



ANNUAL REPORT 1978

**NORTH CENTRAL AIRLINES**

## board of directors

**Hal N. Carr\***  
Chairman of the Board  
North Central Airlines

**Eric Bramley**  
Retired Editor  
Aviation Daily  
(aviation industry news service)

**G. F. DeCoursin\***  
Chairman of the Board and  
Chief Executive Officer  
Media Graphics, Inc.  
(creative graphic arts and  
commercial photography)

**Chan Gurney**  
Retired Member  
Civil Aeronautics Board

**John M. Lawrence III**  
Partner in law firm of  
Lawrence, Thornton,  
Payne & Watson

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

**Theodore R. Miles**  
President and  
Chief Executive Officer  
Stange Co.  
(manufacturer and distributor  
of food products)

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

**Morton B. Phillips**  
Chairman of the Board  
Westland Capital Corporation  
(small business investment  
corporation)

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

**Henry M. Ross**  
President  
Ross Industries, Inc.  
(machinery manufacturer)

**Bernard Sweet\***  
President and  
Chief Executive Officer  
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  
**Bernard Sweet** ..... President and Chief Executive Officer  
**J C Constantz** ..... Vice President-Federal Affairs  
**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** ..... Staff Vice President  
**Joseph W. Ettel** ..... Assistant Secretary  
**Raymond J. Rasenberger** ..... Assistant Secretary  
**Ralph Strangis** ..... Assistant Secretary  
**Walter E. Nielsen** ..... Assistant Treasurer  
**Michael D. Meyer** ..... Controller

**NORTH CENTRAL AIRLINES, INC.**  
7500 NORTHLINER DRIVE • MINNEAPOLIS, MINNESOTA 55450

## highlights

	1978	1977	Change
OPERATING REVENUES .....	\$ 299,053,000	\$ 229,123,000	30.5%
OPERATING PROFIT .....	\$ 35,103,000	\$ 18,535,000	89.4
NET EARNINGS .....	\$ 22,164,000	\$ 13,696,000	61.8
NET EARNINGS PER SHARE AND EQUIVALENT SHARE .....	\$1.70	\$1.11	53.2
WORKING CAPITAL FROM OPERATIONS .....	\$ 42,269,000	\$ 28,505,000	48.3
RETAINED EARNINGS .....	\$ 69,148,000	\$ 48,957,000	41.2
STOCKHOLDERS' EQUITY .....	\$ 89,612,000	\$ 63,280,000	29.3
PASSENGERS .....	6,911,000	5,547,000	24.6
PASSENGER MILES .....	1,925,450,000	1,392,406,000	38.3
CARGO TON MILES .....	17,619,000	13,998,000	25.9

## about north central

North Central Airlines, a scheduled carrier linking intermediate-sized cities with major metropolitan areas, has completed 31 years of service. 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 24 years since 1954, when present management was brought in. Its fleet of 59 jet-powered aircraft makes 725 departures a day over a 22,400-mile route system. Computerized reservations and ticketing provide efficient passenger handling.

The airline serves 103 cities—in 20 states and two Canadian provinces—including Boston and New York; Miami, Atlanta, Houston; Tucson, Denver; Winnipeg and Toronto. Major hubs are Detroit, Milwaukee, Chicago and Minneapolis/St. Paul.

North Central's 4,500 dedicated employees offer the traveling public the finest type of scheduled airline service.

ANNUAL MEETING:  
Wednesday, April 4, 1979  
Wausau, Wisconsin

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 and warrants  
traded under symbol NCA

New York Stock Exchange  
Midwest Stock Exchange

**to our stockholders,  
employees and friends:**



Hal N. Carr

In every area, 1978 was the most outstanding year in the history of North Central Airlines. Here are the highlights:

- *Net earnings reached \$22,164,000, an all-time record.*
- *Earnings per share rose 53 percent to \$1.70, and this year's cash dividend was increased 25 percent.*
- *Revenues soared to nearly \$300 million—a new high.*
- *Passenger miles jumped 38 percent to 1.9 billion. System mileage doubled, as 17 long-haul nonstop routes were added.*
- *The proposed merger of North Central with Southern Airways is nearing reality.*

These achievements demonstrate two of the company's most important assets: financial strength and productive employees, who are able to meet challenges and take advantage of opportunities.

The airline's growth in 1978 exceeded expectations. Revenues hit \$299,053,000, a 31 percent gain. The net earnings of \$22,164,000, or \$1.70 per share, were 62 percent over the \$13.7 million, or \$1.11 per share, for 1977. This \$8.5-million increase in earnings was the largest ever attained. The company has operated profitably for 24 years since 1954, when present management was brought in.



Bernard Sweet

North Central remains a financial leader among the regional carriers, ranking first with \$69,148,000 in retained earnings. Stockholders' equity was up 29 percent to \$89,612,000, raising book value per share to \$7.25.

On the basis of the company's excellent 1978 profits, the Board of Directors declared a cash dividend of \$.20 per share to stockholders of record February 15, 1979. North Central has paid annual cash dividends for the past seven years.

A record 6,911,000 passengers were carried in 1978. Passenger miles climbed to 1.9 billion, while cargo ton miles totaled 17.6 million. To accommodate this traffic growth, seven DC-9-50 jets were acquired. The airline's 59-aircraft fleet is composed of 36 DC-9s and 23 Convair 580s.

North Central added 13 new cities and 17 long-haul nonstop routes to its system in 1978—expanding from 10,900 miles to 22,400 miles. Service was introduced to Baltimore, Syracuse, Philadelphia, Atlanta, Houston and Tucson, plus the Florida cities of Tampa/St. Petersburg, Sarasota/Bradenton, West Palm Beach, Fort Lauderdale and Miami. Minneapolis/St. Paul-San Diego was also awarded by the Civil Aeronautics Board, and flights could begin later this year. The airline now serves 103 cities in 20 states and two Canadian provinces.

Officials of North Central and Southern Airways announced a proposed merger of the two companies in July 1978. The formal agreement, reached in September, was endorsed by directors and stockholders of both airlines. Approval by the Civil Aeronautics Board has been requested, and the Law Judge issued a favorable initial decision in February 1979. Final decisions are expected this Spring from the Board and the President of the United States.

With the combination of North Central and Southern, a dynamic new carrier—Republic Airlines—will emerge. It can provide stronger competition, greatly improved service, and fare savings to over 150 communities and 12 million passengers. As the name implies, Republic will derive its strength from its 7,500 people who will serve air travelers across the nation and from Canada to the Caribbean.

North Central's own unprecedented growth and earnings in 1978 are a tribute to the dedicated efforts of the company's personnel. Their contributions, and those of countless others who support the airline, are gratefully acknowledged.

Prospects for the future are the brightest in North Central's history. The new routes will be vigorously developed, several additional awards are expected, and more jets will be arriving. With further industry growth in 1979 and the pending merger, the company enthusiastically embarks on a new era.

Sincerely,

Hal N. Carr  
Chairman of the Board

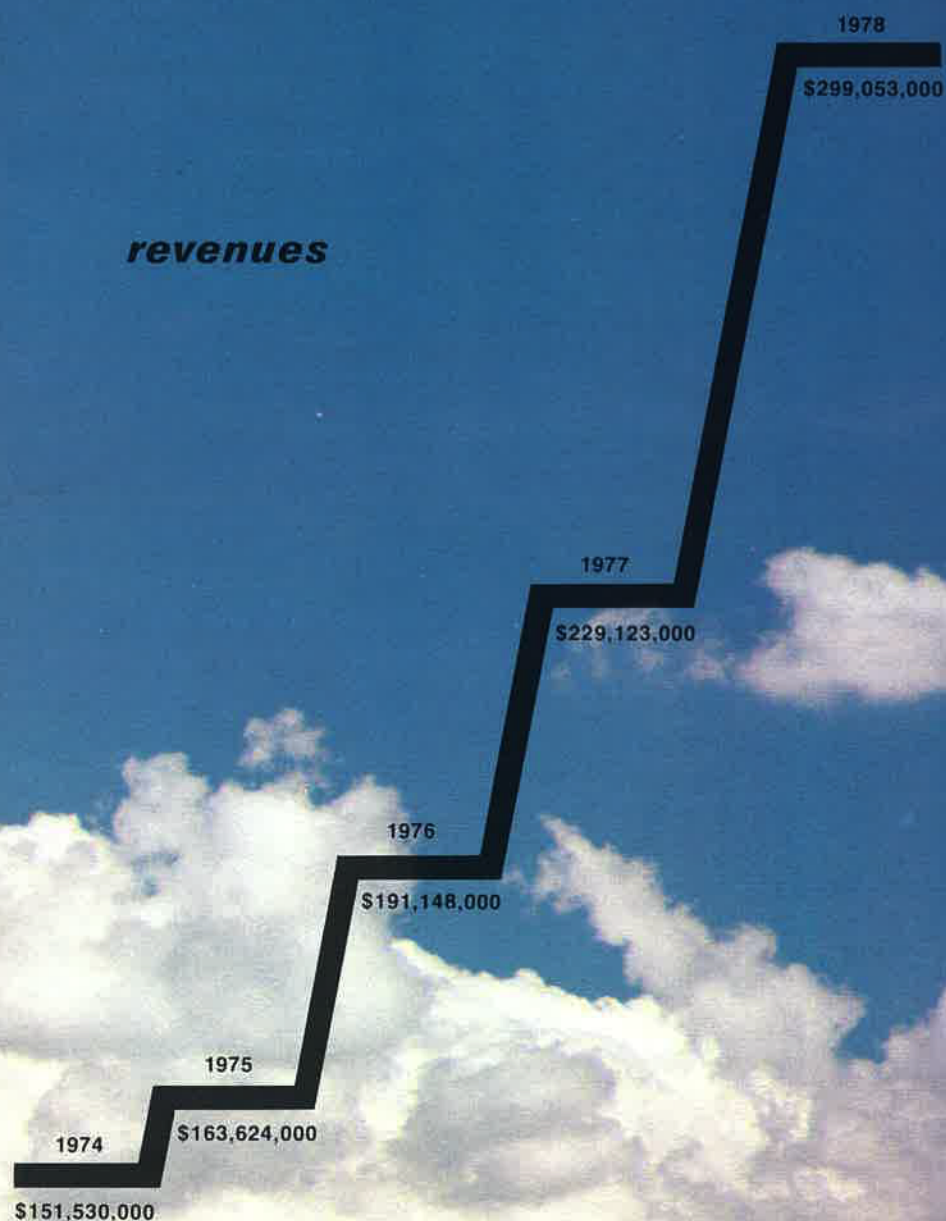
Bernard Sweet  
President and  
Chief Executive Officer

March 5, 1979





## revenues



## financial review

Record net earnings of \$22,164,000 were achieved by North Central in 1978. This surpasses by 62 percent the previous mark of \$13,696,000 in 1977. Revenues reached \$299,053,000 to set an all-time high.

In each of the past two years, earnings have increased more than 60 percent. The company has operated profitably for 24 years since 1954, when present management was brought in. North Central has retained earnings of \$69,148,000—largest among the regional airlines.

The \$299 million in revenues represents a 31 percent gain over the \$229,123,000 reported for 1977. Operating expenses, including depreciation and amortization of \$16,353,000, rose 25 percent to \$263,950,000 from the \$210,588,000 a year earlier. Operating profit jumped 89 percent to \$35,103,000 from \$18,535,000.

With the purchase of new aircraft and equipment in 1977 and 1978, investment tax credits of \$12,720,000 were generated. These credits offset all Federal, state and deferred income taxes except \$4,555,000 in 1978 and \$1,004,000 in 1977.

The 1978 net earnings of \$22,164,000, or \$1.70 per share and equivalent share, compare with the \$13.7 million, \$1.11 per share, the previous year. Stockholders' equity increased 29 percent to a record \$89,612,000. Book value has risen to \$7.25 per share on 12,366,031 shares of common stock outstanding, from \$5.62 per share in 1977.

The Board of Directors declared an annual cash dividend in January 1979. Stockholders of record on February 15 received \$.20 per share, up 25 percent from the \$.16 per share paid in 1978. North Central is the only regional airline which has issued a cash dividend in each of the past seven years.

Operating expenses, 25 percent ahead of 1977, reflect national inflationary trends and extra costs associated with expanded operations. Wages, fringe benefits, and payroll taxes were up 22 percent to \$115,227,000. Interest expense rose to \$11,783,000, because of higher

interest rates and debt incurred to finance additional flight equipment.

A summary of the company's five-year traffic and financial growth appears on Page 27. Supplemental stockholder information, including quarterly statements, is carried on Page 24.

To accommodate traffic growth and implement future route awards, the company will add 11 DC-9-50 aircraft to its fleet by the Spring of 1980.

The first three 727-200 long-range tri-jets will be received by June 1980.

The Airline Deregulation Act of 1978 will affect the company's future financial performance, although the full impact cannot be assessed. One provision of the Act allows the airlines to unilaterally adjust fares up five percent or down 50 percent. This permits faster reaction to cost increases and encourages experimentation with lower fares.

North Central is in an excellent position to take advantage of the benefits of deregulation. Consistent profitability for over two decades has given the company ample resources to develop new markets and generate traffic on established routes. The merger of North Central with Southern Airways offers further opportunities and many challenges. With continued strict cost control and revenue growth, the company expects to achieve another successful year in 1979.

## MAJOR FACTORS OF CHANGE IN REVENUES AND EXPENSES

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

Traffic gains generated the \$69.9-million jump in revenues. Contributing

factors were the introduction of service on 17 major nonstop routes, promotional fares, a strike against another carrier, and the addition of seven DC-9-50 jets. Net passenger revenues climbed \$62 million, even though lower rates on long-haul flights and discount fares reduced the

average yield. Public service revenues were reduced by \$900,000 under the revised formula for calculating the amount paid to the company to serve small communities. Cargo and other revenues were \$8.8 million higher—\$6.1 million from air freight, \$3.4 million from charters and a \$700,000-decline in miscellaneous activities.

Operating expenses were up \$53.3 million. Of that amount, labor and employee benefits showed a \$20.8-million gain due to higher wages, insurance and pension costs, and a 16 percent increase in personnel. Aircraft fuel expenses escalated \$8.6 million with 15 percent greater usage and the average price per gallon up seven percent. Inflation, expanded operations, and the cost of starting new routes affected landing fees, rent, parts, supplies and services. Mutual Aid payments increased by \$5.6 million due to a strike against another carrier.

Under other expenses (income), the gain on disposition of equipment was \$2.8 million less than in 1977. With higher interest rates and more short-term investments, \$1.1 million was added to interest income. The change in interest expense of \$2.9 million reflects the cost of financing new equipment and rising interest rates. Income taxes increased \$3.5 million because earnings exceeded the investment tax credits available to offset 1978 federal income taxes.

The combined effect of these factors was the substantial improvement in net earnings of \$8.5 million.

## VARIANCE ANALYSIS

	Net Changes	
	1978-1977	1977-1976
<b>MAJOR FACTORS OF CHANGE:</b>		
<b>Operating revenues</b>		
Passenger miles	\$63,100,000	\$24,400,000
Passenger fares	(1,100,000)	5,100,000
Public service revenues	(900,000)	(200,000)
Cargo and other revenues	8,800,000	8,700,000
Net revenue changes	69,900,000	38,000,000
<b>Operating expenses</b>		
Labor and employee benefits	20,800,000	14,300,000
Cost of aircraft fuel	8,600,000	7,700,000
Parts, supplies and services	3,600,000	2,800,000
Landing fees and rent	2,000,000	1,400,000
Passenger service and promotion	6,800,000	3,400,000
Mutual Aid payments	5,600,000	(100,000)
Other expenses	4,100,000	1,700,000
Depreciation	1,800,000	3,000,000
Net expense changes	53,300,000	34,200,000
Changes in operating profit	16,600,000	3,800,000
<b>Other expenses (income)</b>		
Gain on disposition of equipment	(2,800,000)	2,500,000
Interest income and other	1,100,000	(100,000)
Interest expense	2,900,000	2,200,000
Income taxes	3,500,000	(2,000,000)
Net other changes	8,100,000	(2,200,000)
Changes in net earnings	\$ 8,500,000	\$ 6,000,000



## north central / southern merger

The proposed merger between North Central and Southern Airways will produce a strong, competitive new airline.

At special meetings in February 1979, stockholders of North Central and Southern endorsed the merger. A final decision by the Civil Aeronautics Board, expected this Spring, must be affirmed by the President because international routes are involved.

In July 1978, officials of the two companies had announced an agreement in principle on the merger. A formal agreement was reached in September, and both Boards of Directors approved the terms. CAB hearings were held in November. The U.S. Department of Justice, Department of Transportation, and the CAB Bureau of Pricing and Domestic Aviation favored the merger, while the CAB Bureau of Consumer Protection expressed some opposition. The Law Judge's initial decision, issued in February, recommended the merger.

North Central has always viewed route expansion through merger as a viable possibility, provided it is consistent with the company's overall management philosophy. As the regional industry matured, it made

sense to seek a partner with the potential for major nonstop routes which could be fed by both systems. After considerable research and analysis, Southern proved to be the most logical choice.

The two airlines do not compete on a single route segment, but they connect at 11 metropolitan areas. The systems integrate well, providing strong traffic demand to support new flights and produce higher load factors.

The proposed merger preserves two regional networks which offer essential air service to 12 million passengers and over 150 cities. North Central believes the combination is an excellent opportunity for greater growth and profitability. Access to winter "sunshine" markets will stimulate traffic in months when business travel ebbs. The fleets are highly compatible, and the increased aircraft utilization will help the new company continue serving small communities and absorb reductions in subsidy.

The merged carrier, much stronger than either airline could be as a separate entity, would rank tenth in the industry in passenger boardings. In the Midwest-Southeast markets,

a vigorous competitor will emerge. The new airline will offer fare savings of nearly \$8 million and greatly improve service to the traveling public.

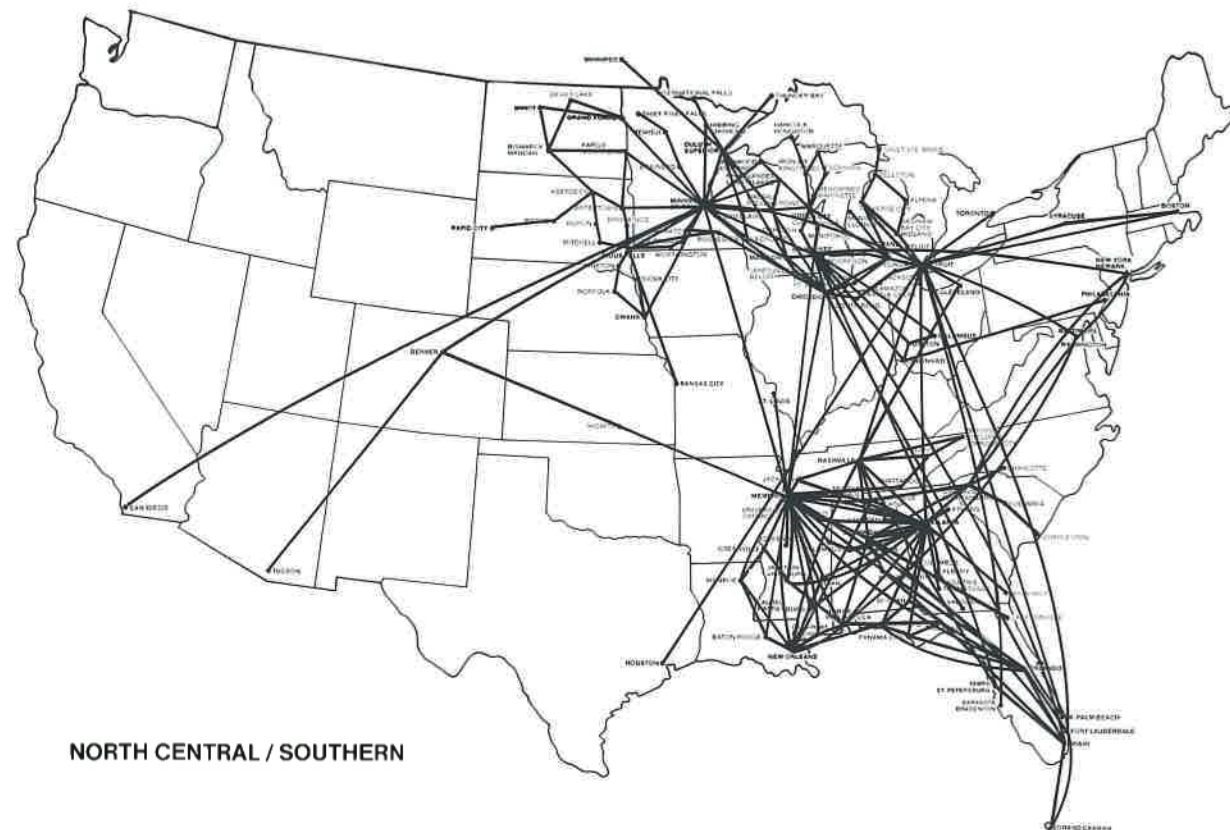
To denote corporate stability and the proud heritage of both North Central and Southern, the name "Republic Airlines" was chosen for the new company. It also reflects the transcontinental image of the carrier which would have routes from New England to Southern California, and from Canada to the Cayman Islands in the Caribbean. Quite significantly, the word Republic describes an organization which derives its strength from its people.

The combined airline will offer employment to all personnel, with salary at the same or improved levels and comparable overall fringe benefits. Future growth will create new positions and provide greater opportunities for advancement.

Management is proud of what North Central has accomplished in the past 31 years. The merger with Southern is a catalyst that will further enhance the company's record of service and profitability that is unsurpassed in the industry.



North Central and Southern, when merged as Republic Airlines, will bring single-carrier service to more than 150 cities.



## traffic growth and performance

Traffic on North Central reached record levels in 1978. More than 6.9 million passengers were carried 1.9 billion passenger miles, and the airline flew 17.6 million cargo ton miles. The increase of 1.4 million passengers over the previous year was by far the largest in the company's history.

These achievements reflect the introduction of service on 17 new nonstop routes—including nine winter "sunshine" cities. Other contributing factors were the addition of seven DC-9-50 fan jets, a strike against another carrier, and discounted fares which attracted thousands of new air travelers.

The passenger boardings of 6,911,130 showed a 25 percent increase—well ahead of the 18 percent average gain for the scheduled airline industry. The 714,105 passengers in August and 29,741 on December 22 also set records. Passenger miles soared 38 percent to 1.9 billion from 1.4 billion in 1977, pushing the passenger load factor to a new high of 56.9 percent.

Complementing its scheduled service, North Central flew 178,728 passengers on charter flights during 1978—a jump of 64 percent, compared with 108,802 a year earlier. The charters went to 38 states and 14 destinations outside the U.S., including Nassau, Freeport, Montego Bay, Mazatlan, Yellowknife and Montreal. During peak travel periods, 1,163 extra sections of scheduled flights accommodated 73,000 passengers.

For the first time, North Central handled over 100 million pounds of cargo in a single year. The 17.6 million cargo ton miles—including freight, express and mail—were 26 percent ahead of 1977. The number of air freight shipments increased 13 percent to 663,000.

The company's popular "VIP" small package service, now in its eighth year, experienced 48 percent growth in 1978. More than 78,000 VIP parcels were carried by the airline. This expedited handling, which can include pickup and delivery, has

proven valuable for shippers of medical supplies, documents, news films, electronic data processing equipment and machine parts.

North Central maintained its outstanding record of service reliability by completing 99 percent of the 34.5 million scheduled miles—although the airline experiences more adverse weather for a longer time than any other U.S. carrier. The company's progressive maintenance program again demonstrated its value. Of the 232,000 departures, only two-tenths of one percent were cancelled for maintenance reasons, and 1.6 percent were delayed by mechanicals.

The company continues to rank among industry leaders in operating performance. This achievement results from total team effort—by flight crews, station and maintenance personnel, flight control people and passenger service employees. Everyone involved in the day-to-day operation can be proud of the company's excellent record.





Seven DC-9-50s were added in 1978. The above jets are lined up at Detroit Metropolitan Airport, where North Central has 69 daily departures.

## new facilities and services

Seven new DC-9-50 fan jets joined North Central's fleet in 1978, enabling the airline to add 11,500 route miles and 17 major long-haul nonstops to its system. DC-9 jets accounted for 83 percent of the 3.4 billion seat miles flown during the year.

The company's 59-aircraft fleet consists of 36 DC-9s and 23 Convair 580 prop jets. Three additional DC-9-50s are to be delivered by June 1979, and another four later in the year. Four more DC-9-50 jets will be received in the first quarter of 1980.

North Central has also ordered three 164-passenger Boeing 727-200

aircraft for use on long-haul routes. The extended range of the Boeing tri-jet, plus its capabilities over water and at high-altitude airports, will provide greater operating flexibility.

The 727-200 with Pratt & Whitney engines integrates well with the DC-9-50. Also, many parts and accessories are common to both. Delivery of the three 727s will be made in the Spring of 1980.

A \$1-million Collins automatic call distributor system has been installed at the airline's Minneapolis Reservations Center, improving service in states west of Lake Michigan. The new equipment permits telephone

calls to be processed faster and more economically. Reservations agents handle over 16,000 phone calls daily at this center.

North Central's unique weather radar, with a six-color digital picture display, is a first in the airline industry. Now in operation at the company's Central Flight Control office, the system is linked directly with the National Weather Service radar network. It shows current data on the location, magnitude and intensity of potentially dangerous thunderstorms in a 250-mile radius. With this information, pilots can detect and avoid turbulent air to insure safe, comfortable flights.

Flight Superintendent Harry Amundson and Captain Paul Dietz consult the airline's new six-color weather radar TV-display to help plan a smooth flight.



The company now has a \$4-million Model 3033 computer, IBM's newest and largest. Computer Services personnel Julie McAlister and Joe Ginter are at the control console, and Trudy Peper is in the background.

In December 1978, a \$4-million IBM central processing unit was added to the Computer Services Department to accommodate the increased amount of data and applications for North Central's ESCORT and SCEPTRE systems. The Model 3033, IBM's newest and largest, marks the beginning of a comprehensive plan to upgrade all data communications and processing equipment.

A SCEPTRE innovation, accomplished during 1978, is the computerized Engineering Control Program which enables the airline to monitor modifications on all aircraft and parts. Maintenance personnel always have a current and complete history of each serialized part on every aircraft in the entire fleet. These records can be retrieved through the 350 receiving units at all stations and maintenance bases.

New ESCORT programs improved preparation of the flight-related information required for each aircraft departure. "Weight Tab," for example, gives both crews and down-line stations the number of on-board passengers, type and amount of

cargo, loading configuration, amount of fuel on board, and other weight and balance data. These essential computations are presented in an efficient, accurate and uniform manner.

To expedite ticketing and passenger fare quote, computer programs were changed to permit processing of longer itineraries. Passenger service and reservations agents can compute fares or prepare complicated tickets in a fraction of the time formerly required. For 1978, some 85 percent of the tickets issued by North Central were computer-produced.

Major construction is underway at the Minneapolis-St. Paul International Airport. The Green Concourse of the terminal is being extended to accommodate North Central's operation. When the \$5.8-million building plan is finished, the company will occupy ten passenger boarding gates—twice the number now used. New station and flight service facilities are being included.

Other airport expansion and renovation projects were completed at Cleveland, South Bend and Thunder

Bay, while those at Devils Lake and Kalamazoo/Battle Creek will be finished in 1979. At Sault Ste. Marie, which is now being served through the new Chippewa International Airport, jet operations were introduced. Terminal buildings have been constructed at Huron and Hibbing/Chisholm; another is being built at International Falls. In Rhinelander, terminal dedication ceremonies are planned for March 1979. Runway and taxiway improvements were made at Rhinelander, Escanaba, Brainerd and Worthington.

Baggage areas have been expanded in Cleveland, Grand Rapids, South Bend, Milwaukee, and Bismarck/Mandan. Carry-on baggage X-ray units speed up passenger security clearance at Rochester and Flint. A new 1,100-square-foot loading dock serves LaCrosse air freight customers, and plans are underway to construct a major air freight building at Detroit.

Each year, North Central seeks new ways to provide better, more efficient service to its customers. Through imaginative planning and development, the airline will maintain its high standards in the years ahead.



Dramatic lighting and pleasing colors are featured in the company's new design for passenger boarding areas.



## social action and environmental programs

North Central continues to expand its programs relating to the environment and to personnel.

In accordance with the company's Affirmative Action policies, jobs are open to all qualified applicants. Women are employed as mechanics, sales personnel and pilots; while men serve as reservationists, flight attendants and clerks. Ten women were added to management positions. North Central now has 19 percent more minority employees and 30 percent more women than it had in 1977. Total employment rose 16 percent.

Applicants are recruited primarily in communities served by the airline. Industrial Relations staff members visit schools and universities to secure top candidates. Career counselors frequently come to North Central seeking information on employment opportunities and position requirements.

The airline's Management Development program is in its third year. Some 330 people have already completed this training. The objectives are more effective communications and better leadership through a series of seminars, lectures and workshops. The company also has special orientation sessions for new supervisors.

Conservation of natural resources, with emphasis on improved fuel management, is one of North Central's most important concerns. In 1978,

by using the DC-9 digital flight simulator in pilot training, the airline conserved 3.8 million gallons of aviation fuel—enough to operate two jets in scheduled service for 324 days. Continued refinement of flight procedures, aircraft loading, and fuel planning techniques have substantially reduced fuel requirements. This attention to conservation was particularly significant when the company sought and was granted extra fuel to provide service to new cities.

The airline's DC-9-30 aircraft are experiencing better engine performance as a result of maintenance programs initiated in 1978. By upgrading components in the engine gas path, air flow has been improved to produce more thrust. Also, a new cleaning device for engine fuel nozzles removes carbon accumulation so spray patterns can be maintained. Both of these changes help to keep jet engines fine-tuned for maximum thrust with lower fuel consumption.

At the Twin Cities Main Operations Base, a recycling tank collects and filters solvents for cleaning aircraft

parts. By reusing these petroleum-based fluids indefinitely, the company can cut its need by about 4,000 gallons yearly, saving over \$5,000.

Five stations now have permanent aircraft deicing systems. This equipment combines hot water with glycol, permitting quick removal of snow and ice with lesser amounts of costly deicing fluids. The systems are in operation at Grand Rapids, Detroit, Traverse City, Sault Ste. Marie and Marquette. Installation is underway at Minneapolis/St. Paul.

Over 210,000 pounds of used paper were salvaged for recycling during 1978. In five years, the airline's "Waste Not" program has reclaimed 833,000 pounds of paper. To produce this amount, about 7,000 trees would be needed.

North Central has worked hard to earn its reputation as a concerned and responsive corporate citizen. The company has demonstrated leadership by continually seeking new ways to develop the talents of its people and conserve vital natural resources, while maintaining high operational standards.



Captain Chet Drag and First Officer Sandra Eisenmenger complete the "receiving airplane checklist" for their DC-9.

## route development

North Central added 17 long-haul routes during 1978, and more than doubled its total mileage. The year was the greatest period of expansion in the company's history.

From a 10,900-mile system of 90 cities and 14 states, North Central's route network has grown to 22,400 miles, 103 cities and 20 states.

For more than two decades, the aggressive route development program has been an important factor in the company's growth. Many applications have been pending before the Civil Aeronautics Board. Several awaited final decisions, and the CAB took action favorable to North Central in four of those proceedings.

The company was granted permanent authority from Bismarck/Mandan to Chicago, via Fargo/Moorhead and Minneapolis/St. Paul. Two daily round-trip flights were inaugurated on May 8, and a third was added by the end of the month.

New Detroit-Baltimore nonstops started August 1. Three round trips daily provide many cities in Wisconsin and Michigan with their first single-carrier and single-plane service to Baltimore Washington International Airport.

On September 5, two other important nonstop routes were inaugurated—Detroit-Atlanta and Cincinnati-Philadelphia. With the airline's four daily round trips between Detroit and Atlanta, eight Michigan communities and Milwaukee have single-plane service. The Cincinnati-Philadelphia route received two round trips, originating and terminating at Milwaukee or points beyond. This provides ten Midwest cities with single-plane Philadelphia service, and 14 other communities with convenient single-carrier connections.

### Regulatory Reform

Following several years of consideration, Congress approved the Airline Deregulation Act of 1978, and it was signed into law by President Carter on October 24. This legislation opens all dormant routes to competition, simplifies route entry, permits fare flexibility, and sets conditions for dissolution of the CAB. The law also assures continuation of air service to smaller cities.

Under the "dormant authority" section of the law, a carrier may seek—and must receive—any domestic route for which another airline

(continued)



Vastly improved deicing systems are in service at the airline's major cold-weather stations. Snow and ice are quickly removed from aircraft, with minimum use of precious petroleum-based fluids.



Southern belles welcome passengers on North Central's inaugural flight to Atlanta from Detroit.



## route development (continued)

has been certificated and is not operating. North Central applied for, and was awarded, 12 new segments. In December, nonstop round-trip flights were inaugurated on these routes:

Denver-Tucson  
Minneapolis/St. Paul-Detroit  
Chicago-West Palm Beach  
Detroit-West Palm Beach  
Detroit-Fort Lauderdale  
Detroit-Sarasota/Bradenton  
Detroit-Houston  
Detroit-Syracuse  
Boston-Syracuse  
Milwaukee-Philadelphia  
Milwaukee-Tampa/St. Petersburg  
Milwaukee-Miami

The company also received approval for Minneapolis/St. Paul-San Diego nonstops, and that service will start as soon as San Diego environmental and regulatory agencies permit.

Until December, North Central had virtually no vacation or weekend "sunshine" markets to promote

during the winter months when travel declines. With the addition of seven popular Florida cities, Houston and Tucson, the airline has tremendous new potential for substantial year-round vacation traffic to on-line communities.

### Expansion in 1979

The Airline Deregulation Act allows every carrier to automatically enter one market each year in 1979, 1980 and 1981. At the same time, one route may be "protected" yearly from competition by other airlines.

Accordingly, in January North Central requested the Chicago-Houston market for automatic entry, and protected its Twin Cities-Denver route.

Another recent development affecting North Central was the discontinuance of Twin Cities nonstops to New York LaGuardia and Washington National by one of the two incumbent carriers. North Central filed for exemption authority to take over the two routes. The Board has not acted on this yet.

In the deregulated environment, certain operating restrictions are no longer applicable. The CAB has stated that requests may be made for gradual removal of those restrictions. North Central responded by asking for approval of single-plane service from Denver to Madison, Chicago and Detroit; nonstops on Denver-Milwaukee and Twin Cities-Madison routes; and turnaround flights between Minneapolis/St. Paul and Chicago.

The airline still has a number of cases pending before the CAB. Decisions could be reached this year on Minneapolis/St. Paul to Phoenix and to Las Vegas, Twin Cities-Dallas/Fort Worth/Houston, Milwaukee-Toronto, Detroit-Montreal and service to the Caribbean.

For many years, North Central vigorously worked on route expansion. Through the company's efforts and provisions of the Deregulation Act, the airline can now pursue system growth opportunities to the full extent of its resources.



North Central's ticket counter is easily identified in the new terminal at Baltimore Washington International Airport. The company inaugurated Detroit-Baltimore service in August 1978.



Tropical beaches and warm sunshine attract thousands of passengers to North Central's new Florida cities—Tampa/St. Petersburg, Sarasota/Bradenton, West Palm Beach, Fort Lauderdale and Miami.

## the future

An exciting new era has begun. North Central has received long-sought routes to destinations which attract winter vacationers, and the merger with Southern Airways opens new vistas.

Continuing as North Central, or combined as Republic Airlines, the company will develop existing routes and enter new markets. With the expanded route structure, passenger demand should become more constant, rather than

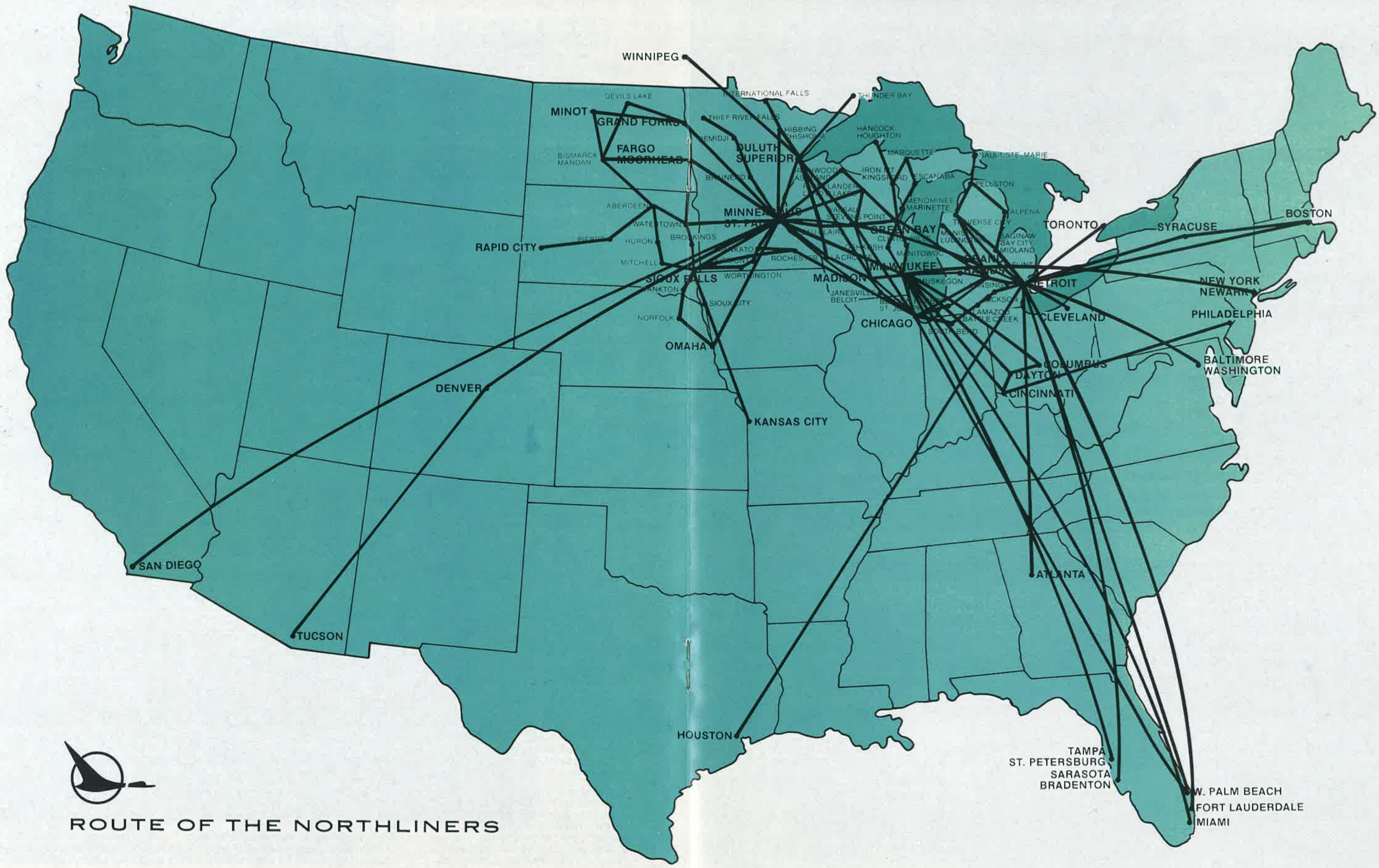
fluctuating by seasons. This permits greater utilization of aircraft, higher productivity from employees, and a broader base for fixed costs. Collectively, these factors should enhance profits.

In the current regulatory environment, the airline can add at least one new route each year. With the guaranteed annual selection—plus routes from conventional hearings, removal of restrictions, or dormant authority—orderly growth can be accomplished.

The financial strength of North Central enables it to be a viable competitor in lucrative markets. Success will be achieved by adhering to the company's fundamental objective of providing safe, dependable airline service.

The name North Central may fade into history, but the type of people who built its reputation will still be the key to the airline's future. Their loyalty and dedicated service assure further progress in the years ahead.





ROUTE OF THE NORTHLINERS



# NORTH CENTRAL AIRLINES, INC.



## balance sheets

	December 31	
	1978	1977
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and short-term investments (note B) .....	\$ 21,652,000	\$ 12,243,000
Accounts receivable, less allowances .....	30,331,000	25,696,000
Flight equipment parts and supplies (notes A and B) .....	6,817,000	6,233,000
Prepaid expenses and other (note A) .....	8,609,000	7,570,000
	<u>67,409,000</u>	<u>51,742,000</u>
<b>PROPERTY AND EQUIPMENT – at cost (notes A, B, C and D)</b>		
Flight equipment .....	237,171,000	185,307,000
Ground property and equipment .....	35,061,000	30,914,000
Improvements to leased property .....	7,256,000	6,052,000
	<u>279,488,000</u>	<u>222,273,000</u>
Less accumulated depreciation and amortization .....	<u>73,960,000</u>	<u>75,835,000</u>
	205,528,000	146,438,000
Advance payments on equipment .....	24,976,000	12,413,000
	<u>230,504,000</u>	<u>158,851,000</u>
<b>DEFERRED CHARGES AND OTHER ASSETS</b>		
Unamortized development costs (note A) .....	2,912,000	1,876,000
Rentals and other (notes A and C) .....	2,158,000	1,982,000
	<u>5,070,000</u>	<u>3,858,000</u>
	<u>\$302,983,000</u>	<u>\$214,451,000</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Current maturities of long-term debt (note B) .....	\$ 15,828,000	\$ 20,410,000
Short-term notes payable (note B) .....	4,000,000	–
Accounts payable .....	15,074,000	9,241,000
Interline payables and tickets outstanding (note A) .....	17,484,000	12,198,000
Accrued compensation and other expenses .....	18,583,000	14,036,000
Income taxes (notes A and I) .....	1,022,000	441,000
	<u>71,991,000</u>	<u>56,326,000</u>
<b>LONG-TERM OBLIGATIONS</b>		
Long-term debt – less current maturities (note B) .....	133,350,000	83,635,000
Deferred income taxes (notes A and I) .....	7,668,000	4,816,000
Other .....	362,000	394,000
	<u>141,380,000</u>	<u>88,845,000</u>
<b>COMMITMENTS (notes C, D and L)</b>		
	–	–
<b>STOCKHOLDERS' EQUITY (notes B, E and L)</b>		
Common stock – authorized 16,000,000 shares of \$.20 par value ...	2,500,000	2,493,000
Additional paid-in capital .....	18,344,000	18,210,000
Retained earnings .....	69,148,000	48,957,000
Treasury stock – at cost .....	(380,000)	(380,000)
	<u>89,612,000</u>	<u>69,280,000</u>
	<u>\$302,983,000</u>	<u>\$214,451,000</u>

The accompanying notes are an integral part of these statements.

## statements of earnings

	Year ended December 31	
	1978	1977
<b>OPERATING REVENUES</b>		
Passenger (note A) .....	\$248,596,000	\$186,641,000
Freight and express .....	19,744,000	13,680,000
Public service revenues (note F) .....	12,196,000	13,079,000
Mail (notes A and G) .....	3,983,000	4,932,000
Non-scheduled service and other .....	14,534,000	10,791,000
	<u>299,053,000</u>	<u>229,123,000</u>
<b>OPERATING EXPENSES</b>		
Flying operations .....	84,047,000	68,348,000
Maintenance .....	32,171,000	29,337,000
Aircraft and traffic servicing .....	61,137,000	50,978,000
Passenger service .....	19,505,000	14,605,000
Reservations, advertising and sales .....	29,377,000	20,999,000
General and administrative .....	14,552,000	10,801,000
Other transport-related expenses .....	1,163,000	930,000
Depreciation and amortization (note A) .....	16,353,000	14,590,000
Mutual Aid payments .....	5,645,000	–
	<u>263,950,000</u>	<u>210,588,000</u>
Operating profit .....	35,103,000	18,535,000
<b>OTHER EXPENSES (INCOME)</b>		
Interest expense .....	11,783,000	7,781,000
Less interest capitalized (note A) .....	1,917,000	832,000
	<u>9,866,000</u>	<u>6,949,000</u>
Interest income and other – net .....	(1,532,000)	(409,000)
(Gain) loss on disposition of equipment .....	50,000	(2,705,000)
	<u>8,384,000</u>	<u>3,835,000</u>
Earnings before income taxes .....	26,719,000	14,700,000
<b>INCOME TAXES (notes A and I)</b>		
Current .....	1,677,000	745,000
Deferred .....	2,878,000	259,000
	<u>4,555,000</u>	<u>1,004,000</u>
NET EARNINGS .....	<u>\$ 22,164,000</u>	<u>\$ 13,696,000</u>
NET EARNINGS PER SHARE AND EQUIVALENT SHARE (note J) .....	<u>\$1.70</u>	<u>\$1.11</u>

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	
	1978	1977
<b>SOURCES</b>		
From operations		
Net earnings	\$ 22,164,000	\$13,696,000
Charges to earnings not using working capital		
Depreciation and amortization	16,353,000	14,590,000
Deferred income taxes	2,852,000	111,000
Other	900,000	108,000
Working capital provided from operations	42,269,000	28,505,000
Net book value of equipment dispositions	4,395,000	3,003,000
Increase in long-term debt	66,726,000	24,978,000
Reduction of rentals and other	275,000	578,000
	<u>113,665,000</u>	<u>57,064,000</u>
<b>APPLICATIONS</b>		
Additions to property and equipment	92,490,000	39,100,000
Reduction of long-term debt	17,011,000	21,410,000
Payment of cash dividend	1,973,000	1,479,000
Additions to deferred charges	2,189,000	1,239,000
	<u>113,663,000</u>	<u>63,228,000</u>
INCREASE (DECREASE) IN WORKING CAPITAL	2,000	(6,164,000)
Working capital (deficit) at beginning of year	(4,584,000)	1,580,000
Working capital (deficit) at end of year	<u>\$ (4,582,000)</u>	<u>\$ (4,584,000)</u>

### NET CHANGE IN WORKING CAPITAL ELEMENTS

Increase in current assets		
Cash and short-term investments	\$ 9,409,000	\$ 3,209,000
Accounts receivable	4,635,000	6,651,000
Flight equipment parts and supplies	584,000	733,000
Prepaid expenses and other	1,039,000	295,000
Net change in current assets	<u>15,667,000</u>	<u>10,888,000</u>
Increase (decrease) in current liabilities		
Current maturities of long-term debt and short-term notes	(582,000)	10,128,000
Accounts payable	5,833,000	1,416,000
Interline payables and tickets outstanding	5,286,000	2,159,000
Accrued compensation and other expenses	4,547,000	3,186,000
Income taxes	581,000	163,000
Net change in current liabilities	<u>15,665,000</u>	<u>17,052,000</u>
INCREASE (DECREASE) IN WORKING CAPITAL	<u>\$ 2,000</u>	<u>\$ (6,164,000)</u>

The accompanying notes are an integral part of these statements.

## statements of changes in stockholders' equity

Years ended December 31, 1978 and 1977

	Common Stock		Additional Paid-In Capital	Retained Earnings (note B)	Treasury Stock	
	Shares Issued	Amount			Shares Held	Amount
Balance at January 1, 1977	12,462,752	\$2,493,000	\$18,056,000	\$36,740,000	285,034	\$804,000
Cash dividend (note E)	-	-	-	(1,479,000)	-	-
Disposition of treasury stock	-	-	154,000	-	(150,440)	(424,000)
Net earnings for the year 1977	-	-	-	13,696,000	-	-
Balance at December 31, 1977	<u>12,462,752</u>	<u>2,493,000</u>	<u>18,210,000</u>	<u>48,957,000</u>	<u>134,594</u>	<u>380,000</u>
Cash dividend (note E)	-	-	-	(1,973,000)	-	-
Exercise of stock options	28,300	5,000	83,000	-	-	-
Conversion of warrants	9,573	2,000	51,000	-	-	-
Net earnings for the year 1978	-	-	-	22,164,000	-	-
Balance at December 31, 1978	<u>12,500,625</u>	<u>\$2,500,000</u>	<u>\$18,344,000</u>	<u>\$69,148,000</u>	<u>134,594</u>	<u>\$380,000</u>

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  
North Central Airlines, Inc.

We have examined the balance sheets of North Central Airlines, Inc. (a Wisconsin corporation) as of December 31, 1978 and 1977, 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 North Central Airlines, Inc., at December 31, 1978 and 1977, 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 22, 1979



## notes to financial statements

December 31, 1978 and 1977 (continued)

vanced \$16,185,000 and capitalized interest of \$693,000. An additional \$50,539,000 will be expended by the company in fulfilling these commitments prior to delivery in 1979. The company has arranged leveraged lease financing for the three aircraft to be delivered in the second quarter of 1979.

The company has advanced \$4,227,000 and capitalized interest of \$39,000 on a purchase commitment for three Boeing 727-200 aircraft to be delivered in 1980 and options on four additional aircraft to be delivered in 1980 and 1981 which contain options to cancel prior to July 1979. If the options to cancel are not exercised, an additional \$99,848,000 will be expended prior to delivery.

In November 1978 the company assumed Southern Airways, Inc. (note L) purchase agreement for four new DC-9-50 aircraft for delivery in 1980 and options for two additional aircraft to be delivered in 1980 which can be cancelled prior to July 1979. The company reimbursed Southern \$3,078,000 including capitalized interest of \$262,000. If the options to cancel are not exercised, an additional \$56,051,000 will be expended prior to delivery.

In January 1979 the company signed a letter of intent to purchase four new DC-9-80 aircraft and obtained options on four additional aircraft. The letter includes provisions for cancellation of the order. The company has advanced \$700,000 and capitalized interest of \$7,000 and, if the order is not canceled, will expend an additional \$103,889,000 prior to delivery in 1981.

**Note E—Common Stock**—At December 31, 1978, 61,250 shares of unissued common stock are reserved for officers and key employees, under a qualified plan adopted in 1965. An additional 197,900 shares are reserved under a plan adopted in 1975.

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.

All options granted expire five years after date of granting. There were 68,900 shares under the 1975 plan available for granting at December 31, 1978.

The following tables summarize information relating to the options outstanding:

Year Granted	Per Share	Option Price and Fair Market Value at Date of Grant			
		December 31, 1978		December 31, 1977	
		Shares	Amount	Shares	Amount
1973	\$4.25	—	\$ —	7,500	\$ 31,875
1974	3.375	8,000	27,000	8,525	28,772
1974	2.75	53,250	146,438	71,425	196,419
		61,250	173,438	87,450	257,066
1975	2.50	92,900	232,250	95,000	237,500
1976	3.875	36,100	139,888	36,100	139,888
		129,000	372,138	131,100	377,388
		190,250	\$545,576	218,550	\$634,454

Year Exercisable	Per Share	Fair Market Value at Date Exercisable			
		December 31, 1978		December 31, 1977	
		Shares	Amount	Shares	Amount
1973	\$4.25	—	\$ —	7,500	\$ 31,875
1974	3.375	8,000	27,000	8,525	28,772
1974	2.75	20,375	56,031	26,425	72,669
1975	3.00	30,750	92,250	42,500	127,500
1977	4.25	2,125	9,031	2,500	10,625
		61,250	184,312	87,450	271,441
1975	2.50	90,400	226,000	92,500	231,250
1976	3.875	35,125	136,110	35,125	136,110
1977	4.25	3,475	14,769	3,475	14,769
		129,000	376,879	131,100	382,129
		190,250	\$561,191	218,550	\$653,570

The following table summarizes information relating to options exercised during 1978 (no options were exercised during 1977):

Year Granted	Shares	Option Price		Fair Market Value	
		Per Share	Amount	Per Share	Amount
1973	7,500	\$4.25	\$31,875	\$7.125-\$8.625	\$ 59,374
1974	525	3.375	1,772	7.00	3,675
1974	18,175	2.75	49,981	7.125- 8.125	134,697
	26,200		83,628		197,746
1975	2,100	2.50	5,250	7.00 - 7.625	14,888
	28,300		\$88,878		\$212,634

At December 31, 1978 and 1977, there were outstanding warrants to purchase 2,639,488 and 2,649,061 shares of common stock, respectively. These warrants resulted from public offerings prior to 1973 and from financial transactions as discussed in note B(d). All warrants enable the holder to purchase common stock at \$5.50 per share and must be exercised by October 31, 1979.

During January 1979, the Board of Directors declared a \$ .20 per share dividend payable March 1, 1979 to shareholders of record, on February 15, 1979. The company paid cash dividends of \$.16 and \$.12 per share to its shareholders during the first quarter of 1978 and 1977, respectively.

**Note F—Public Service Revenues**—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. Public service revenues for the period January 1, 1978 through June 30, 1978 were computed and paid under the provisions of Class Rate VIII, which had been in effect since July 1, 1976. The CAB has proposed Class Rate IX to become effective July 1, 1978, however, a joint objection to some of the provisions of this rate has been filed by the regional airlines, and at

this time no final rule making has been issued by the Board. Estimates of revenues due under the new rate were based upon figures proposed by the CAB as they affect North Central. Class Rate IX and subsequent rates were affected by the Airline Deregulation Act of 1978 with respect to the offsetting of certain revenues not relating to subsidy-eligible services. Effective October 24, 1978, non-related revenues may not be offset against a carrier's need on the eligible portion of its system.

**Note G—Mail Revenue**—In December 1977 the CAB issued an order establishing new temporary mail rates in connection with its Domestic Service Mail Rates Investigation. As a result of this order the company recognized \$2,733,000 of additional revenue in 1977. Approximately \$1,932,000 of this retroactive amount applies to the period March 28, 1973 through December 31, 1976. In November 1978 the final rates were established with no adjustment in revenue for the company.

**Note H—Pension Costs**—Total pension expense was \$7,703,000 for 1978 and \$6,346,000 for 1977. At January 1, 1978, the latest actuarial valuation date, the total market value of fund assets exceeded the actuarially computed value of vested benefits by \$2,691,000 for all plans.

**Note I—Income Taxes**—Income tax expense for the years ended December 31 consists of the following:

	1978	1977
Current income taxes		
Federal	\$11,747,000	\$6,065,000
Investment tax credit used		
in current year	(11,412,000)	(6,065,000)
	335,000	—
State and local	1,342,000	745,000
	1,677,000	745,000
Deferred income taxes		
Federal	1,008,000	1,046,000
Investment tax credit	1,795,000	(898,000)
	2,803,000	148,000
State and local	75,000	111,000
	2,878,000	259,000
	\$ 4,555,000	\$1,004,000

Income taxes of \$4,555,000 in 1978 and \$1,004,000 in 1977 (effective rates of 17.0% and 6.8% respectively) are less than those expected to result by application of the federal income tax rate of 48% to income before taxes. The reasons for these differences are:

	1978	1977
Computed "expected" tax expense	\$12,825,000	\$7,056,000
Increase (decrease) in income taxes		
Investment tax credit utilized	(9,617,000)	(6,963,000)
State and local income taxes net of federal income tax benefit	1,417,000	856,000
Other	(70,000)	55,000
	\$ 4,555,000	\$1,004,000

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

	1978	1977
Increase (decrease) in deferred income tax expense		
Capitalized interest	\$ 821,000	\$ 328,000
Investment tax credit	1,795,000	(898,000)
Other	262,000	829,000
	\$ 2,878,000	\$ 259,000

For federal income tax reporting purposes, investment tax credits of \$932,000 are available to offset future income taxes payable through 1985. This amount has been recognized for financial reporting purposes as an offset to deferred income taxes payable through December 31, 1978.

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): 1977 and 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, 1977.

**Note J—Net Earnings Per Share**—Net earnings per share for 1978 is based on the weighted average number of common and common equivalent shares outstanding (13,027,063). Common equivalent shares result from the assumed exercise of stock options and warrants using the "treasury stock" method.

Net earnings per share for 1977 is based on the weighted average number of shares outstanding for the year (12,328,158). 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 year ended December 31, 1977.

For the years 1978 and 1977 fully diluted earnings per share are the same as primary earnings per share.

**Note K—Selected Financial Data (unaudited)**—The unaudited quarterly results of operations for each of the four quarters ended in 1978 and 1977 and the unaudited asset replacement cost information are presented on page 24 of this annual report and are incorporated by reference into this note.

**Note L—Proposed Merger**—On September 5, 1978, the company and Southern Airways, Inc. executed an Agreement and Plan of Merger containing the definitive terms and conditions of the merger of Southern with and into the company. The Merger Agreement provides a formula which results in the conversion of one share of Southern common stock, exchanged on the effective date of the merger, for 2.1 shares of the company's stock. On February 9, 1979, a Civil Aeronautics Board Law Judge issued an initial decision favoring the merger. Consummation of the merger is subject to the approval of lenders, the CAB and the President of the United States.



## supplemental stockholder information

### Quarterly Statements of Earnings

(unaudited—in thousands of dollars)

	1978 Three Months Ended				1977 Three Months Ended			
	December 31	September 30	June 30	March 31	December 31	September 30	June 30	March 31
<b>OPERATING REVENUES</b>								
Passenger .....	\$64,005	\$72,370	\$64,667	\$47,554	\$48,319	\$51,970	\$45,926	\$40,426
Public service revenues .....	2,533	2,870	3,398	3,395	3,358	3,356	3,231	3,134
Other .....	9,777	8,860	9,153	10,471	10,250	6,607	6,302	6,244
	<u>76,315</u>	<u>84,100</u>	<u>77,218</u>	<u>61,420</u>	<u>61,927</u>	<u>61,933</u>	<u>55,459</u>	<u>49,804</u>
<b>OPERATING EXPENSES</b>								
Flying operations and maintenance ..	30,677	29,499	28,652	27,390	25,752	25,432	23,684	22,817
Other operating expenses .....	32,818	35,491	35,734	27,336	26,733	25,424	23,825	22,331
Depreciation and amortization .....	4,587	4,079	3,800	3,887	3,838	3,832	3,595	3,325
	<u>68,082</u>	<u>69,069</u>	<u>68,186</u>	<u>58,613</u>	<u>56,323</u>	<u>54,688</u>	<u>51,104</u>	<u>48,473</u>
<b>OPERATING PROFIT</b> .....	<u>8,233</u>	<u>15,031</u>	<u>9,032</u>	<u>2,807</u>	<u>5,604</u>	<u>7,245</u>	<u>4,355</u>	<u>1,331</u>
<b>OTHER EXPENSES (INCOME)—net</b> .....	<u>2,337</u>	<u>2,357</u>	<u>1,698</u>	<u>1,992</u>	<u>1,986</u>	<u>1,721</u>	<u>1,401</u>	<u>(1,273)</u>
<b>EARNINGS BEFORE INCOME TAXES</b> .....	<u>5,896</u>	<u>12,674</u>	<u>7,334</u>	<u>815</u>	<u>3,618</u>	<u>5,524</u>	<u>2,954</u>	<u>2,604</u>
Income taxes .....	1,773	2,308	419	55	297	337	189	181
<b>NET EARNINGS</b> .....	<u>\$ 4,123</u>	<u>\$10,366</u>	<u>\$ 6,915</u>	<u>\$ 760</u>	<u>\$ 3,321</u>	<u>\$ 5,187</u>	<u>\$ 2,765</u>	<u>\$ 2,423</u>
<b>NET EARNINGS PER SHARE</b>								
Primary .....	<u>\$.31</u>	<u>\$.77</u>	<u>\$.54</u>	<u>\$.06</u>	<u>\$.27</u>	<u>\$.42</u>	<u>\$.22</u>	<u>\$.20</u>
Fully diluted .....	<u>\$.31</u>	<u>\$.76</u>	<u>\$.53</u>	<u>\$.06</u>	<u>\$.27</u>	<u>\$.42</u>	<u>\$.22</u>	<u>\$.20</u>
<b>DIVIDENDS PER SHARE</b> .....	<u>-</u>	<u>-</u>	<u>-</u>	<u>\$.16</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>\$.12</u>

### STOCKHOLDER'S 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 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 1979 and three in 1980. 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, Secretary, North Central Airlines, 7500 Northliner 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.

	1978		1977	
	High	Low	High	Low
1st Quarter .....	5 $\frac{7}{8}$	4 $\frac{5}{8}$	4 $\frac{1}{8}$	3 $\frac{5}{8}$
2nd Quarter .....	7 $\frac{7}{8}$	5 $\frac{5}{8}$	4 $\frac{1}{2}$	3 $\frac{3}{8}$
3rd Quarter .....	11 $\frac{7}{8}$	6 $\frac{3}{4}$	4 $\frac{1}{2}$	3 $\frac{3}{8}$
4th Quarter .....	10	6	5	3 $\frac{3}{8}$

### ASSET REPLACEMENT COST (unaudited)

Replacing productive capacity of the airline with assets having equivalent capacity has generally required greater capital investment than was required to purchase the assets being replaced. The additional capital investment principally reflects the cumulative impact of inflation during the relatively long lives of the assets (10 to 15 years in the case of flight equipment).

The company's annual report on Form 10-K contains (1) additional quantitative information with respect to the estimated replacement cost of flight equipment parts and supplies and of property and equipment on December 31, 1978 and 1977, and (2) the related estimated effect of such replacement costs on depreciation expense.

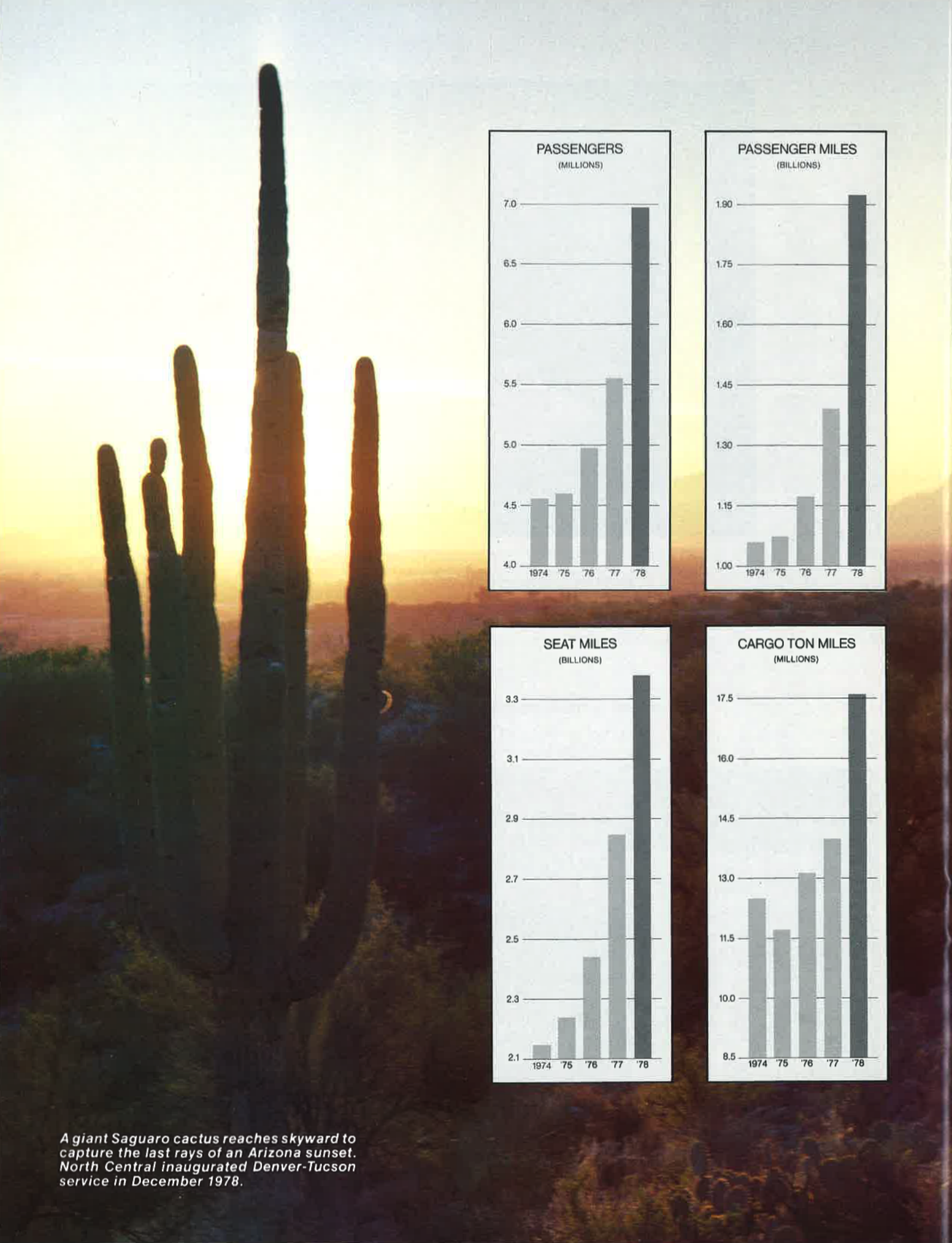


Robert Neumeier and Suzanne Wheeler review the company's stockholder relations program. Each new stockholder receives a personal message of welcome as a part owner of the airline. The letter summarizes the company's performance in the past year and encourages comments or suggestions. Enclosed are the current financial report and flight schedule, along with a card for requesting future schedules and the inflight Northliner Magazine.

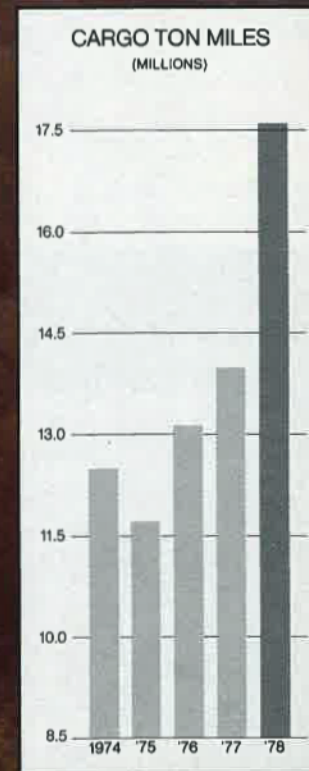
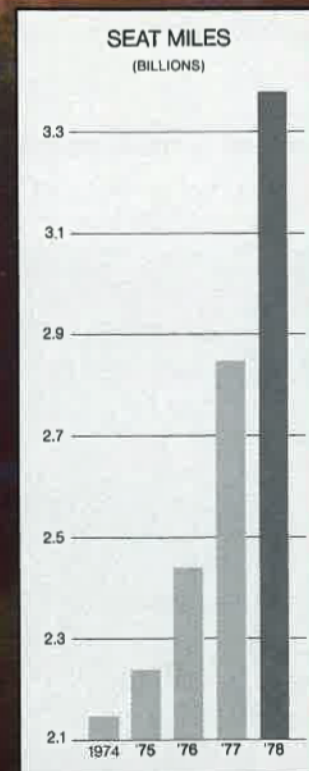
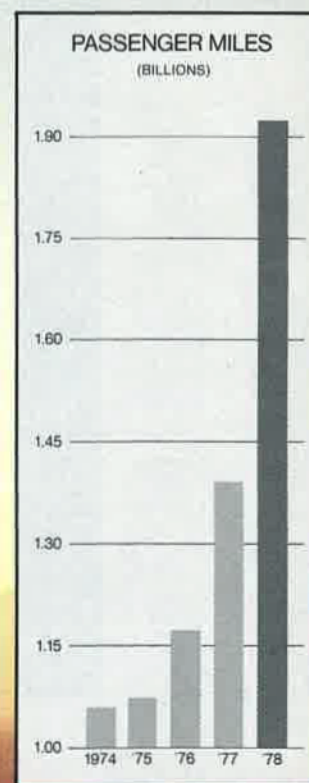
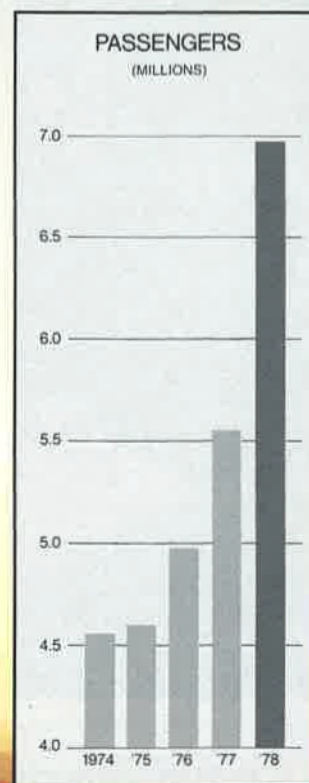


The 1977 North Central Annual Report earned awards from Financial World magazine and the National Association of Investment Clubs.





A giant Saguaro cactus reaches skyward to capture the last rays of an Arizona sunset. North Central inaugurated Denver-Tucson service in December 1978.



## five-year summary

### EARNINGS

	1978	1977	1976	1975	1974
<b>OPERATING REVENUES</b>					
Passenger .....	\$248,596,000	\$186,641,000	\$157,159,000	\$135,664,000	\$124,007,000
Public service revenues .....	12,196,000	13,079,000	13,296,000	12,225,000	12,126,000
Other .....	38,261,000	29,403,000	20,693,000	15,735,000	15,397,000
	<u>299,053,000</u>	<u>229,123,000</u>	<u>191,148,000</u>	<u>163,624,000</u>	<u>151,530,000</u>
<b>OPERATING EXPENSES</b>					
Flying operations and maintenance .....	116,218,000	97,685,000	83,291,000	73,358,000	57,544,000
Other operating expenses .....	131,379,000	98,313,000	81,533,000	72,402,000	65,304,000
Depreciation and amortization .....	16,353,000	14,590,000	11,635,000	10,131,000	9,975,000
	<u>263,950,000</u>	<u>210,588,000</u>	<u>176,459,000</u>	<u>155,891,000</u>	<u>132,823,000</u>
<b>OPERATING PROFIT</b> .....	<u>35,103,000</u>	<u>18,535,000</u>	<u>14,689,000</u>	<u>7,733,000</u>	<u>18,707,000</u>
<b>OTHER EXPENSES (INCOME)</b>					
Interest expense .....	11,783,000	7,781,000	5,503,000	4,084,000	4,515,000
Capitalized interest .....	(1,917,000)	(832,000)	(843,000)	(757,000)	(341,000)
Interest income and other-net .....	(1,532,000)	(409,000)	(501,000)	(540,000)	(1,213,000)
(Gain) loss on disposition of equipment .....	50,000	(2,705,000)	(189,000)	23,000	(16,000)
	<u>8,384,000</u>	<u>3,835,000</u>	<u>3,970,000</u>	<u>2,810,000</u>	<u>2,945,000</u>
<b>EARNINGS BEFORE INCOME TAXES</b> .....	<u>26,719,000</u>	<u>14,700,000</u>	<u>10,719,000</u>	<u>4,923,000</u>	<u>15,762,000</u>
Income taxes .....	4,555,000	1,004,000	3,040,000	(328,000)	7,512,000
<b>NET EARNINGS</b> .....	<u>\$ 22,164,000</u>	<u>\$ 13,696,000</u>	<u>\$ 7,679,000</u>	<u>\$ 5,251,000</u>	<u>\$ 8,250,000</u>
<b>NET EARNINGS PER SHARE AND EQUIVALENT SHARE</b> .....	\$1.70	\$1.11	\$ .63	\$ .43	\$ .67
<b>DIVIDENDS PER SHARE</b> .....	\$ .16	\$ .12	\$ .10	\$ .10	\$ .10

### BALANCE SHEET ITEMS

Current assets .....	\$ 67,409,000	\$ 51,742,000	\$ 40,854,000	\$ 34,178,000	\$ 38,758,000
Working capital from operations .....	\$ 42,269,000	\$ 28,505,000	\$ 21,217,000	\$ 14,854,000	\$ 20,788,000
Property and equipment-net .....	\$230,504,000	\$158,851,000	\$137,410,000	\$101,563,000	\$ 83,279,000
Total long-term debt .....	\$133,350,000	\$ 83,635,000	\$ 80,067,000	\$ 50,124,000	\$ 38,194,000
Retained earnings .....	\$ 69,148,000	\$ 48,957,000	\$ 36,740,000	\$ 30,259,000	\$ 26,236,000
Stockholders' equity .....	\$ 89,612,000	\$ 69,280,000	\$ 56,485,000	\$ 49,785,000	\$ 46,344,000
Shares outstanding .....	12,366,000	12,328,000	12,178,000	12,098,000	12,312,000
Book value per share .....	\$7.25	\$5.62	\$4.64	\$4.12	\$3.76

### STATISTICS

Passengers .....	6,911,000	5,547,000	4,969,000	4,581,000	4,546,000
Passenger miles (000) .....	1,925,000	1,392,000	1,179,000	1,072,000	1,061,000
Available seat miles (000) .....	3,385,000	2,861,000	2,444,000	2,235,000	2,151,000
Passenger load factor .....	56.9%	48.7%	48.2%	48.0%	49.3%
Cargo ton miles .....	17,619,000	13,998,000	13,052,000	11,703,000	12,585,000
Revenue plane miles .....	36,874,000	33,343,000	30,810,000	29,748,000	29,055,000
Number of employees .....	4,460	3,850	3,600	3,410	3,360



## communications

North Central's advertising and promotion activity highlighted the vast number of new routes inaugurated in 1978.

A combination of television and radio commercials, colorful newspaper and magazine ads, outdoor displays, and sales materials informed and attracted the public to 13 new North Central cities. Each campaign was designed to promote the airline's image of quality service, while pointing out special passenger benefits.

Comprehensive advertising was also devoted to the company's "Super Saver" fare (savings up to 40 percent of standard fare) which played an important role in the remarkable traffic and revenue growth in 1978. The "Summer Sun Times" promotion increased vacation travel to Denver, New York City, Toronto, New England and the Canadian Wilderness. Ads in Sunday newspaper travel sections and The Wall Street Journal were reinforced by radio commercials at peak rush-hour traffic periods.

An "I Love New York" campaign premiered in Milwaukee during October. Members from the cast of "Grease," popular Broadway musical, performed show numbers for 400 travel agents and corporate travel people. The airline is offering 16 theater package tours to complement its New York service.

Information about the proposed North Central/Southern merger was summarized in two booklets used by officials of both carriers in visits with business and civic leaders. The literature pointed out the merger benefits to North Central and Southern cities, to investors, and employees.

The National Association of Investment Clubs presented North Central with the 1978 Nicholson Award for producing the industry's best 1977 Annual Report. For the sixth consecutive year, *Financial World* magazine recognized the excellence of the company's Annual Report with a Merit Award.

"Travel Unraveled," a unique 56-page booklet produced by North Central, informs passengers on all facets of air transportation—reservations, baggage service, and tips on traveling with youngsters, pets and sports equipment.

*Northliner Magazine*, the popular inflight periodical, went monthly in January 1979. Now in its eleventh year, the magazine provides North Central passengers with stimulating articles about people, places and events, plus a feature on the company.

Some 46 news releases were issued during 1978, disseminating information on monthly traffic and

financial results. Special stories, receptions and press conferences promoted North Central and its new routes. Each quarter, corporate officers held meetings with business writers and financial analysts.

"The Northliner" newspaper keeps the 4,500 employees up-to-date about the company, their fellow workers and industry matters. It has been a consistent award winner among airline employee publications.

The company sales staff made 27,000 personal calls on travel agencies and businesses with frequent air travelers. Also, North Central employees participated in 1,700 civic, industry and special interest functions as guest speakers or members.

The airline's general office and main operations base in Minneapolis/St. Paul attracts thousands of visitors. Over 6,700 persons, many of them students, were given guided tours of the facilities in 1978. Public events held in the employee cafeteria provided 12,000 additional guests with a look at company headquarters.

North Central continues to benefit from the efforts and support of countless friends and boosters throughout its system. These endeavors are a valuable contribution to the airline's progress.

# NEW! PHILADELPHIA NONSTOPS

Try something new to Philadelphia... the warm, personal service of North Central Airlines.

Return from Philadelphia on our early afternoon nonstop and enjoy a great snack... anything from a hearty sandwich to a crab hors d'oeuvre tray or garden-fresh chef's salad... all complemented by delicious French pastry.

Or return in the morning and sit down to a fantastic Country-Style Breakfast... steak and eggs, hash browns, pastry and more. You'll also enjoy a brunch snack on our morning nonstop from here to Philadelphia.

Relax in roomy 2-3 seating with plenty of leg room. Everything is single class service—the best for everyone, so nobody flies second class.

Ask how to save up to 40% on round-trip air fare with our Super Saver Fare. But hurry, because seating is limited.

**40% OFF**

## FLY NORTH CENTRAL STYLE

### NONSTOP TO PHILADELPHIA

Lv Cincinnati	Ar Philadelphia
10:50 a.m.	12:09 p.m.
7:40 p.m.	8:59 p.m.
Lv Philadelphia	Ar Cincinnati
7:00 a.m.	8:32 a.m.
1:10 p.m.	2:42 p.m.

Call your travel agent or 513-621-3264.

North Central is located in Terminal C at the Philadelphia International Airport.

## NORTH CENTRAL AIRLINES

GOOD PEOPLE MAKE OUR AIRLINE GREAT



(Open on animation of Atlanta nonstop.)



ANNCR: "Do you feel that a flight to Atlanta is just a plane ride?"



"Then relax on North Central! You'll be greeted by real people with warm smiles."



"Sample a hearty country-style breakfast on our morning nonstop to Atlanta."



"Or perhaps a delicious London broil dinner in the evening... with complimentary wine."



"You'll like our style... on all four nonstops to Atlanta."  
SINGERS: "Fly North Central..."

North Central Flight Attendants Carole Darin, Charlene McCarty, Faye Beilke and Martine Anderson were featured in TV commercials promoting the airline's new service to Atlanta, Philadelphia and Baltimore.





NORTH CENTRAL AIRLINES, INC.  
7500 NORTHLINER DRIVE • MINNEAPOLIS, MINNESOTA 55450