

MESA AIR GROUP INC
Form 10-K
December 29, 2003

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)

OF SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended September 30, 2003

Commission File Number 0-15495

Mesa Air Group, Inc.

(Exact name of registrant as specified in its charter)

Nevada

*(State or other jurisdiction of
incorporation or organization)*

**410 North 44th Street, Suite 700,
Phoenix, Arizona**

(Address of Principal Executive Offices)

85-0302351

*(I.R.S. Employer
Identification No.)*

85008

(Zip Code)

Registrant's telephone number, including area code:

(602) 685-4000

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, No Par Value

(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes No

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The aggregate market value of the voting stock held by non-affiliates of the Registrant as of March 31, 2003: Common Stock, no par value: \$153.3 million.

On December 8, 2003, the Registrant had outstanding 31,721,724 shares of Common Stock.

Documents Incorporated by Reference

Portions of the registrant's proxy statement for the 2004 annual meeting of stockholders

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2003 FORM 10-K REPORT

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PART I

Forward-Looking Statements

This Form 10-K Report contains certain statements including, but not limited to, information regarding the replacement, deployment, and acquisition of certain numbers and types of aircraft, and projected expenses associated therewith; costs of compliance with Federal Aviation Administration regulations and other rules and acts of Congress; the passing of taxes, fuel costs, inflation, and various expenses to the consumer; the relocation of certain operations of Mesa; the resolution of litigation in a favorable manner and certain projected financial obligations. These statements, in addition to statements made in conjunction with the words expect, anticipate, intend, plan, believe, seek, estimate, and similar expressions, are forward-looking statements within the meaning of the Harbor provision of Section 27A of the Securities Act of 1933 as amended and Section 21E of the Securities Exchange Act of 1934 as amended. These statements relate to future events or the future financial performance of Mesa and only reflect management's expectations and estimates. The following is a list of factors, among others, that could cause actual results to differ materially from the forward-looking statements: changing business conditions in certain market segments and industries; changes in Mesa's code-sharing relationships; the inability of America West, US Airways or United Airlines to pay their obligations under the code-share agreements; the inability of United Airlines to successfully restructure and emerge from bankruptcy; an increase in competition along the routes Mesa operates or plans to operate; material delays in completion by the manufacturer of the ordered and yet-to-be delivered aircraft; availability and cost of funds for financing new aircraft; changes in general economic conditions; changes in fuel price; changes in regional economic conditions; Mesa's relationship with employees and the terms of future collective bargaining agreements; the impact of current and future laws, additional terrorist attacks; Congressional investigations, and governmental regulations affecting the airline industry and Mesa's operations; bureaucratic delays; amendments to existing legislation; consumers unwilling to incur greater costs for flights; unfavorable resolution of negotiations with municipalities for the leasing of facilities; and risks associated with litigation outcomes. One or more of these or other factors may cause Mesa's actual results to differ materially from any forward-looking statement. Mesa is not undertaking any obligation to update any forward-looking statements contained in this Form 10-K.

Item 1. *Business*
General

Mesa Air Group, Inc. (we, us, Mesa or the Company) is a holding company whose principle subsidiaries operate as regional air carriers providing scheduled passenger and airfreight service. The Company serves 163 cities in 40 states, the District of Columbia, Canada, Mexico and the Bahamas. At September 30, 2003, the Company operated a fleet of 150 aircraft and had approximately 943 daily departures.

Approximately 98% of our consolidated passenger revenues for the fiscal year ended September 30, 2003 were derived from operations associated with code-share agreements. Our subsidiaries have code-share agreements with America West Airlines, Inc. (America West), Frontier Airlines, Inc. (Frontier), Midwest Airlines, Inc. (Midwest Airlines), United Airlines, Inc. (United Airlines or United) and US Airways, Inc. (U Airways). These code-share agreements allow use of the code-share partners' flight designator code to identify flights and fares in computer reservation systems, permit use of logos, service marks, aircraft paint schemes and uniforms similar to the code-share partner and provide coordinated schedules and joint advertising. The remaining passenger revenues are derived from Mesa's independent operations.

In addition to carrying passengers, we carry freight and express packages on our passenger flights and have interline small cargo freight agreements with many other carriers. We also have contracts with the U.S. Postal Service for carriage of mail to the cities we serve and occasionally operate charter flights when our aircraft are not otherwise used for scheduled service.

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Our airline operations are conducted by the following airline subsidiaries:

Mesa Airlines, Inc. (Mesa Airlines), a Nevada corporation, operates regional jet and turboprop aircraft as America West Express under a code-share agreement with America West, primarily at America West's operations hub located in Phoenix; as US Airways Express under a code-share agreement with US Airways, primarily at US Airways' hubs on the East Coast; as United Express under a code-share agreement with United Airlines, primarily in Denver; and as Frontier JetExpress under a code-share agreement with Frontier in Denver, which expires December 31, 2003.

Air Midwest, Inc. (Air Midwest), a Kansas corporation, operates Beechcraft 1900D 19-seat turboprop aircraft as US Airways Express under separate code-share agreements with US Airways at certain US Airways' hubs on the East Coast as well as Kansas City. Air Midwest's flights in Kansas City code-share with both Midwest Airlines and US Airways. Air Midwest operates as America West Express in Phoenix. Air Midwest also operates as Mesa Airlines in Albuquerque, New Mexico and in select Essential Air Service (EAS) markets. The Albuquerque flights and certain EAS markets are Independent Operations and are not subject to a code-sharing agreement with a major carrier.

Freedom Airlines, Inc. (Freedom), a Nevada corporation, operates CRJ-700 and CRJ-900 regional jets pursuant to the Company's code-share agreement with America West. Freedom Airlines began revenue flight operations on October 19, 2002.

Unless the context indicates otherwise, the terms Mesa, the Company, we, us, or our, refer to Mesa Air Group, Inc. and its subsidiaries.

Corporate Structure

Mesa is a Nevada corporation that was originally formed in New Mexico, with its principal executive office in Phoenix, Arizona.

In addition to operating the airline subsidiaries listed above, we also have the following other subsidiaries:

MPD, Inc., a Nevada corporation, doing business as Mesa Pilot Development and MPD ASU, operates our training program for new pilots in conjunction with San Juan College in Farmington, New Mexico and Arizona State University in Tempe, Arizona.

Regional Aircraft Services, Inc., a California corporation, performs aircraft component repair and overhaul services.

MAGI Insurance, Ltd., a Barbados, West Indies based captive insurance company, was established for the purpose of obtaining more favorable aircraft liability insurance rates.

Ritz Hotel Management Corp., a Nevada Corporation, was established to facilitate the Company's acquisition and management of a Phoenix area hotel property used for crew accommodations in training.

Mesa Air Group Aircraft Inventory Management, LLC (MAG AIM), an Arizona Limited Liability Company, was established to purchase, distribute and manage Mesa's inventory of spare rotatable and expendable parts.

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The following table sets forth our aircraft fleet (owned and leased) in operation by aircraft type as of September 30, 2003.

	Canadair Regional Jet-200 (CRJ-200)	Canadair Regional Jet-700 (CRJ-700)	Canadair Regional Jet-900 (CRJ-900)	Embraer Regional Jet-145 (ERJ-145)	Beechcraft 1900D	DeHavilland Dash 8-200	TOTAL
US Airways Express	20			32	26		78
America West Express	18	10	6		3	6	43
United Express		5				6	11
Frontier JetExpress	5						5
Mesa Airlines					8		8
Spares/idle					5		5
Total	43	15	6	32	42	12	150

Code-Share Agreements

Our airline subsidiaries have agreements with America West, US Airways, United Airlines, Frontier, and Midwest Airlines to use those carriers' designation codes (commonly referred to as a code-share agreements). These code-share agreements allow use of the code-share partner's flight designator code to identify flights and fares in computer reservation systems, permit use of logos, service marks, aircraft paint schemes and uniforms similar to the code-share partner's and provide coordinated schedules and joint advertising. The Company's passengers traveling on flights operated pursuant to code-share agreements receive mileage credits in the respective frequent flyer programs of the Company's code-share partners, and credits in those programs can be used on flights operated by the Company.

The financial arrangement with our code-share partners involves either a revenue-guarantee or pro-rate arrangement. The America West (regional jet and Dash-8), United (regional jet and Dash-8), Frontier (regional jet), and US Airways (regional jet) code-share agreements are revenue-guarantee flying agreements. Under the terms of these flying agreements, the major carrier controls marketing, scheduling, ticketing, pricing and seat inventories. The Company receives a guaranteed payment based upon a fixed minimum monthly amount plus amounts related to departures and block hours flown plus direct reimbursement for expenses such as fuel, landing fees and insurance. Among other advantages, revenue-guarantee arrangements reduce the Company's exposure to fluctuations in passenger traffic and fare levels, as well as fuel prices. The US Airways, Midwest Airlines and America West B1900 turboprop code-share agreements are pro-rate agreements, for which the Company receives an allocated portion of the passengers' fare and pays all of the costs of transporting the passenger.

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The following table summarizes our available seat miles (ASMs) flown and revenue recognized under our code-share agreements for the years ended September 30, 2003 and 2002:

In thousands	Fiscal 2003				Fiscal 2002			
	ASMs		Passenger Revenue		ASMs		Passenger Revenue	
America West (Revenue-Guarantee)	2,012,185	45%	\$252,181	44%	1,494,469	43%	\$193,173	40%
US Airways (Revenue-Guarantee)	1,778,365	40%	218,457	38%	1,281,181	37%	166,387	35%
Frontier (Revenue-Guarantee)	154,544	3%	19,199	3%				
United (Revenue-Guarantee)	20,487	1%	6,101	1%				
America West (Pro-rate)	5,790		1,017					
US Airways (Pro-rate)	295,726	7%	63,205	11%	439,515	13%	96,608	20%
Frontier (Pro-rate)	91,746	2%	8,129	1%	185,071	5%	15,736	3%
Mesa Airlines	94,864	2%	9,293	2%	59,191	2%	8,922	2%
Total	4,453,707		\$577,582		3,459,427		\$480,826	

America West Code-Sharing Agreement**Revenue-Guarantee**

As of September 30, 2003, we operated six CRJ-900, ten CRJ-700, 18 CRJ-200, and six Dash-8 aircraft for America West under a revenue-guarantee code-sharing agreement. The code-share agreement, as amended, provides for the Company to increase its fleet up to 38 CRJ-900s and eliminate the CRJ-700 aircraft. In addition, America West has an option to increase its CRJ-900 fleet size to 50 aircraft. In exchange for providing flights and all other obligations under the agreement, we receive a fixed monthly minimum amount plus certain additional amounts based upon the number of flights flown and block hours performed during the month. America West also reimburses us for certain costs on an actual basis, including fuel costs, aircraft ownership and financing costs, landing fees, passenger liability and hull insurance, and aircraft property taxes. We also receive a monthly payment from America West based on a percentage of revenue from flights that we operate under the code-share agreement. Under the amended code-share agreement, America West has the right to reduce the combined CRJ fleets utilized under the code-share agreement by one aircraft in any six-month period commencing in January 2007. In addition, beginning in February 2007, America West may eliminate the Dash-8 aircraft upon 180 days prior written notice. The code-share agreement terminates on June 30, 2012 unless America West elects to extend the contract for two years or exercises options to increase fleet size. The code-share agreement is subject to termination prior to that date in various circumstances including:

If our flight completion factor falls below a specified percentage for a specified period of time, subject to notice and cure rights;

If either America West or we become insolvent, file for bankruptcy or fail to pay our debts as they become due, the non-defaulting party may terminate the agreement;

Failure by us or America West to perform the covenants, conditions or provisions of the code-sharing agreement, subject to 15 days notice and cure rights;

If we or America West fails to make a payment when due, subject to ten business days notice and cure rights; or

If we are required by the FAA or the DOT to suspend operations and we have not resumed operations within three business days, except as a result of an emergency airworthiness directive from the FAA affecting all similarly equipped aircraft, America West may terminate the agreement.

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Pro-Rate

Pursuant to a turboprop code-sharing agreement with America West, we operated three B1900D turboprop aircraft in the Phoenix hub under a pro-rate revenue-sharing arrangement as of September 30, 2003. We control scheduling, inventory and pricing. We are allocated a portion of each passenger's fare based on a standard industry formula and are required to pay all costs of transporting the passenger. The pro-rate agreement terminates on March 31, 2012 unless America West elects to extend the contract for successive one-year periods. The pro-rate agreement could also be terminated prior to the termination under similar circumstances as the revenue-guarantee agreement.

US Airways Code-Sharing Agreements

Revenue-Guarantee

As of September 30, 2003, we operated 52 50-seat regional jets for US Airways under a code-sharing agreement, with an additional four 50-seat regional jets added in December 2003. Under the jet code-share agreement, we provide US Airways Express service between US Airways hubs and cities designated by US Airways. In exchange for performing the flight services under the agreement, we receive from US Airways a fixed monthly minimum amount, plus certain additional amounts based upon the number of flights flown and block hours performed during the month. Additionally, certain costs incurred by Mesa in performing the flight services are pass-through costs, whereby US Airways agrees to reimburse us for the actual amounts incurred for these items: insurance, property tax per aircraft, fuel and oil cost, catering cost, and landing fees. We also receive a fixed profit margin based upon certain costs reimbursements under the agreement. Twenty-four of the fifty-six jets must be in compliance with the jets-for-jobs provisions in the US Airways pilot contract. Jets-for-jobs is an agreement between Mesa, US Airways and their respective pilot unions in which furloughed US Airways Pilots receive an agreed upon number of captain and first officer positions on certain aircraft added to the agreement. Additionally, on November 22, 2002, the Company signed a non-binding letter of intent with US Airways to provide up to an additional 50 70-seat regional jets. The additional aircraft, which will also be subject to jets-for-jobs, are expected to be delivered beginning in mid-fiscal 2004. Mesa and US Airways continue to discuss the terms of the Letter of Intent, but no definitive agreement has been reached and no assurance can be made that a definitive agreement will be reached that is mutually acceptable to both parties. The code-share agreement for (i) the initial 32 ERJ-145s terminates on December 31, 2008, unless US Airways elects to exercise its option to extend the term for three years upon 12 months notice; and (ii) the additional 24 jets terminates in January 2013, unless US Airways elects to exercise its option to extend the term for two years upon 12 months notice. Further, on November 19, 2003, the Company signed a Seventh Amendment to the US Airways code-share agreement in which the number of additional aircraft was increased from 24 jets to 27 jets. These aircraft are expected to be placed in service beginning in the second quarter of fiscal 2004.

Notwithstanding the foregoing, US Airways may terminate the code-share agreement at any time for cause upon 90 days notice and subject to our right to cure under any of the following conditions:

If we fail to retain or utilize the aircraft in the manner required under the jet code-share agreement.

If we admit liability or are found liable for serious safety infractions by the Federal Aviation Administration (FAA), a finding which leads to the suspension or revocation of Mesa's operating certificate.

Pro-Rate

Pursuant to a turboprop code-sharing agreement with US Airways, we operated 26 B1900D turboprop aircraft under a pro-rate revenue-sharing arrangement as of September 30, 2003. We control scheduling, inventory and pricing subject to US Airways' concurrence that such service does not adversely affect its other operations in the region. We are allocated a portion of each passenger's fare based on a standard industry formula and are required to pay all the costs of transporting the passenger. Additionally, we are required to pay certain franchise, marketing and reservation fees to US Airways.

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US Airways may terminate the turboprop agreement at any time for cause upon not less than five days notice under any of the following conditions:

If we fail to utilize the aircraft as specified in the agreements.

If we fail to achieve specified levels of operating performance in completion factors and on-time arrival performance.

If we fail to comply with the trademark license provisions of the agreement.

If we fail to perform the material terms, covenants or conditions of the code-sharing agreement.

Upon a change in our ownership or control without the written approval of US Airways.

The turboprop code-share agreement terminates in October 2006 provided, however, most of the turboprop flying hub markets can be terminated by US Airways for any reason upon 180 days prior advance written notice.

United Code-Sharing Agreement

As of September 30, 2003, we operated five CRJ-700 and six Dash-8 aircraft for United under a code-sharing arrangement. The code-share agreement, which has not been executed by the parties, provides for the Company to increase its fleet to 30 70-seat regional aircraft (15 of which would be replacements for 15 CRJ-200s), 15 CRJ-200s and 10 Dash-8 aircraft. In exchange for performing the flight services under the agreement, we receive from United a fixed monthly minimum amount, plus certain additional amounts based upon the number of flights flown and block hours performed during the month. Additionally, certain costs incurred by Mesa in performing the flight services are pass-through costs, whereby United agrees to reimburse us for the actual amounts incurred for these items: insurance, property tax per aircraft, fuel cost, oil cost, catering cost, and landing fees. We also receive a profit margin based upon certain reimbursable costs under the agreement as well as our operational performance. The code-share agreement for (i) the ten Dash-8 aircraft terminates in July 2013 unless terminated by United Airlines by giving notice six months prior to the fifth anniversary, (ii) the 15 50-seat CRJ-200s terminates in July 2008, which can be accelerated up to two years at Mesa's discretion, (iii) the 15 70-seat regional jets (to be delivered upon the withdrawal of the 50-seat regional jets) terminates ten years from delivery date, and (iv) the remaining 15 70-seat regional jets terminates in three tranches between December 31, 2011 and December 31, 2013. The code-share agreement is subject to termination prior to these dates in various circumstances including:

If certain operational performance factors fall below a specified percentage for a specified time, subject to notice and cure rights;

Failure by us to perform the material covenants, agreements, terms or conditions of the code-share agreement or similar agreements with United, subject to thirty (30) days notice and cure rights;

If either United or we become insolvent, file bankruptcy or fail to pay debts when due, the non-defaulting party may terminate the agreement.

Frontier Jet Code-Sharing Agreement

In September 2001, we entered into a five-year pro-rate revenue-sharing code-share agreement with Frontier which was converted to a revenue-guarantee contract in March 2003. As of September 30, 2003, we operated five CRJ-200 aircraft for Frontier under a revenue-guarantee agreement that expires December 31, 2003.

Fleet Plans and Aircraft Manufacturer Relationships

ERJ Program

In June 1999, we entered into an agreement with Empresa Brasileira de Aeronautica SA (Embraer) to acquire 36 Embraer ERJ-145 50-passenger regional jets. Mesa introduced the ERJ-145 aircraft into revenue

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service in the third quarter of fiscal 2000 as US Airways Express. As of September 30, 2003, we have taken delivery of 32 ERJ-145s, which have been financed as operating leases with initial terms of 16.5 to 18 years. The last four ERJ-145 aircraft were delivered in December 2003. In conjunction with this purchase agreement, Mesa had \$4.2 million remaining on deposit with Embraer, which was included with lease and equipment deposits at September 30, 2003. The remaining deposit was returned to us upon the delivery of the last four aircraft. We also have options for 45 additional aircraft. In October 2003, our contract with Embraer was amended to extend the option exercise date to May 2004.

CRJ Program

In August 1996, we entered into an agreement (the 1996 BRAD Agreement) with Bombardier Regional Aircraft Division (BRAD) to acquire 32 CRJ-200 50-passenger regional jet aircraft. The 32 aircraft have been delivered and are currently under permanent financing as operating leases with initial terms of 16.5 to 18.5 years.

In May 2001, the Company entered into a second agreement with BRAD (the 2001 BRAD Agreement) under which we are now committed to purchase a total of 15 CRJ-700s and 25 CRJ-900s. The transaction includes standard product support provisions, including training, preferred pricing on initial inventory provisioning, maintenance and technical publications. The Company has accepted delivery of all 15 CRJ-700s on order under the 2001 BRAD Agreement. We are the launch customer of the CRJ-900 and as of September 30, 2003, have taken delivery of six CRJ-900 aircraft. In addition to the firm orders, Mesa has an option to acquire an additional 80 CRJ-700 or CRJ-900 regional jets. In conjunction with the 2001 BRAD Agreement, Mesa had \$15.0 million on deposit with BRAD, which was included with lease and equipment deposits at September 30, 2003.

In 2003, the Company acquired 11 used CRJ-200 aircraft in order to meet required deliveries under its code-share agreements. The aircraft are financed as operating leases. The Company continues to actively pursue used 50-seat regional jet aircraft.

The following table summarizes our jet fleet status and fleet expansion plans currently under contract with aircraft manufacturers for the periods indicated:

	<u>CRJ-200</u>	<u>CRJ-700 Firm Orders</u>	<u>CRJ-900 Firm Orders</u>	<u>CRJ-700 Options</u>	<u>CRJ-900 Options</u>	<u>ERJ-145 Firm Orders</u>	<u>ERJ-145 Options</u>	<u>Cumulative Total</u>
Delivered:								
At 9/30/2003	43	15	6			32		96
Scheduled deliveries:								
Fiscal 2004			19			4		119
Fiscal 2005								119
Fiscal 2006				3	3		8	133
Fiscal 2007				12	12		10	167
Fiscal 2008				5	5		12	189
Fiscal 2009 and Beyond				20	20		15	244
Total	<u>43</u>	<u>15</u>	<u>25</u>	<u>40</u>	<u>40</u>	<u>36</u>	<u>45</u>	

Beechcraft 1900D

As of September 30, 2003, we owned 35 and leased seven Beechcraft 1900D aircraft. The seven leased aircraft have leases expiring between October 31, 2004 and October 1, 2005.

Dash-8

As of September 30, 2003, we operated 12 leased Dash-8 aircraft. The Company is negotiating to lease four additional Dash-8 aircraft to be used in its United Airlines operations.

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Marketing

Our flight schedules are structured to facilitate the connection of our passengers with the flights of our code-share partners at their hub airports and to maximize local and connecting service to other carriers.

Under our B1900 turboprop operations, the Company's market selection process follows an in-depth analysis on a route-by-route basis and is followed by a review and approval process in a joint effort with US Airways or America West, as the case may be, regarding the level of service and fares. We believe that this selection process enhances the likelihood of profitability in a given market.

Under the America West, US Airways and United revenue-guarantee code-share agreements, market selection, pricing and yield management functions are performed by our respective partners. Our role is simply to operate our fleet in the safest and most reliable manner in exchange for fees paid under a generally fixed payment schedule. We intend to expand our operations performed pursuant to these revenue-guarantee agreements.

Under our code-share agreements, the code-share partner coordinates advertising and public relations within their respective systems. In addition, our traffic is impacted by the major airline partners' advertising programs in regions outside those served by us, with the major partners' customers becoming our customers as a result of through fares. Under pro-rate code-share arrangements, our passengers also benefit from through fare ticketing with the major airline partners and greater accessibility to our flights on computer reservation systems and in the Official Airline Guide.

Our pro-rate agreements and independent flights are promoted through, and our revenues are generally believed to benefit from, listings in computer reservation systems, the Official Airline Guide and through direct contact with travel agencies and corporate travel departments. Our independent operations utilize SABRE, a computerized reservation system widely used by travel agents, corporate travel offices and other airlines. The reservation systems of our code-share partners are also utilized in each of our other operations through their respective code-share agreements. We also pay booking fees to owners of other computerized reservation systems based on the number of independent and pro-rate passengers booked by travel agents using such systems. We believe that we have good relationships with the travel agents serving our passengers.

Competition

The airline industry is highly competitive and volatile. Airlines compete in the areas of pricing, scheduling (frequency and timing of flights), on-time performance, type of equipment, cabin configuration, amenities provided to passengers, frequent flyer plans, and the automation of travel agent reservation systems. Further, because of the Airline Deregulation Act, airlines are currently free to set prices and establish new routes without the necessity of seeking governmental approval. At the same time, deregulation has allowed airlines to abandon unprofitable routes where the affected communities will not be left without air service.

We believe that the Airline Deregulation Act facilitated our entry into scheduled air service markets and allows us to compete on the basis of service and fares, thus causing major carriers to seek out further contractual agreements with carriers like us as a way of expanding their respective networks. However, the Airline Deregulation Act makes the entry of other competitors possible, some of which may have substantial financial resources and experience, creating the potential for intense competition among regional air carriers in our markets.

We believe our code-share agreements provide a significant competitive advantage in hub airports where our major partner has a predominant share of the market. The ability to control connecting passenger traffic by offering superior service creates difficulty for other regional airlines wishing to compete at such hubs. In addition to enhanced competitiveness offered by the code-share agreements, we compete with other airlines by offering frequent flights, flexible schedules and numerous fare levels.

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Fuel

Historically, we have not experienced problems with the availability of fuel, and believe that we will be able to obtain fuel in quantities sufficient to meet our existing and anticipated future requirements at competitive prices. Standard industry contracts generally do not provide protection against fuel price increases, nor do they ensure availability of supply. However, the Company's revenue-guarantee code-share agreements with America West, Frontier, United and US Airways (regional jet) allow fuel used in the performance of the agreements to be billed to the code-share partner, thereby reducing the Company's exposure to fuel price fluctuations. In fiscal 2003, approximately 84% of the Company's fuel was associated with the Company's America West, Frontier, United and US Airways (regional jet) code-share agreements. A substantial increase in the price of jet fuel, to the extent our fuel costs are not reimbursed, or the lack of adequate fuel supplies in the future may have a material adverse effect on the Company's business, financial condition, results of operations and liquidity.

Maintenance of Aircraft and Training

All mechanics and avionics specialists employed by us have the appropriate training and experience and hold the required licenses issued by the FAA. Using a combination of FAA-certified maintenance vendors and our own personnel and facilities, the Company maintains its aircraft on a scheduled and as-needed basis. We emphasize preventive maintenance and inspect our aircraft engines and airframes as required. We also maintain an inventory of spare parts specific to the aircraft types we fly. We provide periodic in-house and outside training for our maintenance and flight personnel and also take advantage of factory training programs that are offered when acquiring new aircraft.

Insurance

We carry types and amounts of insurance customary in the regional airline industry, including coverage for public liability, passenger liability, property damage, product liability, aircraft loss or damage, baggage and cargo liability and workers' compensation.

As a result of the terrorist attacks on September 11, 2001, aviation insurers have significantly reduced the maximum amount of insurance coverage available to commercial air carriers for war-risk coverage, while at the same time, significantly increasing the premiums for this coverage as well as for aviation insurance in general. Given the significant increase in insurance costs, the federal government is providing insurance assistance under the Air Transportation Safety and System Stabilization Act. In addition, the federal government has issued war-risk coverage to U.S. air carriers that is generally renewable for 60-day periods. However, the availability of aviation insurance is not guaranteed and our inability to obtain such coverage at affordable rates may result in the grounding of our aircraft. Insurance costs are reimbursed under the terms of our code-share agreement with America West, United Airlines and our regional jet service agreement with US Airways.

Employees

As of September 30, 2003, we employed approximately 3,600 employees. Approximately 2,100 of our employees are represented by various labor organizations. Our continued success is partly dependent on our ability to continue to attract and retain qualified personnel. Historically, we have had no difficulty attracting qualified personnel to meet our requirements.

Mesa Airline's flight attendants are represented by the Association of Flight Attendants (AFA). Mesa Airline's contract with the AFA expires in June 2006. Freedom is currently in negotiations with the AFA. As Freedom aircraft are transferred to Mesa Airlines, the affected flight attendants became assimilated into the existing Mesa Airlines/ AFA contract. The Company's pilots, which are represented by Air Line Pilot Association (ALPA) ratified a 54-month contract effective March 19, 2003. This contract covers the pilots from Air Midwest, Freedom and Mesa Airlines.

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Although not currently observing high turnover, pilot turnover at times is a significant issue among regional carriers when major carriers are hiring experienced commercial pilots away from regional carriers. The addition of aircraft, especially new aircraft types, can result in pilots upgrading between aircraft types and becoming unavailable for duty during the extensive training periods required. No assurances can be made that pilot turnover and unavailability will not be a significant problem in the future, particularly if major carriers expand their operations. Similarly, there can be no assurance that sufficient numbers of new pilots will be available to support any future growth.

No other Mesa subsidiaries are parties to any other collective bargaining agreement or union contracts.

Essential Air Service Program

The Essential Air Service (EAS) program administered by the United States Department of Transportation (DOT) guarantees a minimum level of air service in certain communities, predicated on predetermined guidelines set forth by Congress. Based on these guidelines, the DOT subsidizes air service to communities that might not otherwise have air service. At September 30, 2003, we provided service to 27 such cities for an annual subsidy of approximately \$17.0 million. EAS rates are normally set for two-year contract periods for each city. There is no guarantee that we will continue to receive subsidies for the cities we serve. The DOT may request competitive proposals from other airlines at the end of the contract period for EAS service to a particular city. Proposals, when requested, are evaluated on, among other things, level of service provided, subsidy requested, fitness of the applicant and comments from the communities served. If the funding under this program is terminated for any of the cities served by the Company, in all likelihood we would not continue to fly in these markets, and as a result, we would be forced to find alternative uses for the Beechcraft 1900D 19-seat turboprop aircraft affected.

Regulation

As an interstate air carrier, we are subject to the economic jurisdiction, regulation and continuing air carrier fitness requirements of the DOT. Such requirements include minimum levels of financial, managerial and regulatory fitness. The DOT is authorized to establish consumer protection regulations to prevent unfair methods of competition and deceptive practices, to prohibit certain pricing practices, to inspect a carrier's books, properties and records, and to mandate conditions of carriage. The DOT also has the power to bring proceedings for the enforcement of air carrier economic regulations, including the assessment of civil penalties, and to seek criminal sanctions.

We are subject to the jurisdiction of the FAA with respect to its aircraft maintenance and operations, including equipment, ground facilities, dispatch, communication, training, weather observation, flight personnel and other matters affecting air safety. To ensure compliance with its regulations, the FAA requires airlines to obtain an operating certificate, which is subject to suspension or revocation for cause, and provides for regular inspections.

Effective March 1997, the FAA required that regional airlines with aircraft of ten or more passenger seats operating under FAR Part 135 rules to begin operating those aircraft under FAR Part 121 regulations. The Company, which at one time was one of the largest regional airlines operating under FAR Part 135 regulations, completed the transition to Part 121 within the FAA's deadline. These requirements have resulted in a significant increase in Air Midwest's costs, adversely affecting our ability to profitably serve certain markets. Such increased costs are primarily related to additional training, dispatch and maintenance procedures. We continue to work to minimize the cost of these new operating procedures while fully complying with FAR Part 121 operating requirements.

We are subject to various federal and local laws and regulations pertaining to other issues of environmental protocol. We believe we are in compliance with all governmental laws and regulations regarding environmental protection.

We are also subject to the jurisdiction of the Federal Communications Commission with respect to the use of its radio facilities and the United States Postal Service with respect to carriage of United States mail.

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Local governments in certain markets have adopted regulations governing various aspects of aircraft operations, including noise abatement and curfews.

Available Information

We maintain a website where additional information concerning our business can be found. The address of that website is www.mesa-air.com. We make available free of charge on our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, as soon as reasonably practicable after we electronically file or furnish such materials to the SEC.

Item 2. Properties

Our primary property consists of the aircraft used in the operation of our flights. The following table lists the aircraft owned and leased by the Company as of September 30, 2003.

Type of Aircraft	Number of Aircraft			Operating on Sept. 30, 2003	Passenger Capacity
	Owned	Leased	Total		
CRJ-200 Regional Jet		43	43	43	50
CRJ-700 Regional Jet		15	15	15	64
CRJ-900 Regional Jet		6	6	6	90
Embraer Regional Jet		32	32	32	50
Beechcraft 1900D	35	7	42	42	19
Dash 8-200		12	12	12	37
Embraer EMB-120		6	6		30
Total	35	121	156	150	

See Business Airline Operations and MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - Liquidity and Capital Resources for a discussion regarding the Company's aircraft fleet commitments.

In addition to aircraft, we have office and maintenance facilities to support our operations. Our facilities are summarized in the following table:

Type	Location	Ownership	Approximate Square Feet
Headquarters	Phoenix, AZ	Leased	31,000
Training/ Administration	Phoenix, AZ	Leased	27,000
Hangar	Grand Junction, CO	Leased	22,500
Hangar	Farmington, NM	Leased	30,000
Hangar	Phoenix, AZ	Leased	20,000
Hangar/ Office	Phoenix, AZ	Leased	21,425
Engine Shop	Phoenix, AZ	Leased	3,240
Hangar/ Office	Wichita, KS	(1)	30,000
Hangar/ Office	Dubois, PA	Leased	23,000
Hangar	Reading, PA	(1)	56,250
Office (East Coast)	Charlotte, NC	Leased	3,000
Hangar	Charlotte, NC	Leased	30,000

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(1) Building is owned, underlying land is leased.

We lease ticket counters, check-in and boarding and other facilities in the passenger terminal areas in the majority of the airports we serve and staff those facilities with our personnel. America West, US Airways and

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Frontier also provide facilities, ticket handling and ground support services for the Company at certain airports.

Our corporate headquarters facility is leased pursuant to a ten-year lease that commenced November 1, 1998. In October 2002, we entered into an amendment to increase the total square footage to 31,000 and extend the term to August 31, 2012. Our Phoenix Training/ Administration facility is subject to an 89-month lease that commenced on June 1, 2001.

We believe our facilities are suitable and adequate for our current and anticipated needs.

Item 3. *Legal Proceedings*

We are also involved in various other legal proceedings and FAA civil action proceedings that the Company does not believe will have a material adverse effect upon our business, financial condition or results of operations, although no assurance can be given to the ultimate outcome of any such proceedings.

On October 6, 2003, the Company announced that it had made an unsolicited proposal to the board of directors of Atlantic Coast Airlines Holdings, Inc. (Atlantic Coast) to acquire all the outstanding stock of Atlantic Coast whereby the Company would issue 0.9 of a share of its common stock for each Atlantic Coast share. In connection with such proposal, the Company, on October 15, 2003, filed with the SEC the necessary documents to commence a shareholder consent solicitation to replace Atlantic Coast s current board of directors with independent directors who we believe will give fair consideration to our proposal and announced its intention to make an exchange offer for all the outstanding shares of common stock of Atlantic Coast subject to certain conditions. We believe that our nominees, if elected, would take such action, to the event that it is in the best interest of the Atlantic Coast stockholders to (i) remove the impediments to the consideration of the Company s exchange offer/merger proposal and any alternative proposals arising pursuant to that certain Rights Agreement dated as of January 27, 1999 between Atlantic Coast and Continental Stock Transfer & Trust Company, and (ii) exempt the Company s exchange offer/merger proposal, or any other alternative transaction from the restrictions of Section 203 of the Delaware General Corporation Law. We also intended to file with the SEC a Registration Statement on Form S-4 with respect to the issuance of our common stock in connection with the offer to exchange Mesa shares directly with Atlantic Coast shareholders.

In connection with our proposal, several lawsuits have been filed. On October 27, 2003, Atlantic Coast filed a complaint against Mesa in the United States District Court for the District of Columbia alleging that Mesa has made materially false and misleading statements and omissions in violation of the federal securities laws in connection with its proposed consent solicitation and potential exchange offer. Atlantic Coast s complaint alleges, among other things, that (i) Mesa failed to disclose Untied Airlines as a participant in its consent solicitation and proposed transaction; (ii) Mesa s bid to acquire all of Atlantic Coast s outstanding stock is motivated by its desire to use Atlantic Coast s cash on hand to resolve Mesa s difficulties in obtaining financing for additional aircraft purchases; (iii) Mesa CEO Jonathan Ornstein and other Mesa insiders sold a substantial number of Mesa shares in September 2003, shortly before Mesa announced its takeover bid of Atlantic Coast; (iv) other stock transactions produced short-swing profits subject to Section 16(b) of the Securities Exchange Act of 1934, as amended, which requires a corporate insider to disgorge any profit from such transactions; (v) Mesa s directors, who have determined that an acquisition of Atlantic Coast would be in Mesa s best interest and are proposing a transaction in which the stockholders of Atlantic Coast would receive shares of Mesa common stock, are not sufficiently independent and have engaged in self-dealing; and (vi) several of Mesa s nominees to Atlantic Coast s board of directors are subject to conflicts of interest that would impair their ability to fulfill their fiduciary obligations to Atlantic Coast. Atlantic Coast in its complaint seeks injunctive relief with respect to its allegations. Atlantic Coast in its complaint seeks to (i) obtain a declaration that Mesa s consent statement as well as its other statements in conjunction with its proposed consent solicitation violate Section 14(a) of the Exchange Act and SEC Rule 14a-9; (ii) obtain a declaration that Mesa s consent statement as well as its other statements in conjunction with its proposed consent solicitation and exchange offer violate Section 14(e) of the Exchange Act; (iii) require Mesa to correct any alleged material misstatements and omissions; (iv) enjoin Mesa from disseminating its consent statement; and (v) enjoin Mesa from making a proxy consent solicitation and/or tender offer to Atlantic Coast s stockholders.

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On October 29, 2003, Mesa filed a lawsuit in the Court of Chancery of the State of Delaware seeking to require the Atlantic Coast Board to comply with the proper procedures under Delaware law and the Atlantic Coast by-laws with respect to fixing a record date for the consent solicitation and commencing the 60-day solicitation period. The lawsuit alleges that the action taken by the Atlantic Coast board to set a record date of October 23, 2003 impedes Atlantic Coast's shareholders' ability to exercise their voting rights and right to receive superior value for their shares. Mesa is seeking from the Court, among other things, an order for declaratory and injunctive relief declaring that the October 23, 2003 record date is invalid; declaring that the consent solicitation has not yet commenced; and enjoining Atlantic Coast from fixing a record date or declaring that the consent solicitation has commenced.

On November 25, 2003 and December 2, 2003, Atlantic Coast announced respectively (i) that the consent it received had been revoked and (ii) the cancellation of the record date previously set in connection with Mesa's consent solicitation.

On November 26, 2003, Atlantic Coast amended its complaint. The amended complaint, in addition to the allegations contained in its initial complaint filed on October 27, 2003, claims that (i) United Airlines and Mesa acted in concert and conspired in violation of Section 1 of the Sherman Antitrust Act and (ii) Mesa's attempt to acquire Atlantic Coast is in violation of Section 7 of the Clayton Act. Atlantic Coast simultaneously filed a motion for a preliminary injunction that would, among other things, prohibit Mesa from commencing our consent solicitation and from taking any other action to attempt to acquire control of Atlantic Coast or its board of directors.

On November 30, 2003, Mesa filed a counterclaim against Atlantic Coast. Mesa's counterclaim alleges that Atlantic Coast's preliminary proxy statement and other public statements made in connection with Mesa's consent solicitation and Atlantic Coast's business model of becoming an independent low-fare airline are materially false and misleading, in violation of Section 14(a) of the Exchange Act.

On December 8, 2003, the Corporation Counsel for the District of Columbia initiated an antitrust investigation to determine whether Mesa's proposed acquisition of Atlantic Coast violates Section 1 of the Sherman Act or Section 7 of the Clayton Act or the District of Columbia Antitrust Act. Mesa intends to fully comply with this inquiry.

On December 18, 2003, the United States District Court for the District of Columbia enjoined us from proceeding with our consent solicitation and our exchange offer pending final resolution of Atlantic Coast's antitrust claims against Mesa. On December 19, 2003, the United States Department of Justice initiated an antitrust investigation to determine whether Mesa's proposed acquisition of Atlantic Coast violates Section 1 of the Sherman Act or Section 7 of the Clayton Act. Mesa intends to fully comply with this inquiry. On December 23, 2003, Mesa announced that it would not be moving forward with either its proposed consent solicitation or exchange offer for Atlantic Coast.

Table of Contents**Item 4. Submission of Matters to a Vote of Security Holders**

None.

Executive Officers of the Registrant

The following table sets forth the names and ages of the executive officers of the Company and certain additional information:

Name	Age	Position
Jonathan G. Ornstein	46	Chief Executive Officer
Michael J. Lotz	43	President and Chief Operating Officer
George Murnane III	45	Executive Vice President and Chief Financial Officer
Michael Ferverda	59	Senior Vice President – West Coast Operations and President Freedom Airlines, Inc.
Brian S. Gillman	34	Vice President, General Counsel and Secretary
F. Carter Leake	41	Senior Vice President, US Airways Express
Robert B. Stone	47	Senior Vice President and Treasurer

Jonathan G. Ornstein was appointed President and Chief Executive Officer of Mesa Air Group, Inc. effective May 1, 1998. Mr. Ornstein relinquished his position as President of the Company in June 2000. From April 1996 to his joining the Company as Chief Executive Officer, Mr. Ornstein served as President and Chief Executive Officer and Chairman of Virgin Express S.A./N.V., a European airline. From 1995 to April 1996, Mr. Ornstein served as Chief Executive Officer of Virgin Express Holdings, Inc. Mr. Ornstein joined Continental Express Airlines, Inc., as President and Chief Executive Officer in July 1994 and, in November 1994, was named Senior Vice President, Airport Services at Continental Airlines, Inc. Mr. Ornstein was previously employed by the Company from 1988 to 1994, as Executive Vice President and as President of the Company's WestAir Holding, Inc., subsidiary.

Michael J. Lotz, President and Chief Operating Officer, joined the Company in July 1998. In January 1999, Mr. Lotz became Chief Operating Officer. In August 1999, Mr. Lotz became the Company's Chief Financial Officer and in January 2000 returned to the position of Chief Operating Officer. On June 22, 2000, Mr. Lotz was appointed President of the Company. Prior to joining the Company, Mr. Lotz served as Chief Operating Officer of Virgin Express, S.A./N.V., a position he held from October 1996 to June 1998. Previously, Mr. Lotz was employed by Continental Airlines, Inc., most recently as Vice President of Airport Operations, Properties and Facilities at Continental Express.

George Murnane III, Executive Vice President and Chief Financial Officer, was appointed Executive Vice President of the Company effective December 2001 and Chief Financial Officer in January 2003. Mr. Murnane served as a director of the Company from June 1999 until October 2003. Mr. Murnane has served as the President of Barlow Management, Inc. from 1998 until October 2003. From 1996 to December 2001, Mr. Murnane was a Director and Executive Vice President of International Airline Support Group, Inc., a leading redistributor of aftermarket commercial aircraft spare parts and lessor and trader of commercial aircraft and engines, most recently as its Chief Operating Officer. From 1995 to 1996, Mr. Murnane served as Executive Vice President and Chief Operating Officer of Atlas Air, Inc., an air cargo company. For 1986 to 1996, he was an investment banker with the New York investment banking firm of Merrill Lynch & Co., most recently as a Director in the firm's Transportation Group.

Michael Ferverda, Senior Vice President – West Coast Operations and President of Freedom Airlines, Inc. (FAI), joined the Company in 1990. He was appointed President of Freedom Airlines in May 2002 and Senior Vice President – West Coast Operations in February 2003. Prior to the appointments, Mr. Ferverda served as the Senior Vice President of Operations for Mesa Airlines, Inc. Mr. Ferverda has

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served the Company in various capacities including pilot, Flight Instructor/ Check Airman, Assistant Chief Pilot, FAA Designated Examiner, FAA Director of Operations and Divisional Vice President. Mr. Ferwerda was a pilot with Eastern Airlines from 1973 to 1989. Prior to joining Eastern Airlines, Mr. Ferwerda served as an Aviator in the United States Navy. Mr. Ferwerda is a graduate of Indiana University.

Brian S. Gillman, Vice President, General Counsel and Secretary, joined the Company in February 2001. From July 1996 to February 2001, he served as Vice President, General Counsel and Secretary of Vanguard Airlines, Inc. in Kansas City, Missouri. From September 1994 to July 1996, Mr. Gillman was a corporate associate in the law firm of Stinson, Mag & Fizzell, P.C., Kansas City, Missouri. Mr. Gillman received his Juris Doctorate and B.B.A. in Accounting from the University of Iowa in 1994 and 1991, respectively.

F. Carter Leake, Senior Vice President, US Airways Express, joined the Company in 2001. Mr. Leake served as Executive Vice-President of CCAir, Inc., a former wholly-owned subsidiary of the Company in January 2001 and was promoted to President of CCAir in October 2001. In February 2003, Mr. Leake was appointed to Senior Vice President US Airways Express. Prior to joining the Company, Mr. Leake served as a Director of Sales for Bombardier Regional Aircraft from November 1996 to January 2001. Previously, Mr. Leake was an analyst with SH&E, an aviation consulting firm in New York, and a US Air Force military pilot.

Robert B. Stone, Senior Vice President and Treasurer, joined the Company in January 2000 as Chief Financial Officer. Mr. Stone was appointed to the position of Senior Vice President in January 2003. Prior to joining the Company, Mr. Stone was employed by the Boeing Company for more than 20 years, most recently as Vice President, Financial Planning and Analysis. Mr. Stone obtained his MBA from Pacific Lutheran University and his Bachelor of Arts in Business Administration at the University of Washington.

PART II**Item 5. Market for Registrant's Common Equity and Related Stockholder Matters**
Market Price of Common Stock

The following table sets forth, for the periods indicated, the high and low price per share of Mesa common stock for the two most recent fiscal years, as reported by NASDAQ. Mesa's common stock is traded on the NASDAQ National Market System under the symbol MESA.

Quarter	Fiscal 2003		Fiscal 2002	
	High	Low	High	Low
First	\$ 7.09	\$2.71	\$ 7.89	\$2.80
Second	4.97	3.00	11.43	7.51
Third	7.96	4.50	11.74	7.05
Fourth	13.20	8.42	10.49	3.62

On December 8, 2003, we had approximately 1,213 shareholders of record. We have never paid cash dividends on our common stock. The payment of future dividends is within the discretion of our board of directors and will depend upon our future earnings, if any, our capital requirements, bank financing, financial condition and other relevant factors.

Recent Sales of Unregistered Securities

On February 7, 2002, in connection with an agreement entered into with Raytheon Aircraft Company (Raytheon), we granted Raytheon a warrant to purchase up to 233,068 shares of our common stock at a per share exercise price of \$10.00. Raytheon must pay a purchase price of \$1.50 per share underlying the warrant. The warrant is exercisable at any time over a three-year period following its date of issuance. Absent a default by us under the agreement with Raytheon in which case vesting is accelerated, the shares underlying the warrant vest (and are therefore purchasable by Raytheon) according to the following schedule: 13,401 shares in fiscal year 2001; 116,534 shares in fiscal year 2002; 58,267 shares in fiscal year 2003 and 44,866 shares in

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fiscal year 2004. Raytheon has exercised its option to purchase the 2001, 2002 and 2003 warrants but has not yet exercised the warrant. The sale of the warrant and the shares underlying the warrant were made pursuant to an exemption from registration pursuant to Section 4(2) under the Securities Act of 1933, as amended.

In June 2003, the Company completed the private placement of senior convertible notes due 2023. At maturity, the principal amount of each note will be \$1,000 and the aggregate amount due will be \$252 million. The notes are convertible into shares of the Company's common stock at a conversion rate of 39.727 shares per \$1,000 in principal amount at maturity of the notes which equals an initial conversion price of approximately \$10.00 per share. This conversion rate is subject to adjustment in certain circumstances. Holders of the notes may convert their notes only if: (i) the sale price of our common stock exceeds 110% of the accreted conversion price for at least 20 trading days in the 30 consecutive trading days ending on the last trading day of the preceding quarter; (ii) prior to June 16, 2018, the trading price for the notes falls below certain thresholds; (iii) the notes have been called for redemption; or (iv) specified corporate transactions occur. The Company may redeem the notes, in whole or in part, beginning on June 16, 2008, at a redemption price equal to the issue price, plus accrued original issue discount, plus any accrued and unpaid cash interest. The holders of the notes may require the Company to repurchase the notes on June 16, 2008 at a price of \$397.27 per note plus accrued and unpaid cash interest, if any, on June 16, 2013 at a price of \$540.41 per note plus accrued and unpaid cash interest, if any, and on June 16, 2018 at a price of \$735.13 per note plus accrued and unpaid cash interest, if any.

Item 6. Selected Financial Data
Selected Financial Data and Operating Statistics

The selected financial data as of and for each of the five years ended September 30, 2003, are derived from the Consolidated Financial Statements of the Company and its subsidiaries and should be read in conjunction with the Consolidated Financial Statements included elsewhere in this Form 10-K and the related notes thereto and MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS. The Consolidated Financial Statements of the Company for the fiscal years ended September 30, 2003, 2002, 2001 and 2000, have been audited by Deloitte & Touche LLP, independent auditors. The Consolidated Financial Statements of the Company for the fiscal year ended September 30, 1999 have been audited by KPMG LLP, independent auditors.

In thousands of dollars except per share data and average fare amounts and as otherwise indicated.

	<u>2003(1)</u>	<u>2002(2)</u>	<u>2001(3)</u>	<u>2000(4)</u>	<u>1999(5)</u>
Consolidated Statement of Operations Data:					
Operating revenues	\$ 599,990	\$ 496,783	\$ 523,378	\$ 471,612	\$ 404,616
Operating expenses	\$ 547,179	\$ 503,005	\$ 594,020	\$ 429,798	\$ 402,487
Operating income (loss)	\$ 52,811	\$ (6,222)	\$ (70,642)	\$ 41,814	\$ 2,129
Interest expense	\$ 5,890	\$ 5,440	\$ 13,469	\$ 15,463	\$ 19,096
Income (loss) before income taxes	\$ 45,326	\$ (13,524)	\$ (71,375)	\$ 28,031	\$ (12,815)
Net income (loss)	\$ 27,961	\$ (9,309)	\$ (48,076)	\$ 58,872	\$ (13,412)
Net income (loss) per share:					
Basic	\$ 0.89	\$ (.28)	\$ (1.50)	\$ 1.78	\$ (0.40)
Diluted	\$ 0.83	\$ (.28)	\$ (1.50)	\$ 1.77	\$ (0.40)

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	2003(1)	2002(2)	2001(3)	2000(4)	1999(5)
Consolidated Balance Sheet					
Data:					
Working capital	\$ 177,051	\$ 73,501	\$ 80,646	\$ 63,953	\$ 33,040
Total assets	\$ 474,163	\$ 352,343	\$ 423,986	\$ 386,594	\$ 403,773
Long-term debt, excluding current portion	\$ 199,023	\$ 110,210	\$ 118,492	\$ 136,127	\$ 114,234
Stockholders' equity	\$ 116,971	\$ 89,100	\$ 103,126	\$ 144,574	\$ 96,435
Consolidated Operating Statistics:					
Passengers carried	6,444,459	5,118,839	4,789,180	4,457,989	4,255,696
Revenue passenger miles (000)	2,814,480	1,986,164	1,796,058	1,561,197	1,324,867
Available seat miles (ASM) (000)	4,453,707	3,459,427	3,289,216	2,951,116	2,594,861
Block hours	393,335	352,323	383,310	395,446	367,362
Average passenger journey in miles	436	388	375	350	311
Average stage length in miles	337	298	268	250	225
Load factor	63.2%	57.4%	54.6%	52.9%	51.1%
Break-even passenger load factor	46.3%	60.1%	63.8%	48.5%	52.7%
Revenue per ASM in cents	13.4	14.4	15.9	16.0	15.3
Operating cost per ASM in cents	12.3	14.6	18.1	14.6	15.5
Average yield per revenue passenger mile in cents	21.3	25.0	28.8	30.2	30.1
Average fare	\$ 89.44	\$ 93.93	\$ 106.18	\$ 103.45	\$ 93.59
Aircraft in service	150	124	118	133	140
Cities served	163	147	153	120	138
Number of employees	3,600	3,100	2,820	3,480	3,423

- (1) Net income in fiscal 2003 includes the effect of impairment and restructuring charges of \$1.1 million (pretax) and the reversal of CCAir impairment and restructuring charges of \$12.0 million (pretax).
- (2) Net loss in fiscal 2002 includes the effect of impairment and restructuring charges of \$26.7 million (pretax).
- (3) Net loss in fiscal 2001 includes the effect of impairment and restructuring charges of \$80.9 million (pretax).
- (4) Net earnings in fiscal 2000 include the cumulative effect of the accounting change from the accrual method to the direct expense method for maintenance costs of \$18.1 million (pretax) and the benefit of reversing a valuation allowance for deferred tax assets of \$21.9 million.
- (5) Net loss in fiscal 1999 includes the effect of impairment and restructuring charges of \$28.9 million (pre-tax) and the reversal of a previous charge for the cancellation of the UAL code share agreement of \$14.0 million (pretax).

Our June 9, 1999 acquisition of CCAir was accounted for as a pooling of interests and, accordingly, our consolidated financial statements for fiscal 1999 have been restated to include the results of CCAir for the entire year.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis provides information which management believes is relevant to an assessment and understanding of the Company's results of operations and financial condition. The discussion should be read in conjunction with the Consolidated Financial Statements and the related notes thereto, and the Selected Financial Data and Operating Statistics contained elsewhere herein.

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Critical Accounting Estimates and Judgments

The discussion and analysis of our financial condition and results of operations is based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. In connection with the preparation of these financial statements, we are required to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, and expenses, and related disclosure of contingent liabilities. On an ongoing basis, we evaluate our estimates, including those related to revenue recognition, the allowance for doubtful accounts, medical claims reserve, valuation of assets held for sale and costs to return aircraft and a valuation allowance for certain deferred tax assets. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances. Such historical experience and assumptions form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We have identified the accounting policies below as critical to our business operations and the understanding of our results of operations. The impact of these policies on our business operations is discussed throughout Management's Discussion and Analysis of Financial Condition and Results of Operations where such policies affect our reported and expected financial results. The discussion below is not intended to be a comprehensive list of our accounting policies. For a detailed discussion on the application of these and other accounting policies, see Note 1 in the Notes to the Consolidated Financial Statements, which contains accounting policies and other disclosures required by accounting principles generally accepted in the United States of America.

Revenue Recognition

The America West, United, Frontier and the US Airways regional jet code-share agreements are revenue-guarantee flying agreements. Under a revenue-guarantee arrangement, the major airline generally pays a fixed monthly minimum amount, plus certain additional amounts based upon the number of flights flown and block hours performed. The contracts also include reimbursement of certain costs incurred by Mesa in performing flight services. These costs, known as pass-through costs, may include aircraft ownership cost, passenger and hull insurance, aircraft property taxes as well as, fuel, landing fees and catering. The contracts also include a profit component that may be determined based on a percentage of profits on the Mesa flown flights, a profit margin on certain reimbursable costs as well as a profit margin based on certain operational benchmarks. The Company primarily recognizes revenue under its revenue-guarantee agreements when the transportation is provided. The majority of the revenue under these contracts is known at the end of the accounting period and is booked as actual. The Company performs an estimate of the profit component based upon the information available at the end of the accounting period. All revenue recognized under these contracts is presented at the gross amount billed.

The America West, US Airways, and Midwest Airlines B1900D turboprop code-share agreements are pro-rate agreements. Under a prorate agreement, the Company receives a percentage of the passenger's fare based on a standard industry formula that allocates revenue based on the percentage of transportation provided. Revenue from our pro-rate agreements and our independent operation is recognized when transportation is provided. Tickets sold but not yet used are included in air traffic liability on the consolidated balance sheets.

The Company also receives subsidies for providing scheduled air service to certain small or rural communities. Such revenue is recognized in the period in which the air service is provided. The amount of the subsidy payments is determined by the United States Department of Transportation on the basis of its evaluation of the amount of revenue needed to meet operating expenses and to provide a reasonable return on investment with respect to eligible routes. EAS rates are normally set for two-year contract periods for each city.

Allowance for Doubtful Accounts

Amounts billed by the Company under revenue guarantee arrangements are subject to our interpretation of the applicable code-share agreement and are subject to audit by our code-share partners. Periodically our

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code-share partners dispute amounts billed and pay amounts less than the amount billed. Ultimate collection of the remaining amounts not only depends upon Mesa prevailing under audit, but also upon the financial well-being of the code-share partner. As such, the Company periodically reviews amounts past due and records a reserve for amounts estimated to be uncollectible. The allowance for doubtful accounts was \$4.7 million and \$12.8 million at September 30, 2003 and 2002, respectively. If the Company's actual ability to collect these receivables and the actual financial viability of its partners is materially different than estimated, the Company's estimate of the allowance could be materially understated or overstated.

Accrued Health Care Costs

The Company is currently self-insured for health care costs and as such, a reserve for the cost of claims that have not been paid as of the balance sheet date is estimated. The Company's estimate of this reserve is based upon historical claim experience and upon the recommendations of its health care provider. At September 30, 2003 and 2002, the Company accrued \$1.8 million and \$2.0 million, respectively, for the cost of future health care claims. If the ultimate development of these claims is significantly different than those that have been estimated, the reserves for future health care claims could be materially overstated or understated.

Long-lived Assets, Aircraft and Parts Held for Sale

Property and equipment are stated at cost and depreciated over their estimated useful lives to their estimated salvage values using the straight-line method. Long-lived assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the related carrying amount may be impaired. Under the provisions of Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the Company records an impairment loss if the undiscounted future cash flows are found to be less than the carrying amount of the asset. If an impairment loss has occurred, a charge is recorded to reduce the carrying amount of the asset to fair market value. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less cost to sell.

Valuation Allowance for Deferred Tax Assets

The Company records deferred tax assets for the value of benefits expected to be realized from the utilization of alternative minimum tax credit carryforwards and state and federal net operating loss carryforwards. The Company periodically reviews these assets for realizability based upon expected taxable income in the applicable taxing jurisdictions. To the extent the Company believes some portion of the benefit may not be realizable, an estimate of the unrealized portion is made and an allowance is recorded. At September 30, 2003 and 2002, the Company had a valuation allowance for certain deferred tax assets not expected to be realized of \$0.1 million and \$2.9 million, respectively. Realization of these deferred tax assets is dependent upon generating sufficient taxable income prior to expiration of any net operating loss carryforwards. The Company believes it will generate sufficient taxable income in the future to realize these net operating loss carryforwards as the Company has had pretax income in fiscal 2003, 2002 and 2001 (excluding impairment charges) and as the Company has taken steps to minimize the financial impact of its unprofitable subsidiaries. Although realization is not assured, management believes it is more likely than not that the recorded deferred tax asset, net of the valuation allowance provided, will be realized. If the ultimate realization of these deferred tax assets is significantly different than those that have been estimated, the valuation allowance for deferred tax assets could be materially overstated or understated.

Results of Operations

General

Mesa Air Group, Inc. and its subsidiaries (collectively referred to herein a