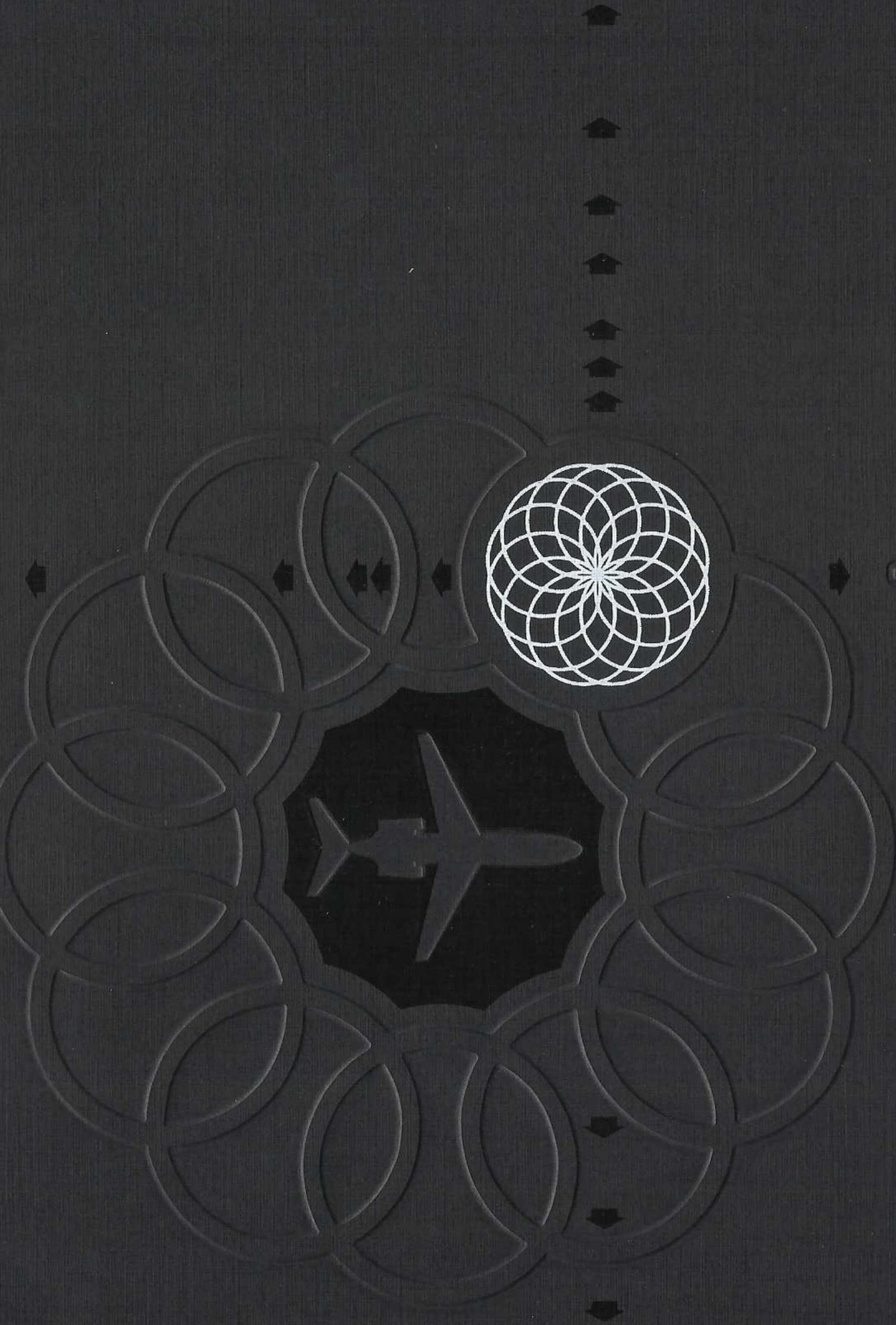


CENTRAL AIRLINES 1966 ANNUAL REPORT

DIRECTORS: A. A. (JACK) BRADFORD, *Chairman of the Board*, Midland, Texas; M. LAMAR MUSE, Dallas, Texas; FRED BOSTON, Oklahoma City, Oklahoma; ROBERT S. BRENNAND, JR., Midland, Texas; J. E. CONNALLY, Abilene, Texas; IRBY L. DYER, Midland, Texas; ROBERT THOMAS, Houston, Texas

OFFICERS: A. A. (JACK) BRADFORD, *Chairman of the Board;* M. LAMAR MUSE, *President;* ROBERT L. SICARD, *Vice President, Operations;* J. L. HERRING, *Vice President, Customer Service;* RICHARD A. ELLIOTT, *Vice President, Marketing;* EVAN LINGLE, *Vice President, Industrial Relations;* C. E. LUNDSTROM, *Treasurer;* IRBY L. DYER, *Secretary;* PAUL F. GLOVER, *Assistant Vice President, Maintenance & Engineering;* WILLIAM R. HUFFMAN, *Assistant Vice President, Training;* JAMES C. DIXSON, *Assistant Vice President, Traffic;* RICHARD FOULK, *Assistant Vice President, Research;*

GENERAL OFFICES: Greater Southwest International Airport, Fort Worth, Texas

WASHINGTON COUNSEL: Koteen and Burt, Washington, D. C.

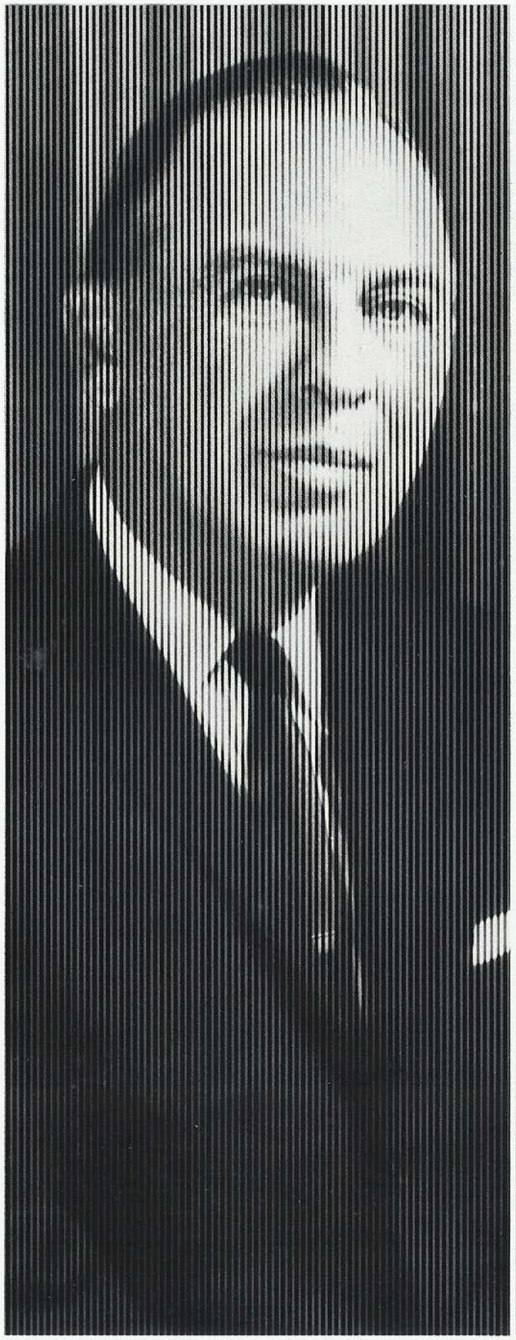
REGISTRAR AND TRANSFER AGENT: The Mercantile National Bank at Dallas, Dallas, Texas

AUDITORS: Price Waterhouse & Co., Dallas, Texas

SERVICE AREA

ARKANSAS: *Fayetteville, Fort Smith, Harrison, Hot Springs, Little Rock.* COLORADO: *Colorado Springs, Denver, Lamar, Pueblo.* KANSAS: *Dodge City, Garden City, Goodland, Great Bend, Hays, Hutchinson, Liberal, Manhattan-Fort Riley-Junction City, Parsons-Independence-Coffeyville, Salina, Topeka, Wichita.* MISSOURI: *Fort Leonard Wood, Joplin, Kansas City, St. Louis.* OKLAHOMA: *Bartlesville, Duncan, Enid, Guymon, Lawton-Fort Sill, McAlester, Muskogee, Oklahoma City, Ponca City, Stillwater, Tulsa.* TEXAS: *Amarillo, Borger, Dallas, Fort Worth, Paris.*

TO OUR SHAREHOLDERS, CUSTOMERS, AND FRIENDS:



A. A. (Jack) Bradford

M. Lamar Muse

Net income for the year ended December 31, 1966 of $404,845 equal to $.27 per share outstanding, established 1966 as the most profitable year in the Company's history. Income of $366,845 before special credit exceeded by some 24% the combined restated earnings of the preceding four-year period, 1962-1965. Commercial revenues of $10,275,000 were 28% greater than 1965 and operating income of $871,000 compared with a loss of $190,000 in the preceding year. Based on these results, your Board of Directors on December 13, 1966 declared a five (5%) percent stock dividend payable to stockholders of record at the close of business December 30, 1966, and 71,394 shares were distributed in early 1967. Thus, the programs and undertakings set in motion during 1965 and dubbed "Operation Turnabout" began to bear fruit.

These heartening results developed during a year in which no route expansion took place and growth was restricted by late deliveries of our DART 600's; nevertheless, thirty-two of our system's forty-one stations exceeded their 1965 revenues and twenty-five stations set record high passenger boarding marks. Including charter services, revenue passenger miles increased 33.4% over 1965 resulting in a passenger load factor rise of six points from 39.9% in 1965 to 45.9% during 1966. Revenue plane miles increased a modest 9.1%. This growth took place despite a heavy loss of traffic in July and August when two trunkline carriers with whom we normally interchange substantial amounts of traffic were on strike while our competitive trunkline carriers remained in full operation. Quick response to demand for government (military) charter movements averted financial loss during this period and accounts for our extraordinary gains in charter revenues. The performance of our DART 600 aircraft and the effort put forth by our operating and traffic personnel during this period was truly exceptional under abnormal circumstances. Our crews and equipment ranged from Miami to Northern Michigan and from El Paso to New York operating a total of 47 flights carrying 1,488 military personnel over 93,000 miles.

The eleventh DART 600 aircraft was delivered in December and by year end DART 600 service was being enjoyed by thirty-one of our forty-one stations. At year end, the operating fleet consisted of the eleven DARTS and nine DC-3s.

Passenger response to the increased speed, comfort and reliability of the DART is reflected in our traffic growth. Stringent budgetary controls coupled with the economy of the new aircraft resulted in steadily declining seat and ton mile costs. Seat mile costs in the first half of 1966 of 5.59¢ reduced to 5.05¢ during the second half. This trend is forecast to continue in 1967 with seat mile costs well below 5¢ per mile.

As stated, no route expansion took place in 1966; however, several seemingly minor operating restrictions were lifted during the year permitting (1) direct service from Dallas to our exclusively served cities in Oklahoma of Stillwater, Ponca City and Enid, (2) right to overfly Ft. Smith on direct service to Fayetteville and Joplin, and (3) new limited stop authority between Oklahoma City and Denver permitting first time DART 600 service in that market. The improved service which resulted from these and other schedule pattern changes have brought gratifying results in terms of new and longer haul traffic as reflected in an increase of average passenger haul from 207 miles in 1965 to 220 miles in 1966.

The Central Airlines Route 81 Investigation proceeded throughout 1966. The case was held in abeyance during the latter part of the year when a merger possibility with Ozark Air Lines was imminent. Following the abandonment of merger plans, the case proceeded and will go to hearing before an Examiner of the Civil Aeronautics Board in Oklahoma City on March 21, 1967. Final action by the Board will probably not occur in this case before 1968. In this case the Company, along with certain other air carriers, is an applicant for new route authority between Kansas City and Memphis via Springfield, Missouri and Little Rock; between Memphis and St. Louis; between Dallas and Amarillo via Wichita Falls; between Oklahoma City and Midland, Texas; and finally an extension of our route system south from Ft. Smith, Arkansas via Texarkana and Shreveport to the co-terminals of New Orleans and Houston.

Our application for route authority to add Chicago and St. Louis as co-terminal points with Kansas City on our Denver-Kansas City Segment 9 has recently received favorable attention from the Civil Aeronautics Board. A new route case styled the Central Airlines Chicago Entry Case in which Central is the only applicant has been set down for an expedited hearing during 1967. The initial flight operations contemplated by this authority include non-stop service to both Chicago (3 round trips daily) and St. Louis (2 round trips daily) from our exclusive Kansas cities of Topeka, Manhattan-Ft. Riley-Junction City and Salina. Hopefully, the award of this authority will coincide with the delivery (late 1967) of our two leased DC-9 aircraft permitting a substantial amount of the new service to be performed with pure jet equipment.

In the last quarter of 1966, the Board of Directors approved the upgrading and strengthening of the management team with the following appointments: Evan B. Lingle, Vice President, Industrial Relations; Richard A. Elliott, Vice President, Marketing; William R. Huffman, Assistant Vice President, Training; Paul F. Glover, Assistant Vice President, Maintenance and Engineering; James C. Dixson, Assistant Vice President, Traffic; and Richard B. Foulk, Assistant Vice President, Research. These fine executives average seventeen years experience in the airline industry.

A 2.9% increase in number of employees (882 versus 857) is noteworthy in view of the very substantial gains in all phases of our business. A great deal of credit is due each employee for the effort, hard work and loyalty demonstrated during a transitional year.

The experience and momentum gained in 1966 will carry forward into 1967. Early traffic results and cost levels indicate a very promising year. Diligent sales effort and customer service coupled with intelligent cost control practices should result in another record year in 1967 for the Company. The wonderful support given our Company by our shareholders, employees, customers and officials representing the six state area served by Central Airlines is most gratifying and its continuation is earnestly solicited.

Cordially yours,

Chairman of Board

President

YEAR OF THE DART 600

The introduction of the eleven Convair/DART 600s to the Central Airlines fleet and route system was the single most significant factor contributing to growth and financial recovery in 1966. In the last quarter of 1966, eighty-two (82%) percent of Central's customers were flying these DART 600 aircraft and service had been introduced to thirty-one of our system's forty-one stations.

Our customers were welcomed aboard a new and fresh airline. "Everything's new But the Sky We Fly" proudly announced new cabin interiors, all-season temperature control, stylish uniforms, stereophonic music, and food service to compliment quieter and faster flights. New customer facilities were installed at five new airport terminals and customer facilities at twenty-three other stations were modified to reflect the new image. In April, a new downtown ticket office was opened in Oklahoma City.

St. Louis and Bartlesville joined eleven other cities serviced by the Consolidated Reservations Center at Fort Worth. This facility now provides twenty-four hour telephone service to twelve on-line communities and the important off-line city of Chicago. 660,000 telephone calls were received in the Center in 1966 and cities served by this facility boarded sixty (60%) percent of the system's total passengers.

Perceptive and timely flight scheduling, combined with comprehensive marketing programs, succeeded in increasing average passenger haul from 207 miles in the fourth quarter of 1965 to 227 miles in the same 1966 quarter and passenger volume increased twenty-seven percent.

In 1966, passenger traffic between pairs of cities more than 200 miles apart increased 29%, while traffic between pairs under 200 miles increased 19%. Specific examples include Kansas City-Little Rock, up 56%; Dallas-Joplin, up 74%; Denver-Oklahoma City, up 100%; Stillwater-Dallas, up 419%; and Denver-Topeka, up 33%.

To stimulate traffic in markets over 200 miles, the $15 Flight Fare was introduced in March. This unique tariff provides a natural fare taper—a progressive fare reduction proportionate to the distance traveled, more relative to the cost of service provided. Roundtrip fare construction is derived by adding $15 to the one-way adult fare—hence its name. Peak period protection is provided by prohibiting travel on Friday or Sunday. In nine and a half months, the $15 Flight accounted for 24,800 passenger boardings, representing 12,400 roundtrip ticket sales of $44.00 each. Passenger travel averaged 328 miles one-way.

1966 will be remembered at Central as the year we moved from our historic position at the bottom of the regional carrier list of revenue passenger miles flown.

In addition to higher traffic volume and revenue, the team effort of Central's six major divisions in accomplishing the change to turbine flight equipment notched several benchmarks of progress in 1966:

(1) Average Aircraft Stage Length increased from 93 to 104 miles, up 12%.

(2) Fleet Speed increased from 141 to 155 m.p.h., up 10%.

(3) Average Length of Passenger Haul increased from 207 to 220 miles, up 6%.

(4) Revenue Ton Miles Flown increased from 9,987,000 to 13,187,000, up 32%.

(5) Revenue Ton Mile Costs decreased from $1.24 to $1.06, down 15%.

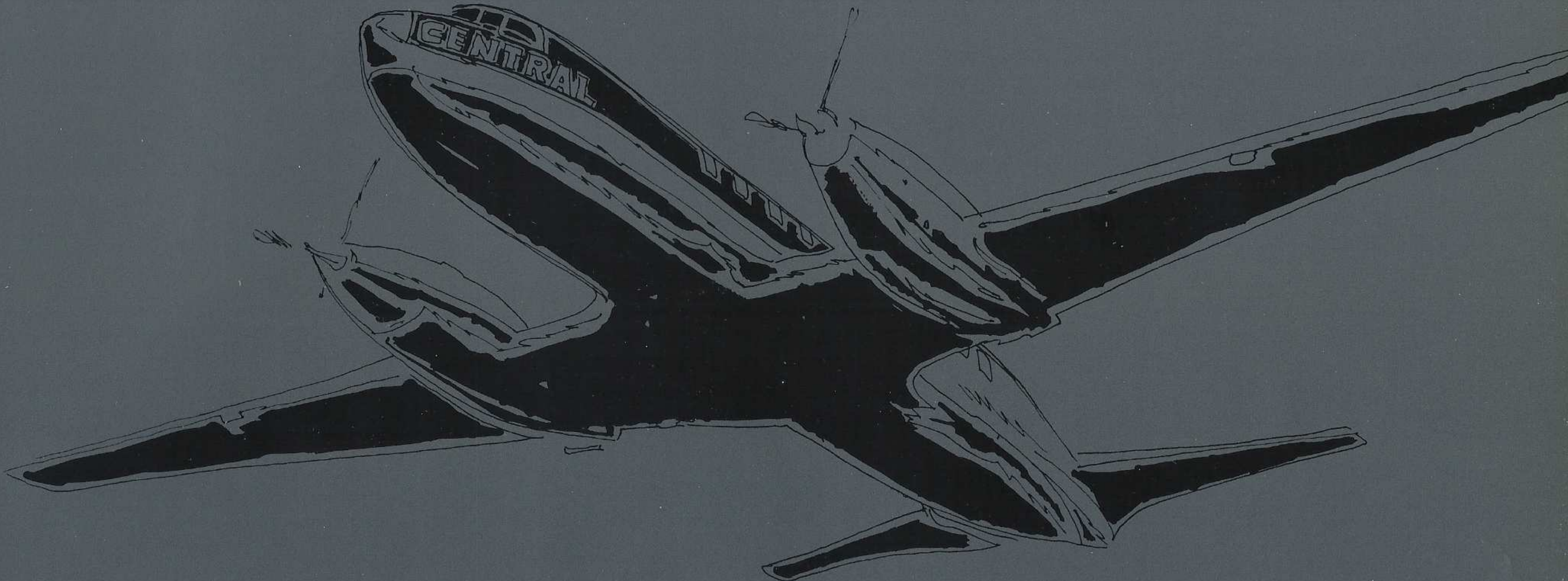
Since the foregoing comparison and others to follow in this report consist of year end figures for a mixed aircraft fleet, the following data highlights the impact of the full DART aircraft fleet compared with a similar 1965 period when the full fleet of piston Convair 240s were in service:

	Nov. 1965 CV-240	Nov. 1966 DART 600	Change Amount	Change %
Number of Aircraft	8	10	2	25
Utilization per Day (Hours)	6.5	8.4	1.9	29
Aircraft Hours Flown	1,562	2,528	966	62
Block Speed	161	190	29	18
Plane Miles	249,167	478,359	229,192	92
Passengers per Mile	16.4	19.1	2.7	16
Passenger Miles Flown (000)	4,098	9,111	5,013	122
Direct Cost per Plane Mile	96.4¢	85.6¢	(10.8¢)	(11)

In accomplishing these forward strides in 1966, Central Airlines led the industry in accumulated Rolls-Royce Dart-10 engine hours. The reliability of this turbine engine has been well established by its performance of 40,000 engine hours flown without a single premature removal. Time between engine overhaul of 1200 hours in the first quarter of 1966 had been extended to 2300 hours in December. Further extensions are anticipated in 1967.

Maintenance expense was controlled and external repair costs were reduced by increasing the number of aircraft components overhauled in our shops at Fort Worth and by transferring DC-3 maintenance from Kansas City to Fort Worth. By year end, DC-3 engine overhaul time had been extended from 1300 to 1400 hours and airframe overhaul time was extended from 13,500 to 14,250 hours.

A major flight training task was completed in 1966 by qualifying 68 Convair 240 and DC-3 pilots in DART 600 aircraft. Additionally, three Federal Aviation Agency Safety Agents received DART 600 ground school and flight training from Central.



82% OF OUR CUSTOMERS WERE DART PASSENGERS IN THE FOURTH QUARTER OF 1966

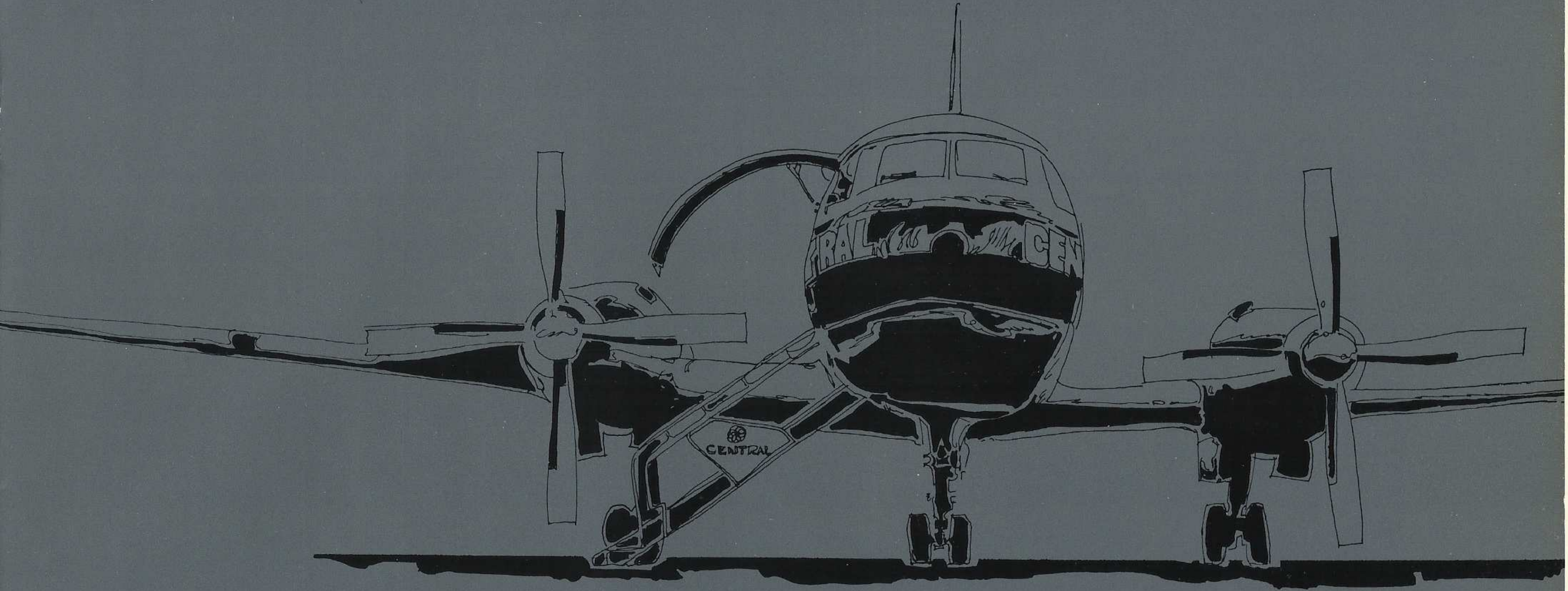
FIVE YEAR STATISTICAL & FINANCIAL SUMMARY

	% Change 1966/65	1966	1965	1964	1963	1962
Operating Statistics						
Passengers boarded	*24.1%*	545,950	440,030	413,381	386,699	334,208
Revenue Passenger Miles (000)	*33.4*	121,619	91,171	85,941	78,982	70,364
Revenue Plane Miles (000)	*9.1*	8,215	7,531	7,726	7,238	7,294
Available Seat Miles (000)	*15.5*	264,758	229,307	222,040	197,899	187,463
Passenger Load Factor	*15.0*	45.9%	39.9%	38.7%	39.9%	37.5%
Statement of Income (000)[1]						
Commercial Revenues	*28.3*	$ 10,275	$ 8,010	$ 7,196	$ 6,395	$ 5,903
Public Service Revenues	*11.5*	4,610	4,136	4,257	4,218	4,505
Total	*22.6*	14,885	12,146	11,453	10,613	10,408
Operating Expenses	*13.6*	14,014	12,336	11,240	10,100	10,025
Operating Income (Loss)	—	871	(190)	213	513	383
Net Income (Loss)	—	$ 405	$(3)	$ 60	$ 97	$ 143
Balance Sheet (000)						
Working Capital (excl. of notes payable to banks)	—	$(249)	$ 22	$(384)	$(179)	$(277)
Operating Property and Equipment	*94.5*	11,220	5,770	2,912	1,881	2,042
Other Assets (Net)	*127.3*	366	161	225	233	265
Total Net Assets	*90.4*	$ 11,337	$ 5,953	$ 2,753	$ 1,935	$ 2,030
Long Term Debt	*111.8*	$ 9,400	$ 4,439	$ 1,755	$ 1,010	$ 1,190
Convertible Debentures	—	500	500	—	—	—
Stockholders' Equity	*41.7*	1,437	1,014	998	925	840
Total Debt and Equity	*90.4*	$ 11,337	$ 5,953	$ 2,753	$ 1,935	$ 2,030
Share Information						
Shares Outstanding	*5.8*	1,499,285[3]	1,417,391	1,406,289	1,325,842	1,254,800[2]
Book Value per Share	*33.3*	$ .96	$ .72	$ .71	$ .70	$ .67
Net Income per Share	*N/A*	$ .27	$ —	$ .04	$ .07	$ .11
Other Information						
Public Service Revenue as % of Comm. Rev.	*(13.2)*	44.8%	51.6%	59.2%	66.0%	76.3%
Passenger Load per Aircraft Mile	*21.3*	14.8	12.2	11.0	10.9	9.6
Average Number of Employees	*2.9*	882	857	798	771	793

1 Statements of Income for 1965 and prior years as well as Stockholders' equity, restated so as to reflect in each applicable year the out-of-period adjustments, including the Extraordinary Charge ($243,921) less tax effect, reflected in 1965 accounts. 1966 Net Income includes Special Credit of $38,000

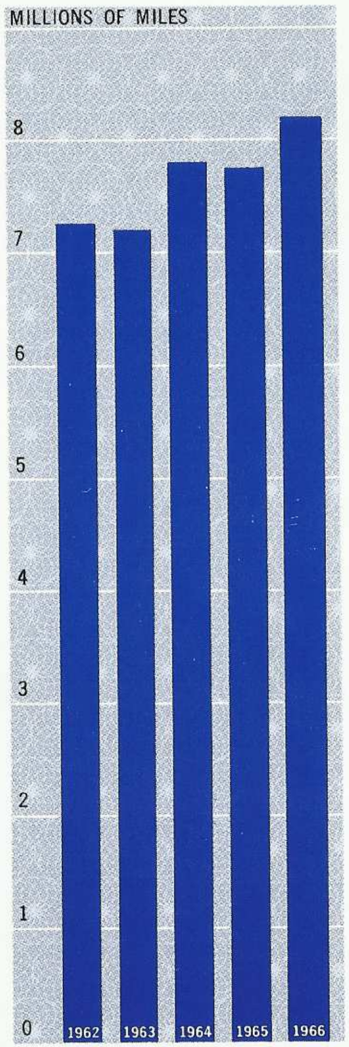
2 Adjusted to give effect to two-for-one stock split in July 1963.

3 Includes 71,394 shares issued as a 5% stock dividend on January 12, 1967 to stockholders of record on December 30, 1966.

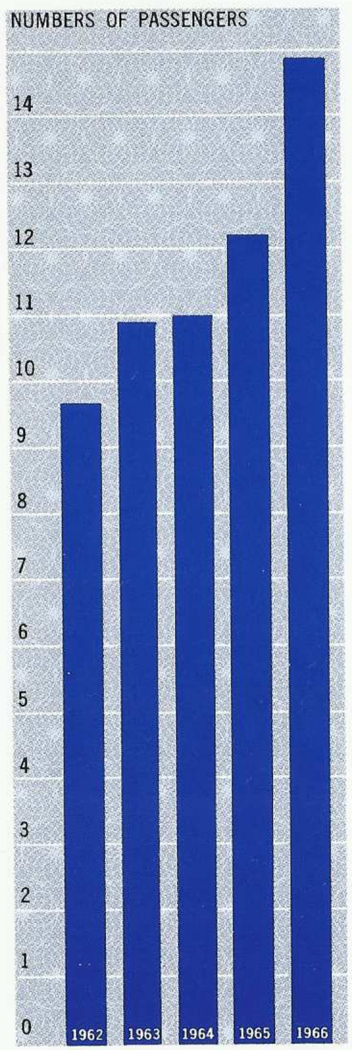


105,920 MORE PASSENGERS FLEW CENTRAL IN 1966

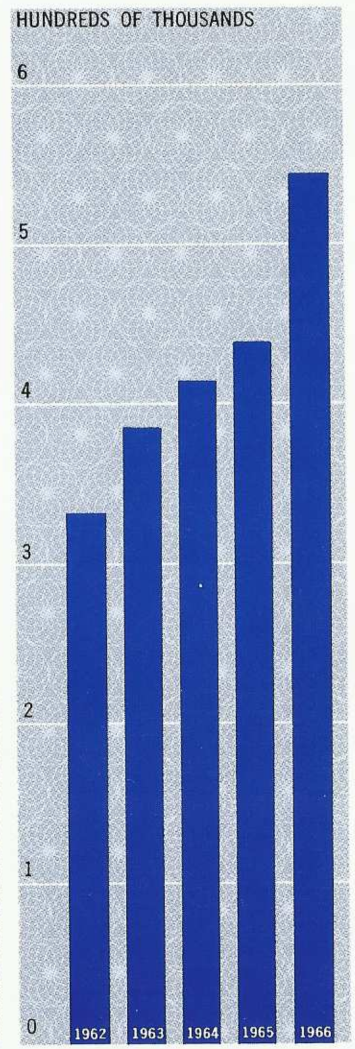
AIRCRAFT MILES FLOWN



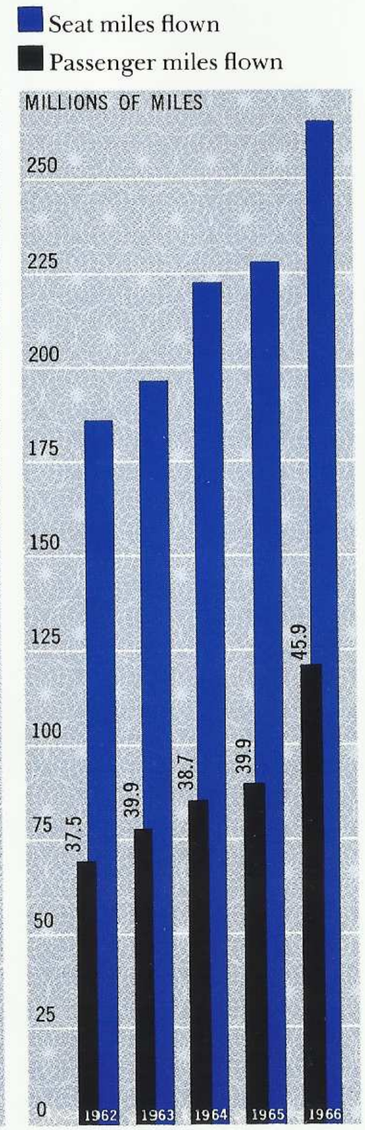
PASSENGER LOAD PER AIRCRAFT MILE



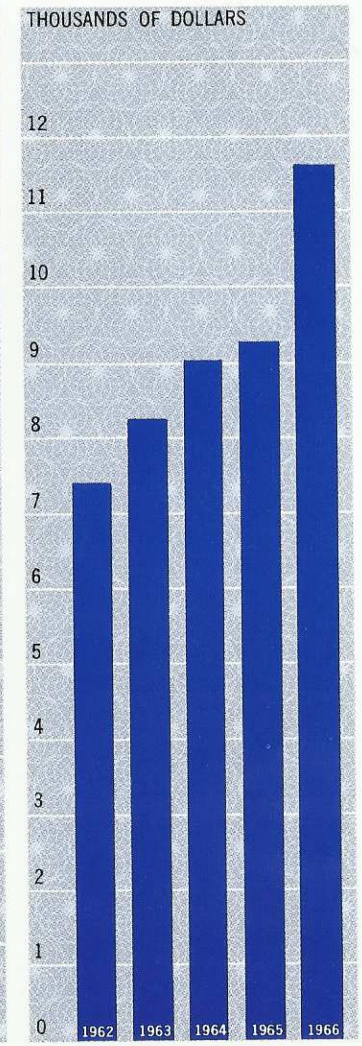
SYSTEM PASSENGERS BOARDED



PASSENGER LOAD FACTOR

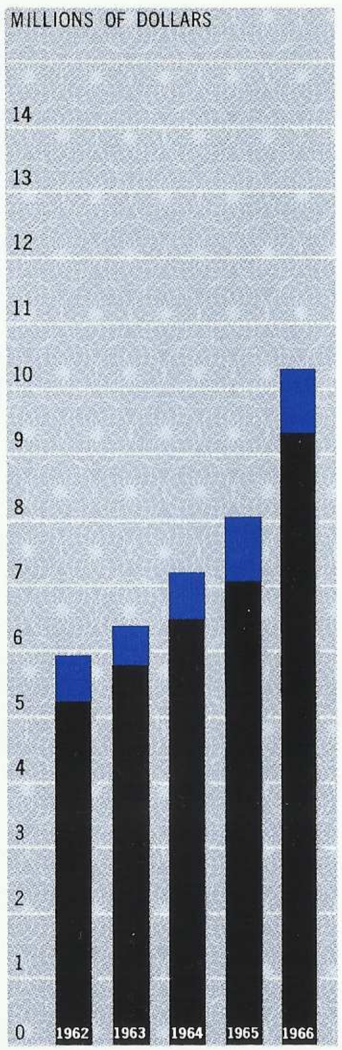


COMMERCIAL REVENUE PER EMPLOYEE



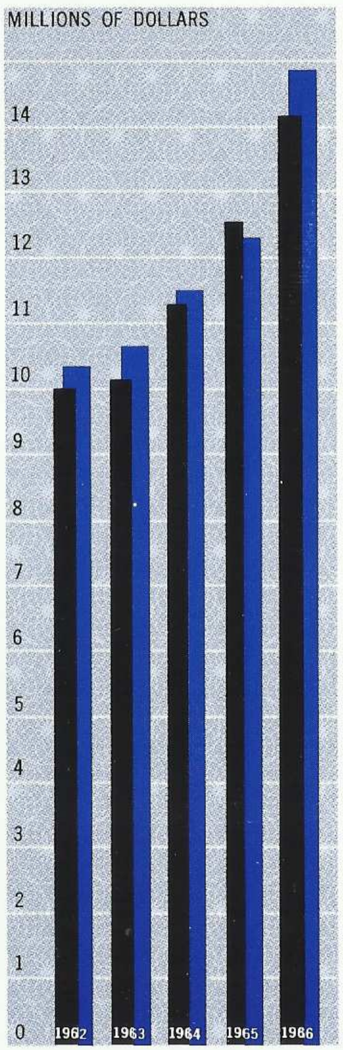
COMMERCIAL REVENUE

Cargo & Incidental
Passenger



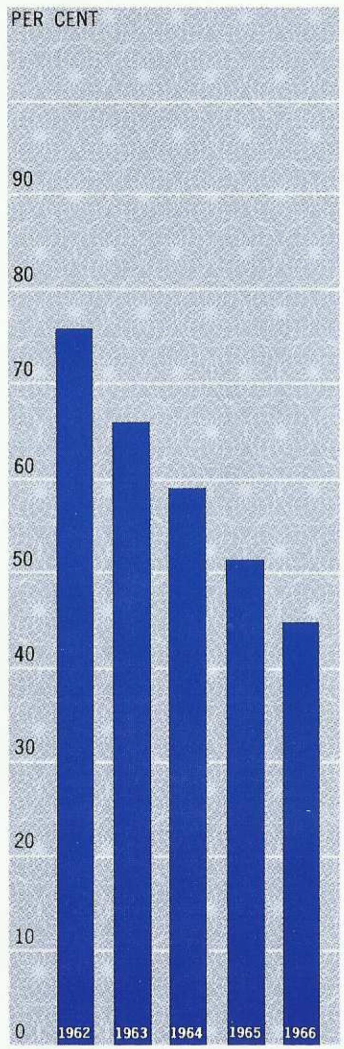
OPERATING INCOME/LOSS

Operating revenue
Operating expense



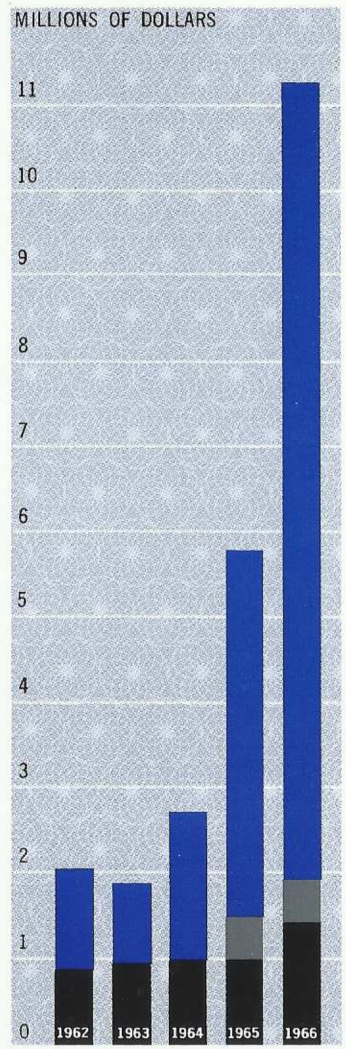
PUBLIC SERVICE REVENUE

As % of commercial revenue



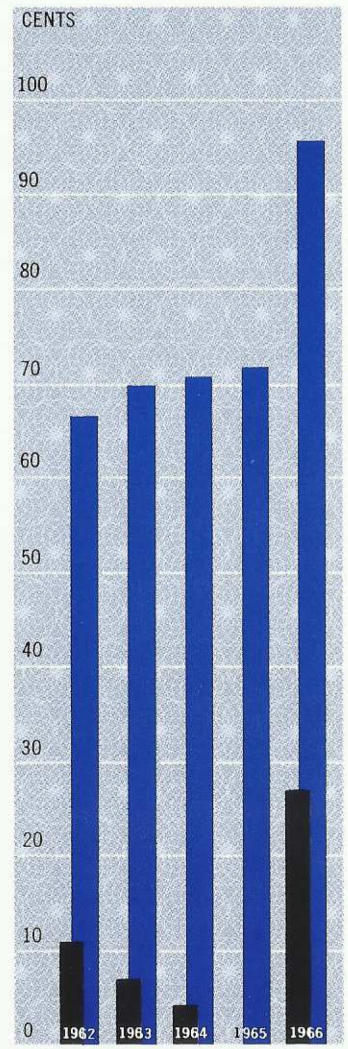
TOTAL INVESTMENT

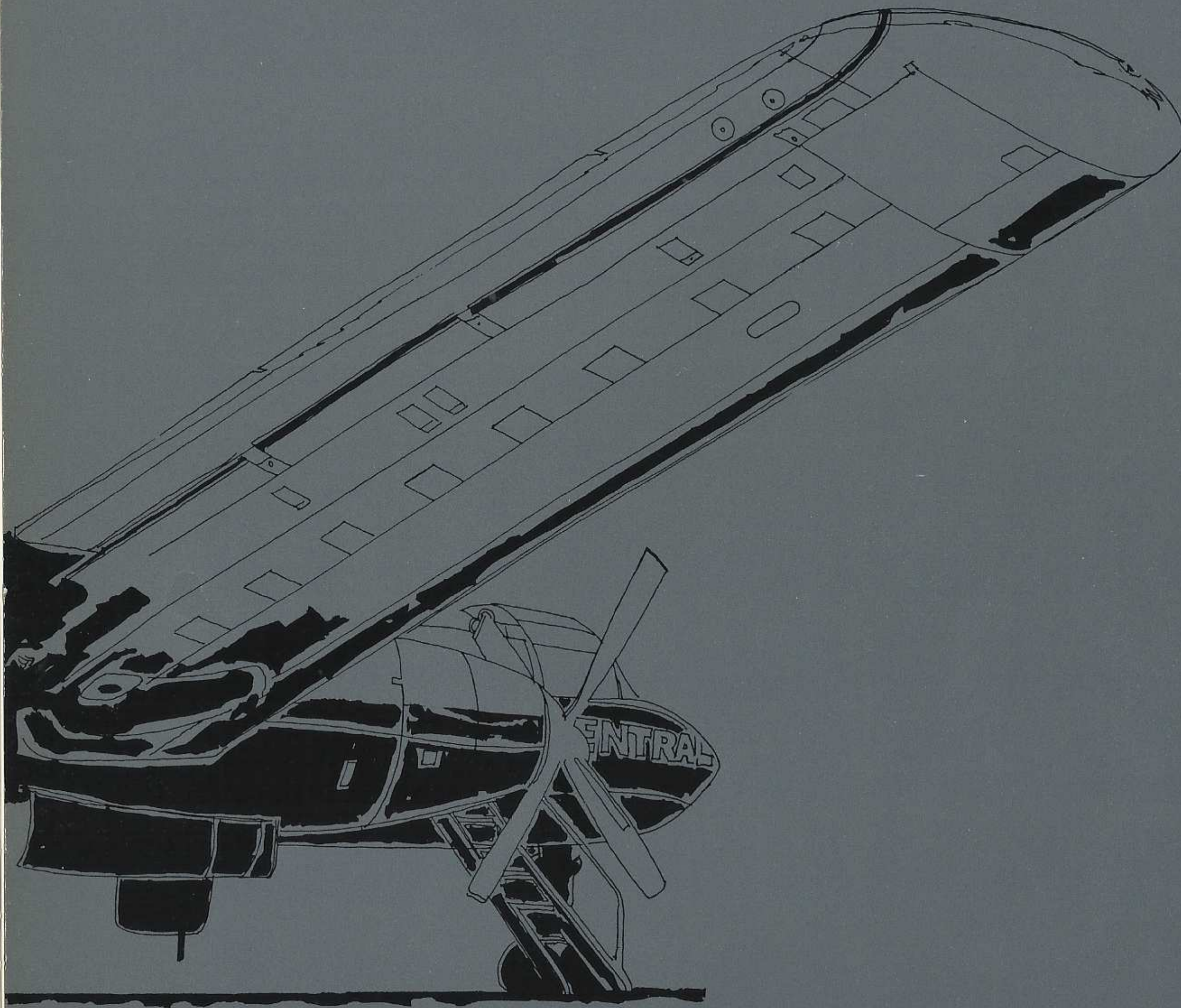
Debentures
Long term debt
Stockholders equity



EQUITY VS. INCOME PER SHARE

Book value per share
Net income per share





1966 INCOME EXCEEDED COMBINED INCOME OF THE FOUR PREVIOUS YEARS

CENTRAL AIRLINES, INC. COMPARATIVE STATEMENT OF OPERATIONS

For the year ended December 31

	1966	1965 (Restated see Note 1)
Operating revenues:		
Passenger	$ 9,234,750	$ 7,187,371
Express and freight	530,756	467,847
Mail	328,206	256,462
Other	181,611	98,524
	10,275,323	8,010,204
Public service revenue	4,610,000	4,136,382
	14,885,323	12,146,586
Operating expenses:		
Flying operations	3,813,507	3,613,494
Maintenance	2,705,705	2,590,301
Passenger service	690,884	613,137
Aircraft and traffic servicing	4,147,823	3,539,479
Promotion and sales	1,070,577	905,194
General and administrative	736,997	703,975
Depreciation	774,200	293,901
Amortization and obsolescence	74,747	76,797
	14,014,440	12,336,278
Operating income (loss)	870,883	(189,692)
Non-operating (deductions) and income:		
Interest expense, less amounts capitalized as part of Dart 600 conversion program ($58,410 in 1966 and $38,567 in 1965)	(415,208)	(108,520)
Other income less miscellaneous deductions	46,170	23,173
	(369,038)	(85,347)
Income (loss) before income taxes	501,845	(275,039)
Income tax (provision) refund, including investment tax credit of $55,000 in 1966 and $91,000 in 1965 (Note 2)	(135,000)	271,953
Income (loss) before extraordinary credit	366,845	(3,086)
Extraordinary credit (Note 6)	38,000	
Net income (loss)	$ 404,845	($ 3,086)

STATEMENT OF STOCKHOLDERS' EQUITY

	Common stock-12½ cents par value Shares	Common stock-12½ cents par value Amount	Capital in excess of par value	Retained earnings (Restated see Note 1)	Total
Balance at December 31, 1964	1,406,289	$175,786	$ 662,556	$160,546	$ 998,888
Net loss for the year 1965				(3,086)	(3,086)
Exercise of employee stock options	11,102	1,388	17,152		18,540
Balance at December 31, 1965	1,417,391	177,174	679,708	157,460	1,014,342
Net income for the year 1966				404,845	404,845
Exercise of employee stock options (Note 5)	10,500	1,313	17,062		18,375
5% stock dividend issued on January 12, 1967	71,394	8,924	428,364	(437,288)	
Balance at December 31, 1966	1,499,285	$187,411	$1,125,134	$125,017	$1,437,562

CENTRAL AIRLINES, INC. COMPARATIVE BALANCE SHEET

ASSETS

	December 31 1966	December 31 1965
Current Assets: —		
Cash	$ 926,533	$ 547,754
Accounts receivable:		
Airline traffic and other	1,088,027	922,601
U. S. Government	798,380	693,694
Refundable federal income tax (Note 2)	131,815	430,543
Replacement parts and operating supplies, at average cost less allowance for obsolescence	423,153	341,427
Prepaid expenses	76,113	68,510
Total current assets	3,444,021	3,004,529
Investments and special deposits	84,832	14,211
Property and equipment, at cost (Note 3)		
Flight equipment	12,931,822	6,018,801
Ground and other equipment	1,027,110	879,428
	13,958,932	6,898,229
Accumulated depreciation and amortization	2,632,394	2,320,621
	11,326,538	4,577,608
Construction in progress and equipment deposits	3,156	1,192,550
	11,329,694	5,770,158
Other assets:		
Route development and preoperating costs, less accumulated amortization	180,747	156,905
Unamortized debt issue expense	2,968	3,396
	183,715	160,301
	$15,042,262	$8,949,199

See accompanying notes

CENTRAL AIRLINES, INC. COMPARATIVE BALANCE SHEET

LIABILITIES & STOCKHOLDERS' EQUITY

	Shares 1966	Shares 1965	December 31, 1966	December 31, 1965
Current liabilities:				
Accounts payable			$ 1,285,290	$ 909,255
Airline traffic accounts payable			1,501,284	1,524,651
Accrued and other liabilities			745,017	506,236
Income taxes payable			97,000	
Unearned transportation revenue			64,000	42,000
Current maturities of long-term notes payable to banks (Note 3)			1,220,000	378,000
Total current liabilities			4,912,591	3,360,142
Long-term debt:				
Notes payable to banks (Note 3)			8,180,000	4,060,500
6% convertible subordinated debentures, due June 15, 1975 (Note 4)			500,000	500,000
Other			12,109	14,215
			8,692,109	4,574,715
Stockholders' equity, per accompanying statement: —				
Common stock, 12½ cents par value (Note 5)				
Authorized	3,000,000	2,000,000		
Issued	1,499,285*	1,417,391	187,411	177,174
Capital in excess of par value			1,125,134	679,708
Retained earnings (Note 3)			125,017	157,460
			1,437,562	1,014,342
Commitments (Note 7)				
			$15,042,262	$8,949,199

**Including 71,394 shares issued on January 12, 1967 as a 5% stock dividend.*

See accompanying notes

CENTRAL AIRLINES

CENTRAL AIRLINES, INC. NOTES TO FINANCIAL STATEMENTS

December 31, 1966

NOTE 1—RESTATEMENT OF 1965 STATEMENT OF OPERATIONS:

The following amounts have been restated directly to retained earnings as of December 31, 1964:
Shown as extraordinary charge in 1965
Statement of Operations:
Writeoff of costs deferred in prior years for route development and pilot training ($130,728); retroactive adjustment of 1962 and 1963 public service revenues ($79,030); writeoff of unrecoverable claim for maintenance warranty ($34,163) $243,921

Income tax adjustments, principally relating to above amounts . . . . (60,084)

Net restatement $183,837

NOTE 2—FEDERAL INCOME TAX:

There are certain differences between the company's financial and taxable income; the more important 1966 and 1965 differences are summarized below:

Financial income exceeds taxable income	Year ended December 31, 1966	Year ended December 31, 1965
Excess of route development and preoperating expenditures (deducted for tax purposes) over related amortization of amounts deferred for financial accounting purposes	$21,672	$71,342
Capitalized interest (deducted for tax purposes) relating to Dart 600 conversion program, net of depreciation	52,796	38,567
Excess of market value over stock option price at exercise date with respect to common stock purchased by former officer (Note 6)	99,156	

Deferred income tax has not been recorded by the company for the foregoing or for similar differences arising in prior years. Under accounting procedures prescribed by the Civil Aeronautics Board for local service carriers, deferred tax accounting for certain tax and financial accounting differences (such as capitalized interest) is prohibited. In other cases (such as route development and preoperating expenses) the Board discourages, but does not prohibit, accrual of deferred income tax. The Board's opposition to recording deferred tax is based on its policy not to recognize deferred tax accruals for subsidy rate-making purposes and to determine such subsidies "on the basis of taxes actually incurred."

If the Board required deferred tax accounting, accumulated deferred federal income tax at December 31, 1964, 1965 and 1966 would be approximately $45,000, $100,000 and $130,000, respectively.

The unused portion of the 1965 and 1966 investment tax credit (approximately $554,000) applicable to the purchases and modification of flight equipment is not recorded in the accompanying financial statements.

Refundable federal income tax at December 31, 1966 reflected in the accompanying balance sheet arises from:

1965 operating loss carried back to prior years	$ 57,815
1965 investment credit carried back to prior years	74,000
	$131,815

NOTE 3—FIRST MORTGAGE EQUIPMENT LOANS:

Notes payable to banks consist of the following first mortgage equipment loans:

	Current portion	Long-term portion
5½%—Mercantile National Bank . .	$1,040,000	$7,260,000
6% —Chase Manhattan Bank .	60,000	440,000
7½%—Chase Manhattan Bank .	120,000	480,000
	$1,220,000	$8,180,000

The above notes are being repaid in aggregate quarterly instalments of $305,000 plus interest beginning January 1, 1967. The loans are secured by a first lien chattel mortgage on all flight equipment and the related loan agreements provide certain restrictions as to additional debt, net worth, cash dividends, equipment purchases and leases and minimum working capital. No common stock cash dividends can be paid without permission of the banks while these loans are outstanding.

As of December 31, 1966 the company is in default with respect to minimum working capital requirements of the above loan agreements; however, the lenders have waived the default which existed at December 31, 1966 and indicated their intention not to accelerate maturities of the notes at this time or in the foreseeable future. The lenders did, however, specifically reserve all rights granted under the loan agreements, including the right to accelerate note maturities.

NOTE 4—6% CONVERTIBLE SUBORDINATED DEBENTURES:

Under the terms of an indenture, 6% debentures were issued on June 15, 1965 in the principal amount of $500,000 with interest payable quarterly beginning September 15, 1965 until June 15, 1975, at which date the unpaid principal amount is due. The debentures are convertible into common stock of the company at the option of the holder at prices ranging between $3.50 and $8.00 per share to maturity. The debentures may be redeemed by the company in whole or in part at any time between June 15, 1969 and June 14, 1975 at principal amount and accrued interest plus redemption premiums ranging from 6% to 1% of unpaid principal amount.

The debentures are subordinate to all senior indebtedness as defined in the indenture.

NOTE 5—COMMON STOCK:

Of the 79,500 shares of common stock (including reinstatement of 9,500 share option, see Note 6) under option at December 31, 1965, options were

CENTRAL AIRLINES, INC. NOTES TO FINANCIAL STATEMENTS Cont.

exercised during 1966 for 10,500 shares at $1.75 per share. At December 31, 1966 unissued shares were reserved for the following purposes:

	Number of shares
Conversion of 6% convertible subordinated debentures (Note 4)	142,855
Stock options granted by the board of directors in 1965 (and expiring in 1971) to three officers, exercisable at $1.75 per share (market value at dates of grant was approximately $2.75) in cumulative instalments of one-fifth of the optioned shares per year beginning in 1966	69,000
	211,855

NOTE 6—EXTRAORDINARY CREDIT:

A former officer filed a suit against the company in 1965, claiming damages arising from the termination of an employment contract and the resulting loss of the right to exercise an option to purchase 42,500 shares of common stock. The suit was settled in 1966 by granting the former officer the right to purchase 9,500 shares of the stock at his option price of $1.75 per share. As a result of this transaction, the company is entitled to an income tax deduction of approximately $99,000 comprising the excess of the over-the-counter market value of the shares purchased by the officer over the aggregate option price thereof. The reduction of income taxes ($38,000) attributable to this deduction is shown as an extraordinary credit in the 1966 statement of operations.

NOTE 7—COMMITMENTS:

At December 31, 1966 the company is committed to lease two DC-9 aircraft for a two year period at an aggregate annual rental of $864,000. The lease terms provide that the company pay to the lessor rental deposits aggregating $216,000 prior to delivery of the aircraft. As of December 31, 1966, $72,000 of this deposit had been paid to the lessor. Integration of the DC-9 aircraft into the company's fleet will require additional expenditures of approximately $1,300,000 for costs of spare engines and other parts, miscellaneous ground equipment and personnel training.

Rental commitments with respect to the long-term leases on various facilities total $3,100,000 at December 31, 1966 and are payable at the approximate annual rates of $200,000 through 1977 and $140,000 from 1978 through 1984.

NOTE 8—PENSION PLANS:

The company has two pension plans covering all pilots with one or more years of service. The plans were converted from contributory to non-contributory plans in May 1964 and May 1965, respectively. Pension costs charged to operations were approximately $245,000 in 1966 and $175,000 in 1965. On the basis of actuarial calculations (determined under the unit credit method), past service liability has been fully funded as of December 31, 1966.

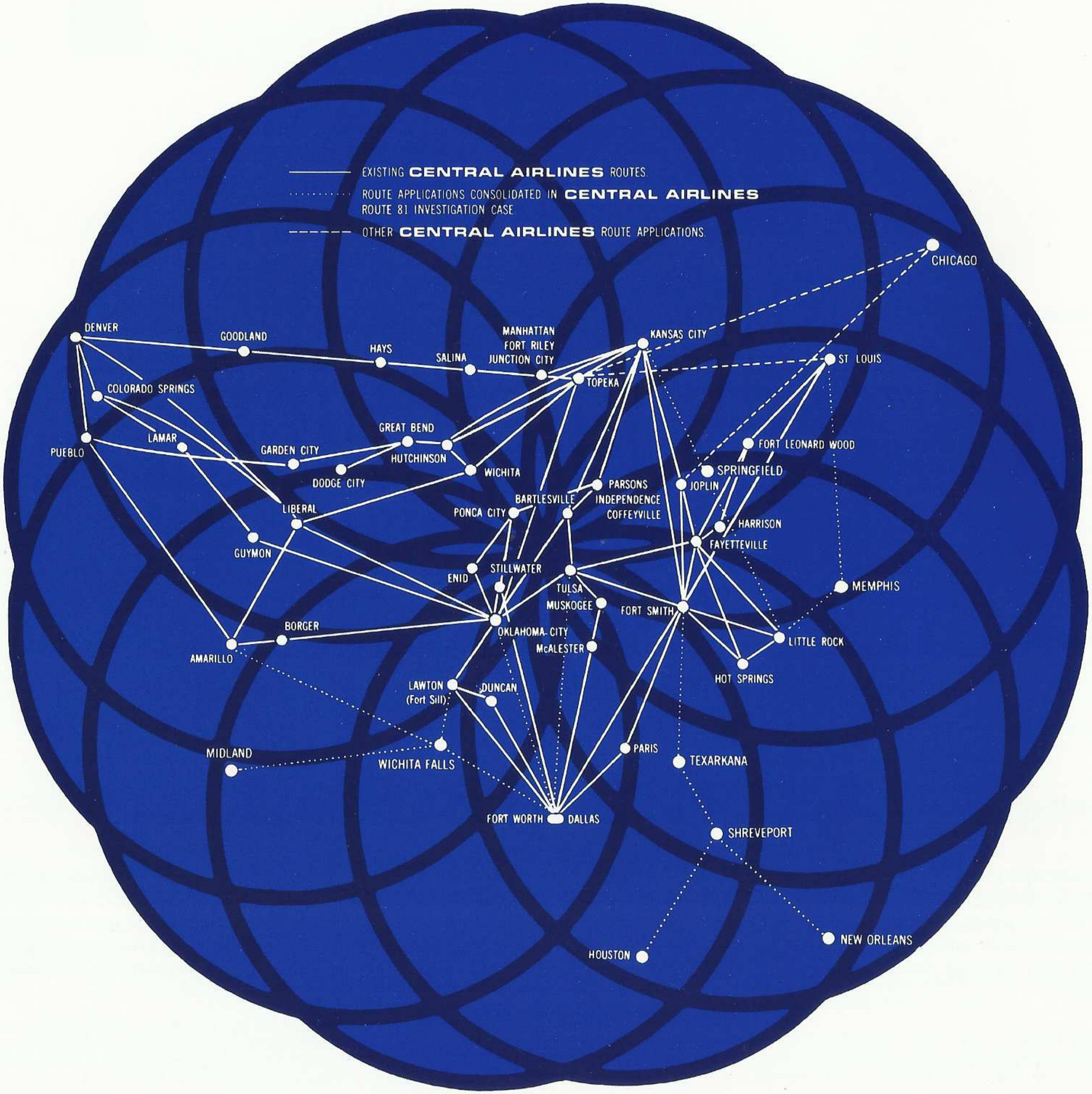
ACCOUNTANTS REPORT

To the Board of Directors of
Central Airlines, Incorporated

In our opinion, the accompanying balance sheet and the related statements of operations and stockholders' equity present fairly the financial position of Central Airlines, Incorporated at December 31, 1966 and the results of its operations for the year in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Our examination of these statements was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Dallas, Texas
February 17, 1967

Price Waterhouse & Co.


EXISTING CENTRAL AIRLINES ROUTES.
ROUTE APPLICATIONS CONSOLIDATED IN CENTRAL AIRLINES ROUTE 81 INVESTIGATION CASE
OTHER CENTRAL AIRLINES ROUTE APPLICATIONS.
CHICAGO
DENVER
GOODLAND
HAYS
SALINA
MANHATTAN
FORT RILEY
JUNCTION CITY
KANSAS CITY
ST LOUIS
TOPEKA
COLORADO SPRINGS
GREAT BEND
LAMAR
PUEBLO
GARDEN CITY
HUTCHINSON
FORT LEONARD WOOD
SPRINGFIELD
DODGE CITY
WICHITA
PARSONS
JOPLIN
BARTLESVILLE
INDEPENDENCE
COFFEYVILLE
LIBERAL
PONCA CITY
HARRISON
FAYETTEVILLE
GUYMON
STILLWATER
ENID
TULSA
MEMPHIS
MUSKOGEE
FORT SMITH
BORGER
OKLAHOMA CITY
McALESTER
LITTLE ROCK
AMARILLO
HOT SPRINGS
LAWTON
(Fort Sill)
DUNCAN
PARIS
MIDLAND
TEXARKANA
WICHITA FALLS
FORT WORTH
DALLAS
SHREVEPORT
NEW ORLEANS
HOUSTON