

NORTHWEST AIRLINES, INC.

ANNUAL REPORT

TO STOCKHOLDERS



YEAR ENDED

JUNE 30, 1939

NORTHWEST AIRLINES, INC.

Saint Paul, Minnesota
September 30, 1939

TO THE STOCKHOLDERS OF NORTHWEST AIRLINES, INC.

Following is the Annual Statement of your company for the fiscal year ended June 30, 1939. You will find that the company sustained a loss of \$123,315.84, but notwithstanding this the financial position of the company at the end of the year was greatly improved.

The Profit and Loss Statement indicates considerable increase in the volume of business done in all departments. The increase of \$338,732 in mail revenue results mostly from a change in our rates of mail pay. We applied to the Civil Aeronautics Authority for an increase in mail pay on November 22, 1938 and a decision was rendered in June, 1939, fixing new mail rates retroactive to the date of our petition. During the fiscal year this increase amounted to approximately \$208,000 and for the coming year is estimated at \$350,000.

Passenger revenues increased \$202,850 due to the introduction of Douglas DC-3 21-passenger airplanes in the spring of 1939, to the increased popularity of air travel and to general improvement in our service and facilities.

The increase of \$750,906 in operating expenses was caused by improvement of our service, by continued high maintenance costs, and by the increased cost of operating Douglas ships in the latter part of the year.

Although the year's operations resulted in a net loss, this loss was only about 32% of our depreciation, as a result of which the current position of the company showed considerable improvement. Both the cost and depreciated values of the company's physical property increased as a result of the replacement of Lockheed Zephyr planes with Douglas DC-3s.

Early in the year it became evident that, with the trend in air travel, it was imperative that we put ourselves in a position to carry the increased loads expected. The Lockheed Aircraft Corporation, which was experiencing a heavy demand for the Zephyr type of ship, entered into a very fair arrangement with us to repurchase our entire fleet of 10-passenger Zephyr planes, and, with the proceeds and a \$480,000 loan from the Reconstruction Finance Corporation, we were able to purchase six Douglas DC-3s, three of which were put into service in April and three more in June. A seventh ship of this type was on order at the end of the year and was received early in September, 1939. These new ships are of the latest type, complete with the latest in instruments and equipment, and are powered with Pratt & Whitney Twin-Row Wasp Engines, which give smoother operation and a greater reserve power than any engines previously used in this type of ship.

The response of the traveling public to the introduction of these ships has been very satisfactory. Passenger revenues in May, June, July, and August, 1939 showed an increase of 47%, 60%, 71%, and 71%, respectively, over the corresponding months of the previous year. The results of these months make it evident that passenger revenues for the new fiscal year will exceed the year just ended by a considerable amount.

In addition to the seven Douglas DC-3 airplanes now owned, the company also operates seven 10-passenger Lockheed Electras. Some of these are in use on one daily round trip schedule between Chicago and Seattle-Portland. It is our intent to replace these small ships on this schedule with Douglas DC-3s and for that purpose we have ordered four more DC-3s, three to be delivered in January and one in May, 1940.

During the year your company made application to the Civil Aeronautics Authority for Certificates of Convenience and Necessity on three proposed routes, and hearings have been held on all applications. One proposed route is from Milwaukee via certain Wisconsin points and Duluth to the Twin Cities. Another is from Chicago via certain Wisconsin points to Marquette, Michigan. Another is from the Twin Cities to St. Louis via Rochester and Des Moines. At the present time we do not know when decisions will be reached on these applications.

In August we filed with the Civil Aeronautics Authority notice of our intention to apply for a Certificate of Convenience and Necessity between Chicago and New York City by way of Toronto. This filing was made about the time that the governments of the United States and Canada completed arrangements for reciprocal international air service.

While the audited figures which follow are for the fiscal year ended June 30, the stockholders will be interested to know that for the first two months of the new fiscal year (July and August) the company made a profit of \$131,770, as compared with a loss of \$25,975 for the same period of the previous year. This improvement results from an increase in revenues of \$209,146 and an increase in expenses of only \$61,917 for the two months' period.

During the past two years your company's operations have been brought up to a high standard of service and our present fleet of ships, together with those now on order, place us in a good competitive position. Previous figures clearly show the rising trend in passenger revenues. Our results for the year ahead will depend largely on the extent to which the improvement in passenger business continues.

Very truly yours,

CROIL HUNTER
President

BALANCE SHEET
NORTHWEST AIRLINES, INC.

June 30, 1939

ASSETS

CURRENT ASSETS

Cash:

Demand deposits	\$ 93,105.68	
For deposit	20,185.32	
Agents working funds	2,158.99	\$ 115,449.99

Accounts receivable:

Due from U. S. and Canadian Governments:

Mail	\$387,284.62	
Tickets, etc.	5,905.31	\$ 393,189.93

Other ticket accounts:

Other airlines and agencies	\$ 96,073.68	
Scrip accounts	3,990.31	
Sundry	879.05	100,943.04

Gasoline tax refund claims	20,370.96	
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Other current accounts:

For services and supplies	\$ 19,193.85	
Insurance claim (paid in July, 1939)	22,870.09	42,063.94

Less reserve for doubtful accounts, adjustments, etc.	\$ 556,567.87	
	2,500.00	554,067.87

Inventories—at lower of cost or market:

Repair parts and supplies	\$ 66,854.19	
Gasoline and oil	13,291.87	80,146.06
		\$ 749,663.92

OTHER ASSETS

Marketable securities on deposit—Note A		\$ 33,792.63
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Accounts receivable:

Employees	\$ 8,652.04	
Officers	3,731.90	
Sundry	345.44	12,729.38

Sundry securities and deposits		2,605.00	49,127.01
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PROPERTY, PLANT AND EQUIPMENT—at cost to the Company of its predecessors less depreciation and amortization

Land		\$ 5,082.47	
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Airplanes and engines—Note B	\$1,449,747.54	
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Buildings and other equipment (including \$178,268.05 representing the cost of buildings situated on leased ground)	646,531.04	
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Less reserves for depreciation and amortization	\$2,096,278.58	
	941,042.06	1,155,236.52

Improvements to leased buildings less amortization		17,150.50	1,177,469.49
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INTANGIBLE

Cost of U. S. Government air mail route			48,736.69
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DEFERRED CHARGES

Prepaid insurance	\$ 37,187.60	
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Prepaid rent	19,795.35	
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Sundry prepaid and deferred items	4,597.14		61,580.09
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\$2,086,577.20

NOTES—

A—The Company is defendant in lawsuits arising from the accidental deaths of several persons. In the one case which has been tried, damages of \$37,500.00 were awarded the plaintiff but the case has been appealed by the Company. In connection with the appeal, the Company has filed a surety bond and has deposited marketable securities carried at \$33,792.63 with the bonding company pending disposition of the case. A second suit for \$10,000.00 arising from the same death has been filed but has not come to trial. The maximum coverage in this death is \$10,000.00.

Four other claims involving aggregate damages of \$63,000.00 in excess of insurance coverages are in litigation or in process of settlement. The management is of the opinion the four claims referred to will be settled without loss to the Company.

B—Six Douglas DC-3 airplanes complete with engines, propellers, radio installation and gyro pilots, seven spare Pratt and Whitney twin-row Wasp engines and six spare Hamilton Standard hydro-matic propellers are assigned under a chattel mortgage as security for the long term debt of \$476,214.19. The cost of the equipment mortgaged is \$870,719.54.

BALANCE SHEET
NORTHWEST AIRLINES, INC.

June 30, 1939

LIABILITIES

CURRENT LIABILITIES

Notes payable:

To banks	\$ 35,000.00	
To shareholders	20,000.00	\$ 55,000.00

Accounts payable:

For equipment, supplies, etc.	\$ 173,233.57	
For transportation sold over other lines.....	51,155.61	
Scrip deposits	27,568.05	
Pay roll taxes	14,201.92	
Salaries and wages	8,015.16	
Employees accounts	2,681.47	276,855.78

Accrued:

Local taxes	\$ 17,347.50	
Federal capital stock tax	2,800.00	
Legal fees (estimated)	15,000.00	
Interest	2,102.30	37,249.80

Federal and state taxes on income—estimated:

Provision for possible additional assessments for prior year		2,462.10
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Current maturities of long term debt—estimated	80,432.72	\$ 452,000.40
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LONG TERM DEBT—Note B

5% note secured by chattel mortgage on equipment carried at \$870,719.54—principal and interest payable in installments of \$12,400.00 monthly beginning November 3, 1939, balance due May 3, 1943		\$ 480,000.00
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Less: Balance of proceeds received in August, 1939.....	\$ 3,785.81	
Portion included in current liabilities	80,432.72	395,781.47

DEFERRED INCOME

Unused tickets		21,475.91
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CAPITAL

Preferred stock—5% cumulative, \$100.00 par value, convertible into common stock on the basis of ten shares of common for each share of preferred, redeemable at \$103.00 per share plus unpaid accumulated dividends:

Authorized—6,000 shares	\$ 600,000.00	
Less: Retired	\$501,000.00	
Unissued	50,000.00	\$ 49,000.00

Common stock—no par value:

Authorized—300,000 shares		
Unissued—69,940 shares of which 4,900 shares are reserved for conversion of outstanding preferred shares		
Outstanding—230,060 shares—aggregate stated capital amount		1,310,600.00

Deficit:

Paid-in surplus	\$ 41,810.86	
Earned surplus—deficit*	184,091.44*	142,280.58*
		1,217,319.42
		\$2,086,577.20

CONTINGENT LIABILITY

As endorser on notes payable issued by Lockheed Aircraft Corporation in connection with the purchase of a portion of the Company's aircraft		\$ 444,320.00
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NOTES—(Continued)

C—Unpaid accumulated dividends on preferred stock at June 30, 1939, amounted to \$6.25 per share or an aggregate of \$3,062.50 on the 490 shares outstanding.

STATEMENTS OF PROFIT AND LOSS AND DEFICIT
NORTHWEST AIRLINES, INC.
Year ended June 30, 1939

PROFIT AND LOSS

OPERATING REVENUE		
Mail		\$1,550,875.84
Passenger		969,512.41
Other transportation		60,444.76
		<u>\$2,580,833.01</u>

OPERATING EXPENSES			
Maintenance	\$ 547,630.74		
Depreciation and amortization		384,458.55	
Other transportation		1,481,924.41	
Traffic and advertising		288,057.30	
Administrative and general		166,479.23	
			<u>2,868,550.23</u>
OPERATING LOSS			<u>\$ 287,717.22</u>

OTHER INCOME			
Net profit from disposal of capital assets	\$ 152,483.73		
Profit from repair and supply services		9,118.95	
Discounts and interest earned		3,960.61	
Sundry		6,824.88	
			<u>172,388.17</u>
			<u>\$ 115,329.05</u>

OTHER DEDUCTIONS			
Interest	\$ 3,034.90		
Additional federal income and excess profits taxes for fiscal year 1936		1,929.49	
Sundry		3,022.40	
			<u>7,986.79</u>
NET LOSS			<u>\$ 123,315.84</u>

DEFICIT*

PAID-IN SURPLUS		
Balance at June 30, 1939		
(no change during the year)		\$ 41,810.86

EARNED SURPLUS—DEFICIT		
Balance at June 30, 1938	\$ 60,775.60	
Net loss for the year	123,315.84	
BALANCE AT JUNE 30, 1939		<u>184,091.44</u>
DEFICIT—JUNE 30, 1939		<u>\$ 142,280.58*</u>

ERNST & ERNST
ACCOUNTANTS AND AUDITORS
SYSTEM SERVICE
ST. PAUL, MINN.

August 28, 1939.

NORTHWEST AIRLINES, INC.,
Saint Paul, Minnesota.

We have made an examination of the balance sheet of NORTHWEST AIRLINES, INC., as of June 30, 1939, and of the statements of profit and loss and deficit for the year ended at that date. In connection therewith, we examined or tested accounting records of the Company and other supporting evidence and obtained information and explanations from officers and employees of the Company; we also made a general review of the accounting methods and of the operating and income accounts for the year, but we did not make a detailed audit of the transactions.

Accounts receivable were tested by direct correspondence with debtors and by reference to documents on file and other records. Notes payable, including long term debt, were confirmed by direct correspondence. Accounts payable were tested by direct correspondence and by inspection of invoices, vouchers, records of subsequent transactions, etc.

In our opinion, based upon our examination, the accompanying balance sheet and related statements of profit and loss and deficit fairly present the position of the Company at June 30, 1939, and the results of its operations for the year ended at that date. Further, it is our opinion that the statements have been prepared in accordance with accepted principles of accounting and on a basis consistent with the preceding year.

ERNST & ERNST
Certified Public Accountants



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