



ANNUAL REPORT · 1966

HERE'S OUR RECORD



RESULTS AT A GLANCE

	1966	1965	Increase (Decrease)
Passengers	1,064,315	866,648	23 %
Passenger Miles (000)	203,342	163,484	24 %
Avg. Passenger Load	18.0	15.4	17 %
Passenger Load Factor	48.8%	43.6%	12 %
Commercial Revenues (000)	\$17,513	\$14,688	19 %
Cash Flow (000)	\$ 1,722	\$ 1,632	6 %
Net Income (000)	\$ 860	\$ 938	(8)%
Stockholders' Equity (000)	\$ 4,979	\$ 4,280	16 %
Common Shares Outstanding	1,005,000	1,005,000 ¹	—
Book Value Per Share	\$ 4.95	\$ 4.26 ¹	16 %
Net Income Per Share	\$.86	\$.93 ¹	(8)%

¹ Adjusted to reflect three-for-two stock split in May 1966



YOUR PRESIDENT'S REPORT

For the record, let me report another important year of growth and development at Southern. Aside from the fact that earnings were slightly lower than last year, new records were established in all areas. For the first time, we boarded a million passengers in a single year—to be exact, 1,064,315 passengers. Net income was \$859,743, contrasted with \$937,975 for 1965.

The company stock was split on a three for two basis. Cash dividends were increased by 20% to 16¢ per share on the new basis. Additional financing was arranged by the sale of debentures and through the use of credit, to provide \$25 million for the purchase of six Douglas DC-9 FanJETS, support equipment and spares.

June 1st will open a new era for Southern Airways when five of our cities will receive jet schedules. A few days later, jet service will be extended to seven additional cities. By September, three DC-9's will provide service to eighteen cities throughout our system.

The Civil Aeronautics Board, in recent policy statements, has indicated that Southern and the other local airlines will be granted entry into certain high density, long-haul markets. To be prepared, we have filed a number of applications to connect our system with several such markets in various parts of the country. Indicative of new thinking at the CAB, was the approval of non-stop authority between Huntsville, Alabama and New Orleans, Louisiana which became effective June 1st. This

was the most important change in our route structure for the year as it permitted the operation of 388 mile long non-stop flights.

For 42 days during July and August, we were called upon to provide a substantial amount of extra service when five of the major airlines were grounded by a strike. Throughout this emergency, our employees worked far beyond the call of duty to accommodate the public. During this period, we made many new friends and gained valuable experience in the operation of longer flights both within our system and beyond its present boundaries.

The Douglas DC-9 has been enthusiastically received throughout the world and I am confident the Southland which we serve will be no exception. With a combination of the finest equipment available and friendly, efficient Southern personnel, we have the greatest opportunity ever to provide expanded service for the public and in turn, to reward our stockholders and employees.

I extend my sincere thanks to our stockholders, customers, friends and employees for the support given management over our eighteen year history.

Frank W. Hulse
President

March 15, 1967

TREASURER — Earnings, Revenue, Financing



THOMAS F. GROJEAN

Your Company's 1966 net income totaled \$859,743 or 86¢ per share compared to \$937,975 or 93¢ per share in 1965. This slight reduction of 7¢ per share was accomplished in spite of a significant reduction in public service revenue (subsidy) and high first quarter costs resulting from unseasonal weather throughout much of the system. The 1966 rate of return before the investment tax credit is equal to the allowable maximum return of 11 per cent on recognized investment stipulated by the Civil Aeronautics Board. Any additional operating profit above that actually earned in 1966 would have been shared with the CAB under provisions of the subsidy formula.

Cash flow (net income plus amortization and depreciation) was at the highest level in the Company's history, reaching a record \$1,721,569, or \$1.71 per share compared to the 1965 level of \$1,631,661, or \$1.62 per share.

Commercial revenue (revenue excluding public service revenue) increased 19 per cent to \$17,513,123 up from the 1965 level of \$14,688,462. Total revenue,



affected by the reduction in public service revenue increased 11 per cent. The revenue yield per passenger mile was reduced 5 per cent as a result of Southern's increased use of promotional fares which offer significant savings to the traveling public. Also, during the strike against five trunk airlines the length of passengers' trips increased, resulting in lower revenue per mile.

Healthy Trend

Public service revenue (subsidy) is payment to the thirteen local service airlines for services they render to cities too small to support scheduled air service. Effective January 1, 1966, the Civil Aeronautics Board reduced the total amount of these funds to be paid in

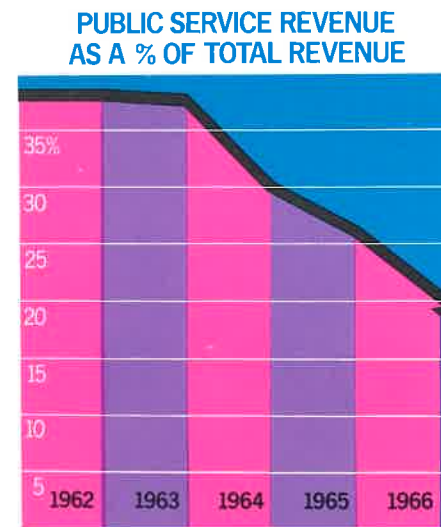
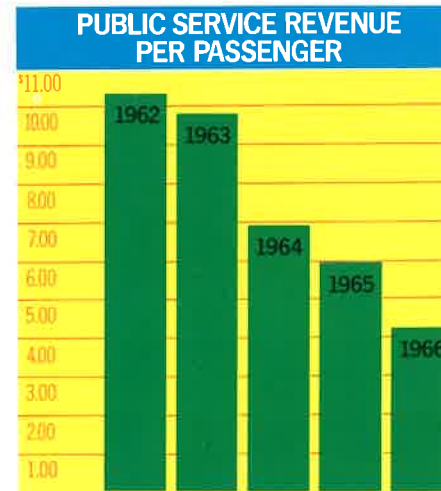
1966 and implemented a new formula placing more emphasis on the actual needs of the individual airlines affected. This resulted in a reduction over the previous year for Southern amounting to \$658,240 or 12.7 per cent.

Southern's dependency on public service revenue has progressively decreased during the last five years from \$10.32 per passenger to \$4.27 per passenger in 1966. The public service revenue received in 1966 was only 20.6 per cent of total revenue as contrasted to 38.1 per cent five years ago. You can see this in more detail in the chart to the right.

Service Increased

Total expenses in 1966, including interest, increased 14 per cent to \$20,635,385. The increase followed additional service; an 11.2 per cent increase in seat miles and a 12 per cent increase in passenger load factor. To improve service and increase revenues we continued upgrading service from DC-3 to Martin 404 aircraft which resulted in greater depreciation and interest expense.

Consistent with our previous reporting, the investment tax credit is deducted from tax expense in the year it is generated. In 1966 income taxes were reduced \$91,417 by investment tax credits compared to a \$27,495 reduction in 1965.



Financing Completed

In order to provide a stronger financial base to support future expansion, \$5,000,000 was raised by your Company through sale of convertible subordinated debentures. These debentures are convertible into common stock at a price of \$16 per share; 312,500 shares are reserved for such conversion. These were sold on December 15, 1966, to a group of underwriters headed by Alex. Brown & Sons. The interest rate until conversion is 5¾ per cent. These debentures are due December 1, 1981.

To protect your interests, the conversion price was approximately 15 per cent above the market price on the date the underwriting agreement was signed.

Proceeds from the sale were immediately invested in certificates of deposit and are shown in the 1966 balance sheet as investments. (On January 3, 1967 \$4,200,000 of these proceeds were applied to required DC-9 predelivery deposits.)

On March 31, 1966 financing was completed for the acquisition of the three DC-9's then on order. A credit agreement with six commercial banks allowed the Company to borrow \$12,155,000 until delivery of the third DC-9. As of December 31, 1966 \$6,055,000 has been borrowed. Quarterly payments on \$9,155,000 begin late in 1967 and extending through 1975. Prepayments beginning in 1968 are due on the remaining \$3,000,000 based upon earnings, with final maturity on December 31, 1975. Interest is payable at a rate ¼ per cent above the lead bank's prime rate.

With the exercise of an option to purchase three additional DC-9 FanJETS, the above credit agreement was supplemented on November 15, 1966, increasing the total number of banks to nine and providing for an additional \$7,000,000. This additional sum is to be available until the delivery of the last DC-9 which is expected in May, 1968. After final delivery, repayment of the additional borrowing is on a quarterly basis through 1974. Interest is payable at a rate ½ per cent above the lead bank's prime rate. In addition, the manufacturer is accepting \$1,500,000 of notes maturing December 31, 1975 with an interest rate ¾ per cent above the prime rate charged by the lead bank in the credit agreement. These notes call for certain prepayments based on earnings.

Stockholders Benefited

In May the stockholders approved a three-for-two stock split and increased the authorized number of shares to

2,000,000 from the previous 1,000,000, while reducing the par value from \$3 to \$2 per share. As a result of the reduction in par value the amount of outstanding shares was increased from 670,000 to 1,005,000.

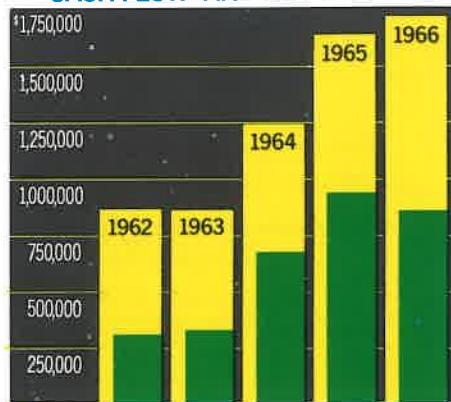
The semi-annual dividends paid in 1966 were 20 per cent higher than the 1965 level, reaching a total of 16¢ per share, up from the 13.4¢ paid in 1965 (adjusted for the three-for-two stock split). The dividends paid on June 15 and December 15 represented the fourth and fifth cash dividends paid by your Company since it began cash payments December 15, 1964.

The shares of common stock outstanding are held by more than 3900 stockholders in 44 states and many foreign countries. Stockholders' equity increased 16 per cent in 1966 to the record level of \$4,978,876, or \$4.95 per share, from the 1965 level of \$4,279,933, or \$4.26 per share. This is a 275% increase over the value five years ago.

DISTRIBUTION OF THE 1966 REVENUE DOLLAR

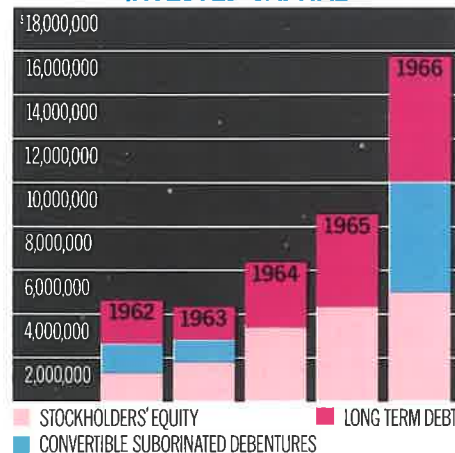


CASH FLOW* AND NET INCOME



*Net income plus amortization and depreciation

INVESTED CAPITAL



STOCKHOLDERS' EQUITY
CONVERTIBLE SUBORDINATED DEBENTURES
LONG TERM DEBT

SALES — Records, Expansion, Service



GRAYDON HALL

For the sales department, 1966 was a year of intensified effort and increased results.

Service between high density markets was expanded and longer flights scheduled, while continuing to maintain a good level of service in our intermediate cities.

Significant passenger growth in 1966, shown in the chart, resulted in new records — for a single day, 4,317 on July 1; a single month, 98,516 in July; and for a single year, 1,064,315.

And for the first time, your Company boarded a half-million passengers in less than six months, achieving this by June 28. Then on December 12, a serviceman on leave boarded Flight 175 in Columbia, S.C. to become our one millionth passenger of 1966 — the first time this milestone has been reached in a single year.

Not only were more passengers boarded in 1966 but also each passenger flew a greater distance. Our average length of haul rose to 187 miles and load factor reached 48.8 per cent, each a new record. Both passenger miles and available seat miles reached new highs. You can see the five-year comparison of these in the chart on your right.

Empty Seats Filled

Through expanded promotional fares, used by 229,475 passengers, your Company produced \$2,385,113 revenue, much of this from otherwise "empty" seats. Thousands of military standby passengers and countless college students with youth cards took advantage of the reduced fares offered them. The Discover America program was actively promoted throughout the year and we became a participant in numerous tours to key tourist areas throughout the United States.

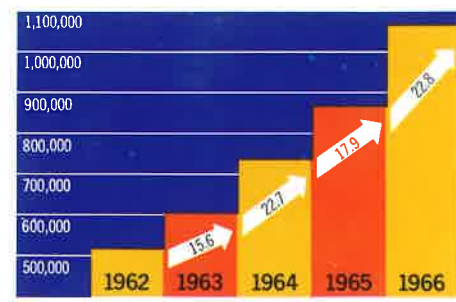
In 1966, Southern sold \$10,270,834 in tickets on other airlines, and other airlines in turn sold \$7,512,203 in tickets on Southern; an indication of the importance your Company plays in the plans of the nation's air travelers when they visit the South.

Air freight reached new highs during the year. Beginning in March, the Company boarded over a million pounds a month and continued at this rate for the remainder of the year. Some stations boarded more air freight during the year than in the eight-year period since your Company began this service. To speed ground handling, additional loading and unloading equipment was installed at many stations.

Credit Use Encouraged

As a convenience to our passengers, a "Ticket By Mail" program was instituted, enabling passengers to receive their tickets by mail, with payment to be sent after receipt. And during the year, agreement was reached for use of three additional credit card plans, Diner's Club, C & S National Bank and Carte Blanche. These are in addition to already accepted American Express, the Universal Air Travel Card and Southern's own air travel card.

Another promotion resulting in beneficial publicity and additional passengers was the selling of Atlanta Braves home



* PASSENGERS BOARDED*

⇨ % INCREASE OVER PRIOR YEAR

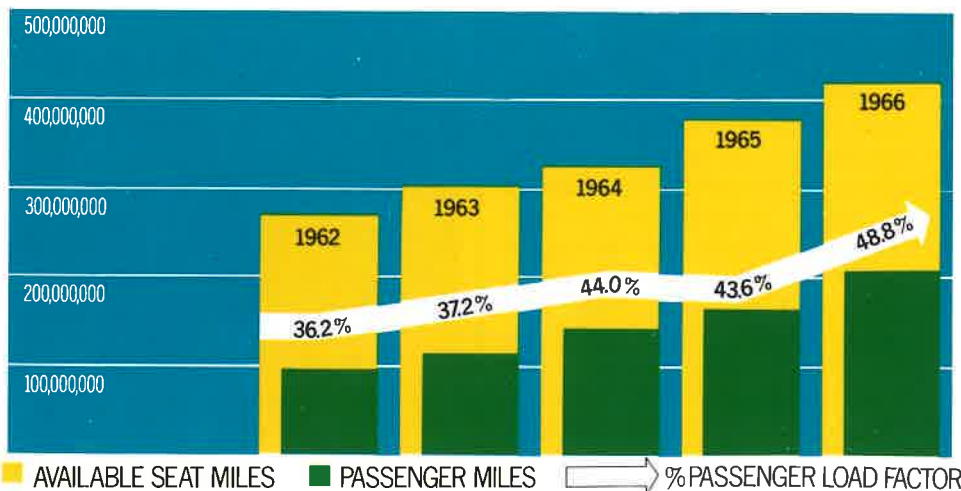
*THESE FIGURES INCLUDE CHARTER

game tickets. Southern's ticket counters offered this convenience in sixty cities to the many baseball fans who flew Southern to the games.

At the beginning of the year, a concentrated public relations program was commenced, taking the Southern story to national as well as regional news media.

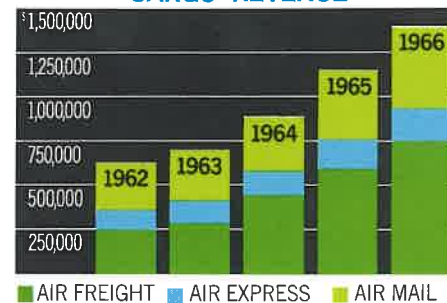
At our annual sales meeting in April, the "New Southern Accent On Service" was introduced as the advertising theme to precede the DC-9 arrival and accompany its first year of operation. By October, the new logotype, which you saw on the cover of this report, began appearing; the ACCENT "S", the sign of a new Southern.

The ACCENT "S" is becoming your Company's identity symbol. By the end of 1966 it began appearing in newspaper



■ AVAILABLE SEAT MILES ■ PASSENGER MILES ⇨ % PASSENGER LOAD FACTOR

CARGO REVENUE



and magazine advertising. All printed items used throughout the Company — literally millions of individual items — will bear the ACCENT "S". And, so will our aircraft.

Department Expanded

Plans were completed and implemented for reorganization of the sales department, including in many jobs and job titles a new word that will parallel Southern's entry into the jet age — SERVICE. New positions were created that will strengthen the department. More emphasis was given to long-range sales planning, sales promotion, field personnel training and community and civic affairs. Realignment of the field sales force was accomplished and city sales managers were established in eleven key market and geographic centers.

Modernization of our Central Reservations Office in Atlanta was commenced and by mid-year 1967 we will have direct computerized connections with all other airlines, established through hook-up with the sophisticated computer of a major trunk airline. Our Central Reservations Office, serving 16 high-density cities, in 1966 answered 1,008,548 telephone calls. This averaged 1.3 calls per passenger boarded in the cities served by this office. The advent of the new system will make this office even more functional.

Service Provided

Our most serious problem during the year resulted from the strike against five

trunk airlines. As a result of the strike our regular passengers traveling to and from the South had to curtail their travel and we were deprived overnight of a major source of business. Southern immediately augmented its existing schedule to provide as much service as possible to the cities on our system most seriously affected by the strike. Southern asked for and immediately received Civil Aeronautics Board emergency authority for non-stop service between major system cities, as well as for additional service from the nation's space center, Huntsville, Ala., to Washington, D. C., St. Louis, Mo., Tallahassee, Fla. and Orlando, Fla. This re-scheduling eliminated potentially staggering passenger losses and enabled us to meet previously projected traffic goals. During the 42-day strike your Company was able to provide a public service to many cities that would otherwise have been without any scheduled airline transportation or which would have had only token flights. At the same time, Southern proved its ability to serve the "long-haul market."

The immediate results achieved during the year interlaced with programs planned for the inauguration of jet-service. Much of the anticipated success of 1967 will emanate from these efforts. Your Company's sales department has become oriented to FanJET thinking!



ADMINISTRATIVE SERVICES— Applications, Information, Data



J. KENNETH COURTENAY

The administrative services department filed a number of route applications during 1966, requesting authority for Southern to provide service in new markets ideally suited for FanJET aircraft. Expansion was proposed to include New York, Washington, Dallas/Ft. Worth, Chicago, Detroit, St. Louis, Louisville, Cincinnati, Greensboro/High Point/Winston-Salem, and Raleigh/Durham.

In addition, a new route was asked for along the Gulf Coast linking our operations in Jacksonville with New Orleans and proposing to add Pensacola and Tallahassee to our system. Hearings were completed during the year on Southern's proposal to operate between Miami and Key West and a CAB decision is expected by mid-1967. The Company has on file other applications for a comprehensive pattern of local service for the State of Florida and these would provide a link between our current operations and the Miami-Key West market.

Capacity Doubled

During the year, the memory capacity of our computer was doubled, substantially improving information services provided to other Company departments. One advancement now available to maintenance and engineering is 13 weeks advance prediction of aircraft overhaul and parts requirements. This assures improved scheduling and utilization of skills, tooling and equipment.

Your Company became the first local service airline to provide its own operations research capabilities. With computer assistance, the operations research area constructs mathematical models of simulated operations in order to determine the optimum performance from parts and equipment investment.

OPERATIONS— Flying, Equipment



W. S. MAGILL, JR.

Recognizing the changes in Southern's fleet, in preparation for the FanJET transition and the phasing out of DC-3 aircraft, a program was completed up-

grading all Company pilots to Martin "Aristocrat" requirements. Preparations were made to advance senior flight personnel to DC-9 service.

The technical training department provided over 20,000 hours of instruction. Company captains and first officers underwent 10,270 hours of training, averaging 51.3 hours per man. Each stewardess received an average of 47.7 hours instruction, totaling 4,533 hours.

Southern's executive training program offered to private and corporate aircraft pilots was extended, and, for the fourth consecutive year the Company was selected to provide a training service for classroom and flight instruction for FAA inspectors.

Procurement plans were completed for a DC-9 procedures trainer, the actual size of the FanJET's cockpit. This sophisticated equipment will simulate normal, emergency, and radio navigation procedures for use in qualifying our flight crews to fly the new aircraft.

In addition to filling job vacancies resulting from normal industry turnover, your Company's personnel department selected 115 new employees for positions created by expansion and growth,



much of which is attributed directly to our forthcoming FanJET service.

Primary activity of the operations department during 1966 centered around early stage preparation for our DC-9's.

FanJET Pre-planning

While the Douglas DC-9 FanJET is a sophisticated aircraft, it possesses many design features that simplify the required maintenance techniques. It is ideally suited to our general operational and maintenance requirements, but your company found that its effectiveness on Southern's system would be optimized if certain modifications were made to the basic Douglas configuration. After thorough evaluation by our engineering department, these modifications were incorporated in the six aircraft being delivered to your Company. Without question, our aircraft are being provided with the latest, most reliable equipment available, representing the most advanced "state-of-the-art" in aircraft engine and equipment design. In addition to determination of the airplane's final configuration, selection was made for interior trim and decoration. Then began a very complex pre-delivery program.

On January 27, 1966, the maintenance and engineering department submitted to the President the "DC-9 Technical Project"—detailed plans for all of the activities that are preceding our FanJET service.

This synchronized schedule of activities established the pattern for the entire company's technical efforts during 1966, assuring smooth and programed transition to jet service.

MAINTENANCE ENGINEERING — Preparation and Training



GEORGE M. GROSS

A program for the planning, provisioning, and management of inventories was instituted. Detailed evaluations were made of needed parts, components, tooling, test equipment, and system-wide ground handling equipment. The provisioning cycle was implemented and orders placed immediately upon completion of each analysis; delivery times were often crucial. This action assured timely availability of critical items.

More refined manual systems were established for controlling FanJET parts and tooling. Care was exercised to insure that the manual systems were compatible with the computerized inventory management system concurrently under development. Arrangements for pooling of parts with other airlines was completed, and a DC-9 parts catalog and cross reference guide for Company use was published. As a result of this detailed approach, your Company effected a lower investment of approximately \$300,000, relative to the original estimates which were based on the experience of other airlines instituting similar aircraft service.

An airplane reliability program was established, using advanced statistical methods, which will provide continuous measurement of the functional performance of the DC-9 and its subsystems. Through this program we will be able to extend the life of costly components and refine our product improvement programs, thereby providing improved levels of service at lower cost.

Data Developed

The engineering department prepared data concerning DC-9 operations over our route system for flight, stations, and maintenance personnel. That your Com-

pany was able to develop this data and corresponding instructions "in house", rather than buying it from larger carriers as others have done, is the result of preparation and competent staff building programs in which we have been engaged over the past several years. In addition, engineering prepared the route application; a very comprehensive document required by the Federal Aviation Agency which specifies in detail exactly how we will operate and maintain the airplane. Based on this document, plus our demonstration of actual flights over the system, the FAA will issue approval for our operation of the DC-9.

Maintenance Preparation

Concurrently with the engineering work, the maintenance department began preparation of programs to provide detailed work specifications, defining each maintenance task to be performed on the airplane and its components. Many special tools and test equipment were manufactured within our shops. We began modification of existing maintenance facilities to accommodate the

DC-9. We began preparation for fueling the aircraft, provided for administration of the manufacturers' warranties, and established programs of quality assurance at Douglas' factory. Experienced Southern maintenance and inspection personnel have been on-site with each aircraft, from the beginning of the manufacturing process, to insure that our quality standards are met and that any deviations requiring our decision are handled promptly.

To augment its present work force, during 1966 the maintenance department added thirty new employees, enabling senior employees to be elevated to greater responsibilities.

Extensive Training

Early in the year, the maintenance department began training programs for the employees who would be directly involved with the day-to-day maintenance of the new aircraft. From our own instructors we selected the most experienced and knowledgeable, and these men were given special DC-9 training at Douglas Aircraft Company's plant in Long

Beach, California, and at plants of the manufacturers who are supplying the engines and major component parts for the aircraft. Under the direction of this group, training manuals were prepared for our maintenance and ground personnel—over a million sheets of printed materials went into the hundreds of copies of this manual, all printed in your Company's print shop. Our continuing detailed training is being conducted by this highly qualified group.

Additionally, over 40 selected supervisors and mechanics were given extensive training at Douglas', at the component system manufacturers' and at the engine manufacturer's plants. Many men received a month or more of such instruction, in addition to that afforded by our own extensive program.

Once the aircraft is in operation the real measure of success of these programs will be evident. It is believed that every contingency has been provided for. Commencement of FanJET service is being awaited with a great deal of satisfaction.



SOUTHERN AIRWAYS INC. BALANCE SHEET

ASSETS

	Dec. 31, 1966	Dec. 31, 1965
CURRENT ASSETS		
Cash	\$ 3,661,329	\$ 1,817,155
Certificates of deposit — at cost and accrued interest	212,447	1,900,994
Accounts receivable:		
U. S. Government — for transportation and public service — Note A	\$ 1,171,422	\$ 1,070,610
Airline traffic and other receivables	1,706,973	1,629,793
	\$ 2,878,395	\$ 2,700,403
Maintenance and other operating supplies — principally at average cost, less allowances of \$179,621 in 1966 and \$143,107 in 1965 for obsolescence	750,161	507,966
Prepaid expenses	74,852	162,767
Total Current Assets	\$ 7,577,184	\$ 7,089,285
INVESTMENTS AND OTHER ASSETS — Note F	4,814,555	29,339
PROPERTY AND EQUIPMENT — Note B		
Cost:		
1966	\$9,844,375	\$2,176,477
1965	8,077,526	1,729,783
	\$12,020,852	\$ 9,807,309
Less allowances for depreciation and maintenance:		
1966	3,442,955	1,144,926
1965	3,200,786	965,240
	4,587,881	4,166,026
Deposits on new equipment — Note F	524,573	150,000
	7,432,971	5,641,283
	\$ 7,957,544	\$ 5,791,283
DEFERRED CHARGES		
Unamortized preoperating, route extension, and development costs	\$ 272,297	\$ 40,700
Unamortized long-term debt expense	229,370	17,642
	\$ 501,667	\$ 58,342
	\$20,850,950	\$12,968,249

LIABILITIES

	Dec. 31, 1966	Dec. 31, 1965
CURRENT LIABILITIES		
Accounts payable and accrued expenses:		
Trade accounts	\$ 1,536,164	\$ 896,345
Collections and withholding as agents	1,805,156	1,310,987
Salaries, wages, and vacation pay	565,084	492,250
Accrued taxes, advertising, and other expenses	281,202	302,679
	\$ 4,187,606	\$ 3,002,261
Unearned transportation revenue	39,135	35,125
Air travel plan deposits	114,725	105,400
Estimated federal and state taxes on income — Note E	475,608	715,530
Current maturities of long-term debt — Note B	312,500	550,000
Total Current Liabilities	\$ 5,129,574	\$ 4,408,316
LONG-TERM DEBT (exclusive of current maturities) — Note B		
Notes payable to banks	\$ 5,742,500	\$ 4,280,000
5¾% Convertible Subordinated Debentures	5,000,000	—
	\$10,742,500	\$ 4,280,000
STOCKHOLDERS' EQUITY — Notes A, B, and C		
Common Stock, par value \$2 a share:		
Authorized — 2,000,000 shares		
Issued — 1,005,000 shares	\$ 2,010,000	\$ 2,010,000
Other paid-in capital	525,246	525,246
Retained earnings	2,443,630	1,744,687
	\$ 4,978,876	\$ 4,279,933
COMMITMENTS — Note F		
	\$20,850,950	\$12,968,249

See Notes to Financial Statements.

SOUTHERN AIRWAYS, INC.
STATEMENT OF INCOME AND RETAINED EARNINGS

Years ended December 31, 1966 and December 31, 1965

	1966	1965
OPERATING REVENUES		
Passenger and excess baggage	\$15,183,956	\$12,723,017
Mail, express, and freight	1,397,345	1,160,467
Public service revenue — Note A	4,540,945	5,199,185
Charter	518,951	507,663
Other operating revenues — net	412,871	297,315
	\$22,054,068	\$19,887,647
OPERATING EXPENSES		
Flying operations	\$ 6,116,730	\$ 5,385,499
Maintenance	4,492,599	4,037,161
Aircraft and traffic servicing	5,506,885	4,798,675
Passenger service	926,301	822,371
Promotion and sales	1,518,177	1,395,025
General and administrative	1,005,671	879,776
Amortization and provision for depreciation	861,826	693,686
	\$20,428,189	\$18,012,193
	\$ 1,625,879	\$ 1,875,454
OTHER DEDUCTIONS AND INCOME		
Interest on long-term debt—net of interest capitalized	\$ 250,038	\$ 213,779
Other income, less miscellaneous deductions	42,842	52,660
	\$ 207,196	\$ 161,119
	\$ 1,418,683	\$ 1,714,335
TAXES ON INCOME — Note E		
	595,485	803,300
	\$ 823,198	\$ 911,035
PROFIT FROM DISPOSAL OF PROPERTY		
Less applicable income taxes	36,545	26,940
NET INCOME	\$ 859,743	\$ 937,975
RETAINED EARNINGS		
Retained earnings at beginning of year	1,744,687	940,712
	\$ 2,604,430	\$ 1,878,687
Cash dividends paid (1966 — \$.16 per share; 1965 — \$.134 per share)	160,800	134,000
Retained earnings at end of year	\$ 2,443,630	\$ 1,744,687

See Notes to Financial Statements.

SOUTHERN AIRWAYS, INC.
STATEMENT OF SOURCE AND APPLICATION OF FUNDS
YEAR ENDED DECEMBER 31, 1966

FUNDS PROVIDED BY		
Net income	\$ 859,743	
Add items not requiring the outlay of funds:		
Provision for depreciation	803,765	
Amortization of deferred charges	53,659	\$ 1,717,167
Increase in long-term debt		6,462,500
Decrease in miscellaneous investments and other assets		14,784
Total Funds Provided		\$ 8,194,451
FUNDS APPLIED TO		
DC-9 jet aircraft program — Note F:		
Equipment and spares	\$1,599,210	
Equipment purchase deposits	374,573	
Certificates of deposit held for equipment purchases	4,800,000	
Preoperating expenses	251,392	\$ 7,025,175
Net increase in other property and equipment		996,243
Payment of cash dividends (\$.16 per share)		160,800
Increase in deferred finance and other costs		245,592
Total Funds Applied		\$ 8,427,810
DECREASE IN WORKING CAPITAL		\$(233,359)
WORKING CAPITAL, DECEMBER 31, 1965		2,680,969
WORKING CAPITAL, DECEMBER 31, 1966		\$ 2,447,610

SOUTHERN AIRWAYS, INC.
NOTES TO FINANCIAL STATEMENTS

Note A — During the eighteen-month period ended December 31, 1960, the Company received public service revenue under a temporary rate which is subject to adjustment upon determination by the Civil Aeronautics Board of a final rate for that period. In the opinion of management, such final determination by the Board will not result in a reduction in public service revenue for that period, and may result in additional public service revenue for that period and for subsequent years in amounts which are not presently determinable.

Since January 1, 1961, the Company has received public service revenue under a Class Rate which provides for profit-sharing refunds when stipulated returns on investment are exceeded. The Civil Aeronautics Board has completed audits for the years 1961 through 1964, and adequate provision has previously been made for the required refunds for those years. In the opinion of management, the amounts stated for public service revenue for the years 1965 and 1966 will not be significantly affected upon final determination by the Civil Aeronautics Board.

Note B — The notes payable to banks (for which all aircraft, engines, and related equipment are pledged as collateral), together with additional borrowings of \$14,600,000 for which the Company has commitments, will be payable generally in installments extending through 1975. The interest rate (6 1/4% at December 31, 1966) is 1/4 of 1% above the lead bank's prime rate.

The 5 3/4% Convertible Subordinated Debentures due December 1, 1981, are convertible (until maturity or prior redemption) into Common Stock at \$16.00 per share; are subordinated, generally, to all existing and future indebtedness for borrowed money; are callable on or after June 1, 1968, at premiums ranging from 5.75% downward; require annual sinking fund payments beginning December 1, 1976, in an amount equal to 10% of the principal amount outstanding at December 1, 1975, with additional voluntary sinking fund payments equal to the mandatory amount.

The agreements relating to the notes payable and to the 5 3/4% Convertible Subordinated Debentures place certain re-

quirements and restrictions upon, among other things, (1) net current assets, (2) net worth, (3) capital expenditures, and (4) payments relating to capital stock, including dividends. The Company has met all of these requirements, and approximately \$304,000 of retained earnings were free of such restrictions at December 31, 1966.

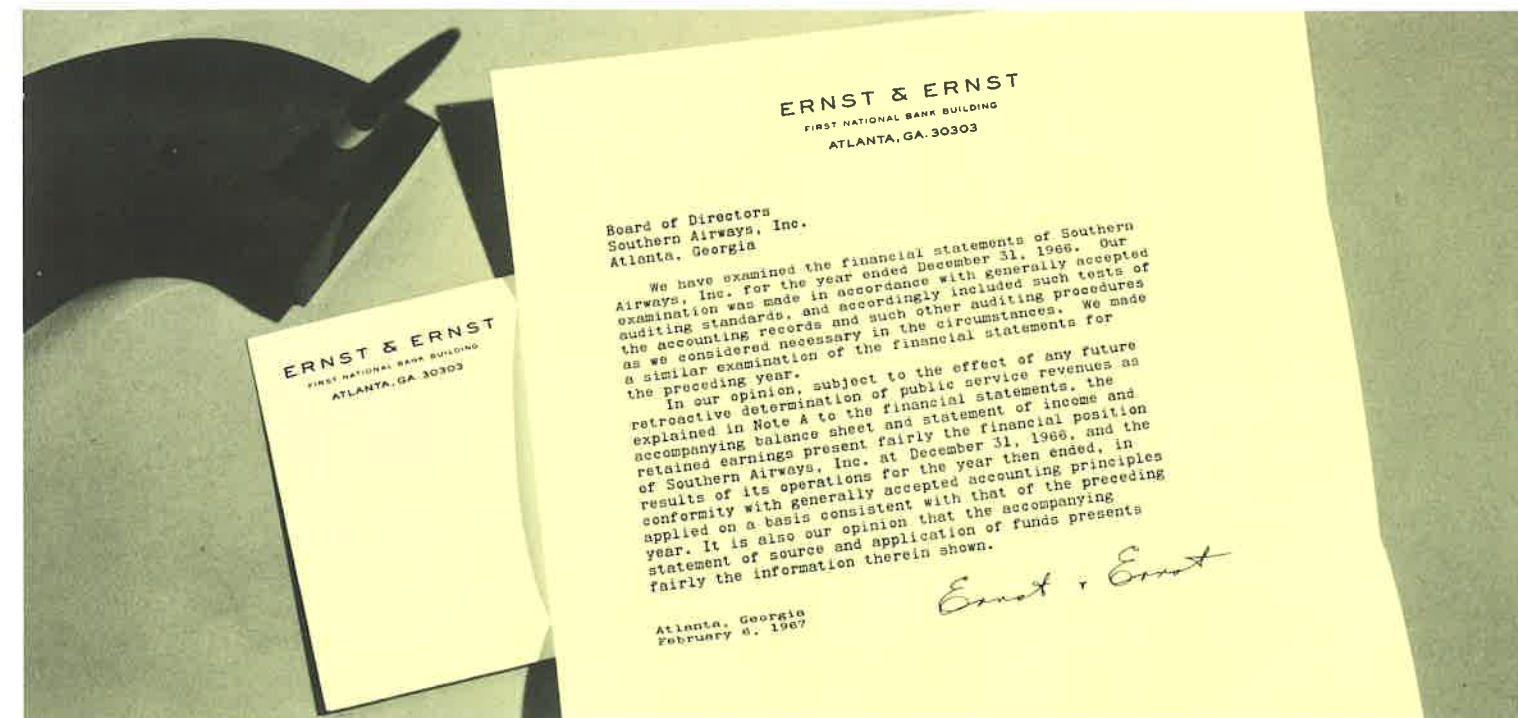
Note C — In 1966, the authorized Common Stock of the Company was increased to 2,000,000 shares; the par value per share was reduced from \$3 to \$2; and a three-for-two stock split was effected. For comparative purposes, 1965 figures have been revised to give effect to the split.

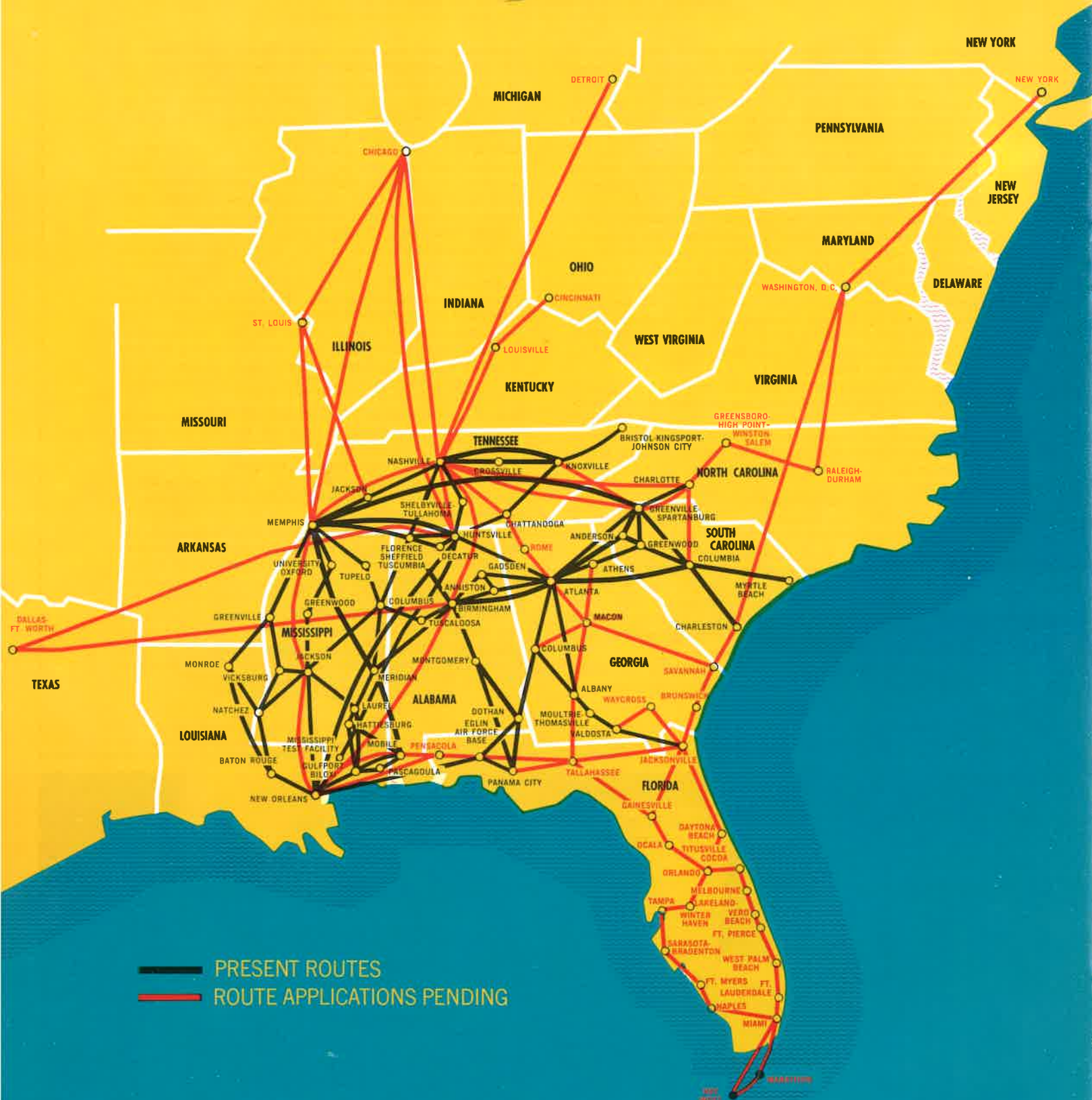
Under terms of a Qualified Stock Option Plan approved by the Board of Directors in 1965, options (exercisable one-third each year beginning in October, 1967) were outstanding at December 31, 1966 for the purchase of 37,500 shares of Common Stock of the Company at a price of \$10.16 2/3 per share, and an additional 7,500 shares were reserved for options which may be granted under the Plan. An option for the purchase of 3,000 shares was cancelled during the year. In addition, 312,500 shares of Common Stock are reserved for issuance upon conversion of the 5 3/4% Convertible Subordinated Debentures.

Note D — The cost to the Company of its employees retirement plans amounted to \$636,635 for the year ended December 31, 1966 and the unfunded past service liability at that date totaled approximately \$670,000.

Note E — In accordance with the policy of reflecting the investment tax credit in income in the year in which it arises, the provision for income taxes for the years 1966 and 1965 includes investment tax credit of \$91,417 and \$27,495, respectively.

Note F — At December 31, 1966, the Company had on order six DC-9 jet aircraft and related spares scheduled for delivery in 1967 and 1968, which represents a commitment of approximately \$21,520,000 in excess of the related deposits (See Note B). Certificates of deposit in the amount of \$4,800,000 (the net proceeds from the sale of the 5 3/4% Convertible Subordinated Debentures) are held for payments required during the first half of 1967 under the DC-9 purchase contract and are classified as non-current investments.





— PRESENT ROUTES
 — ROUTE APPLICATIONS PENDING

DIRECTORS

- Cecil A. Beasley, Jr.
Ballard & Beasley,
Washington, D.C.
- Edward U. Beneke
The Beneke Corporation,
Columbus, Mississippi
- Alexander J. Brunini
Brunini, Everett, Grantham & Quin
Vicksburg, Mississippi

EXECUTIVE COMMITTEE

- Frank W. Hulse
- G. Gunby Jordan
- W. B. White, Jr.
- Graydon Hall
- Elton B. Stephens

OFFICERS

- Frank W. Hulse
President
- Graydon Hall
Vice President—Sales
- W. S. Magill, Jr.
Vice President—Operations
- J. Kenneth Courtenay
Vice President—Administrative
Services and Secretary
- George M. Gross
Vice President—
Maintenance and
Engineering
- Ike F. Jones
Vice President
- Thomas F. Grojean
Treasurer
- W. Bayne Grubb
Assistant Vice President—Flight
Operations
- Thomas A. Wiley, Jr.
Assistant Vice President—
Sales
- Everett L. Martin
Assistant Vice President—
Personnel
- Ray W. Burden
Assistant Treasurer
- A. L. Maxson
Controller
- Mrs. Mary C. Hayes
Assistant Secretary
- Cecil A. Beasley, Jr.
Assistant Secretary
- W. B. White, Jr.
Assistant Secretary

Graydon Hall
Southern Airways, Inc.,
Atlanta, Georgia

F. Barton Harvey, Jr.
Alex. Brown & Sons,
Baltimore, Maryland

Frank W. Hulse
Southern Airways, Inc.,
Birmingham, Alabama

Alton F. Irby, Jr.
Irby-Adams-Cates Co.,
Atlanta, Georgia

Henry P. Johnston
Radio and Television Consultant
Birmingham, Alabama

G. Gunby Jordan
The Jordan Company,
Columbus, Georgia

Sartain Lanier
Oxford Manufacturing Co., Inc.,
Atlanta, Georgia

R. Eugene Orr
Knight, Orr & Company, Inc.,
Jacksonville, Florida

G. Frank Purvis
Pan American Life Insurance Co.,
New Orleans, Louisiana

Francis D. Schas
Bullington-Schas & Co.,
Memphis, Tennessee

Elton B. Stephens
EBSCO Industries, Inc.,
Birmingham, Alabama

Richard A. Trippeer
Trippeer Organizations, Inc.,
Memphis, Tennessee

W. B. White, Jr.
Bradley, Arant, Rose & White,
Birmingham, Alabama

Gen. Ralph H. Wooten
(Honorary Director)
United States Air Force, Retired,
Memphis, Tennessee

GENERAL OFFICES

- Atlanta Airport, Atlanta, Georgia
- COUNSEL: Bradley, Arant, Rose &
White, Birmingham, Alabama
- Ballard & Beasley, Washington, D. C.
- AUDITOR: Ernst & Ernst,
Atlanta, Georgia
- STOCK TRANSFER AGENT:
Trust Company of Georgia,
Atlanta, Georgia
- ADVERTISING COUNSEL: Harris &
Weinstein Associates, Inc.,
Atlanta, Georgia



General Offices: Atlanta Airport
Atlanta, Georgia 30320