UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-K
(Mark One)
X ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [NO FEE REQUIRED]
For the fiscal year ended December 31, 1998
OR
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [NO FEE REQUIRED]
For the transition period from . . . . to . . . .

Commission File Number 1-8957
ALASKA AIR GROUP, INC.
(Exact name of registrant as specified in its charter)

Delaware 91-1292054
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

19300 Pacific Highway South, Seattle, Washington 98188
(Address of Principal Executive Offices)
Registrant's telephone number, including area code: (206) 431-7040

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $1.00 Par Value	New York Stock Exchange
Rights to Purchase Series A Participating Preferred Stock	New York Stock Exchange

As of December 31, 1998, common shares outstanding totaled 26,224,005. The aggregate market value of the common shares of Alaska Air Group, Inc. held by nonaffiliates, 26,156,752 shares, was approximately $1.157 billion (based on the closing price of these shares, $44.25, on the New York Stock Exchange on such date).

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 X 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. (X)

DOCUMENTS TO BE INCORPORATED BY REFERENCE

Title of Document	Part Hereof Into Which Document to be Incorporated
Definitive Proxy Statement Relating to 1999 Annual Meeting of Shareholders	Part III

Exhibit Index begins on page 35.

PART I

ITEM 1. BUSINESS

GENERAL INFORMATION
Alaska Air Group, Inc. (Air Group or the Company) is a holding company that was incorporated in Delaware in 1985. Its two principal subsidiaries are Alaska Airlines, Inc. (Alaska) and Horizon Air Industries, Inc. (Horizon). Both subsidiaries operate as airlines, although their business plans, competition and economic risks differ

substantially. Alaska is a major airline, operates an all jet fleet, and its average passenger trip length is 864 miles. Horizon is a regional airline, operates jet and turboprop aircraft, and its average passenger trip is 260 miles. Individual financial information for Alaska and Horizon is reported in Note 11 to Consolidated Financial Statements. Air Group's executive offices are located at 19300 Pacific Highway South, Seattle, Washington 98188. The business of the Company is somewhat seasonal. Quarterly operating income tends to peak during the third quarter.

Alaska

Alaska Airlines is an Alaska corporation that was organized in 1932 and incorporated in 1937. Alaska serves 35 cities in six states (Alaska, Washington, Oregon, California, Nevada and Arizona), one city in Canada and five cities in Mexico. In each year since 1973, Alaska has carried more passengers between Alaska and the U.S. mainland than any other airline. In 1998, Alaska carried 13.1 million passengers. Passenger traffic within Alaska and between Alaska and the U.S. mainland accounted for 25% of Alaska's 1998 revenue passenger miles, West Coast traffic (including Vancouver, Canada) accounted for 67% and the Mexico markets 8%. Based on passenger enplanements, Alaska's leading airports are Seattle, Portland, Los Angeles and Anchorage. Based on revenues, its leading nonstop routes are Seattle-Anchorage, Seattle-Los Angeles and Seattle-San Diego. At December 31, 1998, Alaska's operating fleet consisted of 84 jet aircraft. The majority of Alaska flights, and certain Northwest Airlines flights, are dual-designated in airline computer reservation systems as Alaska Airlines and Northwest Airlines in order to facilitate feed traffic between the two airlines. Alaska Airlines also serves six smaller cities in California, six in Washington, two in Oregon and many small communities in Alaska through code share marketing agreements with local commuter carriers. In October 1998, Alaska suspended its service to Russia due to economic instability in Russia.

Horizon

Horizon, a Washington corporation, began service in 1981 and was acquired by Air Group in 1986. It is the largest regional airline in the Pacific Northwest, and serves 33 cities in five states (Washington, Oregon, Montana, Idaho, and California) and five cities in Canada. In 1998, Horizon carried 4.4 million passengers. Based on passenger enplanements, Horizon's leading airports are Seattle, Portland, Spokane and Boise. Based on revenues, its leading nonstop routes are Seattle-Portland, Seattle-Spokane and Seattle-Boise. At December 31, 1998, Horizon's operating fleet consisted of 20 jet and 40 turboprop aircraft, with the jets providing 58% of the 1998 capacity. Horizon flights are listed under the Alaska Airlines designator code in airline computer reservation systems. Most Horizon flights are also dual-designated in these reservation systems as Northwest Airlines and Alaska Airlines. In 1998, 25% of Horizon's passengers connected to Alaska and 7% connected to Northwest.

Alaska and Horizon integrate their flight schedules to provide the best possible service between any two points served by their systems. Both airlines distinguish themselves from competitors by providing a higher level of customer service. The airlines' excellent service in the form of advance seat assignments, attention to customer needs, high-quality food and beverage service, well-maintained aircraft a first class section aboard Alaska aircraft and other amenities is regularly recognized by independent studies and surveys of air travelers. Alaska and Horizon offer competitive fares.

BUSINESS RISKS

The Company's operations and financial results are subject to various uncertainties, such as intense competition, volatile fuel prices, a largely unionized labor force, the need to finance large capital expenditures, government regulation, potential aircraft incidents and general economic conditions.

Competition

Competition in the air transportation industry is intense. Any domestic air carrier deemed fit by the DOT is allowed to operate scheduled passenger service in the United States. Together, Alaska and Horizon carry 2.5% of all U.S. domestic passenger traffic. Alaska and Horizon compete with one or more domestic or foreign airlines on most of their routes. Some of these competitors are substantially larger than Alaska and Horizon, have greater financial resources and have more extensive route systems. Due to its shorthaul markets, Horizon also competes with the automobile.

Most major U.S. carriers have developed, independently or in partnership with others, large computerized reservation systems (CRS). Airlines, including Alaska, and Horizon, are charged industry-set fees to have their flight schedules included in the various CRS displays used by travel agents and airlines. These systems are currently the predominant means of distributing airline tickets. In order to reduce anti-competitive practices, the DOT regulates the display of all airline schedules and fares.

Fuel

Fuel costs were 11.4% of the Company's total operating expenses in 1998. Fuel prices, which can be volatile and are largely outside of the Company's control, can have a significant impact on the Company's operating results. Currently, a one cent change in the fuel price per gallon affects annual fuel costs by approximately $3.5 million. The Company has in the past hedged against its exposure to fluctuations in the price of jet fuel, but does not currently do so. The Company evaluates hedging strategies on an ongoing basis.

Unionized Labor Force

Labor costs were 35% of the Company's total operating expenses in 1998. Wage rates can have a significant impact on the Company's operating results. At December 31, 1998, labor unions represented 87% of Alaska's and 45% of Horizon's employees. The air transportation industry is regulated under the Railway Labor Act, which vests in the National Mediation Board certain regulatory powers with respect to disputes between airlines and labor unions. The Company cannot predict the outcome of union contract negotiations nor control the variety of actions (e.g. work stoppage or slowdown) unions might take to try to influence those negotiations.

Leverage and Future Capital Requirements

The Company, like many airlines, is relatively highly leveraged, which increases the volatility of its earnings. Due to its high fixed costs, including aircraft lease commitments, a decrease in revenues results in a disproportionately greater decrease in earnings. In addition, the Company has an ongoing need to finance new aircraft deliveries and there is no assurance that such financing will be available in sufficient amounts or on acceptable terms. See Item 7 for management's discussion of liquidity and capital resources.

Government Regulation; International Routes

Like other airlines, the Company is subject to regulation by the Federal Aviation Administration (FAA) and the United States Department of Transportation (DOT). The FAA, under its mandate to ensure aviation safety, can ground aircraft, suspend or revoke the authority of an air carrier or its licensed personnel for failure to comply with Federal Aviation Regulations and levy civil penalties. The DOT has the authority to regulate certain airline economic functions including financial and statistical reporting, consumer protection, computerized reservations systems, essential air transportation and international route authority. The Company is subject to bilateral agreements between the United States and the foreign countries to which the Company provides service. There can be no assurance that existing bilateral agreements between the United States and the foreign governments will continue or that the Company's designation to operate such routes will continue.

Risk of Loss and Liability; Weather
The Company is exposed to potential catastrophic losses in the event of aircraft accidents or terrorist incidents. Consistent with industry standards, the Company maintains vigorous safety, training and maintenance programs, as well as insurance against such losses. However, any aircraft accident, even if fully insured, could cause a negative public perception of the Company with adverse financial consequences. Unusually adverse weather can significantly reduce flight operations, resulting in lost revenues and added expenses.

OTHER INFORMATION
Frequent Flyer Program
All major airlines have developed frequent flyer programs as a way of increasing passenger loyalty. Alaska's Mileage Plan allows members to earn mileage by flying on Alaska, Horizon and other participating airlines, and by using the services of non-airline partners, which include a credit card partner, telephone companies, hotels and car rental agencies. Alaska is paid by non-airline partners for the miles it credits to member accounts. Alaska has the ability to change the Mileage Plan terms, conditions, partners, mileage credits and award levels.

Mileage can be redeemed for free or discounted travel and for other travel industry awards. Upon accumulating the necessary mileage, members notify Alaska of their award selection Over 70% of the flight awards selected are subject to blackout dates and capacity-controlled seating. Unlike many other airlines, Alaska's miles do not expire. As of the year-end 1997 and 1998, Alaska estimates that 652,000 and 812,000 round trip flight awards could have been redeemed by Mileage Plan members who have mileage credits exceeding the 20,000 mile free round trip domestic ticket award threshold. At December 31, 1998, fewer than 4% of these flight awards were issued and outstanding. For the years 1996, 1997 and 1998, approximately 173,000, 185,000 and 191,000 round trip flight awards were redeemed and flown on Alaska and Horizon. These awards represent approximately 4.4% for 1996, 3.2% for 1997, and 3.1% for 1998, of the total passenger miles flown for each period.

Alaska maintains a liability for its Mileage Plan obligation that is based on its total miles outstanding, less an estimate for miles that will never be redeemed. The net miles outstanding are allocated between those credited for travel on Alaska, Horizon or other airline partners and those credited for using the services of non-airline partners. Miles credited for travel on Alaska, Horizon or other airline partners are accrued at Alaska's incremental cost of providing the air travel. The incremental cost includes the cost of meals, fuel, reservations and insurance. The incremental cost does not include a contribution to overhead, aircraft cost or profit. A portion of the proceeds received from non-airline partners is also deferred. At December 31, 1997 and 1998, the total liability for miles outstanding was $22.3 million and $28.0 million, respectively.

Employees
Alaska had 9,244 active full-time and part-time employees at December 31, 1998. Alaska's union contracts at December 31, 1998 were as follows:

Union	Employee Group	Number of Employees	Contract Status
Air Line Pilots Association International	Pilots	1,156	Amendable 4/30/03
Association of Flight Attendants	Flight attendants	1,635	Amendable 3/14/99
International	Rampservice	932	Amendable 8/31/97

Association of Machinists and Aerospace Workers	and stock clerks		In mediation
	Clerical, office and passenger service	3,211	Amendable 5/20/99 In negotiation
Aircraft Mechanics Fraternal Association	Mechanics, inspectors and cleaners	1,031	Initial contract In negotiation
Mexico Workers Association personnel of Air Transport	Mexico airport	71	Amendable 4/1/99
Transport Workers Union of America	Dispatchers	16	Amendable 2/9/02

Horizon had 3,220 active full-time and part-time employees at December 31, 1998. Horizon's union contracts at December 31, 1998 were as follows:

Union	Employee Group	Number of Employees	Contract Status
International Brotherhood of Teamsters	Pilots	547	Initial contract In negotiation
Association of Flight Attendants	Flight attendants	343	Amendable 1/28/03
Transport Workers Union of America	Mechanics and related classifications	490	Amendable 5/18/01
	Dispatchers	25	Amendable 5/10/02
National Automobile, Aerospace, Transportation and General Workers	Station personnel in Canada	50	Amendable 1/17/01

ITEM 2. PROPERTIES

Aircraft

The following table describes the aircraft operated and their average age at December 31, 1998.

Aircraft Type	Passenger Capacity	Owned	Leased	Total	Average Age in Years
Alaska Airlines					
Boeing 737-200C	111	7	1	8	18.4
Boeing 737-400	140	4	33	37	3.8
McDonnell Douglas MD-80	140	16	23	39	9.0
		27	57	84	7.6
Horizon Air					
de Havilland Dash 8	37	--	40	40	4.1
Fokker F-28	69	7	13	20	14.8
		7	53	60	7.8

Part II, Item 7, "Management's Discussion and Analysis of Results of Operations and Financial Condition," discusses future orders and options for additional aircraft.

Eleven of the 27 aircraft owned by Alaska as of December 31, 1998 are subject to liens securing long-term debt. Alaska's leased B737-200C, B737-400 and MD-80 aircraft have lease expiration dates in 1999, between 2002 and 2016, and between 1999 and 2013, respectively. Horizon's leased de Havilland Dash 8 and Fokker F-28 aircraft have expiration dates between 2000 and 2013 and 2000 and 2002, respectively. Alaska and Horizon have the option to extend most of the leases for additional periods, or the right to purchase the aircraft at the end of the lease term, usually at the then fair market value of the aircraft. For information regarding obligations under capital leases and long-term operating leases, see Notes to Consolidated Financial Statements.

Special noise ordinances or agreements restrict the type of aircraft, the timing and the number of flights operated by Alaska and other air carriers at four Los Angeles area airports plus San Diego, San Jose, San Francisco, Seattle and Vancouver. At December 31, 1998, all of Alaska's aircraft meet the Stage 3 noise requirements under the Airport Noise and Capacity Act of 1990.

Ground Facilities and Services
Alaska and Horizon lease ticket counters, gates, cargo and baggage, office space and other support areas at the majority of the airports they serve. Alaska also owns terminal buildings at various Alaska cities.

Alaska has centralized operations in several buildings located at or near Seattle-Tacoma International Airport (Sea-Tac) in Seattle, Washington. The owned buildings, including land unless located on leased airport property, include: a three-bay hangar facility with maintenance shops; a flight operations and training center; an air cargo facility; a reservations and office facility; two office buildings; its corporate headquarters; and two storage warehouses. Alaska also leases a two-bay hangar/office facility at Sea-Tac. Alaska's other major facilities include: a regional headquarters building, an air cargo facility and a leased hangar/office facility in Anchorage; a Phoenix reservations center; and a leased two-bay maintenance facility in Oakland.

Horizon owns its Seattle corporate headquarters building. It leases an operations, training and aircraft maintenance facility (completed in 1998) in Portland, and a maintenance facility in Boise.

ITEM 3. LEGAL PROCEEDINGS
In July 1998, the Company announced that it had reached an agreement in principle with the trustee for creditors of the defunct MarkAir, Inc. regarding a breach of contract lawsuit. Subsequently, a formal settlement agreement was approved by the bankruptcy court. The $16.5 million settlement resulted in an after-tax charge of $10.1 million ($0.38 per diluted share) in the third quarter of 1998.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS
None.
EXECUTIVE OFFICERS OF THE REGISTRANT

The executive officers of Alaska Air Group, Inc., their positions and their respective ages (as of March 1, 1999) are as follows:

Name	Position	Age	Officer Since
John F. Kelly	Chairman, President and Chief Executive Officer of Alaska Air Group, Inc.; Chairman and and CEO of Alaska Airlines, Inc.; Chairman of Horizon Air Industries, Inc.	54	1981

Harry G. Lehr	Senior Vice President/Finance of Alaska Air Group, Inc. and Alaska Airlines, Inc.	58	1986
Steven G. Hamilton	Vice President/Legal and General Counsel of Alaska Air Group, Inc. and Alaska Airlines, Inc.	59	1988
Keith Loveless	Corporate Secretary and Associate General Counsel of Alaska Air Group, Inc. and Alaska Airlines, Inc.	42	1996

The above officers have been employed as officers of Air Group or its subsidiary, Alaska Airlines, for more than five years except for Keith Loveless, who was elected as Corporate Secretary in 1996. Mr. Loveless joined the Alaska Airlines legal department in 1986 and continues to hold his current position as associate general counsel of Alaska Airlines, a post he has held since 1993.

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

As of December 31, 1998, there were 26,224,005 shares of common stock issued and outstanding and 4,687 shareholders of record. The Company also held 2,750,102 treasury shares at a cost of $62.7 million. The Company has not paid dividends on the common stock since 1992. Air Group's common stock is listed on the New York Stock Exchange (symbol: ALK).

The following table shows the trading range of Alaska Air Group common stock on the New York Stock Exchange for 1997 and 1998.

	1997		1998	
	High	Low	High	Low
First Quarter	27-5/8	20-3/4	61	38-1/4
Second Quarter	26-1/4	23	62-9/16	43-3/8
Third Quarter	33-5/16	25-1/16	61-3/16	32-1/16
Fourth Quarter	40-1/8	30-3/16	45-11/16	26

ITEM 6. SELECTED CONSOLIDATED FINANCIAL AND OPERATING DATA

	1994	1995	1996	1997	1998
Consolidated Financial Data:					
Year Ended December 31 (in millions, except per share amounts):					
Operating Revenues	$1,315.6	$1,417.5	$1,592.2	$1,739.4	$1,897.7
Operating Expenses	1,241.6	1,341.8	1,503.2	1,600.4	1,686.7
Operating Income	74.0	75.7	89.0	139.0	211.0
Nonoperating expense, net (a)	(33.0)	(41.7)	(24.7)	(15.4)	(6.6)
Income before income tax	41.0	34.0	64.3	123.6	204.4
Net Income	$22.5	$17.3	$38.0	$72.4	$124.4
Average shares outstanding	13.367	13.485	14.241	14.785	23.388
Basic earnings per share	$1.69	$1.28	$2.67	$4.90	$5.32
Diluted earnings per share	1.62	1.26	2.05	3.53	4.81
At End of Period (in millions, except ratio):					
Total assets	$1,315.8	$1,313.4	$1,311.4	$1,533.1	$1,731.8
Long-term debt and capital lease obligation	589.9	522.4	404.1	401.4	171.5
Shareholders' equity	191.3	212.5	272.5	475.3	789.5
Ratio of earnings to fixed charges	1.36	1.28	1.57	2.10	2.93
Alaska Airlines Operating Data:					
Revenue passengers (000)	8,958	10,140	11,805	12,284	13,056
Revenue passenger miles (RPM) (000,000)	7,587	8,584	9,831	10,386	11,283
Available seat miles (ASM) (000,000)	12,082	13,885	14,904	15,436	16,807

Revenue passenger load factor	62.8%	61.8%	66.0%	67.3%	67.1%
Yield per passenger mile	12.20c	11.59c	11.67c	12.49c	12.50c
Operating revenues per ASM	8.79c	8.23c	8.70c	9.38c	9.32c
Operating expenses per ASM	8.27c	7.71c	8.10c	8.51c	8.17c
Average full-time equivalent employees	6,486	6,993	7,652	8,236	8,704
Horizon Air Operating Data:					
Revenue passengers (000)	3,482	3,796	3,753	3,686	4,389
Revenue passenger miles (RPM) (000,000)	733	841	867	889	1,143
Available seat miles (ASM) (000,000)	1,165	1,414	1,462	1,446	1,815
Revenue passenger load factor	62.9%	59.5%	59.3%	61.5%	63.0%
Yield per passenger mile	33.35c	31.48c	33.14c	32.56c	29.01c
Operating revenues per ASM	22.06c	19.77c	20.61c	21.00c	19.16c
Operating expenses per ASM	20.95c	19.47c	20.60c	20.60c	18.16c
Average full-time equivalent employees	2,557	2,864	2,891	2,756	3,019

(a) Includes capitalized interest of $.4 million, $.2 million, $1.0 million, $5.3 million and $6.6 million for 1994, 1995, 1996, 1997, and 1998, respectively.
c=cents

Alaska Airlines Financial and Statistical Data

	Quarter Ended December 31			Year Ended December 31		
Financial Data (in millions):	1997	1998	% Change	1997	1998	% Change
Operating Revenues:						
Passenger	$313.0	$333.5	6.5	$1,297.0	$1,410.4	8.7
Freight and mail	20.7	19.8	(4.3)	82.9	83.7	1.0
Other - net	16.2	19.4	19.8	68.0	72.2	6.2
Total Operating Revenues	349.9	372.7	6.5	1,447.9	1,566.3	8.2
Operating Expenses:						
Wages and benefits	106.1	115.0	8.4	423.8	466.1	10.0
Employee profit sharing	2.4	3.7	54.2	12.1	19.7	62.8
Contracted services	11.6	11.8	1.7	42.5	48.7	14.6
Aircraft fuel	49.3	39.1	(20.7)	199.7	162.3	(18.7)
Aircraft maintenance	18.6	17.2	(7.5)	67.4	77.6	15.1
Aircraft rent	38.2	41.2	7.9	148.5	158.9	7.0
Food and beverage service	11.8	12.5	5.9	46.7	49.1	5.1
Commissions	22.9	22.5	(1.7)	100.8	94.4	(6.3)
Other selling expenses	11.7	18.9	61.5	63.9	75.2	17.7
Depreciation and amortization	14.9	15.9	6.7	56.9	61.9	8.8
Loss (gain) on sale of assets	(0.9)	0.6	NM	(1.2)	1.0	NM
Landing fees and other rentals	12.7	14.8	16.5	53.1	59.4	11.9
Other	26.2	24.9	(5.0)	99.4	98.0	(1.4)
Total Operating Expenses	325.5	338.1	3.9	1,313.6	1,372.3	4.5
Operating Income	24.4	34.6	41.8	134.3	194.0	44.5
Interest income	3.9	6.8		12.2	23.2	
Interest expense	(5.9)	(4.0)		(25.0)	(17.4)	
Interest capitalized	1.1	1.5		3.4	5.1	
Other - net	0.1	(0.1)		2.5	(14.4)	
	(0.8)	4.2		(6.9)	(3.5)	
Income Before Income Tax	$23.6	$38.8	64.4	$127.4	$190.5	49.5
Operating Statistics:						
Revenue passengers (000)	2,958	3,211	8.5	12,284	13,056	6.3
RPMs (000,000)	2,490	2,749	10.4	10,386	11,283	8.6
ASMs (000,000)	3,847	4,204	9.3	15,436	16,807	8.9
Passenger load factor	64.7%	65.4%	0.7 pts	67.3%	67.1%	(0.2)pts
Breakeven load factor	60.2%	58.0%	(2.2)pts	60.5%	58.0%	(2.5)pts
Yield per passenger mile	12.57c	12.13c	(3.5)	12.49c	12.50c	0.1
Operating revenue per ASM	9.10c	8.87c	(2.5)	9.38c	9.32c	(0.6)
Operating expenses per ASM	8.46c	8.04c	(5.0)	8.51c	8.17c	(4.1)
Fuel cost per gallon	71.7c	52.6c	(26.7)	72.6c	54.6c	(24.8)
Fuel gallons (000,000)	68.8	74.3	8.0	275.2	297.4	8.1
Average number of employees	8,223	8,787	6.9	8,236	8,704	5.7
Aircraft utilization (block hours)	11.2	11.2	0.0	11.4	11.5	0.9
Operating fleet at period-end	78	84	7.7	78	84	7.7

NM = Not Meaningful
c=cents

Horizon Air Financial and Statistical Data

	Quarter Ended December 31			Year Ended December 31		
Financial Data (in millions):	1997	1998	% Change	1997	1998	% Change
Operating Revenues:						
Passenger	$72.7	$84.9	16.8	$289.5	$331.7	14.6
Freight and mail	2.7	2.7	0.0	11.2	10.7	(4.5)
Other - net	1.0	1.5	50.0	2.9	5.4	86.2
Total Operating Revenues	76.4	89.1	16.6	303.6	347.8	14.6
Operating Expenses:						
Wages and benefits	23.9	28.1	17.6	94.4	105.1	11.3
Employee profit sharing	0.8	0.4	(50.0)	1.4	3.5	150.0
Contracted services	1.7	2.5	47.1	6.3	9.0	42.9
Aircraft fuel	8.4	8.0	(4.8)	32.8	30.2	(7.9)
Aircraft maintenance	8.0	11.3	41.3	41.4	43.3	4.6
Aircraft rent	9.4	10.2	8.5	35.5	40.6	14.4
Food and beverage service	0.5	0.7	40.0	1.9	2.5	31.6
Commissions	4.1	4.3	4.9	17.9	17.3	(3.4)
Other selling expenses	3.6	5.5	52.8	16.5	19.6	18.8
Depreciation and amortization	2.7	4.1	51.9	11.2	12.9	15.2
Loss (gain) on sale of assets	(0.1)	(0.1)	NM	(0.7)	0.0	NM
Landing fees and other rentals	3.5	4.7	34.3	13.5	17.2	27.4
Other	6.7	7.3	9.0	25.7	28.4	10.5
Total Operating Expenses	73.2	87.0	18.9	297.8	329.6	10.7
Operating Income	3.2	2.1	(34.4)	5.8	18.2	213.8
Interest income	0.0	0.0		0.1	0.0	
Interest expense	(0.3)	(0.1)		(1.8)	(1.0)	
Interest capitalized	0.6	0.3		1.8	1.5	
Other - net	0.1	0.1		0.4	0.2	

	0.4	0.3		0.5	0.7	
Income Before Income Tax	$3.6	$2.4	(33.3)	$6.3	$18.9	200.0
Operating Statistics:						
Revenue passengers (000)	938	1,186	26.4	3,686	4,389	19.1
RPMs (000,000)	231	311	34.7	889	1,143	28.6
ASMs (000,000)	376	486	29.4	1,446	1,815	25.5
Passenger load factor	61.5%	64.0%	2.5 pts	61.5%	63.0%	1.5 pts
Breakeven load factor	58.3%	62.2%	3.9 pts	60.2%	59.1%	(1.1)pts
Yield per passenger mile	31.48c	27.28c	(13.3)	32.56c	29.01c	(10.9)
Operating revenue per ASM	20.32c	18.32c	(9.9)	21.00c	19.16c	(8.8)
Operating expenses per ASM	19.47c	17.89c	(8.1)	20.60c	18.16c	(11.9)
Fuel cost per gallon	76.3c	55.6c	(27.1)	77.5c	57.7c	(25.7)
Fuel gallons (000,000)	11.0	14.4	30.9	42.4	52.5	23.8
Average number of employees	2,774	3,257	17.4	2,756	3,019	9.5
Aircraft utilization (block hours)	7.1	7.8	9.9	7.1	7.9	11.3
Operating fleet at period-end	62	60	(3.2)	62	60	(3.2)

NM = Not Meaningful
c=cents

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Industry Conditions

The airline industry is cyclical due to a high correlation between demand for air travel and general economic conditions. Generally speaking, economic conditions have been strong during the years covered by this discussion. Because the industry has high fixed costs in relation to revenues, a small change in load factors or fare levels has a large impact on profits.

For most airlines, labor and fuel account for almost half of operating expenses. The strong economy has increased employee turnover and put upward pressure on labor costs. Fuel prices have been volatile in the last three years. For Alaska Airlines, fuel prices increased 20% in 1996, decreased 4% in 1997 and decreased another 25% in 1998.

In recent years, airlines have reduced their ticket distribution costs by capping travel agent commissions, by decreasing commission rates from 10% to 8%, by partially eliminating paper tickets and by selling tickets directly to passengers via the Internet.

RESULTS OF OPERATIONS

1998 Compared with 1997 Consolidated net income in 1998 was $124.4 million, or $4.81 per share (diluted), compared with net income of $72.4 million, or $3.53 per share in 1997. The 1998 results include an after-tax charge of $10.1 million ($0.38 per diluted share) for settlement of the MarkAir litigation. Consolidated operating income was $211.0 million in 1998 compared with $139.0 million in 1997. Lower fuel prices accounted for $56.9 million of the $72.0 million improvement in operating income. Alaska's annual operating income improved by $59.7 million, while Horizon's improved by $12.4 million. A discussion of operating results for the two airlines follows.

Alaska Airlines (Refer to Alaska's operating and statistical data in Item 6.) Operating income increased 44.5% to $194.0 million, resulting in a 12.4% operating margin as compared to a 9.3% margin in 1997. Operating revenue per available seat mile (ASM) decreased 0.6% to 9.32 cents while operating expenses per ASM decreased 4.1% to 8.17 cents.

The decrease in revenue per ASM was primarily due to a 0.2 point decrease in passenger load factor. The Pacific Northwest-Southern California and Pacific Northwest-Northern California markets experienced modest increases in load factor, while the Seattle-Anchorage market experienced a small decrease. Alaska's top five markets, which represent 79% of its traffic, experienced increases in passenger yield. Several smaller markets, including the new Canadian market, had decreases in yield.

Freight and mail revenues increased 1.0% primarily due to a 4.7% increase in mail pounds and a 0.5% increase in freight pounds carried. Freight rates were down due to increased competition in the Seattle-Anchorage market. Other-net revenues increased 6.2% due to increased revenue from travel partners in Alaska's frequent flyer program.

Wages and benefits increased 10.0% due to a 5.7% increase in the number of employees combined with a 4.1% increase in average wages and benefits per employee. Employees were added in all areas to service the 8.9% capacity (ASM) increase and the 6.3% increase in passengers carried. Average wages and benefits per employee increased primarily due to higher pilot wage rates and pension costs that resulted from a new pilot contract signed in late 1997.

Profit sharing expense increased 63% due to a large increase in pretax income.

Contracted services increased 15%, due to growth in ground handling and security charges as a result of more flights to Canada and other cities, greater use of temporary employees (particularly in computer systems development), higher shipping charges incurred and increased navigation fees in Canada and Mexico.

Fuel expense decreased 19%, as the 8% increase in fuel consumption was more than offset by a 25% decrease in the price of fuel.

Maintenance expense increased 15%, exceeding the 9% increase in capacity, due to a greater number of annual aircraft inspections (C checks) performed, and increased engine overhaul expense.

Aircraft rent increased 7%, primarily due to leasing nine new aircraft in 1998.

Food and beverage expense increased 5%, in line with the 6% increase in passengers carried.

Commission expense decreased 6% (in spite of a 9% increase in passenger revenue), primarily because the commission rate paid to travel agents decreased from 10% to 8% for sales made since October, 1997. As a percentage of passenger revenue, commission expense decreased 14%, from 7.8% to 6.7%. In 1998, 70% of ticket sales were made through travel agents, versus 72% in 1997.

Other selling expenses increased 18%, higher than the 9% increase in passenger revenues, due to increased advertising to promote the new Canada market and other markets.

Depreciation and amortization expense increased 9%, primarily due to modifications (made in late 1997) to the B737-200C fleet to meet Stage 3 noise requirements, a full year of depreciation on two MD-80s purchased in 1997 and added depreciation on computers and related equipment.

Landing fees and other rentals increased 12%, higher than the 9% increase in capacity, primarily due to rental rate and space increases at several airports and higher than average fees in Canada.

Other expense decreased 1%, primarily due to a $2.7 million recovery of California property taxes that resulted from settlement of industry litigation, lower long distance telephone rates and lower insurance rates. These savings were partly offset by higher expenditures for operating supplies, employee hiring, flight crew hotels and legal fees.

Horizon Air (Refer to Horizon's operating and statistical data in Item 6.) During 1998, Horizon completed its transition to a simplified fleet (which at year-end 1998 comprised 20 Fokker F-28-4000 jets and 40 de Havilland Dash 8-200 turboprop aircraft). Over the last few years, Horizon's route structure changed from a largely hub-and-spoke system to more of a point-to-point one, flying people longer distances (260 miles on the average in 1998 versus 241 miles in 1997) with fewer connections. Due to their higher capacity and longer stage lengths, the jets accounted for 58% of the ASMs flown in 1998, versus 21% four years ago. These changes have resulted in a more efficient operation, with lower unit revenues (down 8.8%) and even lower unit costs (down 11.9%). As a result, operating income increased from $5.8 million to $18.2 million, resulting in a 5.2% operating margin as compared to 1.9% in 1997.

Freight and mail revenues decreased 5% primarily due to increased competition from overnight trucking. Other-net revenues increased 86% primarily due to increased freight and ground handling services provided to other airlines.

Wages and benefits increased 11.3% due to a 9.5% increase in the number of employees combined with a 1.6% increase in average wages and benefits per employee. Employees were added in all areas to service the 19% increase in passengers carried.

Profit sharing expense increased 150% due to a large increase in pretax income.

Contracted services increased 43%, due to increased navigation fees in Canada, higher ground handling and security charges and greater use of computer and other consultants.

Fuel expense decreased 8%, as the 24% increase in fuel consumption was more than offset by a 26% decrease in the price of fuel.

Maintenance expense increased 5%, much less than the 26% increase in capacity, due to fewer maintenance requirements for the many new Dash 8-200 aircraft acquired during 1997-1998, better reliability of F-28 4000 jets that have replaced the F-28 1000s and other efficiencies of a more simplified fleet.

Aircraft rent increased 14%, as most of the new aircraft acquired in 1998 were leased.

Food and beverage expense increased 32%, in line with the 29% increase in revenue passenger miles.

Commission expense decreased 3% (in spite of a 15% increase in passenger revenue), primarily because the commission rate paid to travel agents decreased from 10% to 8% for sales made since October, 1997. As a percentage of passenger revenue, commission expense decreased 16%, from 6.2% to 5.2%.

Other selling expenses increased 19%, in line with the 15% increase in passenger revenues.

Depreciation and amortization expense increased 15%, primarily due to purchase of more F-28s in 1998 and added depreciation on aircraft spare parts and station equipment.

Landing fees and other rentals increased 27%, in line with the 26% increase in capacity.

Other expense increased 11%, primarily due to higher expenditures for flight crew training, hotels, per diem charges, employee hiring and computers. These increases were partly offset by lower insurance charges and property taxes.

Consolidated Nonoperating Income (Expense) Net nonoperating items improved $8.8 million over 1997 due to lower interest expense (due to conversion of convertible bonds in 1998 and other debt repayments) and higher interest income (due to higher cash balances). These were partly offset by a $16.5 million charge for a settlement of the MarkAir litigation.

1997 Compared with 1996 Consolidated net income in 1997 was $72.4 million, or $3.53 per share (diluted), compared with net income of $38.0 million, or $2.05 per share in 1996. Consolidated operating income was $139.0 million in 1997 compared with $89.0 million in 1996. Severe winter storms, high fuel prices and matching of competitors' lower fares adversely affected the 1996 results.

Alaska Airlines Operating income increased 49.2% to $134.3 million, resulting in a 9.3% operating margin as compared with a 6.9% margin in 1996. Operating revenue per ASM increased 7.8% to 9.38 cents while operating expenses per ASM increased 5.1% to 8.51 cents. The increase in revenue per ASM was primarily due to a 7.1% increase in system passenger yield. Higher unit costs were largely due to increased labor costs.

Horizon Air Operating income increased from $0.1 million to $5.8 million, resulting in a 1.9% operating margin as compared to a zero margin in 1996. Operating revenue per ASM increased 1.9% to 21.00 cents while operating expenses per available seat mile remained even at 20.60 cents.

Consolidated Nonoperating Income (Expense) Nonoperating expense decreased $9.3 million to $15.4 million, primarily due to smaller average debt balances, lower interest rates on variable interest rate debt and more interest capitalized.

Liquidity and Capital Resources
The table below presents the major indicators of financial condition and liquidity.

(In millions, except debt-to-equity and per share amounts)	Dec. 31, 1997	Dec. 31, 1998	Change
Cash and marketable securities	$212.7	$306.6	$93.9
Working capital (deficit)	(48.7)	2.9	51.6
Long-term debt and capital lease obligations	401.4	171.5	(229.9)
Shareholders' equity	475.3	789.5	314.2
Book value per common share	$26.00	$30.11	$4.11
Debt-to-equity	46%:54%	18%:82%	NA

1998 Financial Changes The Company's cash and marketable securities portfolio increased by $94 million during 1998. Operating activities provided $310 million of cash in 1998. Additional cash was provided by the sale and leaseback of nine B737-400 aircraft and 12 Dash 8-200 aircraft ($402 million) and the return of $33 million of equipment deposits. Cash was used for $613 million of capital expenditures, including the purchase of nine new B737-400 aircraft, a previously leased B737-400 aircraft, 12 new Dash 8-200 aircraft, flight equipment deposits and airframe and engine overhauls and the repayment of debt ($46 million).

Shareholders' equity increased $314 million due to the conversion of $186 million of convertible bonds into common stock, net income of $124 million and issuance of $7 million of common stock under stock plans.

Financing Activities   During 1998, Alaska sold nine B737-400 aircraft and leased them back for 18 years; Horizon sold 12 Dash 8-200 aircraft and leased them back for 15 years.

In February 1998, substantially all of the 6-7/8% convertible subordinated debentures were converted into 1.6 million shares of common stock. In June 1998, all of the 6-1/2% convertible subordinated debentures were converted into 6.1 million shares of common stock.

Commitments During 1998, Alaska's lease commitments increased approximately $414 million due to the sale and leaseback of nine B737-400 aircraft. In addition, Alaska ordered eight Boeing 737 aircraft with a cost of approximately $256 million. Horizon's lease commitments increased approximately $162 million due to the acquisition of 12 new Dash 8-200 aircraft. In addition, Horizon ordered 25 Canadair regional jets with a cost of approximately $580 million. At December 31, 1998, the Company had firm orders for 53 aircraft with a total cost of approximately $1.4 billion as set forth below. In addition, Alaska has options to acquire 26 more B737s and Horizon has options to acquire five CRJ 700s. Alaska and Horizon expect to finance the new planes with either leases, long-term debt or internally generated cash.

	Delivery Period - Firm Orders					
Aircraft	1999	2000	2001	2002	2003-05	Total
Boeing 737-400	3	--	--	--	--	3
Boeing 737-700	5	7	--	--	--	12
Boeing 737-900	--	--	5	5	--	10
de Havilland Dash 8-200	3	--	--	--	--	3
Canadair RJ 700	--	--	--	4	21	25
Total	11	7	5	9	21	53
Cost (Millions)	$281	$217	$175	$267	$483	$1,423

The Company accrues the costs associated with returning leased aircraft over the lease period. As leased aircraft are retired, the costs are charged against the established reserve. At December 31, 1998, $49 million was reserved for leased aircraft returns.

Deferred Taxes At December 31, 1998, net deferred tax liabilities were $91 million, which includes $114 million of net temporary differences offset by $23 million of Alternative Minimum Tax (AMT) credits. The Company believes that all of its deferred tax assets, including its AMT credits, will be realized through profitable operations.

Year 2000 Computer Issue The Company uses a significant number of computer software programs and embedded operating systems that were not originally designed to process dates beyond 1999. The Company has implemented a project to ensure that the Company's systems will function properly in the year 2000 and thereafter. The Company expects to remediate most of its major systems by early 1999 and substantially to complete the project by the end of June 1999. The Company believes that, with modifications to its existing software and systems and/or conversions to new software, the year 2000 issue will not pose significant operational problems. Most of the Company's information technology projects in the last several years have made the affected systems year 2000 compliant. The direct costs of projects solely intended to correct year 2000 problems are currently estimated at less than $2 million. The Company does not track certain costs attributable to year 2000, such as salaries of information technology staff not dedicated entirely to the project. Additional systems currently under review may require further resources. The Company does not expect any cost increases to have a material effect on its results of operations.

The Company is also in contact with its significant suppliers and vendors with which its systems interface and exchange data or upon which its business depends. These efforts are designed to minimize the extent to which its business will be vulnerable to their failure to remediate their own year 2000 issues. The Company's business is also dependent upon certain governmental organizations or entities such as the Federal Aviation Administration (FAA) that provide essential aviation industry infrastructure. The Company is working with the Airline Transport Association (ATA) and the International Airline Transport Association (IATA) to monitor the progress of FAA and airports in making their systems year 2000 compliant. In addition, the Company is independently working with certain rural Alaska airports not within ATA's purview. There can be no assurance that such third parties on which the Company's business relies will successfully remediate their systems on a timely basis. The Company's business, financial condition or results of operations could be materially adversely affected by the failure of its systems or those operated by other parties to operate properly beyond

1999. Areas that could be adversely affected include flight operations, maintenance, planning, reservations, sales, accounting and the frequent flyer program. The Company already has in place certain disaster contingency plans anticipating the potential loss of essential services such as electricity and financial accounting systems. The Company will leverage its year 2000 contingency planning off these existing plans. In addition, the Company is developing and executing additional contingency plans designed to allow continued operation in the event of failure of key third party systems or products. The foregoing Year 2000 Computer Issue comments include forward-looking statements regarding the performance of the Company. Actual results may differ materially from these projections. Factors that could cause results to differ include the availability of adequate resources to complete the Company's year 2000 plan, the ability to identify and remediate noncompliant systems, and the success of third parties in remediating their year 2000 issues.

New Accounting Standards During June 1998, the Financial Accounting Standards Board issued FAS 133, Accounting for Derivative Instruments and Hedging Activities The new standard requires companies to record derivatives on the balance sheet as assets or liabilities, measured at fair value. Gains or losses resulting from changes in the values of those derivatives would be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. Due to the Company's minimal use of derivatives, the new standard is expected to have no material impact on its financial position or results of operations. FAS 133 will be effective for the Company's fiscal year beginning January 1, 2000.

1997 Financial Changes The Company's cash and marketable securities portfolio increased by $111 million during 1997. Operating activities provided $205 million of cash in 1997. Additional cash was provided by the sale and leaseback of four B737-400 aircraft and 13 Dash 8-200 aircraft ($247 million), issuance of common stock ($129 million) and issuance of long-term debt ($28 million). Cash was used for $439 million of capital expenditures including the purchase of two new MD-83 aircraft, three new B737-400 aircraft, a previously leased B737-400 aircraft, 13 new Dash 8-200 aircraft, flight equipment deposits and airframe and engine overhauls, net repayment of short-term borrowings ($47 million) and the repayment of debt ($26 million).

1996 Financial Changes The Company's cash and marketable securities portfolio decreased by $33 million during 1996. Operating activities provided $223 million of cash in 1996. Additional cash was provided by the sale and leaseback of three B737-400 aircraft ($86 million), the sale of three MD-80 aircraft ($52 million) and proceeds received from the issuance of common stock ($21 million). Cash was used for the purchase of two new MD-83 aircraft, two used B737-400 aircraft, two previously leased B737-200Cs, airframe and engine overhauls and other capital expenditures ($209 million), and aircraft purchase deposits ($61 million). Cash was also used to repay net short-term borrowings ($19 million), and $134 million of long-term debt (including $100 million repaid early). During 1996, Alaska replaced its $75 million credit facility with a $125 million credit facility with substantially the same terms and conditions.

Effect of Inflation Inflation and specific price changes do not have a significant effect on the Company's operating revenues, operating expenses and operating income, because such revenues and expenses generally reflect current price levels.

ITEM 8. CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
See Item 14.

Selected Quarterly Consolidated Financial Information (Unaudited)

	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter	
	1997	1998	1997	1998	1997	1998	1997	1998

(in millions, except per share)

Operating revenues	$380.4	$416.4	$435.0	$484.9	$501.2	$539.4	$422.8	$457.0
Operating income (loss)	(5.4)	22.5	40.9	62.6	76.3	89.5	27.2	36.4
Net income (loss)	(5.7)	13.1	20.8	38.9	42.2	45.4	15.1	27.0
Earnings (loss) per share:								
Basic	(0.39)	0.69	1.43	1.77	2.88	1.73	0.98	1.03
Diluted	(0.39)	0.56	1.01	1.51	1.96	1.72	0.73	1.02

The total of the amounts shown as quarterly earnings per share (EPS) may differ from the amounts shown on the Consolidated Statement of Income because the annual computation is made separately and is based upon average number of shares (and equivalent shares for diluted EPS) outstanding for the year.

ITEM 9. DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE
None.

PART III
ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT
See "Election of Directors," incorporated herein by reference from the definitive Proxy Statement for Air Group's Annual Meeting of Shareholders to be held on May 18, 1999. See "Executive Officers of the Registrant" in Part I following Item 4 for information relating to executive officers.

ITEM 11. EXECUTIVE COMPENSATION
See "Executive Compensation," incorporated herein by reference from the definitive Proxy Statement for Air Group's Annual Meeting of Shareholders to be held on May 18, 1999.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT
See "Security Ownership of Certain Beneficial Owners and Management," incorporated herein by reference from the definitive Proxy Statement for Air Group's Annual Meeting of Shareholders to be held on May 18, 1999.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS
See "Transactions with Management and Others," incorporated herein by reference from the definitive Proxy Statement for Air Group's Annual Meeting of Shareholders to be held on May 18, 1999.
PART IV
ITEM 14. EXHIBITS, CONSOLIDATED FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

See Exhibit Index on page 35.

(b) A report on Form 8-K announcing orders for 25 Canadair Regional Jets Series 700 aircraft was filed on December 22, 1998

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.
ALASKA AIR GROUP, INC.

By: /s/ John F. Kelly   Date: February 10, 1999
John F. Kelly, Chairman, Chief Executive Officer and President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on February 10, 1999 on behalf of the registrant and in the capacities indicated.

/s/ John F. Kelly   Chairman, Chief Executive Officer, President and Director
John F. Kelly

/s/ Harry G. Lehr   Senior Vice President/Finance
Harry G. Lehr   (Principal Financial Officer)

/s/ Bradley D. Tilden Controller
Bradley D. Tilden   (Principal Accounting Officer)

/s/ Ronald F. Cosgrave Director
Ronald F. Cosgrave

/s/ Mary Jane Fate Director
Mary Jane Fate

/s/ Bruce R. Kennedy Director
Bruce R. Kennedy

/s/ R. Marc Langland Director
R. Marc Langland

/s/ Byron I. Mallott Director
Byron I. Mallott

/s/ Robert L. Parker, Jr. Director
Robert L. Parker, Jr.

/s/ John V. Rindlaub Director
John V. Rindlaub

/s/ Patricia Q. Stonesifer Director
Patricia Q. Stonesifer

/s/ Richard A. Wien Director
Richard A. Wien

CONSOLIDATED BALANCE SHEET
Alaska Air Group, Inc.

ASSETS

As of December 31 (In Millions)	1997	1998
Current Assets		
Cash and cash equivalents	$102.6	$29.4
Marketable securities	110.1	277.2
Receivables - less allowance for doubtful accounts (1997 - $1.2; 1998 - $1.0)	72.6	70.6
Inventories and supplies	47.2	44.1
Prepaid expenses and other assets	92.1	107.5
Total Current Assets	424.6	528.8
Property and Equipment		
Flight equipment	950.1	1,015.4
Other property and equipment	258.5	283.2
Deposits for future flight equipment	108.9	164.9

	1997	1998
	1,317.5	1,463.5
Less accumulated depreciation and amortization	373.8	417.0
	943.7	1,046.5
Capital leases:		
Flight and other equipment	44.4	44.4
Less accumulated amortization	27.5	29.6
	16.9	14.8
Total Property and Equipment - Net	960.6	1,061.3
Intangible Assets - Subsidiaries	59.6	57.5
Other Assets	88.3	84.2
Total Assets	$1,533.1	$1,731.8

See accompanying notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEET
Alaska Air Group, Inc.

LIABILITIES AND SHAREHOLDERS' EQUITY

As of December 31 (In Millions)	1997	1998
Current Liabilities		
Accounts payable	$73.9	$84.3
Accrued aircraft rent	60.7	75.5
Accrued wages, vacation and payroll taxes	70.1	79.4
Other accrued liabilities	73.5	80.9
Air traffic liability	166.4	178.6
Current portion of long-term debt and capital lease obligations	28.7	27.2
Total Current Liabilities	473.3	525.9
Long-Term Debt and Capital Lease Obligations	401.4	171.5
Other Liabilities and Credits		
Deferred income taxes	72.3	99.2
Deferred income	19.5	41.5
Other liabilities	91.3	104.2
	183.1	244.9
Commitments		
Shareholders' Equity		
Preferred stock, $1 par value		
Authorized: 5,000,000 shares	-	-
Common stock, $1 par value		
Authorized: 50,000,000 shares		
Issued: 1997 - 21,030,762 shares		
1998 - 28,974,107 shares	21.0	29.0
Capital in excess of par value	292.5	473.9
Treasury stock, at cost: 1997 - 2,748,030 shares		
1998 - 2,750,102 shares	(62.6)	(62.7)
Deferred compensation	(1.8)	(1.3)
Retained earnings	226.2	350.6
	475.3	789.5
Total Liabilities and Shareholders' Equity	$1,533.1	$1,731.8

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME
Alaska Air Group, Inc.

Year Ended December 31 (In Millions Except Per Share Amounts)	1996	1997	1998
Operating Revenues			
Passenger	$1,427.7	$1,574.5	$1,728.0
Freight and mail	93.9	94.1	94.4
Other - net	70.6	70.8	75.3
Total Operating Revenues	1,592.2	1,739.4	1,897.7
Operating Expenses			
Wages and benefits	477.0	531.7	594.4
Contracted services	42.7	48.8	55.5
Aircraft fuel	234.2	232.6	192.5
Aircraft maintenance	98.7	108.7	120.9

Aircraft rent	181.2	183.9	199.5
Food and beverage service	46.6	48.5	51.6
Commissions	101.5	106.6	97.5
Other selling expenses	81.8	80.4	94.8
Depreciation and amortization	67.5	68.3	75.1
Loss (gain) on sale of assets	(9.1)	(1.9)	1.0
Landing fees and other rentals	62.4	66.2	76.3
Other	118.7	126.6	127.6
Total Operating Expenses	1,503.2	1,600.4	1,686.7
Operating Income	89.0	139.0	211.0
Nonoperating Income (Expense)			
Interest income	11.1	10.6	22.2
Interest expense	(38.4)	(33.6)	(21.2)
Interest capitalized	1.0	5.3	6.6
Other - net	1.6	2.3	(14.2)
	(24.7)	(15.4)	(6.6)
Income before income tax	64.3	123.6	204.4
Income tax expense	26.3	51.2	80.0
Net Income	$38.0	$72.4	$124.4
Basic Earnings Per Share	$2.67	$4.90	$5.32
Diluted Earnings Per Share	$2.05	$3.53	$4.81
Shares used for computation:			
Basic	14.241	14.785	23.388
Diluted	22.458	22.689	26.367

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
Alaska Air Group, Inc.

(In Millions)	Common Shares Outstanding	Common Stock	Capital in Excess of Par Value	Treasury Stock at Cost	Deferred Compen-sation	Retained Earnings	Total
Balances at December 31, 1995	13.565	$16.7	$155.4	$(71.8)	$(3.6)	$115.8	$212.5
1996 net income						38.0	38.0
Stock issued under stock plans	0.505	0.5	9.7				10.2
Treasury stock sale	0.405		1.7	9.2			10.9
Employee Stock Ownership Plan shares allocated					0.9		0.9
Balances at December 31, 1996	14.475	17.2	166.8	(62.6)	(2.7)	153.8	272.5
1997 net income						72.4	72.4
Issuance of common stock	3.450	3.5	118.4				121.9
Stock issued under stock plans	0.349	0.3	7.1				7.4
Stock issued for convertible subordinated debentures	0.008	0.0	0.2				0.2
Treasury stock sale	0.001						
Employee Stock Ownership Plan shares allocated					0.9		0.9
Balances at December 31, 1997	18.283	21.0	292.5	(62.6)	(1.8)	226.2	475.3
1998 net income						124.4	124.4
Stock issued under stock plans	0.196	0.3	6.4				6.7
Stock issued for convertible subordinated debentures	7.747	7.7	175.0				182.7
Treasury stock purchase	(0.002)			(0.1)			(0.1)
Employee Stock Ownership Plan							0.0
shares allocated					0.5		0.5
Balances at December 31, 1998	26.224	$29.0	$473.9	$(62.7)	$(1.3)	$350.6	$789.5

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS
Alaska Air Group, Inc.

Year Ended December 31 (In Millions)	1996	1997	1998
Cash flows from operating activities:			
Net income	$38.0	$72.4	$124.4
Adjustments to reconcile net income to cash:			
Depreciation and amortization	67.5	68.3	75.1
Amortization of airframe and engine overhauls	34.6	35.1	41.1
Loss (gain) on sale of assets	(9.1)	(1.9)	1.0
Increase in deferred income taxes	8.5	22.8	26.9
Decrease (increase) in accounts receivable	18.8	(2.9)	2.0
Increase in other current assets	(13.9)	(10.6)	(12.3)
Increase in air traffic liability	38.6	3.4	12.2
Increase in other current liabilities	36.9	26.5	41.9
Other-net	3.0	(7.9)	(2.1)
Net cash provided by operating activities	222.9	205.2	310.2
Cash flows from investing activities:			
Proceeds from disposition of assets	58.1	6.9	2.1
Purchases of marketable securities	(53.5)	(443.6)	(323.4)
Sales and maturities of marketable securities	110.4	385.9	156.3
Flight equipment deposits returned	1.1	8.7	33.2
Additions to flight equipment deposits	(60.5)	(68.4)	(182.1)
Additions to property and equipment	(209.3)	(370.6)	(431.3)
Restricted deposits and other	0.5	(2.0)	(1.3)
Net cash used in investing activities	(153.2)	(483.1)	(746.5)
Cash flows from financing activities:			
Proceeds from short-term borrowings	47.0	56.4	-

Repayment of short-term borrowings	(65.9)	(103.4)	-
Proceeds from sale and leaseback transactions	85.6	246.7	402.0
Proceeds from issuance of long-term debt	-	28.0	-
Long-term debt and capital lease payments	(133.9)	(25.9)	(45.5)
Proceeds from issuance of common stock	10.2	129.3	6.6
Proceeds from sale of treasury stock	10.9	-	-
Net cash provided by (used in) financing activities	(46.1)	331.1	363.1
Net increase (decrease) in cash and cash equivalents	23.6	53.2	(73.2)
Cash and cash equivalents at beginning of year	25.8	49.4	102.6
Cash and cash equivalents at end of year	$49.4	$102.6	$29.4
Supplemental disclosure of cash paid during the year for:			
Interest (net of amount capitalized)	$43.5	$28.7	$15.8
Income taxes	20.6	22.1	48.5

Noncash investing and financing activities:
1996 and 1997 - None
1998 - $186.0 million of convertible debentures were converted into 7.7 million shares of common stock.

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Alaska Air Group, Inc.
December 31, 1998

Note 1. Summary of Significant Accounting Policies
Basis of Presentation
The consolidated financial statements include the accounts of Alaska Air Group, Inc. (Company or Air Group) and its subsidiaries, the principal subsidiaries being Alaska Airlines, Inc. (Alaska) and Horizon Air Industries, Inc. (Horizon). All significant intercompany transactions are eliminated. Preparation of financial statements requires the use of management's estimates. Actual results could differ from those estimates. Certain reclassifications have been made in prior years' financial statements to conform to the 1998 presentation.

Alaska and Horizon operate as airlines. However, their business plans, competition and economic risks differ substantially. Alaska is a major airline serving Alaska; Vancouver, Canada; the U.S. West Coast and Mexico. It operates an all jet fleet and its average passenger trip is 864 miles. Horizon is a regional airline serving the Pacific Northwest, Northern California and Western Canada. It operates both jet and turboprop aircraft, and its average passenger trip is 260 miles. Substantially all of Alaska's and Horizon's sales occur in the United States. See Note 11 for operating segment information.

Cash and Cash Equivalents
Cash equivalents consist of highly liquid investments with original maturities of three months or less. They are carried at cost, which approximates market. The Company reduces its cash balance when checks are disbursed. Due to the time delay in checks clearing the banks, the Company normally maintains a negative cash balance on its books which is reported as a current liability. The amount of the negative cash balance was $10.1 million and $18.2 million at December 31, 1997 and 1998, respectively.

Inventories and Supplies
Expendable and repairable aircraft parts, as well as other materials and supplies, are stated at average cost. An allowance for obsolescence is accrued on a straight-line basis over the estimated useful lives of the aircraft. Inventories related to the retired B727 fleet and other surplus items are carried at their net realizable value. The allowance at December 31, 1997 and 1998 for all inventories was $18.0 million and $20.2 million, respectively.

Property, Equipment and Depreciation
Property and equipment are recorded at cost and depreciated using the straight-line method over their estimated useful lives, which are as follows:

Aircraft and other flight equipment	8-20 years
Buildings	10-30 years
Capitalized leases and leasehold improvements	Term of lease

Other equipment	3-15 years

Assets and related obligations for items financed under capital leases are initially recorded at an amount equal to the present value of the future minimum lease payments. The cost of major airframe overhauls, engine overhauls, and other modifications which extend the life or improve the usefulness of aircraft are capitalized and amortized over their estimated period of use. Other repair and maintenance costs are expensed when incurred. The Company periodically reviews long-lived assets for impairment.

Capitalized Interest

Interest is capitalized on flight equipment purchase deposits and ground facilities progress payments as a cost of the related asset and is depreciated over the estimated useful life of the asset.

Intangible Assets-Subsidiaries

The excess of the purchase price over the fair value of net assets acquired is recorded as an intangible asset and is amortized over 40 years. Accumulated amortization at December 31, 1997 and 1998 was $23.1 million and $25.2 million, respectively.

Deferred Income

Deferred income results from the sale and leaseback of aircraft, the receipt of manufacturer or vendor credits, and from the sale of foreign tax benefits. This income is recognized over the term of the applicable agreements.

Frequent Flyer Awards

Alaska operates a frequent flyer award program that provides travel awards to members based on accumulated mileage. The estimated incremental cost of providing free travel is recognized as an expense and accrued as a liability as miles are accumulated. Alaska also defers recognition of income on a portion of the payments it receives from travel partners associated with its frequent flyer program. The frequent flyer award liability is relieved as travel awards are issued.

Passenger Revenues

Passenger revenues are considered earned at the time service is provided. Tickets sold but not yet used are reported as air traffic liability.

Contracted Services

Contracted services includes the expenses for aircraft ground handling, security, temporary employees and other similar services.

Other Selling Expenses

Other selling expenses includes credit card commissions, computerized reservations systems (CRS) charges, advertising and promotional costs. The costs of advertising are expensed the first time the advertising takes place. Advertising expense was $15.6 million, $11.0 million, and $17.9 million, respectively, in 1996, 1997 and 1998.

Nonoperating Expense

During 1998, the Company settled a breach of contract lawsuit with MarkAir, Inc., which resulted in a $16.5 million charge to other nonoperating expense.

Income Taxes

Income taxes are accounted for in accordance with Statement of Financial Accounting Standards No. 109, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in the Company's financial statements or tax returns.

Stock Options

The Company applies APB Opinion No. 25 and related Interpretations in accounting for stock options. See Note 6 for more information.

Derivative Financial Instruments
The Company enters into foreign exchange forward contracts, generally with maturities of less than one month, to manage risk associated with net foreign currency transactions. Resulting gains and losses are recognized currently in other operating expense. The Company periodically enters into interest rate swap agreements to hedge interest rate risk. The differential to be paid or received from these agreements is accrued as interest rates change and is recognized currently in the income statement. The Company periodically enters into hedge agreements to reduce its exposure to fluctuations in the price of jet fuel. A gain or loss is recorded if the fuel index average exceeds the ceiling price or falls below the floor price. There were no interest rate swaps or fuel hedges entered into in 1998.

Note 2. Marketable Securities
Marketable securities are investments that are readily convertible to cash and have original maturities that exceed three months. They are classified as available for sale and consisted of the following at December 31 (in millions):

	1997	1998
Cost:		
U.S. government securities	$75.1	$214.1
Asset backed obligations	35.0	31.7
Other corporate obligations	--	31.4
	$110.1	$277.2
Fair value:		
U.S. government securities	$75.2	$214.9
Asset backed obligations	35.0	31.8
Other corporate obligations	--	31.3
	$110.2	$278.0

There were no material unrealized holding gains or losses at December 31, 1997 or 1998.

Of the marketable securities on hand at December 31, 1998, 49% will mature during 1999 and the remainder will mature during 2000. Based on specific identification of securities sold, the following occurred in 1997 and 1998 (in millions):

	1997	1998
Proceeds from sales	$385.9	$156.3
Gross realized gains	0.1	0.2
Gross realized losses	0.1	--

Realized gains and losses are reported as a component of interest income.

Note 3. Other Assets
Other assets consisted of the following at December 31 (in millions):

	1997	1998
Restricted deposits	$67.5	$69.1
Deferred costs and other	20.8	15.1
	$88.3	$84.2

Deferred costs are amortized over the term of the related lease or contract.

Note 4. Long-term Debt and Capital Lease Obligations
At December 31, 1997 and 1998, long-term debt and capital lease obligations were as follows (in millions):

	1997	1998
8.5%* fixed rate notes payable due through 2001	$103.5	$90.3
6.0%* variable rate notes payable due through 2009	114.9	85.2
6-1/2% convertible senior debentures due 2005	132.1	--
6-7/8% convertible subordinated debentures due 2004-2014	54.0	--

Long-term debt	404.5	175.5
Capital lease obligations	25.6	23.2
Less current portion	(28.7)	(27.2)
	$401.4	$171.5

* weighted average for 1998

At December 31, 1998, borrowings of $175.5 million are secured by flight equipment and real property. During 1998, substantially all of the convertible subordinated debentures were converted into 7.747 million shares of common stock.

At December 31, 1998, Alaska had a $115 million credit facility with commercial banks. Advances under this facility may be for up to a maximum maturity of four years. Borrowings may be used for aircraft acquisitions or other corporate purposes, and they bear interest at a rate that varies based on LIBOR. At December 31, 1998, no borrowings were outstanding under this credit facility.

Certain Alaska loan agreements contain provisions that require maintenance of specific levels of net worth, leverage and fixed charge coverage, and limit investments, lease obligations, sales of assets and additional indebtedness. At December 31, 1998, the Company was in compliance with all loan provisions, and under the most restrictive loan provisions, Alaska had $175 million of net worth above the minimum.

At December 31, 1998, long-term debt principal payments for the next five years were (in millions):

1999	$24.5
2000	$55.5
2001	$45.4
2002	$12.1
2003	$12.3

Note 5. Commitments

Lease Commitments

Lease contracts for 111 aircraft have remaining lease terms of one to 18 years. The majority of airport and terminal facilities are also leased. Total rent expense was $214.7 million, $218.7 million and $241.6 million, in 1996, 1997 and 1998, respectively. Future minimum lease payments under long-term operating leases and capital leases as of December 31, 1998 are shown below (in millions):

	Operating Leases		Capital
	Aircraft	Facilities	Leases
1999	$ 192.9	$24.8	$ 4.1
2000	180.2	22.8	4.1
2001	165.6	16.5	4.1
2002	163.0	10.5	4.1
2003	143.5	9.7	4.1
Thereafter	1,087.1	131.0	9.0
Total lease payments	$1,932.3	$215.3	29.5
Less amount representing interest			(6.3)
Present value of capital lease payments			$23.2

Aircraft Commitments

The Company has firm orders for 25 Boeing 737 series aircraft to be delivered between 1999 and 2002, three Dash 8-200s during 1999, and 25 Canadair RJ 700 jets between 2002 and 2005. The total amount of these commitments is approximately $1.4 billion. As of December 31, 1998, deposits related to the future equipment deliveries were $160 million. In addition to the ordered aircraft, the Company holds purchase options on 26 Boeing 737s and five CRJ 700s.

Note 6. Stock Plans

Air Group has three stock option plans, which provide for the purchase of Air Group common stock at a stipulated price on the date of grant by certain officers and key employees of Air Group and its subsidiaries. Under the 1988 Plan, options for 1,730,700 shares have been granted.

Under the 1996 and 1997 Plans, options for 836,600 shares have been granted and, at December 31, 1998, 90,400 shares were available for grant. Under all plans, the incentive and nonqualified stock options granted have terms of up to approximately ten years. Grantees are 25% vested after one year, 50% after two years, 75% after three years and 100% after four years.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for grants in 1996, 1997 and 1998, respectively: dividend yield of 0%, 0% and 0%; volatility of 36%, 34% and 35%; risk-free interest rates of 6.33%, 5.69% and 5.67%; and expected lives of 5, 5 and 5 years. Using these assumptions, the weighted average fair value of options granted was $9.58, $14.04 and $19.33 in 1996, 1997 and 1998, respectively.

Air Group follows APB Opinion 25 and related Interpretations in accounting for stock options. Accordingly, no compensation cost has been recognized for these plans. Had compensation cost for the Company's stock options been determined in accordance with Financial Accounting Standard 123, net income and earnings per share (EPS) would have been reduced to the pro forma amounts indicated below.

	1996	1997	1998
Net income (in millions):			
As reported	$38.0	$72.4	$124.4
Pro forma	37.4	71.4	122.2
Basic EPS:			
As reported	$2.67	$4.90	$5.32
Pro forma	2.63	4.83	5.23
Diluted EPS:			
As reported	$2.05	$3.53	$4.81
Pro forma	2.03	3.48	4.73

Changes in the number of shares subject to option, with their weighted average exercise prices, are summarized below:

	Shares	Price
Outstanding, Dec. 31, 1995	1,161,588	$16.56
Granted	379,900	22.51
Exercised	(504,138)	17.05
Canceled	(45,525)	17.13
Outstanding, Dec. 31, 1996	991,825	18.57
Granted	245,800	35.25
Exercised	(349,575)	17.36
Canceled	(8,125)	17.03
Outstanding, Dec. 31, 1997	879,925	23.72
Granted	324,900	47.45
Exercised	(159,475)	17.88
Canceled	(5,200)	36.88
Outstanding, Dec. 31, 1998	1,040,150	$31.96
Exercisable at year-end		
December 31, 1996	243,675	$16.70
December 31, 1997	161,775	19.08
December 31, 1998	253,350	22.92

The following table summarizes stock options outstanding and exercisable at December 31, 1998 with their weighted average remaining contractual lives:

Range of Exercise prices	Remaining Life (years)	Shares	Price
Outstanding:			
$15.00 to $17.50	6.4	191,275	$15.57
$21.50 to $24.00	7.6	283,175	22.49
$35.25	9.0	241,800	35.25
$47.00 to $57.31	9.3	323,900	47.45
$15.00 to $57.31	8.3	1,040,150	$31.96
Exercisable:			
$15.00 to $17.50		98,125	$15.75

$21.50 to $24.00	94,775	22.49
$35.25	60,450	35.25
$47.00 to $57.31	--	47.45
$15.00 to $57.31	253,350	$22.92

Note 7. Employee Benefit Plans

Pension Plans

Four defined benefit and five defined contribution retirement plans cover various employee groups of Alaska and Horizon.

The defined benefit plans provide benefits based on an employee's term of service and average compensation for a specified period of time before retirement. Pension plans are funded as required by the Employee Retirement Income Security Act of 1974 (ERISA). The defined benefit plan assets are primarily common stocks and fixed income securities. The following table sets forth the status of the plans for 1997 and 1998 (in millions):

	1997	1998
Projected benefit obligation		
Beginning of year	$230.7	$307.4
Service cost	17.3	22.5
Interest cost	17.3	21.9
Amendments	57.7	--
Change in assumptions	(8.7)	27.1
Actuarial loss (gain)	1.7	(0.4)
Benefits paid	(8.6)	(6.7)
End of year	$307.4	$371.8
Plan assets at fair value		
Beginning of year	$223.7	$289.2
Actual return on plan assets	47.6	54.4
Employer contributions	26.5	36.1
Benefits paid	(8.6)	(6.7)
End of year	$289.2	$373.0
Funded status	(18.2)	1.2
Unrecognized loss (gain)	(0.8)	7.2
Unrecognized transition asset	(0.5)	(0.3)
Unrecognized prior service cost	60.1	49.4
Prepaid pension cost	$ 40.6	$ 57.5
Weighted average assumptions as of December 31		
Discount rate	7.25%	6.75%
Expected return on plan assets	10.0%	10.0%
Rate of compensation increase	3.2%	5.5%

Net pension expense for the defined benefit plans included the following components for 1996, 1997 and 1998 (in millions):

	1996	1997	1998
Service cost	$ 15.9	$ 17.3	$ 22.4
Interest cost	15.4	17.3	21.9
Expected return on assets	(18.5)	(22.1)	(28.7)
Amortization of prior service cost	0.3	0.2	3.8
Recognized actuarial loss	1.4	1.0	--
Amortization of transition asset	(0.3)	(0.3)	(0.2)

Net pension expense	$ 14.2	$ 13.4	$ 19.2

Alaska and Horizon also maintain an unfunded, noncontributory benefit plan for certain elected officers. The $21 million unfunded accrued pension cost for this plan was accrued as of December 31, 1998.

The defined contribution plans are deferred compensation plans under section 401(k) of the Internal Revenue Code. Some of these plans require Company matching contributions based on a percentage of participants' contributions. One plan has an Employee Stock Ownership Plan (ESOP) feature. The ESOP owns Air Group common shares which are held in trust for eligible employees. The Company has recorded deferred compensation to reflect the value of the shares not yet allocated to eligible employees' accounts. As these shares are allocated to employees, compensation expense is recorded and deferred compensation is reduced. Total expense for the defined contribution plans was $10.1 million, $11.7 million and $11.6 million, respectively, in 1996, 1997 and 1998.

Profit Sharing Plans

Alaska and Horizon have employee profit sharing plans. Profit sharing expense for 1996, 1997 and 1998 was $0.9 million, $13.5 million and $23.2 million, respectively.

Other Postretirement Benefits

The Company allows retirees to continue their medical, dental and vision benefits by paying all or a portion of the active employee plan premium until eligible for Medicare, currently age 65. This results in a subsidy to retirees because the premiums received by the Company are less than the actual cost of the retirees' claims. The accumulated postretirement benefit obligation (APBO) for this subsidy at December 31, 1997 and 1998 was $15.7 million and $20.1 million, respectively. The APBO is unfunded and is included with other liabilities on the Balance Sheet. Annual expense related to this subsidy is not considered material to disclose.

Note 8. Income Taxes

Deferred income taxes result from temporary differences in the timing of recognition of revenue and expense for tax and financial reporting purposes. Deferred tax assets and liabilities comprise the following at December 31 (in millions):

	1997	1998
Excess of tax over book depreciation	$161.8	$162.9
Other - net	1.3	3.7
Gross deferred tax liabilities	163.1	166.6
Loss carryforward	(0.5)	(0.1)
Alternative minimum tax	(50.1)	(22.7)
Capital leases	(4.5)	(2.6)
Ticket pricing adjustments	(1.2)	(2.2)
Frequent flyer program	(8.5)	(10.5)
Employee benefits	(7.8)	(5.7)
Aircraft return provisions	(16.0)	(16.4)
Deferred gains	(4.8)	(8.4)
Capitalized interest	(1.4)	(2.2)
Inventory obsolescence	(6.5)	(4.8)
Gross deferred tax assets	(101.3)	(75.6)
Net deferred tax liabilities	$ 61.8	$ 91.0
Current deferred tax asset	$(10.5)	$ (8.2)
Noncurrent deferred tax liability	72.3	99.2

Net deferred tax liabilities	$ 61.8	$ 91.0

After consideration of temporary differences, taxable income for 1998 was approximately $206 million.

The components of income tax expense were as follows (in millions):

	1996	1997	1998
Current tax expense:			
Federal	$17.5	$26.4	$43.0
State	0.9	1.9	7.8
Total current	18.4	28.3	50.8
Deferred tax expense:			
Federal	6.7	18.5	27.8
State	1.2	4.4	1.4
Total deferred	7.9	22.9	29.2
Total tax expense	$26.3	$51.2	$80.0

Income tax expense reconciles to the amount computed by applying the U.S. federal rate of 35% to income before taxes as follows (in millions):

	1996	1997	1998
Income before income tax	$64.3	$123.6	$204.4
Expected tax expense	$22.5	$43.3	$71.5
Nondeductible expenses	2.8	2.9	3.0
State income tax	1.0	4.1	6.2
Other - net	--	0.9	(0.7)
Actual tax expense	$26.3	$51.2	$80.0
Effective tax rate	40.9%	41.4%	39.1%

Note 9. Earnings per Share
Basic EPS is calculated by dividing net income by the average number of common shares outstanding. Diluted EPS is calculated by dividing net income plus the after-tax interest expense on convertible debt by the average common shares outstanding plus additional common shares that would have been outstanding if conversion of the convertible debt and exercise of in-the-money stock options is assumed.

EPS calculations were as follows (in millions except per share amounts):

	1996	1997	1998
Net income	$38.0	$72.4	$124.4
Avg. shares outstanding	14.241	14.785	23.388
Basic earnings per share	$2.67	$4.90	$5.32
Net income	$38.0	$72.4	$124.4
After-tax interest on:			
6-1/2% debentures	5.3	5.3	2.2
6-7/8% debentures	2.3	2.3	0.3
7-3/4% debentures	0.5	--	--
Diluted EPS income	$46.1	$80.0	$126.9
Avg. shares outstanding	14.241	14.785	23.388
Assumed conversion of:			
6-1/2% debentures	6.151	6.151	2.543
6-7/8% debentures	1.608	1.608	0.255
7-3/4% debentures	0.361	--	--
Assumed exercise of stock options	0.097	0.145	0.181
Diluted EPS shares	22.458	22.689	26.367
Diluted earnings per share	$2.05	$3.53	$4.81

Note 10. Financial Instruments
The estimated fair values of the Company's financial instruments were as follows (in millions):

December 31, 1997

	Carrying	Fair

	Amount	Value
Cash and cash equivalents	$102.6	$102.6
Marketable securities	110.1	110.2
Restricted deposits	67.5	67.5
Long-term debt	404.5	521.7

December 31, 1998

	Carrying Amount	Fair Value
Cash and cash equivalents	$29.4	$29.4
Marketable securities	277.2	278.0
Restricted deposits	69.1	69.1
Long-term debt	175.5	175.5

The fair value of cash equivalents approximates carrying value due to the short maturity of these instruments. The fair value of marketable securities is based on quoted market prices. The fair value of restricted deposits approximates the carrying amount. The fair value of publicly traded long-term debt is based on quoted market prices, and the fair value of other debt approximates carrying value.

Note 11. Operating Segment Information

Financial information for Alaska and Horizon follows (in millions):

	1996	1997	1998
Operating revenues:			
Alaska	$1,297.3	$1,447.9	$1,566.3
Horizon	301.3	303.6	347.8
Elimination of intercompany revenues	(6.4)	(12.1)	(16.4)
Consolidated	1,592.2	1,739.4	1,897.7
Depreciation and amortization expense:			
Alaska	55.9	56.9	61.9
Horizon	11.4	11.2	12.9
Interest income:			
Alaska	11.5	12.2	23.2
Horizon	0.3	0.1	--
Interest expense:			
Alaska	29.7	25.0	17.4
Horizon	0.9	1.8	1.0
Pretax income:			
Alaska	74.5	127.4	190.5
Horizon	0.3	6.3	18.9
Air Group	(10.5)	(10.1)	(5.0)
Consolidated	64.3	123.6	204.4
Capital expenditures:			
Alaska	229.9	293.0	420.1
Horizon	39.9	145.9	193.4
Total assets at end of period:			
Alaska	1,247.9	1,370.7	1,548.8
Horizon	173.3	158.0	187.1
Air Group	524.3	668.0	790.5
Elimination of intercompany accounts	(634.1)	(663.6)	(794.6)
Consolidated	1,311.4	1,533.1	1,731.8

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors and Shareholders of Alaska Air Group, Inc.:

We have audited the accompanying consolidated balance sheet of Alaska Air Group, Inc. (a Delaware corporation) and subsidiaries as of December 31, 1998 and 1997, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended December 31, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Alaska Air Group, Inc. and subsidiaries as of December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule listed in Item 14(a) is presented for purposes of complying with the Securities and Exchange Commission's rules and is not a required part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in our audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

/s/ Arthur Andersen LLP
ARTHUR ANDERSEN LLP

Seattle, Washington
January 25, 1999

VALUATION AND QUALIFYING ACCOUNTS
Alaska Air Group, Inc.

Schedule II

(In Millions)	Beginning Balance	Additions Charged to Expense	(A) Deductions	Ending Balance
Year Ended December 31, 1996				
(a) Reserve deducted from asset to which it applies:				
Allowance for doubtful accounts	$1.6	$0.7	$(1.0)	$1.3
Obsolescence allowance for flight equipment spare parts	$13.5	$3.5	$(0.9)	$16.1
(b) Reserve recorded as other long-term liabilities:				
Leased aircraft return provision	$32.5	$9.4	$(3.3)	$38.6
Year Ended December 31, 1997				
(a) Reserve deducted from asset to which it applies:				
Allowance for doubtful accounts	$1.3	$1.0	$(1.1)	$1.2
Obsolescence allowance for flight equipment spare parts	$16.1	$3.4	$(1.5)	$18.0
(b) Reserve recorded as other long-term liabilities:				
Leased aircraft return provision	$38.6	$11.4	$(6.8)	$43.2
Year Ended December 31, 1998				
(a) Reserve deducted from asset to which it applies:				
Allowance for doubtful accounts	$1.2	$1.2	$(1.4)	$1.0
Obsolescence allowance for flight equipment spare parts	$18.0	$6.2	$(4.0)	$20.2

(b) Reserve recorded as other long-term liabilities:				
Leased aircraft return provision	$43.2	$13.1	$(7.6)	$48.7

(A) Deduction from reserve for purpose for which reserve was created.

EXHIBIT INDEX

Certain of the following exhibits have heretofore been filed with the Commission and are incorporated herein by reference from the document described in parenthesis. Certain others are filed herewith.

3.(i) Articles of Incorporation of Alaska Air Group, Inc. as amended through May 21, 1996
3.(ii) Bylaws of Alaska Air Group, Inc., as amended through Feb. 8, 1996 (Exhibit 3.(ii) to 1995 10-K)
4.1 Amended and Restated Rights Agreement dated 8/7/96 between Alaska Air Group, Inc. and The First National Bank of Boston, as Rights Agent (Exhibit 2.1 to Form 8A-A filed 8/8/96)
10.1 Lease Agreement dated Feb. 1, 1979 between Alaska Airlines, Inc. and the Alaska Industrial Development Authority (AIDA) (Exhibit 10-15 to Registration Statement No. 2-70742)
10.2 Lease Agreement dated April 1, 1978 between Alaska Airlines, Inc. and the AIDA (Exhibit 10-16 to Registration Statement No. 2-70742)
10.3 Management Incentive Plan (1992 Proxy Statement)
10.4 Loan Agreement dated as of December 1, 1984, between Alaska Airlines, Inc. and the Industrial Development Corporation of the Port of Seattle (Exhibit 10-38 to 1984 10-K)
10.5 Alaska Air Group, Inc. 1988 Stock Option Plan, as amended through May 19, 1992 (Registration Statement No. 33-52242)
#10.6 Lease Agreement dated January 22, 1990 between International Lease Finance Corporation and Alaska Airlines, Inc. for the lease of a B737-400 aircraft, summaries of 19 substantially identical lease agreements and Letter Agreement #1 dated January 22, 1990 (Exhibit 10-14 to 1990 10-K)
#10.7 Agreement dated September 18, 1996 between Alaska Airlines, Inc. and Boeing for the purchase of 12 Boeing 737-400 aircraft (Exhibit 10.1 to Third Quarter 1996 10-Q)
#10.8 Agreement dated August 28, 1996 between Horizon Air Industries, Inc. and Bombardier for the purchase of 25 de Havilland Dash 8-200 aircraft (Exhibit 10.2 to Third Quarter 1996 10-Q)
10.9 Supplemental retirement plan arrangement between Horizon Air Industries, Inc. and George D. Bagley (1996 Proxy Statement)
10.10 Alaska Air Group, Inc. 1996 Long-Term Incentive Equity Plan (Registration Statement 333-09547)
10.11 Alaska Air Group, Inc. Non Employee Director Stock Plan (Registration Statement 333-33727)
10.12 Alaska Air Group, Inc. Profit Sharing Stock Purchase Plan (Registration Statement 333-39889)
10.13 Alaska Air Group, Inc. 1997 Non Officer Long-Term Incentive Equity Plan (Registration Statement 333-39899)
10.14 Alaska Air Group, Inc. Supplementary Retirement Plan for Elected Officers (Exhibit 10.15 to 1997 10-K)
10.15 1995 Elected Officers Supplementary Retirement Plan (Exhibit 10.16 to 1997 10-K)
*#10.16 Agreement dated December 21, 1998 between Horizon Air Industries, Inc. and Bombardier for the purchase of 25 Canadair regional jets series 700 aircraft
*12 Calculation of Ratio of Earnings to Fixed Charges
21 Subsidiaries of the Registrant (Exhibit 22-01 to 1987 10-K)
*23 Consent of Arthur Andersen LLP
*27 Financial Data Schedule
* Filed herewith.
# Confidential treatment was granted as to a portion of this document.

EXHIBIT 10.16 TO ALASKA AIR GROUP, INC. 1998 FORM 10-K

BOMBARDIER AEROSPACE REGIONAL AIRCRAFT

MASTER PURCHASE AGREEMENT*

BETWEEN

BOMBARDIER INC.

AND

HORIZON AIR INDUSTRIES, INC.

CONFIDENTIAL TREATMENT HAS BEEN SOUGHT FOR CERTAIN PORTIONS OF THIS EXHIBIT. SUCH PROTIONS HAVE BEEN FILED SEPARATELY WITH THE SECURITIES AND EXCHANGE COMMISSION

* The following marking indicates that material has been omitted because it is confidential:
[CONFIDENTIAL TREATMENT REQUESTED]

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SUPPLEMENTS

SCHEDULES TO PA-436-1

This Master Purchase Agreement is made on the 21st day of December, 1998

BY AND BETWEEN: BOMBARDIER INC., a Canadian corporation represented by BOMBARDIER AEROSPACE, REGIONAL AIRCRAFT having an office at 123 Garratt Boulevard, Downsview, Ontario, Canada ("Bombardier"),

AND: HORIZON AIR INDUSTRIES, INC., a Washington Corporation having its head office at 19521 Pacific Highway South, Seattle, Washington 98188, USA, ("Buyer").

WHEREAS Buyer may in future desire to purchase new Aircraft (as defined in Article 1.4 of this Master Purchase Agreement) and related data, documents, and services under this Agreement (as defined in Article 1.4 of this Master Purchase Agreement) from Bombardier, and the parties desire to agree in advance on the terms that will govern such purchase; and

WHEREAS This Master Purchase Agreement and any subsequent amendments thereto, together with the Supplement(s) that may be executed from time to time, will be the governing document for any future transactions between Bombardier and Buyer relating to the purchase and sale of new Bombardier products, currently being offered for sale by Bombardier Aerospace, Regional Aircraft.

NOW THEREFORE, in consideration of the mutual covenants herein contained, Buyer and Bombardier agree as follows:

SECTION I

OF

MASTER PURCHASE AGREEMENT NO. PA-436

TERMS AND CONDITIONS

ARTICLE 1 - INTERPRETATION

1.1 The recitals above have been inserted for convenience only and do not form part of the Agreement.

1.2 The headings in this Agreement are included for convenience only and shall not be used in the construction and interpretation of this Agreement.

1.3 In this Agreement, unless otherwise expressly provided, the singular includes the plural and vice-versa.

1.4 In this Agreement the following expressions shall, unless otherwise expressly provided, mean:

(a) "Acceptance Period" shall have the meaning attributed to it in Article 9.3;

(b) "Acceptance Date" shall have the meaning attributed to it in Article 9.7(a);

(c) "Agreement" means this Master Purchase Agreement, Supplements and Letter Agreements, if any, including their Exhibits, Annexes, Schedules and Appendices, if any, either attached hereto (each of which is incorporated in the Agreement by this reference) or subsequently agreed by the parties, hereto, pursuant to the provisions of this Agreement;

(d) "Aircraft" shall have the meaning attributed to it in the applicable Supplement;

(e) "Aircraft Purchase Price" shall have the meaning attributed to it in the applicable Supplement;

(f) "Base Price" shall have the meaning attributed to it in the applicable Supplement;

(g) "Bill of Sale" shall have the meaning attributed to it in Article 9.7(c);

(h) "BFE" shall have the meaning attributed to it in Article 11.1;

(i) "Buyer Selected Optional Features" shall have the meaning attributed to it in the applicable Supplement;

(j) "Delivery Date" shall have the meaning attributed to it in Article 9.7(c);

(k) "Economic Adjustment Formula", if applicable, shall have the meaning attributed to it in the applicable Supplement;

(l) "Excusable Delay" shall have the meaning attributed to it in Article 13.1;

(m) "FAA" shall have the meaning attributed to it in Article 8.1;

(n) "Non-Excusable Delay" shall have the meaning attributed to it in Article 14.1;

(o) "Notice" shall have the meaning attributed to it in Article 17.1;

(p) "Other Patents" shall have the meaning attributed to it in Article 18.1;

(q) "Permitted Change" shall have the meaning attributed to it in Article 11.2;

(r "Readiness Date" shall have the meaning attributed to it in Article 9.1;

(s "Regulatory Change" shall have the meaning attributed to it in Article 8.4;

(t) "Scheduled Delivery Date" shall have the meaning attributed to it in the applicable Supplement;

(u) "Specification" shall have the meaning attributed to it in the applicable Supplement;

(v) "Supplement" means a supplementary agreement to this Agreement entered into by the parties for the purchase of specific products currently offered for sale by Bombardier Aerospace, Regional Aircraft;

(w) "Taxes" shall have the meaning attributed to it in Article 4.2; and

(x) "TC" shall have the meaning attributed to it in Article 8.1.

1.5 All dollar amounts in this Agreement are in United States Dollars.

ARTICLE 2 - SUBJECT MATTER OF SALE

2.1 A description of the Aircraft being purchased and sold under the terms of this Agreement and the related Bombardier specification document number(s) will be set out in the applicable Supplement. Until a Supplement, in the form of Exhibit V hereto, is executed between the parties hereto, neither party shall have any obligation under the terms of this Agreement.

2.2 This Agreement shall be applicable to the purchase of Aircraft completed during a period of three (3) years from the date hereof as evidenced by the execution of a Supplement.

ARTICLE 3 - CUSTOMER SUPPORT SERVICES AND WARRANTY

3.1 Bombardier shall provide to Buyer the customer support services pursuant to the provisions of Annex A attached hereto and the applicable Supplement.

3.2 Bombardier shall provide to Buyer the warranty and the service life policy described in Annex B attached hereto and the applicable

Supplement which shall be the exclusive warranty applicable to the Aircraft.

3.3 Unless expressly stated otherwise, the services referred to in 3.1 and 3.2 above and the applicable Supplement are incidental to the sale of the Aircraft and are included in the Aircraft Purchase Price.

ARTICLE 4 - PRICE

4.1 (a) The base price for each of the Aircraft is set out in the applicable Supplement;

(b) The base price of the Buyer Selected Optional Features is set out in the applicable Supplement; and

(c) The Aircraft base price shall be the base price for the Aircraft as stated in paragraph (a), plus the base price of the Buyer Selected Optional Features as stated in paragraph (b) (the "Base Price").

4.2 [CONFIDENTIAL TREATMENT REQUESTED]

4.3 [CONFIDENTIAL TREATMENT REQUESTED]
4.4 [CONFIDENTIAL TREATMENT REQUESTED]
4.5 [CONFIDENTIAL TREATMENT REQUESTED]

ARTICLE 5 - PAYMENT

5.1 The terms of payment for the Aircraft purchased and sold under the terms of this Agreement shall be set out in the applicable Supplement.

5.2 Intentionally left blank.

5.3 [CONFIDENTIAL TREATMENT REQUESTED]

5.4 Buyer shall make all payments due under this Agreement and/or any applicable Supplement in immediately available United States Dollars by deposit on or before the due date, to Bombardier's account, in the manner set out in the applicable Supplement.

5.5 All amounts due with respect to each Aircraft shall be paid on or prior to the Delivery Date of the respective Aircraft.

5.6 Bombardier shall remain the exclusive owner of the Aircraft, free and clear of all rights, liens, charges or encumbrances created by or through Buyer, until such time as all payments referred to in this Article 5 have been received in full by Bombardier.

ARTICLE 6 - DELIVERY PROGRAM

6.1 The Aircraft shall be offered for inspection and acceptance to Buyer at Bombardier's facility and during the Schedule Delivery Dates set forth in the applicable Supplement.

ARTICLE 7 - BUYER INFORMATION

7.1 During the manufacture of the Aircraft, Buyer shall provide to Bombardier on or before the date required by Bombardier, all information as Bombardier may reasonably request (with timely notice) to manufacture the Aircraft including, without limitation, the selection of furnishings, internal and external colour schemes.

Buyer will, not less than the number of months set forth in the applicable Supplement, prior to the delivery of the first Aircraft governed by such Supplement:

(a) provide Bombardier with an external paint scheme agreed on by the parties; and

(b) select interior colours (from Bombardier's standard colours).

Failure of Buyer to comply with these requirements may result in an increase in price, a delay in delivery of the Aircraft, or both.

7.2 [CONFIDENTIAL TREATMENT REQUESTED] prior to the delivery of the first Aircraft under a Supplement, where the Supplement includes the purchase of a de Havilland Dash 8 Series 100, 200, 300 or Canadair Regional Jet Series 200 aircraft, and [CONFIDENTIAL TREATMENT REQUESTED] prior to the delivery of the first Aircraft under a Supplement, where the Supplement includes the purchase of a de Havilland Dash 8 Series 400 or Canadair Regional Jet Series 700 aircraft, Buyer shall notify Bombardier, in writing, of the BFE (if any) that Buyer wishes to have incorporated on each Aircraft. Buyer shall also provide details of:

(a) weights and dimensions of the BFE;

(b) test equipment or special tools required to incorporate the BFE; and

(c) any other information Bombardier may reasonably require.

Within [CONFIDENTIAL TREATMENT REQUESTED] thereafter, Bombardier shall advise Buyer of its acceptance or rejection of the BFE, acceptance of which is not to be unreasonably refused, and of the dates by which each item of BFE is required by Bombardier. If required the parties hereto shall execute a Change Order in accordance with Article 11.1 to cover those BFE accepted by Bombardier.

7.3 The BFE accepted by Bombardier pursuant to this Article shall be incorporated in the manufacturing process of the Aircraft subject to the following conditions:

(a) Title to the BFE shall remain at all times with Buyer and risk of loss of the BFE shall remain at all times with Buyer except for damages caused by Bombardier's gross negligence.

(b) The BFE must be received Carriage Paid To (Incoterms 1990) Bombardier's plant or such other place as Bombardier may designate, no later than the date notified pursuant to Article 7.2, free and clear of any taxes, duties, licenses, charges, liens or other similar claims;

(c) The BFE shall meet:

1) the standards of quality of Bombardier, and

2) the requirements of the applicable airworthiness certification agency;

(d) The BFE shall be delivered to Bombardier in good condition and ready for immediate incorporation into the Aircraft. Bombardier shall, upon receipt, inspect the BFE as to quantity and apparent defects and inform Buyer of any discrepancies and the required corrective actions to be taken;

(e) [CONFIDENTIAL TREATMENT REQUESTED]

(f) [CONFIDENTIAL TREATMENT REQUESTED]

7.4 If at any time between receipt of the BFE by Bombardier and the Delivery Date, it is determined by Bombardier that an item of BFE supplied does not meet the standards and requirements described above (provided that same are correct) or [CONFIDENTIAL TREATMENT REQUESTED] the Aircraft or Aircraft systems create delays in the manufacturing or certification process, then such BFE may be removed and replaced by other BFE or by Bombardier's equipment. [CONFIDENTIAL TREATMENT REQUESTED].

7.5 In the event that the delivery of an Aircraft is delayed due to any delay caused by Buyer's failure to:

(a) deliver or have BFE delivered by the date required;

(b) ensure satisfactory design, suitability, use or operation of the BFE;

(c) furnish or obtain applicable BFE data;

(d) perform any adjusting, calibrating, retesting or updating of BFE;

(e) furnish or obtain any approvals in compliance with the provisions of this Article; or

(f) comply with the conditions of this Article.

then Bombardier agrees to discuss with Buyer the steps to be taken to minimize, cure, eliminate or work around the delay, [CONFIDENTIAL TREATMENT REQUESTED].

7.6 Should there be a delay in delivery caused either by a failure of Buyer described in Article 7.5, or by an event to which reference is made in Article 13.0 in connection with the BFE, and if such delay cannot reasonably be minimized, cured, eliminated or worked around by agreement of the parties, [CONFIDENTIAL TREATMENT REQUESTED].

7.7 If this Agreement is terminated in whole or in part in accordance with the provisions hereof Bombardier may elect to, by written notice to Buyer, either:

(a) if concurrence is received from Buyer, purchase the BFE ordered by Buyer and/or received by Bombardier at the invoice price paid by Buyer; or

(b) return the BFE to Buyer Free Carrier (Incoterms 1990) Bombardier's plant, or such other place that Bombardier may designate.

ARTICLE 8 - CERTIFICATION FOR EXPORT

8.1 Bombardier has obtained or will obtain from Transport Canada, Airworthiness ("TC"), a TC Type Approval (Transport Category) and from the Federal Aviation Administration of the United States ("FAA") an FAA Type Certificate for the type of aircraft purchased under this Agreement and any applicable Supplement.

8.2 Bombardier will provide to Buyer a TC Certificate of Airworthiness (Transport Category) for Export, on or before the Delivery Date. This Certificate shall bear a statement of compliance enabling Buyer to obtain an FAA Certificate of Airworthiness.

8.3 Bombardier shall not be obligated to obtain any other certificates or approvals as part of this Agreement. The obtaining of any import license or authority required to import or operate the Aircraft into any country outside of Canada shall be the responsibility of Buyer. Bombardier shall, to the extent permitted by law, and with Buyer's assistance, seek the issuance of a Canadian export license to enable Buyer to export the Aircraft from Canada subject to prevailing export control regulations in effect on the Delivery Date.

8.4 If any addition or change to, or modification or testing of the Aircraft is required by any law or governmental regulation or requirement or interpretation thereof by any governmental agency having jurisdiction in order to meet the requirements of Article 8.2

(a "Regulatory Change"), [CONFIDENTIAL TREATMENT REQUESTED].

8.5 [CONFIDENTIAL TREATMENT REQUESTED]

8.6 If delivery of the Aircraft is delayed by the incorporation of any Regulatory Change, such delay shall be an Excusable Delay within the meaning of Article 13.

8.7 Bombardier shall issue a Change Order, reflecting any Regulatory Change required to be made under this Article 8, which shall set forth in detail the particular changes to be made and the effect, if any, of such changes on design, performance, weight, balance, time of delivery, Base Price and Aircraft Purchase Price. Any Change Orders issued pursuant to this Article shall be effective and binding upon the date of Bombardier's transmittal of such Change Order.

8.8 If the use of any of the certificates identified in this Article 8 are discontinued during the performance of this Agreement, reference to such discontinued certificate shall be deemed a reference to any other certificate or instrument which corresponds to such certificate.

8.9 Reference to a regulatory authority shall include any succeeding department or agency then responsible for the duties of said regulatory authority.

8.10 [CONFIDENTIAL TREATMENT REQUESTED]

ARTICLE 9 - ACCEPTANCE PROCEDURE

9.1 Bombardier shall give Buyer [CONFIDENTIAL TREATMENT REQUESTED] advance notice, by facsimile or telegraphic communication or other expeditious means, of the projected date of readiness of each Aircraft for inspection and delivery.

Bombardier shall give Buyer [CONFIDENTIAL TREATMENT REQUESTED] advance notice, by facsimile or telegraphic communication or other expeditious means, of the date on which an Aircraft will be ready for Buyer's inspection, flight test and acceptance (the "Readiness Date"). If, after the giving of such notice (which has not been withdrawn in a timely manner), an Aircraft is not ready on the Readiness Date for Buyer's inspection, flight test and acceptance, Bombardier shall reimburse Buyer for the reasonable out of pocket living expenses, including but not limited to air travel expenses (regular coach fare) to return the Buyer's acceptance team for additional delivery attempts, which are incremental to the Acceptance Period of Buyer's representatives.

9.2 Within [CONFIDENTIAL TREATMENT REQUESTED] following receipt by Buyer of the notice of Readiness Date Buyer shall:

(a) provide notice to Bombardier as to the source and method of payment of the balance of the Aircraft Purchase Price;

(b) identify to Bombardier the names of Buyer's representatives who will participate in the inspection, flight test and acceptance; and

(c) provide evidence of the authority of the designated persons to execute the Certificate of Acceptance and other delivery documents on behalf of Buyer.

9.3 Buyer shall have [CONFIDENTIAL TREATMENT REQUESTED] commencing on the Readiness Date in which to complete the inspection and flight test (such [CONFIDENTIAL TREATMENT REQUESTED] period being the "Acceptance Period").

9.4 Up to [CONFIDENTIAL TREATMENT REQUESTED] may participate in Buyer's ground inspection of the Aircraft and [CONFIDENTIAL TREATMENT REQUESTED] may participate in the flight test. Bombardier shall, if requested by Buyer, perform an acceptance flight of not less than one (1) and not more than three (3) hours duration. Ground inspection and flight test shall be conducted in accordance with Bombardier's acceptance procedures (a copy of which shall be provided to Buyer at [CONFIDENTIAL TREATMENT REQUESTED] to the Scheduled Delivery Date of the first Aircraft governed by the applicable Supplement hereunder) and at Bombardier's expense. At all times during ground inspection and flight test, Bombardier shall retain control over the Aircraft.

9.5 If no Aircraft defect or discrepancy is revealed during the ground inspection or flight test, Buyer shall accept the Aircraft on or before the last day of the Acceptance Period in accordance with the provisions of Article 9.7.

9.6.1 [CONFIDENTIAL TREATMENT REQUESTED]. Should the inspection reveal a defect or discrepancy which from Buyer's standpoint is not a material defect the cost correction of which would be disproportionate to the impact of such defect or discrepancy or Buyer's operation the parties agree to discuss to resolve the issue in a manner satisfactory to both parties. [CONFIDENTIAL TREATMENT REQUESTED]

9.6.2 If any material defect or discrepancy in the Aircraft is revealed by Buyer's ground inspection or flight test, and Bombardier is not able to promptly correct such defect or discrepancy then Bombardier and Buyer will cooperate to effect acceptance and delivery of such Aircraft following correction of such defect in a timely manner satisfactory to both parties.

9.7 [CONFIDENTIAL TREATMENT REQUESTED]:

(a) Buyer will sign a Certificate of Acceptance (in the form of Exhibit I hereto) for the Aircraft. Execution of the Certificate of Acceptance by or on behalf of Buyer shall be evidence of Buyer having examined the Aircraft and found it in accordance with the provisions of this Agreement. The date of signature of the Certificate of Acceptance shall be the "Acceptance Date";

(b) Bombardier will supply a TC Certificate of Airworthiness for Export; and

(c) Buyer shall pay Bombardier the balance of the Aircraft Purchase Price and any other amounts due, at which time Bombardier shall issue an FAA form Bill of Sale and a bill of sale (in the form of Exhibit II hereto) passing to Buyer good title to the Aircraft free and clear of all liens, claims, charges and encumbrances except for those liens, charges or encumbrances created by or claimed through Buyer (collectively the "Bill of Sale"). The date on which Bombardier delivers the Bill of Sale and Buyer takes delivery of the Aircraft shall be the "Delivery Date".

Delivery of the Aircraft shall be evidenced by the execution and delivery of the Bill of Sale and of the Certificate of Receipt of Aircraft (in the form of Exhibit III hereto).

9.8 Provided that Bombardier has met all of its obligations under this Article 9, [CONFIDENTIAL TREATMENT REQUESTED].

9.9 Provided that Bombardier has met all material obligations under this Article 9, [CONFIDENTIAL TREATMENT REQUESTED].

ARTICLE 10 - TITLE AND RISK

10.1 Title to the Aircraft and risk of loss of or damage to the Aircraft passes to Buyer when Bombardier presents the Bill of Sale to Buyer on the Delivery Date.

10.2 If, after transfer of title on the Delivery Date, the Aircraft remains in or is returned to the care, custody or control of Bombardier, Buyer shall retain risk of loss of, or damage to the Aircraft and for itself and on behalf of its insurer(s) hereby waives and renounces to, and releases Bombardier and any of Bombardier's affiliates from any claim, whether direct, indirect or by way of subrogation, for damages to or loss of the Aircraft arising out of, or related to, or by reason of such care, custody or control.

ARTICLE 11 - CHANGES

11.1 Any change made in accordance with the provisions of this [CONFIDENTIAL TREATMENT REQUESTED] and the cost thereof shall be borne by Bombardier. Other than [CONFIDENTIAL TREATMENT REQUESTED], or a Regulatory Change as described in Article 8.4, any change to this Agreement (including without limitation the Specification) or any features or Buyer Furnished Equipment BFE, if any, changing the Aircraft from that described in the Specification, requested by Buyer, and as may be mutually agreed upon by the parties hereto, shall be made using a change order ("Change Order") substantially in the format of Exhibit IV hereto. Should Buyer request a change, Bombardier shall advise Buyer, to the extent reasonably practical, of the effect, if any, of such change request on:

(a) the Scheduled Delivery Date;

(b) the price and payment terms applicable to the Change Order; and

(c) any other material provisions of this Agreement which will be affected by the Change Order.

Such Change Order shall become effective and binding on the parties hereto when signed by a duly authorized representative of each party.

11.2 [CONFIDENTIAL TREATMENT REQUESTED].

ARTICLE 12 - BUYER'S REPRESENTATIVES AT MANUFACTURE SITE

12.1 From time to time, commencing [CONFIDENTIAL TREATMENT REQUESTED] prior to the Scheduled Delivery Date of the first Aircraft governed by the applicable Supplement, and ending with the Delivery Date of the last Aircraft purchased thereunder, Bombardier shall furnish, without charge, office space at Bombardier's facility for [CONFIDENTIAL TREATMENT REQUESTED] of Buyer. Buyer shall be responsible for all expenses of its representative and shall notify Bombardier at [CONFIDENTIAL TREATMENT REQUESTED] prior to the first scheduled visit of such representative and [CONFIDENTIAL TREATMENT REQUESTED] for each subsequent visit.

12.2 Bombardier's and Bombardier's affiliates' facilities shall be accessible to Buyer's representative [CONFIDENTIAL TREATMENT REQUESTED].

12.3 Bombardier shall advise Buyer's representative of Bombardier's or Bombardier's affiliates' rules and regulations applicable at the facilities being visited and Buyer's representative shall conform to such rules and regulations.

12.4 At any time prior to delivery of the Aircraft, [CONFIDENTIAL TREATMENT REQUESTED]. Bombardier shall provide a written response to any such request including the corrective action to be taken if applicable or otherwise which explains why the part or material in question are in accordance with the Specification. Communication between Buyer's representative and Bombardier shall be solely through Bombardier's Contracts Department or its designate.

12.5 [CONFIDENTIAL TREATMENT REQUESTED].

ARTICLE 13 - EXCUSABLE DELAY

13.1 [CONFIDENTIAL TREATMENT REQUESTED].

13.2 [CONFIDENTIAL TREATMENT REQUESTED].

13.3 [CONFIDENTIAL TREATMENT REQUESTED].

13.4 [CONFIDENTIAL TREATMENT REQUESTED].

13.5 [CONFIDENTIAL TREATMENT REQUESTED].

ARTICLE 14 - NON-EXCUSABLE DELAY

14.1 If delivery of the Aircraft is delayed by causes not excused under Article 13.1 (a "Non-Excusable Delay"), [CONFIDENTIAL TREATMENT REQUESTED].

14.2 [CONFIDENTIAL TREATMENT REQUESTED].

14.3 [CONFIDENTIAL TREATMENT REQUESTED].

14.4 [CONFIDENTIAL TREATMENT REQUESTED].

ARTICLE 15 - LOSS OR DAMAGE

15.1 In the event that prior to the Delivery Date of any Aircraft, the Aircraft is lost, destroyed or damaged beyond repair due to any cause, Bombardier shall promptly notify Buyer in writing. Such notice shall specify the earliest date reasonably possible, consistent with Bombardier's other contractual commitments and production schedule, by which Bombardier estimates it would be able to deliver a replacement for the lost, destroyed or damaged Aircraft. The applicable Supplement and this Agreement as it relates thereto shall automatically terminate as to such Aircraft unless Buyer gives Bombardier written notice, within [CONFIDENTIAL TREATMENT REQUESTED] of Bombardier's notice, that Buyer desires a replacement for such Aircraft. If Buyer gives such notice to Bombardier, the parties shall execute an amendment to the applicable Supplement which shall set forth the Delivery Date for such replacement aircraft and corresponding new replacement Aircraft Purchase Price; provided, however, that nothing herein shall obligate Bombardier to manufacture and deliver such replacement aircraft if it would require the reactivation or acceleration of its production line for the model of aircraft purchased hereunder. The terms and conditions of this Agreement and the applicable Supplement applicable to the replaced Aircraft shall apply to the replacement aircraft.

ARTICLE 16 - TERMINATION

16.1 [CONFIDENTIAL TREATMENT REQUESTED].

16.2 [CONFIDENTIAL TREATMENT REQUESTED].

16.3 [CONFIDENTIAL TREATMENT REQUESTED].

16.4 [CONFIDENTIAL TREATMENT REQUESTED].

ARTICLE 17 - NOTICES

17.1 Any notice, request, approval, permission, consent or other communication ("Notice"), to be given or required under this Agreement or a Supplement shall be provided in writing, by registered mail, facsimile, courier, telegraphic or other electronic communication providing reasonable proof of transmission, except that no notice shall be sent by mail if disruption of postal service exists or is threatened either in the country of origin or of destination, by the party giving the Notice and shall be addressed as follows:

(a) Notices to Bombardier shall be addressed to:

Bombardier Inc.
Bombardier Aerospace, Regional Aircraft
123 Garratt Boulevard
Downsview, Ontario
Canada
M3K 1Y5

Attention: Director of Contracts

Facsimile: (416) 375-4533

(b) Notices to Buyer shall be addressed to:

Horizon Air Industries, Inc.
19521 International Blvd.
Seattle, Washington 98188
U.S.A.

Attention: President
Facsimile: (206) 431-4610

17.2 Notice given in accordance with Article 17.1 shall be deemed sufficiently given to and received by the addressees:

(a) if delivered by hand, on the day when the same shall have been so delivered; or

(b) if mailed or sent by courier on the day indicated on the corresponding acknowledgment of receipt; or

(c) if sent by telex or facsimile on the day indicated by the acknowledgment or the answer back of the receiver in provable form.

ARTICLE 18 - INDEMNITY AGAINST PATENT INFRINGEMENT

18.1 In the case of any actual or alleged infringement of any Canadian or United States patent or, subject to the conditions and exceptions set forth below, any patent issued under the laws of any other country in which Buyer from time to time may lawfully operate the Aircraft ("Other Patents"), by the Aircraft, or by any system, accessory, equipment or part installed in such Aircraft at the time title to such Aircraft passes to Buyer, Bombardier shall defend, indemnify, protect and hold harmless Buyer from and against all claims, suits, actions, liabilities, damages and costs resulting from the infringement, excluding any incidental or consequential damages (which include without limitation loss of revenue or loss of profit) and Bombardier shall, at its option and expense:

(a) procure for Buyer the right under such patent to use such system, accessory, equipment or part; or

(b) replace such system, accessory, equipment or part with one of the similar functionality and quality that is non-infringing; or

(c) modify such system, accessory, equipment or part to make same non-infringing in a manner such as to keep it otherwise in compliance with the requirements of this Agreement.

Bombardier's obligation hereunder shall extend to Other Patents only if from the time of design of the Aircraft, system, accessory, equipment or part until the alleged infringement claims are resolved:

(d) such other country and the country in which the Aircraft is permanently registered have ratified and adhered to and are at the time of the actual or alleged infringement contracting parties to the Chicago Convention on International Civil Aviation of December 7, 1944 and are fully entitled to all benefits of Article 27 thereof; and

(e) such other country and the country of registration shall each have been a party to the International Convention for the Protection of Industrial Property (Paris Convention) or have enacted patent laws which recognize and give adequate protection to inventions made by the nationals of other countries which have ratified, adhered to and are contracting parties to both of the forgoing conventions.

18.2 The foregoing indemnity does not apply to BFE, or to avionics, engines or any system, accessory, equipment or part that was not manufactured to Bombardier's detailed design or to any system, accessory, equipment or part manufactured by a third party to Bombardier's detailed design without Bombardier's authorization.

18.3 Buyer's remedy and Bombardier's obligation and liability under this Article are conditional upon (i) Buyer giving Bombardier written notice within [CONFIDENTIAL TREATMENT REQUESTED] after Buyer receives notice of a suit or action against Buyer alleging infringement or within [CONFIDENTIAL TREATMENT REQUESTED] after Buyer receives any other written claim of infringement (ii) Buyer uses reasonable efforts in full cooperation with Bombardier to reduce or mitigate any such expenses, damages, costs or royalties involved, and (iii) Buyer furnishes promptly to Bombardier all data, papers and records in its possession or control necessary or useful to resist and defend against such claim or suit. Bombardier may at its option conduct negotiations with any party claiming infringement and may intervene in any suit or action. Whether or not Bombardier intervenes, Bombardier shall be entitled at any stage of the proceedings to assume or control the defense. Bombardier shall have no obligation under this Article 18 if Buyer pays or assumes any liabilities, expenses, damages, royalties or costs without Bombardier's prior approval.

18.4 [CONFIDENTIAL TREATMENT REQUESTED].

ARTICLE 19 - LIMITATION OF LIABILITY AND INDEMNIFICATION

19.1 [CONFIDENTIAL TREATMENT REQUESTED].

19.2 [CONFIDENTIAL TREATMENT REQUESTED].

19.3 [CONFIDENTIAL TREATMENT REQUESTED].

19.4 INTENTIONALLY DELETED

ARTICLE 20 - ASSIGNMENT

20.1 Either party may assign, sell, transfer or dispose of (in whole or in part) any of its rights and obligations hereunder or a Supplement to an affiliate or a wholly owned subsidiary provided that there is no increase to the liability and/or responsibility of the non-assigning party and that the assigning party remains jointly and severally liable with any assignee for the performance of its obligation under this Agreement. In addition, either party may assign its interest to a corporation (i) that results from any merger, consolidation, or a reorganization of such party; or (ii) into which such party may be merged or with which it maybe consolidated.

20.2 Except as provided in Article 20.1, Buyer shall not assign, sell, transfer or dispose of (in whole or in part) any of its rights or obligations hereunder or a Supplement without Bombardier's prior written consent. In the event of such assignment, sale, transfer or disposition Buyer shall remain jointly and severally liable with any assignee for the performance of all and any of Buyer's obligations under this Agreement and Bombardier reserves the right as a condition of its consent to amend one or more of the terms and conditions of this Agreement and (including for more certainty) the applicable Supplement.

20.3 Notwithstanding Article 20.2 above, Buyer may assign, after transfer of title of the Aircraft, its rights under this Agreement, save and except for any rights of Buyer which are expressly stated to be personal to Buyer, to a third party purchaser of any one of the Aircraft, upon obtaining from said third party an acknowledgment in writing to be bound by the applicable terms and conditions of this Agreement, including but not limited to the provisions and limitations as detailed Annex A, Customer Support Services, Annex B, Warranty and Service Life Policy and of the provisions and limitations in Limitation of Liability as defined in Article 19 hereof and Indemnity Against Patent Infringement as defined in Article 18 hereof and any other on-going obligations of Buyer, which shall apply to it to the same extent as if said third party was Buyer hereunder and, provided that there is no increase to the liability and/or responsibility of Bombardier.

20.4 Bombardier may assign any of its rights to receive money hereunder without the prior consent of Buyer.

20.5 Notwithstanding the other provisions of this Article 20, Bombardier shall, at Buyer's cost and expense, if so requested in writing by Buyer, take any action reasonably required for the purpose of causing any of the Aircraft to be subjected (i) to, after the Delivery Date, an equipment trust, conditional sale or lien, or (ii) to another arrangement for the financing of the Aircraft by Buyer, providing, however, there shall be no increase to the liability and/or responsibility of Bombardier arising through such financing, and no transfer of title of an Aircraft shall occur until payment therefore as provided in this Agreement.

ARTICLE 21 - SUCCESSORS

21.1 This Agreement shall inure to the benefit of and be binding upon each of Bombardier and Buyer and their respective successors and permitted assignees.

ARTICLE 22 - APPLICABLE LAWS

22.1 THIS AGREEMENT AND (INCLUDING FOR MORE CERTAINTY) SUPPLEMENTS PURSUANT HERETO SHALL BE SUBJECT TO AND CONSTRUED IN ACCORDANCE WITH AND THE RIGHTS OF THE PARTIES SHALL BE GOVERNED BY THE DOMESTIC LAWS OF THE PROVINCE OF ONTARIO, CANADA, EXCLUDING THE CHOICE OF LAW RULES, AND THE PARTIES HAVE AGREED THAT THE APPLICATION OF THE UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS IS HEREBY EXCLUDED.

22.2 Bombardier's obligations under this Agreement shall be subject to and apply only to the extent permitted by applicable laws, regulations, directives and/or orders regarding export controls.

ARTICLE 23 - CONFIDENTIAL NATURE OF AGREEMENT

23.1 Except as required by law, this Agreement including any Supplements hereto are confidential between the parties and shall not, without the prior written consent of the other party, be disclosed by either party in whole or in part to any other person or body except as may be necessary for either party to carry out its obligations under this Agreement. Nevertheless the parties agree to cooperate to keep this Agreement confidential.

23.2 Except as may be reasonably required for the normal operation, maintenance, overhaul and repair of the Aircraft, each party shall hold confidential all technical data and information supplied by or on behalf of the other party. Buyer shall not reproduce any technical data or information or divulge the same to any third party without obtaining a confidentiality agreement in favor of and acceptable to Bombardier.

23.3 Either party may announce the signing of this Agreement by means of a notice to the press provided that the content and date of the notice has been agreed to by the other party.

23.4 It is understood by the parties that this Agreement is required to be filed as an exhibit to a registration statement under the Securities Act of 1933, as amended (the "Securities Act"), or a periodic report under the Securities Exchange Act of 1934, as amended ("Exchange Act"). Buyer shall notify Bombardier, by written notice, at [CONFIDENTIAL TREATMENT REQUESTED] prior to the date of such anticipated filing of such determination and the reasons therefor, and shall use its best efforts to work with Bombardier to prepare and file with the Securities and Exchange Commission (the "Commission") a request for confidential treatment pursuant to Rule 24b-2 under the Exchange Act or Rule 406 under the Securities Act, as the case may be, with respect to information in this Agreement, and such other information as Bombardier may reasonably request.

Subject to compliance with the foregoing, and notwithstanding the other provisions of this Article, portions of this Agreement or a Supplement hereto may be filed as exhibits to such registration statement or periodic report to the extent required by the Commission and such filing shall not constitute a breach hereof by Buyer. This provision shall survive until the latter of (i) the complete performance by Buyer of its obligation hereunder or (ii) [CONFIDENTIAL TREATMENT REQUESTED] from the date hereof.

ARTICLE 24 - AGREEMENT

24.1 This Agreement including any Supplements pursuant hereto, as same may be amended from time to time, and the matters referred to herein constitute the entire Agreement between Bombardier and Buyer with respect to the Bombardier products governed by the applicable Supplements and supersede and cancel all prior representations, brochures, alleged warranties, statements, negotiations, undertakings, letters, memoranda of agreement, proposals, acceptances, agreements, understandings, contracts and communications, whether oral or written, between Bombardier and Buyer or their respective agents, with respect to or in connection with the subject matter of this Agreement and the applicable Supplement and no agreement or understanding varying the terms and conditions hereof shall be binding on either Bombardier or Buyer hereto unless an amendment to this Agreement or the applicable Supplement is issued and duly signed by their respective authorized representatives pursuant to the provisions of this Article hereof. In the event of any inconsistencies between this Agreement and a Supplement or the Appendices, Exhibits and Annexes or other documents referred to herein, the provisions of the Supplement shall prevail.

24.2 If any of the provisions of this Agreement or a Supplement are for any reason declared by judgment of a court of competent jurisdiction to be unenforceable or ineffective, those provisions shall be deemed severable from the other provisions of this Agreement/the Supplement and the remainder of this Agreement/the Supplement shall remain in full force and effect.

24.3 [CONFIDENTIAL TREATMENT REQUESTED].

24.4 Bombardier and Buyer confirm to each other they have each obtained the required authorizations and fulfilled any conditions applicable to enable each of them to enter into this Agreement and any Supplement.

24.5 Buyer and Bombardier agree that this Agreement has been the subject of discussion and negotiation and is fully understood by the parties hereto and that the other mutual agreements of the parties set forth herein were arrived at in consideration of the provisions contained in this Agreement, taken as a whole, [CONFIDENTIAL TREATMENT REQUESTED].

In witness whereof this Agreement was signed on the date written hereof:

For and on behalf of For an on behalf of

HORIZON AIR INDUSTRIES, INC. BOMBARDIER INC.
Bombardier Aerospace

Original signed by G. Johnson	Original signed by R. Gillespie
__________________________	_______________________________
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

____
Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SECTION II

OF

MASTER PURCHASE AGREEMENT NO. PA-436

AIRLINE SERVICES

ANNEX A

TECHNICAL SUPPORT, SPARE PARTS TRAINING AND TECHNICAL DATA

ANNEX B

WARRANTY AND SERVICE LIFE POLICY

ANNEX A

TECHNICAL SUPPORT, SPARE PARTS, TRAINING AND TECHNICAL DATA

The following Airline Services are those services to which reference is made in Article 3 of the Agreement.

ARTICLE 1 - TECHNICAL SUPPORT

1.1 Factory Service

Bombardier agrees to maintain or cause to be maintained the capability to respond to Buyer's technical inquiries, to conduct investigations concerning repetitive maintenance problems and to issue findings and recommend action thereon. This service shall be provided for as [CONFIDENTIAL TREATMENT REQUESTED].

1.2 Field Service Representative

1.2.1 Services

Bombardier shall assign [CONFIDENTIAL TREATMENT REQUESTED] Field Service Representative ("FSR") to Buyer's main base of operation or other location and or such period as may be mutually agreed, all as provided in the applicable Supplement.

1.2.2 Term

The FSR term is as set out in the applicable Supplement.

1.2.3 Responsibility

The FSR's responsibility shall be to provide technical advice to Buyer for the line maintenance and operation of the Aircraft systems and troubleshooting during scheduled and unscheduled maintenance by Buyer's designated personnel ("FSR Services").

1.2.4 Travel

If requested by Buyer, the FSR may, at Buyer's expense, travel to another location to provide technical advice to Buyer.

1.2.5 Office Facilities

Buyer shall furnish the FSR, at no charge to Bombardier, suitable and private office facilities and related equipment including desk, file cabinet, access to two telephone lines, facsimile and photocopy equipment conveniently located at Buyer's main base of operation or other location as may be mutually agreed.

1.2.6 Additional Expenses

Buyer shall reimburse Bombardier (net of any additional taxes on such reimbursement) the amount of any and all taxes (except Canadian taxes on the income of the FSR) and fees of whatever nature, including any customs duties, withholding taxes or fees together with any penalties or interest thereon, except for penalties or interest resulting from Bombardier's fault or negligence, paid or incurred by Bombardier or the FSR or other Bombardier employee as a result of or in connection with the rendering of the services.

1.2.7 Right to Stop Work

Bombardier shall not be required to commence or continue the FSR Services when:

(a) there is a labour dispute or work stoppage in progress at Buyer's main maintenance facilities;

(b) there exist war, risk of war or warlike operations, riots or insurrections which is likely to affect Buyer's facility;

(c) there exist conditions that are dangerous to the safety or health of the FSR or other Bombardier employee; or

(d) the Government of the country where Buyer's facilities are located or where Buyer desires the FSR to travel refuses the Bombardier employees permission to enter said country or Buyer's base of operations.

1.2.8 Work Permits and Clearances

Bombardier and Buyer shall cooperate to arrange for all necessary work permits and airport security clearances required for the FSR or other Bombardier employee to permit timely accomplishment of the FSR services.

1.3 Maintenance Planning Support

1.3.1 Scheduled Maintenance Task Cards

As described in the applicable Supplement, Bombardier shall provide Buyer Bombardier's standard format scheduled maintenance task cards that shall conform to the Aircraft at the Delivery Date. At Buyer's request Bombardier shall provide a proposal for task cards produced to Buyer's format.

1.3.2 In-Service Maintenance Data

Buyer agrees to provide to Bombardier in-service maintenance data in order to provide updates to Bombardier's recommended maintenance program. Buyer and Bombardier shall agree on standards and frequency for communication of such data.

1.4 Additional Services

At Buyer's request Bombardier shall provide a proposal to provide such additional support services as the parties may agree upon, which may include special investigations, maintenance and repair of the Aircraft.

ARTICLE 2 - SPARE PARTS, GSE, TOOLS AND TEST EQUIPMENT

2.1.1 Definitions

a. "Bombardier Parts":

any spare parts, ground support equipment, tools and test equipment which bear an in-house Cage Code number in the Bombardier Provisioning Files (as that expression is defined in ATA Specification 200).

b. "Power Plant Parts":

any power plant or power plant part or assembly carrying the power plant manufacturer's part number or any part furnished by the power plant manufacturer for incorporation on the Aircraft.

c. "Vendor Parts":

any spare parts, ground support equipment, tools and test equipment for the Aircraft which are not Bombardier Parts or Power Plant Parts.

d. "Spare Parts":

all materials, spare parts, assemblies, special tools and items of equipment, including ground support equipment, ordered for the Aircraft by Buyer from Bombardier. The term Spare Parts includes Bombardier Parts, Power Plant Part and Vendor Parts.

e. "Order":

any order for Spare Parts issued by Buyer to Bombardier; and

f. "Technical Data":

shall have the meaning attributed to it in the applicable

Supplement.

2.1 Term and Applicability

The term of this Annex A Article 2 shall become effective on the date hereof and shall remain in full force and effect with respect to the purchase and sale of Spare Parts for each Aircraft so long as [CONFIDENTIAL TREATMENT REQUESTED]. The provisions of Annex A Articles 2.2, 2.6.5, 2.24 and Annex B Article 5.0 shall survive expiration or termination of this Agreement.

2.2 Order Terms

Terms and conditions hereof shall apply to all Orders placed by Buyer with Bombardier in lieu of any terms and conditions in Buyer's purchase orders.

2.3 Purchase and Sale of Spare Parts

2.3.1 Agreement to Manufacture and Sell

Bombardier shall manufacture, or procure, and make available for sale to Buyer suitable Spare Parts in quantities sufficient to meet the reasonably anticipated needs of Buyer for normal maintenance and normal spares inventory replacement for each Aircraft. During the term specified in Annex A Article 2.1 above, Bombardier shall also maintain a shelf stock of certain Bombardier Parts selected by Bombardier to ensure reasonable re-order lead times and emergency support. Bombardier shall maintain a reasonable quantity of Bombardier insurance parts. Insurance parts as used herein shall include, but not be limited to, dispatch-essential parts such as major flight control surfaces.

2.4 Agreement to Purchase Bombardier Parts

2.4.1 Purchase of Bombardier Parts

[CONFIDENTIAL TREATMENT REQUESTED]
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2.4.2 Purchase of Bombardier Parts from Other Approved Sources

Buyer may obtain Bombardier Parts from any source provided that such source is approved by Bombardier and provided that such Bombardier Parts are for Buyer's use only.

2.4.3 Buyer's Right to Purchase, Redesign or Manufacture

Buyer's right to purchase, [CONFIDENTIAL TREATMENT REQUESTED] or to have manufactured Bombardier Parts under the preceding Article shall not be construed as a granting of a license by Bombardier and shall not obligate Bombardier to disclose to anyone Technical Data or other information nor to the payment of any license fee or royalty or create any obligation whatsoever to Bombardier and Bombardier shall be relieved of any obligation or liability with respect to patent infringement in connection with any such [CONFIDENTIAL TREATMENT REQUESTED]. Buyer shall be responsible for obtaining all regulatory authority approvals required by Buyer to repair the Aircraft using[CONFIDENTIAL TREATMENT REQUESTED].
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2.4.4 Notice to Bombardier of Redesigned Parts

[CONFIDENTIAL TREATMENT REQUESTED].

2.5 Purchase of Vendor Parts & Power Plant Parts

Bombardier shall not be obligated to maintain a stock of Vendor Parts or Power Plant Parts. Bombardier may elect to maintain a spares stock of selected Vendor Parts at its own discretion to support provisioning and replenishment sales. Bombardier agrees to use reasonable efforts to require its vendors to comply with the terms and conditions of this Annex A Article 2 as they apply to Vendor Parts. Vendor Parts shall be delivered in accordance with the vendor's quoted lead time plus Bombardier's internal processing time.

2.6 Spare Parts Pricing

2.6.1 Spare Parts Price Catalogue

Prices for commonly used Bombardier Parts stocked by Bombardier shall be published in the spare parts price catalogue ("Spare Parts Price Catalogue"). [CONFIDENTIAL TREATMENT REQUESTED].

2.6.2 Bombardier Prices for Vendor Parts

If Buyer orders Vendor Parts from Bombardier, the price shall be as published in the Spare Parts Price Catalogue.

2.6.3 Quotations

Price and delivery quotations for items not included in the Spare Parts Price Catalogue shall be provided at Buyer's request by Bombardier. [CONFIDENTIAL TREATMENT REQUESTED]
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2.6.4 Price Applicability

The purchase price of Bombardier Parts shall be the applicable price set forth in the Spare Parts Price Catalogue at time of receipt by Bombardier of Buyer's Order or as quoted by Bombardier to Buyer upon request. If Buyer requests accelerated delivery or special handling for Bombardier Parts not included in the Spare Parts Price Catalogue, Bombardier may increase the price from the original quotation to cover any additional costs to Bombardier.

2.6.5 Currency and Taxes

All Spare Parts Price Catalogue and quotation prices shall be in U.S. dollars and exclusive of transportation, taxes, duties and licenses.

[CONFIDENTIAL TREATMENT REQUESTED]

The parties hereto agree, subject to applicable laws, to work together to minimize the imposition of taxes and fees herein. In addition, Buyer shall pay to Bombardier on demand the amount of any customs duties required to be paid by Bombardier with respect to the importation by Buyer of any Spare Parts.

2.6.6 Vendor Pricing

Bombardier shall use reasonable efforts to require its major vendors to maintain any published price for their parts for a period of at [CONFIDENTIAL TREATMENT REQUESTED] with a [CONFIDENTIAL TREATMENT REQUESTED] notice period prior to changing a published price.

2.7 Provisioning

2.7.1 Pre-provisioning/Provisioning Conference

Pre-provisioning and provisioning conferences shall be convened on dates to be mutually agreed between Buyer and Bombardier in order to:

(a) discuss the operational parameters to be provided by Buyer to Bombardier which Bombardier considers necessary for preparing its quantity recommendations for initial provisioning of Spare Parts to be purchased from Bombardier or vendors ("Provisioning Items");

(b) review Buyer's ground support equipment and special tool requirements for the Aircraft;

(c) discuss the format of the provisioning documentation to be provided to Buyer from Bombardier for the selection of Provisioning Items; and

(d) arrive at a schedule of events for the initial provisioning process, including the establishment of a date for the initial provisioning conference ("Initial Provisioning Conference") which shall be scheduled where possible at least [CONFIDENTIAL TREATMENT REQUESTED] prior to delivery of the first Aircraft under an applicable Supplement.

The time and location of the pre-provisioning conference shall be mutually agreed upon between the parties; however, Bombardier and Buyer shall use their best efforts to convene such meeting within [CONFIDENTIAL TREATMENT REQUESTED] after execution of the applicable Supplement.

2.8 Initial Provisioning Documentation

Initial provisioning documentation for Bombardier Parts and Vendor Parts shall be provided by Bombardier as follows:

(a) Bombardier shall provide, as applicable to Buyer, no later than [CONFIDENTIAL TREATMENT REQUESTED]prior to the Scheduled Delivery Date of the first Aircraft under the applicable Supplement or as may be mutually agreed, the initial issue of provisioning files as required by ATA Specification 200, Chapter 1 (as may be amended by Bombardier);

Revisions to this provisioning data shall be issued by Bombardier [CONFIDENTIAL TREATMENT REQUESTED] following the Delivery Date of the last Aircraft under the applicable Supplement or as may be mutually agreed;

(b) Bombardier shall provide, as required by Buyer, all data files defined in Chapter 1 of ATA Specification 200; and

(c) the Illustrated Parts Catalogue designed to support provisioning shall be issued concurrently with provisioning data files and revised at [CONFIDENTIAL TREATMENT REQUESTED].

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2.8.1 Obligation to Substitute Obsolete Spare Parts

In the event that, prior to delivery of the first Aircraft under an applicable Supplement, any Spare Part purchased by Buyer from Bombardier is rendered obsolete or unusable due to the redesign of the Aircraft or of any accessory, equipment or part thereto (other than a redesign at Buyer's request), Bombardier shall deliver to Buyer new and usable Spare Parts in substitution for such obsolete or unusable Spare Parts upon return of such Spare Parts to Bombardier by Buyer. Bombardier shall credit Buyer's account with Bombardier with the price paid by Buyer for any such obsolete or unusable Spare Part and shall invoice Buyer for the purchase price of any such substitute Spare Part delivered to

Buyer.

2.8.2 Delivery of Obsolete Spare Parts and Substitutes

Obsolete or unusable Spare Parts returned by Buyer pursuant to Annex A Article 2.8.1. shall be delivered to Bombardier at its plant in Ontario or Quebec, or such other destination as Bombardier may reasonably designate. Spare Parts substituted for such returned obsolete or unusable Spare Parts shall be delivered to Buyer from Bombardier's plant in Ontario or Quebec, or such other Bombardier shipping point as Bombardier may reasonably designate. Bombardier shall pay the freight charges for the shipment from Buyer to Bombardier of any such obsolete or unusable Spare Part and for the shipment from Bombardier to Buyer of any such substitute Spare Part.

2.8.3 Obligation to Repurchase Surplus Provisioning Items

During a period commencing [CONFIDENTIAL TREATMENT REQUESTED] after the Delivery Date of the first Aircraft under an applicable Supplement, and ending [CONFIDENTIAL TREATMENT REQUESTED] after such Delivery Date, Bombardier shall, upon receipt of Buyer's written request and subject to the exceptions in Annex A Article 2.8.4, repurchase unused and undamaged Provisioning Items which: (i) were recommended by Bombardier as initial provisioning for the Aircraft, (ii) were purchased by Buyer from Bombardier, and (iii) are surplus to Buyer's needs.

2.8.4 Exceptions

Bombardier shall not be obligated under Annex A Article 2.8.3 to repurchase any of the following: (i) quantities of Provisioning Items in excess of those quantities recommended by Bombardier in its Recommended Spare Parts List ("RSPL") for the Aircraft, (ii) Power Plant Parts, QEC Kits, standard hardware, bulk and raw materials, ground support equipment and special tools, (iii) Provisioning Items which have become obsolete or have been replaced by other Provisioning Items as a result of (a) Buyer's modification of the Aircraft or (b) design improvement by the Aircraft manufacturer or the vendor (other than Provisioning Items which have become obsolete because of a defect in design if such defect has not been remedied by an offer by Bombardier or the vendor to provide no charge retrofit kits or replacement parts which correct such defect), and (iv) Provisioning Items which become surplus as a result of a change in Buyer's operating parameters provided to Bombardier pursuant to Annex A Article 2.7, which were the basis of Bombardier's initial provisioning recommendations for the Aircraft.

2.8.5 Notification and Format

Buyer shall notify Bombardier, in writing, when Buyer desires to return Provisioning Items which Buyer's review indicates are eligible for repurchase by Bombardier under the provisions of Annex A Article 2.8.3. Buyer's notification shall include a detailed summary, in part number sequence, of the Provisioning Items Buyer desires to return. Such summary shall be in the form of listings as may be mutually agreed between Bombardier and Buyer, and shall include part number, nomenclature, purchase order number, purchase order date and quantity to be returned.

Within [CONFIDENTIAL TREATMENT REQUESTED] after receipt of Buyer's notification Bombardier shall advise Buyer, in writing, when Bombardier's review of such summary from Buyer will be completed.

2.8.6 Review and Acceptance by Bombardier

Upon completion of Bombardier's review of any detailed summary submitted by Buyer pursuant to Annex A Article 2.8.5., Bombardier shall issue to Buyer a Material Return Authorization notice ("MRA") for those Provisioning Items Bombardier agrees are eligible for repurchase in accordance with Annex A Article 2.8.3. Bombardier will advise Buyer of the reason that any Provisioning Items included in Buyer's detailed summary are not eligible for return. The MRA notice shall state the date by which Provisioning Items listed in the MRA notice must be redelivered to Bombardier and Buyer shall arrange for shipment of such Provisioning Items accordingly.

2.8.7 Price and Payment

The price of each Provisioning Item repurchased by Bombardier pursuant to Annex A Article 2.8.6[CONFIDENTIAL TREATMENT REQUESTED].
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2.8.8 Return of Surplus Provisioning Items

Provisioning Items repurchased by Bombardier pursuant to Annex A Article 2.8.6 shall be delivered to Bombardier Free Carrier (Incoterms), at its plant in Ontario or Quebec, or other such destination as Bombardier may reasonably designate.

2.8.9 Obsolete Spare Parts and Surplus Provisioning Items - Title and Risk of Loss

Title to and risk of loss of any obsolete or unusable Spare Parts returned to Bombardier pursuant to Annex A Article 2.8.8 shall pass to Bombardier upon delivery thereof to Bombardier. Title to and risk of loss of any Spare Parts substituted for an obsolete or unusable Spare Part pursuant to Annex A Article 2.8.1 shall pass to Buyer upon delivery thereof to Buyer. Title to and risk of loss of any Provisioning Items repurchased by Bombardier pursuant to Annex A Article 2.8.3 shall pass to Bombardier upon delivery thereof to Bombardier.

With respect to the obsolete or unusable Spare Parts which may be returned to Bombardier and the Spare Parts substituted therefor, pursuant to Annex A Article 2.8.1, and the Provisioning Items which may be repurchased by Bombardier, pursuant to Annex A Article 2.8.3, the party which has the risk of loss of any such Spare Part or Provisioning Item shall have the responsibility of providing any insurance coverage thereon desired by such party.

2.9 Procedure for Ordering Spare Parts

Orders for Spare Parts may be placed by Buyer to Bombardier by any method of order placement (including but not limited to SITA, ARINC, telecopier, letter, telex, facsimile, telephone or hard copy purchase order).

2.9.1 Requirements

Orders shall include at a minimum order number, part number, nomenclature, quantity, delivery schedule requested, shipping instructions and Bombardier's price, if available. Buyer agrees that orders placed with Bombardier shall conform to the requirements and procedures contained in ATA Specification 200, as applicable to Buyer.

2.9.2 Processing of Orders

Upon acceptance of any Order, unless otherwise directed by Buyer, Bombardier shall, if the Spare Parts are in stock, proceed immediately to prepare the Spare Parts for shipment to Buyer. If Bombardier does not have the Spare Parts in stock, Bombardier shall proceed immediately to acquire or manufacture the Spare

Parts. Purchase order status and actions related to the shipment of Spare Parts shall be generally consistent with the provisions of the World Airline Suppliers Guide and the applicable portions of ATA Specification 200, as applicable to Buyer.

2.9.3 Changes

Bombardier reserves the right, without Buyer's consent, to make any necessary corrections or changes in the design, part number and nomenclature of Spare Parts covered by an Order, to substitute Spare Parts and to adjust prices accordingly, provided that interchangeability is not affected and the[CONFIDENTIAL TREATMENT REQUESTED], whichever is less. Bombardier shall promptly give Buyer written notice of corrections, changes, substitutions and consequent price adjustments. Corrections, changes, substitutions and price adjustments which affect interchangeability or exceed the price limitations set forth above may be made only with Buyer's consent, which consent shall conclusively be deemed to have been given unless Buyer gives Bombardier written notice of objection within [CONFIDENTIAL TREATMENT REQUESTED]days after receipt of Bombardier's notice. In case of any objection, the affected Spare Part will be deemed to be deleted from Buyer's Order and Buyer shall have the right to manufacture or purchase elsewhere such spare part.

2.9.4 Electronic Data Interchange

2.9.4.1 Use of Electronic Data Interchange (EDI)

Bombardier is not currently using EDI, however, if and when Bombardier has the capability and equipment to utilize EDI Bombardier will offer EDI transactions in accordance to the parameters set forth below.

The SPEC 200 Protocol shall be used for any EDI transaction. Buyer and Bombardier shall implement security procedures to ensure proper use of this communication. A message will be considered received only at the point where it is in a format which can be accepted by the receiving computer according to ATA SPEC 200 rules on transmissions. If garbled transmissions are received, the receiver shall promptly notify the sender through use of the S1REJECT command.

2.9.4.2 Acceptance of EDI Transactions

The SIBOOKED transaction creates an obligation on the part of Buyer to purchase the material and quantities as specified in the transmission. Bombardier is obliged to sell the material and quantities as specified except as may be identified in a subsequent SIORDEXC message. With respect to a S1QUOTES transaction, Buyer and Bombardier are bound to respect the prices quoted in the transmission in any resultant S1BOOKED order transaction based upon that S1QUOTES message within the validity period of the S1QUOTES message. An S1NVOICE message will be considered as the official commercial invoice for the goods shipped. An S1STOCKS, S1SHIPPD, S1POSTAT or S1PNSTAT message creates no obligations on either the Buyer or Bombardier. If an S1BOOKED acknowledgment is not sent within 24 hours by Bombardier then Buyer shall resend the original message.

Any document which has been properly received shall not give rise to any obligation unless and until the party receiving such document has properly transmitted in return an acknowledgment document according to SPEC 200 Protocol.

2.9.4.3 Systems Operations

Buyer and Bombardier, at their own expense, shall provide and maintain the equipment, software, services and testing necessary to effectively and reliably transmit and receive documents.

2.9.4.4 Validity of Documents

Annex A Article 2.9.4 has been agreed to by Buyer and Bombardier to evidence their mutual intent to create binding purchase and sale obligations pursuant to the electronic transmission and receipt of documents as described herein.

Such documents properly transmitted pursuant to this Annex A Article 2.9.4 shall be considered, in connection with any transaction or any other agreement, to be a "writing" or "in writing" and shall be deemed for all purposes (a) to have been "signed" and (b) to constitute an "original" when printed from electronic files or records established and maintained in the normal course of business.

Buyer and Bombardier agree not to contest the validity or enforceability of signed documents under the provisions of any applicable law relating to whether certain agreements are to be in writing or signed by either party to be bound thereby. Signed documents, if introduced as evidence on paper in any judicial, arbitration, mediation or administrative proceedings, will be admissible as between Buyer and Bombardier to the same extent and under the same conditions as other business records originated and maintained in documentary form. Neither Buyer nor Bombardier shall contest the admissibility of copies of signed documents under either the business records exception to the hearsay rule or the best evidence rule on the basis that the signed documents were not originated or maintained in documentary form.

2.9.4.5 Limitation of Liability
[CONFIDENTIAL TREATMENT REQUESTED].

2.10 Packing

All Spare Parts ordered shall receive standard commercial packing suitable for export shipment via air freight. Such standard packing will generally be to ATA 300 standards as amended from time to time. All AOG orders will be handled, processed, packed and shipped separately.

2.11 Packing List

Bombardier shall insert in each shipment a packing list/release note itemized to show:

(a) the contents of the shipment,

(b) the approved signature of Bombardier's TC authority attesting to the airworthiness of the Spare Parts.

(c) value of the shipment for customs clearance if required.

2.12 Container Marks

Upon Buyer's request each container shall be marked with shipping marks as specified on the Order. In addition Bombardier shall, upon request, include in the markings: gross weight and cubic measurements.

2.13 Delivery, Title and Risk of Loss

2.13.1 Delivery Point

Spare Parts shall be delivered to Buyer in one of the following manners at Bombardier's sole option:

(a) Free Carrier (Incoterms 1990) Bombardier's plant in either Ontario or Quebec, Canada; or

(b) Free Carrier (Incoterms 1990) other Bombardier depots or shipping points; or

(c) Free Carrier (Incoterms 1990) vendor's or subcontractor's plant.

2.13.2 Delivery Time

Bombardier shall use reasonable efforts so that shipment of Bombardier Parts to Buyer be as follows:

(a) AOG Orders

[CONFIDENTIAL TREATMENT REQUESTED];

(b) Critical Orders (A1)

[CONFIDENTIAL TREATMENT REQUESTED];

(c) Expedite Orders (A2)

[CONFIDENTIAL TREATMENT REQUESTED];

(d) Initial Provisioning Orders

[CONFIDENTIAL TREATMENT REQUESTED]; and

(e) Other Orders

[CONFIDENTIAL TREATMENT REQUESTED].

2.14 Collect Shipments

Where collect shipments are not deemed practicable by Bombardier, charges for shipment, insurance, prepaid freight charges and all other costs paid by Bombardier shall be paid by Buyer promptly upon presentation to Buyer of invoices covering the same.

2.15 Freight Forwarder

If Buyer elects to use the services of a freight forwarder for the onward movement of Spare Parts, Buyer agrees to release Bombardier from and indemnify it for any liability for any fines or seizures of Spare Parts imposed under any governmental Goods in Transit regulations. Any such fines levied against Bombardier will be invoiced to Buyer and any Spare Parts seized under such regulations will be deemed to be received, inspected, and accepted by Buyer at the time of seizure.

2.16 Reimbursement of Expenses

If Bombardier gives Buyer written notice that an Order is ready for shipment and shipment is delayed more than [CONFIDENTIAL TREATMENT REQUESTED] at Buyer's request or without Bombardier's fault or responsibility, Buyer shall promptly reimburse Bombardier upon demand for all costs and expenses, including but not limited to reasonable amounts for storage, handling, insurance and taxes, incurred by Bombardier as a result of such delay.

2.17 Title and Risk of Loss

Property and title to the Spare Parts will pass to Buyer upon payment for the Spare Parts in full. Until payment in full for Spare Parts, (a) title to them will not pass to Buyer, and (b) Bombardier maintains a purchase money security interest in them. Risk of loss of the Spare Parts will pass to the Buyer upon delivery by Bombardier. With respect to Spare Parts rejected by Buyer pursuant to Annex A Article 2.19, risk of loss shall remain with Buyer until such Spare Parts are re-delivered to Bombardier.

Bombardier agrees to notify Buyer when material is shipped and shall provide carrier's reference information (i.e., waybill number).

2.18 Inspection and Acceptance

All Spare Parts shall be subject to inspection by Buyer at destination. Use of Spare Parts or failure of Buyer to give notice of rejection [CONFIDENTIAL TREATMENT REQUESTED] after receipt shall constitute acceptance. Acceptance shall be final and Buyer waives the right to revoke acceptance for any reason, whether or not known to Buyer at the time of acceptance. Buyer's remedies for defects discovered before acceptance are exclusively provided for in Annex A Article 2.19 herein.

2.19 Rejection

Any notice of rejection referred to in Annex A Article 2.18 shall specify the reasons for rejection. If Bombardier concurs with a rejection, Bombardier shall, at its option, correct, repair or replace the rejected Spare Parts. Buyer shall, upon receipt of Bombardier's written instructions and Material Return Authorization ("MRA") number, return the rejected Spare Parts to Bombardier at its specified plant, or other destination as may be mutually agreeable. The return of the rejected Spare Parts to Bombardier and the return or delivery of a corrected or repaired rejected Spare Part or any replacement for any such Spare Part to Buyer shall be at Bombardier's expense. Any corrected, repaired or replacement Spare Parts shall be subject to the provisions of this Agreement including any applicable Supplement.

2.20 Payment

Except as provided in Annex A Article 2.22 below, payment terms shall be net thirty (30) calendar days of invoice date for established open accounts. [CONFIDENTIAL TREATMENT REQUESTED].

2.21 Payment for Provisioning Items

Payment for Provisioning Items shall be made by Buyer as follows:

(a) [CONFIDENTIAL TREATMENT REQUESTED]; and

(b) [CONFIDENTIAL TREATMENT REQUESTED]

2.22 Modified Terms of Payment

Bombardier reserves the right to alter the terms of a payment without prior notice if Buyer fails to pay when due a material, undisputed amount Buyer owes under any agreement with Bombardier.

2.23 Regulations

Buyer shall comply with all applicable monetary and exchange control regulations and shall obtain any necessary authority from the governmental agencies administering such regulations to enable Buyer to make payments at the time and place and in the manner specified herein.

2.24 Warranty

[CONFIDENTIAL TREATMENT REQUESTED].

2.25 Cancellation of Orders

[CONFIDENTIAL TREATMENT REQUESTED].

2.26 Lease

Bombardier shall select and make available certain parts for lease, subject to availability Buyer has the option to negotiate a lease agreement with Bombardier separate from this Agreement and the applicable Supplement.

2.27 Additional Terms and Conditions

Bombardier's conditions of sale are deemed to incorporate the terms and conditions stated herein and within an applicable Supplement. Additional terms and conditions applicable at time of receipt of each order from Buyer may be added providing such terms and conditions do not conflict with the terms and conditions provided herein and within an applicable Supplement. Such additional terms and conditions shall be provided to Buyer at [CONFIDENTIAL TREATMENT REQUESTED] prior to their effective date.

ARTICLE 3 - TRAINING

3.1 General Terms

3.1.1 The objective of the training programs (the "Programs") described in this Agreement and the applicable Supplement is to familiarize and assist Buyer's personnel in the introduction, operation, and maintenance of the Aircraft.

3.1.2 Bombardier shall offer the Programs to Buyer in the English language, at a Bombardier designated facility. The Programs shall be completed prior to the Delivery Date of the last Aircraft purchased under the applicable Supplement.

3.1.3 Buyer shall be responsible for all travel and living expenses (including local transportation) of Buyer's personnel incurred in connection with the Programs.

3.1.4 The Programs shall be designed to reflect the model and/or configuration of the Aircraft and may include differences training to identify such configuration or model. Manuals or other training material which are provided during the Programs exclude revision service.

3.1.5 The Programs are designed for candidates who meet the following minimum prerequisites:

(a) Pilots

[CONFIDENTIAL TREATMENT REQUESTED]

(b) Flight Attendants

[CONFIDENTIAL TREATMENT REQUESTED]

(c) Flight Dispatchers

[CONFIDENTIAL TREATMENT REQUESTED]

(d) Maintenance Technicians

[CONFIDENTIAL TREATMENT REQUESTED]

3.1.6 Prior to commencement of the Programs, upgrade training can be arranged for Buyer's personnel who do not meet the above minimum requirements. Any such upgrade training shall be provided upon terms and conditions to be mutually agreed.

3.1.7 Should any of Buyer's personnel who do not meet the above minimum requirements encounter problems during their training, any additional training or costs (such as costs for interpreters) shall be borne by Buyer.

3.1.8 A training conference shall be held, if practicable, [CONFIDENTIAL TREATMENT REQUESTED]prior to the Scheduled Delivery Date of the first Aircraft under the applicable Supplement to Buyer, or as may be otherwise agreed, to establish the content and schedule of the Programs.

3.1.9 Buyer may convert any of the Programs to any other of the Programs for equivalent value.

3.2 Flight Crew Training

3.2.1 Training Allotments and Course Descriptions

Flight crew training allotments and course descriptions are set out in the applicable Supplement.

3.2.2 Recurrent Training

At Buyer's request, Bombardier shall assist Buyer to obtain recurrent training as set forth in the applicable Supplement

3.3 Maintenance Training

3.3.1 Training Allotments and Course Descriptions

Maintenance training allotments and course descriptions are set out in the applicable Supplement.

3.3.2 Specialist Courses

At Buyer's request, Bombardier shall assist Buyer to obtain specialist courses as set forth in the applicable Supplement.

3.3.3 Recurrent Training

At Buyer's request, Bombardier shall assist Buyer to obtain recurrent training as set forth in the applicable Supplement.

3.3.4 Vendor Training

At Buyer's request, Bombardier shall assist Buyer to obtain vendor maintenance training.

3.4 Insurance

3.4.1 [CONFIDENTIAL TREATMENT REQUESTED]

3.4.2 [CONFIDENTIAL TREATMENT REQUESTED]

ARTICLE 4 - TECHNICAL DATA

4.1 Bombardier shall furnish to Buyer the Technical Data described below (the "Technical Data"). The Technical Data shall be in the English language and shall provide information on items manufactured according to Bombardier's detailed design and in those units of measure used in the Specification or as may otherwise be required to reflect Aircraft instrumentation, as may be mutually agreed.

4.2 Shipment

All Technical Data provided hereunder shall be delivered to Buyer Free Carrier (Incoterms) Bombardier's designated facilities and at the time indicated above.

4.3 Proprietary Technical Data

It is understood and Buyer acknowledges that the Technical Data provided herein and under an applicable Supplement and any revisions thereto is proprietary to Bombardier and all rights to copyright belong to Bombardier and the Technical Data shall be kept confidential by Buyer. Buyer agrees to use the Technical Data solely to maintain, operate, overhaul or repair the Aircraft or to make installation or alteration thereto allowed by Bombardier. In addition, Buyer may transfer the Technical Data to any party in connection with the sale or lease of an Aircraft from Buyer provided Buyer obtains a confidentiality agreement with such purchaser or lessee in favour of and acceptable to Bombardier.

4.4 Technical Data shall not be disclosed to third parties or used by Buyer or furnished by Buyer for the design or manufacture of any aircraft or Spare Parts including Bombardier Parts or items of equipment, except when manufacture or redesign is permitted under the provisions of Annex A Article 2.4 hereof and then only to the extent and for the purposes expressly permitted therein, and provided further the recipient shall provide a non-disclosure undertaking acceptable to Bombardier.

4.5 The Technical Data provisions are set forth in the applicable Supplement.

ARTICLE 5 - HOLD HARMLESS

5.1 [CONFIDENTIAL TREATMENT REQUESTED].

5.2 [CONFIDENTIAL TREATMENT REQUESTED].

ANNEX B

WARRANTY AND SERVICE LIFE POLICY

ARTICLE 1 - WARRANTY

The following warranty is that to which reference is made in Article 3 of Section I of the Agreement.

1.1 Warranty

1.1.1 [CONFIDENTIAL TREATMENT REQUESTED]

1.1.2 [CONFIDENTIAL TREATMENT REQUESTED]

1.1.3 [CONFIDENTIAL TREATMENT REQUESTED].

1.2 Warranty Period

1.2.1 The Warranty set forth in Annex B Article 1.1 shall remain in effect for any defect covered by the Warranty (a "Defect") becoming apparent during the following periods (individually, the "Warranty Period"):

[CONFIDENTIAL TREATMENT REQUESTED]

1.3 Repair, Replacement or Rework

[CONFIDENTIAL TREATMENT REQUESTED]

1.4 Claims Information

Bombardier's obligations hereunder are subject to a Warranty claim to be submitted in writing to Bombardier's warranty administrator, which claim shall include but not be limited to the following information:

(a) the identity of the part or item involved, including the Part number, serial number if applicable, nomenclature and the quantity claimed to be defective;

(b) the manufacturer's serial number of the Aircraft from which the part was removed;

(c) the date the claimed Defect became apparent to Buyer;

(d) the total flight hours (and cycles if applicable) accrued on the part at the time the claimed Defect became apparent to Buyer; and

(e) a description of the claimed Defect and the circumstances pertaining thereto.

1.5 Bombardier's Approval

[CONFIDENTIAL TREATMENT REQUESTED]
.

1.6 Timely Corrections

1.6.1 Bombardier shall make the repair, replacement or rework, following receipt of the defective part or item, with reasonable care and dispatch.

1.6.2 [CONFIDENTIAL TREATMENT REQUESTED]

1.7 Labour Reimbursement

[CONFIDENTIAL TREATMENT REQUESTED]
.

1.8 Approval, Audit, Transportation and Waiver

All Warranty claims shall be subject to audit and approval by Bombardier. Bombardier will use reasonable efforts to advise in writing the disposition of Buyer's Warranty claim [CONFIDENTIAL TREATMENT REQUESTED] following the receipt of the claim and (if requested) return of the defective Bombardier Part to Bombardier's designated facility. Bombardier shall notify Buyer of Bombardier's disposition of each claim.

[CONFIDENTIAL TREATMENT REQUESTED].

1.9 Limitations

1.9.1 Bombardier shall be relieved of and shall have no obligation or liability under this Warranty if:

[CONFIDENTIAL TREATMENT REQUESTED].

1.9.2 The above warranties do not apply to Buyer Furnished Equipment.

1.10 Normal Usage

Normal wear and tear that does not render the part unserviceable and the need for regular maintenance and overhaul shall not constitute a Defect or failure under this Warranty.

1.11 Overhaul of Warranty Parts

Bombardier's liability for a Bombardier Part which has a Defect and is overhauled by Buyer within the Warranty Period [CONFIDENTIAL TREATMENT REQUESTED].

1.12 No Fault Found

In the event that a Bombardier Part returned under a Warranty claim is subsequently established to be serviceable then Bombardier shall be entitled to charge and recover from Buyer any reasonable costs incurred by Bombardier in connection with such Warranty claim. Providing, however, in the event that repetitive in-service failure occurs on the particular Bombardier Part which is subsequently identified by Bombardier on a repeated basis to be "no fault found", then Bombardier and Buyer shall discuss and mutually agree a course of further action to help identify the problem. In the event the fault is ultimately confirmed to be a legitimate Warranty claim then the above mentioned costs incurred by Bombardier and charged to Buyer shall be waived.

ARTICLE 2 - VENDOR WARRANTIES

2.1 Warranties from Vendors

The Warranty provisions of this Annex B apply to Bombardier Parts only. [CONFIDENTIAL TREATMENT REQUESTED] Bombardier shall have no liability or responsibility for any such Vendor Parts and Power Plant Parts and the warranties for those Vendor Parts and Power Plant Parts shall be the responsibility of the vendor and a matter as between Buyer and vendor.

2.2 [CONFIDENTIAL TREATMENT REQUESTED].

2.3 [CONFIDENTIAL TREATMENT REQUESTED]

ARTICLE 3 - SERVICE LIFE POLICY

3.1 Applicability

The Service Life Policy ("SLP") described in this Annex B, Article 3 shall apply if repetitive failures occur in any Covered Component which is defined in Annex B Article 3.7 below.

3.2 Term

[CONFIDENTIAL TREATMENT REQUESTED]

.

3.3 Price

[CONFIDENTIAL TREATMENT REQUESTED]

3.4 Conditions and Limitations

3.4.1 The following general conditions and limitations shall apply to the SLP:

[CONFIDENTIAL TREATMENT REQUESTED].

3.5 Coverage

This SLP is neither a warranty, performance guarantee nor an agreement to modify the Aircraft to conform to new developments in design and manufacturing art. Bombardier's obligation is only to[CONFIDENTIAL TREATMENT REQUESTED].

3.6 Assignment

Buyer's rights under this SLP shall not be assigned, sold, leased, transferred or otherwise alienated by contract, operation of law or otherwise, without Bombardier's prior written consent. Any unauthorized assignment, sale, lease, transfer, or other alienation of Buyer's rights under the SLP shall immediately void all of Bombardier's obligations under the SLP.

3.7 Covered Component

Only those items or part thereof listed in the applicable Supplement shall be deemed to be a Covered Component, and subject to the provisions of this SLP.

ARTICLE 4 - GENERAL

4.1 It is agreed that Bombardier shall not be obligated to provide to Buyer any remedy which is a duplicate of any other remedy which has been provided to Buyer under any other part of this Annex B.

ARTICLE 5 - DISCLAIMER

5.1 [CONFIDENTIAL TREATMENT REQUESTED]

EXHIBIT I TO THE AGREEMENT

CERTIFICATE OF ACCEPTANCE

The undersigned hereby acknowledges on behalf of Buyer acceptance of the Aircraft bearing manufacturer's serial number ____________________ fitted with two (2) /General Electric CF-34-3A1/3B1/8C1 turbofan [Canadair Regional Jet]/ Pratt & Whitney of Canada, Ltd. PWC-120/121/123/150 turboprop [Dash 8]/ engines bearing serial numbers _____________________ and __________________ /and two (2) (Hamilton Standard 14SF-/7/15/23/) (Dowty R408) propellers bearing serial numbers _____________________ and __________________ / as being in accordance with the terms and conditions of this Agreement signed on the day of , 19 between Bombardier Aerospace, Regional Aircraft and Buyer.

Place: Date:

Signed for and on behalf of

Horizon Air Industries, Inc.

Per:

Title:

EXHIBIT II TO THE AGREEMENT

BILL OF SALE

1. FOR VALUABLE CONSIDERATION, BOMBARDIER AEROSPACE, REGIONAL AIRCRAFT, OWNER OF THE FULL LEGAL AND BENEFICIAL TITLE OF THE AIRCRAFT DESCRIBED AS FOLLOWS:

ONE CANADAIR REGIONAL JET MODEL /CL-600-2B19/CL-600-2C10/ [CANADAIR REGIONAL JET] DE HAVILLAND DHC-8-100/200/300/400/ [DASH 8] AIRCRAFT BEARING:

MANUFACTURER'S SERIAL NO.: _________________________, WITH:

CF34-3A1/3B1/8C1 [CANADAIR REGIONAL JET] / PWC -/120/121/123/150/ [DASH 8] ENGINES SERIAL NOS.:___________AND______________, AND

/HAMILTON STANDARD 14SF-/7/15/23] [DOWTY R408] PROPELLERS SERIAL NOS: MFG _____________________AND _______________;/

AUXILIARY POWER UNIT NO.: __________________________

DOES THIS DAY OF 20 HEREBY SELL, GRANT, TRANSFER AND DELIVER ALL RIGHT, TITLE AND INTEREST IN AND TO SUCH AIRCRAFT UNTO: [BUYER'S NAME].

BY VIRTUE OF THE EXECUTION OF THIS BILL OF SALE, BOMBARDIER HEREBY DIVESTS ITSELF OF ALL ITS RIGHT, TITLE AND INTEREST OF ANY KIND IN THE AIRCRAFT, IN FAVOUR OF BUYER.

BUYER:

PLACE: TIME:

For and on behalf of

BOMBARDIER INC.
Bombardier Aerospace, Regional Aircraft

Per:

Title:

EXHIBIT III TO THE AGREEMENT

CERTIFICATE OF RECEIPT OF AIRCRAFT

THE UNDERSIGNED HEREBY ACKNOWLEDGES TO HAVE RECEIVED FROM BOMBARDIER AEROSPACE, REGIONAL AIRCRAFT, AT/ THE DOWNSVIEW AIRPORT, ADJACENT TO BOMBARDIER'S PLANT IN DOWNSVIEW, PROVINCE OF ONTARIO, CANADA [DASH 8]/ DORVAL AIRPORT, ADJACENT TO BOMBARDIER'S PLANT IN DORVAL, PROVINCE OF QUEBEC, CANADA, [CANADAIR REGIONAL JET]/ ON THE _____________ DAY OF ______________ , AT THE HOUR OF _____________ O'CLOCK, ONE (1) / CANADAIR REGIONAL JET MODEL /CL-600-2B19/CL-600-2C10/ SERIES 100/200/700/ de HAVILLAND DHC-8-/100/200/300/400/ AIRCRAFT, BEARING SERIAL NUMBER ______________, INCLUDING WITH THE AIRCRAFT TWO (2) /CF34-3A1/3B1/8C1 TURBOFAN / PWC-/120/121/123/150 TURBOPROP / ENGINES BEARING MANUFACTURER'S SERIAL NUMBERS _____________ & __________________ AND TWO (2) [HAMILTON STANDARD 14SF-/7/15/23] [DOWTY R408] PROPELLERS BEARING MANUFACTURER'S SERIAL NUMBERS _____________ & __________________ AND OTHER MAJOR REPLACEABLE ACCESSORIES ATTACHED TO THE AIRCRAFT AND ENGINES.

Signed for and on behalf of
Horizon Air Industries, Inc.

Per:

Title:

EXHIBIT IV TO THE AGREEMENT

CHANGE ORDER
(PRO FORMA)

CONTRACT CHANGE ORDER

PURCHASER:

PURCHASE AGREEMENT NO.: AIRCRAFT TYPE:

C.C.O. NO.: DATED:

PAGE __ of __

REASON FOR CHANGE:

____

DESCRIPTION OF CHANGE:

ALL OTHER TERMS AND CONDITIONS OF THE AGREEMENT WILL REMAIN UNCHANGED

For administrative purposes only, a consolidation of the amendments contained in this CCO is attached. In the event of inconsistencies between the consolidation and this CCO, this CCO shall prevail.

____

FOR AND ON BEHALF OF: FOR AND ON BEHALF OF:

Bombardier Aerospace [BUYER]
Regional Aircraft

Signed: ______________________ Signed: _________________________

Date: ______________________ Date: _________________________

SUPPLEMENT NO. PA-436-1

TO

MASTER PURCHASE AGREEMENT NO. PA-436

BETWEEN

BOMBARDIER INC.

AND

HORIZON AIR INDUSTRIES, INC.

This Supplement when accepted and agreed to by Horizon Air Industries, Inc. (the "Buyer") will become part of the Master Purchase Agreement No. PA-436 entered into between BOMBARDIER INC., a Canadian corporation represented by Bombardier Aerospace, Regional Aircraft having offices at 123 Garratt Boulevard, Downsview, Ontario, Canada ("Bombardier") and Buyer dated the 21st day of December, 1998 (the "Agreement") and will evidence our further agreement with respect to the matters set forth below.

The provisions of the Agreement shall apply to the Bombardier products purchased and sold in accordance with this Supplement. All capitalized terms herein, unless defined herein, shall have the same respective meanings as in the Agreement. This Supplement is subject to the provisions of the Agreement, all of which are incorporated herein, provided that in the event of any inconsistency between the provision of the Agreement and the provisions of this Supplement, the latter shall take precedence.

Article 1 below supplements Article 2 of the Agreement.

ARTICLE 1 SUBJECT MATTER OF SALE

1.1 Subject to the provisions of the Agreement and this Supplement, Bombardier will sell and Buyer will purchase twenty-five (25) model CL-600-2C10 Canadair Regional Jet Series 700 aircraft manufactured pursuant to Type Specification number RAD-670-100 issue B dated September 1998 attached hereto as Schedule 1 as same may be modified from time to time in accordance with the Agreement and this Supplement (the "Specification"), as supplemented to reflect the incorporation of the Buyer selected optional features ("Buyer Selected Optional Features") set forth in Schedule 2 hereto (individually or collectively the "Aircraft").

Article 2 below supplements Article 4 of the Agreement.

ARTICLE 2.0 PRICE

2.1 (a) The base price for each of the Aircraft (excluding the Buyer Selected Optional Features) [CONFIDENTIAL TREATMENT REQUESTED].

(b) The base price of the Buyer Selected Optional Features (Schedule

2) [CONFIDENTIAL TREATMENT REQUESTED].

(c) The Buyer Selected Optional Features set forth in Appendix IV represents a preliminary listing of those Buyer Selected Optional Features that may be required by Buyer. [CONFIDENTIAL TREATMENT REQUESTED].

[CONFIDENTIAL TREATMENT REQUESTED].

2.2 [CONFIDENTIAL TREATMENT REQUESTED].

Articles 3.1 and 3.2 below supplement Article 5.1 of the Agreement. Article 3.3 below supplement Article 5.4 of the Agreement.

ARTICLE 3.0 PAYMENT

3.1 Bombardier acknowledges having previously received a deposit in the amount of [CONFIDENTIAL TREATMENT REQUESTED]. Such amount shall be applied against the balance of the Aircraft Purchase Price due at the Delivery Date for each Aircraft in accordance with the provisions of Article 3.2 below.

3.2 Terms of payment for each Aircraft are based on the estimated Aircraft Purchase Price and are as follows:

[CONFIDENTIAL TREATMENT REQUESTED]; and

(f) the balance of the Aircraft Purchase Price, less the amounts previously received referred to in Article 3.1 above, on or before the Delivery Date of such Aircraft to Buyer.

All payments referred to in paragraphs (b) to (e) above are to be made on the first day of the applicable month.

3.3 [CONFIDENTIAL TREATMENT REQUESTED].

3.4 Buyer shall make all payments due under this Agreement and for any applicable Supplement in [CONFIDENTIAL TREATMENT REQUESTED] United States Dollars by deposit on or before the due date, to Bombardier's account in the following manner:

[CONFIDENTIAL TREATMENT REQUESTED].

Article 4.0 below supplements Article 6.0 of the Agreement.

ARTICLE 4.0 DELIVERY PROGRAM

4.1 The Aircraft shall be offered for inspection and acceptance to Buyer at Bombardier's facility in Montreal, Quebec during the calendar quarters for each year set forth below (the "Scheduled Delivery Dates"). Bombardier shall advise Buyer of the scheduled month of delivery of each Aircraft (which month Bombardier shall ensure will fall within the applicable quarter listed below) eighteen (18) months prior to such delivery such that the Aircraft are scheduled for delivery evenly throughout the delivery schedule, but in any event no less than thirty (30) days from the preceding delivery.

DELIVERY SCHEDULE

First Aircraft 2nd quarter 2002
Second Aircraft 2nd quarter 2002
Third Aircraft 3rd quarter 2002
Fourth Aircraft 4th quarter 2002
Fifth Aircraft 1st quarter 2003
Sixth Aircraft 2nd quarter 2003
Seventh Aircraft 2nd quarter 2003
Eighth Aircraft 3rd quarter 2003
Ninth Aircraft 3rd quarter 2003

Tenth Aircraft 4th quarter 2003
Eleventh Aircraft 4th quarter 2003
Twelfth Aircraft 1st quarter 2004
Thirteenth Aircraft 1st quarter 2004
Fourteenth Aircraft 2nd quarter 2004
Fifteenth Aircraft 2nd quarter 2004
Sixteenth Aircraft 3rd quarter 2004
Seventeenth Aircraft 3rd quarter 2004
Eighteenth Aircraft 4th quarter 2004
Nineteenth Aircraft 4th quarter 2004
Twentieth Aircraft 1st quarter 2005
Twenty-First Aircraft 1st quarter 2005
Twenty-Second Aircraft 2nd quarter 2005
Twenty-Third Aircraft 2nd quarter 2005
Twenty-Fourth Aircraft 3rd quarter 2005
Twenty-Fifth Aircraft 3rd quarter 2005

Article 5.0 below supplements Article 7.0 of the Agreement.

ARTICLE 5.0 BUYER INFORMATION

5.1 Pursuant to Article 7.1 of the Agreement, Buyer will, provide the information set forth in Article 7.1 of the Agreement [CONFIDENTIAL TREATMENT REQUESTED] .

ARTICLE 6.0 NON-EXCUSABLE DELAY

Article 6.1 below supplements Article 14.1 of the Agreement.

6.1 If delivery of the Aircraft is delayed by causes not excused under Article 13.1 of the Agreement (a "Non-Excusable Delay"), [CONFIDENTIAL TREATMENT REQUESTED].

Article 6.2 below supplements Article 14.3 of the Agreement.

6.2 The period of days referred to in Article 14.3 of the Agreement is [CONFIDENTIAL TREATMENT REQUESTED].

Article 7.0 below supplements Annex A, Article 1.0 of the Agreement.

ARTICLE 7.0 TECHNICAL SUPPORT

7.1 The FSR term referred to in Annex A, Article 1.2.2 is as follows:

Such assignment shall span the Delivery Schedule set forth in Article 4.0 of this Supplement, commencing approximately [CONFIDENTIAL TREATMENT REQUESTED] prior to the Delivery Date of the first Aircraft and [CONFIDENTIAL TREATMENT REQUESTED] thereafter or until one month after the last Aircraft delivery which ever is later. The FSR term will not be extended if the Scheduled Delivery Dates are amended as a result of Buyer's request to postpone deliveries. The FSR assignment may be extended on terms and conditions to be mutually agreed.

7.2 Start-up Operations Management Team
[CONFIDENTIAL TREATMENT REQUESTED]

Article 8.0 below supplements Annex A, Article 3.2 and 3.3 of the Agreement.

ARTICLE 8.0 TRAINING

8.1 Flight Crew Training

8.1.1
[CONFIDENTIAL TREATMENT REQUESTED].

8.1.2
[CONFIDENTIAL TREATMENT REQUESTED]

8.1.3
[CONFIDENTIAL TREATMENT REQUESTED] .

8.1.4
[CONFIDENTIAL TREATMENT REQUESTED]

8.2 Maintenance Training

8.2.1
[CONFIDENTIAL TREATMENT REQUESTED].

8.2.2
[CONFIDENTIAL TREATMENT REQUESTED].

8.2.3
[CONFIDENTIAL TREATMENT REQUESTED].

8.2.4
[CONFIDENTIAL TREATMENT REQUESTED]

8.2.3
[CONFIDENTIAL TREATMENT REQUESTED]

8.2.4
[CONFIDENTIAL TREATMENT REQUESTED].

8.2.5
[CONFIDENTIAL TREATMENT REQUESTED]

Article 9.0 below supplements Annex A, Article 4 of the Agreement.

ARTICLE 9.0 - TECHNICAL DATA

COLUMN HEADING EXPLANATION OF CODES

ITEM
1 DOC DOCUMENT
Title of Technical Data provided.

2 CONFIG CONFIGURATION
G = Contains data common to all aircraft of the same type (Generic).
C = Contains data unique to Buyer's Aircraft (Customized).

3 MEDIUM Buyer selects one of the following media specified in the table:
1 = Print two sides
2 = Microfilm
3 = Print one side
4 = Laminated Cardboard

4 REVISION Y = Periodic revision service applies
N = Revision service not applicable
S = Revised as required by Bombardier

5 QUANTITY
(Number) = Quantity per the Agreement
(Number) PER = Quantity per Aircraft

6 DELIVERY
[CONFIDENTIAL TREATMENT REQUESTED]

7 ATA Y = Document is per ATA Specification 100, Revision 26.
N = Document is to Bombardier's existing commercial practices.

With the delivery of the first Aircraft, Bombardier will provide to Buyer at no additional charge one set of the technical manuals listed below

LIST OF TECHNICAL DATA
[CONFIDENTIAL TREATMENT REQUESTED]

NOTES: See following page.

NOTE 1: REVISION SERVICE

A. Revision services shall only be available for [CONFIDENTIAL TREATMENT REQUESTED] following the Delivery Date of Buyer's last Aircraft. Subsequent revision service shall be provided dependent upon incorporation of Bombardier issued Service Bulletins.

B. Revisions to the Technical Data to reflect the Aircraft at Delivery Date shall be provided to Buyer within [CONFIDENTIAL TREATMENT REQUESTED] following the Delivery Date of each of the Aircraft, respectively.

C. Provided the revision service is being supplied under the terms of this Agreement or by subsequent purchase order, Bombardier shall incorporate in the applicable documents all applicable Bombardier originated Service Bulletins in a regular revision following formal notification by Buyer that such Service Bulletins shall be accomplished on the Buyer's Aircraft. The manuals shall then contain both original and revised configuration until Buyer advises Bombardier in writing that one configuration is no longer required.

NOTE 2: SERVICE BULLETINS
Aperture cards of the service drawing(s) will be provided in lieu of drawings when practical.

NOTE 3: MAINTENANCE PROGRAM DOCUMENT
This manual provides the basis for Buyer's initial maintenance program.

NOTE 4: AIRCRAFT CHARACTERISTICS FOR AIRPORT PLANNING
This manual contains data on Aircraft ground manoeuver and handling.

NOTE 5: ON-BOARD WIRING DIAGRAM BOOK
This book contains wiring diagrams for interim reference until the Wiring Diagram Manual is revised to reflect the Aircraft at the Delivery Date.

NOTE 6: PASSENGER INFORMATION CARDS
Bombardier will provide one (1) reproducible master for the preparation of passenger information cards. [CONFIDENTIAL TREATMENT REQUESTED].

9.2 Vendor Manuals

[CONFIDENTIAL TREATMENT REQUESTED]

These all will be shipped by the vendors directly to Buyer.

All manuals, revisions or amendments will be in the English language.

Article 10.0 below supplements Annex B, Article 1.0 of the Agreement.

ARTICLE 10.0 WARRANTY

11.1 [CONFIDENTIAL TREATMENT REQUESTED].

11.2 [CONFIDENTIAL TREATMENT REQUESTED].

11.3 [CONFIDENTIAL TREATMENT REQUESTED].

11.4 [CONFIDENTIAL TREATMENT REQUESTED].

Article 11.0 below supplements Article 3.7 of the Agreement.

ARTICLE 11.0 COVERED COMPONENTS

11.1 [CONFIDENTIAL TREATMENT REQUESTED].

11.2 [CONFIDENTIAL TREATMENT REQUESTED].

11.3 [CONFIDENTIAL TREATMENT REQUESTED]

11.4 [CONFIDENTIAL TREATMENT REQUESTED].

In witness whereof this Supplement was signed on the date written hereof:

For and on behalf of	For and on behalf of
HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC. Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
___________________________	_______________________________
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

____
Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 1 TO SUPPLEMENT NO. PA-436-1

SPECIFICATION

TYPE SPECIFICATION

Number RAD-670-100 Issue B

September 4 1998

Buyer acknowledges having received the Specification mentioned above

SCHEDULE 2 TO SUPPLEMENT NO. PA-436-1

BUYER SELECTED OPTIONAL FEATURES
PRICES AND DESCRIPTIONS

[CONFIDENTIAL TREATMENT REQUESTED]

SCHEDULE 3 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

SCHEDULE 4 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED].

3.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

4.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

5.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC. Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 5 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

8.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

9.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

10.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC. Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 6 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

12.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

13.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

14.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC. Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
___________________________	_______________________________
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

____

Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 7 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

3.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

4.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

5.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC. Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
___________________________	_______________________________
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

____

Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 8 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

5.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

6.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

7.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC. Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
______________________________	__________________________________
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

____

Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 9 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

9.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

10.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

11.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC. Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
______________________________	__________________________________
Glenn Scott Johnson Vice President and Treasurer.	Robert Gillespie President Regional Aircraft

Original signed by M. Bourgeois

____

Michel Bourgeois
Vice President, Contracts
Regional Aircraft

ATTACHMENT 1

SCHEDULE 9

[CONFIDENTIAL TREATMENT REQUESTED]

SCHEDULE 10 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

5.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

6.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

7.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC. | BOMBARDIER INC. Bombardier Aerospace

Original signed by G. Johnson
____
Glenn Scott Johnson
Vice President and Treasurer.

Original signed by R. Gillespie
____
Robert Gillespie
President
Regional Aircraft

Original signed by M. Bourgeois
____
Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 11 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]
.

3.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

4.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

5.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC. | BOMBARDIER INC. Bombardier Aerospace

Original signed by G. Johnson
____
Glenn Scott Johnson
Vice President and Treasurer.

Original signed by R. Gillespie
____
Robert Gillespie
President
Regional Aircraft

Original signed by M. Bourgeois
____
Michel Bourgeois
Vice President, Contracts
Regional Aircraft

SCHEDULE 12 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

2.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

3.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

4.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC. | BOMBARDIER INC.

	Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
___________________________	_______________________________
Glenn Scott Johnson	Robert Gillespie
Vice President and Treasurer.	President
	Regional Aircraft

Original signed by M. Bourgeois

____
Michel Bourgeois
Vice President, Contracts
Regional Aircraft

ATTACHMENT 1

SCHEDULE 12

[CONFIDENTIAL TREATMENT REQUESTED]

SCHEDULE 13 TO SUPPLEMENT NO. PA-436-1

[CONFIDENTIAL TREATMENT REQUESTED]

3.0 In the event of the termination of the Agreement, this Schedule shall become automatically null and void.

4.0 The provisions of this Schedule are personal to Buyer and shall not be assigned or otherwise disposed of by Buyer without the prior written consent of Bombardier.

5.0 This Schedule constitutes an integral part of the Agreement and subject to the terms and conditions contained therein.

HORIZON AIR INDUSTRIES, INC.	BOMBARDIER INC.
	Bombardier Aerospace
Original signed by G. Johnson	Original signed by R. Gillespie
___________________________	_______________________________
Glenn Scott Johnson	Robert Gillespie
Vice President and Treasurer.	President
	Regional Aircraft

Original signed by M. Bourgeois

____
Michel Bourgeois
Vice President, Contracts
Regional Aircraft

EXHIBIT 12

Alaska Air Group, Inc.
Calculation of Ratio of Earnings to Fixed Charges
(In thousands, except ratios)

	1998	1997	1996	1995	1994
Earnings:					
Income before income tax expense	$204,400	$123,600	$64,349	$33,983	$40,961
Less: Capitalized interest	(6,600)	(5,300)	(1,031)	(208)	(353)
Add:					
Interest on indebtedness	21,200	33,600	38,394	51,479	46,960
Amortization of debt expense	682	685	1,224	1,100	1,368
Portion of rent under long-term operating leases representative of an interest factor	80,547	72,900	71,562	67,295	65,618
Earnings Available for Fixed Charges	$300,229	$225,485	$174,498	$153,649	$154,554
Fixed Charges:					
Interest	21,200	33,600	38,394	51,479	46,960
Amortization of debt expense	682	685	1,224	1,100	1,368
Portion of rent under long-term operating leases representative of an interest factor	80,547	72,900	71,562	67,295	65,618
Total Fixed Charges	$102,429	$107,185	$111,180	$119,874	$113,946
Ratio of Earnings to Fixed Charges	2.93	2.10	1.57	1.28	1.36

Exhibit 23

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation of our report dated January 25, 1999 included in this Form 10-K, into the Company's previously filed Registration Statements, File Numbers 33-22358, 33-52242, 333-09547, 333-33727, 333-39889 and 333-39899.

/s/ ARTHUR ANDERSEN LLP
ARTHUR ANDERSEN LLP

Seattle, Washington
February 10, 1999

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM ALASKA AIR GROUP, INC. 1998 FINANCIAL STATEMENTS AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.
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