avoid expensive maintenance costs associated with older aircraft, but will result in higher maintenance costs in the future as the fleet ages.

- **Proven Management Team**. JetBlue's CEO, David Neeleman, was a) the president and one of the founders of Morris Air, a successful low-fare airline that was acquired by Southwest Airlines, and b) a founder of Westjet. David Barger, the President and Chief Operating Officer served as Vice President in charge of Continental's Newark hub from 1994-1998. The CFO, John Owen, spent 14 years as treasurer of Southwest Airlines. The management team formed the company in 1999 and become operational in February 2000. At the time of its launch, JetBlue was the best funded start-up passenger airline in U.S. aviation history with $130 million in investments from the Chairman and CEO and a group of investors including Chase Capital Partners, David Checketts, and two funds controlled by legendary investor George Soros[11].

Industry-Specific Risks

Despite JetBlue's positive short-term performance, its future earnings potential is unlikely to continue, given the pessimistic industry outlook.

- **Reduced Demand Due to a Faltering Economy.** Over short periods, airline travel can be erratic. Over the longer term, airline travel is very cyclical; it waxes and wanes together with consumer sentiment and disposable income levels. Given the current post-9/11 attack sentiment, economic climate, consumer confidence and unemployment levels, the airline traveler's willingness to pay has gone down even further since September 2001. In addition, airlines are plagued by weak demand for business and leisure travel: recent corporate downsizing has left leaner organizations, with fewer managers and executives authorized to travel and leisure travelers turning to ground transportation as a means to save money.

- **Convenience/Service Compromise.** JetBlue, like other airlines is subject to delays caused by factors beyond its control, such as air traffic congestion at airports, adverse weather conditions and heightened security measures. Delays frustrate passengers, reduce aircraft utilization and increase costs, all of which affect profitability. JetBlue competes for metropolitan passengers by offering priority check-in, expedited baggage handling, departure punctuality and in-flight amenities. The appeal of its strategy is to provide frequent flights, reliable on-time performance, and top safety records. In the wake of the September 11th attacks, the government recently federalized airport security and hired about 28,000 workers in an effort to alleviate security concerns. **The result: Airline travel has become less appealing amid new security requirements, frequent procedure changes, and a rush to get trained personnel in place**. Short-haul airline shuttle routes, traditionally profitable due to high proportions of business travel, are now being over run by rental cars and regional rail due to cumbersome airport checks and delays.

- **Labor**. In 2002, labor costs for JetBlue amounted to 22% of total operating expense and 26.6% of revenue, while the industry's labor costs are averaged 33% of total operating expense, up from 28% in December of 2000. Although the industry had reacted promptly after September 11th with lay-offs of more than 80,000 employees, the rise in labor costs can be explained by lower revenues, and by the normal time lag between employee layoffs and realization of cost savings.[12] JetBlue has not furloughed any employees since September 11th.

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[11] JetBlue IPO Prospectus
[12] Standard & Poor's, Industry Surveys, September 28, 2002

Salaries and Benefits 2001 - 2003E

($ millions)

	2001			2Q 2002 (YTD)			2002E			2003E		
	Revenues	Labor Cost	% Revenues	Revenues	Labor Cost	% Revenues	Revenues	Labor Cost	% Revenues	Revenues	Labor Cost	% Revenues
AirTran Holdings	665	159	23.9%	383	97	25.3%	808	198	24.5%	990	247	25.0%
Alaska Air Group	2,141	798	37.3%	1,071	417	38.9%	2,284	863	37.8%	2,659	991	37.3%
America West Airlines	2,021	604	29.9%	987	288	29.2%	2,086	606	29.1%	2,238	648	29.0%
AMR Corporation	18,963	8,032	42.4%	8,615	4,206	48.8%	16,578	8,103	48.9%	18,721	8,458	45.2%
Continental Airlines	8,968	3,021	33.7%	4,185	1,478	35.3%	8,729	3,039	34.8%	8,734	3,039	34.8%
Delta Airlines	13,879	6,147	44.3%	6,577	3,064	46.6%	13,773	6,259	45.4%	14,813	6,461	43.6%
JetBlue Airways	320	85	26.6%	282	72	25.5%	612	156	25.5%	902	230	25.5%
Midwest Express	457	167	36.5%	220	78	35.5%	442	158	35.7%	545	187	34.3%
Northwest Airlines	9,905	3,843	38.8%	4,586	1,860	40.6%	9,592	3,797	39.6%	10,347	3,909	37.8%
Southwest Airlines	5,555	1,828	32.9%	2,730	963	35.3%	5,637	1,982	35.2%	6,295	2,094	33.3%
UAL Corporation	16,138	7,079	43.9%	7,081	3,379	47.7%	14,894	6,973	46.8%	16,684	7,390	44.3%
US Airways	8,288	3,551	42.8%	3,612	1,632	45.2%	7,517	3,357	44.7%	8,278	3,486	42.1%
Average	7,275	2,943	40.5%	3,361	1,461	43.5%	6,913	2,958	42.8%	7,600	3,095	40.7%

Source: Merrill Lynch, August 2002

Airlines have traditionally suffered from exorbitant union contracts that we believe will be difficult to eradicate from the industry. Although JetBlue is currently non-unionized, if its employees unionize, it could result in demands that may increase its operating expenses. Each of its different FAA-licensed employee groups can unionize at any time and require separate collective bargaining agreements. If this occurs, it may become increasingly difficult to keep labor costs low during this economic downturn[13].

- **Fuel Prices and Impending War with Iraq.** Fuel costs are JetBlue's second-largest operating expense, accounting for about 14.2% of total expenses[14]. Energy expenses depend on the fuel prices as well as the age of the aircrafts and the average flight length[15]. By utilizing a new fleet, JetBlue has gained some efficiency in fuel consumption and in maintenance costs.

  The prospects of oil prices in 2002 do not look as positive as those in 2001. Fuel costs have risen approximately 50% ($.25 per gallon) since January. We believe that the possibility of the US declaring war on Iraq will keep oil prices high during 2002, and a long conflict could lead to even higher prices through 2003. Hence, although JetBlue has implemented a fuel-hedging program under which it enters into crude oil option contracts to protect against significant increases in fuel prices, the program may not be sufficient to cover material adverse effects on operating results as a consequence of an Iraqi invasion. We therefore prefer to stay cautious on this front until some of the event risk (potential invasion of Iraq) has dissipated.[16]

Company-Specific Risks

- **Highly Dependent on JFK Hub**. JetBlue's future profitability is highly dependent on its position at JFK. Over 90% of its capacity operates in JFK[17] and competes with American, Delta or both on 11 of the 16 cities that they service from JFK. A change in regulatory dynamics at JFK could significantly alter their profitability position. JetBlue seems to be able to operate efficiently at low cost levels. However, they have not experienced the full impact of larger carrier predatory pricing due to the industry's current inability to absorb short-term losses.

[13] JetBlue IPO Prospectus
[14] JetBlue IPO Prospectus
[15] Standard & Poor's, Industry Surveys, September 28, 2002
[16] JetBlue IPO Prospectus
[17] Deutsche Bank, Coverage Initiated with a Hold Rating, September 9, 2002

- **High Leverage.** The highly leveraged position could make it difficult to raise the additional capital required to grow and become profitable. Currently JetBlue's debt to equity ratio is 1.36 compared to .99 for the industry.[18]

- **IPO Lockup ends October 9th.** Prices could drop in the near future, as the market is flooded with newly tradable shares of JetBlue. When the lockup period ends on Oct. 9th, over 35 million shares of common stock will be available for sale in the public market at various times, subject, in some cases, to volume limitations under Rule 144 of the Securities Act of 1933. As these resale restrictions come to an end, the market price of JBLU could drop significantly if the holders of these restricted shares sell them or the market perceives that they intend to sell them[19].

Valuation

We used two main approaches to valuing the company: Comparable Companies Analysis and Discounted Cash Flows Analysis (DCF). Since JetBlue doesn't have many comparable companies and most airlines have negative earnings, we relied primarily on the DCF valuation. Further, since there has been no recent transaction activity in the airline industry, we did not include a precedent transaction analysis.

Comparable Companies Analysis

- **Forward P/E**. This method of valuation is the standard practice in the industry. Given the losses expected by most of the players in the industry in 2002, a comparable companies analysis provides a very limited insight into the relative values in the airline industry. The comparison has to be reduced to the benchmarks provided by the companies producing positive results, which are Southwest, JetBlue, AirTrans, and Alaska in 2003. We look primarily at forward P/E ratios using projected earnings in 2003, which we consider more representative of the future performance. JetBlue forward P/E amounts to 24x, 39% premium over the industry mean. Hence, the comps analysis leads to the conclusion that JetBlue stock might be overvalued.

		EPS Estimates ($/share)						P/E	
Company	Price as of 09/30/02	Sep-02	Dec-02	2002E	2003E	Next Year Earnings Growth	5-Year Earnings Growth	2002E	2003E
JBLU	40.06	0.28	0.32	1.25	1.67	33.6%	25.0%	32	24
LUV	12.54	0.05	0.06	0.24	0.52	116.7%	14.5%	52	24
ALK	16.99	0.41	-0.84	-1.94	1.15	-1.593%	8.0%	NM	15
AMR	4.09	-2.95	-3.02	-12.62	-5.64	-0.553%	10.0%	NM	NM
UAL	2.18	-7.14	-7.89	-30.96	-18.14	-41.4%	8.5%	NM	NM
CAL	5.24	-0.78	-1.50	-4.68	-0.37	-92.1%	8.5%	NM	NM
DAL	8.81	-1.72	-1.91	-7.97	-2.47	-69.0%	8.0%	NM	NM
MEH	4.39	-0.58	-0.54	-1.21	-0.26	-78.5%	12.0%	NM	NM
AAI	3.10	-0.01	0.04	0.05	0.51	920.0%	20.0%	62	6
ATAH	3.24	-1.63	-1.88	-5.34	-1.98	-62.9%	NM	NM	NM
Mean								**49**	**17**
Median								**52**	**19**
JetBlue Premium over Industry Mean								*-34%*	*39%*

Source: Yahoo! Finance and Yale SOM estimates

[18] Multex Investor
[19] JetBlue IPO Prospectus

- **Short Ratio**. Additional market data support the abovementioned conclusion. JetBlue's short ratio (percentage of shares short in the market) of 11.31% versus an industry average of 5.5% suggests that the market perceives the stock to be overvalued.

	Short Ratio
JBLU	11.31
AWA (American West)	9.04
NWAC (Northwest)	7.85
AMR (AMR Corp.)	7.06
UAL (United)	6.01
FRNT (Frontier)	5.69
BA (British Airways)	5.27
DAL (Delta)	5.26
ALK (Alaska Air)	5.20
LUV (Southwest)	5.17
CAL (Continental)	5.01
ATAH (ATA Holdings)	3.28
AAI (AirTran)	3.20
MEH (Midwest Express)	2.18
ACAI (Atlantic Coast)	1.01
Average	**5.50**

- **Historical Ratio Performance**. In general, historical P/E ratios are above that of the industry by 18%, whereas other similar airlines such as Southwest trade at a 2% premium. Other valuation ratios for JetBlue show consistently a premium over the industry average.[20]

Valuation Ratios	JBLU	Industry	Sector	S&P 500	JetBlue Premium to Industry
P/E Ratio (TTM)	34.37	29.19	25.27	23.83	17.75%
P/E High - Last 5 Yrs.	N/A	34.87	54.78	49.86	
P/E Low - Last 5 Yrs.	N/A	15.5	12.78	17.36	
Price to Sales (TTM)	3.68	1.59	1.62	2.7	131.45%
Price to Book (MRQ)	4.7	2.17	3.89	4.18	116.59%
Price to Tangible Book (MRQ)	4.7	2.25	4.19	6.99	108.89%
Price to Cash Flow (TTM)	33.77	15.76	13.11	16.2	114.28%
Price to Free Cash Flow (TTM)	NM	57.75	32.32	26.12	
Beta	N/A	1.07	0.64	1	
% Owned Institutions	58.97	64.88	56.53	61.38	

Dividends	JBLU	Industry	Sector	S&P 500
Dividend Yield	0	0.26	1.16	2.34
Dividend Yield - 5 Year Avg.	N/A	0.11	1.2	1.35
Dividend 5 Year Growth Rate	NM	13.65	-21.93	7.78
Payout Ratio (TTM)	0	2.47	22.19	29.68

Growth Rates(%)	JBLU	Industry	Sector	S&P 500
Sales (MRQ) vs Qtr. 1 Yr. Ago	90.44	5.67	2.96	3.58
Sales (TTM) vs TTM 1 Yr. Ago	N/A	-10.18	0.45	1.34
Sales - 5 Yr. Growth Rate	NM	10.18	7.91	11.45
EPS (MRQ) vs Qtr. 1 Yr. Ago	1.23	-29.03	3.38	12.2
EPS (TTM) vs TTM 1 Yr. Ago	N/A	-42.96	2.13	3.93
EPS - 5 Yr. Growth Rate	NM	18.57	11.63	8.77
Capital Spending - 5 Yr. Growth Rate	NM	14.96	3.48	10.48

Financial Strength	JBLU	Industry	Sector	S&P 500
Quick Ratio (MRQ)	1.41	1.27	1.04	1.1
Current Ratio (MRQ)	1.46	1.46	1.34	1.62
LT Debt to Equity (MRQ)	1.16	0.93	0.62	0.74
Total Debt to Equity (MRQ)	1.36	1.01	0.65	1.01
Interest Coverage (TTM)	3.7	2.98	12.27	9.45

Profitability Ratios (%)	JBLU	Industry	Sector	S&P 500
Gross Margin (TTM)	43.01	64.79	60.01	47.47
Gross Margin - 5 Yr. Avg.	N/A	69.41	76.38	48.72
EBITD Margin (TTM)	16.43	9.26	18.24	20.87
EBITD - 5 Yr. Avg.	N/A	16.87	18.06	22.02
Operating Margin (TTM)	12.87	3.29	11.12	17.69
Operating Margin - 5 Yr. Avg.	N/A	11.59	11.86	18.28
Pre-Tax Margin (TTM)	15.59	5.11	9.54	14.89
Pre-Tax Margin - 5 Yr. Avg.	N/A	11.85	9.78	17.13
Net Profit Margin (TTM)	10.57	3.2	5.96	10.58
Net Profit Margin - 5 Yr. Avg.	N/A	7.18	5.89	11.27
Effective Tax Rate (TTM)	32.18	37.59	38.15	33.35
Effective Tax Rate - 5 Yr. Avg.	N/A	39.02	40.17	35.83

Management Effectiveness (%)	JBLU	Industry	Sector	S&P 500
Return On Assets (TTM)	5.8	2.23	6.04	6.24
Return On Assets - 5 Yr. Avg.	N/A	7.1	6.42	7.98
Return On Investment (TTM)	7.64	2.43	7.72	9.98
Return On Investment - 5 Yr. Avg.	N/A	8.71	8.33	12.8
Return On Equity (TTM)	31.5	2.12	14.41	17.82
Return On Equity - 5 Yr. Avg.	N/A	16.66	15.1	21.71

[20] In this chart Industry refers to airlines while Sector refers to the entire transportation sector.

DCF Analysis

Key Assumptions. We have used the following assumptions in the DCF model to value JetBlue:

1. The Revenue per aircraft will remain flat at $17 million per aircraft going forward from 2003-2009 since the airline is at the height of the industry in terms of load factors. This estimate will drive the revenue growth rates in the DCF model.

2. From 2009-2012, the revenue growth rate will flatten out and remain constant from year to year. We expect the Company to experience significant growth (22% CAGR) in the next five years and then stabilize to more reasonable growth levels from 2009 through 2012 (10.26% CAGR) and finally achieve a terminal growth rate of 4%.

3. Operating expenses and depreciation are projected as a percentage of revenues (see expense section below).

4. The capital expenditures estimates are based on the information presented in Jet Blue's IPO Prospectus, which we feel is reasonable given the Company's forecasted levels of expansion.

5. The future working capital requirements remain constant at the 2002E percentage of revenues.

6. The target debt-to-equity structure is 65% is based on the target Long-Term Debt to Equity estimate for the Airline Industry (*Source: Multex Market Guide*).

7. The levered beta for the Airline Industry is 1.08 (*Source: Multex Market Guide*).

8. The risk-free rate is 3.8% (*Source: 9/30/02 WSJ Yield Curve for the 10-Year Treasury Note*).

9. The market premium is 8%, based on an average return of the US Stock Market of the past 75 years (*Source: Ibbotson & Associates*).

10. The cost of debt is 5.3% (Risk-free rate plus a 150 basis point spread for BBB-rated Bond).

11. Expenses as a percentage of revenues are based on historical margins with appropriate adjustments for future trend projections.

12. Corporate income tax rate remains flat at the 2002 level of 41%.

13. The Aircraft Acquisition Schedule was derived from the presentation in the JetBlue IPO Prospectus.

14. The DCF model assumes that JetBlue will exercise all available options for additional aircraft acquisitions.

15. A terminal growth rate of 4%, which is a reasonable estimate of GDP growth based official estimates.[21]

[21] The Bureau of Labor Statistics' projections for US real GDP growth by 2005 range from 1.6%-3%. In addition we assume an inflation rate between 1.5% and 2%.

Revenue

We estimated a 5-year Revenue CAGR of 23%, based upon the aircraft acquisition schedule in the IPO prospectus. Our methodology calculates the annual revenue as the product of the average number of aircrafts in the fleet for each projection year times the revenues per aircraft.

The projected fleet includes the number of orders for acquisition and options to purchase aircrafts since we believe this is a reasonable approximation of the number of new aircrafts in the fleet. It is in the best interest of the company to order as many planes as possible in order to get the highest possible discount. At the same time, the airline tries to be moderate with the orders to avoid building overcapacity.

We also assume that revenues per aircraft will remain constant at the current levels.

Aircraft Acquisition Schedule	2001A	2002E	2003E	2004E	2005E	2006E	2007E	2008E	2009E
New A/C		15	13	16	12	16	16	16	8
1 Firm purchase		15	13	13	12	5	5		
2 Option				1		7	7	10	5
3 Rights to 19 additional aircrafts				2		4	4	6	3
Revenue Growth (with Options)									
Year End	21	36	49	65	77	93	109	125	133
Average	21	28.5	42.5	57	71	85	101	117	129
Revenues	320	612	722	968	1,206	1,444	1,716	1,987	2,191
Rev / Aircraft	15.3	17.0	17.0	17.0	17.0	17.0	17.0	17.0	17.0
Growth Rev/AC			0%	0%	0%	0%	0%	0%	0%
Revenue Growth Rate			18%	34%	25%	20%	19%	16%	10%
5-year CAGR			23%						
Revenue Growth (without Options)									
Year End	21	36	49	62	74	79	84	84	84
Average	21	28.5	42.5	55.5	68	76.5	81.5	84	84
Revenues	320	612	722	943	1,155	1,299	1,384	1,427	1,427
Rev / Aircraft	15.3	17.0	17.0	17.0	17.0	17.0	17.0	17.0	17.0
Growth Rev/AC			0%	0%	0%	0%	0%	0%	0%
Revenue Growth Rate			18%	31%	23%	13%	7%	3%	0%
5-year CAGR			18%						

Source: Jet Blue's IPO Prospectus and Yale SOM Estimates

Operating Expenses (Exhibit 2a)

- *Labor*. Salaries will eventually increase in future years due to likely unionization of FAA licensed employees. We estimated a 1% over revenue increase per year until 2006 and will remain constant thereafter.
- *Fuel*. We assumed a 1% increase in 2003 given the current instability in the Middle East. However, we do not see fuel growing as a percentage of revenues after 2003, since we believe that current prices represent a peak in oil prices.
- *Maintenance*. As the fleet gets older, the aircrafts will require more intensive maintenance schedule and overhauls. Hence, we assume slightly higher (an increase to 2% over revenues) levels in the future.
- *Aircraft Rentals*. We assume a declining percentage of revenues since the schedule to expand the fleet in the next 7 years is focused on purchases rather than leases.
- *Depreciation & Amortization*. Depreciation and amortization as a percentage of revenue will increase as the number of owned aircraft increases.

- *Rentals & Landing Fees*. We assume these expenses will continue to go down as utilization of destination infrastructure increases.
- *Sales & Marketing*. We anticipate that this category of expenses will continue to decrease slightly from the current levels. JetBlue's cost strategy is to increase frequency between points. Once a route is established, it requires less marketing. JetBlue plans to continue with its current strategy of introducing only one or two new destinations per year.

Other Expenses

- *Interest Expense*. We believe the company will need external funds to finance the projected capital expenditures in the coming years. Raising equity does not appear to be a likely alternative given the current state of the capital markets. Hence, we believe that JetBlue will increase its debt levels to finance the projected investments during the next few years.

Conclusion

The resulting share price from the DCF analysis is $29.44, which supports our sell recommendation. To achieve the current market price one would have to believe that revenues would outpace our assumptions. For this to occur fares would increase significantly and that load factors would also increase. JetBlue is already getting maximum feasible load factors and we don't believe that raising prices is consistent with their strategy or their customers' price elasticity. Other means of outpacing our revenue growth assumptions would include major industry changes such as acquisitions or the bankruptcy and exit of other major players. However at this point the likelihood and impact of these events is very uncertain.

Exhibit 1. Discounted Cash-Flows Analysis

	2000A	2001A	2002E	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Revenue Growth	104.6	206.26%	90.86%	18.06%	34.12%	24.56%	19.72%	18.82%	15.84%	10.26%	10.26%	10.26%	10.26%
Operating Expenses *	116.43%	88.39%	79.69%	79.39%	78.39%	78.14%	77.89%	77.89%	77.89%	77.89%	77.89%	77.89%	77.89%
Depreciation & Amortization *	3.82%	3.25%	3.83%	4.83%	5.33%	5.83%	6.33%	6.33%	6.33%	6.33%	6.33%	6.33%	6.33%
CAPEX *	196.91%	73.03%	105.81%	82.70%	60.32%	43.70%	19.81%	13.34%	9.21%	6.68%	4.85%	3.52%	2.55%
%WCR *	-29.74%	-23.91%	9.47%	9.47%	9.47%	9.47%	9.47%	9.47%	9.47%	9.47%	9.47%	9.47%	9.47%
Revenues	105	320	612	722	968	1,206	1,444	1,716	1,987	2,191	2,416	2,664	2,937
Operating expenses	122	283	487	573	759	942	1,125	1,336	1,548	1,707	1,882	2,075	2,288
Depreciation	4	10	23	35	52	70	91	109	126	139	153	169	186
EBIT	(21)	27	101	114	158	193	228	271	314	346	381	420	464
Taxes on EBIT	(0)	3	37	47	65	80	94	112	130	143	157	174	191
NOPLAT	(21)	23	64	67	93	114	134	159	184	203	224	247	272
Depreciation	4	10	23	35	52	70	91	109	126	139	153	169	186
Delta WCR	-	(45)	135	10	23	23	23	26	26	19	21	23	141
CAPEX	206	234	647	597	584	527	286	229	183	146	117	94	75
FCF	(223)	(155)	(694)	(506)	(463)	(366)	(83)	13	101	176	238	298	242
Continuation Value													5,273
Discounted FCF			(174)	(465)	(392)	(284)	(60)	9	61	98	122	140	2,380

PV(FCF)	1,435
Long Term Debt	437
Cash	240
Equity Value	1,238
# of Shares (million)	42.045
Price per Share in US$	**29.44**

WACC Calculation	
Target D/E	0.65
Levered Beta	1.08
Market Risk Premium	8.00%
Cost of Equity	12.44%
Beta of Debt	0.19
Cost of Debt	5.30%
Risk-free Rate	3.80%
Debt-to-Cap	39.39%
Equity-to-Cap	60.61%
WACC	**8.76%**

Terminal Value Growth Rate	4.00%

Sensitivity Analysis

		Terminal Growth Rate		
($/Share)		*3%*	*4%*	*5%*
WACC	*7.76%*	34.67	51.06	79.31
	8.76%	19.62	29.44	44.47
	9.76%	9.4	15.78	24.84

* As a percentage of revenues

Exhibit 2: JetBlue Earnings Model Projections

($ in millions, except for share amounts)

	2000A	2001A	Q1-02	Q2-02	Q3-02E	Q4-02E	2002E	2003E	2004E	2005E	2006E
Revenue											
Passenger	101.7	310.4	129.1	144.3	153.6	164.7	591.7				
Other	3.0	10.0	4.3	5.0	5.0	5.5	19.8				
TOTAL REVENUE	**104.6**	**320.4**	**133.4**	**149.3**	**158.6**	**170.2**	**611.5**	**721.9**	**968.2**	**1206.0**	**1443.8**
% Growth Rate											
Operating Expenses											
Salaries & Benefits	32.9	84.8	33.6	37.6	40.7	43.8	155.7	186.0	259.1	334.8	415.3
Fuel	17.6	41.7	13	17.0	20.5	22.5	73	93.4	125.3	156.0	186.8
Maintenance	1.1	4.7	1.9	1.5	2.4	3.4	9.2	14.5	19.4	24.2	28.9
Aircraft Rentals	13.0	32.9	9.5	10.3	11.7	13.4	44.9	49.4	56.6	58.4	55.5
Rentals & Landing Fees	11.1	27.3	9.9	9.7	11.1	11.2	41.9	42.2	47.0	55.5	62.8
Depreciation and Amortization	4.0	10.4	4.7	5.7	6.2	6.8	23.4	34.8	51.6	70.3	91.3
Sales Marketing	17.0	28.3	9.9	11.8	12.6	12.4	46.7	50.8	68.1	84.9	101.6
Other	29.1	63.5	27.5	28.0	29.9	30.5	115.9	136.8	183.5	228.6	273.7
Total Operating Expenses	**125.8**	**293.6**	**110.0**	**121.6**	**135.1**	**144.0**	**510.7**	**608.0**	**810.5**	**1012.6**	**1215.9**
OPERATING INCOME	**(21.2)**	**26.8**	**23.4**	**27.7**	**23.5**	**26.2**	**100.8**	**113.9**	**157.7**	**193.4**	**227.9**
Other (Income) Expense											
Airline Stabilization Act Compensation	0.0	18.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Interest Income & Other	7.0	10.5	1.8	0.6	1.0	1.1	4.5	5.3	7.1	8.9	10.6
Interest Expense	-7.4	-14.1	-2.9	-3.3	-5.2	-4.8	-16.2	-22.7	-35.3	-50.0	-67.1
Total Other Income	**-0.4**	**15.1**	**-1.1**	**-2.7**	**-4.2**	**-3.7**	**-11.7**	**-17.4**	**-28.2**	**-41.2**	**-56.5**
Pretax Income	**(21.6)**	**41.9**	**22.3**	**25.0**	**19.3**	**22.5**	**89.1**	**96.5**	**129.5**	**152.2**	**171.4**
Income Taxes	(0.2)	3.4	9.3	10.4	7.9	9.2	36.8	39.9	53.5	62.9	70.8
Income Tax rate	NM	8%	42%	42%	41%	41%	41%	41%	41%	41%	41%
NET INCOME	**(21.3)**	**38.5**	**13.0**	**14.6**	**11.4**	**13.3**	**52.3**	**56.7**	**76.0**	**89.3**	**100.6**
Fully Diluted # Shares (million)	N/A	N/A					43.54	46.80	46.80	46.80	46.80
EPS	**N/A**	**N/A**					**1.20**	**1.21**	**1.62**	**1.91**	**2.15**

Source: Company Financials and Yale SOM Projections

Exhibit 2a: JetBlue Earnings Model Projections - Percentage Structure

	2000	2001	Q1-02	Q2-02	Q3-02E	Q4-02E	2002E	2003	2004	2005	2006
Revenue											
Passenger		205.3%					90.6%				
Other		238.6%					98.0%				
TOTAL REVENUE		**444.0%**					**188.6%**	**18%**	**34%**	**25%**	**20%**
% Growth Rate											
Operating Expenses											
Salaries & Benefits	31.5%	26.5%	25.2%	25.2%	25.7%	25.7%	25.5%	25.8%	26.8%	27.8%	28.8%
Fuel	16.9%	13.0%	9.7%	11.4%	12.9%	13.2%	11.9%	12.9%	12.9%	12.9%	12.9%
Maintenance	1.0%	1.5%	1.4%	1.0%	1.5%	2.0%	1.5%	2.0%	2.0%	2.0%	2.0%
Aircraft Rentals	12.5%	10.3%	7.1%	6.9%	7.4%	7.9%	7.3%	6.8%	5.8%	4.8%	3.8%
Rentals & Landing Fees	10.6%	8.5%	7.4%	6.5%	7.0%	6.6%	6.9%	5.9%	4.9%	4.6%	4.4%
Depreciation and Amorti	3.8%	3.2%	3.5%	3.8%	3.9%	4.0%	3.8%	4.8%	5.3%	5.8%	6.3%
Sales Marketing	16.2%	8.8%	7.4%	7.9%	7.9%	7.3%	7.6%	7.0%	7.0%	7.0%	7.0%
Other	27.8%	19.8%	20.6%	18.8%	18.9%	17.9%	19.0%	19.0%	19.0%	19.0%	19.0%
Total Operating Expenses	**120.3%**	**91.6%**	**82.5%**	**81.4%**	**85.2%**	**84.6%**	**83.5%**	**84.2%**	**83.7%**	**84.0%**	**84.2%**
OPERATING INCOME	**-20.3%**	**8.4%**	**17.5%**	**18.6%**	**14.8%**	**15.4%**	**16.5%**	**15.8%**	**16.3%**	**16.0%**	**15.8%**
Other (Income) Expense											
Airline Stabilization Act (	0.0%	5.8%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Interest Income & Other	6.7%	3.3%	1.3%	0.4%	0.6%	0.6%	0.7%	0.7%	0.7%	0.7%	0.7%
Interest Expense	-7.1%	-4.4%	-2.2%	-2.2%	-3.3%	-2.8%	-2.6%	-3.1%	-3.6%	-4.1%	-4.6%
Total Other Income	**-0.4%**	**-1.1%**	**-0.8%**	**-1.8%**	**-2.6%**	**-2.2%**	**-1.9%**	**-2.4%**	**-2.9%**	**-3.4%**	**-3.9%**
Pretax Income	**-20.6%**	**7.2%**	**16.7%**	**16.7%**	**12.2%**	**13.2%**	**14.6%**	**13.4%**	**13.4%**	**12.6%**	**11.9%**
Income Taxes	-0.2%										
Income Tax rate	NM	8%	42%	42%	41%	41%	41%	41%	41%	41%	41%
NET INCOME	**-20.4%**	**12.0%**	**9.7%**	**9.8%**	**7.2%**	**7.8%**	**8.6%**	**7.8%**	**7.8%**	**7.4%**	**7.0%**

Source: Company Financials and Yale SOM projections

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