

ALASKA AIR GROUP INC
Form 8-K
April 07, 2005

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549**

FORM 8-K

**CURRENT REPORT PURSUANT
TO SECTION 13 OR 15(D) OF THE
SECURITIES EXCHANGE ACT OF 1934**

April 7, 2005

(Date of earliest event reported)

ALASKA AIR GROUP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware

(State or Other Jurisdiction of Incorporation)

1-8957

(Commission File Number)

91-1292054

(IRS Employer Identification No.)

19300 International Boulevard, Seattle, Washington

(Address of Principal Executive Offices)

98188

(Zip Code)

(206) 392-5040

(Registrant's Telephone Number, Including Area Code)

(Former Name or Former Address, if Changed Since Last Report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (*see* General Instruction A.2. below):

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
- Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
- Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
- Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

FORWARD-LOOKING INFORMATION

This report may contain forward-looking statements that are intended to be subject to the safe harbor protection provided by Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements relate to future events or our future financial performance and involve known and unknown risks and uncertainties that may cause our actual results or performance to be materially different from those indicated by any forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as forecast, may, will, could, should, expect, plan, believe, potential or other similar words indicating contingencies. Some of the things that could cause our actual results to differ from our expectations are: changes in our operating costs including fuel; our ability to meet our cost reduction goals; the competitive environment and other trends in our industry; economic conditions; actual or threatened terrorist attacks; global instability and potential U.S. military involvement; the outcome of contract talks with the Air Line Pilots Association, whether as a result of negotiations or binding arbitration; labor disputes; our reliance on automated systems; changes in laws and regulations; liability and other claims asserted against us; failure to expand our business; interest rates and the availability of financing; our ability to attract and retain qualified personnel; changes in our business plans; our significant indebtedness; downgrades of our credit ratings; and inflation. For a discussion of these and other risk factors, see Item 1 of the Company's Annual Report for the year ended December 31, 2004 on Form 10-K. All of the forward-looking statements are qualified in their entirety by reference to the risk factors discussed therein. These risk factors may not be exhaustive. We operate in a continually changing business environment, and new risk factors emerge from time to time. Management cannot predict such new risk factors, nor can it assess the impact, if any, of such new risk factors on our business or events described in any forward-looking statements. We disclaim any obligation to publicly update or revise any forward-looking statements after the date of this report to conform them to actual results.

ITEM 7.01. Regulation FD Disclosure

Pursuant to 17 CFR Part 243 (Regulation FD), the Company is submitting information relating to its financial and operational outlook for 2005. This report includes information regarding forecasts of available seat miles (ASMs), cost per available seat mile (CASM) excluding fuel consumption and impairment charge, as well as certain actual results for revenue passenger miles (RPMs), load factor and revenue per available seat mile (RASM), for its subsidiaries Alaska Airlines, Inc. and Horizon Air. Our disclosure of operating cost per available seat mile, excluding fuel and impairment charge provides us the ability to measure and monitor our performance without these items. In addition, we believe the disclosure of financial performance without mark-to-market hedging gains is useful to investors in evaluating our ongoing operational performance. The most directly comparable GAAP measure is total operating expense per available seat mile. However, due to the large fluctuations in fuel prices, we are unable to predict total operating expense for any future period with any degree of certainty. Please see the cautionary statement under Forward-Looking Information.

In accordance with General Instruction B.2 of Form 8-K, the following information shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the Exchange Act), nor shall such information be deemed incorporated by reference in any filing under the Securities Act of 1933, as amended, except as shall be expressly set forth by specific reference in such a filing. This Report will not be deemed an admission as to the materiality of any information required to be disclosed solely to satisfy the requirements of Regulation FD.

References in this report on Form 8-K to Air Group, the Company, we, us, and our refer to Alaska Air Group, Inc. and its subsidiaries, unless otherwise specified. Alaska Airlines, Inc. and Horizon Air Industries, Inc. are referred to as Alaska and Horizon, respectively, and together as our airlines.

First Quarter 2005

| | Forecast Q1 | Change Yr/Yr |
|--|------------------------|-------------------------|
| Alaska Airlines | | |
| Capacity (ASMs in millions) | 5,370 | 3.7% |
| Fuel gallons (000,000) | 84.0 | 1.4% |
| Cost per ASM as reported on a GAAP basis (cents)* | 11.0 | 5.5% |
| Less: Fuel cost per ASM (cents)* | 2.4 | 32.6% |
| Less: Impairment charge per ASM (cents)* | 0.1 | NM |
| Cost per ASM excluding fuel and impairment charge (cents)* | 8.5 | (1.7%) |

NM = Not Meaningful

Alaska Airlines March traffic increased 10% to 1.464 billion RPMs from 1.330 billion flown a year earlier. Capacity during March was 1.880 billion ASMs, 1.9% higher than the 1.845 billion in March 2004. The passenger load factor (the percentage of available seats occupied by fare-paying passengers) for the month was 77.9%, compared to 72.1% in March 2004. The airline carried 1,445,200 passengers compared to 1,336,300 in March 2004.

For February 2005, RASM remained flat as compared to February 2004. For January 2005, RASM decreased by 0.8% as compared to January 2004.

* For Alaska Airlines, our forecast of cost per ASM, fuel cost per ASM and impairment charge per ASM is based on forward-looking estimates, which will likely differ from actual results due to the volatility of fuel prices and the finalization of the impairment charge as discussed below. There are several factors impacting our estimates including, but not limited to, the volatility of fuel prices. As we are unable to apply hedge accounting, the majority of the benefit we realize from settled fuel hedge contracts is classified in other non-operating income on our statement of operations and is thus not reflected in fuel cost per ASM above. See pages 6 & 7 for additional information regarding fuel costs.

In March, Alaska Airlines notified the Port of Oakland that it would be terminating its Oakland hanger lease. As a result of the decision to exit the facility, certain leasehold improvements will be impaired. Alaska Airlines will record an associated impairment charge during the first quarter ranging from \$6.5 to \$7.5 million. The impairment charge per ASM computed above assumes total impairment of \$7 million, which is preliminary and subject to finalization.

| | Forecast Q1 | Change Yr/Yr |
|---|------------------------|-------------------------|
| Horizon Air | | |
| Capacity (ASMs in millions) | 778 | 12.4% |
| Fuel gallons (000,000) | 12.1 | 0.5% |
| Cost per ASM as reported on a GAAP basis (cents)* | 16.5 | (2.6%) |
| Less: Fuel cost per ASM (cents)* | 2.4 | 20.5% |
| Cost per ASM excluding fuel (cents)* | 14.1 | (5.7%) |

Horizon Air's March traffic increased 15.4% to 204.8 million RPMs from 177.5 million flown a year earlier. Capacity for March was 280.0 million ASMs, 5.5% higher than the 265.3 million in March 2004. The passenger load factor for the month was 73.1%, compared to 66.9% in March 2004. The airline carried 550,600 passengers compared to 485,100 in March 2004.

For the first quarter of 2005, CASM excluding fuel is expected to decrease 5.7% compared to the first quarter of 2004, reflecting changes in Horizon's flying mix from the traditional native network to a mix of native network flying and contract flying with Frontier Airlines, which began in January of 2004 and built up through the first half of 2004.

For February 2005, RASM decreased by 7.7% compared to February 2004 resulting from an increase in contract flying with Frontier. For January 2005, RASM decreased by 4.9% as compared to January 2004.

* For Horizon Air, our forecast of cost per ASM and fuel cost per ASM is based on forward-looking estimates, which will likely differ significantly from actual results. There are several factors impacting our estimates including, but not limited to, the volatility of fuel prices. As we are unable to apply hedge accounting, the majority of the benefit we realize from settled fuel hedge contracts is classified in other non-operating income on our statement of operations and is thus not reflected in fuel cost per ASM above. See pages 6 & 7 for additional information regarding fuel costs.

Other Financial Information*Liquidity and Capital Resources*

Cash and short-term investments totaled approximately \$761 million at March 31, 2005.

Fuel Hedging

Beginning in the second quarter of 2004, we lost the ability to defer, as a component of Accumulated Other Comprehensive Income, recognition of any unrealized gain or loss on our fuel hedge contracts until the hedged fuel is consumed (also known as the ability to use hedge accounting). The implications of this are :

we will have more volatile earnings as we mark our entire hedge portfolio to market each period-end and report the gain or loss in other non-operating income or expense,

because we mark our portfolio to market each period, the impact of the fuel hedging program will not be included in our results in the same period as the related fuel is purchased and consumed.

To help investors understand our results, we are providing unaudited information about fuel price movements and the impact of our hedging program on our financial results. Management believes it is useful to compare results between periods that exclude the hedging gains/losses recorded on a GAAP basis and include the cash received or due on hedge positions settled during the period (although the related impact may have been recognized for financial reporting purposes in a prior period). We refer to this as the comparison of economic fuel cost, which is presented below for the first two months of 2005.

Calculation of Economic Fuel Cost Per Gallon

January and

| | Alaska Airlines | Alaska Airlines | Horizon Air | Horizon Air Cost/Gal |
|---|--------------------|--------------------|----------------|-------------------------|
| (unaudited) | (000s) | Cost/Gal | (000s) | (cents) |
| February 2005 | | | | |
| Fuel expense before hedge activities (raw fuel) | \$ 79,440 | \$ 1.45 | \$ 11,669 | \$ 1.51 |
| Gains on settled hedges included in fuel expense | 2,328 | .04 | 227 | .03 |
| GAAP fuel expense | \$ 77,112 | \$ 1.41 | \$ 11,442 | \$ 1.48 |
| Gains on settled hedges included in non-operating income* | 8,809 | .16 | 1,437 | .19 |
| Economic fuel expense | \$ 68,303 | \$ 1.25 | \$ 10,005 | \$ 1.29 |
| % Change from prior year | 14.1% | 12.6% | 9.6% | 9.3% |

Mark-to-Market Adjustment Related to Unsettled Hedges January and February 2005 (unaudited)

Mark-to-market gains included in non-operating income related to hedges that settle in future periods \$ 38,805 NM \$ 6,459 NM

*Amounts may include mark-to-market hedging gains (losses) recognized in non-operating income (expense) in previous periods.

For Alaska Airlines and Horizon Air, GAAP fuel expense per gallon for the quarter is expected to be approximately \$1.54 and \$1.59, respectively. The economic fuel expense per gallon for the quarter is expected to be approximately \$1.34 and \$1.39 for Alaska Airlines and Horizon Air, respectively. March mark-to-market gains included in non-operating income related to hedges that settle in future periods are expected to be approximately \$45 million for the combined Air Group, bringing the total for the quarter to approximately \$90 million.

Our forecast of GAAP and economic fuel expense per gallon for the first quarter is based on forward-looking estimates, which will likely differ from actual results. There are several factors impacting our estimates including, but not limited to, the volatility of fuel prices and consumption.

Alaska Air Group's future hedge positions are as follows:

| | Approximate % of Expected Fuel Requirements | Approximate Crude Oil Price per Barrel |
|---------------------|---|--|
| Second Quarter 2005 | 50% | \$ 28.97 |
| Third Quarter 2005 | 50% | \$ 28.81 |
| Fourth Quarter 2005 | 50% | \$ 31.85 |
| First Quarter 2006 | 50% | \$ 35.70 |
| Second Quarter 2006 | 50% | \$ 39.76 |
| Third Quarter 2006 | 40% | \$ 41.58 |
| Fourth Quarter 2006 | 30% | \$ 42.70 |
| First Quarter 2007 | 20% | \$ 43.09 |
| Second Quarter 2007 | 15% | \$ 43.86 |
| Third Quarter 2007 | 15% | \$ 43.50 |
| Fourth Quarter 2007 | 9% | \$ 47.29 |
| First Quarter 2008 | 5% | \$ 51.56 |

Operating Fleet Plan

The following table provides a fleet summary for Alaska and Horizon for actual airplanes on hand as of the date of this report and changes during the remainder of 2005 based on our contractual commitments and expected retirement plans:

| | Seats | On Hand April 07, 2005 | Expected change During Remainder of 2005 |
|------------------------|--------------|---|---|
| Alaska Airlines | | | |
| B737-200C | 111 | 7 | (1) |
| B737-400 | 144 | 40 | |
| B737-700 | 120 | 22 | |
| B737-800 | 160 | 2 | 1 |
| B737-900 | 172 | 12 | |
| MD-80 | 140 | 26 | |
| Total | | 109 | 0 |
| Horizon Air | | | |
| Q200 | 37 | 28 | |
| Q400 | 70 | 19 | (1) |
| CRJ 700 | 70 | 19 | |
| Total | | 66 | (1) |

Alaska has commitment to acquire three B737-800 aircrafts in 2006. Horizon has two CRJ 700s scheduled for delivery per year from 2006 to 2009 and none thereafter.

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ALASKA AIR GROUP, INC.

Registrant

Date: April 7, 2005

/s/ Brandon S. Pedersen

Brandon S. Pedersen
Staff Vice President/Finance and Controller

/s/ Bradley D. Tilden

Bradley D. Tilden
Executive Vice President/Finance and Chief Financial
Officer