ANNUAL REPORT 1979

REPUBLIC AIRLINES

Highlights

	1979	1978	Change
OPERATING REVENUES	$ 609,230,000	$ 487,565,000	25%
OPERATING PROFIT	$ 28,053,000	$ 42,809,000	(34)
NET EARNINGS	$ 13,061,000	$ 24,571,000	(47)
NET EARNINGS PER SHARE—Primary	$.70	$1.42	(51)
WORKING CAPITAL FROM OPERATIONS	$ 41,717,000	$ 57,806,000	(28)
RETAINED EARNINGS	$ 93,634,000	$ 83,050,000	13
STOCKHOLDERS' EQUITY	$ 145,514,000	$ 113,288,000	28
PASSENGERS	12,156,000	11,143,000	9
PASSENGER MILES	3,846,805,000	3,364,094,000	14
CARGO TON MILES	32,324,000	28,062,000	15

Contents

REPUBLIC AIRLINES, INC.
7500 Airline Drive • Minneapolis, Minnesota 55450 • 612-726-7406

About Republic

Republic Airlines, the nation's newest major carrier, was formed by the merger of North Central Airlines and Southern Airways on July 1, 1979. The company's principal function is to provide safe, dependable air transportation.

Each of the merged carriers had more than 30 years of airline experience. North Central, originally called Wisconsin Central, inaugurated service on February 24, 1948. Southern began scheduled flights on June 10, 1949. The two companies grew steadily and assumed positions of leadership among the regional carriers. Together, they have earned $77 million in the last five years.

Republic serves more cities—158 —than any other airline in the country. It flies to most of the nation's major metropolitan areas and many intermediate-sized cities in the Upper Midwest and Southeast. The airline's 38,400-mile route system extends from New England to California, and from Canada to the Cayman Islands in the Caribbean. (See center pages.)

The airline ranks among the top ten U.S. carriers in passenger traffic and operates one of the largest commercial jet fleets in the world. Republic carried 12.2 million passengers and flew 3.8 billion passenger miles in 1979. The company's 107 jet-powered aircraft—Boeing 727s, Douglas DC-9s and Convair 580s—make over 1,100 departures daily.

Republic's 9,000 dedicated employees offer the traveling public the finest type of scheduled airline service.

ANNUAL MEETING
Wednesday, April 9, 1980

AUDITORS
Alexander Grant & Company

REGISTRARS &
STOCK TRANSFER AGENTS

Citibank, N.A.
New York, New York 10043

Northwestern National Bank
Minneapolis, Minnesota 55480

STOCK TRADING
Common stock (RAI)
New York Stock Exchange
Midwest Stock Exchange
Warrants (RPALW)
Over the Counter market

To our stockholders, employees and friends:

We are pleased to report many achievements for Republic Airlines in 1979. Most notable is the formation of the company by the merger of North Central Airlines and Southern Airways. Here are other highlights:

- Revenues reached a record $609,230,000, a 25 percent increase.
- Earnings totaled $13,061,000, in a year of escalating fuel costs and substantial one-time merger charges.
- Passenger miles were up 14 percent to 3.8 billion. Passengers carried were 12.2 million, a gain of nine percent.
- The system has grown to 38,400 route miles, with service to 158 cities.
- 13 DC-9 jets were added to the fleet.
- $370 million was committed to acquire 32 jet aircraft in a 30-month period through 1981.

Republic became the nation's newest major carrier on July 1, 1979, when the merger took place. It serves more cities—158—than any other airline in the country and flies to 28 states, the District of Columbia, Canada, and the Cayman Islands in the Caribbean.

The complex program for the integration of the operations of the two carriers is progressing well ahead of schedule and will be completed by the third quarter of this year.

In recognition of its accomplishments in 1979, Republic was named "Airline of the Year" by *Air Transport World* magazine, a leading industry publication. The company's management and personnel were cited "for their ability to construct this new carrier to meet the challenges of the '80s, while continuing to fulfill their service obligation" to the many communities on the system. Previous recipients of the award are Swissair, Delta Air Lines, Air France, British Airways, Pan American World Airways, and United Air Lines.

In 1979, Republic carried 12,155,644 passengers. Some 3.8 billion passenger miles and 32.3 million cargo ton miles were flown. The company set a monthly record in August by serving 1,183,202 passengers, and a daily mark on July 9 with 44,149 passengers. To handle this traffic growth, 13 additional DC-9 jets were acquired during 1979.

The $13.1-million profit was realized although expenses included substantial nonrecurring charges related to the merger and an extensive DC-9 inspection required by the Federal government. Earnings per share were $.70 primary, or $.68 fully diluted. The 1979 profit pushed earnings for the last five years to $77 million.

Based on the company's strong financial condition, the Board of Directors declared a cash dividend of $.20 per share payable March 17, 1980 to stockholders of record March 3. Annual cash dividends have been paid for the past eight years.

The airline added nonstop flights in several important markets during 1979: Chicago-Houston, Detroit-Memphis, Atlanta-Washington, D.C., Minneapolis/St. Paul-Washington, D. C., and Twin Cities-Atlanta.

Already in 1980, Republic has inaugurated Twin Cities-Las Vegas, Chicago-Nashville, Birmingham-Tampa/St. Petersburg/Clearwater, and Omaha-Kansas City-Memphis service. On April 1, Milwaukee-St. Louis flights begin. Minneapolis/St. Paul-San Diego and Detroit-New York routes are being introduced April 27.

To undertake this expansion, Republic embarked on a $370-million fleet development program that calls for 120 jet-powered aircraft—one of the ten largest fleets in the world—by the end of 1981. This will include 90 DC-9s, seven Boeing 727-200s, and 23 Convair 580s.

The first of the new Boeing 164-passenger jets was received on February 28, 1980. Two 727s enter scheduled service on April 1, bringing the company's fleet to 107 jet-powered aircraft.

Plans for future growth emphasize additional "bridge routes" between cities presently served by Republic. Passengers from major hubs, and cities beyond, can then reach their destinations on direct flights or with same-carrier connections. This approach greatly improves passenger convenience while increasing the airline's share of the travel market.

Many opportunities lie ahead. The company has the financial strength, efficient aircraft, and skilled personnel so vital to its progress. Republic is confident that 1980—its first full year of operation—will be a solid beginning to a profitable decade.

Sincerely,

Hal N. Carr
Chairman of the Board

Bernard Sweet
President and Chief Executive Officer

March 7, 1980

Republic was named "Airline of the Year" by Air Transport World magazine, a leading industry publication.

Financial review

Republic Airlines earned $13,061,000 in 1979, and revenues reached a record $609,230,000. The company, formed by the merger of North Central Airlines and Southern Airways on July 1, has had earnings of $77 million over the last five years.

Excellent results were achieved through the third quarter of 1979. Heavy demand for special fares, a strike against another carrier, and strong business activity had stimulated travel. In September, traffic began to drop as escalating fuel prices forced up fares and some segments of the economy experienced a slowdown.

Republic's $609 million in revenues showed a 25 percent increase, compared to the $487,565,000 for the combined companies in 1978. Operating expenses, including depreciation and amortization, rose 31 percent to $581,177,000 from $444,756,000.

At the time of the merger, Republic recognized the extended life expectancy of the DC-9 jet aircraft and revised the estimated depreciation, which reduced expenses. However, substantial non-recurring charges related to the merger and an extensive DC-9 inspection required by the Federal government added to expenses. The operating profit was $28,053,000, down 34 percent from the $42,809,000 the previous year.

The acquisition of jet aircraft in 1979 generated considerable investment tax credits. These offset current Federal and State income taxes and some previously deferred taxes, resulting in an income tax credit of $1,750,000 for 1979. The net earnings of $13,061,000 were equal to $.70 per share primary, or $.68 on a fully-diluted basis. A year earlier, the company had income tax expense of $5,464,000 and earned $24,571,000, or $1.42 per share primary, and $1.31 fully diluted.

Stockholders' equity was up 28 percent to a record $145,514,000. Based on 20,620,000 shares of common stock outstanding, book value was $7.06 per share and $6.93 per share in 1978.

Republic now has retained earnings of $93,634,000—more than any other regional airline. The availability of these funds to the company has contributed greatly to the airline's rapid growth.

Expanded operations and inflation pushed up operating expenses 31 percent. Wages, fringe benefits and payroll taxes rose 28 percent to $249,535,000. Interest expense was $26,497,000, as the prime rate reached a record high and the company increased borrowing to finance new aircraft. Jet fuel, which nearly doubled in price, accounted for $132,385,000 of expenses.

The company's five-year traffic and financial data is summarized on Page 31. Supplemental stockholder information, including Quarterly Statements, begins on Page 27.

After concluding an extremely significant year with reasonable earnings, Republic looks ahead to the challenges of the future. With anticipated revenue growth and stringent cost control, the company expects continued profitability in 1980.

MAJOR FACTORS OF CHANGE IN REVENUES AND EXPENSES

The table below summarizes major changes in revenues and expenses which have occurred in Republic's operation over the past two years.

Under operating revenues, traffic gains combined with higher fares generated a $119.6-million increase in passenger revenues. The introduction of new nonstop routes, promotional fares, and additional DC-9 jets contributed to the 21 percent increase in scheduled passenger miles. The average yield per scheduled revenue passenger mile increased 7 percent as a result of fare increases.

Public service revenues rose $9.8 million under a revised formula which compensates the company for providing service to small communities. Of this amount, $3.1 million was retroactive to 1978. (See note I of Notes to Financial Statements.)

Charter activities were greatly curtailed in 1979 because these aircraft were needed for the expansion of scheduled service. While charter revenue declined $9.7 million, freight and mail revenue increased $7.4 million due to increases in rates and aircraft capacity. Other revenues declined $5.4 million.

Operating expenses were up $136.4 million. Labor and employee benefits which rose $53.9 million accounted for 40 percent of the increase. Besides salary and benefit increases in 1979, some 1,300 employees were added. The $52.4 million of additional jet fuel costs represented 38 percent of the increase. Route expansion and higher aircraft utilization increased jet fuel consumption by 22.6 million gallons, and the price of jet fuel nearly doubled to $.76 per gallon by the end of 1979.

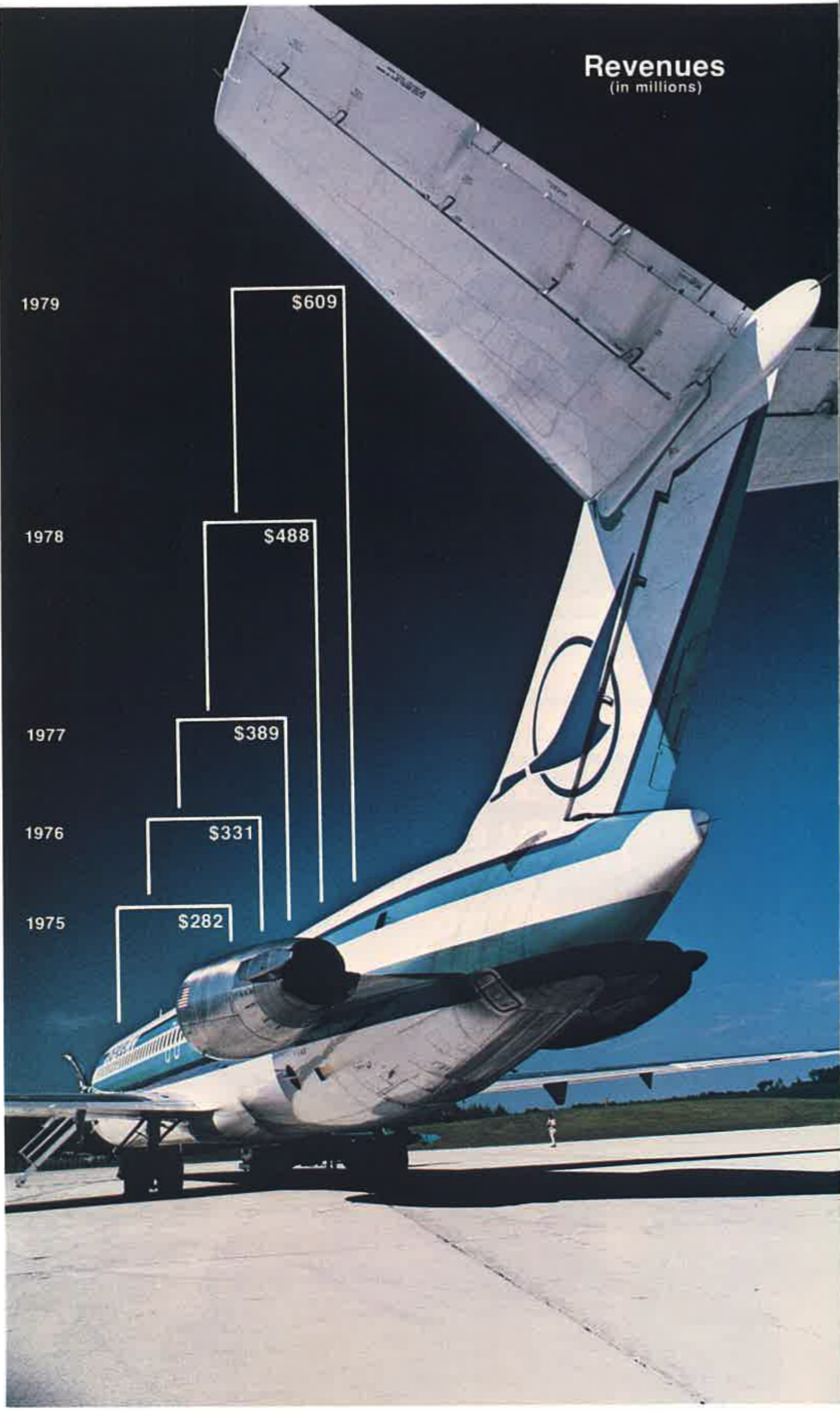
Maintenance parts, supplies and service expense rose $8.2 million due to increased aircraft maintenance, including an extensive DC-9 inspection required by the Federal government. Rent and landing fees rose $4.1 million and outside service expense, $4.9 million. Passenger commission expense was up $6.1 million, reflecting the industry trend of increased travel agency sales. Many other operating costs reflected the expanding operating levels and inflationary pressures.

Included in other expenses (income) is the increase in interest expense of $7.8 million from 1978 to 1979. This relates to the additional borrowing to finance aircraft and the increase in prime interest rates. This was partially offset by a $4.4-million increase in capitalized interest on predelivery deposits for new aircraft. (See notes B and E of Notes to Financial Statements.)

Substantial investment tax credits generated in 1979 from the acquisition of jet aircraft offset both current and previously deferred income taxes, resulting in a tax credit of $1.75 million in 1979 and a reduction of income tax expense of $7.2 million.

The combined effect of these changes was a reduction in net earnings of $11.5 million for 1979.

MAJOR FACTORS OF CHANGE	Net Changes	
	1979-1978	1978-1977
Operating revenues		
Passenger miles	$ 86,600,000	$98,700,000
Passenger fares	33,000,000	(7,900,000)
Public service revenues	9,800,000	(1,800,000)
Cargo and other revenues	(7,700,000)	9,900,000
Net revenue changes	121,700,000	98,900,000
Operating expenses		
Labor and employee benefits	53,900,000	34,800,000
Cost of jet fuel	52,400,000	13,900,000
Other operating expenses	30,100,000	35,200,000
Net expense changes	136,400,000	83,900,000
Changes in operating profit	(14,700,000)	15,000,000
Other expenses (income)	4,000,000	10,900,000
Income taxes	(7,200,000)	2,600,000
Changes in net earnings	$(11,500,000)	$ 1,500,000



Traffic growth and performance

In 1979, Republic Airlines carried 12,155,644 passengers over 3.8 billion passenger miles, and flew 32.3 million cargo ton miles in 1979. Passenger boardings were up nine percent; passenger miles, 14 percent; and cargo ton miles, 15 percent.

These increases are attributable to the benefits derived from merging the northern and southern route systems, introduction of new service, increased capacity from new DC-9-50 jets, and the high demand for special fares.

The 1,183,202 passengers carried in August 1979 set a monthly record. On July 9, a daily high was achieved when the airline boarded 44,149 passengers.

In addition to scheduled service, Republic flew 124,924 passengers on charter trips during 1979. These operated to 31 states, plus such diverse points as Montego Bay and Nassau in the Caribbean, and Ottawa and Yellowknife in Canada. During peak travel periods, 312 extra sections of scheduled flights carried 79,479 travelers.

Passenger gains were substantial for the first eight months of 1979. By September, constantly rising fuel costs brought on fare increases which adversely affected leisure travel. Business traffic also slipped as some industries felt the effects of inflation and the sluggish national economy.

Cargo sustained its upward trend in 1979. The 32,324,000 cargo ton miles flown—including freight, express and mail—were 15 percent ahead of 1978. Freight and express ton miles rose 10 percent, while mail ton miles were up 28 percent.

Popularity of the airline's VIP small package service grew as volume climbed 27 percent over 1978. The expedited handling afforded by VIP, which can include pickup and delivery, has proven valuable for shippers of medical supplies, documents, news films, electronic data processing equipment, and machine parts. More than 170,000 VIP parcels were shipped in 1979.

Republic has established high goals for flight completion and on-time performance. During 1979, the airline flew 79,305,000 of its 82,656,000 scheduled miles for a completion factor of 96 percent. This is somewhat below the operating records established in previous years due primarily to a special government-directed inspection affecting DC-9 aircraft, together with unusually severe weather in the early part of the year.

The performance record reflects the work of everyone involved with day-to-day operations, and Republic is determined to maintain its position as an industry leader in providing dependable scheduled air service.

The company has new facilities at the Sarasota/Bradenton terminal which opened in December 1979. Passenger Service Agents Mary Jansen and Ron Bishop check in passengers at the counter.

The first Boeing 727-200 jets in Republic colors enter scheduled service on April 1. The 164-passenger 727s are part of the company's fleet development program involving the acquisition of 32 jet aircraft in a 30-month period.

Fleet development

At the time of the merger on July 1, 1979, Republic's fleet consisted of 68 DC-9s, 23 Convair 580s and eight Swearingen Metro IIs—a total of 99 aircraft. The company then embarked on an extensive fleet development program which involved the acquisition of 32 additional jets within a 30-month period.

The airline is purchasing the Boeing 727 for the first time, and seven have been ordered. The other 25 aircraft are Douglas DC-9 jets. Republic has committed $370 million to this aircraft program.

Fifteen of the DC-9 jets are already delivered, and two will arrive later in 1980. The first 727 was delivered in February 1980, and another is coming in March. Both of the new 164-passenger tri-jets enter scheduled service on April 1, 1980. Two more 727s are due by September.

In 1981, Republic will be introducing the DC-9-80, the quietest and most fuel-efficient jet on the market today. Eight are on order, and all are to be delivered next year. Also, three Boeing 727s arrive in March 1981.

Republic's fleet, which already ranks as one of the ten largest in the world, is projected to include 120 aircraft by the end of 1981—seven 727s, 90 DC-9s and 23 Convair 580s.

The new aircraft have greatly improved existing service and also enabled the company to add new routes. Because the 727s use the same basic Pratt & Whitney jet engine as the DC-9s, no major changes have been required for maintenance purposes.

The progressive modular maintenance system developed by the company has been studied and adopted by many airlines around the world. Republic does virtually all of its own maintenance work, thereby reducing dependence on vendors to meet quality standards. To assure operating reliability and performance, the company employs over 1,200 licensed and highly trained mechanics and technicians.

The program to install wide-body interiors on earlier DC-9 jets is well underway. Enclosed overhead luggage compartments and improved lighting provide passenger benefits. Bright side panels and a new decor give the aircraft a more spacious look. The changeover is to be completed in 1980.

Supplemental fuel tanks have been installed in some DC-9-30s, giving them longer-range capability, which is also useful for charters. Several new DC-9-50s are equipped with auxiliary fuel tanks. Because the 727s have three engines, they can travel farther and perform well at high-altitude airports.

This comprehensive fleet development program assures that Republic will have dependable, versatile, and efficient equipment to serve the public, while earning a reasonable profit for the company.

New facilities and services

Republic Airlines takes pride in carrying on a tradition of high service standards. Working in cooperation with civic leaders, the airline made numerous improvements in facilities throughout its system in 1979.

New terminal buildings were completed at International Falls, Rhinelander/Land O'Lakes, Hibbing/Chisholm, Sarasota/Bradenton, and Huron. Construction was begun on an addition to the terminal at Minneapolis/St. Paul. Republic will transfer its operation to the new Green Concourse and occupy ten gates. The Concourse, which was extended 800 feet, is scheduled for occupancy April 1. At Hartsfield Atlanta International Airport, a completely new terminal is being built, a third main runway added, and a modern people-moving system installed. Republic will move into Airside D on September 1.

Terminals were remodeled at Bismarck/Mandan, Devils Lake, Kalamazoo/Battle Creek, and Memphis.

New enlarged space was secured for passenger service at airport facilities in Chattanooga, Meridian and New York La Guardia. At Madison, Republic is the first airline to provide a gate area passenger lounge. The company has new information centers at Chicago O'Hare and Memphis, and has added a new passenger service counter and station facilities in the Tucson terminal. Baggage facilities were improved at Iron Mountain/Kingsford, Memphis, Eglin AFB, Jackson (MS) and Chicago.

Cargo operations, a substantial revenue-producer for Republic, also required expanded quarters. Construction has begun on a new cargo building in Birmingham. At Huntsville/Decatur, Republic has acquired a larger cargo area. New cargo facilities are planned for St. Louis, Memphis and Tallahassee.

Several changes were made to accommodate new or additional jet service. All gates at Detroit now have jet bridges, and new jetways were installed at Eglin AFB, Fargo/Moorhead, International Falls and Hibbing/Chisholm.

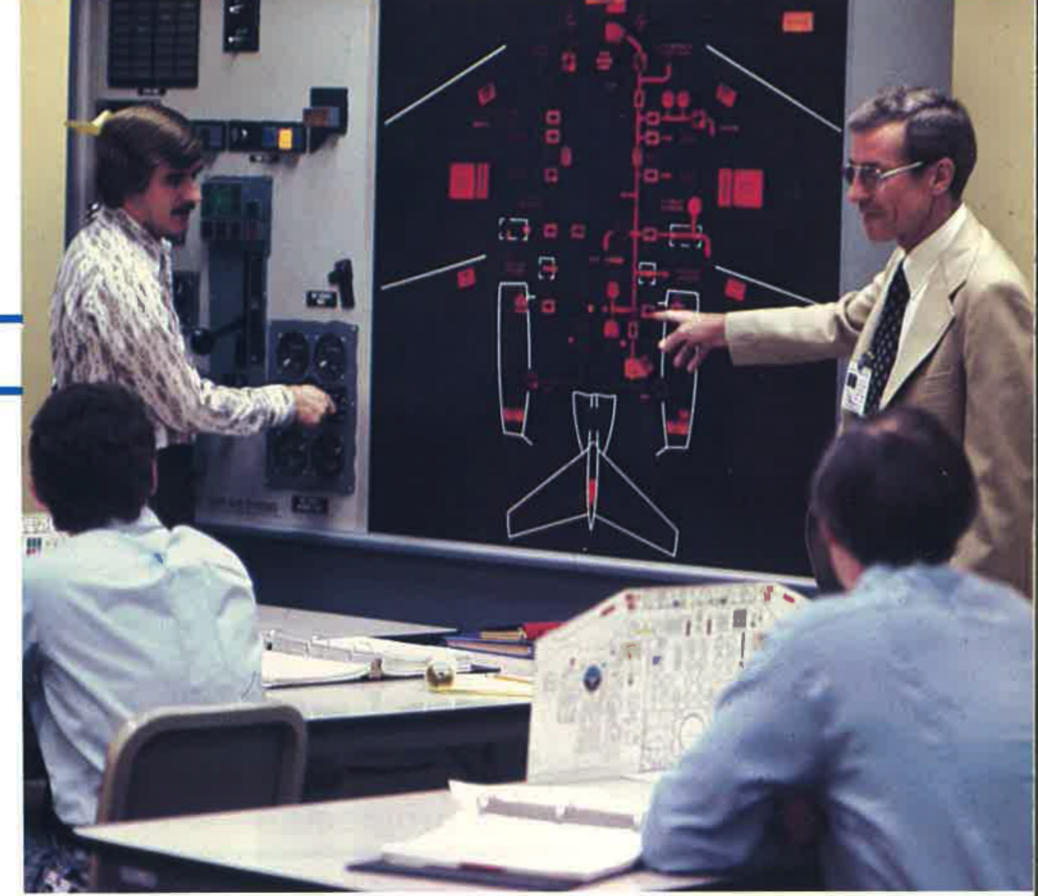
Improved passenger security and convenient screening resulted from the installation of x-ray units for carry-on luggage inspection at Kalamazoo/Battle Creek, Traverse City and Wausau/Stevens Point. New walk-through metal detectors were added in Greenville (SC)/Spartanburg, Minneapolis/St. Paul, Milwaukee, Green Bay/Clintonville, and New Orleans.

The company's three Reservations Centers—Minneapolis, Atlanta and Detroit—were substantially expanded. The airline hired over 100 reservations agents, bringing total personnel in this department to nearly 900. By year-end, the reservations staff was answering more than 275,000 calls a week. ESCORT, the company's computerized reservations system, automatically prints and prices a greater variety of tickets and itineraries. Improved computer processing of bookings from other airlines resulted in 180,000 fewer messages to be entered manually—freeing agents to answer more telephone calls.

Two new IBM Central Processing Units were acquired in 1979 to handle the company's volume of passenger reservations. One is the prime ESCORT computer, and the other is the "backup" computer usable for ESCORT and SCEPTRE, Republic's maintenance and corporate data system. This represents $6 million of equipment. The SCEPTRE program includes on-line tracking of all major aircraft parts for maintenance and repair. Several other airlines have purchased this program. Revenues received from the sale of computer time and software programs totaled $750,000 in 1979.

Customer Service Representatives are now assigned to Republic's Flight Control Center. When weather and other factors cause irregular operations, these representatives provide flight superintendents with information relating to passenger service. They determine the number of connecting passengers, the passenger inconvenience involved with special stops or overflights, and the need for extra sections. They also arrange for alternate forms of transportation and estimate loss of passengers due to flight delays. Flight control decisions are first based on safety. Then passenger convenience is considered, and finally economic impact.

The Green Concourse at the Minneapolis-St. Paul International Airport has been substantially expanded. Republic will occupy 10 gates, with new areas for passenger service and ground operations.



The increased needs of the expanded airline required many changes in administration facilities. At the company's Minneapolis/St. Paul headquarters, the lower level was transformed from storage space into offices and classrooms. The Flight Crew Training Department was moved to Atlanta to make full use of the excellent facilities there and the area's more moderate climate. Various functions, such as baggage claim service and cargo accounting, have been consolidated at one location.

The company is continually evaluating its facilities so improvements and additions can be made on a timely basis to meet the airline's changing needs.

The Flight Crew Training Center is located in Atlanta where the climate is moderate and the company has excellent facilities. Instructor William McCarty explains DC-9 hydraulic systems to First Officer Elwyn Gaissert and other pilots.

The company's employment practices follow Affirmative Action guidelines approved by the Federal Aviation Administration. Republic hired over 1,300 new employees in 1979. Many are among the nearly 900 people who handle 275,000 calls a week at Reservations Centers in Detroit (right), Atlanta and Minneapolis/ St. Paul. (Shown are Elizabeth Hockney and William Plumb.)

Social and environmental programs

Republic Airlines is firmly committed to fulfilling its obligations as a responsible corporate citizen. Through fuel conservation, noise abatement, safety, educational assistance and extensive employee programs, the company is directly involved with the diversified needs of a complex society.

Employees are the airline's greatest resource. Republic has 9,000 people, most of them with proven technical skills and many years of experience in the airline industry. About 1,300 new employees were selected in 1979 from over 100,000 applicants. Affirmative action guidelines, reviewed and approved by the Federal Aviation Administration (FAA), are followed in the hiring process.

Republic provides many outstanding benefit programs for its employees, including group life insurance, medical coverage, and pensions. Specialized programs are offered, such as the Idea Dollars suggestion system, management training, care for chemical dependency, and educational assistance.

Safety, always a prime concern to the company, was emphasized by each division. Corporate safety committees coordinate programs and respond to Federal regulations by developing new plans. For example, the airline's hazardous materials training was expanded, after approval by the FAA. Flight crews, flight superintendents, stock clerks, passenger service agents and station agents received this specialized training.

Environmental matters are also of great importance to the airline's operation. Republic's extensive route system covers 28 states, the District of Columbia, two Canadian provinces and the Cayman Islands in the Caribbean.

The company has been very active in programs to reduce aircraft noise and its effect on communities the airline serves. Substantial effort is being devoted to noise studies and environmental impact statements. Frequent meetings are held with local airport noise and environmental groups to advise them of Republic's operational policies and to keep informed on the communities' views.

The Flight Operations Division, which coordinates this activity, also works with FAA air traffic controllers to divert aircraft noise to less-populated areas–by designating certain runways for takeoff and special flight paths for landing aircraft. Republic was a leader in the development of the new noise-abatement takeoff and landing procedures adopted by the FAA as the standard for all airlines.

Over the next several years, the company will be replacing many of the smaller DC-9 jets with the much quieter DC-9-80s.

The airline's weather reporting system was enlarged in 1979 to provide weather data for 1,500 cities. Flight crews, flight superintendents, station agents, and passenger service agents now have access to this additional information and other improvements which upgrade the flexibility and reliability of weather data processing.

Fuel conservation measures also apply to ground facilities. In the company's headquarters, for example, equipment which reclaims heat generated by computer equipment was installed during a recent remodeling program. The entire cost of the system will be realized in about three years with energy savings at 1979 prices.

Republic believes that prudent use of resources and concern for the environment are vital to the company's progress.

Jet fuel outlook

Of critical concern to Republic is the jet fuel supply situation and escalating costs. During 1979, the company had to intensify fuel conservation measures and locate new sources of supply. Although prices rose significantly throughout the year, related fare increases lagged several months behind.

As the supply of crude oil and imported products decreased, less jet fuel was available, and contract suppliers cut their allocations to the airlines. Republic then had to buy some of its jet fuel in the retail "spot market" where a minimum purchase is usually a million gallons, and the price is considerably higher than contract fuel. About 13 percent is now acquired in this manner. The average price per gallon in December 1979 was 76 cents, nearly double the 40 cents in December 1978.

To fly the present 20.5 million seat miles a day, Republic jets require 650,800 gallons of fuel, or 31.5 seat miles per gallon. To meet that need, Republic purchases contract jet fuel at 79 locations throughout the system under 95 individual allocations from many different vendors. At one city, fuel is supplied by five companies.

Republic and other carriers in the industry have continued to make significant progress in fuel conservation. These concerted efforts began in 1973 during the initial fuel crisis. According to the Air Transport Association, airline traffic has increased nearly 50 percent in this period, but fuel use is up only five percent.

To reduce its fuel consumption and increase operating efficiency, Republic made further refinements in aircraft operating procedures and routings. In addition, lighter-weight seats are being used, and passenger capacity has been increased on some DC-9s. The airline is also benefiting from the latest technological developments as new DC-9-50 and Boeing 727 jet aircraft are delivered.

Republic keeps accurate detailed information on fuel in its computerized Fuel Inventory Management System (FIMS). This provides data for long-range planning and the day-to-day operation. Recent improvements permit even greater flexibility in reporting.

The company also has computerized information allowing Flight Control to calculate fuel requirements by flight segments. This is "tailored" to the aircraft's type of engine, fuel capacity and seating configuration. Knowing the fuel needed and the inventory at refueling stations, planners can better utilize the supply.

To insure jet fuel availability in the future, the company is pursuing several courses. Direct purchases are being made from a greater number of independent refineries, which usually limit delivery to nearby locations. The company is considering purchase of producing oil wells, financing of independent oil exploration, or acquiring an interest in a refinery–through partial ownership or by underwriting conversion costs to produce jet fuel.

Flight Attendants June Haugen (right) and Kathy Collias serve passengers in flight. Since 1973, U.S. airline passenger traffic has increased nearly 50 percent, but fuel consumption is up only five percent. Republic and other airlines are continuing to make more efficient use of jet fuel.

Communications

A highly effective communications program was carried out in 1979. Public awareness of Republic Airlines was assured through well-researched marketing and advertising activities, and employees were kept informed of company developments.

The advertising campaign introducing Republic was launched on June 28, 1979. Ads ran in 172 newspapers and 25 magazines, and on 124 radio stations and 109 television stations across the nation.

The approach—emphasizing the merger of two established carriers—was chosen. Research had indicated that the public placed confidence in a large airline with experience. For authenticity, visual ads featured Republic employees. One of the country's top commercial musicians wrote original music for radio and TV spots. The "Americana" style was selected to represent the transcontinental scope of Republic.

A nationally-known testing service reported that Republic's TV commercials demonstrated "outstanding performance in attracting viewer attention." Another research firm learned that 93 percent of the people surveyed knew of Republic Airlines. They concluded that "Awareness of advertising, on an unaided basis, placed Republic and one other airline at the top of the industry."

Public relations activities were coordinated with the advertising effort. About 2,000 press kits containing news items, feature material and photographs were distributed to national and regional publications. Television and radio stations also received taped presentations on the new company.

The visual aspects of the change to Republic started on July 1 and were completed in a few days. Temporary signs were put on equipment and facilities until overall design standards could be implemented. To reduce expenses, major changes at some places were delayed to coincide with planned remodeling or relocation.

Corporate design standards apply to aircraft, ground support equipment, buildings, billboards, printed materials, uniforms and all other items viewed by the public.

To support the advertising and publicity activities, the sales staff made over 48,000 calls on travel agencies and key industrial accounts. Unique mailings also kept them informed of merger developments and offered special information and assistance. Officers, station managers and other employees participated in 1,450 civic events.

More than 7,000 visitors received guided tours of Republic's headquarters in Minneapolis/St. Paul. Another 10,700 guests attended public functions held in the employee cafeteria.

The airline's inflight magazine was expanded and renamed *Republic Scene*. Each issue of the monthly publication carries one story about the company, along with numerous other articles of general interest.

Presentations for employees were made at major cities, prior to the July 1 merger, with corporate officers available to answer questions. Teletype messages, letters, special mailings and a toll-free telephone line kept communications open.

A monthly newspaper for employees, *Republic People*, was introduced after the merger, and also a weekly newsletter entitled *Extra Section*. A feedback program, "Direct Approach," permits employees to phone or write directly to the general office with any comments or questions.

Through the successful communications efforts of the company, employees and the public are well aware of the identity and progress of Republic Airlines.

Employees were featured in advertising announcing the formation of Republic Airlines. A comprehensive program emphasized that the name was new, but the company was a combination of two experienced airlines.

Route development

Primary factors affecting the company's route development in 1979 were the merger which formed Republic and the Airline Deregulation Act of 1978.

With the merger on July 1, 1979, a unique aviation network resulted. Virtually every major city in the Upper Midwest was linked with similar metropolitan communities in the Southeast, so travelers could move between the two areas without changing airlines. Therefore, the company's route development program in 1979 focused on securing nonstop "bridge routes" connecting the two geographic regions.

On October 28, Republic began to integrate flight schedules between the northern and southern route systems. This provided more single-plane service, better connections, and additional capacity. Also, nonstop service was inaugurated between Minneapolis/St. Paul and Atlanta.

These changes benefited southern passengers traveling to hubs such as Minneapolis/St. Paul, Detroit and Toronto, while people in the northern states had improved service to Atlanta, Memphis and New Orleans.

In subsequent months, more refinements were made to schedules. On March 1, 1980, new service was introduced: Chicago-Nashville, Omaha-Kansas City-Memphis, and Birmingham-Tampa/St. Petersburg/Clearwater. On April 1, Milwaukee-St. Louis service begins. As demand grows and markets develop, more bridge routes will be added.

By improving connections from intermediate-sized cities to major hub areas, Republic makes travel more convenient for passengers and carries them farther. This approach increases revenues, while reducing passenger-handling costs.

As a result of the Airline Deregulation Act, significant expansion occurred. Early in 1979, service was inaugurated on the Chicago-Houston, Detroit-Memphis, and Atlanta-Washington, D.C. routes. Later in the year, the Civil Aeronautics Board began granting route authority to any "willing and able" applicant. Republic used this expedited procedure to connect Minneapolis/St. Paul with Washington, D.C.

Two long-standing route applications were favorably concluded in recent months. The first authorized Twin Cities-Las Vegas nonstops, and flights began January 15, 1980. The other application involves Minneapolis/St. Paul-San Diego service, and this is scheduled to start April 27. Local environmental studies delayed entry into San Diego.

Additional changes on April 27 primarily affect the Michigan area. Republic is scheduling Detroit-New York City nonstops and increased service connecting Grand Rapids, Lansing and Saginaw/Bay City/Midland with Detroit and Chicago. The airline has served these cities for nearly 20 years.

By actively participating in CAB route cases, Republic has been awarded a great number of routes in the United States and also authority to overseas points. With this potential and Republic's strong financial resources, new markets will be carefully selected to assure improved passenger service and productive, stable growth.

Las Vegas is the most recent addition to Republic's system. Convenient nonstop flights connect the famous vacation area with Minneapolis and St. Paul.

New Chicago-Nashville nonstop flights began March 1, 1980. Republic Skycap Stanley Seals offers "curbside" baggage check-in at Nashville.

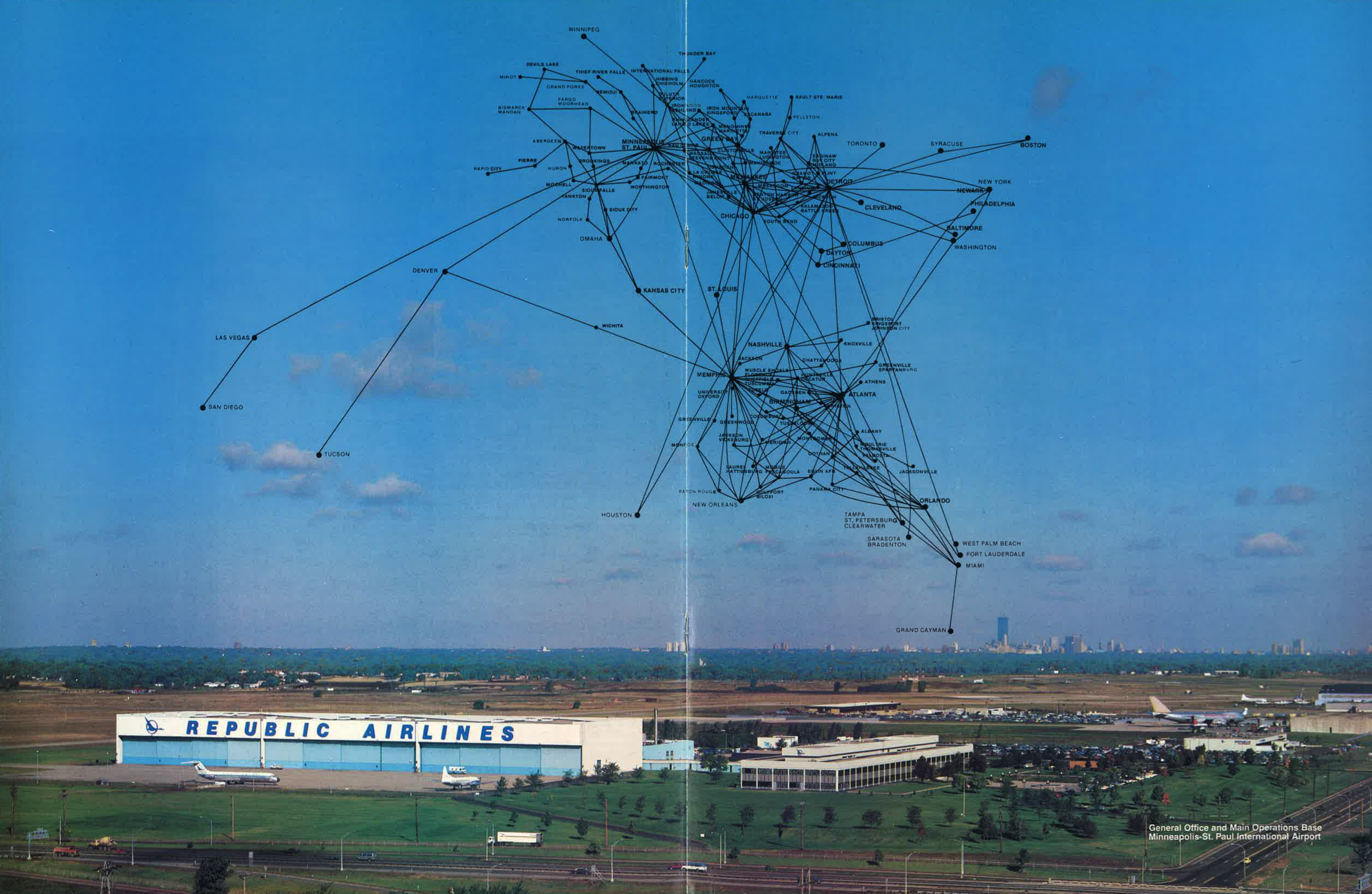
The future

The full impact of deregulation in the airline industry is still unclear, and fuel continues to be a major concern. However, Republic is expecting continued growth in the months ahead.

The company will concentrate on developing markets within its system. This approach is the most economical way to accomplish expansion because facilities and staffing are established. Nonstop service between cities Republic is already serving will be vigorously promoted. When new destinations are added, they will be lucrative, long-haul routes.

As the nation's economy regains momentum, business and leisure travel should stabilize and gradually increase. Demand for seats and cargo space will push 1980 revenues close to a billion dollars, while cost control programs hold down expenses.

The airline has virtually unlimited potential in the decade of the '80s, and "the people" of Republic are confident the company will be a strong, profitable carrier.



General Office and Main Operations Base
Minneapolis-St. Paul International Airport

REPUBLIC AIRLINES, INC.

Balance sheets

	December 31 1979	December 31 1978
ASSETS		
CURRENT ASSETS		
Cash and short-term investments (note C)	$ 13,178,000	$ 33,399,000
Accounts receivable, less allowances	84,820,000	46,232,000
Flight equipment parts and supplies (notes A and C)	30,771,000	16,223,000
Prepaid expenses and other (note A)	15,922,000	11,910,000
	144,691,000	107,764,000
PROPERTY AND EQUIPMENT—at cost (notes A, C, D, E and I)		
Flight equipment	436,734,000	344,184,000
Ground property and equipment	74,177,000	63,296,000
	510,911,000	407,480,000
Less accumulated depreciation and amortization	146,554,000	125,450,000
	364,357,000	282,030,000
Advance payments on equipment	35,275,000	32,024,000
	399,632,000	314,054,000
DEFERRED CHARGES AND OTHER ASSETS	5,058,000	6,606,000
	$549,381,000	$428,424,000
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Current maturities of long-term debt (note C)	$ 18,219,000	$ 24,157,000
Accounts and notes payable (note C)	40,183,000	25,731,000
Interline payables and tickets outstanding (note A)	37,918,000	27,797,000
Accrued compensation and other expenses	39,390,000	29,925,000
Income taxes (notes A and F)	520,000	3,061,000
	136,230,000	110,671,000
LONG-TERM OBLIGATIONS		
Long-term debt—less current maturities (note C)	263,035,000	196,637,000
Deferred income taxes and other (notes A and F)	4,602,000	7,828,000
	267,637,000	204,465,000
COMMITMENTS (notes D and E)	–	–
STOCKHOLDERS' EQUITY (notes C, G and H)		
Common stock—authorized 30,000,000 shares of $.20 par value	4,151,000	3,297,000
Additional paid-in capital	48,109,000	27,321,000
Retained earnings	93,634,000	83,050,000
Treasury stock—at cost	(380,000)	(380,000)
	145,514,000	113,288,000
	$549,381,000	$428,424,000

The accompanying notes are an integral part of these statements.

Statements of earnings

	Year ended December 31 1979	Year ended December 31 1978
OPERATING REVENUES		
Passenger (note A)	$527,792,000	$408,243,000
Freight and mail	41,510,000	34,062,000
Public service revenues (note I)	26,362,000	16,523,000
Non-scheduled service and other	13,566,000	28,737,000
	609,230,000	487,565,000
OPERATING EXPENSES		
Flying operations	211,260,000	144,106,000
Maintenance	70,436,000	54,774,000
Aircraft and traffic servicing	128,059,000	103,789,000
Passenger service	43,782,000	30,467,000
Reservations, advertising and sales	66,300,000	46,093,000
General and administrative	28,054,000	24,468,000
Other transport-related expenses	3,846,000	11,806,000
Depreciation and amortization (notes A and I)	29,440,000	29,253,000
	581,177,000	444,756,000
Operating profit	28,053,000	42,809,000
OTHER EXPENSES (INCOME)		
Interest expense	26,497,000	18,688,000
Less interest capitalized (notes A and B)	6,375,000	2,015,000
	20,122,000	16,673,000
Interest income and other—net	(1,378,000)	(2,593,000)
Gain on disposition of equipment	(2,002,000)	(1,306,000)
	16,742,000	12,774,000
Earnings before income taxes	11,311,000	30,035,000
INCOME TAXES (notes A and F)		
Current	706,000	2,724,000
Deferred	(2,456,000)	2,740,000
	(1,750,000)	5,464,000
NET EARNINGS	$ 13,061,000	$ 24,571,000
NET EARNINGS PER SHARE (note K)		
Primary	$ .70	$1.42
Fully diluted	$ .68	$1.31

The accompanying notes are an integral part of these statements.

Statements of changes in financial position

SOURCES AND APPLICATIONS OF WORKING CAPITAL	Year ended December 31 1979	1978
SOURCES		
From operations		
Net earnings	$ 13,061,000	$ 24,571,000
Charges (credits) to earnings not using (providing) working capital		
Depreciation and amortization	29,440,000	29,253,000
Deferred income taxes	(2,220,000)	2,714,000
Other	1,436,000	1,268,000
Working capital provided from operations	41,717,000	57,806,000
Net book value of equipment dispositions	2,159,000	7,018,000
Increase in long-term debt	187,797,000	105,998,000
Conversion of debentures to common stock	7,864,000	1,031,000
Options and warrants exercised	13,490,000	462,000
Other	328,000	429,000
	253,355,000	172,744,000
APPLICATIONS		
Additions to property and equipment	116,857,000	114,207,000
Reduction of long-term debt	113,449,000	50,958,000
Conversion of debentures to common stock	7,864,000	1,031,000
Payment of cash dividend	2,477,000	2,014,000
Additions to deferred charges and other assets	1,340,000	2,896,000
	241,987,000	171,106,000
INCREASE IN WORKING CAPITAL	11,368,000	1,638,000
Working capital (deficit) at beginning of year	(2,907,000)	(4,545,000)
Working capital (deficit) at end of year	$ 8,461,000	$ (2,907,000)

NET CHANGE IN WORKING CAPITAL ELEMENTS		
Increase (decrease) in current assets		
Cash and short-term investments	$ (20,221,000)	$ 10,151,000
Accounts receivable	38,588,000	3,875,000
Flight equipment parts and supplies	14,548,000	3,231,000
Prepaid expenses and other	4,012,000	1,419,000
Net change in current assets	36,927,000	18,676,000
Increase (decrease) in current liabilities		
Current maturities of long-term debt	(5,938,000)	(5,868,000)
Accounts and notes payable	14,452,000	9,073,000
Interline payables and tickets outstanding	10,121,000	6,128,000
Accrued compensation and other expenses	9,465,000	7,039,000
Income taxes	(2,541,000)	666,000
Net change in current liabilities	25,559,000	17,038,000
INCREASE IN WORKING CAPITAL	$ 11,368,000	$ 1,638,000

The accompanying notes are an integral part of these statements.

Statements of changes in stockholders' equity

Years ended December 31, 1979 and 1978

	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Stock	
	Shares Issued	Amount			Shares Held	Amount
Balance at January 1, 1978	16,117,191	$3,223,000	$25,902,000	$60,493,000	134,594	$380,000
Cash dividend (note G)	–	–	–	(2,014,000)	–	–
Exercise of stock options (note G)	38,798	8,000	104,000	–	–	–
Exercise of warrants (note G)	113,748	23,000	327,000	–	–	–
Conversion of debentures (note C)	213,093	43,000	988,000	–	–	–
Net earnings for 1978	–	–	–	24,571,000	–	–
Balance at December 31, 1978	16,482,830	3,297,000	27,321,000	83,050,000	134,594	380,000
Cash dividend (note G)	–	–	–	(2,477,000)	–	–
Exercise of stock options (note G)	89,150	18,000	218,000	–	–	–
Exercise of warrants (note G)	2,561,323	512,000	13,030,000	–	–	–
Conversion of debentures (note C)	1,621,013	324,000	7,540,000	–	–	–
Net earnings for 1979	–	–	–	13,061,000	–	–
Balance at December 31, 1979	20,754,316	$4,151,000	$48,109,000	$93,634,000	134,594	$380,000

The accompanying notes are an integral part of these statements.

Auditors' report

Alexander Grant
& COMPANY
CERTIFIED PUBLIC ACCOUNTANTS

INTERNATIONAL FIRM
ALEXANDER GRANT TANSLEY WITT

Stockholders and Board of Directors
Republic Airlines, Inc.

We have examined the balance sheets of Republic Airlines, Inc. (a Wisconsin corporation) as of December 31, 1979 and 1978, and the related statements of earnings, changes in stockholders' equity and changes in financial position for the years then ended. Our examinations were 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 Republic Airlines, Inc., at December 31, 1979 and 1978, 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 except for the change, with which we concur, in the method of capitalizing interest as discussed in note B to the financial statements.

Alexander Grant & Company

Minneapolis, Minnesota
February 25, 1980

Notes to financial statements

December 31, 1979 and 1978

Note A—Summary of Significant Accounting Policies— The company, as a regional airline providing scheduled service for passengers, mail and property, is regulated by the Civil Aeronautics Board (CAB) and uses the Uniform System of Accounts and Reports for Certificated Air Carriers as required by the CAB. The significant policies followed by the company are:

Flight Equipment Parts and Supplies: These are priced at average cost. An allowance for obsolescence ($2,970,000 in 1979 and $2,464,000 in 1978) is provided for repairable parts by allocating their cost over the life of the related aircraft.

Prepaid Expenses—Engine Overhaul: The company reclassifies to a current prepaid expense the estimated portion of the purchase price of flight equipment attributable to its overhaul expected to be consumed within the next twelve months ($10,303,000 in 1979 and $8,515,000 in 1978). Actual overhaul costs are charged to expense as incurred.

Capitalized Interest: To properly reflect their total cost, major additions to flight equipment and ground facilities include capitalized interest based on the interest rate of the related debt outstanding. The capitalized interest is amortized over the useful lives of the related assets for financial reporting purposes. For income tax reporting purposes, interest is expensed as incurred (note B).

Property, Equipment and Depreciation: Owned property and equipment are stated at cost. Property and equipment acquired under capital leases are stated at the lower of the present value of minimum lease payments or fair market value at the inception of the lease. Depreciation and amortization of property and equipment are provided on a straight-line basis over estimated useful lives of 7-18 years for flight equipment and 7-10 years for other property and equipment.

Deferred Charges: Significant costs, such as major computer software development, traffic promotion related to the inauguration of service over major new routes, and personnel training relating to the introduction of new types of aircraft are deferred and amortized over periods of up to five years.

Passenger Revenues: Passenger revenue is recognized when the transportation service is provided. Unused ticket sales are included as a current liability.

Pension Costs: The company has pension plans for substantially all of its employees, and funds its current expense of normal costs. Prior service costs are amortized over 40 years. Pension funding is determined under the unit credit and aggregate frozen liability methods (note J).

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. Investment credits not applied currently are offset against deferred income taxes to the extent they are applicable to previously deferred taxes becoming payable in the carry-over periods. The company recognizes deferred income taxes resulting from differences in financial and income tax reporting (note F).

Note B—Change in Accounting Method—In the fourth quarter of 1979, the company changed its method of computing capitalized interest to conform with the requirements of Financial Accounting Standards Board Statement No. 34. The company previously capitalized interest based on the weighted average interest rate of debt outstanding. The effect of the change was to increase capitalized interest recognized in 1979 by $895,000 and increase net income by $806,000 ($.04 per share primary and fully diluted). The impact on the unaudited quarterly results of operations for the three prior quarters in 1979 was immaterial and therefore the quarterly financial information has not been restated.

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

	1979	1978
Revolving credit agreement (a)	$103,382,000	$ –
Quarterly installment notes due in 1984 (a)	–	73,335,000
Notes payable to banks under a Credit agreement (a)	–	16,807,000
Quarterly installment notes due in 1987 (b)	35,279,000	46,284,000
Equipment Trust Certificates (c)	43,500,000	45,000,000
Capital lease obligations (d)	84,291,000	18,117,000
Convertible subordinated debentures (e):		
5¾% due December 1, 1981	–	3,016,000
6½% due November 1, 1983	–	5,047,000
Sundry (f)	14,802,000	13,188,000
Total long-term debt (g)	281,254,000	220,794,000
Less current maturities (h)	18,219,000	24,157,000
	$263,035,000	$196,637,000

(a) On October 1, 1979, the company refinanced quarterly installment notes due in 1984 and notes payable to banks under a credit agreement into a Revolving credit agreement. Under this agreement, the company may borrow up to a maximum of $150,000,000 until December 1980, when it will be converted into a term loan. Proceeds from this agreement were used to refinance a portion of existing debt and will be used to finance a portion of the purchase price of four new B-727-200 aircraft scheduled for delivery in 1980. The loan will be payable in twenty-eight quarterly installments of approximately $5,357,000 beginning November 1981 through August 1988. Interest is to be paid at each of the participating banks' prime rate plus percentages ranging from ¼% to ½% over prime. Effective rates at December 31, 1979 were 15% to 15½%.

(b) Consists of various installment notes with due dates from 1986 through 1987 at interest rates ranging from 8¼% (for notes 90% guaranteed by the Federal Aviation Administration) to ¾% over the lending bank's prime rate. Effective rate at December 31, 1979 was 15%. The aggregate quarterly installment payments are approximately $1,734,000 including interest.

(c) The Equipment Trust Certificates require semi-annual sinking fund payments of $750,000 in 1980, $2,250,000 in 1981 and 1982, $1,575,000 from 1983 through 1992 and $1,500,000 at maturity in May 1993, plus interest at 9%. The company may make semi-annual optional sinking fund payments beginning in May 1983 up to $1,575,000 and may pay off the remaining balance in full on or after May 1, 1988 at a premium.

(d) In the first half of 1979, the company took delivery of three DC-9-50 aircraft under a capital lease agreement. The debt obligation relating to the capitalization of this lease was $25,000,000 at December 31, 1979. The obligation is payable in semi-annual installments of $1,354,000 through January 1997, including interest at 8⅛%. During the fourth quarter of 1979, the company took delivery of four additional DC-9-50 aircraft under a capital lease agreement. The debt obligation relating to the capitalization of this lease was $39,446,000 at December 31, 1979. The obligation is payable in quarterly installments of $1,030,000 through April 1998, including interest at 8⅜% (note D).

In December 1979, the company took delivery of two used DC-9-10 aircraft under a capital lease agreement. The debt obligation relating to the capitalization of this lease was $4,298,000 at December 31, 1979. The obligation is payable in quarterly installments of approximately $233,000 through December 1986, including interest at 12½%.

(e) All 5¾% and 6½% debentures were converted or redeemed during 1979.

(f) Includes $5,717,000 of promissory notes with interest at 1.25 times prime. Effective rate at December 31, 1979 was approximately 19%. These notes were issued in place of deposits and are due at delivery of four DC-9-50 aircraft in 1980 (note E).

(g) Substantially all the flight equipment and spare parts owned and leased by the company are pledged as collateral against the above debt. Among the loan covenants are requirements for the maintenance of tangible net worth and coverage of fixed charges. At December 31, 1979 the company was in compliance with those restrictive covenants.

The company is required to maintain average compensating balances ranging from 5% to 15% of the quarterly average loan outstanding or commitment and is required to pay interest ranging from ¼% to ½% over prime on any average compensating balance shortfall. During 1979 the company was required to maintain average compensating balances of $8,916,000. At December 31, 1979, the required compensating balances (adjusted for float) were approximately $6,764,000.

(h) Current maturities of all long-term debt obligations due in each of the next five years following December 31, 1979 are as follows:

1980	$18,219,000
1981	30,135,000
1982	29,029,000
1983	28,704,000
1984	29,261,000

At December 31, 1979 and 1978, $500,000 and $4,000,000, respectively was outstanding under short-term lines of credit with several banks at principally their prime lending rate. Effective rate at December 31, 1979 was 15½%. At December 31, 1979 an additional $11,500,000 was available at the banks' prime rate. In 1979 the maximum borrowing at the end of any calendar month was $5,000,000 and the approximate average loan balance and weighted average interest rate computed using the days outstanding method was $3,208,000 and 12%, respectively.

Note D—Leases—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. The annual lease commitments are not determinable due to the usage and adjustment factors. The company also leases flight equipment, its main operating facilities, its maintenance and training facilities, and other property and equipment.

The following is a summary of property under capital leases included in property and equipment at December 31:

	1979	1978
Flight equipment	$84,185,000	$21,116,000
Ground property and equipment	8,786,000	8,936,000
	92,971,000	30,052,000
Less accumulated amortization	12,760,000	13,943,000
	$80,211,000	$16,109,000

Notes to financial statements

December 31, 1979 and 1978 (continued)

At December 31, 1979, future minimum rental payments under capital leases and non-cancellable operating leases with initial or remaining terms of more than one year are as follows:

Period	Operating Leases	Capital Leases
1980	$ 10,237,000	$ 11,446,000
1981	8,724,000	11,084,000
1982	7,692,000	10,955,000
1983	7,137,000	10,573,000
1984	7,104,000	9,382,000
1985-2007	98,045,000	97,674,000
Total minimum lease payments	$138,939,000	151,114,000
Less amounts representing interest		66,823,000
Present value of future minimum lease payments		$ 84,291,000

Total rent expense, including landing fees, was $29,890,000 in 1979 and $25,800,000 in 1978.

Note E–Commitments–The company has purchase commitments on six new DC-9-50 aircraft to be delivered in 1980 on which it has advanced $18,466,000 and capitalized interest of $3,003,000. The company has arranged capital lease financing of approximately $43,000,000 for four of these aircraft and will be refunded approximately $13,591,000 by the lessor for advanced deposits. The company will expend an additional $14,614,000 on the remaining two aircraft.

The company has advanced $18,470,000 and capitalized interest of $1,255,000 on purchase commitments for seven Boeing 727-200 aircraft, four to be delivered in 1980 and three in 1981. The total purchase price will be approximately $104,075,000.

The company has advanced $5,911,000 and capitalized interest of $304,000 on a purchase commitment for four DC-9-80 aircraft for delivery in 1981. In addition, the company has advanced $400,000 and capitalized interest of $57,000 on options for four additional DC-9-80 aircraft to be delivered in 1981. If all eight aircraft are purchased, an additional $99,389,000 will be expended prior to delivery.

The company has a commitment under a capital lease for a used DC-9-10 aircraft to be delivered in January 1980. The capitalized present value of the aircraft will be approximately $2,142,000 with the lease term running through January 1987.

In October 1979, the company signed a letter of intent to purchase four new DC-9-80 aircraft. The letter includes provisions for cancellation of the order. The company has advanced $400,000 and capitalized interest of $15,000 and, if the order is not canceled, will expend an additional estimated $56,800,000 through delivery in 1982.

Note F–Income Taxes–Income tax expense for the years ended December 31 is as follows:

	1979	1978
Current income taxes		
Federal	$ 2,471,000	$13,521,000
Investment tax credit	(2,090,000)	(12,322,000)
	381,000	1,199,000
State and local	325,000	1,525,000
	706,000	2,724,000
Deferred income taxes		
Federal	3,153,000	884,000
Investment tax credit	(6,005,000)	1,795,000
	(2,852,000)	2,679,000
State and local	396,000	61,000
	(2,456,000)	2,740,000
	$ (1,750,000)	$ 5,464,000

Differences between income tax expense and amounts derived by applying the statutory federal income tax rates of 46% in 1979 and 48% in 1978 to income before income taxes are as follows:

	1979	1978
Income tax expense computed at statutory federal income tax rates	$ 5,203,000	$14,417,000
Investment tax credit utilized	(8,095,000)	(10,527,000)
Employee Stock Ownership Plan	715,000	552,000
State and local taxes net of federal income tax benefit	389,000	766,000
Other	38,000	256,000
	$ (1,750,000)	$ 5,464,000

Deferred income taxes arise from timing differences between financial and tax reporting. The tax effects of these differences are as follows:

	1979	1978
Capitalized interest	$ 2,953,000	$ 821,000
Investment tax credit	(6,005,000)	1,795,000
Group insurance	(290,000)	(460,000)
Capitalized leases	(472,000)	186,000
Training and development	498,000	365,000
Depreciation	754,000	186,000
Other	106,000	(153,000)
	$ (2,456,000)	$ 2,740,000

For federal income tax reporting purposes, investment tax credits of $10,400,000 are available to offset future income taxes payable through 1986. Of this amount, $6,937,000 has been recognized for financial reporting purposes as an offset to deferred income taxes payable through December 31, 1979.

During the fourth quarter of 1979, the company adjusted the estimated effective income tax rate for the year to take into effect the reduction of earnings due to the industry-wide softening of traffic. As a result, income tax expense was reduced by $4,910,000 during the fourth quarter.

Under the Revenue Act of 1978 and existing law, a special provision allows the company to offset its federal tax liability by the following approximate percentages (subject to the availability of sufficient investment tax credits): 1978–100%; 1979–90%; 1980 and 1981–80%; 1982 (and later years) –90%.

The Internal Revenue Service has examined and cleared the company's federal tax returns through December 31, 1976.

Note G–Common Stock, Options and Warrants–At December 31, 1979, 109,500 shares of unissued common stock are reserved for officers and key employees under a plan adopted in 1975 of which 73,400 shares (at $2.50 per share) expire in 1980 and 36,100 shares (at $3.87 per share) expire in 1981.

When options are exercised, the excess of the option price over par value of the shares is credited to additional paid-in capital. Options are exercisable at not less than 100% of the fair market value of the stock on the date of the grant. The company makes no charges to income in connection with shares issued under the stock option plan.

Option transactions during the two years ended December 31, 1979 are summarized as follows:

	Number of Shares	Option Price Per Share	Option Price Total
Outstanding January 1, 1978	241,650	$1.40-$4.25	$680,000
Exercised	(38,798)	1.40- 4.25	(112,000)
Expired or cancelled	(2,802)	1.40- 2.77	(7,000)
Outstanding December 31, 1978	200,050	1.40- 4.25	561,000
Exercised	(89,150)	1.40- 3.38	(236,000)
Expired	(1,400)	1.40	(2,000)
Outstanding December 31, 1979	109,500	2.50- 3.87	$323,000

All outstanding options at December 31, 1979 were exercisable.

At December 31, 1979 and 1978, there were outstanding warrants to purchase 541,057 and 3,495,494 shares of common stock, respectively. The warrants outstanding at December 31, 1979 enable the holder to purchase common stock at $2.86 per share and expire in 1981.

In February 1980, the Board of Directors declared a $.20 per share dividend payable March 17, 1980 to shareholders of record on March 3, 1980. The company paid cash dividends of $.20 and $.16 per share to its stockholders during the first quarter of 1979 and 1978, respectively.

Note H–Merger–On July 1, 1979, Southern Airways, Inc. was merged into North Central Airlines, Inc., which changed its name to Republic Airlines, Inc. As a result of the merger, Southern stockholders received 2.1 shares of Republic common stock for each share of Southern common stock held by them. The terms of the merger were arrived at as a result of arms-length negotiations between management of Southern and North Central. The combination was accounted for as a pooling of interests, and accordingly, all prior financial statements have been restated to include both companies, and reclassified to conform to the 1979 presentation.

The results of operations of the separate companies for the periods prior to the combination are summarized as follows:

	Operating Revenues	Net Earnings
Six months ended June 30, 1979 (unaudited)		
North Central	$182,957,000	$ 8,231,000
Southern	105,602,000	2,025,000
	$288,559,000	$10,256,000
Year ended December 31, 1978		
North Central	$299,053,000	$22,164,000
Southern	188,512,000	2,407,000
	$487,565,000	$24,571,000

Note I–Significant Transactions Affecting Operating Results–As a regional 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. On October 9, 1979, Class Rate IX became effective for the period beginning July 1, 1978. As a result, during 1979, revenue of $3,096,000 ($2,786,000 after income taxes–$.15 per share primary and $.14 per share fully diluted) relating to public service revenues was recognized applicable to the period July-December 1978.

During the fourth quarter of 1979, the company revised the estimate of the remaining service lives of certain of its flight equipment effective January 1 and July 1, 1979. As a result, depreciation expense decreased by $4,154,000 ($3,739,000 after income taxes–$.20 primary and $.19 fully diluted for the year and $.19 per share primary and fully diluted for the fourth quarter).

Notes to financial statements

December 31, 1979 and 1978 (continued)

Note J—Pension Costs—Pension expense was $14,978,000 in 1979 and $11,872,000 in 1978. At January 1, 1979, the latest actuarial valuation date, the actuarially computed value of vested benefits exceeded the total value of fund assets by $7,513,000 for all plans.

Note K—Net Earnings Per Share—Primary earnings per share for 1979 and 1978 are based on the weighted average number of common and common equivalent shares outstanding (18,561,082 in 1979 and 17,332,195 in 1978). Common equivalent shares result from the assumed exercise of stock options and warrants using the "treasury stock" method.

If the debentures converted into common stock during 1979 were assumed converted at the beginning of the period, primary earnings per common and common equivalent share would have been $.67 or a decrease of $.03 per share.

Fully diluted earnings per share for 1979 and 1978 are based on the assumed issuance of additional common shares (932,131 in 1979 and 1,829,244 in 1978) relating to the conversion of the 5¾% and 6½% debentures, and related interest (net of income tax effect) was added to income for purposes of the calculation.

Note L—Selected Financial Data (unaudited)—The unaudited quarterly results of operations for each of the four quarters ended in 1979 and 1978 and the unaudited effects of changing prices information are presented on pages 27 to 29 of this annual report and are incorporated by reference into this note.

Letters 10 feet high identify Republic's maintenance base in Atlanta. The company also has major maintenance facilities at Minneapolis/St. Paul, Chicago and Detroit.

Supplemental stockholder information

STOCKHOLDER'S DISCLOSURE OF OWNERSHIP

The Civil Aeronautics Board requires that any person who owns as of December 31 of any year or who subsequently acquires ownership, either beneficially or as trustee, of more than 5%, in the aggregate, of the Company's common stock shall file with the Board, within the time limits prescribed, a report containing the information required by Section 245.13 of Economic Regulations of the Civil Aeronautics Board, unless such person has previously filed such a report. Any shareholder who believes that he may be required to file such a report may obtain further information by writing to the Director, Bureau of Pricing and Domestic Aviation, Civil Aeronautics Board, Washington, D.C. 20428.

LABOR AGREEMENTS

Among the agreements the airline has with six labor unions, three are amendable in 1980, one in 1981, one in 1982, and one is currently being negotiated. The company expects to reach equitable agreements with these unions.

FORM 10-K REPORT

For the Form 10-K report to the Securities and Exchange Commission, write to Mr. John P. Dow, Vice President and Secretary, Republic Airlines, Inc., 7500 Airline Drive, Minneapolis, MN 55450.

STOCK MARKET QUOTATIONS

The following tabulation sets forth the price range for the company's common stock which is traded on the New York Stock Exchange and the Midwest Stock Exchange.

	1979		1978	
	High	Low	High	Low
1st Quarter	8	5⅞	5⅞	4⅝
2nd Quarter	7⅜	6	7⅞	5⅜
3rd Quarter	9⅝	6½	11⅞	6¾
4th Quarter	8⅝	5⅜	10	6

QUARTERLY STATEMENTS OF EARNINGS

(unaudited—in thousands of dollars except per share amounts)

	1979 Three Months Ended				1978 Three Months Ended			
	December 31	September 30	June 30	March 31	December 31	September 30	June 30	March 31
OPERATING REVENUES								
Passenger	$137,781	$142,689	$137,014	$110,308	$105,476	$115,098	$105,298	$ 82,371
Public service revenues	5,668	9,309	7,896	3,489	3,305	3,769	4,750	4,699
Other	12,520	12,704	14,090	15,762	16,037	14,993	15,263	16,506
	155,969	164,702	159,000	129,559	124,818	133,860	125,311	103,576
OPERATING EXPENSES								
Flying operations and maintenance	80,666	75,177	66,335	59,518	51,100	50,911	48,731	48,138
Other operating expenses	74,007	71,882	66,362	57,790	53,573	58,316	57,303	47,431
Depreciation and amortization	5,420	7,381	8,404	8,235	8,009	7,407	7,001	6,836
	160,093	154,440	141,101	125,543	112,682	116,634	113,035	102,405
OPERATING PROFIT (LOSS)	(4,124)	10,262	17,899	4,016	12,136	17,226	12,276	1,171
OTHER EXPENSES (INCOME)—NET	3,532	4,104	4,611	4,495	3,108	3,518	2,896	3,252
EARNINGS (LOSS) BEFORE INCOME TAXES	(7,656)	6,158	13,288	(479)	9,028	13,708	9,380	(2,081)
Income taxes	(4,910)	607	2,880	(327)	2,612	2,726	1,375	(1,249)
NET EARNINGS (LOSS)	$ (2,746)	$ 5,551	$ 10,408	$ (152)	$ 6,416	$ 10,982	$ 8,005	$ (832)
NET EARNINGS (LOSS) PER SHARE*								
Primary	$(.14)	$.29	$.60	$(.01)	$.36	$.62	$.48	$.(05)
Fully diluted	$(.14)	$.29	$.55	$(.01)	$.34	$.56	$.43	$.(05)
DIVIDENDS PER SHARE				$ .20				$. 16

*Quarterly earnings per share do not total annual earnings per share because the computation for certain quarters did not include common stock equivalents which were included on an annual basis.

Supplemental stockholder information

(continued)

EFFECTS OF CHANGING PRICES (unaudited)

Basis of preparation of 1979 supplemental data

As required by Financial Accounting Standards Board (FASB) Statement No. 33, "Financial Reporting and Changing Prices," the company has provided supplemental information concerning the effects of changing prices on its financial statements. The disclosures are intended to address two different aspects of an inflationary environment: (1) the effect of a rise in the general price level on the exchange value or purchasing power of the dollar (called "general inflation") and (2) the specific price changes in the individual resources used by the company.

The supplemental information on changing prices does not reflect a comprehensive application of either type of inflation accounting. During the experimental period, the FASB decided to focus on those items most affected by changing prices, that is: (1) the effect of both general inflation and specific price changes on inventories and property and equipment and the related impact on earnings, and (2) the effect of general inflation on monetary assets and liabilities.

Earnings from continuing operations

Net earnings as reported in the primary statements represent amounts reported on the historical cost basis of accounting. Net earnings adjusted for general inflation represent the historical amounts of revenues and expenses stated in dollars of the same (constant) general purchasing power, as measured by the average level of the Consumer Price Index (CPI) for 1979. Under this measurement method, historical amounts of depreciation expense, gain on equipment dispositions, and spare parts inventory are adjusted to reflect the change in the level of the CPI since the date the properties were acquired.

Current cost accounting attempts to deal with a different issue than earnings adjusted for general inflation. The specific prices of the company's goods and services have risen at a different rate than the general inflation rate as measured by the CPI. Net earnings adjusted for changes in specific prices (current cost) measure spare parts inventory, property and equipment, and gain from disposition of equipment at current cost (rather than historical cost) at the balance sheet date.

Income taxes

The provision for income taxes included in the supplemental statement of income from continuing operations is the same as reported in the primary financial statements. Present tax laws do not allow deductions for higher depreciation adjustments for the effects of inflation. Thus, taxes are levied on the company at rates which, in real terms, exceed established statutory rates. During periods of persistent inflation and rapidly increasing prices, such a tax policy effectively results in a tax on shareholders' investment in the company.

Purchasing power gain from holding net monetary liabilities during the year

When prices are increasing, the holding of monetary assets (e.g., cash and receivables) results in a loss of general purchasing power. Similarly, liabilities are associated with a gain of general purchasing power because the amount of money required to settle the liabilities represents dollars of diminished purchasing power. The net gain in purchasing power is shown separately in the accompanying supplemental data. The amount has been calculated based on the company's average net monetary liabilities for the year multiplied by the change in the CPI for the year. Such amount does not represent funds available for distribution to shareholders.

Increases in current cost of spare parts inventory and property and equipment

Under current cost accounting, increases in specific prices (current cost) of spare parts inventory and property and equipment held during the year are not included in earnings from continuing operations but are presented separately. The current cost increase is reduced by the effect of general inflation measured by applying the annual rate of change in the CPI to the average current cost balance of spare parts inventory and property and equipment.

Current cost measurements

Current cost calculations involve a substantial number of judgments as well as use of various estimating techniques that have been employed to limit the cost of accumulating the data. The data reported should not be thought of as precise measurements of the assets and expenses involved, but instead represent reasonable approximations of the price changes that have occurred in the business environment in which the company operates.

Current cost asset amounts were derived principally through a reference guide to current selling prices supplied by an airline industry organization. Current cost depreciation is based on the average current cost of property and equipment during the year. Depreciation expense was computed by applying the ratio of historical depreciation expense to average historical asset cost to the average current cost of these assets. The result should be approximately the same as would be calculated using the depreciation methods used in preparing the primary financial statements.

Current cost does not purport to represent the amount at which the assets could be sold.

Five-year comparison of selected financial data

As described above, the determination of net assets reflects a partial application of the two inflation accounting methods. Other assets, consisting primarily of deferred charges, have not been adjusted for general inflation, nor specific price changes. In addition, noncurrent payables have not been converted to reflect specific price changes (i.e., changes in interest rates).

STATEMENT OF EARNINGS FROM CONTINUING OPERATIONS —ADJUSTED FOR CHANGING PRICES

Year ended December 31, 1979 (unaudited)

	As Reported in the Primary Statements	Adjusted for General Inflation	Adjusted for Changes In Specific Prices (Current Cost)
Total operating revenues	$609,230,000	$609,230,000	$609,230,000
Depreciation and amortization expense	29,440,000	39,960,000	46,167,000
Other operating expenses	551,737,000	553,555,000	553,555,000
Other expenses—net	18,744,000	18,744,000	18,744,000
Gain on disposition of equipment	(2,002,000)	(1,107,000)	(1,345,000)
Provision for income taxes	(1,750,000)	(1,750,000)	(1,750,000)
	596,169,000	609,402,000	615,371,000
Earnings (loss) from continuing operations	$ 13,061,000	$ (172,000)	$ (6,141,000)
Gain from decline in purchasing power of net amounts owed		$ 33,461,000	$ 33,461,000
Increase in specific prices (current cost) of inventory and property and equipment held during the year (*)			$ 43,565,000
Effect of increase of general price level			25,345,000
Excess of increase in specific prices over increase in the general price level			$ 18,220,000

(*) At December 31, 1979, current cost of inventory was $34,040,000, and the current cost of property and equipment, net of accumulated depreciation, was $548,258,000.

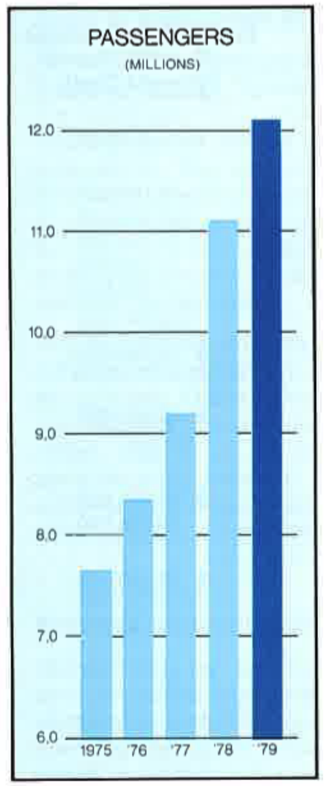
FIVE-YEAR COMPARISON OF SELECTED SUPPLEMENTARY FINANCIAL DATA —ADJUSTED FOR EFFECTS OF CHANGING PRICES

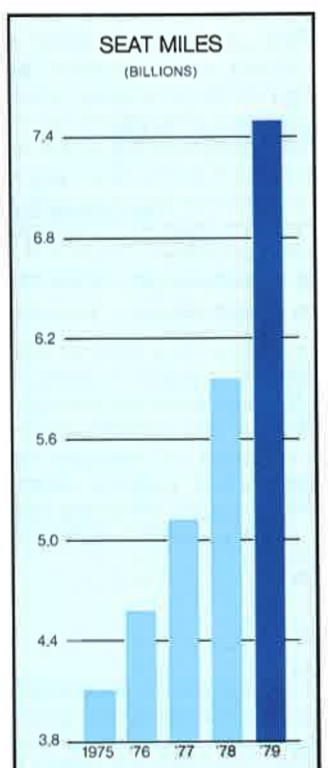
(In average 1979 constant dollars—unaudited)

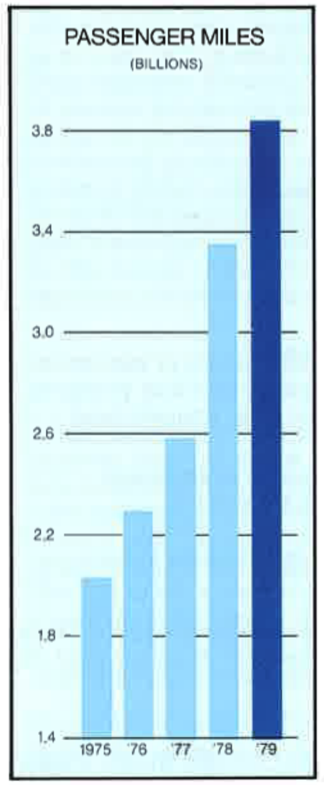
	Year ended December 31				
	1979	1978	1977	1976	1975
Total operating revenues—at historical costs	$609,230,000	$487,565,000	$388,634,000	$331,315,000	$281,574,000
Total operating revenues—in average 1979 dollars	$609,230,000	$542,460,000	$465,504,000	$422,451,000	$379,741,000
Historical cost information— adjusted for general inflation					
Loss from continuing operations	$ (172,000)	–	–	–	–
Loss from continuing operations per common share	$(.01)	–	–	–	–
Equity in net assets at year-end	$210,226,000	–	–	–	–
Current cost information					
Loss from continuing operations	$ (6,141,000)	–	–	–	–
Loss from continuing operations per common share	$(.30)	–	–	–	–
Excess of increase in specific prices over increase in the general price level	$ 18,220,000	–	–	–	–
Equity in net assets at year-end	$314,040,000	–	–	–	–
Gain from decline in purchasing power of net amounts owed	$ 33,461,000	–	–	–	–
Cash dividends declared per common share—historical	$.20	$.16	$.12	$.10	$.10
Cash dividends declared per common share—in average 1979 dollars	$.20	$.18	$.14	$.13	$.13
Market price per common share at year-end—historical	$6.00	$7.12	$5.00	$3.88	$2.38
Market price per common share at year-end— in average 1979 dollars	$6.00	$7.93	$5.99	$4.94	$3.20
Average consumer price index	217.4	195.4	181.5	170.5	161.2

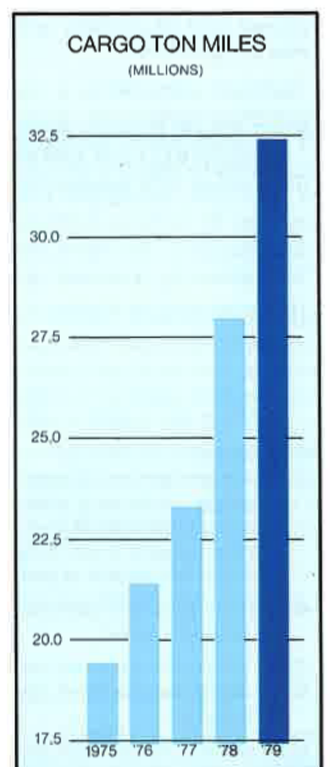
NOTE: Certain data for years prior to 1979 have been omitted as permitted by FASB No. 33.

Five-year summary









EARNINGS

	1979	1978	1977	1976	1975
OPERATING REVENUES					
Passenger	$527,792,000	$408,243,000	$317,469,000	$272,365,000	$231,330,000
Public service	26,362,000	16,523,000	18,299,000	19,019,000	18,186,000
Other	55,076,000	62,799,000	52,866,000	39,931,000	32,058,000
	609,230,000	487,565,000	388,634,000	331,315,000	281,574,000
OPERATING EXPENSES					
Flying operations and maintenance	281,696,000	198,880,000	169,187,000	146,529,000	126,892,000
Other operating expenses	270,041,000	216,623,000	166,392,000	144,051,000	120,773,000
Depreciation and amortization	29,440,000	29,253,000	25,260,000	21,444,000	18,418,000
	581,177,000	444,756,000	360,839,000	312,024,000	266,083,000
OPERATING PROFIT	28,053,000	42,809,000	27,795,000	19,291,000	15,491,000
OTHER EXPENSES (INCOME)					
Interest expense	26,497,000	18,688,000	12,424,000	10,190,000	8,839,000
Less interest capitalized	6,375,000	2,015,000	948,000	843,000	757,000
	20,122,000	16,673,000	11,476,000	9,347,000	8,082,000
Interest income and other—net	(1,378,000)	(2,593,000)	(700,000)	(924,000)	(1,296,000)
Gain on disposition of equipment	(2,002,000)	(1,306,000)	(8,904,000)	(280,000)	(17,000)
	16,742,000	12,774,000	1,872,000	8,143,000	6,769,000
EARNINGS BEFORE INCOME TAXES	11,311,000	30,035,000	25,923,000	11,148,000	8,722,000
Income taxes	(1,750,000)	5,464,000	2,885,000	3,144,000	657,000
NET EARNINGS	$ 13,061,000	$ 24,571,000	$ 23,038,000	$ 8,004,000	$ 8,065,000
NET EARNINGS PER SHARE					
Primary	$ .70	$1.42	$1.38	$.48	$.48
Fully diluted	$ .68	$1.31	$1.23	$.43	$.43

BALANCE SHEET ITEMS

	1979	1978	1977	1976	1975
Current assets	$144,691,000	$107,764,000	$ 89,088,000	$ 71,362,000	$ 66,329,000
Working capital provided from operations	$ 41,717,000	$ 57,806,000	$ 48,639,000	$ 31,177,000	$ 26,188,000
Property and equipment—net	$399,632,000	$314,054,000	$235,671,000	$195,807,000	$158,277,000
Total long-term debt	$263,035,000	$196,637,000	$142,648,000	$129,512,000	$102,173,000
Retained earnings	$ 93,634,000	$ 83,050,000	$ 60,493,000	$ 39,052,000	$ 32,305,000
Stockholders' equity	$145,514,000	$113,288,000	$ 89,266,000	$ 67,247,000	$ 60,281,000
Shares outstanding	20,620,000	16,348,000	15,982,000	15,832,000	15,752,000
Book value per share	$7.06	$6.93	$5.59	$4.25	$3.83

STATISTICS

	1979	1978	1977	1976	1975
Passengers	12,156,000	11,143,000	9,180,000	8,397,000	7,685,000
Passenger miles (000)	3,847,000	3,364,000	2,584,000	2,304,000	2,054,000
Available seat miles (000)	7,479,000	6,010,000	5,152,000	4,617,000	4,141,000
Passenger load factor	51.4%	56.0%	50.2%	50.0%	49.6%
Cargo ton miles	32,324,000	28,062,000	23,346,000	21,537,000	19,047,000
Revenue plane miles	80,915,000	70,850,000	61,981,000	58,456,000	55,282,000
Number of employees	8,982	7,676	6,772	6,366	5,929

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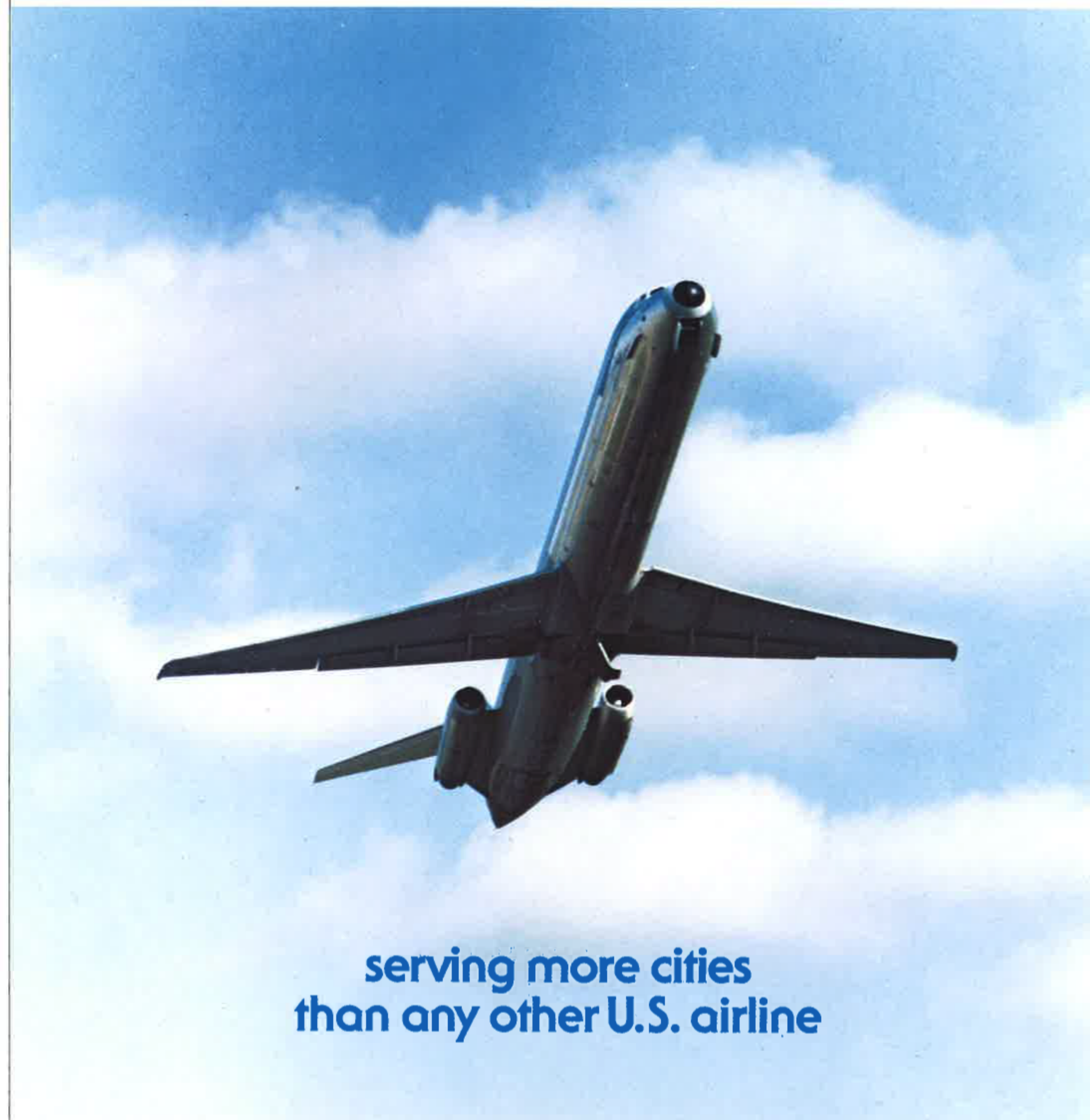
REPUBLIC AIRLINES



REPUBLIC AIRLINES, INC.
MINNEAPOLIS, MINNESOTA 55450