

AVANTAIR, INC. (OTC BB: AAIR)

INDUSTRY: AIR SERVICES

DISCLOSURES: 1, 4A, 5, 10

RATING: STRONG BUY

RISK: HIGH

CLOSING PRICE 10/01/10	TRAILING P/E (TTM)	SHARES OUT (MILS.)	MARKET CAP (MILS.)	3-5 YEAR REV. GROWTH	PRICE TARGET (Est)
\$2.40	NM	26.3	\$63.1	N/A	\$4.50

ANNUAL DATA – JUNE YEAR END			
	2010A	2011E	2012E
EPS	\$ (0.27)	\$ 0.20	\$ 0.42
P/E	N/M	12.0x	5.7x
REVENUE (MIL.)	\$140.0	\$152.2	\$165.0
P/S	0.45	0.41	0.38

EARNINGS					
	Q1	Q2	Q3	Q4	ANNUAL
2012E	N/A	N/A	N/A	N/A	\$ 0.42
2011E	\$ (0.03)	\$ 0.07	\$ 0.10	\$ 0.06	\$ 0.20
2010A	\$ (0.11)	\$ (0.06)	\$ (0.04)	\$ (0.08)	\$ (0.27)
2009A	\$ (0.24)	\$ (0.15)	\$ (0.10)	\$ 0.10	\$ (0.39)

Reports 4Q and FY2010 Financial Results

- In what had to be one of the most trying periods in executive air flight history, AAIR reported 5% YTY sales growth for FY2010 (ended June 30, 2010) increasing to \$143.0 million from \$136.8 million a year ago, albeit marginally below CFR's estimate of \$145.0 million.
- EBITDA (excluding extraordinary items) increased 20.1% YTY to \$6.33 million from \$5.27 million.
- Loss attributable to common shareholders was (\$6.36 million) or a loss of (\$0.27) per share (excludes \$0.9 million gain on sale of aircraft) versus a loss of (\$5.95 million) or (\$0.39) per share last year and below CFR's estimate of a loss of (\$3.36 million) and (\$0.14) per share.
- Lower-than-expected sales of fractional aircraft shares adversely impacted revenues, while the Company's strategic decision to front-load certain fleet maintenance items to the tune of \$1.7 million into the 4Q FY2010 period accounted for much of the variance related to the net loss and EPS for the period.
- Flight hour cards increased 143% to 388 from 160 last year (CFR estimate 406), while Axis Club Membership sales grew >400% to 51 from 10 in FY2009 (CFR estimate 30). Fractional shares sales tallied 7.5 for FY2010 compared with 39 in FY2009 and CFR's estimate of 11.
- Cash increased to \$9.4 million from \$3.8 million at FY2009 YE due to cash generated from operations, completion of an \$8.0 million private placement and the receipt of \$5.5 million in cash from the sale of an aircraft and the return of aircraft deposits; this was offset by the addition of four aircraft to the fleet increasing the total number of planes in service to 55 at period end.

Management discussed its strong customer-retention rate: upwards of 90% of customers with expiring card, membership or management contracts renewed in the period, while 80 new customers joined the Avantair family in 4Q. Further, management noted a distinct upstream migration of customers from flight hour cards to Axis Club Membership and/or fractional shares.

On the cost front, management's decision to strategically reposition certain maintenance items into the 4Q period accounted for the bulk of our "miss" in terms of income from operations. While revenues were light, the

shift from fractional sales to flight hour cards and Axis Club Memberships actually increased margins slightly; \$1.7 million of the \$1.9 million variance traces directly to accelerated maintenance. The good news is that the Company will benefit down the road: by taking the maintenance downtime during the slow season, the Company can enjoy the benefit of greater aircraft availability in subsequent periods reducing the need for costly charter flights.

Outlook: We expect 1Q FY2011 to incorporate a similar level of accelerated maintenance compared to 4Q FY2010 – for 2Q & 3Q we expect those benefits to materialize in terms of lower absolute cost of flight operations. Further, the Company is experiencing benefits from advanced flight management software, which boosted revenue generating flight hours by 14% in the June quarter alone as a result of these efficiencies. Management reported that fractional share sales activity was brisk through August; they indicate that 8-9 have been sold so far in Q1, exceeding the total for the entire year of FY2010 and bringing the total available fractional shares covered under the costly flooring plan to ~20 at 1Q FY2011 end. Further, we expect flight hour card and Axis Club Membership sales to remain robust; netting this expectation against the expense containment backdrop we discussed earlier and we are looking for a profitable FY2011 for Avantair, Inc. The Company is scheduled to take delivery of another aircraft in the October 2010 timeframe, we expect this aircraft will be added to the core fleet at very favorable lease terms under a new financing plan available through Avantair and the Italian government; another four aircraft will be added through the FY2011 period. We expect three of these will be core aircraft, and that one will be brought in under the floor plan to accommodate further fractional sales, based on our expectation of a modest rebound of fractional sales in the FY2011 period.

We believe the value proposition offered to private travelers by Avantair will continue drive market share gains, even in a slow recovery market. Flight hour cards and memberships provide more financial reward to the Company while bolstering utilization rates and productivity. The trade-off is a shorter time-commitment from the customer, hence elevated financial risk for Avantair: at term's end they must resell that commitment to stay "level". The good news is they have experienced strong loyalty and high retention rates among customers and are a low cost producer, we believe this move will pay off significantly when an economic recovery eventually shows and the Company can lock in more favorable terms longer term.

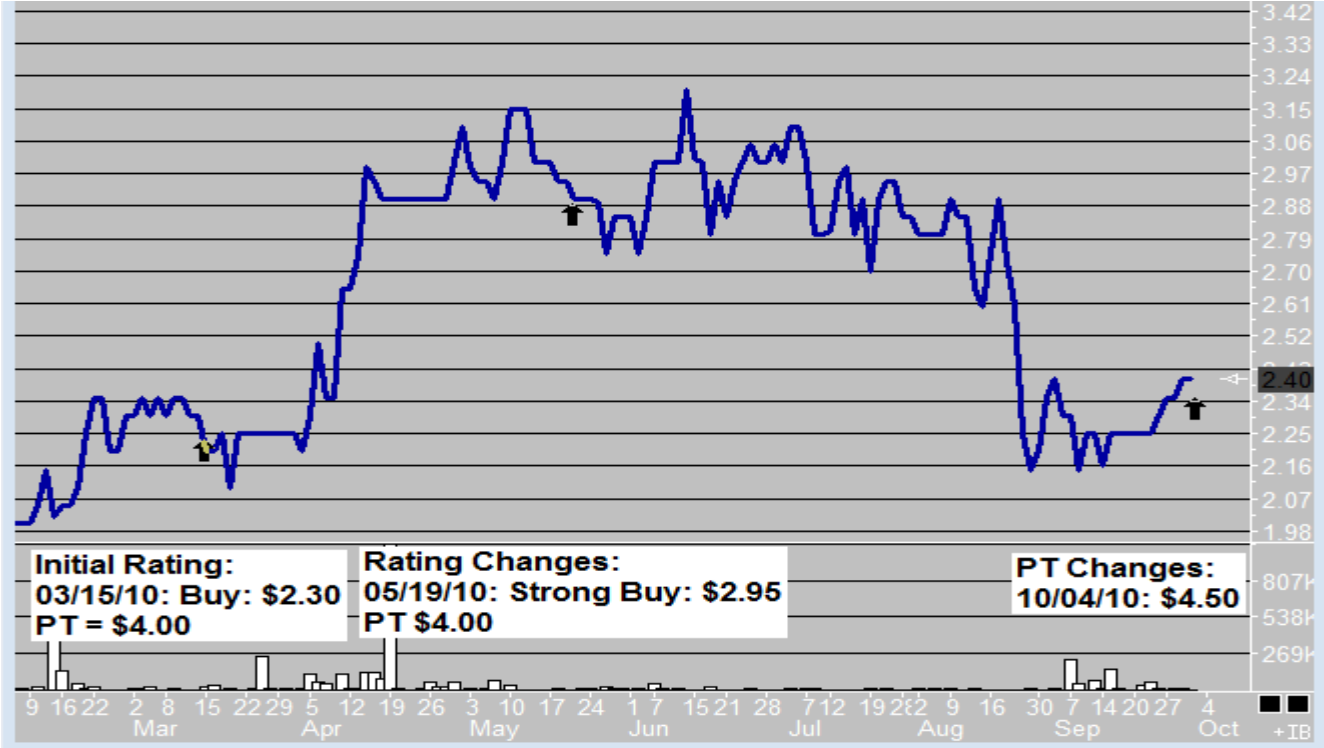
Meanwhile, they have managed to grow through a very difficult economic environment the past eighteen months, while taking market share from competitors in the light cabin jet space. We believe the business has fundamentally bottomed, and is poised for a rebound as business and consumer confidence mends, although we have moderated our view somewhat to reflect the protracted weakness in the fractional share segment, offset by more robust expectation for the flight hour card/Axis Club line.

We now expect FY2011 revenues of \$152.2 million (+6.45% YTY; down from \$157 million previously) and EPS of \$0.20 (from \$0.30); further, we are initiating estimates for FY2012 with a top-line expectation of \$165 million (+8.4%) and EPS of \$0.43. Applying a modest 12-18x PE to the midpoint of these estimates yields a twelve-month price target of \$4.50 (+87%) for AAIR shares.

We rate these share a "Strong Buy".

Please see detailed earnings model.

AAIR Price Chart



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Accumulate	Purchase of the stock is recommended for above average appreciation over the next 12 to 18 months, but the buyer may have an opportunity to acquire the stock within a 10% trading range.
Hold	Holding the stock is recommended because the share price has moved above the specific "Buy" range and, therefore, appreciation potential is less than or equal to the market.
Sell	The stock has reached the target price objective and/or conditions have changed sufficiently to alter the outlook for the stock.

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High	The security is more volatile than the market and/or the company is more leveraged than its peer group.
Moderate	The security has about the same volatility as the market and/or the company carries a level of leverage in line with its peer group.
Low	The security is less volatile than the market and/or the company is less leveraged than its peer group.

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