

### BUY

Price **8.5p**  
(S€19.5)

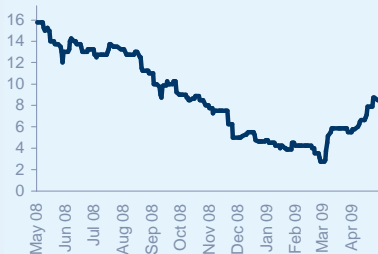
Target Price 25p

Reuters/BBG SKYW.L / SKYW LN  
 Index FTSE AIM  
 Sector Transport  
 Market Cap £17.1m (S\$39.3m)  
 Shares in Issue 195.3m  
 NAV 9.9p (S€22.8)  
 Gearing Nil  
 Interest Cover N/A

Performance (%) AIM  
 1 month: +44  
 3 months: +68  
 12 months: +4

Key Data:  
 Free Cashflow Yield 5.7%

Last Results Interims: Feb 2009  
 Next Results Finals: November 2009



Source: ProQuote

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\*WH Ireland acts as Broker and Nomad.

### Marketing Communication

This document has not been prepared in accordance with legal requirements designed to promote the independence of investment research. Please refer to important disclosures towards the end of this document.

## Skywest Airlines\*

### Update on Recent Performance & Business Development

- **Skywest Airlines, headquartered in Singapore, is the holding company for the major regional scheduled and charter airline operating in Western Australia.** The shares are quoted on London's Alternative Investments Market. The company is currently mulling the merit of having a dual listing on the Australian Stock Exchange.
- **Results for the six months to December 2008 covered a difficult period for the regular scheduled airline business with falling passenger numbers, offset by growth in charters.** There were adverse swings in fuel prices and currency rates leading to unrealised exchange losses on translation, and further one-off costs associated with gearing up for the major Rio Tinto air services contract win. Overall, a pre-tax loss of S\$2.5m was incurred on turnover of S\$97.3m.
- **Ten months into the current financial year, passenger numbers on scheduled routes are down by 9%.** With available seat kilometres up by 8.8% as services expand but revenue passenger kilometres up by only 5.8%, load factors have fallen from 57.1% to 55.5%. This remains comfortably above the level at which Skywest breaks-even (circa 48%). **Charter flights remain strong with 67% more flown than at the comparable point in FY08.** This has resulted in a more even revenue split between the two types of operation.
- **We have based our revenue estimates on projected passenger decline of 10% for FY09, recovering by 2.5% in FY10 and a further 7.5% in FY11.** Zero fares inflation has been assumed. **Charter income increases by S\$5m per annum from S\$80m in FY09.** Cost of sales reflects the H1 improvement and lower fuel costs. In the current year S\$9.5m of one-off costs have been expensed and if these are added back, adjusted EPS double to S€6.6 rather than the S€3.3 shown below.
- To arrive at a target share price, we have capitalised these adjusted earnings at the average prospective multiple of three comparator companies quoted on the UK Stock Exchange: Dart Group (owner of Jet2), Easy Jet and Ryan Air. **On this basis, we attribute a valuation of 25p per share – a 194% premium to the current share price. We therefore reiterate our 'Buy' recommendation.**

Y/E June	2008A	2009A	2010E	2011E
Sales (S\$m)	184.2	176.0	190.0	203.0
PTP (S\$m)	14.5	9.3	21.4	23.8
EPS (S€)	5.2	3.3	7.7	8.6
P/E (x)	3.7	5.9	2.5	2.3
DPS (S€)	1.4	0.8	1.9	2.1
Dividend Yield (%)	7.2	4.1	9.7	10.8

Source: WH Ireland estimates

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## Interim Results

(\$'000 unless stated)	6m to Dec-07	6m to Dec-08	%	12m to Jun-08
			Change	
<b>INCOME STATEMENT</b>				
<b>Revenue</b>	<b>74,186</b>	<b>97,309</b>	<b>+31.2</b>	<b>184,202</b>
Cost of Sales	<u>(39,355)</u>	<u>(51,025)</u>		<u>(86,542)</u>
Gross Profit	34,831	46,284	+32.9	97,660
Other Operating Income	105	0		368
Other Operating Expenses	<u>(13,840)</u>	<u>(32,651)</u>		<u>(58,621)</u>
EBITDAR*	21,096	13,633	-35.4	39,407
Rental of Aircraft	(8,048)	(10,439)		(14,990)
Depreciation & Amortisation	<u>(4,727)</u>	<u>(5,734)</u>		<u>(10,298)</u>
Operating Profit (Loss)	8,321	(2,540)	n.m.	14,119
Net Interest	<u>351</u>	<u>28</u>		<u>361</u>
<b>Profit (Loss) before Tax</b>	<b>8,672</b>	<b>(2,512)</b>	<b>n.m.</b>	<b>14,480</b>
Taxation	<u>(2,186)</u>	<u>(274)</u>		<u>(4,080)</u>
Profit (Loss) after Tax	6,486	(2,786)	n.m.	10,400
Weighted Shares in Issue (m)	198.7	199.5		199.4
<b>Basic EPS (LPS) (S¢)</b>	<b>3.26</b>	<b>(1.40)</b>	<b>n.m.</b>	<b>5.22</b>
Net Dividend (S¢)	0.7	0.0		1.4
Gross Margin (%)	47.0	47.6		53.0
EBITDAR Margin (%)	28.4	14.0		21.4
Operating Margin (%)	11.2	-2.6		7.7
Tax Rate (%)	25.2	n.a.		28.2
<b>CASH FLOW STATEMENT</b>				
Operating Profit (Loss)	8,321	(2,540)		14,119
Depreciation & Amortisation	4,727	5,734		10,298
Non-cash Trading Items	<u>761</u>	<u>(1,323)</u>		<u>1,794</u>
<b>Gross Cash Flow</b>	<b>13,809</b>	<b>1,771</b>	<b>-87.2</b>	<b>26,211</b>
Interest & Dividends Received	351	28		474
Tax	<u>(295)</u>	<u>0</u>		<u>(2,393)</u>
<b>Net Cash Flow</b>	<b>13,865</b>	<b>1,799</b>	<b>-87.0</b>	<b>24,292</b>
Working Capital	(5,157)	(7,022)		(3,189)
Net Capital Expenditure	<u>(10,893)</u>	<u>(6,514)</u>		<u>(18,930)</u>
<b>Free Cash Flow</b>	<b>(2,185)</b>	<b>(11,737)</b>	<b>(+437.2)</b>	<b>2,173</b>
Equity Dividends Paid	(3,673)	0		(5,088)
Financial Investment	(2,264)	(93)		(131)
Shares Issued (Net of Buy-backs)	1,682	0		505
Increase (Decrease) in Borrowings	<u>2,118</u>	<u>(1,651)</u>		<u>(1,143)</u>
<b>Increase (Decrease) in Cash</b>	<b>(4,322)</b>	<b>(13,481)</b>		<b>(3,684)</b>
<b>Closing Net Cash</b>	<b>2,944</b>	<b>(1,554)</b>		<b>6,865</b>

\*EBITDAR: Earnings before Interest, Tax, Depreciation, Amortisation & Rental Cost of Leased Aircraft.

Source: Company Data

February's interim results recorded a loss of S\$2.5m on turnover of S\$97.3m

Results for the 6 months to Dec-08 were announced on February 26th 2009. In summary, a pre-tax loss of S\$2.5m was incurred on turnover of S\$97.3m. The comparable figures for H1 2008 were S\$74.2m turnover and S\$8.7m profit. The loss per share was S¢1.4 against earnings per share of S¢3.3 last year. No dividend was declared. Investment in fixed and working capital resulted in a sizeable cash outflow for the period with the balance sheet moving from net cash of S\$6.9m to net debt of S\$1.6m over the half-year.

Net debt of S\$1.6m at half-year end

Falling passenger numbers on scheduled routes offset by growth in charter services

This was a difficult period for the regular scheduled airline business with falling passenger numbers. However, the diminution was offset by growth in charters. Skywest also had to contend with significant negative swings in both fuel prices and currency rates. Unrealised exchange losses of S\$3.4m were taken on translation because of recent currency movements, particularly the 24% and 28% deterioration in the exchange rate between the Australian dollar and the Singapore & US dollars, respectively. Further one-off costs estimated at A\$5.7m (c. S\$5.2m) were expensed associated with the gearing up for the major Rio Tinto air services contract win (extra aircraft, additional pilots and support staff etc.). Absent these items and the airline operations were comfortably profitable.

Currency movements, fuel prices and one-off costs impacted the financial result

Lower passenger numbers accompanied by capacity expansion lay behind decline in load factors

The operating statistics showed regular passenger transport numbers down by 2.3% from 197,000 to 192,000. Following the acquisition of additional aircraft to satisfy its charter service contracts, Skywest operated an average fleet of 14 aircraft compared to 10 in the comparable period and was thus able to sell a larger number of seats to paying passengers. This enabled capacity, measured by available seat kilometres, to rise by 17.8% relative to the same months of 2007. In turn, this enabled revenue passenger kilometres to increase by 11.3% from 151.8m to 169.1m. Load factor decreased from 59.1% to 55.9%. Charter services flown almost doubled from 631 to 1,228.

Higher gross margin as a result of passing on fuel cost escalation

Gross margin increased from 47.0% to 47.6%. To mitigate the fuel cost issue where revenues are booked in A\$ but fuel is paid for in US\$, Skywest operates a fuel levy policy on the pricing of ticket sales to the public. It also has rise-and-fall provisions in contracts with mining companies where, as far as possible, fuel increases are passed on via an agreed formula. The cost of operating the fleet – in rental costs for leased, or depreciation for owned, aircraft – fell slightly by 0.6% of sales. Therefore, it was the aforementioned currency and gear-up costs contained in 'other operating expenses' that conspired to produce the operating loss.

Airline operation remained profitable

Charter business remains strong

Regarding the outlook, economic recession is having a significant impact with a noticeable drop in customer confidence. In the circumstances, management believes that the ability to redeploy assets between regular scheduled passenger transport and scheduled charter services is a significant advantage. The group's scheduled charter sector has remained strong despite the well publicised problems currently besetting areas of the Western Australian mining and resources sector. The significant decline in the price of fuel over the past few months is also exerting a beneficial effect.

Recent decline in fuel price a bonus

A\$10m of cost savings being realised

Lastly, Skywest is on course to realise major cost savings with the aim of cutting operating costs by a minimum of A\$10m per annum. Initiatives include significant reductions in supply costs from major suppliers, staff savings due to greater efficiency in human resources management, changes to aircraft parts procurement processes, pay freezes for senior management, reduction in capacity on some routes and relinquishment of inefficient office space.

Skywest still in expansion mode

The company continues to aggressively compete for major scheduled charter work throughout Western Australia. The resources industry, in particular the gas sector, is continuing to expand, and will provide further opportunities for scheduled charter services. Additional opportunities for profitable regular passenger transport services are also being undertaken, including increased flights to Darwin, Kununurra and Karratha.

Operating performance YTD

### Operating Statistics

The next Table sets out Skywest's Operating Statistics for the ten months to April 2009 compared with the same period last year. This shows that the three additional aircraft have increased the available seat kilometres by 8.8% but revenue passenger kilometres have only risen by 5.8%. Hence the 159 bps fall in the load factor impacting profitability. It is usual to see load factors diminish initially as new routes and services are introduced.

July - April Period	FY08	FY09	Change
Passengers Carried ('000)	318	289	-9.0%
Revenue Passenger Kilometres ('000)	242,284	256,307	+5.8%
Available Seat Kilometres ('000)	424,229	461,653	+8.8%
Load Factor (%)	57.1	55.5	-159 bps
Average Aircraft in Fleet	11	14	+3

Source: Company Data

### Changes to Services

Changes to scheduled services introduced from April 1st

Skywest operates scheduled services as per the route map shown. Despite difficult trading conditions, the airline is still increasing its services to key markets. With effect from April 1st, the following changes to scheduled services were implemented:

1. Commencement of a new service linking Geraldton & Carnarvon with Karratha (three per week) to assist in the development of the mid west, Gascoyne and Pilbara regions;
2. An increase in direct jet services from Perth to Karratha, taking the total to five per week;
3. Resumption of four jet services per week to Darwin, operating via Broome and/or Kununurra;
4. Resumption of services between Exmouth and Broome.

Additional charter work being sought

Also additional long-term contracts for scheduled charter services with key resource companies are being sought. Such charters involve flying workers from the residential areas of Perth and other regional centres into remote mining areas. Typically clients sign a contract for three or more years. This area continues to grow significantly notwithstanding the global downturn and its effect on the Western Australian resources and mining sector. In the financial year to date, charter services have grown by 66.9% over the same period last year from 1,291 to 2,154.

Large Rio Tinto contract started in H1

In H1, Skywest commenced the major contract with Rio Tinto providing regular charter services between Perth and its Pilbara iron ore operations (20 services per week). This is a three-year contract with a potential two-year extension. Additionally, the contract with Argyle Diamonds (part of RT) to transport employees between Perth and the Kimberley mine was renewed. Scheduled charters for other clients continue, including, inter alia, Fortescue Metals Group, Newcrest Mining and Newmont Mining.

### Other Developments

Share repurchases

During May, Skywest bought in 5 million shares: 4 million for cancellation and 1 million to be held in Treasury. The cost of this share repurchase was £327,000.

Dual listing in Australia?

Also, the Company has announced that it is considering a dual listing. Whilst remaining committed to staying on AIM, it is considering listing in Australia as well. The belief is that dual listing may enable Australian investors to compare Skywest with other airline stocks listed on the Australian Stock Exchange and so help increase liquidity in the shares.

## Earnings Estimates

Downturn starting in November has left passenger numbers down by 9% YTD

In FY09 to date, passenger numbers have fallen by 9%. The domestic and tourist routes are likely to have held up best with destinations such as Newman, Karratha & Port Hedland (iron ore) and Kalgoorlie/Boulder (nickel) worst affected. The first four months recorded passenger growth (+2.8% overall), but there then followed a sharp downturn in November and December. This gathered pace throughout the third quarter with the nadir in February (-25.6%), March (-21.0%) and April (-10.8%) provided some respite.

We estimate a 10% full-year decline

In the circumstances, we have based our revenue estimates on projected passenger decline of 10% for the full year – producing a tally of 348,000. For FY10, we have assumed that this recovers slightly by 2.5% before the pace picks up to 7.5% in FY11. This implies passenger numbers rising to 357,000 and 384,000, respectively.

Zero fares inflation assumed

In FY08, total revenue of approximately S\$184.2m was split 62:38 between passenger revenue (S\$114.2m) and charter revenue (S\$70m). Based on the then prevailing average exchange rate for the year of A\$1 = S\$1.29, and with 386,600 passengers carried, the average passenger fare comes out at S\$295 (A\$229). Assuming zero fare inflation (reasonable given that fuel costs have actually declined), passenger revenues for FY09-FY11 are A\$79.7m, A\$81.8m and A\$87.9m, respectively.

Charter currently contributing similar revenue to regular scheduled services

Projected charter revenue is currently running about 50:50 with scheduled passenger revenues. Assuming this ratio continues through the year-end, FY09 charter revenues should contribute an additional A\$80m or so. Reflecting new contracts signed, this climbs to A\$85m in FY10 and A\$90m in FY11.

Exchange rate assumptions

To convert these into Singapore dollars, we have used an average rate of A\$1 = S\$1.10 for FY09 and the current spot rate of approximately S\$1.14 for FY10 & FY11. In aggregate, therefore, we have revenue projections of A\$160m (S\$176m), A\$167m (S\$190m) and A\$178m (S\$203m) for each respective year.

One-off costs in current financial year

Cost of sales has been allowed for at 46.5% – reflecting the H1 improvement and lower fuel costs. We have assumed indirect overheads run at 25% of sales, to which is added S\$9.5m of one-off costs in the current year. EBITDAR is struck after these items. After rental and depreciation costs are taken into account, operating margins come out at 5.4% in FY09 climbing through 11.3% in FY10 to 11.7% in FY11.

Small net debt position

Skywest has mainly run through the current financial year with a small net debt position, which has increased recently with the share repurchases made. This is reflected in the interest charge.

Tax losses exhausted

Skywest has exhausted the tax losses available to it. The main composition of tax is statutory Singaporean tax at 18% augmented by the Australian taxes. We have taken a composite rate of around 30% for each year.

25% payout ratio assumed

We have further assumed a dividend pay-out ratio of approximately 25%.

## Cash Flow

Capex assumptions do not include additional aircraft purchases or leases

The base assumption is that S\$15 of additional working capital is required to finance each S\$1 of revenue growth. Capital expenditure is required for property, plant and equipment with additional amounts being invested in operating leases for additional aircraft. On an ongoing basis, we have taken capex payments to acquire tangible fixed assets at 1.1x depreciation to allow for 4% inflation between the original purchase of assets and their ultimate replacement 6 years later. This does not allow for expansionary capex associated with an increase in the size of the fleet.

**Profit & Loss Account &  
Cash Flow Estimates  
for 2009-2011**

Year to June (\$m unless stated)	2009E	2010E	2011E
<b>PROFIT &amp; LOSS ACCOUNT</b>			
Turnover	176.0	190.0	203.0
Cost of Sales	<u>(81.8)</u>	<u>(88.4)</u>	<u>(94.4)</u>
Gross Profit	94.2	101.6	108.6
S,G & A Expenses	(53.5)	(47.5)	(50.8)
Rental Costs	(20.0)	(21.0)	(22.0)
Depreciation & Amortisation	<u>(11.2)</u>	<u>(11.6)</u>	<u>(12.0)</u>
Operating Profit	9.5	21.5	23.8
Net Interest	<u>(0.2)</u>	<u>(0.1)</u>	<u>0.0</u>
Profit before Tax	9.3	21.4	23.8
Taxation	<u>(2.8)</u>	<u>(6.4)</u>	<u>(7.1)</u>
Attributable Earnings	6.5	15.0	16.7
Weighted Shares in Issue (m)	199.0	195.3	195.3
EPS (S¢)	3.3	7.7	8.6
Dividend (S¢)	0.8	1.9	2.1
<b>CASH FLOW</b>			
Operating Profit	9.5	21.5	23.8
Depreciation & Amortisation	<u>11.5</u>	<u>12.0</u>	<u>12.5</u>
EBITDA	21.0	33.5	36.3
Interest	(0.2)	(0.1)	0.0
Tax	<u>(2.8)</u>	<u>(6.4)</u>	<u>(7.1)</u>
Net Cash Flow	18.0	27.0	29.2
Working Capital	(5.0)	(2.1)	(2.0)
Capital Expenditure	<u>(12.7)</u>	<u>(13.2)</u>	<u>(13.8)</u>
Free Cash Flow	0.3	11.7	13.4
Dividends	(1.4)	(1.6)	(4.0)
Share Repurchases	<u>(0.8)</u>	=	=
Movement in Cash	(1.9)	10.1	9.4
Opening Net Cash	6.9	5.0	15.1
Cash Flow	<u>(1.9)</u>	<u>10.1</u>	<u>9.4</u>
Closing Net Cash	5.0	15.1	24.5

Source: WH Ireland estimates.

## Valuation

### PER

Lowly PER ...

The current share price of 8.5p translates to S¢19.5 based on the £1 = S\$2.30 exchange rate used. Based on our forecasts, the prospective PER for FY09 is 5.9x falling to 2.5x in FY10 and 2.3x in FY11. These multiples look undemanding when set against the projected increase in earnings, which is for a compound annual growth rate of 17.9% over the next three financial years.

### EV / EBITDA

... and EV / EBITDA multiple

The current market capitalisation of Skywest is £16.6m (S\$38.2m). At the half-year end, net debt was S\$1.6m. Therefore the current enterprise value is S\$39.8m. This compares with forecast EBITDA for FY09 of S\$21.0m placing the shares on an EV / EBITDA multiple of 1.9x. Based on our forecasts this falls to 1.2x in FY10 and 1.1x in FY11.

### Free Cash Flow Yield

High free cash yield and dividend yield

The historic free cash flow yield is 5.7%, which we are expecting to fall to around 0.8% this year before recovering very sharply from FY10 onwards. The magnitude of the projected free cash yields (over 30%) is very attractive indeed, particularly in the context of the expected dividend distributions, giving a dividend yield of 4.1% in FY09 rising to 9.7% in FY10.

### Discounted Cash Flow

DCF model based on 5% p.a. growth and 10% discount rate projects fair value of S¢21 (in line with the current share price)

Taking last year's free cash flow of S\$2.17m, running it in perpetuity and discounting back at 10% produces a net present value of \$21.7m. Less net debt of S\$1.6m, this equates to S¢10 per share. If growth in free cash flow of 2.5% is projected, this being a reasonable approximation for long-run GDP growth, fair value rises to S¢14 per share. At 5% growth the value is S¢21 per share. Choosing last year's free cash flow as the base is not unreasonable: FCF in FY07 was S\$0.9m and in FY08, S\$1.7m. Whilst we have considerably higher free cash projections in our explicit forecasts for FY10 and FY11, no allowance is included for the cost of buying or leasing additional aircraft. Such expenditure would, in our view, become necessary to underpin future growth.

### Share Price Target

Peer group comparison PER is 9x ...

The nearest comparison companies quoted in the UK are Dart Group (owner of Jet2), Easy Jet and Ryan Air. The prospective PER for each, based on consensus earnings estimates, are Dart Group 5.9x, Easy Jet 10.4x and Ryan Air 10.8x. Applying the average multiple for this comparator group (9.0x) to our estimate of earnings for the current year (S¢3.3) produces a price of S¢29.7 (12.9p). Excluding the one-off costs taken into the current year figures gives adjusted EPS of S¢6.6, which, when capitalised up at 9 times produces a price of S¢59.4 (25.8p). This is our target share price based on the analysis and assumptions contained in this Report.

... giving a target share price of 25p based on Skywest adjusted EPS for FY09

## Disclosures

### WH Ireland Recommendation Definitions

#### Buy

Expected to outperform the FTSE All Share by 15% or more over the next 12 months.

#### Outperform

Expected to outperform the FTSE All Share by 5/15% over the next 12 months.

#### Market Perform

Expected to perform in line with the FTSE All Share over the next 12 months.

#### Underperform

Expected to underperform the FTSE All Share by 5/15% or more over the next 12 months.

#### Sell

Expected to underperform the FTSE All Share by 15% or more over the next 12 months.

#### Speculative Buy

The stock has considerable level of upside but there is a higher than average degree of risk.

### Share Price Target

The share price target is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon.

### Stock Rating Distribution

As at the quarter ending 31 March 2009 the distribution of all our published recommendations is as follows:

Recommendation	Total Stocks	Percentage %	Corporate
Buy	40	41%	12
Speculative Buy	12	12%	12
Outperform	16	16%	1
Market Perform	19	19%	0
Underperform	8	9%	0
Sell	3	3%	0
<b>Total</b>	<b>98</b>	<b>100%</b>	<b>25</b>

This table demonstrates the distribution of WH Ireland recommendations. The first column illustrates the distribution in absolute terms with the second showing the percentages.

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WH Ireland acts as broker and NOMAD to this company

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The research analyst or analysts attest that the views expressed in this research report accurately reflect his or her personal views about the subject security and issuer. Furthermore, no part of his or her compensation was, is, or will be directly or indirectly related to the specific recommendation or views expressed in this research report.

### Exchange Rates

The following exchange rates have been used based on data obtained from Proquote: £1 = S\$2.30; A\$1 = S\$1.14

### Companies Mentioned

Company Name	Recommendation	Price	Price Date/Time
Dart Group	N/A	57p	27/5/2009 12:00
Easy Jet	N/A	320p	27/5/2009 12:00
Ryanair	N/A	€3.485	27/5/2009 12:00

Source: WH Ireland

### Share Price Date/Time

Company Name	Recommendation	Price	Price Date/Time
Skywest Airlines	Buy	8.5p	27/5/2009 12:00

Source: WH Ireland

### Summary of Company Notes

Headline	Recommendation	Price	Price Date/Time
Initiation of Coverage	Buy	10.5p	15/5/2006 13:30
Review	Buy	12p	15/11/2006 14:35
Review	Buy	14.75p	28/11/2007 10:00
Review	Buy	15.25p	20/3/2008 07:00
Review	Buy	8.5p	27/5/2009 12:00

Source: WH Ireland

### Summary of Security Recommendations

Skywest Airlines (formerly Advent Air)			
Recommendation	From	To	Analyst
Buy	16 May 2006	17 November 2006	PA
Buy	17 November 2006	Present	CA

Source: WH Ireland Current Analyst (CA), Previous Analyst (PA)

### Disclaimer

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