ANNUAL REPORT 1974

NORTH CENTRAL AIRLINES

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7500 northliner drive, minneapolis, minnesota

board of directors

Hal N. Carr*
Chairman of the Board and Chief Executive Officer
North Central Airlines

G. F. DeCoursin*
President
April Company
(manufacturer and distributor of seasoned food products)

Chan Gurney
Retired Member
Civil Aeronautics Board

Samuel H. Maslon*
Partner in law firm of
Maslon, Kaplan, Edelman, Borman, Brand & McNulty

Jay Phillips
Chairman of the Board
Ed. Phillips & Sons Co.
(wholesale beverage distributor)

Morton B. Phillips
President
Ed. Phillips & Sons Co.

Joseph E. Rapkin
Partner in law firm of
Foley & Lardner

H. P. Skoglund
Chairman, Executive Committee
North American Life & Casualty Company

Bernard Sweet
President
North Central Airlines

Kenneth B. Willett
Chairman of the Board
First Financial Savings and Loan Assn. of Stevens Point

**Executive Committee*

management

Hal N. Carr.................... *Chairman of the Board and Chief Executive Officer*

Bernard Sweet................................ *President*

John P. Dow................. *Vice President and Secretary*

Robert L. Gren................ *Vice President-Maintenance and Engineering*

George J. Karnas............ *Vice President-Inflight Service*

Daniel F. May...................... *Vice President-Finance*

Gowan J. Miller.......... *Vice President-Industrial Relations*

David E. Moran............ *Vice President-Traffic and Sales*

T. M. Needham........... *Vice President-Ground Operations*

J. F. Nixon................... *Vice President and Treasurer*

G. F. Wallis............... *Vice President-Flight Operations*

Charlotte G. Westberg.... *Vice President-Staff Administration*

Joseph W. Ettel....................... *Assistant Secretary*

Raymond J. Rasenberger............... *Assistant Secretary*

Walter E. Nielsen..................... *Assistant Treasurer*

Michael D. Meyer............................ *Controller*

John W. Dregge.................. *Assistant to the Chairman*

REGISTRARS AND STOCK TRANSFER AGENTS:
First National City Bank,
New York, New York
Northwestern National Bank of Minneapolis
Minneapolis, Minnesota

STOCK TRADING:
Common stock and warrants
Traded under symbol NCA

New York Stock Exchange

Midwest Stock Exchange

ANNUAL MEETING:
First Wednesday in April
(April 2, 1975)
Wausau, Wisconsin

AUDITORS:
Alexander Grant & Company

highlights

	1974	1973	Change
OPERATING REVENUES	$151,490,000	$127,983,000	18.4%
OPERATING PROFIT	$ 17,994,000	$ 12,001,000	49.9
EARNINGS BEFORE TAXES	$ 15,696,000	$ 9,210,000	70.4
NET EARNINGS	$ 8,204,000	$ 6,447,000	27.3
NET EARNINGS PER SHARE	66¢	52¢	26.9
DIVIDENDS PER SHARE	10¢	5¢	100.0
WORKING CAPITAL FROM OPERATIONS	$ 18,784,000	$ 14,176,000	32.5
WORKING CAPITAL AT YEAR-END	$ 4,834,000	$ 4,654,000	3.9
RETAINED EARNINGS	$ 27,044,000	$ 20,086,000	34.6
STOCKHOLDERS' EQUITY	$ 47,152,000	$ 40,611,000	16.1
PASSENGERS	4,546,000	4,263,000	6.6
PASSENGER MILES	1,060,865,000	1,011,525,000	4.9
CARGO TON MILES	12,585,000	13,394,000	−6.0

(North Central Airlines' 10K report to the Securities and Exchange Commission may be obtained without charge by writing to the Secretary of the Company.)

about north central

North Central Airlines is a regional scheduled carrier linking intermediate-sized cities with major metropolitan areas. Its principal function is to provide safe, dependable air transportation.

Incorporated as Wisconsin Central Airlines in 1944, the company received its Federal operating certificate three years later. Scheduled service was inaugurated on February 24, 1948. When headquarters were moved to Minneapolis/St. Paul in 1952, the name was changed to North Central Airlines. Traffic grew steadily, setting a regional industry record by 1960 with one million passengers, and then doubling every six years to reach four million in 1972.

The company has operated profitably for 20 of the 21 years under present management. Its fleet of 50 jet-powered aircraft makes 600 departures a day over the 10,200-mile route system. Efficient passenger handling includes computerized reservations and automated ticketing.

Now in its twenty-eighth year, the airline serves 90 cities—in 13 states and two Canadian provinces—including Chicago, Detroit, Cleveland, New York, Toronto, Milwaukee, Winnipeg, Minneapolis/St. Paul, Omaha, Kansas City, and Denver.

North Central's 3,360 dedicated employees offer the traveling public the highest type of regional airline service.

to our stockholders, employees and friends:

We are pleased to report that 1974 was the most profitable year in North Central's history. Net earnings reached $8,204,000, and record revenues exceeded $151,000,000. Over 4.5 million passengers were carried more than a billion passenger miles.

With these achievements, the company maintained its position as the leader in financial performance among the regional airlines. North Central has the highest earnings before taxes, the largest retained earnings, and the best profit consistency—having operated profitably for 20 of the 21 years under present management.

Considering the airline's solid overall financial condition and 1974 earnings, the Board of Directors continued its policy of paying an annual cash dividend. Stockholders of record February 17, 1975 received 10 cents per share of common stock.

The $151,490,000 in revenues were 18 percent ahead of the $127,983,000 in 1973. With operating expenses rising 15 percent and other expenses (primarily interest offset by interest income) decreasing, the 1974 earnings before taxes were $15,696,000. This is a 70 percent improvement over the $9,210,000 in the previous year.

Although taxes nearly tripled—from $2,763,000 to $7,492,000—the company still earned $8,204,000, or 66 cents a share, compared with $6,447,000 and 52 cents a share in 1973.

The record profit boosted North Central's retained earnings to $27,044,000 in 1974 and stockholders' equity to $47,152,000. The company's .69 to 1 debt/equity ratio is one of the best among the nation's 19 scheduled airlines.

Passenger boardings for 1974 were a record 4,546,000, seven percent over the 4,263,000 the year before. Passenger miles reached 1,060,865,000 for a five percent increase. The 12,585,000 cargo ton miles reflect a six percent drop, partially due to a two-month suspension of air express.

In operating performance, North Central again ranked with the top carriers in the industry. The airline completed 99.2 percent of the 28 million scheduled miles, and 83 percent of its flight arrivals were on time.

Three of these DC-9 Series 50 fan jets are on order for Spring 1976 delivery. North Central's aircraft will carry 125 passengers and feature the wide-body look with completely new decor.

The Civil Aeronautics Board awarded the company a new nonstop route between Winnipeg and Duluth/Superior, and service was inaugurated on October 27. With this 314-mile segment, North Central now has a 10,200-mile system serving 90 cities in 13 states and two Canadian provinces.

Late in 1974, the company filed an application for a Chicago-New Orleans nonstop route. Only one of the two authorized carriers is operating nonstop service. The company estimates that 40 percent of its projected passenger traffic on this route would originate or terminate on North Central flights serving cities beyond Chicago.

A CAB decision in the North Central Route Realignment case was released February 5, 1975. It gives the airline better scheduling flexibility between city pairs on its system.

Three DC-9 Series 50 fan jets were ordered in 1974 for delivery in the Spring of 1976, and the company has an option to purchase three more later in that year. This "stretched" aircraft will carry 25 more people than the 100-passenger Series 30 jet. North Central now has 19 DC-9-30s and 31 Convair 580 prop-jets in its 50-aircraft fleet. Two more DC-9-30s will be received this April and May.

A variety of improvements were made in services and accommodations for passengers and shippers. Among these is the company's new $1-million air freight facility, added to the headquarters complex at the Minneapolis-St. Paul International Airport.

Responsible corporate citizenship is demonstrated by North Central's social action programs. These promote human development, conserve natural resources, and help the company operate as a compatible neighbor.

The financial and traffic records for 1974 are attributable to the dedication and efficiency of the airline's employees, the assistance of its stockholders and friends, and the loyalty of passengers who choose North Central. With this strong support, the company can meet the challenges of 1975 and achieve another profitable year.

Sincerely,

HAL N. CARR
Chairman of the Board and Chief Executive Officer

BERNARD SWEET
President

March 4, 1975

HAL N. CARR

BERNARD SWEET

financial review

Record net earnings of $8,204,000 were achieved by North Central in 1974, and revenues climbed 18 percent to reach $151,490,000. The airline retained its position as the leader among regional carriers in financial performance.

Revenues increased for the twenty-seventh consecutive year. The $151,490,000 revenues for 1974 are $23,507,000 greater than the $127,983,000 in 1973. Operating expenses, including depreciation and amortization of $8,017,000, rose 15 percent to $133,496,000 from $115,982,000. The operating profit of $17,994,000 jumped 50 percent compared with the $12,001,000 the year before. Other expenses, primarily interest offset by interest income, decreased by 18 percent to $2,298,000 from $2,791,000.

The $15,696,000 earnings before taxes were the highest in the regional industry and a 70 percent gain over the $9,210,000 in 1973. Even with income taxes of $7,492,000—nearly triple the $2,763,000 for the previous year—the resulting net earnings of $8,204,000 (66 cents per share) set a record high and were 27 percent ahead of the $6,447,000 (52 cents per share) in 1973.

The Variance Analysis table at the right summarizes factors relating to the net changes in revenues and expenses from 1972 through 1974. Further data on the company's operations for the last five years is provided on Page 19.

Total operating revenues climbed in 1974 and 1973. Scheduled passenger miles flown, up 60.3 million for 1974, added $7.4 million to passenger revenues. In 1973, scheduled passenger miles were 20.7 million under the previous year when extra traffic was generated by a strike against another airline serving some North Central cities. This reduction in passenger miles accounts for the $2.3-million drop in 1973 revenues.

Fare increases were granted during the last two years to help offset the effects of increased fuel costs, overall inflation, and the passenger security program. As a result, revenue per scheduled passenger mile rose in 1974 and in 1973. These higher yields improved 1974 revenues by $12.3 million and 1973 revenues by $7.3 million.

Public service revenues vary according to the Federal government formula for paying airlines to provide air transportation to small cities which cannot fully support such service. Cargo and other revenue gains show normal growth.

Under operating expenses, new labor agreements reflect the rising cost of living. The increased wages and fringe benefits, together with higher payroll taxes, amounted to $7.1 million in 1974 and $4.8 million in 1973. A substantial jump of 64 percent in the cost per gallon of aircraft fuel added $5.2 million to 1974 expenses. Inflation boosted the cost of parts, supplies, services, landing fees and rent in 1974.

In early 1973, the Federal government required airlines to screen all passengers boarding flights. For North Central, the cost of providing this security amounts to $2 million a year. Normal cost increases prevailed for passenger service and promotion.

Payments to members of the airlines' Mutual Aid Pact dropped by $1.3 million in 1973, compared with 1972, a year of prolonged strikes in the industry. These outlays were reduced by an additional $200,000 in 1974.

The climb in interest income is the result of investing the company's surplus funds generated from operations. Interest expense increased $300,000 in 1973 due to higher interest rates and more outstanding debt. In 1974, outstanding debt declined, but because of continuing high rates, interest expense remained constant.

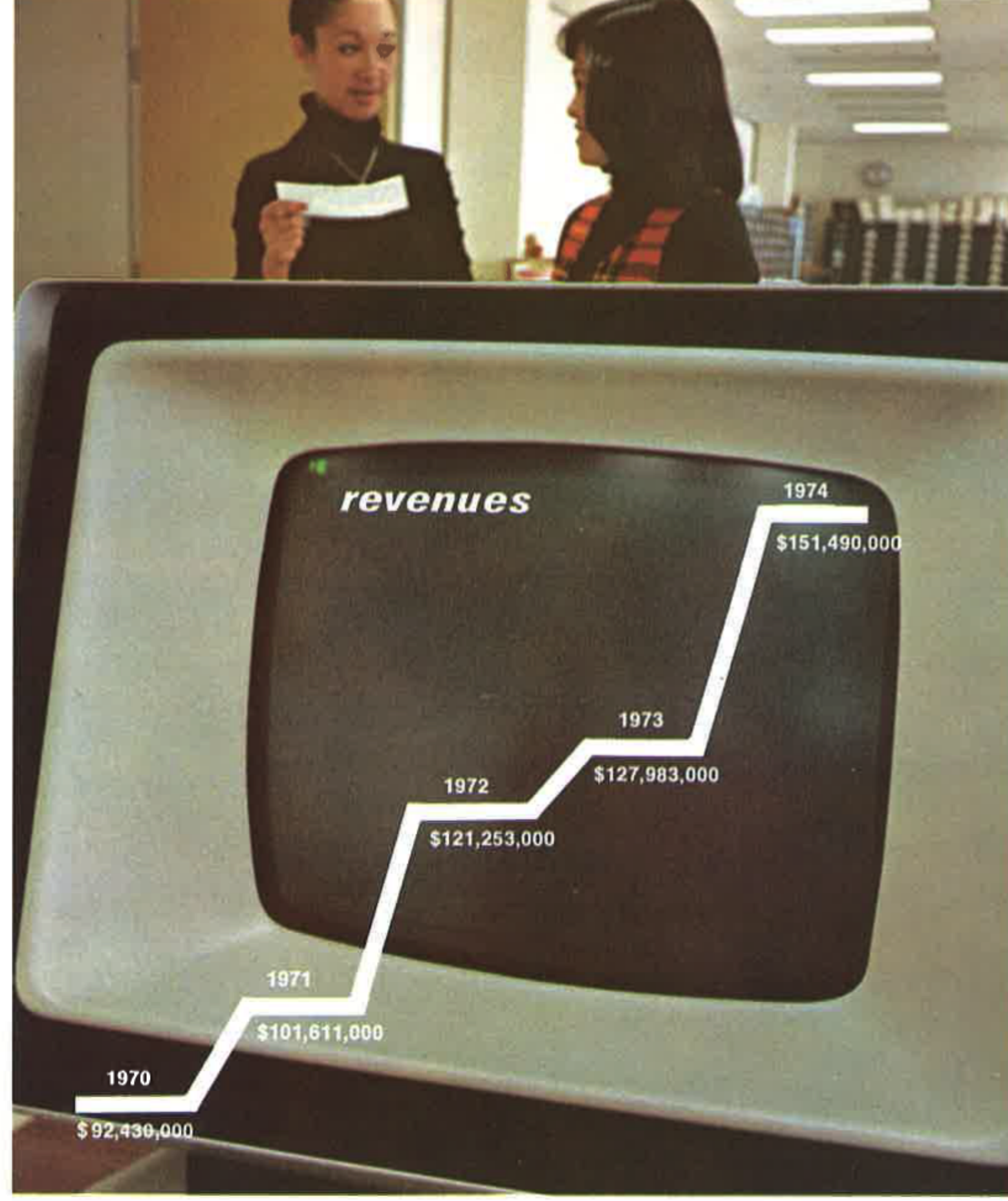
The income tax jump of $4.7 million in 1974 reflects the company's record earnings and the higher tax rate applicable because little investment tax credit was available, compared with 1973. The extraordinary gain on disposition of flight equipment added $1 million of nonoperating income to 1972 earnings. The final item in the Variance Analysis shows the gain in net earnings of $1.8 million for 1974.

The company's long-term debt to equity ratio is .69 to 1 and continues to be one of the best among the nation's 19 scheduled carriers. The substantial increase in working capital from operations provided cash for short-term investments, averaging $9.7 million, which yielded $1,128,000 in interest income. In addition, the company implemented a program to repurchase up to 500,000 shares of the airline's own stock on the open market. This decision was made because the stock was selling at four times earnings and below book value. Some 150,900 shares had been acquired as of December 31, 1974.

North Central's $27,044,000 in retained earnings, highest in the regional airline industry, is the result of profitable operations for 20 of the 21 years under present management. Stockholders' equity reached a record $47,152,000, the equivalent of $3.83 per share.

VARIANCE ANALYSIS

	Net Changes	
NET EARNINGS	**1974-1973**	**1973-1972**
1974	$ 8,200,000	
1973	6,400,000	$ 6,400,000
1972		7,500,000
Change in net earnings	$ 1,800,000	$(1,100,000)
MAJOR FACTORS OF CHANGE:		
Operating revenues		
Passenger miles	$ 7,400,000	$(2,300,000)
Passenger fares	12,300,000	7,300,000
Public service revenues	2,500,000	500,000
Cargo and other revenues	1,300,000	1,200,000
Net revenue changes	23,500,000	6,700,000
Operating expenses		
Labor and other payroll items	7,100,000	4,800,000
Cost of aircraft fuel	5,200,000	900,000
Parts, supplies and services	3,500,000	(1,000,000)
Landing fees and rent	700,000	800,000
Security costs (passengers)	—	2,000,000
Passenger service and promotion	900,000	500,000
Mutual Aid payments	(200,000)	(1,300,000)
Other expenses	(400,000)	—
Depreciation	700,000	400,000
Net expense changes	17,500,000	7,100,000
Change in operating profit	6,000,000	(400,000)
Nonoperating items		
Interest income and other	500,000	400,000
Interest expense	—	300,000
Income taxes	4,700,000	(200,000)
Extraordinary gain—equipment	—	(1,000,000)
Net nonoperating changes	4,200,000	(700,000)
Change in net earnings	$ 1,800,000	$(1,100,000)



The price range of North Central common stock (from first to fourth quarter) was 4-2⅝, 3⅞-3⅛, 3⅝-2¾, 3-2⅛ in 1974 and 5-4¼, 5¼-3⅝, 4⅜-3⅜, 4⅛-2½ in 1973.

During this two-year period, the composite Airline Industry Stock Index declined from an average of 76.7 for the first quarter of 1973 to an average of 34.6 in the fourth quarter of 1974—a drop of 55 percent. North Central common stock was off 41 percent.

Tentative arrangements have been made with major banks to finance the acquisition of the two DC-9-30 and three DC-9-50 fan jets on order. These jets are replacing Convair 580s, two of which were sold in 1974. More Convairs will be disposed of as the new jets are delivered.

Based on the airline's strong financial position and 1974 earnings, the Board of Directors again declared an annual cash dividend. Ten cents per share of common stock was paid March 3, 1975, to stockholders of record February 17.

Continuing its policies of sound money management and strict cost control, North Central expects to meet the challenges ahead and make 1975 another profitable year.

traffic growth and performance

North Central set new passenger traffic records in 1974 while continuing to rank among industry leaders in operating performance.

By carrying 4,546,209 passengers, the company achieved a seven percent increase over the 4,263,231 passengers in 1973. Revenue passenger miles topped one billion for the third consecutive year, reaching 1,060,865,304—a five percent gain compared with the previous year.

Complementing scheduled service, the airline operated 622 extra sections to carry an additional 20,084 passengers. The 447 charter flights accommodated 54,659 passengers. Destinations included popular vacation ports in the Caribbean, several major Canadian cities, and numerous points in 35 states across the country.

With passenger traffic at record levels and available seat miles up just six-tenths of one percent, the passenger load factor rose 4.3 percent to 49.3 percent.

North Central completed 99.2 percent of its 28,212,672 scheduled miles for 1974. Of the 218,830 scheduled arrivals, some 82.8 percent were on time.

The airline's performance has averaged 99 percent over the last 17 years. This achievement is particularly significant because of the severe, adverse weather conditions which prevail for many months over most of the 10,200-mile system.

Outstanding operating performance contributed to the high level of passenger traffic. Another factor was the shortage of automobile fuel in the early part of 1974 and low highway speed limit which prompted many people to fly rather than drive. Softening of the general economy, however, led to reduced business travel by some depressed industries.

Cargo was affected by the national economic decline. Cargo ton miles for 1974 totaled 12,584,535, down six percent from the 13,393,664 the year before. Freight ton miles were off less than one percent, express dropped 42 percent because of its temporary suspension in July and August, and mail declined nine percent.

The airline's progressive and exacting maintenance program, implemented by skilled mechanics, has proved its value. Again in 1974, less than one-tenth of one percent of the scheduled departures were cancelled for maintenance reasons and only 1.3 percent were delayed by mechanicals.

North Central has grown dramatically over the years, and the company's 3,360 employees consistently prove themselves equal to the challenging demands of providing safe, dependable scheduled air transportation.

new facilities and services

Facilities for passengers and shippers were significantly improved through the combined efforts of North Central and the communities it serves. Foremost are the impressive new terminals in Duluth/Superior and Thief River Falls and the company's new air freight facility, added to the headquarters complex at the Minneapolis-St. Paul International Airport.

North Central's $1-million air freight facility features an expanded storage area for in-transit freight. The large walk-in cooler improves handling of perishable items, and a new security area is now provided for international shipments. Half of the 30,000 square feet available will be used by North Central for air freight operations and specialized pilot training. The other half is being leased to another carrier.

Second-level jet bridges highlight the futuristic Duluth/Superior terminal. The four-level structure offers a variety of passenger conveniences, from indoor parking to elegant dining. The $6.2-million building was dedicated in October.

The new Thief River Falls terminal, part of a $5.1-million airport program, opened in August. It is 16 times larger than the 21-year-old wooden structure it replaces. A baggage claim section, spacious lounge, and concessions area are among the major attractions.

Larger baggage claim facilities were completed at Grand Forks, Rapid City, Rochester, Madison and Lansing in 1974. Passenger service counters were renovated at Pierre, Rochester, International Falls, Alpena, Kalamazoo and Muskegon.

Terminals are under construction in Marquette and Sault Ste. Marie, with completion scheduled for 1975, and renovations at Cincinnati are nearly finished.

To further accommodate air freight shippers, North Central is operating out of new facilities at Madison, Lansing and Omaha. Also, an air freight customer service area has been added at Chicago O'Hare.

Continuing its flight equipment modernization program, North Central has ordered three DC-9 Series 50 fan jets for delivery in the Spring of 1976 and has an option to purchase three more later that year. These "stretched" versions of the DC-9 will carry 25 more passengers than the 100-passenger Series 30 now operated. DC-9-50 interiors will have the wide-body look and a completely new decor featuring dramatic cabin lighting; coordinated colors for fabrics and carpeting; fold-down center seats; 15 percent more legroom; and enclosed overhead luggage compartments.

Fold-down seats are also being installed in the other DC-9s. On the three-seat side, passengers have the convenience of a table when the center seat is unoccupied.

The airline currently has 19 DC-9-30s and 31 Convair 580 prop-jets in its fleet of 50 aircraft. Two more of the 100-passenger fan jets will be delivered in April and May.

"Quick Tickets", introduced just a year ago, are now available at North Central passenger service counters in 40 locations. This automated system produces machine-printed tickets in 10 seconds for passengers with advance reservations.

A unique customer service, the Passenger Action Line (PAL), was begun last fall. Personnel in the Customer Relations Department act as ombudsmen, by telephone, for both passengers and North Central agents in the field to resolve travel problems and misunderstandings quickly and amicably. Although in operation just a few months, PAL is already a significant part of the airline's effort to show personal concern for its customers.

The company's new $1.8-million DC-9 digital flight simulator for pilot training is scheduled to be operational this August. The simulator, located in the new air freight facility, employs a six-axis motion system synchronized with visual equipment to duplicate actual flight sensations. It permits realistic emergency training which cannot be performed in an aircraft. Briefing rooms for check pilots and students will be available, along with offices for simulator engineers. The simulator can be used for nearly all DC-9 pilot training, saving the company many hours of actual flight time, besides providing more complete training.

During 1974, the maintenance department continued its efforts to have more work for company personnel to perform. Specialized equipment was installed for inspection of jet engines and components. Other acquisitions include new tooling, for the complete testing and overhaul of aircraft auxiliary power units, and another precision mill for machining metal parts. These improvements expedite production and allow closer control of reliability and costs.

The computerized data base system called SCEPTRE is nearing reality. The cutover is scheduled to begin this September. The system is designed to provide "up-to-the-minute" information on the service records of all aircraft and components, the parts inventory, and maintenance work schedules. Through TV-type screens, and some hard-copy printers, personnel throughout the system will have immediate access to the real-time data that SCEPTRE accumulates. Ultimately, the system may be applied to other departments in the company.

Through creative planning, North Central is making prudent use of its resources to improve the reliability and efficiency of its service to the traveling and shipping public.

North Central's new $1-million air freight facility is part of the company's headquarters complex at the Minneapolis-St. Paul International Airport.

Coordinator, Flight Control

Flight crew

Mechanic

Station Agent

Reservationists

Flight Attendant

Passenger Service Agents

Food Service Manager and Chef

good people make ~~an~~ an airline great

route development

Winnipeg became the newest and northernmost city on North Central's system when nonstop flights from Duluth/Superior were inaugurated on October 27, 1974.

North Central now offers the first single-plane service between the Manitoba capital and several Minnesota, Wisconsin, and Michigan cities. With this 314-mile route, the airline's system now spans 10,200 miles.

The Winnipeg route was awarded by the Civil Aeronautics Board (CAB) under an amendment to the 1966 Bilateral Air Transport Agreement between the United States and Canada. The amendment, which was formally ratified in May 1974, also authorizes Detroit-Montreal flights after 1978. The company has filed to serve that route via Toronto.

In a decision issued February 5, 1975, the CAB ruled in favor of the company's request that its nine existing domestic route segments be redesignated as one. North Central sought the change to allow greater scheduling flexibility between city pairs on its system.

Late in 1974, North Central filed an application with the CAB for a Chicago-New Orleans nonstop route and requested an expedited hearing because one of the two authorized carriers has suspended nonstop service. North Central is proposing three round-trip flights between the two cities with 100-passenger DC-9 fan jets.

If approved, the new service would generate about $8 million in revenues the first year, with an estimated $2.6-million operating profit. Approximately 40 percent of the projected North Central passenger traffic on this 840-mile segment would originate or terminate on the airline's flights serving 25 cities in Michigan, Wisconsin, Minnesota and North Dakota. The new route would provide these cities with single-carrier service to New Orleans for the first time.

In addition, passengers from Milwaukee, Green Bay/Clintonville, Minneapolis/St. Paul, Grand Forks, Marquette and Grand Rapids would have new single-plane service to New Orleans via North Central.

Four other applications for major nonstop routes are awaiting Board action to start proceedings. In 1974, the CAB denied the company's request for expedited hearings on the proposed Milwaukee-Philadelphia and Detroit-Boston service. The same action was taken earlier on Milwaukee-Denver and Detroit-New York. These four long-haul routes would generate about $25 million annually in operating revenues and $6 million in operating profit.

Hearings on one or more of these filings are expected during 1975. In recent years, however, the Board had drastically curtailed the granting of new routes because of the adverse economic conditions of some carriers and the uncertain fuel situation.

In the Detroit, Cleveland, Cincinnati-Atlanta case, all carriers' applications were denied by the Board, and one airline's appeal is pending.

North Central is continuing to pursue its present applications, totaling 6,647 miles, and to evaluate new routes that would improve service to the traveling public and be economically beneficial to the airline. Principal cases now pending are summarized below:

CHICAGO-NEW ORLEANS NONSTOP

The airline requested an expedited hearing on this application because one of the two authorized carriers has suspended nonstop flights. North Central would provide the first single-carrier service for 25 cities in Michigan, Wisconsin, Minnesota and North Dakota. Eight of those cities would have single-plane service. Three daily round trips are proposed. (840 miles)

MILWAUKEE-PHILADELPHIA NONSTOP

New nonstop service has been proposed between Milwaukee and Philadelphia, providing single-plane service for 10 Minnesota and Wisconsin communities. Although two other carriers are certificated on the route, only one nonstop flight is available in each direction. (690 miles)

DETROIT-BOSTON NONSTOP

North Central would offer the first competitive nonstop service between Detroit and Boston and also the only single-plane service between Boston and seven Michigan cities, plus South Bend, Indiana, via Detroit. (632 miles)

MILWAUKEE-DENVER NONSTOP

North Central would provide the first competitive service in this market, with flights originating in cities east of Milwaukee. (908 miles)

DETROIT, CLEVELAND, CINCINNATI-ATLANTA

The CAB denied all applications, and another carrier's appeal is pending. The company filed to serve Atlanta from Detroit and Cincinnati. (968 miles)

MICHIGAN POINTS-DETROIT-NEW YORK

This proposed authority would enable North Central to provide new, single-plane service through Detroit to New York City from ten Michigan cities. (501 miles)

COLUMBUS, DAYTON, CINCINNATI-PHILADELPHIA NONSTOP

The company's request to serve Philadelphia from Columbus, Dayton, and Cincinnati has been consolidated into the CAB's Ohio/Indiana Points Nonstop Service Investigation. (1,389 miles)

TWIN CITIES-KANSAS CITY NONSTOP

This application would permit North Central to operate nonstop flights in addition to the present two-stop service. (404 miles)

DETROIT-MONTREAL, VIA TORONTO

Authority to serve Montreal from Detroit, via Toronto, was requested under an amendment to the 1966 Bilateral Air Transport Agreement between the United States and Canada. With this route, North Central could also offer convenient single-plane service from Minneapolis/St. Paul and Milwaukee to Montreal. The amendment authorizes Detroit-Montreal flights by a U.S. carrier after 1978. (315 miles)

NORTH CENTRAL ROUTE REALIGNMENT

North Central's request that its nine existing route segments be redesignated as one has been approved by the CAB. The airline now has greater flexibility for scheduling between city pairs on its system.

Nonstop service to Winnipeg was inaugurated from this new $6.2-million terminal at the Duluth International Airport.

social action programs

An expanded, aggressive "Affirmative Action" program was implemented by North Central in 1974. The program, approved by the Federal Aviation Administration, complements the equal opportunity policy the airline has followed for many years.

The company feels that Affirmative Action is vital to the successful conduct of business and to basic human dignity and welfare. This approach establishes goal-setting procedures to promote job opportunities for women and minorities. Affirmative Action is a commitment to hire and advance minorities and women at an accelerated pace until employee totals reach parity with the workforce available at each location.

North Central is conducting a vigorous recruiting drive to seek minority and female applicants who meet the airline's job standards. Some 30 minority organizations visited the company in 1974, and applications are being received directly from minority employment agencies, colleges and vocational schools.

The Affirmative Action program is providing benefits to North Central and the communities it serves—through fuller utilization and development of people's talents.

The airline is making a concerted effort to establish mutually profitable business relationships with minority vendors who offer needed goods and services. The objective is to help these firms develop into stable enterprises that will be competitive and reliable suppliers for years to come.

North Central has 3,360 employees, 90 percent of whom are represented by one of six unions. Negotiations are held in a positive atmosphere which contributes to reaching equitable agreements while considering employee needs, the company's financial condition, industry developments and the general economy. During 1974, contracts were signed with three unions for two-year periods, and discussions are currently being held with two others. The sixth agreement expires in September 1975.

The company believes that high employee morale is one of its most important assets. The excellent working relationship between management and contract employees is evidenced by the fact that North Central has never had a single day of work stoppage in its 27-year history.

Fuel conservation measures at North Central saved 200,000 gallons of aviation fuel monthly—or nearly two-and-a-half million gallons in 1974. Revised flight procedures are an important part of this continuing program to conserve jet fuel. Among these are lower cruising speed, delayed use of landing flaps on approach, deferred engine-startup in the gate-hold area, reduced use of the auxiliary power unit, taxiing aircraft with one engine, conducting flight training in simulators when possible, and absorbing most departure delays at the gate.

Additional steps taken to conserve fuel include selective equipment substitution, some schedule reduction, and curtailed extra sections and scenic flights.

Thermostats in company buildings are at 68° for working hours and turned down to 60° in off-hours. General lighting remains at a lowered level which saved over three million watts in 1974. Numerous employee car pools are operating.

"Waste Not" is the theme of North Central's new paper recycling program. About 60 percent of all paper material discarded at the airline's headquarters can be recycled. In less than a year, 54 tons of material have been sent for reprocessing.

To minimize the effect of aircraft noise on the community, standardized flight procedures have been adopted. In addition, all jets on order will be equipped with acoustically-treated engine nacelles.

On a more personal note, flight crews respond to distress calls whenever they can without jeopardizing the safety of their passengers. Recently, a private pilot whose aircraft had malfunctioning navigational aids was guided through overcast skies to safety. Last summer, a Northliner captain spotted and reported a disabled boat on Lake Michigan. The message was relayed to the U.S. Coast Guard, which towed the boat ten miles to shore.

By word and deed, the airline is operating as a responsible corporate citizen—and North Central people are carrying out social action programs with individual concern.

Affirmative Action Program assists minorities and women.

the future

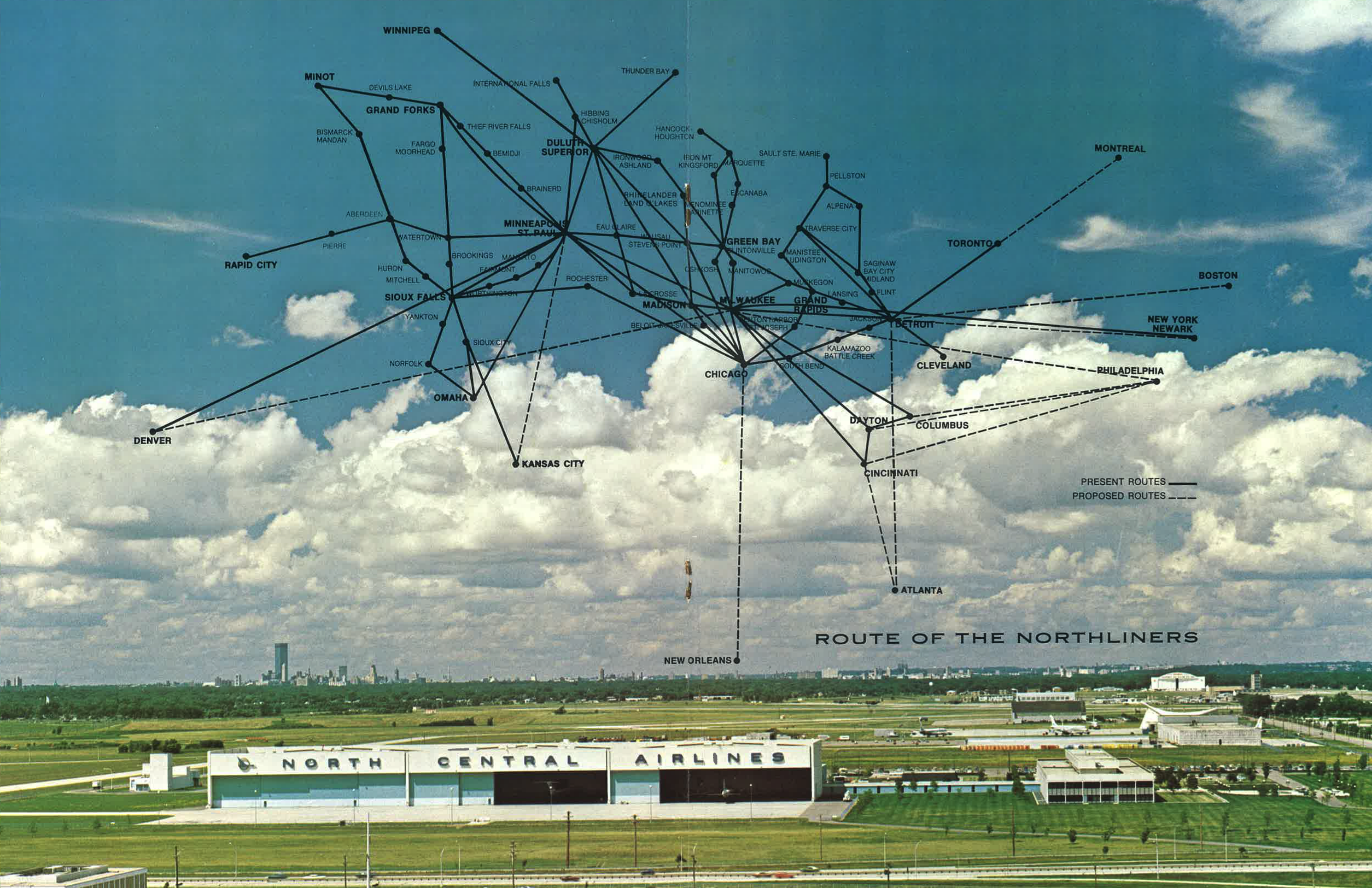
North Central, having just completed the most profitable year in its history, looks forward to further traffic and revenue growth in 1975. Final results will reflect the airline's ability to capitalize on current market advantages and participate in the nation's economic recovery.

In the past year, reduced highway speed limits, along with the scarcity and high price of gasoline, prompted many people to fly rather than drive. Federal programs to spur the economy should generate more business and pleasure travel, and vacationers are showing greater interest in taking domestic trips. Increased jet service always stimulates traffic, and North Central will be adding two new DC-9 fan jets to the Spring schedule. Freight volume is likely to improve as inventories dwindle and businessmen turn to air service for quick delivery rather than keeping large supplies on hand.

These combined factors, which influence the demand for air transportation, are expected to increase revenues. Some benefit is also anticipated from the new fare structure ordered by the Civil Aeronautics Board effective April 29, 1975.

Current supplies of aviation fuel are adequate, although prices continue to climb at an accelerated rate. Other expenses are also rising, but at a more moderate pace.

The company's 3,360 employees have proved themselves dedicated and productive. Their efforts, combined with tight cost controls and additional revenues, should make 1975 another profitable year for North Central.


ROUTE OF THE NORTHLINERS
PRESENT ROUTES
PROPOSED ROUTES
WINNIPEG
MINOT
DEVILS LAKE
GRAND FORKS
THIEF RIVER FALLS
INTERNATIONAL FALLS
THUNDER BAY
HIBBING
CHISHOLM
BISMARCK
MANDAN
FARGO
MOORHEAD
BEMIDJI
DULUTH
SUPERIOR
HANCOCK
HOUGHTON
IRONWOOD
ASHLAND
IRON MT
KINGSFORD
MARQUETTE
SAULT STE. MARIE
PELLSTON
ESCANABA
ALPENA
BRAINERD
RHINELANDER
ABERDEEN
MINNEAPOLIS
ST. PAUL
EAU CLAIRE
TRAVERSE CITY
WATERTOWN
PIERRE
RAPID CITY
GREEN BAY
CLINTONVILLE
MANISTEE
LUDINGTON
BROOKINGS
MANKATO
HURON
FAIRMONT
ROCHESTER
OSHKOSH
MANITOWOC
SAGINAW
BAY CITY
MIDLAND
MITCHELL
MUSKEGON
FLINT
SIOUX FALLS
WORTHINGTON
LACROSSE
MADISON
MILWAUKEE
GRAND RAPIDS
LANSING
YANKTON
JACKSON
DETROIT
BENTON HARBOR
ST. JOSEPH
SIOUX CITY
KALAMAZOO
BATTLE CREEK
NORFOLK
SOUTH BEND
CHICAGO
CLEVELAND
OMAHA
DENVER
KANSAS CITY
DAYTON
COLUMBUS
CINCINNATI
ATLANTA
NEW ORLEANS
MONTREAL
TORONTO
BOSTON
NEW YORK
NEWARK
PHILADELPHIA
NORTH CENTRAL AIRLINES

NORTH CENTRAL AIRLINES, INC.

balance sheet

ASSETS	December 31 1974	1973
CURRENT ASSETS		
Cash, including certificates of deposit of $512,000 in 1973 (note B)	$ 5,055,000	$ 3,458,000
Short-term investments — at cost, which approximates market	9,750,000	8,987,000
Accounts receivable, less allowances (note A)	14,764,000	13,910,000
Flight equipment parts and supplies (notes A and C)	3,998,000	3,331,000
Prepaid expenses and other (note A)	5,030,000	4,478,000
	38,597,000	34,164,000
PROPERTY AND EQUIPMENT — at cost (notes A and F)		
Flight equipment (note C)	92,452,000	93,853,000
Ground property and equipment	9,741,000	7,623,000
Improvements to leased property	3,677,000	3,612,000
	105,870,000	105,088,000
Less accumulated depreciation	(36,962,000)	(31,026,000)
	68,908,000	74,062,000
Advance payments on equipment	4,984,000	2,262,000
	73,892,000	76,324,000
DEFERRED CHARGES AND OTHER ASSETS		
Unamortized development and preoperating costs (note A)	1,600,000	1,814,000
Rentals and other (notes A, D and F)	4,607,000	2,759,000
	6,207,000	4,573,000
	$118,696,000	$115,061,000
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Current maturities of long-term debt (note C)	$ 8,400,000	$ 8,097,000
Trade accounts payable	6,619,000	7,277,000
Interline payable and tickets outstanding (note A)	8,190,000	6,457,000
Accrued compensation and other expenses	8,122,000	7,363,000
Income taxes (notes A and J)	2,432,000	316,000
	33,763,000	29,510,000
LONG-TERM OBLIGATIONS		
Long-term debt — less current maturities (note C)	32,633,000	42,172,000
Deferred income taxes (notes A and J)	4,867,000	2,504,000
Warrant obligation (note C)	281,000	264,000
	37,781,000	44,940,000
COMMITMENTS (note F)	—	—
STOCKHOLDERS' EQUITY (notes C, G and H)		
Common stock — authorized 16,000,000 shares of $.20 par value	2,493,000	2,493,000
Additional paid-in capital	18,032,000	18,032,000
Retained earnings	27,044,000	20,086,000
Less treasury stock — 150,900 shares at cost	(417,000)	—
	47,152,000	40,611,000
	$118,696,000	$115,061,000

The accompanying notes are an integral part of this statement.

statement of earnings

	Years ended December 31 1974	1973
OPERATING REVENUES		
Passenger (note A)	$124,007,000	$104,279,000
Freight and express	8,158,000	7,123,000
Public service revenues (note I)	12,126,000	9,631,000
Mail	2,041,000	1,789,000
Non-scheduled service and other	5,158,000	5,161,000
	151,490,000	127,983,000
OPERATING EXPENSES		
Flying operations	38,077,000	30,929,000
Maintenance	20,983,000	17,551,000
Aircraft and traffic servicing	34,923,000	32,036,000
Passenger service	9,028,000	8,094,000
Promotion and sales	13,912,000	11,866,000
General and administrative	7,179,000	6,594,000
Other transport-related expense	1,377,000	1,562,000
Depreciation and amortization (note A)	8,017,000	7,350,000
	133,496,000	115,982,000
Operating profit	17,994,000	12,001,000
OTHER EXPENSES (INCOME)		
Interest expense	3,868,000	3,623,000
Less interest capitalized (note A)	341,000	142,000
	3,527,000	3,481,000
Interest income and other — net	(1,229,000)	(690,000)
	2,298,000	2,791,000
Earnings before income taxes	15,696,000	9,210,000
INCOME TAXES (notes A and J)		
Currently payable	5,348,000	2,530,000
Deferred	2,144,000	233,000
	7,492,000	2,763,000
NET EARNINGS	$ 8,204,000	$ 6,447,000
NET EARNINGS PER SHARE (note K)	$ .66	$ .52

The accompanying notes are an integral part of this statement.

statement of changes in financial position

SOURCES AND APPLICATIONS OF WORKING CAPITAL	Years ended December 31 1974	1973
SOURCES		
From operations		
Net earnings	$ 8,204,000	$ 6,447,000
Charges to earnings not using working capital		
Depreciation and amortization (note A)	8,017,000	7,350,000
Deferred income taxes (note J)	2,363,000	184,000
Other	200,000	195,000
Working capital provided from operations	18,784,000	14,176,000
Proceeds in excess of gain from property and equipment dispositions	1,061,000	799,000
Increase in long-term debt	—	15,105,000
Reduction of insurance receivable	—	4,300,000
Other	—	71,000
	19,845,000	34,451,000
APPLICATIONS		
Additions to property and equipment	5,881,000	24,355,000
Additions to deferred charges	2,582,000	730,000
Reduction of long-term debt	9,539,000	9,260,000
Purchase of treasury stock	417,000	—
Payment of cash dividend	1,246,000	623,000
Other	—	268,000
	19,665,000	35,236,000
INCREASE (DECREASE) IN WORKING CAPITAL	180,000	(785,000)
Working capital at beginning of year	4,654,000	5,439,000
Working capital at end of year	$ 4,834,000	$ 4,654,000
NET CHANGE IN WORKING CAPITAL ELEMENTS		
Increase (decrease) in current assets		
Cash and certificates of deposit	$ 1,597,000	$ (5,439,000)
Short-term investments	763,000	2,487,000
Accounts receivable	854,000	2,825,000
Flight equipment parts and supplies	667,000	596,000
Prepaid expenses and other	552,000	(111,000)
Net change in current assets	4,433,000	358,000
Increase (decrease) in current liabilities		
Current maturities of long-term debt	303,000	1,022,000
Trade and interline payables and tickets outstanding	1,075,000	2,579,000
Accrued compensation and other expenses	759,000	(494,000)
Income taxes	2,116,000	(1,964,000)
Net change in current liabilities	4,253,000	1,143,000
INCREASE (DECREASE) IN WORKING CAPITAL	$ 180,000	$ (785,000)

statement of changes in stockholders' equity

Years ended December 31, 1974 and 1973

	Common Stock Shares Issued	Common Stock Amount	Additional Paid-In Capital	Retained Earnings (note C)	Treasury Stock Shares Held	Treasury Stock Amount
Balance at January 1, 1973	12,462,752	$2,493,000	$18,032,000	$14,262,000	—	$ —
Cash dividend (note H)	—	—	—	(623,000)	—	—
Net earnings for the year	—	—	—	6,447,000	—	—
Balance at December 31, 1973	12,462,752	2,493,000	18,032,000	20,086,000	—	—
Cash dividend (note H)	—	—	—	(1,246,000)	—	—
Purchase of treasury stock	—	—	—	—	150,900	417,000
Net earnings for the year	—	—	—	8,204,000	—	—
Balance at December 31, 1974	12,462,752	$2,493,000	$18,032,000	$27,044,000	150,900	$417,000

The accompanying notes are an integral part of these statements.

notes to financial statements

December 31, 1974 and 1973

Note A—Summary of Significant Accounting Policies—The company, regulated by the Civil Aeronautics Board (CAB), uses the Uniform System of Accounts and Reports for Certificated Air Carriers as required by the CAB, which are consistent with generally accepted accounting principles. The significant policies consistently followed by the company are:

Flight Equipment Parts and Supplies: These are priced at average cost. An allowance for obsolescence ($551,000 in 1974 and $465,000 in 1973) is provided for parts expected to be on hand at the date the related aircraft are fully depreciated by allocating costs of repairable items over their useful lives.

Prepaid Expenses — Engine Overhaul: Engine overhaul costs are charged to expense as incurred except for those overhaul costs included in the purchase price of Flight Equipment. The company reclassifies to a current prepaid expense the cost of those overhauls estimated to be consumable within the next twelve months by reducing costs included in Flight Equipment ($2,175,000 in 1974 and 1973).

Capitalized Interest: Interest is capitalized on funds associated with major project expenditures such as acquisition of flight equipment, construction of ground facilities and expenditures for route development and preoperating costs. Capitalization of interest ceases when projects become operational. The capitalized interest is amortized over the useful lives of the related assets for financial reporting purposes but charged to current period expense for income tax reporting purposes. The effect on net earnings (after taxes) of capitalizing interest rather than expensing as incurred for financial reporting purposes was approximately $118,000 in 1974 and $29,000 in 1973.

Depreciation: Depreciation is provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives on a straight line basis for financial and tax reporting purposes. Prior to 1968, accelerated depreciation methods were used for tax purposes. Flight equipment is being depreciated to residual values (15% of cost): Convair 580 based on a common retirement date of June 1979 and DC-9-30 based on 15-year lives.

Deferred Charges: Expenditures for route development are deferred and amortized over the life of temporary certificates, or five years for permanent certificates. Aircraft preoperating costs are amortized over approximately eight years. Certain expenditures are expensed when incurred for tax reporting purposes.

Passenger Revenues: Revenues are recognized when the transportation service is rendered. Tickets sold by others and lifted by the company prior to December 31, are included in accounts receivable until payment is received. Tickets sold for flights on other airlines, for which reimbursement has not been made, and tickets sold by the company for their flights which are unused at December 31, are included in interline payable and tickets outstanding.

Pension Costs: The company has pension plans for substantially all of its employees, and funds its current expense of normal costs and amortization of prior service costs over periods ranging from 25 to 40 years. Asset appreciation or depreciation is applied to the unfunded prior service cost. Pension funding is determined primarily by using the Unit Credit Method (note E).

Income Taxes: The company uses the flow-through method of accounting for investment tax credit which reduces income tax expense when the related liability is reduced. The company recognizes deferred income taxes resulting from differences in financial and income tax reporting (note J).

Note B — Compensating Cash Balances — The company maintains compensating cash balances in connection with its long-term debt financing (note C) and for general operating purposes. Such balances averaged approximately $2,000,000 during 1974 and 1973 and are not legally restricted.

Note C — Long-Term Debt — Long-term debt at December 31 consists of the following:

	1974	1973
Quarterly installment notes (a)	$25,566,000	$31,247,000
Semi-annual installment notes (b)	—	1,705,000
Semi-annual installment notes (c)	13,800,000	15,000,000
Total due banks and insurance companies (d)	39,366,000	47,952,000
Semi-annual subordinated notes (e)	900,000	1,500,000
Subordinated convertible debentures (f)	690,000	692,000
Sundry	77,000	125,000
Total long-term debt	41,033,000	50,269,000
Less current maturities (g)	(8,400,000)	(8,097,000)
	$32,633,000	$42,172,000

(a) Payable as follows: a regular quarterly payment of $1,420,000 plus interest, in January 1975, and a required prepayment of $1,058,000 plus interest, in March 1975 resulting from the sale of two CV-580 aircraft which were collateral for the obligation; the remainder in quarterly installments of $1,358,000 plus interest, from April 1975 through April 1976 and alternating quarterly installments of $1,358,000 and $1,811,000 plus interest, from July 1976 through October 1978; interest at 7%.

(b) Fully paid in November 1974; effective rate at December 31, 1973 was 11%.

(c) Payable in semi-annual installments of $600,000 plus interest, through July 1978 and quarterly installments of $2,250,000 plus interest, from January 1979 through October 1979; interest at ½% above bank's prime rate; effective interest rate at December 31 was 10½%-11% in 1974 and 10½% in 1973 (note B).

(d) Total due banks and insurance companies is collateralized by substantially all flight equipment and spare aircraft parts owned by the company. Two equipment manufacturers partially guarantee these loans. Included in the loan agreement provisions are restrictions on dividend payments, capital expenditures, additional borrowings and requirements related to minimum working capital and net worth. The company has a commitment to retire 259,511 warrants at $1.50 per warrant within 30 days after the expiration date of October 31, 1979 for any of these warrants not then exercised. These warrants were issued to loan holders in consideration of deferring certain debt repayments. The obligation is being accrued as additional interest expense through 1979.

(e) Payable in semi-annual installments of $300,000 plus interest at 7% through March 1976. Stock purchase warrants issued in connection with this debt enable the holders to purchase a total of 200,000 common shares (note H).

(f) Convertible into common shares at $8.55 a share to maturity, June 1, 1978; interest at 5½%.

(g) Current maturities of all long-term debt due in each of the next five years following December 31, 1974 are as follows:

1975	$ 8,400,000
1976	7,867,000
1977	7,538,000
1978	8,228,000
1979	9,000,000
	$41,033,000

Note D — Investment Leasing — During 1974, the company entered into lease agreements as a lessor. These leasing activities are recorded under the finance method of accounting. At December 31, 1974, investment in leased equipment, net of the $1,500,000 note, totals $1,255,000, which includes estimated residual values of $267,000.

Under the terms of a leverage lease transaction, the company received approximately $1,500,000 on a 10% note and has assigned future lease payments and the associated equipment, costing approximately $1,880,000, as collateral. The loan agreement provides that the company's liability is limited to its remaining investment in this equipment. The 10% note is recorded as an offset against the receivable from lessee.

notes to financial statements

December 31, 1974 and 1973 (continued)

The leases contain renewal options and transfer essentially all costs of ownership to the lessees.

Note E — Pension Costs — Total pension expense was $4,150,000 for 1974 and $3,014,000 for 1973. At January 1, 1974, the latest actuarial valuation date, the actuarially computed value of vested benefits for all plans exceeded the total market value of fund assets by approximately $5,523,000. Changes in funding methods for certain of the plans did not have a material effect on pension expense for 1974. Market value declines and improvements in benefits account for the major portion of the increase of vested benefits over the market value of fund assets.

The Pension Reform Act of 1974 is not expected to have a significant future effect on the amount of the company's pension expense, funding or unfunded vested benefits.

Note F — Commitments — Total rent expense, including landing fees, was $12,876,000 in 1974 and $12,177,000 in 1973, including rentals under "financing leases" (as defined by the Securities and Exchange Commission) of $6,375,000 in 1974 and $6,523,000 in 1973.

The company has lease commitments for various airport facilities based upon usage and landings, subject to adjustment depending upon the needs of the airport operating authority. These leases expire over varying periods, and future annual lease commitments are not determinable due to the usage and adjustment factors.

At December 31, 1974, the company's minimum rental commitments under non-cancellable leases with initial or remaining terms of more than one year were as follows (in thousands of dollars):

Period	DC-9-30 Aircraft	CV-580 Aircraft	Computer Equipment	Facilities	Other	Total
1975	$2,088	$1,715	$1,227	$1,634	$283	$ 6,947
1976	2,088	392	1,227	1,634	283	5,624
1977	2,088	—	1,227	1,634	215	5,164
1978	2,088	—	1,227	1,634	48	4,997
1979	2,088	—	1,023	1,634	28	4,773
1980-1984	4,045	—	—	8,170	28	12,243
1985-1989	—	—	—	8,105	—	8,105
1990-1994	—	—	—	7,500	—	7,500
1995-2000	—	—	—	3,852	—	3,852

The lease commitments for CV-580 aircraft and various facilities included in the above tabulations reflect both the current period expense and the rental prepayment required under the terms of the leases. Since the DC-9-30 leases are related to the prevailing prime interest rate, the 1974 expense was approximately $600,000 in excess of the minimum commitment. Nearly all leases contain renewal or extension options which are to be negotiated within specified periods prior to the expiration of the leases.

The present value of the noncapitalized financing leases and the related interest rates at December 31 are (in thousands of dollars):

	Interest Rate	1974	1973
Five DC-9-30 aircraft	6½%	$11,520	$12,828
Nine CV-580 aircraft	5¾%	2,344	3,611
Computer equipment	8½%	5,050	5,628
Facilities	4½%	16,436	16,909
Other	6¾%	724	1,029
Total		$36,074	$40,005

The impact on net earnings by capitalization of such leases would have been immaterial. The company, regulated by the CAB, is unable to determine what impact the above capitalization might have on the rate base and any consequent rate adjustments.

At December 31, 1974, the company had purchase commitments on two new DC-9-30 aircraft and three new DC-9-50 aircraft for which it has advanced $3,638,000 and capitalized interest of $216,000. An additional $29,161,000 will be expended by the company in fulfilling these commitments. The two DC-9-30 aircraft are scheduled for delivery in April and May, 1975 and the three DC-9-50 aircraft are to be delivered in 1976. The total purchase price of $32,799,000 could be adjusted upwards since it is based upon an agreement which allows for changes in specifications. In addition, the company also purchased an option for $75,000 to buy three additional DC-9-50 aircraft. If this option is exercised prior to May 1975, the total purchase commitment for the three aircraft would be an additional $21,673,000 and would be expended prior to delivery in December 1976.

A spare engine for the DC-9-50 aircraft, with a cost of $588,000, is scheduled for delivery in March 1976, for which the company has advanced $29,000.

At December 31, 1974, the company had a purchase commitment for a digital flight simulator and visual system for Douglas DC-9 aircraft which amounted to $1,750,000 of which $984,000 had been paid in advance deposits. The company has capitalized interest of $42,000 on these deposits. The scheduled delivery date is July 1975.

Under provisions of the Mutual Aid Agreement, the company would pay struck carriers who are a party to this agreement. The company would receive such payments in the event of a strike by its employees.

Note G — Stockholder Disclosure of Ownership — The company is required by §245.16 of the Civil Aeronautics Board Economic Regulations to include in its annual report to stockholders the following notice:

(1) Any person who either owns, as of December 31, of the year preceding issuance of such annual report, or subsequently acquires, beneficially or as trustee, more than 5 percent, in the aggregate, of any class of the capital stock or capital of the air carrier, shall file with the Board a report containing the information required by §245.12, on or before April 1, as to the capital stock or capital owned as of December 31, of the preceding year, and in the case of stock subsequently acquired, a report under §245.13, within 10 days after such acquisition or ownership;

(2) any bank or broker covered by (1), to the extent that it holds shares as trustee on the last day of any quarter of a calendar year, shall file with the Board, within 30 days after the end of the quarter, a report in accordance with the provisions of §245.14; and

(3) any person required to report under this subpart who grants a security interest in more than 5 percent of any class of the capital stock or capital of the air carrier shall within 30 days after granting such security interest file with the Board a report containing the information required in §245.15. The notice shall also state that any stockholder who believes that he may be required to file such a report may obtain further information by writing to the Director, Bureau of Operating Rights, Civil Aeronautics Board, Washington, D. C. 20428.

Note H — Common Stock — Under a qualified plan, 350,000 shares of unissued common stock were reserved for officers and key employees. When options are exercised, the excess of the option price over par value of the shares is credited to additional paid-in capital. The company makes no charges to income in connection with the shares issued under the stock option plan.

Options Outstanding		Option Price and Fair Market Value at Date of Grant				
			December 31, 1974		December 31, 1973	
Year Granted	Year Exercisable	Per Share	Shares	Amount	Shares	Amount
1969	1969	$4.125	—	$ —	18,000	$ 74,250
1970	1970	4.125	—	—	47,500	195,937
1970	1970	3.25	95,000	308,750	105,000	341,250
1971	1971	3.1875	36,100	115,069	38,050	121,284
1972	1972	6.375	—	—	2,500	15,937
1973	1973	4.25	7,500	31,875	7,500	31,875
1974	1974	3.375	8,525	28,772	—	—
1974	1974	2.75	23,925	65,794	—	—
1974	1975	2.75	45,000	123,750	—	—
1974	1977	2.75	2,500	6,875	—	—
			218,550	$680,885	218,550	$780,533
Options exercised			131,450		131,450	
			350,000		350,000	

All options granted expire five years after date of granting. There were no additional options available for granting as of December 31, 1974 or 1973.

At December 31, 1974 and 1973, there were outstanding warrants to purchase 2,649,061 shares of common stock. These warrants resulted from public offerings prior to 1973 and from financial transactions as discussed in note C(d) and (e). All warrants enable the holder to purchase common stock at $5.50 per share and must be exercised by October 31, 1979.

During January 1975, the Board of Directors declared a $.10 per share dividend payable on March 3, 1975 to shareholders of record on February 17, 1975. The company paid cash dividends to its shareholders during the first quarter of 1974 and 1973, of $.10 and $.05 per share, respectively.

Note I — Public Service Revenues — As a local service carrier, the company receives public service revenues for serving small and intermediate size communities which do not generate sufficient traffic to fully support profitable air service. The amount of such payments is determined by the CAB on the basis of its evaluation of the amount of revenue needed to meet operating expenses and provide a reasonable return on investment with respect to eligible routes. The amount so determined is reduced by a portion of the company's earnings on routes not eligible for public service revenue. The CAB adopted Class Rate VII effective as of July 1, 1973. It provides for semiannual review of the company's public service revenue rate and has no specified expiration date.

Note J — Income Taxes — Income tax expense for the years ended December 31 is made up of the following components:

	1974	1973
Currently payable income taxes		
Federal	$7,214,000	$4,413,000
Investment tax credit	(2,798,000)	(2,275,000)
	4,416,000	2,138,000
State and local	932,000	392,000
	5,348,000	2,530,000
Deferred income taxes		
Federal	190,000	396,000
Investment tax credit	1,933,000	(200,000)
	2,123,000	196,000
State and local	21,000	37,000
	2,144,000	233,000
	$7,492,000	$2,763,000

The income tax expense of $7,492,000 in 1974 and $2,763,000 in 1973 (effective rates of 47.7% and 30.0%, respectively) are less than those expected to result by application of the Federal income tax rate of 48% to income before taxes. For the years ended December 31, the reasons for these differences are:

	1974	1973
Computed "expected" tax expense	$7,534,000	$4,421,000
Increase (decrease) in income taxes		
Investment tax credit utilized	(865,000)	(2,475,000)
State and local income taxes	953,000	429,000
Other	(130,000)	388,000
Actual tax expense	$7,492,000	$2,763,000

The deferred income taxes resulted from the reversal of previously deferred investment tax credit and the tax effect of the following timing differences for the years ended December 31:

	1974	1973
Increase (decrease) in deferred income tax expense		
Excess of tax over book depreciation	$ 98,000	$ 71,000
Interest capitalized for book, not for tax	181,000	43,000
Vacation pay expensed for tax, previously expensed for book	86,000	48,000
Amortization for book, of items already expensed for tax		
Training and development	(248,000)	(140,000)
Extension and development	(73,000)	(40,000)
Capitalized interest	(56,000)	(30,000)
Gain on sale of equipment	(59,000)	(41,000)
Lessor leasing activities	61,000	—
Deferred investment tax credit	1,933,000	—
Adjustment to previously deferred tax	221,000	322,000
	$2,144,000	$233,000

The company has no remaining investment tax credit available to offset future income taxes payable.

Note K — Net Earnings Per Share — Net earnings per share is based on the weighted average number of shares outstanding for the year (12,431,869 in 1974 and 12,462,752 in 1973). Conversion of debentures into common stock, exercise of stock options and warrants to purchase stock would not result in material dilution of net earnings per share for the years ended December 31, 1974 and 1973.

Note L — Reclassifications — Certain of the 1973 figures have been reclassified where appropriate to conform with the financial statement presentation used in 1974.

auditors' report

Alexander Grant
& COMPANY
CERTIFIED PUBLIC ACCOUNTANTS

MIDWEST PLAZA BUILDING MINNEAPOLIS, MN 55402
FIRST NATIONAL BANK BUILDING ST. PAUL, MN 55101
INTERNATIONAL FIRM
ALEXANDER GRANT TANSLEY WITT

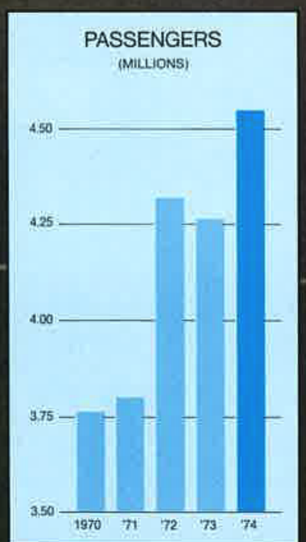
Stockholders and Board of Directors
North Central Airlines, Inc.

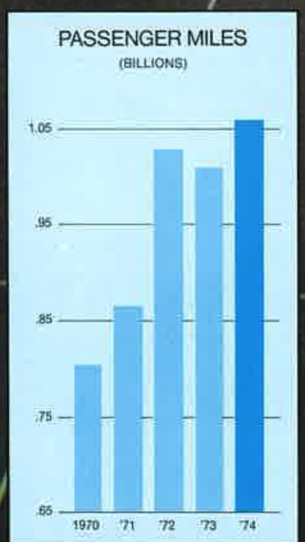
We have examined the balance sheet of North Central Airlines, Inc. (a Wisconsin corporation) as of December 31, 1974 and 1973, and the related statements of earnings, changes in stockholders' equity and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

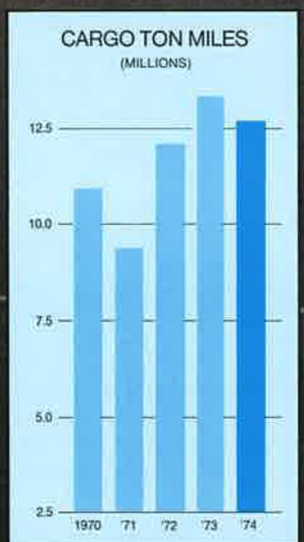
In our opinion, the financial statements referred to above present fairly the financial position of North Central Airlines, Inc., at December 31, 1974 and 1973, and the results of its operations and changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

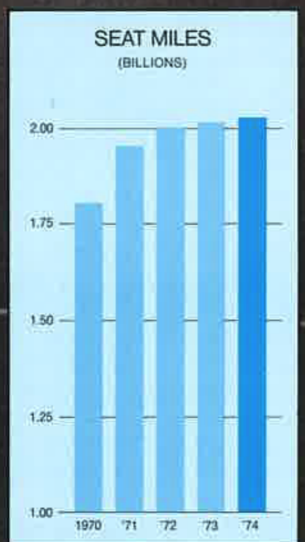
Alexander Grant & Company

Minneapolis, Minnesota
February 17, 1975









five-year summary

EARNINGS

	1974	1973	1972	1971	1970
OPERATING REVENUES					
Passenger	$124,007,000	$104,279,000	$ 99,260,000	$ 83,821,000	$ 76,954,000
Public service revenues	12,126,000	9,631,000	9,090,000	6,885,000	5,131,000
Other	15,357,000	14,073,000	12,903,000	10,905,000	10,345,000
	151,490,000	127,983,000	121,253,000	101,611,000	92,430,000
OPERATING EXPENSES					
Flying operations and maintenance	59,060,000	48,480,000	46,732,000	43,360,000	39,133,000
Other operating expenses	66,419,000	60,152,000	55,176,000	45,196,000	38,353,000
Depreciation and amortization	8,017,000	7,350,000	6,990,000	7,240,000	6,779,000
	133,496,000	115,982,000	108,898,000	95,796,000	84,265,000
OPERATING PROFIT	17,994,000	12,001,000	12,355,000	5,815,000	8,165,000
OTHER EXPENSES (INCOME)					
Interest expense	3,868,000	3,623,000	3,229,000	4,252,000	5,055,000
Capitalized interest	(341,000)	(142,000)	(14,000)	(23,000)	(156,000)
Interest income and other—net	(1,229,000)	(690,000)	(256,000)	(183,000)	20,000
	2,298,000	2,791,000	2,959,000	4,046,000	4,919,000
EARNINGS BEFORE TAXES	15,696,000	9,210,000	9,396,000	1,769,000	3,246,000
Income taxes	7,492,000	2,763,000	2,903,000	544,000	451,000
EARNINGS BEFORE EXTRAORDINARY GAIN AND ACCOUNTING ADJUSTMENT	8,204,000	6,447,000	6,493,000	1,225,000	2,795,000
Extraordinary gain on disposition of equipment (net of income taxes)	—	—	1,043,000	—	—
Prior years' adjustment due to accounting change (net of income taxes)	—	—	—	—	(617,000)
NET EARNINGS	$ 8,204,000	$ 6,447,000	$ 7,536,000	$ 1,225,000	$ 2,178,000
NET EARNINGS PER SHARE	$.66	$.52	$.60	$.11	$.21
DIVIDENDS PER SHARE	$.10	$.05	—	—	—

BALANCE SHEET ITEMS

	1974	1973	1972	1971	1970
Current assets	$ 38,597,000	$ 34,164,000	$ 33,806,000	$ 25,725,000	$ 24,606,000
Working capital from operations	$ 18,784,000	$ 14,176,000	$ 14,263,000	$ 9,204,000	$ 9,980,000
Working capital at year-end	$ 4,834,000	$ 4,654,000	$ 5,439,000	$ 3,900,000	$ (8,368,000)
Property and equipment—net	$ 73,892,000	$ 76,324,000	$ 59,143,000	$ 62,891,000	$ 73,038,000
Total debt	$ 41,033,000	$ 50,269,000	$ 43,402,000	$ 50,496,000	$ 66,651,000
Retained earnings	$ 27,044,000	$ 20,086,000	$ 14,262,000	$ 6,726,000	$ 5,502,000
Stockholders' equity	$ 47,152,000	$ 40,611,000	$ 34,787,000	$ 27,192,000	$ 17,823,000
Shares outstanding	12,312,000	12,463,000	12,463,000	12,446,000	10,463,000
Book value per share	$3.83	$3.26	$2.79	$2.18	$1.70

STATISTICS

	1974	1973	1972	1971	1970
Passengers	4,546,000	4,263,000	4,319,000	3,793,000	3,753,000
Passenger miles (000)	1,061,000	1,012,000	1,029,000	866,000	806,000
Available seat miles (000)	2,151,000	2,139,000	2,048,000	1,961,000	1,810,000
Passenger load factor	49.3%	47.3%	50.3%	44.2%	44.5%
Cargo ton miles	12,585,000	13,394,000	12,180,000	9,473,000	10,985,000
Revenue plane miles	29,055,000	29,422,000	29,200,000	28,204,000	26,693,000
Number of employees	3,360	3,250	3,120	3,020	3,150

communications

A dramatic advertising campaign introduced North Central's "Explorer's bill of fare" food service. Full-page newspaper advertisements in color highlighted the new cuisine now being offered on long-haul nonstop flights. This exclusive culinary adventure features savory dishes from around the world.

Portuguese specialties were used first in this series of uniquely prepared foods. The ad text carried the various menus, along with flight schedules and special tour packages. The impact was particularly noticeable in the Denver-Minneapolis/St. Paul market, where traffic increased 15 percent in 1974.

Another major advertising theme, "Get up on Cloud Nine", encouraged passengers to try North Central's DC-9 custom-jet service. This series promotes the three-and-two seating with fold-down center seat and complimentary meals on selected flights at regular coach fares.

Passengers were told of savings, through "interline" joint fares, when they start a trip on North Central and then transfer to another carrier. Popular give-away items, such as the "Frostbite Kit" and Ski Tips brochure, were again available, and a Fishing Tips booklet with a lure was added for travelers to major summer vacation spots.

A new skiing film was produced for groups interested in winter fun on the slopes and shown extensively. For the third consecutive year, reduced-rate "Broadway Show" tours were offered to New York travelers who fly North Central.

Media emphasis is reflected by audience figures. Advertising reached an estimated 8.1 million newspaper readers, 7.1 million television viewers, 4.4 million radio listeners and 1.5 million magazine subscribers. Ads in the different media are coordinated to reinforce each specific campaign.

The financial public relations program, expanded when the company was listed on the New York Stock Exchange in 1973, is continuing. Company officers periodically address major security analyst groups around the country about the airline's achievements and current news. Stories are regularly carried in The Wall Street Journal and on the Dow Jones and Reuters wire services.

Communications with stockholders included distribution of the 1973 Annual Report—selected by Financial World for an award in its industry class—and quarterly statements. Some 50 news releases reported financial results, traffic records and other North Central developments to media outlets. About 12,000 company history booklets, aircraft information sheets, and DC-9 postcards are given away annually.

Sales people made nearly 25,000 personal calls on principal industrial accounts and travel agencies over the airline's 13-state area and Canada. North Central personnel participated in 800 meetings with civic, industry, and special interest groups.

The Northliner Museum at the General Office officially opened in June 1974 and has already attracted more than 1,000 guests. Nearly 4,000 people, ranging from grade school children to adults, took conducted tours through the airline's facilities. Another public relations activity brought over 9,000 Twin Cities residents to the company's headquarters.

These visitors, who attended public functions in the cafeteria, saw part of the airline's operation and were introduced to food service from the North Central Flight Kitchen. Company people at other cities around the system also hosted groups interested in aviation.

Aboard the aircraft, the Northliner Magazine and the Northliner Gifts catalog are carried in each seat pocket. The 32-page magazine has entertaining articles about areas served by North Central and some phase of the airline's operation, as well as stories on travel and business. The catalog offers merchandise of interest to passengers, and many items carry the company name and mallard duck insignia.

The Northliner newspaper, judged in 1974 as the top paper published for regional airline employees, keeps personnel informed of company news on a monthly basis. Memos and bulletin board announcements provide interim communications. Corporate officers personally meet with employees at each station for an informal visit at least once a year.

As in the past, North Central receives additional support and publicity from many individuals and organizations. This invaluable assistance contributes measurably to the company's progress and is greatly appreciated.

1973 Annual Report and The Northliner newspaper received awards.

The Northliner Museum opened at the airline's headquarters.

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