

ALASKA AIR GROUP INC  
Form 8-K  
March 17, 2006

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**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**

March 17, 2006

(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)

**(206) 392-5040**

**98188**  
(Zip Code)

(Registrant's Telephone Number, Including Area Code)

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(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)

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- “ 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))
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FORWARD-LOOKING INFORMATION

This report contains forward-looking statements 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 and involve known and unknown risks and uncertainties that may cause actual outcomes to be materially different from those indicated by any forward-looking statements. Some of the things that could cause our actual results to differ from our expectations are: the competitive environment and other trends in our industry; changes in our operating costs including fuel, which can be volatile; our ability to meet our cost reduction goals; our inability to achieve or maintain profitability and fluctuations in our quarterly results; our significant indebtedness; our inability to secure new aircraft financing; the implementation of our growth strategy; the timing of the MD-80 fleet disposal, the market value of MD-80 aircraft, and the amounts of potential lease termination payments with lessors and sublease payments from sublessees; compliance with our financial covenants; potential downgrades of our credit ratings and the availability of financing; the concentration of our revenue from a few key markets; general economic conditions, as well as economic conditions in the geographic regions we serve; actual or threatened terrorist attacks; global instability and potential U.S. military actions or activities; insurance costs; labor disputes; our ability to attract and retain qualified personnel; an aircraft accident or incident; liability and other claims asserted against us; operational disruptions; increases in government fees and taxes; changes in laws and regulations; our reliance on automated systems; and our reliance on third-party vendors and partners. For a discussion of these and other risk factors, see Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2005. 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 press release 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 costs and other noted items, 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 other noted items, provides us the ability to measure and monitor our performance without these items. 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. 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. 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 2006**

On March 13, 2006, the Company announced its plan to transition to a single fleet type, the Boeing 737, by the end of 2008, which includes an acceleration of the retirement of its MD-80 fleet. The Company's fleet currently includes 15 owned and 11 leased MD-80 aircraft. As a result of this decision, during the first quarter of 2006, we will record a non-cash impairment charge associated with the owned MD-80 fleet. Although the actual amount has not yet been finalized, we expect the impairment charge to be between \$130 million and \$150 million, before tax (between \$80 million and \$95 million, after tax). For purposes of the first quarter forecast, Alaska assumed a \$140 million pre-tax charge. The actual charge could differ materially from this forecast.

	Forecast Q1	Change Yr/Yr
<b>Alaska Airlines</b>		
Capacity (ASMs in millions)	5,531	3%
Fuel gallons (000,000)	84.4	
Cost per ASM as reported on a GAAP basis (cents)*	13.75	24%
Less: Impairment charges and fleet exit costs per ASM (cents)	2.50	NM
Less: Fuel cost per ASM (cents)*	3.00	26%
<b>Cost per ASM excluding fuel, impairment charges and fleet exit costs (cents)*</b>	<b>8.25</b>	<b>(4)%</b>

NM = Not meaningful

Alaska Airlines February traffic increased 6.4% to 1.260 billion RPMs from 1.184 billion flown a year earlier. Capacity during February was 1.711 billion ASMs, 2.1 % higher than the 1.676 billion in February 2005. The passenger load factor (the percentage of available seats occupied by fare-paying passengers) for the month was 73.7%, compared to 70.7% in February 2005. The airline carried 1,209,400 passengers compared to 1,174,800 in February 2005.

In February 2006, RASM increased 11% compared to February 2005 due primarily to an increase in yields per RPM.

\* For Alaska, our forecasts of cost per ASM and fuel cost per ASM are based on forward-looking estimates, which will likely differ from actual results due to the volatility of fuel prices. There are several factors impacting our estimates including, but not limited to, the volatility of fuel prices and the finalization of labor agreements. 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 page 5 for additional information regarding fuel costs.

	Forecast Q1	Change Yr/Yr
<b>Horizon Air</b>		
Capacity (ASMs in millions)	874	12%
Fuel gallons (000,000)	13.0	8%
Cost per ASM as reported on a GAAP basis (cents)*	17.2	3%
Less: Fuel cost per ASM (cents)*	3.0	26%
Cost per ASM excluding fuel (cents)*	14.2	(1)%

Horizon Air's February traffic increased 19.7% to 195.3 million RPMs from 163.2 million flown a year earlier. Capacity during February was 273.2 million ASMs, 12.8% higher than the 242.2 million in February 2005. The passenger load factor for the month was 71.5%, compared to 67.4% in February 2005. The airline carried 502,300 passengers compared to 449,800 in February 2005.

In February 2006, RASM increased 10.3% compared to February 2005 due primarily to an increase in yields per RPM, offset by the decrease in load factor.

\* For Horizon, our forecasts of cost per ASM and fuel cost per ASM are 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 page 5 for additional information regarding fuel costs.

#### **Other Financial Information**

##### *Liquidity and Capital Resources*

Cash and short-term investments increased as of February 28, 2006 to approximately \$961 million compared to \$927 million at January 31, 2005.

##### *Fuel Hedging*

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 mark-to-market 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 January and February 2006.

Calculation of Economic Fuel Cost Per Gallon

January and February 2006 (unaudited)	Alaska Airlines		Horizon Air	
	(\$ in millions)	Alaska Airlines Cost/Gal	(\$ in millions)	Horizon Air Cost/Gal (cents)
Fuel expense before hedge activities ( raw fuel )	\$ 107.8	\$ 1.97	\$ 17.2	\$ 2.07
Gains on settled hedges included in fuel expense	(0.4)	(.01)	(0.1)	(.01)
GAAP fuel expense	\$ 107.4	\$ 1.96	\$ 17.1	\$ 2.06
Gains on settled hedges included in non-operating income*	(17.0)	(.31)	(2.8)	(.34)
Economic fuel expense	\$ 90.4	\$ 1.65	\$ 14.3	\$ 1.72
% Change from prior year	32%	30%	43%	33%

Mark-to-Market Adjustment Related to Unsettled Hedges

Mark-to-market gains included in non-operating income related to hedges that settle in future periods, net of the reclassification of previously recorded mark-to-market gains to <i>Gains on settled hedges included in non-operating income</i>	\$ (6.3)	NM	\$ 0.4	NM
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\* 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 \$1.97 and \$2.05, respectively. The economic fuel expense per gallon for the quarter is expected to be approximately \$1.67 and \$1.73 for Alaska Airlines and Horizon Air, respectively.

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

	Approximate % of Expected Fuel Requirements	Approximate Crude Oil Price per Barrel
First Quarter 2006	52%	\$ 35.70
Second Quarter 2006	53%	\$ 39.76
Third Quarter 2006	46%	\$ 43.41
Fourth Quarter 2006	35%	\$ 46.10
First Quarter 2007	20%	\$ 43.09
Second Quarter 2007	19%	\$ 45.11
Third Quarter 2007	22%	\$ 45.27
Fourth Quarter 2007	17%	\$ 47.89
First Quarter 2008	11%	\$ 50.44
Second Quarter 2008	6%	\$ 49.26
Third Quarter 2008	6%	\$ 48.97
Fourth Quarter 2008	5%	\$ 48.68

**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. One CRJ700 was delivered in January, two B737-800s were delivered in February, and two Q400s were delivered in March.

	Seats	On Hand March 17, 2006
<b>Alaska Airlines</b>		
B737-200C	111	7
B737-400	144	40
B737-700	124	22
B737-800	157	5
B737-900	172	12
MD-80	140	26
Total		112
<b>Horizon Air</b>		
Q200	37	28
Q400	74	20
CRJ 700	70	21*
Total		69

\* Includes one CRJ700 on a short-term operating lease agreement.

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The following table summarizes firm aircraft commitments for Alaska (B737-800) and Horizon (Q400) by year, excluding aircraft that have already been delivered in 2006:

	2006 (Remaining)	2007	2008	2009	2010	Thereafter	Total
B737-800	8	11	7	4	6	3	39
Q-400	2	10					12
<b>Totals</b>	<b>10</b>	<b>21</b>	<b>7</b>	<b>4</b>	<b>6</b>	<b>3</b>	<b>51</b>

In addition to the firm orders noted above, Alaska has options to acquire 32 additional B737-800s and purchase rights for 27 more. Alaska has also entered into operating lease agreements for two B737-800 aircraft to be delivered in 2006. Horizon has options to acquire 20 Q400s and 15 CRJ700s.

As noted above, on March 13, 2006, the Company announced its plan to transition to a single fleet type, the Boeing 737, by the end of 2008, which includes an acceleration of the retirement of its MD-80 fleet. As a result, the Company expects to exercise additional options and purchase rights on its Boeing 737-800 order in the future.

Giving consideration to the fleet transition plan discussed above, the following table displays the anticipated fleet count for Alaska Airlines, Inc. as of December 31:

	2005	2006	2007	2008
737-200	7	3	0	0
MD80	26	21	15	0
737-400	40	40	40	40
737-700	22	22	20	20
737-800*	3	15	28	42
737-900	12	12	12	12
	<b>110</b>	<b>113</b>	<b>115</b>	<b>114</b>

\* Includes options for 2 aircraft in 2007 and 6 aircraft in 2008 which have not yet been exercised. The total also assumes Alaska will identify one airplane for delivery in 2008 for which the Company has not secured a delivery position.



**Signatures**

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: March 17, 2006

/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