

Pacific Air Lines 26th Annual Report 1965



*Nineteen hundred sixty-five
annual report
marking twenty-six years
of service*

26

***Pacific Air Lines 727 Jet Service
sets a new World Standard
for Local Air Travel***



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DIRECTORS AND OFFICERS

MATTHEW E. McCARTHY, *Chairman of the Board and Chief Executive Officer, Member of the Executive Committee*

DAVID R. GRACE, *Director and Member of the Executive Committee*
General Partner, Sterling, Grace & Co., New York

RICHARD E. LANG, *Director and Member of the Executive Committee*
Chairman of the Board of Lang & Co., Seattle

JOSEPH MARTIN, JR., *Director*
Partner in the Law Firm of Allan, Miller, Groezinger, Keesling & Martin, San Francisco

LLOYD W. MARTIN, *Director*
President of Reed & Martin, Inc., Honolulu

IAN G. THOMSON, *Director*
President of The Chartered Bank of London, San Francisco

MAX H. WYMAN, *Director*
Partner—M. A. Wyman Lumber Co., Seattle

HARRY S. WHITE, *Director and President*

ROBERT SETRAKIAN, *Director*
President of Setrakian and Company, San Francisco
Chairman of the Board of the Valley National Bank

C. A. MYHRE, *Director and Executive Vice President*

JAMES T. KILBRETH, JR., *Senior Vice President, Marketing*

R. C. COUK, *Vice President, Flight Operations*

DARROL G. DAVISON, *Vice President,*
Engineering and Maintenance

R. E. COSTELLO, *Vice President, Traffic*

E. R. DAHL, *Secretary Treasurer*



Matthew E. McCarthy



David R. Grace



Richard E. Lang



Harry S. White



Joseph Martin, Jr.



Lloyd W. Martin



Ian G. Thomson



Max H. Wyman



Robert Setrakian



C. A. Myhre



James T. Kilbreth, Jr.



R. E. Costello



Darrol G. Davison



R. C. Couk



E. R. Dahl

*Matthew E. McCarthy, seated,
Pacific's Board Chairman
and Chief Executive Officer, with
William M. Allen, President of
The Boeing Company, after affixing
his signature to the agreement for
727 and 737 pure jet aircraft.*

DEAR STOCKHOLDER: The year 1965 surpassed 1964, the previous high in gross revenues and net operating earnings for Pacific Air Lines. Sharing proportionately in the general gains in the aviation industry, your company's gross revenues were \$14,684,589 in 1965, compared to \$13,446,890 in 1964. Net income in 1965 was \$700,337, compared to \$583,504 in the previous year, which, on an adjusted share basis, represented \$0.70 a share in 1965, compared with \$0.62 a share in 1964. The year 1965 was highlighted by major policy moves. After careful evaluation, your company purchased four Boeing 737's for delivery in late 1967 and early 1968 and secured options for four additional Boeing 737's. Two Boeing 727's were leased for delivery in June and July 1966, and options for two additional 727's for delivery in early 1967 were obtained. Based on present and projected traffic, we believe that the pure jet equipment under contract meets our needs and provides adequate flexibility for growth potential. During 1965 a long term lease was negotiated for 16 acres at San Francisco International Airport whereon our new, up-to-date administration building and maintenance base will be completed in October 1966. Our computer installation (IBM 360) will be in operation in our new administration building in 1966, and much needed consolidation of our personnel will be obtained. These acquisitions will entail personnel training and other introductory costs which will add to the 1966 operational expenses. In late 1965 the company's outstanding



convertible debentures were called and practically all were converted to capital stock, thus increasing our net worth and eliminating interest and reserve requirements. Your company, recognizing in 1965 that aviation's expanding market and the addition of jet equipment would require an aggressive, new marketing philosophy, reorganized its marketing department and new promotion programs are underway. ✚ During the year, Mr. James T. Kilbreth, Jr., was appointed senior vice president in charge of marketing, Mr. R. C. Couk was advanced to vice president in charge of flight operations and Mr. Darrol G. Davison was advanced to vice president in charge of engineering and maintenance. ✚ The Civil Aeronautics Board hearings in the transfer of United Air Lines' route in the San Joaquin Valley to Pacific Air Lines were completed in 1965, and we are awaiting the Board's decision. We believe that it will be favorable, and we anticipate a large passenger increase through this transfer. ✚ Your company's relations with the unions representing our employees have continued on a friendly, cooperative basis. In view of increasing competition and rising costs, it is pleasant to acknowledge again the excellent cooperation of stockholders, management, the staff and employees.
In behalf of the Board of Directors

Matthew E. McBeth Chairman



Construction is underway for occupancy in October of a new general office and jet-age maintenance base, including installation of IBM computer equipment for greater efficiency.

FINANCIAL HIGHLIGHTS

FINANCIAL

	1965	1964	
Total revenues	\$14,684,589	\$13,446,890	9%
Operating income	\$ 1,462,036	\$ 1,291,343	13%
Net earnings	\$ 700,337	\$ 583,504	20%
Earnings per share—based upon average number of shares outstanding during the year	\$ 0.70	\$ 0.62	13%
Long-term debt	\$ 2,518,405	\$ 4,980,253	49%
Working capital	\$ 837,833	\$ 903,593	(7%)
Stockholders' equity	\$ 6,237,502	\$ 4,391,818	42%
Shares outstanding at end of year	1,186,580	978,598	21%
Book value per share	\$ 5.26	\$ 4.49	17%

STATISTICAL

Revenue miles flown	6,302,180	5,766,794	9%
Available seat miles (000)	261,311	239,802	9%
Revenue passenger miles (000)	138,379	128,386	8%
Revenue passengers	695,131	612,539	13%
Passenger load factor	53.0%	53.5%	—
Passenger revenues per passenger mile	7.3¢	7.0¢	4%
Number of airports served	30	30	—
Number of aircraft	18	18	—
Number of employees at end of year	802	768	4%

PACIFIC AIR LINES

Present

16 PACIFIC WONDERLAND HOLIDAYS

FOR THOSE WHO THINK THEY'VE SEEN EVERYTHING



"We Fly to the Nicest Places" is the theme of an intensive nationwide sales promotion campaign, designed to encourage local residents and visitors to the West from all over the world to travel the entire Wonderland served by Pacific.

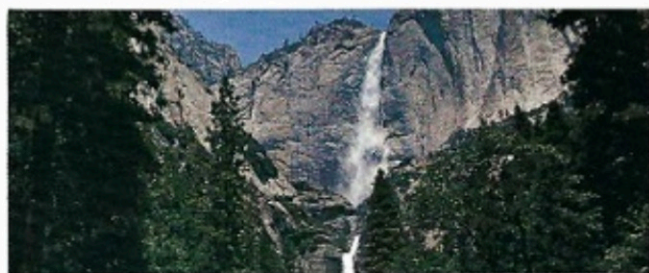
MONTEREY/CARMEL HOLIDAY 3 DAYS 2 NIGHTS



YOSEMITE HOLIDAY

3 DAY TOUR FROM FRESNO

1 NIGHT in both Fresno and Yosemite



LAKE TAHOE HOLIDAY 3 DAYS 2 NIGHTS



RENO HOLIDAY 3 DAYS 2 NIGHTS

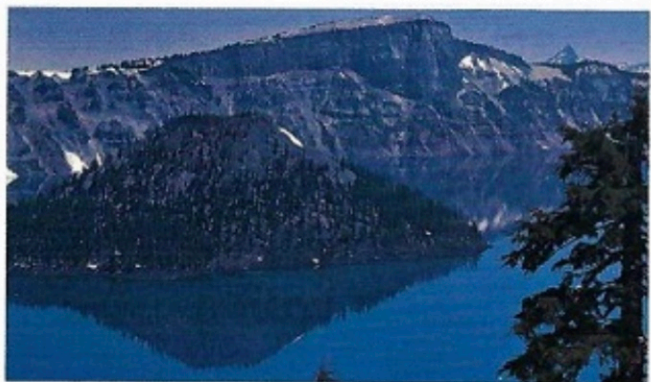


GIANT REDWOODS HOLIDAY 3 DAYS 2 NIGHTS



OREGON HOLIDAY

3 DAYS 2 NIGHTS



SAN FRANCISCO HOLIDAY 3 DAYS 2 NIGHTS



LAKE SHASTA HOUSEBOAT HOLIDAY

8 DAYS 7 NIGHTS



LOS ANGELES/ HOLLYWOOD HOLIDAY

3 DAYS 2 NIGHTS



PACIFIC AIR LINES, INC.

Assets

CURRENT ASSETS:	<i>December 31</i>	
	<i>1965</i>	<i>1964</i>
Cash (including time deposits, 1965— \$1,000,000; 1964—\$1,200,000)	\$ 2,230,168	\$ 2,198,215
Accounts receivable:		
United States Government— mail, passenger and other	614,807	563,883
Traffic and agents	475,396	423,823
Miscellaneous, less allowance for doubtful accounts (1965 and 1964—\$8,000)	60,270	66,231
Expendable parts and supplies, at approximate cost, less reserves	545,745	678,457
Prepaid expenses	193,222	102,184
Total current assets	<u>4,119,608</u>	<u>4,032,793</u>
PROPERTY AND EQUIPMENT, at cost—pledged under notes payable (Note 1):		
Flight equipment	11,780,154	11,722,732
Ground and other equipment	1,124,358	1,145,726
	<u>12,904,512</u>	<u>12,868,458</u>
Less—Accumulated depreciation and amortization	5,296,604	4,451,345
	<u>7,607,908</u>	<u>8,417,113</u>
Advance payments on flight equipment (Note 6)	288,855	
	<u>7,896,763</u>	<u>8,417,113</u>
OTHER ASSETS:		
Unamortized debt discount and expense (Note 4)	14,632	127,007
Route extension and development expense, less amortization	120,323	38,510
Preoperating cost of new flight equipment, less amortization	65,977	46,743
Other	48,006	5,971
	<u>248,938</u>	<u>218,231</u>
	<u>\$12,265,309</u>	<u>\$12,668,137</u>

BALANCE SHEET **Liabilities**

CURRENT LIABILITIES:

	<i>December 31</i>	
	<i>1965</i>	<i>1964</i>
Notes payable—current instalments (Note 1)	\$ 986,448	\$ 1,053,448
Accounts payable	1,224,401	1,013,550
Taxes collected or withheld from others	238,049	173,267
Accrued expenses	316,080	352,443
Unearned transportation revenue	211,265	202,492
Federal income taxes (Note 3)	178,754	334,000
6½% convertible subordinated debentures, redeemed in January, 1966 (Note 2)	126,778	
Total current liabilities	<u>3,281,775</u>	<u>3,129,200</u>

LONG-TERM DEBT:

Notes payable to bank (Note 1)	2,518,405	3,605,353
6½% convertible subordinated debentures (Note 2)		1,374,900
	<u>2,518,405</u>	<u>4,980,253</u>
FEDERAL INCOME TAXES DEFERRED TO FUTURE YEARS	<u>227,627</u>	<u>166,866</u>

STOCKHOLDERS' EQUITY (Notes 1, 2 and 4):

Common stock:		
Authorized, 40,000,000 shares of 50¢ par value per share		
Outstanding, 1965—1,186,580; 1964—978,598 shares	593,290	489,299
Paid-in surplus	2,438,079	1,396,723
Earnings retained for use in the business, per accompanying statement	3,206,133	2,505,796
	<u>6,237,502</u>	<u>4,391,818</u>

COMMITMENTS AND CONTINGENT LIABILITIES (Note 6)

	<u>\$12,265,309</u>	<u>\$12,668,137</u>
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STATEMENT OF EARNINGS

	<i>December 31</i>	
	<i>1965</i>	<i>1964</i>
Operating revenues:		
Passenger	\$10,134,450	\$ 8,940,197
Mail	266,622	233,271
Express, freight and excess baggage	394,977	342,707
Other	193,857	236,565
	<u>10,989,906</u>	<u>9,752,740</u>
Public service revenue	3,694,683	3,694,150
	<u>14,684,589</u>	<u>13,446,890</u>
Operating expenses:		
Flying operations	3,364,356	3,101,332
Maintenance	2,983,030	2,660,339
Passenger service	506,538	411,975
Aircraft and traffic servicing	3,038,357	2,807,546
Promotion and sales	1,316,260	1,369,331
General and administrative	969,663	864,915
Depreciation	1,016,967	902,654
Amortization of preoperating and route development costs	27,382	37,455
	<u>13,222,553</u>	<u>12,155,547</u>
Operating income	<u>1,462,036</u>	<u>1,291,343</u>
Other expenses:		
Interest (less interest income, 1965—\$64,465; 1964—\$29,873)	258,718	354,818
Loss on disposition of assets	8,398	27,165
Other	19,583	59,542
	<u>286,699</u>	<u>441,525</u>
Income before federal income taxes	<u>1,175,337</u>	<u>849,818</u>
Estimated federal income taxes (including \$61,000 in 1965 and \$56,000 in 1964 deferred to future years) (Note 3)	475,000	266,314
Net income for the year	<u>700,337</u>	<u>583,504</u>
Excess of insurance proceeds over carrying value of aircraft destroyed, net of income taxes of \$123,983		387,724
Earnings retained for use in the business:		
Balance, beginning of year	2,505,796	1,534,568
Balance, end of year (Note 1)	<u>\$ 3,206,133</u>	<u>\$ 2,505,796</u>

NOTES TO FINANCIAL STATEMENTS

NOTE 1—Notes payable:	December 31	
	1965	1964
5 $\frac{1}{4}$ % note payable in monthly instalments of \$38,550 to April 1967 and thereafter in monthly instalments of \$5,550 to Feb. 1969	\$ 754,690	\$1,217,290
5 $\frac{3}{4}$ % note payable in monthly instalments of \$43,654 to March 1971	2,750,163	3,274,011
6% note paid in 1965		167,500
	<u>\$3,504,853</u>	<u>\$4,658,801</u>
Less: Instalments due within one year	986,448	1,053,448
Instalments due after one year	<u>\$2,518,405</u>	<u>\$3,605,353</u>

The Company's turbo-prop aircraft and related spare parts are pledged as security under chattel mortgages for the loans. The Civil Aeronautics Board has guaranteed 90% of the principal amount and 100% of the interest on the 5 $\frac{1}{4}$ % loan.

Under the terms of the loan agreements, the Company has agreed that (1) it will not, without the prior consent of the bank, pay any dividends (except in stock) or purchase, redeem or otherwise acquire for value any of its outstanding shares, and (2) it will main-

tain current assets at least equal to current liabilities (excluding the current portion of notes payable).

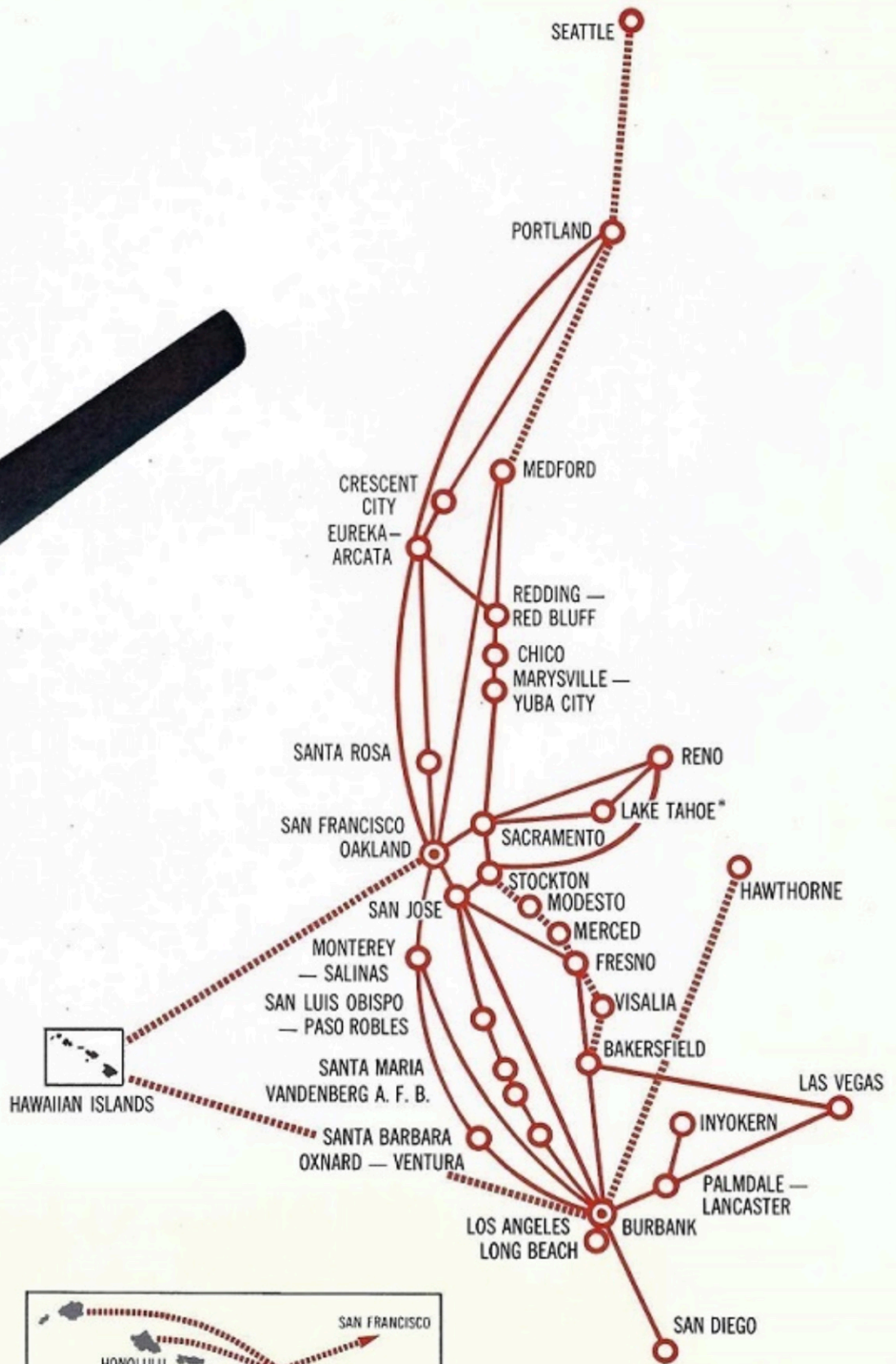
NOTE 2—Debentures:

On December 9, 1965, the Company called all outstanding 6 $\frac{1}{2}$ % convertible subordinated debentures for redemption at 105% of the principal amount. In accordance with the terms of indenture agreement, the debentures alternatively were convertible into common stock of the Company at the conversion price of \$6.00 per share. As of December 31, 1965, debentures in the principal amount of \$579,700 were outstanding, of which \$452,922 were converted by January 5, 1966 into 75,487 shares of common stock and the remainder redeemed on January 10, 1966. The redemptions and conversions subsequent to the year end have been reflected in the accompanying financial statements, the debentures redeemed being included in current liabilities and those converted in common stock as if issued as of December 31, 1965.

NOTE 3—Investment tax credit:

The Company's provision for federal income taxes charged against current income has been reduced by investment tax credits of \$94,000 in 1965 and \$153,000 in 1964 resulting from acquisitions of qualified property.





ROUTE APPLICATIONS

*In addition to Pacific's present service to Lake Tahoe your Company is awaiting decision by the Civil Aeronautics Board on its application to fly non-stop between Lake Tahoe and all other points in California.

