

MESA AIR GROUP INC
Form 10-Q
May 10, 2006

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**SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the quarterly period-ended March 31, 2006

or

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

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)*

85-0302351

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

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

(Address of principal executive offices)

85008

(Zip code)

Registrant's telephone number, including area code:

(602) 685-4000

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 last 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

On May 3, 2006, the registrant had outstanding 36,144,455 shares of Common Stock.

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MESA AIR GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

	Three Months Ended		Six Months Ended	
	March 31, 2006	March 31, 2005	March 31, 2006	March 31, 2005
(Unaudited)				
(In thousands, except per share amounts)				
Operating revenues:				
Passenger	\$ 305,652	\$ 255,530	\$ 621,066	\$ 511,917
Freight and other	6,412	8,286	14,615	16,703
Total operating revenues	312,064	263,816	635,681	528,620
Operating expenses:				
Flight operations	90,833	79,115	180,697	158,339
Fuel	103,157	65,194	208,006	132,308
Maintenance	47,606	46,928	103,144	95,534
Aircraft and traffic servicing	18,310	17,591	34,520	34,368
Promotion and sales	882	815	1,654	2,160
General and administrative	14,515	15,655	32,906	31,188
Depreciation and amortization	8,824	10,113	18,007	19,286
Impairment and restructuring charges (credits)				(1,257)
Total operating expenses	284,127	235,411	578,934	471,926
Operating income	27,937	28,405	56,747	56,694
Other income (expense):				
Interest expense	(8,710)	(10,194)	(18,296)	(18,935)
Interest income	2,600	464	5,598	1,058
Other income (expense)	(13,229)	(1,094)	(14,326)	1,255
Total other income (expense)	(19,339)	(10,824)	(27,024)	(16,622)
Income before income taxes	8,598	17,581	29,723	40,072
Income taxes	3,310	6,733	11,443	15,348
Net income	\$ 5,288	\$ 10,848	\$ 18,280	\$ 24,724
Income per common share:				
Basic	\$ 0.15	\$ 0.37	\$ 0.58	\$ 0.83
Diluted	\$ 0.14	\$ 0.26	\$ 0.48	\$ 0.58

See accompanying notes to condensed consolidated financial statements.

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MESA AIR GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2006	September 30, 2005
(Unaudited)		
(In thousands, except share amounts)		
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 103,281	\$ 143,428
Marketable securities	167,474	128,162
Restricted cash	11,672	8,848
Receivables, net	27,132	28,956
Income tax receivable	1,209	704
Expendable parts and supplies, net	32,766	36,288
Prepaid expenses and other current assets	106,736	98,267
Deferred income taxes	7,036	8,256
Total current assets	457,306	452,909
Property and equipment, net	609,599	642,914
Lease and equipment deposits	25,072	25,428
Other assets	76,926	46,420
Total assets	\$ 1,168,903	\$ 1,167,671
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Current portion of long-term debt	\$ 29,594	\$ 27,787
Short-term debt	82,110	54,594
Accounts payable	45,584	52,608
Air traffic liability	2,088	2,169
Accrued compensation	3,872	3,829
Deposit on pending sale of rotatable spare parts		22,750
Rotatable spare parts financing liability		19,685
Income taxes payable		2,863
Other accrued expenses	32,411	30,512
Total current liabilities	195,659	216,797
Long-term debt, excluding current portion	556,482	636,582
Deferred credits	100,504	97,497
Deferred income tax liability	32,729	25,684
Other noncurrent liabilities	16,282	14,441
Total liabilities	901,656	991,001

Stockholders equity:

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Preferred stock of no par value, 2,000,000 shares authorized; no shares issued and outstanding		
Common stock of no par value and additional paid-in capital, 75,000,000 shares authorized; 36,109,834 and 28,868,167 shares issued and outstanding, respectively	168,425	96,128
Retained earnings	98,822	80,542
Total stockholders equity	267,247	176,670
Total liabilities and stockholders equity	\$ 1,168,903	\$ 1,167,671

See accompanying notes to condensed consolidated financial statements.

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MESA AIR GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months Ended	
	March 31, 2006	March 31, 2005
	(Unaudited) (In thousands)	
Cash Flows from Operating Activities:		
Net income	\$ 18,280	\$ 24,724
Adjustments to reconcile net income to net cash flows provided by (used in) operating activities:		
Depreciation and amortization	18,007	19,286
Impairment and restructuring charges (credits)		(1,257)
Deferred income taxes	8,265	14,905
Unrealized (gain) loss on investment securities	962	198
Amortization of deferred credits	(5,688)	(3,241)
Amortization of restricted stock awards	589	588
Stock option expense	1,450	
Excess tax benefit from stock compensation	(2,609)	
Tax benefit-stock compensation		57
Provision for obsolete expendable parts and supplies	(17)	600
Provision for doubtful accounts	540	1,704
Changes in assets and liabilities:		
Net (purchases) sales of investment securities	(40,274)	(65,049)
Receivables	8,496	7,675
Income tax receivables	(505)	(29)
Expendable parts and supplies	1,911	2,133
Prepaid expenses and other current assets	(8,469)	(15,119)
Contract incentive payments	(20,000)	
Accounts payable	(7,025)	2,058
Income taxes payable	(254)	(55)
Other accrued liabilities	3,530	1,899
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(22,811)	(8,923)
Cash Flows from Investing Activities:		
Capital expenditures	(9,164)	(28,227)
Proceeds from sale of flight equipment	16,034	
Change in restricted cash	(2,824)	(862)
Change in other assets	1,147	(2,688)
Net returns (payments) of lease and equipment deposits	1,356	(10,208)
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	6,549	(41,985)
Cash Flows from Financing Activities:		
Principal payments on long-term debt	(16,015)	(12,942)

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Proceeds from short-term debt		13,241	
Proceeds from exercise of stock options and issuance of warrants	5,565		307
Proceeds (payments) on financing rotatable inventory	(17,768)		
Tax benefit-stock compensation	2,609		
Common stock purchased and retired	(193)		(3,430)
Proceeds from receipt of deferred credits	1,917		2,198
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(23,885)		(626)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(40,147)		(51,534)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	143,428		173,110
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 103,281	\$	121,576
SUPPLEMENTAL CASH FLOW INFORMATION:			
Cash paid for interest, net of amounts capitalized	\$ 19,310	\$	17,192
Cash paid for income taxes, net	6,618		650
SUPPLEMENTAL NON-CASH INVESTING AND FINANCING ACTIVITIES:			
Aircraft delivered under interim financing	\$ 27,516	\$	160,883
Conversion of convertible debentures to common stock	62,278		
Inventory and other credits received in conjunction with aircraft financing	4,604		

See accompanying notes to condensed consolidated financial statements.

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MESA AIR GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Business and Basis of Presentation

The accompanying unaudited, condensed consolidated financial statements of Mesa Air Group, Inc. (Mesa or the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for a complete set of financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the results for the periods presented have been made. Operating results for the three and six-month periods ended March 31, 2006, are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2006. These condensed consolidated financial statements should be read in conjunction with the Company s consolidated financial statements and notes thereto included in the Company s annual report on Form 10-K for the fiscal year ended September 30, 2005.

The accompanying condensed consolidated financial statements include the accounts of Mesa Air Group, Inc. and its wholly-owned operating subsidiaries: Mesa Airlines, Inc. (Mesa Airlines), a Nevada corporation and certificated air carrier; Freedom Airlines, Inc. (Freedom), a Nevada corporation and certificated air carrier; Air Midwest, Inc. (Air Midwest), a Kansas corporation and certificated air carrier; MPD, Inc. (MPD), a Nevada corporation, doing business as Mesa Pilot Development; Regional Aircraft Services, Inc. (RAS) a Pennsylvania corporation; Mesa Leasing, Inc., a Nevada corporation; Mesa Air Group Airline Inventory Management, LLC (MAG-AIM), an Arizona Limited Liability Company; Ritz Hotel Management Corp., a Nevada Corporation; and MAGI Insurance, Ltd. (MAGI), a Barbados, West Indies based captive insurance company. MPD, Inc. provides pilot training in coordination with a community college in Farmington, New Mexico and with Arizona State University in Tempe, Arizona. RAS performs aircraft component repair and overhaul services and ground handling services. MAGI is a captive insurance company established for the purpose of obtaining more favorable aircraft liability insurance rates. All significant intercompany accounts and transactions have been eliminated in consolidation. In addition, the Company has announced that Mesa Airlines will begin providing inter-island service in Hawaii as *go!* beginning in the third quarter of fiscal 2006. This operation is referred to herein as *go!* .

2. Segment Reporting

Statement of Financial Accounting Standard (SFAS) No. 131, Disclosures about Segments of an Enterprise and Related Information, requires disclosures related to components of a company for which separate financial information is available that is evaluated regularly by a company s chief operating decision maker in deciding the allocation of resources and assessing performance. The Company has three airline operating subsidiaries, Mesa Airlines, Freedom Airlines and Air Midwest, as well as various other subsidiaries organized to provide support for the Company s airline operations. In addition, Mesa Airlines plans to begin providing inter-island service in Hawaii as *go!* beginning in the third quarter of fiscal 2006. The Company has aggregated these subsidiaries into three reportable segments: Mesa Airlines/ Freedom, Air Midwest/*go!* and Other. Mesa Airlines and Freedom Airlines operate regional jets and Dash-8 aircraft pursuant to revenue guarantee contracts. Air Midwest operates the Company s Beech 1900 turboprop aircraft and *go!* will operate regional jets, whereby the Company assumes revenue risk. The Other reportable segment includes Mesa Air Group (the holding company), RAS, MPD, MAG-AIM, MAGI, Mesa Leasing, Inc. and Ritz Hotel Management Corp., all of which support Mesa s operating subsidiaries. In October 2004, the Company transitioned certain of its regional jets from Freedom into Mesa and transferred a B1900D aircraft from Air Midwest into Freedom. As a result, Freedom was grouped with Air Midwest in fiscal 2005 for segment purposes. In fiscal 2006, Freedom began operating under a revenue-guarantee code-share agreement with Delta utilizing ERJ145 aircraft that were transitioned from Mesa Airlines. As such, the Company has aggregated Freedom with Mesa Airlines beginning in the first quarter of fiscal 2006. Operating revenues in the

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Other segment are primarily sales of rotatable and expendable parts to the Company's operating subsidiaries and ground handling services performed by employees of RAS for Mesa Airlines.

Mesa Airlines and Freedom Airlines provide passenger service with regional jets under revenue-guarantee contracts with United Airlines, Inc. (United), Delta Air Lines, Inc. (Delta) and America West Airlines, Inc. (America West), which currently operates as US Airways and is referred to herein as US Airways. The current US Airways is a result of a merger between America West and US Airways, Inc. (Pre-Merger US Airways). Mesa Airlines also provides passenger service with Dash-8 aircraft under revenue-guarantee contracts with US Airways and United. As of March 31, 2006, Mesa Airlines and Freedom Airlines operated a fleet of 160 aircraft 108 CRJs, 36 ERJs and 16 Dash-8s. Prior to operating ERJ 145 aircraft, Freedom most recently operated Beechcraft 1900D under a pro-rate agreement with US Airways.

Air Midwest provides passenger service with Beechcraft 1900D aircraft under pro-rate contracts with US Airways and Midwest Airlines, Inc. (Midwest Airlines) as well as independent operations as Mesa Airlines. As of March 31, 2006, Air Midwest operated a fleet of 20 Beechcraft 1900D turboprop aircraft.

The Other category consists of Mesa Air Group, RAS, MPD, MAG-AIM, MAGI, Mesa Leasing, Inc. and Ritz Hotel Management Corp. Mesa Air Group performs all administrative functions not directly attributable to any specific operating company. These administrative costs are allocated to the operating companies based upon specific criteria including headcount, available seat miles (ASM's) and other operating statistics. MPD operates pilot training programs in conjunction with San Juan College in Farmington, New Mexico and Arizona State University in Tempe, Arizona. Graduates of these training programs are eligible to be hired by the Company's operating subsidiaries. RAS primarily supplies repair services and ground handling services to the Company's operating subsidiaries. MAGI is a captive insurance company located in Barbados. MAG-AIM is the Company's inventory procurement and sales company.

Three Months Ended	Mesa/ Freedom	Air Midwest/ go!	Other	Eliminations	Total
March 31, 2006 (000 \$)					
Total operating revenues	\$ 298,035	\$ 12,585	\$ 61,488	\$ (60,044)	\$ 312,064
Depreciation and amortization	7,897	31	896		8,824
Operating income (loss)	25,942	(1,298)	11,504	(8,211)	27,937
Interest expense	(6,395)		(2,460)	145	(8,710)
Interest income	2,258	3	484	(145)	2,600
Income (loss) before income tax	21,441	(1,905)	(2,727)	(8,211)	8,598
Income tax (benefit)	8,233	(712)	(1,050)	(3,161)	3,310
Total assets	1,343,416	7,425	413,218	(595,156)	1,168,903
Capital expenditures (including non-cash)	2,409	7	3,672		6,088

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MESA AIR GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Three Months Ended March 31, 2005 (000 s)	Mesa	Air Midwest/ Freedom	Other	Eliminations	Total
Total operating revenues	\$ 247,667	\$ 13,813	\$ 67,159	\$ (64,823)	\$ 263,816
Depreciation and amortization	8,891	53	1,169		