

ALASKA AIR GROUP INC
Form 8-K
January 06, 2005

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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**

January 5, 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 Pacific Highway South, 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)

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o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

o 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 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; the competitive environment and other trends in our industry; economic conditions; our reliance on automated systems; actual or threatened terrorist attacks, global instability and potential U.S. military involvement; our ability to meet our cost reduction goals; the outcome of contract talks with the Air Line Pilots Association, whether as a result of negotiations or binding arbitration; labor disputes; 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 Amendment No. 1 to its Annual Report for the year ended December 31, 2003 on Form 10-K/A. 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.

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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 2004. This report includes information regarding forecasts of available seat miles (ASMs), cost per available seat mile (CASM) excluding fuel consumption and the restructuring charges associated with our recently announced restructuring efforts, 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 restructuring charges provides us the ability to measure and monitor our performance without these items. In addition, we believe the disclosure of financial performance without restructuring charges and 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.

Table of Contents**Fourth Quarter 2004**

| | Forecast Q4 | Change Yr/Yr |
|-----------------------------|------------------------|-------------------------|
| Alaska Airlines | | |
| Capacity (ASMs in millions) | 5,452 | 5.0% |
| Fuel gallons (000,000) | 86.4 | 3.6% |

* For Alaska, our forecast of cost per available seat mile, fuel cost per available seat mile and restructuring charge per available seat mile is based on forward-looking estimates which will likely differ from actual results due to the volatility of fuel prices. Factors impacting our estimates include (but are not limited to) volatility of fuel prices and estimated severance and benefit costs associated with our restructuring activities as discussed in previous periods.

Alaska Airlines December traffic increased 8.6% to 1.413 billion RPMs from 1.301 billion flown a year earlier. Capacity during December was 1.860 billion ASMs, 4.2% higher than the 1.785 billion in December 2003. The passenger load factor (the percentage of available seats occupied by fare-paying passengers) for the month was 76.0%, compared to 72.9% in December 2003. The airline carried 1,407,300 passengers compared to 1,317,000 in December 2003.

Alaska Airlines November traffic increased 11.2% to 1.312 billion RPMs from 1.180 billion flown a year earlier. Capacity during November was 1.791 billion ASMs, 6.2% higher than the 1.687 billion in November 2003. The passenger load factor for the month was 73.3%, compared to 70.0% in November 2003. The airline carried 1,320,200 passengers compared to 1,211,600 in November 2003.

Based on preliminary yield information and actual load factor, we expect fourth quarter RASM to decline modestly compared to prior year.

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| | Forecast Q4 | Change Yr/Yr |
|-----------------------------|------------------------|-------------------------|
| Horizon Air | | |
| Capacity (ASMs in millions) | 793 | 28.1% |
| Fuel gallons (000,000) | 12.4 | (5.3%) |

* For Horizon, our forecast of cost per available seat mile and fuel cost per available seat mile is based on forward-looking estimates which will likely differ significantly from actual results. Factors impacting our estimates include (but are not limited to) volatility of fuel prices.

Horizon Air's December traffic increased 40.5% to 201.0 million RPMs from 143.1 million flown a year earlier. Capacity for December was 270.5 million ASMs, 30.2% higher than the 207.8 million in December 2003. The passenger load factor for the month was 74.3%, compared to 68.9% in December 2003. The airline carried 548,200 passengers compared to 430,900 in December 2003.

Horizon Air's November traffic increased 39.7% to 187.6 million RPMs from 134.3 million flown a year earlier. Capacity for November was 255.9 million ASMs, 27.6% higher than the 200.6 million in November 2003. The passenger load factor for the month was 73.3%, compared to 67.0% in November 2003. The airline carried 511,000 passengers compared to 402,500 in November 2003.

For the fourth quarter of 2004, CASM excluding fuel is expected to decrease 18.3% compared to the fourth quarter of 2003, 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. Under the contract flying agreement with Frontier, Horizon does not incur many of the normal costs of operations such as fuel, marketing costs and station labor and rents, resulting in significantly lower CASM (excluding fuel) and RASM. Horizon is currently operating nine 70-seat Bombardier CRJ-700 aircraft under the Frontier JetExpress brand, representing approximately 20% to 25% of total Horizon capacity and approximately 9% to 10% of total Horizon revenue.

For the quarter, we expect RASM to decline substantially compared to prior year due to the contract flying with Frontier and yield reductions offset by higher load factors.

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Other Financial Information

Liquidity and Capital Resources

Cash and short-term investments totaled approximately \$872 million at December 31, 2004.

Alaska's \$150 Million Credit Facility expired on December 23, 2004. The Company is currently negotiating a replacement facility and expects to close the new transaction during the first quarter 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 loss going forward are as follows:

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 October and November 2004.

Table of Contents*Calculation of Economic Fuel Cost Per Gallon*

| October and November 2004 (unaudited) | Alaska Airlines (000s) | Alaska Airlines Cost/Gal | Horizon Air (000s) | Horizon Air Cost/Gal (cents) |
|--|------------------------------|--------------------------------|--------------------------|------------------------------------|
| Fuel expense before hedge activities (raw fuel) | \$ 95,236 | \$ 1.66 | \$ 14,199 | \$ 1.73 |
| Gains on settled hedges included in fuel expense | 2,444 | .04 | 334 | .04 |
| GAAP fuel expense | \$ 92,792 | \$ 1.62 | \$ 13,865 | \$ 1.69 |
| Gains on settled hedges included in non-operating income* | 10,739 | .19 | 1,465 | .18 |
| Economic fuel expense | \$ 82,053 | \$ 1.43 | \$ 12,400 | \$ 1.51 |
| % Change from prior year | 62.9% | 55.4% | 49.9% | 58.9% |

Mark-to-Market Adjustment Related to Unsettled Hedges

| | | | | | |
|---|--|-----------|----|----------|----|
| Mark-to-market gains (losses) included in non-operating income related to hedges that settle in future periods | | \$ 11,786 | NM | \$ 1,607 | NM |
|---|--|-----------|----|----------|----|

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

Based on fluctuations in fuel prices during the month of December, we expect to record a significant mark-to-market loss in December in non-operating income related to hedges that settle in future periods.

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

| | Approximate % of Expected Fuel Requirements | Approximate Crude Oil Price per Barrel |
|---------------------|--|--|
| Fourth Quarter 2004 | 50% | \$ 30.39 |
| First Quarter 2005 | 50% | \$ 29.86 |
| 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 | 40% | \$ 37.05 |
| Third Quarter 2006 | 30% | \$ 38.78 |
| Fourth Quarter 2006 | 20% | \$ 40.60 |
| First Quarter 2007 | 10% | \$ 39.78 |
| Second Quarter 2007 | 10% | \$ 39.44 |
| Third Quarter 2007 | 10% | \$ 39.12 |
| Fourth Quarter 2007 | 5% | \$ 42.65 |

Operating Fleet Plan

The following table provides a fleet summary for Alaska and Horizon for actual airplanes on hand at the end of 2003 and changes in 2004 and 2005 based on our contractual commitments and expected retirement plans:

| | Seats | Change On Hand YE 2003 | Change During 2004 | Change During 2005 |
|------------------------|-------|------------------------------|--------------------------|--------------------------|
| Alaska Airlines | | | | |
| B737-200C | 111 | 9 | (2) | (1) |
| B737-400 | 138 | 40 | | |
| B737-700 | 120 | 22 | | |
| B737-800 | 160 | 0 | | 3 |
| B737-900 | 172 | 11 | 1 | |
| MD-80 | 140 | 27 | (1) | |

| | | | | |
|--------------------|----|-----|-----|---|
| Total | | 109 | (2) | 2 |
| Horizon Air | | | | |
| Q200 | 37 | 28 | | |
| Q400 | 70 | 16 | 2 | |
| CRJ 700 | 70 | 18 | | 1 |
| Total | | 62 | 2 | 1 |

Alaska has no firm commitments for aircraft deliveries beyond 2005. However, we plan to acquire three B737-800s in 2006. These planned acquisitions are not included in the table above since we do not have firm commitments at this time. Horizon has two CRJ 700s scheduled for delivery per year from 2006 to 2009 and none thereafter.

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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: January 5, 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